



LITHUANIA: Headwinds from the east

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While the economic tide is low in the countries bordering the Baltic Sea, the economy of Lithuania will continue to grow at a stable rate of 3% in 2014. Rising employment and wages are backed by public investment; things are encouraging and conducive to keeping households in a good spending mood. Nonetheless, the trade sanctions on Russia will pose a threat to the economic viability of a number of exporters in the agro-food sector.

Lithuania, apart from Finland, will be the EU country hit hardest by the Russian economic sanctions enacted in August 2014 in terms of declining trade volumes. Close to 20% of Lithuanian exports are destined for the neighbouring country. However, about 80% of those goods are re-exported from other EU countries, thus the effective reduction in Lithuanian value added will be much lower. Estimations for the negative impact of the current sanctions range between 0.6% and 1% of GDP. The highest losses will be faced by meat and dairy producers, as well as the wholesale and transport sectors. In general, growth of export to the EU has not been less disappointing than trade with the Eastern neighbourhood. Since import activity lost momentum in line with exports, the current account remained in surplus in the first half of this year and is expected to move into deficit not earlier than next year.

Growth of investment is taking place in all sectors of the economy. While Lithuania's external conditions are not conducive to fostering growth prospects, a strong impulse stems from public outlays in infrastructure, which translates into higher investment activity in most industries and particularly in manufacturing. Furthermore, the deleveraging process of firms and households in the case of mortgage loans has come to an end. Construction volumes are increasing not only concerning non-residential buildings and infrastructure but particularly in the case of dwellings. Figures for granted building permits give rise to expectations that the development of construction activity will remain lively in the coming quarters.

Lively economic activity will keep employment growing by more than 1% in 2014. Particularly construction and agriculture create new jobs this year. In addition household incomes are increasing due to net wages rising significantly, by 4.4% on average in real terms in the first half of the year. Also remittances have kept on growing ever since emigration has peaked in 2010. A rise in the minimum monthly wage, which is expected to amount to between 5% and 10% in 2015, and the planned rise in the non-taxable income threshold will further prop up the purchasing power of the citizens.

Thus household consumption, which increased by more than 5% in the first half of 2014, will remain the most significant driver of GDP growth in Lithuania also in the coming two years. Retail trade figures show that household expenses are swiftly rising for consumer durables and services.

The general budget deficit is expected to decline further, to 2% in 2014. In the medium run the share of public expenditures is expected to fall towards the pre-crisis level of 33% of GDP, the lowest rate in the European Union.

In January 2015 Lithuania will finally become the 19th member of the euro area. A significant influx of additional foreign direct investment due to the accession is not likely. Long-term interest rates for 10-year government bonds already declined to 2.6% in August 2014. A remarkable further reduction of refinancing costs for the public debt is not to be expected.

In 2014 the Lithuanian economy is expected to expand at a stable growth rate of 3% in real terms. In the two years thereafter consumption of households will remain the main driver of growth, supported by public investments in transport and energy infrastructure. Although predictions about the development in the relations between Russia and the EU in the coming year are difficult, we suppose that the trade sanctions will not be broadened. A slight upswing of external demand in the EU countries is far from certain, but our baseline scenario. Thus we keep our forecasts for the coming two years almost unchanged and expect GDP growth to rise to 3.2% in 2015 and 3.4% in 2016.

Table 1 / Lithuania: Selected Economic Indicators

	2010	2011	2012	2013 ¹⁾	2013 January-June	2014	2014	2015	2016
								Forecast	
Population, th pers., average ²⁾	3,097	3,028	2,988	2,958	.	.	2,928	2,900	2,875
Gross domestic product, LTL mn, nom.	95,676	106,893	113,735	119,575	56,776	59,055	123,500	129,000	135,800
annual change in % (real)	1.6	6.0	3.7	3.3	3.7	3.3	3.0	3.2	3.4
GDP/capita (EUR at exchange rate)	8,900	10,200	11,000	11,700	.	.	.	.	.
GDP/capita (EUR at PPP)	15,100	16,900	18,300	19,500	.	.	.	.	.
Consumption of households, LTL mn, nom.	61,285	66,894	71,709	75,870	36,470	38,424	.	.	.
annual change in % (real)	-3.7	4.8	3.9	4.7	4.1	5.2	4.5	3.8	3.5
Gross fixed capital form., LTL mn, nom.	15,589	19,270	18,934	21,913	9,408	10,523	.	.	.
annual change in % (real)	1.9	20.7	-3.6	12.8	9.3	9.8	9.0	8.0	9.0
Gross industrial production (sales)									
annual change in % (real)	6.4	6.4	3.7	3.4	7.9	-2.3	2.0	6.0	7.0
Gross agricultural production									
annual change in % (real)	-7.2	10.3	14.2	-1.6	.	.	.	.	.
Construction industry									
annual change in % (real)	-7.3	22.1	-7.3	11.5	2.8	23.1	.	.	.
Employed persons, LFS, th, average ³⁾	1,344	1,371	1,276	1,293	1,282	1,302	1,308	1,320	1,328
annual change in %	-5.1	2.0	1.8	1.3	1.1	1.6	1.2	0.9	0.6
Unemployed persons, LFS, th, average ³⁾	291	249	197	173	182	174	170	157	144
Unemployment rate, LFS, in %, average ³⁾	17.8	15.4	13.4	11.8	12.4	11.8	11.5	10.6	9.8
Reg. unemployment rate, in %, end of period ³⁾⁴⁾	14.4	11.0	11.4	11.1	10.2	8.6	.	.	.
Average monthly gross wages, LTL ⁵⁾	1,988	2,046	2,124	2,232	2,243	2,336	.	.	.
annual change in % (real, gross)	-4.6	-1.2	0.7	4.0	2.8	4.0	.	.	.
Average monthly net wages, LTL ⁵⁾	1,552	1,595	1,651	1,730	1,738	1,818	.	.	.
annual change in % (real, net)	-4.3	-1.3	0.5	3.8	2.5	4.4	.	.	.
Consumer prices (HICP), % p.a.	1.2	4.1	3.2	1.2	1.8	0.3	0.3	1.2	1.8
Producer prices in industry, % p.a.	10.3	13.9	5.0	-2.4	-1.4	-4.0	.	.	.
General govern.budget, EU-def., % of GDP									
Revenues	35.0	33.2	32.7	32.2	.	.	32.0	31.5	31.4
Expenditures	42.3	38.7	36.1	34.4	.	.	34.0	33.3	33.2
Net lending (+) / net borrowing (-)	-7.2	-5.5	-3.3	-2.2	.	.	-2.0	-1.8	-1.8
Public debt, EU-def., % of GDP	37.8	38.3	40.5	39.4	.	.	40.8	39.8	39.0
Central bank policy rate, % p.a., end of period ⁶⁾	1.07	1.24	0.52	0.27	0.38	0.26	.	.	.
Current account, EUR mn ⁷⁾	-92	-1,202	-396	549	142	263	400	-150	-200
Current account, % of GDP	-0.3	-3.9	-1.2	1.6	1.8	1.7	1.1	-0.4	-0.5
Exports of goods, BOP, EUR mn ⁷⁾	14,891	19,422	22,427	23,998	11,611	11,187	23,600	25,200	27,000
annual change in %	34.7	30.4	15.5	7.0	15.7	-3.7	-1.7	6.8	7.1
Imports of goods, BOP, EUR mn ⁷⁾	16,539	21,487	23,530	24,918	11,857	11,882	24,700	26,700	28,800
annual change in %	35.3	29.9	9.5	5.9	9.0	0.2	-0.9	8.1	7.9
Exports of services, BOP, EUR mn ⁷⁾	3,423	4,033	4,793	5,390	2,523	2,826	5,500	5,800	6,300
annual change in %	16.7	17.8	18.8	12.5	10.6	12.0	2.0	5.5	8.6
Imports of services, BOP, EUR mn ⁷⁾	2,301	2,766	3,404	4,033	1,881	2,074	4,200	4,500	5,000
annual change in %	3.7	20.2	23.1	18.5	23.2	10.2	4.1	7.1	11.1
FDI inflow (liabilities), EUR mn ⁷⁾	653	1,095	454	537	185	-534	200	.	.
FDI outflow (assets), EUR mn ⁷⁾	46	94	215	213	149	95	150	.	.
Gross reserves of NB excl. gold, EUR mn	4,788	6,120	6,203	5,705	5,431	6,009	.	.	.
Gross external debt, EUR mn ⁷⁾	24,015	25,041	25,921	24,358	24,857	24,821	.	.	.
Gross external debt, % of GDP	86.7	80.9	78.7	70.3	71.8	69.3	.	.	.
Average exchange rate LTL/EUR	3.4528	3.4528	3.4528	3.4528	3.4528	3.4528	3.45	3.45	3.45
Purchasing power parity LTL/EUR	2.0416	2.0842	2.0816	2.1173	.	.	.	.	.

1) Preliminary. - 2) According to census March 2011. - 3) From 2012 according to census March 2011. - 4) In % of working age population. - 5) Annual data including earnings of sole proprietors. - 6) VILIBOR one-month interbank offered rate (Lithuania has a currency board). - 7) BOP 6th edition.

Source: wiiw Databases incorporating Eurostat and national statistics. Forecasts by wiiw.