

LETTLAND

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The Social Gap: A Continuing Problem in the Growing Lithuanian Economy

V. DIKIL FORUM "SOCIAL MARKET ECONOMY"

Lithuanian economy is already growing almost most rapidly in the European Union (EU) for several years. According to Eurostat projections, the country's GDP will grow by 3,1 percent in this year, while the EU's – only by 0,1 percent. However, despite such positive economic prospects, according to 2011 data, Lithuania was the fifth from the bottom between all the EU Member States by the persons living below the at-risk-of-poverty threshold – the at-risk-of-poverty rate was 20 percent. The situation was worse in Spain (21,8 percent), Greece (21,4 percent), Romania (22,2 percent) and Bulgaria (22,3 percent). The question is how to deal with this sensitive lasting post-crisis issue.

In "Europe 2020" strategy one of the five targets is to reduce the number of persons living below the risk-of-poverty threshold by 25 percent, i.e. to bring at least 20 million people out of poverty and exclusion. It needs to be noted that 16,1 percent the EU's residents were living below the risk-of-poverty threshold in 2011. So, it is seeking to reduce this rate up to about 12,1 percent by 2020.

However, talking about goals, needs to talk about ways to achieve these goals, i.e. on what particular way should be followed, what welfare state model is the most appropriate in dealing with social exclusion issue – **implementing poverty and social exclusion reduction measures. It is said that crisis has passed has opened new opportunities. Is it learned to use**

them? Will it be going on the same way as by the end of 2008?

I should note, that the fusion of post-soviet economy and neo-liberal economic model that has been thriving in Lithuania for the latter two decades and irresponsible fiscal policy not only determined that Lithuania is one of the leading in terms of social exclusion but also deepened social and economic dividing lines between Vilnius and other regions. Or it will nevertheless be selected such a model which would ensure a sustainable economic development and long-term rather than short-term welfare.

What does it say about poverty?

In Lithuania, 20 percent of residents were living below the risk-of-poverty threshold. This is one fifth of the country's residents. By the way, it may be noted that both during rapid economic growth and crisis this rate remained practically the same. It was determined by the fact that during economic crisis of 2008–2010, fiscal consolidation burden had been allocated on all social groups almost equally to stabilize public finances and ensure confidence of financial markets. Saving policy, implemented structural reforms have helped to deal the crisis. Lithuania and other Baltic states has become an example for other EU Member States, especially for the Southern ones, of how to responsibly manage finances.

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Persons with monthly income less than LTL 691 (200 Euro) were living in poverty. On the other hand, average annual inflation was 1,2 percent in 2010 and 4,1 percent in 2011. Thus because of increasing prices residents have to spend more disposable income for the minimum consumer basket of goods and services. Given the current prices and residents' purchasing power, the monthly net income should be around LTL 1000 to live with dignity.

So, this is an issue of persons with the lowest income, their income level and absolute poverty. By solving this it needs that income of such residents would increase. **Only increasing redistribution is not sufficient way, because in order to redistribute more, needs more those who can earn relatively higher income. For example, currently, the share of those who earn more than LTL 5000 per month and are able to pay a higher income tax amounts to about 5 percent of all employees.** Therefore, it is also important increase the share of such residents.

When there is a narrow distribution of people with high income and rather broad one with low income, attempts to increase income redistribution to pay higher benefits **could promote "dependant society" phenomenon that has emerged during economic crisis.** Having reduced wages of many employees, increased unemployment, some benefits, for example, unemployment, became close to wage or even began to exceed it. So, this reveals a problem. The person is encouraged to be a state dependant rather than look for a job and earn himself. Moreover, the share of such "poor ones" does not avoid cheating the state: receiving social benefits they work unofficially and their total income are often higher than the net minimum monthly salary (MMS).

Social security system should be efficient so that ensure an adequate social security for people who have no chances to receive income under adequate market conditions, while encourage them to work and earn. **One of these decisions – more responsible distribution of social benefits, but**

so as to avoid the poverty trap. Another – increasing the MMS to LTL 1000 to encourage people to work. Of course, the latter increased the net incomes of MMS receivers but also increased the price of job. Hopefully, labour market and public finances were not destabilized.

Concerning wages, it is worth noting that, in Lithuania, **labour is taxed more than capital (wealth) which amounts to about 4 percent of all tax base while in euro zone – to about 17 percent.** Therefore, by seeing to help for those with low income, first of all, it needs to reduce taxation burden on labour through increasing the monthly tax-exempt amount (TEA). This would also contribute to reducing unofficial wage, increase the motivation to work and country's economy attractiveness to investors and competitiveness.

Moreover, families, especially large and single-parent ones, have the highest probability of falling below the at-risk-of-poverty threshold. **Therefore, to help them, ensure their financial stability, it would be appropriate additionally to increase TEA for married couples, i.e. for residents formalized their property relations, and the additional tax-exempt amount (ATEA) for children.** Such a financial support for families is likely partially to contribute to strengthening family's institute and increasing fertility.

Furthermore, support for poor ones through TEA is much more effective rather than through social benefits which, as mentioned before, does not encourage person to work. Of course, such decisions should be well measured, taking into account the state's financial possibilities that public finances would not be destabilized (3 percent of fiscal deficit).

It needs to consider introduction of a universal real estate with tax-exempt amount or capital gains tax. These would also allow equalizing taxation burden between labour and capital and providing more progressiveness to taxation system.

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What kind of welfare system does Lithuania need?

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We need Social market economy model, which we can be named as a Motivational model. Where social policy is an element of economic policy encouraging work, to improve skills of qualification and to contribute to job effectiveness and productivity.

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