



## Economic Outlook for Lithuania

11 February 2010

**In the second half of 2009, the economy of Lithuania stabilised. After the growth in the third quarter, the seasonally and working day adjusted real GDP remained broadly unchanged in the fourth quarter.** The recent positive changes in the tradable sector are partly related to the economic stimulus programmes in various countries and the prevailing optimism related to the started global economic recovery. More favourable trends have not been observed yet in the non-tradable sector, which depends on the domestic demand changes. For example, the retail trade data for the fourth quarter showed the ongoing recession, which allows predicting that household consumption is still falling.

**Compared to November, the general assessment of the domestic economy improved, taking into consideration better prospects for the global economy, a more rapid than forecasted recovery of the exports and a more favourable country risk assessment in international financial markets.** At the end of the previous year, a more rapid than expected economic recovery was observed in the US and China, the main world economies, whereas in the United Kingdom the end of recession was announced on the basis of preliminary results for the fourth quarter 2009. It is projected that the recovery of foreign demand will establish conditions for the further growth of the Lithuanian exports. Due to improved situation in the global financial markets and the stabilisation of the Baltic economies, the risk assessment for this region became more moderate. Better economic conditions enable to expect that crediting in individual economic activities will be more pronounced this year.

**It is forecasted that the GDP of Lithuania will increase by 0.5 per cent in 2010 and by 3.4 per cent in 2011.** According to the baseline projection scenario, the real GDP will start growing faster in the second half of 2010. Net exports will remain the main factor behind the economic growth, although their positive impact on the GDP will be subdued by a rise in the imports of energy products after the closure of the Ignalina Nuclear Power Plant, particularly at the beginning of the year. It is projected that real exports will grow by as much as 9.3 per cent this year, but a part of this growth will be determined by the base effect – a rapid fall of exports in the first half of 2009. Export results improved significantly in the second half of the previous year. At the end of 2009, investments declined more than expected in November forecasts, but they should recover faster in 2010, taking into consideration slightly better prospects for the loan portfolio changes and the planned more intensive utilisation of the EU support. Still, it is projected that both general government expenditure and private consumption expenditure will continue to fall this year.

**Taking into consideration a more favourable assessment of the economic development, it is projected that the unemployment rate will increase to 16.7 per cent in 2010 (slightly less than expected in the previous quarter) and decline to 15.5 per cent in 2011.** The unemployment rate increased and the number of vacancies decreased in the third quarter of 2009, however, these changes were much more subdued than in the first half of the year. This allows expecting a stabilisation of the unemployment rate already in the first quarters of 2010, i.e. earlier than expected in forecasts of autumn 2009. However, wages will continue to decrease. Owing to administrative decisions, the decline of wages in the public sector in 2010 should be faster than in the private sector, which started adapting to the changes in economic conditions earlier.

**The average inflation in 2009 (4.2%) was only slightly higher than the forecast of the Bank of Lithuania, which remained unchanged since May last year. It is forecasted that the inflation will be respectively 0.4 per cent and 1.6 per cent in 2010 and in 2011.** Compared to a moderate deflation forecasted for 2010 in November, the forecasts were increased mostly due to the changes in the global commodity prices. In the last quarter of 2009, food and oil prices in

international markets were already higher than a year ago. The prevailing expectations of the global economic recovery should prevent their fall. In Lithuania, the growth of prices in 2011 will be slackened by slowly rising wages and restrained recovery of domestic demand.

#### ECONOMIC OUTLOOK FOR LITHUANIA IN 2010–2011

	February 2010 projection			November 2009 projection		
	2009*	2010*	2011*	2009*	2010*	2011*
<b>Price and Cost Developments (annual percentage changes)</b>						
Average annual inflation (based on HICP)	4.2	0.4	1.6	3.9	-0.8	-
GDP deflator	-2.1	0.1	1.9	-2.0	-2.3	-
Wages (compensation per employee)	-7.2	-6.1	1.7	-5.7	-6.2	-
Import deflator	-9.9	5.3	3.8	-11.8	3.2	-
Export deflator	-13.9	3.8	3.2	-11.9	4.0	-
<b>Economic Activity (constant prices; annual percentage changes)</b>						
Gross Domestic Product**	-15.0	0.5	3.4	-15.2	-1.5	-
Private consumption expenditure	-15.6	-5.2	2.3	-15.1	-1.6	-
General government consumption expenditure	-1.3	-6.4	-1.6	-2.4	-7.4	-
Gross fixed capital formation	-39.3	-0.6	12.3	-38.4	-0.5	-
Exports of goods and services	-14.7	9.3	4.1	-18.9	4.4	-
Imports of goods and services	-29.5	5.3	3.9	-30.1	3.0	-
<b>Labour Market</b>						
Unemployment rate (as a percentage of labour force)	13.8	16.7	15.5	13.9	17.7	-
Employment (annual percentage changes)	-7.1	-4.4	0.8	-7.2	-5.4	-
<b>External Sector (as a percentage of GDP)</b>						
Balance of goods and services	-1.6	-0.3	-0.6	-1.4	-0.3	-
Current account balance	1.5	1.6	0.7	0.0	0.6	-
Current and capital account balance	7.9	6.7	4.9	4.7	5.1	-

\* Projection.

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