



Economic Outlook for Lithuania

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In Lithuania, economic development has been losing momentum. Such economic development is basically in line with previous outlook assessments, thus the projections for the development of real GDP remain basically unchanged: real GDP is projected to grow by 3.0 per cent in 2012 and by 3.4 per cent in 2013. Economists from international and other institutions in the meantime project that global economic development is likely to recover in the projected period, yet uncertainty surrounding it has been quite high. The situation in the euro area, whose economy is close to a second recession, is particularly complicated. The countries in the region have to address problems related to huge general government and private sector debt, financial sector losses and the need to strengthen capital. To address the euro area financial problems, in mid-2012 it was agreed to lay the foundations for a banking union in the euro area. Further solutions, especially regarding the development of a fiscal union, will probably not be taken shortly, and structural changes in the economy will take time, thus the sustainable economic development in the euro area remains hardly to be expected in the near future.

Weaker external demand has been taking its toll on foreign trade. Growth in Lithuanian producers' exports has been decelerating: apart from mineral products, whose export growth had been impacted for some time by a suspension of operations of the oil refinery, trading in other key industries' output in foreign markets has been losing momentum, too. Moreover, growth in re-export volumes has been decelerating – mainly on account of a base effect related to intensified trading in vehicles a year ago. It is projected that external demand will grow less in the quarters to come, thus export growth in Lithuania may decline more; it is likely to recover only next year, if global economic development is more dynamic.

Growth in private consumption has been uneven. Following a rather significant rebound in consumption last year and early this year, consumption growth has now been much weaker. It is affected by volatile consumer confidence and expectations for the economic situation: while the change in these indicators was insignificant in the last few quarters, they are worse than a year ago. This stems from uncertainty surrounding the global economic situation and just a slow and unsteady recovery in Lithuania's labour market. When the level of confidence and expectations is below the average of these indicators for over a decade, real private consumption growth is likely to be quite sluggish during the projected period: 4.2 per cent in 2012 and 2.8 per cent in 2013.

Cautious assessment of the outlook has been affecting investment. Investment has been rising substantially, yet the major contribution to its developments comes from EU funds-supported investment in infrastructure – road building and reconstruction, and building of other engineering constructions. There is a great degree of volatility in investment in machinery and equipment, from strong growth in the second half of 2010 and the first half of 2011, a stop afterwards, a rebound again in late 2011, to stabilisation this year. Investment in vehicles has been contracting quite significantly, impacted by uncertainty surrounding global economic development. Uneven and lethargic development of investment is expected during the projected period, too. Investment is projected to increase by 4.5 per cent this year, down substantially from the figure in 2011 and from the average since the beginning of data collection. It is expected to grow by 7.6% in 2013.

Employment growth has been cautious as well. An increase in employment has been somewhat more pronounced in the tradable sector, notably manufacturing. There are, however, economic activities with the employment declining, for instance, accommodation and catering services, education, administration and support services. Prudent business development is reflected in the application of flexible labour forms – newly hired staff work mainly part-time. Wage policy is also cautious. Though average wages have been rising for some time already, nearly a third of the increase accounts for irregular payments, such as bonuses. This is observed notably in the private sector, where the share of irregular payments in total wages is now larger than before the economic downturn. Assessment of the outlook for the country's economic development will post a significant contribution to the development of the labour market and to investment in output growth alike. Amid moderate

business confidence and expectations, the labour market situation is likely to improve moderately. Employment is projected to increase by 1.4 per cent in 2012 and by 1.5 per cent in 2013.

Annual inflation has been declining recently, reflecting external factors. A fall in global prices led to weaker food price growth in Lithuania; its contribution to inflation has declined substantially compared with mid-2011, when it was the highest in several years. Nevertheless, it is food prices along with administered prices whose contribution to inflation is the highest. The contribution of fuel prices has waned, yet their contribution along with the contribution of other external factors to inflation may be greater in the projected period as is currently expected: lower harvest is projected in some important grain growing regions, the outlook for oil price developments is uncertain. The domestic situation-related core inflation is low and is not likely to pick up significantly amid still quite difficult labour market situation and relatively low wage growth. Inflation is projected to be 2.9 per cent in 2012 and 2.4 per cent in 2013.

Outlook of Lithuania's Economy in 2012-2013

	August 2012 projection			May 2012 projection		
	2011	2012*	2013*	2011	2012*	2013*
Price and Cost Developments (annual percentage changes)						
Average annual inflation (based on HICP)	4.1	2.9	2.4	4.1	2.9	2.7
GDP deflator	5.3	3.2	2.4	5.3	3.2	2.6
Wages (compensation per employee)	4.0	3.1	2.9	4.0	2.3	2.6
Import deflator	12.8	4.4	1.8	12.8	5.4	1.9
Export deflator	11.7	3.9	1.9	11.7	5.7	2.0
Economic Activity (constant prices; annual percentage changes)						
Gross domestic product**	5.9	3.0	3.4	5.9	3.0	3.5
Private consumption expenditure	6.1	4.2	2.8	6.1	4.6	3.1
General government consumption expenditure	0.2	0.7	1.9	0.2	0.6	1.9
Gross fixed capital formation	17.1	4.5	7.6	17.1	5.0	8.0
Exports of goods and services	14.1	4.4	6.5	14.1	5.3	5.8
Imports of goods and services	12.9	5.3	7.2	12.9	7.1	6.3
Labour Market						
Unemployment rate (annual average as a percentage of labour force)	15.4	13.4	11.9	15.4	13.7	12.2
Employment (annual percentage changes)	2.0	1.4	1.5	2.0	1.1	1.4
External Sector (as a percentage of GDP)						
Balance of goods and services	-1.3	-2.3	-3.0	-1.3	-2.8	-3.1
Current account balance	-1.6	-3.1	-3.5	-1.6	-3.0	-3.3
Current and capital account balance	0.9	-1.1	-1.9	0.9	-1.0	-1.6

* Projection.

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