

# **ASSESSMENT OF BUSINESS ENVIRONMENT DEVELOPMENT PERCEPTION UNDER THE INFLUENCE OF COVID-19: THE CASE OF LATVIA**

**Prof. Dr. oec. Andra Zvirbule** <sup>1</sup>

**Prof. Dr.oec. Gunta Grinberga-Zalite** <sup>2</sup>

**Assoc.prof. Dr. oec. Aina Muska** <sup>3</sup>

<sup>1,2,3</sup> Latvia University of Life Sciences and Technologies, Latvia

## **ABSTRACT**

Not only macroeconomic growth scenarios and forecasts but also business environment assessments and development forecasts have changed as a result of the worldwide COVID-19 pandemic. Many of the forecasts are based on objective data on the performance of economic sectors; however, some of them are based on business perceptions or business sentiment assessments. There is no doubt that these perceptions and business sentiment assessments differ within business sectors and according to the size of the company, regional location, and type of business. The aim of the research is to identify and provide an assessment of the business environment development perceptions in the COVID-19 situation in Latvia and compare them with business sentiment assessments from other countries. Specific tasks of the research: to collect information on business environment changes in Latvia in the COVID-19 situation; to compile business perceptions of the impact of COVID-19 on the business environment in the world and in Latvia; to identify the perceptions of the business environment in the most important business sectors in Latvia. Methods: monographic, data grouping, logical construction and mathematical and statistical analysis. The research identified business environment changes in business sectors in Latvia under COVID-19's influence and business perceptions of the impact of COVID-19 on the business environment for the next 6 months. Based on the research, the authors have drawn conclusions about the future development of the business environment and have identified the sectors that will be negatively affected by the COVID-19 crisis in the coming months.

**Keywords:** *COVID-19 crisis, business environment, business sentiment*

## **INTRODUCTION**

The cyclicity of economic processes and various challenges, including crises, are now becoming a normal business risk factor and a factor affecting competitiveness. Theoretically, the life cycle of companies certainly involves changes in conditions and new challenges, which are initiated both by external environmental factors and by the internal environment. Several authors [3],[4] emphasize that rapid changes in the company's revenue and a decline in its

turnover are the cause of a crisis situation in the company. Other authors [1], [2], [9] however, recommend companies to use crisis strategic planning (CSP) to deal with the crisis and, in some situations, forecast a potential crisis, thereby focusing on business marketing, opportunity seeking, resource management, customer values, and risk-taking. There is no doubt that crisis management solutions and relative conditions for crisis situations in relation to an assessment of previous crises have yielded results and given a possibility to deal with any crisis situation in a faster or more predictable way. However, the crisis caused by the COVID-19 pandemic could be viewed as a completely unexpected and unforeseen situation affecting a very wide range of economic and business sectors, and a number of information sources [5], [6], [7] emphasize that lockdowns, travel bans, physical distancing and the widespread impacts of the global crisis have significantly changed not only the business environment but also the behaviour of every individual. The way we shop, where we do our work, how we travel and many other everyday things have changed. Even if the COVID-19 measures imposed are changed (eased), changes in our behaviour have already occurred, thereby significantly impacting business. Such changes cannot be predicted, and it does not make sense to enter data into algorithmic models developed before the crisis. Therefore, it reduces the ability to predict the emergence of a crisis. Moreover, the “lessons learnt” from previous crises and the responses based on analysis and experience transfer are not effective in this case. For example, reducing costs, creating new products, lowering prices, reorientation towards exports, retaining loyal customers, cutting wages, reviewing company functions and other responses under the COVID-19 conditions cannot be implemented because demand has not only decreased but has also shifted to other types of goods/services. The role of countries and governments in tackling the crisis is emphasized in the context of the global COVID-19 pandemic. The governments of several countries already actively work or already implement economic stabilization plans concerning the global pandemic, and most of the plans have two pillars: health care and the economic situation in the country. At the end of May 2020, the European Commission (EC) published proposals for a European Economic Recovery Plan concerning COVID-19, which provides support to all the European Union (EU) Member States. A novelty in the EC plan is a new temporary recovery instrument Next Generation EU (NextGen) designed to mitigate the damage caused by the COVID-19 crisis and to “prepare a better future for the next generation”. The funding raised for NextGen will be invested across three pillars: 1) helping the Member States to recover (support to the Member States with investments and reforms, support for fair restructuring); 2) kick-starting the EU economy by incentivising private investments (support for important sectors and technologies, investment in key value chains, solvency support for viable companies); 3) addressing the lessons of the crisis. However, a number of research papers [8], [10] and real data showed that the impacts of the COVID-19 pandemic on economic sectors, national regions and companies of all sizes in the same sector were completely different. Therefore, the aim of the research is to identify and provide an assessment of the business environment development perceptions in the COVID-19 situation in Latvia and compare them with business sentiment

assessments from other countries. Specific tasks of the research: to collect information on business environment changes in Latvia in the COVID-19 situation; to compile business perceptions of the impact of COVID-19 on the business environment in the world and in Latvia; to identify the perceptions of the business environment in the most important sectors in Latvia.

## **MATERIALS AND METHODS**

A number of scientific research and practical studies on global crisis management capabilities and “lessons learnt”, COVID-19 situation assessments – entrepreneur and businessperson opinions –, statistics, EU regulatory and strategic documents, business and consumer surveys in the EU and the McKinsey researcher group’s global surveys on COVID-19 were used to do the present research. The research employed the following methods: monographic, data grouping, logical construction and mathematical and statistical analysis.

## **RESULTS**

### **Impacts of the COVID-19 pandemic on the national economy and the business environment in Latvia and the other Baltic States**

The COVID-19 pandemic makes a major impact not only on the economy as a whole but also on the pattern of consumption and the structure of the economy. Several research studies have been carried out on the impacts of the pandemic on specific industries of the economy. Global research studies showed that the industries least affected were those involved in the extraction and processing of natural resources, as well as the construction industry and public administration. Global crises make significant changes in a number of business areas. The COVID-19 pandemic crisis has made a major impact on transport, trade, tourism, healthcare, IT services, education and logistics. According to research studies (surveys) on the impacts of the COVID-19 crisis by the McKinsey researcher group, the business areas that were resilient and would definitely restructure their business become explicitly apparent. The business areas with the highest probability of restructuring are trade, telecommunications and banking, whereas those with the lowest probability are natural resources (including agriculture), public administration and medicine trade. In order to be able to assess certain trends in the global crisis in national economies, especially small countries, and in this case small neighbouring ones, a common crisis management strategy and cooperation are needed. It has been established that all the three Baltic States (Latvia, Lithuania and Estonia), the Nordic bloc (Finland and Sweden) and also the rest of Europe focus on three main courses of action: 1) provide direct support, i.e. allocate financial resources from the government budget to support specific areas; (2) various kinds of payments, including taxes, are deferred by extending payment deadlines; 3) issue various kinds of credit guarantees and grant loans for various business areas. At present, there is no fundamental difference in the allocation of support among the Baltic States. The success of the COVID-19

pandemic management strategy in the Baltic States and the stabilization of the economic and economic situation is also evidenced by the indicators of business sentiment.

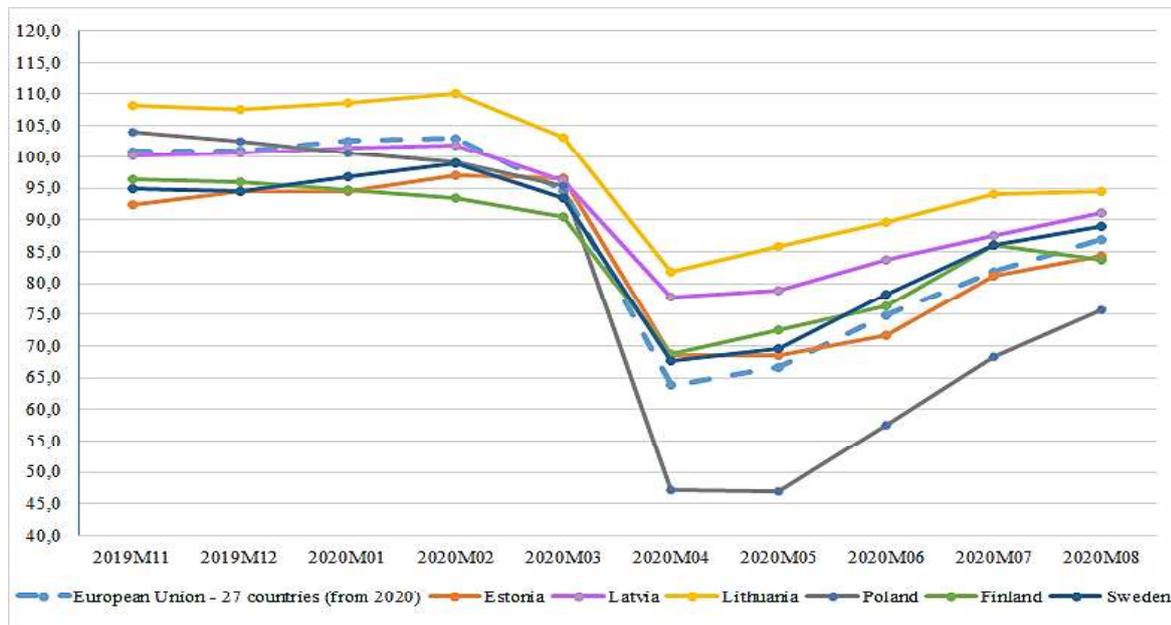


Fig. 1. Economic sentiment indicator (index), November 2019 - August 2020

The economic sentiment indicator shown in Figure 1 reveals that since March 2020 there has been a considerable decline in the sentiment, which indicates that business and economic activity were impacted by the crisis. The most considerable decline was observed in April 2020 – the sentiment indicator in all the Baltic States decreased by about 30-40% compared with February 2020. It is interesting to note that the average trend of the Estonian sentiment indicator coincided with the trends of the indicator for the Nordic countries (Finland and Sweden), which could be explained by the fact that the economy, labour market and exports of Estonia were strongly connected to these countries. The trends in Latvia, however, were more similar to those in Lithuania than in Estonia. It is a surprising fact that the economic sentiment in Lithuania’s neighbouring country, Poland, was not only more pessimistic than that in Lithuania but also significantly more pessimistic than that in all the three Baltic States and also in the rest of Europe. This indicates that the pattern of exports and potential markets of Poland have suffered more from the COVID-19 crisis than those of the Baltic States.

A number of business analysts and economists point out that such a positive trend in the Baltic States, including Latvia, was due to their fast responsiveness and the fact that all the three Baltic States sought to support companies that tried to use the current situation to expand and restructure their business. After summarizing the opinions of the analysts, it could be concluded that a number of measures were effective, and they were as follows:

- support measures for the tourism industry in Estonia were adopted in a very timely manner;
- in Lithuania, special support was provided to small and micro enterprises employing up to nine people through granting subsidies;
- in all the Baltic States, employment subsidies and support for job preservation were provided; in Latvia, the measures in terms of money paid out were the smallest among the Baltic States. In Lithuania, the total amount of employment subsidies was almost EUR 300 million;
- Latvia has stood out among the Baltic States in providing direct support to companies. Namely, EUR 250 million was allocated to the national airline airBaltic; in Estonia, Tallink (Estonian shipping group operating in the Baltic Sea) received EUR 100 million in support;
- in Lithuania, company tax payments in the amount of EUR 400 million were deferred. Lithuania, however, has stood out among the Baltic States as a nation giving helicopter money – the money for all or almost everyone without any conditions. In Lithuania, a one-off payment of EUR 120 was given to each child and a one-off payment of EUR 200 to each pensioner, which were credited to their accounts;
- most of the entrepreneurs concluded that the response to the crisis made by the Baltic governments was quick and easy to understand, and the rules were similar in all the Baltic States.

An in-depth assessment of the business environment for the main industries of the economy was based on information on the three Baltic States – Estonia, Latvia and Lithuania –, comparative indicators for the EU-27 and a comparative assessment of the Baltic States and Poland. The assessment used business confidence indicators, which revealed the overall situation in an industry and were obtained by conducting business surveys in the manufacturing and retail industries and the services sector. An indicator value above zero indicated a positive business environment, whereas a value below zero – a negative sentiment of entrepreneurs.

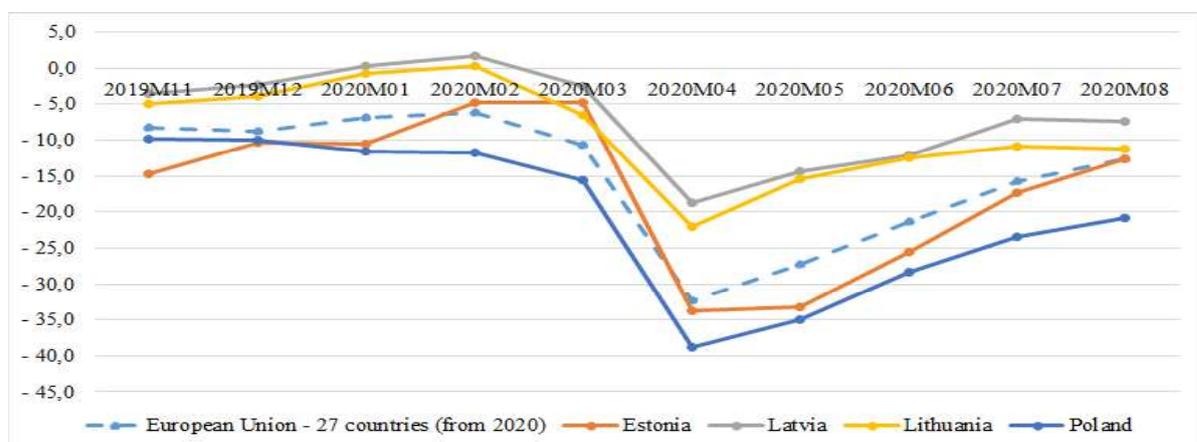


Fig. 2. Industrial confidence indicator (November 2019 - August 2020)

The industrial confidence indicator remained negative in all the countries analysed, while the most optimistic situation was in Latvia, which could be explained by the relatively low proportion of manufacturing in its economy – 12%. For comparison, the proportions of manufacturing in the other countries analysed were as follows: 17% in Estonia, 20% in Lithuania and 28% in Poland. This could be explained the fact that the industrial confidence indicator for Poland was at its lowest level, as the recovery of Polish manufacturing companies after the global crisis could be slower and the consequences could be more lasting. Nevertheless, comparing August 2020 with the previous month allows us to find that the forecasts of business activity (expected business activity) for the next three months as well as the forecasts of expected sales prices and employment for the next months, made by company managers for their companies, were slightly more optimistic, and their assessments of the current level of orders and overall economic activity were slightly more positive. The largest increase was observed for manufacture of textiles, clothing, furniture and basic pharmaceutical products. Owing to extensive teleworking, people spent more time at home and renovated their homes, which resulted in a growing demand for building materials and furniture. There was also a growing interest in buying private homes in many parts of the world, which boosted construction, and timber prices reached record highs.

There were no significant differences in the trends of the retail confidence indicator and the confidence indicator for the services sector between the countries analysed.

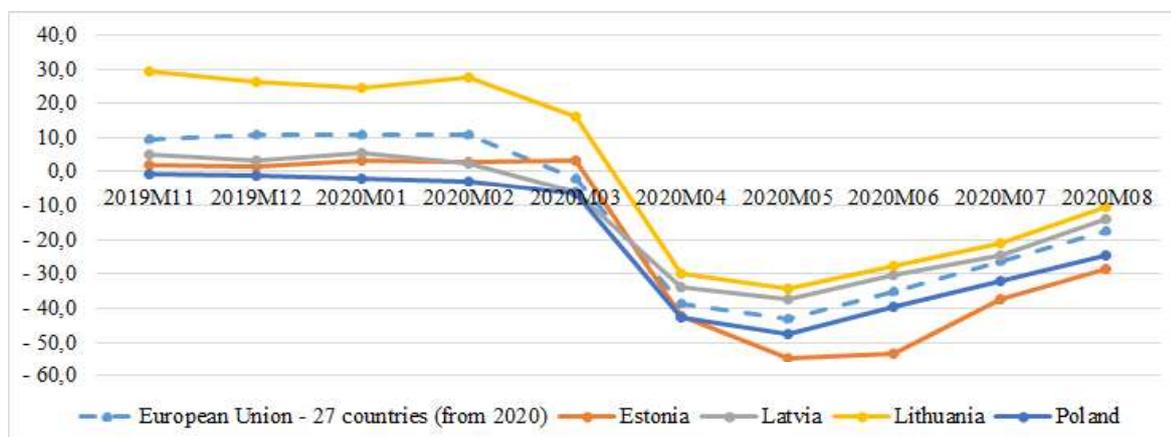


Fig. 3. Services confidence indicator (November 2019 - August 2020)

The confidence indicator for the services sector improved significantly in all the countries analysed, yet remained negative. In August, the confidence indicator was still negative for most service industries, whereas positive indicator values were reported only for building maintenance services, computer programming, information services, postal and courier activities. In all the countries analysed, the lowest indicator values were reported for accommodation and travel agency as well as tour operator activities.

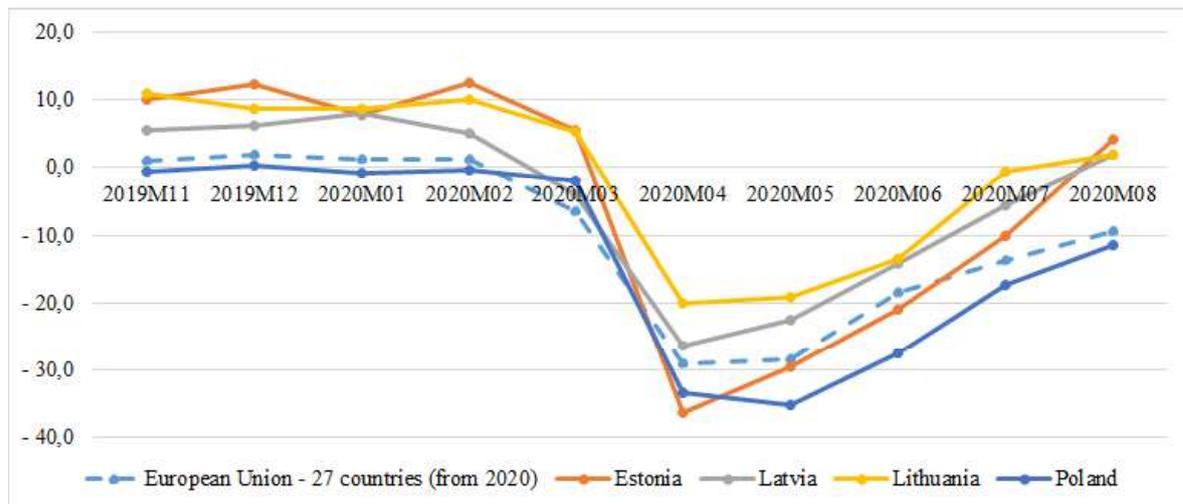


Fig. 4. Retail confidence indicator (November 2019 - August 2020)

In August 2020 in the Baltic States, the confidence indicator for retail trade was positive for the first time since the COVID-19 crisis began, whereas in Poland and the rest of the EU the average indicator values were still negative. The improvement of the confidence indicator in the Baltic States was mainly influenced by the respondents' positive assessments of the growth of economic activity for their enterprises in recent months, as a positive trend was observed for food and non-food retail trade, as well as fuel retail trade.

### Perception of the business environment in the most important sectors in Latvia

The recovery of manufacturing in Latvia in recent months was unexpectedly fast, and with the cessation of paying furlough benefits, most companies were able to resume their operation. This means that the producers were currently competitive, yet the risks remained high and the impacts of the COVID-19 shock were not fully eliminated. There were explicit signs that the economy stabilized after initial improvements in May and June, yet strong economic growth did not continue. In addition, during the period since the beginning of the COVID 19 crisis, the incomes of the population decreased, which made an impact on consumption. In Europe as a whole, business sentiment also deteriorated slightly in August, which hindered export industries from exiting the crisis. This allows us to conclude that strong continued growth in manufacturing over the next months is unlikely and that further growth depends on both progress in the fight against COVID-19 and the effectiveness of national business support programmes.

Nevertheless, new companies emerged in the production sector even during the COVID crisis, filling market niches and using this global crisis situation to develop their business ideas. *Case study 1*: the family company "TingPrint" started producing T-shirts, the designs of which relate to the time of COVID-19. The designs of T-shirts are created by artists living in various parts of Europe.

Each designer reflects in the design of a T-shirt the feelings experienced in recent months when the usual rhythm of life stopped due to COVID-19. *Case study 2:* since hand hygiene became an integral part of everyday life during the COVID-19 pandemic, three like-minded people implemented their business idea of a fully automated, contactless hand disinfection solution that is especially suitable for public places. After the emergency was declared, there was some chaos and disorder at the entrances to shops. To disinfect his/her hands, a buyer needed to touch surfaces that have been touched by almost all previous buyers. This suggested an idea of a safe hand disinfection solution. Basic hand hygiene has now become an integral part of everyday life; therefore, a product called Handbox was created to make the process of disinfection even simpler, safer and more cost-effective. The product is manufactured in Latvia and sold by our own efforts and using our own knowledge and relatively small resources. It is important that due to the pandemic, the classic situation is no longer observed in the tourism industry and, therefore, it is no longer necessary to rely on the assumptions that were true until now. The Baltic and Nordic tourism markets should now be viewed completely separately from global tourism markets and based on domestic demand. Currently, Latvia actively works on supplying autumn tourism products to the Finnish market, which mostly relate to cultural and culinary tourism. The situation in tourism companies is very different – there are companies that successfully implement their ideas and supply their products to local consumers and consumers in the Baltic States, and there is a critical situation in tour operator companies and large hotels that focus on business tourism and conferences. However, regional and coastal tourism in all the Baltic States survived the summer season and experienced no large changes. *Case study 3:* the emergency situation in the tourism industry becomes an opportunity, and the risk of opening a campsite this year was justified because people chose to travel to Latvia more this summer, and this situation in the tourism industry become an opportunity for national businesses. The company Camping Milk opened a new campsite this summer, and demand has been high since the beginning of July, with 100% occupancy from the first weeks to the end of the summer. The main audience was young couples, as well as families with young children and their four-legged pets, mostly from other parts of Latvia, and the company owners, seeing that the demand was high, plan to expand their business in the future. There are still problems in overcoming the COVID-19 crisis in all industries in Latvia and the Baltic States as a whole, yet the problems are increasingly viewed and assessed at the level of individual companies rather than at the level of an industry as a whole.

## CONCLUSION

1. The crisis caused by the COVID-19 pandemic could be viewed as a completely unexpected and unforeseen situation affecting a very wide range of economic and business sectors. The global COVID- 19 crisis have significantly changed not only the business environment but also the behaviour of every individual.

2. The retail industry in the Baltic States could be among the industries that prove to be relatively less affected by COVID-19; however, an assessment of consumer sentiment reveals that the sentiment was more pessimistic in Estonia and Latvia (consumer confidence indicator values ranged from -14.7 to -12.8), whereas in Lithuania it was almost positive (-3.5)

3. The industrial confidence indicator remained negative in all the countries analysed, while the most optimistic situation was in Latvia, which could be explained by the relatively low proportion of manufacturing in its economy – 12%.

4. Nevertheless, new companies emerged in the production sector even during the COVID crisis, filling market niches and using this global crisis situation to develop their business ideas.

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