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UN ESTUDIO SOBRE EL IMPACTO ECONÓMICO DE LA ADHESIÓN DE LOS PAÍSES BÁLTICOS A LA UNIÓN EUROPEA

(A STUDY ABOUT THE ECONOMIC IMPACT OF THE BALTIC COUNTRIES' ACCESSION TO THE EUROPEAN UNION)

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ATR Law- The Administrative-Territorial Reform Law

C- Consumption

CAP- Common Agricultural Policy

CPI- Consumer Price Index

CSCE- Commission on Security and Cooperation in Europe

CY- Cyprus

CZ- Czech Republic

DE- Denmark

EA16- Euro Area of 16 countries

ECB- European Central Bank

ECOFIN- the Economic and Financial Affairs Council of the European Union

EDP- Excessive Deficit Procedure

EE- Estonia

EEK- Estonian kroons

EFSF- European Financial Stability Facility

EFTA- European Free Trade Area

EMP- Exchange Market Pressure

EMU- European Monetary Union

ERDF- European Regional Development Fund

ERM II- Exchange Rate Mechanism

ES- Spain

EU- European Union

EU27- European Union of 27 countries

EUBSR- European Union Strategy for the Baltic Sea Region

EUR- Euros

FDI- Foreign Direct Investment

G- Government spending

GDP- Gross Domestic Product

HICP- Harmonized Index of Consumer Prices

HU- Hungary

I- Investment

IM- Imports

IMF- International Monetary Fund

LT- Lithuania

LTL- Lithuanian litas

LV- Latvia

LVL- Latvian lats

NA- National Accounts

NAIRU- Non Accelerating Inflation Rate of Unemployment

NCB- National Central Bank

NEET- Not in Education, Employment or Training

NPISH- Non-Profit Institutions Serving Households

OECD- The Organization for Economic Co-operation and Development

PL- Poland

R&D- Research & Development

SGP- Stability Growth Pact

SI- Slovenia

SK- Slovakia

SPS- Single Payment Scheme

SSR- Soviet Socialist Republic

TFEU- Treaty on the Functioning of the European Union

TFR- Total fertility rate

UK- United Kingdom

UN- United Nations

VAT- Value Added Tax

X- Exports

ABSTRACT

Hace ya diez años desde que los países bálticos entraron a la Unión Europea y, a día de hoy, poco se sabe sobre lo que esto ha supuesto para ellos en este país. Mediante el siguiente estudio, lo que pretenderemos será conocer cuáles han sido los principales efectos económicos que la adhesión al grupo europeo ha supuesto para estos estados y si han sido favorables o no. Desde temas tan generales como la demografía, pasando por los principales aspectos de un país como el crecimiento económico o la inflación hasta el tema del comercio extranjero, haremos un repaso de las tres naciones analizando los resultados obtenidos de cada una de ellas. También, al final de este trabajo, encontraremos un apartado más específico, dedicado a la revisión de las relaciones comerciales entre España y Estonia, Letonia y Lituania.

Palabras clave: *Efectos económicos; Unión Europea; adhesión; Estonia; Letonia; Lituania*

ABSTRACT

The Baltic countries accessed to the European Union for ten years now and still nowadays in this country we do not know what this event has implied to them. Through this study, the intention will be to have a clearer idea about the economic effects in these states which come from the joining to the European group and if it has been positive to them or not. From general issues as demography, explaining then the main topics of a country's economy such as growth rates or inflation, to international trade, we are going to analyze all aspects to draw relevant conclusions about individual countries. At the end of the report, we have focused in a more specific subject like commercial relations between Spain and Estonia, Latvia and Lithuania.

Key words: *Economic effects; the European Union; accession; Estonia; Latvia; Lithuania*

1. INTRODUCTION

2014 is a year with an important meaning for these three countries. In this date, at the Baltic region, there are two historical events that changed in that moment their concept as a country.

Starting from the oldest event, 25 years ago, on 23 August 1989, Baltic population started a pacific movement, the Singing Way, demanding their independence from the Soviet Union. Many things happened from this protest to the official date when Russia accepted them as countries, but it was that day when population realized that they wanted their country free, independent of any occupation.

The second episode changed the Estonian, Latvian and Lithuanian states in others in accordance with the current economic situation, being part of one of the main international groups of the world, the European. With the accession on 1 May of 2004, the Baltic region left to be isolated from the rest of economies and started to have the benefits of being a EU member, such as the common market, financial support, free movement of people and even the possibility of joining to the monetary union, but this only if they fulfil the criteria asked.

With any doubt, the joining to the European Union has done that these three countries can be closer to us. Most of times in this country, if we asked people about the Baltic economy the answer would be nothing. There is an absolute lack of knowledge about this region and everything around it. We know where they are, but about other aspects such as employment, national production, public finances... the gap is quite surprising.

We are in a global economy, where every day millions of transactions (monetary, commercial, business...) are done between different parts at different countries. So, in a dynamic economic situation like this, it is advisable to pay attention to all economies in the world.

In 2000, the group formed by Estonia, Latvia and Lithuania was called “Baltic Tigers”, as the “Asian Tigers”, because of their great growth rates at the first part of 2000’s. Nowadays, 10 years later, that power has not disappeared, so what we will try from here to the end of this study, is to know what has been the impact of being at the European Union to these countries, if it has collaborated with the growth or not.

2. OBJECTIVES

The objective of this study is to know the impact on the economy of Estonia, Latvia and Lithuania owed to the accession to the European Union. As this event was ten years ago, we are going to use information from 2004 to 2014.

Within this period what we want to analyse is the development of some relevant economic aspects such as national production, inflation, unemployment and labour market situation, interest rates, exchange rates, public finance, imports and exports and FDI. Also, there will be a part just for Spanish and Baltic trade relations, where we expect to know if the integration to the group of the Baltic countries has reinforce exchanges of goods, services and capital between both.

Data collection will be through international data bases as can be Eurostat, International Monetary Fund, European Central Bank… but also there will be some statistical information that will have to be extracted from national statistical offices from these countries (Statistics Estonia, Central Statistical Bureau of Latvia and Statistics Lithuania). Once all data will have been extracted, the use of graphs and tables is quite important to can compare between different years and countries.

Once we will have all data collected and analysed, we are going to try to create a relation between what has happened in these countries along the ten years since they entered at the European Union and the fact of being in the group.

The practical use of this study is to know how relevant is for developing economies being in an economy union as the European Union is. Also, it is useful to know about the Baltic economy, if there is any expectancy of becoming relevant economies at the group or not. Around the Baltic countries and their development there is not too much information about, so this report will try to concentrate all economy of Estonia, Latvia and Lithuania and analysed their current situation and how they have reached that point.

3. METHODOLOGY

To make a research, empirical facts are important to give a meaning about what books say. To obtain that information, people in charge of looking for it will have two possibilities of information, primary and secondary.

Secondary information is data extracted by other person, so it can be easier or not the use of this data, because results have been selected following author's criteria. Primary information is data observed and collected by ourselves. Because of the kind of this study using primary data is impossible, because we are dealing with historical data and we will have to make the information research through information observed in that time.

International statistics from institutions like Eurostat, the International Monetary Fund, the European Central Bank, International Labour Organization or the Organization for Co-operation and Economic Development have been essential for the success of this study. These organizations published information about all aspects related with countries (economy, politics, society...) at least once a year. We can't forget too, national Statistical services of these countries, Statistics Estonia, Central Statistical Bureau of Latvia and Statistics Lithuania, which in most of cases support the function of international statistics data bases.

Also, it has been used information coming from other resources such as reports, mainly from the European Commission, the Council of the European Union, but also from national Ministries of these countries, to give meaning to numbers extracted from statistics.

Books and articles of economic journals as the Baltic Journal of Economy have been the support for the theoretical part of the study. This part is important to create a common base for possible distortions at the economical behaviour of Estonia, Latvia and Lithuania.

4. GENERAL ASPECTS

As a first approach to the Baltic States, we will start with the historical and geographical topics. The history and geography of a country determine its culture and can help us to understand some developments at the economy.

In this case, we will see that Estonia, Latvia and Lithuania will have a close relation in several parts of this study as consequence of a common part of their history and the fact of being neighbour countries.

4.1HISTORY

The last part of Baltic countries' history begins around twenty five years ago and contains two important dates: their independence from the Union of Soviet Socialist Republics and their joining to European Union.

The first event started when Mikhail Gorbachev, General Secretary of the Soviet Union in that time, went further than his predecessors and established an innovative economic plan which consisted on an absolute restructure of the economy of the group. The structural conversion lead to those countries which Soviets had took by force felt that they were excluded of the process, which would end in a high number of popular revolutions along all occupied nations, including the Baltic ones.

At the end of 1989, there was an independence movement created in the Baltic triad whose result was the Singing Way, a human chain where citizens from the three countries joined their hands among more than 650 kilometres, from Tallinn until Vilnius. After this social revolution, they would get that they do not have to follow the new Soviet economic plan, in other words the economic independence from Moscow and, consequently, the first step to the freedom.

Once they had reached the control over their economies, the next step was the political independence. In Estonia, in May 1990, at the first general elections since 1940, the winner party proclaimed the Republic of Estonia totally separated from Soviet Union.

Nevertheless, the date when Soviet country accepted this consideration was on 6 September 1991 and in that moment they joined also to UN and CSCE.

In the case of Latvia, the independence process was similar. In 4 May 1990, general elections were won by an independence-ideology party who established a transition period until the real independence. The global acceptance of Latvia as a country did not happen until 21 August 1991, when the Latvian Supreme Council accepted the Constitutional Law of 1922 which, in Chapter 1, article 1, says: "*Latvia is an independent democratic republic*" (Saeima, 1922). Although, they considered themselves independent the data of the independence is 23 August 1991, when Russian accepted Latvia as a country.

We could say that the most controversial independence process was the Lithuanian one, because during the period when they tried to get their self control, the Soviets invaded them in several times. After the Singing Way, this territory declared itself independent from the Soviet Union on 11 March 1990. Lithuania was the first of the three Baltic nations that started this procedure, so, the Russian Federation decided to occupy Vilnius militarily, to avoid any revolution in the other two, but they left the city in January 1991, after thirteen citizens were killed. The official independence date of Lithuania is the 17th of September of 1991, when Soviet Union recognized it.

The second event of their recent history is the application and joining European Union. The application procedure started in Estonia in 1998 (Government of Estonia, 2014) and in Latvia (Ministry of Foreign Affairs of the Republic of Latvia, 2005) and Lithuania (Lietuvos Respublikos Vyriausybė, 2014)in 1995. But it was in 2002 when they were officially invited to join to the European Union during a summit in Copenhagen (n.n., Europe prepares to make history, 2002).

TABLE 4.1 Results of the Referendum on the Accession to the European Union, 2003 (percentages)

	YES	NO	Electorate	Votes	Valid votes	Invalid votes
Estonia	66.83%	33.17%	100.00%	64.06%	63.74%	0.31%
Latvia	67.49%	32.51%	100.00%	71.45%	70.90%	0.55%
Lithuania	91.07%	8.93%	100.00%	63.37%	62.59%	0.78%

Source: Own elaboration based on European Election Database data

Population of the three countries voted in favour of the European Union and the proposals that it would bring to them. Being a member of the group means improving their political and economic profile, really important for international business. The Lithuanian absolute majority is due to that voters understand the benefits that the EU could provide to them such as: the opening of new possibilities of business at European common market, strengthening and fostering the modernization of the country through judicial regulation, financial support and structural reforms…, the possibility of travelling, working, studying in another European country without having to fill documents or having the right to influence the EU decision-making process to enhance the impact of the country on the policy formation (Lietuvos Respublikos Vyriausybė, 2014)

This fact is relevant to have a clearer idea about the relationship of Baltic countries and Russia, because it implies that they are in favour of Europe instead of Russia. Not all population was satisfied with the result as happened in Latvia. In a new of the newspaper The New York Times (Latvia Votes to Join The European Union, 2003) was reflected that some part of Latvian population disagreed with the addition to the EU because it reminded to them the same as the Soviet Union was some years before and, therefore, their interest as country would not be taken in consideration by the European group. Also, in this country there is a Russian minority who was worried about the possibility of a distance with Russia, but this concern was not reflected at the referendum owed to the fact that they were not Latvian citizens, consequently they could not vote.

Once Governments made official their application for the European Union, they signed the Treaty of Amsterdam and then, in 2003, they will sign the Treaty of Nice. Therefore, they will be members of the European Union since 1 May 2004 and that means that have the same rights as the other countries, which were part of the group before, for "*free movement of goods, persons, services and capital*" as Maastricht Treaty says in Title II, art. G,b,2,a (Treaty of Maastricht, 1992).

As a consequence of the previous mentioned agreement, also two of the three Baltic republics have changed their currency to the Euro. In Title I, article B (Treaty of Maastricht, 1992), it declares: "*The Union shall set itself the following objectives: […] the establishment of economic and monetary union, ultimately including a single* *currency in accordance with the provisions of this Treaty*". Despite the fact that some of the strongest countries in the Union such as United Kingdom or Denmark have rejected adopt the Euro as their national currency, for Estonia which adopted it in 2011 and Latvia in 2014. Finally, Lithuania fulfils the convergence conditions (European Commission, 2014a,) will join to the Euro area in 1 January 2015. The fact of having the same currency will make even easier capital transactions, trade, movement of citizens among countries, etc.

4.2 GEOGRAPHY

Baltic countries are located at the North-East part of Europe. Following a geographical order from North to South, Estonia is the first country, then Latvia and, finally, Lithuania. The Eastern and Western frontiers are equal at the three countries, in the East we find Russia and at the West it is the Baltic Sea. At the South, Lithuania borders with Poland and at the North, Estonia borders with the Baltic Sea.

The area of these nations is smaller in contrast with their neighbouring countries as Poland or Finland… The Estonian area is of 45,228 km^2, the Latvian of 64,589 km^2 and of 65,303 km^2 the Lithuanian one.

About other physical aspects, their height above sea level is not too elevated. The highest parts are located in some areas of Latvia and Estonia with 300 meters high. Consequently, there is not any mountain in the Baltic region. In contrast, the water is a significant natural resource represented by numerous lakes, rivers…of glacial origin which covers most of territory of the countries. Thanks to the abundance of water, the characteristic vegetation of this part is forests that will help to have wood for manufacturing industries.

The administrative division of Estonia is the same of the Estonian SSR (Eesti Instituut, 2014). There are 15 counties (maakond), 33 towns (linnad), 24 townships (vallad), 189 village councils (allevid), 167 (alevikud) and 3274 villages (külad). Of the 33 linnad, there are 5 of them which have an especial consideration in terms of self administration as Tallinn, which the capital of the county, Tartu, Narva, -Järve, Pärnu and Sillamäe.

Latvia is divided in counties too, but just 5 and besides in counties, it is also divided in 109 municipalities (novadí) and 9 cities-republics (republikas pilsētas*)*. Riga, the capital of Latvia, is a county by itself and a city-republic owed to the representative character of the nation. This structure was established in 2008/2009, in the third stage of the Amendments of the Administrative-Territorial Reform Law (Saeima, 2005).

Lithuania is formed by counties (apskritys) and districts (savivaldybių), as the Law on the Territorial Administrative Units of the Republic of Lithuania and Their Boundaries says. In section 2, article 5 of the same law (Law on the Territorial Administrative Units of the Republic of Lithuania and Their Boundaries states, 1994), it is detailed the name of the 10 counties. Inside of Vilnius county, Vilnius, the capital of the country is located. In the same section of the ATR Law, article 4, there are mentioned the 60 districts of Lithuania.

5. SOCIAL ASPECTS

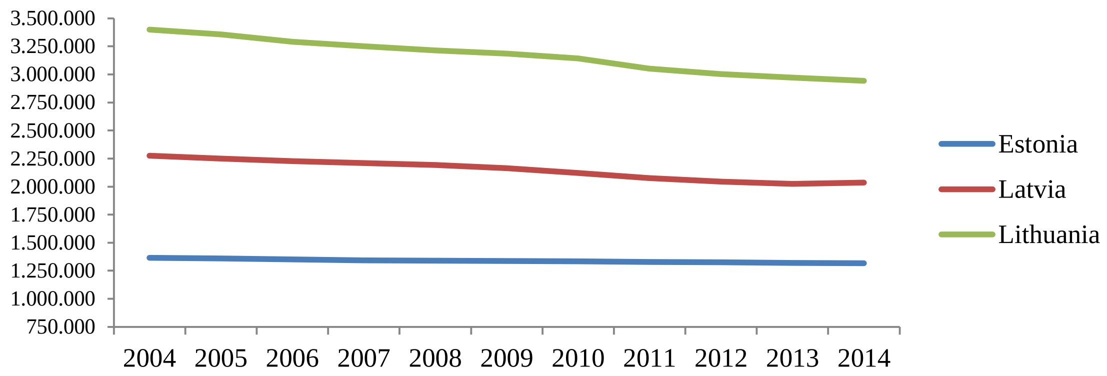
Population is who makes a country with their individual characteristics and culture. The way of how they are (age, gender, nationality, level of studies...) will really affect economy. Economic system turns around people and their needs and, depending mainly on social features, it is more likely to grow or not.

This is why studying social issues as demography and education in these countries is so relevant. They will help to understand how matters related with inhabitants have affected to the development of the Baltic region.

5.1 DEMOGRAPHY

The Baltic group has the lowest population of the Northern countries. The lowest populated country of our 3 objective countries is Estonia, where only 1,315,819 citizens lived in May 2014. The next one in population was Latvia with 2,036,000 and, finally, Lithuania, which at the beginning of this year counted with 2,943,472 people living there. In GRAPH 5.1, as we could see, Estonian population has always been around 1,300,000 people. In contrast, Latvian and Lithuanian population from 2004 to May 2014 has decreased -10.57% and -13.4% respectively.

GRAPH 5.1 Population from Baltic countries from January 2004 to January 2014 (number of inhabitants at the beginning of the period)

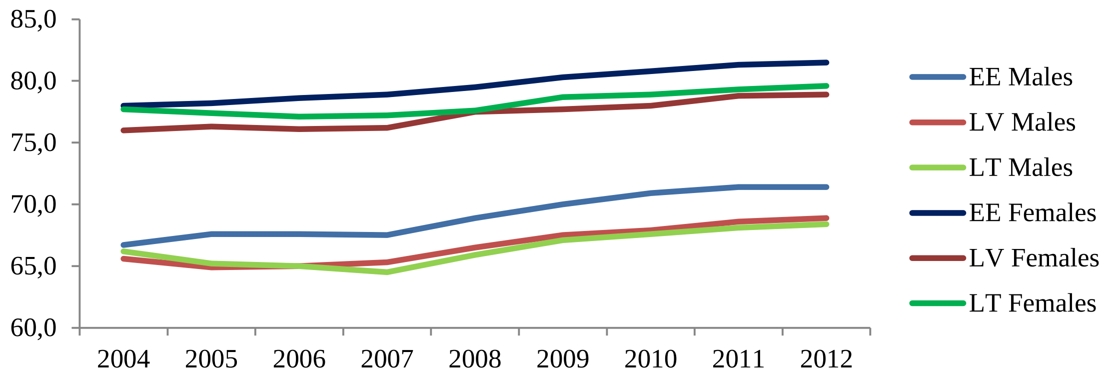


Source: Own elaboration based on Statistics Estonia, Central Statistical Bureau of Latvia and Official Statistics Portal of Lithuania data

It could seem an irrelevant per cent, but if we check the annual rate of change, they have decreased at a steady rate of -1%. Just the 2011/2010 rate is bigger than the others, when the decrease was of -2.86% in Lithuania and -2.16% in Latvia. There are several studies and opinions about this behaviour, like the one suggested by the Lithuanian Tribune (n.n., 2013) .The reasons used in this article to explain this trend are:

- Low total fertility rates (TFR). A developed country needs to have a fertility rate of 2.1 children per woman to achieve "zero growth" where population will maintain stable. Latvia and Lithuania have been under this value during more than 2 decades (e.g. in 2000 the total fertility rate was 1.25 in Latvia and 1.39 in Lithuania), so it has affected to the growth of population. Governments were concerned about this problem and started policies to help the maternity. Thanks to these plans and a better economic situation of the countries, the fertility rate turned to grow again in 2004. Nowadays, it is still far of 2.1 children per woman (Latvia 1.44 and Lithuania 1.60) but not so as before. During crisis period, rates decreased caused by the idea of having a child is expensive and they did not have enough money to afford it.
- Life expectancy. The number of years that is expected that a man or woman will live when he/she was born has increased last years. This increase is thanks to better political, economical and social conditions which create a welfare state in which population can live more and better.

GRAPH 5.2 Expectancy at birth by gender from 2004 to 2012 in Baltic states (years)



Source: Own elaboration based on Eurostat

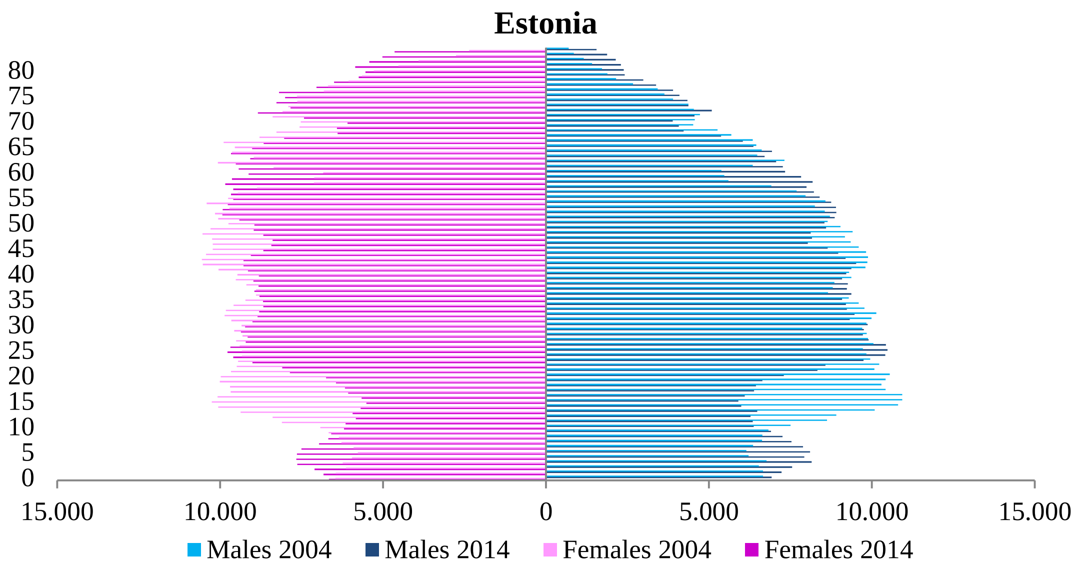
If people can live more years, population's median age increases too. Usually, nobody lives more than 110 years, so median is in a range between 30 and 50 years, but inside of it, the number can be bigger or lower, depending on the effect of several factors, like fertility rate. Reductions in TFR caused that population growth decreases and with it, a growth of median age (Weil, 2006). Median age of Baltic countries has increased from 2004 to 2013, that points out that the trend is the same as developed countries where population is ageing each year.

TABLE 5.1 Median age of Baltic countries in 2004 and 2013 (years)

	Median age 2004	Median age 2013
Estonia	38.9	41.0
Latvia	39.0	42.1
Lithuania	37.7	42.1

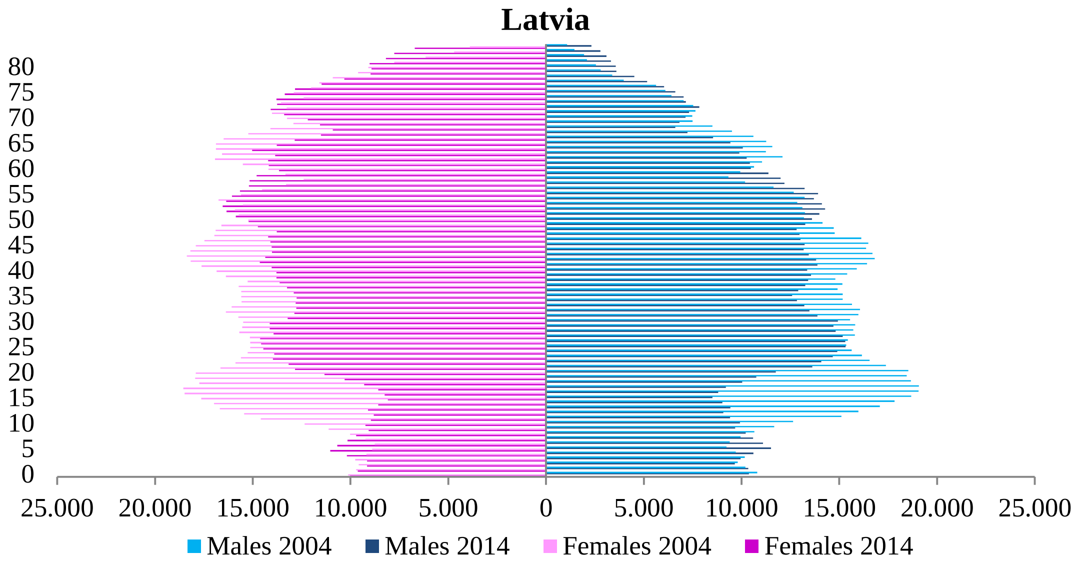
Source: Own elaboration based on Eurostat data

GRAPH 5.3 Distribution of population in Estonia, 2004 and 2014 (number of inhabitants at the beginning of the period)



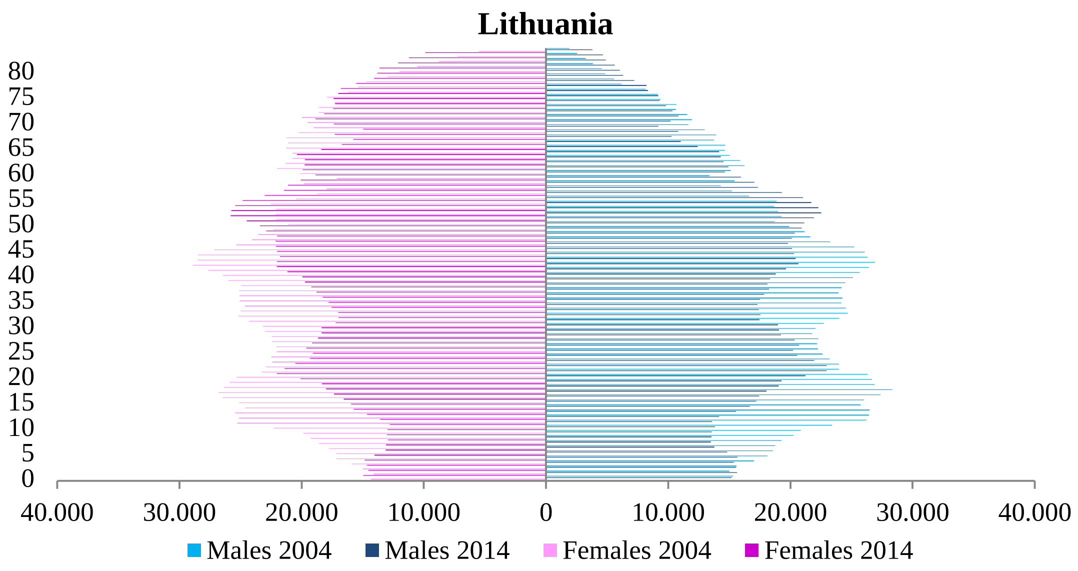
Source: Own elaboration based on Statistics Estonia data

GRAPH 5.4 Distribution of population in Latvia, 2004 and 2014 (number of inhabitants at the beginning of the period)



Source: Own elaboration based on Statistical Bureau of Latvia data

GRAPH 5.5 Distribution of population in Lithuania, 2004 and 2014 (number of inhabitants at the beginning of the period)



Source: Own elaboration based on Statistics Lithuania data

As we can see at the previous graphs, there is a decrease from 18 years old to 36 years old population. The answer to this gap is migration. A recent OECD study (2013) has concluded that, since these countries entered to the European group, the number of emigrants has increased significantly, starting to be a national worry. Business cycles had determined the behaviour of migration flows, as we can check with high negative net migration rates in 2004, 2008 and 2010 in these three states. Emigrants look for permanent skilled employment in countries like United Kingdom, Ireland, Norway, Germany and Finland, this last one especially for Estonians. So, the common profile of emigrant is a high educated person, male sex, between 20 and 35 years old. Entire families are also leaving Baltic countries, which implies a long-term emigration or never returning to the country of birth. The consequences for the sending countries are definitely negatives. Despite of the decrease of unemployment, the reason is a decrease of working age population, not an improvement of labour market conditions or an economic growth. Also, there are skills shortages and a brain-drain caused by the emigration of high educated population.

5.2 EDUCATION

Education is one of the biggest supports of society and economy. A good educational system prepares population to the global economy.

There are some similarities between the education systems of the three countries, as European countries they are. We will find differences, mainly at compulsory age of starting school and at compulsory education levels. Just Latvia considers the pre-primary as compulsory, while the other two have as compulsory primary and lower secondary. This early start is reflected at the compulsory age of starting that in Latvia is 5 and in Estonia and Lithuania it is 7. The age until it is compulsory studying is 16, when it is supposed to finish the lower secondary level.

Most of students do not leave their education after having passed the compulsory period. Tertiary education, which corresponds with bachelor degrees at universities and colleges, is becoming more frequent in recent years. In 2012, students of bachelor degrees were a 26% of the total of enrolled population at any education level in Estonia and Lithuania, in contrast with the 21% from 2004. Post graduates still represent a minimum part of the students (i.e. in Latvia and Lithuania, this population represented less than 1% in 2012).

The problem of early leavers from education and training is becoming more serious at recent years. This young population is between 18 and 24 years, left school at secondary education or earlier and currently they are not in another enrolled at any other education programme. These early leavers, next to NEET population, are the main problems of governments in terms of youth, because most of them are unemployed. At international databases it is shown how the percentage of early leavers has decreased in last 10 years at the three countries (e.g. Estonia -30.2%, Latvia -33.3% and Lithuania -38.8%). One of the reasons could be the high outflows of young people from these states to foreign countries as consequence of the economic crisis. In fact, in 2008 and 2010 the percentage of early leavers decreased respect of the previous year at the three regions.

The weight of education in a country is strong because it can determine the possibility of doing business with foreign partners. A high educational level and skilled workforce next to cost competitiveness are the key attractive factors of Lithuanian and Latvian economies in 2014 (IMD, 2014). More than a half of population between 25 and 74 years old has secondary studies and around 40% of 25-54 years population has studied at the university at the three countries.

TABLE 5.2 Distribution by education levels of some segments of Baltic population in 2013 (percentage)

	Basic education(1)		Secondary education(2)		Tertiary education	
	25-54	55-74	25-54	55-74	25-54	55-74
Estonia	9.3%	15.5%	51.4%	51.1%	39.3%	33.4%
Latvia	10.3%	18.1%	56.8%	59.3%	32.9%	22.6%
Lithuania	6.4%	18.2%	55.6%	58.9%	38.0%	22.9%

(1)= Pre primary, primary and lower secondary education

(2)= General secondary education

Source: Own elaboration based on Eurostat data

Nothing of this would have possible if there had not been good investment rates for education from Governments. The total public expenditure on education has been around 5% of GDP at the Baltic States for 15 years, near of the EU average. The country which had the biggest participation of public expenditure on education in its GDP in 2011 was Denmark, 8.75% and the lowest participation was in Romania, 3.07%.

To have a good education system, it is needed to invest to can provide population the best possible services. A good indicator of the quality of the system is the number of pupils and students by teacher. Low rates help to teachers to be able to give their lessons better. Pupil-teacher ratio in primary education is one of the strength that IMF has seen at the infrastructure of the three countries, because of rates as 11.41, 12.41 and 13.2 pupils per teacher in Latvia, Lithuania and Estonia respectively.

Future developments in education at the Baltic countries are linked to the Europe 2020 strategy. The Country-specific Recommendations from the Council are:

- For Estonia, it will be necessary making more efforts to align education and labour market to facilitate the employability of young people through vocational education and training, apprenticeships… Also continuing with the internationalization and prioritization of the research and development and innovation system. Stopping the R&D programme is not advisable because of its small size (Council of the European Union, The, 2014a).
- In Latvia, the implementation of the higher education reform would be useful to reward quality. The idea of provide career guidance at all education levels next to a reinforcement of the vocational education and training and apprenticeships will make easier the employability of young population. The last recommendation given is to improve the research system by concentrating financing towards internationally competitive research institutions (Council of the European Union, The, 2014b).
- Lithuania has the challenge for 2014 of increasing the employability of young population, giving more relevance to the quality of programmes like apprenticeships and other forms of work-based learning. Strengthening the partnership with private sector will be useful for this purpose (Council of the European Union,The, 2014c).

6. MACROECONOMICS FEATURES

Becoming a member of the European Union is more than just being part of a common market. It also has other benefits at numerous economic aspects and thus consequences at the economy.

Along the following chapter we are going to analyse different topics of the economy of the Baltic countries in order to have a general view of it. We will start with national production followed by unemployment and labour market. Inflation comes from the relation between production and unemployment, so it will be studied after them. As we are talking about countries, public finance has to be taken into account because national governments are who create fiscal and monetary policies depending on the economic situation in that moment. Finally, as a part of monetary policies as they are, interest rates and exchanges rates have their section in this chapter.

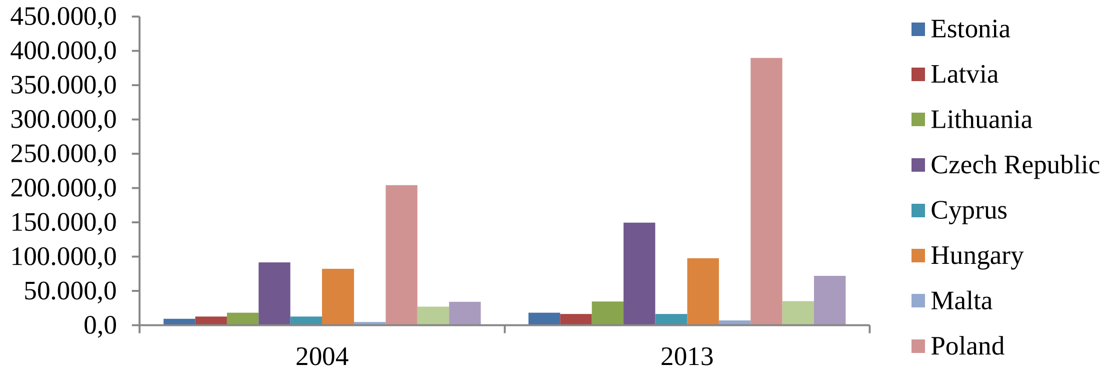
6.1 GROSS DOMESTIC PRODUCT

'*Output is the level of production of the economy as a whole*'. In scientific terms, output refers to the aggregate national production of a country. Output and production have the same meaning and both refer to goods and services which have been created to be used by consumers who will pay a price for them (Blanchard, 2009, p. 44).

In order to know the ability of a nation to generate incomes from national production, the most common measure is gross domestic product, because it is the market value of all final output produced by internal sources in a year within a country's borders.

Comparing the GDP of all countries which entered to the European Union in 2004, the Baltic States are not the biggest economies of this group. From the 10 new nations, the country which has reached the highest position in absolute values is Poland, which its GDP has reached € 389,695.1 million in 2013. In relative values, the country which has increased more since 2004 is Slovakia with 112.19%, followed by Latvia 109.53% and, again, Poland with 90.81%. From 2004 to 2013, the EU27 GDP just increased 22.6%, so these huge results got by Central and Eastern Europe countries helped to improve the total value.

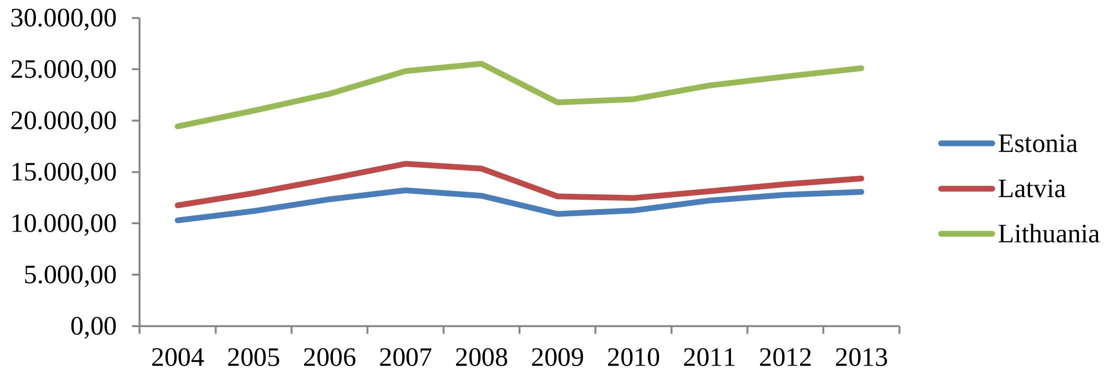
GRAPH 6.1 Gross domestic product of countries which joined to the European Union in 2004 at market prices, 2004 and 2013 (€ million, adjusted 2005 prices)



Source: Own elaboration based on Eurostat data

Focusing now on the 3 Baltic countries, Lithuania is the biggest economy because its national incomes were higher than Estonian and Latvian ones. Despite the fact of not being the biggest economies of the group (none of the three countries has had a level of national incomes higher than € 35,000), they have grown significantly. GDP development has been positive from 2004 to 2013, when the growth rate was 90.34% in Estonia, 109.53% in Latvia and 89.81% in Lithuania. So, all of them increased the money received from their output, despite of crisis period at the middle of the period.

GRAPH 6.2 Gross domestic product of the Baltic countries at market prices, 2004-2013 (€ million, adjust prices 2005)



Source: Own elaboration based on Eurostat data

In macroeconomics, the most frequent GDP decomposition is based on the different kinds of buyers of domestic production (Blanchard, 2009).

- Consumption (C): It refers to all purchases of goods and services made by consumers.
- Investment (I): Also, it can be named as fixed investment. Here, we can find 2 different kinds of investment, depending on who puts the money: Non residential investment, or the purchase by firms of new assets; Residential investment which is the purchase of houses by individuals.
- Government spending (G): This value is the sum of all purchases of products by the federal, state, and local governments. It does not include government transfers for the reason that, despite of being government expenditures, they are not purchases of goods or services.
- Trade balance (X-IM): GDP is the sum of all purchases of goods and services of a country during a given period, but the definition does not explain from where these products come or go from. The difference between exports, X, (purchases of national products by foreigners) and imports, IM, (purchases of foreign products by national buyers) is called net exports, or trade balance. If X is bigger than IM, there is a trade surplus and, at the contrary if IM has been greater than X, there is a trade deficit. (see chapter 7)

GDP is equal to production, but in a given period output and sales could not be equal because some of the goods which have been produced have not been sold in that year, so they will stay as inventory. To delete the difference between production and sales, there is the inventory investment that can be positive or negative, depending on whether production has been bigger or smaller than sales.

TABLE 6.1 Composition of Estonian GDP, 2004-2013 (percentage of GDP)

	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013
Consumption (C)	56.3	55.5	55.4	54.1	54.8	54.0	52.4	50.5	51.2	52.1
Investment (I)	30.9	32.1	36.0	35.5	30.3	21.2	19.0	23.6	25.2	25.3
Government exp. (G)	17.6	17.2	16.2	16.4	19.3	21.7	20.8	19.2	19.2	19.5
Exports (X)	73.1	77.7	72.7	67.1	71.0	61.9	79.2	90.5	90.6	88.0
Imports (IM)	80.1	84.2	82.9	76.3	75.1	58.3	72.3	86.8	90.3	87.2
Trade balance (X-IM)	-7.1	-6.5	-10.2	-9.2	-4.0	5.5	7.0	3.7	0.2	0.8
Inventory investment	2.2	1.7	2.7	3.1	-0.4	-2.5	0.8	3.1	2.9	1.6

Source: Own elaboration based on Eurostat data

TABLE 6.2 Composition of Latvian GDP, 2004-2013 (percentage of GDP)

	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013
Consumption (C)	63.0	63.1	65.7	62.4	62.5	61.4	63.1	62.2	62.4	62.5
Investment (I)	27.7	31.0	32.9	34.1	29.7	21.6	18.2	21.3	22.8	21.1
Government exp. (G)	19.8	17.8	16.8	17.8	20.0	19.6	18.4	17.7	16.6	16.5
Exports (X)	44.0	48.2	45.1	42.5	43.1	43.9	53.6	58.8	61.6	59.7
Imports (IM)	59.7	62.6	66.6	62.6	56.8	45.4	54.9	63.6	65.5	61.5
Trade balance (X-IM)	-15.6	-14.5	-21.6	-20.1	-13.7	-1.5	-1.4	-4.8	-3.9	-1.9
Inventory investment	5.1	2.5	6.1	5.9	1.6	-1.1	1.6	3.6	2.2	1.7

Source: Own elaboration based on Eurostat data

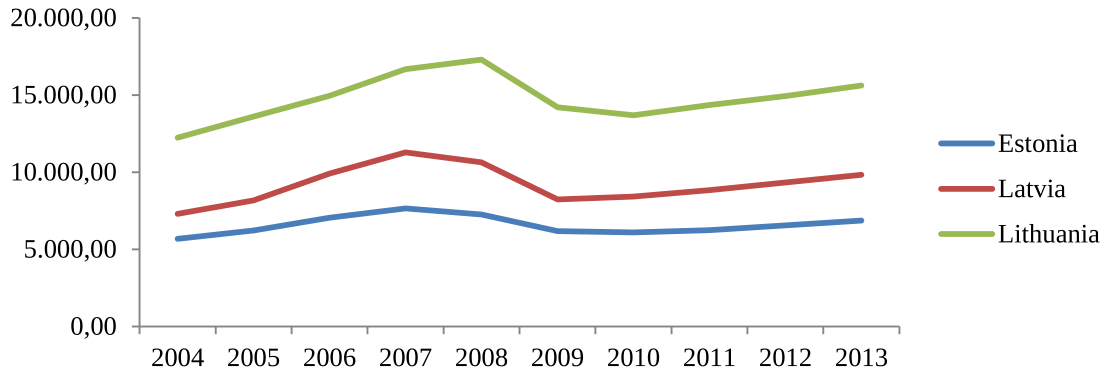
TABLE 6.3 Composition of Lithuanian GDP, 2004-2013 (% of GDP)

	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013
Consumption (C)	65.5	64.9	65.0	64.3	65.6	68.5	64.3	62.8	63.3	63.7
Investment (I)	22.4	22.9	25.3	28.1	25.3	17.2	16.3	18.0	16.6	18.3
Government exp. (G)	19.3	18.6	19.1	17.8	19.2	21.9	20.4	18.7	17.6	16.9
Exports (X)	51.9	57.3	58.8	53.8	59.6	54.2	67.7	77.2	83.9	86.9
Imports (IM)	58.9	64.4	69.0	67.1	71.5	56.0	69.7	79.9	83.1	85.9
Trade balance (X-IM)	-7.1	-7.1	-10.1	-13.3	-11.8	-1.8	-1.9	-2.7	0.8	1.0
Inventory investment	-0.1	0.7	0.7	3.0	1.6	-5.8	1.0	3.1	1.6	0.1

Source: Own elaboration based on Eurostat data

As we shall at the previous tables, C component represents the most part of GDP in each nation. The reason of the majority of consumption in GDP is because population has their needs and they have to satisfy them through purchases of goods and services. However, consumption is not an independent variable, whether it depends on factors such as disposable income. The income that consumers have after having paid taxes determines the spending income.

GRAPH 6.3 Final consumption expenditure of households and NPISH at market prices in the Baltic countries, 2004-2013 (€ million, adjust prices 2005)



Source: Own elaboration based on Eurostat data

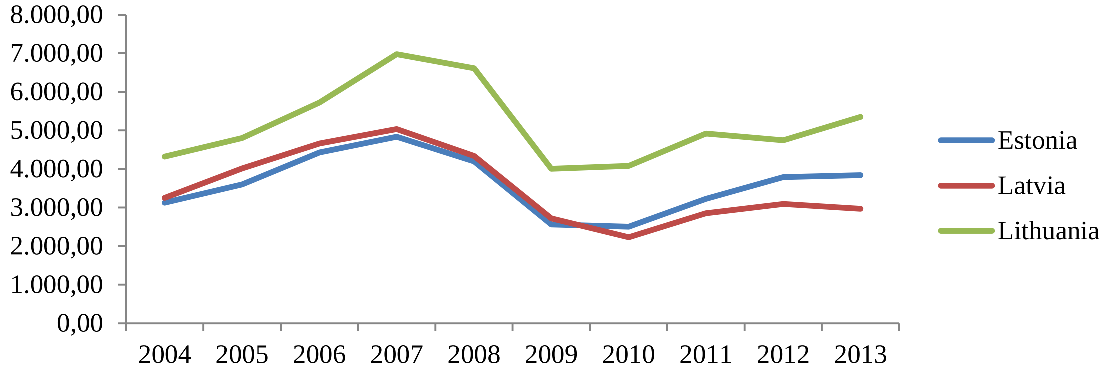
From 2000 to 2007, global economy was in an expansion period, so incomes, in general, grew. In the Baltic nations, this fact joined to the addition to the European Union in 2004 did that population increased their expectations of grow, because their countries were increasing and were part of a group with solid institutions which could help them in a close future.

The trust of citizens in their domestic capacities made people spent more money, so the propensity to consume was positive not only by the growth of disposable income, but also by a psychological factor like the reliance on a better position. The same thinking was used by foreign investors, who saw in these countries the perfect destination of capital and inter-banks loans (European Commission, 2010).

But, business cycles are composed by: expansions, recessions and recoveries. The boom of the economy lasted to 2007, when the 2 main Swedish banks which operated in Latvia had already noticed the possibility of a crisis closer owed to the trend of bubbling that some economic sectors as the construction was suffering. A year later, in 2008, the actual financial and economic crisis started and all of those optimistic expectations were past. A lot of people lost their jobs owed to the closure of many enterprises (in GRAPH

6.4 we can see how, in 2008 and 2009, investment in current prices was near of quantity invested at early 2004, so in real terms it could be lower).

GRAPH 6.4 Gross investment in fixed capital in the Baltic countries at market prices, 2004-2013 (€ million, adjust 2005 prices)



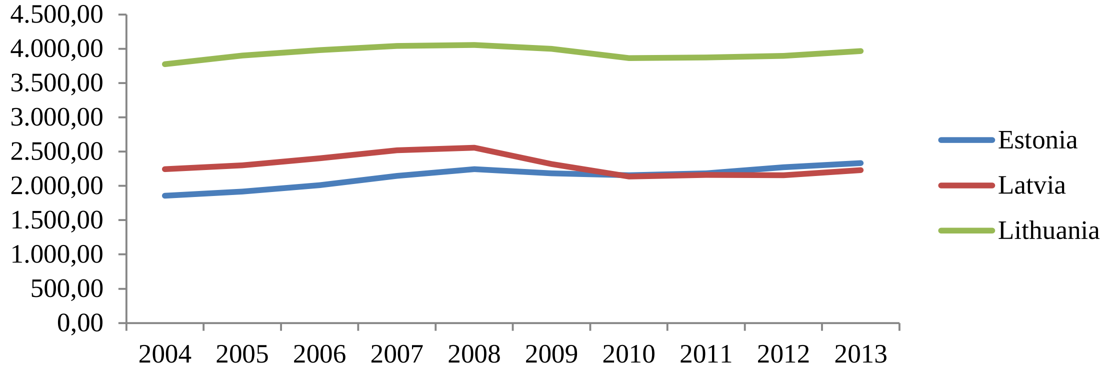
Source: Own elaboration based on Eurostat data

Another factor, which was the reason of the reduction of incomes, was the implementation of austerity policies by national governments. Most of decisions were focused on the reduction of public deficit, so that implied rising taxes, cutting of government expenditures in education, social insurance or freezing government's workers wages as some examples of the actions.

A fiscal contraction of these characteristics, with an increase in taxes and decrease of government spending, leads to lower disposable income and, consequently to decrease people's consumption. Concerning the investment, it was also affected in a negative sense. Investment, in goods market equilibrium condition, is the result of private saving plus public saving. In this case, even if public saving had increased reasonably, a positive investment would not have been possible, because private saving had decreased in a higher proportion than the increase of public saving.

Government spending, in contrast with the other two components of domestic demand, did not decreased as much they did. Since 2008, Baltic national governments had been used austerity plans to their economies which implied a decline of public expenditure. Nevertheless, this element is not so easy to manage because the numerous social and economic aspects behind of it.

GRAPH 6.5 General government expenditure in the Baltic countries at market prices, 2004-2013 (million Euros, adjusted 2005 prices)



Source: Own elaboration based on Eurostat data

Estonia did not suffer a decrease so accused as Latvia and Lithuania did. The reason was that they predicted the fall and started austerity plans in 2007, so when global financial crisis began, they had already implanted tax increases and a control over government expenditures. Another factor of the lower recession was the Estonian financial situation, with surpluses at national budget and high public saving that could help the economy in case of a recession.

Since 2010, the Baltic States have returned to grow. Austerity plans had helped to national economies to increase again, despite of the opinions of some macroeconomists, who think that austerity policies suggested by the European Commission are not as good as they are presented. The reasons on which they are based are that fiscal consolidation is not politically or socially sustainable, the Commission is inflexible with its approach and it is one-sided and puts the entire burden on the implied country. In contrast, Buti and Carnot (2013), conclude that EU fiscal policy is not a strict one, whether it is flexible to can be in line with the approach of other international institutions. Flexibility has helped to make softer the consequences of a fiscal contraction and to get a sustainable increase of the economy and of employment.

The consequences of this policy in Baltic GDP were an increase of consumption owed to an improvement in labour market and monetary facilities; an increase of investment thanks to the expectations of business of an economic improvement as last results were showing (the decrease of investment in Latvia in 2013 was caused by the completion of large investment projects and the decrease of inflow FDI in manufacturing, energy, transport and storage sector, (Ministry of Economics of the Republic of Latvia, 2013); a sustainable increase of government spending, supported by a good level of national incomes.

Overall, the Baltic Three have improved their economic situation, as most of countries which joined to the European Union in 2004. We can't compare economies between them, because of the differences in internal economic characteristics. Nevertheless, we can say that there has been a common development, which are exactly the same of business cycles.

TABLE 6.4 Real GDP at market prices growth of the 2004 New Member States, 2004-2015 (annual percentage change)

	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014_f	2015_f
Czech Republic	4.7	6.8	7.0	5.7	3.1	-4.5	2.5	1.8	-1.0	-0.9	2	2.4
Estonia	6.3	8.9	10.1	7.5	-4.2	-14.1	2.6	9.6	3.9	0.8	1.9	3
Cyprus	4.2	3.9	4.1	5.1	3.6	-1.9	1.3	0.4	-2.4	-5.4	-4.8	0.9
Latvia	8.8	10.1	11.0	10.0	-2.8	-17.7	-1.3	5.3	5.2	4.1	3.8	4.1
Lithuania	7.4	7.8	7.8	9.8	2.9	-14.8	1.6	6.0	3.7	3.3	3.3	3.7
Hungary	4.8	4.0	3.9	0.1	0.9	-6.8	1.1	1.6	-1.7	1.1	2.3	2.1
Malta	-0.3	3.6	2.6	4.1	3.9	-2.8	4.2	1.5	0.8	2.6	2.3	2.3
Poland	5.3	3.6	6.2	6.8	5.1	1.6	3.9	4.5	2.0	1.6	3.2	3.4
Slovenia	4.4	4.0	5.8	7.0	3.4	-7.9	1.3	0.7	-2.5	-1.1	0.8	1.4
Slovakia	5.1	6.7	8.3	10.5	5.8	-4.9	4.4	3.0	1.8	0.9	2.2	3.1

f: forecast of European Commission

Source: Own elaboration based on Eurostat and European Commission data

At the first part of the studied period, from 2004 to 2007, for the Baltics the entry in a common market, the security of being in a supranational group and the global good economic situation helped to their positive results, over 6% of real GDP growth. In 2007, Estonia started with its austerity policies, so its growth values were not as high as the Latvian and Lithuanian, but still one of the highest of the group.

During the second division (2008-2010), which we have define as the crisis period in the Baltic countries, their good internal structure made easier the implementation of restrictive fiscal policies, which in other states would not have been possible. Thanks to the anticipation in fiscal terms, Estonia got lower decrease rates than its neighbours and returned to grow earlier. Already in 2010, the Estonian real GDP growth was of 2.6%, in contrast with the Latvian, -1.6%, or the Lithuanian one, 1.6%. The reason of the negative Latvian result in 2010 was the previous high public deficit rates which had made that this country had to be intervened by the IMF.

Finally, in the third part (2011-2013), the recovery of economies, there are some aspects that must be analyzed. In 2011, Estonia increased 9.6%, but in the following years just 3.9% and 0.8%. The reason is the negative contribution of trade balance, because there is a weak demand of Estonian products, especially services. Austerity fiscal policies in Latvia and Lithuania lasted more years than in Estonia, so the effects to get back to increase started later in these countries.

Concerning forecasts for 2014 and 2015 (European Commission, 2014c), it is expected that the Baltic economies keep increasing during the next 2 years. The worst predictions go to Estonia because, despite of the optimistic forecasts for consumption and investment, net exports will be still close to balance. Latvia is the country which has the best forecasts of the 3 with expectations. Private consumption will be the main supporter to increase helped by an improvement in labour market. About, investment and net exports are expected to suffer geopolitical consequences from Russia. Lastly, Lithuania will grow too, owed to the boost of domestic demand (consumption, investment and government expenditure). In the opposite side of economic growth, in this country, net exports are expected to be negative for the next 2 years.

6.2 UNEMPLOYMENT AND LABOUR MARKET

Labour force is one of the three productive factors of the economy which involves all aspects related to human resources. People are not just those who purchased products at markets, also they participate at the production phase.

In a country there are a limited number of resources which can be used to create products and it is infrequent the total use of them. Unemployment is the number of people of working age who have not a work (that means not having a paid employment or being a self-employed person), are available to work and are looking for a job (International Labour Organization, 2013). The sum of employment and unemployment is the labour force or active population.

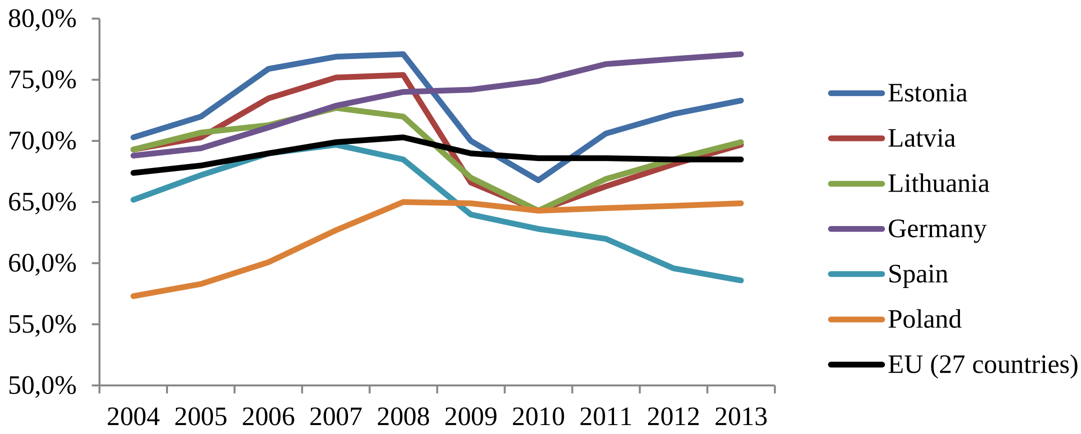
Not all population of working age is considered within the active population. There are people who are not unemployed, but they are not employed either. Groups like students, housekeepers, pensioners or compulsory military servants are included in that classification according with Eurostat methodology.

The activity rate is the percentage of people who employed or unemployed from the total population of working age in a country in a specific period. It can provide us better idea of the size of the labour market in that region.

The activity rate of the EU27 is around the 70%, similar to the Estonian, Latvian and Lithuanian one. During the first years in the group and coinciding with the boom in national economies, the Baltic countries maintained an activity level above the EU27 thanks to the economic expansion which attracted to population to labour markets. With the economic bust, the labour market volume decreased from 2007 to 2010 13.1% in Estonia, 14.5% in Latvia and 11.6% in Lithuania. As consequence of the bad economic situation, many people decided to leave their home countries and looking for better labour conditions in foreign markets. The result in national markets was the decrease of labour force which reached levels around 65% in 2010.

With the recover, these outflows of population have decreased but, still are one of the main social problems in the Baltic countries. Also, as we have seen at chapter 5, inhabitants are ageing and this leads to exits of the labour market. The gap left by the retirees is not filled by young population, because a high percentage of them are going abroad to work. The consequence is a shorter increase because, despite of the good performance of the economy, the labour force has increased in Estonia 4.27%, in Latvia 0.58% and in Lithuania 0.87%. At least still there are people willing to work, because in Spain, at the same period from 2004 to 2013, the labour market decreased -10.12%.

GRAPH 6.6 Activity rate in some European countries and the EU 27, 2004-2013, annual values (percentage of population between 15 and 64 years old)



Source: Own elaboration based on Eurostat data

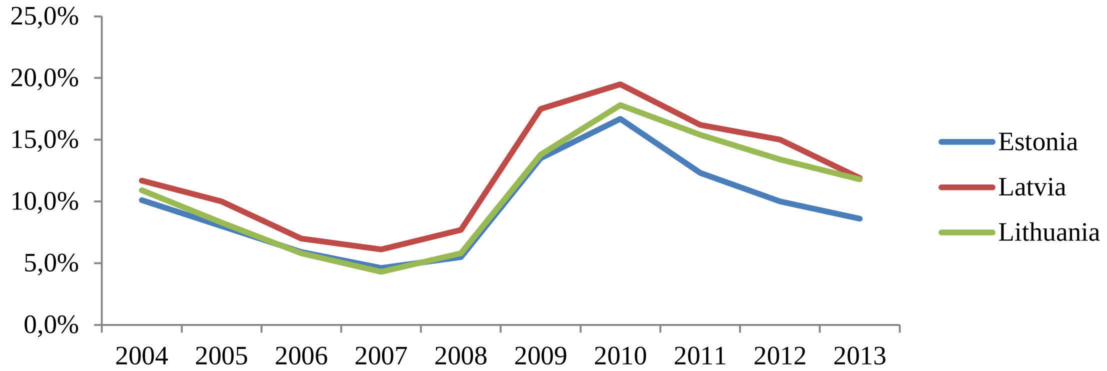
Unemployment is a real worry in all economies, not just in the Baltic countries, owed to the social and economic consequences that it has. About the social problems, one of the most important is the general pessimism suffered by population who does not any possibility of recovering previous welfare levels. The economic effects are the waste of a key resource, the human factor, which moves away GDP from its potential level. GDP and unemployment rate are highly related as Okun's Law determines. This economic model states that there is a linear relation between changes in real GDP growth and in unemployment rate (Samuelson & Nordhaus, 2006). For every percentage point that unemployment rise, the real GDP decrease approximately 2%.

Taking into account this macroeconomic model, and after having studied real GDP growth rates, the unemployment rate can be looked by another point of view connected with the economic growth.

From 2004 to 2007, the Baltic countries were in one of the best periods of their history economically. The joining to the European Union opened the door for national economies to new possibilities in foreign markets and to can receive external factors without restrictions from abroad. Investment in new fixed capital, fostered by the increase of housing and industrial markets, and an increase of households' consumption did that companies needed employees for vacancies. Unemployment rate in 2007, the best year of the period, was 4.3% in Estonia and Lithuania and 6.1% in Latvia. In 2008, the crisis began to become effective and unemployment rose slightly. The exception of

Okun's Law is Lithuania, where despite of the real GDP growth of 2.9%, the unemployment rate increased 1.5% points, reaching 5.8%. It was owed to the decrease the active population in the country.

GRAPH 6.7 Unemployment rate of the Baltic countries, 2004-2013, annual average (percentage of labour force)



Source: Own elaboration based on Eurostat data

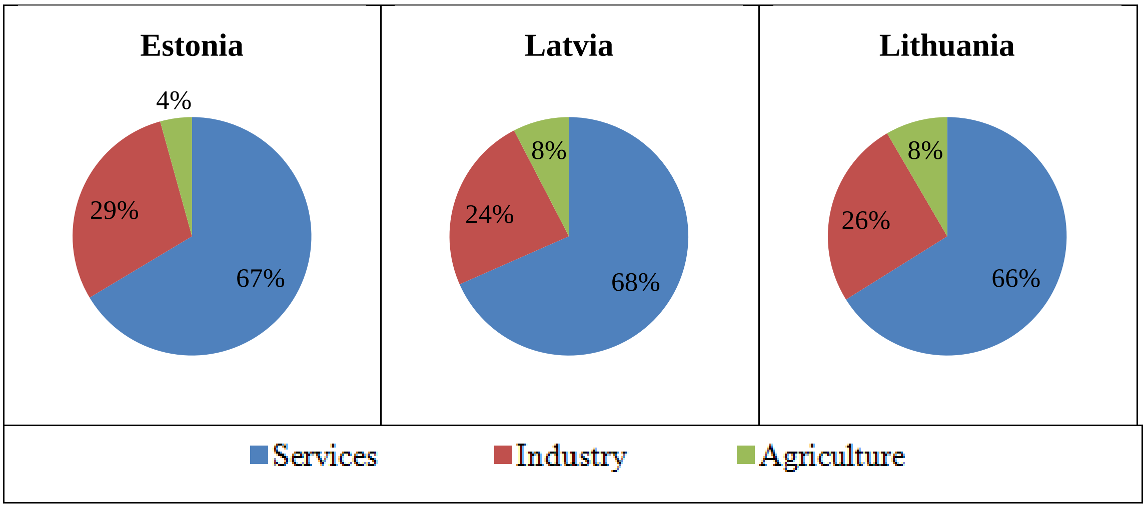
The worst years were 2009 and 2010, when the three countries reached the highest unemployment rates of the period. The crisis was a fact in 2009 and the downturn of the economy did that many companies, mostly from manufacturing and building sectors were at bankruptcy causing that employees lost their jobs (European Commission, 2010). Owed to the loss of their work place, the recent unemployed people suffered a reduction in their disposable income, which lead to the decrease of households' consumption. Those who kept their jobs also were affected by a decrease of disposable income as consequence of employment policy reform and fiscal reform, which meant a reduction of wages and a rise of income taxes. In 2010, the first signs of economic prosperity were visible thanks to the austerity policies used in last 2 years, in fact Estonia came back to grow as consequence of the earlier establishment of the reforms. Also in that year, the Baltic countries suffered the biggest outflow of population which reduce the activity rate and did slighter the increase of the unemployment rate (Organization for Co-operation and Economic Development, 2013).

Since 2011, the unemployment rate in these states has been decreasing reaching almost the pre-crisis levels. The economic growth helped to the positive development of the employment in aspects like the recovery of a relevant sector for the Baltic economies as the industrial activity is (the most exported products of these three countries are produced in this economic sector).

Last year, of the three countries, just Estonia (8.6%) was below the EU27 unemployment rate established in 10.8%. The other two were close enough, but above the European average (Latvia 11.9% and Lithuania 11.8%). The European level shows that there are countries which suffer higher unemployment rates. Spain is one of the countries with the highest unemployment rates of the group, around 25% in last two years.

As developing countries that they are, secondary sector is important to their economies, concentrating in this activity a third of total employment. In this economic activity, thanks to developments in technology, innovation... human factor is becoming less important owed to the replacement person-machine. In Estonia, Latvia and Lithuania tertiary sector employment has increased around 10 percentage points from 2004 to 2012. The employment rate in primary sector gives an idea of the importance of the rural areas in that country. At the beginning of the period, in Latvia and Lithuania near of 15% of the employment population was related with the agricultural activity, but at the end it was just 8% which shows the decline of primary sector.

GRAPH 6.8 Distribution of the employment by economic sectors in the Baltic countries, 2013 (percentage of total employment)



Source: Own elaboration based on Eurostat data

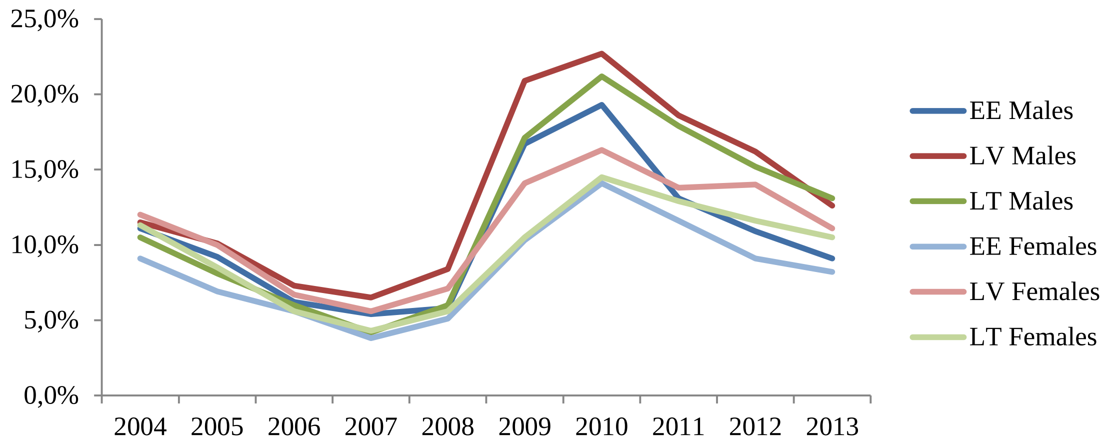
Discrimination is a real problem inside of unemployment. There are social groups that owed to their characteristics (gender, age, nationality...) are more sensitive to changes at the labour market.

Gender discrimination usually damages woman, because this group has aspects as the maternity which supposes higher costs to enterprises. If a woman got the same occupation as a man, she would receive fewer wages than him.

The gap between salaries of men and women is a fact, but not at the same level depending on the country. In the European Union, in 2012 the 5 countries which have a higher distinction between female and male salaries were: Estonia (30%), Austria (23.4%), Germany (22.4%), Czech Republic (22%) and Slovakia (21.5%). So, Estonian women earned a third less than their male workmates. Latvian and Lithuanian labour markets are more equal treatment of gender salaries than Estonia and than the average of the European Union (EU27: 16.4%; Latvia: 13.8%; Lithuania: 12.6%).

Estonia has the lowest unemployment rates by gender in both cases, in males and females. From 2004 to 2008, the rates had approximately the same values in the three countries. Global economy was in a good moment and the expansion of economic sectors did that the unemployment decreased. But, as we saw at the previous part, crisis arrived to the Baltic countries in 2008 and the labour market worsened significantly. In 2009, male unemployed population in Latvia was 20.9% meanwhile females was just 14.1%. That was owed to the great importance of industrial and construction sectors, the most affected by the burst of housing bubble, at Latvian economy. One year later, the growth of unemployment in the Baltic States was not as strong as the previous year, as result of migratory flows, mainly of men but also of women. Lower female unemployment rates in Estonia, Latvia and Lithuania are the consequence of the great participation of women at tertiary or services sector. The most common jobs for a woman in these countries are linked to education and health, both from the services sector (e.g. the percentage of females at tertiary sector respect of total female employment in 2013 was 81.2% in Estonia, 81.4% in Latvia and 77.7% in Lithuania), so it is clear that women have not suffered the crisis as men do thanks to the kind of work.

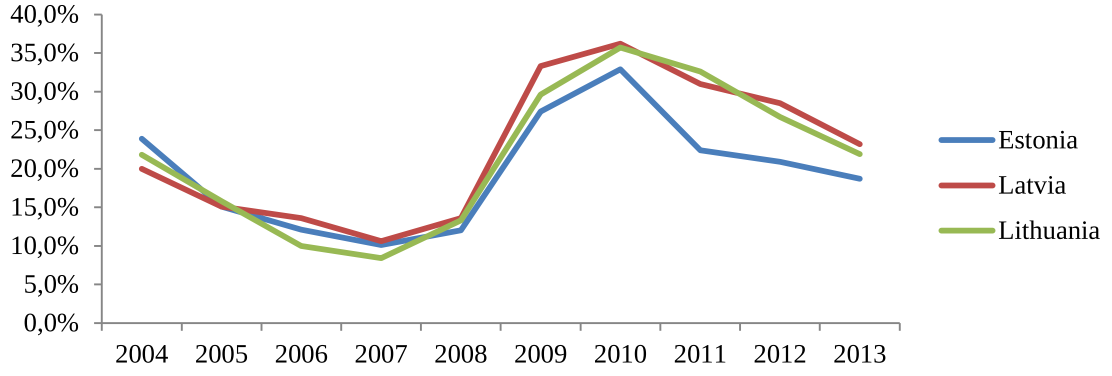
GRAPH 6.9 Unemployment rate by gender in the Baltic countries, 2004-2013, annual rates (percentage of active population by gender)



Source: Own elaboration based on Eurostat data

Another discriminated population is young people. The transition from education to the labour market is not always easy, because their expectancies use to be higher than the reality. A recent research (Brazien, et al., 2013) shows how NEET population in Lithuania had limited possibilities of finding a job owed to a mismatch between the level of the education of young people and the labour market demands and an unfavourable labour market situation in last few years. Also, they feel that they do not the competences required for the work or that the working conditions are too stressful (long working hours, delay in pay of wages...), so most of them will reject the job. This conclusion could be used for the rest of countries, because of the globalization of young people behaviour. This problem should be dealt by national authorities to avoid serious social problems in young population as drugs, criminality, social exclusion, etc. Since 2010, youth unemployment has decreased 43.2%, 35.9% and 38.7% in Estonia, Latvia and Lithuania, coinciding with the beginning Europe 2020 strategy.

GRAPH 6.10 Youth unemployment at the Baltic countries, 2004-2013, annual average (percentage of less than 25 years active population)



Source: Own elaboration based on Eurostat data

None country will ever have a situation of full employment. We say this statement, because within the unemployment, there are three kinds of unemployment (Samuelson & Nordhaus, 2006):

- Frictional unemployment: These the sum of population of working age which has not a job because it is the result of changes at area where they lived, rural migration for example, new active population like students who have just finished or left their studies...
- Structural unemployment: As consequence of an imbalance between supply and demand at the labour market. Sometimes firms ask for a kind of job different that unemployed people offer, so none of both parts finds what they are looking for.
- Cyclical unemployment: It is associated with short run fluctuations of the market. When product prices and total expenditures rise, labour demand level is lower and unemployment increases.

The two first types of unemployment joined are what macroeconomists called “the natural unemployment rate”. This term refers to the percentage of labour force which will not find a job regardless of the economic situation, a boom or a recession (Jones, 2011). The natural unemployment could be linked to aspects such as the determination of wages or the behaviour of unemployed, but this is just theory. At the real world, still there are gaps at empirical knowledge around the reasons why the natural rate of unemployment exists (Blanchard & Katz, 1996).

The natural rate of employment and NAIRU rate (Non Accelerating Inflation Rate of Unemployment) have not the same meaning despite of being formed by frictional and structural unemployment in both cases. The first refers to the percentage of unemployed as consequence of labour market characteristics. NAIRU is "*the unemployment rate at which inflation increasing effects of the excess-demand markets just balances the inflation-decreasing impacts of the excess-supply markets*" (Tobin, 1997, p. 8). .

NAIRU can be better explained through the Philips curve. This representation shows the relation between the unemployment rate and the year-to-year change variation of inflation and of wages. If the unemployment rate increases, the rates of inflation and wages are lower, so prices and salaries will decrease, decreasing the amount of incomes of households to expend. Behind of this it is productivity, which reduces the impact of an increase on wages in average companies' costs. If wages increased in higher rates than productivity, the consequence would an increase in cost and, to afford the increase of firms' expenditures, prices would rise.

Productivity in the Baltic countries has improved last years. Aspects like technology, education, innovation... have done that employed people can produce more monetary units per hour worked. Thanks to the higher efficiency at the production process, expenditures are lower and the objectives are still achieved. Last productivity ratio data, published in 2013, shows that despite of the downturn years in 2008 and 2009, the three nations have increased in 10 years their productivity per hour worked 28.74% (Estonia), 52.73% (Latvia) and 41.33% (Lithuania).

But also, wages and salaries have increased. This is good for households which their main source of incomes comes from the labour market. The economic expansion collaborated with a raise of the annual salaries, but with the contraction of the economy in 2008, wages fell down in 2009. The recovery in wages did not happen until 2011, when it seemed that national economies had got back to growth. However, not all wages have suffered the same developments. In Estonia, last year wages increased more were from agriculture, forestry and fishing, mining and quarrying and transportation and storage sectors (Statisitcs Estonia, 2014a). At the same year, in Latvia the average monthly gross salaries that suffered higher percentages of changes were found at economic activity such as manufacturing, public administration and defence and construction (Central Statistical Bureau of Latvia, 2013).

In conclusion, if we put together changes year-to-year of wages and productivity, the difference between wages less productivity would be an approximated inflation rate that year. It will not be exactly the real inflation owed to the method, which is focused just in one type of prices, as wages and salaries are.

TABLE 6.5 Estimated “inflation” extracted by Philips model

	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013
Estonia	2.6%	4.8%	11.5%	13.7%	16.7%	-7.5%	-3.9%	5.8%	2.2%	6.9%
Latvia	0.3%	9.9%	16.2%	5.4%	28.5%	-2.4%	-10.2%	1.5%	-1.0%	2.5%
Lithuania	1.2%	9.4%	10.5%	14.8%	17.5%	2.0%	-17.2%	-4.3%	4.0%	4.1%

Source: Author’s calculation

6.3 INFLATION AND PRICE LEVEL

Inflation refers to the sustained rise in the general level of prices, the price level (Blanchard, 2009). Obviously, prices do not always rise, whether there are some periods of decline, called deflation, but they are quite unfrequent.

The price level of a country is not as simple as we could think. It is formed by the prices of all national products without distinguishing the type of good or service it comes from. So, to define easier a country’s price level,experts use 2 price indexes: the GDP deflator and the consumer price index (CPI). The HICP is the European equivalent of the CPI and gives comparable measures of consumer price inflation in the EU27 area and other important economies. Both values show the cost, in dollars (CPI) or euros (HICP), of a consumption basket composed by goods and services which a typical urban consumer buys.

TABLE 6.6 GDP deflator at market prices, 2004-2013 (2005 =100, Euro)

	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013
Estonia	94.3	100.0	108.7	121.4	128.1	128.2	128.6	132.5	136.9	143.7
Latvia	95.0	100.0	111.3	133.1	148.9	146.7	144.5	153.6	160.9	162.2
Lithuania	93.9	100.0	106.5	115.9	126.8	122.7	125.6	132.1	135.3	138.0

Source: Own elaboration based on Eurostat data

TABLE 6.7 All-items HICP in the Baltic countries, 2004-2013 (2005= 100, Euro)

	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013
Estonia	96.05	100.00	104.45	111.49	123.31	123.56	126.95	133.40	139.02	143.53
Latvia	93.55	100.00	106.57	117.32	135.21	139.62	137.91	143.73	147.02	147.03
Lithuania	97.41	100.00	103.79	109.83	122.01	127.09	128.60	133.90	138.14	139.75

Source: Own elaboration based on Eurostat data

The differences in the variation of these two numbers are implicit in their definitions. GDP deflator calculates the price changes of goods and services produced by domestic companies and CPI is the index of the variation of goods and services consumed by population in a country. Hence, if imported goods price increased relative to domestic goods price, the CPI would increase more than GDP deflator. In this case, there are no significant contrasts in the annual change trend of each measure, so the price level of these countries is related with their movements.

Nevertheless, to study the inflation in a clearer form, we will take HICP annual change rates. This index concerns to the main GDP component, the consumption of population, but also includes goods, from other countries, purchased in domestic markets.

From mid-2004 to 2007, the inflation in Estonia, Latvia and Lithuania was due to domestic demand pressures because the expectations of economic expansion were positive and the domestic markets had grown.

But, it was in 2008 when HICP reached its highest rates in the three countries. The reason was the increasing dynamics of global oil price, which directly affects to energy prices, and global food prices, mainly agricultural. For instance in Lithuania energy prices were considerably volatile due to, besides oil price changes in international markets, the gas price revisions of Russia, Lithuanian main supplier (European

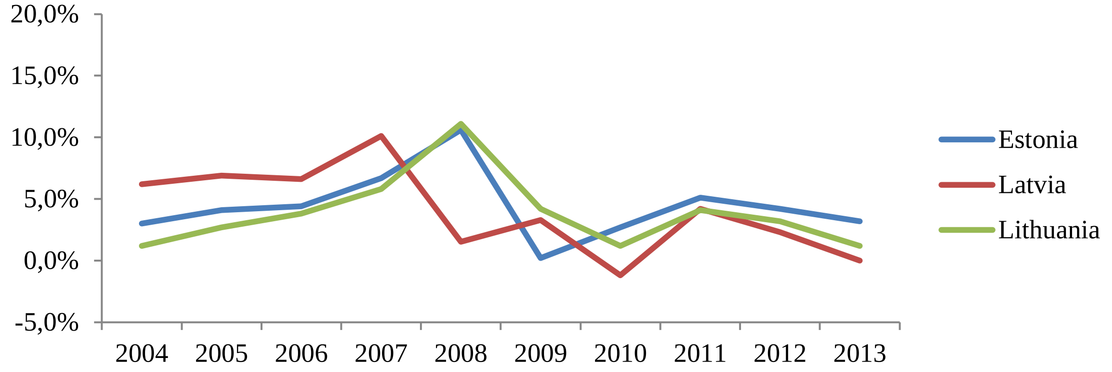
Commission , 2010). As they are small and open economies, they are more sensitive to external price changes and thus their import price will have the same behaviour as the global oil and agricultural prices (the major import price contributors) has. In contrast with we may think, exchange rates have not helped to inflation because it stayed stable most of period. Just in Latvia and the lats appreciation, the impact of decreasing international commodity prices was reinforced (*ibid*, 2010). Administered prices and indirect taxes (VAT, excise duties on alcoholic beverages and tobacco…) were other contributors of the increase in 2008 of the inflation in Baltic countries.

Global crisis started in 2008, so in 2009 the recession drove HICP inflation to fall owed to the impact of the new bad economic situation which contracted domestic demand and the fall of wages and imports prices. In this year austerity fiscal policies helped public finance to become weaker and contributed to make softer the price changes. As consequence of the fiscal consolidation programmes and a strategy to harmonize taxes, indirect taxes, as VAT or excise duties on tobacco and alcohol, increased their rates. About administered prices, they increased to mitigate the fall of the rest of prices, so they next to indirect taxes were the main contributor of the inflation in the Baltic countries.

A year later, the situation did not improve and prices kept decreasing. One of the reasons of the Latvian deflation results is a regional food price shock which this country suffered in 2010 (European Commission, 2013a). Nevertheless, not all inflation components decreased, global energy prices increased and, consequently, heating and electricity prices increased too. Indirect taxes increased as a part of revenues-side of public sector stabilization.

Since 2011, Baltic economy seems having overcome the crisis and prices have stayed in a stable range. A drop of world oil and food prices has caused a moderate, and in sometimes negative, contribution of import prices to HICP. So, the developments on administered prices, indirect taxes and global commodity prices have been determinant for the inflation. The two first are controlled by the national governments and the third one depends on global markets, which usually tend to raise prices.

GRAPH 6.11 All-items HICP (2005=100) annual average change rate (percentage)



Source: Own elaboration based on Eurostat data

In conclusion, the price level of a country and its changes does not depend on just one kind of price, whether on numerous prices. Some of them are internal factors, but others come from external markets, as the global oil price or the import price.

To can compare price levels of diverse countries, economists employ the Purchasing Power Parity. This indicator shows how many currency units a given number of goods and services cost in different states (Eurostat, 2008). Its main use is to convert national accounts aggregates, as GDP, into comparable real expenditures. After the conversion, comparing price level differences is easier and more reliable, because it ensures that the GDP of the compared countries is valued at a uniform price level and it only reproduces differences at the current economic volume.

Accordingly with GDP values in PPS in base of the European Union of 27 countries, Hungary is the biggest economy of the 2004 New Member States. Hungarian GDP is around 150 times bigger than the EU27 GDP, a brilliant rate for an emerging economy.

Estonian and Latvian economies joined to the EU in 2004, when they were a half of the dimension of the European economy. Since 2007, when GDP was in its highest position, they got decreasing the price level difference and just being 30% smaller than the EU. Lithuania is an example of how a small country has almost the double size of European economy.

TABLE 6.8 GDP in Purchasing Power Parity, 2004-2013 (EU27=1)

	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013
EU27	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00
CZ	16.96	17.10	17.24	17.17	18.24	18.46	18.27	17.87	17.67	17.94
DE	1.06	1.04	1.03	1.02	1.04	1.07	1.04	1.03	1.03	1.04
EE	0.58	0.60	0.64	0.68	0.70	0.70	0.69	0.70	0.71	0.74
ES	0.90	0.91	0.90	0.90	0.92	0.94	0.94	0.94	0.91	0.91
CY	0.87	0.87	0.87	0.88	0.88	0.89	0.89	0.89	0.88	0.86
LV	0.46	0.51	0.57	0.66	0.72	0.68	0.64	0.66	0.66	0.67
LT	1.67	1.78	1.87	1.98	2.17	2.14	2.04	2.08	2.08	2.11
HU	149.93	153.58	157.77	161.69	165.53	166.79	164.29	164.11	166.06	170.70
MT	0.67	0.68	0.69	0.70	0.72	0.73	0.73	0.74	0.74	0.75
PL	2.21	2.23	2.26	2.27	2.37	2.48	2.38	2.42	2.42	2.42
SI	0.73	0.73	0.75	0.77	0.81	0.86	0.84	0.83	0.80	0.80
SK	0.68	0.68	0.68	0.67	0.68	0.68	0.67	0.67	0.68	0.68
UK	0.75	0.76	0.77	0.79	0.83	0.87	0.91	0.93	0.92	0.92

Source: Own elaboration based on Eurostat data

GDP, inflation and unemployment have a strong relation which can change the performance of the economy of a country. The reason is that an increase of production implies a decrease of unemployment and its corresponding rate. If unemployment rate has decreased, likely there will be an increase in nominal wages. To can afford the increase of labour factor, firms will raise their prices and, as a consequence of that price growth, there will be an inflation period (Blanchard, 2009).

If we put together GRAPH 6.2 and GRAPH 6.11, we will see the parallel behaviour of the Estonian, Latvian and Lithuanian GDP and their corresponding inflation rates. In 2007 and 2008, the Baltic economies reached the highest GDP level since they added to the European Union, but also, the price levels had increased over 6% respect the previous year.

6.4 PUBLIC FINANCE

All economies have three economic agents (households, companies and Government) whose interactions are which creates value in a country. These exchange relations can be: physical, when a good or a service is purchased by a different agent to the one who has produced it; and monetary, in form of payment from a purchase, subsidies from Government to private sector (companies and households), payment of taxes from private sector to Government…

The two basis of NA are revenues and expenditures and the difference between total revenues less total expenditure is equal to net lending and net borrowing. The result of this calculation is the general government budget deficit or surplus, depending on if Government has spent more than their incomes (deficit) or not (surplus).

In the European Union, the Stability Growth Pact (SGP) delimited a maximum deficit and a maximum general government debt. General government debt is the nominal value of total gross debt outstanding at the end of the year composed from the sum of all sub-sectors of government (Eurostat, 2013). This pact is a procedure to the pre adoption of the euro, so any country which wants to adopt it must meet the following requirements: a budget deficit lower than 3% of GDP and a public debt lower than 60% of GDP. Who will decide the national fiscal policies of the country which have exceeded the limits is the ECOFIN, the council of Finance Ministers of the Euro area next to the Commission, which creates proposals to be followed by the ECOFIN.

Owed to the financial crisis, which affected global economy, this plan recognizes that there might be existed situations beyond than government's decisions which have had consequences at national economies. Some countries could have arrived to an excess deficit situation, because of international environment brought them to that point. Consequently, SGP considers an exceptional situation in which a deficit above 3% of GDP is not excessive only if GDP has decreased 2% or more in the same year. Besides of the exceptional situation, there is another intermediate one which considers the excessive deficit in a situation of GDP's decline between -0.75% and -2%.

Latvia and Lithuania were at the EDP during the crisis period as consequence of their high levels of government deficit. Fortunately, they could overcome quickly that situation and could join to the Euro Area recently (Lithuania has been accepted to be part of the Eurozone since 1 January 2015). Other economies have not had the same luck and still are suffering the consequences of the excessive deficit as Greece, Portugal and Ireland.

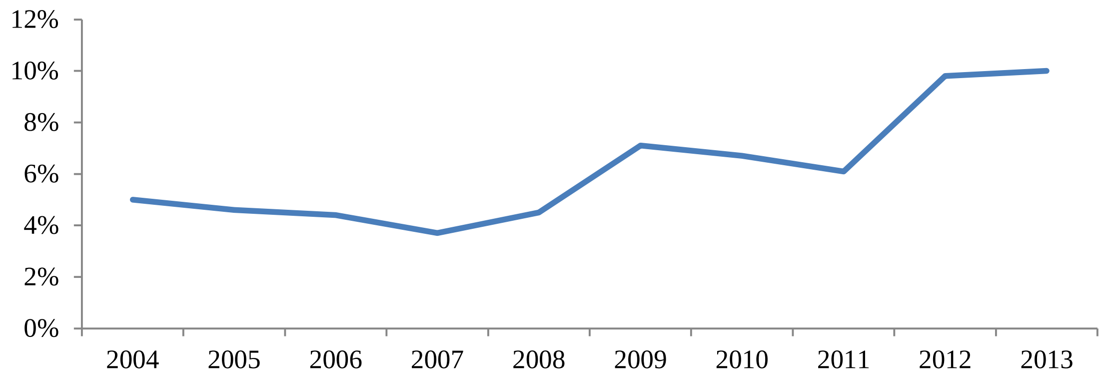
Despite of being the smallest economy of Baltic group, Estonian public finances have got being in surplus most of years at the period 2004-2013. The exceptions are found at crisis years and last 2 years, when expenditures have increased more than revenues. The good results obtained until 2007 were thanks to abundant revenues, the increase of domestic demand due to economic expansion and a bubbling effect on prices. If we take in consideration the adjustment after having discounted inflation from official information, during the entire period the result decreases, so inflation has helped to Estonian government's finances.

GRAPH 6.12 General government balance and cyclically-adjusted budget balance in Estonia, 2004-2013 (percentage of GDP)

Sources: Own elaboration based on Eurostat data and author's calculations

From 2004 to 2007, the expenditure-to-GDP ratio stayed around 34% of GDP on average, a low rate respect of results of other European countries. At the same time, there was a tax cut, so structural balance worsened three points in three years. The reasons of having kept revenues over expenditures were that government had accumulated some fiscal buffers for any possible recession and a good net asset position. Unfortunately, the crisis arrived to Estonia in 2008 and those fiscal buffers, which government still, had to be used next to fiscal consolidation policy to finance 2008 and 2009 deficits. These restrictive decisions implied the reduction of net assets and use non-market borrowing which implied a little increase in general government debt, from 3.8% in 2007 to 7.2% in 2009.

GRAPH 6.13 General government gross debt in Estonia, 2004-2013 (percentage of GDP)

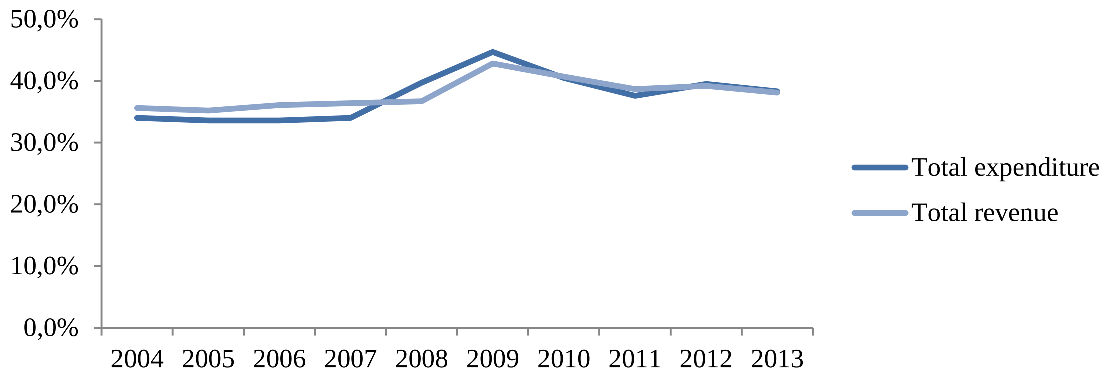


Source: Own elaboration based on Eurostat data

In 2009, other actions from the austerity plans were the increase in several tax rates (VAT reform on 1 July), which did not affect as much as expected domestic demand and the reduction of government wage bill and limiting social benefits as part of the reduction of government expenditures. The following years, the dynamic of government decisions was similar cutting expenditures and increasing taxes, which did that expenditure and revenue ratio stayed at the same in last part of the studied period.

Since 2012, general government deficit is due to the increase of expenses of local governments and central government (which makes bigger its percentage of foreign debts in loan liabilities) and the involvement of Estonia at the rescue mechanism, EFSF, for Portuguese, Greek and Irish economies (Statistics Estonia, 2014b).

GRAPH 6.14 Total general government expenditure and revenue in Estonia, 2004-2013 (percentage of GDP)



Source: Own elaboration based on Eurostat data

Forecasts to 2014 and 2015 are not optimistic, because Estonian finances will stay in a small deficit, -0.5% in 2014 and -0.6% in 2015. Economists expect these values based on reasons as a possible increase of public wage bill, the effect of pension contributions payment in revenues… But, not all is going to be bad news. A new revenue-enhancing package will contribute to compensate the increase of expenditures. Besides, excise tax rates will increase even more and there will be a reschedule of distribution of dividend of state-owned companies. The VAT reform planned to this year has been postponed to 2015 and, consequently, the planned deficit could be higher. General government gross debt is expected to decrease to from 10% in 2013 to 9.8% in 2014 and 9.6% in 2015 and it will be owed to the arrival of new EU development funds in 2014 (European Commission, 2014c).

About Latvia, it has been who has had the worst balance results of the three. The crisis truly affected them, having to ask for international financial assistance to the IMF and the European Commission. In 2009, the Council alerted by a deficit of 4 % in 2008, declared Latvia in a situation of excessive deficit and recommended national government to start corrective plans before 7 January 2010. The main recommendations were related to improving transparency and fiscal governance, as well as financial market regulation and supervision. After 2010, when the Council concluded that these measures had been taken, it took a position of supervisor of government budget situation set a medium-term financial assistance from 2009 to 2011.

When the international financial assistance concluded in 2012, the effects did not disappear with it. General government deficit decreased as reflect of previous consolidation efforts and the beginning of an economic recovery. Tax efficiency is one of the main results from the consolidation actions, which also has helped to decrease the government deficit. In last two years, the major part of government deficit comes from local governments instead of state government, so it proves that consolidation has been assimilated deeply in state fiscal policies.

It is important to adjust the results, because as it happened in Latvia, deficit was partly masked by inflation as structural balance shows. The procyclical fiscal effects of the economic expansion can be seen clearly in the period between 2004 and 2009, where the increase of price level caused higher government deficits.

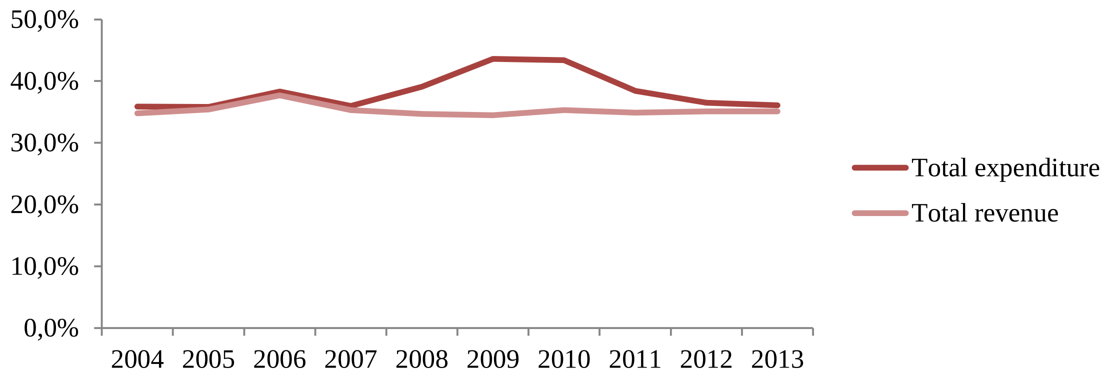
GRAPH 6.15 General government balance and cyclically-adjusted budget balance in Latvia, 2004-2013 (percentage of GDP)

Source: Own elaboration based on Eurostat data and author's calculations

The highest revenue ratio was reached in 2006, but since that year it fell significantly for reasons like a decrease from taxes revenues as a consequence of the economic downturn. The principal actions to improve the deficit situation in the crisis period were related to the increase of tax rates, but domestic demand was not as strong as it was. The revenue ratio stopped decreasing in 2010, despite the fact that in 2009 revenues coming from other sources which are not taxes were higher. At the last part, from 2012 to 2013, total revenue-to-GDP ratio has kept a stable value owed to the compensation between the improvement of non-tax revenues and the decrease of tax incomes.

Expenditures increased highly in 2008 and 2009 following the development of economic situation. To try to cut them, the Latvian Government focused on diminishing wages and employment in the public sector, social benefits and some indexation mechanisms were deleted. Nevertheless, they had to pay interest from the financial assistance, so the slight revenue increase was not enough for them. In 2013, despite the peak of government's consumption, total expenditures did not increase as much and remained stable.

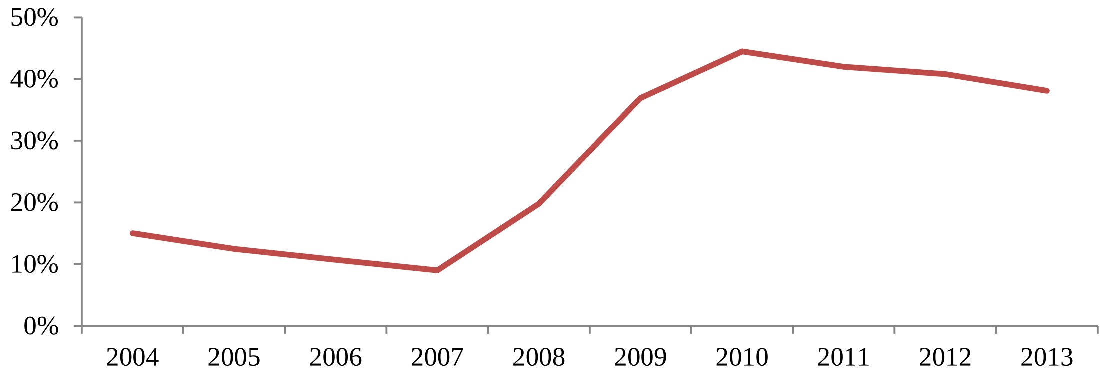
GRAP 6.16 Total general government expenditure and revenue in Latvia, 2004-2013 (percentage of GDP)



Source: Own elaboration based on Eurostat data

The sudden and high increase of government debt ratio was a consequence of the increase of deficit in boom years. Despite of being a good period to improve the government budget, national balance was worsening each year and the debt next to it. But it was not the only reason, the Government of Latvia made financial injections to the banking sector and after having nationalized Parex Bank in 2008. Also there was the international financial assistance which implied a repayment, but very low interest rates. The debt ratio stabilized in 2011 and declined in 2012 thanks to the access again to financial markets and favourable financing conditions which could help in an early repayment to the IMF in late 2012.

GRAPH 6.17 General government gross debt in Latvia, 2004-2013 (percentage of GDP)



Source: Own elaboration based on Eurostat data

For 2014 and 2015, it is expected that general government deficit will have a rate of -1% as consequence of lower labour taxes and the pension reform. Total government expenditure will also increase and the reasons of it are an increase in minimum wages and the resumption of pension indexation. Concerning government gross debt, firstly it will increase, from 38.1% in 2013 to 39.5% in 2014, to find enough investment to repay the EU due, but once the payment will have been made, the debt will decrease to 33.4%.

Lithuanian finances are closer to the Latvians than the Estonians. From 2004 to 2007, the results of the general government balance were small, but negative (around -1.5%). The crisis in this country concerned not only private sector, but also the public one. In 2008 and 2009, the domestic bubble burst and the global environment caused that the economic situation of government worsened, reaching deficit levels of -3.2% in 2008 and -9.4% the following year.

Lithuania is another country where the Commission had to take actions because of the excessive deficit in 2008. Despite of being a rate near of the reference value, 3% of GDP, it was considered exceptional, as it is stated in the SGP. The recommendations purposed by the European institution were in direction of correcting the deficit result before 2011 and of taking effective actions before January 2010. Unfortunately, the Lithuanian government found difficulties in applying corrective plans owed to the economic situations which were happening in that moment.

Thanks to consolidation measures took in 2010 and in the following years, deficit decreased to -7.2% in 2010 and -5.5% in 2011, proving the effectiveness of austerity fiscal policies. A year later, 2012, when the economic situation seemed to recover, the result of government balance was considerably closer to the 3% deficit limit, just 0.2% over it. It was not until the 21st of July 2013, when the Council decided to close the Lithuanian excessive deficit procedure.

The cyclical-adjusted balance decreased from -1% in 2005 to -5.8% in 2008, pointing out the existence of a procyclical fiscal stance during the expansion period. As the government did not exploited the potential of the economic growth through its budgetary targets and higher revenues, the consequence was that it spend more than its possibilities instead of saving money for possible downturns. The structural deficit in 2009 of -10.6% was estimated in a volatile economic environment, so it is not easy to handle with because of the cyclical components of the deficit.

GRAPH 6.18 General government balance and cyclically-adjusted budget balance in Lithuania, 2004-2013 (percentage of GDP)

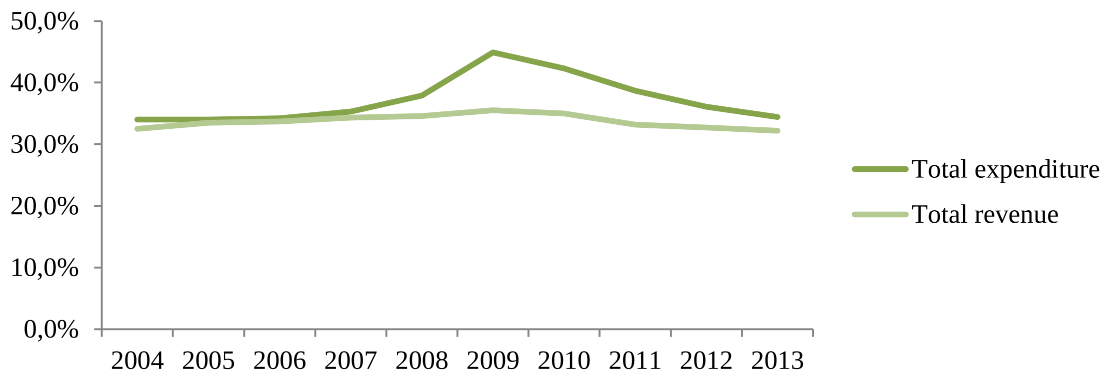
Source: Own elaboration based on Eurostat data and author's calculations

Concerning Lithuanian general government revenues, it increased 2.5% of GDP points in the period 2004-2008 as consequence of the good economic moment found in the country and higher inflows of EU funds. When the national economy arrived to the worst part of the crisis in 2009, revenue ratio did not decreased as much as it could be thanks to the arrival of new EU funds and, mainly, a considerable tax reform in taxes, such as VAT or excise duties. In 2012, revenues did not reach the target of increasing 3% points owed to facts like state-owned companies paid a half of the expected dividends to the budget, sales of carbon rights fell and local governments had a higher deficit than the expected. Despite of seeming that in 2013 the economy was recovering its previous levels, government revenues decreased as result of a slow indirect tax revenue growth, because the other kinds of revenues, like direct taxes, were increasing.

But not all in public finances is revenues. Expenditures also have an important role in the development of government results and, as it happened in Lithuania where they were controlled to avoid worse financial situations. Until 2007, the expenditure ratio was low, around 34% of GDP. In 2008, there were parliamentary elections, so to attract voters the Lithuanian government expended more money in social transfers and public sector wages.

The worst year of the studied period was 2009. In that year general government expenditures reached a level of 43% of GDP because of the contraction of the economy. It would have been worse unless Lithuanian had not taken consolidation measures. Examples of the actions taken are: the cut on public sector wages, which later ended in a wage freeze, temporary cuts in pensions and a reduction of social benefits. In 2012, the progress got in overall was mostly owed to expenditure restrictions on personnel, goods and services and social transfers. Last year, the expenditure ratio was 34.4% of GDP, close to pre-crisis levels thanks to previous and actual consolidation measures.

GRAPH 6.19 Total general government expenditure and revenue in Lithuania, 2004-2013 (percentage of GDP)



Source: Own elaboration based on Eurostat data

Lithuanian general government gross debt decreased along the economic expansion period, from 19.5% in 2004 to 15.5% in 2008, but when the European Commission and the IMF decided to give them financial assistance in 2008, the debt of the public sector in the following year increased to a 29%, almost the double. One of the reasons of this increase was in interest expenditure caused by higher financial needs and interest rates. These financial needs stayed in the following years as a consequence of having to repay the financial assistance given by international institutions and the injection of funds in banking system. General government debt has decreased from 40.5% of GDP in 2012 to 39.4% in 2013 as consequence of the new financial conditions in markets.

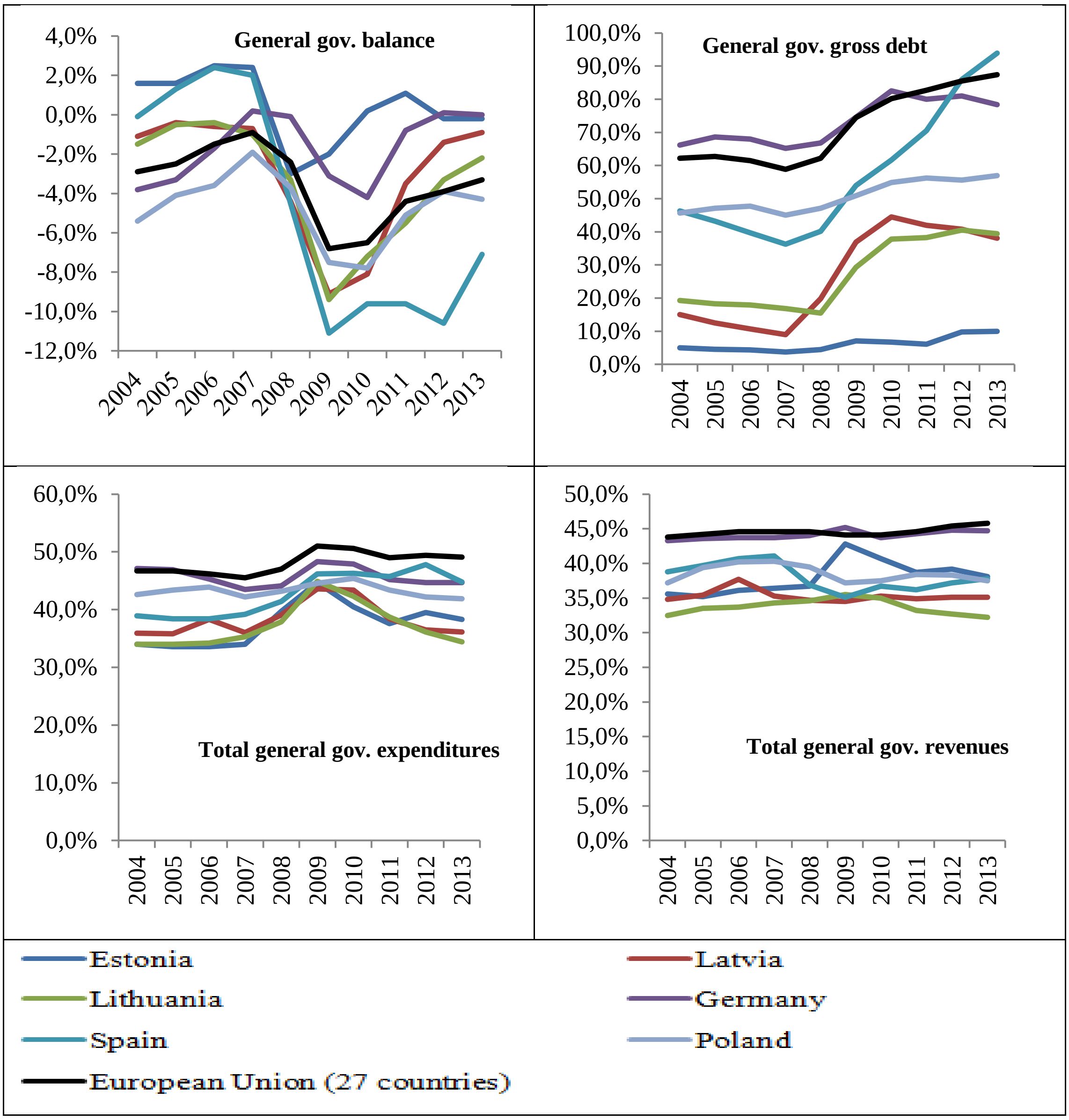
GRAPH 6.20 General government gross debt in Lithuania, 2004-2013 (percentage of GDP)

Source: Own elaboration based on Eurostat data

Last European Commission's forecasts from expect a decrease of government deficit in 2014 (-2.1%) and 2015 (-1.6%). These rates will be obtained if the expenditure growth keeps stable and the tax reform planned to 2014 is implemented, which will increase excise duties rates on tobacco and alcohol and thus an increase of tax revenues. At the other side, it is the compensation of cuts in public wages and pensions that will increase total expenditures. In April of this year, the Lithuanian Government approved paying cuts made during crisis in the pension system. During the next 3 years, Lithuanian government will expend a total amount of LTL 450 million (LTL 90 million for this year, LTL 180 million for 2015 and the same amount for 2016) (n.n., 2014). The European institution expects that the general government debt of Lithuania will increase to 41.8% in 2014 owed to the need of pre financing to 2015 bond payment. After having paid this debt, the debt will decrease to 41.4% of GDP in 2015.

The Baltic economies have not far from the results obtained by other countries. As an example, the German economy got worse ratios than the Estonian in general government balance and government debt. Estonia is the country with the lowest government debt ratio in Europe, which has got thanks to its fiscal model. During the boom period, Spain maintained similar rates to the rest of the countries. However, when the housing bubble burst in this state, in 2008, this economy suffered one of the worst fall downs of its history. Since that year, the Spanish government has kept excessive deficits and an increasing general government debt. Along this period, Lithuania has been the country with lower revenues and expenditures respect of GDP from this selection, followed by Latvia.

GRAPH 6.21 Public finances of some European countries (percentage of GDP)



Source: Own elaboration based on Eurostat data

All countries receive subsidies from the European Union, to help to general government revenues. The aim of these funds is the improvement of the country through the investment in some sectors of the economy or society.

In the European Union, there are 3 main policies which provide funds to countries which are: The Common Agricultural Policy, European Union regional policy and

European Union Competition and State Aid Policy. Just the two first policies concern this study of the integration of the Baltic countries, because the third it is more focused in private sector than in the public one.

- The Common Agricultural Policy (CAP) is a set of a lot of policies which has the aim of raising farm incomes in the European Union. This policy accounts near of 50% of the budget of the European Union, so we can see the importance in the group. What the CAP tries is to move from a simple agricultural sector to another one much more developed. The CAP last version has planned the funds which will be sent to countries from 2014 to 2020 and follows the same structure of 2003 version based on 2 pillars.

  The Baltic States are some of the countries which have received these funds to try to improve the life in rural areas, which are suffering a relevant emigration due to the low level of live in these parts of the countries. Recently, in 2012, Baltic parliaments have expressed their disagreement with the inequality of the distribution of rural development subsidies, because they consider that Baltic interests have been underestimated, in favor of other countries' interests (n.n., 2012).

  In Estonia, the preference will be the rural development (the distribution of subsidies gives to this pillar around the 55% of the funds). The total rural development budget breakdown in this country from 2007-2013 was €1,375,261,859 (Ministry of Agriculture of Estonia, 2009).

  Latvia gives more funds to its primary sector to try to help it to grow. The distribution this time so, is more balanced to the SPS pillar (almost 60% of 2007-2013 subsidies). Nevertheless, the total expenditure in rural development programmes is quite high, €2,035,636,340 (Ministry of Agriculture of Latvia, 2013).

  Lithuania is more close to the Estonian distribution, because rural development funds will be the 60% of total subsidies, a total of €3,145,885,773. As 97.4% of this country is considered as rural, this money will be really useful to can improve these areas and avoid the difference which exists between the urban and the rural area (Ministry of Agriculture of Lithuania, 2007).

  In 2014-2020 CAP, it is planned to progressively adjust the gap in direct payments which exists between the baselines for CAP reform and CAP reform agreement. After the CAP reform agreement, they will receive 200€/ha, but at the previous plan they had levels of 150€/ha (Lithuania) or less (around 100 €/ha in Latvia and Estonia), (European Commission, 2013c).

- The EU regional policy has the aim of taking care of the most disadvantaged regions. Not all the territories have had the same opportunities to grow and with this kind of subsidies, countries as Estonia, Latvia and Lithuania are benefit.

  Since Central and Eastern countries entered to the European group in 2004, the sum of these funds has increased considerably, giving less importance to CAP.

  To this policy, European Commission sends a third of its annual budget. Inside of the total amount, there will be 3 parts depending of the objective: Convergence (reducing income differences across EU regions; for instance, real GDP per capita of Baltic countries in 2013 were between the 10 lowest European Union rates); Regional competitiveness and employment (this topic is concerning about strengthening the competitiveness and attractiveness of the regions, as well as regional employment); and Territorial cooperation (it will aim to reinforce cooperation at transnational level).

  From this policy, Lithuania was the country from the Baltic group which has received more money, mainly from the Convergence Objective. None of these countries have received funds from the Regional Competitiveness and Employment Objective. The reason is because they have already received funds from the Convergence Objective with the same aim.

TABLE 6.9 EU Cohesion policy, distribution of subsidies by objective (€ million)

	Convergence Objective	Regional Competitiveness and Employment Objective	Territorial Cooperation Objective	Total
Estonia	3404	0	52	3456
Latvia	4531	0	90	4621
Lithuania	6775	0	109	6884

Source: Own elaboration based on European Commission data

Inside of EU Cohesion policy we will find the EU Strategy for the Baltic Sea Region (EUBSR). '*It is the first macro-regional strategy in Europe. It aims at* *reinforcing cooperation within this large region in order to face several challenges by working together as well as promoting a more balanced development in the area. The Strategy also contributes to major EU policies and reinforces the integration within the area'* (European Commission, 2014b, p. (online)).

The participants in this strategy are: Sweden, Poland, Denmark, Germany, Finland, Estonia, Latvia and Lithuania. Approved in 2009, this strategy follows three main objectives: saving the sea, connecting the region and increasing the prosperity in the area.

With all this money, project partners were co-financed in different percentages of costs generated by them depending of country provenience. About which concerns us now, we can say that Estonian, Latvian and Lithuanian partners were co-financed up to 85% (European Union,the, 2014).

In May 2014, it has been approved the Baltic Region Programme 2014-2020. Funds for this plan have increased 21.1% comparing the previous plan, a total of € 269.8 million which will be divided in 4 priorities: Priority 1, 'Capacity of innovation'; Priority 2, 'Efficient Management of Natural Resources'; Priority 3, 'Sustainable Transport'; Priority 4, support to the stakeholders of the EU Strategy for Baltic Sea Region.

Concerning about project partners co-financiation, the new programme to 2014-2020 follows the same structure of 2007-2013 programme, so they will have to co-finance their activities with their resources and, later, costs generated in the activities will be co-financed to Estonian, Latvian and Lithuanian partners up to 85% (European Commission, 2014c).

6.5 INTEREST RATES

Interest rates are one of the main topics of the monetary policy of a country, because they establish the money price.

If we wanted to compare cross country interest rates, we should use real interest rates. Otherwise, we will be comparing at the same level different price levels which it is incorrect, because each country has its own pricing characteristics (Knoot, 1996).

As we have just seen, governments have debts from that they have to pay to creditors. However, most of times, the public institution does not the money enough coming from its incomes and it has to use other financial resources to solve the lack of liquidity. The corresponding national government will launch bonds to be purchased by investors, who look for profitability in financial markets. The public debt bonds are considered by some investors as the safest financial assets, because it is ensured that they will be paid at the expiration date (Samuelson & Nordhaus, 2006). This kind of bonds offers long term interest rates, but the exact maturity will depend of the country. It may be 5, 6, 9, 10 years… varying of the need of funds and the time in which the Government expects to be able to pay shareholders. Because of its long length, interest rates are lower than the rest from other types of financial assets.

Not all countries have emitted public debt at the same amount, there are states which have more financial needs than other as consequence of higher levels of the debt-to-GDP ratio. For example, Estonia does not the need of creating public debt bonds because of its governemtent financial situation is the best of the European Union, being in surpluses at the balance several years, and its cautious fiscal policies.

Consequently, if there is no emmission for public debt financing, it will not be an interest rate. In article 140, fourth indent, of the TFEU (2012), it is declared the following criterion to be fulfilled by countries which want to join to the EMU: "*the durability of convergence achieved by the Member State with a derogation and of its participation in the exchange-rate mechanism being reflected in the long-term interest-rate levels*". In Estonia there are no sovereign debt securities that comply with the definition of 'long-term interest rate for convergence purposes' (European Central Bank, 2014). Either it has been found another indicator which could be adequate for that concept, so this country is not going to be analyzed because it does not fulfill the requirement of a homogeneous concept with the asked.

The interest rate analyzed from Latvia is extracted from secondary market yields on a single benchmark bond with a residual maturity of below but close to ten years. After having joining to the European Union in May 2004, long term interest rates of this country were falling from 4.95% to 3.56% in November 2005. Since that moment, interest rates were increasing more and more until 2009. The reasons of so high interest rates in mid-2008 and 2009 are the reactions in finacial markets and investors about the financial and economic situation in the country. Interest rates above 10% in 2009, (the peak was reached in November with an interest rate of 13.75%), reflected "*sharply rising risk premia and subsiding demand for LVL-denominated securities amid rising uncertainty about the exchange rate regime"* (European Commission, 2010, p. 112). In March 2010, the reference value of long term interest rates was fixed at 6% (resulting from the average of long term interest rates from Portugal and Belgium plus two percentage points), but Latvia was above it more than six percentage points, 6.8% higher.

From 2009 to July 2011, long term interest rates decreased thanks to the financial assistance which provided to the Government funds for the recover of the economy and the austerity fiscal policies. The end of the decreasing trend was because of the pressure in international financial markets returned, followed by stopping emitting 10 years bonds. Yields of 10 years bonds suffered pressures from the political uncertainty, in September, as consequence from early parlamentary elections and from the confussion coming from euro area sovereign debt markets, but still they behaved well, keeping a rate under the two digits.

In March 2012, the maturity of the single benchmark government bond which was used to asses the long term interest rate criterion changed to 9 years. In that time, the reference value was 5.8%, the same as the Latvian value (European Commission, 2012) so they fulfilled that aspect for the durability in case of convergencing with the EMU. In that year, the Treasury launched new public debt funds with a maturity of 10 years, but just a limited amount, being benefit from a better liquidity position of the governmnent. Consequently, the 10 years yields decreased on the primary and the secondary market.

In 2013, the reference value was stablished at 5.5% and a interest rate 3.8% below the reference, this country fulfilled the criteria. Thanks to the fulfillment of this criterion and the other three was possible to join to the Euro Area in 2014.

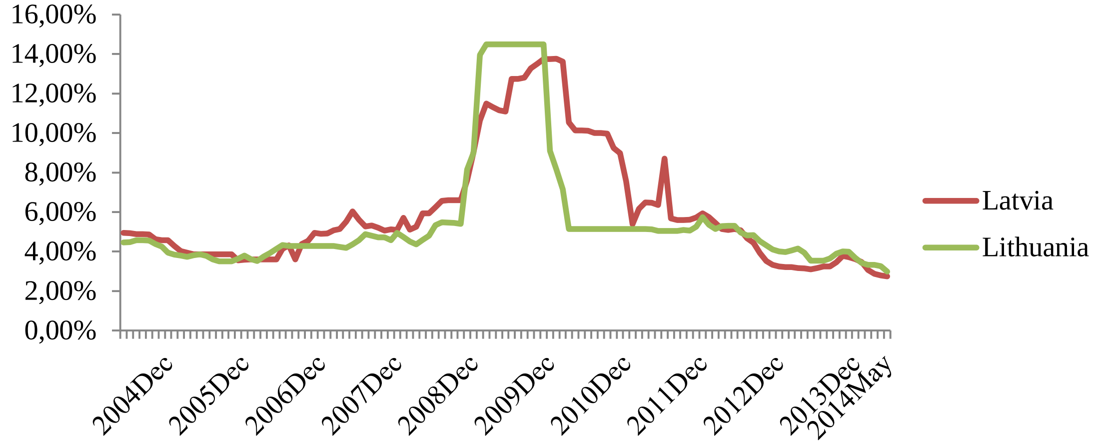
Lithuania has had approximately the same behaviour as Latvia in its long term interest rates. The long term interest rate used for asses the convergence report's purpose in 2010 was from a single benchmark bond on the secondary market with a residual maturity of 6 years, because there was not any other kind of bonds with longer maturity. From 2004 to 2008, interests were below the references which points out the good economic situation that the country was living in these years as the main reason of low interest rates.

Nevertheless, during most of 2009, when the pressure in the Baltic countries was high and lead to low or zero volume trades, Lithuanian long term interest rates were above the reference value required reaching the highest points (i.e.14.5% from February to November). Fortunately, in late 2009 and 2010 average long term yields started to decrease as consequence of "*an improved macroeconomic outlook, the successful issuance of long-term euro- and dollar-denominated bonds and a revival of risk appetite compressed litas"* (European Commission, 2010, p. 131). For instance, in March 2010 the reference value was 6% and in this country rates were around 12.1%, twice the convergence indicator but lower than the peak reached some months before.

Interest rates were kept the same level, 5.1%, from May 2010 to October 2011 owed to the recover of the economy which removed previous pressures about its financial markets. In March 2012, Lithuanian long term interest rate was at 5.2% , 0.6% point less than the reference, so, already in that date the country fulfilled this criterion. Interest rates still continued decreasing during 2012 and 2013 as reflect of improved investor feelings about the country supported by low inflation rates and higher sovereign credit ratings.

The long term interest rate used to asses the fourth criterion in Convergence Report 2014 was extracted from a single benchmark government bond on the secondary market with a residual maturity of around 9 years. In April of this year, interest rates were 3.6%, 2.6% less than reference value.

GRAPH 6.22 Long-term interest rates for convergence assessment purposes in Latvia and Lithuania, monthly, from May 2004 to May 2014 (percentage)



Source: Own elaboration based on European Central Bank and European Commission data

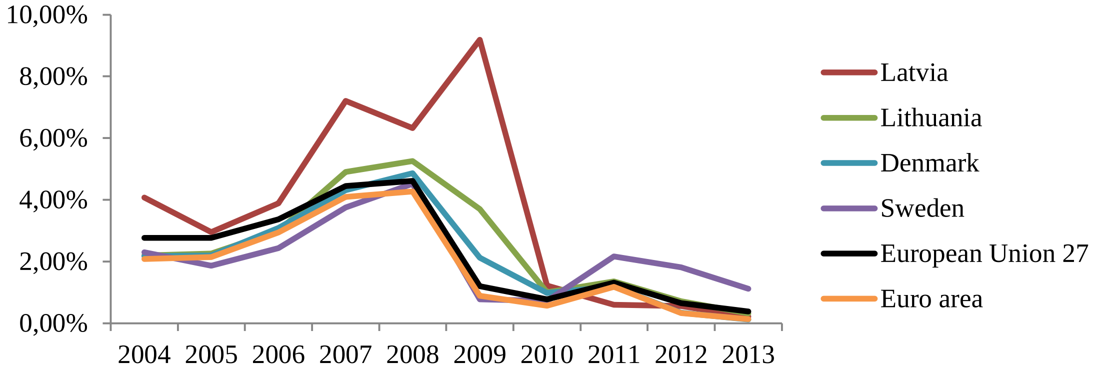
Obviously, these interest rates are not the only ones at the economies. There other types of interests at the money market which are important in order to create a monetary policy in a country. These rates from the money market, in case of the European Union, are controlled and fixed by the European Central Bank. They are who creates the common monetary policies which are followed by Euro Area countries and non Euro Area countries. Monetary policies are related with the control of money supply through the establishment of interest rates.

The money supply is the money in circulation at the economy, in paper or coins, the cash. It is determinate by the private banking sector and the National Banks, who provides reserves to private banks. The demand of this cash money will depend on the needs of private and public sectors of having money to do financial transactions or as a store of value (Samuelson & Nordhaus, 2006). Changes at demand of money go at the same direction of consumption and price level, inversely from interest rates. So, this is why it is important to European Central Bank and the rest of national banks controlling developments on interests, to crank up or to slow the economy (Barro, 1998).

A raise of interest rates, as at the period from 2004 to 2008, had the aim of controlling the increase of the European price levels which were rising reasonably. As we saw at part 6.3, in 2008 inflation rates were too high (i.e. in the three Baltic countries, the HICP reached the double digit), so it was necessary to control them to avoid increasing even more the price bubble. Unluckily, predictions about the burst were true and global economy fell down, including consumption, prices, investment... National governments and the ECB, worried about the fall down of the European economy, reduced the interest rates, in order to attract the private sector. Since 2009, European interest rates remain in low values below 2% (i.e. in 2013 Euro area's 1-month term interest rate was 0.13%, in Lithuania it was 0.32% and in Latvia 0.21%). This monetary policy has had

Latvia is an especial case, because, as we already know, they were in an excessive government deficit situation from 2008 to 2010. In 2009, they established an interest rate 9.19% monthly, much higher than in most of European countries, with the aim of maintaining price stability (European Central Bank, 2009).

GRAPH 6.23 1-month term interest rates at money market, 2004-2013, annual data (percentage)



Source: Own elaboration based on Eurostat data

Estonia has not been mentioned in this case either. The reason is because its interest rates are included at the Euro area data, even when they were not part of the group, from 2004 to 2010.

6.6 EXCHANGE RATES

Into economy, there are two types of exchange rates: nominal and real exchange rates. Nominal exchange rates are defined as the price of the domestic currency in terms of a foreign currency or as the price of a foreign currency in terms of the domestic currency

(Blanchard, Amighni, & Giavazzi, 2010). To avoid mistakes related to the currency base, we will use the Euro as domestic currency and kroons, lats or litas as foreigners.

The nominal appreciation or depreciation of a currency which is not the euro, but it is in the European Union, is controlled in a first part by the European Central Bank, which asses what effects could have that change of value in the euro, and then by the respective national central bank of that country. The non-euro area NCB is recommended to fix the bilateral upper and lower rates between the national currency and the euro for automatic intervention. Consequently, the ECB will act as intermediary between the euro area and non-euro national currency.

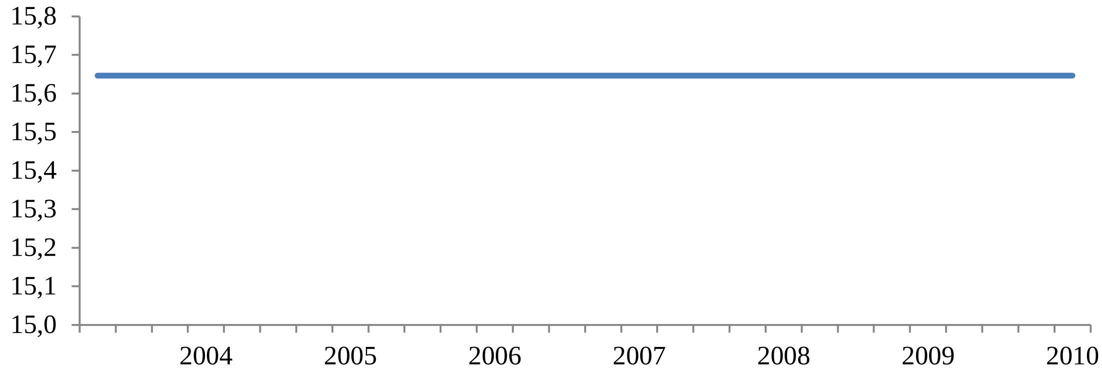
'Real exchange rate is the price of domestic goods in terms of foreign goods' (*ibid*, 2010, p. 112). This ratio is calculated through nominal exchange rate, which multiplied by the domestic price level is the dividend of real exchange rate. The divisor is the GDP deflator for the foreign currency area, in this report, for the euro area.

In 1st May 2004, when Estonia, Latvia and Lithuania adhered to the European Union, they already knew that one day they had to adopt the Euro and enter at the European Monetary Union. To can be part the Euro Area, a country has to fulfill the convergence criteria created by the European Commission and under control of the European Central Bank. One of the compulsory aspects to accomplish is the participation in ERM II at least two years before receiving the qualification for adopting the euro, always if there has not been any important tension. ECB will act as a supervisor of national monetary policies, because once the country adopt the Euro, the common monetary policy will be equally good for all countries. This equal result is due to a high business cycle synchronization between the New Member States and the European Union economy (Stanisic, 2013).

Estonian Bank set its central exchange rate following the parity rate in the existing currency board arrangement, pegged to the Euro since 1999, in 1 euro = 15.6466 kroon. This value could fluctuate between a standard deviation of ± 15% around the central rate, but that never happened. The currency board arrangement has been essential for Estonian economy, because it was an important pillar for fiscal policies during the economy contraction.

Until its disappearance, the Estonian kroon did not change its exchange rate in six years, despite the fact that some financial market indicators advise of an increase of risk perceptions in the financial crisis period.

GRAPH 6.24 Exchange rate EUR/ EEK, from January 2004 to December 2010 (quarterly values at the end of the period)



Source: Own elaboration based on European Central Bank data

Depreciation indicates an increase in market pressure and this does a loss of foreign exchange reserves or an interest-rate hike (Hewegerty, 2012). Owed to the stable value of Estonian currency, foreign exchange reserve in this economy stayed strong during the participation in the system, covering about 40 % of short-term external debt, mainly banks' liabilities to their foreign parent banks, (European Commission, 2010).

About Latvian lat, the central exchange rate was set at the parity in which lats were re pegged to the Euro in 2005 with a value of 1 euro = 0. 702804 Latvian lats. The standard deviation band agreed was ± 15% of the central rate, but during eight years, while this currency was in the system, it suffered changes in a fluctuation range ± 1%, as it has been proposed by local authorities.

There were periods of monetary tensions, mostly in 2007 and 2008, when Latvia was in troubles by macro-imbalances. The consequent currency devaluation rumours caused that during these two years exchange rate values were changing rapidly.

At the end of 2008, markets got increasing thanks to the sustainability of the peg with the Euro and the possibility of the absorption of contingent financial sector liabilities by the Latvian government. Also in that moment, as the country had already been suffering macroeconomic problems, they signed an agreement with the IMF and the European

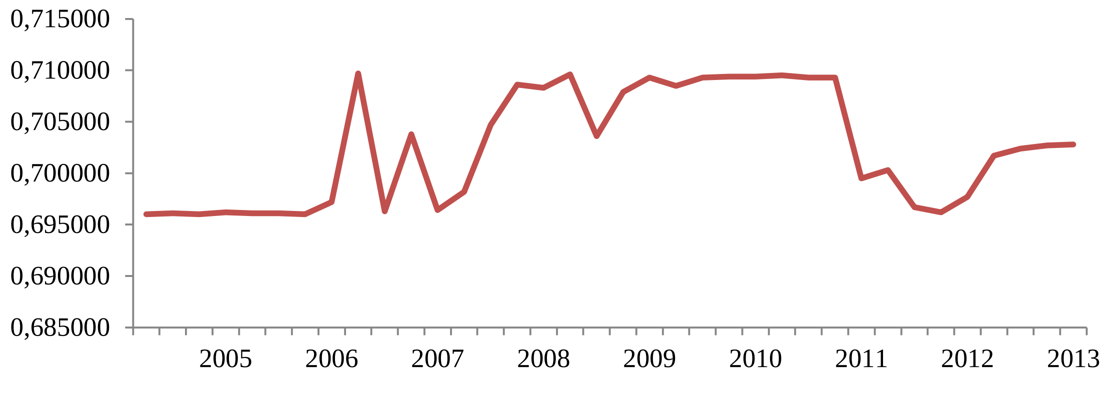
Union to receive international financial assistance. This last fact did that pressure over the exchange rate decreased.

In 2009, we could consider two clearly different parts. In the first one, from January to June approximately, instability in politics, a worsening economic outlook and contracting credit contributed to increase pressure on the exchange rate peg. In the second part, from July to December, pressures disappeared and international reserves stabilized. They were thanks to capital outflows from the banking sector.

The last IMF and EU payments from the financial assistance agreed in 2008 were in 2010. That year, Latvian economy had return to grow, so there were not rumours about a possible devaluation of the exchange rate.

From 2011, the Treasury of this country started to buy lats on foreign currency markets. This activity did lats stayed strong in the exchange rate band. Nevertheless, this practice does not last too much time and the financial institution left to purchase at the late 2012. Consequently, the supply of foreign currency decreased and the lat depreciated its nominal exchange rate. Another reason of the lower of foreign currency supply was that Latvian market was already expecting the adoption of the euro.

GRAPH 6.25 Exchange rate EUR/ LVL, from January 2005 to December 2013 (quarterly values at the end of the period)

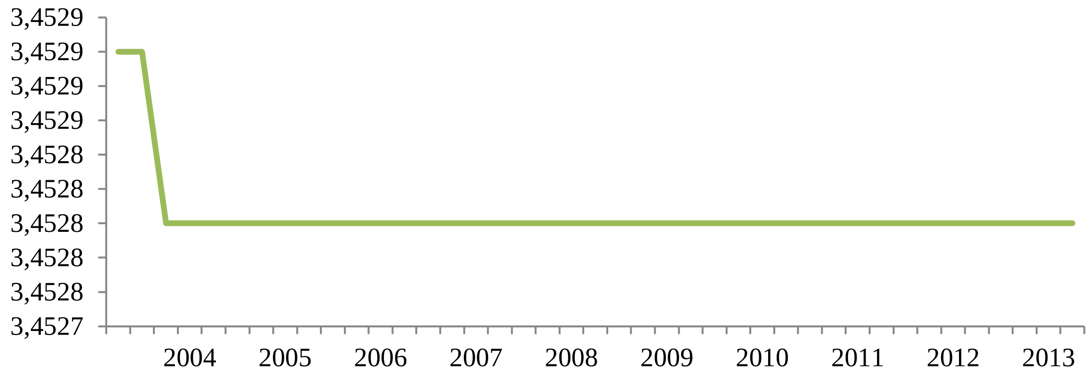


Source: Own elaboration based on European Central Bank data

International reserves of the Latvian Central Bank has been important for its monetary market, covering around 150% of base money and around 60% of M3 (the broadest measure of an economy's money supply) in 2013.

Lithuania is the only Baltic economy which still has its national currency. This monetary market established the central exchange rate in 1 euro = 3.4528 Lithuanian litas (following the existing currency board arrangement) and a standard fluctuation deviation of ± 15%, as the other currencies. However, it has not been needed any standard for rate changes. Since June 2004, litas have kept the same exchange rate which is good to fulfil the convergence criteria for adopting the euro. Even during the crisis, when risk perceptions increased, Lithuania maintained its rate.

GRAPH 6.26 Exchange rate EUR/LTL at the end of the period, from January 2004 to December 2013 (quarterly values)



Source: Own elaboration based on European Central Bank data

Foreign exchange reserves in this country have remained solid along the period, covering 144% in 2008-2009 and 165% in 2010 of monetary base (European Commission, 2014a). Therefore, they have a great support for all domestic liabilities of the central bank.

Summing up, for national banks have not been easy to deal with the challenges coming from the global economic environment. Maintaining a stability including supporting the currency pegs and the currency board agreement. All this is controlled through monetary policies, the European Central Bank is who creates plans and fixes interest rates at the Euro area. Those countries from the European Union and which have pegged its national currency with the Euro are not able to establish the level of interest rates, because they will be influenced by euro area’s interests. Therefore, nowadays the three Baltic countries owed to its national currency, Euros in Estonia and Latvia and litas in Lithuania, are under the control of the European Central Bank between other reasons.

7. INTERNATIONAL TRADE

International trade is an economic activity based on the exchanges of goods, services and capital between the countries from all over the world (Ballesteros Román, 1998). The reasons of exchanging products between purchasers and suppliers who are from different countries are several and quite different. For instance, Jones (2011) points out to the difference in population's assessment about what they have created and what others have done, most of times thought like better. Other reasons are the distance, (countries closer to each other are likely to trade between them), the available resources (in Estonia, Latvia and Lithuania, as consequence of their geographical characteristics, wood is an important national resource; human resources are high qualified as well), absolute advantage, comparative advantage... (Feenstra & Taylor, 2011).

Along the following chapter we are going to explain the different parts of foreign trade, exports and imports and foreign direct investment. Also at the end, we will find an explanation about the situation of international trade between our country and the Baltic group.

7.1 EXPORTS AND IMPORTS

Joining to the European Union has meant for these countries the opening to other countries' markets where they had already trading, but then with better conditions. Nowadays, they are well integrated at foreign markets, some more than others, as can be seen from last their ratios. The trade-openness ratios establish that in 2013 Estonia was 87.6%, Latvia 60.6% and Lithuania 86.4% opened to foreign markets. This shows a high trade orientation of Estonian and Lithuanian economy, mainly towards EU27 market which proves the integration of these countries at the group.

Trade balance is the result of the difference between exports less imports and it has the function of compensating domestic demand and domestic production (Jones, 2011). We have seen that production and incomes are equal when at GDP, so if there has been a gap between these two, the foreign trade will match both sides.

The trade balance can be considered as a way of knowing how attractive national products are for the rest of the world. If net exports component is positive that will mean that other countries wants to our products and it will act as an incentive to keep national economy growing. At the opposite, if there is a trade deficit, it points to national population prefers foreign products, which it will cause being further from economic potential (*ibid*, 2011).

When in an economy GDP increases and imports too, it is owed to facts as: a part of domestic demand's purchases is from foreign economies; some inputs for domestic production are produced abroad; and foreign price is lower as consequence of the exchange rate, it is obvious that purchasers will buy the cheapest product (Samuelson & Nordhaus, 2006). Therefore a trade deficit is not as bad as we thought at the beginning. If the increase of imports is linked to an increase of GDP too, it means that the domestic economy is growing in higher rates than other countries, so this is why demand needs more products.

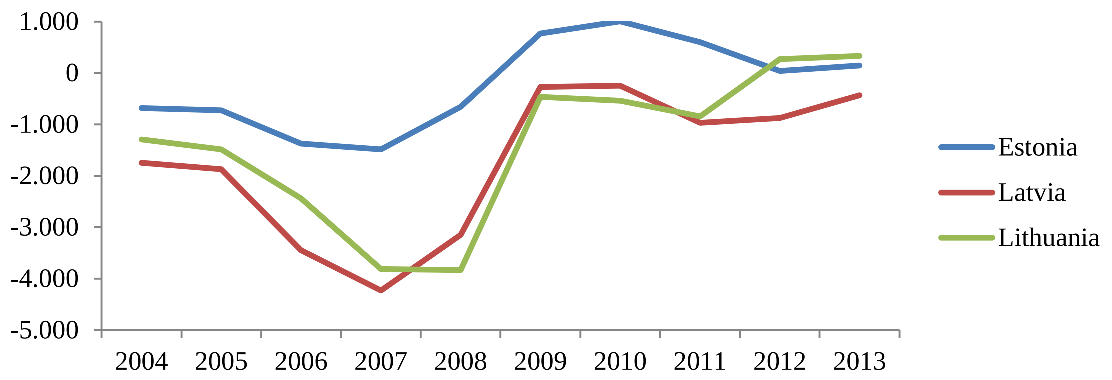
Real GDP growth rates of the Baltic countries between 2004 and 2007 were the highest ones of the European Union. If we use this information, next to the GDP composition of the three countries, we can conclude that the increase of imports was a consequence of the increase of private sector, mainly of investment of companies. During those years, the main supports of the Baltic economies were the industrial and construction sectors, economic activities which need high amounts of investment and inputs, which a part of them came from abroad.

With the economic contraction and the burst of real state bubble in 2008, the base of the economy suffered high financial difficulties and most of industrial and building firms had to close. It was not a good situation for households either. As consequence of higher unemployment rates and higher taxes, disposable income of individual fell down and with it consumption too.

Thanks to the recovery, economy in general seems to have reached pre crisis levels. Concerning imports, now Estonia, Latvia and Lithuania are at the opposite side, where economy grows and it is helped by an increase of exports. Baltic products are required by other economies and imports lose their previous significance. In fact, in 2013 Estonia and Lithuania exported more than imported (e.g. Estonian trade surplus: € 143.3 million; Lithuanian trade surplus: € 329.5 million).

We can remark that Estonia's trade balance has not been too many years in negatives values. This is owed to their economic stability, in which government balance had surpluses along most of period.

GRAPH 7.1 Net exports in the Baltic countries, 2004-2013 (€ million)



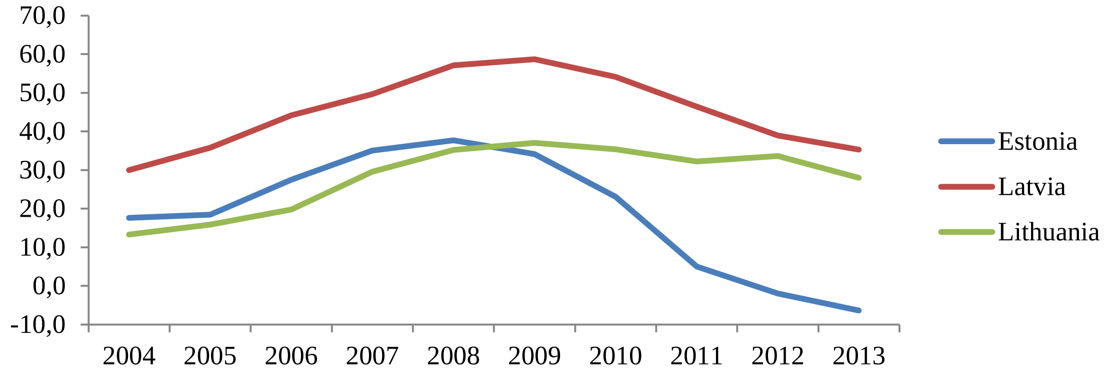
Source: Own elaboration based on Eurostat data

Another level in which trade balance can be used is to know the amount of net capital outflows. Taking into account that see in part 6.1 about investment and savings, the money used to purchase products from foreign countries comes from the money which was not expended at domestic economy.

Therefore, a trade deficit can be seen as an additional borrowing that an economy does to finance the gap between investment and domestic savings. The external debt of that country will change inversely to trade balance, because if a country buys more products to foreign market and contract a debt, the trade balance will be negative and the external debt positive. To this phenomenon, economists use the term "the emergence of the *twin deficits*" (*ibid*. 2006, pp: 494-495).

When the external debt of country is lower than debts which others have with it, that nation will be a debtor. Since 2012, Estonia has become in a net debtor to the rest of the world. Last information from 2013, it is that the debt contracted by third countries was 2% of Estonian GDP. At the same year, the other two Baltic countries had a net external debt of 28% (Lithuania) and 35.3% (Latvia). Having these debt rates does not imply any financial problem for them, because, as usual in these cases, there is not a date to return the money.

GRAPH 7.2 Net external debt in the Baltic countries, 2004-2013 (percentage of GDP)



Source: Own elaboration based on Eurostat data

About the structure of the trade balance in the Baltic countries, it is divided by extra EU27 trade and intra EU27 trade. Within the intra EU27 trade, it is contained exchanges between the 27 countries of the European Union. The extra EU27 trade includes exchanges between a European Union country and any other country of the world, including EFTA countries.

In Estonia, intra EU trade has had more relevance than extra EU trade in its international commercial relations. So, the joining to the group has meant for this country the strengthening of trade relations and the growth of foreign trade.

From 2004 to 2007, Germany, Finland, Sweden were the main European suppliers of products of Estonia. Imports from Latvia grew 160.81% and from Lithuania 121.02%, very high growth rates which shows the importance which had the accession to the common market for the three countries. Exports increased too, but not at the same rates than imports. The countries which imported more Estonian products were Finland, Latvia, Lithuania and Sweden. The extra EU27 trade was almost in balance, supported by exchanges with Russia, Norway and the United States.

The fall of the economy caused that domestic demand and foreign trade declined. Intra EU27 trade decreased, mainly imports which dropped from € 8,694 million to € 5,843 million. The reason can be found at the cut of imports from its European partners. In 2009, the year-on-year variation of imports coming from countries such as Finland, Germany, Latvia or Sweden decreased reasonably.

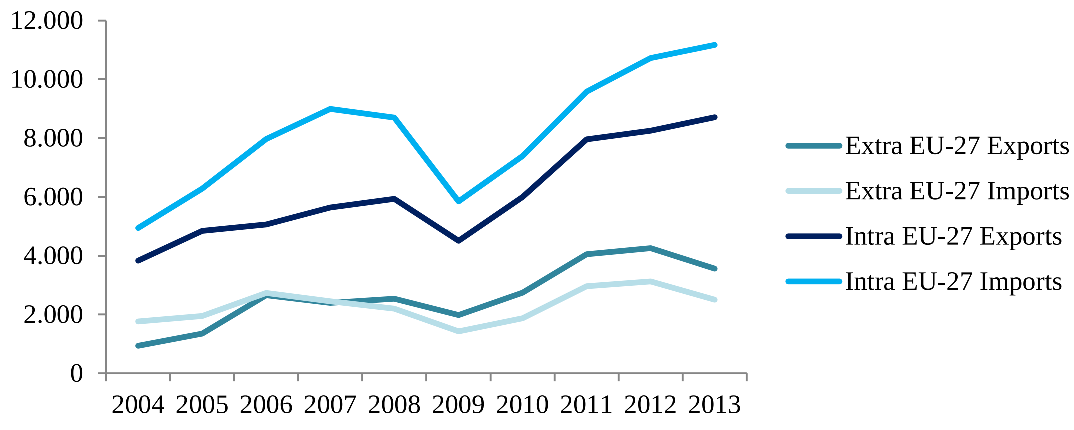
Thanks to the early recovery of national economy, mainly at the private sector, foreign trade has achieved higher levels of exchange comparing with the ones during the economic expansion.

From 2008 to 2013, intra EU27 imports grew 28.47%. A great part of this growth is owed to the increase of imports coming from partners like Finland, Germany, Latvia, Lithuania, Sweden and Poland. Exports with European countries increased at the same period 46.7% as a result of greater requirements of Estonian products at the Finnish, the Latvian, the Lithuanian and Swedish markets.

About the extra EU27, it has increased too, but still it does not reach intra trade levels. Russia is the greatest extra partner, with imports of € 787.2 million and exports of € 1,404.1 million in 2013, so last year Estonia was more exporter than importer with Russia. Other countries where Estonian exported frequently are Norway and the United States. At the import side, the structure is almost the same, with the difference of a new trade partner, China. Since 2008, Chinese imports have increased 215.73%, being last year the second extra EU27 supplier of products, behind of Russia. The increase of imports from this country is owed to its low prices and the power of its economy in the world.

The decline of imports and exports in 2013 is the consequence of the slowdown of Estonian economy, that has not had negative growth rates, but they were lower than previous years. Therefore, Estonia was not as attractive as it was during the economic expansion to foreign markets.

GRAPH 7.3 Extra and Intra-trade in Estonia (€ million)



Source: Own elaboration based on Eurostat data

The 5 main Estonian trade partners from 2004 to 2013 have been almost the same. There have been countries which have lost their relevance in favour of other countries, such as Germany at exports side and Russia at imports side. In overall, Estonian foreign trade has diversified its partners than and that has means the loss of significance of most of trade partners respect the total volume.

TABLE 7.1 Main foreign trade partners of Estonia and market share, 2004 and 2013 (percentage of total exports and total imports)

	Exports			Imports	
	2004	2013		2004	2013
1	Finland (23%)	Sweden (17%)	1	Finland (22%)	Finland (15%)
2	Sweden (15%)	Finland (16 %)	2	Germany (13%)	Germany (11%)
3	Latvia (9%)	Russia (11%)	3	Sweden (10%)	Sweden (10%)
4	Germany (8%)	Latvia (10%)	4	Russia (9%)	Latvia (9%)
5	Russia (6%)	Lithuania (6%)	5	Lithuania (5%)	Lithuania (9%)

Source: Own elaboration data based on Statistics Estonia data

The composition of Estonia’s trade in terms of goods is basically based on raw materials and labour-intensive products as consequence of the great weight of industrial and housing sector at the economy (European Commission, 2010). In 2013, the most import products were: oil and its derivatives (8.11%), chemicals (9.13%), telecommunications equipment (7.74%) and electrical devices (5.73%). About the export products, the most important were: oil and its derivatives (5.76%), telecommunication equipment (9.33%), chemicals (5.96%) and electrical devices (6.13%) (European Commission, 2014c).

Latvia has had a similar trade development as Estonia about the supremacy of intra EU27 trade at foreign market. Imports from European Union countries are the highest trade flows in Latvia, which evidences the great importance of relations with other European states to supply products to national demand.

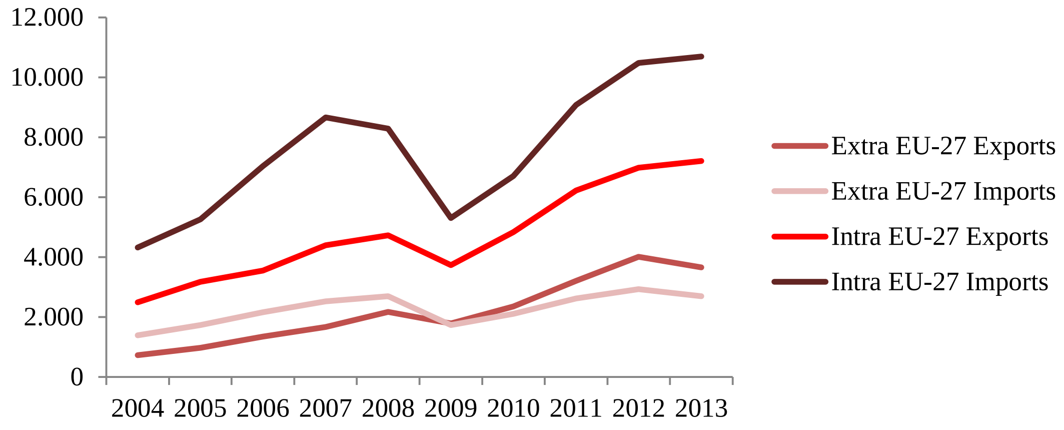
From 2004 to 2007, intra EU27 imports grew 29.1%. This rate is composed by the total of Latvian intra EU27 imports, but if we look a little more closely at data, we will check that imports coming from Estonia increased 131.3%, from Lithuania 126.7%, from Germany 118.7%... The exports obtained closer, or even better, rates than imports. As a whole, intra exports grew 52.4% and checking specifically some countries of the common market, for instance exports to Germany increased 32%, to Poland 83.44%, to Lithuania 213.83% and to Estonia 222.78%. So, the accession to the European group was a success for Latvian foreign trade.

Concerning the extra EU trade, it also increased its levels as result of the good economic situation and the reliability of foreign markets in Latvia (exports 40.5% and imports 13.5%). That growth came from stronger trade relations between Latvia and Russia, in which Latvian imports raised 96.8% and exports 180.93%.

In 2009, when crisis caused that all trade flows fell down, imports and exports of both trades. The financial assistance created doubts about Latvian economy and its national situation, so a great part of its partners reduced trade relations as consequence of the great government deficit and expectations about possible payment delays.

Fortunately, with the implementation of IMF and European Commission's recommendations, Latvia returned to grow in 2011, but foreign trade had started one year before. In 2010, consumption growth helped to increase Latvian domestic demand and consequently foreign trade, mainly imports. An improvement at the economic situation of its partners teamed up with the increase of entry of foreign products at Latvian market as the Lithuanians which increased 144.06% from 2009 to 2013 (this country was at the same time with Latvia at the EDP programme).

GRAPH 7.4 Extra and Intra-trade in Latvia (€ million)



Source: Own elaboration based on Eurostat data

Latvian trade partners are close to this country, to make easier commercial transactions. The strategic location of Latvia, at the middle of the Baltic region, has been important then. Trade relations with Germany are owed to the kind of product that each one produced and market characteristics, both highly-oriented to industry sector.

TABLE 7.2 Main foreign trade partners of Latvia and market share, 2004 and 2013 (percentage of total exports and total imports)

	Exports			Imports	
	2004	2013		2004	2013
1	Germany (13%)	Lithuania (17%)	1	Germany (15%)	Lithuania (20%)
2	Lithuania (10%)	Estonia (13%)	2	Lithuania (13%)	Germany (12%)
3	Estonia (8%)	Russia (12%)	3	Russia (9%)	Poland (10%)
4	Russia (6%)	Germany (7%)	4	Estonia (7%)	Russia (8%)
5	Poland (4%)	Poland (7%)	5	Finland (7%)	Estonia (8%)

Source: Own elaboration based on Central Statistical Bureau of Latvia data

The main tradable products of this country are related with industrial sector, but mainly in medium-to-low technology products as machinery or electrical equipment. However, in last few years medium-to-high technology products are becoming more important at the structure of Latvian goods market as consequence of improvement in R&D and higher skilled workforce (European Commission, 2013a). Also, a natural and abundant resource as wood is very significant for national economy. In 2013, the most exported products were: wood and articles of wood (16.1%), electrical equipment (10.1%), mineral fuels and mineral oils (8.1%), machinery (5.4%) and iron and steel (5.1%). The most imported products at the same year were: mineral fuels and mineral oils (16.6%), electrical equipment (9.7%), machinery (8.7%), motor vehicles (6.7%) and plastics (3.9%).This year, the economic activities which are supporting more Latvian foreign trade are manufacturing and wholesale and retail trade, as at exports as at imports (Central Statistical Bureau of Latvia, 2014).

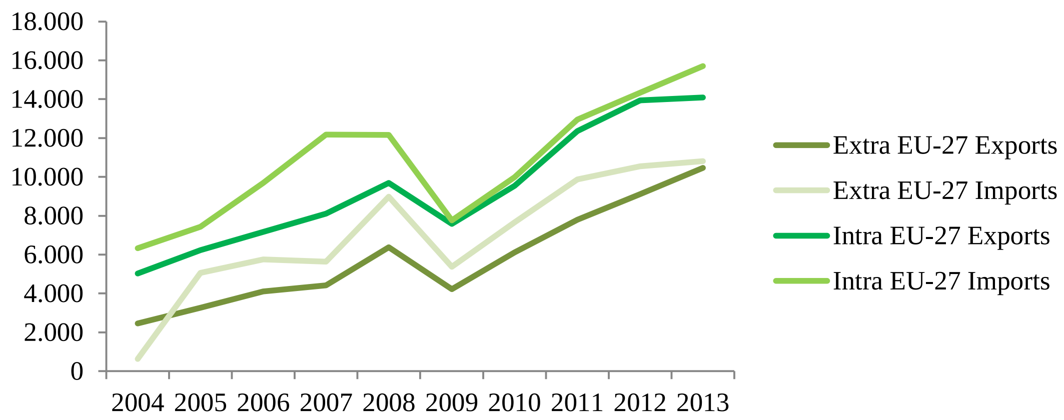
Of the three Baltic countries, Lithuania is the one which has had a more equal contribution of intra and extra trades to the total foreign trade. Intra imports increased from € 6,323 million in 2004 to € 12,169 million in 2008, 92.46% in 4 years as result of the increase of imports from Latvia, Poland and Germany. Exports to countries such as

Poland or Germany increased in each case 118.21% and 71.12% respectively, so we can imagine who will be the main Lithuanian trade partners and why.

The economic fall down caused that in 2009 intra exports and imports were much closer than ever, with a intra trade balance of € -170 million. The decrease of imports from Germany, -40.64%, and Poland, -38.05%, is owed to the critical situation of industrial sector in Lithuania that year. For investment, it was not a good moment. The expectations around their government deficit and limited financial possibilities did that the expending of private sector, which is the greatest part of domestic demand, decreased and next to it imports too.

With the recovery of Lithuanian economy, imports and exports returned to grow. The trade flow which has increased more since 2008 has been extra EU27 exports, 64%, in front of the 45.3% intra EU27 exports. Higher volumes of exports to Russia are the cause of this extra exports growth in last 5 years. In 2013, Lithuanian exports to Russia were 46.52% of total extra EU exports, so it is clear where this country sends more products. Imports also increased, as intra EU imports as extra EU. The greatest import growth rates, from its partners, were with Netherlands (85.96%) and Latvia (48.08%) from 2008 to 2013.

GRAPH 7.5 Extra and Intra-trade in Lithuania (€ million)



Source: Own elaboration based on Eurostat data

As we can see, bilateral relations between Lithuania and Poland and Lithuania and Germany were more important for its foreign trade than relations with the other two Baltic countries. In fact, Estonia in 2013 was the tenth supplier and the third customer, so Lithuanian products are required by Estonian markets, but not at the opposite. Russia has been the country which has achieved that intra and extra trades were closer, owed to the great importance that it has at international trade of Lithuania, despite the fact that there are some conflictions with the entry of some Lithuanian products at Russian market.

TABLE 7.3 Main foreign trade partners of Lithuania and market share, 2004 and 2013 (percentage of total exports and total imports)

	Exports			Imports	
	2004	2013		2004	2013
1	Germany (10.26%)	Russia (20%)	1	Russia (22.91%)	Russia (29.3%)
2	Latvia (10.19%)	Latvia (10%)	2	Germany (16.72%)	Germany (10.3%)
3	Russia (9.28%)	Estonia (7.5%	3	Poland (7.62%)	Poland (9.4%)
4	United Kingdom (5.32%)	Poland (7.4%)	4	Netherlands (4.02%)	Latvia (6.1%)
5	Sweden (5.05%)	Germany (7.2%)	5	Latvia (3.82%)	Netherlands (5.2%)

Source: Own elaboration based on Eurostat data

As it is usual at Baltic countries, a frequent exported product is that with medium-to-low technology level (machinery and electrical equipment). After the policy implementation to improve education and workforce skills, medium-to-high technology goods are becoming more important at national economy. Nevertheless, in Lithuania the profile of most exported products is mineral products. The most imported products in 2013 were: Mineral fuels, mineral oils and products of their distillation (30%); Nuclear reactors, boilers, machinery and mechanical appliances (8.2%); Vehicles other than railway or tramway rolling-stock, and parts (7.8%); and electrical machinery and equipment (5.3%). The products which had higher shares of total exports in 2013 were mineral fuels, mineral oils and products of their distillation (23%), nuclear reactors, boilers, machinery and mechanical appliances (7.4%), vehicles other than railway or tramway rolling-stock, and parts (5.8%) and plastics (5.6%) (Statistics Lithuania, 2014).

This year, the political conflict between Russia and Ukraine is having a direct effect on international trade, and mainly to Russia's partners as Estonia, Latvia and Lithuania. As answer to the international intervention, Moscow has established a ban on imports of some agricultural goods (dairy products, fruit and vegetables, fish and meat) whose provenance is the United States of America, the European Union, Canada, Australia and

Norway (Birnbaun, 2014). This measure could cause millions of losses in European economies, like in Lithuania, where these types of products of exports to Russia made a total of € 881.23 million in 2013. (European Commission, 2014c).

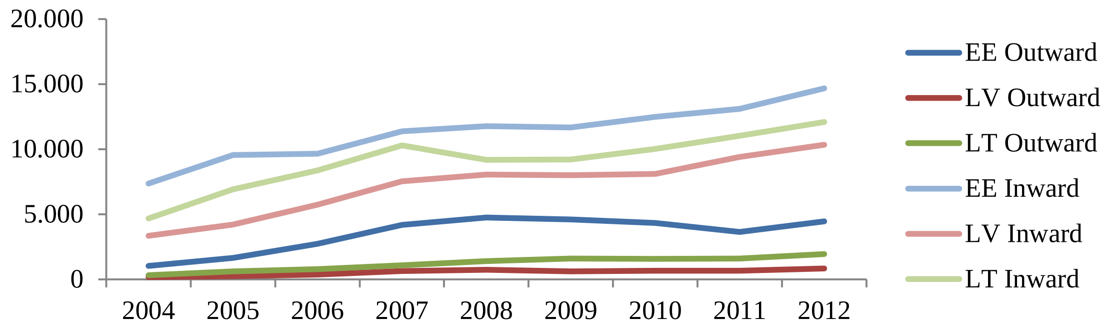
7.2 FOREIGN DIRECT INVESTMENT

Capital markets are also important at a country's foreign trade. With an exchange of money, companies could get the amount which they need for larger projects. If they staid just with national resources, growth would be quite difficult, almost impossible for small countries as the Baltic States. FDI is a common instrument of expansion for company. Through this method, a company sends capital to other firm in a different country with the aim of control a part of the foreign company or to acquire it.

The Baltic countries have the perfect profile for foreign investors: new EU developing countries; political stability; high GDP growth rates; low price levels; high skilled workforce; integration at the European common market; euro as national currency… Most of these characteristics thanks to the accession to the European.

This is why is not strange that inwards flows have been increasing since they joined to the group, in fact the inward flows growth rates from 2004 to 2013 were 98.9% in Estonia, 208.54% in Latvia and 158.02% in Lithuania. But, also there has been outwards of investment, Latvian and Lithuanian foreign investments lose less than € 2,000 million each year. Estonia, despite of being the country which less suffered the crisis, lost in 2008 € 4,674 million of investment as consequence of the austerity plans and their plans of increasing taxes.

GRAPH 7.6 Inward and outward investment flows in the Baltic countries, 2004-2013 (€ million)



Source: Own elaboration based on Eurostat data

The specialization of these nations in medium-to-low-technology goods can be explained by FDI. Most of countries which invest in Estonia, Latvia and Lithuania are developed economies which are looking for lower labour costs to outsource the production phase to decrease expenditures. There are some exceptions as FDI from Cyprus to Latvia. Banking sector in the Cypriot country has had to be intervened by international institutions in 2012 as consequence of a financial crisis caused by the accession to the Euro, the involvement with Greek economy and the failure of national policies to appreciate banking industry (Central Bank of Cyprus, 2013).

TABLE 7.4 Main FDI investor countries of the Baltic countries, 2013 (percentage of total FDI)

	Estonia	Latvia	Lithuania
1	Sweden (27.1%)	Sweden (21.2%)	Sweden (23.68%)
2	Finland (22.4%)	Netherlands (7.9%)	Poland (10.09%)
3	Netherlands (10.7%)	Cyprus (7.4%)	Germany (10.06%)
4	Norway (5.7%)	Norway (5.2%)	Netherlands (8.72%)
5	Russia (5.5%)	Russia (5.1%)	Norway (6.21%)

Source: Own elaboration based on Eesti Pank, Latvijas Banka and Bank of Lithuania data

The economic activities which received more investment are principally those related with the main exporter sector of these economies due to FDI's inflows have been great contributors to increase the export capacity of the Baltic countries. Lithuania will be a country where investment for R&D received more investment than many of manufacturing sector in which it is based its foreign trade. The reason is the high educational level of this country, as we have been mentioning previously. In 2013, the economic activities which had the largest FDI investment were:

- In Estonia, at the following order, wholesale and retail trade, financial and insurance activities and real estate activities.
- In Latvia, by this order, financial and insurance activities, wholesale and retail trade and manufacturing were the 3 main economic activities.
- Of the Lithuanian economic activities professional, scientific and technical activities, manufacturing and wholesale and retail trade, by this order.

7.3 THE BALTIC COUNTRIES AND SPAIN

Since Estonia, Latvia and Lithuania accessed to the European Union, the relevance of intra trade has been great. In fact, as we have just seen, the main support of their commercial relations is with exchanges with countries of the group. However, not all states will have the same significance at the Baltic foreign trade. The main trade partners are close to them, could it be another Baltic country or Russia, in which they were part of during long years.

Spain and the Baltic countries are at opposite of the European territory. Despite of the fact that trading between them is not easy because of distance, being at the same economic union has helped to establish commercial relations.

The relevance of Spanish products at Baltic imports is insignificant, less than 2% along the entire period. In 2013, market rates of Spain in these countries were 0.96% in Estonia, 1.38% in Latvia and 1.71% in Lithuania. Therefore, we can see that, despite of the fact that imports grew from 2004 to 2007 increased 89% in Estonia, 198% in Latvia and 215% in Lithuania, as in absolute values they are quite small that Spain has not a relevant position as main exporter to the Baltic nations.

At the export side, there is not too much difference with imports about the relevance of Spain at Baltic market. Spanish market does not purchase too many products from Baltic region, as we can see at their market share. The highest rate was reached by

Lithuania in 2005, 2.7%, but along the rest of the period, rates have been below of 2% in the three countries. For instance, last year imports in Spain from Estonia were 0.88%, from Latvia 0.50% and from Lithuania 0.74%.

Therefore, the common goods market has not helped quite much to Spain and Estonia, Latvia and Lithuania about a growth of trade relations between these states. They have their trade partners much closer than Spain and also within the intra EU trade, just with the exception of Russia.

Investments flows have had a similar behaviour where Spain is not an important investor at none of the three countries. In fact, in 2013 FDI from Spain to Estonia was € 15.1 million, to Latvia € 2.37 million and to Lithuania € 35.39 million, at the three cases less than 2% of total FDI in these countries. Spain received in 2013 from Estonia € 63.7 million, from Latvia there was an outward flow of € -0.75 million and from Lithuania € 14.08 million. So, Baltic and Spanish capital markets have not a great exchanging relation either.

All is not lost. If Spain wanted to increase their trade relations with Baltic markets, there are possibilities to export to some economic activities which are increasing their volumes at the domestic demand. In base of the cumulative growth rate calculated by data from last 10 years, the key products to export to Estonia are chemicals, machinery, transport equipment, oil and its derivatives and office and telecommunication equipment. To Latvia it would be advisable to send products like oil and its derivatives, gas, chemicals and machinery. Lithuanian market has increased their imports in products like fruits and vegetables, oil and its derivative, gas, chemicals and machinery.

8. CONCLUSIONS

After having analyzed all topics, we will be able to extract some conclusions:

The first, and the most important, it is that the accession to the European Union implies in fact an economic growth. With the integration in the group, they accessed to the European common market of goods, services and capital and to the free movement of people between countries. This last aspect has been relevant in terms of employment because when the crisis started, a part of Baltic population, mainly young people and families, went to other European countries looking for better labour conditions.

The two Baltic countries which more suffered population outflows were Latvia and Lithuania. With a low number of contributors in taxes, government deficits were worsening from 2004 to 2008. At the beginning of the crisis and the decrease of national production, the financial situation of public sector was even worse. Owed to the excessive public sector's deficits, Latvian and Lithuanian countries had to be intervened by the IMF and the European Commission which gave a number of recommendations to national governments to go out of the excessive deficit. The new plans implied changes in fiscal and monetary policies, as a decrease of government spending, tax reforms, rise of government bond interest rates… Estonia, although it maintained surplus levels along the pre crisis period, also used austerity plans. Economists in that country had predicted the close burst of the economy, so, before the global recession, they already were in a fiscal contraction. The fact of starting earlier did that they also returned to grow earlier, in 2010, when most of European economies were still decreasing. The welfare of these states worsened due to the cut of social benefits, pensions, health and education. This reduction was another reason why people left the Baltic countries.

These policies meant falls at households' consumption and at investment. Population saw how their disposable income was lower and investors, worried about if these measures would have the expected effects, decreased the money. Consequently, domestic demand at the Baltic countries fell along the crisis period and this reduction implies that foreign market decreased too. Imports fell down and the trade balance in Latvia and Lithuania achieved to be closer to be in balance in 2008 and 2009. Estonia had been closer of trade surpluses and nowadays, this country exports more than imports as result of their high integration at European good markets.

Deleting all trade barriers with European Union's members has helped to the Baltic countries to reinforce their foreign trade. Since they have entered to the group, their commercial relations are mainly with countries from the Union. Russia is the only extra EU country which has a strong weight in these economies, owed to historical aspects and the short distance between them.

The fact that Russia is one of the largest oil suppliers in the world can explain why when oil prices increased, import prices in the Baltic States increased too. Buying goods from abroad was more expensive for them. Consequently the general price level increased and this lead to high inflation rate periods from 2004 to 2008, when inflation rates reached the double digit. Exchange rates can't be use to explain the increase of imports, because in Lithuania and Estonia, until their addition to the EMU, these numbers stayed stable. Latvia used the appreciation of their national currency as a method to stabilize the economy, but that created negative expectancies to foreign investors. Nowadays, just Lithuania keeps its national currency, but not for long. Next 1 January, Lithuania will be the 19th country in adopting the euro thanks to their good economic situation.

Having a stable national currency was relevant for foreign investors. Inward capital flows have been increasing since they joined to the EU. The fact of being at the common capital market has been good for their main FDI investors because most of them are member of the group, as Sweden, Finland or Germany. They look for cheaper labour force to outsource manufacturing activities, which are the base of Baltic economies.

Once the crisis has passed away, Baltic economies seem to be returning to pre crisis levels, or higher, in domestic production. In fact, in 2013, Latvian and Lithuanian real GDP growth rates were the highest rates of the European group. Estonia did not suffered the same growth as their colleagues owed to problems with the austerity plans, that could be not so good at it was believed at the beginning of the crisis. National productions has done unemployment rates decrease, because it is needed again labour force to produce goods and services which will be sold at domestic demand mainly, but also at foreign markets, each day with a larger weight at national economy. Owed to expectations of keep growing, firms' prices are increasing. This last aspect can be a risk if it is not controlled, because this was how crisis in 2008 started between other reasons.

In conclusion, to avoid excessive inflation rates, wages should be low, but always maintaining population's welfare. By this way, if labour costs do not increased highly, prices will not increase either and consequently there will not be a decline in national production. Another decline in GDP, as it happened in 2008 and 2009, will mean higher unemployment rates, people will leave the Baltic countries and Government will reduce their revenues as consequence of less tax contributors, worsening public finance and deficits.

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RESUMEN

El objeto de este trabajo es analizar el impacto económico que los países bálticos han experimentado desde que se unieron a la Unión Europea en 2004, hace ahora 10 años. También este año se cumple el 25 aniversario de la Marcha Cantada, unos de los movimientos independentistas, que supuso el comienzo de la revolución social. Dado el escaso conocimiento que hay en España sobre esta región, lo que pretende a lo largo de todo el trabajo es analizar diversos aspectos económicos para, al final, poder concluir si realmente la adhesión al grupo ha supuesto algún cambio para estas naciones o no.

A partir de estadísticas internacionales procedentes de diversas fuentes, tanto a nivel supranacional como Eurostat, Fondo Monetario Internacional u Organización para la Cooperación y Desarrollo económico, como nacional, tales como las oficinas centrales de estadística de los tres países, se ha extraído la información relevante y elaborado tablas y gráficos que faciliten su análisis.

Estonia, Letonia y Lituania son tres países que tienen una historia en común con Rusia, ya que hasta 1991 pertenecieron a la Unión Soviética. Aunque las relaciones con este país siguen siendo muy importantes para sus economías, en 2004 estas naciones dieron un cambio de dirección a su futuro intengrándose en la UE junto con otros 7 nuevos estados miembros.

Este hecho sin duda ha marcado un antes y un después en estas economías, ya que desde hace diez años hasta 2013, la tasa de crecimiento media anualizada del PIB ha sido de 6,65% en Estonia, 7,68% en Letonia and 6,62% en Lituania. Durante los años de expansión económica, de 2004 a 2007, el hecho de formar parte de la Unión Europea fue positivo para estos países, ya que recibieron la confianza tanto de los inversores como de la propia población. Este optimismo por la economía se tradujo en un aumento del consumo de los hogares y de la inversión de las empresas.

Como podemos ver en el GRÁFICO 6.2, como consecuencia del comienzo de la crisis de 2008, sufrieron en 2009 un acusado periodo de recesión durante el que decrecieron en un año -14,1% (Estonia), -17.7% (Letonia) y -14.8% (Lituania). El menor descenso de la economía Estonia fue gracias al reajuste de la política fiscal y monetaria iniciado

en 2007, tras el avistamiento de una posible explosión de la burbuja de los precios inmobiliarios.

Los principales motivos de esta caída fueron varios como la caída del consumo de los hogares. Como consecuencia de la implantación de medidas de austeridad fiscales, hubo subida de impuestos, congelación de los salarios públicos… y con ello la población vio como sus ingresos disponibles eran cada vez menores, con lo que disponían de menos dinero para consumir. Otro motivo fue la caída de la inversión. Muchas empresas tuvieron que cerrar debido a la falta de financiación, por lo que la tasa de paro en este año aumentó significativamente. En 2009 y 2010, el porcentaje de desempleados alcanzó niveles superiores al 16% (GRÁFICO 6.7). Los sectores más afectados por los cierres de empresas fueron el sector de manufacturas y el de la construcción, muy importantes durante la época de expansión.

El gasto público participó en menor medida en la caída de la economía, puesto que estaba siendo regulado por las políticas de austeridad. Hasta entonces, dos de los países bálticos (Letonia y Lituania) habían estado acumulando grandes niveles de déficit público porque, a pesar de que los gastos habían crecido ligeramente (GRÁFICO 6.5), los ingresos fueron decreciendo a lo largo de los años. El motivo de que los ingresos, y más exactamente los procedentes de los impuestos, bajaran fue la emigración.

La Unión Europea cuenta con una libertad absoluta de circulación de personas entre países sin necesidad de permisos. Muchas personas, entre ellas jóvenes altamente formados y familias, abandonaron el país en busca de oportunidades en mercados de trabajo extranjeros, como el de Gran Bretaña, Alemania, Suecia y Finlandia. Estos movimientos migratorios fueron más acusados con la crisis y el año de mayor salida de personas fue 2010, cuando estos países ya habían sido intervenidos y no se auguraba un futuro próspero para estos.

En 2009m tanto Letonia como Lituania fueron intervenidos por el FMI y la Comisión Europea. Estonia consiguió mantenerse al margen de esta operación gracias a sus niveles de superávit público durante todo el periodo de expansión económica. Las causas de que las instituciones internacionales tomaran medidas fueron: los altos niveles de déficit público (GRÁFICOS 6.15 y 6.18) y los altos niveles de deuda pública (GRÁFICOS 6.17 y 6.20).

Las medidas que los organismos internacionales recomendaron a los gobiernos lituano y letón fueron dirigidas a recortes en las partidas de gastos públicos y un aumento de los impuestos. Con ello se pretendería reducir los niveles de déficit antes de 2012, fecha esperada de la recuperación económica. A raíz de esta intervención, ambos países contrajeron una deuda con el FMI por la asistencia financiera ofrecida, lo que repercutió en sus tipos de intereses.

Los niveles de déficit y de deuda pública son los fijados en el Procedimiento de Déficit Excesivo, creado para mantener una estabilidad económica general. Este programa fue clave para la entrada de los 3 países en la Euro zona, ya que estos dos aspectos son tenidos en cuenta en el Mecanismo de Tipos de Cambio II. Estonia gracias a sus buenos niveles económicos pudo unirse a la Euro zona el 1 de enero de 2011, cuando ya había retomado el camino de crecimiento económico. Letonia entró este mismo año, el 1 de enero, tras haber cumplido con los requisitos. Lituania se encuentra ya en periodo de ajuste, puesto que en 2015 ha sido fijada la fecha de entrada a la unión monetaria. Con ello, los tres países bálticos serán parte de la zona Euro, lo que les podría beneficiar su comercio internacional.

Para dar salida a los valores de deuda pública, los gobiernos de Letonia y Lituania han ido subiendo y bajando los tipos de intereses de los bonos del estado a largo plazo en los últimos años, según las necesidades del momento. Estonia no ha tenido la necesidad de tener que emitir estos valores a los mercados financieros gracias a los resultados positivos de las finanzas públicas. La principal subida de intereses se produjo en 2008: como consecuencia de la crisis, los gobiernos nacionales intentaron atraer a los inversores con altos tipos. Al encontrarse en un periodo de incertidumbre en los mercados financieros, se esperaba una posible apreciación de los lats de Letonia y las litas de Lituania, por lo cual aquellos interesados en invertir en los fondos públicos desde el extranjero, se vieron limitados por las circunstancias económicas.

Aunque los tipos de cambio de las litas sí que han conseguido mantenerse estables durante todo el periodo del estudio (GRÁFICO 6.26), al igual que lo hicieron las kroons de Estonia en su momento (GRÁFICO 6.24), los lats han sufrido periodos de apreciación y depreciación. El Banco Nacional letón fue cambiando el valor de la moneda nacional como consecuencia de la situación económica del país y de la intervención financiera del FMI. Los principales cambios de valor de los lats frente al

Euro, moneda con la cual estableció su tipo de cambio, fueron en 2007 y 2008 en los que el valor de los lats fue depreciado debido a los desequilibrios económicos (GRAFICO 6.25).

Por tanto, en el comercio internacional de estas tres naciones más que un tipo de cambio favorable, los factores de su crecimiento provienen de otras causas. Sin duda, desde que entraron en la UE, y con ello en el mercado común de bienes y servicios, los países bálticos se vieron altamente beneficiados. Estos países, dadas sus características nacionales, fuertes en la producción de bienes industriales de media baja tecnología, donde basan su comercio exterior. Desde que entraron en el grupo las importaciones han ido incrementando cada año, al igual que las exportaciones. La procedencia de estos flujos de bienes es principalmente europea (TABLAS 7.1, 7.2 y 7.3), aunque Rusia sigue teniendo gran relevancia en los intercambios comerciales.

Debido a la gran importancia de las importaciones en las economías bálticas, un incremento del precio de las importaciones junto a la subida de precios del petróleo (unos de los productos base del comercio extranjero de estos) hizo que los precios fueran subiendo cada año más hasta 2008, donde alcanzaron su máximo (GRÁFICO 6.11). El nivel de inflación en 2008 era tan insostenible que, como consecuencia de los altos precios, las producciones nacionales cayeron y con ello el aumento del desempleo el mismo año.

La inversión extranjera directa en estos países no ha hecho más que aumentar en los últimos diez años. Aunque haya flujos de salida de capitales extranjeros, estos representan una mínima parte de toda la cantidad recibida. Estos flujos de dinero tienen como destino empresas filiales de otras pertenecientes a la Unión Los principales inversores de estos países buscan llevar allí parte del proceso de producción para así abaratar los costes, de ahí el gran aumento de las importaciones y de las exportaciones. Debido a este proceso de outsourcing, hay una gran relación entre los países inversores con los que realizan sus operaciones de intercambios de bienes, por lo que principalmente serán naciones del grupo y Rusia.

En cuanto a las relaciones comerciales entre España y los países bálticos. Desde que entraron en la UE, tanto las importaciones como las exportaciones han aumentado, pero el valor de estas operaciones es tan bajo que la cuota de España en los mercados de

Estonia, Letonia y Lituania es casi simbólica en todo el periodo. Tampoco las importaciones en España de productos procedentes de estos tres países han sido muy significativas, por lo que estos países y España realizan muy pocos intercambios. No ya solo las relaciones comerciales de bienes y servicios son escasas, sino también las de capitales, en las cuales se ha invertido poco dinero por ambas partes.

Una vez pasados los efectos de la crisis en estos países, parece que la actividad económica vuelve a crecer. Aunque Estonia en el último año tuviera una tasa de crecimiento baja, a causa de un largo periodo de contracción fiscal, el resto de países bálticos ha tenido unos niveles de crecimiento muy buenos, entre los mejores de toda la Unión Europea. Gracias a este crecimiento, también se están viendo mejoras en el desempleo, el cual se encuentra en decrecimiento desde 2010 y en la inflación con un nivel de precios controlado.

Como conclusión, podemos decir que el hecho de haber entrado a la Unión Europea no ha supuesto más que beneficios para estas naciones. Desde el poder entrar en un mercado común, en el que existen mayores posibilidades de oferta, hasta el poder usar una moneda común con sus principales clientes y proveedores para facilitar las transacciones, los efectos en su economía han sido más que notables. Su crecimiento de producción nacional para poder satisfacer tanto las necesidades nacionales como las extranjeras, ha supuesto que el nivel de desempleo haya sido bajo en el periodo 2004-2013, a excepción de los años de la crisis. Con una baja tasa de desempleo, los precios han ido aumentando durante estos años, lo cual no es mala indicación, siempre y cuando este ascenso sea moderado. El hecho de contar con el respaldo de un grupo tan importante a nivel internacional como es la Unión Europea, ha hecho que estas economías hayan podido crecer a lo largo de estos diez años y según las previsiones su crecimiento no parará aquí, sino que se prolongará al menos unos años más.