



Economic Outlook for Lithuania

6 May 2010

Compared to the February forecast, the assessment of the economic development of Lithuania remained broadly unchanged: real GDP is expected to increase by 0.5 per cent in 2010 and by 3.1 per cent in 2011. As for the quarterly changes of GDP, after marginal increase in the second half of 2009, the economy of Lithuania shrank in the first quarter of 2010. However, it was in line with the expectations taking into consideration negative effect of the closure of Ignalina nuclear power plant on the economy. The economy is anticipated to get on a more sustainable growth path from the second quarter. Although the projection of GDP growth in 2010 was not changed, it is worth noting that downside risks to this scenario have emerged recently. Economic activity might be more subdued due to lower than expected private consumption and tensions in financial markets related to the stance of public finances in Greece and some other countries.

Tradable sector is still expected to be the main factor behind the economic recovery – real exports should increase by 7.1 and 4.2 per cent in 2010 and 2011, respectively. Over the first half of 2009, real exports stood at the levels of 2005-2006, the lowest over the current decline; however, it started to increase in subsequent quarters. Optimism stems from still improving outlook for the main trading partners in the European Union and for Russia. Changes in the market shares of Lithuania in the main export regions also allow expecting favourable trends of exports: after a slump in the first half of 2009, market shares increased and reached or even exceeded the level of 2007-2008.

As in the previous projections, domestic demand is expected to dampen the economic recovery. Over the current year, private consumption should contract by 7.9 per cent as the growth of household expenditure will be impeded by a high unemployment, continued decrease in wages and still tight lending conditions. Recovery of consumption is projected only for the next year when the situation in the labour market and consumer expectations improve. The investment level will stabilise in the second half of 2010 and will grow at relatively rapid pace (11.6 per cent) in 2011, however, barely reaching the level of 2005.

Compared to February, almost the same level of unemployment is projected: 17.1 per cent in 2010 and 15.9 per cent in 2011. The unemployment rate may go up due to the intensified registration of the unemployed in the Labour Exchange in the second quarter of 2010, following the widespread information about compulsory health insurance contributions that must be paid by the unregistered unemployed. However, it is still projected that the unemployment level will stabilise around the middle of the year and start to diminish gradually in subsequent quarters.

In the fourth quarter of last year, the decrease in compensation per employee was more pronounced than projected in February; therefore, a slightly stronger decline of this indicator is projected for 2010. Although wages should stabilise in the middle of the year, their annual decline will remain significant due to previous decreases. This year, unlike the previous years, a stronger impact will be exerted by wage reductions in the public sector. Compensation per employee will increase marginally, i.e. by 2.9 per cent, only in 2011.

Compared to February, inflation projections remained broadly the same: consumer prices are expected to increase by 0.4 and 1.7 per cent in 2010 and 2011, respectively. Price increases in Lithuania will be mainly determined by growing prices of energy and food in global markets. In the first quarter of this year, global oil price in litas was around 60 per cent higher than a year ago while food price was higher by one fifth. Improving expectations for the global economic recovery prevent from stronger fall of commodity prices in the near future. Downward pressure on headline inflation will stem from the price changes of market services and industrial goods that mostly depend on domestic demand. Apart from sharp rise in electricity prices after the closure of Ignalina nuclear power plant, administered prices are expected to remain relatively

stable as no other administrative decisions which could have a major influence are taken to date. However, administered prices might increase along with stronger than projected growth of energy prices.

ECONOMIC OUTLOOK FOR LITHUANIA IN 2010–2011

	May 2010 projection			February 2010 projection		
	2009	2010*	2011*	2009*	2010*	2011*
Price and Cost Developments (annual percentage changes)						
Average annual inflation (based on HICP)	4.2	0.4	1.7	4.2	0.4	1.6
GDP deflator	-2.9	1.0	1.8	-2.1	0.1	1.9
Wages (compensation per employee)	-8.3	-7.8	2.9	-7.2	-6.1	1.7
Import deflator	-10.2	8.4	3.8	-9.9	5.3	3.8
Export deflator	-13.7	4.7	3.1	-13.9	3.8	3.2
Economic Activity (constant prices; annual percentage changes)						
Gross Domestic Product**	-14.8	0.5	3.1	-15.0	0.5	3.4
Private consumption expenditure	-16.8	-7.9	2.3	-15.6	-5.2	2.3
General government consumption expenditure	-1.2	-2.1	0.9	-1.3	-6.4	-1.6
Gross fixed capital formation	-39.1	-1.7	11.6	-39.3	-0.6	12.3
Exports of goods and services	-14.3	7.1	4.2	-14.7	9.3	4.1
Imports of goods and services	-29.4	2.4	4.2	-29.5	5.3	3.9
Labour Market						
Unemployment rate (annual average as a percentage of labour force)	13.7	17.1	15.9	13.8	16.7	15.5
Employment (annual percentage changes)	-6.9	-4.6	0.9	-7.1	-4.4	0.8
External Sector (as a percentage of GDP)						
Balance of goods and services	-0.7	-0.6	-1.0	-1.6	-0.3	-0.6
Current account balance	3.8	1.5	-0.6	1.5	1.6	0.7
Current and capital account balance	7.2	5.2	2.9	7.9	6.7	4.9

* Projection.

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