Economic Development Scenario 2024–2027

June 2024

The Economic Development Scenario (hereinafter – the scenario) has been developed[1] after assessment of the data of National Accounts for the first quarter of 2024 and other statistical data published by 31 May 2024, taking into account the measures provided for in the Republic of Lithuania Law on the Approval of Financial Indicators of the State Budget and Municipal Budgets for 2024 (hereinafter – the 2024 budget) as well as changes in the external environment and monetary policy that occurred after the scenario was published by the Ministry of Finance in March 2024 and other information. The scenario assumptions on external environment and energy (oil and natural gas) prices are in line with the European Commission's[2] (EC) Economic Forecast published in May this year.

The EC Economic Forecast published in May 2024 projects the European Union's (EU) gross domestic product (GDP) to grow 1% in 2024, and in 2025 the growth rate will accelerate up to 1.6%. The EC foresees that after economic stagnation in 2023, at the beginning of 2024 with the economy growing faster than expected and inflation continuing to decline, economic activity will gradually increase over the forecast period. Uncertainty and downside risks to the economic outlook have continued to increase in recent months, largely due to russia's protracted war of aggression against Ukraine and the conflict in the Middle East. Wider geopolitical tensions also continue to pose a threat. The outlook is increasingly negatively affected by climate change-related risks.

At the beginning of 2024, Lithuania's economy experienced growth – in the first quarter of this year, Lithuania's GDP was 2.9% higher compared to the corresponding period in 2023. Economic development was driven by positive net exports (5.2 percentage points to foster economic development) and household consumption, which recovered at the end of 2023 and strengthened at the beginning of 2024 (leading to a 1.5 percentage points in GDP development).

According to the GDP production method data, only one economic activity experienced a contraction in the first quarter of 2024 compared to the corresponding quarter of 2023. Ranking the activities according to their positive impact, the largest contribution to the growth of gross value added (GVA) was made by: (1) a nearly tenth increase in construction (0.6 percentage point contribution to the change in GVA), (2) a tenth increase in information and communication activities (0.6 percentage point contribution), (3) a 5.2% increase in professional, scientific, technical, administrative and support services (0.5 percentage point contribution) and (4) a 1.0% increase in wholesale and retail trade and transport and storage services (0.3 percentage point contribution). Industrial activities, which had a significant negative impact on the economic contraction in 2023, showed moderate but positive growth in the created GVA at the beginning of this year (0.4% growth, 0.1 percentage point impact on the GVA). Its improved performance was strongly influenced by

[1] The date of inclusion of statistical data to the scenario – 31 May 2024, and other information – by 6 June 2024, inclusive.
[2] EC Spring 2024 Forecast: [Spring 2024 Economic Forecast: A gradual expansion amid high geopolitical risks - European Commission (europa.eu)]

manufacturing, which showed signs of recovery (its GVA grew by 1.2%), for which the latest production data confirmed an improving trend – in April, after a long break, no group of manufacturing activities experienced a contraction. Economic growth was moderately dampened by the contraction of the created GVA in financial and insurance activities (decreased by 4.0% but resulted only in –0.1 percentage points of the change in the GVA).

After a slight contraction last year, with stronger domestic and external demand in 2024, Lithuania's GDP growth is expected to reach 2.1% this year, while in 2025-2027, the GDP growth rate could accelerate to 2.9% per year on average.

The labour market situation remained relatively good in the first quarter of 2024. While the unemployment rate increased to 8.2%, the number of employed population increased by 2.8%, and the number of the labour force increased significantly by 3.3%. These statistics suggest that favourable developments in labour demand and supply continued in the first quarter. Net migration remained positive and contributed significantly to the growth of labour supply. Like last year, positive net migration was determined by the rapid immigration of foreign nationals from third countries, which was determined by the ongoing war in Ukraine and the favourable state of the Lithuanian labour market, characterised by strong labour demand. Another important indicator, the labour force participation rate, increased rapidly over the year (by 1.1 percentage points for the 15-64 age group) and shows that a higher labour market participation of the working-age population contributed to an increase in labour supply. Increased labour supply allowed to fill part of the vacancies, which led to a significant increase in the number of employed population in the country. Employment growth was mainly driven by the private sector, especially in administration and servicing, manufacturing, information and communication, accommodation and food activities. The persistence of a relatively high job vacancy rate in the country (1.9%) indicates that, while employment growth has been strong, not all participants entering the labour market have matched its skills needs, leading to a slight increase in unemployment as well. As economic activity recovers, the number of employed population is expected to increase by 1.4% in 2024 due to continued strong labour demand and increased labour supply. The unemployment rate, calculated according to the methodology of the population employment survey, will increase to 7.2% this year due to rapidly growing labour supply. The economic development scenario is based on Eurostat's latest[3] demographic projections (the baseline scenario[4]). They foresee that as of 2025, due to negative natural population replacement and less favourable net migration, the working-age population in Lithuania will start to decrease, therefore, there will be little space for labour force and employed population growth. Against this background, the number of employed population is expected to start decreasing from 2026 onwards, dropping by 0.1% in 2026 and by 0.3% in 2027. Nevertheless, the expected high economic activity will gradually reduce the unemployment rate to close to 6% at the end of the medium term.

Wage growth has slowed down in the country but remains rather strong. Average gross monthly earnings grew by 10.3% in the first quarter of 2024 – by 0.8 percentage points slower than at the end

[3] The date of publication is June 2023.
[4] For 2024, the employment projections have been adjusted to take into account favourable statistics on the development of net migration in the first months of this year.

of 2023 and 3 percentage points slower than in the first quarter of 2023. Trends across sectors have remained the same: in the public sector, wage growth was higher than in the private sector, 12.7% and 9.3% respectively. The growth rate of wages in the private sector slowed for the fifth consecutive quarter. Although wage growth slowed down in the country, it significantly outpaced price growth. Real wages in January-March were 8.9% higher compared to January-March 2023. Wage growth in the country was driven by a persistent shortage of suitably qualified workers, an increase in the minimum monthly wage (MMW), which has increased by 10% since January 2024 to EUR 924, and increases in salaries for teachers, doctors, nurses, residents, cultural and artistic workers, statutory officials and social workers provided for in the State and municipal budgets for 2024. However, in a context of continued economic uncertainty and reduced financial possibilities for businesses to increase wages rapidly – data for the first quarter of 2024 shows that the share of compensation of employees in GDP reached 54.3%, was historically the highest in Lithuania and above the EU average (47.4%) – wage growth is slowing down in the country. In addition, wage pressures in certain sectors are mitigated by an increase in the labour force. As a result, average gross monthly earnings are expected to grow at a more moderate rate of 9.5% in 2024 as compared to 2023 (12.6% increase). In the following medium-term years, in the absence of new decisions by economic policy makers affecting wage developments in the country, and without a significant change in the financial situation of the business, the average gross monthly wage in the country could grow by 6.4% annually in 2025 and 2026, and by 5.5% in 2027.

In the first months of this year, annual inflation in Lithuania remained low. Calculated on the basis of the Harmonised Index of Consumer Prices, it fell to 0.4% in March and April. According to preliminary data, annual inflation rose to 0.8% in May. Although this increase was due to the expiry of the refund period for value added tax on heating energy, some monthly increases in the prices of certain food products and some services, annual inflation remained one of the lowest in the last three years. In the first five months of this year, the low inflation rate in the country was supported by favourable developments in energy, food and non-energy industrial goods prices, while services inflation remained broadly stable. While some downward pressure was exerted by the high comparable base, especially in the case of energy deflation, the relatively weak monthly developments in inflation also contributed to low inflation, reflecting the easing of inflationary pressures. In the first four months of this year, energy commodity inflation remained double-digit negative (on average 12.7%) and contributed most to low headline inflation. The deflation of energy commodities was driven by favourable energy commodity prices in the markets, a high comparable base, and a reduction in administered prices (especially for gas) for household consumers. Food price developments have also dampened headline inflation. The annual fall in food prices in April was observed for the fourth month in a row. Food deflation, although less pronounced than in the case of energy, was widespread in almost all food categories and reflected lower prices for both processed and unprocessed food. While prices for non-energy industrial goods remained higher than a year ago, inflationary pressures in this product group also declined significantly. The rapid disinflation of these goods shows that shipping disruptions in the Red Sea have not yet had a tangible impact on consumer prices, while the prevailing price deflation of Chinese producers has also had a favourable effect on the development of these import prices. Average annual inflation is expected to fall to 1.1% in 2024. Lower inflation is mainly due to a more favourable evolution of food prices for consumers and reduced pressure on the prices of non-energy industrial goods. Some changes in administered prices will also have a dampening impact on inflation, with a further reduction in the public price of electricity for households from July onwards. In the outer years of the medium term, inflation is expected to remain close to 2%. Uncertainty about the course and consequences of the war in Ukraine and geopolitical tensions in the Middle East, as well as the evolution of energy prices, will remain key risk factors for inflation over the medium term.

The strengthening of the purchasing power of the population and improved consumer expectations stimulated the consumption of the population at the beginning of the year. Household consumption expenditure in January-March 2024 was 2.5% higher than a year ago. According to retail trade turnover data, the turnover of both food (5.5%) and non-food goods (2.2%) grew in the first quarter of 2024 (2.8%). The increase in retail turnover recorded in April (3.4%) indicates a further increase in spending on consumer goods. This year, the increase in household consumption expenditure is driven by the improving financial situation of the population, low inflation and better consumer sentiment. Although the amount of household funds held in deposits is increasing, however at a significantly slower pace compared to last year, and because of the stronger purchasing power of the population, the possibilities to purchase more of the desired goods and services are increasing, even if part of the income is allocated to saving. Deposit statistics show that the financial reserve accumulated by the population amounted to EUR 22.8 billion in April 2024, which was lower only compared to the record results of December 2023 (EUR 22.9 billion in December). Deposits increased steadily on a monthly basis between February and April this year. There was an increase both in the amount of overnight deposits that can be drawn immediately and with agreed maturity. The increasing income allows for not only increasing savings but also increasing consumption. The disposable income of the population will grow this year not only due to higher employment income, but also due to increased social benefits. In addition, the tax-free allowance is increasing this year. Revenue growth will significantly exceed price developments (estimated inflation rate of 1.1% this year). As a result of these factors, household consumption expenditure is expected to grow by 3.3% in 2024. In the following medium-term years (2025-2027), as the financial situation of the population continues to improve, household consumption expenditure could also grow above 3% annually.

Investment contracted slightly at the beginning of 2024. Expenditure on gross fixed capital formation (GFCF) was 0.3% lower in January-March 2024 compared to January-March 2023. The GFCF components developed differently. The lack of a suitably skilled workforce has maintained the need to invest in increasing labour productivity. Investment expenditure on intellectual property products (9.4 %) and other machinery, equipment and weapon systems (7.4 %) grew the fastest out of GFCF components in the first quarter. Investments in other machinery, equipment and weapon systems were the component that contributed most positively (1.6 percentage points) to the GFCF change. Investment in construction projects (housing and other buildings and structures) also contributed positively to the development of investment in the country and grew by 2.6% in the first quarter. The implementation of projects financed by EU funds is likely to have contributed to the positive result of investments in other buildings and structures. In other areas, however, the results were weaker. Investment in transport equipment in the country fell by a quarter, while expenditure on information and communication technologies fell by 21.4%. Data on investment in fixed tangible assets also show an ambiguous situation. Many economic activities recorded a contraction in the first quarter of 2024. Nevertheless, investment in tangible fixed assets by enterprises in manufacturing, one of the main investing activities in Lithuania, grew by 4.5%. In addition, recent data suggest that, after a sluggish start of the year, the performance of manufacturing firms improved and output growth accelerated to 7.2% in April 2024, which could encourage firms in this economic activity to invest. The investment process in the country will be supported by the changes in the ECB's monetary policy that started in June 2024, with lower interest rates (although they are still at high levels), so although the investment process will be more moderate this year, the annual change in GFCF is expected to be positive. GFCF expenditure could grow by 3.5% in 2024. In the following medium-term years (2025-2027), the growth rate of GFCF expenditure could accelerate (5.4%) as the financial situation of enterprises improves, external and domestic demand grows faster, there is a need to increase national security, energy efficiency and invest in green technologies and measures to increase labour productivity.

Lithuania's exports of goods and services, which fell last year, returned to growth in the first months of 2024. According to the data of National Accounts, this indicator (at constant prices) grew by 0.6% per year in the first quarter of 2024. This result was driven by the rapid growth of exports of services (at constant prices), which amounted to 12% per year. Exports of goods (at constant prices) decreased by 4.6% per year in this period. The biggest negative impact on the export of goods was caused by the decline in the re-export of goods, which is significantly affected by geopolitical tensions and, since mid-2023, the Lithuanian Customs tightened the checks on dual-use goods, limiting the quantities of re-exported goods to the countries of the Commonwealth of Independent States. Data for the first quarter of 2024 shows that re-exports of goods were mostly negatively affected by declining re-exports of vehicles. In the first quarter of 2024, the contribution of exports of goods of Lithuanian origin to total exports of goods was negative, but much smaller than that of re-exports of goods. The decrease in exports of miscellaneous manufactured articles (furniture), mineral products, textiles and plastic products contributed the most to the decrease in exports of goods of Lithuanian origin. On the other hand, the decline in exports of goods of Lithuanian origin was mitigated by the export of prepared foodstuffs and the recovery of chemical and engineering industry production.

The scenario projects an annual change in exports of goods and services (at constant prices) of 2.3% in 2024. The moderate recovery of this indicator compared to the decline recorded in 2023 will be determined by the low comparative base formed in the second half of last year and the favourable development of the economies of Lithuania's main export partners projected by the EC in 2024. The recovery in exports of goods of Lithuanian origin will be supported by the easing of monetary policy related to the reduction of interest rates. The downward trend in re-exports is likely to continue throughout the year, dampening the overall growth of the country's exports of goods. In the medium term, the recovery of export volumes of goods and services will be influenced by the development of the geopolitical situation and the resulting international trade risks, the flexibility of exporting companies to adapt to the changed market conditions, their decisions to invest in technological progress and productivity-enhancing measures. It is likely that the annual growth rate of this indicator could reach 4.2% between 2025 and 2027.

The scenario was drawn up in a context of exceptionally high external environmental instability and economic uncertainty, ongoing active military actions in Ukraine and other geopolitical tensions and changes in monetary policy.

Due to russia's ongoing war against Ukraine and the geopolitical turmoil in the Middle East at the beginning of October 2023, uncertainty about the development of prices of energy raw materials remains extremely high. In the scenario, the technical assumptions for prices of energy raw materials for 2024-2025 were based on the assumptions published by the European Commission on 15 May. The Brent oil price assumption makes up USD 85.4 /bar in 2024 and USD 80/bar in 2025. The natural gas price assumption is EUR 30.9/MWh in 2024, EUR 34.8/MWh in 2025. The technical assumption applied since 2026 is that the prices of these energy raw materials will remain stable. In case these technical assumptions change, the outlook for inflation development would change. The short and medium-term inflation estimates could also change due to other factors, including possible decisions in the area of administered prices and changes in monetary, fiscal and labour market policies.

The assumptions for the demographic development of the scenario were based on Eurostat's latest published demographic projections. Changes in demographic projections, international migration trends or labour force activity assumptions would change the outlook for labour market indicators.

The estimates of the indicators of export of goods and services presented in the scenario may change due to unrealised technical assumptions about external demand based on which this scenario was drafted and the decisions of third countries to apply restrictive trade measures for goods from Lithuania.

Increased needs for strengthening energy independence as a result of the adverse geopolitical situation, accelerated implementation of the European Green Deal projects could speed up the investment process in the country faster than foreseen in this scenario. Investment developments could also change due to other circumstances, among which also due to more active implementation of the RRF, EU-funded projects, increased investment in defence, changes in the monetary policy and developments in domestic and external demand.

In the event of changed population habits and behaviour, financial situation of households and purchasing power as well as demographic situation, the development of consumption expenditure of households would be different as foreseen in this scenario.

New decisions on minimum monthly wage, public sector workers' wages would affect the estimates of the average gross monthly earnings foreseen in this scenario. In the event of demand fluctuations, changes in the labour force, protracted high uncertainty and instable situation as well as changed financial situation of companies, wages in the private sector would also be affected.

The estimates of indicators presented in the scenario largely depend on relevant actual statistical data disposed during the time of drafting the scenario, which after the revisions and/or reviews by the State Data Agency change significantly lately. Also, the estimates foreseen in the scenario could change following the decisions made by the economic policy makers, for example, further easing of monetary policy, new decisions on defence spending and its financing.

If the underlying assumptions based on which this scenario was drawn up were not met, the estimates for most of the indicators in this scenario would change.

Key indicators of the economic development scenario

Title of the indicator	2023	2024P	2025P	2026P	2027P
GDP (at current prices), MEUR	71, 986	75, 559	79, 637	83, 927	88, 468
GDP (at constant prices), rate of change, %	–0.3	2.1 (1.6)	2.9 (2.9)	2.9 (2.9)	2.9 (2.9)
Harmonised consumer price index (average annual), rate of change, %	8.7	1.1 (1.9)	2.2 (2.2)	2.2 (2.2)	2.2 (2.2)
Investment (at constant prices), rate of change, %	10.6	3.5 (3.5)	5.4 (5.4)	5.4 (5.4)	5.4 (5.4)
Exports of goods and services (at constant prices), rate of change, %	–3.3	2.3 (3.5)	4.2 (5.2)	4.2 (5.2)	4.2 (5.2)
Unemployment rate (based on definition of the Labour Force Survey), %	6.8	7.2 (6.7)	6.9 (6.5)	6.6 (6.4)	6.3 (6.3)
Average monthly gross earnings, rate of change, %	12.6	9.5 (8.6)	6.4 (5.0)	6.4 (5.0)	5.5 (5.0)
Number of employed persons, rate of change, %	1.4	1.4 (0.5)	0.2 (–0.1)	–0.1 (–0.3)	–0.3 (–0.5)

Sources: Ministry of Finance, State Data Agency.

P – projection. An estimate of a relevant indicator of the Economic Development Scenario published in March 2024 is presented in brackets.