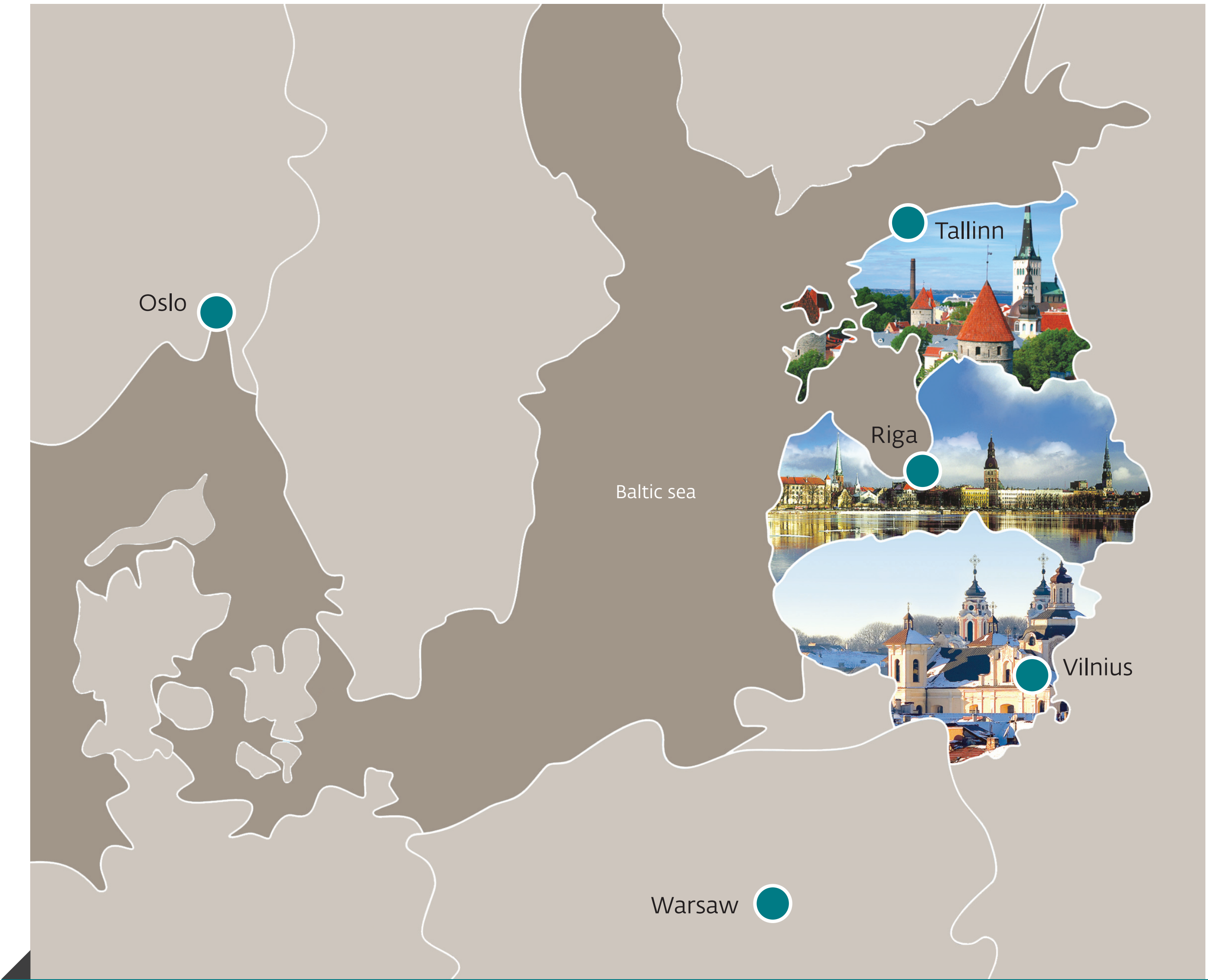


BALTIC ECONOMIC OUTLOOK

2011

DNB

FOREWORD

"Change is the only constant", as the saying goes. In order to succeed in these turbulent times, we have to stand tall and embrace the things that we cannot change – and have courage to change the things we can. Now the bank has a new name, DNB, which says loud and clear that we are a part of strong Norwegian financial group.

DNB has proven its commitment to the Baltic countries as the bank to do business with, through good times and bad. We are confident in our long-term strategy as we are confident in the Baltic economies – economies which have been hit hardest during the crisis, but have shown a remarkable ability to quickly straighten up and grow again.

However, in light of the current events in the European financial markets there is little room to relax. To defend their successes, all businesses must find additional resources to increase efficiency and maintain a clear, down-to-earth view on the economic environment. Therefore, I'm pleased to present the latest publication of the DNB research team on the three Baltic economies. It provides a clear macro-economic outlook, emphasizing these three economies' comparative strengths and shortfalls.

Let us bravely face the changes of the times and look for ways to succeed together.

Terje Turnes
Executive Vice President
DNB Baltic Division

BALTIC ECONOMIC OUTLOOK WAS PREPARED BY DNB BALTICS ECONOMIC RESEARCH TEAM:

Jekaterina Rojaka
Chief Economist
Tel.: +370 5 2393590, +370 612 73515, +370 685 47578
E-mail: jekaterina.rojaka@dnb.lt

Prof. Rimantas Rudzkis
Chief Analyst
Tel.: +370 5 2393402, +370 686 59638
E-mail: rimantas.rudzkis@dnb.lt

Vytautė Pilipauskaitė
Analyst
Tel.: +370 5 2393678, +370 612 73515
E-mail: vytaute.pilipauskaite@dnb.lt

Mindaugas Jurgelis
Analyst
Tel.: +370 5 2393369, +370 618 79964
E-mail: mindaugas.jurgelis@dnb.lt

Baltic Economic Outlook

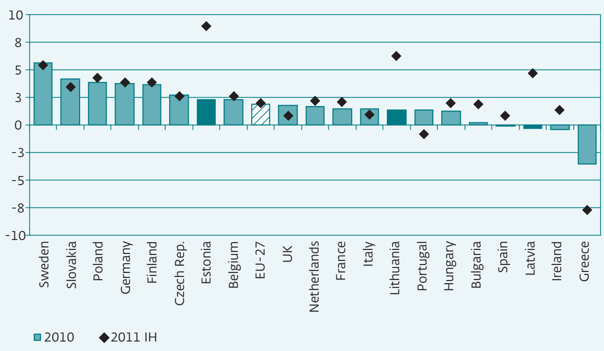
Table of contents

1. Macroeconomic overview ---------- 5
2. Lithuania ---------- 10
3. Latvia ---------- 15
4. Estonia ---------- 19
Annex ---------- 23
Comments ---------- 32

1. Macroeconomic overview

In 2009, the Baltic countries underwent the steepest economic downturn in the EU. Compared to the best pre-crisis result, GDP at constant prices shrank by 15% in Lithuania, 17% in Estonia and more than a fifth in Latvia that year. However, their economies began to recover in 2010 and this year the three countries together with Sweden have been among the EU leaders in terms of real GDP growth (Diagram 1.1). According to the latest projections of the European Commission, the Baltic trio will continue to play first violin in 2012–2013 as well.

Diagram 1.1
REAL GDP, ANNUAL CHANGE, %

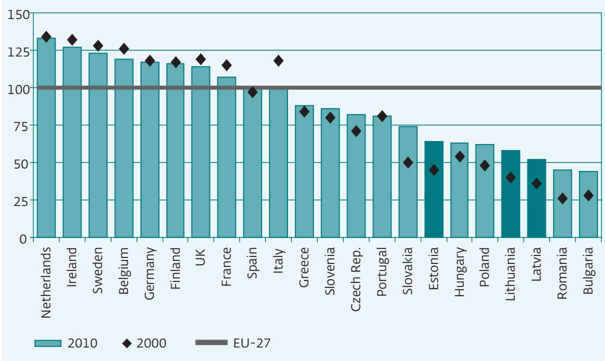


Source: Eurostat

THE BALTICS WILL NEED TO WORK HARD FOR MANY YEARS TO REACH THE AVERAGE OF THE EU ECONOMIES

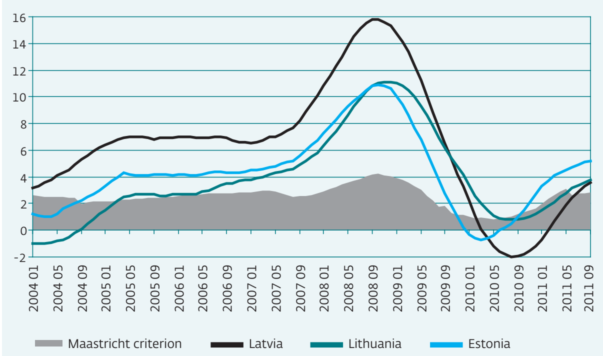
Lithuania, Latvia and Estonia grew strongly throughout the last decade and managed to bridge the gap considerably between their economies and the EU average. In 2010, GDP per capita made up 58%, 52% and 64% of the EU average respectively in terms of purchasing power (Diagram 1.2), while the same indicators were nearly 1.5 times lower in 2000. Because of the recent downturn, the convergence process came to a halt but has been gaining momentum this year. Nevertheless, catching up with the purchasing power of the old EU member states will require significant effort. Although the economies of the Baltic countries are much more dynamic than the economy of the EU as a whole, prices have also grown faster there (Diagram 1.3).

Diagram 1.2
GDP IN PPS PER CAPITA (EU-27 = 100), %



Source: Eurostat

Diagram 1.3
HICP, MOVING 12 MONTHS AVERAGE RATE OF CHANGE, %



Source: Eurostat

ESTONIA HAS BECOME THE UNDISPUTED LEADER AMONG THE BALTIC COUNTRIES

Average income in the countries concerned has remained at a level much lower than in Western Europe. As can be seen from Table 1.1, GDP per capita stood at EUR 8,000 in Latvia (a third of the EU average), Lithuania enjoyed a slightly higher indicator and the Estonian figure was almost EUR 11,000 in 2010. Estonia also had the healthiest public finance structure, a much higher level of accrued foreign direct investment (FDI), a higher average wage and the lowest unemployment rate. Its unique position was further highlighted by the country's accession to

Table 1.1
KEY MACROECONOMIC INDICATORS

	EU-27	Estonia	Latvia	Lithuania
Nominal GDP, EUR billion				
2009	11761.6	13.8	18.5	26.6
2010	12257.5	14.3	18.0	27.5
GDP per capita, EUR thousand				
2009	23.5	10.3	8.2	8.0
2010	24.4	10.7	8.0	8.4
GDP per capita in purchasing power standards, EUR thousand				
2009	23.5	15.0	12.2	12.9
2010	24.4	15.7	12.6	14.2
Real GDP, annual change, %				
2009	−4.3	−14.3	−17.7	−14.8
2010	1.9	2.3	−0.3	1.4
2011 I H	2.0	8.9	4.6	6.2
Inflation, HICP, e-o-p, annual change, %				
2009	1.5	−1.9	−1.4	1.2
2010	2.7	5.4	2.4	3.6
2011 Sep	3.3	5.4	4.5	4.7
Current account balance, ratio to GDP, %				
2009	−0.9	3.7	8.6	4.4
2010	−0.8	3.6	3.0	1.5
2011 I H	−1.1	−0.2	1.0	−2.1
Net average monthly earnings, e-o-p, EUR				
2009	:	634	456	477
2010	:	653	455	478
2011 I H	:	685	468	475
Harmonized unemployment rate, sa, e-o-p, %				
2009	9.5	16.2	20.1	16.0
2010	9.6	14.6	17.0	17.3
2011 I H	9.5	12.8	16.1	15.5
Average annual interest rate on new loans in national currency, e-o-p, %[1]				
2009	:	4.7	9.1	8.4
2010	:	4.6	7.4	5.5
2011 Sep	:	4.7	7.3	5.5
Loans granted to non-financial corporations and households, e-o-p, ratio to GDP, %				
2009	108.1[2]	104.0	98.1	66.6
2010	107.4[2]	96.0	94.0	59.3
Loans granted to non-financial corporations and households, annual change, %				
2009	−0.7[2]	−4.0	−5.9	−7.1
2010	1.9[2]	−4.6	−7.0	−7.9
2011 Sep	2.3[2]	−5.4	−7.6	−2.3
General government budget balance, ratio to GDP, %				
2009	−6.9	−2.0	−9.7	−9.5
2010	−6.6	0.2	−8.3	−7.0
2011 I H	−4.8	1.3	−0.7	−6.3
General government debt, ratio to GDP, %				
2009	74.7	7.2	36.7	29.4
2010	80.2	6.7	44.7	38.0
2011 I H	80.9	6.2	45.2	37.9
Foreign direct investment, e-o-p, per capita, EUR				
2009	:	8696	3557	2872
2010	:	9179	3636	3174
Gross country's external debt, e-o-p, ratio to GDP, %				
2009	:	124.7	156.5	87.0
2010	:	115.2	165.4	87.4

[1] For Estonia – estimated weighted average interest rates on loans for non-financial corporations and households; Latvia – arithmetical mean of long-term and short-term rates

[2] In euro area

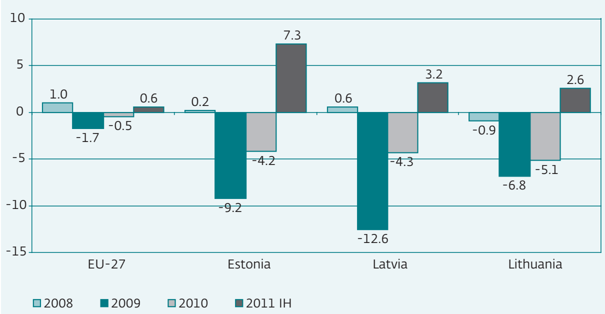
Source: Eurostat, national statistics offices, ministries of finance and central banks, IMF, ECB Data Warehouse

the OECD in late 2010 and the Eurozone in early 2011. Estonia became the clear leader among the Baltics mainly because of its superior public administration and strategic economic planning.

SLOW EARNINGS GROWTH AND HIGH UNEMPLOYMENT ADD TO EMIGRATION FROM LATVIA AND LITHUANIA

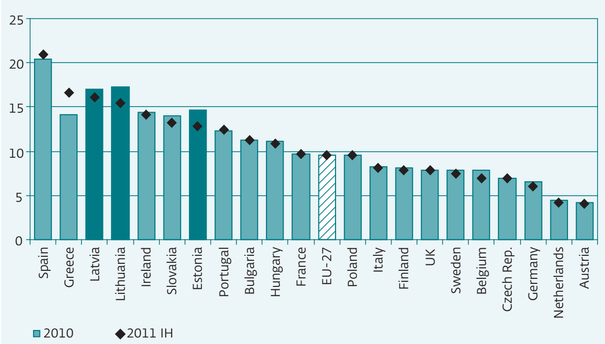
This year, faster economic growth has been accompanied by an increase in the number of employed people. In the second quarter, Lithuania and Latvia saw an increase of around 4% year-on-year, while the relevant Estonian figure went up by nearly 8% (Diagram 1.4). Nevertheless, the unemployment rate remained high (especially among young people) in the middle of the year in Estonia, while the rates in Lithuania and Latvia were higher than the indicators of all other EU member states with the exception of Spain (Diagram 1.5). Although the average cost of labour is much lower in the Baltic countries than in Western Europe and manufacturing began to recover, the growth of wages was modest last year and in the first half of this year due to high unemployment and could not fully offset the rising consumer prices. Therefore, it is not surprising that

Diagram 1.4
EMPLOYMENT, ANNUAL CHANGE, %



Source: Eurostat

Diagram 1.5
UNEMPLOYMENT RATE, SEASONALLY ADJUSTED, END OF PERIOD, %



Source: Eurostat

emigration strengthened in Lithuania and Latvia, while Estonia was the only country where it did not reach an ominous level.

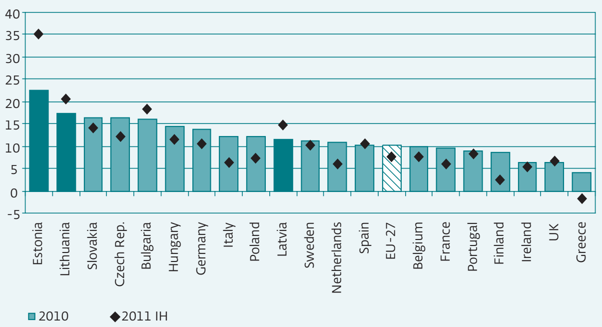
FOREIGN TRADE HAS ACCELERATED AND BALANCED OUT IN THE BALTIC COUNTRIES

Exports have been the driving force behind economic growth in all the countries concerned. Estonia was the top performer in the EU in terms of the annual increase in the export of goods and services (at constant prices), both last year and in the first half of this year. Lithuania was second and Latvia also had a double-digit growth rate (Diagram 1.6). Estonia was far ahead of the other two countries in terms of the volume of exports per capita. As can be seen from Diagram 1.7, the difference was extremely large in invisible exports; the Estonian indicator in 2010 was almost triple that of Lithuania. However, Lithuania had the best diversification of exports in the region as less than 60% of its exports of goods and services have gone to the EU this year while the percentage going to the CIS countries has risen. This suggests that the Lithuanian economy has better prospects given that the EU market is expected to remain stagnant. Compared to pre-crisis levels, foreign trade in the Baltics has become more balanced. Lithuania was the only country to have a small deficit last year, while the Estonian foreign trade balance remained positive in the first half of this year and the indicators for Latvia and Lithuania, although negative, were modest. All three countries enjoyed positive balances in their current accounts in 2010.

INVESTMENTS ARE UP IN 2011 BUT STILL WELL BELOW PRE-CRISIS LEVELS

Whether the strong economic growth seen this year across the Baltic region is sustainable will largely depend on the investment processes there and the health of their export markets. Sadly, the Eurozone has been caught up in the sovereign debt crisis and the weaker competitiveness of many EU countries and political disagreements suggest that there will be no quick fixes to the problem, which is worsening the expectations of businesses and households and slows investment across the EU. Moreover, the inevitable cuts to budget expenditure are putting pressure on domestic consumption and the EU market is unlikely to grow in the coming years. At the same time, growth in the Russian economy, which is also important for the three countries, has been slow despite the positive impact of high oil prices. Given these developments, any strong growth in the Baltic economies must be supported by more active investments and the recovery of the domestic market. Analysis of the GDP structure using the expenditure approach indicates that the level of tangible investments has

Diagram 1.6
EXPORTS OF GOODS AND SERVICES (VOLUMES), ANNUAL CHANGE, %



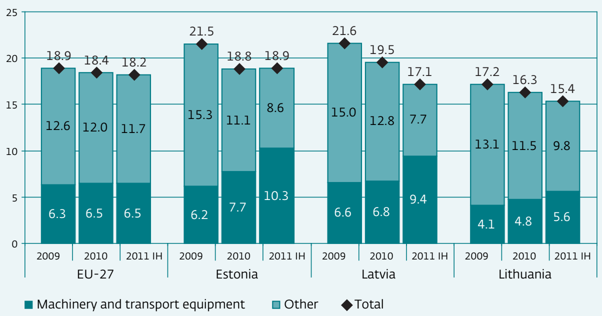
Source: Eurostat

Diagram 1.7
EXPORTS OF GOODS AND SERVICES (AT CURRENT PRICES), PER CAPITA, EUR THOU

* Annual estimate based on the data of the first half

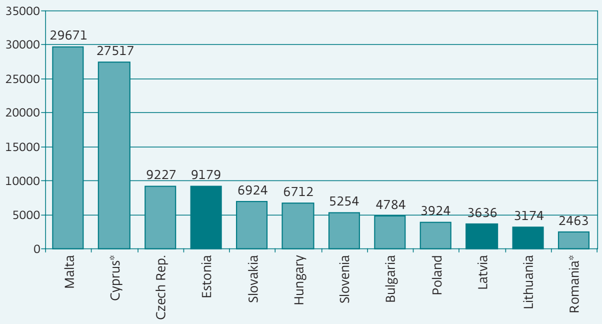
Source: Eurostat

Diagram 1.8
EXPENDITURE ON GROSS FIXED CAPITAL FORMATION, RATIO TO GDP, %



Source: Eurostat

Diagram 1.9
FOREIGN DIRECT INVESTMENT (OUTSTANDING AMOUNTS) PER CAPITA, END OF PERIOD, EUR



* Population on Jan 1, 2010

Source: Eurostat

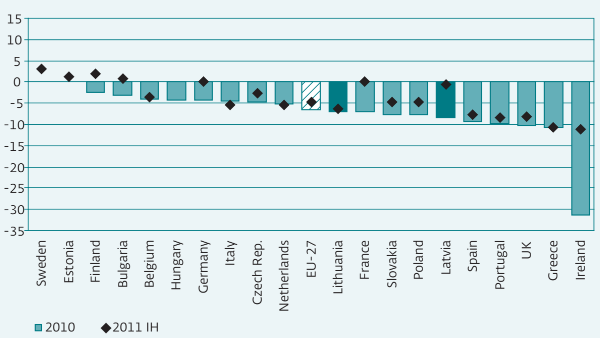
remained much lower in the countries concerned than before the crisis (Diagram 1.8). Lately, Lithuania has had a particularly low level of expenditure on gross fixed capital formation, and Diagram 1.9 indicates that the country lags behind Latvia and Estonia as well as the majority of the EU newcomers in terms of its accrued FDI per capita.

The low level of investment into capital goods can be explained by a fall in the profit margins of businesses and tighter bank lending policies. Diagram 1.9 shows that the contraction of the portfolio of loans granted to private companies which began in late 2008 has not yet fully stopped. Although banks have already relaxed their lending standards, businesspeople are reluctant to take risks because of the uncertain prospects of neighbouring markets. Incidentally, the debt level of Lithuanian companies and households is much lower than in the other two countries, which shows better growth potential for the Lithuanian economy.

CLEAR PROGRESS OF FISCAL DISCIPLINE IN LITHUANIA AND LATVIA DOES NOT ENSURE THE SUSTAINABILITY OF PUBLIC FINANCE

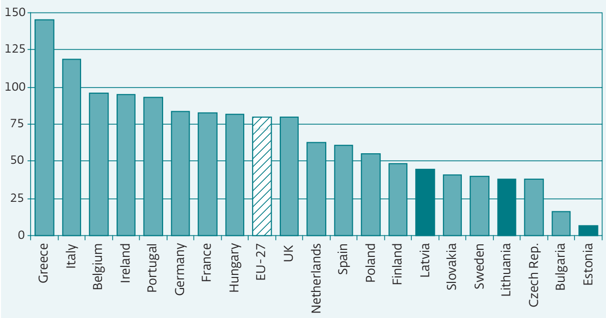
There was some concern over the sustainability of public finances in the Baltic countries at the outset of the global financial crisis. However, last year showed that the countries were able to tackle their budget problems with some degree of success. Although the ratio between fiscal deficits and GDP was quite high in Lithuania and Latvia in 2010, measurable progress has been made since 2009 and this ratio is expected to fall by around two more percentage points this year. Given the magnitude of the downturn in these countries, the Baltics must be applauded for their achievements in consolidating their public finances compared to other EU countries (Diagram 1.10). Moreover, all the three countries still have relatively low public debts (Diagram 1.11) despite a considerable increase in this indicator in Latvia and Lithuania in the last few years. Growing confidence in the Baltic states has also been reflected by the lower cost of insurance for their securities (Diagram 1.12) and upgrades to the sovereign credit ratings or outlook by all of the leading international rating agencies: *Moody's*, *Standard & Poor's* and *Fitch Ratings*. Estonia has the best rating and continues to impress. It was the only EU member state to have a balanced budget and tiny public debt last year. However, it is still too early to relax as regards Latvia and Lithuania. Both countries will have to borrow considerably in the coming years to refinance their previous obligations and cover their budget deficits, and international financial markets have been

Diagram 1.10
GENERAL GOVERNMENT BUDGET BALANCE, RATIO TO GDP, %



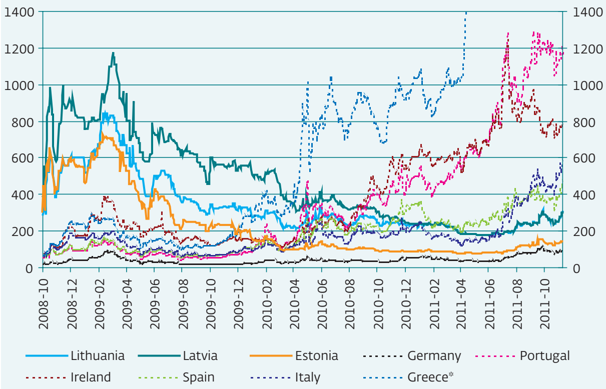
Source: Eurostat

Diagram 1.11
GENERAL GOVERNMENT DEBT, RATIO TO GDP, %



Source: Eurostat

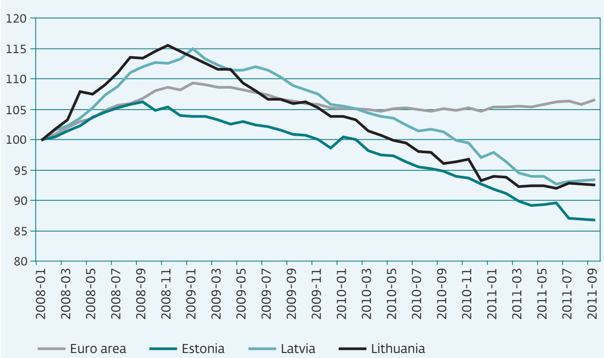
Diagram 1.12
5 YEAR CDS, BP



* Greece: Apr 18, 2011 – 1424.439 bp; Nov 16, 2011 – 5560.820 bp

Source: Reuters Ecowin

Diagram 1.13
OUTSTANDING AMOUNTS OF LOANS TO NON-FINANCIAL CORPORATIONS, END OF PERIOD, 2008-01 = 100%



Source: ECB

Table 1.2
PROJECTIONS OF THE MAIN MACROECONOMIC INDICATORS

	Lithuania			Latvia			Estonia		
	2011	2012	2013	2011	2012	2013	2011	2012	2013
Real GDP, annual change, %	6.0	2.5	3.0	5.0	2.5	3.0	7.5	3.0	5.0
Current account balance, % of GDP	−1.0	−2.0	−3.0	0.0	−2.0	−3.0	0.0	−1.0	−2.0
Inflation, HICP, eop, %	4.0	3.0	2.5	4.0	2.5	2.5	5.0	3.5	3.0
Net monthly earnings, annual change, eop, %	3.0	4.0	4.0	4.0	3.0	4.0	5.0	4.0	4.5
Harmonized unemployment rate, eop, %	14.0	12.0	10.0	15.0	13.0	11.0	10.0	9.0	7.0
General government deficit, % of GDP	−4.5	−3.5	−3.0	−4.0	−3.0	−3.0	0.5	−2.0	−1.0

Source: DNB

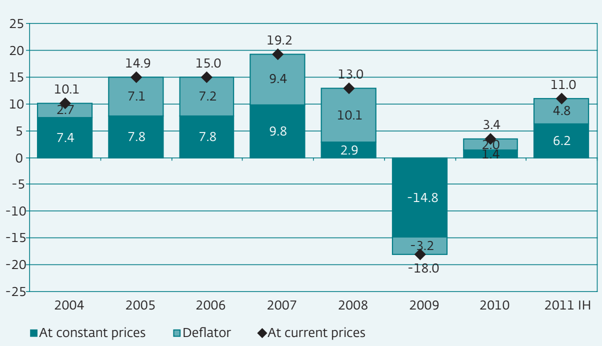
extremely nervous lately. The favourable treatment of these countries can change in an instant and the cost of borrowing may rocket if financial discipline begins to wane.

The immediate prospects for the Baltic countries appear quite bright even though the degree of uncertainty is very high as all the three countries are highly dependent on neighbouring markets, the outlook for which remains vague. If the EU manages to put the sovereign debt crisis under control, there is no doubt the Baltics will enjoy economic growth next year. Projections based on this scenario are presented in Table 1.2. Unfortunately, painful experience tells us that other options must also be considered as it is equally likely that European political leaders will fail to find consensus, preventing quick, radical decisions. In that case, the economy of the European Union may remain at a standstill for several years or even slide into double-dip recession and the Baltic countries will face serious difficulties.

2. Lithuania

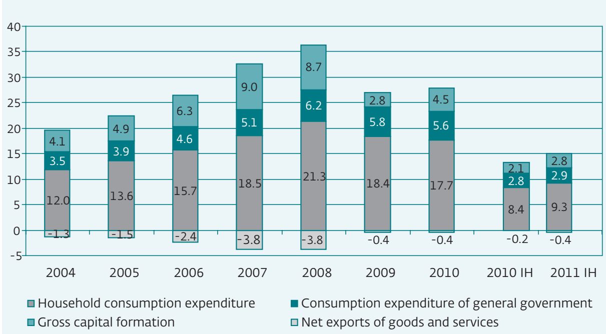
Last year, Lithuania had a positive overall growth indicator because of recovering exports as the latest estimates indicate that GDP at constant prices rose by 1.4%. GDP at current prices comprised EUR 27.5 billion and went up by 3.4% from 2009 as a significant portion of the nominal GDP growth was ensured by higher producer prices (Diagram 2.1). Due to Lithuania's shrinking population, the GDP share per capita increased by a larger margin of over 5% to EUR 8,400. According to Statistics Lithuania, last year's indicator measured in purchasing power standards increased by more than three percentage points to over 58% of the EU average. Judging from the preliminary data of the latest population census, this indicator is likely to be higher and will be raised once the population figures are officially revised downward. This year, Lithuania has enjoyed much stronger economic growth. Preliminary estimates indicate that real GDP rose by 6.4% year-on-year in the first three quarters of 2011.

Diagram 2.1
LITHUANIA'S GDP, ANNUAL CHANGE, %



Source: Eurostat

Diagram 2.2
LITHUANIA'S GDP COMPONENTS BY EXPENDITURE APPROACH, EUR BILLION



Source: Eurostat

Diagram 2.3
LITHUANIA'S FOREIGN TRADE, RATIO TO GDP, %

Source: Eurostat

LITHUANIA'S ECONOMY PROPELLED BY EXPORTS, THIS YEAR INVESTMENT CONTRIBUTES AS WELL

A comparison of the GDP structure before the crisis in 2007 and 2010 shows that the share of exports went up from 53.8% to 68.3% over three years, while the gross capital formation indicator declined from 31.2% to 16.4%. The percentages of other components changed by much smaller margins. Last year, both household and general government consumption slightly weakened, while the volumes of exports and imports increased considerably compared to 2009 (Diagram 2.2–3). Expenditure on gross capital formation also rose sharply as a result of the decline in stocks in 2009 rather than an increase in tangible investments. Meanwhile, the latter expenditure went up in the first quarter of this year because of the core capital component. All other GDP components were also on the rise. Unfortunately, deteriorating economic sentiments will not allow for the sustaining of a rapid growth of investment next year – it may be partially fed through assimilating record high EU structural fund support.

Recently, the manufacturing industry, which exports about 60% of its output, transport and domestic trade (especially wholesale) have been the main growth drivers of the Lithuanian economy. Last year, the manufacturing industry, domestic trade and transport industries generated about half of the national GDP on aggregate: 18.8%, 18.4% and 11.7%, respectively (Table A1), which is well above the EU average. The growth of all these sectors accelerated in the first half of this year. Even the construction industry, which contracted almost by half in 2009–2010, began to recover (see Table A2).

Last year, the volume of Lithuanian exports of goods and services rose by 17.4% at constant prices and exceeded the pre-crisis maximum. In the first half of this year, the growth rate was above 20%. In that period, visible and invisible monthly exports per capita made up almost EUR 500 and EUR 100 on average, which ranks 18th and 23rd among the EU-27, respectively. These indicators highlight Lithuania's weakness, which is the slender export of services (with the exception of transportation services, as their exports are relatively substantial). Nevertheless, Lithuania led the EU in terms of the annual growth of invisible exports in the first half of this year and was far ahead of all the remaining member states. Despite this surge in exports and a surplus balance of services, the total balance of foreign trade (in goods and services) remained negative in Lithuania, both last year and this year (Diagram 2.3–4). In contrast to the situation before the crisis, the foreign trade deficit was quite small, as was the current account deficit.

Diagram 2.4
LITHUANIA'S CURRENT ACCOUNT AND FOREIGN TRADE (GOODS AND SERVICES) BALANCES, RATIO TO GDP, %

Source: Eurostat

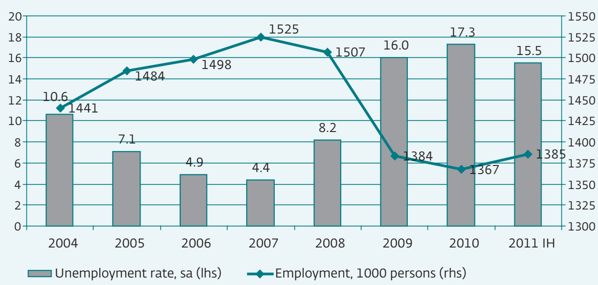
WHILE THE EU REMAINS LITHUANIA'S MAIN TRADE PARTNER, IMPORTANCE OF CIS INCREASES

In the last decade, the EU was the main market for visible exports. Around 61% of total Lithuanian exports and nearly 57% of imports of goods went to the EU last year (Tables A5 and A6) and these indicators fell by 3.2 and 2.5 percentage points, respectively, during the year. Meanwhile, the relative weight of the CIS in Lithuania's foreign trade went up by a very similar margin as this region accounted for 27% of exported goods and around 35% of imported goods. Russia strengthened its position as Lithuania's largest foreign trade partner as its shares of visible exports and imports went up sharply last year to 15.6% and 32.6%, respectively. Analysis of the mineral fuel (MF) goods sector shows that exports to Russia soared by 57% and its relative weight exceeded by a fifth. Nevertheless, the Russian leadership relied on re-exports, as less than a quarter of goods sold in this country were made in Lithuania. Meanwhile, exports to the EU went up by a smaller margin of 22.5% and the relevant weight of this region in total exports of goods excluding MF fell by 3.4 percentage points to 59% in 2010 and dropped to 56% in the first half of this year. As a result of strong competition on the latter market and uncertain prospects for the economy of Western Europe, the relative weight of the EU is unlikely to increase in Lithuanian exports in the next few years. Germany stood out among the EU members as it accounted for almost 12% of visible exports (net of MF) in 2010. The relative weight of this country was almost 17% if only products of Lithuanian origin are taken into account. The country was followed by Russia, Sweden, Latvia and Poland, whose indicators were much lower and hovered in the range between 7.5% and 6.3%. **To achieve a sustainable growth of exports, Lithuania and other Baltic states should be more active in penetrating emerging markets as the EU and CIS regions, which are facing serious challenges at the moment, account for over 90% of exports of goods.**

LABOUR MARKET IS RECOVERING AFTER A RECORD SLUMP

Despite the recovery of manufacturing, the average annual number of the unemployed (according to the data of the labour force survey conducted by Statistics Lithuania) rose by almost 30% last year to 291,000 and increased more than four-fold from 2007. The unemployment rate rose to unprecedented highs and stood at almost 17% (Diagram 2.3). Only Spain and Latvia had higher indicators in the EU. Around one in three young people (under the age of 24) were unable to find work. The number of employed people, which fell by almost 7% two years ago, contracted by 5.1% last year and dropped to 1,344,000, its lowest level in the history of independent Lithuania (Diagram 2.4, Tables A3 and A4). Measured in full-time equivalents, this indicator contracted by more than 18% compared to the pre-crisis level of 2007. Finally, the situation on the labour market began to improve this year. The number of employed people went up by 4.3% year-on-year in the second half of 2011 and the unemployment rate fell to 15.5%. Unemployment fell not only because of job creation but also due to strong emigration (Diagram 2.10). Statistics Lithuania estimates that the Lithuanian population shrank by 41,000, or 1.3%, between January and October of this year. We expect the

Diagram 2.5
LITHUANIA'S LABOUR MARKET INDICATORS, END OF PERIOD



Source: Eurostat

unemployment rate in Lithuania to go down to 14% by the end of the year, while in 2012 it is forecast to reach 12% on the back of easing emigration flows.

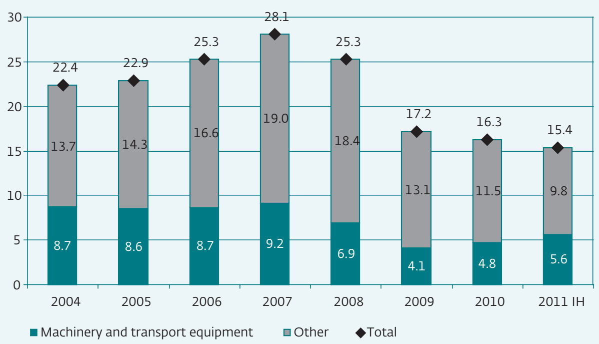
PEOPLE'S EARNINGS ARE EXPECTED TO GROW

The real average wage has been declining recently. It fell by around 3% in the last quarter of 2010 and by the middle of this year was about 2% lower than a year ago. During the previous year, the gross average wage did not change much, in the second quarter of 2011 went up by 2.5% year-on-year and stood at EUR 610 (EUR 475 after taxes). However, this increase was insufficient to offset inflation. The harmonised consumer price index rose by 3.6% in 2010 as prices for food, electricity, gas and other fuel as well as transport services soared. Inflation went up this year, with the annual change of this index reaching 4.8% in June. But the latest data suggest that the inflation rate may go down slightly by the end of the year and the real wage may be higher than a year ago. Although the unemployment rate is not expected to improve much in Lithuania in the coming years, employers are under increasing pressure to raise salaries. The current high unemployment rate is largely structural in nature as the vocational mismatch between labour supply and demand is reflected by a growing deficit of skilled labour. Moreover, the rising profit margins of businesses and improving labour productivity also add to the pressure to increase wages. For several successive years, the annual change in average wages was higher than the increase of productivity, but the trend was reversed last year as labour costs did not change and value added per worker at current prices went up by around 9%.

INVESTMENTS ARE INSUFFICIENT TO ENSURE RAPID ECONOMIC GROWTH

Further strong improvement in labour productivity depends on the increasing flows of investment. Sadly, Diagram 2.6 indicates that expenditure on core capital formation was negligible in 2009 and 2010, making up 17.2% and 16.3% of GDP, respectively. Investments in productive capital goods (metal products, machinery and transport equipment), which are of utmost importance for the competitiveness of the economy, rose slightly last year but still made up a mere 4.8% of GDP, which is much lower than in the majority of EU newcomers. In the first six months of the year, this indicator stood at 5.6% and went up by two percentage points year-on-year. This means that tangible investments continued to recover this year but still have not reached the pre-crisis level.

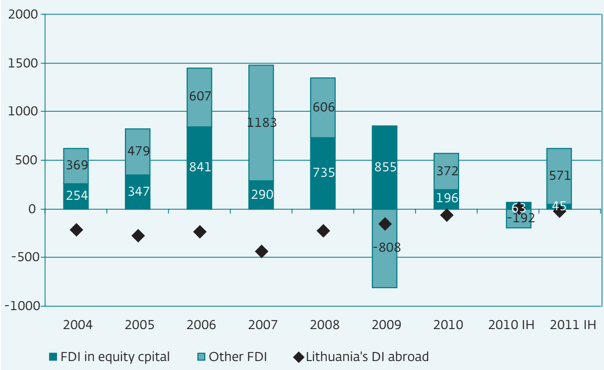
Diagram 2.6
LITHUANIA'S EXPENDITURE ON GROSS FIXED CAPITAL FORMATION, RATIO TO GDP, %



Source: Eurostat

Figures of foreign direct investment are also less than encouraging. Last year, the flow of net FDI remained miserable and made up EUR 508 billion. Although it was an improvement from the previous year when the indicator was negative, statistics indicate that Estonia managed to raise much more FDI in the last two years. The FDI flow to equity capital, which is extremely important, stood at just EUR 196 million in Lithuania last year and was weak in the first half of this year as well (Diagram 2.7).

Diagram 2.7
FOREIGN DIRECT INVESTMENT FLOWS OF LITHUANIA, EUR MILLION

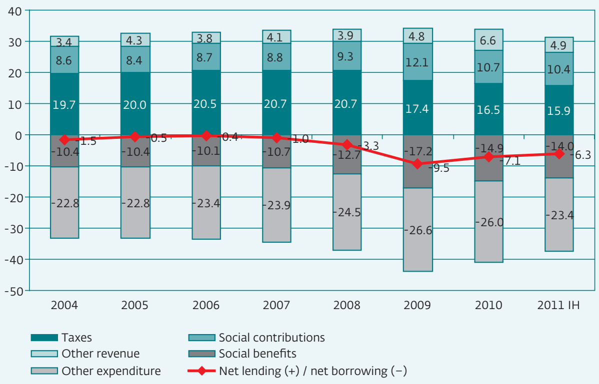


Source: Eurostat

BUDGET DEFICIT IS BEING SUCCESSFULLY REDUCED

The situation in public finance indicates that the Cabinet's efforts to patch up the hole in the Lithuanian treasury have borne fruit as the fiscal deficit shrank by about a quarter last year to 7% of GDP. Although the indicator remained high, the result was quite good given the magnitude of the downturn and unemployment seen in 2009. In the EU, nine countries had worse balances and the economies of all of them, with the exception of Latvia, contracted by a much smaller margin than the Lithuanian economy during the crisis. A partial consolidation of public finance was achieved by spending cuts as the ratio between government expenditure and GDP shrank by almost 3 percentage points to 41.3%. The ratio was a little bit lower only in Luxembourg, Slovakia, Romania and Estonia and was below 38% in Bulgaria. Although the total income of the Lithuanian government sector increased, the income- to- GDP ratio in 2010 was slightly lower than it was a year ago and stood at 34.2% (Diagram 2.8). Only the Slovakian government's income level was lower. The renewed convergence programme states that the fiscal deficit- to- GDP ratio will fall to 5.3% this year, will be below 3% in 2012 and will continue to decline in 2013–2014. The latest statistics show that the government is

Diagram 2.8
REVENUES, EXPENDITURE AND SURPLUS/DEFICIT OF LITHUANIA'S GENERAL GOVERNMENT, RATIO TO GDP, %



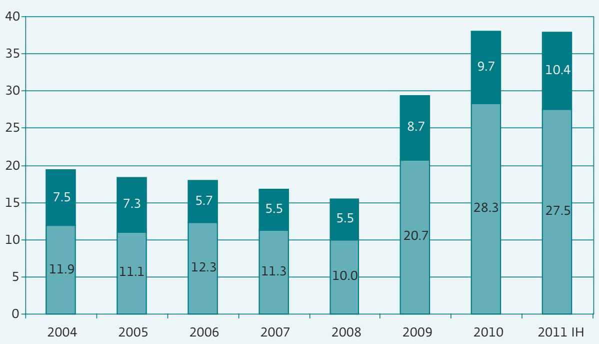
Source: Eurostat

on the right track as the fiscal deficit stood at 6.3% of GDP in the first half of this year and shrank by two percentage points year-on-year. However, next year's target, due to the worsening macroeconomic environment and the rising burden of debt service, will be a real challenge to achieve.

PUBLIC DEBT REMAINS WORRISOME

An important factor favourable for the economic development of the country is a low government debt to GDP ratio, which remains one of the lowest in the European Union (Diagram 2.9) despite growing quite strongly for the last two years. The indicator nearly doubled to 29.4% in 2009 and went up to 38% by the end of last year. If the trend is not reversed, the costs of servicing this debt will become unbearable in time as they would grow both because of the large amount of debt and more expensive borrowing as confidence in Lithuania's solvency would be undermined. In addition, central banks in the EU and USA will in a few years begin tightening their monetary policies because of inflation, which means that the average interest rate will inevitably go up worldwide. Therefore, the Cabinet seeks to ensure a better scenario and plans a gradual reduction of the public debt for the next couple of years. The Ministry of Finance expects the debt to go down to less than

Diagram 2.9
GENERAL GOVERNMENT DEBT OF LITHUANIA, RATIO TO GDP, %



Source: Eurostat

Diagram 2.10
LITHUANIA'S INDICATORS OF EXTERNAL MIGRATION, THOU

Source: Statistics Lithuania

38% of GDP by the end of 2012. It would be good if the Cabinet manages to achieve this target, but experience has shown that belt tightening is a nearly impossible exercise during a year of parliamentary elections. So far, international financial markets have kept their confidence in Lithuania's ability to control the situation. In November 2011, the country managed to launch a successful issue of USD 750 million 10-year bonds with the annual coupon of 6.125%.

SOCIAL SECURITY SYSTEM PROBLEMS REQUIRE STRUCTURAL REFORM

The guidelines for reforming the State Social Insurance Fund, which have been in preparation for some time, finally reached the Parliament this year and were approved. According to this document, the basic portion of old-age pensions will be separated from state social insurance and will be paid from the state budget. Benefits will be more closely tied to the contributions paid and the pension age will be gradually raised to 65 years. Although the latter proposal is popular in many EU countries it is questionable because it raises the unemployment rate, reduces competitiveness and aggravates youth employment. The average life expectancy in Lithuania is much shorter than in developed countries and postponement of the pension age must be accompanied by more liberal conditions for early retirement. In general, the most effective solution to social insurance problems would be strong economic growth, which should be a priority of the government. More attention should be paid to the promotion of manufacturing and investment, reforming the public sector and more thorough planning of public financing of infrastructure projects to ensure their higher cost effectiveness in order to ensure the sustainability of public finance.

FOSTERING COMPETITIVENESS IS A KEY PRECONDITION TO SUSTAINABLE GROWTH

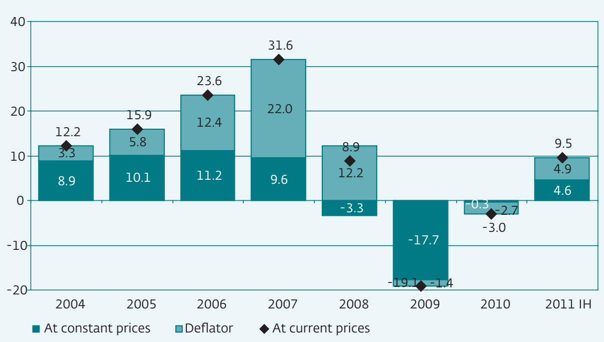
The long-term prospects of the national economy are worrying. Experience shows that being a small and open economy Lithuania is extremely sensitive to changes in demand on the EU and CIS markets. In the case of a new recession in the EU, the negative impact on the national economy would be strong, although it could be offset by growing investments and improving competitiveness. But that requires a consistent, energetic and targeted public policy, which has not yet been pursued. It looks as if the Cabinet has set the right targets and is trying to achieve them but progress has been modest so far, as reflected by the results of both business surveys and international competitiveness studies. We can take a look at Lithuania's rankings among 142 countries in the latest competitiveness report of the World Economic Forum, particularly those categories where the country ranked low (the position of the previous year is given in brackets). The overall ranking of Lithuania is satisfactory and indicates progress as it stands at 44 (47), but the results are much worse in most areas relating to the public authorities, namely the extent and effect of taxation at 124 (down from 126, the main rates of which are quite low in Lithuania and are not the problem; the country needs a simpler tax system), the impact of FDI regulation on business at 113 (124), burden of government regulation at 111 (115), wastefulness of government spending at 104 (117), budget deficit at 123 (123), hiring and firing practices at 117 (107), brain drain at 117 (110), ease of access to loans at 114 (112), venture capital availability at 101 (103), and state of cluster development at 114 (105). The government declares its support for the latter area, but no progress has been made in practice.

We believe that a broad reform plan for the business environment and public sector must be drawn up and put in place giving high priority to the promotion of competitiveness in order to ensure that the strong growth of the national economy is sustainable.

3. Latvia

Having undergone the steepest downturn among the countries of the EU in 2008-2009, the Latvian economy stabilised last year and has demonstrated accelerating growth this year. While the annual change in gross domestic product at constant prices was small in 2010, preliminary estimates for the first three quarters of this year indicate an average annual increase of 5%. Last year, GDP at current prices made up EUR 18 billion, down by almost 3% from 2009. This decline was caused by a negative change in the deflator (Diagram 3.1). GDP per capita declined to EUR 8,000. The same indicator in purchasing power standards shrank marginally and represented around 52% of the EU average. The latter indicator reached its highest level of 56% in 2008, while a decade ago it was as low as 36%. However, according to provisional figures of the population census, it may increase by several percentage points.

Diagram 3.1
LATVIA'S GDP, ANNUAL CHANGE, %

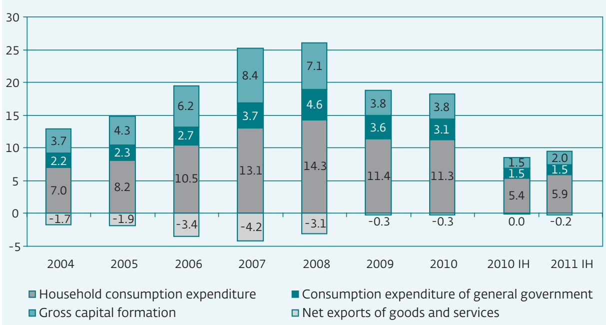


Source: Eurostat

LATVIA'S ECONOMY RETURNS TO STRONG AND BALANCED GROWTH

GDP components at the expenditure approach (current prices) are presented in Diagram 3.2. Last year, household consumption and expenditure on gross capital formation weakened slightly compared to 2009, while general government consumption expenditure decreased by 13% and exports and imports (of goods and services) rose by 19% and 18%, respectively. After a sharp decline in 2009, stocks of goods went up slightly last year, but expenditure on core capital formation fell by 12% compared to the previous year and more than halved compared to 2007. A comparison of the GDP structure in pre-crisis 2007 and 2010

Diagram 3.2
LATVIA'S GDP COMPONENTS BY EXPENDITURE APPROACH, EUR BILLION



Source: Eurostat

shows significant changes: the share of exports rose from 42.5% to 53.8%, the share of imports fell from 62.6% to 55.2% (Diagram 3.2) and the indicator of expenditure on gross capital formation fell below 21%, shrinking by almost half in a period of three years. Meanwhile, economic growth was obvious in the first half of this year as all of the above GDP components improved year-on-year. The smallest increase (2.5%) was in general government consumption expenditure, the indicator of household expenditure went up by around 9%, while expenditure on gross capital formation, exports and imports surged by about 30%. The total increase in nominal GDP was 9.5%, but price changes accounted for almost half this amount. Next year, Latvia's growth in GDP will be balanced as internal activities push economic growth and weigh a slowdown in exports. The frontloading of EU co-financed projects will stimulate a revival in the construction sector. We expect real GDP to expand by 2.5% in 2012 and, despite a significant slowdown, to outgrow the EU average.

MANUFACTURING AND TRANSPORT SECTORS ARE THE MAIN FACTORS POWERING GROWTH

Lately, the manufacturing and transport sectors have been the driving forces of the Latvian economy. Domestic trade has started to recover after the steep downturn and the construction sector eventually approached a turning point and expanded by roughly 20% in the third quarter of this year. Last year, manufacturing, domestic trade, transport and construction generated almost half of the country's value added: 13.4 (11.7), 16.7 (19.5), 12.1 (7.8) and 5.9 (10.4) percent, respectively. The relative weights in 2007 are indicated in brackets (Table A1). We can see that the importance of manufacturing and transport in particular increased significantly and the construction industry shrank by the largest margin after the crisis. In the first half of this year, manufacturing continued to grow strongly. Its value added at constant prices went up by nearly 15% year-on-year. Retail and transport industries also grew quite strongly at a rate of around 8%, while construction fell by 5% (Table A2).

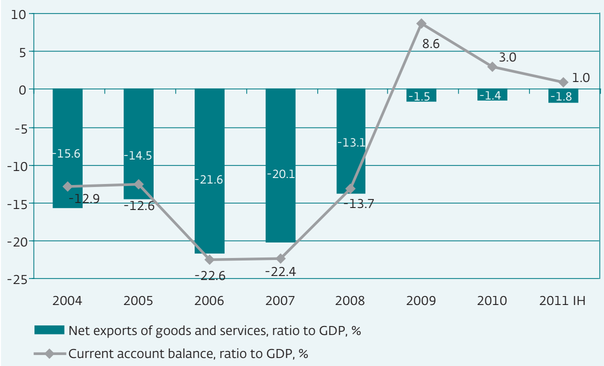
RECOVERY INITIALLY DRIVEN BY EXPORTS

Like the other Baltic countries, Latvia saw its foreign trade spring back to life last year (Diagram 3.3). The volume of both visible and invisible Latvian exports and imports at constant prices went up by 11.5% last year, while the annual change in exports and imports rose to around 15% and 22%, respectively, in the first six months of this year. In the latter period, the monthly export of goods and services per capita averaged EUR 415. This figure was higher than before the crisis but ranked only 23rd across the EU-27. Given that the degree of openness of small economies is higher than that of large economies, this Latvian indicator was especially poor, caused by a small volume of goods exports. However, while manufacturing broadly uses local commodities, the value added of Latvia's goods exports increases. In terms of the services indicator, the country would climb up several places. Latvia has consistently had a surplus balance of trade in services. Last year, the balance exceeded one billion euro and accounted for 5.6% of GDP. The indicator went up slightly in the first half of this year. Nevertheless, the balance of overall foreign trade (in goods and services) has remained negative, even though the deficit was much lower than it was before the crisis. The relevant indicators stood at 1.4% and 2.7% of GDP, in 2010 and the first half of this year, respectively (Diagram 3.4). Meanwhile, the current account balance of the national balance of payments has been positive for a third consecutive year thanks to a considerable flow of current transfers. Last year, its ratio to GDP stood at 3% and fell to 1% in the first six months of this year.

Diagram 3.3
LATVIA'S FOREIGN TRADE, RATIO TO GDP, %

Source: Eurostat

Diagram 3.4
LATVIA'S CURRENT ACCOUNT AND FOREIGN TRADE (GOODS AND SERVICES) BALANCES, RATIO TO GDP, %



Source: Eurostat

IF EU FALLS INTO RECESSION, GROWTH OF LATVIA'S EXPORTS OF GOODS WILL COME TO A HALT

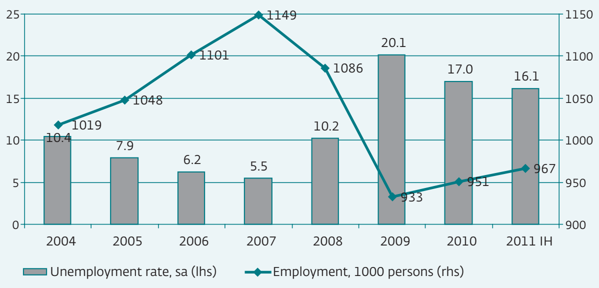
A breakdown of the Latvian foreign trade by region shows that the EU was the main market for visible exports in the last decade. It accounted for over 67% of total exports of goods and 76% of imports of goods last year (Tables A5 and A6). These indicators did not change much from 2009 and remained stable in the first half of this year as well. Lithuania and Russia were the largest foreign trade partners of Latvia. In 2010, they accounted for 15% of exports of goods each and 16% and 10% of imports respectively. The Latvian visible exports are clearly insufficiently diversified. To achieve sustainable growth of exports, Latvia, like the other Baltic states, should intensify its penetration of new markets because domestic consumption in the European Union may weaken because of austerity packages adopted by many of its member states.

STEADY FALL IN UNEMPLOYMENT AND PICK UP IN REAL WAGES BOOSTS CONSUMER SPENDING

Despite the stagnating GDP, the number of employed people rose slightly in 2010 and the unemployment rate fell by three percentage points, standing at 17% in the last quarter of 2010 (Diagram 3.5, Tables A3 and A4). This year, the trend has continued. The unemployment rate went down to around 16% in the second quarter, but youth unemployment (under the age of 24) was as high as almost 30%. Like Lithuania, Latvia has been concerned lately about the dangerous level of emigration, which has not been reliably estimated by statistical services.

Despite the high unemployment rate, the average gross wage increased by more than 3% last year and made up EUR 647 in the last quarter (EUR 459 after taxes). The increase of real wages was very similar because inflation was low in Latvia in 2010. This year, the growth of wages accelerated and the increase in the second quarter made up 5.5% year-on-year. Unfortunately, the consumer price index also rose quite sharply with annual growth standing at 4.7% in June. Although the increase in real wages was small, domestic consumption has been recovering alongside the falling unemployment rate, as

Diagram 3.5
LATVIA'S LABOUR MARKET INDICATORS, END OF PERIOD



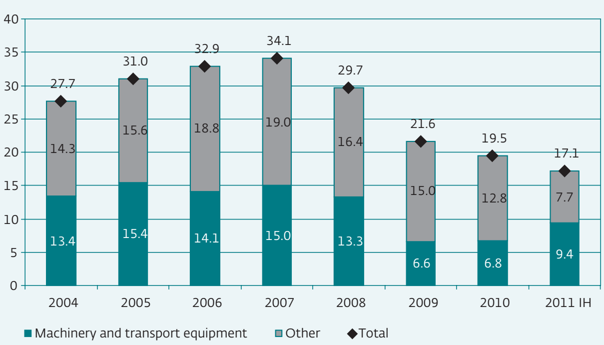
Source: Eurostat

reflected by rejuvenated retail trade. This year, retail trade in Latvia has grown at one of the fastest rates in the EU.

INVESTMENTS ON TRACK BUT GENERAL PROCESSES STALL

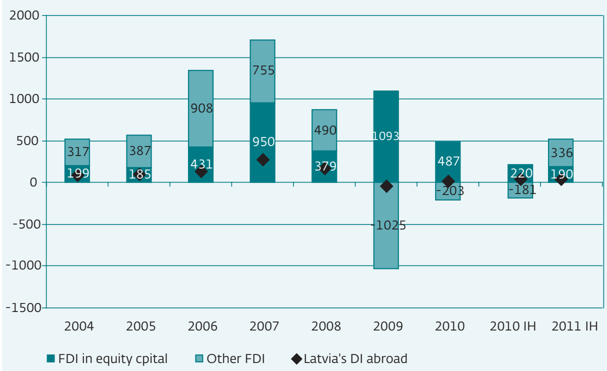
Further development of the Latvian economy depends strongly on investment processes. Diagram 3.6 indicates that the level of expenditure on gross fixed capital formation stood at 21.6% and 19.5% of GDP, respectively, in 2009 and 2010, which was much lower than the average level in 2004–2008, but considerably higher than the EU average or Lithuania's indicator. The ratio between investments in productive capital goods (metal products, machinery and transport equipment) and GDP went up fractionally last year to 6.8%, which made up about half of the average of the previous five-year period. However, the latter indicator rose to 9.4% in the first half of this year (by comparison, the EU average is 6.5%). This suggests that tangible investments continued to recover this year but still have not reached the pre-crisis level. The recovery in investment processes and domestic consumption has been hampered by a very high debt level in households and companies. At the end of last year, the total liabilities to GDP ratio exceeded 94% and receded by just 4 percentage points during the year. Meanwhile, the EU indicator stood at around 80% and the Lithuanian indicator was below 60%.

Diagram 3.6
LATVIA'S EXPENDITURE ON GROSS FIXED CAPITAL FORMATION, RATIO TO GDP, %



Source: Eurostat

Diagram 3.7
FOREIGN DIRECT INVESTMENT FLOWS OF LATVIA, EUR MILLION



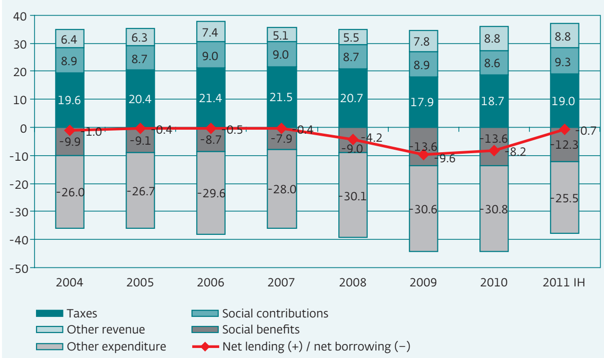
Source: Eurostat

The data for foreign direct investments have not been impressive lately. The flow of net FDI remained weak last year and stood at EUR 268 million, then rose to EUR 492 million in the first six months of this year (Diagram 3.7). However, the FDI flow to equity capital in Latvia has been quite encouraging, equivalent to EUR 487 and 190 million, or 2.7% and 2.1% of GDP, in the respective periods.

FURTHER AUSTERITY NEEDED, DIFFICULTIES IN BORROWING ON INTERNATIONAL FINANCIAL MARKETS EXPECTED

Efforts taken by the Latvian government to stabilise public finance have been successful. Last year, Latvia's fiscal deficit to GDP ratio went down by 1.4 percentage points to 8.2% and declined by a further 4.4 percentage points in the first half of this year. These results are not bad in view of the magnitude of the downturn and unemployment in 2008–2009. The reduction of this deficit depended on the rising budget revenue to GDP ratio last year and significant general government spending cuts in the first half of 2011. Compared to the relevant indicator from last year, the government expenditure to GDP ratio contracted by nearly 5 percentage points to 37.8% (Diagram 3.8). Despite

Diagram 3.8
REVENUES, EXPENDITURE AND SURPLUS/DEFICIT OF LATVIA'S GENERAL GOVERNMENT, RATIO TO GDP, %



Source: Eurostat

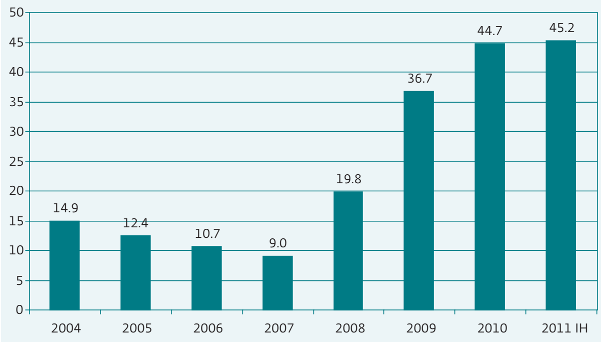
these achievements, the Latvian Cabinet has to negotiate hard with the International Monetary Fund to receive the final instalments. There is no demand to seek new financing assistance from the International Monetary Fund.

LATVIA MUST ENHANCE ITS COMPETITIVENESS FURTHER TO CLEAR NEW HURDLE FOR GROWTH

Although Latvia has some of the lowest public debt to GDP ratios in the European Union, recent growth in its public debt has been disconcerting. This soared by almost 36 percentage points between 2008 and 2010 and exceeded 45% at the beginning of this year (Diagram 3.9). Because of the dwindling confidence of financial markets in EU member states, it may entail high debt servicing costs in the future, even though the growth of this debt has slowed considerably this year.

The long-term prospects for the national economy are not excellent. The economy is particularly sensitive to changes in the EU region, which faces recession. The country needs to penetrate new markets and raise its competitiveness, which has been weak so far. Latvia ranked 64th (70th) among 142 countries covered in the latest competitiveness report of the World Economic Forum (the result of the previous study is given in brackets). We will identify several areas in which Latvia needs to make progress because its ranking is low. These are the extent and effect of taxation at 111, business impact of rules on FDI at 101, wastefulness of government spending at 106, budget deficit at 127, rigidity of employment index at 114

Diagram 3.9
GENERAL GOVERNMENT DEBT OF LATVIA, RATIO TO GDP, %



Source: Eurostat

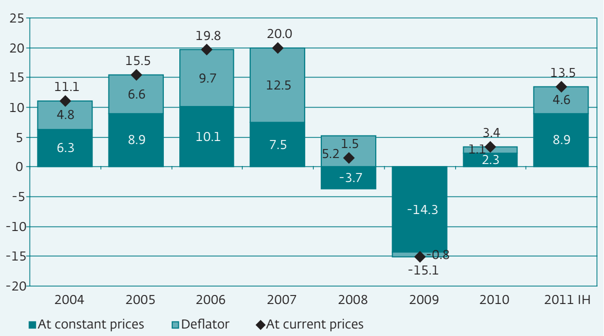
and efficiency of legal framework in settling disputes at 104. According to the results of business surveys conducted by the WEF, the main obstacles to doing business are tax rates, access to financing, corruption and inefficient government bureaucracy. Incidentally, the latter obstacle was identified as being the main one in Lithuania.

To ensure that strong economic growth is sustainable, Latvia (like Lithuania) needs to improve its business environment considerably by putting in place measures that promote investment, eliminating red tape barriers and making the public sector more effective.

4. Estonia

The Estonian economy, which underwent a steep downturn in 2008–2009, went up by 2.3% last year and demonstrate an incredible leap in 2011. Preliminary estimates indicate that the Estonian GDP at constant prices went up by 8.6% in the first nine months of this year. Only the emerging economies in the Far East were able to enjoy such a high growth rate. GDP at current prices made up EUR 14.3 billion last year and rose by 3.4% compared to 2009 (Diagram 4.1). GDP per capita went up to EUR 10,700 and was almost by a third higher than in Latvia and by 27% higher than in Lithuania. The relative GDP per capita indicator measured in the purchasing power standards, which peaked at 70% of the EU average in 2007, was stagnant in 2009–2010 (64%). However, it is likely that Estonia will regain its previous position thanks to this year's rise.

Diagram 4.1
ESTONIA'S GDP, ANNUAL CHANGE, %

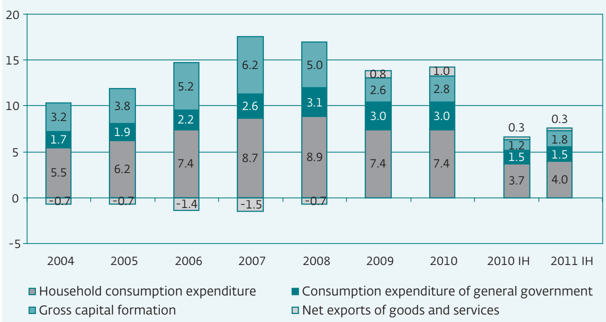


Source: Eurostat

ESTONIA ACTIVELY BOOSTS ITS EXPORTS ON FOREIGN MARKETS

One of the fundamental changes in the GDP structure during the pre-crisis and post-crisis periods is the fact that the net export component has been positive in the Estonian GDP since 2008. This once again confirms that foreign trade has been the main driving force of the national economy in recent years. In the first half of 2011, the annual growth of visible exports stood at 47%. Electronic equipment and machinery delivered to Sweden accounted for the majority of exports of goods. In the nine months of this year, exports to Sweden soared by almost 75% year-on-year and made up 19.3% of total exports of the country, going ahead of Finland (17%). By the way, exports to Russia, which has lifted trade barriers, also increased significantly this year. Between January and September, exports to Russia grew by 56.1% and accounted for 11.6% of total exports. Estonian exports have also been penetrating new markets such as China, India, Singapore, Libya, Nigeria, Australia and others, diversification of exports to the EU has also improved. Such successful sales on new export markets were ensured by both a concerted search for trading partners by the companies and the fruitful government policy aimed at raising foreign investments.

Diagram 4.2
ESTONIA'S GDP COMPONENTS BY EXPENDITURE APPROACH, EUR BILLION



Source: Eurostat

Household consumption, which stalled at the level of 2006, did not change in the last two years and the share of general government expenditure was also modest. The ratio between GDP and expenditure on gross capital formation shrank by more than half in 2010 compared to the maximum reached in 2007 – from 38.6% to 18.8%. The recovery of domestic demand has been obvious this year. The annual increase in the component was roughly 10% in the first half of this year and was based on both stock corrections, which accounted for nearly one half of the total increase, and positive changes in investments and household consumption.

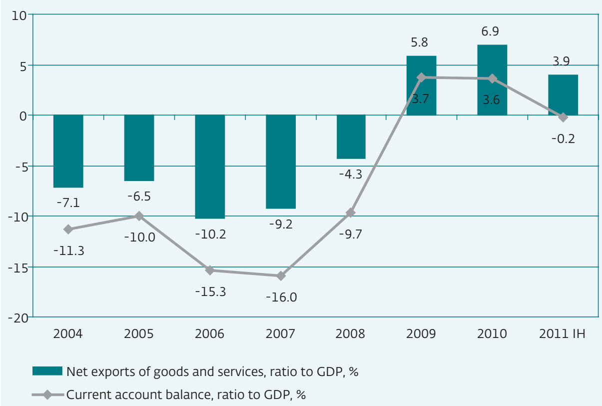
ESTONIAN EXPORTS OF SERVICES PER CAPITA REMAIN HARD TO CATCH

Estonia has been more effective than its Baltic neighbours in taking advantage of invisible export opportunities. Throughout 2010, its exports of services made up around EUR 3.5 billion (the relevant indicators in Latvia and Lithuania stood at EUR 2.8 and 3.1 billion respectively). The relative indicators in Estonia are superior as exports per capita stand at EUR 2,600 in Estonia which is much higher than in Latvia and Lithuania (EUR 1,200 and 1,000 respectively). The transport industry generates around 40% of total exports of services and the share of construction, computer and IT as well as other business services is considerably higher than in other Baltic states (Table A9). It is hardly surprising that Estonia has enjoyed a constant surplus balance of trade in services. The balance made up 9.3% of GDP last year and nearly 7.5% of GDP in the first half of this year. This surplus has compensated the negative indicator of net exports of goods keeping the total balance of foreign trade (in goods and services) in the positive territory since 2009 (Diagrams 4.3 and 4.4). The current account of the national balance of payments was also positive for two consecutive years but has gone down just below zero this year on the back of improved profitability of foreign companies.

Diagram 4.3
ESTONIA'S FOREIGN TRADE, RATIO TO GDP, %

Source: Eurostat

Diagram 4.4
ESTONIA'S CURRENT ACCOUNT AND FOREIGN TRADE (GOODS AND SERVICES) BALANCES, RATIO TO GDP, %

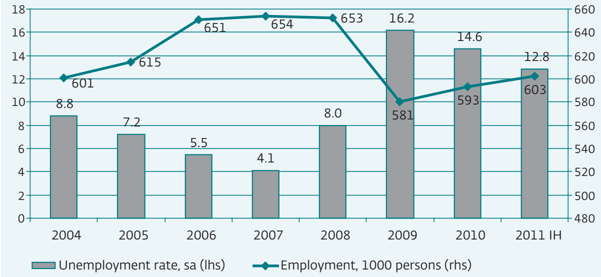


Source: Eurostat

FALLING UNEMPLOYMENT AND STRUCTURAL LACK OF SKILLED LABOUR DRIVE THE RECOVERY OF EARNINGS

The unemployment rate, which more than doubled in 2009, has been on the downward slide since last year in Estonia and stood at 12.8% in the first half of this year (Diagram 4.5). Latest

Diagram 4.5
ESTONIA'S LABOUR MARKET INDICATORS, END OF PERIOD



Source: Eurostat

data of the national statistical service indicate that the ratio between the unemployed and employed people went down to 10.9% in the third quarter. Better changes on the labour market compared to the other Baltic countries resulted from strong economic growth in Estonia as well as much more flexible labour market system and its constant improvement. In the first half of 2011, the number of working people in Estonia rose by 7.3% year-on-year, and this growth was 2.3 and 2.8 times faster than in Latvia and Lithuania respectively. Despite considerably revised growth projections, the employment rate should continue to grow next year, albeit at a slowing pace. The growing gap between the labour supply and demand is a source for concern. The Estonian economic activity is directed at the most advanced areas (green energy production, higher value added creation, etc.) which enables the country to improve its competitiveness year by year but makes some workforce go by the board. Therefore, high unemployment may become structural in nature in this country and labour costs may increase considerably if no special programmes are put in place. So far, labour productivity has grown faster than labour costs and there are no signs that the country may be losing its competitive edge. The average wage, which rose by 4% by the end of 2010 to EUR 814, has continued to grow this year. It went up by 4.5% and 4.3% year-on-year in the first and second quarters of 2011 respectively, while value added per worker at current prices increased by around 4% last year and by more than a tenth this year. **Because of the above reasons, the growth of wages is likely to remain strong despite a slowdown in economic development and changes in real wages will become negative next year.**

DECLINING PRICES IN FOOD AND ENERGY SECTORS WILL REIN IN INFLATION BUT IT WILL REMAIN HIGH

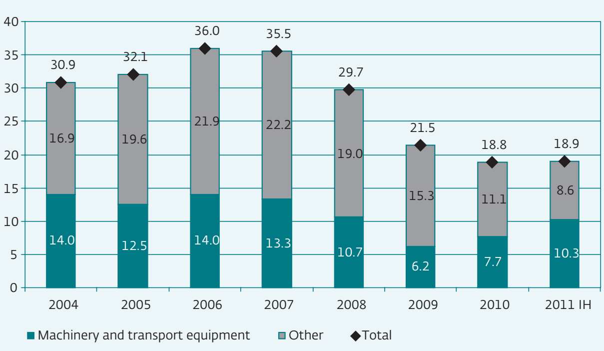
The rising gross wage cannot offset high inflation and the real average wage in Estonia has been declining for 11 consecutive quarters. After deflation at the beginning of last year, the growth of prices accelerated to 5–5.5% in the second half of 2010 and this year. The food and energy sectors account for a significant portion of the consumption basket in Estonia. As prices in these two sectors soared, the impact of imported inflation was much stronger. Estonia led the EU in terms of changes in the harmonised consumer price index in 2010. In addition to the above factors, higher taxes and administered prices also pushed the average price level upwards. Meanwhile, the European Commission estimates that the effect of euro adoption on average prices was quite limited (prices went up by 0.2–0.3% in the first quarter of this year after the common currency was adopted) and was most obvious in the services sector. Similar growth was recorded in other countries that had just joined the Eurozone. Inflation should slow down significantly in Estonia because of falling food and energy prices given the deteriorating condition of the global economy. Nevertheless, the structural causes of higher inflation such as the small market, shorter agreements in retail trade and dominance of oligopolistic markets, unification of prices in the closed sector, etc. will remain and inflation will be higher than the Eurozone average in the medium term.

AFTER A DECLINE OF SEVERAL YEARS, TANGIBLE INVESTMENTS ARE ON THE UP IN ESTONIA

Investments in core capital, which continued to decline since 2006, have finally begun to recover this year. However, the overall level of investment has remained almost twice as low as before the crisis (Diagram 4.6). On the other hand, Estonia returned to the leading position in the EU in terms of the productive investments (in machinery and vehicles) to GDP ratio. In the first half of this year, the indicator exceeded the EU average by nearly four percentage points. The rejuvenation of investment processes was caused by better corporate financial results and economic sentiment indicators. And although the latter began to slide down because of increasing uncertainty on foreign markets, we expect the expenditure on gross capital formation to remain at a high level in Estonia next year. Although the high debt ratio among businesses will slow down investment processes, investments by general government in absorbing generous structural assistance of the EU and implementation of environmental projects in 2012–2013 should compensate its effect.

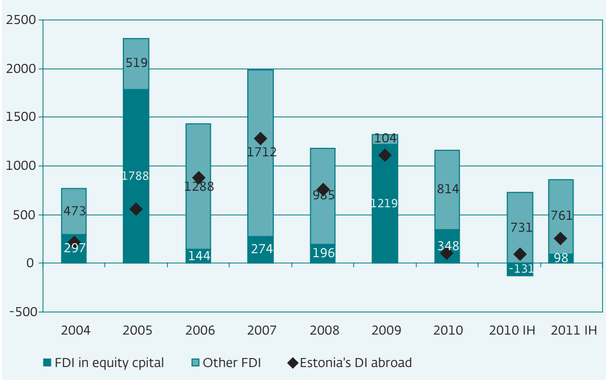
The figures of foreign direct investment are simply impressive. Estonia has clearly outperformed its Baltic neighbours reviewed here in terms of FDI per capita. In the middle of 2011, the indicator stood at EUR 9,700 in Estonia and was much higher than in Latvia and Lithuania where it made up EUR 4,100

Diagram 4.6
ESTONIA'S EXPENDITURE ON GROSS FIXED CAPITAL FORMATION, RATIO TO GDP, %



Source: Eurostat

Diagram 4.7
FOREIGN DIRECT INVESTMENT FLOWS OF ESTONIA, EUR MILLION



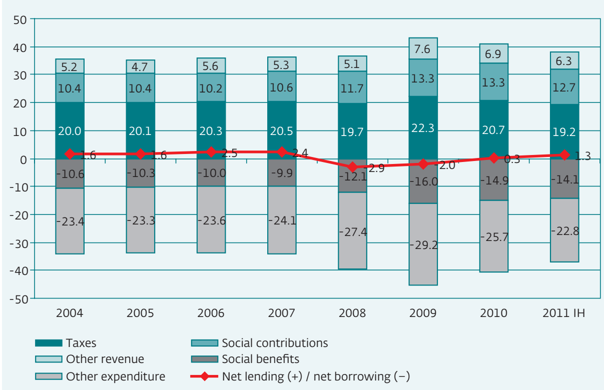
Source: Eurostat

and EUR 3,300 respectively. Although the latter countries are trying very hard to raise more investment from abroad, there is little chance that they could overcome Estonia in the nearest future. The statistics of FDI flows have been less than encouraging in Estonia lately. In 2010, there was a significant drop in investments in equity capital and Estonian companies are gradually intensifying their investments in foreign countries (Diagram 4.7).

FISCAL DISCIPLINE LEADS TO STRONGER ECONOMIC GROWTH

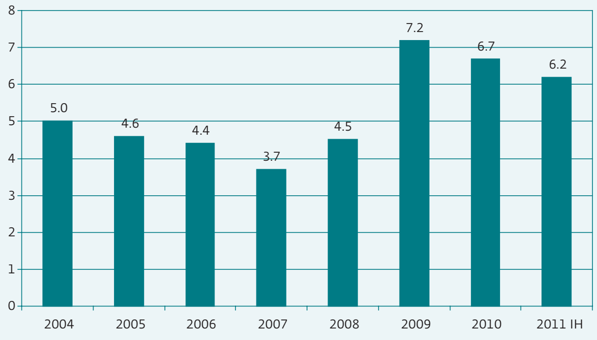
The country receives constant praise for its conservative fiscal policies implemented by the government. Estonia has probably been the only country in the EU to enjoy a surplus budget of general government for a third consecutive year. Table A14 shows that general government revenues in Estonia account for a much larger share of GDP than in Latvia and Lithuania (almost 41% of GDP was redistributed through budget last year). Generation of revenues was significantly boosted not only by accelerating economic growth but by a successful sale of emissions allowances as well. Estonia sold emissions allowances for EUR 334 million in 2010–2011 and most of this

Diagram 4.8
REVENUES, EXPENDITURE AND SURPLUS/DEFICIT OF ESTONIA'S GENERAL GOVERNMENT, RATIO TO GDP, %



Source: Eurostat

Diagram 4.9
GENERAL GOVERNMENT DEBT OF ESTONIA, RATIO TO GDP, %



Source: Eurostat

amount should be invested in climate change management instruments in 2012–2013. Next year, the Estonian budget will sink into the red because of planned general government investments and increased social benefits (especially pensions). However, the Cabinet expects to return to a healthy surplus in a couple of years. The government debt may also rise slightly but the Cabinet has no intention to borrow heavily and the debt level is likely to remain the lowest in the EU.

Despite these excellent achievements, the Estonian economy is vulnerable to negative external conditions, especially bearing in mind its openness. The prospects of economic development in the main foreign partners of the country in the next two years have deteriorated and a leap and exports and real GDP similar to that of this year is highly unlikely in 2012–2013. On the other hand, the targeted investment policy by the Estonian government was successful as many companies moved production to this country in 2010–2011 in an attempt to cut costs, thereby offsetting at least some of the potential losses.

Annex

Table A1
VALUE ADDED CREATED BY ECONOMIC ACTIVITIES, %

NACE 2	Activity	Estonia			Latvia			Lithuania		
		2004	2007	2010	2004	2007	2010	2004	2007	2010
total	All NACE activities, EUR billion	8.6	14.1	12.5	10.0	18.6	16.1	16.5	25.8	24.7
total	All NACE activities	100	100	100	100	100	100	100	100	100
a	Agriculture, forestry and fishing	3.8	3.0	3.3	4.3	3.5	4.5	4.6	3.9	3.3
b	Mining and quarrying	1.0	1.0	1.4	0.2	0.4	0.6	0.5	0.5	0.4
c	Manufacturing	16.7	15.4	16.4	13.5	11.7	13.4	20.0	17.8	18.8
d	Electricity, gas, steam and air conditioning supply	2.9	2.5	4.0	3.0	2.4	3.6	4.0	3.0	3.3
e	Water supply; sewerage, waste management and remediation activities	0.9	1.0	1.1	0.7	0.6	1.1	0.8	0.7	0.9
f	Construction	7.0	9.9	5.7	6.6	10.4	5.9	7.2	11.2	6.0
g	Wholesale and retail trade; repair of motor vehicles and motorcycles	14.1	13.4	11.9	19.0	19.5	16.7	17.7	16.9	18.4
h	Transportation and storage	9.4	7.9	8.8	10.8	7.8	12.1	9.2	9.9	11.7
i	Accommodation and food service activities	1.6	1.5	1.1	1.4	1.7	1.5	1.5	1.3	1.2
j	Information and communication	4.7	4.7	4.6	5.2	3.9	4.0	4.4	3.7	3.5
k	Financial and insurance activities	3.8	4.3	3.6	3.8	5.4	3.7	1.7	3.3	2.4
l	Real estate activities	10.6	10.2	10.9	8.2	8.2	8.3	6.2	6.5	6.5
m	Professional, scientific and technical activities	4.2	4.3	5.1	2.9	4.0	4.7	3.3	3.9	3.7
n	Administrative and support service activities	2.9	4.0	3.6	2.1	2.2	2.6	1.5	2.0	2.2
o	Public administration and defence; compulsory social security	5.7	6.4	7.3	7.5	7.9	7.4	7.4	6.4	6.8
p	Education	4.8	4.7	5.1	5.2	4.6	4.5	5.0	4.2	5.3
q	Human health and social work activities	2.9	3.6	3.8	2.7	2.8	2.9	2.7	3.0	3.6
r, s, t	Other activities	2.8	2.5	2.4	2.9	3.0	2.5	2.3	1.8	1.9

Source: national statistics offices

Table A2

VALUE ADDED CREATED BY ECONOMIC ACTIVITIES (AT CONSTANT PRICES), ANNUAL CHANGES, %

NACE 2	Activity	Estonia		Latvia		Lithuania	
		2009	2010	2009	2010	2009	2010
total	All NACE activities	−14.8	2.6	−15.6	−0.5	−14.8	1.4
a	Agriculture, forestry and fishing	12.4	−9.3	9.1	2.0	1.4	−7.1
b	Mining and quarrying	−23.4	25.7	24.2	14.9	−27.8	10.0
c	Manufacturing	−26.0	21.2	−17.8	16.5	−16.0	9.9
d	Electricity, gas, steam and air conditioning supply	−3.9	7.8	−4.5	7.5	−2.0	−4.0
e	Water supply; sewerage, waste management and remediation activities	−14.8	2.7	−16.6	−5.9	−11.7	5.5
f	Construction	−36.1	−8.7	−32.0	−23.9	−45.6	−6.2
g	Wholesale and retail trade; repair of motor vehicles and motorcycles	−28.9	1.6	−25.5	3.3	−21.6	2.6
h	Transportation and storage	−12.1	5.2	1.1	5.6	−8.1	7.2
i	Accommodation and food service activities	−33.5	−5.7	−20.5	−0.2	−19.1	−6.2
j	Information and communication	−7.9	−11.4	−17.6	−7.4	0.1	−0.6
k	Financial and insurance activities	−23.2	−6.5	−14.2	−8.6	−8.6	8.4
l	Real estate activities	11.6	2.9	−0.9	−0.1	−3.8	−2.6
m	Professional, scientific and technical activities	−4.8	8.9	−16.1	−12.8	−16.8	−3.5
n	Administrative and support service activities	−20.9	−8.4	−34.3	−2.2	−13.4	2.6
o	Public administration and defence; compulsory social security	1.1	−0.5	−8.8	−7.5	−1.7	−1.8
p	Education	−2.7	−1.7	−9.9	−6.3	−2.7	−4.1
q	Human health and social work activities	−4.0	−2.4	−9.7	−3.1	−1.4	−1.3

Source: national statistics offices

Table A3

UNEMPLOYMENT RATE, SA, E-O-P, %

	Unemployment rate					Youth unemployment rate[1]				
	2008	2009	2010	2011 Q1	2011 Q2	2008	2009	2010	2011 Q1	2011 Q2
EU-27	7.5	9.5	9.6	9.5	9.5	17.0	21.1	21.0	21.1	21.1
Estonia	8.0	16.2	14.6	13.6	12.8	17.6	32.6	25.9	20.4	21.8
Latvia	10.2	20.1	17.0	16.3	16.1	19.6	40.8	30.9	31.1	29.7
Lithuania	8.2	16.0	17.3	16.5	15.5	18.3	31.7	34.2	33.8	32.7

[1] Youth unemployment – up to 24 years old

Source: Eurostat

Table A4

EMPLOYMENT BY ECONOMIC ACTIVITIES, AVERAGE, %

NACE 2	Activity	EU-27			Estonia			Latvia			Lithuania		
		2009	2010	2011 I H	2009	2010	2011 I H	2009	2010	2011 I H	2009	2010	2011 I H
total	Total number of employed, thousand	217447.5	216405.4	216619.6	595.8	570.9	597.0	983.1	940.9	955.4	1415.9	1343.7	1362.8
		structure		annual change	structure		annual change	structure		annual change	structure		annual change
total	Total – All NACE activities	100	100	0.5	100	100	7.3	100	100	3.2	100	100	2.6
a	Agriculture, forestry and fishing	5.1	5.1	−2.9	4.0	4.2	11.6	8.7	8.8	18.2	9.2	9.0	−5.0
b	Mining and quarrying	0.4	0.4	−1.2	1.1	1.2	−4.8	0.3	0.5	−23.6	:	:	:
c	Manufacturing	16.1	15.7	0.6	19.1	19.0	17.6	13.8	13.7	3.0	16.0	15.5	1.6
d	Electricity, gas, steam and air conditioning supply	0.8	0.8	1.6	1.3	1.5	−19.7	1.4	1.5	−13.4	1.3	1.1	4.4
e	Water supply; sewerage, waste management and remediation activities	0.7	0.7	5.0	:	:	:	1.3	1.2	−26.1	0.9	0.8	17.4
f	Construction	8.0	7.7	−2.3	9.8	8.4	24.6	8.1	7.1	11.9	8.7	6.9	−1.0
g	Wholesale and retail trade; repair of motor vehicles and motorcycles	14.1	14.1	−0.1	14.0	14.0	5.9	16.6	15.9	4.1	17.6	18.1	−1.1
h	Transportation and storage	5.1	5.1	0.5	8.3	7.6	9.8	9.0	8.7	1.2	6.4	6.8	16.3
i	Accommodation and food service activities	4.3	4.4	1.5	3.4	3.4	−1.3	2.6	3.1	−12.8	2.5	2.5	12.9
j	Information and communication	2.8	2.8	2.6	2.4	2.2	31.2	2.3	3.1	7.0	1.7	1.8	26.7
k	Financial and insurance activities	3.0	3.0	0.6	1.9	1.6	7.3	2.0	2.0	0.9	1.6	1.7	−10.3
l	Real estate activities	0.8	0.8	3.9	1.5	1.8	9.6	1.4	1.9	8.7	0.8	1.0	−1.5
m	Professional, scientific and technical activities	4.9	4.9	1.9	3.4	3.7	10.6	2.7	2.8	−6.5	3.2	3.6	10.0
n	Administrative and support service activities	3.8	3.9	3.0	2.8	3.3	−14.6	3.1	3.2	17.9	3.0	3.2	9.4
o	Public administration and defence; compulsory social security	7.2	7.2	−0.7	6.2	7.1	−6.5	7.0	6.6	−1.5	6.0	6.1	1.0
p	Education	7.2	7.4	0.5	10.5	9.8	−5.1	9.4	10.3	1.2	10.5	11.0	1.6
q	Human health and social work activities	10.0	10.2	2.2	5.5	6.1	6.6	4.7	5.0	3.0	6.5	6.9	2.3

Source: Eurostat

Table A5

EXPORTS OF GOODS BY REGION, FOB PRICES, %

	Estonia				Latvia				Lithuania			
	2009	2010	2010 I H	2011 I H	2009	2010	2010 I H	2011 I H	2009	2010	2010 I H	2011 I H
Total, EUR million[1)]	6489	8753	3851	5919	5521.9	7190.5	3167	4338	11797	15651	6838	9613
Total	100	100	100	100	100	100	100	100	100	100	100	100
EU-27	69.5	68.6	69.4	67.0	67.6	67.2	67.8	67.9	64.3	61.0	62.3	60.0
Estonia	–	–	–	–	13.6	12.5	13.1	13.5	7.0	5.0	5.3	5.8
Latvia	9.5	9.0	8.7	6.6	–	–	–	–	10.1	9.4	9.1	9.5
Lithuania	4.8	4.9	4.8	4.4	15.2	15.1	14.3	16.0	–	–	–	–
Poland	1.7	1.6	1.7	1.7	3.6	4.7	4.3	5.1	7.2	7.7	7.1	7.4
Finland	18.5	17.0	18.0	14.9	2.6	2.9	2.8	2.9	1.7	1.4	1.6	1.4
Germany	6.1	5.2	5.4	4.5	8.2	8.1	8.1	8.0	9.7	9.9	10.6	9.2
Sweden	12.6	15.6	13.6	16.9	5.7	5.8	6.1	6.1	3.6	3.6	3.9	3.5
UK	2.0	2.0	2.1	1.8	3.0	3.2	3.2	2.9	4.4	4.9	5.2	4.4
France	2.3	2.5	3.4	4.0	1.7	1.5	1.6	1.5	3.2	3.3	3.4	3.9
Italy	1.1	0.9	1.0	1.6	1.5	1.8	2.1	1.6	2.0	1.9	2.0	1.8
Spain	0.6	0.7	0.7	1.6	1.0	1.1	1.2	0.7	1.7	1.0	1.2	1.1
Denmark	3.5	2.5	3.0	2.8	3.8	3.6	3.7	3.0	3.8	3.0	3.5	2.2
Netherlands	2.5	2.3	2.5	2.1	2.4	2.1	2.0	2.0	5.1	5.6	5.2	5.7
Belgium	1.9	1.3	1.5	1.3	1.1	1.1	1.2	1.0	1.7	1.4	1.4	1.3
Extra EU-27	30.5	31.4	30.6	33.0	32.4	32.8	32.2	32.1	35.7	39.0	37.7	40.0
Norway	3.2	3.4	3.2	2.8	2.5	2.6	3.1	2.3	2.5	2.3	2.1	1.9
US	4.2	3.8	4.7	7.0	1.5	1.3	1.5	1.1	2.9	2.7	2.3	3.3
Russia	9.3	9.7	8.6	8.8	13.0	15.3	13.7	15.4	13.2	15.7	13.8	15.9

[1)] Data provided in compliance with Balance of Payments Methodology

Source: Eurostat

Table A6

EXPORTS OF GOODS BY REGION, CIF PRICES, %

	Estonia				Latvia				Lithuania			
	2009	2010	2010 I H	2011 I H	2009	2010	2010 I H	2011 I H	2009	2010	2010 I H	2011 I H
Total, EUR million[1)]	7272	9242	4200	6257	7034	8819	3788	5115	13123	17653	7720	10975
Total	100	100	100	100	100	100	100	100	100	100	100	100
EU-27	80.4	79.7	78.1	75.4	75.4	76.1	75.4	75.3	59.1	56.6	55.9	56.4
Estonia	–	–	–	–	7.8	7.1	7.2	6.6	2.6	2.9	2.6	2.8
Latvia	10.5	10.8	11.3	10.6	–	–	–	–	6.4	6.3	6.0	6.4
Lithuania	10.9	7.7	8.2	7.9	16.4	16.3	16.0	16.7	–	–	–	–
Poland	5.7	6.4	5.7	6.8	8.0	7.5	7.7	7.2	10.0	8.9	8.9	8.9
Finland	14.4	14.9	14.8	11.6	3.7	4.7	5.0	4.7	1.9	1.8	1.7	1.9
Germany	10.7	11.3	11.0	10.3	11.3	11.4	11.3	11.9	11.3	10.5	10.3	10.0
Sweden	8.4	10.9	10.0	10.7	3.5	3.5	3.7	3.8	2.7	3.3	3.3	3.6
UK	2.2	2.0	1.8	3.0	1.8	1.8	1.6	2.7	1.7	1.6	1.5	1.6
France	2.6	1.8	1.7	1.6	3.1	3.2	3.3	2.4	2.5	2.6	2.7	2.6
Italy	2.3	2.4	2.2	2.1	3.9	3.9	3.8	3.9	3.8	3.3	3.1	3.1
Spain	1.0	0.7	0.8	0.6	1.4	1.3	1.2	1.2	1.5	1.2	1.4	1.2
Denmark	2.4	1.9	2.0	1.5	2.7	2.3	2.4	2.3	2.2	1.7	1.9	1.8
Netherlands	3.5	3.3	3.4	3.2	4.0	3.9	4.3	3.7	4.1	4.5	4.1	5.2
Belgium	2.1	1.7	1.8	1.6	1.5	1.7	1.8	2.1	3.0	3.3	3.5	3.2
Extra EU-27	19.6	20.3	21.9	24.6	24.6	23.9	24.6	24.7	40.9	43.4	44.1	43.6
Norway	1.3	1.3	2.0	1.4	1.3	1.0	0.7	0.6	0.5	0.3	0.4	0.4
US	1.3	0.9	1.0	1.6	0.8	0.5	0.6	0.7	1.1	1.0	1.0	1.4
Russia	8.1	8.1	10.0	10.3	10.7	9.9	10.6	9.7	29.9	32.6	33.5	32.3

[1)] Data provided in compliance with Balance of Payments Methodology

Source: Eurostat

Table A7

EXPORTS OF GOODS BY COMMODITY GROUP, FOB PRICES, %

CN section	CN section	Estonia				Latvia				Lithuania			
		2009	2010	2010 I H	2011 I H	2009	2010	2010 I H	2011 I H	2009	2010	2010 I H	2011 I H
1–22	Total, EUR million[1]	6489	8753	3851	5919	5522	7190	3167	4338	11797	15651	6838	9613
1–22	Total	100	100	100	100	100	100	100	100	100	100	100	100
1–4	Food and beverages, tobacco products	10.5	9.7	9.5	7.5	18.8	18.0	16.9	14.5	19.6	18.0	16.3	16.0
5	Mineral products	17.0	15.8	18.9	19.7	5.4	5.8	6.2	8.1	21.5	23.6	24.1	24.3
6	Products of chemical or allied industries	5.5	4.5	4.5	3.8	8.3	7.4	7.8	8.8	9.1	8.1	8.3	9.6
7	Plastics, rubber and articles thereof	3.1	3.2	3.2	2.8	2.8	3.3	3.2	3.0	6.8	6.8	7.4	6.3
9	Wood and articles of wood	8.7	9.1	9.9	8.0	15.8	17.9	18.9	17.2	3.3	3.5	3.6	3.5
10	Pulp, paper and articles thereof	3.3	3.2	3.3	2.6	1.7	2.0	1.9	1.9	1.6	1.9	1.8	1.8
11	Textiles and textile articles	4.0	3.5	3.7	2.9	4.9	4.5	4.5	4.4	6.4	6.0	6.1	5.4
13	Articles of stone, cement; ceramic products; glass and glassware	1.8	1.6	1.7	1.3	1.9	1.8	1.9	2.1	0.9	0.9	0.9	0.8
15	Base metals and articles of base metals	8.6	9.1	9.4	8.2	12.4	14.0	13.5	15.0	4.5	4.5	4.4	4.7
16	Machinery and mechanical appliance; electrical equipment	19.6	22.6	19.1	27.7	15.7	14.3	13.7	13.8	10.0	10.4	9.9	9.7
17	Vehicles, aircraft, vessels and associated transport equipment	6.5	6.5	5.5	5.1	6.6	5.8	6.3	6.2	7.3	7.8	8.6	9.8
18	Optical, precision, medical instruments; parts and accessories thereof	1.8	1.9	1.9	2.1	1.0	1.2	1.1	1.2	1.7	1.6	1.6	1.6
20	Furniture, toys	8.3	7.6	8.0	6.6	3.4	3.0	3.1	2.5	6.4	5.8	6.0	5.4
8, 12, 14, 19, 21, 22	Other	1.2	1.6	1.4	1.7	1.1	1.1	1.1	1.2	0.9	1.0	1.0	1.1

[1] Data provided in compliance with Balance of Payments Methodology

Source: Eurostat

Table A8

IMPORTS OF GOODS BY COMMODITY GROUP, CIF PRICES, %

CN section	CN section	Estonia				Latvia				Lithuania			
		2009	2010	2010 I H	2011 I H	2009	2010	2010 I H	2011 I H	2009	2010	2010 I H	2011 I H
1–22	Total, EUR million[1]	7272	9242	4200	6257	7034	8819	3788	5115	13123	17653	7720	10975
1–22	Total	100	100	100	100	100	100	100	100	100	100	100	100
1–4	Food and beverages, tobacco products	12.9	11.1	11.2	9.3	18.7	16.7	17.4	15.1	14.7	13.1	13.1	12.4
5	Mineral products	19.5	17.5	20.2	20.5	16.3	14.5	15.1	16.3	29.0	33.3	33.6	34.3
6	Products of chemical or allied industries	9.5	8.0	8.4	7.0	11.5	11.0	12.3	10.7	12.3	11.0	11.9	10.5
7	Plastics, rubber and articles thereof	5.4	5.6	5.5	4.8	4.9	5.5	5.6	5.4	4.5	4.5	4.5	4.3
9	Wood and articles of wood	2.6	2.8	2.9	2.5	1.7	1.9	2.0	1.9	1.5	1.4	1.5	1.4
10	Pulp, paper and articles thereof	2.8	2.4	2.4	1.8	2.8	2.7	2.9	2.5	2.4	2.3	2.3	2.1
11	Textiles and textile articles	5.4	5.0	5.2	4.1	4.8	4.5	4.5	4.4	5.0	4.5	4.6	4.0
13	Articles of stone, cement; ceramic products; glass and glassware	1.8	1.6	1.5	1.3	2.0	1.7	1.7	1.6	1.3	1.1	1.1	1.1
15	Base metals and articles of base metals	7.7	9.0	8.7	8.8	8.3	10.6	10.2	11.8	5.0	4.9	4.9	5.1
16	Machinery and mechanical appliance; electrical equipment	19.2	23.5	20.0	26.7	16.6	17.0	16.3	16.5	13.2	12.6	11.6	11.9
17	Vehicles, aircraft, vessels and associated transport equipment	6.2	7.1	7.3	8.2	6.2	6.9	6.0	8.3	6.5	7.6	7.2	9.4
18	Optical, precision, medical instruments; parts and accessories thereof	2.0	1.9	1.9	1.6	1.7	1.7	1.6	1.6	1.5	1.3	1.3	1.3
20	Furniture, toys	2.6	2.2	2.2	1.7	2.5	2.5	2.6	2.2	1.6	1.3	1.3	1.1
8, 12, 14, 19, 21, 22	Other	2.2	2.4	2.5	1.7	1.9	2.8	1.6	1.4	1.3	1.1	1.1	1.0

[1] Data provided in compliance with Balance of Payments Methodology

Source: Eurostat

Table A9

EXPORTS OF SERVICES, %

	Estonia				Latvia				Lithuania			
	2009	2010	2010 I H	2011 I H	2009	2010	2010 I H	2011 I H	2009	2010	2010 I H	2011 I H
Services, EUR million	3174	3422	1567	1777	2747	2763	1292	1455	2657	3115	1441	1771
Services	100	100	100	100	100	100	100	100	100	100	100	100
Transportation	36.8	39.3	39.4	41.2	50.6	49.2	51.8	52.5	56.6	58.7	60.5	62.0
Travel	24.6	23.6	23.1	23.0	18.7	17.4	15.6	15.7	27.2	25.0	23.5	23.4
Other services	38.6	37.1	37.5	35.8	30.6	33.4	32.4	31.8	16.3	16.4	16.0	14.5
Communications services	4.3	4.4	4.8	4.3	2.7	2.6	2.8	2.3	2.8	2.8	3.0	2.2
Construction services	4.8	4.7	4.1	5.1	0.9	2.1	2.0	1.5	1.8	2.1	1.8	2.1
Insurance services	0.3	0.2	0.3	0.2	0.7	0.7	0.5	0.8	0.0	0.1	0.1	0.0
Financial services	1.6	2.0	2.1	2.2	6.4	6.2	6.6	6.5	1.1	0.9	1.1	0.7
Computer and information services	4.2	4.5	4.8	4.4	3.3	3.6	3.6	3.8	1.1	1.0	1.0	1.0
Royalties and licence fees	0.6	0.5	0.4	0.5	0.1	0.3	0.3	0.3	0.0	0.0	0.0	0.0
Other business services	21.5	19.5	19.7	17.9	15.4	16.6	15.8	15.1	7.6	8.0	7.4	6.9
Personal, cultural and recreational services	0.3	0.3	0.3	0.3	0.1	0.4	0.3	0.7	0.5	0.4	0.3	0.3
Government services	1.0	0.9	1.0	1.0	0.9	0.9	0.9	1.0	1.4	1.3	1.3	1.2

Source: Eurostat

Table A10
IMPORTS OF SERVICES, %

	Estonia				Latvia				Lithuania			
	2009	2010	2010 I H	2011 I H	2009	2010	2010 I H	2011 I H	2009	2010	2010 I H	2011 I H
Services, EUR million	1815	2109	985	1220	1625	1666	743	854	2140	2141	1008	1255
Services	100	100	100	100	100	100	100	100	100	100	100	100
Transportation	32.3	34.7	34.2	37.1	25.3	29.6	28.9	30.9	37.2	50.1	46.9	59.1
Travel	23.9	22.5	23.4	21.6	35.2	29.1	28.7	27.5	37.7	28.0	31.1	21.2
Other services	43.9	42.8	42.4	41.1	39.5	41.2	42.4	41.6	25.1	21.9	22.0	19.7
Communications services	6.8	7.1	7.5	6.2	4.6	4.6	4.8	4.8	3.7	4.3	4.4	3.5
Construction services	4.3	3.8	3.2	5.9	4.1	3.1	4.6	2.5	4.5	1.0	1.9	0.4
Insurance services	0.0	0.1	0.0	0.2	1.1	1.1	1.7	1.5	0.9	1.4	1.3	1.2
Financial services	1.4	1.8	1.7	1.1	3.6	5.0	3.2	6.9	0.8	0.6	0.5	0.5
Computer and information services	3.5	3.4	3.4	3.1	4.4	4.5	4.6	4.6	1.2	1.4	1.3	1.0
Royalties and licence fees	1.8	2.1	1.6	2.0	1.0	1.4	1.5	2.0	0.9	1.2	1.2	1.0
Other business services	24.1	23.0	23.4	21.5	18.8	20.3	21.0	17.7	8.0	7.6	6.6	8.4
Personal, cultural and recreational services	0.5	0.4	0.5	0.4	0.9	0.7	0.8	0.7	0.3	0.4	0.4	0.3
Government services	1.4	1.0	1.0	1.0	0.7	0.8	0.8	0.7	4.7	4.1	4.4	3.6

Source: Eurostat

Table A11
FOREIGN DIRECT INVESTMENT STOCK BY ECONOMIC ACTIVITIES, END OF PERIOD,[1] %

NACE 2	Activity	Estonia			Latvia			Lithuania		
		2009	2010	2011 I H	2009	2010	2011 I H	2009	2010	2011 I H
	Total, EUR million	11654	12302	12979	7998	8108	9005	9560	10297	10706
	Total	100	100	100	100	100	100	100	100	100
a	Agriculture, forestry and fishing	0.7	1.1	1.4	2.6	2.7	2.5	0.9	0.9	0.9
b	Mining and quarrying	0.5	0.5	0.5	0.6	0.6	0.5	0.2	0.5	0.5
c	Manufacturing	13.9	16.1	16.5	11.5	12.6	12.7	27.0	28.0	30.5
d, e	Electricity, gas and water	3.2	4.1	4.2	3.4	3.8	4.5	8.2	8.8	7.8
f	Construction	2.7	2.0	1.5	2.2	1.9	1.4	3.1	3.0	3.0
g	Wholesale and retail trade; repair of motor vehicles and motorcycles	12.2	11.4	14.1	13.4	12.0	12.1	13.8	13.4	13.6
h	Transportation and storage	4.7	5.4	5.3	4.2	4.2	3.9	2.0	2.2	2.2
i	Accommodation and food service activities	0.6	0.5	0.5	1.1	0.7	0.8	0.7	0.7	0.5
j	Information and communication	2.1	3.0	2.5	3.4	3.1	2.8	10.4	10.7	10.1
k	Financial and insurance activities	32.0	31.3	28.7	29.1	23.5	23.4	14.9	12.4	11.8
l	Real estate activities	11.1	12.2	13.9	13.3	15.8	16.5	11.9	12.4	11.8
	Other	15.3	12.3	11.3	15.3	19.2	18.9	6.7	7.1	7.5

[1] Bank of Latvia publishes this data according to NACE1, therefore in this table the estimates of FDI structure are stated

Source: Eurostat, national central banks

Table A12

FOREIGN DIRECT INVESTMENT STOCK BY COUNTRIES, END OF PERIOD, %

	Estonia			Latvia			Lithuania		
	2009	2010	2011 I H	2009	2010	2011 I H	2009	2010	2011 I H
Total, EUR million	11654	12302	12979	7998	8108	9005	9560	10297	10706
Total	100	100	100	100	100	100	100	100	100
Estonia	–	–	–	16.9	14.2	14.0	7.6	6.1	6.6
Latvia	0.8	0.9	1.0	–	–	–	4.3	3.8	3.3
Lithuania	1.4	1.9	2.1	3.4	3.1	2.9	–	–	–
Poland	0.1	0.3	0.4	0.1	0.1	0.1	10.8	11.4	13.9
Denmark	1.8	2.5	1.8	6.9	7.0	4.3	10.2	10.4	5.1
Finland	22.1	23.4	24.1	4.1	4.5	4.2	4.8	4.8	5.2
Germany	1.5	2.4	2.2	6.4	5.2	5.3	10.4	11.0	10.5
Sweden	38.6	35.0	33.3	13.8	12.9	14.9	9.2	8.9	12.1
United Kingdom	2.3	2.0	2.0	2.0	2.2	2.9	1.7	1.2	1.3
France	1.5	1.8	1.8	0.7	0.7	0.6	2.3	2.5	2.0
Netherlands	8.9	8.9	8.4	5.7	6.7	6.6	7.8	8.8	9.5
Belgium	0.4	0.4	0.1	0.5	0.2	0.4	0.6	0.6	0.6
Luxembourg	1.6	1.8	1.9	2.5	3.4	2.3	2.2	2.7	1.8
Ireland	1.0	0.7	0.8	4.7	4.0	4.2	0.9	0.5	0.5
Austria	1.1	1.1	1.0	2.3	2.0	2.0	0.7	0.6	0.5
Italy	0.4	0.6	0.6	0.4	0.5	0.6	0.2	0.1	0.1
Cyprus	2.6	2.7	2.9	4.1	4.9	5.1	2.6	3.1	3.4
Norway	3.4	2.9	4.9	3.0	3.1	4.7	3.8	3.3	5.1
Switzerland	1.2	1.0	1.2	1.1	1.8	1.6	2.6	2.5	2.5
United States	1.5	1.6	1.7	3.8	3.2	2.9	2.7	1.4	1.5
Russian Federation	3.5	3.5	3.4	4.6	4.1	4.4	6.5	8.2	6.6
Other countries	4.4	4.5	4.5	13.0	16.4	16.2	8.2	8.3	8.1

Source: Eurostat, national central banks

Table A13

INVESTMENT IN TANGIBLE ASSETS BY ASSET CLASS, %

	EU-27				Estonia				Latvia				Lithuania			
	2009	2010	2010 I H	2011 I H	2009	2010	2010 I H	2011 I H	2009	2010	2010 I H	2011 I H	2009	2010	2010 I H	2011 I H
Total, EUR million	2226002	2260957	1084328	1133967	2973	2694	1179	1446	3997	3510	1152	1457	4578	4486	1686	2243
Total	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
Metal products and machinery	24.7	25.6	24.9	25.7	25.3	31.0	31.6	34.8	24.4	27.4	43.1	47.8	20.2	22.0	23.0	25.2
Transport equipment	8.7	9.5	10.1	10.0	3.4	10.0	11.1	19.6	6.2	7.2	10.9	12.1	3.8	7.2	5.3	11.1
Construction work: housing	26.0	25.3	25.3	25.3	16.6	17.4	17.8	16.2	14.7	10.2	9.0	7.6	19.2	11.4	12.5	10.9
Construction work: other constructions	31.6	30.4	30.6	29.8	51.5	38.3	36.0	26.7	51.8	51.7	31.8	26.7	48.7	50.1	47.8	44.2
Other products	9.0	9.2	9.1	9.2	3.2	3.3	3.5	2.7	2.9	3.5	5.2	5.8	8.1	9.3	11.4	8.6

Source: Eurostat

Table A14

REVENUES, EXPENDITURE AND SURPLUS/DEFICIT OF GENERAL GOVERNMENT, AS PERCENTAGE OF GDP

	Estonia				Latvia				Lithuania			
	2009	2010	2010 I H	2011 I H	2009	2010	2010 I H	2011 I H	2009	2010	2010 I H	2011 I H
Total revenue	43.2	40.9	39.0	38.2	34.6	36.1	37.4	37.1	34.3	33.8	33.0	31.2
Taxes	22.3	20.7	19.4	19.2	17.9	18.7	19.5	19.0	17.4	16.5	16.0	15.9
Indirect taxes	14.7	13.9	13.6	13.2	10.7	11.3	11.5	11.2	11.4	11.8	11.8	11.8
Direct taxes	7.6	6.8	5.8	6.0	7.2	7.4	8.0	7.8	6.0	4.7	4.2	4.1
Social contributions	13.3	13.3	14.2	12.7	8.9	8.6	9.0	9.3	12.1	10.7	11.1	10.4
Other revenue	7.6	6.9	5.4	6.3	7.8	8.8	8.8	8.7	4.8	6.6	5.9	4.9
Total expenditure	45.2	40.6	42.8	36.9	44.2	44.4	42.5	37.8	43.8	40.9	41.4	37.4
Gross fixed capital formation	5.2	3.9	2.6	0.6	4.4	4.4	3.4	3.2	3.9	4.6	2.8	2.9
Social benefits	16.0	14.9	16.0	14.1	13.6	13.6	14.5	12.3	17.2	14.9	15.8	14.0
Other expenditure	24.0	21.8	24.2	22.2	26.2	26.4	24.6	22.3	22.7	21.4	22.7	20.5
Net lending (+) / net borrowing (−)[1]	−2.0	0.3	−3.8	1.3	−9.6	−8.2	−5.1	−0.7	−9.5	−7.1	−8.3	−6.3

[1] Due to the methodological disparities between ESA95 and excessive deficit procedure, the difference between total government revenue and expenditure is not in all cases equal to net lending (+) / net borrowing (−)

Source: Eurostat

Abbreviations

CAB	Current account balance
CAD	Current account deficit
Cif	Cost insurance and freight – the pricing term indicating that the cost of the goods, insurance, and freight are included in the quoted price
CIS	Commonwealth of Independent States
DI	Direct investment
ECB	European Central Bank
E-o-p	End of period
EU	European Union, here the EU-27
EU-27	EU since January 2007
EURIBOR	Euro Interbank Offered Rate
Eurostat	Statistical Office of the European Commission
Fob	Free on board – the pricing term of exports and imports of goods indicating the market value of the goods at the point of uniform valuation (the customs frontier of the economy from which they are exported)
FDI	Foreign direct investment
FTB	Foreign trade balance
GDP	Gross domestic product
HICP	Harmonized index of consumer prices
LFS	Labour force survey
NACE	Classification of economic activities in the European Community
Qoq	quarter-on-quarter
PPI	Producer price index
PPS	Purchasing power standards
RIGIBOR	Riga Interbank Offered Rate
Sa	Seasonally adjusted
Sq. m	Square meters
TALIBOR	Tallinn Interbank Offered Rate
VAT	Value added tax
VILIBOR	Vilnius Interbank Offered Rate
Yoy	year-on-year

Symbols in the tables:

:	no data available
–	the ratio has no sense

Terms

Unemployment rate	the number of unemployed as a percentage of labour force (*working age population*), as according to Labour force survey data
Youth unemployment	unemployment of those up to 24 years old
Vacancy	vacancy rate of real estate premises – the ratio between vacant and gross letable area of real estate premises, %

Sources of statistical data

Statistical data for the EU are provided by Eurostat, ECB Data Warehouse, national statistics offices, ministries of finance and economy and national central banks of individual countries. Additional sources: commercial data provider *Reuters EcoWin*, *Bloomberg*, statistics on the real estate markets is provided by national land and real estate registers, various real estate agencies and advisors.