VALSTYBĖS KONTROLĖ
BUDGET POLICY MONITORING

To the Seimas of the Republic of Lithuania

OPINION ON THE ENDORSEMENT OF THE ECONOMIC DEVELOPMENT SCENARIO

5 July 2023 No BPE–4

Vilnius

GROWING INVESTMENT AND A STABLE LABOUR MARKET WILL CONTRIBUTE TO A LOWER CONTRACTION OF THE LITHUANIAN ECONOMY IN 2023 COMAPARED TO THAT OBSERVED AT THE BEGINNING OF THE YEAR

The National Audit Office, implementing the functions of the fiscal institution (hereinafter – Fiscal Institution in the NAO), submits to the Seimas its opinion on the Economic Development Scenario (hereinafter – the EDS) for 2023–2026 published by the Ministry of Finance in June.

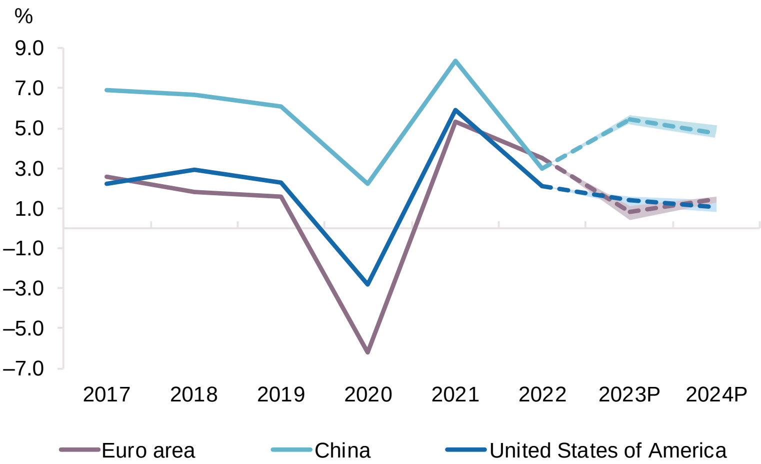
The year 2023 has started with a larger-than-expected economic downturn and after two consecutive quarters of contraction, Lithuania entered a technical recession. In the first quarter of 2023, GDP was negatively affected by a decline in external demand in 2023, which led to a contraction of the industrial sector. Lithuania's small and open economy is highly dependent on its trading partners, and the slowdown in the development of export markets is expected to have a negative impact on Lithuania's international trade. However, the second half of the year is expected to be more favourable for economic growth, avoiding a more severe downturn. Investment and a stable labour market will contribute to this development. Rising wages and slowing inflation will keep household consumption from falling. Public investment can also contribute to the strengthening of the resilience of the economy and ensuring energy independence.

1. **The economies of Lithuania's main export partners will slow down in 2023, with a recovery expected in 2024.**
2. **The decreased external demand led to a stronger-than-expected economic contraction in Q1 2023.**
3. **In the face of declining exports, investment and a favourable labour market will mitigate the GDP contraction in 2023.**
4. **More favourable population projections and the increased influence of the capital factor drive the potential GDP growth projected by the Fiscal Institution in the NAO for 2023–2026.**
5. **The National Audit Office of Lithuania, implementing the functions of the fiscal institution endorses the Economic Development Scenario, but persisting risks could affect economic development.**

1. THE ECONOMIES OF LITHUANIA'S MAIN EXPORT PARTNERS WILL SLOW DOWN IN 2023, WITH A RECOVERY EXPECTED IN 2024.

International institutions provide similar assessments of the growth prospects for the world's major economies in 2023 (Figure 1). The favourable global growth performance in Q1 2023 was underpinned by the continued resilience of the US labour market and, albeit more sluggish than expected, – by China's economic recovery. The euro area (EA) also contributed to this result, with a smaller-than-expected economic contraction. On the other hand, data for May shows deterioration in consumer and business expectations in the world's major economies, implying a possible slowdown in growth between 2023 and 2024. The Purchasing Managers' Index (PMI) for May showed growth in the services sector, supported by strong demand, and a persistent contraction in the manufacturing sector (Annex 1, Figure 1).

Figure 1. International institutions project slowing US and Chinese growth in 2024 and accelerating EA growth*



* The dashed lines and the background around them represent the average of the projections of the international institutions and their distribution.

Source: European Commission, Organisation for Economic Cooperation and Development, International Monetary Fund, World Bank, calculations by the National Audit Office implementing the functions of a fiscal institution

- **As the US labour market shows resilience, the challenges to its economic development continue.** In the first quarter of 2023, the US annual growth (1.3%) was mainly driven by rising household spending. Consumers' and businesses' expectations in Q1 were negatively affected by the prevailing uncertainty about the increase in the government debt ceiling. The contraction in the manufacturing PMI in May 2023 was driven by falling demand. Although in May, the unemployment rate rose the most since the start of the pandemic, the increase in job vacancies was the largest since January. Wage growth also slowed down, while inflation continued to decline reaching 4.0%. The US central bank paused its interest rate hike in June, but considers extending it.
- **China's economic recovery remains sluggish.** In Q1 2023, China's economy grew by 4.5%. This was due to the recovery of the services sector driven by rising consumption opportunities since the beginning of the year and the strengthening of the industrial sector. On the other hand, the weaker-than-expected domestic consumption, the real estate market which remains sluggish and the risk of continued deflation are negatively weighing on expectations of a rapid recovery in China. The Chinese government's considerations of possible decisions on additional support measures for the real estate market and the domestic demand, as well as the central bank's decision to keep interest rates low, are indicative of the desire to stimulate the Chinese economy.

- **Weak domestic demand and continuing low consumer and business expectations reflect the prevailing uncertainty about the economic development of the euro area in 2023.** In the first half of 2023, a weakening of supply chain disruption, falling inflation (6.1% in May) and labour market resilience (the unemployment rate was 6.5% in April) was observed. Electricity and gas prices have returned to their early 2021 levels (Annex 1, Figure 2). Compared to Q4 2022, the EA economy contracted by 0.1% in Q1 2023, which was mainly due to declining household and government spending. Weak demand, both domestic and external, and the resulting decline in the number of orders continue to have a negative impact on EA industry expectations. The economy of Germany, Lithuania's main export partner, contracted in Q1, mainly due to a contraction in government and household consumption spending. European Central Bank's (ECB) further interest rate increase due to persistently high inflation remains a challenge. The Recovery and Resilience Facility (RRF) can make a positive contribution to the development of the EA economy.

The EDS projections for June reflect a slower development of Lithuania's main export partners compared to 2022 (Table 1). When publishing its forecasts for economic development in May 2023, the European Commission (EC) updated the assumptions which the Ministry of Finance uses to draft the EDS. The EC estimates that the exchange rate of the euro against the US dollar will remain stable over the medium term. In view of the uncertainty about further interest rate hikes by the US central bank and the ECB, futures contracts point to a slight appreciation of the euro against the US dollar (Annex 1, Table 1). This would lead to cheaper imports of raw materials into the EU. The EC's technical assumption for 2023–2026 shows that the oil price will remain at a similar level. On the other hand, Brent oil futures point to a decline in the price, driven by expectations of slower global economic growth in the medium term (Annex 1, Figure 2). In May, the European Commission provides better assumptions for global and EU growth in 2023 compared to its March forecasts. The expected slower expansion of the main export partners in 2023 compared to 2022 will slow down the growth of Lithuania's external demand. As domestic consumption by the main trading partners stabilises, a recovery is expected as from 2024.

Table 1. Assumptions for the Economic Development Scenario of the Ministry of Finance for June 2023

Indicator	2022	2023P	2024P	2025P	2026P
USD/EUR exchange rate*	1.05	1.09 (1.08) ▲	1.10 (1.09) ▲	1.10 (1.09) ▲	1.10 (1.09) ▲
Global (excl. EU) GDP growth, %*	3.2	3.1 (3.0) ▲	3.3 (3.3)	3.3 (3.3)	3.3 (3.3)
European Union’s GDP growth, %*	3.5	1.0 (0.8) ▲	1.7 (1.6) ▲	1.7 (1.6) ▲	1.7 (1.6) ▲
Growth of the main Lithuania's export markets, %	3.4	1.8 (1.6) ▲	2.3 (2.2) ▲	2.3 (2.2) ▲	2.3 (2.2) ▲
Oil prices (*Brent*, USD/barrel)*	100.7	76.3 (84.8) ▼	72.1 (79.9) ▼	72.1 (79.9) ▼	72.1 (79.9) ▼

* Technical assumption made public by the EC on 15 May 2023.

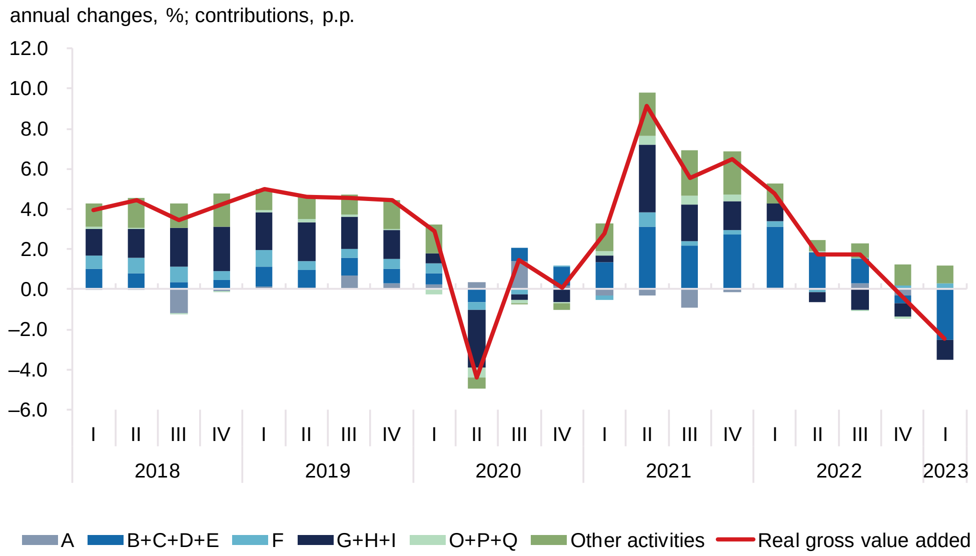
The EDS assumptions for March 2023 are presented in brackets.

Source: Ministry of Finance

2. THE DECREASED EXTERNAL DEMAND LED TO A STRONGER-THAN-EXPECTED ECONOMIC CONTRACTION IN Q1 2023.

The Lithuanian economic development was worse than expected in Q1 2023. The real GDP contracted by 2.5% in Q1 2023 compared to the same period of last year.[1] Exports and household consumption had a negative impact on the downturn, while investment positively contributed to GDP growth. Manufacturing (–8.5%) contributed the most to a drop in the gross value added, with the contraction in the chemical and wood products industries, furniture and metal products having the largest negative impact on its results. Gross value added was also reduced by poor performance of domestic trade and transport activities (Figure 2). It was observed that not all businesses face economic difficulties. Some manufacturing activities (electrical equipment; computer, electronic and optical products; motor vehicles) have increased their output rapidly. The main contributors to gross value added were growth in the value of information and communication, financial and insurance services.

Figure 2. The fall in the real gross value added was driven by the decline in industry, trade, transport and storage, accommodation and food activities in Q1 2023[2]



Source: State Data Agency, calculations by the National Audit Office implementing the functions of a fiscal institution

The negative economic performance in Q1 2023 was also driven by a high base effect: in the same period last year, manufacturing (excluding refined petroleum products) demonstrated a double-digit annual growth rate of 17.8% in Q1 2022 (Annex 2).

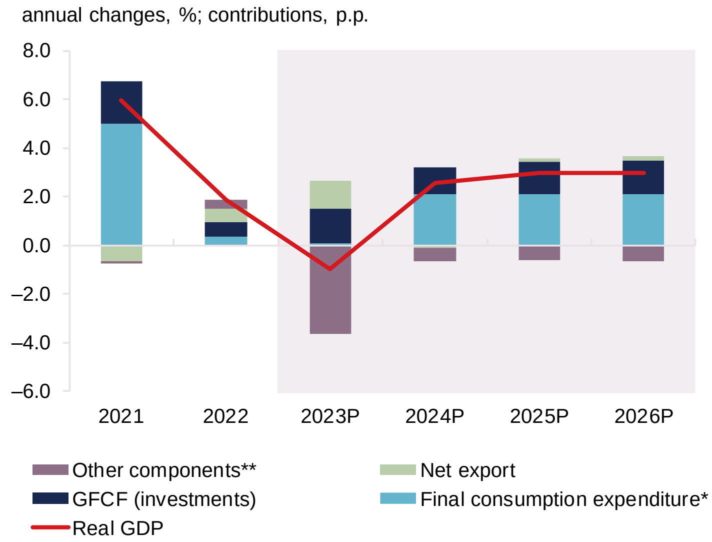
[1] The opinion uses data of GDP of 31/05/2023 and its contributions according to the production and expenditure method.

[2] A - Agriculture, forestry and fishing, B+C+D+E - Mining and quarrying; manufacturing; electricity, gas, steam and air conditioning supply; water supply; sewerage, waste management and remediation activities, F - Construction, G+H+I - Wholesale and retail trade; repair of motor vehicles and motorcycles; transportation and storage; Accommodation and food service activities, O+P+Q - Public administration and defence; compulsory social security; education; human health and social work activities, Other activities - Information and communications; financial and insurance activities; real estate activities; professional, scientific and technical activities; administrative and support service activities; arts, entertainment and recreation activities; repair of household goods and other services.

3. IN THE FACE OF DECLINING EXPORTS, INVESTMENT AND A FAVOURABLE LABOUR MARKET WILL MITIGATE THE GDP CONTRACTION IN 2023.

Lower-than-last-year raw material and energy resource prices will facilitate the development of the Lithuanian economy in the second half of 2023, but the remaining uncertainties about prices and external demand do not allow to expect strong GDP growth. The base effect, which had a negative impact on annual growth in Q1, will have a weaker impact thereafter. The EDS for June projects that the real GDP will contract by 1.0% in 2023 (Figure 3). Investment and net exports are projected to have a positive impact on the domestic economy, while changes in inventories are expected to be negative. The real GDP is projected to grow by 2.5% in 2024 as the economy recovers. In the medium term, Lithuania's economic development will be highly dependent on external demand, both in the EA and in other export partners.

Figure 3. In June, the EDS projects that the contraction in real GDP in 2023 will be mitigated by investment and net exports, with economic growth projected in the medium term



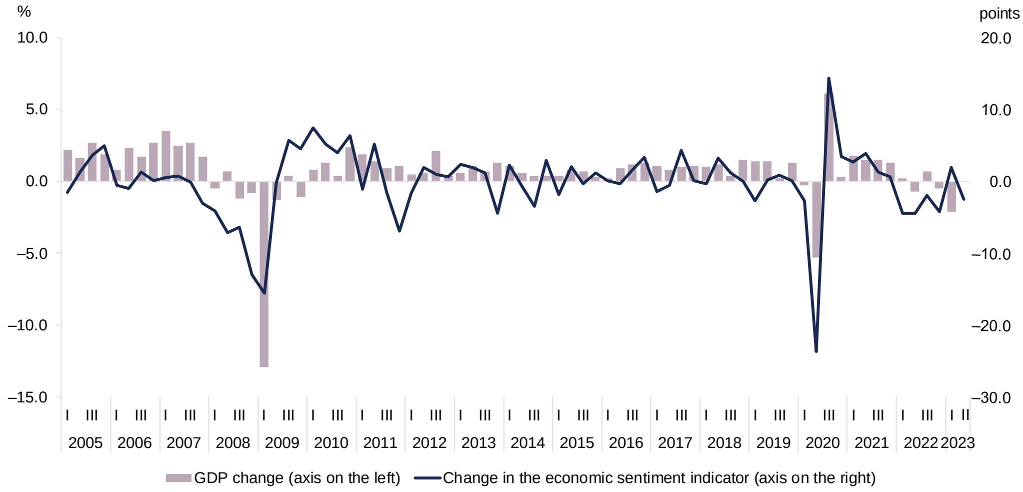
* Excluding NPISH, ** NPISH, changes in inventories, acquisitions less disposals/transfers

Source: State Data Agency, Ministry of Finance, calculations by the National Audit Office implementing the functions of a fiscal institution

Trends in business expectations are a good reflection of GDP developments in periods of downturn or uncertainty. It was observed that in Q1 2023, the GDP contraction was significant compared to the previous quarter (2.1% seasonally and working day adjusted). The current economic situation can be defined as a technical recession, where GDP falls for two consecutive quarters. Meanwhile, the negative volatility of the economic sentiment indicator in January–June has been significantly lower than in 2008/2009 or 2020 (Figure 4). It should be noted that a growth was observed in manufacturing (excluding refined petroleum products) and retail trade[3] in March–April 2023, seasonally and working day adjusted, while the value of construction works carried out in the country is rising from December 2022 onwards. Given the slightly better performance of the indicators in recent months, the second half of the year is expected to be more favourable for the country's economic development, averting a severe economic downturn in 2023.

[3] Except for the sale of motor vehicles and motorcycles; the sale of automotive fuels.

Figure 4. Business expectations do not show a strong economic downturn in Lithuania in 2023[4]



Source: European Commission, State Data Agency, calculations by the National Audit Office implementing the functions of a fiscal institution

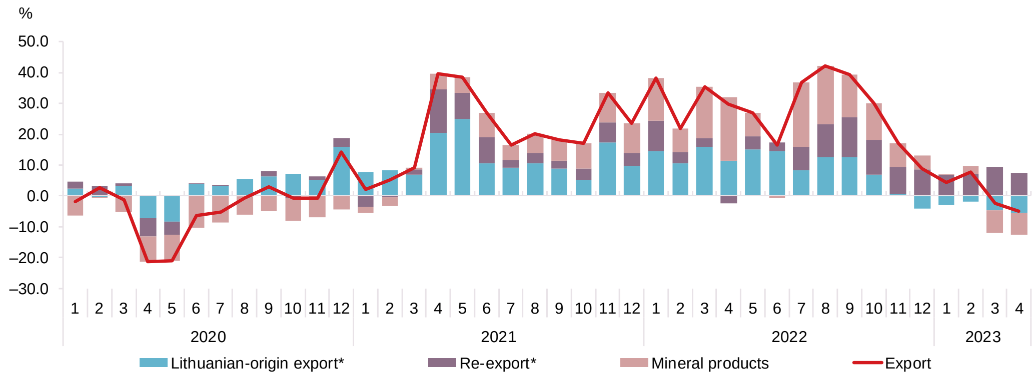
With a significant slowdown in external demand, a drop in Lithuania's real exports of goods and services is projected in 2023. Rising interest rates and a decline in the purchasing power of the households in 2022 have a negative impact on the manufacturing and retail trade of Lithuania's main export partners. In January–April 2023, the value of exports of goods of Lithuanian origin (excluding mineral products) fell by 7.3% during the year[5] (Figure 5). This was mainly due to a contraction in exports of chemical products, furniture, iron and steel and wood and wood products. Upon the change in the structure of re-exports in 2022,[6] the growth of exports in this category continues. In January–April 2023, the value of re-exports (excluding mineral products) grew by 25.3% during the year. The value of exports of services grew by almost a third in the same period. Challenges are likely to persist in industrial sectors vulnerable to energy prices, while the slowdown in external demand is likely to continue to have a negative impact on the export of Lithuanian-origin goods in 2023. It may be dampened by the drought-induced decline in cereal harvests. However, with continued opportunities for international trade with Eastern countries, re-exports are likely to mitigate the contraction in exports of goods this year. The June's EDS projects real exports of goods and services to fall by 0.7% in 2023.

[4] The analysis uses the economic sentiment indicator (ESI), seasonally adjusted, and GDP, seasonally and working day adjusted. The quarterly ESI is obtained by taking the average of the three respective months. The change in the ESI compared to the previous quarter is calculated by subtracting the value of quarter t-1 from the value of quarter t.

[5] The revision of data of 2022 of international trade in goods of 23/06/2023 was not taken into account.

[6] Re-export flows to Russia have contracted significantly, but have increased significantly to other member states of the Commonwealth of Independent States, especially to Belarus, Kazakhstan and Kyrgyzstan. The most significant growth was in re-exports of land vehicles, parts, other machinery and equipment.

Figure 5. Re-exports mitigated the annual drop in the value of goods exports in January–April 2023



* Excluding mineral products

Source: State Data Agency, calculations by the National Audit Office implementing the functions of a fiscal institution

The value of goods imports (excluding mineral products) increased by 3.3% in January-April 2023 compared to the same period of last year. This was driven by rising import prices and re-exports. However, imports of raw materials important for industry, such as iron and steel, organic chemicals and timber, declined. The value of imports of mineral products also fell in line with the fall in oil prices. Real imports of goods and services are projected to fall by 2.0% in 2024–2026, reflecting sluggish developments in industry and private consumption. A growth in real exports and imports of goods and services is expected as external and domestic demand recovers in 2024–2026 (Annex 3).

With uncertainty constraining the investment decisions of some private sector firms, a positive impact on investment in 2023 is expected from the implementation of public sector projects. In Q1 2023, the annual change in gross fixed capital formation (investment) was significant reaching 12.3%. This growth was mainly positively influenced by an increase in expenditure on other buildings and structures and machinery and equipment. With the industrial capacity utilisation rate reaching 69.3% in May 2023 (8.4% p.p. lower than a year ago), new investment decisions may be made more cautiously, which would have a negative impact on the dynamics of gross fixed capital formation. In terms of tangible investment, data at current prices show a 69.1% increase in investment expenditure in the public sector in Q1 2023 compared to the same period last year, and a 26.7% increase in the private sector. Taking into account the actual investment developments at the beginning of the year, the continuation of favourable trends in the public sector, together with the efficient use of financial flows from both the 2014–2020 and the 2021–2027 EU Multiannual Financial Framework and the RRF, the growth in the gross fixed capital formation is expected to reach 6.3% in 2023 (Annex 3).

With inflation declining at a slower pace than expected at the time of preparing March EDS, the 2023 HICP growth projection was revised upwards. Growth in the Harmonised Index of Consumer Prices (HICP) is projected to slow to 8.9% in 2023. This estimate is 0.4 percentage points higher than the one published in the March EDS. Although prices dropped in May compared to April, the persistently high annual inflation is driven by a sharp rise in price levels in the second half of 2022. The deceleration of inflation will be affected by falling energy prices, the high base formed in 2022 and the slowing economic expansion. Despite the HICP growth which was projected to be higher in 2023, the projection for the GDP deflator has been lowered to 9.4%. This is due to lower projections for all deflators, except for household consumption expenditure. Inflation is projected to continue declining in the medium term, but at a slower pace than that projected in the March EDS, reaching 2.3% at the end of the medium term.

Slowing inflation and personal income growth will keep private consumption at the same level in 2023, while a recovery in household consumption expenditure is expected in the medium term. With rising prices of goods and services still suppressing household's purchasing power, household consumption expenditure fell by 1.8% in Q1 2023 compared to Q1 2022. The contraction was also driven by a high base[7], cautious consumers' expectations. Although the scenario projects a slowdown in the inflation rate in 2023, price increases will remain significant, and a moderate decline in the number of employed persons will have a negative impact on private consumption. The increase in interest rates will also constrain the consumption possibilities of some households. However, a stronger-than-inflation growth of wages, combined with the decisions taken in the 2023 budget to raise personal income, and the savings accumulated by the population, are projected to keep households' real consumption expenditures in 2023 at the 2022 level (Annex 3). In the medium term, the purchasing power of the households will be strengthened by slower price growth and rising incomes, and household consumption expenditure could grow by 3.4% annually.

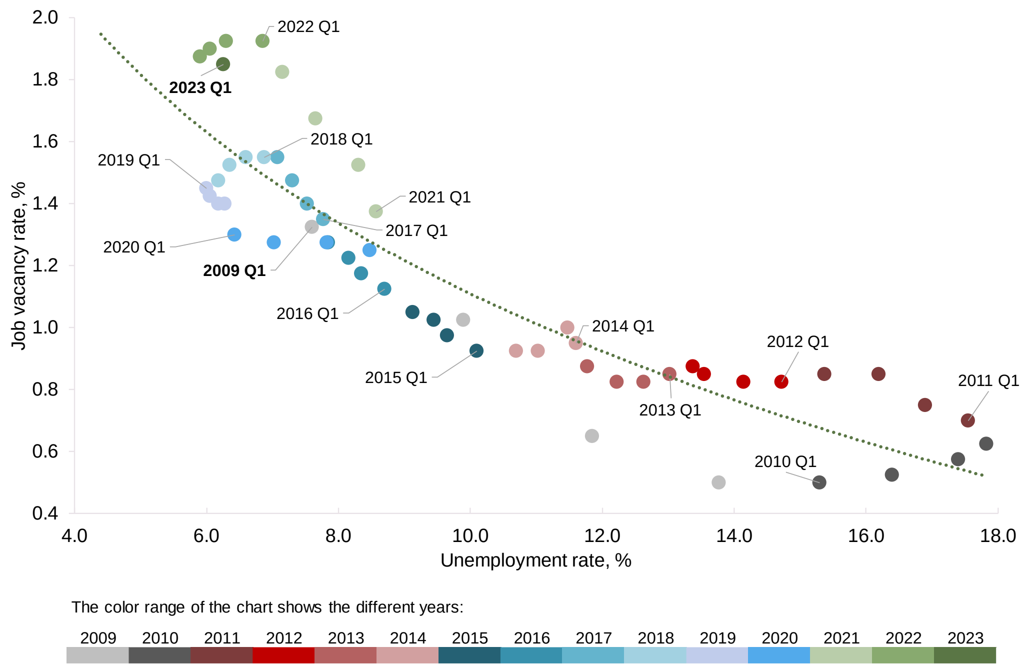
The projected contraction of the country's economy in 2023 is likely to be mitigated by continued favourable labour market development. According to the data of Q1 2023, the unemployment rate in the country increased by 1.4% p.p. during the year in Q1 2023 compared to Q1 2022, reaching 7.7%. On the other hand, the registered unemployment rate in January–March this year was lower than in the same period of the previous year[8] accounting for an average of 9.1%, while it decreased to 8.3% in May. The trend in the number of insured persons covered under all types of social insurance in January–May 2023, as published by *Sodra*, shows a stable and active labour market situation. The problem of labour shortages is indicated by the increase in the number of job vacancies in the country in the first quarter of this year, which has returned to the level of the beginning of 2022 after the decrease in the previous quarter. Although the pressure on the labour market[9] due to the increase in the unemployment rate eased slightly in Q1 2023, the need for new employees, as reflected by the high job vacancy rate, remains (Figure 6). As a result, the labour market situation remains stable. The opposite situation was observed in 2009, when the labour market situation deteriorated in the face of rapidly rising unemployment rate and declining job vacancies.

[7] In Q1 2022, the annual change in household consumption expenditure was 6.9%.

[8] According to data of the Employment Services, registered unemployment averaged 10.0% in January–March 2022.

[9] The labour market situation can be illustrated by plotting the relationship curve between job vacancy rate and the unemployment rate, known as the Beveridge curve. Movement along the curve indicates a change in the labour market pressure. In Q1 2023, the pressure in the labour market decreases as the curve slopes downwards.

Figure 6. While the increase in the unemployment rate in Q1 2023 has eased labour market tensions, the need for new employees, as reflected by the high job vacancy rate, remains



Source: State Data Agency, calculations by the National Audit Office implementing the functions of a fiscal institution

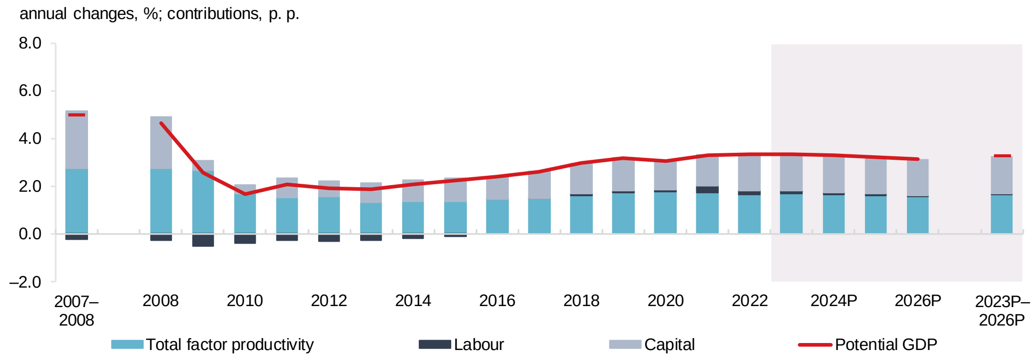
Average monthly gross earnings grew by 13.6% during the year (compared to Q1 2022) in the face of persistent labour market tensions. With some economic activities experiencing difficulties due to reduced demand for goods and (or) services, the growth in the average monthly gross earnings in 2023 is likely to be slower than in 2022, but will remain in the double-digits. Subdued problem of employee shortages and the rising cost of borrowing, which will encumber the financial capacity of companies with also contribute to a slower growth of average monthly gross earnings. In the medium term, wage growth will be affected by possible decisions on the minimum monthly wage and public sector earnings increases.

The June EDS forecasts a moderate decline in the number of employed persons in 2023 (–0.8%). This change is likely to be driven by reduced demand in some economic activities, which may lead to adjustments in hiring plans of companies, most notably in the manufacturing and retail. Given the current stable labour market, employers' expectations of retaining employees and the expectation of a more favourable development of the national economy in the second half of the year, the unemployment rate is expected to reach 7.3% in 2023. With the projection of a stronger economic growth in the 2024–2026 period, the unemployment rate is likely to decline over this period, while the number of employed persons is not likely to change significantly.

4. MORE FAVOURABLE POPULATION PROJECTIONS AND THE INCREASED INFLUENCE OF THE CAPITAL FACTOR DRIVE THE POTENTIAL GDP GROWTH PROJECTED BY THE FISCAL INSTITUTION IN THE NAO FOR 2023–2026.

The National Audit Office implementing the functions of a fiscal institution projects potential GDP[10] to increase by an average of about 3.3% annually in 2023-2026 (Figure 7). By highlighting change factors, the total factor productivity contributes around 1.6% p.p. to potential GDP growth. The contribution of capital, which is closely linked to the overall development of investment, also contributes 1.6% p.p. The impact of the labour[11] factor is positive at 0.1% p.p. This is driven by the increase in the labour force due to the favourable migratory trends in recent years which have led to better population projections. According to the Fiscal Institution in the NAO assessment, the output gap from potential is likely to be –2.8% of potential GDP in 2023, and it will reach –3.6% of potential GDP by 2024. The updated heatmap for the Lithuanian economy shows a further cooling in Q2 2023, in line with the multi-year average (Annex 4).

Figure 7. Total factor productivity and capital will be the main drivers of Lithuania's potential GDP growth in 2023–2026



Source: Eurostat, calculations by the National Audit Office implementing the functions of a fiscal institution

[10] The assessment methods are further detailed in the Description of the Assessment and Approval of the Economic Development Scenario. Available online at: https://www.valstybeskontrole.lt/TVS/Content/Biudzeto_stebesena/ERS_vertinimo_ir_tvirtinimo_aprasas.pdf.

[11] Projections of the working-age population (15-74 years) are based on the EUROPOP2023 baseline scenario published on 30/03/2023.

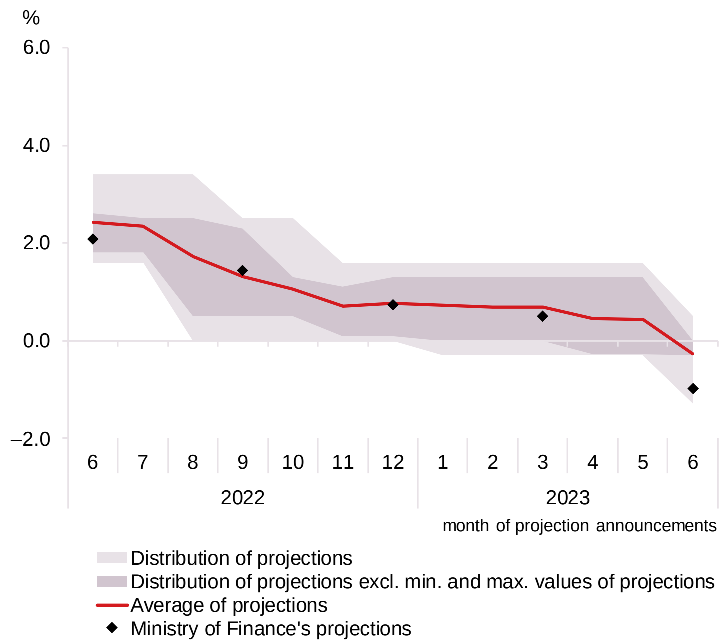
5. THE NATIONAL AUDIT OFFICE OF LITHUANIA, IMPLEMENTING THE FUNCTIONS OF THE FISCAL INSTITUTION ENDORSES THE ECONOMIC DEVELOPMENT SCENARIO, BUT PERSISTING RISKS COULD AFFECT ECONOMIC DEVELOPMENT

The Fiscal Institution in the NAO endorses[12] the Economic Development Scenario for 2023–2026 published by the Ministry of Finance on 30/06/2023. It complies with the assumptions identified, is based on relevant statistical data, and the presented projections do not contradict the expert evaluation of the National Audit Office implementing the functions of a fiscal institution.

The Economic Development Scenario for 2023–2026 of the Ministry of Finance has been prepared and published in accordance with the legal framework under the exceptional circumstances identified. The Ministry submitted the draft EDS to the Fiscal Institution in the NAO on 08/06/2023 for initial alignment. There were no significant differences between the assessments of the economic development of the NAO and the Ministry. At the meeting held on 14 June, the questions raised by the Fiscal institution in the NAO were answered, the main technical assumptions and risk factors were presented. The Ministry of Finance published the Economic Development Scenario for 2023–2026 on its website on 30/06/2023.

The remaining uncertainty in 2023 is illustrated by the distribution of projections by institutions publishing Lithuania's GDP projections (Figure 8). The distribution of GDP projections of other institutions in 2023 shows that it is currently difficult to predict the economic outlook for 2023. The real GDP projection for 2023 remains cautious in the June EDS.

Figure 8. The June 2023 EDS projections for real GDP in 2023 remains cautious



The following institutions have been included in the projection distribution: European Commission, International Monetary Fund, Organisation for Economic Cooperation and Development, Bank of Lithuania, AB Swedbank, AB SEB (Annex 5).

Source: calculations by the National Audit Office implementing the functions of a fiscal institution

[12] The decision on the endorsement is based on the data that was available until 09/06/2023. The Ministry of Finance is obliged to publish an updated EDS at least once a quarter until the exceptional circumstances are lifted.

According to the assessment of the Fiscal Institution in the NAO, Lithuania's economic development may be significantly affected by the lingering persisting risks in the face of the ongoing war in Ukraine:

- **Higher energy prices.** While the decrease in energy prices and high filling of gas storage facilities have eased concerns about the supply of energy resources, the geopolitical situation and a higher demand as China's economy recovers could lead to higher prices in the cold season than currently expected. Higher energy prices would increase inflation and have negative impact on the competitiveness of the energy-intensive Lithuanian industry.
- **Faster food products price growth.** Reduced fertiliser consumption due to high prices in 2022, unfavourable natural conditions and uncertainties regarding agricultural exports from Russia and Ukraine could lead to higher-than-expected food prices in 2023.
- **Stronger negative impact of ECB rate hikes.** Because of persisting high inflation further ECB interest rate hikes could have a stronger-than-expected impact on household consumption and investments in the euro area. Although Lithuania has one of the lowest private sector debt-to-GDP ratios in the EU, monetary policy decisions could influence the economies of Lithuania's main export trading partners and negatively affect the country's exports. Also, the rising cost of public debt financing reduce the ability of the governments to respond to emerging challenges and to stimulate economies.
- **Deterioration of the labour market situation.** The unfavourable situation in Lithuanian manufacturing sector may have a stronger impact on the labour market than expected. Higher unemployment and slower wage growth would lead to lower household consumption.
- **Slower implementation of EU-funded projects.** There still are risks regarding the implementation of the European Union's Structural Funds and the Recovery and Resilience Facility, which could lead to a slower growth in public consumption and investment.
- **More favourable impact of public sector investment on the economy.** More efficient public investments can provide a stronger stimulus to the economy while supporting domestic consumption, tackling energy dependency issues, and building economic resilience.

The National Audit Office of the Republic of Lithuania, implementing its functions as a budget policy monitoring institution (fiscal institution) set out in the Constitutional Law on the Implementation of the Fiscal Treaty of the Republic of Lithuania, has carried out an assessment and issued an opinion on the Economic Development Scenario for 2023–2026 prepared by the Ministry of Finance of the Republic of Lithuania and published on 30 June 2023. Pursuant to Article 7(3) of the Constitutional Law on the Implementation of the Fiscal Treaty of the Republic of Lithuania and Article 8(7)(3) of the Law on National Audit Office, the National Audit Office submits its opinion to the Seimas of the Republic of Lithuania.

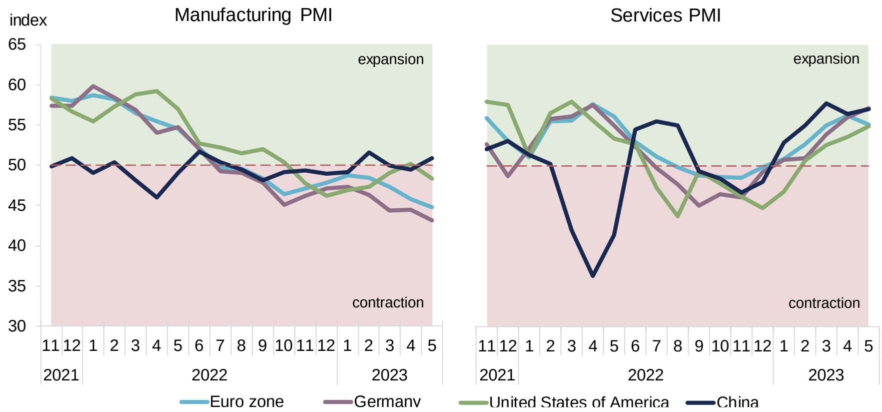
Head of Budget Monitoring Department   Jurga Rukšėnaitė

ANNEXES

Opinion
“On the Endorsement of the Economic Development Scenario”
Annex 1

BUSINESS ACTIVITY IN GLOBAL ECONOMY AND COMPARISON OF ASSUMPTIONS OF INTERNATIONAL INSTITUTIONS

Figure 1. In 2023, the manufacturing Purchasing Managers' Index shows contraction in the world’s major economies, except China, with expansion of services driven by strong demand



Source: https://www.pmi.spglobal.com

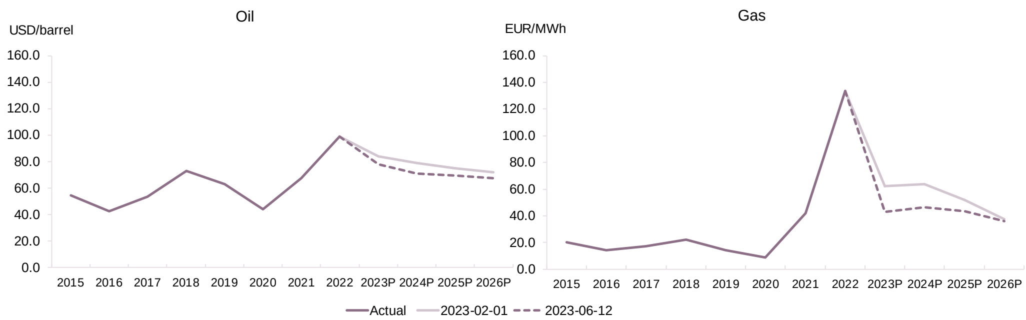
Table 1. Comparison of projections of international institutions for oil prices and the USD/EUR exchange rate

Period	EC (15/05/2023)		OECD (07/06/2023)		ECB (15/06/2023)		World Bank (06/06/2023)		Futures (12/06/2023)	
	Oil price	USD/EUR	Oil price	USD/EUR	Oil price	USD/EUR	Oil price	USD/EUR	Oil price	USD/EUR
2022	100.7	1.08	100.7	1.08	103.7	1.05	100.8	–	100.7	1.03
2023P	76.3	1.10	75.0	1.04	78.0	1.08	80.0	–	73.3	1.08
2024P	72.1	1.10	75.0	1.04	72.6	1.09	82.0	–	71.2	1.10
2025P	72.1	1.10	75.0	1.04	70.4	1.09	84.4	–	69.3	1.11
2026P	72.1	1.10	75.0	1.04	70.4	1.09	84.4	–	67.5	1.12

The date of data publication is presented in brackets.

Source: European Commission, Organisation for Economic Co-operation and Development, European Central Bank, World Bank, https://www.barchart.com

Figure 2. Brent oil and gas TTF futures in June 2023 show lower prices than expected at the beginning of the year



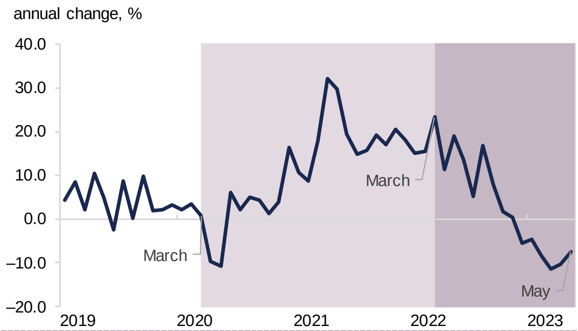
Source: https://www.barchart.com

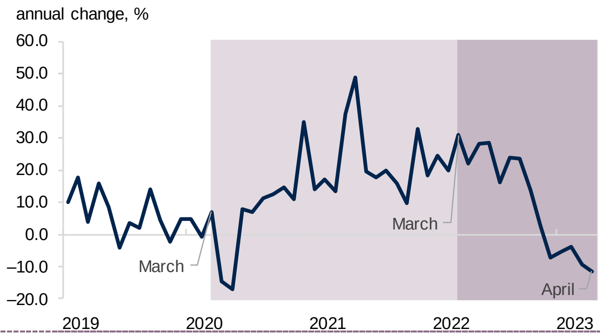
Opinion
"On the Endorsement of the Economic
Development Scenario"
Annex 2

DEVELOPMENTS IN THE LITHUANIAN ECONOMY DURING A PERIOD OF EXCEPTIONAL CIRCUMSTANCES

① The contraction in the **manufacturing sector**[1] led by chemicals, metals, wood and furniture production continued in May.

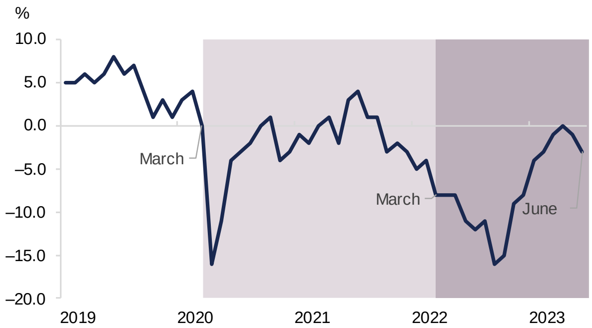
② As manufacturing output contracted, the **value of exports of goods of Lithuanian origin**[2] continued to decline in April.

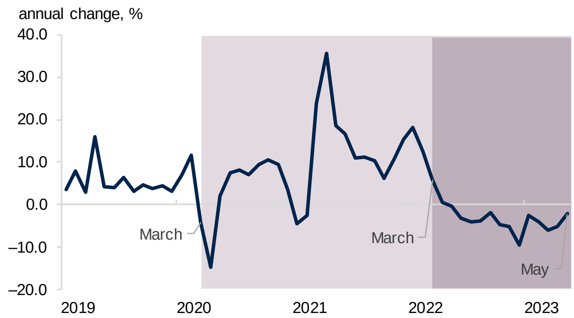




③ After recovering at the beginning of the year, **consumer expectations** remain cautious in June due to a weaker assessment of the financial situation of households and the national economic situation.

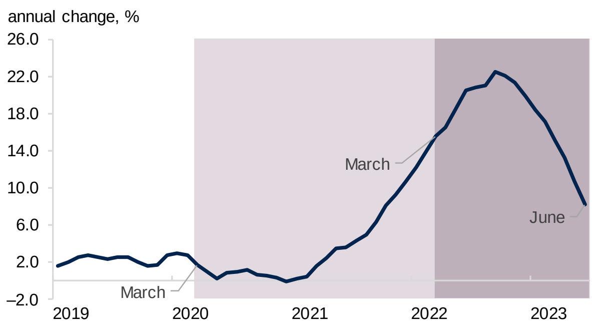
④ A smaller decline in food sales in May led to a 2.2% annual decrease in **retail turnover**[3].

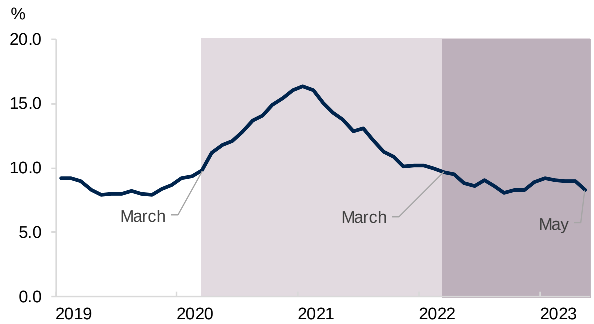




⑤ According to preliminary data of June, annual June **inflation** reached single digits at 8.2%

⑥ **In May unemployment** is close to the 2019 levels.





[1] Except refined petroleum products.
[2] Except mineral products.
[3] Except for the sale of automotive fuels.
The purple background indicates a period of exceptional circumstances.
Russia's war in Ukraine is marked separately in a darker colour.

Source: State Data Agency, Employment Service, calculations by the National Audit Office implementing the functions of fiscal institution

Opinion
"On the Endorsement of the Economic
Development Scenario"
Annex 3

THE MINISTRY OF FINANCE'S JUNE 2023 PROJECTIONS FOR THE ECONOMIC DEVELOPMENT SCENARIO

Indicator, %	2022	2023P	2024P	2025P	2026P
Key macroeconomic indicators, rate of change					
GDP at constant prices	1.9	–1.0 (0.5) ▼	2.5 (3.0) ▼	3.0 (3.0)	3.0 (3.0)
Household consumption expenditure	0.5	0.0 (0.5) ▼	3.4 (3.4)	3.4 (3.4)	3.4 (3.4)
General government consumption expenditure	0.5	0.5 (0.5)	0.0 (0.0)	0.0 (0.0)	0.0 (0.0)
Gross fixed capital formation	2.6	6.3 (2.7) ▲	4.5 (5.4) ▼	5.4 (5.4)	5.4 (5.4)
Exports of goods and services	11.9	–0.7 (0.0) ▼	4.5 (4.9) ▼	4.9 (4.9)	4.9 (4.9)
Imports of goods and services	12.3	–2.0 (0.3) ▼	5.1 (5.2) ▼	5.2 (5.2)	5.2 (5.2)
GDP at current prices	18.9	8.3 (10.3) ▼	5.2 (5.3) ▼	5.3 (5.1) ▲	5.3 (5.1) ▲
Price indicators, rate of change					
GDP deflator	16.7	9.4 (9,8) ▼	2.6 (2.3) ▲	2.3 (2.0) ▲	2.3 (2.0) ▲
Harmonised index of consumer prices (annual average)	18.9	8.9 (8.5) ▲	2.6 (2.3) ▲	2.3 (2.0) ▲	2.3 (2.0) ▲
Labour market indicators					
Change in average gross monthly earnings	13.3	10.4 (9.1) ▲	6.3 (5.0) ▲	5.0 (5.0)	5.0 (5.0)
Unemployment rate (according to the Labour Force Survey methodology)	5.9	7.3 (7.0) ▲	6.9 (6.8) ▲	6.5 (6.5)	6.3 (6.3)
Change in the number of employed persons (according to the Labour Force Survey methodology)	3.8	–0.8 (–0.7) ▼	0.1 (0.0) ▲	0.1 (–0.1) ▲	–0.2 (–0.2)

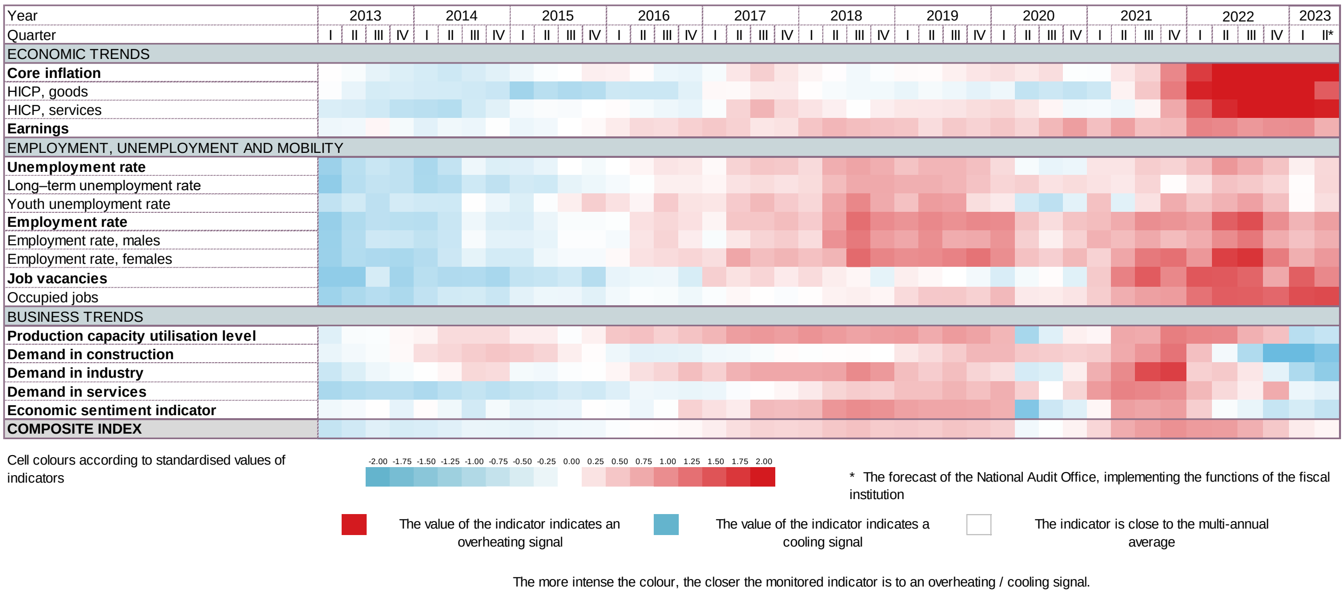
The projections of March 2023 for the Economic Development Scenario are shown in brackets.
According to the EDS assessment and the endorsement description, the purple background indicates the EDS indicators to be approved by the Fiscal Institution in the NAO.

Source: Ministry of Finance

Opinion
"On the Endorsement of the Economic Development Scenario"
Annex 4

THE HEATMAP OF LITHUANIA'S ECONOMY

The monitoring of macroeconomic imbalances[13] shows that persistently weak business expectations continue to keep the temperature of the Lithuanian economy cool, supported by high inflation and a favourable labour market[14].



Detailed Heatmap data may be found on the web page https://www.valstybeskontrole.lt/LT/BiudzetoStebesena under Makroekonominiai duomenys tab (En. Macroeconomic data).

Source: Eurostat, State Data Agency, calculations by the National Audit Office implementing the functions of a fiscal institution

[13] The methodology for drawing up the map and the description of the indicators are set out in the Fiscal Institution's Opinion No BP–5 "On the Endorsement of the Economic Development Scenario" of 20/09/2018. The map shows the deviations from the long-term average. The 05/04/2022 Opinion "On the Endorsement of the Economic Development Scenario" contains a description of the calculation of the construction demand indicator.

[14] Some of the statistical indicators used in the map for Q2 2023 are provisional. Net inflation, the April – May change in the HICP indexes of goods and services compared to the corresponding period of the previous year are equated to Q2. Unemployment and employment rates, job vacancies, and jobs occupied in Q2 are estimated using econometric models, taking into account data available from a State Data Agency, the Employment Service and Sodra (State Social Insurance Fund).

Opinion
"On the Endorsement of the Economic Development Scenario"
Annex 5

REAL GDP PROJECTIONS BY OTHER INSTITUTIONS

Institution	Date of publication	2023P
The Bank of Lithuania	19/06/2023	–1.3
European Commission	15/05/2023	0.5
OECD	07/06/2023	0.0
IMF	12/04/2023	–0.3
AB SEB	05/05/2023	–0.2
AB Swedbank	25/04/2023	–0.3
Average of institutions		–0.3
The Ministry of Finance	30/06/2023	–1.0

Source: the following institutions are included in the projections – European Commission, the International Monetary Fund, the Organisation for Economic Co-operation and Development, the Bank of Lithuania, AB Swedbank, AB SEB, calculations by the National Audit Office implementing the functions of the fiscal institution