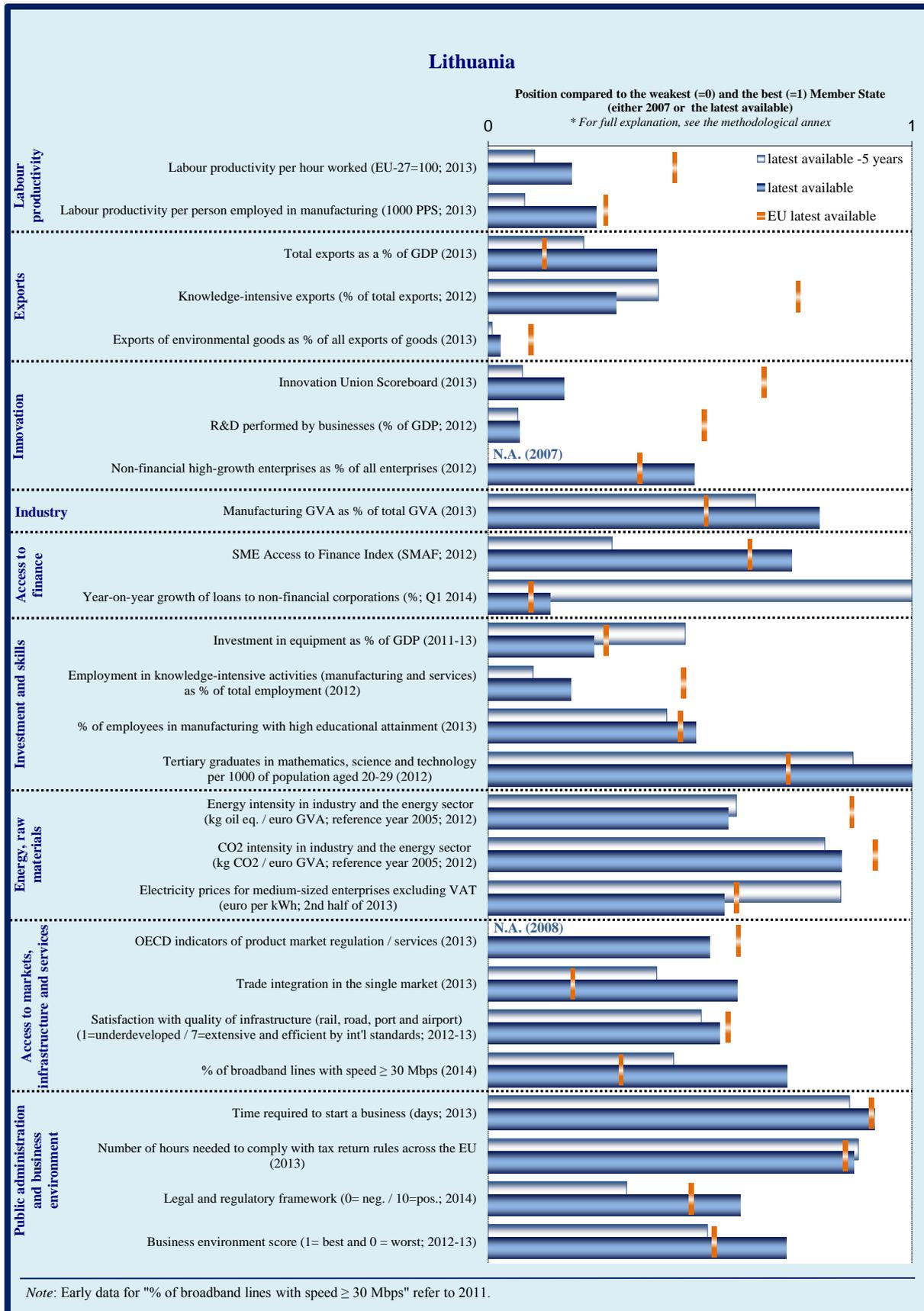
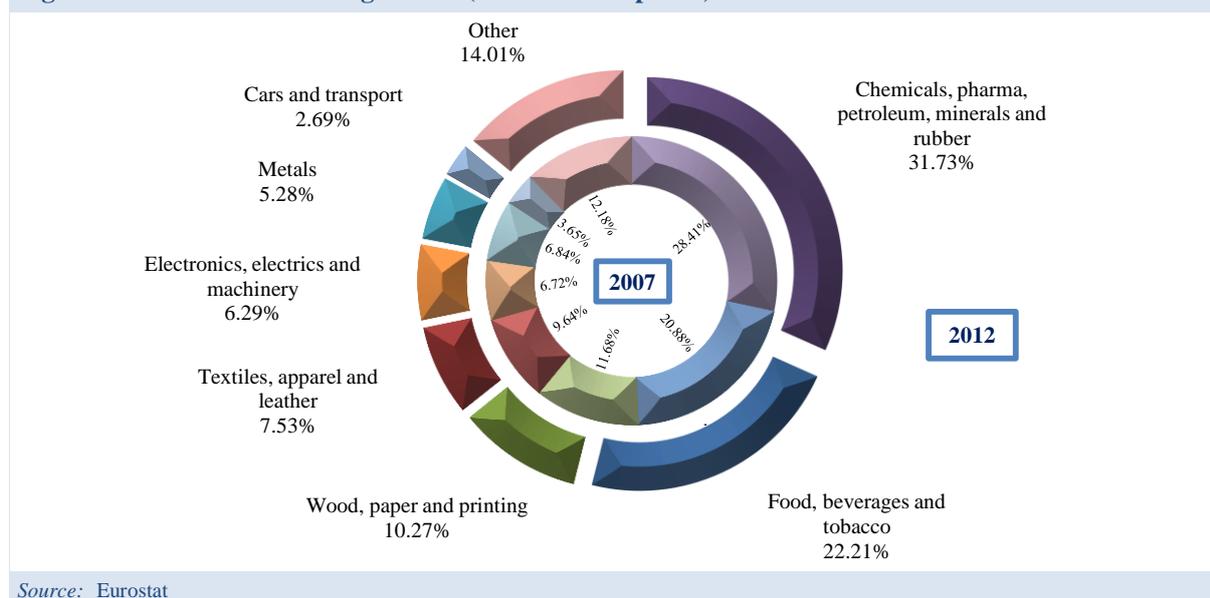


### 3.15 Lithuania



**Figure 3.15.1: Manufacturing sectors (GVA at basic prices) - Lithuania**

Source: Eurostat

### 3.15.1 Introduction and performance

Lithuania has a large manufacturing sector compared to the EU average; it represented around 21 % of GDP in 2012. In contrast to the downward trend in the EU as a whole, the proportion of manufacturing to GDP in Lithuania increased between 2000 and 2012, by two percentage points. This was the third largest increase in a Member State in this period. Lithuania's manufacturing sector is based mainly on low- to medium technology industries.

In 2011, Lithuania had a revealed comparative advantage in wood and wood products, furniture, tobacco, food, beverages, paper, clothing, refined petroleum, chemicals, rubber and plastics, and furniture. For services, it has a revealed comparative advantage in transport and travel. <sup>(1)</sup> The challenge for Lithuanian industry is to move up the technology ladder for manufactured products, and to develop more knowledge-intensive services. The Lithuanian government has set a strategic goal to become a northern European services hub by 2015, and to do this it has developed a high standard of ICT infrastructure.

Lithuanian industry has scope to boost competitiveness in terms of labour productivity. Although its performance has improved relative to that of other Member States since 2008, productivity in terms of output per hour worked is well behind the

best performing Member State. There is also still scope for further gains in labour productivity per person employed in manufacturing. Labour productivity (output per person employed) in Lithuania reached 72 % of the EU average in 2012.

The real effective exchange rate (REER) <sup>(2)</sup> increased by 1.7 % between December 2012 and December 2013, reversing the decrease over the previous four years. This can be partly linked to the falling currencies of several trading partners in most notably Russia and the Ukraine. The CIS makes up 31.6 % of Lithuanian export demand. Export growth started to stabilise in 2013, and the competitiveness gains achieved since 2009 are under pressure as a result of increasing labour costs and falling currencies in the CIS. In real terms, monthly earnings have started to increase, though partly because of a one-off increase in the minimum wage. Unit labour costs have risen slightly. Rising labour costs should be offset by further gains in productivity if Lithuania's competitiveness is to stay at its current level. There is a need to increase business investment and to continue to undertake reforms to improve the business climate. Labour supply could also be improved through more active labour market policies. The net migration rate in Lithuania is the highest in the EU and includes a high proportion of young people. The long-term impact of this population movement is unclear, but it may result in skills shortages in the labour market and hence act as a drag on competitiveness.

<sup>(1)</sup> EUIS report 2013.

### 3.15.2 Access to finance and investment

The banking sector remains stable and applies strict lending standards. Uncertainty about the external economic environment has dampened demand for credit. At the same time many companies have sufficient cash reserves to finance investments internally. In 2013, there were signs that lending continued to grow following a rise in 2012. It is expected that demand for credit will increase without a further tightening in lending conditions.

According to the most recent research carried out by the Lithuanian business support agency (2013), the most common barriers to obtaining credit are tight financing requirements, lack of collateral and the high cost of obtaining finance (interest rates, guarantee fees, administrative costs, etc.). There is also a reluctance to lend to start-up companies. Over three-quarters of SMEs that received external funding with supplementary conditions indicated that they had to pledge additional assets, provide additional personal guarantees, provide state guarantees or guarantees from other institutions, or had to increase their capital share in an investment proposal. The SME Access to Finance Index improved significantly in 2012 compared to 2008.

Lithuania runs several programmes that support access to finance for SMEs, primarily the INVEGA Fund, the Jeremie Guarantee Fund and the Entrepreneurship Promotion Fund, which are supported by EU structural funds. The Jeremie Guarantee Fund supports the provision of risk capital through a variety of instruments. The INVEGA Fund provides debt instruments for SMEs to support business expansion. The Jeremie Guarantee Fund finances guarantees for SMEs, and the Entrepreneurship Promotion Fund provides microcredit for the purpose of starting-up businesses. Up to the end of 2013, 626 SMEs have received more than EUR 450 million, including financing from EU structural funds and the banking sector.

In order to improve access to credit, Lithuania strengthened its secure transactions system by: broadening the range of movable assets that can be used as collateral; making it possible to include a general description in the security agreement of the

assets pledged as collateral; and permitting out-of-court enforcement.

### 3.15.3 Innovation and skills

Based on the Commission's Innovation Union Scoreboard 2014, Lithuania still lags behind other Member States. Lithuania's performance measured by the indicator on R&D carried out by businesses, as a percentage of GDP, is one of the lowest in the EU.

The Lithuanian economy is categorised as a 'moderate innovator', having been upgraded from the lowest performance group of 'modest innovator' several years ago. Lithuania can still improve its science base and the research links between academic and private-sector organisations. Lithuania's smart specialisation strategy should encourage more cooperation between business and academia in the field of R&D and innovation. Priority should be given to key technologies or processes that have a high potential to transform the Lithuanian economy. R&D spending remains well below its 2020 target of 1.9 % of GDP.

The Lithuanian authorities are currently drafting recommendations for public authorities on organising and implementing innovative public procurement, including the pre-commercial procurement of innovative services. In 2013, the Agency for Science, Innovation and Technology started a new project on pre-commercial procurement, financed by EU structural funds. Several new projects have recently been launched by the Agency for Science, Innovation and Technology. These include a new technological entrepreneurship project called 'Innovative Business Promotion' which will promote technological start-ups and development in Lithuania. The project brings together the largest Lithuanian universities, science- and technology parks, and other academic and research institutions.

There are indications of possible skills shortages in the labour market. Structural unemployment remains high, there has been a large outflow of the working age population, and wage levels started to increase during 2013. There is also a low level of entrepreneurship and self-employment. Although Lithuania has already reached the Europe 2020 15% target to lower the percentage of "low achievers in reading" the Europe 2020 target to have at least 40% of 30-34 years old with tertiary education, it scores

<sup>(2)</sup> Based on statistics from the Bank of Lithuania.

below EU average in PISA (in reading and mathematics).

Lithuania should address the current skills shortages in the labour market through training and active labour market policies. This should include improving the education system to better meet the demands of the labour market, and promoting entrepreneurial skills and self-employment opportunities.

### 3.15.4 Investment

At the start of the crisis in 2009, gross fixed capital formation fell by around 40 %. Investment rebounded rapidly in 2010 and 2011, before stabilising in 2012. It increased by around 13 % in 2013. Compared to the best performing Member State, investment in equipment as a percentage of GDP has fallen since 2008. Private-sector investment growth should remain positive due to a range of factors: historically low interest rates; growth in enterprise cash reserves; survey data suggesting that businesses are planning new investments as the economic outlook improves; and increasing the use of existing industrial capacity above the long-term average. It is expected that public investment will be supported by projects co-financed by the EU. The stock of foreign direct investment in Lithuania has been growing since 2000. Foreign direct investment inflows have slowed in recent years, from 3.4 % of GDP in 2010 to 1.5 % of GDP in 2012, but are expected to have increased in 2013.

### 3.15.5 Energy, raw materials and sustainability

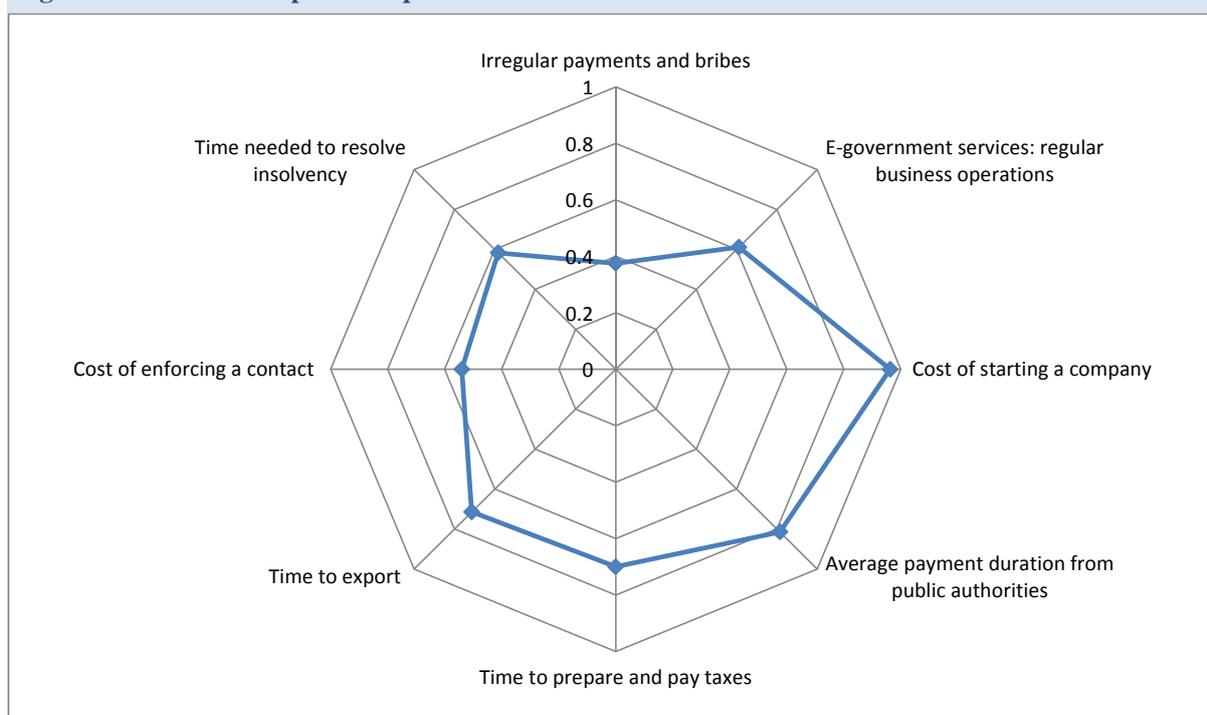
Lithuania still operates a relatively old electricity distribution network, which was designed around centralised and large-scale electricity generation. The lack of diversified energy supply infrastructure hinders competition. Electricity and gas networks also have weak interconnectivity with continental Europe and Nordic networks, meaning that energy can be imported from relatively few countries and that natural gas is imported from a single external supplier (Russia). Until 2013, Lithuania paid the highest price for natural gas in the EU, and electricity prices were above the EU average.

The Lithuanian authorities are supporting: the ongoing construction of new advanced power transmission lines to build interconnectivity with Poland and Sweden; the reconstruction and modernisation of existing power transmission lines to ensure reliable power supply to consumers; and the renovation of internal gas transmission and distribution networks. A liquefied natural gas terminal in Klaipėda is expected to be operational by the end of 2014. These activities will help reduce costs and improve the security of the energy network.

Given Lithuania's large industrial sector, its economy is heavily reliant on the supply of raw materials, particularly crude oil, natural gas, sulphur, caustic soda and cast iron. As noted above, the authorities are undertaking projects to improve the security of energy supply. In addition, Lithuania's industry has significant scope to improve its resource efficiency and production methods, which would reduce its reliance on imported raw materials.

In terms of energy intensity, the Lithuanian economy is around twice as intensive as the EU average, while the level of environmental taxation is below the EU average. This is partly on account of the emission-intensive transport sector, but also due to the residential and service sectors. Household heating, particularly in apartment blocks, is inefficient and in need of renewal. Although there has been some progress in renovating old apartment buildings under a government-supported programme, it is estimated that several thousand apartment buildings still need to be renovated.

Although the quantity of waste per capita in Lithuania is below the EU average, the waste management system remains dependent on landfilling, and recycling levels are low. Eleven regional non-hazardous waste landfills have been constructed and old, unexploited landfills and waste-polluted territories are in the process of re-cultivation. To improve biodegradable waste management, green waste composting facilities are being built, containers for individual composting are being provided, and sewage sludge treatment plants are being constructed. One mechanical sorting plant and nine mechanical-biological sorting plants are planned to start operations from 2016. Mixed municipal waste treatment plants will be introduced and waste sorting and recycling capacity will be increased. The amount of waste going to landfills is gradually decreasing (in

**Figure 3.15.2: Overall profile of public administration - Lithuania**

*Note:* Values have been scaled so that the best observation (Member State) gets 1 and the worst gets 0.

*Source:* World Bank Doing Business Report; Intrum Justitia; OECD; World Economic Forum; European Commission

2011 it was 1 million tonnes compared to 1.092 million tonnes in 2009).

### 3.15.6 Access to markets, infrastructure and services

Lithuania is an open economy, partly due to its well-established industrial base. It has one of the highest rates of exports as a percentage of GDP in the EU, at around 83 %. Its main export partner is the EU (57 %), followed by the CIS (31 %). Since 2009, the increase in exports to the EU has been lower than the increase of exports to CIS countries, mainly due to weak demand from the euro zone. Service exports are a small proportion of overall exports, but have been growing rapidly in recent years.

Lithuania's international competitiveness in the transport and logistics sector is to a large extent determined by its geographical position, as east- and west-bound freight flows cross the country connecting the Baltic Sea region, the CIS and Western Europe. This makes the transport sector the largest contributor to the Lithuanian economy (around 13 % of GDP).

Lithuania is linked to the CIS' railway network because it uses the same (1520 mm) railway gauge. This is advantageous for the national logistics market, especially for long-distance routes, for example from Asia. Lithuania is working with Latvia and Estonia to implement the Baltica railway project, involving the construction of a new European standard gauge railway line (1435 mm) to connect the Baltic States with the rest of Europe.

Road infrastructure is a very important component of the transport network, carrying over half of the freight that crosses Lithuania and nearly all passenger travel. Lithuanian road hauliers carry a significant amount of freight between the EU and neighbouring markets, particularly Russia, Kazakhstan and other CIS countries.

Klaipėda Sea Port is the most northern ice-free deep-water port, and handles long-distance shipments travelling from Eastern to Western Europe, and other continents. The port includes facilities for handling containers, oil products, fertilisers, roll/on-roll/off cargo, and has the capacity to handle 'Panamax' vessels, making it a regional container-distribution hub.

The three international TEN-T airports in Lithuania (Vilnius, Kaunas and Palanga) that have become the economy's main gateways for business and tourism. The Lithuanian airport cargo hub provides an integrated supply chain system comprising airport infrastructure, a cargo terminal, and logistics services.

### 3.15.7 Public administration and business environment

Lithuania scores quite high in terms of the efficiency of its public administration and how this affects the business environment. In comparative terms, it is closer to the best-performing EU Member State for: the time required to start a business, the number of hours needed to comply with tax return rules across the EU, and the overall business environment score. For the legal and regulatory framework, Lithuania is roughly equidistant between the worst- and best-performing EU Member States. Compared to 2008, it has also made significant improvements in the time required to start a business, the legal and regulatory framework, and its business environment score. Since 2012, impact assessments have been compulsory for all new draft business legislation, with the potential to increase the administrative burden on businesses. In 2013, impact assessments were carried out on nearly fifty items of legislation was assessed.

The Lithuanian authorities are currently preparing a plan for the consolidation of business inspection agencies. In addition, an ongoing reform process is helping inspection agencies introduce such measures as: checklists, to ensure inspections are consistent; risk management, to reduce inspection burdens for trustworthy businesses; and key performance indicators to measure agencies' progress. In 2013, Lithuania continued its process of reducing the administrative burden, which began in 2012. The process encompasses 24 measures, of which several were implemented in 2013, for example the procedures for acquiring land for business purposes were reduced and the possibility of submitting applications electronically was introduced. In 2012, the authorities began to screen all licenses and permits needed to start a business, and finished the exercise by the end of 2013. Draft legal amendments to existing legislation on licences and permits will be submitted in November 2014.

Lithuania made it easier to start a business by creating a new form of private limited liability

enterprise with no minimum capital requirement — a 'small partnership'. Like the other, most common, forms of legal business entities in Lithuania, it may be set up online. Lithuania reduced the time needed to register a company as a VAT payer from 13 to three days. In some cases, the online company registration procedure makes it possible for a company to open a bank savings account online at the same time as registering the company. With regard to obtaining credit, Lithuania strengthened its secure transactions system by: broadening the range of movable assets that can be used as collateral; allowing a general description of the security agreement of the assets pledged as collateral; and permitting out-of-court enforcement. With respect to trading across borders, it reduced the number of export and import documents needed and the cost of export and import procedures. It also reduced the time required to obtain a construction permit (from 142 to 105 days).

### 3.15.8 Conclusions

Sustainable strong growth will require improving long-term competitiveness. Lithuania must continue reforming its energy market in order to improve the security of energy supply and to bring down prices. Industry's use of energy should also be made more efficient to lower costs and increase sustainability. There is a need to boost skills in the labour market and to encourage more self-employment and entrepreneurs. The Lithuanian authorities have continued to improve the business environment and the recent reforms of public administration should bear fruit in the medium-term.