LIETUVOS RESPUBLIKOS FINANSŲ MINISTERIJA
MINISTRY OF FINANCE OF THE REPUBLIC OF LITHUANIA

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RE: LITHUANIA – REQUEST FOR CLARIFICATIONS ON THE COMPLIANCE OF LITHUANIA'S DBP FOR 2024

Dear Mr Verwey,

Thank you for your letter of 27 October 2023 (Ref.: Ares(2023)7343523 – 27/10/2023) regarding the compliance of Lithuania's DBP for 2024 with the Council Recommendation of 14 July 2023.

In 2020-2022, Lithuania – like other European countries – suffered the consequences of the prolonged COVID-19 pandemic crisis and the Russian invasion of Ukraine for our social life, economy and, accordingly, they negatively impacted public finance. Reacting to the changing pandemic situation, and afterwards – the need to help the Ukrainian refugees fleeing to Lithuania, as well as experiencing secondary effects of geopolitical tensions resulting in surge in global energy prices and hampered economic growth, the Government took the necessary steps to respond to these shocks with temporary discretionary measures.

Funds were allocated for COVID-19 related measures in 2020 – 2021, while following the outbreak of the war in Ukraine, the funding has been ensured for the support measures related to the needs of the Ukrainian refugees staying in Lithuania. The third set of temporary measures was related to the support for households and businesses in the environment of high energy prices. Due to relatively strong economic performance and gradual withdrawal of the aforementioned support measures, general government deficit stood at 1.2 % of GDP in 2021 and 0.6 % of GDP in 2022, while general government debt accounted for 38.4 % of GDP in 2022 and is expected to be 37.9 % of GDP in 2023. According to the fiscal projections provided in the 2024 Draft Budgetary Plan, general government deficit is expected to be 1.9 % of GDP in 2023.

As general government debt remains well below 60 % of the GDP threshold, Lithuania has the fiscal space to react to the challenges at hand. In line with the Council recommendations[1], as the energy prices stabilised and even decreased in international markets, support measures related to energy prices have been gradually phased out. However, the geopolitical situation and the economic outlook remains very uncertain, underlining the need to be ready to react in terms of allocation of additional resources as needed.

Therefore, the Government, aiming to further help the Ukrainian refugees staying in Lithuania and aiming to contribute to EU-level and international support initiatives for Ukraine, has foreseen a set of temporary measures for 2024. The cost of these measures, having a negative impact on the 2024 general government balance, accounts for 0.4 % of GDP. Besides the aforementioned measures, Lithuania plans to allocate higher amounts of funds to military mobility – roads, air and sea ports, bridges and other necessary infrastructure that allows the armed forces to move quickly. The costs of these measures account for almost 0.4 % of GDP in 2024.

Moreover, in 2024 the Government plans to maintain the level of nationally financed investments, as recommended by the Council, and to focus on effective and timely investment of EU funds, with attention to strengthening the growth potential of the economy, increasing its resilience to future shocks and reaching national and EU wide strategic goals in areas such as green and digital transitions.

Taking into account the costs of the aforementioned measures, general government deficit of the year 2024 is projected to be 2.9 % of GDP. Furthermore, based on the latest available economic development scenario produced by the Ministry of Finance of the Republic of Lithuania (dated 11 September 2023), the negative output gap for the Lithuanian economy is set to deepen from 1.9% of GDP in 2023 to 2.3% of GDP in 2024. This deterioration underpins the need for counter-cyclical fiscal policy, supporting economic growth.

The Government emphasizes the importance to keep the sustainable debt level over the medium-term horizon, thus saving the fiscal space for potential future shocks and challenges. It should be noted that the Lithuanian authorities have channeled higher-than-expected revenues and/or unspent funds – for instance, earmarked for energy compensations in the 2023 budget – into reducing the budget deficit. Also, the Ministry of Finance intends to follow the same strategy next year. More detailed qualitative and quantitative information on general government finance in 2023 and 2024, as well as the medium-term fiscal policy guidelines are presented in the 2024 Draft Budgetary Plan.

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[1] **Council Recommendation on the 2023 National Reform Programme of Lithuania and delivering a Council opinion on the 2023 Stability Programme of Lithuania**, https://eur-lex.europa.eu/legal-content/LT/TXT/PDF/?uri=CELEX:52023DC0615.

Finally, it should be stressed that substantial uncertainty persists due to the highly stressful geopolitical situation – both when looking ahead to the rest of this year and beyond. It is hard to project how much Lithuania's economy will directly or indirectly be affected by the geopolitical crisis and how this could affect general government finance. Therefore, the Government stands ready to adjust fiscal policy with regard to a changing geopolitical situation and its possible impact on Lithuania's social environment, economic activity and public sector viability.

Sincerely yours,

Mindaugas Liutvinskas
Vice-Minister