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Analysis of the recovery and resilience plan of Latvia

Accompanying the document

Proposal for a COUNCIL IMPLEMENTING DECISION

on the approval of the assessment of the recovery and resilience plan for Latvia

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1. EXECUTIVE SUMMARY

Latvia's economy stood up to the COVID-19 crisis relatively well with a sharp decline counterbalanced by a robust recovery. However, achieving a sustainable growth path will be more challenging. Latvia's GDP contracted by 3.6% in 2020 due to COVID-19 pandemic-related restrictions. After the initial shock in the second quarter of 2020, the economy rebounded strongly during the rest of the year. The economy declined again in the 1st quarter of 2021due to the measures aimed at containing the second wave of the pandemic, however, the setback is expected to be temporary. A significant easing of measures in the second half of 2021 should help the economy recover, to reach a growth rate of 3.5% overall in 2021. The momentum is expected to carry into 2022, when GDP growth is projected to reach 5.6% driven by buoyant private consumption and investments. Over the medium term, Latvia's growth prospects will depend on its ability to counter the pre-crisis trend of falling labour supply. Employment decline in 2020 has been mitigated thanks to the deployment of furlough schemes, which incentivized businesses to keep people in employment. The number of people employed declined by 2.3% in 2020 with the unemployment rate reaching 8.3% from 6.3% in 2019. However, the recovery in employment is expected to lag GDP growth somewhat, with the unemployment rate seeing a more pronounced improvement only in 2022. Low-wage earners working in the services sector have been disproportionally affected by the crisis, further widening the already existing disparities in income level and adequacy of social protection.

Government support to employees and businesses was prompt during the first wave of the pandemic, but faced some delays during the second wave. At the outset of the crisis, Latvia promptly deployed support for businesses and people affected by the crisis and dedicated additional resources to the health sector. As a result, the government deficit increased to 4.5% in 2020 and is expected to reach 7.3% in 2021. The deficit is expected to decline rapidly in 2022, however, as support measures are being phased out. Government debt is projected to increase by almost 10 pps. by the end of 2022 compared to 2019.

Latvia submitted its Recovery and Resilience plan on 30 April 2021[1]. Latvia's plan consists of 6 components, covering 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 twin transitions, health infrastructure, social and regional infrastructure as well as research and innovation. The measures include direct investments in public infrastructure, capacities and processes as well as extensive support programmes for private investment in the twin transitions and innovation. The investments are accompanied by reforms that will make them more effective at achieving their intended policy goals and by helping to attract private investments for bigger impact. In addition, Latvia's plan includes a few self-standing reforms that aim to address challenges in areas that have been prominently identified in the Country Specific recommendations – tax administration, the judicial system, the capacity of the public administration and public procurement. Latvia requested EUR 1.826 billion and no loans.

The plan includes measures addressing all key challenges, constituting an adequate response to the economic and social situation and is expected to strengthen Latvia's growth potential. The challenges identified in the most recent Country-Specific recommendations pertain to six

[1] Latvia submitted its National Reform Programme on 14 April 2021. The information provided in the National Reform Programme is being considered and jointly assessed in this Staff Working Document together with the Recovery and Resilience Plan.

broad policy areas – fiscal and financial challenges, challenges related to social inclusion and skills, challenges related to productivity growth and convergence, challenges related to the efficiency and accountability of public administration, as well as challenges related to the twin transitions. Latvia's plan contributes to effectively addressing a significant subset of challenges identified in the country specific recommendations. Moreover, by contributing to effectively addressing Latvia's key economic and social challenges identified in the country-specific recommendations, the plan presents a comprehensive and adequately balanced response to the economic and social situation, thereby contributing appropriately to all six pillars referred to in Article 3 of the RRF Regulation.

The plan proposes significant reforms in health, social inclusion, higher education and skills. The plan's most ambitious measures are related to the reform of governance and financing of higher education institutions, the preparation of a comprehensive human resources strategy in healthcare, and the introduction of annual indexation of minimum income benefits. These measures are expected to have a lasting impact and to contribute significantly to addressing challenges in higher education, health and social inclusion.

Investments in green and digital infrastructure, regional development, as well as extensive support schemes for business investment is expected to bolster Latvia's growth potential over the medium to long term. Investments and accompanying reforms to the Riga transport system are expected to boost the city's competitiveness and ability to attract investments and talent. Measures to foster private investments in wind energy are set to contribute to reaching renewable energy targets and becoming a competitive low-carbon economy. Business investment support schemes are set to accelerate Latvia's pursuit of higher export capacity and productivity growth. Investments in housing and infrastructure for peripheral regions are expected to strengthen Latvia's lagging regions' growth opportunities. Altogether, these measures address long-standing challenges of Latvia's economy – low innovation spending, low uptake of modern technologies as well as significant regional disparities.

Latvia's recovery and resilience plan is compliant with the 'do no significant harm' principle. The assessment follows the methodology set out in the Commission's Technical guidance on the application of 'do no significant harm' under the Recovery and Resilience Facility Regulation (2021/C 58/01) and the six corresponding environmental objectives. Where necessary, respect of the 'do no significant harm' principle is ensured by milestones.

Reforms and investments in clean transport, energy efficiency and climate adaptation, as well as reforms fostering investment in renewable energy will address Latvia's climate challenges. Latvia's main green climate transition challenges are to reverse the trend of growing energy consumption in transport and buildings as well as to continue increasing the share of renewable energy in its energy consumption. The greening of Riga metropolitan transport system is expected to contribute to increasing the renewable energy share, reducing energy consumption and greenhouse gas emissions in transport sector through making public transport a more attractive option for commuting. Investments in energy efficiency of public and residential buildings will contribute to the achievement of Latvia's energy efficiency target for 2030. Investments in the electricity network aimed at facilitating the development of self-generation and extending the electric charging infrastructure to densely populated areas will help promote renewable energy use both in housing and transport sectors. Moreover, Latvia aims to remove barriers to private investments in wind energy, which is crucial to Latvia's ability to reach its 2030 renewable energy target. Furthermore, a support instrument to businesses will support a variety of green investments, including renewable energy, energy efficiency and green R&D. Finally, greening of Riga transport

system and investments in a new customs control post are expected to yield improvements in air quality thus contributing to environmental objectives. Altogether, Latvia's plan dedicates 37.6% of the available funding to climate-related investments.

Latvia's plan addresses its key digital challenges – poor skills, insufficient rural connectivity and low level of business digitalisation. Poor basic digital skills among the working age population, insufficient uptake of digital solutions by businesses as well as a shortage of ICT specialists are Latvia's key digital challenges, negatively affecting workforce availability, competitiveness, business digitalisation, use of government e-services and digital innovation. Significant reforms and investments are planned to address the country-specific recommendations in this area. The measures supporting digital objectives account for an amount which represents 21% of the plan's total allocation. The plan includes sizeable investments in basic and advanced digital skills to foster Latvia's digital transition. Latvia's plan also includes measures for the digital modernisation of public administration and the digital transformation of public services, including centralised public solutions. Latvia addresses the challenge also by supporting the digital transformation of businesses, in particular SMEs and R&D as well as by creating the necessary framework for Latvia's participation in the network of European of Digital Innovation Hubs. The plan includes measures to deploy very high-speed broadband that will help further improve the digital infrastructure.

Investments in human capital, digital capacities, research and innovation capacity, and public transport are expected to have the largest impact on the economy's long-term potential. Latvia's plan includes investments and reforms aimed at improving skills. The importance of this is reflected by the high unemployment rate differential between the high and the low skilled. There has also been a recurring trend of shortages of qualified workforce and tight labour supply, aggravated by aging and declining population and emigration. A structural improvement in the skills composition has the potential to boost the use of digital solutions, services, exports and to spur regional development. Furthermore, investments in modernising the public IT infrastructure, support for business digitalisation as well as investments in 5G should lead to synergies that will help increase the country's capacity for use of digital solutions. Support for private R&D investments are aimed at creating sustainable innovation ecosystems that are expected to boost Latvia's innovation capacity in the long term. Finally, the reform of the governance of the Riga metro area public transport system as well as its associated investments are aimed at improving public transport's attractiveness and achieve a higher proportion of mobility needs being served by public transport. If successfully implemented, the measures will improve Latvia's growth potential, and economic and social resilience in the medium term, and facilitate the green and digital transitions. The stakeholder consultation process was overall adequate, enhancing the ownership of stakeholders and supporting the lasting impact of the measures.

Latvia has provided estimates of the total costs of the recovery and resilience plan which are to a medium extent reasonable and broadly plausible. Latvia has provided individual cost estimates for all investments included in the plan. The cost breakdown is generally detailed and well-substantiated. The estimates are based on comparisons with past investments of similar nature and on market and price analysis. While Latvia did not provide an independent validation for the cost estimates proposed, the assessment of the cost estimates and inherent supporting documents show that most of the costs are well justified and reasonable. The amounts proposed for financing were deemed appropriate and seen as establishing the plausibility of the cost estimates to a medium extent. Although the costs of most measures are deemed highly plausible that is the amount asked for is in the low to medium range compared to costs of similar reforms or investments, there are a limited set of measures for which the costing is deemed to be plausible to a low extent. Finally, the

estimated total cost of the recovery and resilience plan is in line with the principle of cost-efficiency and is commensurate to the expected national economic and social impact.

The individual components provide clear information about additional investments from other EU funds. Projects funded by other EU sources are demarcated in time and scope from the projects in the RRP. Furthermore, Latvia has put in place arrangements to avoid double EU funding.

The arrangements proposed in the recovery and resilience plan are adequate to ensure its effective monitoring and implementation, including the envisaged timetable, milestones and targets, and the related indicators. The Ministry of Finance will be tasked with monitoring of the plan, whereas line ministries will be responsible for its implementation. The milestones and targets are realistic and relevant, but monitoring mechanisms are not always mentioned. The targets and milestones are robust, but tend to be back loaded in the cases of infrastructure investment and support schemes for business investment. The control system and arrangements proposed in the recovery and resilience plan are based on robust processes and structures used in the existing Cohesion Policy framework. The plan clearly identifies responsible actors for carrying out the internal control tasks. The functions are appropriately segregated and the arrangements for the collection and publication of data on final recipients are adequate.

The Latvian recovery and resilience plan is coherent, with consistent, mutually reinforcing reforms and investments, and synergies between the different components. The recovery and resilience plan contains measures for the implementation of reforms and public investment projects that represent coherent actions. The six components structure the investments and reforms and show their thematic relation and interlinkages well. Coherence is ensured within the components, with investments accompanying relevant reforms, as well as between the different components in the plan. The components included in the RRP of Latvia form a single framework for reforms and investments, the core task of which is to promote productivity, reduce inequalities, as well as promote the climate transition and digital transformation. The six components are mutually reinforcing and coherent in their aims.

Table 1: Summary of the assessment of the Plan under the RRF criteria

(1) Balanced Response	(2) CSRs	(3) Growth, jobs…	(4) DNSH	(5) Green target	(6) Digital target	(7) Lasting impact	(8) Milestones & Targets	(9) Costing	(10) Control Systems	(11) Coherence
A	A	A	A	A	A	A	A	B	A	A

2. RECOVERY AND RESILIENCE CHALLENGES: SCENE-SETTER

2.1. Macroeconomic outlook and developments since the 2020 country report

Macroeconomic developments since the 2020 country report

The Latvian economy shrank by 3.6% in 2020, in the wake of the COVID-19 crisis. In particular, the first two quarters of 2020 saw a significant fall in output due to restrictions. The economy mounted a strong recovery in the third quarter before slowing at the end of the year amid renewed restrictions in response to the second wave of infections. Demand for household

consumption and exports saw the largest decline as consumers stayed home and travel restrictions made exports of services more difficult. Investments held up better than initially expected, remaining at the 2019 level, largely helped by the construction sector's continued activity during the first wave of the pandemic.

Employment held up better than GDP, thanks to furlough schemes. The average unemployment rate increased by 1.8 pps. in 2020 compared to 2019. The unemployment rate increased significantly in the first half of the year before decreasing somewhat during the summer and early autumn. However, the second wave of the pandemic reversed this trend and the unemployment rate started to increase again in December. Most jobs were lost in sectors directly affected by restrictive measures – hospitality, catering, transport and other service sectors. Moreover, the job losses mostly affected low-wage earners. As a result, wage growth slowed only marginally compared to its pre-crisis pace, recording 5.3% growth in 2020. It is estimated that the emergency measures to protect incomes during the COVID-19 crisis, together with the pre-existing tax-benefit system, cushioned about 78% of the shock on household incomes in Latvia, almost half of the effect due to furlough schemes[2].

Social conditions were improving before the COVID-19 crisis, thanks to an improving labour market, but the COVID-19 crisis is likely to exacerbate the pre-existing inequalities. Poverty declined noticeably since its peak in 2011, with the share of people at in poverty rate declining by more than 10 pps. This is largely attributable to the continuous improvement of the labour market. Inequality, on the other hand, has largely remained steady over the past 10 years. The share of people at risk of poverty or social exclusion fell slightly from 28.4% in 2018 to 27.3% in 2019, but remained among the highest in the EU.

Macroeconomic outlook

The macroeconomic scenario included in Latvia's Recovery and Resilience plan (RRP) expects GDP to rebound, reaching 3.0% growth in 2021. The scenario assumes the restrictions related to the pandemic will be lifted in the second part of the year, giving a boost to the private consumption and exports. In 2022, the scenario expects GDP growth to reach 4.5% as investments take over as the main growth driver. Growth is expected to moderate thereafter at around 2.8%.

Compared with the macroeconomic scenario of the Latvian government, the Commission forecast is somewhat more optimistic for both 2021 and 2022 due to differences in the appraisal of government support measures for 2021 and inflow of EU funded investments for 2022. Latvia's forecast dates back to early February when part of the support measures for 2021 had not yet been announced and there was less clarity about the timeline of both the RRF investments and other EU-funded investments. According to the Commission's forecast, inflation is set to recover from a near standstill in 2020 to 1.7% in 2021 and 2.0% in 2022.

Employment is expected to follow a similar path to economic growth. The unemployment rate is expected to decline towards the end of 2021 thanks to the jobs gained in the second part of the year when most services hit by pandemic restrictions are expected to reopen. The unemployment

[2] See Christl, M, De Poli, S., Figari, F., Hufkens, T., Leventi, C., Papini, A. and Tumino, A. (2021) "The cushioning effect of fiscal policy in the EU during the COVID-19 pandemic", JRC Working Papers on Taxation and Structural Reforms, 02/2021 (forthcoming); and Almeida, V., Barrios, S., Christl, M., De Poli, S., Tumino, A., Van der Wielen, W. (2020): 'Households´ income and the cushioning effect of fiscal policy measures during the Great Lockdown', JRC Working Paper on Taxation and Structural Reforms, 06/2020, available at https://ec.europa.eu/jrc/sites/jrcsh/files/jrc121598.pdf.

rate is set to decline further in 2022, reaching 6.9%. The tightening of the labour market is expected to lead to increased pressure on wage growth, which is expected to remain modest in 2021.

The budget deficit increased to 4.5% of GDP in 2020 and is expected to increase to 7.3% of GDP in 2021 before declining sharply in 2022. The government deficit increased from 0.6% in 2019 to 4.5% of GDP in 2020. The sharp worsening reflects the drop in tax revenue, in line with the decline in consumption, the loss of jobs, and the impact of temporary support measures for households and businesses. The government deficit is projected to further increase to almost 7¼% of GDP in 2021 due to temporary support measures, before narrowing to 2% by 2022. The government debt-to-GDP ratio increased from 37% in 2019 to almost 43.5% in 2020. The debt-to-GDP ratio is expected to reach around 47% in 2021, but to decline in 2022, on the back of the lower fiscal deficit and the rebound in GDP. The 2020 Debt Sustainability Monitor projects debt to peak in 2026 at slightly below 50% of GDP before resuming to decline. Hence, Latvia's fiscal policy remains on a sustainable path at the beginning of 2021.

A delay in the COVID-19 vaccination strategy is considered to be the main negative risk to the macroeconomic scenario. The macroeconomic scenario included in Latvia's plan assumes that the government's target of 70% of the adult population having been vaccinated by the end of summer will be met, allowing for a return to close to unrestricted economic activity by that time. However, vaccine availability and vaccination rollout may slow, leading to delayed easing of restrictions. On the positive side, Latvia's scenario does not account for the full range of support measures for 2021 and its forecast of EU-funded investments for 2022 is markedly cautious.

Table 2: Comparison of macroeconomic developments and forecasts

	2019	2020		2021		2022		2023	2024	2025	2026
	COM	COM	RRP	COM	RRP	COM	RRP	RRP	RRP	RRP	RRP
Real GDP (% change)	2.0	-3.6		3.5	3.0	6.0	4.5	3.2	2.8	2.8	2.8
Employment (% change)	-0.1	-2.3		0.1	-0.4	1.8	1	0.3	0	0.1	-0.6
Unemployment rate (%)	6.3	8.1		8.2		6.9					
HICP inflation (% change)	2.7	0.1		1.7		2.0					
General government balance (% of GDP)	-0.6	-4.5		-7.3		-2.0					
Gross debt ratio (% of GDP)	37.0	43.5		47.3		46.4					

Source: [Commission Spring Forecast 2021] (COM); Recovery and resilience plan (RRP)

2.2. Challenges related to sustainable growth, cohesion, resilience and policies for the next generation

Smart, sustainable and inclusive growth

Strong economic and fiscal fundamentals enabled Latvia to provide necessary support to the economy, but challenges related to the social safety of vulnerable groups have become more apparent. The COVID-19 pandemic had a significant impact on economic activity and business sentiment. The government reacted swiftly to the challenges posed by the COVID-19 crisis and adopted a support package to ensure the necessary liquidity for businesses and income support for households. The support made available in 2020 to businesses and citizens amounted to EUR 1.3 billion, or 4.5 % of GDP. However, the support granted turned out to be lower than initially expected. This was partly due to strict eligibility conditions and the relatively high prevalence of envelope wages among the groups most severely affected by the crisis. This experience highlighted the interlinked challenges of the shadow economy and social safety nets.

Latvia's main economic objective remains to ensure steady income convergence with the EU average. In 2020 Latvia's income per capita declined by 3% compared to 2019, however, over a 5-year period it had increased by a 12%. Yet in 2019 it stood at only 69% of the EU average in purchasing parity standards. The income difference compared to the richer EU countries remaining a powerful driver of emigration. Therefore, continued convergence remains Latvia's key challenge in terms of improving its population's living standards. However, a number of structural issues raise concern about sustained convergence: firstly, the country's declining population weighs on the sustainability of social systems, shrinks the domestic market and raises infrastructure costs per capita. Secondly, the high share of the shadow economy holds back fair competition, weakens affected workers' social protection and increases occupational risks. It is also among the main reasons for lacklustre credit growth. The lack of affordable housing also inhibits internal labour mobility. Finally, Latvia's innovation performance is relatively low and stagnating.

Latvia's fiscal position remains strong and sustainable, but poor tax compliance persists and there are insufficient resources for critical public services. Strong growth and a prudent fiscal policy helped Latvia maintain its debt level at sustainable levels – 43.5% of GDP at the end of 2020. Moreover, Latvia's pension and health systems do not pose a fiscal challenge in the long term. However, Latvia's tax revenue as a share of GDP remains among the lowest in the EU, limiting its redistributive power to improve critical public services like healthcare and social assistance. Furthermore, weak tax compliance has been a long-running issue in Latvia, with undeclared transactions, envelope wages, undeclared income and tax fraud all being part of the problem.

There are difficulties in ensuring that growth benefits all parts of society. Inequality remains high and peripheral regions are lagging behind the Riga region. The divergent population dynamics, with a growing population in the Riga metropolitan area and a rapidly declining population in the rest of Latvia, have created challenges for the quality of service delivery across regions, as well as the quality of the public administration at municipal level.

Latvia's labour force is declining, while employment conditions differ across regions and skill levels. There is a shortage of skilled workers, especially in STEM (science, technology, engineering, mathematics) sectors. Meanwhile, low-skilled, older workers, ethnic minorities and those living further away from the regional centres have more limited access to the labour market. As only a small share of the unemployed register with the public employment service, many cannot be reached with upskilling, reskilling and job search measures. The delivery and composition of

active labour market measures have to be strengthened and adapted to mitigate the impact of COVID-19 crisis. Job opportunities are concentrated in urban centres, while labour mobility is hampered by the lack of affordable housing and limited transport connections. Furthermore, social partners' capacity remains limited, restricting their engagement to reinforce equal opportunities and jobs for all and deliver on the European Pillar of Social Rights.

Research and innovation in Latvia has still an ample scope in developing its potential to contribute to the diversification and competitiveness of the economy. With an R&D intensity of 0.64% of GDP, the R&I system is hindered by underfunding, making it less attractive to researchers. Human capital imbalances represent a significant bottleneck of the Latvian research and innovation landscape and are evident in the current shortage of R&D personnel and skills, both in the private and public sectors. Research-industry and intra-industry links remain key challenges. In spite of the recent advances in the development of a technology-oriented start-up ecosystem, Latvia lags behind other EU Member States in terms of the innovative capacity of start-ups and SMEs.

Social and territorial cohesion

Regional economic and social disparities remain among the widest in the EU. While Riga's GDP per capita reached 91% of the EU average in 2018, in the Latgale region in the east of the country it was only 25%. Population is decreasing in all regions of Latvia (NUTS3) due to natural change and migration, except for the Pieriga region where numbers are on the rise. The Latgale region has the highest unemployment rate, the highest risk of poverty, the lowest wages and the lowest economic activity in the country, it is also experiencing the most rapid depopulation.

The quality of public services varies considerably among Latvian regions. The shortages of health and social workers outside Riga restrict access to quality care. Ensuring inclusive and quality education for all remains a challenge for smaller rural schools. Private housing conditions in rural areas are worse than in urban areas. Some regions outside the Riga metropolitan area still struggle with providing utilities like central sewerage and water. The road network is of low quality with poor public transport connections.

In 2020, Latvia adopted an administrative-territorial reform that significantly reduces the number of municipalities. Its aim is to consolidate local authorities' administrative capacity, improving their services and governance, allowing for better planning and cost savings. However, the municipalities will need reforms and investments to ensure that quality public services are accessible to all, including to those living further away from the new administrative centres.

Latvia is lagging behind in the completion of the TEN-T conventional rail core network. The main TEN-T corridor railway infrastructure (the Rail Baltica railway corridor connecting the Baltic States to the standard-gauge European network) is not yet in place, but construction has started. Only 14% of railway lines are electrified. A projected decline in international rail freight transport will force a shift from freight to more passenger rail services. Multimodal transfer points between Rail Baltica and national and regional transport networks need to be developed.

Health, economic, social and institutional resilience

Weak health outcomes are linked to poor lifestyle choices and an under-resourced health system. Their effect on the health status of the population impacts negatively on labour supply and Latvia's growth potential too. Many of the challenges in the sector – workforce shortages, lack of timely access to affordable health and long-term care, and limited disease prevention – are linked to low public financing. Latvia spent around 3.7% of GDP on healthcare in 2019, the second lowest ratio in the EU. Access to publicly funded healthcare services is limited by a quota system and lack of health workforce; this has led to a high level of unmet needs and a high prevalence of out-of-pocket payments. Moreover, the quality and efficiency of service delivery is uneven, with service delivery focused more on hospital care (which is more expensive) and less on the use of home care and community-based services. Whilst the intensive care capacity has increased during the COVID-19 pandemic, the Latvian health system has still come under immense pressure.

Relative poverty in Latvia remains high and is increasing, while spending on social protection remains low. The poor funding of the social system is the main driver of income inequality. Income distribution is more unequal in Latvia than in the EU on average. While the inequality of market incomes is about average, redistribution through taxes and social transfers is among the lowest in the EU[3]. The poor funding of the social system is linked indirectly with the relatively low tax intake as a share of GDP, limiting the amount of funding that can be spent on social programmes. The elderly, the unemployed and persons with disabilities are the most affected groups. Despite the recent increase in 2021, the guaranteed minimum income remains significantly below the poverty threshold and lacks a clear indexation mechanism. As a result, the share of people at risk of poverty or social exclusion and the poverty gap both remain wide. Income inequality is associated with unequal access to healthcare, which is significantly more difficult for low-income groups, who cannot afford private healthcare.

Access to adequate housing is a challenge, particularly for low-income groups. The share of people facing severe housing deprivation is high**.** The social housing stock is low and often not fit for living, while waiting lists are long. The lack of affordable housing is among the main barriers to labour mobility and regional development. A comprehensive housing strategy is not yet in place, nor are the strategies to address homelessness and housing exclusion.

Latvia has a generally favourable business environment, but some areas suffer from expensive administrative obstacles and legal uncertainty. Latvia ranks 19th on the World Bank Doing Business index, reflecting its quick firm establishment process, openness to trade and robust legal framework. This is thanks to such measures as company registration e-service, introduction of "Zero Bureaucracy" and "Consult first" approach to public services. Latvia has also put efforts into boosting its start-up ecosystem, by providing various types of support including financial support, a special tax regime for start-ups, a start-up visa program, acceleration funds and incubation support. As a result, the number of start-ups has increased four times since 2012, reaching 450 active start-ups in 2020, which have attracted EUR 303 million of investments. At the same time, construction and wind energy sectors face notable barriers to investment related to lengthy administrative procedures and legal unpredictability. Getting a construction permit and other construction-related approvals is a lengthy and costly process, particularly in Riga. This has been among the key factors holding back investment in buildings. Moreover, implementation of onshore wind energy investments face legal unpredictability related to municipalities' competence

[3] In 2018, social transfers (excluding pensions) reduced the risk of poverty rate by 19.1 % in Latvia vs 32.94 % in the EU. Latvia spent 11.6% of GDP on social payments, well below the EU average of 20.4%.

regarding final approval of the projects. Despite having successfully completed of an extensive and lengthy environmental impact assessment process, the projects may still be rejected without giving a justified reason. Moreover, the appeal process of municipalities' decisions are lengthy. Municipalities' decisions are often influenced by community opposition to wind projects. In this regard, an equitable profit sharing mechanism that would benefit local communities is missing and could be explored as another means to foster wind energy deployment[4]. Due to this risk, investment in onshore wind in Latvia has been paltry. Finally, administrative and tax obstacles have hindered business investment in skills.

The main areas of public administration facing hurdles include tax administration, law enforcement and the judiciary, and public procurement. The VAT gap in Latvia is estimated to have markedly declined over the past years, slipping below the EU average indicator in 2019. Nevertheless, other measures point to a persistently high level of shadow economy and its prevalence is estimated to have increased in 2018-2019[5]. The large shadow economy partly reflects a lack of efficiency in the tax administration, which needs to adapt its organisation, operational practices and information sharing throughout the country to fight tax evasion and fraud more effectively. Overall, Latvia's performance in the area of public procurement is satisfactory. Latvia's main difficulties reside in the share of procedures with a single bidder (32%) and public procurement procedures negotiated without any call for bids (8%). 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 in some case 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 public procurers of the importance of competition[6]. Moreover, public procurers often lack capacity to prepare and carry out large and complex procurement projects effectively.

Policies for the next generation, children and young people, including education and skills

A key challenge for education in Latvia is to ensure a comparable quality of education across schools and regions. Access to inclusive and quality education remains dependent on place of residence, with larger urban schools outperforming smaller rural ones (as per the latest PISA report). Latvia has started to consolidate its large and inefficient school network, but progress is slow, delaying gains in quality and efficiency. The share of students in vocational education and training remains lower than in general education, and graduate tracking is not yet in place. Renewing the teaching workforce is a challenge and teacher shortages are becoming apparent, especially in sciences and maths. Furthermore, COVID-19 restrictions exposed digital and social inequalities (availability of hardware and internet connections), leading to uneven access to distance learning.

The main challenge for Latvia's higher education is taking action to reduce the fragmentation of the higher education system, which hinders its quality and competitiveness. The inefficient higher education governance model coupled with non-performance based funding impairs scientific excellence and the attractiveness of the public science base for business and international

[4] For example, residents are often opposed to wind farms as they believe that it would have negative impacts such as visual presence, noise, flickering, and falling property value, among others (source: A breath of fresh air: Analysis of factors affecting deployment of wind energy in Latvia and potential solutions, 2019, by CEE Bankwatch Network)
[5] Sauka and Putnins, Shadow Economy Index for the Baltic Countries 2009–2019, https://www.sseriga.edu/sites/default/files/2020-06/BROCHURE_English_2020.pdf.
[6] Single Market Scoreboard https://ec.europa.eu/internal_market/scoreboard/performance_per_policy_area/public_procurement/index_en.htm

partners. A set of reforms of the governance of higher education institutions in general and of academic careers in particular is under way and could increase higher education's strategic capacity and academic competitiveness. Existing plans to reduce the fragmentation of study programmes need to be given new momentum.

Labour market skills shortages remain. The low level of digital skills among the labour force, flagged 'critical' on the Social Scoreboard, limits the use of digital technologies by businesses and the potential for innovation. The adult learning participation rate is low, especially among the low-skilled. The challenge remains to strengthen the governance of the skills system, including planning, and to deliver high-quality adult learning to all, especially to vulnerable groups.

2.3. Challenges related to the green and digital transition

2.3.1. Green dimension

The recovery and resilience plan should include a minimum level of 37% of expenditure related to the green dimension. 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. They should also contribute to meeting the environmental targets for waste, water, pollution control, sustainable mobility, biodiversity protection and restoration, marine and water resources, and support the transition to sustainable food systems as well as to a circular economy as appropriate, while ensuring that nobody is left behind. This can be achieved by equipping workforce with adequate green skills and providing support for sustainable innovation and competitiveness.

Reducing energy consumption in transport and buildings and boosting its renewable energy capacity are Latvia's key energy and climate policy challenges. Latvia's greenhouse gas emissions per capita are among the lowest in the EU. This is because its energy consumption per capita is lower than the EU average, while its share of renewable energy is also among the highest in the EU. Nevertheless, Latvia faces major challenges over its non-ETS emissions reduction, which have been increasing due to rising energy consumption in transport and buildings. As a result, to meet its 2030 target for greenhouse gas emissions, Latvia would need to break the current trend of increasing energy consumption and emissions in transport and buildings. It would also need to continue increasing the share of renewables, which it has successfully done in heating and power generation, thanks to the widespread use of biomass-based cogeneration. Looking forward, the scope for increased use of sustainable biomass is limited and Latvia will need to tap the potential of wind and solar power as long-term solutions. Latvia also needs to boost its recycling rates and improve circular economy and the sustainability of its agricultural and forestry practices.

Renewable energy

Latvia already achieved its 2020 renewable energy target of 40% in 2019. Latvia has set a renewable energy share of 50% in gross final energy consumption for 2030, but risks falling short of it if the speed of renewables deployment is not accelerated, especially for wind energy. Latvia would therefore benefit from policies and measures to help speed up renewables deployment. Reducing the legal uncertainty and investment risk to onshore wind farm developers is necessary to boost wind energy, which plays a central role in Latvia's plans to reach its 2030 contribution on renewable energy. It is equally important to make low-cost long-term financing available for green

investments, including investments in renewables. Latvia needs to develop an enabling framework for the uptake of local renewable sources other than biomass, focusing instead on sources such as ambient, geothermal, wind and solar energy, including promoting renewable self-consumption and renewable energy communities and citizen energy communities.

Latvia plans to achieve a 7% share from renewable energy in transport by 2030. It plans to achieve 3.5%with advanced biofuels and by increasing the electrification of rail and through electro-mobility. Latvia needs to provide sufficient safeguards for the production of advanced biofuels in accordance with Annex IX to the Directive (EU) 2018/2001. More specific policies would be welcome to diversify and increase the uptake of renewables in transport.

Energy efficiency

For Latvia to achieve its energy efficiency target for 2030, it needs to break the trend of rising energy consumption. The transport and buildings sectors are the largest contributors to rising energy consumption. The key to curbing energy consumption growth in transport is to incentivise a modal shift from cars to public transport, particularly within the Riga metropolitan area, where more than half the country's commuter traffic takes place.

To achieve its 2030 energy efficiency target, Latvia should speed up building renovation. Current renovation plans fall significantly short of the efforts needed to achieve the 2030 national contribution. Speeding up renovation (in line with Renovation Wave) involves: (i) scaling up current support programmes; (ii) reducing the administrative cost of building renovation, including through project standardisation and aggregation; and (iii) greater availability of low-cost, long-term financing and private capital to reduce the public cost of renovating private buildings. Energy efficiency measures combined with renewable solutions should be encouraged, and due attention to energy poverty should be given when designing support measures. 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 2050.

Circular economy

Latvia's performance in the transition to a circular economy is improving. In 2019, Latvia's municipal waste recycling rate (including composting) was 41%, up from 25% in 2016.[7] However, a rate of 4.7% circular material in 2019 remains below the EU-27 average of 11.9%. Latvia is taking steps to move towards a more circular economy. Nevertheless, it falls behind in its re-use and recycling targets as a lack of incentives for municipalities holds back investment in separate collection, in particular in Riga. Furthermore, the quality of data on waste collection could be improved. Latvia stands to benefit from boosting recycling and separate collections of waste, including bio-waste.

Land use

Latvia reduced its greenhouse gas emissions from agriculture between 1990 and 2018, but recent years and projections show a renewed, increasing trend. Although Latvia's agricultural sector emits less greenhouse gas emissions than the EU average, the share of its total emissions stemming from agriculture is relatively high, particularly for agricultural soils. At the same time, there has been a significant decrease in total net greenhouse gas emission removals in LULUCF

[7] https://ec.europa.eu/eurostat/databrowser/view/cei_wm011/default/table?lang=en.

(land use, land use change and forestry) sectors, mainly due to the increase in logging and the extension of peat.

Forests cover 54.9% of the country's territory. Latvia could focus efforts on: (i) fostering sustainable forest management and promoting the efficient use of sustainable biomass; (ii) enhancing the multi-functionality of forests; (iii) promoting forest protection; and (iv) restoring forest ecosystems.

Biodiversity

The economic growth of Latvia in the latest decades has intensified pressures on the environment and biodiversity. The main pressures are agricultural, industrial and urban pollution and land use change. The latest report required by Article 17 of the Habitats Directive on the conservation status of habitats and species shows that less than 10% of protected habitats and less than 40% of species have a favourable conservation status. Adopting conservation objectives and measures to maintain and upgrade species and habitats of community interest to a favourable conservation status and mainstreaming biodiversity conservation and sustainable use in other areas, notably forestry, agriculture, fishery and tourism could help address that situation.

Air quality

Measures targeting reducing air pollution and emissions, particularly from transport, agriculture and through improved energy efficiency of housing would support the National Air Pollution Control Programme and help Latvia comply with the 2020 commitments for nitrogen oxide (NOx) and ammonia (NH3) emission reduction according to the National Emission Reduction Commitments (NEC) Directive ((EU) 2016/2284.

The table below gives an overview of Latvia's objectives, targets and contributions under Regulation (EU) 2018/1999 of the European Parliament and of the Council of 11 December 2018 on the Governance of the Energy Union and Climate Action.

Table 3: Latvia's national targets and contributions regarding energy and climate

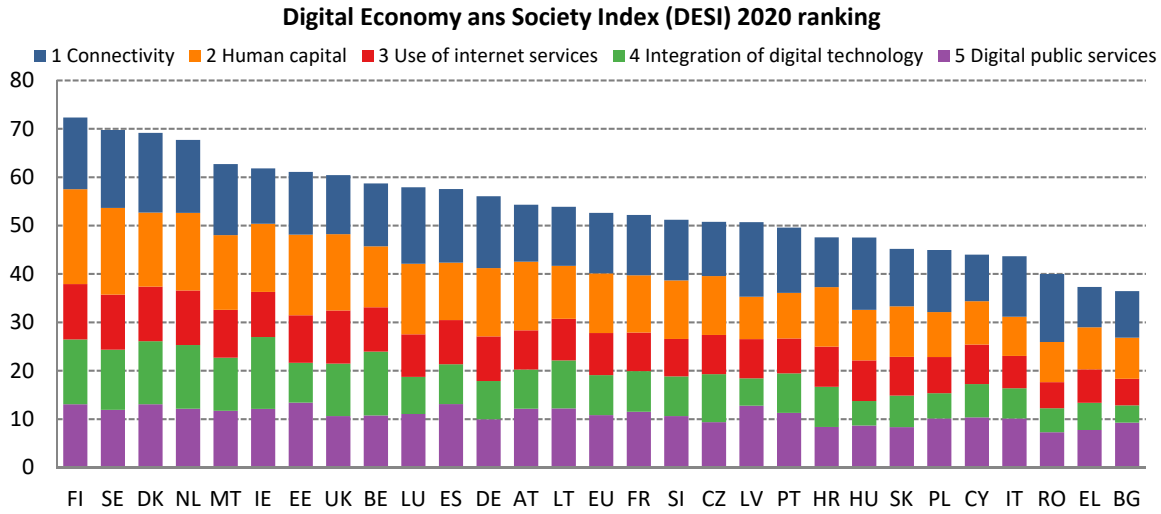
	National targets and contributions	Latest available data	2020	2030	Assessment of 2030 ambition level
	Binding target for greenhouse gas emissions compared to 2005 under the Effort Sharing Regulation (%)	8	+17	-6	As in ESR
	National target/contribution for renewable energy: Share of energy from renewable sources in gross final consumption of energy (%)	40%	40%	50%	Adequate (50% is the result of RES formula)
	**National contribution for energy efficiency:**				
	Primary energy consumption (Mtoe)	4.6	5.4	4.1	Modest
	Final energy consumption (Mtoe)	4.1	4.5	3.6	Modest
	Level of electricity interconnectivity (%)	50%	10%	60%	n/a

Source: Assessment of the final national energy and climate plan of Latvia, SWD (2020) 926 final.

2.3.2. Digital dimension

The recovery and resilience plan should contribute to the digital transition and at least 20% of the financial allocation needs to contribute to digital objectives. The measures in the plan should, inter alia, contribute to the digital transformation of the economic and social sectors (including public administration, public services, and the justice and health systems). The objective of the measures in the plan should be to improve not only the competitiveness, but also the resilience, agility and security of companies and public actors, all while ensuring inclusiveness.

Latvia ranks 18th in the European Commission's Digital Economy and Society Index (DESI) for 2020. It is three ranks lower than the 2019 DESI and progressing slower than other EU Member States.



Source: 2020 DESI report
Note: EU aggregate corresponds to EU28, based on 2020 DESI report.

While Latvia is a front-runner in broadband coverage and take-up, and is well prepared for the 5G rollout, problems in ensuring accessibility to fast and reliable internet in rural regions remain. The country's main strengths are the extremely advanced coverage of fast broadband (NGA) (93% against the EU average 86%), and near complete average 4G coverage (99% against EU average 96%). In 2018, Latvia signed a memorandum of understanding for the Via Baltica 5G corridor with Estonia and Lithuania. In 2020, Poland also joined the Via Baltica 5G initiative. Latvia also performs well as regards to very high capacity networks (VHCN) and reaches coverage rates of almost 90%, far above the EU average of 49.6%. Fixed broadband coverage in Latvia is around 95 %, with wider disparities in rural areas at 80%. Ensuring fast and reliable broadband access to rural regions remains a challenge, highlighted by the difficulty these regions faced in organising distance learning during the COVID-19 pandemic. Extensive investments in middle-mile connections in rural regions have been made; however, private investment in last-mile connections has not taken place due to such investments' lack of commercial viability. For this reason, public funds are needed to ensure fast internet access to rural regions. Also, regulatory changes as well as investments are needed to lower the administrative cost of 5G infrastructure deployment, and for connected and automated mobility development.

The low level of digital skills in Latvia hampers its digital transformation. Latvia is far below the EU average in all indicators in the human capital dimension, ranking 24th in the EU. As of 2019, 57% of the Latvian population lacked basic digital skills and Latvia had the lowest share of ICT specialists among its workforce in the EU. The shortage of digital skills is a key obstacle to more widespread use of digital solutions by the private sector. Almost half of Latvian firms that tried to fill vacancies for digital specialists find it difficult to do so.

The digital provision of public services is strong, Latvia ranking fifth in the DESI. The number of e-government users continues to increase and there was a further improvement in the provision of online public services. The government adopted its 2020-2023 public service development plan, which aims at proactive service provision, user-centricity built around key life events, coordinated and integrated approach in service design, cross-border services, digital-by-default and digital-first principles. Overall, the plan continues promoting the use of ICT as a tool to build a knowledge-based economy and to improve the overall quality of life.

At the same time, only 14% of companies are highly digitalised with Latvia ranking 23rd among EU Member States in the DESI. Latvian firms make limited use of cloud services and big data. Latvian firms also engage in less e-commerce than their EU counterparts: only 11% of Latvian SMEs sell online (compared to the EU average of 18%), and the SME turnover generated from e-commerce (5%) is less than half of the EU average (11%). Latvian enterprises also lag behind their EU counterparts in electronic information sharing, use of social media and selling online cross-border, despite recent progress.

Box 1: Progress towards the Sustainable Development Goals

Sustainable Development Goals and the four dimensions underpinning the Annual Sustainable Growth Strategy

In this figure, the United Nations' Sustainable Development Goals are represented under a specific Commission guiding principle for competitive sustainability from the 2021 Annual Sustainable Growth Strategy, to which they are strongly associated. It should be noted that most Sustainable Development Goals contribute, to varying degrees, to several guiding principles.



1. No poverty
2. Zero hunger
3. Good health and well-being
4. Quality education
5. Gender equality
6. Clean water and sanitation
7. Affordable and clean energy
8. Decent work and economic growth
9. Industry, innovation and infrastructure
10. Reduced inequalities
11. Sustainable cities and communities
12. Responsible consumption and production
13. Climate action
14. Life below water
15. Life on land
16. Peace, justice and strong institutions
17. Partnership for the goals

This section outlines Latvia's performance with respect to SDGs with particular relevance for the four dimensions underpinning the recovery and resilience plans (green transition, fairness, digital transition and productivity, and macroeconomic stability), indicating possible areas where investments and reforms in line with the objectives of the Facility could further accelerate the progress on the SDGs.

Green transition. Latvia has achieved a relatively high share of renewable energy in electricity and heating, but to achieve its long-term climate goals it will need to invest substantially in wind and solar energy and promote renewables in transport. Latvia's performance in energy efficiency has been more modest, and significant investments in buildings and transport sectors are needed to achieve country's energy efficiency goals. Latvia lags behind in resource efficiency and its circular material use rate is below the EU average.

Fairness. While poverty has declined significantly in the past decade thanks to a higher employment rate, income inequality in Latvia remains high. The high income inequality primarily reflects the weak social safety net. The most vulnerable groups are the elderly, the unemployed, persons with disabilities and families with 3+ children.

Digital transition and productivity. Latvia has achieved remarkable productivity growth over the past two decades and remains on a solid path going forward. However, a declining population, poor innovation performance and struggling private investments pose a challenge to productivity growth in the medium term. Latvia enjoys world-class digital connectivity and has generally wide availability of public digital services; however, the population's digital skills and use of digital solutions among businesses are low.

Macroeconomic stability. Latvia has pursued a prudent fiscal policy and its public debt, at 43.5% of GDP, remains sustainable. Its current account is balanced, and house prices and credit growth remain low. However, labour costs have been rapidly rising in recent years, raising some concerns about the country's price competitiveness.

3. OBJECTIVES, STRUCTURE AND GOVERNANCE OF THE PLAN

3.1. Overall strategy of the plan

Latvia's Recovery and Resilience Plan aims to support the recovery from the COVID-19 pandemic, promote sustainable growth and job-creation based on increased productivity and exports, and stimulate Latvia's economic convergence, while contributing to the twin transition. The plan is based on the priorities of the National Development Plan 2021-2027, National Industrial Policy 2021-2027, Latvia's Smart Specialisation Strategy, Post-COVID-19 Economic Resilience Strategy and the National Energy and Climate Plan (NECP). Furthermore, Latvia's plan takes into account sectoral development strategies, joint EU-level priorities, Latvia's international commitments and long-standing challenges to social and economic convergence.

The strategy of Latvia's plan is to exit from the COVID-19 crisis with a stronger and more resilient economy than when it entered the crisis. According to the plan, Latvia's exit strategy contains three phases: stabilisation (2020), reorientation (2021-2022), and new growth (from 2023 onwards). While budgetary means and crisis-response instruments have been used for short-term financial stabilisation, the plan is expected to foster medium-term economic reorientation and renewed growth. In the reorientation phase, the plan is expected to create new opportunities for businesses by supporting innovation, digital transformation, life-long learning and upskilling, by structural changes in the economy and targeted public sector intervention. In the new growth phase, the plan is expected to help economic transformation by boosting exports, stimulating productivity, driving digital transition and automation, supporting fast-growing firms, industries and innovation ecosystems.

Latvia's plan (for EUR 1 826 000 000 in non-repayable support) is divided into six components: green transition, digital transition, reduction of inequality, healthcare, productivity and the rule of law. The components broadly correspond to the six pillars of the RRF. All the components contain both reform and investment measures. However, investments are somewhat more prominent than reforms. Across the components, the Plan contains 85 measures in total, including 24 reform and 61 investment elements.

Table 4: List of components and associated costs in Latvia's RRP

Component	Costs (€ million)
1. **Green transition** (sustainable transport, energy efficiency, renewable energy and decarbonisation of electricity grids, climate adaptation)	676.2
2. **Digital transition** (public and private sector digitalization, e-government services, data management, digital skills, 5G and last-mile connectivity)	365.3
3. **Reduction of inequality** (road renovation, school infrastructure, affordable housing, industrial parks, social services, long-term care, upskilling)	370.0
4. **Healthcare** (hospital and ambulatory care infrastructure, human resources, resilience, public health)	181.5
5. **Productivity** (innovation governance, boosting private R&D investment, higher education and science governance, research careers)	196.0
6. **Rule of law** (combating economic crime, justice sector training, AML, public administration, procurement)	37.0

Green transition. Comprising EUR 676.2 million or 37.6% of the total allocation of the plan, the green transition component is the largest component of the plan. This component aims to address the challenges identified in Latvia's National Energy and Climate Plan, such as energy efficiency of buildings, emissions from transport, deployment of renewables and de-carbonisation of electricity. The component contains two main reforms – the creation of a joint multimodal transport network in the Riga metropolitan area and the overhaul of fire and rescue services. Another reform – incentives for wind power development through better regulatory framework, improved community relations and reduced legal uncertainty for investors – is associated with the modernisation of the electricity grid to make it fit for decentralised electricity generation and infrastructure for electric charging. In this component, 46% of investments will target energy efficiency in multi-apartment buildings, central government, historical and municipal buildings and the business sector, while 43% – a sustainable transport system in Riga metropolitan area. It is planned that 81 km of rail lines will be electrified, 7 new electric battery powered trains and 21 low-emission busses and trams procured and 60 km of cycling lanes will be developed in the Greater Riga area. In addition, the investments will enable the State Fire and Rescue Service to build 8 new modular depots and help implement 29 polder and dam projects to reduce flood risks in 59 000 ha of Latvia's territory. As a result, Latvia aims to save 36 241 tons of CO2 and 49 812 MWh/year in primary energy use.

Digital transition. With EUR 383.8 million or 21% of the total allocation of the plan, the digital component (EUR 365.3 million) and separate measures in rule of law and inequality components aim to address the challenges for Latvia identified in EU's Digital Society and Economy Index (DESI), notably, the low level of digital skills, low uptake of digitisation by businesses, and missing last-mile digital connection infrastructure. The component also aims to improve e-government, interoperability of systems and data management and to develop ICT supporting infrastructure and e-services. The component includes 7 reforms, such as centralised planning of ICT development; consolidation of public IT systems, platforms and infrastructure; improved data management; full-cycle support to business digitisation; a reform of general and digital skills delivery as well as common broadband infrastructure standards (for 5G and last-mile connections). In this component, 35% of investments will target public sector digitisation, 34%for the– private sector, and 26% for digital skills. According to the plan, Latvia intends to modernise 11 e-government solutions,

develop 15 centralised platforms/systems, place 10 systems on the national federated cloud, help more than 7000 businesses to digitalise, improve the digital skills of 54,500 individuals, 62,900 public sector employees, 3000 businesses, educate 1000 high-level ICT professionals, and make 26,620 digital equipment available for schools to ensure access to ICT for all schoolchildren. The plan is expected to ensure 100% broadband connectivity along the *Via Baltica* route and link up to 1500 homes, businesses and socio-economic drivers to last-mile broadband connections. The level of population with at least basic digital skills should increase from 43% in 2020 to 54% in 2026.

Reduction of inequality. Accounting for EUR 370 million or 20% of the total allocation of the plan, this component attempts to address the twin challenges of territorial and social disparities in Latvia. The objective of the component is to reduce inequality by creating more jobs in the regions, improving regional connectivity and access to services, providing more affordable housing, improving school infrastructure, helping to up-skill and re-skill workers and unemployed, strengthening the social safety net, improving accessibility to private and public buildings for persons with disabilities, and construction of new long-term care facilities for the elderly. The component includes two reforms – the ongoing administrative territorial reform and a minimum income reform, which foresees setting the minimum income level at 20% of the national median income and introducing annual indexation. In the component, 70% of investments target territorial disparities, while 30% target social inequality. On the basis of the plan, Latvia will renovate 210km of regional roads, construct 4 regional industrial centres, upgrade the infrastructure of 20 schools, procure 15 low-emission school busses, train 1300 municipal employees, provide 700 affordable housing units, upskill 20,450 jobseekers, provide accessibility to private homes for 259 persons with disabilities and to 63 public buildings and build long-term care facilities for 852 elderly persons. Planned investments should take into account regional and local development strategies, thus ensuring an integrated approach and sustainability of investments.

Healthcare. With EUR 181.5 million or 10% of the total allocation of the plan, the component aims to contribute to the accessibility, efficiency and resilience of Latvia's health system, which was heavily tested during the COVID-19 pandemic. The component contains three broad reforms – building a human-centred, integrated and resilient care system through development of a health infrastructure investment strategy, recommendations for integrated and epidemiologically safe care provision, guidelines for oncological care, participation in the "Genome for Europe" project and the development of a digital health strategy; improvement of human resources and skills through the development of a human resource strategy and mapping; and strengthening the effectiveness, governance and sustainability of the health system through more effective service delivery and assessment and piloting of new service models. In the component, 82% of the investments target the improvement of infrastructure of 3 university hospitals in Riga, 7 regional hospitals and 40 ambulatory care institutions.

Productivity. This component accounts for EUR 196 million or 11% of the total allocation of the plan and responds to the R&I challenges identified in the European Semester, such as low private sector investment in R&D (business expenditure on R&D was 0.18% of GDP, and total R&D investment was 0.64% of GDP in 2019) and a fragmented research and innovation system. The component contains two main reforms – improved innovation governance through an ecosystem approach and full-cycle support for innovation clusters and continuation of a higher education and science governance reform through consolidation of higher education institutions and support for research and academic careers. In the component, 58% of the investment measures target support for stimulating private sector R&D, while 42% target consolidation, academic careers and research grants. Owing to the investments, 5 functional innovation clusters would be developed and

supported, 4-6 universities would receive consolidation grants in exchange for mergers, 315 students will receive doctoral and post-doctoral grants, and 90 researchers research grants.

Rule of law. With EUR 37.0 million or 2% of the total allocation of the plan, this is the smallest component and responds to the long-standing challenges in dealing with economic crime (including tax evasion), effectiveness of public administration and professionalism in public procurement. The component contains 8 reforms: improved analytics and data management in tax and customs administration; development of remote imaging; modernisation of money-laundering and other economic crime investigation and judicial procedures; training of public officials; development of public procurement contract registry; fostering the competition culture; development of a procurement professionalisation strategy and IT and analytical capacity-building in public procurement. The component also contains various diverse investment projects, including procurement of customs technical equipment, a Judicial Training Academy, capacity-building of NGOs, and training of more than 16.000 officials in ethics, integrity, anti-corruption and more than 20.000 officials in leadership, change management, strategic planning and related competences.

3.2. Implementation aspects of the plan

Consistency with other programmes, including the National Reform Programme, is ensured. Latvia's plan is broadly consistent with the National Reform Programme, National Climate and Energy Plan, National Just Transition Plan (in negotiation), Partnership Agreement (in negotiation) and Operational Programmes (in negotiation). The plan makes appropriate references to demarcation and complementarities across the various funding programmes. In general terms, Latvia intends to use the RRF funding first, and other funding programmes afterwards, as RRF is a more time-limited instrument. However, in certain areas, such as social housing, de-institutionalisation, youth, education content, support to SME IPOs and some others, Latvia has made a conscious choice not to use RRF, but Cohesion Policy instruments linked to thematic logic. While Latvia's RRF allocation is sizable in relation to the country's GDP, it is not with respect to the magnitude of the challenges, especially, in green transition and social policy, RRF funding will therefore serve as a top-up to existing support schemes, funded by Cohesion Policy, such as in increasing energy efficiency of multi-apartment houses and helping businesses with the green transition.

The plan is broadly consistent with the challenges and priorities identified in the most recent euro area recommendation. The draft[8] Council recommendation on the economic policy of the euro area recommended to euro area Member States to take action, including through their recovery and resilience plans, to, inter alia, ensure a policy stance which supports the recovery, including by strengthening the coverage, adequacy and sustainability of the health system. The RRP contributes to EAR 1, as it pursues reforms and investments to support provision of integrated and human-centred health care, raise the capacity of health institutions to adapt to crisis situations and addresses the shortages of health workforce included in the component 4 on health, while component 3 on inequalities reduction will improve the adequacy of the minimum income support system. The Council recommendation also recommended euro area Member States to, inter alia, further improve convergence, resilience and sustainable and inclusive growth, including by

[8] Pending final adoption by the Council, after endorsement by the European Council. The text agreed by the Eurogroup on 16 December 2020 is available at: https://data.consilium.europa.eu/doc/document/ST-14356-2020-INIT/en/pdf.

ensuring effective active labour market policies and support to job transitions, notably towards the green and digital transition, as well as by improving the functioning of public administration. Components 1 and 2 include reforms and investments to promote the climate change adaptation and mitigation and digital transition respectively, while component 3 on reducing inequalities includes measures aimed to improve the labour market participation. The component 6 contains significant reforms to improve the functioning of public administration such as increasing the efficiency of tax administration, strengthening the competencies of the justice system, modernizing public administration and improving the quality and efficiency of public procurement.

The plan sets out a clear administrative organisation for its implementation. Latvia's Ministry of Finance, which is the Managing Authority for Cohesion Policy programmes, will also be the national coordinator for the RRF. The Ministry of Finance will work closely with line ministries, the State Chancellery and the Central Finance and Contracting Agency in order to ensure and monitor the implementation of the plan.

The plan's implementation set-up will be based on the existing cohesion policy framework. On 18 August 2020, the Cabinet of Ministers adopted a decision that the implementation process of the RRF will be ensured in the framework of the existing management and control system for EU funds 2014-2020. Based on this and the RRF regulation, the Cabinet of Ministers regulation for RRF implementation will be adopted by the end of 2021. The Cabinet of Ministers shall lay down the procedures for implementing and monitoring recovery and resilience plan and the procedures for using the IT system KPVIS.

Latvia plans the implementation of various measures to promote gender equality and equal opportunities for during the implementation phase of the key investments. With regard to gender equality and equal opportunities for all, the plan describes existing national challenges mainly in terms of gender equality and needs of persons with disabilities, and explains which investments are expected to contribute to overcoming the challenges identified. The challenges are supported by statistics disaggregated by gender. This description includes a wider reference to legislative and policy initiatives that are due to complement the reforms and investments in the plan in order to overcome the identified national equality challenges.

The RRP was the subject of various public discussions and debates, which covered the plan's main elements. Series of thematic public consultations open to civil society organisations, social partners, local authorities and other stakeholders have been organised between December 2020 and March 2021. Representatives from social partners, business organisations, local governments and other stakeholders have been taking part in the Plan negotiation process between the Commission and the Latvian authorities. Partners' suggestions for the draft Plan are publicly available and have been published along with the draft plan. From 8 February to 9 March 2021, all interested parties had the opportunity to submit their views and comments by taking part in the public consultation on the draft plan. Stakeholders' engagement in the implementation is planned to be established through the management and control system used for the implementation of the Cohesion policy support, where stakeholders' representatives form an integral part of the EU funds Monitoring Committee.

A preliminary security self-assessment is included in each component and enlists the measures that have a security dimension. Latvia will address cybersecurity and other digital security aspects of these measures during implementation. Overall, investments are contributing to strengthen the digital security. However, the types of controls employed to mitigate the risks are not explained in detail and the described security self-assessment is rather general. Strategic

measures mentioned in the security self-assessment would need to be closely monitored during the implementation of the plan.

The Latvian RRP includes the following cross-border projects:

- **Via Baltica 5G corridor**: Latvia has planned a series of measures that support the objectives of the EU's digital sovereignty, including investments in connectivity at European level – the VIA Baltica 5G corridor. Latvia has concluded a memorandum of cooperation with Estonia, Lithuania and Poland on the development of this corridor.
- **Baltic States' X-ray image exchange system (Baxe):** Within the framework of the reform and investment direction "Reducing the shadow economy for the promotion of fair business", the planned investments envisage the expansion of the Baltic States' X-ray image exchange system (Baxe), by connecting the uniform image exchange system of x-ray equipment in the three Baltic States.
- Latvia has identified potential linkages with **several European transnational project initiatives**, including those whose activities are expected to be co-financed under the Digital Europe Programme, e.g. Establishment of the Latvian Federal Cloud and linking the development of the National Data Sharing Platform to the Single European Data Infrastructure and Service, as well as the United Public Administration Priorities, network of European Digital Innovation Hubs, Genome Europe, etc.
- **GoLatvia project**: The development of the genomic reference of Latvian citizens will be implemented in the framework of the European Union's 1+MG initiative involving 23 European countries.

The RRP broadly outlines Latvia's communication plans. The objectives of the communication strategy are in line with the RRF Regulation and aim to raise awareness about the RRP's contribution to the Latvian and European recovery and to the twin transition. Moreover, the RRP related communication will be integrated in the overall communication strategy of EU funds, EU Funds Communication Management Group.

Latvia plans to target three main groups, consistent also with the geographical and thematic scope of the RRP: specific target audiences (potential applicants and final recipients, entities participating in the implementation of the RRP, social partners and NGOs), corporate (internal) target groups and the general public. A wide range of communication channels will aim to provide objective and comprehensive information to all the above-mentioned target groups. A single EU funds homepage (to be developed in 2021) will provide a direct access to all information and communication materials. The communication channels used will range from information sessions (workshops, conferences, trainings, press conferences), advertising, printed material, as well as social media, in line with the specificities of the target audience. It is expected that Latvia will ensure the necessary funding of all these measures.

The plan foresees a series of coordinated communication activities with the European Commission, including joint press releases, social media posts, possible events with the participation of Commissioners and members of the European Parliament. These would focus on key areas such as the greening of the Riga Metropolitan Area Transport System, improving energy efficiency in public, residential and historic buildings, climate change adaptation, digital transformation of the public administration, digitalisation and innovation of SMEs, digital skills at all levels, reducing inequality, strengthening the health infrastructure.

State aid and competition rules fully apply to the measures funded by the Recovery and Resilience Facility. Union funds channelled through the authorities of Member States, like the

RRF funds, become State resources and can constitute State aid if all the other criteria of Article 107(1) TFEU are met. When this is the case and State aid is present, these measures must be notified and approved by the Commission before Member States can grant the aid, unless those measures are covered by an existing aid scheme or comply with the applicable conditions of a block exemption regulation, in particular the General Block Exemption Regulation (GBER) declaring certain categories of aid compatible with the internal market in application of Articles 107 and 108 TFEU[9]. When State aid is present and it requires notification, it is the duty of the Member State to notify State aid measures to the Commission before granting them, in compliance with Article 108(3) TFEU. In this respect, the State aid analysis carried out by Latvia in the recovery and resilience plan cannot be deemed a State aid notification. In as far as Latvia considers that a specific measure contained in the recovery and resilience plan entails de minimis aid or aid exempted from the notification requirement, it is the responsibility of Latvia to ensure full compliance with the applicable rules.

4. SUMMARY OF THE ASSESSMENT OF THE PLAN

4.1. Comprehensive and adequately balanced response to the economic and social situation

The plan includes a balanced set of reforms and investments aimed at addressing the country's key challenges, stimulating the recovery from the COVID-19 crisis and laying the foundation for its long-term growth. The plan includes 85 measures (21 reforms and 64 investments) that are structured around the country's main challenges and the policy areas of European relevance, thus covering all 'six pillars' in a balanced way. The plan includes 6 components: green transition, digital transition, inequality reduction, health, productivity, and rule of law. The components' objectives are complementary and the reforms leverage the impact of associated investments, notably by bringing structural change and increasing the participation and financing of private agents. However, the plan is stronger on the investments side than on the reforms side. Latvia submitted its National Reform Programme on 14 April 2021. The information provided in the National Reform Programme is being considered and jointly assessed in this Staff Working Document together with the Recovery and Resilience Plan.

Overall, the plan is balanced and focuses on Latvia's main challenges: the twin transitions, social inclusion, including healthcare, social safety net and regional disparities, skills, including digital skills, adult learning, and higher education, productivity, including research and innovation and support for business investments, and administrative capacity, including tax administration, public procurement and the judicial system. As a result, the balance among the six pillars is sufficient. The coverage of the Latvian plan's components toward the six pillars is summarized in Table 5. below. **The green and digital pillars also meet the allocation targets.**

Table 5: Coverage of the six pillars of the Facility by the Latvian RRP components

	Green transition	Digital transitio n	Smart, sustainable & inclusive growth	Social and territorial cohesion	Health, and economic, social and institution	Policies for the next generati on

[9] Commission Regulation 651/2014, OJ L 187, 26.6.2014, p. 1.

					al resilience	
1. Green transition	●		●			
2. Digital transition		●	●			●
3. Inequality		○		●		●
4. Health				●	●	
5. Productivity			●			●
6. Rule of law		○			●	

Key: "●" investments and reforms of the component significantly contribute to the pillar; "○" the component partially contributes to the pillar

1st Pillar: green transition

The plan adequately covers the 'first pillar' with one main component 'green transition'.

Measures under the component 1 'green transition' directly contribute to the 'first pillar'. The aim of this component is to support the transition to climate neutrality: improvements of energy efficiency of public and private buildings, support to businesses to improve their energy efficiency, increase of the production and use of renewable energies, greening of the transport system of the Riga Metropolitan area (including developing multimodal connections to Rail Baltica and cycling infrastructure), support to increase the production of electricity from renewable sources and the modernisation of electricity transmission and distribution networks (smart grids), also contributing to the synchronisation of the Baltic electricity networks with the Continental European network.

Latvia's recovery and resilience plan puts particular focus on sustainable mobility. This is reflected by measure 1.1.1 *Riga - Transport reform*. As part of the green transition and to reduce greenhouse gas emissions in Riga, the measure 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 4 low-floor trams, 17 electric buses and 7 electric bus charging stations, construction of cycle roads).

The Plan also has a strong pillar focused on energy efficiency improvement (subcomponent 1.2). This subcomponent notably includes energy efficiency measures for multi-apartment buildings (1.2.1.1), businesses (1.2.1.2), municipal buildings and infrastructure (1.2.1.3) as well as public sector buildings, including historical buildings (1.2.1.4) with business being the largest recipient of funds. Lastly, beyond energy efficiency, this subcomponent is completed by a measure supporting the modernisation of electricity transmission and distribution networks and the deployment of renewable energy (1.2.1.5).

The Plan also has a pillar focused on climate change adaptation (subcomponent 1.3). This subcomponent consists in a fire prevention measure renovating fire rescue centres as newly built energy efficient buildings as part of an overall reform (see explanation above 1.3.1.1i. Strengthening the capacity of the rescue services). It also includes flood prevention measures including the rehabilitation of polder pumping stations, the restoration of protective dikes and of regulated sections of rivers. This contributes to the objective of climate change adaptation.

These measures contribute to the green transition and help to enhance energy efficiency.

Based on the methodology for climate tracking set out in Annex VI to Regulation (EU) 2021/241, the quantitative assessment of the plan in relation to the climate target finds a contribution of 37.6% of the total allocation, thereby complying with the minimum threshold of 37%.

2nd Pillar: digital transition

The plan adequately covers the 'second pillar', with 3 main components directly contributing to the 'digital transition'.

Measures under the digital transition component (component 2) directly contribute to the 'second pillar'. The component addresses the main digital challenges - a lack of basic and advanced digital skills and low digital integration of the businesses. Moreover, the component addresses all the aspects of the digital transformation - public and private sector, skills and connectivity. The measures planned aim to develop the necessary infrastructure, capacities and skills, improve efficiency, digital processes and data management in public administration, provide support to the digital transformation of businesses and improve connectivity. There is considerable support for digital skills which shall have a significant long-term impact on digital transformation. Measures fostering business digital transformation, and measures aimed at fostering connectivity, would also contribute to this pillar.

Some measures under the component 6 (rule of law) and component 3 (inequality) are also expected to contribute to the 'second pillar' and benefit from it. These measures address the participation in the labour market of the unemployed, job-seekers and people at risk of unemployment (3.1.2.5.i.) and modernising the technical and analytical capacities for the implementation of rule of law enforcement, including using AI solutions (6.1.1.1.i., 6.1.1.2.i., 6.1.1.3i., 6.1.2.1.i.). The accompanying digitalisation efforts of the procurement and tax reforms also contribute to the digital transformation.

Based on the methodology for digital tagging set out in Annex VII to Regulation (EU) 2021/241, the quantitative assessment of the Plan in relation to the digital target finds a contribution of 21% of the total allocation, therefore complying with the minimum threshold of 20%, with a direct contribution from 3 Components out of 6.

3rd Pillar: smart, sustainable and inclusive growth, including economic cohesion, jobs, productivity, competitiveness, research, development and innovation, and a well-functioning internal market with strong SMEs

The plan adequately covers the 'third pillar', with 3 main contributing components.

The plan's components related to green and digital transition, and productivity (i.e. components 1, 2 and 5) contribute most to the 'third pillar'. The key measures that contribute to the third pillar are the greening of Riga metro area transport system, the development of the digital services economy, the investments in basic and advanced digital skills, the investments in 5G infrastructure for automated mobility, and the grant support programmes for business investment in energy efficiency, uptake and production of renewable energy and digital solutions, as well as in innovation. These measures are expected to help improve the country's competitiveness, resilience, productivity and innovation capacity, as well as the availability of workforce. Moreover, the business support schemes are expected to benefit primarily SMEs.

Moreover, an ambitious reform of the higher education institutions is expected to achieve improvements in the quality of higher education and the universities' research output. Measures at reducing the shadow economy and measures aimed at promoting the competition for public tenders is expected to contribute to levelling the playing field. Finally, investments in affordable housing, industrial infrastructure, and roads in peripheral regions will help support territorially inclusive growth.

4th Pillar: Social and territorial cohesion

The plan adequately covers the 'fourth pillar', with 2 main contributing components.

The plan's inequality and health components (i.e. components 3 and 4) include measures that aim at improving social inclusion and addressing regional disparities. An introduction of the annual indexation of minimum income, as well as investments in social infrastructure and services (under component 3) are key measures of the plan to address social challenges. Investments and reforms aimed at improving accessibility to healthcare services (under component 4) will strengthen the inclusive provision of healthcare. Finally, a major administrative territorial reform (under component 3), which was passed in 2020 lays the foundation of Latvia's plan to provide peripheral regions with better growth opportunities and citizens with better quality local public services.

Investments and reforms in social inclusion and healthcare are expected to strengthen social cohesion and social protection. The introduction of indexation of minimum income benefits will ensure they will be annually adjusted to the median wage growth, maintaining their adequacy levels. Under the previous system, indexation of minimum income benefits followed a haphazard pattern which in practice led to their decrease in real terms over the previous 8 years. This measure is expected to improve the livelihoods of some of the most vulnerable parts of the society and therefore contribute to Latvia's social cohesion. Combined with the increase of the minimum income benefits from around 10% of the median income to 20% which was introduced starting from 2021, these measures are expected to improve Latvia's performance on the Social scoreboard, where income inequality and the impact of social transfers have been Latvia's main challenges. Furthermore, investments in health infrastructure combined with a reform aimed to attract more human resources to the sector are expected to improve accessibility of healthcare, the lack of which has predominantly affected the low-income earners and people living in peripheral areas.

The administrative territorial reform coupled with investments in affordable housing, industrial infrastructure, schools and renovation of regional roads comprise Latvia's efforts to help its lagging regions develop. There are marked income level differences within the country – with Riga and its surroundings enjoying approximately twice the income level of the rest of the country. The peripheral regions have suffered from a vicious cycle of labour emigration and diminishing work opportunities on the one hand and dwindling resources for essential public services on the other hand. Latvia's plan refers to the recently adopted administrative territorial reform, which will merge the number of municipalities from 119 to 42, thus making them stronger and better capable to ensure the provision of quality public services and to make the investments necessary to create more employment opportunities. Building on this reform, Latvia's plan includes measures that would improve public services and their accessibility, through investments in roads, hospitals, schools and some social infrastructure. Furthermore, it includes investments in affordable housing and industrial infrastructure. Investments in affordable housing should help foster labour supply for businesses in peripheral regions which has been hampered by the lack of

housing opportunities in the places with the best employment opportunities. Investments in industrial infrastructure are aimed at attracting private sector investors to these regions. Taken together, these measures make up a sizable effort of creating better growth opportunities in peripheral regions and therefore reducing regional disparities.

5th Pillar: Health and economic, social and institutional resilience, with the aim of increasing crisis preparedness and crisis response capacity, among others

The plan adequately covers the 'fifth pillar', with 2 components directly contributing.

The resilience of Latvia's health system is expected to improve as a result of the measures proposed in the component on health (component 4). As the health sector has become one of the most vulnerable during the COVID-19 pandemic, strategic investments have the potential to improve its resilience and reduce its vulnerability to shocks. The reforms and related investments planned in the RRP focus on modernising infrastructure and organisational processes to ensure greater resilience and preparedness of the health system for epidemiological crises. The reform shall put in place guidelines for integrated care and epidemiological preparedness, while complementary investments in the necessary infrastructure of three university and seven regional hospitals will support the provision of integrated health services and will raise the capacity of health institutions to adapt to crisis situations. Improved human resources development shall be ensured through better planning, new remuneration model and improved training of health professionals. The long-term impact of these reforms shall be ensured if the measures are financed over the long run.

The institutional resilience of the public administration shall be strengthened through reforms and investments included in the component on rule of law (component 6). To improve the institutional resilience and crisis response, the plan contributes to a broader reform plan for the modernisation of the public administration. The measures aim to strengthen policy development, implementation and evaluation capacity, increase transparency and integrity of public administration, attract the necessary human resources, centralise public administration support functions, and improve digital service delivery. This reform will be coupled with investments in professionalisation of public administration, training for horizontal policies, and fostering of the innovation capacity of the public sector. These actions contribute to strengthening the capacity and resilience of the public administration that in return should improve the response to crisis, and better support policy development and implementation. Furthermore, measures on strengthening NGOs (6.3.1.4.) also contribute to the 'sixth pillar', by improving representation of socially vulnerable groups in dialogue with public administration.

6th Pillar: Policies for the next generation, children and young people, such as education and skills

The plan extensively covers the 'sixth pillar', with 3 main contributing components.

Policies aiming at ensuring access to quality of education across schools and regions (component 3) shall contribute to the 'sixth pillar'. The inequality component shall support the efficiency of the network of general education institutions to ensure more equal access to quality education and bridging the urban rural divide. The mobility of students while optimising the school network shall be ensured through purchase of zero-emission vehicles for the municipalities. The

digital component includes pilot project on "computer libraries" that aim to ensure not only access to technology, but also to develop a framework for remote learning and in each municipality and to all schoolchildren.

Measures on higher education under the productivity component (component 5) shall also contribute to this pillar. A comprehensive reform of governance and financing of the higher education institutions is expected to improve their efficiency, quality, promote excellence and international competitiveness in higher education. The structural changes are set to contribute to higher quality study programmes and equip students with the knowledge and skills required for the labour market.

Measures to equip people with the skills required for the labour market, included in 2 components (components 2 and 3), shall also contribute to the 'sixth pillar'. The component 2 on digital transition includes reforms aimed to create sustainable and socially responsible system for adult learning and improved skills management framework. It is envisaged to establish new approaches for the organisation of the adult learning process, notably by piloting the Individual Learning Accounts for individual needs-based adult learning and the Skills Funds' approach to enterprise- and sector-based adult learning. Investments are planned for development of digital skills for society, including for young people. Reskilling and upskilling measures for unemployed are also included in the component 3 on reducing inequalities as part of Active Labour Market Policy investments.

Taking into consideration all reforms and investments envisaged by Latvia, its Recovery and Resilience plan represents, to a large extent a comprehensive and adequately balanced response to the economic and social situation, thereby contributing appropriately to all six pillars referred to in Article 3 of the RRF Regulation, taking the specific challenges and the financial allocation of Latvia into account. This would warrant a rating of A under the assessment criterion 2.1 in Annex V to the RRF Regulation.

4.2. Link with country-specific recommendations and the European Semester

The six components of Latvia's plan cover a broad range of Latvia's key challenges. Latvia's plan includes measures addressing to varying extent all six broad challenges stemming from 2019 and 2020 CSRs – fiscal, human capital, public administration, productivity and the twin transitions. The plan includes an extensive set of mutually reinforcing reforms and investments that contribute to effectively addressing a significant subset of the economic and social challenges outlined in the country-specific recommendations addressed to Latvia. These measures are expected to boost the growth potential of the economy in a sustainable manner. The recommendations related to the immediate fiscal policy response to the pandemic can be considered as falling outside the scope of Latvia's plan, notwithstanding the fact that Member State has generally responded adequately and sufficiently to the immediate need to support the economy through fiscal means in 2020 and 2021, in line with the provisions of the General Escape Clause. Moreover, the recommendation to achieve the medium-term budgetary objective in 2020 is no longer relevant, due both to the lapsing of the corresponding budgetary period and the activation in March 2020 of the General Escape Clause of the Stability and Growth Pact in the context of the pandemic crisis.

Fiscal

Measures aim to improve compliance and reduce the shadow economy (CSR 1, 2019). Weak tax compliance is a long-running issue in Latvia with undeclared transactions, undeclared income and tax fraud all being part of the problem. The component on rule of law through its reform and investment strand *6.1.Reducing the shadow economy to promote fair entrepreneurship* aims to address the challenge to reduce the shadow economy and improve tax collection that relates to the 2019 CSR on improving tax compliance. *A National Institutions Work Plan for Restraining the Shadow Economy for 2021-2022* will be adopted and will address unregistered and illegal economic activity, undeclared employment, tax fraud and others. Investments will strengthen the analytics and data management in the field of tax administration and customs. The CSR on reducing taxation for low-income earners by shifting it to other sources (CSR 1, 2019) is not addressed in the plan.

Further steps are taken to strengthen the anti-money laundering (AML) framework (CSR 1, 2019 and 4, 2020). The anti-money laundering system was overhauled in 2018. In particular, Latvia banned the servicing of non-resident shell companies and amended a number of laws. The capacity and capability of key supervisory, financial intelligence and law enforcement institutions was strengthened. Supervision of financial institutions has been tightened considerably. However, most reforms so far have been aimed at the financial sector. Less attention has been paid to recognise money laundering of domestic origin, which takes place mostly outside of the banking sector, e.g. through purchases of real estate, cars or other liquid valuables. Moreover, the police capacity has not received the level of attention that it deserves in this context. The plan is expected to continue work on the implementation of the AML strategy by reforming the cooperation, information exchange and training systems between law enforcement agencies involved in the identification, investigation and trial of economic crimes, while strengthening their technical capacity. In addition, it is planned to strengthen the capacity of civil society organisations, in particular, to improve the representation of interests of vulnerable groups.

Human capital

Investments in healthcare partly address concerns about access, quality and integration across care levels. Low public spending and unhealthy lifestyle choices are the main reasons for the population's poor health outcomes. Timely and equal access to healthcare is limited. There is a shortage of health workers in Latvia, in particular nurses, which hinders the provision of health care and threatens the success of health reforms. Spending on health in Latvia remains among the lowest in the EU. Despite recent boosts in government spending on health, further financing and a sustainable solution for it is needed to address the longstanding shortcomings in health care. These challenges have been exacerbated in particular by the crisis caused by the COVID-19 pandemic. The component on health partly addresses the challenges related to resilience, accessibility, quality and cost-effectiveness of the health system and its human resources (CSR 2, 2019, CSR 1, 2020). The health component aims to improve the resilience, accessibility and quality of healthcare through two key reform strands – integrated healthcare and strengthening the health workforce. The new remuneration model for healthcare staff shall include a transparent wage calculation mechanism and streamlines the wages across the health sector contributing to improving the availability and quality of services. Significant investments are planned for the infrastructure in university and regional hospitals, as well as in secondary outpatient settings, with the goal of providing integrated health services, reducing the spread of infectious diseases and meeting epidemiological requirements. The component does not contain measures for sustainable increase of the healthcare financing from the national budget (CSR 1, 2020). Complementary measures will

also be funded by the State budget and the Cohesion Policy funds, e.g. in primary care, disease prevention, eHealth and healthcare workforce, which will help address the CSRs further.

Poverty reduction and social inclusion are addressed through reforms and investments, albeit their scope and ambition could be further scaled up. The risk of poverty and social exclusion in Latvia is high, especially for vulnerable groups. In 2021, some progress has been noted on the 2019 CSR 2 to address social exclusion, notably by improving the adequacy of minimum income benefits, and the 2020 CSR 2 to strengthen the social safety net. The plan seeks to further improve the minimum income support system, including through an annual indexation mechanism and setting the threshold at 20% of median income, but it still remains below the poverty threshold. Other investments in accessibility and rehabilitation infrastructure for persons with reduced mobility and disabilities, as well long-term care investments for elderly will also contribute to achieving some progress of the above CSRs and fight social exclusion. The investment on growth of NGOs also contributes to addressing the 2019 CSR 2 on social exclusion and 2020 CSR 2 on strengthening the social safety net. The measure is welcome and a novel element in the current approach to inclusion of social vulnerable groups in Latvia.

The quality and efficiency of the education system (CSR 2, 2019) is expected to be improved through reforms in general and higher education. The education system faces a challenge to consolidate resources while improving quality and efficiency. While Latvia's education system performs well in terms of learning achievement, access to quality education remains dependent on the place of residence and type of school. At the same time, the implementation of a major school network reform was postponed and the higher education system remained fragmented. The plan addresses the challenges linked to the general education through the component on reducing inequality. It commits the entry into force of a legal framework that will establish quantitative and qualitative criteria for creating general secondary education establishments. As a result, it aims to create a network of general secondary education institutions in line with the demographic situation and reduce urban-rural divide in access to quality education. Infrastructure of 20 schools will also be improved and further investments are planned in the framework of the Cohesion Policy. The component on productivity puts forward an ambitious reform in higher education that focuses on consolidation, modernising the governance and financing model of the higher education institutions. The implementation is supported with investments in the development of human capital through research and development grants. It is a significant contribution to an overall transformation of the human resources' system in R&I and to the improvement of higher education sector, including thanks to specialisation and research grants. It is therefore likely that the reform – once completed – would contribute substantially to the implementation of the CSR.

Reforms and investments aim to ensure the skills, including digital skills, necessary for the labour market (CSR 2, 2019, CSR 2, 2020). Adult participation in learning and the involvement of the unemployed in active labour market measures is lower than the average of the European Union. Digital skills are insufficient at all levels, from basic to advanced. The low level of digital skills among the labour force limits the use of digital technologies by businesses and the potential for innovation. The CSRs are covered to a large extent as there is a strong focus on digital skills (all levels) and adult learning, albeit not targeting the low-skilled (CSR 2, 2019). The digital transition component envisages reforms that would ensure the necessary skills for the labour market through creating sustainable and socially responsible system for adult learning and improved skills management framework. Pilot projects for development of individual learning accounts and enterprise and sector-based skills funds aim to remove barriers in access. Investments

are planned for the development of digital skills at all levels, developing the digital capacities of enterprises and investing in improving the digital skills of the public administration. Reskilling and upskilling measures for unemployed are included in the component on reducing inequalities as part of active labour market measures. These measures are also aligned with the flagship *reskill and upskill* included in the Commission's Annual Sustainable Growth Strategy (COM/2020/575) and are complemented with funding from cohesion policy.

Public administration and regional disparities

Latvia's rule of law component includes reforms aimed at strengthening the accountability and efficiency of public sector (CSR 4, 2020). The reforms are aimed at increasing the efficiency of tax administration, strengthening the competencies of the justice system, modernising public administration and improving the quality and efficiency of public procurement. The plan includes a reform entailing the centralisation of public administration support functions as well as investments in training to improve the capacity. The measures are part of a broader reform which aims at a more efficient, better motivated, innovative and competent public administration addressing the CSR to a large extent. The creation of a justice school shall improve the training for the justice system and strengthen their competences and capacity to fight crime. The measures also 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 concluded.

The plan builds on the administrative territorial reform to tackle regional disparities (CSR 3, 2019). There are significant regional differences in mobility and economic development, in the accessibility of public (health, education, administrative) services and integration with centres of economic activity of the surrounding (functional urban) marginalised territories. In 2020 the Parliament approved the administrative territorial reform, which aims to reduce the number of local governments to 119 to 42 with the aim of creating economically viable administrative areas. In order to address the above-mentioned challenges, substantial investments are planned in the renovation of roads, industrial parks, municipal transport, schools and affordable housing. The latter will also contribute to 2019 CSRs 2 and 3 on improved quality of education system and affordable housing respectively.

Investments in affordable housing (CSR 3, 2019) aim to remove barriers in labour mobility. Lack of affordable housing is among the chief barriers to labour mobility and regional development. The plan aims to ensure a substantial progress on the 2019 CSR 3 on provision of affordable housing and investment-focused policies taking regional disparities into account. The component on inequality reduction includes the strategic framework on housing accessibility and entry into force of a new rental law ensuring a fair balance between the interests of the tenant and the landlord. Significant investments are planned to develop a new financial instrument to incentivize the construction of subsidized rental housing units in the regions to attract qualified labour force. This provides a good basis for further measures to address the severe housing deprivation in Latvia (among the highest in Europe), including with a national strategy for social housing and homelessness. Social housing is not covered by the RRP and remains part of 2021-2027 Cohesion Policy framework.

Productivity

The measures on research and innovation (CSR 3, 2019) aims to increase productivity, lead to considerably higher R&D investments, boost competitiveness and foster cooperation. Latvia's key innovation-related challenges are low innovation investment, particularly in the

private sector, a shortage of highly-skilled human resources, and the fragmentation of innovation system governance. The plan addresses the CSR to focus investment-related policy on innovation. Latvia's ambition is to pursue an ecosystem-based innovation policy that would offer support throughout the entire life cycle of innovation process, seek close cooperation between the system's key stakeholders, and aim to improve the conditions for higher R&D investment by the private sector. The investments are planned for increasing the highly-skilled human resources in R&D, for the development of innovation clusters that would develop R&D capacity in enterprises, increase digital skills, promote cooperation of all representatives and increase the share of innovative enterprises in the economy, thereby promoting the volume of private R&D and the return on public investment. In the context of the modernisation of the public administration, it is also planned to foster the innovation culture and increase the innovation output within public administration.

Green transition

Investments in sustainable transport, energy efficiency, and climate change adaptation as well as reforms fostering investment in renewable energy are expected to contribute to address Latvia's climate challenges (CSR 3 2019, CSR 3, 2020). Latvia's main green transition challenges are to reverse the trend of growing energy consumption in transport and buildings as well as to continue increasing the share of renewable energy in its energy consumption. The Riga transport reform plans investments in greening urban rolling stock, improving public transport infrastructure and constructing cycling lanes which are expected to contribute to both increasing the share of renewable energy used and reducing energy consumption in transport, both pertinent challenges to Latvia. Investments in energy efficiency renovations of public and multi-apartment buildings will contribute to reducing their energy consumption. Investments in modernising electricity grids aimed at facilitating development of microgeneration and extending the electric charging infrastructure to densely populated areas will help promote renewable energy use both in housing and transport. Moreover, Latvia has committed to study ways to reduce the legal uncertainty for investments in wind energy. Coupled with measures to boost their acceptability among population, the planned measures will help boost private investment in wind energy, which is crucial to Latvia's ability to reach its 2030 renewable energy targets. Furthermore, a support instrument to businesses will support a variety of climate friendly investments, including R&D for innovative products and technologies linked to the low carbon economy, climate change mitigation and adaptation. Finally, investments are planned in anti-flood infrastructure. According to the plan's estimates, the investments will yield 36 241 tonnes of savings in CO2 equivalent emissions and 49.8 GWh of primary energy savings. This amounts to 0.3% of Latvia's total CO2 emissions and 0.1% of Latvia's primary energy consumption, respectively. The estimates are admittedly cautious as they take into account only the direct effects of investments and do not consider the impact of reforms or synergies of the measures.

Digital transition

Latvia's key digital challenges – poor skills, insufficient rural connectivity and low level of business digitalisation, are duly covered by Latvia's plan. Low basic digital skills among the working age population, insufficient uptake of digital solutions by businesses, as well as a shortage of ICT specialists are Latvia's key digital challenges, impacting on workforce availability, competitiveness, resilience, use of government e-services and innovation alike. Latvia's plan includes sizeable investments in basic and advanced digital skills that so far are keeping back Latvia's digital transition. Latvia's plan also includes measures for the digital modernisation of public administration and the digital transformation of providing public services, including centralised public solutions. Latvia addresses the digital CSRs (CSR 3, 2019, CSR 3, 2020) also

by supporting the digital transformation of businesses, in particular SMEs and creating a better environment for R&D as well as by creating the necessary framework for Latvia's participation in the network of European Digital Innovation Hubs. Most urban areas in Latvia have excellent digital infrastructure, but fixed broadband take-up in rural areas, especially last-mile connections, is low. The plan includes continued and strengthened efforts to deploy very high-speed broadband that will help further improve the digital infrastructure. Investments in digital infrastructure in all regions of Latvia will also be financed from other EU funds. These measures are also aligned with the flagship *modernise, connect* and *scale up* included in the Commission's Annual Sustainable Growth Strategy (COM/2020/575).

Response to the economic and social situation

The recovery and resilience plan represents to a large extent a comprehensive and adequate response to the economic situation of Latvia. Continued convergence remains Latvia's key challenge both in terms of improving its population's living standards and halting emigration. Reforms and investments are needed to diversify the economy, increase its level of technical advancement to generate higher value-added and make it more resilient and competitive, strengthen the investment in research and innovation and human capital and alleviate the socio-economic costs of the twin transition. The plan provides a comprehensive response to these challenges. In addition, Latvia's business environment will also benefit from reforms and investments aimed to reduce the shadow economy and improve tax collection and those aiming to increase the availability of skilled workforce and stepping up efforts to improve the quality and availability of public services provided digitally. The plan aims to improve participation in adult learning through sustainable and socially responsible system and better skills management. Investments are envisaged for upskilling and reskilling measures, including digital skills that aim to equip the workforce with necessary skills needed for the labour market. Labour market participation will be strengthened through investments in active labour market policies. Increased affordable housing provision aim to improve regional labour mobility. High risks of poverty and social exclusion are addressed through reform to improve the adequacy minimum income support, investments in long-term care for the elderly, accessibility infrastructure and rehabilitation services for people with disabilities. To address the inequalities of opportunity, reforms and investments are planned to improve the access to healthcare and access to quality education in regions. Policies to support the country's digital and green transition should take into account the significant regional disparities. Improving intermodal transport infrastructure within and around Riga would both facilitate labour mobility and help curb growing energy consumption from passenger cars. Measures are planned to address the structural weaknesses of the current innovation policy model, strengthening research and innovation.

Growth potential

The challenges addressed by the plan would ensure a significant boost to the growth potential of the Latvian economy in a sustainable manner. Increasing productivity is a common thread across several components, namely, component 2 on digital transition, component 3 on reducing inequalities and component 5 on productivity. The planned measures shall contribute to addressing the structural weaknesses of the current innovation policy model and thus have a long-lasting positive impact. In this regard, the long-term sustainable financing model will be key. Complementary investment in research and innovation is also foreseen under the component 1 on green transition, where support will be directed towards research and development of innovative

products and technologies linked to the low carbon economy, climate change mitigation and adaptation and thus contributing to achieving the objectives of the European Green Deal. The digital transition component envisages reforms and investment that would ensure the necessary skills for the labour market through creating sustainable system for adult learning and investments in digital skills for transformation of society and government. With regard to the inclusiveness, the component on reduction of inequalities includes investments in training of the unemployed, which will allow for the expansion of active employment measures financed from the national budget and other EU instruments, as well as improve the skills of the Latvian population in general.

Taking into consideration the reforms and investments envisaged by Latvia, its recovery and resilience plan is expected to contribute to effectively addressing all or a significant subset of challenges identified in the country-specific recommendations, or challenges in other relevant documents officially adopted by the Commission under the European Semester, and the recovery and resilience plan represents an adequate response to the economic and social situation of Latvia. This would warrant a rating of A under the assessment criterion 2.2 in Annex V to the RRF Regulation.

Table 6: Mapping of country challenges identified in 2019-20 country-specific recommendations and the Latvia's RRP components

Country challenges (as identified in Section 2)	Associated CSR (2019-2020) and European Semester recommendations	Component 1- Green transition	Component 2: Digital transition	Component 3: Reduction of inequality	Component 4: Healthcare	Component 5: Productivity	Component 6: Rule of law
Fiscal sustainability							
Improve tax compliance	2019.1.2, 2020.1.1						○
Financial sector							
Strengthen anti-money laundering framework	2020.4.1 and 2019.1.3						●
Healthcare							
Resilience, accessibility, quality and cost-effectiveness of the healthcare system	2020.1.2 and 2019.2.3				●		
Additional human and financial resources to healthcare sector	2020.1.2				○		
Education							
Quality and efficiency of the education system	2019.2.2			●		●	
Training of low-skilled and adult learning	2020.2.4 and 2019.2.2		○				
Skills, including digital skills	2020.2.4 and 2019.2.4		●	○			
Social inclusion							
Strengthen the social safety by increasing minimum social benefits	2020.2.1 and 2019.2.1			○			
Active labour market policies	2020.2.4 and 2019.2.3			●			
Research and innovation							
Low innovation performance	2020.3.4. and 2019.3.1.					●	
Investment							
Digital transformation and infrastructure	2020.3.7., 2019.3.5.		●	○	○	○	○
Sustainability, resource efficiency and energy efficiency of transport	2020.3.6, 2019.3.3.	●		○			
Clean and efficient production and use of energy	2020.3.5, 2019.3.4.	●					
Affordable housing	2019.3.2.			●			
Public administration and business climate							
Accountability and efficiency of public administration	2019.4.1.						●
Regional disparities	2019.4.1.			●	○		

Key: "●" investments and reforms of the component significantly address the challenge; "○" the component partially addresses the challenge

4.3. Growth potential, job creation, economic, institutional and social resilience, European Pillar of Social Rights, mitigating the impact of the crisis, and social territorial cohesion and convergence

The plan aims to accelerate Latvia's economic recovery by increasing aggregated demand through investments and reforms. The main objectives of the plan are to improve Latvia's growth potential, job creation, and economic, social and institutional resilience that will ultimately reduce the country's vulnerability to shocks. The plan is also aimed at contributing to the implementation of the European Pillar of Social Rights, including through the promotion of policies for children and youth, and to mitigating the economic and social impact of the COVID-19 crisis, thereby enhancing the economic, social and territorial cohesion and convergence within the Union.

Fostering economic growth and jobs

The plan's estimated impact on GDP and employment is notably cautious. Latvia's plan estimates its impact on cumulative GDP growth to be 0.6% in 5 years and 1.5% in 20 years. Its impact on employment is estimated at 0.2% and 0.7% in 5 and 20 years, respectively. The model used to assess the quantitative impact assumes both demand and supply side effects of the planned investment, however it does not consider the impact of reforms. Moreover, the model assumes some replacement of baseline public investment. The plan's medium-term impact appears slightly cautious given the plan's size of around 6% of GDP. Spread over 5 years and assuming some investment replacement effects as well as some import leakage, the demand effects, which are expected to dominate at the 5-year mark, appear reasonable. However, the time profile of the GDP impact assessment points to an inexplicably low impact in the first years of the plan's implementation. The supply side effects, measured at the 20-year mark, translate to 0.07% of additional annual GDP growth that results from initial investment worth around 6% of GDP, which implies a rather cautious return on investment. The main contributions to both economic growth and employment are expected to come from investments in the green and digital transitions as well as investments in social inequalities and territorial cohesion. In the long term, these three areas are projected to generate nearly three quarters of the overall contribution to the higher growth and employment potential. Overall, the plan's quantitative assessment of its economic and employment impact is cautious.

Latvia's Stability programme for 2021 points to a clear macro-additionality of Latvia's plan. The average public investment level in the three years before the crisis was 5.1% of GDP. It occurred during an upswing of EU-financed investments and therefore represents the high side of Latvia's public investment level. According to Latvia's Stability Programme, the public investment level is expected to be significantly above the pre-crisis level at 5.9% of GDP on average over 2021 to 2024. Total public expenditure reaching 42.6% of GDP for years 2021 to 2024 is also forecast to significantly exceed the pre-crisis levels of 38.8% of GDP on average over 2017 to 2019.

Box 2. Stylised NGEU impact simulations with QUEST – Latvia

Model simulations conducted by the Commission using the QUEST model show that the economic impact of the NGEU in Latvia could lead to an increase of GDP of between 1.3% and 2.0% by 2026[1]. After 20 years, GDP could be 0.7% higher. Spillovers account for a large part of such impact.

According to these simulations, this would translate into up to 7,000 additional jobs. Cross border (GDP) spillovers account for 0.5 pps in 2026, showing the value added of synchronised expenditure across Member States (line 2). Even in a scenario with a lower productivity of NGEU funds, it would still lead to a significant impact (line 3)[2].

Table 1: QUEST simulation results (%-deviation of real GDP level from non-NGEU case, linear disbursement assumption over 6 years)

Scenario	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030	2040
Baseline	1.1	1.8	1.8	1.8	1.9	2.0	1.5	1.0	1.1	1.1	0.7
of which spillover	0.4	0.5	0.5	0.5	0.5	0.5	0.4	0.3	0.3	0.2	0.0
Low productivity	0.8	1.4	1.3	1.2	1.3	1.3	0.8	0.3	0.3	0.4	0.3

This stylised scenario does not include the possible positive impact of structural reforms, which can be substantial. A model-based benchmarking exercise shows that undertaking structural reforms that would result in halving the gap vis-à-vis best performers in terms of indicators of structural reforms could raise Latvian GDP by around 11% in 20 years time, in line with findings for the EU average[3].

Due to the differences in the assumptions and methodology, **the results of this stylised assessment cannot be directly compared to the numbers reported in chapter 4 of Latvia's RRP.**

[1] RRF amounts to roughly 90% of NGEU, which also includes ReactEU, Horizon, InvestEU, JTF, Rural Development and RescEU.
[2] Technically, the low productivity scenario considers a significantly reduced output elasticity of public capital.
[3] Varga, J, in 't Veld J. (2014), "The potential growth impact of structural reforms in the EU: a benchmarking exercise" ,European Economy Economic Papers no. 541.
http://ec.europa.eu/economy_finance/publications/economic_paper/2014/pdf/ecp541_en.pdf.

Investments in human capital, digital capacities, innovative capacity and public transport are expected to have the largest impact on the economy's long-term potential. Latvia's plan foresees investments and reforms aimed at boosting the population's skills, which have been among Latvia's key challenges as evidenced by high unemployment rate differences between the high and the low skilled. There has also been a recurring trend of shortages of qualified workforce and tight labour supply, aggravated by aging and declining population and emigration. Achieving a structural improvement in the workforce's skills composition has the potential to provide a boost to the use of digital solutions, innovation, services exports and spur regional development. Furthermore, investments in modernising public IT infrastructure, support for business digitalisation as well as investments in 5G passive infrastructure on the one hand and investment in digital skills on the other hand are expected to lead to synergies that have the potential to boost the country's capacity for use of digital solutions. Moreover, support for private R&D investments are aimed at creating sustainable innovation ecosystems that will boost Latvia's innovation capacity in the long term. Finally, the reform of the governance of the Riga metro area public transport system as well as its associated investments are aimed at improving public transport's attractiveness and achieve a higher proportion of mobility needs being served by public transport. This will not only limit the rise in energy consumption due to increasing use of private cars, but also improve access to services, labour mobility and transport productivity. If achieved, such an

outcome would improve the competitiveness of the Riga metro area and therefore increase its growth potential.

The broad-ranging reform of the higher education aims to boost the quality and efficiency of higher education and deliver better skills to Latvia's population in the longer term. Latvia's higher education sector is characterised by a large number of small higher education institutions (HEIs) that are underfunded. As a result, most HEIs lack resources to deliver good quality education and to create critical mass for high quality research. The reform of the higher education system consists of several elements – changes to the governance of the HEIs, changes to the accreditation mechanism and funding principles, as well as instruments to incentivize consolidation among the HEIs. The changes in the governance will separate HEIs' administrative and academic management and thus make them more transparent, efficient and open. The introduction of HEIs typologies and cyclical accreditation combine with the changes to the financing model are expected to ensure higher standard of HE programmes and better alignment of HEIs' incentives with their academic performance. Finally, the RRP will finance grants that will incentivise HEI mergers, which should help concentrate the scarce resources both in higher education and academic research. Altogether, the proposed reforms should improve Latvia's skills level and innovative capacity over medium term and beyond.

The substantial construction works related to the plan's green transition, health and inequality components are expected to foster job creation over the medium term. Investments in bike lines, mobility hubs, tram line extensions, buildings' energy efficiency, fire rescue centres, flood protection infrastructure, hospitals and ambulatory care facilities, road renovation, industrial parks, affordable housing, social facilities and customs facilities will involve major construction works which will considerably boost labour demand during their implementation. The volatility of public investments has in the past caused adverse effects on the construction sector which had to downsize or ramp up its capacity depending on the demand. Therefore, in order to avoid these adverse effects, it is crucial that the RRF-funded investments are integrated within the broader public investment planning, including other EU-funded investments.

Strengthening social cohesion

Investments and reforms in social inclusion and healthcare are expected to strengthen social cohesion and social protection. The introduction of the indexation of minimum income benefits will ensure they will be annually adjusted to the wage growth and thus their adequacy levels maintained. Under the previous system, indexation of minimum income benefits followed a haphazard pattern which in practice led to their decrease in real terms over the previous eight years. This measure is expected to improve the livelihoods of some of the most vulnerable parts of the society and therefore contribute to Latvia's social cohesion. Combined with the increase of the minimum income benefits from around 10% of median income to 20% which was introduced starting from 2021, these measures are expected to improve Latvia's performance on the Social scoreboard, where income inequality and the impact of social transfers have been Latvia's main challenges. Furthermore, investments in health infrastructure combined with a reform aimed to attract more human resources to the sector are expected to improve accessibility of healthcare, the lack of which has predominantly affected the low-income earners and people living in peripheral areas. The plan is expected to also contribute to the implementation of several principles of the European Pillar of Social Rights (EPSR), such as education, training and life-long learning; active support to employment; minimum income; right to timely access to affordable, preventive and curative health care of good quality; inclusion of people with disabilities; long-term care; access to essential services.

Latvia's plan contains some measures that are expected to contribute to addressing the country's challenges in the area of gender equality and equal opportunities for all. The plan foresees an investment to address specific needs of persons with disabilities, such as ensuring accessibility of public and private buildings. In addition, all new public transport vehicles will be equipped with easy access for older persons and persons with reduced mobility.

The situation of socially vulnerable groups is addressed in several parts of the plan, such as in those dealing with health. The plan also includes measures to improve educational opportunities for school children.

As regards gender equality, the plan includes measures aiming specifically at women's engagement in ICT career opportunities, with a view to increase the gender balance among ICT specialists. The labour market situation for female jobseekers is expected to be improved by targeted measures aiming at the promotion of reconciliation of work and family life through the creation of remote and part-time work opportunities for parents with children.

The plan foresees that the management and implementation of projects ensure equal pay for work of equal value for women and men and diversity in management. In addition, the selection process of projects will be subject to the principle of non-exclusion and the obligation to combat any discrimination based not only on sex, but also on grounds of race or ethnic origin, religion or belief, disability, age, and sexual orientation.

Reducing vulnerabilities and increasing resilience

Sound fiscal and economic policy over the past decade have ensured Latvia's macroeconomic resilience in face of the COVID-19 pandemic. Latvia entered the pandemic with low budget deficit and a public debt level below 40% of GDP. Its current account had remained broadly balanced over the previous 5 years and private sector debt level at 90% of GDP was also among the lowest in the EU. The strong macroeconomic fundamentals meant Latvia could increase public debt to support the economy during the shutdowns and the private sector also remained resilient to the temporary drop of income. Its main macroeconomic challenge was related to the rapid wage growth caused by declining labour supply. This led to a fairly rapid appreciation of unit labour costs, which in turn threatened Latvia's price competitiveness. The falling labour supply is part of a broader set of challenges related to Latvia's demographic composition and the response to these challenges is closely linked with Latvia's long-term productivity growth, reduction of social and regional inequalities. Latvia's plan contains measures addressing all three of these areas, as discussed in the relevant sections of this assessment.

Latvia's plan includes a number of reforms aimed at addressing challenges related to its capacity for effective policy implementation and fostering a growth-friendly business environment. Latvia's rule of law component includes most of the plan's key reforms – increasing the efficiency of tax administration, strengthening the competencies of the justice system, modernizing public administration and improving the quality and efficiency of public procurement. Moreover, the reform measures aimed at fostering private investments in wind energy, discussed above, are also expected to contribute to the effectiveness of policy implementation.

Measures aimed at reducing the size of shadow economy and therefore generate more budget revenue and contribute to a fairer and more competitive business environment. The measures aimed at improving the tax administration include drawing up an action plan for fighting tax evasion and fraud, introducing a taxpayer segmentation system and adjusting the audit and control practices to better target the risk of non-compliance. The plan also includes investments in research

of taxpayer behaviour that would be used to design a more effective policy response. Altogether, the measures are expected to yield better tax compliance and a more efficient tax administration. Better tax compliance should lead to improved conditions for competition and business investment through higher credit growth and help fund needed social and health programmes.

Investments into training for the justice professionals will strengthen the system's capacity to address crime and support a growth-friendly business environment. The introduction of a justice school would unify the training of all judges, prosecutors, staff of courts and public prosecution offices, and specialised investigators under the roof of a single institution. This will allow to set coherent training objectives, develop unified training programmes, enhance exchange of experience among the different branches of the judicial system, and allow for better quality training through better resource efficiency. Over the medium term this improvement should lead to a strengthened justice system's capacity to fight crime and economic crime, in particular. To this end, it would however be important that the judiciary itself be involved in the governance, supervision and setting of priorities of the new Justice School, in line with European standards. Latvia faces several challenges related to economic crime – tax evasion and fraud, smuggling, and money laundering. Moreover, inefficient and unpredictable treatment of insolvency cases in the wake of the previous crisis was a major challenge until a few years ago when the system was reformed. Therefore, a competent, efficient and adequately equipped justice system is crucial to fostering trust in Latvia's business environment.

Steps to modernise public administration will help build Latvia's capacity to deliver better policy and its implementation. In the wake of the COVID-19 crisis Latvia's response to the health crisis, economic support and containment policy was made more difficult by insufficient capacity, expertise and experience in dealing with health crisis of such scale and its economic and social consequences and ensuring efficient and timely inter-institutional coordination of the response to the crisis. This was particularly evident during the onset of the second wave of the pandemic in autumn of 2020. In this context, it is particularly pertinent to address the weaknesses of the public administration. The plan includes a reform entailing the centralisation of public administration support functions. Moreover, it includes the development of a new framework and investments in training for horizontal competencies like ethics, integrity and anti-corruption as well as specialised competencies like policy design, project management, procurement and others. Furthermore, it includes measures to strengthen the public innovation capacity through adjusting the legal framework, attracting the necessary human resources as well as investing in infrastructure. These measures form a part of a broader plan for the modernisation of public administration, which will also be delivered as part of the plan and which will include a comprehensive plan to achieve a more efficient, better motivated, innovative and competent public administration.

Provisions to improve the legal framework to foster competition, improve capacity of procurers, and measures to improve efficiency are expected to make Latvia's public procurement system more effective and resilient. Latvia's public procurement system generally performs well on key parameters like transparency, efficiency, award criteria, and others. However, it has a relatively high share of tenders with only a single bidder and the system has occasionally found it challenging to deal with high value and complex procurement projects often due to lack of adequate capacity of public procurers. Latvia's plan includes measures aimed at addressing those weaknesses as well as improvements in areas where it already performs well. Stricter requirements for procurers to conduct market consultation should lead to more competitive bidding for public contracts. A standardised competency and training framework should improve the overall competency of public procurers and lead to better quality outcomes, especially for the more

complex projects. Latvia also plans to improve the transparency of its system by introducing new disclosure requirements. Finally, Latvia will study the best approach to centralising procurement and depending on the results of the study will centralising procurement in certain areas. The measures included in Latvia's plan should lead to overall improved quality, efficiency and integrity of its public procurement system and will help with the quality of implementation of the plan itself.

Cohesion and convergence

Territorial administrative reform coupled with investments in affordable housing, industrial infrastructure, schools and regional roads comprise Latvia's efforts to help its lagging regions develop. Latvia 's income level remains significantly below EU average, besides there are marked income level differences within the country – with Riga and its surroundings enjoying approximately twice the income level of the rest of the country. The peripheral regions have suffered from a vicious cycle of labour emigration and diminishing work opportunities on the one hand and dwindling resources for essential public services on the other hand. Latvia's plan refers to the recently adopted administrative territorial reform, which will merge the number of municipalities from 119 to 42, thus making them stronger and better capable to ensure provision of quality public services and to make the investments necessary to create more employment opportunities. Building on this reform, Latvia's plan includes measures that would improve public services and their accessibility, through investments in social infrastructure, schools, hospitals and roads. Furthermore, it includes investments in affordable housing and industrial infrastructure. Investments in affordable housing should help foster labour supply for businesses in peripheral regions which has been hampered by lack of housing opportunities in the places with the best employment opportunities. Investments in industrial infrastructure are aimed at attracting private sector investors to these regions, but should be based on the assessment of the local potential, a thorough mapping and take into account integrated regional development strategies. Taken together, these measures make up a significant effort of creating better growth opportunities in peripheral regions and therefore reducing the regional disparities.

Taking into consideration all reforms and investments envisaged by Latvia, its recovery and resilience plan is expected to have a high impact on strengthening the growth potential, job creation, and economic, social and institutional resilience of the Member State, on contributing to the implementation of the European Pillar of Social Rights, including through the promotion of policies for children and youth, and on mitigating the economic and social impact of the COVID-19 crisis, thereby enhancing the economic, social and territorial cohesion and convergence within the Union. This would warrant a rating of A under the assessment criterion 2.3 of Annex V to the RRF Regulation.

Box 3: Employment and social challenges in light of the Social Scoreboard accompanying the European Pillar of Social Rights

The Social Scoreboard supporting the European Pillar of Social Rights points to a number of employment and social challenges in Latvia. The COVID-19 crisis has slowed down the positive economic and labour market developments observed in Latvia in the past years, and risks leading to an increase in the share of people at risk of poverty or social exclusion. While the employment rate remained among the highest in the EU in 2020 (77.0 % vs 72.4% EU average), the unemployment rate has increased significantly to 8.1 % from 6.3 % in 2019 (EU average: 7.1%). Although increasing, net earnings of a full-time single worker on average wage remain weak. Access to affordable healthcare is a challenge and self-reported unmet needs for medical care are still high, although decreasing.

Social Scoreboard for LATVIA

Equal opportunities and access to the labour market	Early leavers from education and training (% of population aged 18-24) (2020)	Best performers
	Youth NEET (% of total population aged 15-24) (2020)	Best performers
	Gender employment gap (2020)	Good but to monitor
	Income quintile ratio (S80/S20) (2019)	Critical situation
	At risk of poverty or social exclusion (in %) (2019)	Critical situation
Dynamic labour markets and fair working conditions	Employment rate (% population aged 20-64) (2020)	Better than average
	Unemployment rate (% population aged 15-74) (2020)	To watch
	Long term unemployment (% population aged 15-74) (2020)	On average
	GDHI per capita growth (2019)	On average
	Net earnings of a full-time single worker earning AW (2019)	Weak but improving
Social protection and inclusion	Impact of social transfers (other than pensions) on poverty reduction (2019)	Critical situation
	Children aged less than 3 years in formal childcare (2019)	On average
	Self-reported unmet need for medical care (2019)	Weak but improving
	Individuals' level of digital skills (2019)	Critical situation

Critical situation | To watch | Weak but improving | Good but to monitor | On average | Better than average | Best performers

Update of 29 April 2021. Members States are classified on the Social Scoreboard according to a statistical methodology agreed with the EMCO and SPC Committees. It looks jointly at levels and changes of the indicators in comparison with the respective EU averages and classifies Member States in seven categories. For methodological details, please consult the Joint Employment Report 2021; NEET: neither in employment nor in education and training; GDHI: gross disposable household income.

Despite the pandemic, Latvia has improved in terms of its rate of young people not in education, employment or training (NEET). The figure decreased from 7.9 % in 2019 to 7.1% in 2020 and is now among the best performers in the EU (average 11.1%). This was achieved through upskilling measures for students and a temporary unemployment benefit for young graduates during the pandemic in 2020. At the same time, while the overall rate of early school leavers remains well below the EU average (7.2% vs 10.1 % in 2020), rural-urban disparities (11% in rural areas) are present alongside more general regional inequalities. Latvia's gender employment gap remains among the lowest in the EU with over 75% of women in employment.

Although improving, several social inequality indicators remain critical. Disparities continue to persist in employment across regions and skills levels as the situation worsens for the unemployed, older people and persons with disabilities. Income inequality (S80/S20) is among the highest in the EU, despite a slight decrease from 6.8 in 2018 to 6.5 in 2019. Risks of poverty or social exclusion remain critical, alongside self-reported unmet needs for medical care, despite a small improvement. At the same time, the impact of social transfers (other than pensions) in reducing poverty remains low. Finally, the share of individuals with basic digital skills dropped to 43% in 2019, reversing the previous trend of approaching the EU average of 56%.

Access to social housing remains limited. The availability of social housing continues to be scarce and waiting lists are long due to limited funding and lack of a strategic approach. Government support for low-income households to improve access to housing includes mainly housing allowances (covering rent payment and payment for utilities) but the coverage is low. The share of people facing severe housing deprivation (12.7 % vs. the EU average of 3.8 %) and that of people facing overcrowding are among the highest in the EU.

The Recovery and Resilience Plan submitted by Latvia addresses some of the social and regional inequalities, skills, labour market and health-related challenges relevant for the implementation of the Pillar. The Plan includes measures in support of the administrative territorial reform, the minimum income reform (including annual indexation), and healthcare reform. Special attention is paid to reskilling and upskilling, including piloting of Individual Learning Accounts and improving digital skills for all groups of the population. Although some actions targeting long-term care and improved accessibility for persons with disabilities are foreseen, their ambition does not match the considerable needs for social investments, even with additional funding from cohesion funds. The healthcare component is organized around two reforms - integrated healthcare and strengthening the health

workforce. The investments seek to improve accessibility, quality and resilience of healthcare, notably by upgrading the hospital and outpatient clinic infrastructure, including in the regions. The component does not entail commitments for a sustainable solution to increase healthcare financing from the national budget.

To mitigate the negative impact of the COVID-19 pandemic and the economic crisis, Latvia has implemented a number of measures in the social and employment area, ranging from laptops to disadvantaged children for remote learning to various benefits to the unemployed and families with children, as well as short-time work schemes. For example, unemployment benefits were extended to young graduates and a one-off family benefit of 500 EUR paid for each child. Some measures in the RRP are expected to boost their impact, such as Active Labour Market Policies for unemployed and job-seekers, and purchase of laptops to set up "computer libraries" in schools.

4.4. The principle of 'do no significant harm'

Latvia's recovery and resilience plan assesses compliance with the 'do no significant harm' (DNSH) principle. The assessment follows the methodology set out in the Commission's Technical guidance on the application of 'do no significant harm' under the Recovery and Resilience Facility Regulation (2021/C 58/01). It covers the six environmental objectives within the meaning of Article 17 of Regulation (EU) No 2020/852, namely climate change mitigation, climate change adaptation, sustainable use and protection of water and marine resources, circular economy, pollution prevention and control, and protection and restoration of biodiversity and ecosystems. The environmental impact is assessed at measure-level, i.e. one individual assessment per reform or investment. The 24 reforms and 61 investments in Latvia's recovery and resilience plan translate to 95 'do no significant harm' assessments (with specific assessments for sub-components of measures).

Each 'do no significant harm' assessment follows a two-step approach. In a first step, it is assessed if there is a risk that a measure could do significant harm to any of the environmental objectives. In some cases, the assessment concludes that there is no risk of significant harm, in which case the measure is assessed as compliant with this objective of the regulation. In cases where the analysis identifies a risk, a more detailed assessment is performed in which Latvia demonstrates the absence of significant harm.

Where needed, the requirements of the DNSH assessment are enshrined in the design of a measure and specified in a milestone or target of this measure. This ensures that any disbursement for the respective measures can only be made once compliance with the DNSH principle is ensured. For instance, regarding the different horizontal schemes of the plan in the digital and industrial sectors (measures 2.2.1.2i., 2.2.1.3i., 2.2.1.4i., 2.3.1.2.i., 3.1.1.3i.), the DNSH assessment states that investments will exclude sectors incompatible with DNSH and this is integrated in the milestones of each measure.

Latvia's recovery and resilience plan puts particular focus on sustainable mobility with measure 1.1.1 *Riga Transport reform*. This notably entails investments in railway and public transportation which could potentially represent harm to the objective of climate mitigation. This will be prevented by a focus on electrification regarding rail (with the purchase of seven battery electric trains) and the financing of zero-emission vehicles regarding other transport investments (electric buses, trams). Potential harm to the objective of circular economy is also addressed in the DNSH assessment: for instance, for the vehicles acquired under 1.1.1.2i. *Environmentally friendly improvements to the public transport system of the city of Riga*, it is planned that after the end of the vehicle's life cycle, they will be disposed of in accordance with the requirements of Directive

2000/53/EC on end-of-life vehicles[10]. Similarly, for complementary infrastructure, it is planned that waste generation during construction will be limited in accordance with the EU construction and demolition waste management protocol and reuse and high-quality recycling of materials will be encouraged.

The plan also has a strong pillar focused on energy efficiency improvement (subcomponent 1.2). While this has a positive impact on emission reductions, it can also create significant amounts of construction waste. Latvia ensures that there will be no significant harm to the circular economy objective by detailing in the plan for each of the measures that at least 70% (by weight) of the non-hazardous construction and demolition waste generated on the construction sites will be prepared for reuse, recycling and other material recovery.

The plan also has a strong pillar focused on climate adaptation (subcomponent 1.3). While this naturally contributes to one of the six climate objectives under the DNSH assessment, it could nonetheless represent a risk to other environmental objectives. For instance, to address risks to circular economy, measure 1.3.1.1i. *Strengthening the capacity of the rescue services* confirms that demolition and construction operators will ensure that 70 % (weight) of hazardous, construction and demolition waste will be properly collected and disposed of.

Particular attention is paid to measures whose impact on environmental objectives warrants close scrutiny. Regarding measure 3.1.1.1.i. *Improvement of the national network of regional and local roads*, the recovery and resilience plan proposes to upgrade the quality of existing national regional and local roads (indicatively 210 km) to ensure better accessibility of the municipality's administrative centres. In order to prevent risks to climate mitigation, investments in regional roads should emphasise road safety, address bottlenecks and negative externalities arising from road transport, and promote a shift towards more sustainable mobility, such as by facilitating and prioritising public transport. A positive element is that this measure is accompanied by the acquisition of zero-emission vehicles: "3.1.1.6i.i. *Purchase of zero-emission vehicles for municipal functions and services* which focuses on electricity-powered school buses as a complementary investments that will reduce GHG emissions. The Latvian plan also puts forward the acquisition of zero-emission vehicles under 1.1.1 *Riga Transport Reform*. Similarly, with measure 1.3.1.2.i. *Investments in flood risk reduction infrastructure,* investments will contribute to the implementation of 29 projects, including the renovation of the polder pumping stations, the restoration of protective dikes and the rehabilitation of the regulated sections of the rivers. While this measure contributes to climate adaptation and will aim to protect 59000 ha from flooding, it could lead to significant harm to biodiversity and the good status of water bodies. Harm is nevertheless prevented by conducting an Environmental Impact Assessments and corresponding mitigations measures have been identified and reflected in each of the 29 projects. Moreover, a specific milestone shall ensure that no harm to biodiversity and the good status of water results from the measure and that the measure is compliant with the Birds Directive (Directive 2009/147/EC), the Habitats Directives (Council Directive 92/43/EEC) and the Water Framework Directive (Directive/2000/60/EC).

The plan also includes a number of regulatory reforms (in the social field for instance measure 3.1.2.5.i. *Participation in the labour market of unemployed, jobseekers and people at risk of unemployment* and measure 3.1.2.1i. *Measure to promote access to public services and employment for people with disabilities*) or more generally measures related to health (Component 4) or rule of

[10] Directive 2000/53/EC of the European Parliament and of the Council of 18 September 2000 on end-of life vehicles.

law (Component 6). The DNSH assessment has confirmed that their environmental impacts are rather negligible, ensuring that they do no significant harm to any of the six environmental objectives.

Taking into consideration the assessment of all the measures envisaged, no measure for the implementation of reforms and investments projects included in Latvia's recovery and resilience plan is expected to do a significant harm to environmental objectives within the meaning of Article 17 of Regulation (EU) No 2020/852 (the principle of 'do no significant harm'). This would warrant a rating of A under the assessment criterion 2.4 of Annex V to the RRF Regulation.

4.5. Green transition

Latvia's RRP correctly follows the methodology for climate tracking set out in Annex VI to the RRF Regulation by identifying intervention fields and corresponding coefficients for the calculation of support to the climate objectives, for each measure. It should be noted that:

- the measures of the RRP often consist of several sub-measures – for these measures, the RRP indicates an intervention field for each sub-measure and computes the climate contribution at sub-measure level.

- where relevant, milestones and targets include specifications that ensure that the requirements of an intervention field are met. For instance, where intervention field 025bis – "*Energy efficiency renovation of existing housing stock, demonstration projects and supporting measures compliant with energy efficiency criteria*" is used, a milestone/target specifies that the measure must achieve the conditions of the intervention field, i.e. on average, at least a medium-depth level renovation as defined in Commission Recommendation on Building Renovation (EU) 2019/786.

- the choice of intervention fields for the climate transition is well justified and reflects the nature, focus, objective or expected outcome of the investments.

- the RRP proposes to increase the climate coefficients for measure 1.3.1.1i. *Strengthening the capacity of the rescue services*. This measure relates to the building of new energy-efficient fire rescue centres which will be part of an overall reform of the fire and civil recue service of Latvia. According to Annex VI of the RRF Regulation, building a new energy efficient building calls for tag 025ter *Construction of new energy efficient buildings* and a 40% climate contribution. However, to take account of the accompanying reform measures that credibly increase their impact on the climate objectives the coefficients for support to the climate objectives has been increased to 100 % for this investment. As explained in the recovery and resilience plan, the reform accompanying the measure will contribute to the objective of climate mitigation by decreasing the response time for intervention by fire rescue services: the sites and location of fire rescue centres will be updated to new needs and they will be integrated with other services of the Ministry of Interior to improve their coordination. The reform will also directly contribute to fire prevention and therefore to the climate adaptation objective thanks notably to the development and implementation of warning, monitoring and analytical tools for risk analysis and a public awareness campaign. This impact of the reform on the climate objectives is also covered by a target: a decrease of 33% of the surface of wildfires is expected from 2020 to 2025 (on a multiannual average). Moreover, the increase resulting from the 100% tag does not exceed a total amount of 3 % of the allocation of the recovery and resilience plan for individual investments.

Measures supporting climate change objectives in Latvia's recovery and resilience plan account for EUR 683.894.500 which represents 37.6% of the plan's total allocation. Of the 6 components in the plan, 2 components include expenditure that contribute to the climate objectives (almost exclusively Component 1 Climate change and sustainable development and with one measure from Component 3).

With a total of EUR 311 128 000, the largest climate contribution of the recovery and resilience plan results from sub-component 1.2 devoted to energy efficiency intervention. This subcomponent notably includes energy efficiency measures for multi-apartment buildings (1.2.1.1), businesses (1.2.1.2), municipal buildings and infrastructure (1.2.1.3) as well as public sector buildings, including historical buildings (1.2.1.4) with business being the largest recipient of funds. These investment measures benefit from a 100% climate tag as they will respect the energy efficiency criteria of at least 30% primary energy savings and this level is guaranteed in their respective milestones and target. Lastly, this subcomponent is completed by a measure supporting the modernisation of electricity transmission and distribution networks and the deployment of renewable energy (1.2.1.5) which also benefits from a 100% climate tag mainly under 033 *Smart energy systems (including smart grids and ICT systems) and associated storage facilities.* Support to clean mobility will be complemented in component 3 by measure 3.1.1.6.i. of a more limited size dedicated to the purchase of zero-emission vehicles for the performance of municipal functions and services.

Sustainable transport measures also provide a significant contribution to the climate objectives. As part of the green transition and to reduce greenhouse gases emissions in Riga, measure 1.1.1 *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 4 low-floor trams, 17 electric buses and 7 electric bus charging stations, construction of a cycle roads). These different investments benefit from a full 100% climate tag as they represent clean urban rolling stock or infrastructure. With a total of EUR 295,413 million, this subcomponent represents the second biggest climate contribution to the 37% target.

Measures for the adaptation to climate change and prevention (subcomponent 1.3) also support the Latvian plan's climate ambition. This subcomponent consists of the construction of fire rescue centres as newly energy efficient buildings as part of an overall reform (see explanation above 3.1.1i. *Strengthening the capacity of the rescue services).* It also includes flood prevention measures including the rehabilitation of polder pumping stations, the restoration of protective dikes and of regulated sections of rivers. This fully contributes to the objective of climate adaptation. Altogether, this subcomponent accounts for EUR 69 587 000 of the plan's climate contribution.

The measures in Latvia's recovery and resilience plan effectively contribute to the green transition, and to addressing the challenges resulting therefrom. The plan supports Latvia's decarbonisation and energy transition objectives, as set out in the National Energy and Climate Plan (NECP). In the NECP, Latvia commits to reducing GHG emissions (-6% compared to 2005), increasing energy efficiency (reduction in primary energy consumption down to 4.1 Mtoe in 2030), and increasing renewable energy (50% renewables in gross final energy consumption). Together with the NECP, the Strategy of Latvia for the Achievement of Climate Neutrality (SLACN) by 2050 ensures coherence between the energy and climate areas, as well as the interconnection with the green and energy transition dimension of the investments envisaged in the recovery and resilience plan. Latvia has systematically indicated through its do-no-significant-harm assessment that none of the proposed measures generate harm to the protection and restoration of biodiversity

and ecosystems in some cases with milestones but has not included any biodiversity measure as such, going beyond climate contribution, and the plan has not demonstrated in detail how the measures in the plan contribute to biodiversity specifically, beyond the contribution to biodiversity brought by climate-related measures.

Various components of the recovery and resilience plan contribute to the commitments made in the NECP and will have a lasting impact:

- Regarding greenhouse gases emissions, Latvia underlines in its 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. It is for instance expected that measure 1.2.1.2 *Increasing energy efficiency in business* will lead to GHG emission savings of 13 115 Co2 equivalent in t/year.
- Regarding primary energy consumption, Latvian estimates consider that a reduction of 49 814 MWh/year could be achieved. Subcomponent 2 which is almost entirely devoted to energy efficiency renovation projects will contribute to the energy efficiency target of the NECP. Investments improving the energy efficiency of multi-apartment buildings (1.2.1.1), of municipal buildings and infrastructure buildings (1.2.1.3) and public sector buildings (1.2.1.4) are respectively expected to lower primary energy consumption by 14 423 MWh/year, 4 544 MWh/year and 4 456 MWh/year according to the Plan.

These measures are expected to contribute to the green transition to some limited extent to biodiversity. The plan contains no measures having biodiversity as their objective. However, some of the measures for climate mitigation may indirectly benefit biodiversity, given that climate change is one of the main threats to biodiversity. For example, the plan argues that the measures to be implemented by the Plan in greening the transport sector and improving energy efficiency are also expected to have an indirect positive impact on biodiversity. The recovery and resilience plan therefore contributes to helping Latvia meet the national energy and climate ambition set out in the NECP and Strategy of Latvia for the Achievement of Climate Neutrality by 2050 and thus in achieving climate neutrality in 2050.

Taking into consideration the assessment of all the measures envisaged, the recovery and resilience plan is expected, to a large extent, to make a significant contribution to the green transition or to address the challenges resulting from it and ensures that at least 37% of its total allocation contribute to the climate target. This would warrant a rating of A under criterion 2.5 of Annex V to the RRF Regulation.

4.6. Digital transition

Digital tagging

With all measures in the digital component digitally tagged as well as adding measures in the Rule of Law and Inequality components, the Plan reaches a 21% digital target or EUR 383.8 million. The main investment measures contributing to reaching digital target are upgrading public IT platforms and infrastructure (EUR 129 million), digitization of businesses (EUR 125 million), reskilling and upskilling, including basic and advanced digital skills (EUR 95 million).

Digital transition

The digital component covers all the aspects of the digital transformation - public and private sector, skills and connectivity. Measures are to a large extent in line with the identified needs, in particular, digital skills at all levels and support to the private sector for the uptake of digital technologies. The digital transition measures focus on creating medium and long-term changes to improve the competitiveness of the Latvian economy.

The digital component structurally addresses a number of digital transition challenges that are important for Latvia. The plan makes a significant contribution to the development of basic digital skills of citizens and entrepreneurs; supports equal provision of society for access to digital technologies and communications; contributes to effective public ICT governance by implementing administrative centralisation reforms; provides a systemic solution for sharing state and commercial sector data and modernises state and local government processes and services essential to society.

The digital component consists of 25 measures in four areas to support the digital transformation. It addresses boosting public administration's digital capacities, investing in digital services and infrastructure, uptake of digital solutions and technologies for the private sector, focusing on basic and advanced digital skills, as well as improving connectivity via 5G and last mile connections in rural areas. The measures aim to develop the necessary infrastructure, capacities and skills, improve efficiency, digital processes and data management in public administration, provide support to the digital transformation of businesses and improve the connectivity.

The reforms and investments in public administration will focus on digital processes and data management in public administration with national ICT solutions, e-services and applications to produce a more efficient public administration closer to citizens and businesses. The federated national cloud will allow the development of the national economy data and digital services economy. The measures will ensure the data availability, sharing and analytics. Specific reforms aim at interoperability of the public administration and once only principle and therefore at least indirectly contributing to the entry into force of the Single Digital Gateway Regulation11. The reforms and investments consist of building the common ICT public administration conceptual architecture for centralised as well as individualised public administration IT systems and solutions. The implementation of the reforms will be coordinated and managed by the national ICT governance organisation. Measures reducing burden on enterprises and citizens, and those aiming to provide support for the adaptation to use of advanced technologies are also contributing to the digital transition.

Measures addressed at digital transformation of businesses will enhance capacities through a broad spectrum of actions. The reforms and investments include the establishment of a European Digital Innovation Hub (EDIC), a supporting digital transition as a one-stop-shop, establishing a digital maturity test system; ensuring the regional contact points provide new digital transition support functions. The investments include grant schemes and financial instruments to support the digital transformation of businesses; including digitalisation of businesses processes, research and innovation actions to develop new high-tech digital products and services, training actions, as well as industry 4.0 solutions related to advanced technologies such as Internet of

[11] Regulation (EU) 2018/1724 of the European Parliament and of the Council of 2 October 2018 establishing a single digital gateway to provide access to information, to procedures and to assistance and problem-solving services.

Things, Artificial Intelligence, Machine Learning, Blockchain, big data, High Performance Computing, Cloud computing, and Virtual and Augmented Reality.

Latvia aims to increase the share of people aged 16-74 with at least basic skills to 54% in 2026 (43% in 2020). Digital upskilling addresses improving basic and advanced digital skills for citizens, enterprises and public administration with a wide range of digital skills measures. The skills reforms and investments will be implemented by adopting and implementing the Education Development Guidelines; setting responsibilities of enterprises in education of their employees and creation of wider opportunities and rights for employees to participate in education; establishing framework and piloting individual learning accounts; and establishing three Skills funds. In addition, "computer libraries" will be created in schools to help to close the digital divide, in particular, in relation to socially vulnerable schoolchildren. Number of training programmes are envisaged for basic digital skills for youth, private sector and public administration specialists.

Connectivity will be improved by providing backhaul for 5G corridors and last mile connections. The connectivity measures are aimed at ensuring 100% of fibre backhaul along the Via Baltica 5G corridor as well as last mile connectivity in rural areas, aligned with private investment and Cohesion policy funds.

Outside the digital component there are 5 measures contributing to the digital transition in the rule of law and reduction of inequality components. These other measures address participation in the labour market of unemployed, jobseekers and people at risk of unemployment (3.1.2.5.i.) and modernizing the technical and analytical capacities for the implementation of rule of law enforcement, including using AI solutions (6.1.1.1.i., 6.1.1.2.i., 6.1.1.3i., 6.1.2.1.i.).

Significant investments are foreseen in digital transition to address CSRs. The main reform measures in the plan, covering a subset of the CSRs refer to introduction of sectoral and individual skills accounts and improving digital sector governance. Investment CSRs are addressed by investments in public sector IT systems, basic and advanced digital skills, both in public and private sectors and in businesses digital adaptation, as well as by improving last mile and 5G connectivity.

Investments in digital transition and skills create synergies and complementarities with planned Cohesion Policy investments and other European level initiatives[12]. The Plan includes measures with a higher maturity, taking into account the relatively shortest eligibility period of the plan by end 2026 compared to Cohesion policy investments. Demarcation between different projects or their implementation stages are set out. The plan is aligned with the European Digital Strategy, focused on improving competitiveness and boosting digitization, including taking part in Multi Country Projects and planned IPCEIs: Via Baltica 5G - corridor, network of European Digital Innovation Hubs, European Common Data Infrastructure and Service (trough the set-up of a planned IPCEI on Next Generation Cloud), Connected Public Administration, Genome Europe, Baltic States' X-ray image exchange system (Baxe**),** microprocessors and semiconductor technologies. The plan includes measures that are expected to be co-financed under the Digital Europe Programme, Connecting Europe Facility, and Cohesion policy funds. This concerns measures aimed at establishing the Latvian Federal Cloud and linking the development of the National Data Sharing Platform to the Single European Data Infrastructure and Service, as well as the United Public Administration Priorities.

[12] Such as the communication 'Updating the 2020 New Industrial Strategy: Building a stronger Single Market for Europe's recovery'(COM(2021) 350 final) and its accompanying staff working documents

Taking into consideration the assessment of all the measures envisaged, the Recovery and Resilience plan is expected, to a large extent, to make a significant contribution to the digital transition or to address the challenges resulting from it and ensures that at least 20% of its total allocation contribute to support digital objectives. This would warrant a rating of A under criterion 2.6 of Annex V to the RRF Regulation.

4.7. Lasting impact of the plan

The implementation of envisaged reforms and investments is expected to bring structural changes in the economy. If successfully implemented, the measures shall improve Latvia's growth potential, and economic and social resilience in the medium term, and facilitate the green and digital transitions. In particular, the RRP is intended to improve labour supply, with such measures as upskilling and reskilling, and help private firms to become greener, digital and more innovative, with energy efficiency, digital audit and new R&D support measures.

In addition, the stakeholder consultation process was overall adequate, which can enhance the ownership of stakeholders, in turn supporting the lasting impact of the measures. Overall, the RRP has had an adequate stakeholder consultation process, especially in the final months/weeks ahead of the submission. The government consulted various stakeholders, including social partners. Several suggestions have been presented during a live-streamed Cabinet meeting and some were accepted, and included in the RRP.

However, the sustainability of the financing of some measures once the RRF ends is not ensured. The lack of sustainable finance in some sectors (e.g. on healthcare) risks weakening the impact of proposed measures in the long run, in particular once the RRF funding comes to an end.

The macroeconomic simulation (as shown in the macroeconomic simulation in Part IV) shows little long-lasting effects from infrastructure and human capital investment, partly due to a restricted scope considered in the model. On the whole, the estimated macroeconomic impact over 2021-29 appears cautious, given the size of the investment 6.0% of 2019 GDP over six years, i.e. approximatively 1% of GDP per year. These low estimates are partly due to the restricted scope of the model used for assessment, which considers investment only (and does not factor in the effects of reforms), as well as to assumptions, notably regarding the crowding-out effects of RRF funds on private investment, or the replacement of domestic investments by EU funds.

Structural change in administration and institutions, as well as in policies

Structural changes on administration and relevant institutions, as well as in policies, can be expected from the implementation of the RRP. However, for some measures such changes would appear limited due to the lack of a comprehensive set of measures, or because their lasting feature is not fully ensured.

The reform of the governance and financing of the higher education institutions is one of the most ambitious reform proposals of the plan (under component 5 'Productivity). If successful in achieving its goals, it would have a profound, long-lasting impact on the quality of higher education and research in Latvia. It would lead to a structural change to both the institutions of higher education and the higher education policy, and increase quality of human capital in R&I. This would better reward academic performance and focus the scarce resources to achieve better quality (as opposed to quantity). A number of other proposals under component 5, involving important, but smaller steps in their respective areas – tax administration, judicial system, public

administration, and public procurement – would lead to long-term changes both to administrations and policy implementation.

Other measures shall lead, if successfully implemented, to some lasting structural changes in administration and institutions, as well as in policies.

In principle, measures under component 2 'digital transition' shall have lasting positive impact on public administration efficiency and policy making (e.g. Reform 2.1.1 Modernisation of national processes and services and digital transformation and Investment 2.1.1.1i: Modernisation of government and digital transformation of services, including business environment). There is an institutional commitment to establish legal and institutional frameworks tackling structural problems, especially in public services and digital skills, including training for students, jobseekers, civil servants and workforce (e.g. Measure 2.3.r. Digital skills for the digital transformation of society and government). This shall contribute to lasting structural changes. However, securing the improvements of the digital sector governance remains a pending issue.

The reorganisation of municipalities, implying a regrouping and reduction in number, (measure 3.1.1 Administrative territorial reform under component 3 'Reduction of inequalities'), shall also help making public services more cost-efficient and of better quality. The investments in support of the administrative territorial reform will also bring about structural changes both in public administration and policy making, by increasing the municipal capacities and contributing to improved policy-making. Moreover, Reform 3.1.2.r. Access to social and employment services in support of the minimum income in component 3 will contribute to improving the social safety net, reduce inequality and foster social inclusion in Latvia.

Under component 6 'rule of law', measures on shadow economy (6.1.), modernisation of public administration (6.3), centralisation and professionalisation strategy with regard to procurement (6.4.3.r.) and strengthening NGOs (6.3.1.4.) are expected to contribute to long-term changes and improved capacities of public administration and policy making. In details, the measure 6.1.1. Strengthening analytics and developing data management in the field of tax administration and customs are expected to establish a system of compliance risk analysis in the areas of taxation, customs, excise goods, anti-money laundering and crime reduction; the reform on modernising public administration (6.3) is expected to contribute to an efficient public administration that delivers better quality services, designs and implements better policies, and attracts and retains competitive and professional staff; the NGO measure (6.3.1.4.) is expected to improve representation of socially vulnerable groups in dialogue with public administration; and the measure 6.4.3.r. Development and implementation of a professionalisation strategy is expected to lead to the centralisation of procurements in specific areas, thereby ensuring cost efficiency and enhancing the professionalisation of contracting authorities. Investments in customs control capacities (6.1.2.1.i, 6.1.2.2.i and 6.1.2.3.i) are expected to contribute to reducing the risk of non-compliant and/or illegal goods being placed on the internal market also ensuring a level playing field for businesses and adequate protection of consumers.

However, the lasting effects of some measures may be somewhat narrowed, due to the absence of complementary policies, or the lack of a strategy for ensuring long-term sustainable financing.

For instance, under component 1 'green transition', whereas the materialisation of the public transport plan and the increased importance of rail transport, if successful, could be considered as a policy shift, the current planning of public transport offer in Riga region is scattered and not interlinked to any transport mode. Whereas the measures aiming at energy efficiency renovation

of buildings will result in long term impacts as saved energy, reduced GHG emissions and improved quality of air, opportunities of undertaking necessary reforms and enabling conditions to attract private investment for renovations and use of ESCOs (energy performance contracting especially in public and tertiary buildings) are not explored. Moreover, while potentially addressed by other means, a number of challenges and opportunities resulting from the green transition, namely circular economy, sustainable innovation (business models, products and services), green skills, have been left outside the plan.

The component 3 'reduction of inequalities' proposes a number of measures aiming to address several inequality challenges in Latvia. The component aims to reduce inequality by creating more jobs in the regions, improving regional connectivity and access to quality services, providing more affordable housing, improving the school infrastructure, helping to up-skill and re-skill workers and unemployed, strengthening the social safety net, improving accessibility to buildings for persons with disabilities, and new long-term care facilities for the elderly. This constitutes a good basis for taking further measures necessary to strengthen social resilience and adapt dwellings for persons with limited mobility.

Regarding measures under component 4 'Health', whereas the resilience, accessibility and effectiveness of Latvia's health system are expected to improve in several years, the long-term effect is not ensured and shall depend on the sustainability of financing. The measures shall notably contribute to improved governance of the health system, including reinforcing the capacities of the Ministry of Health. The sector will also benefit from the research, modelling and training measures. The digital strategy (elaborated in digital component) and modernisation of the e-health system will improve efficiencies in the health sector. However, for the impact of the measures to be sustainable and lasting, complementary and sustainable financing in Latvia's health system needs to be ensured in the long-run, and the shortages in the healthcare workforce need to be addressed. In absence of a sustainable approach to increase the level of financial and human resources to the system, the impact is likely to be rather short-term.

Under component 4, an example of measures expected to bring about a structural change in the administration or in relevant institutions is Reform: 4.3.1: Sustainability of health care, strengthening governance, efficient use of health resources, increase of total public budget in the health sector. The objectives of the measure are to improve the efficiency of the provision of state-funded health services by ensuring the availability of services and establishing a systemic change mechanism for state-paid services.

Another example of measures expected to bring about a structural change in relevant policies is Reform 4.2.1: Provision of human resources and upskilling. The reform aims at preparing a health workforce strategy, which will encompass health workforce planning, including aspects around the development of skills and competences of medical practitioners. A further example is reform 4.1.1: Sustainability and resilience of a human-centred, comprehensive, integrated healthcare system. The reform aims to develop recommendations for integrated care and epidemiological safety, as well as a health infrastructure investment strategy. These will link to investments in hospital infrastructure under investment 4.1.1.2.i.: Support for strengthening the health infrastructure of university and regional hospitals in order to provide a comprehensive sustainable integrated health service, reduce the spread of infectious diseases, ensure epidemiological requirements and under investment 4.1.1.3i.: Investments in infrastructure for secondary outpatient service providers.

Taking into consideration all reforms and investments envisaged by Latvia in its recovery and resilience plan, their implementation is expected, to a large extent to bring about a structural

change in the administration or in relevant institutions and in relevant policies and to have a lasting impact. This would warrant a rating of A under criterion 2.7 of Annex V to the RRF Regulation.

4.8. Milestones, targets, monitoring and implementation

The national institutions involved in the implementation of the plan, monitoring progress and reporting have clearly assigned responsibilities and an adequate structure (see Section 4). Latvia envisages to ensure the implementation process of the plan in the framework of the existing management and control system for EU Cohesion Policy. The system is complemented to meet the conditions and requirements of the RRF framework. Within this system, the implementation of the plan will be coordinated by the Ministry of Finance which will also perform the functions of a Managing Authority. The functions performed by the Ministry of Finance as the Managing Authority will be separated from its other functions, including those of the Audit Authority. The Audit Authority, which is independent from the other departments of the Ministry of Finance in its planning and auditing, reporting and opinion, develops an RRP audit strategy and prepares a summary of the audits carried out for submission to the European Commission of the payment requests. The sectoral ministries and the State Chancellery will perform the responsibilities assigned to them, mostly related to practical implementation of the plan.

Institutions involved in the monitoring and implementation of the plan and their functions are clearly presented (see section 4, figure 14). The Managing Authority is involved in the organisation of the plan and is in charge of the development of the management and control system of the plan, coordinating the reporting process during the implementation of the plan (a half-yearly report on the compilation and progress of the plan) and other functions. This structure has defined responsibilities enshrined by law, which ensures a priori a sound coordination and reporting mechanism between this structure and other bodies responsible for implementing the investments and reforms under the various components.

The necessary administrative resources for the management and supervisory functions of the plan will be provided within the institution's existing resources, with additional human resources if needed. This should ensure the proper implementation process and does not impose a disproportionate additional administrative and financial burden as the institutions involved possess the necessary knowledge, experience and skills. However, Latvia's public administration is relatively small, and the necessity to implement both the RRF and Cohesion Policy programmes could be an additional burden. The involvement of the authorities in the implementation of the plan takes place within the defined framework of their core activities and functions. Latvia envisages that the financing of sectoral ministries for the implementation of the plan will be allocated in accordance with the relevant national procedures for the financing of the state budget. A separate budget programme is provided in the state budget, which ensures the traceability and separability of the financial flows. The issue of allocating state budget resources to cover the administrative resources expenditure of the plan will be examined by the Cabinet of Ministers in accordance with the financial capacity of the state budget.

The plan describes adequately the intended monitoring and reporting mechanisms. An information system will collect the necessary information to monitor the reforms and investments, including milestones, targets and results. The information system will also ensure the availability of information related to the investments and reforms of the RRP, including data on the final recipients of the measures of the plan. Information related to the implementation and monitoring of the plan will be stored in a data management system – the existing EU funds management and

control system KPVIS. The KPVIS will be adapted to the requirements of the RRF framework for data collection, progress reports and payment requests, including to collect indicators and other information necessary to demonstrate and report the achievement of milestones and targets. The KPVIS module for the collection, storage and analysis of project data is planned to be implemented at the beginning of Q1 2022, which is somewhat late. In case project applications are submitted earlier than the creation of the KPVIS module, the Central Finance and Contracts Agency (CFCA) will register and store documentation in the existing DocLogix filing system. Information on the checks carried out will be collected and entered into the KPVIS after the creation of the KPVIS module. The available IT systems that can contribute to the monitoring process will be used during the implementation of the plan, including ARACHNE. Arachne will be used for both ex-ante and ex-post checks of CFCA and audits carried out by the AA. KPVIS will be used by all institutions involved in the implementation of the plan, including beneficiaries and monitoring authorities between the CFCA, line ministries and the Audit Authority and others. In terms of reporting, sectoral ministries are to continuously manage and update information in the KPVIS on the progress and results of the plan on the checks carried out, controls, including deficiencies identified and all corrective actions taken. Access to all information and data related to the plan in the KPVIS will be provided upon on request.to the European Commission, OLAF, the European Court of Auditors, the Office of the Public Prosecutor's Office of the European Union. In terms of reporting, the Ministry of Finance will prepare, coordinate with sectoral ministries and the Central Finance and Contracts Agency (CFCA) and submits a six-monthly progress report, including an evidence-based offer for payment requests, taking into account the information entered by sectoral ministries and CFCA.

The milestones and targets of the Latvian plan constitute broadly an appropriate system for monitoring the plan's implementation. The milestones and targets chosen represent mostly the key elements of the measures and as such can be considered relevant for their implementation. The verification mechanisms, data collection and responsibilities described by the Latvian authorities appear sufficient to justify in an adequate manner the disbursement requests once the milestones and targets are completed. Sectoral ministries will be responsible for achieving milestones and targets and for collecting traceable and valid data on milestones and targets achieved and, where necessary, for ensuring access to or to provide the necessary information. The Latvian Cabinet of Ministers will be informed of significant risks, problems, including in particular when the milestones and targets set out in the plan are not met. The measures in the plan are to some extent fragmented. This results in a high number of milestones and targets which are back-loaded towards 2026, especially in the cases of infrastructure investment and horizontal schemes for business investment. The monitoring indicators are in general sufficiently clear and robust to ensure that their completion can be traced and verified. They reflect adequately the overall level of ambition of the plan and appear realistic.

Latvia provided detailed indicators, which it will use to monitor informally the progress of the implementation of individual measures between the disbursement requests. These indicators are expected to be included in the Operational Agreement and provide an adequate early warning system to ensure that Latvia can take corrective actions in time if necessary to avoid missing the objective set up in the relevant milestone/target. In addition, milestones and targets sufficiently cover sub-investments so that the plan's measures can be monitored.

The RRP's overall political steering will be ensured by the Latvian Cabinet of Ministers. In order to ensure the effective implementation of the plan, the Latvian Cabinet of Ministers is to establish effective, transparent and sound financial management supervisory procedures for the

implementation and monitoring of the plan. In this context, the Cabinet of Ministers will delegate the coordinating and audit functions to the Ministry of Finance. The line ministries and the State Chancellery are responsible for the implementation of the components, while the CFCA will ensure the verification of the plan.

Technical cooperation between the relevant national institutions (Ministry of Finance, the CFCA, sectoral ministries, the State Chancellery, Audit authority and other) will be critical for the plan's implementation. Latvia developed an internal control system for the relevant institutions for preventing corruption and the risk of conflict of interest within the institution. CFCA as a direct administrative body subordinate to the Minister of Finance and accredited (certificate of compliance with the ISO 27001:2013 – Information Security Management – Standard) will monitor progress, including indicators, assessment of risks, state aid monitoring, ensure double funding checks, detection of non-compliance and recovery of irregular expenditure, as well as compliance with the conditions for support for commercial activity. It will cooperate with other entities including the Audit Authority, which will develop a plan audit strategy and prepare a summary of the audits carried out for submission to the European Commission of the plan progress report. These audits will be complemented by an assessment of the existing control system in the institutions involved in the implementation of the plan to mitigate the risk of double funding, the risk of conflict of interest and the risk of corruption and fraud, as well as an assessment of the reliability of the data on the results achieved. Sectoral ministries will be responsible for achieving milestones/objectives, in cooperation with CFCA non-compliance detection and reporting, data input into KPVIS, monitoring progress, ensuring the whole implementation process and its compliance with EU and national regulatory requirements, verifying corruption, conflict of interest and fraud risk. The experience and knowledge of the Ministry of Finance, sectoral ministries, the CFCA and the Audit Authority, accumulated in the planning, implementation and verification of EU funds projects should be sufficient to ensure correct implementation of the plan.

The plan describes the institutional actors that are responsible for implementation the individual reforms and investments at component level. The various actors in charge of the measures are clearly indicated in the description of the components of the plan. Sectoral ministries are responsible for the implementation of the specific reforms and investments of the Plan. Each line ministry is responsible for providing the necessary capacity to implement and monitor the plan. The sectoral ministries or actors involved in the execution of each reform and investment will liaise with the Ministry of Finance which ensures overall coordination with line ministries and the Central Finance and Contracts Agency (CFCA). All institutions involved in the implementation of the plan will develop and supplement their internal procedures for the specificity of the plan.

The arrangements proposed by Latvia in its recovery and resilience plan are expected to be the adequate to ensure effective monitoring and implementation of the recovery and resilience plan, including the envisaged timetable, milestones and targets, and the related indicators. This would warrant a rating of A under the assessment criterion 2.8 of Annex V to the RRF Regulation.

4.9. Costing

Latvia has provided individual estimated costs for all investments and three reforms in the recovery and resilience plan. The three reforms with associated costs are in the health component of the plan, namely (i) on sustainability and resilience of a human-centred, comprehensive, integrated healthcare system; (ii) on human resources and upskilling; and (iii) on sustainability of health care, strengthening governance, efficient use of health resources, increase of the total public budget in the health sector.

The cost breakdown is generally detailed and well-substantiated. For almost all cost estimates the assumptions used are well described and can be understood. The estimates are based on comparisons with past investments of similar nature and on market and price analysis. While the tables proposed in the standard template were duly completed and presented, Latvia did not provide an independent validation for any of the cost estimates proposed.

The assessment of the cost estimates and inherent supporting documents shows that most of the costs are well justified, reasonable and plausible.

Reasonable costs

To support the cost estimates, Latvia provided an extensive list of documents to justify and explain the amounts proposed and gave explanations on how those amounts were computed. For the most part, older projects or comparative cost data for the main cost drivers were presented to serve as a benchmark for the cost estimates. While for the most part the calculations were clearly spelt out and it is possible to clearly identify the methodology used, for a limited number of sub-investments the information provided proved less clear. Nevertheless, there is no evidence that would allow doubting the costing estimates provided.

In this context, it is deemed that the reasonability of the cost estimates has been established to a medium extent.

Plausible costs

The amount of the estimated total costs of the recovery and resilience plan is in line with the nature and type of the envisaged reforms and investments. Latvia provided an extensive collection of documents to substantiate the cost estimates. However, for several investments, clear explanations were missing as to how the past projects presented as the basis for the estimates were used or adjusted to provide for the cost estimates presented. Without these explanations, it is difficult to assess the plausibility of the costing. Only for a very limited number of measures the costs were deemed not within the plausible range compared to costs of similar investments.

Considering the limitations of an *ex ante* assessment of cost estimates, the amounts proposed for financing were deemed appropriate and seen as establishing the plausibility of the cost estimates to a medium extent.

No double EU financing

The individual components provide clear information about additional investments from other EU funds. Projects funded by other EU sources are demarcated in time and scope from the projects in the RRP. Furthermore, Latvia has put in place arrangements to avoid double EU funding. The Central Finance and Contracting Agency (CFCA) will carry out checks and monitor double funding. The existing management and control system for the EU funds 2014-2020 also provides for double-financing risk control matrix, which checks the absence of double funding within the framework of planned investment projects. Based on this information, the responsible bodies will effectively plan, control and monitor measures to ascertain that the beneficiaries are not implementing similar or identical projects with other financial instruments.

To note, the 2021-2027 Partnership Agreement is currently under negotiation, and as such a completely developed delineation is not possible at this moment. However, the Commission did a preliminary check to reduce the risks of double European Union financing, and no evidence of clear risks was identified.

Commensurate and cost-efficient costs

The recovery and resilience plan is expected to effectively help address a significant subset of challenges identified in the country-specific recommendations (CSRs). Moreover, the recovery and resilience plan contains measures to support economic growth and economic cohesion in an inclusive manner. The main objectives of the plan are to improve Latvia's growth potential, job creation, and economic, social and institutional resilience that will ultimately reduce the country's vulnerability to shocks. Several of these measures also contribute effectively to the implementation of the European Pillar of Social Rights, including through the promotion of policies for children and youth, and to mitigating the economic and social impact of the COVID-19 crisis, thereby enhancing the economic, social and territorial cohesion and convergence within the Union. The significant economic and social impact of the plan in combination with the positive cost assessment, indicates that the **cost is in line with the principle of cost-efficiency.**

The justification Latvia provided on the amount of the estimated total costs of the recovery and resilience plan is, to a medium extent reasonable and plausible, in line with the principle of cost-efficiency and commensurate to the expected national economic and social impact. Latvia provided sufficient information and evidence that the amount of the estimated cost of the reforms and investments of the recovery and resilience plan to be financed under the Facility is not covered by existing or planned Union financing. This would warrant a rating of B under the assessment criterion 2.9 of Annex V to the RRF Regulation.

4.10. Controls and audit

RRP Control and audit systems are developed based on the existing Cohesion Policy structures. The implementation of the RRP will be ensured by the sectoral ministries in cooperation with the Ministry of Finance as the lead ministry, the Central Finance and Contracting Agency (CFCA), the Audit Authority and the Procurement Monitoring Bureau. The audit authority, an independent and appropriately segregated unit of the Ministry of Finance, performs horizontal system audits, creates an audit strategy, and gives opinions about the management and control system compliance with the requirements EU and national normative acts. It also prepares a summary of the audits carried for the RRP progress report and payment requests. CFCA will ensure the monitoring process of investment projects with a focus on double funding, state aid checks, as well as controls on the detection and prevention of corruption, conflict of interest and fraud. The procurement monitoring bureau performs public procurement procedure pre-checks.

Adequacy of control systems and other relevant arrangements

The Audit Authority will carry out audits similar to those of the EU funds 2014-2020 and 2021-2027 periods. These audits will be complemented by an assessment of the existing control system in the institutions involved in the implementation of the RRP plan to mitigate the risk of double funding, the risk of conflict of interest and the risk of corruption and fraud, as well as an assessment of the reliability of the data on the results achieved. Where necessary, expenditure checks and other additional audit tasks may be carried out in accordance with the risk assessment.

All information related to the implementation and monitoring of the RRP plan will be stored in a single IT system. The existing EU funds management and control system KPVIS will be used by all institutions involved in the implementation of the RRP plan, including beneficiaries and monitoring authorities such as CFCA, the procurement monitoring bureau, the Ministry of Finance,

line ministries and audit authorities. The KPVIS will ensure the necessary audit trail and milestones and targets reporting of the components under RRF. The RRF module in KPVIS will become available by 1st quarter 2022, before the first payment request is submitted to the Commission. Until then, the existing documentation tool DocLogix shall be used for storing the RRP related documentation. Until the deployment of KPVIS RRF module, a copy of the EU funds module in the KPVIS, which provides for a full data storage structure, may also be used. Once the KPVIS RRF module is developed, the information dating back to February 2020, including information on the checks carried out, shall be migrated to the new module. A dedicated audit report on the system is expected to be undertaken. In case that the report identifies any weaknesses, the audit report will recommend corrective actions.

The process to prevent, detect and correct fraud, corruption and conflict of interest is in place. These controls will be carried out by the Procurement monitoring bureau and CFCA during the implementation of investments/projects, and by line ministries in the implementation of reforms. In addition, the audit authority will also look at these areas when carrying out system audits. Fraud, corruption and conflict of interest will be prevented, detected and corrected through (1) procurement checks, whereby the most significant procurement requirements with the highest risk of detection of derogations related to risks of corruption, conflict of interest or fraud will be examined on a sample basis in a risk-based approach; (2) data analysis of various information systems (Arachne, VID, Lursoft, firm.lv), (3) on-the-spot checks in order to ascertain whether the planned investments and objectives are being implemented as foreseen in the project, (4) including obligations and responsibilities for the implementation of the investment projects to prevent conflicts of interest, corruption and fraud; (5) media monitoring, information from third parties and in collaboration with law enforcement bodies. A horizontal instrument for the whistle-blower protection is in place.

Adequacy of arrangements to avoid double EU funding

Arrangements to avoid double EU funding are put in place. Latvia indicates funding and, in some instances, amounts from other sources, such as REACT-EU, Cohesion Policy, Connecting Europe Facility, Digital Europe and others supporting the implementation of certain measures. The CFCA will carry out checks and monitoring double funding. The existing management and control system for the EU funds 2014-2020 also provides for double-financing risk control matrix, which checks the absence of double funding within the framework of planned investment projects. The matrix contains the following details: the number and the title of the specific objective, the number of the support measure, selection method, responsible ministry, source of funding, description of the specific objective and the supported measure, beneficiaries, target group. Based on this information, the responsible bodies can effectively plan control and monitoring measures to ascertain that the beneficiaries are not implementing similar or identical projects with other financial instruments.

Legal empowerment and administrative capacity of control function

The RRP implementation set up will be based on the existing cohesion policy framework. On 18August 2020, the Cabinet of Ministers adopted a decision that the implementation process of the RRF will be ensured in the framework of the existing management and control system for EU funds 2014-2020 which complies with internal control environment, risk management, management and control and supervision set out in Annex XIII of Regulation No 1303/2013 and is approved by the Cabinet of Ministers and accredited by the Commission. Based on this and the RRF Regulation, the Cabinet of Ministers regulation for RRF implementation will be adopted by the end of 2021.

The Cabinet of Ministers will delegate the coordinating and audit functions of the Ministry of Finance as the lead ministry, the line ministries and the State Chancellery will be delegated the function to be responsible for the implementation of the components, while the CFCA will ensure the verification. An update upon the adoption of those acts and relevant obligations is expected to be included in the Financing Agreement to be concluded in accordance with Article 23(1) of Regulation (EU) 2021/241.

The RRP provides sufficient information on the administrative capacity of coordinating and implementing bodies. The experience and knowledge of Ministry of Finance, line ministries, CFCA and Audit Authority, accumulated in the planning, implementation and verification of EU funds projects, are sufficient to ensure a correct implementation of the RRP plan. The Ministry of Finance, in cooperation with line ministries, carries out an assessment of the administrative burden of implementing the RRP and identifies the need for additional time-limited human resources to ensure that the administration and monitoring of the RRP are ensured. In addition, the administrative capacity of the institutions in the form of knowledge will be strengthened within the framework of the administrative capacity road map within the framework of Cohesion Policy implementation activities carried out within the framework of the plan. The financial resources required for the implementation of the requirements of the RRF for 2021 will be channeled from the State budget resources to the extent necessary, while the financing required for the remaining of the implementation period will be examined during the preparation of the draft Law on the State Budget for 2022 and the draft law on the medium-term budgetary framework for 2022, 2023 and 2024.

The arrangements proposed by Latvia in the recovery and resilience plan to prevent, detect and correct corruption, fraud and conflicts of interest when using the funds provided under the Facility, including the arrangements aimed to avoid double funding from the Facility and other Union programmes, are assessed to be adequate. This would warrant a rating of A under the assessment criterion 2.10 of Annex V to the RRF Regulation.

4.11. Coherence

The Latvian recovery and resilience plan is coherent, with consistent reforms and investments, and synergies between the different components. The recovery and resilience plan contains measures for the implementation of reforms and public investment projects that represent coherent actions. The six components structure the investments and reforms and show their thematic relation and interlinkages well. Coherence is ensured within the components, with investments accompanied with relevant reforms, as well as between the different components in the plan through mutually reinforcing reforms and investments. However, the plan remains stronger on investments than on reforms.

The RRP builds on the national industrial policy (NIP) 2021-2027. The NIP is based on the objectives set in the National Development Plan, the Smart Specialisation Strategy, as well as the Resilience Strategy for Latvia, focusing not only on stabilising the economy, but also on reorienting the economy and exploiting the growth opportunities created by the crisis. A large share of RRP funding (64%) is dedicated to implementing the NIP. In addition, the RRP is coherent with other national planning documents, such as the National Energy and Climate plan.

Mutually-reinforcing measures

The reforms and investments in each component included in the plan are consistent and mutually reinforcing. Reforms included in the plan enable and underpin the planned investments.

No cases have been observed of areas where the measures proposed within any component (be it reforms or investments) contradict or undermine each other's effectiveness.

Climate change and environmental sustainability is based on the National Energy and Climate plan (NECP) approved in 2019. The reforms and investments in this component are targeted to achieve the same objectives: (1) reduce GHG emissions in the transport sector; (2) increase energy efficiency and (3) strengthening adaptation to climate change. The measures are coherent in that the general reforms address these objectives, while the individual investments seek to implement and support the objectives of the reforms. The most significant investments are planned in sustainable transport infrastructure in Riga and the Pieriga region, promotion of energy efficiency in the public and private sectors, strengthening crisis response capacity, as well as adaptation to climate change. The above measures are strategically important elements in Latvia's NECP in order to achieve the 2030 and 2050 climate targets.

The component 2 on digital transition covers all the aspects of the digital transformation from both reform and investment perspective. The proposed measures are consistent with relevant national strategies and plans and focus on digital processes and data management in public administration with National ICT solutions, e-services and applications to produce a more efficient public administration closer to citizens and businesses. Particular emphasis is placed on the importance of RRP investments for the skills development. The reforms on adult learning framework are mutually supportive with the investments. The component is also aligned with the European Digital Strategy, focused on improving competitiveness and boosting digitisation, including taking part on Multi Country Projects and IPCEIs.

The component 3 on the reduction of inequalities has two distinctly different elements – support to the administrative territorial reform and social inclusion. As cohesion remains the common goal, it does not pose a prohibitive problem. Both parts are built around key reforms – administrative territorial reform (retroactive) and minimum income reform that are supported with a coherent set of investments.

The measures in the component 4 on health are coherent, but remain stronger on investment. The health component aims to improve the resilience, accessibility and quality of healthcare through two reform strands – integrated healthcare and strengthening the health workforce. The reforms will prepare recommendations for integration of care and for meeting epidemiological requirements, and these will guide the investments in hospital infrastructure. Similarly, regarding the healthcare workforce, there is a reform measure and an investment measure, linked to each other, although the reform element lacks ambitious commitments for the implementation. The corresponding investment aims at supporting the education and training of the healthcare workforce, thus contributing to the implementation of the health workforce planning prepared in the context of the reform.

The component 5 on productivity is coherent with the overall objectives regarding productivity. The measures included in the component focus primarily on the efficiency of the higher education system by promoting the concentration of resources of higher education and scientific institutions, as well as the reform of the innovation management system with the aim of increasing private sector investment. It contributes to the expected productivity impact and the reform is in line with the overall education policy, R&I policies and intended investments.

The component 6 on rule of law measures aims to contribute to the implementation of the reform of the modernisation of the public administration. The reform on the modernisation of the public administration and the reform on public procurement are complementary and coherent.

The reforms and investments are expected contribute to the increased transparency, accountability and efficiency of the public administration.

Complementarity of measures

The recovery and resilience plan includes measures that are complementary to one another. The components included in the RRP of Latvia form a single framework for reforms and investments, the core task of which is to (1) promote productivity, (2) reduce inequalities, as well as (3) green transition and (4) digital transition. The six components are mutually reinforcing and coherent in their aims. They do not have contradictory aims or possible negative effects on one another.

Complementary reforms to increase productivity and efficiency are planned in several components of the RRP. The main structural reforms and support measures for increasing the productivity of the Latvian economy are concentrated in the component on productivity. At the same time, as part of the component on green transition, an important role is given to improving the energy efficiency of businesses, including investments to improve technological processes, which have a complementary impact on increasing productivity.

The digital transition component plays an important horizontal role in Latvia's RRP. It provides horizontal support for the implementation of other structural reforms and the achievement of the objectives of several national strategies. Given the cross-sectoral nature and benefits of the digital skills, the links between the investments, including in other components of the RRP, are clear and reinforcing. At the same time, the digital transition component is complementary to a number of reforms in other components, such as increasing access to health and education services, improving the rule of law and the business environment and modernising the public administration and ensuring the quality and accessibility of the services it provides.

The overall balance of the response is adequate in view of the main challenges, but the plan remains stronger on investments than on reforms. Ensuring sustainable economic growth, catching up with the EU average and decarbonising its economy while coping with a decreasing population remain Latvia's main challenges. The reforms and investments in innovation and skills, strengthening social inclusion and reducing regional disparities are essential. In this context, the key reform measures provide an adequate response. Significant investments are planned for sustainable transport, energy efficiency and regional development, while the digital infrastructures, social inclusion and clean energy receive less funding relative to the size of their challenge.

In order to promote wider coherence across instruments, notably with the European cohesion policy funds, a balanced territorial allocation of resources is encouraged.

Taking into consideration the qualitative assessment of all components of Latvia's recovery and resilience plan, their individual weight (importance, relevance, financial allocation) and their interactions, the plan contains measures for the implementation of reforms and public investments which, to a high extent, represent coherent actions. This would warrant a rating of A under the assessment criterion 2.11 of Annex V to the RRF Regulation.

ANNEX: CLIMATE AND DIGITAL CONTRIBUTION OF THE MEASURES OF THE LATVIAN RECOVERY AND RESILIENCE PLAN

		Climate		Digital	
Measure/Sub-Measure Name (with ID)	**Budget (EUR)**	**Int. Field**	**Coeff. %**	**Int. Field**	**Coeff. %**
1.1.1.1.i.1. Competitive rail passenger transport in the common public transport system of the city of Riga (acquisition of electric rolling stock)	74.400.000	074	100%		
1.1.1.1.i.2. Competitive rail passenger transport in the common public transport system of the city of Riga (railway modernisation -TEN-T)	32.450.000	067	100%		
1.1.1.1.i.3. Competitive rail passenger transport in the common public transport system of the city of Riga (railway modernisation)	40.250.000	069 bis	100%		
1.1.1.2.i.1. Environmental improvements in the city of Riga's public transport system (clean urban transport)	24.270.000	n/a[13]	100%		
1.1.1.2.i.2. Environmental improvements in the city of Riga's public transport system (clean urban transport infrastructure)	87.285.492	073	100%		
1.1.1.3.i. Complete rolling infrastructure – (cycling infrastructure)	34.514.008	075	100%		
1.2.1.1.i.I. Improving the energy efficiency of multi-apartment buildings and transition to renewable energy technologies	57.282.000	025 bis	100%		
1.2.1.2.i. Increasing energy efficiency in business, which is planned to be implemented nationally in the form of a combined financial instrument	120.586.000	024 ter	100%		
1.2.1.3.i.I. Improving municipal buildings and infrastructure by promoting the transition to renewable energy technologies and improving energy efficiency	29.304.000	026 bis	100%		
1.2.1.4.i.I. Improving the energy efficiency of public sector buildings, including historical buildings	23.956.000	026 bis	100%		
1.2.1.5.i. Modernisation of electricity transmission and distribution networks	80.000.000	033	100%		

[13] The 'Methodology for climate tracking' annexed to the Recovery and Resilience Facility Regulation does not set out intervention fields that would allow for climate or environmental tracking of electric vehicles or plug-in hybrid vehicles, except for vehicles for urban transport falling under intervention field 074. According to Article 18(4)(e) of the Regulation, the methodology should however 'be used accordingly for measures that cannot be directly assigned to an intervention field listed in Annex VI'. In this context, the Commission has applied a 100% climate contribution coefficient for zero-emission vehicles of all categories (this includes battery electric and fuel cell/hydrogen-powered vehicles).

1.3.1.1.i.1. Capacity building for rescue services, in particular the upgrading of the infrastructure and the logistical base of the VUGD (tag increased to 100% - see section 4.5)	36.630.000	025ter	100%		
1.3.1.2.i. Investments in flood risk reduction infrastructure	32.967.000	035	100%		
2.1.1.1i. Administration modernisation and digital transformation of services, including business environment	24.437.280			011	100%
2.1.2.1i. Centralised governance platforms and systems	70.177.920			011	100%
2.1.2.2i. National Federal Cloud of Latvia	12.490.800			055	100%
2.1.3.1.i. Data availability, sharing and analysis	21.756.000			011	100%
2.2.1.1i. Support for the establishment of Digital Innovation Hubs and Regional Contact Points	10.000.000			010	100%
2.2.1.2i. Support for the digitisation of processes in commercial activities	40.000.000			010	100%
2.2.1.3i. Aid for business introduction of new products and services	24.300.000			010	100%
2.2.1.4i. Financial instruments to facilitate the digital transformation of economic operators	45.143.000			010	100%
2.2.1.5i.Fostering the digital transformation of media companies	5.700.000			010	100%
2.3.1.1.i. Delivering high-level digital skills	17.000.000			108	100%
2.3.1.2.i. Development of key digital skills of enterprises	20.000.000			108	100%
2.3.1.3.i. Development of a self-accompanied training approach for ICT specialists	7.600.000			108	100%
2.3.1.4.i. Development of the approach to individual learning accounts	14.306.000			108	100%
2.3.2.1 Digital skills for citizens, including young people	12.632.000			108	100%
2.3.2.2.i. Development of state and local government digital transformation skills and capabilities	8.250.000			108	100%
2.3.2.3i.Closing the digital divide for socially vulnerable students and educational institutions	15.000.000			108	100%
2.4.1.1.i. Construction of the Passive Infrastructure on the Via Baltica Corridor for 5G coverage	12.500.000			054bis	100%
2.4.1.2i.Broadband or very high capacity network “last mile” infrastructure development	4.000.000			053	100%

3.1.1.6.i. Purchase of zero-emission vehicles for the performance of municipal functions and services	10.000.000	n/a[14]	100%		
3.1.2.5.i. Participation in the labour market of unemployed, job-seekers and people at risk of unemployment	28.710.000			016	40%
6.1.1.1.i. Modernisation of existing analytical solutions	2.100.000			011	100%
6.1.1.2.i. Development of new analytical systems	1.880.000			11	100%
6.1.1.3i. Personnel training to work with an analytical platform and consultancy	20.000			108	100%
6.1.2.1.i. Linking railway x-ray equipment to Baxe and use of artificial intelligence for rail freight scanning image analysis	3.000.000			11	100%

[14] The 'Methodology for climate tracking' annexed to the Recovery and Resilience Facility Regulation does not set out intervention fields that would allow for climate or environmental tracking of electric vehicles or plug-in hybrid vehicles, except for vehicles for urban transport falling under intervention field 074. According to Article 18(4)(e) of the Regulation, the methodology should however 'be used accordingly for measures that cannot be directly assigned to an intervention field listed in Annex VI'. In this context, the Commission has applied a 100% climate contribution coefficient for zero-emission vehicles of all categories (this includes battery electric and fuel cell/hydrogen-powered vehicles).