



Economic Outlook for Lithuania

10 February 2011

Global economic growth has decelerated with the weakening impact of the short-term factors, such as phasing out impact of fiscal measures and inventory cycle. Slower growth is observed in many developed countries, where the economic development is unfavourably affected by the adverse situation in labour markets and debt problems. In some emerging economies, the economic development is also losing momentum. **Nonetheless, favourable changes in economic activity are observed in several larger foreign trade partners of Lithuania.** Economic activity, supported by foreign demand, has recently increased in Estonia and Latvia, whereas situation in Poland and Germany remains favourable.

The rising demand in foreign countries has a favourable effect on the indicators of the tradable sector of Lithuania, first of all, industry and transport activity. The value added created in industry and transport activity has been growing for several consecutive quarters, whereas production expectations of enterprises remain optimistic. At the same time, domestic demand-based activities are just stabilising or starting to grow slowly. Such economic developments basically support earlier expectations; therefore, the economic growth forecasts for the forecast horizon have not been altered much. It is expected that in 2011 and 2012 the real GDP will rise by 3.3 per cent and 4.1 per cent, respectively, after 1.3 per cent growth in 2010.

Good foreign trade results of Lithuania are also related to favourable external environment. Real export of goods and services has already reached the previous peak recorded in 2008. The export of all main product groups has been growing markedly. The export of goods both to the EU and to the CIS countries has been growing strongly. It is expected that the real export grew by 17.0 per cent in 2010. In the coming years, the export of Lithuania should continue growing, albeit at a slower rate.

Fairly rapid import growth confirmed earlier forecasts. The import growth was supported by the continued rise in demand for intermediate products used in industrial production. The import of such products is closely related to the export dynamics. In addition, the import of capital goods has also been growing for some time already, which is related to the recovery of domestic investment in Lithuania. It is foreseen that the real import of goods and services rose by 16.9 per cent in 2010, whereas the import growth in the coming years will be slower.

The assessment of domestic demand shows that gross fixed capital formation rose earlier than expected, whereas the private consumption development was in line with previous assessment. Investment grew in the public sector, where investment in infrastructure and means of production rose. Private sector investment still remains more sluggish. Nonetheless, it is expected that it will start recovering in this sector as well. The need for these investments has been reflected for some time already by the rising level of production capacity utilisation. At present, it is expected that, following the investment stabilisation in 2010, in 2011 and 2012 it will grow by 14.4 per cent and 9.7 per cent, respectively.

Private consumption remains subdued and its recovery is hindered by the still complex situation in the labour market and reserved future expectations that encourage saving. Therefore, private consumption forecasts have been altered only slightly. It is expected that, following the fall by 4.2 per cent in 2010, in 2011 and 2012 it will rise by 3.1 per cent and 4.4 per cent, respectively.

Labour market indicators broadly support earlier forecasts. As expected, unemployment peaked in the second quarter of 2010, whereas in the third quarter it declined already, partially owing to seasonal factors. It is anticipated that over the forecast period the level of unemployment will decline gradually, in line with the rise of economic activity. However, the situation in the labour market will depend on the ability of the unemployed to meet market needs, their determination to change qualification and geographical mobility.

The annual inflation in 2010 confirmed the Bank of Lithuania forecast. The annual inflation in Lithuania accelerated almost since the beginning of the year and in the end of the year it was noticeably higher than in the EU and in euro area. In the course of the year, inflation in Lithuania was essentially determined by higher than a year ago prices of food, fuel and administered prices. As domestic demand remained subdued, there was no upward pressure for the prices of industrial goods and market services; however, it may emerge later due to the acceleration of the economic recovery. In the short run, the prices of food and energy resources, however, may continue rising. It is

expected that inflation will be 2.8 per cent in 2011 and 3.4 per cent in 2012.

ECONOMIC OUTLOOK FOR LITHUANIA IN 2010–2012

	February 2011 projection			November 2010 projection		
	2010*	2011*	2012*	2010*	2011*	2012*
Price and Cost Developments (annual percentage changes)						
Average annual inflation (based on HICP)	1.2	2.8	3.4	1.2	2.3	-
GDP deflator	1.3	2.9	3.0	1.2	1.2	-
Wages (compensation per employee)	1.4	1.9	4.7	-0.2	1.8	-
Import deflator	9.6	6.0	4.5	8.7	4.4	-
Export deflator	10.3	6.3	4.3	9.7	5.0	-
Economic Activity (constant prices; annual percentage changes)						
Gross Domestic Product**	1.3	3.3	4.1	0.5	3.1	-
Private consumption expenditure	-4.2	3.1	4.4	-5.7	1.9	-
General government consumption expenditure	-3.1	-1.5	2.5	-0.7	-0.2	-
Gross fixed capital formation	0.1	14.4	9.7	-5.3	13.9	-
Exports of goods and services	17.0	11.6	4.1	13.6	5.2	-
Imports of goods and services	16.9	12.6	5.0	15.3	6.8	-
Labour Market						
Unemployment rate (annual average as a percentage of labour force)	17.8	16.2	13.9	17.9	16.5	-
Employment (annual percentage changes)	-5.4	1.6	2.4	-5.7	1.2	-
External Sector (as a percentage of GDP)						
Balance of goods and services	-1.0	-1.9	-2.8	-1.7	-3.0	-
Current account balance	2.0	1.0	0.1	2.1	0.2	-
Current and capital account balance	4.4	3.4	2.4	5.1	3.2	-

* Projection.

** Changes in inventories are not included in GDP components.