

LATVIA: THE ECONOMIC CRISIS AND (IM)POSSIBLE CHANGES?

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Abstract

The aim of this paper is to analyze the effects of the economic decline in Latvia on the political system, with a particular emphasis on socio-political divisions. At the core of the analysis are mutual relationships between the economy and the socio-political sphere taking place in Latvia during and after the crisis. In the first part of this article, the determinants of the economic collapse in Latvia will be defined, and both the external and the internal circumstances of the crisis situation will be taken into account. The second part of the article will describe how the economic crisis affected the political system in Latvia during the period 2009-2011. At the end, the (im)possible changes in Latvian politics will be defined.

Introduction

The economic crisis in the years 2008–2010 and its consequences since then have proven to be extremely painful for the Baltic States, especially for Latvia. At the same time, however, the recession showed how significant the differences are that divide these three small, seemingly homogenous, states.¹ This is evidenced by the diverseness of the situations in each of the Baltic republics. Lithuania, Latvia and Estonia are frequently jointly referred to as the “small states” not only because of the size of their territories and populations, but also because some of the most important historical events in the 20th century happened to them simultaneously (the so-called “first independence”, the annexation of the Baltic States by the Soviet Union, and then the restoration of independence), which makes them quite commonly seen as

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¹ Ingves S., *The crisis in the Baltic – the Riksbank’s measures, assessments and lessons learned*, Governor of the Sveriges Riskbank, to the Riksdag Committee on Finance, Stockholm, 2 February 2010; <http://www.bis.org/review/r100203b.pdf> See also: “Wrongly labelled. The economic downturn has made it harder to speak sensibly of a region called “Eastern Europe””, http://www.economist.com/world/europe/displaystory.cfm?story_id=15213108

related and similar in many respects. However, the perception of the Baltic States as identical because of the several important traits they have in common seems to be somewhat misleading if these traits are considered to be dominant and decisive for the common interest of these countries.

Estonia fared best during the crisis because of its timely response to the early symptoms of the impending economic collapse. In this way, in January 2011, the euro was implemented.² However, the Latvian and the Lithuanian economies found it far more difficult to cope with the crisis. Both countries needed to significantly reduce their budgetary spending. Thus in 2009, Lithuania recorded its highest budget deficit (8.9%)³ and had to introduce rather drastic cuts. The situation in Latvia was even more serious, in effect, causing Latvia to apply for a €7.5 billion stabilization loan from the International Monetary Fund and European Commission, the World Bank, the European Bank for Reconstruction and Development (EBRD) and others.⁴

The aim of this paper is to analyze the effects of the economic decline in Latvia on the political system, with particular emphasis on socio-political divisions. At the core of the analysis are mutual relationships between the economy and the socio-political sphere in Latvia during and after the crisis. The economic and the political systems are inter-related and often have feedback effect. The main argument of this article is that, as a result of complex processes, the economic collapse in Latvia has created conditions conducive to the current political system of Latvia and especially to political cleavages in that system, which, following Douglas Rae and Michael Taylor, are understood as “the criteria which divide the members of a community or sub-community into groups, and the relevant cleavages are those which divide into important political differences at specific time and place”⁵, but with the assumption that different kinds of dividing lines can cross each other and that they do not exclude each other (according to Stefano Bartolini and

² “Baltic economies. The Estonian exception”, *The Economist*, October 31st 2009, p. 38.

³ Kossow M. ed., *Kronika Sejmowa*, Warszawa Wydawnictwo Sejmowe, 2010, No. 62(698), p.38.

⁴ Sumilo E., Apsalone M., “The impact of international financial crisis on capital migration into Latvia”, *Baltic Rim Economies*, No. 2, 2009, p.34.

⁵ Römmele A., “Cleavage Structures and Party Systems in East and Central Europe”, in Lawsan K., Römmele A., Karasimenov G. eds., *Cleavages, Parties, and Voters. Studies from Bulgaria, the Czech Republic, Hungary, Poland, and Romania*, PRAEGER Publishers, 1999, p. 6

Peter Mair).⁶ Therefore, the objective of this paper is to clarify whether and to what extent the economic crisis could affect changes in the political and social system.⁷

For explanatory purposes, the author will refer to the classical definition of a political system,⁸ according to which it “is a network of links through which the government produces outputs in response to inputs.”⁹ In this case, the concept of the political system includes not only the mechanisms of governance and institutions operating within its framework, but also all the structures and processes in its space that influence each other. The main subject of this analysis is the party system of Latvia — the component of the entire political system upon which the basis of feedback reactions occurs at the inputs and outputs, and including the political cleavages, which are defined by the social divisions relevant to voters.¹⁰

1. Determinants of the Economic Crisis in Latvia

As is the case with the other Baltic States, the Latvian economy was restructured in the early 1990s, and then it gradually changed from the agricultural and industrial to service economy. Before 1991, the leading branches of

⁶ Ibid., p. 6. See also: Whitefield, “Political Cleavages and Post-Communist Politics”, *Annual Review of Political Science*, No. 2, 2002, p. 181 – 184.

⁷ For elaboration on the arguments of this article and more information on the development of the party system in Latvia, see: Dudzińska, K., “*Rewolucja versus ewolucja – polityczne konsekwencje kryzysu gospodarczego*” [Revolution versus evolution – the political consequences of the economic crisis in Latvia], in Vall du M., Majorek M., Walecka Rynduch A. eds., *Współczesna przestrzeń polityczna. Ewolucja czy rewolucja?* [‘The contemporary political sphere. Evolution or Revolution?’], Krakowska Akademia im. A. F. Modrzewskiego, 2011, p. 143-160.

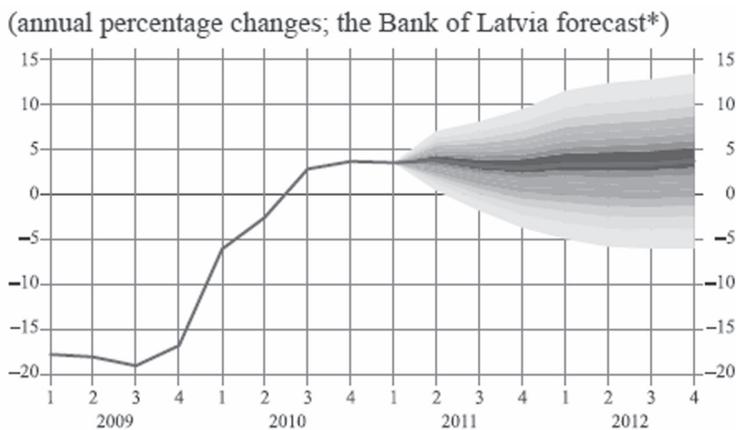
⁸ Nowak S., *Metodologia badań społecznych* [‘Methodology of social research’], Warszawa PWN, 2007, p. 352.

⁹ Heywood A., *Politologia* [Politics], Warszawa PWN, 2006, p. 30. Moreover, according to Marek Żmigrodzki the political system is defined as the state apparatus, political parties, organizations and social groups, both formal and informal. See: Żmigrodzki M., „System polityczny”, in Chmaj M., Sokół W. eds., *Mała encyklopedia wiedzy politycznej*, [The Small Encyclopedia of Politics], Toruń Adam Marszałek, 2001, p. 370-371.

¹⁰ Dalton R.J., “Political Cleavages, Issues, and Electoral Change”, in Lawrence LeDuc et al. *Comparing Democracies: Elections and Voting in Global Perspective*, Sage Publications, 1996, p. 329-335.

the manufacturing industries were chemicals, foods and wood processing. However, the importance of agriculture and industry to the Latvian economy shrank every year in the '90s. The opposite was true of the services sector, which grew with each passing year (1990: 31.9%; 2009: 72.4%).¹¹ After regaining its independence, Latvia's authorities closed many factories and production facilities (including the famous VEF as well as RAF and Alpha). Although the economic crisis over the period 2008–2010 was not the first crisis with which Latvia had to cope, it was so severe that forced changes in the political arena. In the third quarter of 2009, Latvia's GDP decreased by almost 20% year on year.¹²

Graph 1. **Percent GDP in the Baltic States (year on year)**



* The coloured area represents 90% of potential scenarios (the lighter the colour, the lower the scenario's probability).

Source: Macroeconomic Developments Report, Latvijas Banka, 2011 July, p. 35.

¹¹ See: Norgaard O., Hindsgaul D. eds., *The Baltic States after Independence*, Edward Elgar Publishing, 1996, p.141. See: "Latvia Economic Structure", Economy Watch http://www.economywatch.com/world_economy/latvia/structure-of-economy.html See: Vanags A., Štrupiņš A., *Corporate Governance in Latvia*, Seminar on Corporate Governance in the Baltics, Vilnius, Lithuania 21-22 October, 1999, p. 5. See: Hansen M., *The Latvian Economy: The Harder They Come, the Harder They Fall?*, Friedrich Ebert Stiftung, September 2010, p. 4-8. Gopanenko A., Rodin M., "System crisis of the Latvian society—the reasons, scenarios of development, possibility of overcoming", *Baltic Rim Economies Bimonthly Review*, No 2, 2009, p. 41.

¹² Macroeconomic Developments Report, Latvijas Banka, 2011 July, p. 35.

Also surprising was the dynamic growth of the budget deficit, which before the economic collapse, was not expected to exceed the 3% of GDP threshold that defines one of the euro-entry criteria; however, in 2008 the deficit grew to 4% from a budget surplus of 0.1% GDP in 2007.¹³ Meanwhile, in 2010, the budget deficit in Latvia was estimated to be nearly 8%,¹⁴ mainly as a result of a decline in the construction industry. That was a very important indicator since in previous years the industry had made up over 7% of GDP. At the same time, there was also a drastic fall in property prices (by 60%).¹⁵ From this data, it is clear that in Latvia, just as in many other countries at the same time, the crisis originated from the collapse in the real estate market as well as the finance and the banking sectors.¹⁶ However, the economic collapse in Latvia was also the result of many internal factors that contributed to such a drastic deterioration of the national economy. Latvia's economy grew at a rapid pace until 2007, which eventually caused it to overheat.¹⁷ And because the currency was pegged to the euro, the country was unable to fight inflation through the use of monetary policy to lower interest rates to encourage taking out ever larger loans, mainly for consumption.¹⁸

Moreover, in 2004, Norwegian and Swedish investors entered the Latvian market (primarily the banks Swedbank, SEB and Nordea). EU accession accounted for a surprising early turning point in economic growth. Then the economies of Lithuania, Latvia and Estonia opened to foreign markets and the economy was hailed as a "Baltic tiger". However, it should be emphasized that, especially in Latvia, it was the influx of capital and foreign investment

¹³ Rozenvalds J. ed., *Latvija. Pārskats par tautas attīstību. Atbildīgums*, Sociālo un politisko pētījumu institūts, 2009, p. 88.

¹⁴ European Union Balance of Payments Assistance. Latvia. EC Staff Report from the 4th Review Mission to Riga, Directorate General Economic and Financial Affairs, Brussels, 20 May 2011, p. 2.

¹⁵ Truszewicz I, „Kryzys pożera pensję łotewskiego ministra” http://www.rp.pl/arttykul/259197,424396_Kryzys_pożera_pensje_lotewskiego_ministra.html (10.10.2011)

¹⁶ Nyberg L., *The Baltic region in the shadow of the financial crisis*, Deputy Governor of the Sveriges Riksbank, at Intervalor and Baltic Property Trust, Stockholm, 9 September 2009, p. 4-5. See also: Lannin P., “Latvia crisis strikes across society”, <http://uk.reuters.com/article/2009/06/10/feature-latvia-idUKLNE55902E20090610> 10.09.2011.

¹⁷ Bank of Latvia: Annual Report 2010, Latvijas Banka 2010, p. 18-20. See also: “Economic Reviews: Latvia”, *Baltic Rim Economy*, No. 2, 29 April 2009, p. 2.

¹⁸ Erixon F., *Baltic Economic Reforms: A Crisis Review of Baltic Economic Policy*, European Centre for International Political Economy, No 04., 2010, p. 4 -7.

as well as the favourable conditions created for foreign investors that developed the high economic indicators. Once in the crisis, the intervention of Sweden in funding its banks resulted, among other factors, in the deterioration of one of the largest Latvian banks, Parex, and, confronted with the impending threat of losing financial liquidity, the government nationalized it (the government took a 51% share initially, but then it rose to 85%).¹⁹ In addition, after joining the EU, Latvia generally benefited from the easy access to low-interest loans, including foreign currency. Besides, a large influx of money from EU funds was not adequately exploited. As Gopanenko and Rodin emphasize, the money was often absorbed by the bureaucratic apparatus itself. Because of this, the country's credit load in 2005—from both financial and non-financial institutions and households—amounted to 52.4% of GDP, and in late 2008 it rose to 110% of GDP. Meanwhile external state debt in 2005 was 25.4% of GDP, and in 2008 it constituted 57.6%.²⁰

Another factor that contributed to the country's economic crisis was the growing weight of public administration. In 1990, the ratio of people employed in public institutions was constituted 3%, but in 2008 it was 7.8% of total employment. To compare, it is worth noting the share of spending on salaries in the administration: in 1991, the bureaucracy comprised 2.9% of the budget, while in 2008 the indicator rose to 12.3%.²¹ At the same time, the unemployment rate was getting to a higher level.²²

Moreover, a very important factor that analysts point out is demographics: the population of Latvia has been steadily decreasing since the late '80s, and the number of working-age people has decreased as well. Between 2010 and 2060, a sharp decline of the population is predicted for Latvia (-26%), and in 2060, the share of the population aged 65 or more will probably amount to 35%.²³

¹⁹ Gopanenko A., Rodin M., (note 11), p. 42.

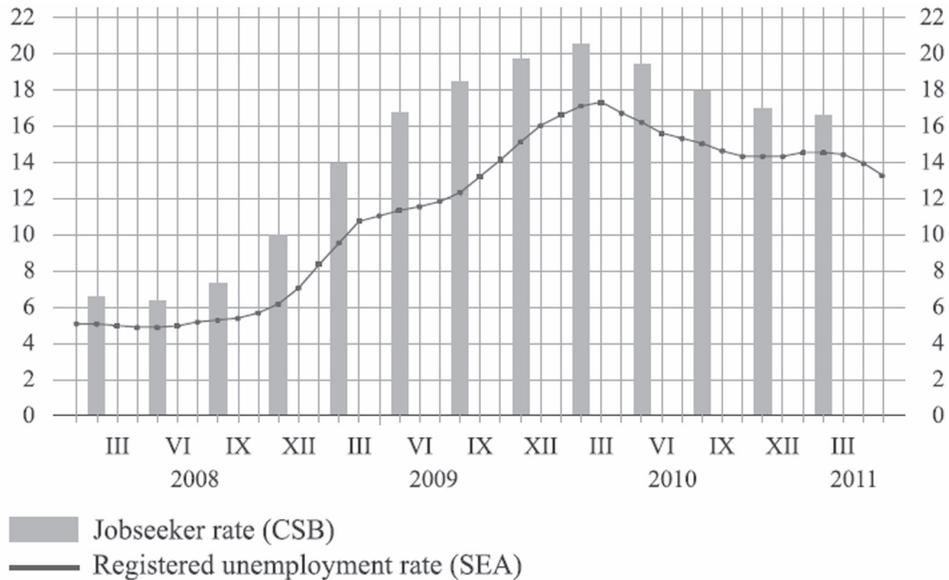
²⁰ Ibid., p. 43. See also: Republic of Latvia Third Review Under the Stand-By Arrangement and Financing Assurances Review, Request for Rephrasing of Purchases Under the Arrangement, and Request for Waiver of Applicability of a Performance Criterion, IMF Country Report No. 10/357, December 2010, p. 23. See: Weisbrot M., Ray R., *Latvia's Recession: The Cost of Adjustment With An „Internal Devaluation”*, Center for Economic and Policy Research CEPR, February 2010, p. 11.

²¹ Gopanenko A., Rodin M., (note 11), p. 42.

²² Ibid., p. 41.

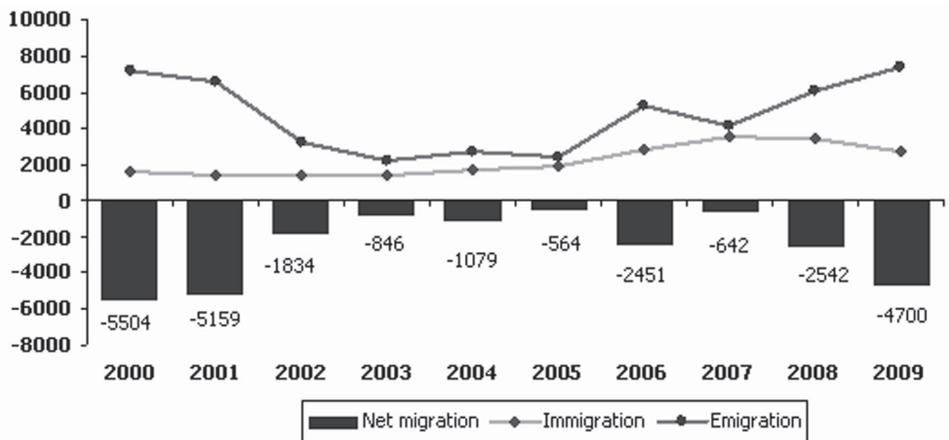
²³ Population projections 2010-2060, Eurostat News Release, 80/2011 - 8 June 2011. http://epp.eurostat.ec.europa.eu/cache/ITY_PUBLIC/3-08062011-BP/EN/3-08062011-BP-EN.PDF

Graph 2. Registered unemployment in Latvia



Source: Macroeconomic Developments Report, Latvijas Banka, 2011 July, p. 24.

Graph 3. Registered emigration in Latvia



Source: Central Statistical Bureau in Latvia

At the same time, there have been several years of successive increases in the levels of emigration from Latvia, mainly to the EU and Western countries.

All of the factors mentioned so far clearly show that the crisis was apparent in various segments of the economy. Attention should also be paid to the negative impact of the country's financial policy, which was often the result of poor political decisions. Although the economic crisis in Latvia has many elements, it is primarily the incompetent use of the resources for growth and economic development that made stable development impossible.²⁴

2. The Political System and the Economic Crisis in Latvia

The economic crisis in Latvia is systemic in nature and is not based only on elements of economics and finance. The international crisis itself did not cause the economic downturn in Latvia, but it made the country's recession more severe and serious. Moreover, while the Latvian crisis was based on the economic recession, it was precipitated by internal factors as well as economic and political backgrounds.

2.1. The Economic and the Government Crisis

The deteriorating economic situation was not indifferent to Latvia's political system. On 13 January 2009, Riga witnessed the largest protest since the restoration of Latvia's independence. Originally a peaceful demonstration organized by NGO activists, it transformed into a riot. An estimated 10,000 people gathered in front of the Latvian Parliament, and about 50 demonstrators were injured and 100 were arrested.²⁵ The consequences were immediate: the very next day, President Valdis Zalters announced that he was considering the dissolution of parliament.

Later came the collapse of the ruling government in February 2009 when the conservative–liberal government of Ivars Godmanis (Latvia's First Party/

²⁴ Gopanenko A., Rodin M., (note 11), p. 43.

²⁵ Kažoka I., Akule D., *Latvia: Extreme political turbulence*, Commentary European Policy Institutes Network, No 3/9 February 2009, s. 2. EPIN <http://www.ceps.be/system/files/book/1794.pdf>

Latvian Way, or LPP/LC) resigned under pressure from his party opponents.²⁶ As a result of the events in March 2009, a new government headed by Valdis Dombrovskis was finally sworn into office. The new government was composed of the New Era (JL), the People's Party (TP), the Civic Alliance (PS) and the Union of Greens and Farmers (ZZS), as the Union for Fatherland and Freedom (TB/LNNK) earning a total of 64 votes in the 100-seat parliament (the Saeima). While multi-party government coalitions have been typical for Latvia since the nineties, they have been mostly unstable and impermanent.²⁷ However, at that time a broad coalition was also formed, and within a few months after Dombrovskis had taken power, budget reductions in social assistance and pensions as well as wages in the public sphere were booked on the list of savings.²⁸

2.2. The Elections During the Economic Crisis

In the face of the economic collapse that brought about a government crisis, it seems to be appropriate to analyze the results of the elections that have taken place in Latvia from 2009 to 2011. The analysis should reveal whether, over these few years, the difficult economic situation has created conditions for potential changes at the political and social levels of the system in Latvia. During this period, Latvia held elections for both local offices and the European Parliament in 2009 and for the Saeima in 2010. Because of the dissolution of parliament, the latter were held again almost one year later in 2011. Taking this into consideration, it is worth mentioning that, after regaining its independence, Latvia developed a multiparty system in which both the effective number of electoral parties (5.06) and the effective number of par-

²⁶ For the PCTVL home page and available programs, see: www.pctvl.lv

²⁷ From 1990 to 2011, the majority of governments were established in Latvia alternating between opposition forces in accordance with the so-called "pendulum principle" until 2010. The first exception to this rule was the Dombrovskis government in 2010. For more about political parties in Latvia, see: Auers D., "Latvia's 2002 Elections-Dawn of a New Era?", *East European Constitutional Review*, Fall 2002/Winter 2003, pp. 107–110.

²⁸ See: Ministru prezidenta Valda Dombrovskā uzruna Saeimā 2009.gada 12.martā [Speech of the Prime Minister] <http://www.mk.gov.lv/lv/mp/runas-pazinojumi/dombrovskā-runas/12032009/> 25.08.2010. Ministru prezidenta Valda Dombrovskā uzruna 16.jūnijā Saeimas ārkārtas sēdē par 2009.gada valsts budžeta grozījumiem [Speech of the Prime Minister], <http://www.mk.gov.lv/lv/mp/runas-pazinojumi/dombrovskā-runas/17062009-Dombrovskā-runā-16-jūnija-Saeimas-sedē/> 25.08.2010.

liamentary parties (4.52) exceed the European average.²⁹ At the same time, the emerging political parties often cause transformation as well as connections to or divisions within the existing parties. In 2002, there were more than 60 registered political organizations in Latvia.³⁰ The multiplication of the number of the parties in Latvia resulted in many parties lacking enough votes to cross the electoral threshold, especially in the initial stage, which effectively stabilized the number of relevant political parties. Only in 1995 was a threshold of 4% formally introduced, and later it was raised to 5%.

The municipal and the European Parliament elections were held on 6 June 2009. A new conservative group, Civic Alliance (PS), which was established in 2008 by Sandra Kalniete, former Foreign Minister and European Commissioner, won 24% of the votes and two of Latvia's eight possible seats in the EP.³¹ Another two seats (with 20% of votes) were won by the Harmony Centre (SC), which opposed the centre-right government of Dombrovskis. The other parties (the For Human Rights in United Latvia (PCTVL), LPP/LC, TB/LNNK, JL) won one seat each in the EP. But in local elections, Nils Ušakovs from the Harmony Centre was elected mayor of Riga. In comparison to For Human Rights in United Latvia, this moderate party represented mainly the interests of the Russian-speaking minority and obtained a majority of votes in Riga (34.29%).³² However, local elections in the capital city resulted in a second batch of wins for the Civic Alliance, which gained 14 seats. The party with the biggest number of losses in these elections was the People's Party, which did not win any seats on the City Council. Observers commented that the result was a direct response to the actions of the then ruling party (the People's Party was part of the coalition government and had the most seats in the Latvian Parliament). This situation indicated a radical change in the political landscape, at least in Riga, where the pro-Russian party won with 26 out

²⁹ Election indices: http://www.tcd.ie/Political_Science/staff/michael_gallagher/ElSystems/Docts/ElectionIndices.pdf (10.10.2011). See: Jungerstam - Mulders S., *Parties and Party Systems in Post – Communist EU Member States: Comparative Aspects*, in Jungerstam - Mulders S. ed., *Post – Communist EU Member States. Parties and Party System*, ASHGATE, 2006, p. 5.

³⁰ Ikstens J., *Party Organizations in Latvia*, The National Council for Eurasian and East European Research, Vidzeme University College Washington D.C., 2006, p. 6. See: Schmidt T., *Das politische System Lettlands*, in Ismayr W. ed., *Die politischen Systeme Osteuropas*. Opladen 2002. p. 133.

³¹ www.cvkv.lv

³² www.cvkv.lv

of 60 members elected to the City Council. In other regions, though, the results of the local council elections proved to be more predictable. The outcome in the capital city was attributed to the concentration of a leftist electorate dominated by a Russian-speaking minority. But there were non-pro-Russian urban voters, too, who in the general election profile are much less conservative than the traditional inhabitants of villages and small towns.³³

Moreover, the parliamentary elections in October 2010 proved that the Harmony Centre was becoming a stronger party in Latvia, even while remaining in the opposition with 29 seats. Then the election was won by a new coalition of centre-right parties — the Unity (33 seats) formed a government with the centrist Union of Greens and Farmers (22 seats), over which the mayor of Ventspils, Aivars Lembergs, one of the richest men in the Baltics, enjoys considerable influence. It is worth mentioning that the right-wing coalition National Alliance (8 seats) did not join the new government, but often supports it in parliament. The so-called “party of Latvian oligarchs,” the coalition For a Good Latvia (8 seats), also remained outside the government. Despite the risk of devaluation, the second government of Dombrovskis continued its disciplined budgetary policies aimed at stabilizing the economic situation. It passed a number of restrictive decisions (an increase in VAT, an excise tax and reductions in social benefits) and at the same time, the average monthly wages fell again to €630 per person in 2010.³⁴

In this economic atmosphere, people were getting tired of the crisis. On 17 September 2011, less than a year after the change in the parliament, the parliament elections took place again. Early elections for the Latvian parliament took place after former President Valdis Zatlers had requested the dissolution of parliament in May. Most of the population (94%) supported his proposal during the referendum which took place in July. The impetus to this action was spurred by the Saeima’s decision to reject a request by the Corruption Prevention and Combating Bureau (KNAB) for permission to search the private property of influential entrepreneur and politician Ainārs Šlesers. In his speech, Zatlers warned against the rampant “privatization of policy”, the growing influence of “oligarchs” and urged to fight against corruption. The

³³ K. Rizga, “Latvia Moves Leftward in Recent Elections”, <http://pulitzercenter.org/blog/untold-stories/latvia-moves-leftward-recent-elections>

³⁴ Rekke E., “Average monthly gross wages and salaries in Latvia reduced by 3.5% in Q4”, see: <http://www.baltic-course.com/eng/analytics/?doc=24221>

president's decision to hold early parliamentary elections came as a surprise. As a result, Zatlers lost his chances for re-election, and in June, the MPs in vote for a new president, supported the candidacy of Andris Bērziņš from the Union of Greens and Farmers.³⁵

In the early elections in 2011, the pro-Russian Harmony Centre obtained 31 seats (or two more than a year ago). After the elections, it seemed likely that the Harmony Centre would cooperate with the Reform Party, which had been founded by former President Zatlers and which won 22 seats and came second in the previous elections. Perhaps its success may be partly attributed to the fact that it took votes from its potential coalition partner, the centre-right Unity Party, which won only 20 seats (relative to 33 in 2010). On the other hand, it is worth mentioning that the Reform Party mobilized that part of the electorate which was probably not willing to vote for the Unity. In this way, the parties concerned obtained 42 seats in total. At the same time, the radical National Union Party strengthened its positions in parliament and increased its number of seats from eight to 14, while the Union of Greens and Farmers, which retained 13 of its 22 parliament seats, and Ainārs Šlesers' new Reform Party LPP/LC, which did not surpass the minimum threshold, suffered a painful defeat. The latter two parties are commonly associated with Latvia's biggest businessmen, the so-called "oligarchs".³⁶

3. The (Im)Possible Socio-Political Changes in Latvia

Between the years 2009 and 2011, Latvia had four governments and, in the same period, held elections five times: once for local governments, the European Parliament and the presidency, and twice for parliament. While taking into account the fact that the elections were held first at the time of the economic crisis and later in its shadow, the question arises whether and how this situation has changed the political system in Latvia, especially in view of the functioning of the political parties. Among other factors are vot-

³⁵ www.cvk.lv, see also: Dudzińska K., *Implications of the Referendum on the Dissolution of the Latvian Parliament*, Bulletin PISM, Bulletin PISM No 64 (281), June 16, 2011, p. 528.

³⁶ Dudzińska K., *Parliamentary Elections in Latvia: Problems with the Appointment of the Coalition Government*, Bulletin PISM, No. 92 (309), October 5 2011, p. 582.

er preferences of the Latvian electorate, which seemed to disturb the existing lines, such as socio-political divisions, only at first glance.

It is worth mentioning that the modern party divisions in Latvia that were shaped after 1991 have little in common with the shape of the political life during the first independence. According to an analysis by Seymour Lipset and Stein Rokkan, political cleavages, the traditional lines of divisions, had not evolved in Latvia enough to become as permanent as in Western democracies.³⁷ They were distorted largely because of the experience of the communist era, then by specific circumstances associated with the crystallization of the political scene during the transition state.³⁸ Moreover, contemporary research suggests that the lines of conflict are generated by two main issues in Latvia. The first is ethnic politics, which had been especially important before rules were adopted that regulated the right of citizenship and the naturalization process. This largely affected the Russian-speaking minority. The second issue involves attitudes towards socio-economic development, including, in particular, the issue of privatization.³⁹

Since 1991, the polarization of political parties was especially pronounced in Latvia, primarily, with regard to nationality. However, it should be emphasized that the distinction between leftist and rightist parties is not clear in Latvia. Left-wing parties represent mainly the interests of Russian-speaking minorities. For this reason, these organizations cannot be overlooked. This is particularly true of the For Human Rights in United Latvia party (PCTVL), which for a long time was the core organization fighting for the rights of the ethnic Russian minority in Latvia. Although the radical position of seeking equal rights for ethnic Russians is not represented by the Harmony Centre, its programs also contain elements of social equity and solutions that involve economic processes by the government. Moreover, the Harmony Centre has become the only important party defending the interests of ethnic Russians. According to 2004 data, ethnic Latvians constitute 58.5% of the residents of

³⁷ Zarzycki T., „W poszukiwaniu peryferii. Teoria podziałów politycznych Lipseta - Rokkana w kontekście polskim”, in Dajnowicz J. ed. *Oblicze polityczne regionów Polski* [The political nature of regions in Poland], Białystok, Wydawnictwo Wyższej Szkoły Finansów i Zarządzania 2007, p. 13-15. See also: Pabriks A., Štokenberga A., “Political Parties and Party System in Latvia” in Jungerstam-Mulders S. ed., *Post-Communist EU Member States. Parties and Party System*, ASHAGATE 2006, p. 53.

³⁸ Pabriks A., Štokenberga A., (note 37), p. 51 -53.

³⁹ *Ibid.*, p. 52-58. See: Auers D., (note 27), p. 108.

the country, while 29% are ethnic Russians. Latvian citizenship comprises 77%–79% of the population of the country, including 48.96% of the ethnic Russians living in Latvia.⁴⁰ Speaking more broadly, the problem of the Russian-speaking minority was extremely important across the Baltic States and was a flashpoint in relations with Russia.⁴¹

In this light, though running as a Latvian leftist party supporting state-run economic mechanisms, the Latvian Social Democratic Workers' Party (LSDSP), does not play a significant role. This is mainly because of the historical connotations to the previous system, and also as result of personal conflicts among Latvian leftists (another leftist party, the Socialist Party of post-communist Latvia, or LSP, represents Russian speaking minorities and belongs to the Harmony Centre). In fact, the LSDSP does not fall within the categories of the current political system. Overall, in recent years and particularly during the crisis, and regardless of the ideological identity of individual lots, each of the political parties in Latvia defined social issues in their programs. These were clearly displayed apart from national identity issues and raised questions about the social sphere, welfare and health care. In 2011, the latter proved to be decisive and ruled the outcome of parliamentary elections.

Furthermore, the fact that social issues became the most important elements of the public discourse during the last elections in Latvia might make one expect that leftist parties could count on having the most support among the Latvian population. However, as has been mentioned above, although the communist period distorted the political divisions, Social Democrats are not currently playing a significant role in the Latvian political arena. Meanwhile, only the Harmony Centre, while representing mainly the interests of the Russian-speaking minority, but at the same time, by using social demands for such guarantees, has built its electoral capital on social slogans promising to index pensions to inflation and to allocate more money for education and health care.⁴² These promises brought the Harmony Centre not only Russian-speaking votes, but are also likely to have attracted ethnic Latvians.

However, lack of stability in the party system determines the condition of political life only within a specified range. In Latvia, the quality of political life

⁴⁰ Hyndle J., Kutysz M., *Rosyjskojęzyczni na Łotwie i w Estonii* ['Russian-speaking population in Latvia and Estonia'], CES Studies, Warsaw 2004, p. 43.

⁴¹ A. Pabriks, A. Štokenberga, (note 37), p.59-64.

⁴² See: Program of the Harmony Centre http://www.saskanascents.lv/lv/musu_programma/

has been to a large extent dominated by corruption and a tendency to link state policy to business needs.⁴³ The relations between business and politics were confirmed by the sale of votes in local elections in 2005 (“Jurmagate”) as well as practices involving bribery.⁴⁴ Political parties gave promises to increase financial transparency and to fight corruption. The New Era (JL) used this to win the elections in 2002. Moreover, the desire to fight corruption prompted former President Zatlers to submit the request to dissolve parliament in 2011. Besides the huge impact on the functioning of the party system, Latvia experienced a lack of restrictive laws on the foundation of political parties. As early as 2002, the permissible amount of donations made to political parties by individuals and other entities was reduced from 25,000 to 10,000 lats.⁴⁵

Conclusions

Latvia’s political system is still not very stable and is characterized by the above-average fragmentation of the parties. Since 2000, on average six political parties have sat in parliament. However, the economic crisis has had a clear impact on the political system of the state. First of all, for the first time since 1991, Latvia witnessed mass demonstrations. Then, the economic downturn brought about a crisis in the government and changes to cabinet. In addition, the collapse in the economy eventually determined the outcome of local and European Parliament elections in June 2009. Efforts to combat the crisis also determined the election results in 2010 and 2011. Analysis of each election, especially over the past two years, has shown that there seemed to be new conditions for a change in the political system of Latvia.

So far, the political parties representing the Russian-speaking minority have not yet become part of any coalition government. However, changes in the political sphere indicate that the role and importance of these parties is gradu-

⁴³ Rusu A., *Latvia Report*, Civil Society Against Corruption, September 2010, p. 11-12. See: Dombrovsky V., *Campaign Contributions and Firm Performance: The ‘Latvian Way’*, August 2010, http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1168298

⁴⁴ Auers D., *On Potemkin Villages and Campaign Finance Reform*, <http://www.politika.lv/print.php?id=15776> (10.09.2011) See also: Progress and Results in Preventing and Combating Corruption in Latvia, KNAB, January – September 2011. http://www.knab.gov.lv/uploads/eng/periodic_update_september_2011.pdf

⁴⁵ Auers D., (note 27), p. 109.

ally increasing. If the moderate line is maintained in relation to national issues, the parties will have a chance to strengthen its role on the political scene. If the Harmony Centre decided to prioritize the issue of the Russian-speaking minority, then it should be emphasized that the party would be unlikely to have a chance to be in power. In the election campaign before the local elections, the Harmony Centre called for cooperation with ethnic Latvians and for the integration of the Russian-speaking minority. Also, before the 2011 parliamentary elections, the party effectively avoided the problematic issues, and, due to the accompanying growing tension, abandoned the ethnicity-focused platform. Moreover, it has to be taken into account that the early parliamentary elections in 2011 took place in the shadow of the crisis, and the low electoral score of the ruling Unity Party clearly showed that the society was tired of the restrictive financial policy. At the same time, the Harmony Centre had built its electorate on social slogans, which must have been the main cause of its good results.

However, a permanent change in the qualitative nature of Latvian politics could be expected, when the leftist pro-Russian party won the elections for the first time. The aggregation of a majority vote of both Latvians and the Russian-speaking minority by one party could lead one to believe that the post-communist political lines have gradually faded away. But compared to 2010, the role of right-wing parties that have clear national origins has also increased. This rise in support of the National Alliance evidences that there is no significant change in political cleavages with regard to nationality, especially given the fact that, despite having scored best results in the elections, the Harmony Centre still remains in the opposition and will not become part of ruling coalition.

Meanwhile quite different changes are more probable, such as stabilization of the political system, since Dombrovskis has been appointed Prime Minister for the third time. At the same time, the consolidation of the political parties seems to be moving forward. Thus in 2011, parties that acted as electoral coalitions unified themselves. As a result, the Unity Party (the New Era, the Civic Union, the Society for Other Politics), and the National Alliance (All for Latvia! and For Fatherland and Freedom, or VL-TB/LNNK) have been set up. Moreover, the ruling coalition of Zatlers's Reform Party, the National Alliance and the Unity should guarantee the continuity of the previous policy. The Unity seeks to introduce the euro by 2014, which means maintaining strict financial discipline. This would also continue Latvia's pro-European course, which is set to intensify regional cooperation.