Lietuvos Respublikos
FINANSŲ MINISTERIJA

2020 Lithuanian Draft Budgetary Plan

15 October 2019

CONTENT

TABLES

ABBREVIATIONS

Draft budget	Draft Republic of Lithuania Law on the Approval of Financial Indicators of the State Budget and Municipal Budgets for 2020
Budget framework reform	Reform of budget building and strategic planning framework started in 2017 in Lithuania
GDP	Gross domestic product
Economic development scenario	Economic development scenario of Lithuania for 2019-2022 developed by the Ministry of Finance, published on 11 September 2019 and approved by the Budget Policy Monitoring Authority
EU	European Union
ESA	European System of Accounts
Ministry of Finance	Ministry of Finance of the Republic of Lithuania
PIT	Personal income tax
Constitutional Law	Constitutional Law of the Republic of Lithuania on the Implementation of the Fiscal Treaty (of 6 November 2014 No. XII-1289)
DBP	2020 Lithuanian Draft Budgetary Plan
MMW	Minimum monthly wage
NTA	Non-taxable amount
CHIF	Compulsory Health Insurance Fund
VAT	Value added tax
SGP	EU Stability and Growth Pact[1]
Recommendation to Lithuania	EU Council Recommendation on 2019 National Reform Programme of Lithuania along with Council Opinion on 2019 Stability Programme of Lithuania
Seimas	Seimas of the Republic of Lithuania
Social model	Structural reform including legal-administrative model of the Lithuanian labour relations and state social insurance started in 2017[2]
Stability Programme	2019 Stability Programme of Lithuania approved by Government of the Republic of Lithuania Resolution No. 385 of 24 April 2019[3]
Structural reforms	Structural reforms in the fields of education, health care, shadow economy reduction, innovation, social insurance (pensions) and tax regulation approved by the Seimas of the Republic of Lithuania in Spring 2018 [4]
AW	Average wage
Government	Government of the Republic of Lithuania
SSIF	State Social Insurance Fund

[1] The Stability and Growth Pact: https://ec.europa.eu/info/business-economy-euro/economic-and-fiscal-policy-coordination/eu-economic-governance-monitoring-prevention-correction/stability-and-growth-pact/legal-basis-stability-and-growth-pact_en.

[2] A detailed description of the social model, information about promoters, related studies, cost-benefit analysis and other information are available on website http://www.socmodelis.lt/.

[3] 2019 Stability Programme of Lithuania: http://finmin.lrv.lt/uploads/finmin/documents/files/LT_SP2019(1).pdf.

[4]The description of structural reforms: https://lrv.lt/lt/aktuali-informacija/xvii-vyriausybe/prioritetiniai-darbai/strukturines-reformos.

INTRODUCTION

Having regard to Regulation (EU) No 473/2013 of the European Parliament and of the Council of 21 May 2013 on common provisions for monitoring and assessing draft budgetary plans and ensuring the correction of excessive deficit of the Member States in the euro area[5], Lithuania hereby presents the DBP [6] to the European Commission and the Eurogroup.

DBP presents Lithuania's macroeconomic situation and prospects in 2019–2022, general government balance, revenue and expenditure projections under policy and no-policy-change scenarios, comparison of indicators laid down in DBP and the Stability Programme.

The DBP has been drawn up in line with the draft budget, the draft Law on the Approval of Indicators of the SSIF Budget for 2020 and the draft Law on the Approval of Indicators of the CHIF for 2020 as well as considering revenue and expenditure projections of other subsectors attributable to general government. The aforementioned draft laws and projections of the entire general government have been drawn up by taking into account the economic development scenario, medium-term targets set out in the Stability Programme, provisions of the Constitutional Law, SGP provisions and implementing the EU Council Recommendations to Lithuania[7].

The social model has been implemented in Lithuania since 2017. This structural reform has been recognized by the EU Council as consistent with the SGP flexibility clauses, which has led to an exemption under SGP for Lithuania for 2017-2019. The DBP Annex presents the Social Model Implementation Report drawn up by the Ministry of Social Security and Labour of the Republic of Lithuania.

The medium-term objective of Lithuania for 2019–2021 is the structural general government deficit 1 % of GDP set by Seimas Resolution No. XIII-1058 of 22 March 2018.

The plan for implementation of the Recommendations to Lithuania[8] was aproved on 18 September 2019 by Government Meeting Protocol Resolution No. 38[9].

National goals of Europe 2020 have been approved by Government Resolution No. 461 on the Approval of the 2019 National Reform Agenda [10].

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[5] Regulation (EU) No. 473/2013: https://eur-lex.europa.eu/legal-content/EN/ALL/?uri=CELEX:32013R0473.
[6] DBP general government revenue and expenditure projections have been made based on the information available on 15 October 2019.
[7] EU Council Recommendation to Lithuania:
https://ec.europa.eu/info/sites/info/files/file_import/2019-european-semester-country-specific-recommendation-commission-recommendation-lithuania_en.pdf.
[8] Reference (see material of question 3): http://lrv.lt/lt/posedziai/lietuvos-respublikos-vyriausybes-pasitarimas-68.
[9] Reference: http://lrv.lt/uploads/main/meetings/docs/9555_imp_7e459ec0c9ae58b47533c39ea844f43d.pdf.
[10] Reference: https://e-seimas.lrs.lt/portal/legalAct/lt/TAD/810f32d6759311e99ceae2890faa4193?positionInSearchResults=0&searchModelUUID=6839c750-6437-49c9-adfb-0a03adadbb57.

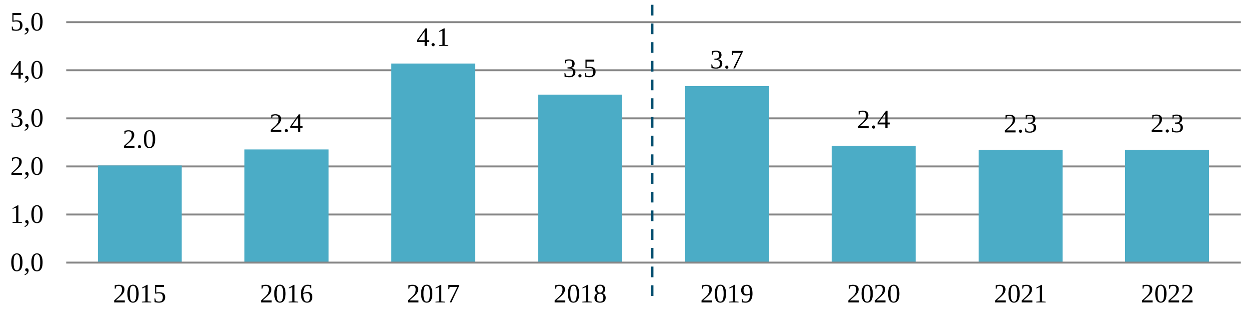
PART I
MACROECONOMIC SITUATION AND PROSPECTS

The DBP presents the economic development scenario, which was published on the website of the Ministry of Finance on 11 September 2019[11].

The economic development scenario has been drawn up on the basis of the data published and received by 30 August 2019. The assumptions of the external economic environment (trading partners development, oil prices and the euro-to-dollar exchange rate) match the estimates published in July 2019 by the European Commission and by the International Monetary Fund. The conclusion of the Budget Policy Monitoring Authority on the approval of the economic development scenario was posted on 19 September 2019[12] .

The GDP growth is estimated at 3.7 % in 2019. A moderate Lithuania's economic growth should continue in medium term – in 2020 GDP development should account for 2.4 %, while in 2021–2022 stabilise at 2.3 %.

Chart 1. Lithuania's GDP developments, %



Sources: Ministry of Finance, Statistics Lithuania.

Domestic demand during the medium term should remain the main driver of Lithuania's economy. It will be stimulated by the Government decisions aimed at increasing personal income and strengthening investment incentives, implementation of investment projects financed by direct foreign investments and EU financial support funds. In order to optimize profits, business should invest in the automation of processes, technological renewal, innovations and other efficiency and productivity enhancing measures.

The situation in the labour market will remain favourable to employees in the medium-term. Although recent migration trends have improved, with the first seven months of 2019 more people arriving in Lithuania than leaving, the natural change in population will lead to a decline in the working-age population throughout the medium term, and competition between employers for skilled workers should remain. However, people returning to the country raised labour supply and decreased recent tension on the labour market as well as enabled a more sustainable growth of wages in private sector. In medium term wage developments in the national economy will be mainly governed by the public sector wage policy pursued by the Government, decisions on MMW rate and business endeavour to attract and retain skilled workers.

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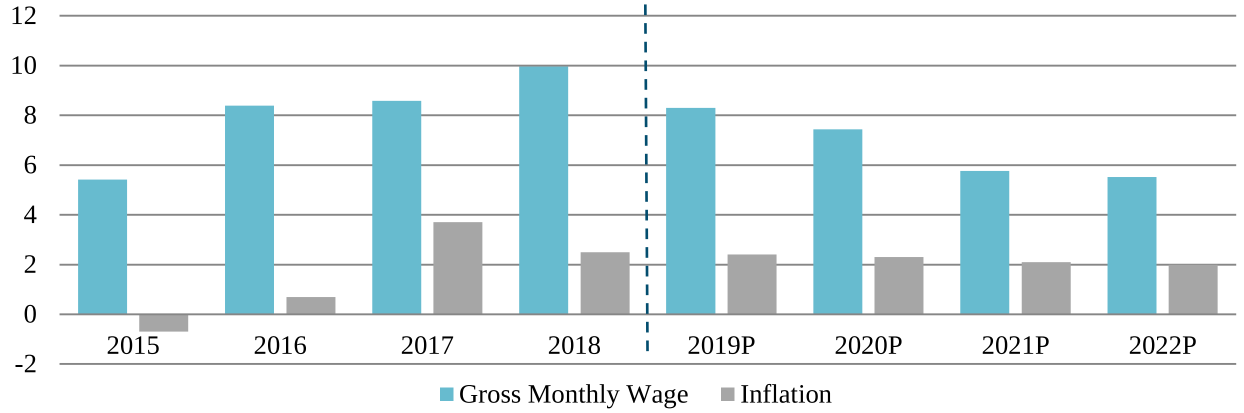
[11]Reference: http://finmin.lrv.lt/lt/aktualus-valstybes-finansu-duomenys/ekonomines-raidos-scenarijus.
[12]Reference: http://www.vkontrole.lt/bp/isvada.aspx?id=10317.

Fluctuations of prices of energy goods and on-going convergence process of prices of services in medium term will remain to be the core inflation development determinants. The economic development scenario projects that the average annual inflation will keep decreasing moderately from year to year, while personal income in medium term will grow faster than prices, therefore, the household purchasing power in medium term will remain strong.

Chart 2. Monthly gross wage and inflation developments, %



Sources: Ministry of Finance, Statistics Lithuania.

Lithuanian exporters will face challenges – in medium term they will have to adapt to changing economic conditions, make investments to increase competitiveness, manage currency risk, make decisions reducing production costs and enhancing operational efficiency, diversify export markets.

Uncertainty in external environment posing threat for the economic development scenario come true in March 2019 increased, and some identified risks materialised: international trade constraints increased, international institutions damped the prospects for the global economic development, the slowest Chinese economic growth over several decades was recorded in II quarter of 2019, and GDP growth of the euro area and the EU in the first half of 2019 slowed down markedly, good Lithuanian business expectations dominating for several last years deteriorated. If economic and political uncertainty of external environment continues to grow, recent exceptionally positive expectations of the Lithuanian consumers may start deteriorating, population may cut consumption expenditure, and enterprises postpone the investment plans.

When drawing up the economic development scenario the Brexit process was not completed which may have adverse effects on both the EU and Lithuanian economy. Geopolitical tensions and uncertainty in international trade have not expired and may increase. A high sovereign debt of some countries and challenges related to its financing still pose a risk for global economic sustainability. All this increases global, euro area and Lithuanian economy vulnerability. The risk for the economic development scenario come true also arises due to unclear outcome in negotiations between the EC, EU Council and the European Parliament concerning the Mobility Package.

Recent trends in the Lithuanian economy and perspectives of the key macroeconomic indicators set in the economic development scenario may change due to existing uncertainty. If the essential assumptions based on which the economic development scenario was drafted are not fulfilled, the estimates of the majority of indicators set in the scenario would also change.

Table 1. Macroeconomic indicators

	ESA code	2018	2018	2019	2020
		MEUR	Change, %		
1. GDP, chain-linked volume	B1*g	37,216.2*	3.5*	3.7	2.4
2. Potential GDP		35,931.2	2.8	3.7	3.8
o/w:					
- labour			0.4	0.7	0.6
- capital			1.4	1.5	1.6
- total factor productivity			1.0	1.4	1.7
3. GDP, at current prices	B1*g	45,113.8*	6.9*	7.1	5.2
GDP components (at constant prices)					
4. Household consumption expenditure + consumption expenditure of NPI serving households	P.3	24,602.6*	3.9*	3.9	3.9
5. General government consumption expenditure	P.3	5,699.6*	0.8*	0.9	0.5
6. Gross fixed capital formation	P.51	7,645.2*	6.5*	7.5	4.9
7. Changes in stocks and acquisitions of valuables less disposals, % of GDP	P.52 + P.53	N.A.	N.A.	N.A.	N.A.
8. Exports of goods and services	P.6	33,742.9*	5.1*	4.7	3.9
9. Imports of goods and services	P.7	33,687.0*	4.3*	5.1	4.0
Contributions to change in GDP, percentage points (excl. level in MEUR in 2018)					
10. Final domestic demand		37,927.5*	3.9*	4.2	3.6
11. Changes in inventories and net acquisitions of valuables less disposals	P.52 + P.53	N.A.	N.A.	N.A.	N.A.
12. External balance of goods and services	B.11	56.0*	0.7*	–0.2	0.0

* Economic development scenario drafted in accordance with statistical data published by 30 August 2019
Sources: Ministry of Finance, Statistics Lithuania.

PART II
GENERAL GOVERNMENT FINANCES

SECTION 1
BALANCES AND FISCAL POLICY ASSESSMENT

The years 2018 and 2019

In 2018 for the third year in a row, the general government surplus was attained which accounted for 0.6 % of GDP. The year 2018 saw no deviation from the medium term objective which, taking into account the SGP flexibility clause[13], was -1.5 % GDP structural general government balance. In 2018 the structural general government balance accounted for -0.8 % of GDP [14].

[13] The assessment of the indicator of the structural general government balance of 2017 under the SGP takes into account the systemic pension reform implementation costs of 0.1 % of GDP and social model implementation costs of 0.4 % of GDP. The European Commission provided the opportunity to Lithuania to apply for the SGP's flexibility in relation to the social model on 23 May 2017 in its Assessment of the Stability Programme of Lithuania for 2017: https://ec.europa.eu/info/sites/info/files/15_lt_sp_assessment.pdf.

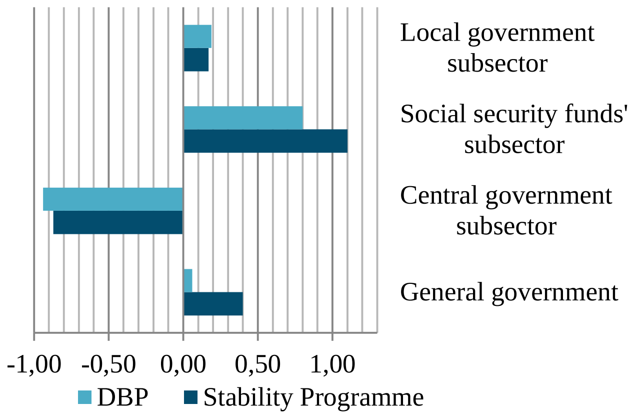
[14] The assessment of the structural general government balance presented in this DBP is based on the output gap calculated on the basis of the economic development scenario and the cyclical budget component.

The Republic of Lithuania Law on the Approval of Financial Indicators of the State Budget and Municipal Budgets for 2019 sets the targeted surplus of general government of 0.4 % of GDP.

Considering the latest budget execution data received by the Ministry of Finance before 15 October 2019, also State, municipal, social insurance funds' revenue and expenditure projections updated in accordance with the economic development scenario, local government balance trends, it is projected that in 2019 general government surplus will account for 0.1 % of GDP.

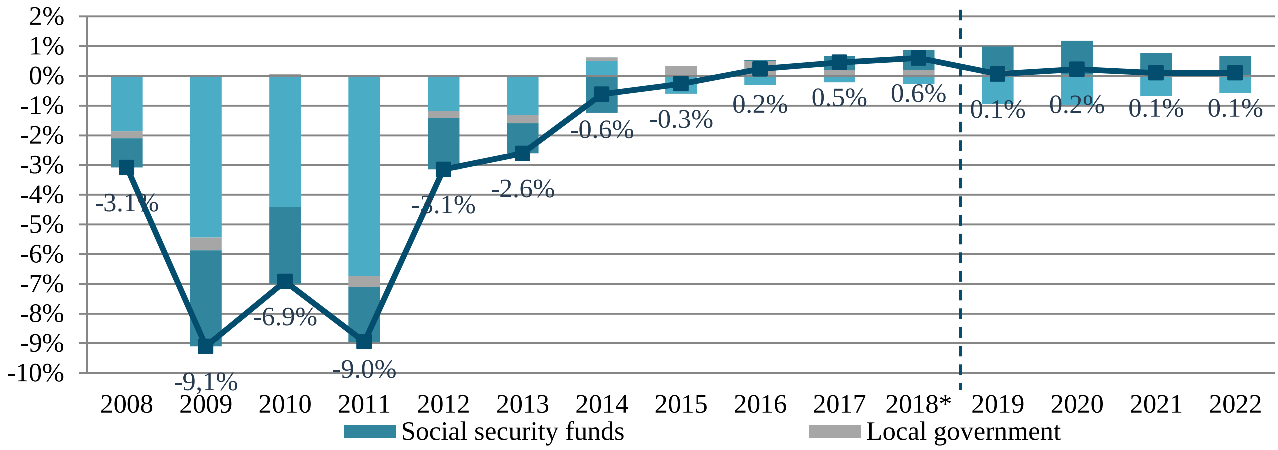
The main reasons for weakening surplus, as compared with the targeted surplus, are lower than planned SSIF budget surplus and higher than planned State budget expenditure. The drop in the SSIF budget surplus, as compared with the estimates presented in the Stability Programme, was a result of reclassification of funds transferred to SSIF budget by the private pension funds. This (0.24 % of GDP) reclassification of funds from revenue to liabilities has been made considering actual data of the first half of 2019. It is projected that the State budget expenditure, considering potential savings, will increase by EUR 109.4 million, as compared with the expenditure presented in the Stability Programme. The main reasons for expenditure growth are a higher demand for funds for contributions to the EU budget, additional expenditure for child's benefits, implementation of NATO commitments, State budget contributions to Pillar II pension funds.

Chart 3. General government sector and subsector balances in 2019, % of GDP



Source – Ministry of Finance.

Chart 4. General government and its subsectors balances in 2008–2022, % of GDP



Sources: Ministry of Finance, Statistics Lithuania.

** After writing off the SSIF debt, central government balance represents –8.4 % of GDP, and the balance of social security funds accounts for 8.8 % of GDP.*

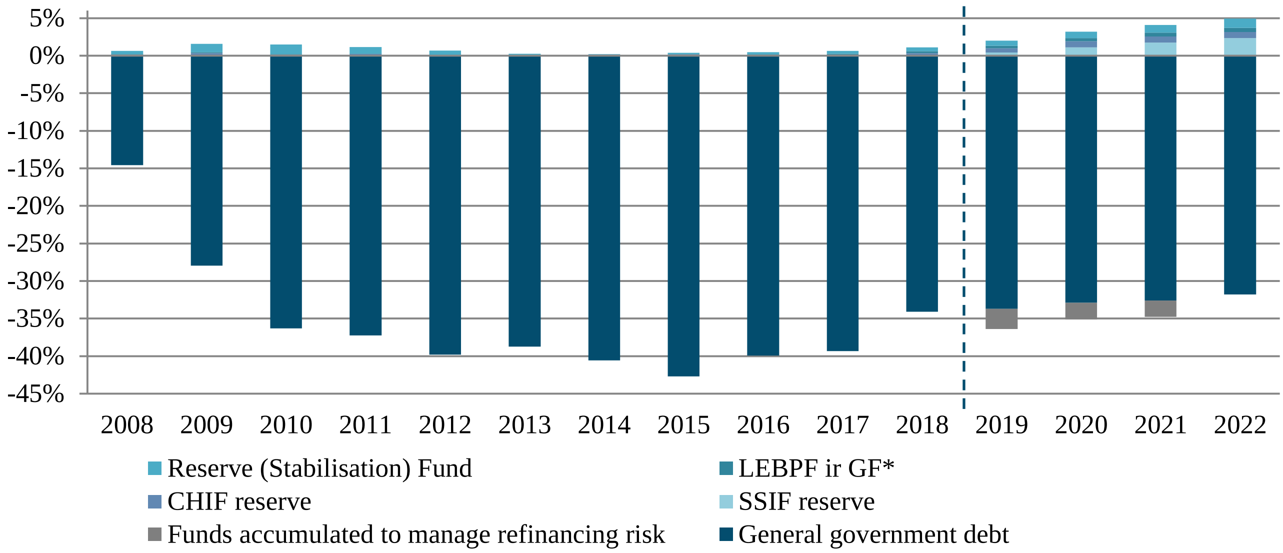
Under more accelerated economic growth than projected during the preparation of the Republic of Lithuania Law on the Approval of Financial Indicators of the State Budget and Municipal Budgets for 2019, it is projected that the 2019 State budget revenue plan in cash terms will be exceeded approximately EUR 73 million (0.8 %). It is planned to collect about EUR 75 million (4.3 %) more than planned from personal income tax due to a faster growth of wage bill.

The structural general government deficit in 2019 will stand at 1.4 % of GDP; it will over perform by 0.1 % of GDP the medium-term objective estimated considering the SGP flexibility clause applied as a result of the social model structural reform. By *ex-ante* assessment, the annual change of 0.7 percentage point of GDP in the structural primary balance in 2019, considering a positive output gap, demonstrates that the fiscal policy pursued in 2019 may become from planned neutral to pro-cyclical[15]. Pro-cyclicality is stemming not only from the projected lower (by 0.3 percentage point of GDP) general government surplus than planned in the Stability Programme, but also from the significantly (from 2 to 3.5 % of potential GDP) increased output gap, as compared with the estimate presented in the Stability Programme.

Year 2020

Considering the EU Council recommendations for the euro area economic policy, Recommendations to Lithuania and Lithuania's economic cycle position, in exploiting still favourable economic circumstances in 2020, the aspirations for further gradual accumulation of fiscal reserves, continuous implementation of structural reforms, increasing general government expenditure for social sphere, fulfilment of NATO commitments and other strategically significant commitments will be coordinated.

Chart 5. General government debt and fiscal reserves, % of GDP



**LEBPF – Long-Term Employee Benefit Fund; GF – Guarantee Fund.*
Source – Ministry of Finance.

While drafting the 2020 budgets, the SGP expenditure growth limitation and structural balance rules as well as national rule of surplus general government sector are applied. The national expenditure growth limitation rule will not be applied in medium term, as the arithmetic average[16] of general government sector balance indicators in 2014–2018 is positive and accounts for 0.1 % of GDP.

Under prevailing external uncertainty, internal challenges of demographic processes and growing economy over its potential, it is important to strive for a surplus general government sector

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[15] Fiscal policy is considered to be neutral if the change in the structural primary general government balance falls within –0.2 and 02 range inclusive.

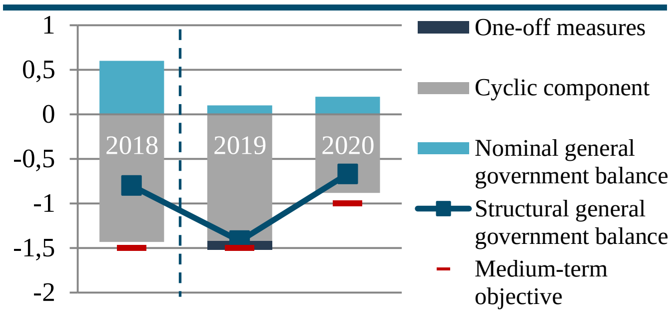
[16] The clause stipulated in Article 3(3) of the Constitutional Law provides for that when the arithmetic average of the general government sector balance of five expired years is positive, the expenditure limitation rule may not be applied.

by applying the revenue and expenditure policy measures (the description of the measures is presented in Section 2). 2020 budgets attributed to general government are planned so that the general government balance is in compliance with a 0.2 % GDP general government surplus stipulated in the Stability Programme, and financial reserves are further accumulated.

In 2020 structural deficit of general government will account for 0.7 % of GDP and will over-perform the medium-term objective by 0.3 % of GDP. Considering the annual change of 0.5 % of GDP of primary structural balance in 2020 and a positive output gap, the counter-cyclical fiscal policy will be pursued in 2020.

The indicators of 2019 and 2020 presented in DBP may change, if in 2019 and 2020 the risks for the economic development scenario or other fiscal risks specified in the Stability Programme and in table 18 materialise.

Chart 6. Structural balance components in 2018–2020



Source – Ministry of Finance.

General government debt

It is projected that general government debt at the end of 2020 will account for 35.1 % of GDP and will be lower by 1.3 percentage point than at the end of 2019, which is planned to reach 36.4 % of GDP. Formed general government surplus and global financial market trends led to reduced interest payment costs.

Table 2. General government debt projections

	2019	2020
	% of GDP	
General government debt at the end of the year	36.4	35.1
Change in general government debt	2.4	–1.3
Contributions to changes in general government debt		
Primary balance	0.8	0.7
Interest expenditure	0.8	0.5
Stock-flow adjustment	5.0	0.6
Implicit interest rate on debt	2.2	1.7

Source –Ministry of Finance.

Table 3. Contingent liabilities

	2019	2020
	% of GDP	
State guarantees	0.8	1.1
o/w: related to financial sector	0.0	0.0

Source –Ministry of Finance.

SECTION 2
GENERAL GOVERNMENT REVENUE AND EXPENDITURE PROJECTIONS UNDER POLICY SCENARIO

Implementing the EU Council Recommendations to Lithuania and considering the Government Programme Implementation Plan approved by Government Resolution No. 164 of 13 March 2017, the provisions concerning the improvement of the structure of the taxation system to make it more favourable for economic growth and optimisation of the tax base, the redistributable GDP share (tax inflows-to-GDP ratio) will be increased in 2020. By increasing excise duty rates on petrol and gas oil, ethyl alcohol and tobacco products, reducing excise duty relief on gas oil used in agriculture and eliminating excise duty relief on heating gas oil, introducing the pollution (registration) tax for vehicles, the tax base less harmful to economic growth will be expanded, thus contributing to the implementation of environmental and health promotion objectives. The planned further gradual increase of non-taxable amount (up to EUR 350 in 2020 and up to EUR 400 in 2021) will lead to reduction of the labour burden by transferring it to other sources the taxation of which has less harm to the economic growth. The 2020 State budget revenue forecast was made also considering the latest economic development scenario, expected positive outcome of administration improvement measures, as well as revenue loss due to existing tax reliefs. It is projected that the State budget revenue (excluding the EU and other international financial assistance) will grow 9.4 % in 2020.

To improve further tax administration, reduce shadow economy and increase GDP redistribution through budget, the following tax administration improvement measures are implemented in III quarter of 2019 - 2020 and planned to be launched (it is projected that in 2020 it will amount to additional revenue of approximately 0.4 % of GDP):

1. Application of the reverse VAT mechanism in case of commercial transactions in electronic goods. Objective – more efficient VAT administration in trade of electronic goods, when VAT is paid not by the vendor, but the purchaser himself which is registered as VAT payer;

2. Development of subsystems of the smart tax administration system (i.MAS):

- A subsystem of smart cash registers (i.EKA). Objective — to enhance efficiency of STI activities and to reduce the administrative burden by replacing the paper (written) form of data administration of retail trade sales and service supply to the electronic form;
- A subsystem of permanent control of taxpayers (i.KON). Objective — to enhance efficiency of STI activities by automatically determining the most risky taxpayers, developing and deploying the smart control process management, thus ensuring the prevention of tax infringements.

3. Introduction of the mandatory construction worker identity card (hereinafter – CID card) and installation of the information system. CID card will ensure real working time recording, reduced possibilities of non-declaring a part of working time and wages;

4. Introduction of mandatory declaration of vehicle transactions and installation of the centralised vehicle owner accounting system. The efforts are made to preclude the conclusion of fictitious contracts in vehicle trade, to offer possibilities for control institutions to identify real vendors (dealers) of vehicles and owners as well as ensure inevitability of tax obligations falling on them;

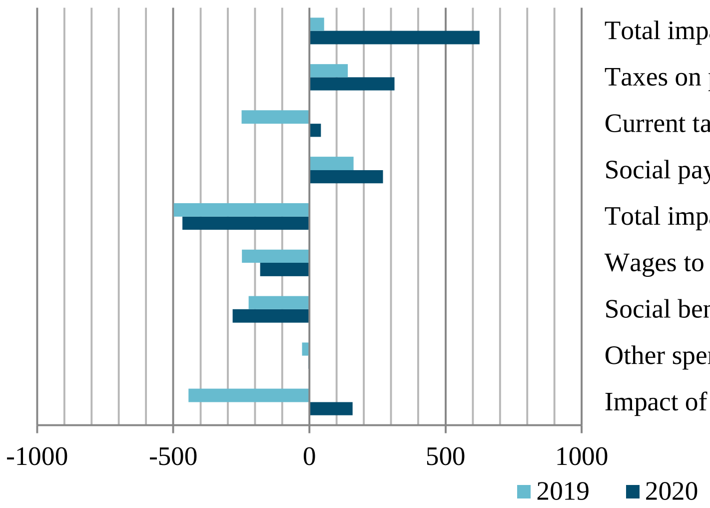
5. Reinforcing controls of tax calculation, declaration and payment by persons engaged in activities in digital platforms;

6. Integration of tasks resolved during the project of the Competence Centre on Analysis, Modelling and Risk Management (i.MAMC) into STI processes, e.g. performed control of potentially risky group of undertakings based on risks of possible tax evasion and aggressive tax planning, by the help of this task the relationship between the undertakings is expeditiously

identified, as well as the chains of transactions between undertakings which disclose potential corporate income tax optimisation schemes. After integration of the pre-bankruptcy prediction model, the debtor's bankruptcy rate will be projected. This information will be used in selecting recovery actions.

The main State budget expenditure growth trends – increase in the child benefit, financing of the implementation of the National Collective Agreement[17], gradually increased financing for national defence to fulfil the NATO commitments. Also, further pursued commitments related to contributions to social security funds for persons insured by the State, as well as larger contributions to the EU budget, financing of indexed basic pension from the State budget. Information on discretionary expenditure measures is presented in table 16.

Chart 7. Discretionary revenue and expenditure measures, % of GDP



Source –Ministry of Finance.

Table 4. General government expenditure and revenue indicators under policy scenario

General government (S13)	ESA code	2019	2020
		% of GDP	
1. Total revenue	TR	35.5	36.7
1.1. Taxes on production and imports	D.2	11.5	12.1
1.2. Current taxes on income and wealth, etc.	D.5	8.7	9.0
1.3. Capital taxes	D.91	0.0	0.0
1.4. Social contributions	D.61	10.1	10.6
1.5. Property income	D.4	0.6	0.5
1.6. Other		4.5	4.5
Tax burden (D.2 + D.5 + D.61 + D.91 – D.995)		30.4	31.7
2. Total expenditure	TE	35.4	36.5
2.1. Compensation of employees	D.1	9.7	10.0
2.2. Intermediate consumption	P.2	5.0	5.0
2.3. Social benefits	D6M	13.9	14.6
o/w: unemployment benefits		0.4	0.4
2.4. Interest expenditure	D.41	0.8	0.5
2.5. Subsidies	D.3	0.3	0.3

[17] The National Collective Agreement signed on 10 July 2019: https://socmin.lrv.lt/lt/naujienos/pasirasyta-nacionaline-kolektyvine-sutartis-darbo-uzmokestis-kitamet-augs-apie-286-tukst-darbuotoju.

2.6. fixed capital formation	P.51	3.6	3.8
2.7. Capital transfers	D.9	0.2	0.2
2.8. Other		2.0	2.1

Source –Ministry of Finance.

SECTION 3
COMPARISON OF INDICATORS IN DBP AND STABILITY PROGRAMME

Table 5. Comparison of GDP in DBP and Stability Programme

	ESA code	2018	2019	2020
		% of GDP		
Real GDP growth:				
Stability Programme		3.45	2.64	2.43
DBP		3.49	3.67	2.43
Difference		0.05	1.03	0.00

Source –Ministry of Finance.

The projections of the general government balance indicator for 2019 specified in the Stability Programme and DBP differ due to a lower SSIF budget surplus than planned and higher State budget expenditure than planned. The projections for 2020 are the same.

Table 6. Comparison of general government net lending (borrowing) in DBP and Stability Programme

	ESA code	2018	2019	2020
		% of GDP		
General government net lending (borrowing) projection under the no-policy change scenario	B.9			
Stability Programme		0.7	1.2	0.5
DBP		0.6*	1.0	–0.1
Difference		–0.1	–0.2	–0.6
General government net lending (borrowing) projection under policy scenario	B.9			
Stability Programme		0.7	0.4	0.2
DBP		0.6*	0.1	0.2
Difference		–0.1	0.3	0.0

Source –Ministry of Finance.

*Actual statistical data under excessive deficit procedure presented to Eurostat on 30 September 2019

Considering the refinancing risk management, updated GDP projections, as well as the 2019 State budget, including the EU and other international financial assistance, general government balance projections, the general government debt level in 2019 is expected to be lower by 0.6 percentage point, in 2020 – lower by 1.1 percentage point, as compared with previous projections specified in the Stability Programme.

Table 7. Comparison of general government debt projections in DBP and Stability Programme

	2019	2020
	% of GDP	
General government debt:		
Stability Programme	37.0	36.2
DBP	36.4	35.1
decrease (–) / increase (+)	-0.6	-1.1

Source –Ministry of Finance.

PART III
BUDGET FRAMEWORK REFORM

The aim of the budget framework reform is to develop a sound and effective medium-term framework of budgeting and programme management that is closely linked to the updated strategic planning system and is integrating strategic, regional and territorial planning processes. Such establishment of close links between budgeting and strategic planning processes is aimed at ensuring a long-term and balanced progress of the State as well as effective planning and use of allocated public finances. The budget framework reform is carried out in two stages. The first stage covers the improvement of the current budgeting framework; the second stage covers the formulation of the rules governing the new structure of the budget framework, budgeting, execution, spending review processes to be launched from 2021.

During the first stage of the reform – in 2019 – three pilot spending reviews were carried out in the spheres of health care, social security and education. The reviews aimed to measure effectiveness of the use of public finances and to determine inefficiently used funds and potential savings. The expenditure (designed for acquisition of remedies: medicines, medicinal solutions, first-aid measures) review of individual health care protection institutions took place. The expenditure attributable to core operational costs of social care institutions and expenditure attributable to environment management of general education schools took place as well. The results of the reviews were included into the budgeting process and used at negotiations for appropriations of the 2020 budget.

Based on the results of pilot spending reviews, the spending review methodology was developed in 2019 which is planned to be incorporated into the legal acts regulating the strategic management system and to be applied in drawing up the budgets for 2021–2023 and subsequent years. It should be noted that in carrying out spending reviews the efforts will be further made to determine non-priority, inefficient expenditure to be cut or to reorganise their structure, as well as to reduce the expenditure level or expenditure growth trends.

To disclose information on budget in a more clear and simple manner and to promote participation of residents in the budgeting process, as in previous year, the public will be presented with the publication “2020 Budget at a Glance” along with the draft 2020 budget. The information is presented in the publication by government activity areas and planned State budget appropriations allocated for them. A new structure of the publication of informative nature will enable the disclosure of information on allocation of the State budget funds in a more clear and understandable for the public manner.

In carrying out the reform works at the second stage, the medium-term budget programme structure model has been developed by separating clearly in the programmes the progress and follow-up activity structural elements and setting for them different performance indicators. At present the basic national strategic planning document – the National Progress Plan is under development, which will set all national medium-term strategic goals and progress tasks for their implementation which will be transferred to the national development programmes drawn up by the ministries. The progress tools and projects will be planned in the programmes, as well as financial projections necessary for their implementation will be presented. For planning the progress tools and projects, the uniform rules will be applied despite financing source. It is planned that the updated Strategic Management Methodology will provide for that the elements (progress tasks, progress tools, projects, their performance criteria) of strategic planning documents (National Progress Plan, national development programmes) will be directly transferred to strategic action plans, i.e. budget programmes of appropriation managers. Follow-up activity elements (follow-up activity tasks, measures and their performance criteria) will be planned in the strategic action plan of the appropriation manager.

The updated framework covering the aforementioned structural changes in budget programmes is planned to be applied in drafting the State budgets for 2021–2023.

PART IV
METHODOLOGICAL ASPECTS

Table 8. Preparation of the economic development scenario

Estimation technique	Budgetary process stage of the technique applied	Relevant features of the models (techniques) used	Assumptions
Principles of national accounting, econometric and expert evaluation	Economic development scenario	Macroeconomic forecasts are prepared for the medium term by using the macroeconomic model developed according to national accounts. In analysis of individual or more than one potentially interrelated macroeconomic indicators, econometric equations are made, also expert evaluation is carried out. Estimates of potential GDP are based on methodology approved by ECOFIN in 2002.	Technical assumptions (oil price, currency exchange rate and interest rates)

Revenue forecasting

Tax revenue forecast is prepared based on macroeconomic forecasts, statistical data, revenue dynamics and the information provided by public authorities. The forecast of revenue from individual taxes may be adjusted through peer review, i.e. considering other circumstances than those provided for in draft amendments that may affect revenue collection.

Depending on the tax, one or several forecasting methods are applied:

- ✓ Detailed modelling method. Data is collected on the number of taxpayers in each category and the total amount of revenue and revenue structure of that category. A simulation model is created from two blocs: typical tax payer and aggregating bloc. According to this model, it is estimated how much on average an individual taxpayer representing a certain group, the entire group and, ultimately, all taxpayers of the country will pay in taxes.
- ✓ Effective average rate method. The tax rate established by law is adjusted considering the applied reliefs, tax base exemptions and etc. The effective average rate thus assessed is multiplied by the scope of the tax base to obtain a forecast of revenue from appropriate taxes.
- ✓ Elasticity method. A relationship between revenue from a tax increase (decrease) and dynamics of an appropriate base is established. The forecast of revenue from the tax is made considering the elasticity coefficient specific to a specific tax and the forecasted tax base changes.

PART V
STATISTICAL ANNEX

Table 9. Key assumptions

	2018	2019	2020
Short-term interest rates (average annual)	0.0	-0.1	-0.1
Long-term interest rates (average annual)	1.2	0.3	0.4
USD/EUR exchange rate (average annual)	1.18	1.13	1.13
Nominal effective exchange rate	5.2	-0.6*	0.5*
Global (excl. EU) GDP growth, %	3.8	3.4	3.6
EU GDP growth, %	2.0	1.4	1.6
Growth of main export markets, %	2.2	1.5	1.8
Global (excl. EU) import growth, %	4.7	1.6	3.1
Oil prices (*Brent*, USD per barrel)	71.5	64.7	61.5

* The European Central Bank updated forecast published on 12 September 2019.

Sources: European Commission, European Central Bank, Ministry of Finance.

Table 10. Price indicators

	2018	2018	2019	2020
	Index	Change, %		
1. GDP deflator	121.2*	3.3*	3.3	2.7
2. Private consumption deflator	114.8*	2.4*	2.4	2.3
3. Harmonised index of consumer prices (in 2015 = 100)	107.1	2.5	2.4	2.3
4. General government consumption expenditure deflator	130.7*	6.8*	8.0	5.0
5. Gross fixed capital formation deflator	113.8*	0.8*	1.3	1.3
6. Export (goods and services) price deflator	110.0*	3.5*	1.3	1.2
7. Import (goods and services) price deflator	106.7*	4.5*	-0.4	0.6

* The economic development scenario drawn up based on statistical data published by 30 August 2019.

Sources: Eurostat, Statistics Lithuania, Ministry of Finance.

Table 11. Labour market indicators

	ESA code	2018	2018	2019	2020
		Indicator value	Change, %		
1. A number of employed population, thou.		1,374.7	1.5	0.7	0.1
2. Employment, hours worked, thou.		2,549,830	2.1	-	-
3. Unemployment rate, %		6.1	-	6.0	5.9
4. Labour productivity (gross value added per one employed), EUR thou.		27.1*	2.0*	2.9	2.3
5. Labour productivity, hours worked		-	-	-	-
6. Compensation of employees, EUR million	D.1	20,221.2	9.5	9.1	7.6
7. Compensation per employee, EUR		16,645.7	7.4	8.3	7.4

* The economic development scenario drawn up based on statistical data published by 30 August 2019.

Sources: Eurostat, Statistics Lithuania, Ministry of Finance.

Table 12. Sectoral balances

	ESA code	2018	2019	2020
		% of GDP		
1. Net lending	B.9	3.1	3.4	3.3
o/w:				
- balance of goods and services		2.6*	3.6	3.9
- balance of primary incomes and transfers		–1.0**	–1.9**	–2.3**
- capital account		1.5**	1.7**	1.7**
2. Net lending/net borrowing of the private sector	B.9	2.5	3.3	3.2
3. General government net lending / net borrowing	B.9	0.6	0.1	0.1
4. Statistical discrepancy		0	0	0

* The economic development scenario drawn up based on statistical data published by 30 August 2019.

** Forecasts for 2019 and 2020 prepared based on the data published by 20 August 2019 (actual data of 2018 used for preparation of forecasts).

Sources: Bank of Lithuania, Ministry of Finance.

Table 13. General government indicators under policy scenario

	ESA code	2019	2020
		% of GDP	
Net lending (+) / net borrowing (–) (B.9) by subsector			
1. General government	S.13	0.1	0.2
2. Central government	S.1311	–0.9	–1.0
3. National government	S.1312		
4. Local government	S.1313	0.2	0.0
5. Social security funds	S.1314	0.8	1.1
6. Interest expenditure	D.41	0.8	0.5
7. Primary balance		0.8	0.7
8. One-off and other temporary measures		0.1	0.0
9. Real GDP growth (%)		3.7	2.4
10. Potential GDP growth (%)		3.7	3.8
O/w:			
- labour factor		0.7	0.6
- capital factor		1.5	1.6
- total factor productivity		1.4	1.7
11. Output gap (% of potential GDP)		3.5	2.2
12. Cyclical component of the budget (% of potential GDP)		1.4	0.9
13. Balance corrected by cycle (1 – 12) (% of potential GDP)		–1.4	–0.7
14. Primary balance corrected by cycle (13 + 6) (% of potential GDP)		–0.6	–0.2
15. Structural balance (13 – 8) (% of potential GDP)		–1.4	–0.7

Source –Ministry of Finance.

Table 14. General government revenue and expenditure indicators under no-policy-change scenario

General government (S13)	ESA code	2019	2020
		% of GDP	
1. Gross income under no-policy-change scenario	TR	35.3	35.4
1.1. Taxes on production and imports	D.2	11.2	11.5
1.2. Current taxes on income and wealth, etc.	D.5	5.8	8.9
1.3. Taxes on capital	D.91	0.0	0.0
1.4. Social contributions	D.61	13.2	10.0
1.5. Property income	D.4	0.6	0.5
1.6. Other		4.5	4.5

General government (S13)	ESA code	2019	2020
		% of GDP	
Tax burden (D.2 + D.5 + D.61 + D.91 – D.995)		30.2	30.5
2. Gross expenditure under no-policy-change scenario	TE	34.4	35.5
2.1. Compensation of employees	D.1	9.2	9.7
2.2. Intermediate consumption	P.2	5.0	5.0
2.3. Social benefits	D6M	13.4	14.1
o/w: unemployment benefits		0.4	0.4
2.4. Interest expenditure	D.41	0.8	0.5
2.5. Subsidies	D.3	0.3	0.3
2.6. Fixed capital formation	P.51	3.6	3.8
2.7. Capital transfers	D.9	0.2	0.2
2.8. Other		1.9	2.1

Source – Ministry of Finance.

Table 15. Discretionary revenue measures taken by general government

No.	Description of the measure	ESA code	Accounting principle	Adoption status	Budgetary impact, EUR million	
					2019	2020
1.	Increase of MMW from EUR 516 to EUR 555 starting from 1 January 2019	D.5	Accrual	Approved	12.4	
2.	Increase of MMW from EUR 555 to EUR 607 starting from 1 January 2020	D.5	Accrual	Approved		14.6
3.	Increase of NTA from EUR 300 in 2019 by expanding the NTA application limit to 2 AW	D.5	Accrual	Approved	–186	
4.	Increase of NTA to EUR 350 in 2020	D.5	Accrual	Approved		–100
5.	Increase of individual NTA for the disabled: for people with greater capability for work up to EUR 600, people with lower capability for work up to EUR 645	D.5	Accrual	Approved		–17
6.	Reduction of PIT rate	D.5	Accrual	Approved	–145.0	
7.	Increase of PIT rate by 9.36 percentage points (under a new system)	D.5	Accrual	Approved	1,663.0	
8.	Application of 20 % PIT rate to the share of other income (except for income from individual activity, dividends and sickness, paternity and maternity benefits, parental leave allowances, benefits related to long-term employment) exceeding 120 AW per year	D.5	Accrual	Approved	10.0	
9.	Introduction of a progressive (27 %) PIT rate	D.5	Accrual	Approved	5.5	
10.	Introduction of a progressive (32 %) PIT rate	D.5	Accrual			13.9
11.	Increase of the wage coefficient applied in calculating refunds of missions (non-taxable daily allowances) from 1.3 to 1.65 (x MMW)	D.5	Accrual			34.6
12.	Application of 20 % PIT rate to income from bonus shares, remuneration for services in the supervisory board, loan committee, income of heads of small partnerships under civil contracts as well as royalties from the employer, when this income does not exceed	D.5	Accrual	Approved	2	

No.	Description of the measure	ESA code	Accounting principle	Adoption status	Budgetary impact, EUR million	
					2019	2020
	120 AW, and application of 27 % of PIT rate when income exceeds 120 AW					
13.	Basic salary amount increase from EUR 132.5 to EUR 134 for State politicians, judges, State officials and civil servants as well as persons employed in public and municipal budget institutions	D.5	Accrual	Approved	6.6	
14.	Funds allocated for the implementation of the National Collective Agreement (incl. increase in basic salary amount)	D.5	Accrual	Approved		26.2
15.	Application of taxation of income of individual activity by granting a tax credit	D.5	Accrual	Approved	4.7	
16.	Withdrawal of a 5 % corporate income tax relief for agricultural companies (except cooperatives)	D.5	Accrual	Approved	1.5	
17.	Expansion of a corporate income tax relief applied to movies by increasing the limit of the amount of funds granted for film making by tax payers to 30 % of the film budget	D.5	Accrual	Approved	-1.6	
18.	Withdrawal of 0 % corporate income tax rate on profits of non-profit organisations which does not exceed EUR 7, 250	D.5	Accrual	Approved	1	
19.	Introduction of the interest limitation rule (upto 30 % of EBITDA or EUR 3,000,000 whichever is higher)	D.5	Accrual	Approved	0.4	
20.	Introduction of vehicle pollution tax	D.5	Accrual			29
21.	Increase of the value reduction coefficient applied to agricultural land from 0.35 to 0.5	D.5	Accrual			1.2
22.	Improvement of administration in relation to the corporate income tax	D.5	Accrual	Approved	10.0	15.0
23.	Improvement of administration in relation to VAT	D.5	Accrual	Approved	30.0	25.0
24.	Increase of excise duty rates on ethyl alcohol and alcoholic beverages	D.2	Accrual		5.6	12.2
25.	Increase of excise duty rates on tobacco products and liquid of electronic cigarettes	D.2	Accrual	Approved	15.6	8.1
26.	Increase of excise duty rates on heated tobacco products from 1 March 2020	D.2	Accrual			7.8
27.	Introduction of the pollution tax on waste going to a landfill	D.2	Accrual	Approved	5.0	2.0
28.	Introduction of VAT relief of 9 % for household consumers on the supplied firewood and wood products for heating	D.2	Accrual	Approved	-7	
29.	Decrease of the reduced VAT rate of 9 % on newspapers, magazines and other periodicals down to 5 %	D.2	Accrual	Approved	-2	
30.	Increase of excise duty rate on diesel fuels	D.2	Accrual			26.2
31.	Increase of excise duty rate on petrol	D.2	Accrual			7.6
32.	Increase of excise duty rate on diesel fuels used in agriculture from 1 January 2020	D.2	Accrual			7.1
33.	Reduction of quotas on diesel fuels used in agriculture by 15 %. Reduced quotas will be applied in issuing permits for 2019–2020	D.2	Accrual			7.8

No.	Description of the measure	ESA code	Accounting principle	Adoption status	Budgetary impact, EUR million	
					2019	2020
	farming year, i.e. from 1 July 2020					
34.	Withdrawal of excise duty reliefs on heating gas oil	D.2	Accrual			16.1
35.	Decrease of the non-taxable amount of the immovable tax for individuals down to EUR 100, 000	D.2	Accrual			8.0
36.	Introduction of the tax for financial market participants	D.2	Accrual			52.2
37.	Introduction of the major trade tax	D.2	Accrual			31.9
38.	Increase of the value reduction coefficient applied to agricultural land from 0.35 to 0.5	D.2	Accrual			5.8
39.	Improvement of administration in relation to VAT	D.2	Accrual	Approved	104.0	110.0
40.	Improvement of administration in relation to excise duties	D.2	Accrual	Approved	20.0	10.0
41.	Increase of MMW from EUR 516 to EUR 555 starting from 1 January 2019	D.61	Accrual	Approved	13.5	
42.	Increase of MMW from EUR 555 to EUR 607 starting from 1 January 2020	D.61	Accrual	Approved		15.3
43.	Basic salary amount increase from EUR 132.5 to EUR 134.2 (EUR 173 under a new system) for State politicians, judges, State officials and civil servants as well as persons employed in public and municipal institutions	D.61	Accrual	Approved	6.9	
44.	Funds allocated for the implementation of the National Collective Agreement (incl. increase in basic salary amount)	D.61	Accrual	Approved		27.5
45.	Reduction of the Long-term Employee Benefit Fund rate by transferring a share to the unemployment insurance contribution rate	D.61	Accrual	Approved	–34.6	
46.	Increase of unemployment insurance contribution rate by transferring share of the Long-term Employee Benefit Fund rate	D.61	Accrual	Approved	40.7	
47.	Impact of the reduced SODRA rate on the ’floor’ for SODRA contributions	D.61	Accrual	Approved	–6.8	
48.	Unification of the social insurance system applied to self-employed (ceiling amounts to 28 AW)	D.61	Accrual	Approved	11.0	
49.	Recalculation of SODRA and compulsory health insurance rates, reduction of SODRA rate and transfer of a share of the rate to PIT for self-employed	D.61	Accrual	Approved	–45.0	
50.	Increase of the taxable base applied to self-employed from 50 % to 90 % of taxable income while at the same time increasing the contribution ‘ceilings’ from 28 AW to 43 AW	D.61	Accrual	Approved	19.0	
51.	SODRA contribution ‘ceilings’	D.61	Accrual	Approved	–11.0	–13.0

No.	Description of the measure	ESA code	Accounting principle	Adoption status	Budgetary impact, EUR million	
					2019	2020
52.	Reduction of the social security contribution rate paid by the employee by 0.55 percentage point (from 13.07 % to12.52 %)	D.61	Accrual	Approved	–99.0	
53.	Reduction of social security contribution rates by 9.36 % (under a new system)	D.61	Accrual	Approved	–1,663.0	
54.	Suspension of SODRA transfers to Pillar II for accumulation of pension from 1 January 2019	D.61	Accrual	Approved	211.0	181.5
55.	Increase of the wage coefficient applied in calculating refunds of missions (non-taxable daily allowances) from 1.3 to 1.65 (x MMW)	D.61	Accrual			31.7
56.	Improvement of administration in relation to social insurance contributions	D.61	Accrual	Approved	56.0	27
TOTAL:					**54.4**	**625.3**

Source – Ministry of Finance.

Table 16. Discretionary expenditure measures taken by general government

No.	Description of the measure	ESA code	Accounting principle	Adoption status	Budgetary impact, EUR million	
					2019	2020
1.	Development of financial incentives and services for young families and families with children	D6M	Accrual	Approved	–8.0	
2.	Increase of social assistance benefits and targeted compensations in implementing new legal provisions (in 2020 increase of social assistance pension base (from 54 % to 56 % of minimum amount of consumption needs) and increase of the small pension bonus cap)	D6M	Accrual	Approved	–32.4	–16.9
3.	Centralisation of the child's rights centres and improvement of the system ensuring the protection of the child's rights	D.1	Accrual	Approved	–7.1	
4.	Increase of officials' pensions as a result of basic pension increase and indexation	D6M	Accrual	Approved	–2.8	–1.8
5.	Increase of MMW from EUR 380 to EUR 400, in 2019 – to EUR 555, in 2020 up to EUR 607	D.1	Accrual	Approved	–13.2	–19.6
6.	Increase of wages for persons employed in budgetary institutions as a result of a basic salary rate increase (increase from EUR 130 to 132 starting as of 1 January 2018; EUR 173 as of 2019, EUR 176 as of 2020)	D.1	Accrual	Approved	–33.5	–52.1
7.	Contributions in relation to persons insured from the State budget funds	D6M	Accrual	Approved	–63.0	–89.9
8.	Increase of the child benefits from EUR 30 to EUR 50 in 2019; from EUR 50 to EUR 60 in 2020.	D6M	Accrual	Approved by the Government, planned in the draft budget	–101.5	–149.04
9.	Indexation of basic rates of social benefits	D6M	Accrual	Approved	–5.1	–20.0
10.	Increase of wages of persons employed in education sector	D.1	Accrual	Approved	–73.3	–54.6
11.	Increase of wages of lecturers, research staff and researchers	D.1	Accrual	Approved	–22.9	

No.	Description of the measure	ESA code	Accounting principle	Adoption status	Budgetary impact, EUR million	
					2019	2020
12.	Increase of wages of persons employed in public and municipal institutions	D.1	Accrual	Approved	–7.2	–13.1
13.	Increase of wages of persons employed in municipal institutions	D.1	Accrual	Approved	–8.8	–15.9
14.	Increase of wages of public health care professionals (in 2020 increase of wages of employees working in institutions subordinate to the Ministry of Health under employment contracts)	D.1	Accrual	Approved	–10.5	–2.0
15.	Increase of remuneration of residents	D.1	Accrual	Approved	–16.6	–0.5
16.	Increase of wages of statutory officials employed in the interior service, prisons, customs offices, State Security Department and prosecutors	D.1	Accrual	Approved	–29.2	–10.2
17.	Increase of wages and financing of additional positions of culture and art workers, STI, Ministry of Justice, courts, Special Investigation Service, Dignitary Protection Department (central government)	D.1	Accrual	Approved	–7.6	–5.4
18.	Increase of wages and financing of additional positions of culture and art workers, STI, Ministry of Justice, courts, Special Investigation Services, Dignitary Protection Department (local government)	D.1	Accrual	Approved	–9.2	–6.7
19.	Remuneration of mediators (as of 2020)	D.1	Accrual	Approved		–0.4
20.	Free meals for pre-primary (as of 1 January 2020) and primary schoolchildren (as of 1 September 2020)	P.2	Accrual	Draft legal act		–4.0
21.	Insurance from State resources of carers for persons with disabilities with the need of permanent care	D.62	Accrual	Approved		–4.0
22.	10 % one-off compensation of State pensions and other social benefits which were cut during the crisis		Accrual	Draft legal act	–9.93	
23.	Support of social undertakings		Accrual	Approved by the Government, planned in the draft budget	–17.0	
24.	Support for housing provided to disadvantaged families	D6M	Accrual	Approved by the Government, planned in the draft budget	–3.3	
25.	Increase of wages of social workers	D.1	Accrual	Approved	–6.0	
26.	Benefits for employees from the Long-term Employee Benefit Fund (according to the Social Model)	D6M	Accrual	Approved	–7.4	
27.	Increase of wages of judges	D.1	Accrual	Approved	–2.3	
TOTAL:					**–497.9**	**–466.1**

Source – Ministry of Finance.

Table 17. Amounts not included in the expenditure benchmark

	ESA code	2018		2019	2020
		MEUR	% of GDP	% of GDP	
1. Expenditure on the EU programmes fully matched by the EU funds' revenue		557.7	1.2	1.7	1.9
1a. of which investments fully matched by EU funds revenue	P.51	308.5	0.7	0.9	1.0
2. Cyclical unemployment benefit expenditure		–48.4	–0.1	–0.1	0.0
3. Discretionary revenue measures		281.4	0.6	0.1	1.2
4. Revenue increases mandated by laws		0.0	0.0	0.0	0.0

Source – Ministry of Finance.

Table 18. A list of medium-term fiscal risks*

Risk	Risk source	Degree of a risk	Likelihood of occurrence of a risk
Activities of state-owned enterprises	Improving or deteriorating performance may increase or decrease the amounts of dividends paid to the State budget	average	average
Deposit and investment insurance	In the event of bankruptcy of credit institutions, central government expenditure would increase due to fulfilment of obligations to depositors	low	low
Increase in the EU budget contributions	National contributions to the EU budget may increase due to acceleration of implementation of the EU 2014–2020 Multiannual Financial Framework and as a result of feasible chaotic UK withdrawal from the EU. Also predicted increase in national contributions to the EU budget under forthcoming EU (2021–2027) Multiannual Financial Framework due to UK Withdrawal from the EU and national economic growth (the major share of contribution is calculated on the basis of the country's gross national income)	average	high
Statistical corrections of national security expenditure data	Significant differences between forecast of acquisition costs of military equipment, weapons and inventories and actual data in general government financial statistics on accrual basis (acc. to ESA) may increase or decrease general government expenditure	high	high
Implementation costs of structural changes	Changing (as compared with projected) economic development has effect on cost assessment of structural changes – costs may increase or decrease	average	high
Political cycle	A higher pressure before elections and during the election year to assume long-term commitments may increase expenditure	high	high
Environment in global financial markets	Changes in global financial markets may increase Government borrowing costs	average	low
Changes in the EU funds	The financing allocated to Lithuania from the EU budget under the EU 2021–2027 Multiannual Financial Framework may decrease	high	high
Natural disasters	Torrential rain, fires, epidemics may increase general government expenditure	average	average
Demographic	Changing age structure of the society, better or worse than expected migration balance may affect the general government	average	average

Risk	Risk source	Degree of a risk	Likelihood of occurrence of a risk
changes	balance either positively or negatively		

** The detailed information on medium-term fiscal risks and their assessment is presented in Section 3 "Risk Assessment" of Part IV of the Stability Programme.*

ANNEX

SOCIAL MODEL IMPLEMENTATION REPORT

The Social model in full was launched from 1 July 2017. It aims to ensure for the employees necessary guarantees and better the work-life balance, and for the employers – to offer more favourable conditions for hiring and maintaining a workforce. In applying more flexible employment relationship, the efforts are made to attract more investments, to create additional jobs, to offer conditions ensuring financial sustainability of the pension system and adequacy of pensions.

A new Labour Code aims to eliminate labour-relation regulatory weaknesses, to reduce the volumes of undeclared work, to promote various forms of employment contracts, to balance the employment guarantees, to coordinate the employment flexibility and security.

New types of employment contracts and increasing number of temporary contracts

624,711 employment contracts were concluded in 2018 (on average 52,000 contracts per month). The employment contracts of indefinite duration represented 76 % of total concluded employment contracts, while temporary contracts – 19 %, other – 5 %. As compared with II half of 2017, the distribution in percentage terms of the employment contracts remains the same. During II half of 2017 the total number of concluded employment contracts makes up 308,452 (o/w: 229,394 contracts of indefinite duration, 65,304 temporary contracts, 1,188 new types of employment contracts).

Total number of employment contracts concluded over II half of 2018 is 314,046. Total number of employment contracts concluded over II half of 2017 and I half of 2018 constitutes 623,857 (approx. 3 % of employment contracts with foreigners), i.e. on average about 52,000 contracts per month.

The decreasing trend of temporary employment contracts is observed (in II half of 2017 the number of temporary employment contracts was 65,304, in I half of 2018 – 59,049 temporary employment contracts, i.e. decreased by approx. 10 %). Over 2016 total number of hired persons made up 610,466. In 2017 – 624,562 persons.

Though the number of concluded employment contracts of indefinite duration is still the highest, however the number of temporary employment contracts has also increased; this demonstrates the enhanced flexibility of the labour market. In total number of contracts valid on 31 December 2018 temporary employment contracts represented 5.2 %.

Total number of concluded new employment contracts over II half of 2017 was 1,185, while over II half 2018 – 1,717. The most popular type of new employment contracts – project type work contracts, their number increased from 883 contracts in II half of 2017 to 1,364 contracts in II half of 2018. The number of apprenticeship contracts increased more than twofold (155 contracts in II half of 2017 and 352 contracts in II half of 2018).

Table 19. New types of employment contracts

	II half of 2017	I half of 2018	II half of 2018
Project type work contract	883	1,890	1,364
Apprenticeship contract	155	262	352
Employment contract for work for several employers	128	270	227
Site sharing contracts	13	9	1

Source – Ministry of Social Security and Labour.

The number of new types of employment contracts, other than site sharing contracts the number of which in II half of 2018 decreased, is growing. This demonstrates that new type contracts are required.

More flexible termination of employment contracts

The distribution of basis for termination of employment contracts remains analogous: the major share of employment contracts, approx. 73 %, is terminated on the employee's initiative without valid reasons, on the employer's initiative – 5 %, by common agreement between the parties – approx. 5 % of employment contracts. In 2017 at the request of an employee without valid reason were terminated 72.29 % of employment contracts, by common agreement between the Parties – 5.3 % of employment contracts and on the employer's initiative – 0.9 % of employment contracts. In 2018 71.6 % of employment contracts were terminated at the request of an employee without valid reason, by common agreement between the parties – 5.37 % of employment contracts and on the employer's initiative – 1.65 % of employment contracts.

The employers are increasingly using the possibility to terminate the employment contract at employer's request (by paying out the average salary severance compensation of no less than six months): in II half of 2017 the number of terminated employment contracts was 125, over 2018 – 381 employment contracts. However, the number of termination of the employment contract at employer's request is not as high as anticipated by trade union organisations.

Long-term employee benefits

Since 1 July 2017 the employees, who have been dismissed at employer's request in absence of the employee's fault, have the possibility of receiving a long-term employee benefit. The benefit may be paid to a person who till the date of dismissal at the same employer has been working continuously for more than 5 years; has been dismissed at employer's request in absence of the employee's fault; during 3 months after the date of dismissal does not get job with the same employer; applied for the benefit no later than within 6 months. The amount of the long-term employee benefit depends on continuous working relationship with the same employer.

Over 2018 the Long-Term Employee Benefit Fund generated EUR 52,352 thousand, while paid out – EUR 6,512 thousand. In 2018 in private sector at employer's request were dismissed

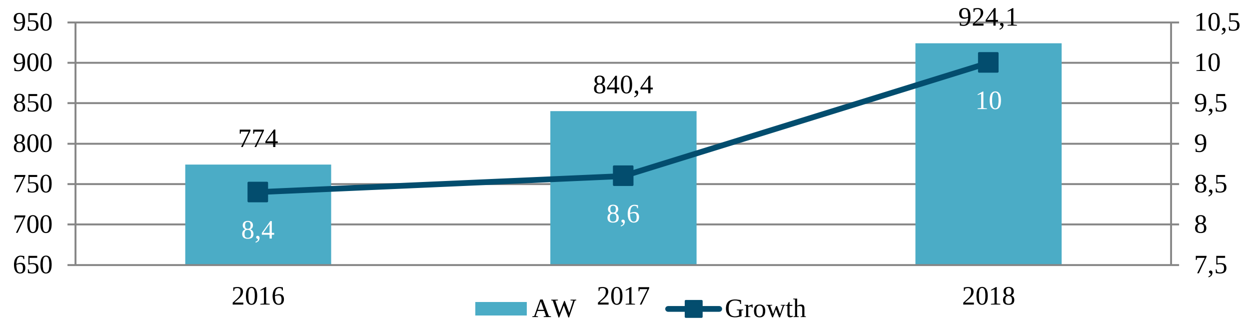
3,986 persons who had been working in one workplace for 5 and more years. It is estimated that in 2018 long-term employee benefits were paid out to 4.4 thousand persons. The average amount of the benefit – EUR 572.6.

Wage growth

In recent years wages are rapidly growing. In 2017 the average monthly gross wages (AMGW) grew 8.6 % (up to EUR 840.4), in 2018 the growth was 10 % (acc. to the data by Statistics Lithuania), in 2018 AMGW made up EUR 924.1).

AMGW growth in 2018 was governed by the following factors: MMW increased up to EUR 400 (previously EUR 380) (MMW increase had effect on AW growth in 2018, as compared with 2017); enforced provision of the Labour Code that MMW is paid only for unskilled jobs; commenced lower limit of social insurance contributions; increasing shortage of workforce.

Chart 8. Wage growth



Source – Ministry of Social Security and Labour.

In October 2018 2.5 % of full-time employees who worked in the national economy earned MMW. In total, 25.5 thousand persons earned MMW. Over the year the share of employees earning MMW decreased by 0.8 percentage point. This was driven by the MMW increased from 1 January 2018, corrected minimum coefficients of the fixed portion of the salary for skilled employees in budgetary institutions.

Table 20. Minimum monthly wages and portion of lower-wage earners, %

Year	Sector		
	National economy, including private companies	Public sector	Private sector, including private companies
2014	9.2	5.7	10.9
2015	8.8	5.9	10.2
2016	9.8	6.8	11.3
2017	3.3	3	3.4
2018	2.5	2.2	2.7

Source – Statistics Lithuania.

Table 21. Employees earning MMW and less, per cent of total number of insured persons

01/01/2014	01/01/2015	01/01/2016	01/01/2017	01/01/2018	01/01/2019
23.4	23.3	25.6	23.6	17.1	15.5

Source – Statistics Lithuania.

Increased employee representation

Out of 108,797 economic entities operating in the Republic of Lithuania, despite their size, number of employees and legal status, to date the State Tax Inspectorate (STI) collected the data on approx. 42,585 economic entities and employee representation in these entities. According to the data by STI, till 31 December 2018 in 16,578 economic entities (39 %) the employees were represented by appointed representatives (some undertakings apply several different types of representation). It was observed that in 4,904 cases the employees in economic entities were represented by the works council (30 % of economic entities, where the employees were represented), employees represented by the trade union – 1,351 cases (8 %), employees represented by the trade union of the economic branch – 138 cases (almost 1 %). In majority cases – even 65 % – in the economic entity the staff attorney is elected instead of the work council (10,769 cases). In 3,247 economic entities, in total, the signed collective agreements are in force, of which in 425 – provisions of branch collective agreements.

A number of collective agreements in Lithuania

The Collective Agreement on Basic Salary at national level for the first time was concluded on 5 November 2018 and applied in 2019. While the National Collective Agreement for 2020 was concluded on 10 July 2019. Also, according to the data of September 2019, 10 collective agreements at branch level and 256 collective agreements at employer level were registered in the Ministry of Social Security and Labour and currently valid. It should be noted that till the new Labour Code came into force, the collective agreements at employer level were not registered.

Labour market forecast

The officials of the Employment Service via stratified random sampling method interviewed 4.5 thousand employers whose undertakings employ 238 thousand employees of the country. 24 % of employers expect the number of employees to grow (will be the same – 71 %, decrease – 5 %); 42 % expect the wages of employees to grow (will not change – 57 %, decrease – 1 %); 35 % plan investments in equipment and technology (that investments in principal will not increase was affirmed by 62 %, that investments will decrease – 3 % of the interviewed)

According to the data by the Employment Service, in 2019 national employers plan to create 32.6 thousand new jobs, of which 51 % will be created in the service sector. Thus, the number of employees and concluded employment contracts should grow about 5 % in 2019.

Changes of the terms of unemployment benefits and increase of this type of benefits

To increase the number of the insured with the right to the unemployment benefit, the amendments have been made to the Republic of Lithuania Law on Unemployment Social Insurance (came into force on 1 July 2017) and established that the right to the unemployment benefit have the persons with the unemployment insurance period of 12 months during the last 30 months (instead of 18 months during the last 36 months) before registration in the Employment Service.

The Law on Unemployment Social Insurance embeds a new formula for calculating the unemployment benefit by linking the amount of benefit with MMW. The period for paying out the unemployment benefit has been extended to 9 months.

The adopted amendments to the Law on Unemployment Social Insurance led to the increase in coverage of persons receiving unemployment benefits by 10 percentage points: from 30 % to 40 % of all registered unemployed persons. The number of beneficiaries also increased almost by one third – from 42.6 thousand on average per month in 2017 to 57.9 thousand in 2018. The average unemployment benefit, as the year 2018 compared with 2017, increased by more than 36 %.

To ensure financing of the unemployment benefits, the unemployment insurance premium rate from 1 July 2017 was increased by 0.5 percentage point up to 1.6 %. This increase boosted the revenue of the State Social Insurance Fund budget of 2017 by EUR 31.3 million. For 2018 a lower unemployment insurance premium rate by 0.2 percentage point was approved by designating these funds to unbalanced sickness social insurance. For 2019 after a transfer of a share of the rate of the premium to the Long-Term Employee Benefit Fund for unemployment insurance, the unemployment insurance premium rate of 1.31 % has been approved.

Reduction of overall rate of the state social insurance contribution for employers

Implementing the reform, the decision was made to reduce the employers' pension social insurance contribution rate, to finance the basic pension from the State budget. It was decided to do it gradually and pursuing fiscal discipline.

Thus, from 1 July 2017 the insurers' pension contribution rate was reduced from 23.3 % to 22.3 %, the unemployment insurance contribution rate, due to higher and paid for a longer period unemployment benefits, was increased by 0.5 percentage point up to 1.6 %. To offset the reduced 1 percentage point of the pension contribution rate, it is planned to allocate target appropriations from the State budget. EUR 61.5 million was allocated for II half of 2017. In 2018 EUR 134.8 million were allocated to offset the general part of pension. In 2018 the decision was made to finance the whole general part of pension from the State budget funds starting from 1 January 2019. For this reason the amount of EUR 1,772.1 million is foreseen for 2019.

The tax system was reformed in 2019 in order to reduce the amounts of social insurance contributions, to make the wage taxation fairer and clearer, pension, sickness and maternity social insurance contributions paid by the employer were transferred to the insured person. To ensure fairer social guarantees, to strengthen the interlinkage between contributions and benefits, social insurance contribution 'ceiling' has been set up.

Increased quality of social protection for self-employed

Social insurance for self-employed was unified and expanded on 1 January 2017. These persons were started to be insured additionally by sickness social insurance, while the owners of private companies, members of small communities and full members of economic partnerships – also by unemployment social insurance.

In 2017 the decision was made and came into force since 2018 to unify taxation of self-employed (abolished requirement to pay social insurance contributions from MMW). All self-employed persons who declare income, pay social insurance contributions from half of declared taxable income or amounts withdrawn for their needs). A one-year ‘holiday’ for social insurance contributions was legitimised for start-ups, i.e. one year from the start of the first activity the self-employed persons may not pay social insurance contributions, however, in this case, this period will not be included into work experience and during this period they will not be considered to be insured under a social security.

After a transfer of the major share of social insurance contributions paid by the employer to the insured person since 2019 and after establishment that the general part of pension is in full financed from the State budget, social insurance contribution bases for self-employed persons were also revised, accordingly. They were changed so that the tax burden for self-employed persons does not increase.

Table 22. The amount of social insurance contributions of self-employed persons, EUR thousand*

Actually paid in 2017	Actually paid in 2018	Approved in 2019
69,492	88,653	66,230

Source – Ministry of Social Security and Labour.

**Self-employed persons have to pay current- year social insurance contributions till 1 May next year.*

Financial sustainability of the pension scheme and adequacy of pension levels

Republic of Lithuania Law No. XII-2512 Amending the Law No. I-549 On State Social Insurance Pensions of 29 June 2016 implements the following main changes in social insurance pension scheme – automatic pension indexation is based on wage bill growth rates (considering the mean variation in wage bill of previous 3 years, current year and 3 forecast years) and strengthened requirement for compulsory work experience from 30 to 35 years increased every year by half a year from 2018 to 2027.

When the pension index calculation rule based on a 7-year wage bill growth indicator came into force from 1 January 2017, the main indicators of the retirement pension – the basic pension and insurable earnings – were increased by 7 %. The major share of planned costs for 2017 under social model (EUR 167 million) was allocated to financing the increased pension expenditure as a result of automatic indexation. Actual expenditure on pension indexation remained unchanged. However, the decision on additional increase of social insurance basic pension by 8.3 % (from EUR 120 to EUR 130) made in September 2017 led to the increase in the average retirement pension in December 2017, as compared with the same month in 2016, where instead of planned 7 %, it increased by 12.4 % (from EUR 255.4 to EUR 287.09). Pension expenditure in 2017, as compared with 2016, increased by EUR 180.96 million, or 0.43 % of GDP. These measures enabled the growth of 8.7 % of the average annual retirement pension in 2017 – the same as AW growth in the country.

In 2018 pensions were indexed by a 6.94 %. The planned increase in pension expenditure due to indexation was EUR 170 million. However, actual expenditure amounted to about EUR 185 million. Pension calculations made following the Republic of Lithuania Law on State Social Insurance Pensions, which came into force on 1 January 2018, (due to changed calculation formula) necessitated approx. EUR 89 million additional funds, as compared with planned expenditure of EUR 59 million. This increase occurred due to the possibility of a more precise inclusion into pensionable service (by 31 December 2017 all pension was automatically included for employed retirement pensioners and old pensions recalculated based on actual pension service, other than only all years of work experience and upon request by a person, as it was required according to the old law) and more favourable method of calculation of the retirement pension for retirement-age beneficiaries of disability (work incapacity) pension. In comparison of the average annual retirement pension in 2017 and 2018, the growth of even 15.1 % is observed and the average retirement pension ratio, as compared with AW in the country, grew from 33 % to 34.6 %.

Table 23. The amount of social insurance contributions of self-employed persons, EUR thousand *

Year	2015	2016	2017	2018	2019*
Average national gross wages	714.1	774	840.4	924.1	1,290
Average retirement pension	244.63	255.28	277.46	319.4	344.8
Growth of average retirement pension, %	1.9	4.4	8.7	15.1	7.8
Pension replacement rate (gross)	34.3	33.0	33.0	34.6	34.5

Source – Ministry of Social Security and Labour

**Projected wages, average retirement pension and its growth; pension replacement rate is calculated by eliminating tax changes.*

The positive effects on social environment have been observed, as all social insurance pensions increased and this increase involved approximately 800 thousand beneficiaries. Thus creating the opportunity to decrease the risk of poverty.

Due to a rapid wage growth and improving employment, the pension index keeps further to be high – in 2019 it represents 7.63 %. The funds for indexation of pensions are projected in 2019 to amount to EUR 221 million. Also, in 2020 and 2021, according to the economic development scenario drawn up by the Ministry of Finance on 11 September 2019 it is projected that pensions will grow 8.11 % and 7.55 % , accordingly, and funds for indexation will, accordingly, amount to EUR 239.8 and EUR 246.2 million. In 2022 the pensions, according the same scenario, will grow 6.97 % and this will require EUR 242 million.

At the current stage, the pension scheme generates surplus. In long-term, when based on demographic and macroeconomic assumptions, an adverse impact of aging society will increase (deteriorating ratio between the employed and persons receiving pensions), the pension scheme measures planned according to a social model will start functioning as scheme measures maintaining financial stability. Automatic indexation of pensions based on wage bill growth will act as the fiscal stability factor – it will not allow the pension growth at wage growth rate under falling employment and slowing GDP growth. The strengthening requirement for compulsory work experience from 30 to 35 years to receive a full size gross pension will enable not to assume more commitments under longer life expectancy.

A long-term effect of the aforementioned pension reform measures, after elimination of the effect of changes in demographic and macroeconomic assumptions, i.e. the comparison of pension expenditure before and after the reform (% of GDP), was calculated and presented in table 19

"*Decomposition of the difference between 2015 and the new public pension projection (% of GDP)"* of the Lithuanian pension projections 2018 (task of pension projections in the EC 2018 Ageing Report).

Table 24. Changes in pension expenditure due to policy measures, % of GDP

2016	2020	2030	2040	2050	2060
0.07	0.4	–1.0	–2.5	–3.1	–3.6

Source – Ministry of Social Security and Labour.