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# Economic Outlook for Lithuania

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**The economy of Lithuania exhibits steady growth and is broadly in line with earlier assessments.** Therefore the real GDP outlook in the projected period does not change: growth is expected to be at 2.8 per cent in 2013, and at 3.5 per cent in 2014. **Export still exerts a strong influence on economic expansion.** Although the impact of a good harvest of the previous year, which significantly increased export at the end of 2012 and the beginning of 2013, has already waned, now economic expansion is positively affected by much larger than a year ago production of petroleum products — last year it has been halted due to the overhaul of the oil refinery. Export, excluding petroleum products, as was expected, is growing less than before due to a rather unfavourable external environment. Nevertheless export growth is not decelerating as much as was expected, therefore the projections for this year and the coming year have been revised upwards. Although the total export volume is increasing much more than could be expected from the foreign demand, it is still anticipated to grow slower and be more in line with projected foreign demand developments.

**Recovering domestic demand, especially the larger than expected private consumption, also significantly contributes to economic growth.** In the nearest future, once the effect of short-term export-stimulating factors disappears, domestic demand should become an important factor of economic growth. Private consumption is increased by growing disposable income, while the latter is influenced by both higher wages (related to, inter alia, increased minimum wage) and increased employment. However, the growth in employment recently has been encouraged mainly by the smaller tradable sector, while in the non-tradable sector, which makes up the larger part of the economy, the number of employed grew little, dropping in some activities of this sector. Therefore, total employment is growing rather moderately, and this, along with value added growing faster than employment, leads to quite large increases in productivity. Higher productivity is related to the rather small growth in unit labour costs after the rise of the minimum wage. This shows that the increase in minimum wage has so far had a limited effect on prices, thus barely inhibiting the expansion of domestic demand.

**Investment increased as well.** Unlike in the previous several quarters, investments related to production capacity increased — more was invested in machinery and equipment. Although the need for such investments is felt, it is unclear whether such investments will continue to rise — only the expectations of retail trade enterprises are improving, while assessment of the external environment remains broadly unchanged. Investment in transport equipment has increased markedly, too. Such investments, which already for some time have had a great influence on total investment growth, can be explained by a temporary factor, not related to the demand for transport services — more stringent environmental regulations will enter into force next year, due to which the prices of vehicles required for transportation will increase. This encourages carriers to hurry to purchase vehicles before they are subject to more stringent regulations. Once companies have the means of transport, such investments should not grow. The overall change in investments should be significantly influenced by state investments. There is less investment in infrastructure objects — civil and engineering structures — than last year; however, these investments should grow if expenditure for such objects would increase as much as planned in the State Investment Programme.

**The trends, which are favourable to consumers, in unit labour costs and global commodity prices result in much lower inflation.** Not only the current global prices of commodities are favourable, but also their projections. The Food and Agriculture Organization of the United Nations has announced that this year global grain harvest will be exceptionally large. The situation is completely different than in 2012, when the harvest in some major grain-growing countries was weak due to poor weather conditions. The drop in oil prices in 2013 and 2014, compared to 2012, is indicated by both market expectations, visible from futures prices, and the projections of international and other institutions. The risk of geopolitical unrest in the Middle East and Northern Africa could lead to different oil prices than are currently projected. Nevertheless, the possibility of the formation of upward pressure on global commodity prices in the nearest future is small, and this leads to the diminished risk that the prices of food and energy in Lithuania will rise significantly. Inflation in recent months was smaller than expected, and such data, along with the expected favourable internal and external factors — limited unit labour cost growth and the optimistic commodity price developments, motivates a significant downward revision of the inflation projection. In 2013, inflation is expected to amount to 1.4 per cent, and in 2014 —

1.5 per cent. Although the newest data has a downward effect on the 2014 projections, their effect is suppressed by several approved tax changes, such as the increased excise duties on tobacco and alcohol that will come into effect in spring of 2014.

**Outlook of Lithuania's economy in 2013–2014**

| | August 2013 forecast | | | May 2013 forecast | | |
|---|---|---|---|---|---|---|
| | 2012 | 2013* | 2014* | 2012 | 2013* | 2014* |
| **Price and cost developments (annual percentage changes)** | | | | | | |
| Average annual inflation (based on HICP) | 3.2 | 1.4 | 1.5 | 3.2 | 2.0 | 2.4 |
| GDP deflator | 2.8 | 1.2 | 2.5 | 2.8 | 2.2 | 2.9 |
| Wages (compensation per employee) | 3.4 | 4.1 | 3.2 | 3.2 | 4.1 | 3.3 |
| Import deflator | 4.2 | –1.2 | 0.3 | 4.2 | 2.0 | 1.7 |
| Export deflator | 3.5 | –1.0 | 0.6 | 3.5 | 1.8 | 1.5 |
| **Economic activity (constant prices; annual percentage changes)** | | | | | | |
| Gross domestic product** | 3.7 | 2.8 | 3.5 | 3.7 | 2.8 | 3.5 |
| Private consumption expenditure | 4.3 | 2.9 | 3.3 | 4.3 | 2.5 | 3.2 |
| General government consumption expenditure | 0.4 | 1.6 | 2.1 | 0.4 | 1.2 | 2.4 |
| Gross fixed capital formation | –2.5 | 4.0 | 6.4 | –2.5 | 2.6 | 6.2 |
| Exports of goods and services | 11.9 | 7.1 | 6.3 | 11.9 | 5.8 | 5.9 |
| Imports of goods and services | 6.6 | 7.5 | 7.0 | 6.6 | 5.9 | 6.3 |
| **Labour market** | | | | | | |
| Unemployment rate (annual average as a percentage of labour force) | 13.2 | 11.6 | 10.3 | 13.2 | 11.6 | 10.1 |
| Employment (annual percentage change) | 1.8 | 1.3 | 1.4 | 1.8 | 1.4 | 1.7 |
| **External sector (as a percentage of GDP)** | | | | | | |
| Balance of goods and services | 0.6 | 0.5 | 0.0 | 0.7 | 0.1 | –0.3 |
| Current account balance | –0.5 | –0.1 | –0.6 | –0.4 | –1.8 | –2.1 |
| Current and capital account balance | 1.7 | 1.7 | 1.1 | 1.8 | –0.1 | –0.5 |

* Projection.

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