

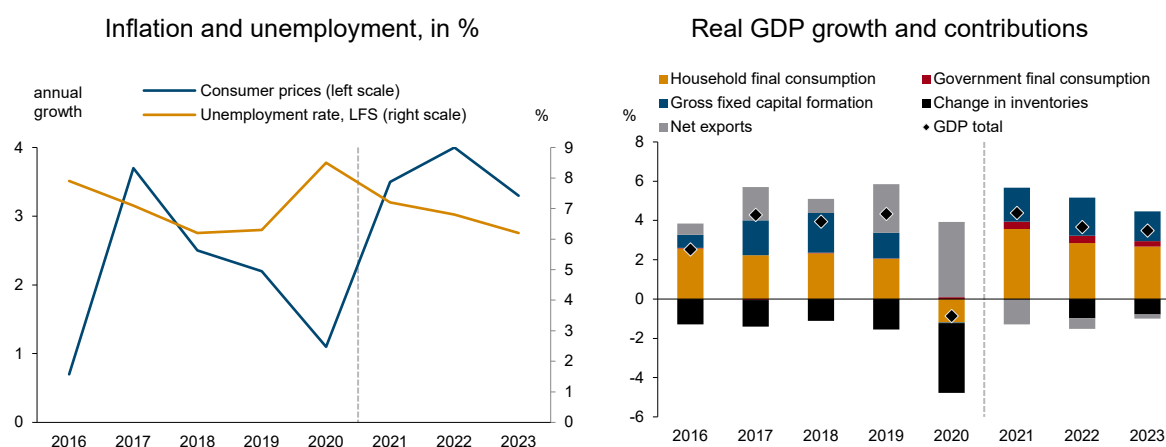


LITHUANIA: After the storm, the prospects are bright

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The Lithuanian economy recovered strongly in Q2 2021. Better-than-expected export performance and swiftly rebounding household consumption were coupled with an upswing in capital investment and a substantial accumulation of stocks. Sharply rising infection statistics may force the government to reintroduce stricter containment measures, but we do not expect that to choke off the ongoing revival. The government is continuing to deliver substantial fiscal stimuli, and the public investments announced will support recovery over the next two years. For 2021, we expect real GDP to grow by 4.4%, followed by a strong, steady increase of 3.7% in 2022 and 3.5% in 2023.

Figure 4.12 / Lithuania: Main macroeconomic indicators



Source: wiiw Annual Database incorporating national and Eurostat statistics, own calculation. Forecasts by wiiw.

With COVID-19 infections and related deaths rising rapidly in Lithuania, the government was forced to reintroduce restrictions in mid-September – however, these largely affect only unvaccinated persons. At the beginning of October, the European Centre for Disease Prevention and Control ranked Lithuania second highest on its list of countries by epidemiological risk. In particular, the maximum capacity of intensive care may be reached by late autumn. The number of beds for COVID-19 patients has increased; however, skilled personnel are in short supply. Thus, even harsher lockdown measures may need to be reintroduced. At the same time, Lithuania is one of the most successful EU-CEE countries in terms of its vaccination programme: by the beginning of October, close to 60% of the total population had been fully vaccinated.

Compared to other EU countries, goods exports did not fall much last year (-1.6% in nominal terms); nevertheless, the first half of 2021 saw a substantial hike of 21.7%. In a few product categories with a high share of value added of Lithuanian origin, the growth rates were substantial: pharmaceuticals, plastics, chemical and refined petroleum products, metals and furniture. Like exports, total industrial production also rebounded strongly: from January to August 2021, real growth attained almost 17% year on year. At the same time, capacity utilisation reached an all-time high in the Lithuanian economy. Goods imports have picked up even more strongly, as businesses have sought to replenish their depleted stocks. Trade in services has likewise bounced back: exports attained a level last seen in 2019, and the service account surplus amounts to almost 10% of GDP. With the slump in domestic demand, the current account surplus jumped to an unprecedented 8% of GDP last year; this year and in 2022, we expect the surplus to remain at above 2% of GDP.

In September 2021, the Lithuanian government started to build a fence along its eastern border with Belarus, in order to keep refugees from entering the country. Following economic sanctions by the EU against the government of Belarus and the country's enterprises, migration has increased substantially: whereas in the previous four years, only about 100 individuals (or even fewer) had crossed the Belarus-Lithuania border in search of asylum annually, in the first half of 2021 over 4,000 refugees, mainly from Iraq, arrived via that route. The Lithuanian government has asked the EU to revise its migration policy and legalise the pushback of migrants; such action has already been taken by Lithuanian forces and has been criticised by EU and NGO observers. Erection of the fence along the 670 km border is due to be completed by September 2022. The EU sanctions against Belarus (particularly on its potash products) affect Lithuania's transport sector, especially its railways and ports. The estimated economic loss may attain about 0.5% of GDP annually.

Following quite a slight decline in 2020 overall, investment activity has revived strongly this year. Business is again spending heavily on machinery, equipment and vehicles. Looking ahead, we expect a sharp increase in overall investment, as the public sector in particular acts as an engine of growth. Investment by households in real estate is again increasing this year, according to the latest figures on dwelling construction and building permits. House prices are continuing to grow and were not even depressed in 2020. After a slump in Q2 2020, new mortgage loans have also continued to rise. Since incomes are rising steadily, the robust demand for real estate is likely to continue.

The government's substantial fiscal support initiatives are expected to result in a budget deficit of 6.2% in 2021, down from 7.4% in 2020. The measures cover wage subsidies for affected firms, additional public investment, loan guarantees and support for the health sector and agriculture. At the beginning of 2021, during the second lockdown, more than 10% of Lithuanian employees were supported by short-time work measures (as in the first lockdown of March-May 2020). In the medium term, the Lithuanian government has ample resources available to invest in the recovery and restructuring of the economy. As in the previous planning period (2014-2020), the annual inflow of EU funds (including from the Next Generation EU recovery package) in 2021-2027 will amount to about 4% of Lithuanian GDP. About a third of the funds are earmarked for agriculture and fisheries, and about 20% for climate-related projects. There is a further focus on digital transformation, health, science and innovation, education and social issues. The biggest single investment project is Rail Baltica, the high-speed rail service linking the capital of Estonia (Tallinn) with Latvia, Lithuania and Poland. The main construction work on the railway line will take place in 2022-2026. More than 80% of the cost is covered by EU capital.

In many sectors, employment in Q2 2021 already surpassed the pre-crisis levels of 2019. This is particularly the case in business services and manufacturing. The job losses sustained in hospitality services, domestic trade and agriculture will persist for some time yet (though jobs in construction are growing again). We expect the growth in total employment that has already begun this year to gain momentum in 2022. The increase in vacancies in the business sector indicates that demand for skilled labour is even higher today than it was in pre-crisis Lithuania. The unemployment rate has already declined and is likely to drop to 7.2% in 2021 on average. We expect this rate to fall to 6.2% in 2022. Net migration into Lithuania remains positive; however, more is needed to compensate for the adverse natural demographic trend and to provide workers for the growing economy.

Following a remarkable rise of 6.6% in January 2021, the government is planning another massive hike in the minimum wage in 2022 – of more than 13%, to EUR 730 a month. Taken together, these measures will deliver a huge impetus to overall income growth that – alongside a tighter labour market – will result in wages increasing by about 10% this year and in 2022. Last year household consumption declined markedly only during the first lockdown. The release of last year's pent-up demand resulted in private consumption increasing by more than 13% in real terms in Q2 2021. Consumer surveys show household confidence to be robust in early autumn 2021. Over 2021 as a whole, we expect a rise in consumer demand of 6%; and in the coming two years we anticipate a high propensity for households to spend their rapidly growing income.

Due to the upsurge in international energy costs, consumer prices picked up strongly this year and will attain 3.5% in 2021. The substantial growth in wages will further push inflation upwards to 4% next year. Thereafter, in 2023, we expect price rises to slow to 3.3% per year.

Since our previous interim report in the summer, the faster recovery has allowed us to improve our GDP forecast for 2021 to 4.4%. And in 2022, we expect the strong recovery to continue at 3.7%. In terms of both external and domestic demand, growth in Q2 2021 picked up much faster than anticipated. Exports have increased substantially this year; however, imports have revived even more rapidly, as entrepreneurs ran down their stocks in 2020. Public investment has picked up strongly in 2021, and that will continue in coming years. Sharply rising household incomes – pushed upwards by increases in the minimum wage – will help private consumption to grow steadily again. Thus, we expect GDP growth to be 4.4% in 2021 and 3.7% in 2022, and to continue in 2023 at a rapid 3.5%.

Table 4.12 / Lithuania: Selected economic indicators

	2018	2019	2020 ¹⁾	2020 January-June	2021	2021 Forecast	2022 Forecast	2023
Population, th pers., average	2,802	2,794	2,795	2,801	2,794	2,780	2,770	2,760
Gross domestic product, EUR m, nom.	45,491	48,809	48,930	22,799	25,052	52,900	57,000	60,900
annual change in % (real)	3.9	4.3	-0.9	-1.2	4.7	4.4	3.7	3.5
GDP/capita (EUR at PPP)	24,640	26,040	25,880	.	.	.	.	.
Consumption of households, EUR m, nom.	27,903	29,445	29,105	13,743	15,002	.	.	.
annual change in % (real)	3.8	3.3	-2.0	-4.1	7.0	6.0	4.8	4.5
Gross fixed capital form., EUR m, nom.	9,531	10,429	10,585	4,620	5,483	.	.	.
annual change in % (real)	10.0	6.2	-0.2	-4.6	14.8	8.0	9.0	7.0
Gross industrial production (sales)								
annual change in % (real)	4.8	3.4	-1.8	-4.7	17.0	14.5	7.0	4.0
Gross agricultural production								
annual change in % (real)	-10.0	10.1	10.6	.	.	.	.	.
Construction industry								
annual change in % (real)	13.8	8.4	-1.6	-1.8	1.8	.	.	.
Employed persons, LFS, th, average	1,375	1,378	1,358	1,369	1,356	1,350	1,360	1,360
annual change in %	1.5	0.3	-1.5	-0.7	-0.9	-0.5	0.5	0.4
Unemployed persons, LFS, th, average	90	92	126	116	109	105	99	90
Unemployment rate, LFS, in %, average	6.2	6.3	8.5	7.9	7.5	7.2	6.8	6.2
Reg. unemployment rate, in %, eop ²⁾	8.9	8.7	16.1	12.1	12.9	.	.	.
Average monthly gross wages, EUR ³⁾	924	1,296	1,429	1,379	1,530	1,630	1,860	2,050
annual change in % (real, gross)	7.1	6.4	8.3	7.2	11.0	10.0	10.0	6.5
Average monthly net wages, EUR ³⁾	720	822	913	878	974	1,040	1,190	1,310
annual change in % (real, net)	6.2	11.6	9.3	7.5	10.9	10.0	10.0	6.5
Consumer prices (HICP), % p.a.	2.5	2.2	1.1	1.5	2.0	3.5	4.0	3.3
Producer prices in industry, % p.a.	5.6	0.0	-9.0	-8.8	4.2	6.0	3.0	4.0
General governm.budget, EU-def., % of GDP								
Revenues	34.5	35.1	36.0	.	.	35.0	34.8	35.0
Expenditures	33.8	34.6	43.4	.	.	41.2	38.8	37.5
Net lending (+) / net borrowing (-)	0.6	0.5	-7.4	.	.	-6.2	-4.0	-2.5
General gov.gross debt, EU def., % of GDP	33.7	35.9	47.1	.	.	49.0	49.0	48.0
Stock of loans of non-fin.private sector, % p.a.	6.0	3.3	-1.8	0.0	3.1	.	.	.
Non-performing loans (NPL), in %, eop	2.4	1.6	1.3	.	.	.	.	.
Central bank policy rate, % p.a., eop ⁴⁾	0.00	0.00	0.00	0.00	0.00	.	.	.
Current account, EUR m	132	1,702	3,633	1,639	603	1,300	1,200	1,200
Current account, % of GDP	0.3	3.5	7.4	7.2	2.4	2.5	2.1	2.0
Exports of goods, BOP, EUR m	24,552	25,954	25,536	11,721	14,301	29,200	31,000	32,500
annual change in %	7.9	5.7	-1.6	-6.9	22.0	14.4	6.2	4.8
Imports of goods, BOP, EUR m	27,398	28,303	25,938	12,067	15,490	31,300	33,900	36,000
annual change in %	10.4	3.3	-8.4	-13.8	28.4	20.7	8.3	6.2
Exports of services, BOP, EUR m	9,678	11,822	10,853	5,242	5,941	11,600	12,900	14,600
annual change in %	15.9	22.2	-8.2	-5.8	13.3	6.9	11.2	13.2
Imports of services, BOP, EUR m	6,003	6,902	5,854	2,857	3,341	6,400	7,300	8,400
annual change in %	12.9	15.0	-15.2	-12.9	16.9	9.3	14.1	15.1
FDI liabilities, EUR m	1,096	3,060	3,979	2,849	131	100	.	.
FDI assets, EUR m	866	1,921	3,438	2,797	-49	200	.	.
Gross reserves of CB excl. gold, EUR m	4,831	4,273	3,662	3,934	4,244	.	.	.
Gross external debt, EUR m	35,619	34,266	37,457	35,601	38,731	38,600	39,900	40,800
Gross external debt, % of GDP	78.3	70.2	76.6	72.8	73.2	73.0	70.0	67.0

1) Preliminary. - 2) In % of working age population. - 3) Including earnings of sole proprietors. From 2019 income tax reform and transfer of the employer's social security contribution (28.9%) to employees; real growth in 2019 estimated by wiiw. - 4) Official refinancing operation rate for euro area (ECB).

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