Political-Economic realities in the Baltic Region

Andris Vilks

SEB banka
<table>
<thead>
<tr>
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<tbody>
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<td>Latvia</td>
<td>2,26</td>
<td>23204</td>
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<td>Estonia</td>
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<td>Lithuania</td>
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<td>Baltic market</td>
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<td>71358</td>
<td>8,1</td>
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Simultaneous double shock

Baltic States GDP changes (%, quarters yoy)

Data: nat.statistcs
Consequences of the deep recession

Latvia

- GDP -22% in 2 years
- S&P credit rating down from A- to BB in 2 years
- Tax revenues down by 30% yoy in 2009
- Public expenditure cuts by 15% compared to 2008
- Unemployment from 7% to 17% in 12 months
- Wages down by 20% in 2 years
- Tax increases: VAT, excise, property
- Apartments' prices down by 70% from the peak in 2007
- NPL in banks up to 20% in 2009
Sharp downturn – recovery in 2011

GDP Growth in Baltics and Euro zone

Source: statistics, SEB
Bumpy road and experience from crisis

GDP 1991-2012 (% yoy)

- Transition -56% in 1991-1993
- Banking crisis
- Russian crisis +33% in 2004-2007
- EU accession
- Global/local crisis -25% 2008-2010

Source: statistics, SEB banka
Slight improvement in confidence

Economic Sentiment Indicators

Dat: Eurostat
Deleveraging is unavoidable
Estonia and Latvia: high foreign debt
Rapidly corrected external imbalances

**Current Account Balance (% of GDP)**

<table>
<thead>
<tr>
<th>Year</th>
<th>Estonia</th>
<th>Latvia</th>
<th>Lithuania</th>
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<td>2010F</td>
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<tr>
<td>2011F</td>
<td>8</td>
<td>6</td>
<td>4</td>
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</tbody>
</table>

Source: National statistics, Central banks, SEB
Astonishing surplus in current account

Balance of Payments (LVL mln)

Source: Bank of Latvia
Adjustments in prices. Deflation!?  

HCPI in the Baltics and Eurozone (% yoy)
Unemployment in the Baltics

Estonia
Latvia
Lithuania
Euro zone

Source: Eurostat, SEB
Flexibility in wages – eroded purchasing power

Latvia: Purchasing power and unemployment (% yoy)

Source: CSB, SEB banka
Fiscal troubles – enlarged public debt

Public sector financial balance (% to GDP)

-10  -8  -6  -4  -2  0  2  4


Estonia  Latvia  Lithuania  Euro zone

Source: Statistics, SEB
## Exit strategy – euro adoption

### Latvia - 2013/2014

<table>
<thead>
<tr>
<th></th>
<th>2009</th>
<th>2010</th>
<th>2011</th>
<th>2012</th>
<th>2013</th>
<th>2014</th>
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<tbody>
<tr>
<td>Fiscal balance</td>
<td>-8.5-9.5</td>
<td>-7.0-8.5</td>
<td>-4.0-5.5</td>
<td>-3.0-4.0</td>
<td>-2.5-3.0</td>
<td>-1.0-0.0</td>
</tr>
<tr>
<td>CPI (%)</td>
<td>3.2-3.6</td>
<td>2.5-3.5</td>
<td>1.0-2.0</td>
<td>1.5-2.5</td>
<td>1.5-2.0</td>
<td>1.5-2.0</td>
</tr>
</tbody>
</table>

- Budget deficit
- Prices
- Euro adoption

### Estonia - 2012/2013

- Euro adoption

### Lithuania - 2013/2014

- Euro adoption
Conclusion:

- Sharpest downturn in Q2 (Q3)
- Imbalances shrinking: current account, inflation
- Main policy – internal devaluation:
  - Massive public expenditure cuts (incl. pensions)
  - State functions restructuring
  - Wage cuts
  - Focus on productivity
- Deleveraging, debt stock
- Economy activisation measures
- Strong political focus on euro zone accession
- Pan Baltic market, Scandinavian domestic market
Thank you