

**Edmunds Krastiņš**

**Why Latvia Cannot Do Better**

Historical economic essay

2023

TABLE OF CONTENTS

Introduction ..... 3  
Economies of the Baltic States before World War II..... 5  
Current Situation ..... 11  
What happened during the occupation? ..... 23  
Regaining independence and the path to further development ..... 35  
Causes of lagging behind ..... 48  
What can be done? ..... 53  
Literature ..... 55

## Introduction

How to assess Latvia's achievements since regaining independence?

On the one hand, we have managed, albeit not without mistakes and sacrifices, to move from an administrative-directive economy to a market economy, to join the European Union (EU) and NATO, as well as the European Monetary Union (eurozone). Long forgotten are the empty shelves, restrictions on freedom of speech and travel. It is internationally believed that Latvia is already among the countries with a high standard of living<sup>1</sup>.

Latvia has had the longest period of democracy in its history. Latvia's achievements look particularly striking against the backdrop of the former Soviet republics that gained independence.

However, it cannot be denied that economic inequalities in society have risen sharply, and corruption and shadow economy which flourished in the 1990s are still endemic, many indicators of living standards and well-being place Latvia at the bottom of the EU statistical tables, and the country's population is shrinking year by year.

How to determine whether the best possible results have been achieved after regaining independence? I think the best way to do this is to compare Latvia with neighbouring Estonia and Lithuania. These countries are similar in size, historically we have a lot in common. That is why for more than 10 years I have been preparing comparative overviews of the economies of the three Baltic states, which have so far been presented to a small number of interested parties, mostly within the *Association of Economists*.

I soon noticed that Latvia was lagging behind not only Estonia, as is traditionally the case, but also Lithuania in many indicators. This became especially noticeable after the 2009 financial crisis. At first, I looked for a reason in political mistakes: wrong laws, tax rates, spread of corruption. However, there was no clear correlation with economic performance.

I was also not satisfied with the explanation that it was the 2009 crisis with the severe consequences of the bankruptcy of Parex Bank that was to blame. This only raised an additional question: why was it Latvia that suffered such a crisis?

---

<sup>1</sup> From 2020, the World Bank defines high-income countries as those with a GDP per capita above USD 12 535.

My work on books<sup>2</sup> on the Latvian economy suggested that during the Soviet occupation Latvia might have undergone some fundamental changes that made society less competitive.

It is possible that the economists are not able to find the reasons for this lag in development because the reasons lay in a different field, meanwhile the researchers in other fields largely ignore the issues of economic development. In this case, an interdisciplinary analysis of the problem is needed.

I will start by looking back at the economies of the Baltic states and their achievements in the last years before the war, and then compare their performance today. I will then move on to the events during the occupation, the restoration of independence and the transition to a market economy.

---

<sup>2</sup> Edmunds Krastiņš (2018). *Latvijas rūpniecība XIX–XXI gadsimtā*. (Latvian Industry in the XIX-XXI Century.) Riga: Jumava.

Edmunds Krastiņš (2019). *Kuģniecība Latvijā*. (Shipping in Latvia.) Riga: Self-published.

## **Economies of the Baltic States before World War II**

The fates of Latvians and Estonians have been very similar over the centuries. For more than six hundred years, both peoples lived under the rule of the Baltic German elites within Livonia, gradually losing their freedom and, with rare exceptions, being relegated to the status of peasants. Even after incorporation into the Russian Empire<sup>1</sup>, the status of the indigenous peoples of these territories did not change much, but rather their situation worsened. For almost 200 years, Estonians and Latvians lived side by side in the same Russian administrative territory, the Vidzeme province. The Baltics under Baltic German rule<sup>2</sup> still included the Latvian-populated Courland Governorate and the Estonian-populated Governorate of Estonia.

Under Emperor Alexander I, the peasants of the three Baltic provinces were granted their freedom (1816-1819), which triggered a rapid national awakening in the second half of the XIX century. Moreover, the Latvians were some 5-10 years ahead of the Estonians in this regard. Those Latvians who lived in the Vitebsk Governorate, the so-called Inflants<sup>3</sup>, were freed from serfdom together with other Russian peasants, including Lithuanians, in 1861. They hardly took part in the national awakening, and closer ties with the Baltic Latvians began to be established only in the beginning of the XX century.

The fate of Lithuanians was different. Lithuania once stretched from the Baltic Sea to the Black Sea, the Lithuanians had their own aristocracy and kings, and an independent country until 1569. The establishment of the Polish-Lithuanian Commonwealth was followed by polonization of Lithuania. For educated Estonians and Latvians in the Baltics it was natural to transition toward becoming Germans, while for Lithuanians it were Poles. At the end of the XVIII century, after the Third Partition of Poland, a large part of Poland was incorporated into the Russian Empire. A part of the territory populated by Lithuanians became a part of Germany.

The fate of Lithuanians in the XIX century was significantly affected by the repeated Polish uprisings. After the 1830 uprising, the Vilnius University was closed, the name 'Lithuania' was not used in documents from 1842, and from 1852 only Russian was used in state institutions in the

---

<sup>1</sup> Estonia and Vidzeme were annexed to Russia in 1721, and Courland in 1795 after the Third Partition of Poland.

<sup>2</sup> This rule was described in 1869 by Professor Carl Schirren from the University of Tartu: "Freedom of belief. German rule and language. German law."

<sup>3</sup> From the name of the principality of Inflantia, which was a part of Poland until 1772.

Lithuanian-populated provinces. After the 1863 uprising, russification intensified, and Latin script was banned. The Lithuanian national awakening did not begin until the 1880s.

When the rapid industrialisation of Russia began in the late XIX century, Riga became one of its most important industrial centres.

All three nations managed to establish independent states at the end of the World War I, which gave them just over 20 years of independent development. Lithuania, however, was in a politically different situation, having briefly gained and then lost the Vilnius region to Poland in the changing post-war environment.<sup>4</sup> Germany's Memel (Klaipėda)<sup>5</sup> became an Entente protectorate under the Treaty of Versailles and was to be transformed into a free city. However, Lithuania acted too fast and took Klaipėda by force in 1923.

Latvia, which for almost the entire duration of the war was crossed by the front line and where there was active warfare, is believed to have been the second most affected country after Belgium.<sup>6</sup> When the threat of German troops invading Riga became very real in 1915, almost all factories were evacuated to the inner Russia. However, in the 1920s, despite the need to reorient itself away from the lost market of the Soviet Russia, the economy was successfully developing. 1938 was the last year when the economies of the Baltic states were not yet affected by the outbreak of World War II. I will therefore use this year or, if data are not available, another closer pre-war year to compare the progress made by the countries in the short period of independence.

The population and national composition at that time can be found in Table 1.

Table 1

<b>Population and national composition in 1939 (within 1945)</b>					
<b>Country</b>	<b>Population (thousands)</b>	<b>Main ethnic group</b>	<b>Germans</b>	<b>Jews</b>	<b>Russians</b>
Estonia	1 052	92%	1.5%	-	8%
Latvia	1 951	77%	3%	5%	10%

<sup>4</sup> According to the 1897 Russian census, Vilnius had 155 000 inhabitants, whose native language was Yiddish (46%), Polish (31%) and Lithuanian (only 2%) (ethnic origin was not counted). (*Первая всеобщая перепись населения Российской империи 1897 года. IV. Виленская губерния, тетр. 3* (The First General Census of the Population of the Russian Empire in 1897. IV. Vilna Governorate, book 3) (1904), St. Petersburg. p. 91)

<sup>5</sup> According to the 1910 German census, there were 150 000 inhabitants living in Memel, 67 000 of whom had Lithuanian as their native language.

<sup>6</sup> Mārgeris Skujenieks (1928). *Latvija 1918.–1928. gados*. (Latvia in 1918-1928.) Riga: *Valsts statistiskā pārvalde*. (State Statistical Office.) p. 3

Lithuania<sup>7</sup>                      3 100                      76%                      5%                      7.7%                      3%<sup>8</sup>

In Latvia, the number of both Germans and Jews had fallen since 1925, while the number of Russians had risen.

These figures show that Estonia was the most ethnically homogeneous, Latvia had significant number of Russians and Jews, and a small but economically influential German minority. In Lithuania, Jews were economically important, as were the Germans of Klaipėda.

The role of minorities in Latvian industry did not correspond to their proportion in the population. The 1935 census of craft and industrial enterprises found that out of a population of 1 000 of a given ethnic group, 24 Latvians, 32 Germans and 53 Jews were individual entrepreneurs. The census also classified commercial enterprises according to the ethnicity of their owners and found that of the products produced by 922 collective enterprises, 24% were produced by Latvian companies, 36% German and 35% Jewish.<sup>9</sup>

Although Germans accounted for only three percent of Latvia's total population, they received 16% of all revenue of income tax payers in 1934.<sup>10</sup>

The comparative level of industrial development in the current territory of the Baltic states in 1937 is shown in Table 2.

Table 2

Country	Industry in the Baltic States in 1937			
	Number of enterprises	Employees (thousands)	Produced in million lats	Produced per capita in lats
Estonia <sup>11</sup>	1 149	54.8	221.8	196
Latvia	5 139	100.2	570.3	292
Lithuania <sup>12</sup>	1 834	43.8	421.7	111

<sup>7</sup> The only inter-war census in Lithuania happened in 1923. It did not take place in the Vilnius and Klaipėda regions and counted 2 029 000 inhabitants. (*Lietuvos gyventojai: pirmojo 1923 m. rugsėjo 17 d. visuotino gyventojų surašymo duomenys, Kauno* (Population of Lithuania: Data of the First General Population Census of 17 September 1923, Kaunas), 1924, p. 13)

<sup>8</sup> Poles.

<sup>9</sup> Krastiņš. *Latvijas rūpniecība*. (Latvian Industry.) pp. 102-103.

<sup>10</sup> Arnolds Aizsilnieks (1976). *Latvijas saimniecības vēsture 1914–1945*. (History of the Latvian economy 1914–1945.) Stockholm: Daugava, p. 605.

<sup>11</sup> Estonian Economic Yearbook for 1938 (1939). Tallinn: Eesti Pank.

<sup>12</sup> *Lietuvos statistikos metraštis 1937 m.* (Lithuanian Statistical Yearbook 1937) Kaunas: Spindulio. Data for Vilnius region from: *Mały rocznik statystyczny 1939*. (Small Statistical Yearbook 1939.) Warsaw: Nakład głównego urzędu statystycznego. (Circulation of the Central Statistical Office.)

It can be concluded that industry in Latvia and Estonia was much more developed than in the territory of the present-day Lithuania.

In 1935, 13.5% of Latvia's economically active population worked in industry, 15.5% – in Estonia, 6.5% – in Lithuania (excluding Vilnius region). The Klaipėda region was important to Lithuania, whose industry employed more than 9 000 workers in 1937 (20% of the total number of employed in national industry).

At that time, agriculture remained the dominant economic sector in all Baltic states. It accounted for the largest share in Lithuania, where the workforce employed in agriculture amounted to 79%, 67% in Latvia and 63% in Estonia. The yields of the main crops and the number of livestock are summarised in Table 3, with tonnes of cereal crops produced and the number of livestock per 100 capita in brackets. It can be seen from this table that agriculture was developed in all three countries, however, it was relatively less important in Estonia, while Latvia led the way in most indicators. It should be concluded that Lithuania having by far the highest share of employment in agriculture was less productive.

Table 3

**Agriculture the Baltic States in 1938<sup>13</sup>**  
(In brackets – tonnes or number per 100 capita)

<b>Indicator</b>	<b>Estonia</b>	<b>Latvia</b>	<b>Lithuania</b>
Rye, thousand tonnes	410 (36)	825 (42)	1 359 (53)
Wheat	186 (16)	418 (21)	548 (21)
Barley	211 (19)	481 (24)	597 (23)
Potatoes	2 174 (192)	3 817 (194)	4 616 (181)
Horses, thousands	219 (19)	400 (20)	557 (22)
Cattle	661 (58)	1 224 (62)	1 193 (47)
Sheep	650 (57)	1 360 (69)	619 (24)
Pigs	385 (34)	813 (41)	1 249 (49)

Let us look at a number of other indicators of national economic development in the late 1930s (Table 4).

---

<sup>13</sup> Statistical Yearbook of Latvia 1939. Riga: *Valsts statistiskā pārvalde*. (State Statistical Office.) pp. 268-271, the author's calculations.



This table shows that Lithuania is lagging far behind in a number of important indicators of economic development. In addition, the illiteracy rate is particularly striking: 33% in Lithuania in 1923, 13% in Latvia in 1930 and only 5% in Estonia in 1934.<sup>14</sup>

Table 4

**Some indicators for the economies of the Baltic states<sup>15</sup>**  
**(In brackets – units per capita)**

<b>Indicator</b>	<b>Estonia</b>	<b>Latvia</b>	<b>Lithuania</b>
Electricity generated, million kWh	112 (99)	193 (98)	37 (15)
Newspapers, million copies	24 (21)	27 (14)	33 (13)
Telephone calls, millions	30 (27)	114 (58)	22 (9)
Export, million lats	144 (127)	227 (115)	212 (9)
Cars (in brackets per 1000 capita)	5003 (4.4)	6687 (3.4)	2722 (1.1)

Unfortunately, the Latvian government's currency policy after the 1929 world economic crisis had a negative impact on its economic development. Estonia had already abolished its currency peg to gold in 1933, while Latvia did so only in 1936.

As a result, for example, the tonnage of Latvia's merchant fleet had risen from 190 000 tonnes in 1935 to only 194 000 in 1938, while that of Estonia during the same period rose from 126 000 to 177 000 tonnes, almost catching up with Latvia.<sup>16</sup>

In summary, it can be concluded that all three Baltic states were still predominantly agrarian economies before the outbreak of World War II. However, Estonia and Latvia had made significant progress in industrialisation and modernisation, reflected in higher living standards.

<sup>14</sup> Voldemārs Salnais (1937). *Latvija skaitļos starp Eiropas valstīm*. (Latvia in Numbers among European Countries.) From: *Latvijas zeme, daba, tauta*. (Latvian Land, Nature, People.) Riga: Valters un Rapa. pp. 605-676, here p. 620.

<sup>15</sup> Statistical Yearbook of Latvia 1939. Riga: *Valsts statistiskā pārvalde*. (State Statistical Office.) pp. 276, 281, 283 - 284, the author's calculations.

<sup>16</sup> Voldemārs Salnais (1937). *Latvija skaitļos starp Eiropas valstīm*. (Latvia in Numbers among European Countries.) Here p. 659.

According to the researchers' calculations<sup>17</sup>, Latvia's per capita gross domestic product had risen from 1 929 US dollars<sup>18</sup> in 1922 to 4 048 US dollars in 1938, Estonia's – from 2 311 US dollars to 3 771 US dollars. In 1938, Latvia's per capita GDP might have been around 65% of the level of Great Britain and 81% of that of Germany.

---

<sup>17</sup> Joan N. Roses, Nikolaus Wolf (2011). Aggregate growth, 1913–1950. In: edited by Stephen Broadberry and Kevin H. O'Rourke. The Cambridge economic history of modern Europe, volume 2. New York: Cambridge University Press. pp. 182–207. Here p. 190.

<sup>18</sup> Calculations in 1990 international US dollars. See Angus Maddison (2003). The World economy: Historical statistics. OECD.

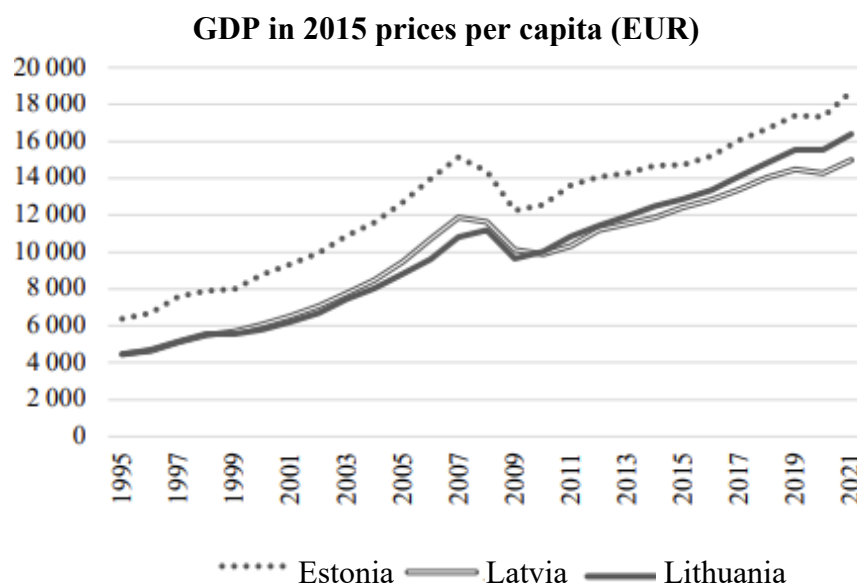
## Current Situation

First, we need to make sure that the current economic and social development indicators compared to Estonia and Lithuania really show Latvia in a bad light. For this purpose, I will first show the dynamics of the main indicators since the Baltic states regained independence and joined the EU, and then the positions in the ranking tables of various social indicators.<sup>1</sup>

The main indicator of a country's overall economic situation is its gross domestic product (GDP) – the value created in a country during the year. To compare economies of different sizes, it is usually measured per capita. However, to eliminate the effects of inflation in comparisons, GDP is converted into constant prices taking as the basis prices in a given year. The purchasing power of money is measured using the concept of purchasing power parity, i.e. comparing the prices of different goods and services between countries. GDP expressed in this way is called GDP at Purchasing Power Parity (PPP).

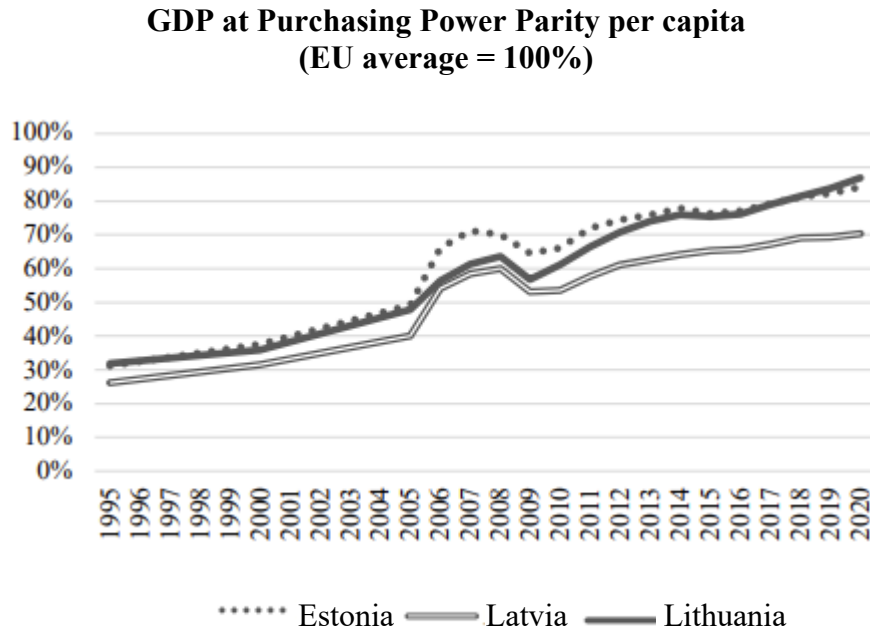
GDP per capita in 2015 prices is shown in Graph 1, and GDP at Purchasing Power Parity as a percentage of the EU average is shown in Graph 2. These show that since the 1990s, Latvia has been lagging far behind Estonia, while the gap with Lithuania has become more pronounced after the 2009 crisis.

Graph 1

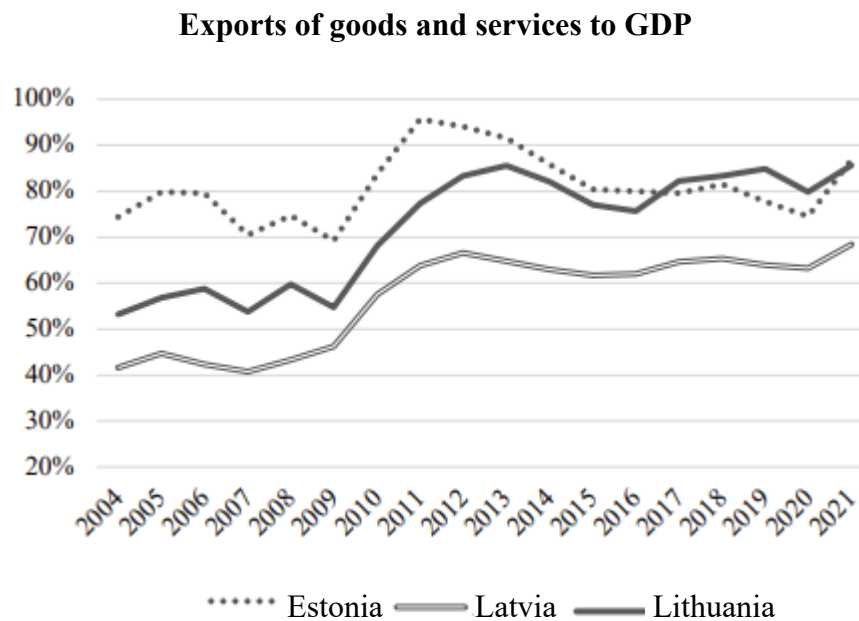


<sup>1</sup> All data, unless otherwise indicated, are taken from the Eurostat database. In some cases, the author's calculations.

Graph 2



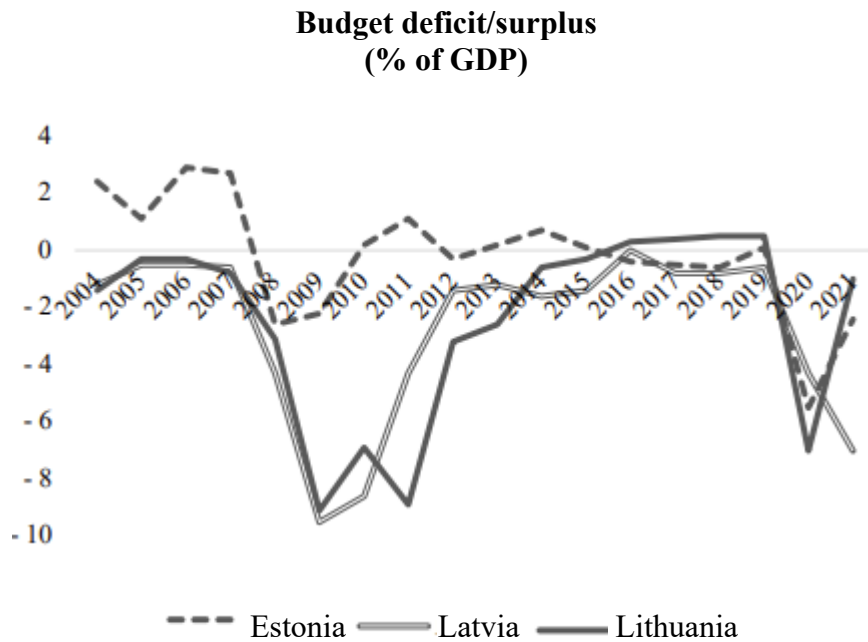
Graph 3



One of the reasons for these GDP figures is Latvia's lower export performance, as shown in Graph 3.

Since regaining independence, Estonia has pursued a very conservative fiscal policy, avoiding budget deficits. This may also have led to a different attitude towards the development of the banking system. Latvia and Lithuania were much more relaxed in this respect, as shown in Graph 4. However, since 2014, Lithuania's financial discipline has improved significantly (of course, the deviation caused by the Covid-19 crisis and the European Commission's requirements in all Baltic states have to be taken into consideration).

Graph 4



The use of GDP as the main performance indicator of a country's development has been criticised as too one-sided and ignoring other factors of well-being. There have therefore been attempts to create more inclusive development performance indicators that take into account not only economic performance but also other relevant indicators. One such indicator is the UN Human Development Index (HDI).

The UN proposes the HDI as a summary indicator of the main aspects of development, including life expectancy, human education and economic level.<sup>2</sup> The index is calculated according to a formula, taking into account life expectancy at birth, years of schooling for adults

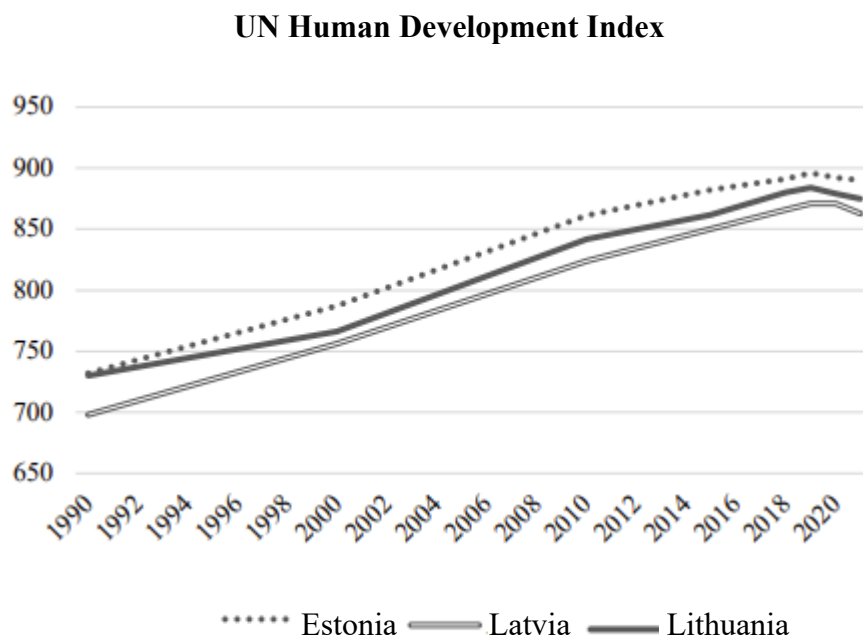
<sup>2</sup> Human Development Index (HDI). Available at: <https://hdr.undp.org/data-center/humandevlopment-index#/indicies/HDI> (viewed 01.11.2022.).

and national income per capita. The dynamics of the HDI for the Baltic states are shown in Graph 5.<sup>3</sup>

Latvia has been lagging behind in this indicator since regaining independence, but unlike what can be observed in Graphs 1 and 2, it has not been affected by the 2009 crisis. The HDI for all Baltic states, however, has worsened since 2018, likely due to the impact of the Covid-19 pandemic.

A more detailed index, taking into account more indicators, has been developed by the non-profit organisation *Social Progress Imperative*. The index stands out because its academic advisor is a world-renowned researcher of competitiveness, Professor Michael Porter of Harvard Business School. The Social Progress Index consists of three elements: basic needs, foundations of wellbeing and opportunity. In 2022, Estonia ranked 18<sup>th</sup>, Lithuania 29<sup>th</sup> and Latvia 32<sup>nd</sup> in this index.<sup>4</sup>

Graph 5



<sup>3</sup> Trends in the Human Development Index, 1990-2021. Available at: [https://hdr.undp.org/sites/default/files/2021-22\\_HDR/HDR21-22\\_Statistical\\_Annex\\_HDI\\_Trends\\_Table.xlsx](https://hdr.undp.org/sites/default/files/2021-22_HDR/HDR21-22_Statistical_Annex_HDI_Trends_Table.xlsx) (viewed 01.11.2022).

<sup>4</sup> Available at: <https://www.socialprogress.org/global-index-2022overview> (viewed 18.01.2023).

In the Global Competitiveness Index,<sup>5</sup> which measures the institutions, policies and factors that determine the level of productivity, published by the World Economic Forum in 2019, Estonia ranked 31<sup>st</sup>, Lithuania 39<sup>th</sup> and Latvia 41<sup>st</sup>. Here the gap, at least with Lithuania, does not seem to be large.

Eurostat publishes statistics on many socio-economic indicators. The most representative (in my opinion) of them I have summarised in Table 5, taking the most recent data available and selecting as few interrelated indicators as possible. The table includes three causes of mortality, which are representative of different social manifestations. Homicides reflect the level of violence, deaths from road accidents are influenced by driving culture, suicides are a sign of a disturbed relationship between the individual and society, which may be caused by exclusion, poverty, health problems. Here are the rankings of countries in the EU table, sorted with higher rankings being more socially desirable.<sup>6</sup>

Table 5

**Various socio-economic indicators  
(ranking in EU countries table)**

<b>Indicator</b>	<b>Estonia</b>	<b>Latvia</b>	<b>Lithuania</b>
Years of healthy life	23	27	25
Total fertility rate	10	12	16
Infant mortality rate (from lowest)	1	18	10
Proportion of university graduates	24	19	11
Unemployment	15	23	20
Income inequality <sup>7</sup>	17	26	25
Risk of poverty	19	23	21
Homicides <sup>8</sup>	25	27	26
Road deaths	4	23	19
Suicides	22	23	27
Use of the internet <sup>9</sup>	12	13	20
Digital skills <sup>10</sup>	13	16	17
Sum of rankings	185	250	237

<sup>5</sup> Klaus Schwab (editor) (2019). The Global Competitiveness Report 2019. Geneva: World Economic Forum. p. xiii.

<sup>6</sup> For example, years of healthy life are ranked first for longer life expectancy, while unemployment is ranked first for lower unemployment.

<sup>7</sup> Gini coefficient.

<sup>8</sup> All deaths are expressed per 100 000 inhabitants.

<sup>9</sup> People who have used the internet in the last three months.

<sup>10</sup> People with skills beyond basic.

Eurostat data do little to reflect the results achieved in important sectors such as education. Nor are there indicators on tax discipline, business culture, level of corruption, loyalty to the state, trust between people.

However, the OECD<sup>11</sup> regularly assesses countries' primary education achievements by testing 15-year-old students' proficiency. This assessment is abbreviated as PISA<sup>12</sup> and was last carried out in 2018. The results for the Baltic states are presented in Table 6. They show a significant advantage for Estonian students, with Latvia and Lithuania close behind. However, the level of bullying/harassment in schools found in Latvia is ominous, and may result in young people being less competitive, psychologically scarred, who will struggle to achieve high results in life.

Table 6

<b>PISA assessment results</b>				
<b>Indicator</b>	<b>Estonia</b>	<b>Latvia</b>	<b>Lithuania</b>	
Literacy	523	479	476	
Mathematics	523	496	481	
Natural sciences	530	487	482	
Low results for all indicators, %	4.2	9.2	13.9	
Plan to work in ICT at age 30, %	9.9	7.2	10.1	
Experienced bullying/harassment, % <sup>13</sup>	25.4	35.5	22.6	

In higher education, comparative indicators are published by many of the organisations that rank universities. Table 7 summarises the latest university rankings published by several well-known organisations. Critics of these rankings, however, point out that they reflect the quality of research rather than the quality of teaching. And, as we know, Latvia is not doing well in research at all. However, there is also no reason to believe that the quality of teaching is any better.

---

<sup>11</sup> Organisation for Economic Co-operation and Development (OECD), which unites 38 of the world's developed countries (including the Baltic states).

<sup>12</sup> Programme for International Student Assessment. No country in the world has a student proficiency score higher than 600.

<sup>13</sup> The OECD average is 23%.



**Rankings of Baltic universities**

University	QS	Times	ARWU	U.S. News	CWUR
University of Tartu	296	201-250	501-600	256	526
Vilnius University	400	801-1000	701-800	801	699
University of Latvia	1001-1200	801-1000	-	1022	1542
Riga Technical University	751-800	1201-1500	-	-	-
Riga Stradiņš University	801-1000	601-800	-	-	-

The Stockholm School of Economics in Riga (SSE Riga) annually assesses the size of the shadow economy in the Baltics.<sup>15</sup> The study shows that Latvia has had the highest share of the shadow economy since at least 2009, rising to 25.5% in 2020 after a temporary decrease since 2016. Lithuania had a shadow economy rate of 20.4% and Estonia 16.5%.

The authors of the study link the level of the shadow economy to the state of business environment. When it comes to assessment of satisfaction with the state revenue service, tax policy, quality of business legislation and government support, Latvian entrepreneurs have for years been markedly more dissatisfied than their counterparts in Estonia and Lithuania.

One example is the attitude towards the State Revenue Service, which in Estonia has been a highly rated institution since the 1990s, as opposed to Latvia, where the State Revenue Service has long been the bane of entrepreneurs.

The same study also provides insight into the potential level of corruption, concluding that companies paid 8.3% of their income in Latvia, 8.4% in Lithuania and 6.4% in Estonia to “settle cases” in 2020.<sup>16</sup> In Latvia, the amounts paid to secure winning public contracts have also risen since 2016. In 2020, they have reached 6.9% of the contract amount. The corresponding figure for Estonia was 3.9% and for Lithuania 5.6%.<sup>17</sup>

<sup>14</sup> QS – QS World University Rankings; Times – Times Higher Education World University Rankings; ARWU – Academic Ranking of World Universities; U.S. News – U.S. News & World Report Best Global Universities Rankings; CWUR – Center for World University Rankings.

<sup>15</sup> Arnis Sauka, Tālis Putniņš (2021). *Ēnu ekonomikas indekss Baltijas valstīs 2009.–2020. gadā* (Shadow Economy Index in the Baltic States 2009-2020) Available at: [https://www.sseriga.edu/sites/default/files/2021-06/SSERiga\\_Enu\\_ekonomikas\\_indekss\\_2009-2020\\_1.pdf](https://www.sseriga.edu/sites/default/files/2021-06/SSERiga_Enu_ekonomikas_indekss_2009-2020_1.pdf) (viewed 03.11.2022).

<sup>16</sup> This is unprecedentedly high for Estonia, which in previous years has been within the 3-5.8% range.

<sup>17</sup> In Lithuania, the rate was as high as 13.8% in previous years, but has fallen sharply in the last two years.

The Corruption Perceptions Index is published annually by Transparency International. The dynamics of this index over the last 20 years are shown in Table 8.<sup>18</sup> Moreover, Latvia has been “leading” the Baltics in this index almost every year since 2000.

Table 8

### Corruption Perceptions Ranking

Year	Estonia	Latvia	Lithuania
2021	13	36	34
2010	26	62	49
2000	27	57	43

It can be concluded that Estonia has already joined the ranks of relatively corruption-free countries, while Latvia and Lithuania are still lagging behind, although showing progress. Transparency International’s index, however, is accused of being subjective, i.e. that it does not measure the level of corruption that actually exists, but only perception of it based on feelings.

An important indicator is the country’s demographic dynamics. Graph 6 shows the evolution of the total population, while Graph 7 shows the number of the employed. These show that Latvia and Lithuania have been hit by severe depopulation, which makes them very different from Estonia, whose population has remained virtually unchanged over the last 20 years, while the number of the employed has even increased. Consequently, since 2000, Estonia’s share of the Baltics population has risen from 19% to 22%.

Recently, Oļegs Krasnopjorovs, Chief Economist of the Bank of Latvia, published a study comparing the competitiveness of the Baltic capitals. His conclusions: “Riga is the only city among the Baltic capitals where the death rate exceeds the birth rate and where more people leave than enter. This may be due to the relatively large number of Rigans who are not satisfied with either living in the city or the progress in quality of life over time.”<sup>19</sup> The reasons he gives for this are the poor quality of housing, which is prevented from improving by complex building formalities; safety; environmental pollution; and quality of governance. Because of these shortcomings, Vilnius has already overtaken Riga in terms of population.

<sup>18</sup> Data from <https://www.transparency.org/en/cpi/2021> (viewed 03.11.2022).

<sup>19</sup> Oleg Krasnopjorov (2022). *Kā Rīgai panākt Viļņu, Tallinu un Ziemeļeiropu?* (How Can Riga Catch up with Vilnius, Tallinn and Northern Europe?) <https://www.makroekonomika.lv/ka-rigai-panakt-vilnu-tallinu-un-ziemeleiropu-laikssecinajumiem> (viewed 24.11.2022.).

Differences in the pace and course of economic development can also be linked to the culture of the society. It is therefore worth looking at the *World Values Survey Association* data. This organisation has been active since the 1980s, surveys have been carried out in many countries around the world, asking people questions on a variety of topics about society, including whether they feel happy.

Table 9 summarises the percentage of affirmative responses to some of the important questions asked in the seventh wave of the survey.<sup>20</sup> For comparison, I have added Denmark, a prosperous Nordic country, to the table.

Table 9

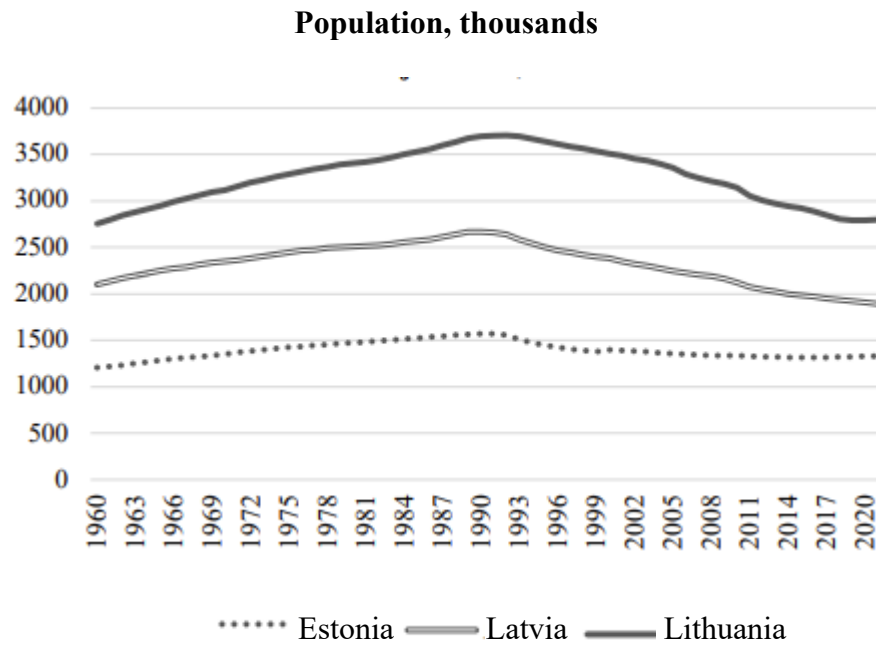
**Some questions from the World Values Survey**

<b>Question</b>	<b>Estonia</b>	<b>Latvia</b>	<b>Lithuania</b>	<b>Denmark</b>
Feeling very happy or quite happy	84	79	74	90
Most people can be trusted	34	22	32	74
Have a lot or quite a lot of trust in government	40	30	39	39
One should never cheat on taxes	64	52	46	74
It is absolutely essential to live in a democracy	50	35	40	78

---

<sup>20</sup> Data from <https://www.worldvaluessurvey.org/WVSONline.jsp> (viewed 04.11.2022). Surveys were conducted in Denmark in 2017, in Estonia and Lithuania in 2018 and in Latvia in 2021.

Graph 6



Graph 7



It can be seen that in terms of these answers, Estonia is almost always closer to Denmark than to its Baltic neighbours. The exception is mutual trust, but the situation here again in Estonia is much better than in Latvia. Mutual trust among people is crucial for an efficient and well-

functioning economic and political system. Its absence, as well as presence of corruption, creates additional bureaucracy and formalism, making it more difficult to solve problems quickly.

The OECD's assessment of trust in any given country's government is consistent with this survey, and its dynamics are shown in Graph 8.<sup>21</sup> It shows significant fluctuations linked to electoral cycles, possibly also to the Covid-19 pandemic. However, trust in government has almost always been higher in Estonia than in its neighbouring countries, and lower in Latvia.

There are many more such indicators, but I think there is a clear trend that Estonia almost always scores best, while Lithuania is usually close to Latvia, but in recent years it is more and more often ahead. It is quite likely that Lithuania's rapid economic development will continue to have a positive impact on these indicators.

Moreover, it cannot be said that this is a fluctuating or a temporary phenomenon. Estonia has been in the lead since regaining independence, so for 30 years, Lithuania has improved sharply since the 2009 economic crisis, so the trend has been sustained for more than 10 years.

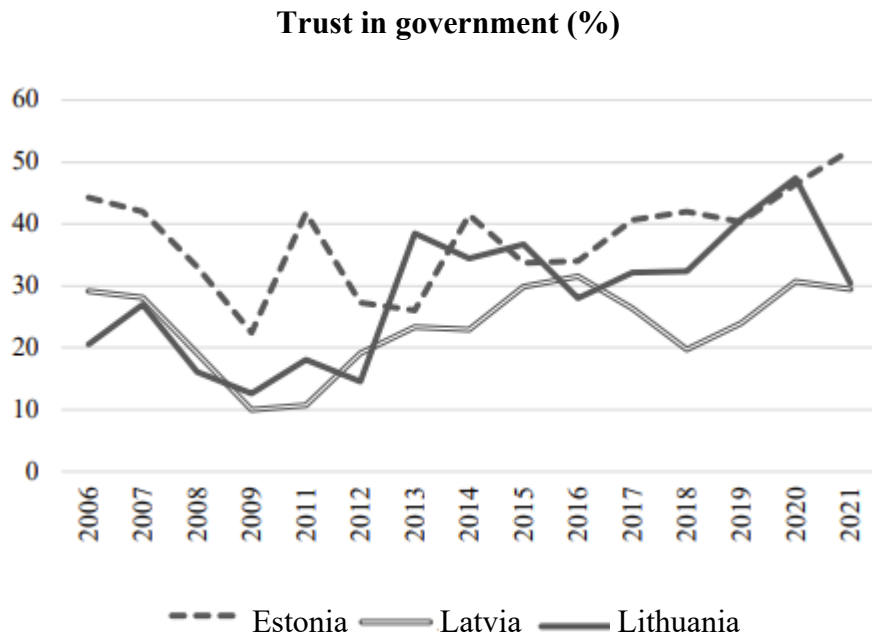
After consideration of what has been written in the previous chapters, the question arises: why has Latvia gone from being the Baltic leader in 1938 to a laggard? Moreover, the lag was already apparent immediately after regaining independence, and has become even more pronounced after the financial crisis of 2009.

In order to attempt to answer this question, we need to look at what happened during the 50 years of occupation.

---

<sup>21</sup> From <https://data.oecd.org/gga/trust-in-government.htm> (viewed 04.01.2023).

Graph 8



## What happened during the occupation?

On 22 March 1939, Lithuania was forced to give in to Germany's ultimatum and cede Klaipėda. But the outbreak of war on 1 September 1939 brought rapid changes to the usual life of Estonia and Latvia as well. The blockade of the Baltic Sea had a major impact on international trade, with many ships unable to return to their ports of call. The economic crisis in the Baltic States began.

Only the Lithuanians, who were given Vilnius by the USSR in October 1939 after the partition of Poland and a month-long occupation, could rejoice for a short time. The threat of occupation loomed ever larger over the Baltics.

The Secret Protocol of the German-Soviet Non-Aggression Pact of 23 August 1939 brought the Baltics within the sphere of influence of the USSR. Germany, acting in accordance with this treaty and anticipating the imminent occupation of the Baltics, began the resettlement of the Baltic Germans at the end of 1939, with a further departure taking place after the occupation, in the spring of 1941. In the course of this campaign, more than 60 000 people left Latvia (not only Germans, but also Latvians), and more than 20 000 people left Estonia. In Latvia, at least in official documents and in the press, this departure was greeted with joy, in an attempt to suppress signs of panic and anxiety about the loss of an educated and influential part of society.

In 1941, more than 50 000 so-called *Deutsche aus Litauen*<sup>1</sup> (Germans from Lithuania) were resettled from the territories annexed to Lithuania after the partition of Poland.

At the end of 1939, the Baltic states were forced to conclude agreements with the USSR to establish military bases on their territories. But in June 1940 they received an ultimatum from the USSR regarding the entry of their troops and change of governments. None of the countries launched armed resistance. Lithuanian President Antanas Smetona, who voted against the USSR ultimatum, left the country.

Under the supervision of USSR representatives, puppet governments were appointed, parliamentary elections were simulated, after which all three countries asked to be admitted to the USSR. Even before that, the sovietisation of the economy had already begun, with the nationalisation of land, enterprises and the introduction of top-down management methods.

---

<sup>1</sup> Lithuanian Germans are not regarded as Baltic Germans, their history is different. In 1920, about 45 000 Germans lived in Lithuania.

The incorporation into the USSR was accompanied by increasing repression of people who were not wanted by the Soviet authorities, culminating in June 1941, when mass deportations were directed against the most socially and economically active part of the population. It should be noted that the Jews were disproportionately affected by the deportations. In Estonia, 10% of all Jews were deported, in Latvia 1.9%, in Lithuania 1%. This was a higher proportion than for the core nationalities and can be explained by the fact that there were more economically active people among the Jews.

Germany attacked the USSR on 22 June 1941, and within a month the Baltic states were occupied by the German army. The extermination of the Jews began in the first days of the German occupation. Such actions affected Latvia and Lithuania extensively, in contrast to which Estonia was left with a very small number of Jews. By 1943, the Jewish minority in these territories had been virtually wiped out.

When the German army was driven out in 1944, a large number of Baltic citizens went with it, seeing their existence under Soviet rule as severely threatened, remembering the experience of 1941. Data on the number of these refugees is controversial, and it is not known how many died fleeing.

Another wave of repressions hit the Baltics in March 1949, during the collectivisation campaign, when mostly peasants were deported.

Table 10 summarises the population loss between 1939 and 1949. It should be remembered that those who were subjected to repressions in 1941 and 1949, but survived, could return to their homeland in large numbers only after 1956. And even then they were often subjected to discrimination in terms of employment, education and housing. Information on war-related deaths and refugees is scarce and often contradictory, so the direct losses caused by the war have been calculated as the difference between the more reliably known figures.

Lithuania's population loss is even harder to calculate, given its rapidly changing borders during this period. For example, after the war, around 150 000 Poles left the Vilnius region and moved to Poland, while at least 100 000 Germans left Klaipėda.

The loss of population since 1939 has been enormous, both in terms of numbers and quality. Influential minorities (Germans, Jews) and a large part of the most educated<sup>2</sup> and active people

---

<sup>2</sup> Claims have been made that only half of those who had higher education stayed in Latvia.



were lost. It is very likely that it was Latvia that suffered the greatest losses, both in terms of minorities and in terms of the quality of those who left.

One of the most detailed estimates of the loss of population is given by Misiunas and Taagepera, who estimate that in 1939-1945 Estonia lost 25% of its population, Latvia 30%, Lithuania 15%.<sup>3</sup>

Table 10

**Loss of population in the Baltic states 1939-1949  
(thousands)**

	<b>Estonia</b>	<b>Latvia</b>	<b>Lithuania</b>
Resettlement of Germans	21	61	52
Deportations of 1941	10 <sup>4</sup>	15	17
Holocaust	1	70	190
Losses in war/resistance	16	80	55
Refugees in 1944-1945	80	165	440
Deportations of 1949	21	42 <sup>5</sup>	75 <sup>6</sup>
Total	149	433	512
% of population in 1939	14	22	14

The Soviet regime sought to fill the vacuum, all the more so because it wanted to establish itself more firmly in the newly acquired region. This is why the reversal of war damage was faster in the Baltics than in other war-ravaged areas. From the 1950s onwards, the Baltic republics began to industrialise intensively, which, under the conditions of extensive Soviet management, required continuous recruitment of labour.

An eyewitness wrote in his diary in 1946 about the influx of newcomers: “Everybody is flocking here because Russia is telling legends about the prosperity of our land... I guess they want to colonise our land rapidly. Murder, theft, etc. everywhere” and “Our land is being flooded by horribly ragged, filthy and starving Russian hordes. Filth, misery, deceit everywhere. It hasn’t been this hard ... since 1919.”<sup>7</sup>

<sup>3</sup> Romuald Misiunas, Rein Taagepera (1993). *The Baltic States. Years of Dependence 1940–1990*. London: Hurst&Company. p. 354.

<sup>4</sup> In the second half of the 1950s, 4.3 thousand of deported in 1941 returned to Estonia and around 10 thousand returned to Latvia.

<sup>5</sup> More than five thousand did not return.

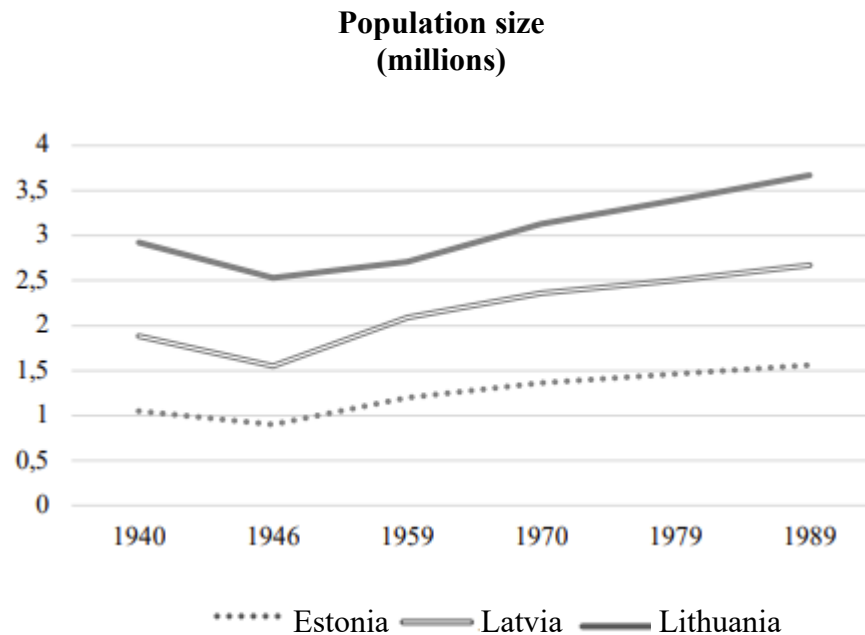
<sup>6</sup> Three deportations were carried out due to the widespread resistance movement in Lithuania after the war. Some 60 000 later returned to Lithuania.

<sup>7</sup> Kaspars Irbe (2021). *Slēptā dzīve*. (The Hidden Life) Riga: Ascendum. pp. 385, 387.

The growth of the Baltic population during the Soviet period is shown in Graph 9. In the 40 post-war years, Estonia's population grew by 72%, Latvia's by 73% and Lithuania's by only 45%. Lithuania's lower population growth can be explained by the fact that it still had significant reserves of potential labour in the countryside – in contrast to more urbanised Estonia and Latvia.

Population growth was largely due to both controlled and uncontrolled migration from other regions of the USSR. The changes in the share of the population of the main ethnic group in 1959-1989 are shown in Graph 10. The stable share of Lithuanians was also due to the significantly higher natural growth rate. In the 1950s, in Lithuania it was 9-12 per 1 000 inhabitants, while in Estonia and Latvia it was only 4.1-6 per 1 000 inhabitants.

Graph 9



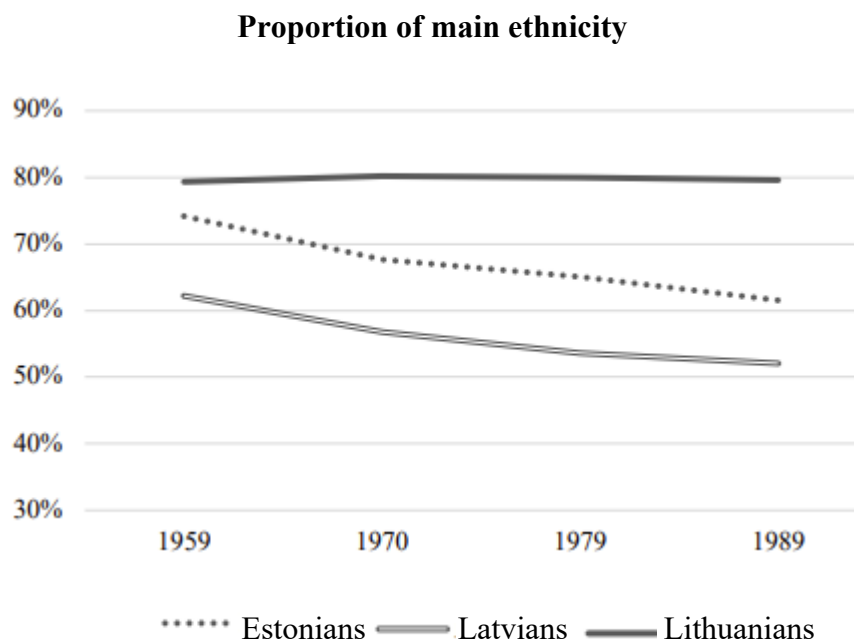
Immediately after the war, both party functionaries and specialists from the USSR came to the Baltics to implement the Soviet system of governance. The peculiarity of Latvia was that in the USSR, even after Stalin's great terror in 1937-1938, there was still a much larger number of communists of Latvian origin (4346) than of Estonian (1804) and Lithuanian (1228) origin put together.<sup>8</sup> This was probably a consequence of the importance of Riga for the development of

<sup>8</sup> Елена Зубкова (2008). *Прибалтика и Кремль: 1940–1953 гг.* (Elena Zubkova (2008). *The Baltic States and the Kremlin: 1940–1953*) Moscow: *Российская политическая энциклопедия.* (Russian Political encyclopedia.) p. 146.

social democracy in the Russian Empire, the large refugee movement from Latvia in 1915 and the important role of the Red Riflemen in strengthening the Bolshevik regime.

Researcher Yelena Zubkova calls such people, who have lived in Russia for a long time or who were born in the Baltic ethnic groups, ethnic fringe groups.<sup>9</sup> According to the questionnaire of the party cadres, they belonged to the core ethnic group of the Union Republic, but they usually had little or no knowledge of its language. However, they were socialised into the Soviet culture, knew the workings of the Soviet administrative system, were grateful to Moscow for their promotion and were therefore obedient. In Moscow, such ethnic fringe groups were considered more loyal than local communists. In 1945 alone, 540 such “national” cadres were sent to Latvia.<sup>10</sup>

Graph 10



Richard Mole writes: “... the sovietisation of Estonia, Latvia and Lithuania had to achieve two objectives simultaneously: first, to dismantle the bourgeois socio-economic structures and the democratic multi-party political system associated with the inter-war period (at least for the first years) and to introduce a new social organisation that would meet the requirements of Marxism-Leninism; and second, to create a new social reality in which the Soviet control and the Communist

<sup>9</sup> *Зубкова. Прибалтика и Кремль.* (Zubkova. The Baltic States and the Kremlin.) p. 278.

<sup>10</sup> *Krastiņš. Kuģniecība Latvijā.* (Shipping in Latvia.) p. 207.

Party power would appear legitimate.”<sup>11</sup> At least in Latvia, the achievement of the first objective was made much easier by the years of the authoritarian regime of Ulmanis, during which a great deal of preparatory work had been done.

As Epp Annus points out, “... the early Soviet years in the Baltic states were years of discursive confusion, where two different value systems, Soviet and pre-Soviet, clashed unhappily.”<sup>12</sup> Initially, both official and artistic (socialist realism) discourse was dominated by official Soviet values. According to Annus, later the official and artistic discourses partially separated, which in the XX century led to the emergence of a new Soviet discourse. In the 1980s, this suddenly manifested itself in two radically different assessments of the past: the majority of immigrants did not recognise that the Baltic states was occupied in 1940.

The massive migration and russification probably caused at least some discomfort even among the local communists, who occasionally tried to resist it. This resistance, however, could not take a consistent form, especially under Stalin’s rule.

Already in 1949-1950, the leadership of the Communist Party of Estonia was replaced under accusations of nationalism. This, however, can hardly be regarded as a purge of national communists, since the replaced first secretary, Nikolai Karotamm, was one of the organisers of the post-war repressions. Rather, it was a personal relations reshuffle, which Moscow used to effect a major change in the power structures, replacing many local communists.

These changes were led by Johannes Käbin, the Propaganda and Agitation Secretary of the Central Committee of the Communist Party of Estonia, who had grown up in the USSR and was initially a strong Stalinist. He was afterwards the First Secretary of the Central Committee of the Communist Party of Estonia for many years (1950-1978), however, after Stalin’s death he took a more moderate, manoeuvring position in relations with Moscow, also taking into account Estonia’s interests. From the late 1950s onwards, he appointed to leading positions people who under the Soviet rule could be considered “national communists”.

In the 1970s, Käbin himself was accused of defending national communists (e.g. Arnold Rüütel, later President of Estonia).

---

<sup>11</sup> Richard Mole (2012). *The Baltic States: from Soviet Union to European Union*. Routledge. p. 57.

<sup>12</sup> Epp Annus (2016). *Between arts and politics: A postcolonial view on Baltic cultures of the Soviet era*. *Journal of Baltic Studies*, 47 (1), pp. 1–13. Here p. 3.

The change of leadership in Estonia can be seen as a dress rehearsal for Moscow's relations with the recalcitrant Union Republics. This time, however, it was limited to a "coup" against the leadership, without turning into a full-scale "purge" of the party ranks.

Vilis Krūmiņš (Second Secretary of the Central Committee of the Communist Party of Latvia) and Eduards Berklavs (Vice-Chairman of the Council of Ministers), who came to the leadership of Latvia after Stalin's death, exploited the passivity of Jānis Kalnbērziņš, First Secretary of the Central Committee of the Communist Party of Latvia, and Vilis Lācis, Chairman of the Council of Ministers, to promote local Latvians to positions of responsibility and tried to curb uncontrolled immigration and subsequent russification. In 1958, restrictions on registration<sup>13</sup> and requirements for Latvian language skills were imposed, and attempts were made to reorient the economy away from heavy engineering towards industries more typical of Latvia.

These measures provoked dissatisfaction among conservative party members and a flood of complaints to Moscow. This was exploited by the consistent Stalinist, the cunning master of the Soviet bureaucracy, the Propaganda and Agitation Secretary of the Central Committee, Arvīds Pelše. Having gained support in Moscow, he, with the help of Augusts Voss, who at that time headed the Party Organs Department of the Central Committee, began to take over the Communist Party of Latvia. This campaign, later called the purge of the national communists, lasted about two years. First, Pelše secured the dismissal of the presumed national-communist leader Berklavs and his transfer to Russia in July 1959. This was done, moreover, while isolating Berklavs and getting almost all other leading national-communists to stand against Berklavs and try to save themselves by self-criticism.

Pelše then became First Secretary of the Central Committee of the Communist Party of Latvia and led the replacement of dozens of leading party figures, mainly by reassignment to minor posts outside Riga. The editor of the newspaper *Cīņa* Pāvels Pizāns, the First Secretary of the Riga Party Committee Aleksandrs Straujums, the Trade Union Chairman Indriķis Pinksis, the Secretary of Industry Nikolajs Bisenieks, the Deputy Chairman of the State Plan Committee Edgars Mūkins, the Deputy Health Minister Jānis Prombergs, the First and Second Secretaries of the Komsomol, Vladislavs Ruskulis and Jānis Brence, were dismissed from their posts.<sup>14</sup> Pelše then took control

---

<sup>13</sup> Since the 1930s, the USSR has had a registration system that limited the freedom to choose where to live. This could be circumvented when attracting labour to new factories or sectors where labour was scarce.

<sup>14</sup> Michael Loader (2017). The death of "Socialism with a Latvian Face": The purge of the Latvian national communists, July 1959–1962, *Journal of Baltic Studies*, 48(2), pp. 161–181.

of the Bureau of the Central Committee of the Communist Party of Latvia, followed by the establishment of control in the Central Committee, and the replacement of the leading figures in the ministries and the main towns. The non-Latvians and Russian Latvians appointed in their place continued the purges at a lower level. Voss, in turn, was appointed to Pelše's previous post of Secretary of Ideology.

It is estimated that several thousand officials have been replaced within those few years. The purges significantly reduced the role of Latvians in the administration of the Latvian SSR, opening the door to immigration and russification.

Not only did A. Pelše get rid of leaders he did not want in the Latvian power structures, but in the early 1960s he initiated large-scale repressions of nationally-minded people by the KGB and banned the celebration of *Līgo* (Midsummer). Fun fact, Pelše proposed to rename Riga into Gagarin.

Like Kābin in Estonia, Antanas Sniečkus in Lithuania was also initially a staunch Stalinist, but as circumstances changed, he became more moderate and, as a true autocrat, stood up for the interests of the province he governed. He retained the post of First Secretary of the Central Committee of the Communist Party of Lithuania until his death in 1974<sup>15</sup>, and no purge of national communists was ever started in Lithuania. On the contrary, the Communist Party of Lithuania became Lithuanian. Of course, Sniečkus also followed a careful balancing act in his relations with Moscow, his masterful ability allowed him to stay in his post for so long. Lithuania can be seen as an example of what Ronald Suny argues: "As Khrushchev and particularly Brezhnev permitted national Communists to remain in power for many years, entrenched ethnic elites emerged in the non-Russian republics. By the last decades of the Soviet power, nationalities experienced an unprecedented degree of local autonomy."<sup>16</sup>

In stark contrast to Lithuania, under both Pelše and his successor in the position of First Secretary of the Central Committee, Augusts Voss, the Communist Party of Latvia was controlled by Russian Latvians together with representatives of other nationalities. Thus, in 1971, only three of the 13 members of the Bureau of the Central Committee were born in Latvia.<sup>17</sup> Another Russian

---

<sup>15</sup> Sniečkus had held this post since 1940.

<sup>16</sup> Ronald Grigor Suny (2012). The contradictions of identity: being Soviet and national in the USSR. In: Mark Bassin, Catriona Kelly (eds.). Soviet and Post-Soviet Identities. Cambridge University Press. pp. 17–36. Here p. 31.

<sup>17</sup> Romuald Misiunas, Rein Taagepera. The Baltic States. p. 206.

Latvian, Roberts Kīsis, Chairman of the Party Control Commission, was not far from Pelše and Voss in his views. In 1970, criticising teachers, he said: "... [they say] What do we need the Russian language for? We have Latvian – such a neutral position. And this is a broad base for aggressive nationalism."<sup>18</sup> Latvians made up less than half of the membership of the Communist Party of Latvia.

The policy of the Communist Party of Latvia was characterised by indulgence of and subservience to Moscow's interests, exaggerated industrial development, and strict control of cultural life. It is quite safe to say that cultural life was more restricted in Latvia than in Estonia and Lithuania.

Augusts Voss headed the Communist Party of Latvia for almost 20 years, until he was replaced in 1984 by the next "Latvian" – Boriss Pugo, who did not even know the Latvian language.

The proportion of ethnic minorities in the Communist Party of Estonia was much lower (52%)<sup>19</sup> than in Lithuania, but significantly higher than in Latvia. Russian Estonians, who were in the leadership of the Communist Party, are believed to have reintegrated better into their ethnic homeland than Russian Latvians. However, in 1978 Kābin was replaced as First Secretary by the Siberian-born Karl Vaino, who, like Voss, refused, at least publicly, to speak Estonian.

The Baltic states, the Soviet outpost in the Cold War against the West, were overflowing with military units and other military objects. The headquarters of the Baltic Military District was located in Riga. Riga also became one of the most popular places for Soviet army officers to retire.<sup>20</sup> It has been reported that in the 1980s up to a quarter of the newly built apartments were allocated to the Ministry of Defence.

Estonia was in a unique position as even under the Iron Curtain, when information from the West was kept to a minimum, the people living in the northern part of the country were able to watch Finnish television programmes. This became possible in 1971, when the Espoo TV broadcasting tower was built in Finland. This gave many Estonians the opportunity to learn the related Finnish language, to get impartial information and to become culturally closer to the West.

---

<sup>18</sup> Sauļus Grībkausks (2020). *Padomju "ģenerālgubernatori"*. (Soviet "Governors-General") Riga: Latvian media. p. 186.

<sup>19</sup> Romuald Misiunas, Rein Taagepera. *The Baltic States*. p. 207.

<sup>20</sup> After 20-30 years of service, officers could choose their place of residence (except Moscow and Leningrad), where an apartment was allocated to them.

Although the authorities tried to stop people taking advantage of this opportunity, Finnish TV broadcasts were much more popular in Estonia than Moscow TV.

Over a period of 20 years those Estonians who were able to watch Finnish TV acquired skills that later helped them adapt to life in a market economy and make better decisions during the period of regaining and establishing independence.

This Finnish TV presence was probably one of the reasons why, in the context of the increasing russification pressure in the second half of the 1970s, Estonians were the only ones whose positive self-assessment of their knowledge of Russian had fallen from 29% to 24% in 10 years. In Latvia it had risen to 57%, in Lithuania to 52%.<sup>21</sup> Ronald Suny writes of Estonians: “Some, like most Estonians, simply rejected the Soviet Union and along with it Russia, and lived exclusively within their own ethnic community.”<sup>22</sup>

After a break of more than 25 years, regular ferry services between Tallinn and Helsinki resumed in 1965. In the first year, more than 10 000 passengers arrived in Tallinn; the following year, the number exceeded 25 000. The contacts of these tourists with the locals were limited and monitored, but they did occur.<sup>23</sup> Many exiled Estonians also came to visit by ferries. The contacts established after the regaining independence helped to start businesses and facilitate other types of relations.

Another opportunity to get closer to the free world came in 1980, when the sailing competitions of the XXII Summer Olympics were held in Tallinn. Although many countries boycotted the Games in protest against the USSR’s invasion of Afghanistan, Tallinn benefited greatly.

The International Sailing Federation originally proposed to hold the regatta in Riga, but the Latvian SSR leadership hesitated and spent half a year making calculations before Tallinn took the initiative.<sup>24</sup>

All three Baltic republics underwent intensive Soviet-style industrialisation from the 1950s onwards, focusing on capital-intensive industries (mechanical, electromechanical and electronic,

---

<sup>21</sup> Romuald Misiunas, Rein Taagepera. *The Baltic States*. p. 213.

<sup>22</sup> Ronald Grigor Suny (2012). *The contradictions of identity: being Soviet and national in the USSR*. p. 29.

<sup>23</sup> Kirsi Lauren (2014). *Facing the Otherness: Crossing the Finnish-Soviet Border as Narrated by Finnish Tourists*. *Culture Unbound*, 6 (6), pp. 1123–1143.

<sup>24</sup> *Прибалтика на Олимпиаде-80*. (The Baltics at the Olympics-80.) Available at: <https://vid1.ria.ru/ig/infografika/BN/olimpiada-80/page12441869.html> (viewed 22.11.2022).



and chemical plants). The production of consumer goods remained in an afterthought. In the USSR, the production of certain products was often concentrated in 1-3 factories, creating a kind of monopoly. Examples include the Riga Wagon Factory, *Radiotehnika*, *Sarkanā zvaigzne*, the Šiauliai Television Factory, Tallinn *Dvigatel* and *Norma*. Many companies were part of the military-industrial complex and did not even have names, just post boxes or military unit numbers.

Decisions to expand or open companies were taken in Moscow according to the USSR's, not local, needs.

In Estonia and Latvia, the rapidly growing demand of companies for labour led to an influx of workers from other regions of the USSR. The situation was different in Lithuania, where in 1964 the majority of the population still lived in the countryside. Some scholars believe<sup>25</sup> that an important factor was that serious industrialisation began in Lithuania at a time when the establishment of Regional Economic Soviets<sup>26</sup> significantly increased the role of local authorities in the management of industrial enterprises and also in economic planning. Where there was a will to do so, it was possible to plan the location of new factories more rationally, making the best use of local labour resources. By 1970, the number of people working in Lithuanian industry (415 000) had already surpassed the corresponding figure for both Estonia and Latvia. In 1985, industrial production in Lithuania amounted to 11.2 billion roubles, while in 1989 industrial production in Latvia was 10.6 billion roubles and in Estonia 6.72 billion roubles.<sup>27</sup>

Statistics show that in the 40 post-war years, Lithuania had not only become an industrially developed region, but had even surpassed its neighbours, while avoiding over-russification. Of course, the Soviet accounting system did not reflect the competitiveness of enterprises, they operated without the threat of bankruptcy, within the framework of a command economy.

National income in the USSR was calculated according to a different methodology than was used internationally, and was not published. However, estimates show that by 1970 per capita national income in Lithuania (1 336 roubles) was already very close to that of its two neighbours (Estonia – 1 590, and Latvia – 1573).<sup>28</sup>

---

<sup>25</sup> Misiunas, Taagepera. *The Baltic States*. p. 187.

<sup>26</sup> Regional Economic Soviets existed in 1957-1965.

<sup>27</sup> Krastiņš. *Latvijas rūpniecība*. (Latvian Industry.) p. 193.

<sup>28</sup> Krastiņš. *Latvijas rūpniecība*. (Latvian Industry.) p. 191.

From the mid-1980s onwards, the USSR increasingly began to show signs of a general economic, social and political crisis, leading to a increasing loss of legitimacy. In the Baltic states it was gradually replaced by demands for national independence.

## **Regaining independence and the path to further development**

When the changes in the USSR began in the second half of the 1980s, economists in the Baltic republics immediately set to work on developing various concepts of regional autonomy. The Estonians, led by Edgar Savisaar, were the leaders in this respect and in 1987 began working on the concept of Self-Sufficient Estonia (*Isemajandav Eesti*, shortened to *IME*). The *IME* also provided for the introduction of its own currency. The work on such a programme prepared future Estonian leaders, among them the later central bank governor Siim Kallas, for the reforms ahead.

From 1987 onwards, an opportunity emerged for freer expression, for protests against ecologically dangerous projects and migration, for true reflection of history, for ideas of autonomy and independence. Estonia was the leader on this path.

After the declarations of independence in 1990, while still part of the USSR, the Baltics moved towards a kind of duality of power, trying to take over as many areas and enterprises as possible for the republics, and starting to free themselves from the stranglehold of the directive economy.

However, the unrestricted opportunities for independent economy only opened up after the failed August 1991 putsch, when the Baltic states regained their independence within a week and rapidly began to implement most far-reaching reforms. The introduction of national currencies and the 1992 unpeg from the Russian rouble cut the umbilical cord that still bound the Baltic economies to the former USSR.

Soaring rates of national currencies, the chaos of the former USSR's payments system, and the increasing prices of raw materials and energy have pushed many industrial companies into bankruptcy. Sales to the former USSR dried up, while it was very difficult, if not impossible, to find a market elsewhere. Many company managers were not prepared to work in the new conditions and did not have the necessary skills. Nor did the state institutions have the means or the skills to carry out fundamental industrial restructuring. Privatisation was virtually the only instrument.

Companies that had a domestic market (food industry) or a domestic raw material base for export production (timber industry) had a better chance of survival. Consumer goods producers, on the other hand, could not compete with foreign products in terms of quality and price. The radioelectronics industry, which employed 50 000 people in Latvia, was hit particularly hard.

Changes in the volume of industrial production are shown in Graph 11. In the USSR, industry accounted for a disproportionately large share of the economy, this share declined during the transition period and brought the structure of the economy closer to that of the market economy at the end of the XX century. Consequently, the overall economic downturn was not as sharp as in industry, as the hitherto suppressed service sector developed rapidly.

However, according to the International Monetary Fund (IMF) publication<sup>1</sup>, the situation in Latvia was even more unfavourable: in 1992, GDP fell by almost 40%, compared with a 20% decline in Estonia and Lithuania. In Lithuania, the decline continued for another two years, also resulting in a contraction of almost 40%, while in Estonia the contraction did not exceed 30%. In Estonia and Lithuania, the economic upturn already resumed in 1995, in Latvia it happened a year later.

In Estonia, the volume of industrial production declined less (by no more than 50%) and a gradual recovery already started in 1997. Some researchers<sup>2</sup> believe that this was due to the fact that Estonia had fewer large and technologically sophisticated enterprises. I think this was due to the cultural factors mentioned above, the sectoral proportions and the much faster pace of reforms, in particular privatisation, which was basically completed by 1995. Estonia's GDP returned to 1991 level in 2002.

In Latvia and Lithuania, privatisation did not proceed as smoothly, and by the year 2000 the volume of production had not even reached half the 1990 level.

In Latvia, after the initial delay in the introduction of privatisation certificates and an initial choice of a decentralised (ministry-led) approach, it was only in 1994 that large-scale centralised privatisation began. It was essentially completed by 1998. Among the largest privatised companies in the non-food sectors, *Latvijas finieris*, the former wood processing company *Bolderāja*, the Valmiera fibreglass factory, the pharmaceutical companies *Grindeks* and *Olainfarm* are still operating today.

In Lithuania, the government also implemented a privatisation certificate programme, limiting the participation of foreigners in privatisation until 1996 and thus facilitating the transfer of companies into the hands of their management and employees. In Estonia and Latvia, there was

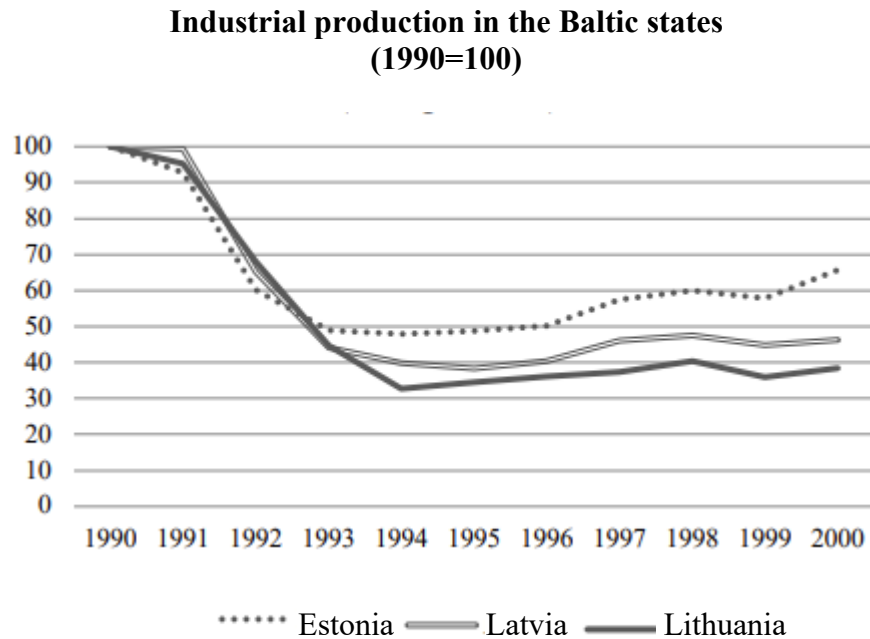
---

<sup>1</sup> Adalbert Knöbl, Richard Haas (2003). IMF and the Baltics: A Decade of Cooperation. International Monetary Fund. p. 8.

<sup>2</sup> Daunis Auers (2015). Comparative politics and government of the Baltics. Palgrave Macmillan. p. 181.

no political support for this approach because of the sharply different national composition. The theory was that the restriction of the range of investors would have been less effective than the approach taken in Estonia.

Graph 11<sup>3</sup>



Privatisation in Lithuania was essentially completed in the year 2000. The results of privatisation in Lithuania are better than in Latvia: the *Žalgiris* engineering plant, the *Elfa* electric motor manufacturer, the *Snaigė* refrigeration plant, the *Achema* group developed on the basis of the *Azotas* fertiliser production association, the Mažeikiai oil refinery and the Klaipėda shipbuilding plant are still in operation.

To what extent have politicians been involved in the privatisation of enterprises?

In Latvia, two people are notorious for this. The story of how Andris Šķēle, as Deputy Minister of Agriculture, took advantage of decentralised privatisation opportunities and acquired significant stakes in the food companies *Laima*, *Uzvara*, *Rīgas vīna un šampanieša kombināts*, and *Rīgas alus*, was widely publicised. Later, during centralised privatisation, A. Šķēle also gained control of *Latvijas Balzams*, Salacgrīva fish cannery and *Kaijā*.<sup>4</sup> By merging several privatised

<sup>3</sup> Krastiņš. *Latvijas rūpniecība*. (Latvian Industry.) p. 234.

<sup>4</sup> Krastiņš. *Latvijas rūpniecība*. (Latvian Industry.) p. 259.

bakeries, *Hanzas maiznīca* was established. Later, all these companies were sold mainly to foreign investors and are still in operation.

In turn, Aivars Lembergs, Chairman of the Ventspils Executive Committee, had been working on joint ventures in the Port of Ventspils since the early 1990s, gradually privatising its stevedores. This is how *Kālija parks*, Ventspils Commercial Port, *Ventbunkers* and *Ventamonjaks* were created. However, the main generator of cash flow in Ventspils was the oil and oil products transshipment terminal *Ventspils nafta*, the privatisation of which was decided by the government in 1997 on very favourable terms for the acquirer of control. The funds from *Ventspils nafta* were used to buy the *Preses nams* and the daily newspaper *Neatkarīgā Rīta Avīze*.

The next target for the Ventspils investor group was one of the largest state-owned companies, *Latvijas kuģniecība*, whose controlling stake was also acquired in 2002 after a long period of political turbulence. Both *Ventspils nafta* and *Latvijas kuģniecība* thus came under the control of five Ventspils investors.<sup>5</sup>

However, business disagreements caused a split in the Ventspils investor group, which gave rise to criminal proceedings and a lawsuit against Aivars Lembergs. As a result of this conflict, in 2006-2010, *Ventspils nafta* and *Latvijas kuģniecība* came under the control of *Vitol* group registered in the Netherlands. The Prosecutor's Office also investigated a criminal case regarding large payments (around 8.7 million USD) to politicians from three parties for making decisions in the privatisation of *Ventspils nafta*. After five years of investigation, the case was dropped for lack of sufficient evidence.<sup>6</sup>

The relationship between Lembergs and Šķēle was also to a large extent determined by the Latvian political environment and unfolding of events in 1996-2009. When a crisis emerged in 1995 after the insolvency of *Banka Baltija* and the elections to the Saeima, as the government failed to be approved twice, A. Šķēle became a non-party Prime Minister. He held the post for a year and a half, making a significant contribution to the implementation of reforms. In the next elections in 1998, he ran with the newly founded People's Party (Latvian: *Tautas partija*), while Lembergs, under the banner of the Union of Greens and Farmers (Latvian: *Zaļo un Zemnieku savienība, ZZS*), had consolidated the previously unsuccessful forces that would have a significant

---

<sup>5</sup> Krastiņš. *Latvijas rūpniecība*. (Latvian Industry.) p. 370.

<sup>6</sup> Indra Sprance (2021). Privatisation Ventspils style: offshore firms linked to political parties have received millions. Available at: <https://www.lsm.lv/raksts/zinas/zinu-analize/privatizacija-ventspilnieku-stila-ar-partijam-saistitas-arzonu-firmas-sanemusas-miljonus.a403275/> (viewed 03.01.2023).

influence in Latvian politics for the next 20 years. Despite court proceedings and even imprisonment, Lembergs has retained his influence in the political process, although it weakened considerably. Šķēle, on the other hand, has been out of politics since 2011, when the People's Party was dissolved.

The richest people in Estonia have been much less involved in politics, business has almost always been separated from politics.<sup>7</sup> Take, for example, the former Prime Minister Tiit Vähi, he controlled the rare earth metals recycling company *Silmet*, but his participation in politics was limited to donating to the party and lobbying for Sillamäe's interests. *Hansapank* founder Jüri Mõis turned to politics only after selling his shares in the bank, later becoming the Minister of Interior and the Mayor of Tallinn. One of the most controversial politicians to have made his fortune in the metals business in the 1990s was Robert Lepikson, who briefly served as the Minister of Interior and the Mayor of Tallinn. His influence on Estonian politics, however, cannot be called significant.

In Lithuania, the biggest influence was wielded by the former Prime Minister Bronislovas Lubys, head of the Lithuanian Confederation of Industrialists (Lithuanian: *Lietuvos pramonininku konfederacija, LPK*). He was the former head of the chemical plant *Azotas*, who had gained control of the company (later the *Achema Group*) through privatisation<sup>8</sup> in 1992-1993 and went on to be involved in several more privatisations, as well as to acquire significant positions in the Port of Klaipėda in 1999. The influence of Lubys and *LPK* in Lithuanian politics has been growing, especially with regard to privatisation. This continued until 1999, but never reached the level of the most influential Latvian business politicians.<sup>9</sup> In 2008, Lubys was recognised in publications as Lithuania's richest man, but he died in 2011.

In the late 1990s, the World Bank even wrote, based on a study, that Latvia had a high level of a specific form of corruption, which was attractively called "state capture" in the study, and further turned into "state theft" in the interpretation of the newspaper *Diena*. Political scientists, however, usually classify it as political or systemic corruption, i.e., a situation where laws and other normative documents, as well as court rulings, are adopted in the interests of a narrow circle

---

<sup>7</sup> Mel Huang (2002). *Wannabe Oligarchs: Tycoons & Influence in the Baltic States*. ETH Zurich, Conflict Studies Research Centre. pp. 3–4.

<sup>8</sup> During this time, he briefly, from 12 December 1992 to 10 March 1993, served as the Prime Minister of Lithuania.

<sup>9</sup> Mel Huang. *Wannabe Oligarchs*. pp. 5–6.

of people or companies and can be bought. The World Bank has argued that systemic corruption reduces economic efficiency and growth opportunities to a much greater extent than administrative corruption.

By surveying around 150 companies in each country, the researchers sought to understand the role of systemic and administrative corruption and its impact on decision-making in transition economies. The results for the Baltic states are summarised in Table 11.<sup>10</sup>

Table 11

### Systemic and administrative corruption indices

	<b>Estonia</b>	<b>Latvia</b>	<b>Lithuania</b>
Systemic corruption	10	30	11
Administrative corruption	1.6	1.4	2.8

Of course, these indices show the subjective mood of business people, but they demonstrate that Latvia was similar to Estonia in terms of administrative corruption, while the systemic corruption index showed that it is close to Bulgaria, Kyrgyzstan and Russia. However, the common perception that a few “oligarchs” were responsible for systemic corruption in Latvia is too simplistic. In addition to the “oligarchs”<sup>11</sup> directly involved in politics, there were a number of individuals and companies with a strong influence on decision-making. One example is *Parex Bank* and its shareholders Valērijs Kargins and Viktors Krasovickis. Unfortunately, this study has not been repeated, so we can only guess how the situation has changed over the past 20 years.

However, despite the above-mentioned differences, by the mid-1990s it was already clear that all the Baltic states were planning their development along a path that would bring them closer to the European Union and NATO, by implementing the requirements of the EU, the International Monetary Fund and the World Trade Organisation.

Moving towards membership in these organisations required an enormous number of reforms, including the adoption of a large number of laws. In the pre-accession period (1995-2004), the number of laws adopted in the Baltic states almost doubled. After accession, the number of laws adopted in Estonia decreased substantially, demonstrating the achievement of a certain

---

<sup>10</sup> Joel S. Hellman, Geraint Jones, Daniel Kaufmann (2000). *Seize the State, Seize the Day*. The World Bank. pp. 8, 10.

<sup>11</sup> Ainārs Šlesers, founder of many parties, is often included among them.



degree of legal stability. On the contrary, in Latvia and Lithuania, the pace of law adoption remained relatively high. Martin Mendelski<sup>12</sup> calls this legislative pathology.

It is likely that the move towards membership in important international organisations gave rise to the hope in the Baltics that the existing problems could gradually be eliminated and that the country would move more and more towards Western European and perhaps even Nordic standards.

This was particularly pronounced in Estonia, which consciously oriented its economy towards cooperation with the Nordic countries and adopting their model. Meanwhile, slogans such as “Latvia must become a bridge between East and West” and “Latvia is closer than Switzerland” gained popularity in Latvia. And these were not just slogans, as the high proportion of ethnic minorities meant that there were extensive contacts with the CIS countries, where it was possible to make good money taking advantage of price arbitrage and differences in financial systems.

Similar ideas could be heard in Lithuania, even from the nationalist Vytautas Landsbergis: “It is quite natural that we should cooperate with both East and West and, in a way, acting as mediators. We can benefit from such mediation thanks to the geographical position that history has given us.”<sup>13</sup>

The development of the Latvian banking system in the 1990s is a striking example of this approach. Based on the almost libertarian stance of the Bank of Latvia’s management, commercial banks grew like mushrooms after the rain. Their number reached as many as 62 (in Lithuania it was no more than 26, in Estonia – 22). By 1998, this number had shrunk to 27, with only 10 banks remaining in Lithuania and 6 in Estonia.<sup>14</sup> Bank supervision was rudimentary at first, with neither proper accounting nor auditing standards in place. Several banks in Latvia had owners and managers with criminal backgrounds. As it was believed at the time, they had been punished in Soviet times for speculation and dealing in foreign currencies, which was now no longer a crime.

Experience and expertise in supervising commercial banks was lacking in all Baltic states, but in Latvia it had the most devastating consequences. Estonia’s decisive handling of the 1992-

---

<sup>12</sup> Martin Mendelski (2016). The EU’s rule of law promotion in post-Soviet Europe: what explains the divergence between Baltic States and EaP countries? *Eastern Journal of European Studies*, 7 (2). pp. 111–144. Here p. 119.

<sup>13</sup> Mole. *The Baltic States*. p. 84.

<sup>14</sup> Helena Tang, Edda Zoli, Irina Klytchnikova (2000). *Banking Crises in Transition Economies*. The World Bank. pp. 5–6.

1994 banking crisis resulted in loss of 1.6% of GDP, in Lithuania 2.9% in 1995-1996. Estonia has not had a serious banking crisis since then. The bank restructuring cost governments in 1993-1998 was 1.4% of GDP in Estonia, 1.7% in Lithuania and 2.5% in Latvia.<sup>15</sup>

Estonia and Lithuania, unlike Latvia, did not try to establish a financial centre to serve non-residents.

In Lithuania, however, the closure of *Snoras Bank* in 2011 resulted in a loss of around 2% of GDP and triggered the closure of *Latvijas krājbanka*. The press reports suggest that this was a situation caused by negligence and possibly corruption on the part of the bank's supervisory authorities.

By contrast, Latvia's loss in the 1995-1996 banking crisis amounted to 3% of GDP, and even 3.9% of GDP in 2008-2012.<sup>16</sup> The assets of Latvian banks closed in 1995 represented 40% of the assets of the entire banking system.

During the Russian debt crisis in 1998, Latvian banks had the largest exposure to Russian securities, amounting to 8% of total bank assets. Lithuanian banks' exposure was only 1.4% and Estonia's 0.1%. Several Latvian banks suffered serious losses, and *Rīgas komercbanka* had to temporarily suspend its operations and to undergo restructuring.

Until 2008, the Association of Latvian Commercial Banks was one of the most powerful lobbying organisations, significantly influencing the regulatory environment.

Unfortunately, relying on the slogan "Latvia is closer than Switzerland" had already created a broad base for money laundering operations, which not only brought good profits to those involved, but also had a negative impact on the business and political environment. It may seem that financial sector supervisors did not learn much from previous crises, including the collapse of *Latvijas krājbanka* in 2011 (loss of around 2% of GDP) and finally the closure of *ABLV Bank* in 2018, triggered by the U.S. Treasury Department's announcement that the bank was involved in money laundering schemes.

Ilmārs Rimšēvičs, Deputy President of the Bank of Latvia, has been responsible for the supervision of commercial banks in Latvia since 1992. After the establishment of the Financial and Capital Market Commission (FCMC) in the year 2000, the Bank of Latvia retained the supervisory functions of the FCMC. Meanwhile, in 2001, I. Rimšēvičs became President of the

---

<sup>15</sup> Helena Tang, Edda Zoli, Irina Klytchnikova (2000). *Banking Crises*. p. 22.

<sup>16</sup> Luc Laeven, Fabian Valencia (2018). *Systemic Banking Crises Revisited*. IMF. pp. 35–36.

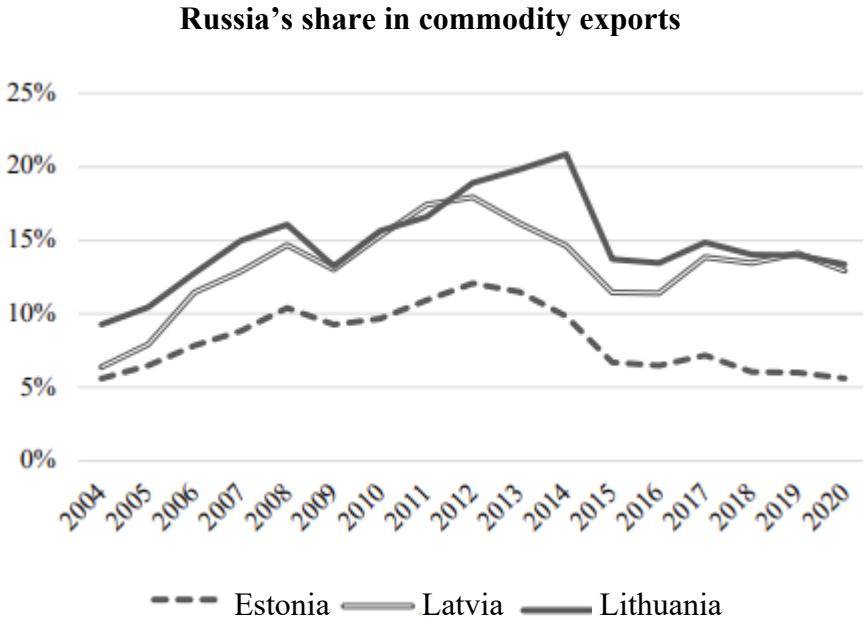
Bank of Latvia. As if it were a coincidence, an exception or even a provocation that in 2018 the Prosecutor's Office charged I. Rimšēvičs with bribery in connection with banking supervision. But one can also think otherwise.

Only after the closure of *ABLV Bank* did the Latvian authorities take extensive measures to prevent money laundering, however, as is often the case in Latvia, it was done in a way that also hampered normal economic activity and actually reduced competition between banks.

Estonia has also been reserved with its exports when dealing with Russia since the beginning of the century, and since 2012, Russia's share of Estonian exports has been declining. In Latvia and Lithuania, Russia's share of exports has traditionally been more than twice as high, as shown in Graph 12.

It has been argued on many occasions that Latvia's failures are due to the fact that power was not completely purged of the representatives of the Communist Party *nomenklatura*. However, the other two Baltic states are not much different from Latvia in this respect. Furthermore, in Lithuania the party *nomenklatura* retained power to a much greater extent after regaining independence. Kazimira Prunskienė, who had been a member of the Bureau of the Central Committees of the Communist Party of Lithuania, became the head of the government, Algirdas Brauskas had been the Secretary of the Central Committee from 1977, the First Secretary from 1988, became the President of Lithuania in 1992-1998 and the head of the government in 2001-2006.

Graph 12



The initial support for independence by the national cadres of the Communist Party of Lithuania explains their high share in the new administrative structures. However, researchers also attribute to this factor Lithuania's initially slower pace of reforms.

In Estonia, Arnold Rüütel became the President in 2001, despite the fact that he had been the Chairman of the Supreme Council from 1983 to 1992, and before that a member of the Bureau of the Central Committees of the Communist Party of Estonia from 1977 and the First Deputy Chairman of the Council of Ministers from 1979.

After the restoration of independence in Estonia and Latvia, the flow of immigrants from the former USSR was stopped. Once Russian troops withdrew in 1994, the population declined and the exodus continued. This contributed to the increase in the share of the native population, the results of which are shown in Table 12.

Table 12

Country	Native population <sup>17</sup>		Citizens
	1989	2011	
Estonia	62%	69%	85%
Latvia	52%	63%	87%
Lithuania	79%	85%	99%

As can be seen, Estonia and Latvia still have a significant proportion of non-citizens. This is a result of the different approach to defining the circle of citizens from that in Lithuania. Due to the high proportion of native people, Lithuania was able to follow the path of minority inclusion, granting citizenship to practically all residents. Estonia and Latvia had a more complicated situation, having to follow the path of political restoration, restoring citizenship only to pre-war citizens and their descendants, while offering naturalisation to Soviet-era immigrants.

As a result of the restoration of citizenship, there are still many so-called non-citizens in both countries – former residents of Estonian SSR and Latvian SSR who were not eligible for citizenship restoration and have not gone through the naturalisation process. The number of non-citizens was much higher, but after EU pressure in the late 1990s led Estonia and Latvia to facilitate the acquisition of citizenship, many of them either naturalised or opted for Russian citizenship.

---

<sup>17</sup> Data from statistical offices of Estonia, Latvia, Lithuania.

There are 40 000 Russian citizens permanently residing in Latvia, 82 000 in Estonia and only 8 000 in Lithuania.

The restoration of citizenship initially succeeded in preventing a serious ethnically-based fragmentation of politics, while replacing the Soviet ruling elite with representatives of the native population. According to Mendelski, by 1997 they already occupied more than 90% of positions in the bureaucracy and judiciary system in all three countries.<sup>18</sup> In this way, relatively united elites were created, which allowed the Baltic states to avoid internal resistance on the road to the EU and NATO.

It can be said that in the 1990s non-citizens, as well as some Russian-speaking citizens, those who had worked for the system, were disoriented and frustrated by the abandonment of the Soviet past. Russian-speakers moved from the position of a dominant group to the political periphery. This, of course, caused resentment and a sense of being wronged in many people. As Ammon Cheskin points out, “If Russian speakers wish to find discursive acceptance in contemporary Latvia, then it is important to recognise the importance of “occupation” as a nodal point that anchors official Latvian identities and discourses.”<sup>19</sup>

Many Russian-speakers were dissatisfied with the official interpretation of this and other issues, turning to the messages from Moscow steeped in nostalgia for the Soviet past and Russian nationalism, which Leah Greenfeld has described as follows: “Russia did not have liberty and equality, and so it revolted against rationality, rejecting both the thinking individual and the responsible faculty .. Reason had to do with calculation, reflection, predictability; its opposing values were spontaneity, the unexpected, the unmeasurable. By their very nature, these qualities were vague; it was much clearer what they were not than what they were. They became the qualities of the *enigmatic Russian soul*.”<sup>20</sup>

Given the structure of society, there is hardly any party division along national lines in Lithuania. It is believed that Estonia has largely avoided it because since the second half of the 1990s the leading parties (Centre Party and Reform Party) have been trying to attract Russian

---

<sup>18</sup> Mendelski. The EU’s rule of law promotion in post-Soviet Europe. p. 132.

<sup>19</sup> Ammon Cheskin (2016). Russian Speakers in Post-Soviet Latvia: Discursive identity strategies. Edinburgh University Press. p. 55.

<sup>20</sup> Leah Greenfeld (2019). Nationalism. A Short History. Brookings Institution Press. p. 79.

politicians and voters.<sup>21</sup> For Latvia, on the other hand, party division along national lines has long been a serious problem.

The ethnic vote in Latvia has determined that predominantly Russian-speaking parties<sup>22</sup> won between 23 and 30 seats in the Saeima in 2002-2018. Moreover, support for these parties increased after 1998 as the naturalisation of non-citizens expanded. The different coverage of events by the press in Latvian and Russian languages and their distinctly separated audiences certainly contributed to this. In Estonia, such strict segregation of the press as in Latvia has not been observed.<sup>23</sup>

Since pro-Russian parties could not participate in the Latvian government because of their geopolitical orientation, the formation of governments in these 20 years has been limited to the remaining 70-77 MPs, from whom a majority of at least 51 had to be formed. This has limited political competition, often making difficult the adoption of rational decisions.

The post-independence environment in Estonia and Latvia was not favourable for political nation building. A large part of the Russian-speaking population and a small number of native population had developed a strong sense of identity tied to the USSR. Trying to replace it with belonging to a political nation has not worked very well, the backlash from Russia has not helped matters either. As a result, a significant proportion of Russian speakers (regardless of citizenship) identify stronger with Russia than with their home country.

And only after Russia's invasion of Ukraine, this picture may be starting to change. In Latvia, in the 2022 parliamentary elections, with votes split between several pro-Russian parties, *Stabilitātei!* won only 11 seats in the Saeima, while the former leader, *Saskaņa*, did not get in at all. It is possible that the votes of Russian-speaking voters were not only divided among several pro-Russian parties, but some of them also voted for "Latvian" parties.

The principles of government formation and the length of governments do not differ much among the Baltic states. They have been multi-party, fragmented governments with separate ministries controlled by the parties. In addition, coalitions have rarely had large majorities in

---

<sup>21</sup> Dovile Budryte (2005). Taming Nationalism? Political Community Building in the Post-Soviet Baltic States. Aldershot: Ashgate. p. 77.

<sup>22</sup> *Saskaņa, Saskaņas centrs, Par cilvēka tiesībām vienotā Latvijā, Tautas saskaņas partija.*

<sup>23</sup> Auers. Comparative politics and government of the Baltics. p. 52–53.

parliaments, allowing individual parties to make ultimatums towards their coalition partners. The length of governments has gradually stabilized coming closer to the electoral cycle.<sup>24</sup>

Latvia has a much lower level of civic engagement in political life. In 2009, party membership accounted for 4.84% of voters in Estonia, 2.66% in Lithuania and only 0.74% in Latvia.<sup>25</sup>

The lack of competition between parties that actually claim power in Latvia also seems to have led to such unusual phenomena when even the parties that have been in government for a long time do not have party programmes. Apparently, they consider that it is quite sufficient to publish a 4 000-character collection of slogans every four years and the country can be run in a response mode, relying on policies developed elsewhere (EU, OECD).

By contrast, the leading political parties in Estonia and Lithuania have extensive, publicly available party programmes.<sup>26</sup>

---

<sup>24</sup> Auers. *Comparative politics and government of the Baltics*. p. 135.

<sup>25</sup> Tõnis Saarts (2011). *Comparative Party System Analysis in Central and Eastern Europe: The Case of the Baltic States*. *Studies of Transition States and Societies*, 3, pp. 83–104. Here p. 98.

<sup>26</sup> For example, in Estonia <https://reform.ee/erakond/programm/>; <https://keskerakond.ee/et/erakonna-liikmed/programm.html>; <https://ekre.ee/konservatiivne-programm/>. In Lithuania <https://tsajunga.lt/wp-content/uploads/2020/12/XVIII-osios-LRV-programa.pdf>; <https://www.lsdp.lt/wp-content/uploads/2021/02/Programa-2020-atnaujinta-final.pdf>

## Causes of lagging behind

Despite the various political and economic developments over the past 30 years, the common course towards the EU has resulted in broadly similar political and economic systems in the Baltic states. There are some differences between the countries, but these can hardly be considered significant.

However, looking at what has been achieved over these 30 years, it is clear that there are reasons that prevent Latvia from developing faster and from doing better according to many indicators.

So, what could be the reasons for Latvia's lagging behind?

In his seminal work<sup>1</sup> on national competitiveness, Michael Porter argues that competitiveness depends on the capacity of a country's economy to innovate and improve. In a modern economy, the conditions of competitiveness are the same as those that determine economic development.

A country's competitiveness is directly linked to its companies, whose ability to compete globally is based on the interaction of four attributes. These attributes, according to Porter, are:

1. production factors (labour, land, infrastructure);
2. local demand;
3. related and supporting industries;
4. company strategy, structure, and rivalry.

In addition to these four attributes, Porter's theory also includes two additional variables: chance and government. Porter argues that, in the face of global competition, the role of governments has become more important in strengthening the competitiveness of companies. Differences in national values, culture, economic structures, institutions, and histories all contribute to competitive success.

Ģirts Rungainis has expressed the opinion that since the 1990s, redistribution industries have been dominant in Latvia, i.e. those in which, by taking advantage of a successfully acquired market position, funds can be redistributed in order to obtain a kind of annuity. In his view, too few creative industries that could bring high added value have developed.

---

<sup>1</sup> Michael E. Porter (1990). *The Competitive Advantage of Nations*. New York: The Free Press.



This finding is consistent with the World Bank research on the level of systemic corruption and with the view that there is significant influence of wealthy companies and individuals (“oligarchs”) on government and judicial decisions.

It cannot be said that the Latvian government has not tried to find ways to speed up the country’s development. Many strategies and plans have been drawn up and approved. Moreover, it has been done not only on our own, but also with the help of internationally renowned experts.

In 2009, the government set up a working group with prominent foreign experts to discuss economic recovery. Among them was Christian Ketels of the Institute for Strategy and Competitiveness, Harvard Business School, who in 2012, when presenting a study *Development of a National Competitiveness Assessment and a Sustainable Model for Monitoring National Competitiveness*, said: “Most of them [competitiveness indicators] show that Latvia is consistently failing to reach its potential.”<sup>2</sup> It should be noted that the study cost the state 240 000 lats.

During the Covid-19 pandemic in 2020, the government approved an information report, *Strategy for Latvia to Mitigate the Consequences of the Covid-19 Crisis*,<sup>3</sup> which, according to televised statements,<sup>4</sup> involved experts from the London Business School.

During that period, a further 500 000 euros were allocated to the *reCOVery-LV* project, which aimed to develop a framework for preserving the economy’s potential and boosting competitiveness. The publication resulting from the project reads: “Working together, 80 economists, lawyers, political scientists and sociologists, including 19 PhD students, were able to combine scientific expertise with the practical experience of state, municipal and non-governmental organisations to find adequate tools for economic breakthrough.”<sup>5</sup> Unsurprisingly, in this work the radical changes in the geopolitical situation just one year later could not have been anticipated. What is surprising, however, is the general conclusions that have been drawn and the inability to formulate coherent, specific recommendations in the course of the project.

---

<sup>2</sup> Available at: <https://www.mk.gov.lv/lv/media/5282/download> (viewed 18.01.2023).

<sup>3</sup> Available at: <https://www.em.gov.lv/lv/strategija-latvijai-0> (viewed 18.01.2023).

<sup>4</sup> TV24 programme *Kārtības rullis* (Rules of Order). Available at: [https://xtv.lv/rigatv24/video/46VpoEv37Eb08\\_06\\_2020\\_kartibas\\_rullis\\_1\\_dala](https://xtv.lv/rigatv24/video/46VpoEv37Eb08_06_2020_kartibas_rullis_1_dala)

<sup>5</sup> Inna Šteinbuka (academic supervision) (2021). *Latvijas tautsaimniecība pandēmijas ēnā un pēckrīzes izrāviena iespējas*. (Latvia's Economy in the Shadow of the Pandemic and Post-Crisis Breakthrough Opportunities.) p. 8.

Unfortunately, all the plans, documents and strategies developed so far have failed to deliver tangible benefits. Either because the recommendations have not been correct, or because the will and the capacity to implement them have not been there.

Was the development of Latvia after regaining independence discussed above caused by a random concatenation of events or a part of a consistent pattern? For example, Professor Ivars Austers of the University of Latvia believes that “... but it seems that the answer is simpler: by chance, some people ended up in influential positions.”<sup>6</sup>

He is echoed by the Chairman of the Budget Committee of the Saeima, a former Minister of Finance Jānis Reirs: “The example of Estonia, when a high-ranking manager of a multinational company moved to the SRS [State Revenue Service], put things in perspective – this is an exception, not a standard, the Estonians were just lucky. We have not been lucky yet.”<sup>7</sup>

If we accept that a lot could have been determined by random chance, we should also consider that random people ended up in the top management of the central bank and the main universities. In the first case, this caused significant losses in the banking sector; in the second case, it prevented universities from gaining a proper place in the global rankings. This analysis could be continued in other areas.

As early as in the 1990s, scholars such as Ole Nørgaard and Anatol Lieven pointed out that Latvian national identity was less developed than that of Estonians.<sup>8</sup> Consequently, the Estonian elite was more loyal to the state and more committed to the common good. As described in the previous chapters, Latvia’s national structure has been undermined the most, arguably suffering the greatest loss of human capital in the Baltics during the World War II.

In turn, Misiunas and Taagepera, as mentioned above, note the much lower rate of participation of Latvians in the governance of the republic during Soviet times, which could have affected knowledge and management skills during the critical transition period.

---

<sup>6</sup> Auster’s New Year’s Speech. *Sestdiena*, 6.–12.01.2023. p. 9.

<sup>7</sup> *VID ir jāmaina attieksme pret nodokļu maksātājiem.* (The SRS Needs To Change Its Attitude Towards Taxpayers.) *Diena*, 27.01.2023, p. 4.

<sup>8</sup> Li Bennich-Björkman (2002). *State Capture in the Baltics: Identity, International Role Models and Network Formation.* From: *The Baltic Sea Region.* Witold Maciejewski (editor). Uppsala: Baltic University Press. pp. 345– 369. Here p. 351.

However, as Dovilė Budrytė notes, “... there is an emerging consensus among scholars of nationalism that in the case of the post-Soviet nations, numerous aspects of their identity were constituted during the Soviet period and were not miraculously reawakened in the late 1980s.”<sup>9</sup>

In summary of these observations, I think it can be argued that it was the culture of Latvian society that experienced the greatest deformation during the years of occupation. Here I understand culture as “... is that complex whole which includes knowledge, belief, art, morals, law, custom and any other capabilities and habits acquired by man as a member of society”,<sup>10</sup> from the culture of business, public administration, interpersonal relations to driving culture.

Although in the euphoria of regaining independence it seemed that the consequences of the occupation could be overcome quickly, this has only partially been the case. Latvia has not developed into a true political nation, and too often we are faced with the manifestations of a bicomunal state. Moreover, Latvian identity and culture have been seriously distorted during the occupation.

Of course, the two communities are not separated by an impermeable wall, their cultures influence each other, but we have to conclude that this does not always lead to positive results. Moreover, the culture of neither community is homogeneous, there are different undercurrents, subcultures. In their interaction, they determine the vector that directs the country’s development. Unfortunately, it seems that this vector is not favourable to Latvia in the Baltic competition.

It has been argued in the past, and especially since Russia’s aggression against Ukraine, that integration policies in Latvia have not been successful. But could it actually have been more successful? Integration can hardly be successful if those to be integrated resist it, and live in the information space and culture of another country.

It should be stressed that not only teaching in the national language is long overdue, but the segregation of schools along ethnic lines should also be stopped. This view is also advocated by, for example, Ivars Austers, but for it to be put into practice, the majority of both communities must really want it.

It should be remembered, however, that changing the language of teaching was not possible before we joined the EU and NATO, because we had to constantly prove how much we respect human rights principles and do not discriminate against other nationalities. It is clear that the

---

<sup>9</sup> Budrytė (2005). *Taming Nationalism?* p. 23.

<sup>10</sup> Edward B. Tylor (1920). *Primitive Culture*. Vol. 1. London: John Murray. p. 1.

accusations were made with the direct support of Russia, opposing successful integration. Western politicians, on the other hand, were still under the illusion that Russia could be integrated into the international community.

However, until today Estonians have not integrated their schools either, and this has not prevented them from achieving much more than us.

Culture is passed on from generation to generation, and even when affected by major external shocks, it changes slowly. At the moment, the main forces driving our cultural change are Europe, which many are getting to know by travelling, studying, working; Russia, which until 2022 was conducting intensive brainwashing promoting the ideas of *Russkiy Mir* (the Russian World); and America, whose cultural wars are echoing even in Latvia.

Thus, my hypothesis is that the main obstacle on the path of Latvia's development is the culture of society deformed during the occupation, it has never been fully modernised and sufficiently elevated to the standards of the free world in the 30 years of independence.

This deformed culture hinders optimal decision-making, no matter how high-minded and well-educated the decision-makers.

## What can be done?

Many analysts believe that the world economy is currently undergoing a paradigm shift that will fundamentally change the structure of the economy and society, as well as the value system.<sup>1</sup> Some call it the fourth industrial revolution, in which artificial intelligence and big data, virtual reality, synthetic biology and robotics will be the defining factors. On the other hand, the world is threatened by climate change, which is forcing dramatic changes in energy and transport. Business methods are also changing rapidly, with the proliferation of sharing models and internet platforms. Those countries that do not implement appropriate techno-economic and institutional changes risk falling decades behind the leaders.

If my hypothesis about the reasons for Latvia's lagging behind is at least partly true, we can hardly hope for rapid progress in this process. No matter how hard politicians, activists, businessmen, other elites try to achieve more, they will inevitably bump against cultural constraints. This does not mean that nothing will be achieved, rather the achievements will be lower than in more development-friendly societies.

It cannot be denied that accepting such a hypothesis carries the risk of hopelessness, decision paralysis. As I mentioned earlier, culture usually changes very slowly, serious change takes several generations. Of course, there are times when a more rapid change is possible, as in the post-war period or the collapse of the USSR, but such events are difficult to predict and therefore difficult to rely on. So, what are the instruments that can bring about change in Latvia?

First, political nation-building. Until now, the Russian-speaking population of Latvia has been caught between two poles of identity formation, as Cheskin writes: "On the one hand, they live, work and study in contemporary Latvia and are exposed to the national discourses of the Latvian state ... On the other hand, many of these individuals also inhabit a media and cultural space that exposes them to the narratives and discourses of the Russian state."<sup>2</sup> The integration policy has not proved effective so far, but one can hope that after the Russian invasion of Ukraine this contradictory situation can be changed in favour of the Latvian discourse.

---

<sup>1</sup> Timo J. Hämäläinen (2003). National competitiveness and economic growth: the changing determinants of economic performance in the world economy. Cheltenham: Edward Elgar. p. 289.

<sup>2</sup> Cheskin. Russian Speakers in Post-Soviet Latvia. p. 181.

In my opinion, Latvia will not be able to develop successfully in the current geopolitical conditions if a strongly polarized bicomunal society continues to exist. And relying on slogans such as

“We must be masters of our own land” or inferiority complexes in the form of “Latvian” car stickers will not help here.

However, for a political nation to be successful, it must find content and form that is attractive to the majority.

Second, a fundamental transformation of education. Education can help establish a common system of values, rationality, mutual trust and help build a political nation. The most important thing is to finally arrive at an education system not divided by ethnicity, without segregation into two opposing parts. In the short term, such a change might not be to the liking of either the Russian-speakers or the Latvians, but in the long term it would bring significant benefits. It is equally important that schools and universities produce competitive graduates who meet the demands of the modern world.

Third, the position of the state. The state must take a clear stance on values and communication, establishing and maintaining a culture consistent with a civilised country in various areas: business, relationships between people, businesses and the state.

None of these tasks is easy and their implementation will be hampered by the existing structure of society and its established culture. However, without their implementation, the sustainable development of Latvia will not be possible.

## Literature

1. Epp Annus (2016). Between arts and politics: A postcolonial view on Baltic cultures of the Soviet era. *Journal of Baltic Studies*, 47 (1), pp. 1–13.
2. Daunis Auers (2015). *Comparative politics and government of the Baltics*. Palgrave Macmillan.
3. Mark Bassin, Catriona Kelly (editors) (2012). *Soviet and Post-Soviet Identities*. Cambridge University Press.
4. Li Bennich-Björkman (2002). State capture in the Baltics: Identity, International Role Models and Network Formation. No: The Baltic Sea Region. Witold Maciejewski (editor). Uppsala: Baltic University Press. pp. 345–369.
5. Ammon Cheskin (2016). *Russian Speakers in Post-Soviet Latvia: Discursive identity strategies*. Edinburgh University Press.
6. Dovyliū Budrytė (2005). *Taming Nationalism? Political Community Building in the Post-Soviet Baltic States*. Aldershot: Ashgate.
7. Sauļus Grībkauskis (2020). *Padomju “ģenerālgubernatori”*. Riga: Latvian media.
8. Timo J. Hämäläinen (2003). *National competitiveness and economic growth: the changing determinants of economic performance in the world economy*. Cheltenham: Edward Elgar.
9. Joel S. Hellman, Geraint Jones, Daniel Kaufmann (2000). *Seize the State, Seize the Day*. The World Bank.
10. Mel Huang (2002). *Wannabe Oligarchs: Tycoons & Influence in the Baltic States*. ETH Zurich, Conflict Studies Research Centre.
11. Kaspars Irbe (2021). *Slēptā dzīve (The Hidden Life)*. Riga: Ascendum.
12. Edmunds Krastiņš (2018). *Latvijas rūpniecība XIX–XXI gadsimtā. (Latvian Industry in the XIX-XXI Century.)* Riga: Jumava.
13. Edmunds Krastiņš (2019). *Kuģniecība Latvijā. (Shipping in Latvia.)* Riga: Self-published.
14. Adalbert Knöbl, Richard Haas (2003). *IMF and the Baltics: A Decade of Cooperation*. International Monetary Fund.
15. Luc Laeven, Fabian Valencia (2018). *Systemic Banking Crises Revisited*. IMF.
16. Kirsi Lauren (2014). Facing the Otherness: Crossing the Finnish-Soviet Border as Narrated by Finnish Tourists. *Culture Unbound*, 6 (6), pp. 1123–1143.
17. Michael Loader (2017). The death of “Socialism with a Latvian Face”: The purge of the Latvian national communists, July 1959–1962, *Journal of Baltic Studies*, 48(2), pp. 161–181.
18. Martin Mendelski (2016). The EU’s rule of law promotion in post-Soviet Europe: what explains the divergence between Baltic States and EaP countries? *Eastern Journal of European Studies*, 7 (2). pp. 111–144.
19. Romuald Misiunas, Rein Taagepera (1993). *The Baltic States. Years of Dependence 1940–1990*. London: Hurst&Company.
20. Michael E. Porter (1990). *The Competitive Advantage of Nations*. New York: The Free Press.
21. Joan N. Roses, Nikolaus Wolf (2011). Aggregate growth, 1913–1950. In: edited by Stephen Broadberry and Kevin H. O’Rourke. *The Cambridge economic history of modern Europe*, volume 2. New York: Cambridge University Press. pp. 182–207.
22. Tõnis Saarts (2011). Comparative Party System Analysis in Central and Eastern Europe: The Case of the Baltic States. *Studies of Transition States and Societies*, 3, pp. 83-104.

23. Voldemārs Salnais (1937). Latvija skaitļos starp Eiropas valstīm. (*Latvia in Numbers among European Countries.*) From: Latvijas zeme, daba, tauta. (*Latvian Land, Nature, People.*) Riga: Valters un Rapa. pp. 605–676.
24. Mārgēris Skujenieks (1928). Latvija 1918.–1928. gados. (*Latvia in 1918-1928.*) Riga: Valsts statistiskā pārvalde. (*State Statistical Office.*)
25. Helena Tang, Edda Zoli, Irina Klytchnikova (2000). Banking Crises in Transition Economies. The World Bank.
26. Edward B. Tylor (1920). Primitive Culture. Vol. 1. London: John Murray.
27. Елена Зубкова (2008). Прибалтика и Кремль: 1940–1953 гг. (*Elena Zubkova (2008). The Baltic States and the Kremlin: 1940–1953*) Moscow: Российская политическая энциклопедия. (*Russian Political encyclopedia.*)



ISBN 978-9934-23-822-2  
(bar code)  
9 789934238222

© Edmunds Krastiņš

ISBN 978-9934-23-822-2  
UDK 33(474.3)

Rīga, 2023