



PARLIAMENT OF ESTONIA

**A comparative review of socio-economic  
implications of the coronavirus pandemic  
(COVID-19) in the Baltic States**

FORESIGHT CENTRE



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This review is a joint work of Foresight Centre of Parliament of Estonian, LV PEAK of the University of Latvia and Government Strategic Analysis Center (STRATA) of Lithuania. The review was finalized in October 2020.

## **Introduction and aims**

The COVID-19 crisis has been a true black swan – an unexpected event that is having enormous consequences on virtually every aspect of our daily life. Next to the 1918 flu pandemic that occurred in a very different socio-economic context, there are no historical parallels close to the current crisis, which makes forecasting and future prediction a tough task. Due to the global scale of the crisis, the collaboration and joint efforts are at the heart of solutions to the COVID-19 situation. Close cooperation is especially important in the Baltic region with highly interconnected economies and societies. This paper aims to provide a comparative picture of the effects of the crisis and describe the key factors and uncertainties affecting the recovery. Despite the sharp recession, there are also some opportunities arising from the situation, which are discussed in the third section of the paper. The concluding section presents possible coordinated policy actions that could support speedier recovery, long term technological progress and sustainable growth.

### **1. The uneven geography of the crisis: economic effects in Estonia, Latvia and Lithuania**

Three states entered the crisis in slightly different positions. The economic momentum was slowing down in Estonia and Latvia already in the second half of 2019 whereas Lithuania was still showing a steady growth. The reasons behind the slowing growth in Estonia and Latvia were the structural problems and labour shortage that resulted in lower manufacturing output and decline in exports. Significant shrinkage of the oil-shale energy sector as a response to the increasing environmental charges also accounted for a slowing growth in Estonia, while decrease in transit cargo and anti money-laundering efforts in the banking sector considerably contributed to a slowing growth in Latvia.

The growth in Latvia and Estonia was replaced by a decline in the first quarter of 2020 due to COVID-19 induced economic crisis and the lockdown measures implemented in March. The GDP decreased by a -1% in Latvia and -0.7% in Estonia<sup>1</sup>. Remarkably, the GDP in Lithuania was still growing in the first quarter of 2020 that can be associated with the stable government expenditures and lower decline in exports only 0.2% decline y-o-y, while export decline in Estonia and Latvia was respectively 2.4% and 2.6%. The export performance was quite reversed in the second quarter, as Latvia recorded only 10.9% decrease y-o-y, while Estonia and Lithuania 14.7% and 16.4% respectively.<sup>2</sup>

The second quarter 2020 has been the most difficult for all of the Baltic States as the economies had to act under the lockdown measures around half of this three-month

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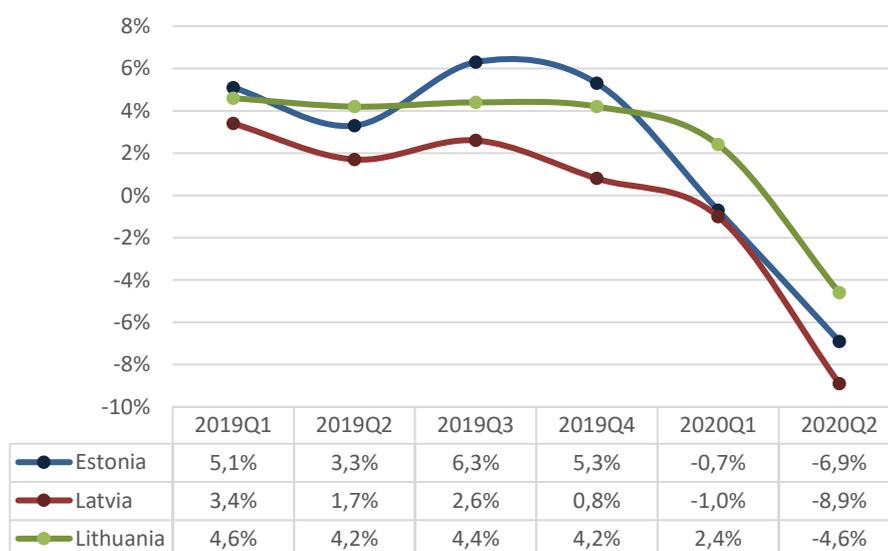
<sup>1</sup> Eurostat (table namq\_10\_gdp)

<sup>2</sup> Export statistics from the Statistics authorities of Estonia, Latvia, and Lithuania.

period. The GDP decline reached to -8.9% in Latvia, -6.9% in Estonia and -4.6% in Lithuania. However, these are still remarkably good figures compared to the other EU states (EU27 -14%) and only Finland, Sweden and Norway have shown comparable numbers<sup>3</sup>. Hence, the relatively limited shrinkage of Baltic economies can be associated, among other things, with close trade relations among the resilient Baltic-Nordic economies. This has been especially important for Estonia and Latvia where the Nordic countries are the most important export markets.

The economic sectors mostly hit across the Baltic States are similar, including transportation, entertainment and recreation as well as accommodation and food services. In all three states, the crisis has not yet reached to the construction sector. This is very different from the previous financial crisis in 2008 where the construction was the most affected. Even though the real estate market has bounced back during the summer months, the turmoil might once again reach the real estate sector as well as the closely related construction sector in case of the second wave. Some differences between countries also occur – for instance, the information and communication sector has gone through a considerable decline in Latvia but has been more resilient in Estonia.

Figure 1\_GDP growth rate (% , non-adjusted)



Source: Eurostat (table namq\_10\_gdp)

Unemployment levels have been decreasing in recent years in Baltic States with Estonia showing the lowest and Latvia the highest unemployment rate (Figure 2). The trend in unemployment in all Baltic countries changed at the beginning of 2020. Since then, the

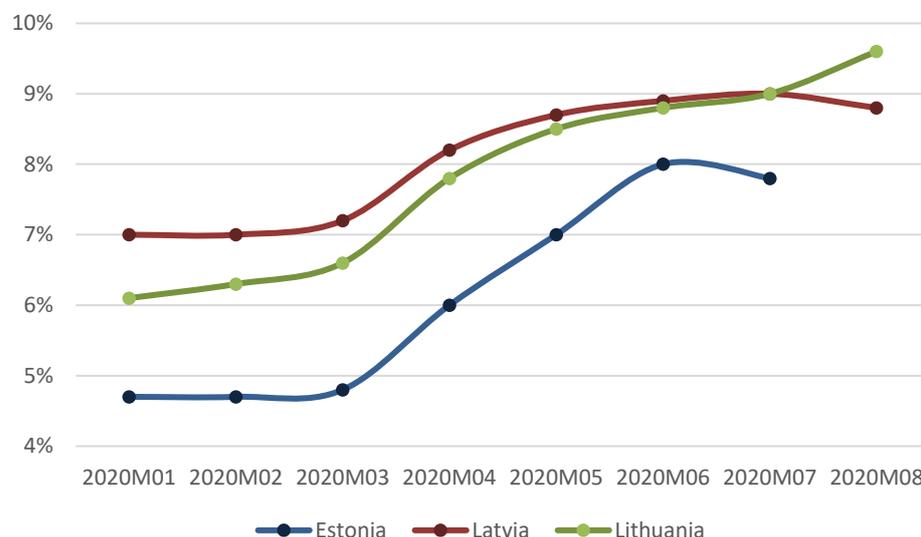
<sup>3</sup> Eurostat, table namq\_10\_gdp

unemployment rate has been increasing every month. Meanwhile in Estonia, the unemployment only shoot off with the lockdown situation.

Job retention schemes have been applied in all three states in order to prevent high increase in unemployment rate. These support measures can be considered effective, as the unemployment levels have remained moderate in comparison with other EU states. Unemployment in Estonia and Latvia has followed a similar pattern where after the sharp increase in March and April the rate has stabilised. In Lithuania, contrarily, the unemployment level has continued to increase during the summer months. This can be, at least partly, explained by the fact that the economic support package included unemployment prevention measures such as a 200-euro job seekers' monthly allowance, which served as a strong incentive for unemployed people to register.

Despite the promising overall trend in the labour market, significant differences exist at the sectoral level. This crisis is different from the previous financial crisis in a sense that the most affected sectors are very labour intensive, which means that if the restrictions will be sustained for a longer period, the employment situation might quickly worsen. Several uncertainties persist, especially related to the weaker expected demand in the tourism sector and possible decline in export demand in manufacturing. In addition, the real effect of the closure of job retention schemes might become visible in the upcoming months.

Figure 2. Rate of unemployment (% , seasonally-adjusted)



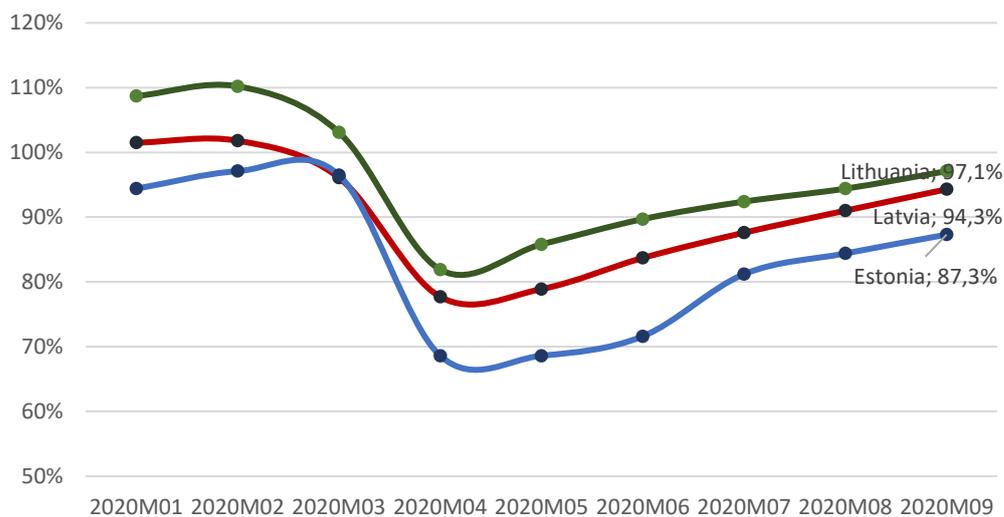
Source: Eurostat (table une\_rt\_m)

The three countries have quite different unemployment patterns in the crisis. Estonia entered the crisis with the lowest level of unemployment, but recorded sharp increases in the unemployment before a slight decrease in July and August. Latvia and Lithuania

had the sharpest increase in employment in April and then more moderate and slowing increase in unemployment. Surprisingly, the unemployment rate again increased in Lithuania, but decreased in Latvia in September. This is even more odd, as Lithuania still has operational furlough shema whose main objective is to prevent unemployment. At the moment, the number of registered vacancies remains low compared to the previous year in Latvia and Estonia, but increased in Lithuania<sup>4</sup>. Combined with the unemployment data, this suggests that Lithuanian labour is more prone choosing voluntary unemployment.

Economic sentiment index also reveals that following the very fast decline in March, business sector confidence is about to recover (Figure 3). Estonian business sector stands out as the most pessimistic whereas Lithuanian firms tend to be the most optimistic in the region. Still, a significant share of the firms is still feeling the effects of the coronavirus. As expected, this is more pronounced in the service sector and less in industry.

Figure 3 Economic sentiment indicator (seasonally adjusted)



Source: Eurostat (table TEIBS0101)

From the fiscal perspective, all three Baltic States have applied vast stimulus measures to stabilise economy. Different organizations apply different methods on how to calculate the impact of the stimulus measures. In accordance with EC Economic forecast, the measures accounted for 2.2%, 2.9% and 4.3% of GDP in Lithuania, Latvia and Estonia respectively<sup>5</sup> in spring. More recent European fiscal monitor<sup>6</sup> estimate that

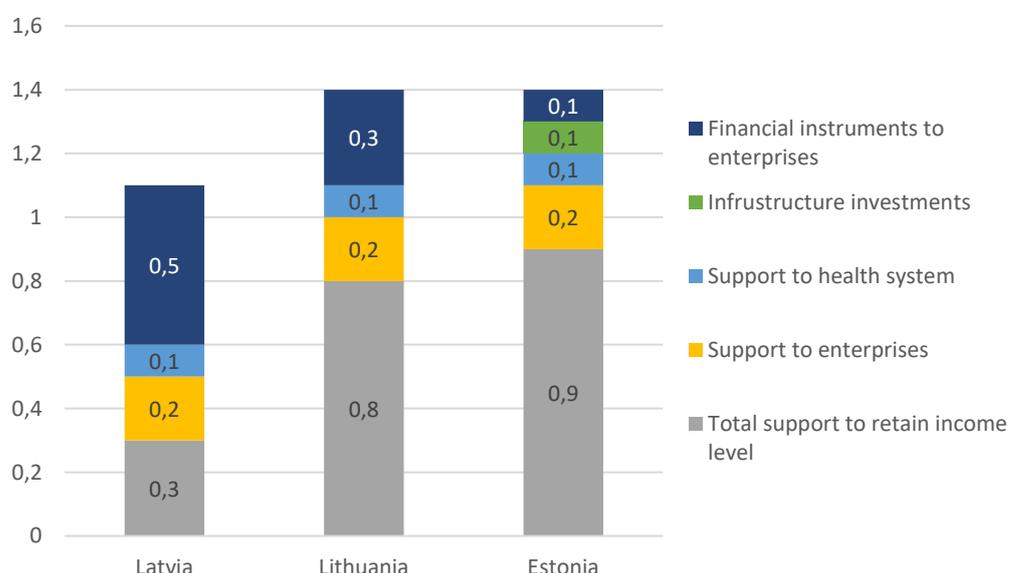
<sup>4</sup> Eurostat (table jvs\_q\_nace2)

<sup>5</sup> European Commission Economic Forecast - Spring 2020

<sup>6</sup> [https://www.euifis.eu/download/european\\_fiscal\\_monitor\\_special\\_updatevol2\\_01.pdf](https://www.euifis.eu/download/european_fiscal_monitor_special_updatevol2_01.pdf)

the size of expected fiscal response is 13% of GDP in Estonia, 15% of GDP in Lithuania, and only 4% of GDP in Latvia. These calculations include “indirect measures” such as guarantees and loans that might not have impact on government deficit. The Bank of Latvia (BoL), in its recent presentation<sup>7</sup> noted that by the end of summer Estonia had actually disbursed more in support measures, especially in its furlough scheme which is by far more generous than in Latvia and Lithuania. In accordance with BoL calculations Estonia has disbursed furlough support in amount of 0.9% of GDP to 200.6 thousand employees, while the respective figures are 0.8% of GDP and 137.7 thousand for Lithuania and 0.2% of GDP and 55.2 thousand for Latvia (See figure 4 below). The generous furlough support in Estonia seems to contradict the sharpest increase in unemployment (See figure 2 above).

Figure 4 Actual support measures expenditure (% of GDP)



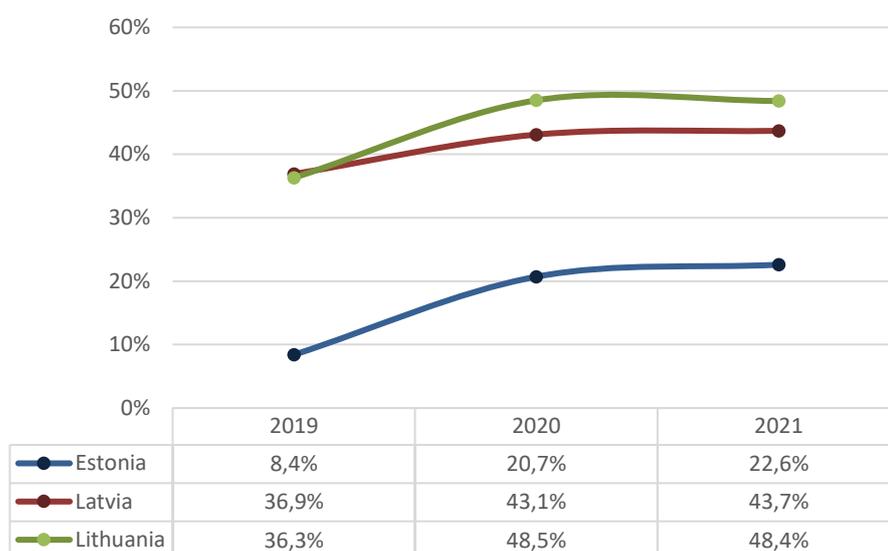
Source: Bank of Latvia

The stimulus measures naturally increase the expected budget deficits: 6.6% in Estonia, 7.6% in Latvia and 8.8% in Lithuania for 2020 and increased general government debt<sup>8</sup>. Despite the debt levels are still considerably low compared to the other EU member states, a question remains open whether certain instruments used such as tax and debts deferrals helped to mitigate the negative effects of the pandemic and facilitated economic recovery, or just postponed emergence of certain negative outcomes of the economic crisis. This brings risk for the long-term growth and potential challenge of state’s budget deficit management.

<sup>7</sup> Available: <https://www.bank.lv/darbibas-jomas/monetaras-politikas-istenosana/prognozes>, accessed 18/10/2020

<sup>8</sup> Ministry of Finance Estonia, Ministry of Finance Latvia, Ministry of Finance Lithuania

Figure 5 General government debt (% of GDP)



Source: European Commission Economic Forecast - Spring 2020 (table 36)

Altogether, the recent figures suggest that the Baltic economies are strongly recovering as the employment is stabilising, the turnover of companies is growing and the sentiment index has rebounded. In accordance with the estimates, in 2020 GDP will contract by 7.0% in Latvia, 7.1% in Lithuania and 7.7% in Estonia<sup>9</sup>. These estimates are based on an assumption of no major second wave, which now increasingly seems unrealistic

## 2. Key factors in overcoming the crisis and the potential long-term economic impact

Baltic States have succeeded in managing the challenges related to the first wave of viral health crisis. As for mid-October Latvia, Estonia and Lithuania have one of the lowest Covid-19 infection rates in the EU<sup>10</sup>. As the second wave is here, this inevitably raises a question whether the states would not be trapped by their previous success and people might not be willing to accept restrictions and safety measures once more. One of the success factors in overcoming the acute crisis in spring has been a sharp and timely government's response.

### *Government response*

<sup>9</sup> European Commission, Summer 2020 Economic forecast:  
file:///C:/Users/normunds.malnacs/Downloads/Summer\_2020\_Tables\_EN.pdf.pdf

<sup>10</sup> <https://www.ecdc.europa.eu/en/covid-19/country-overviews>

All three countries have adopted and implemented strategies for overcoming the crisis and exiting the state emergency. In its Strategy adopted in May 2020,<sup>11</sup> Latvia identified three steps in overcoming the crisis. The first step (survival) was aimed at limiting the spread of the virus and improving financial stability in lockdown. This initial step was followed by reorientation phase, which defined the post-crisis strategy and included immediate measures for activating business continuity and structural adjustment. Finally, the growth phase is aimed at securing higher growth in the future by implementing a set of medium-term support measures for economic transformation based on stimulus for export and productivity, automation and digital transformation, green course, etc.

Similarly, Lithuanian government adopted the Economic and Financial Action Plan<sup>12</sup> in mid-March, which had five focus areas such as providing necessary resources for the efficient operation of health and social security systems, preservation of jobs and income, maintaining business liquidity and boosting the economy. Compared to these, Estonian Strategy for Exiting the Situation Caused by the Spread of COVID19<sup>13</sup> was more tilted towards solving the public health problems and mitigating the societal effects of the emergency situation. .Therefore, the exiting strategy was a subject of public criticism as the economic support measures and the strategy for ensuring continued competitiveness of enterprises was rather broadly defined.

The Government Strategic Analysis Centre (STRATA) concluded that the Lithuanian Action Plan received some criticism because it was too general and used standard measures in extraordinary circumstances, thus several adjustments of the Plan followed. Next to the Action Plan, the government of Lithuania has approved an economic stimulus package 'Future Economy DNA' in June 2020. This is aimed at “promoting conditions for qualitative transformation of Lithuanian economy, sustainable development and development of innovative, high value-added business”. The public discussion on possible measures for taking advantage of the crisis in order to foster economic restructuring is still ongoing in Estonia.

Several temporary emergency measures were accepted in each of the three states in order to limit the spread of the virus and stabilize the financial situation of people and entrepreneurs in the turbulent conditions. Economic stabilization involves a number of actions such as promoting the availability of working capital for entrepreneurs, activating the internal market, reducing business costs, upgrading/reorienting the skills and qualifications of the workforce. Significant fiscal stimulus for business sector involved measures such as issuing new loans and providing guarantees for existing ones, grants, tax exemptions and postponement of tax payments without interest etc. Among the measures with the immediate and greatest impact has been the temporary

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<sup>11</sup> <http://tap.mk.gov.lv/lv/mk/tap/?pid=40487682&mode=mk&date=2020-05-26>

<sup>12</sup> <https://koronastop.lrv.lt/en/news/eur-5-billion-for-public-health-and-the-national-economy>

<sup>13</sup> [https://www.riigikantselei.ee/sites/default/files/riigikantselei/strateegiaburoo/covid19/the\\_strategy\\_for\\_exiting\\_the\\_situation\\_caused\\_by\\_the\\_spread\\_of\\_covid-19.pdf](https://www.riigikantselei.ee/sites/default/files/riigikantselei/strateegiaburoo/covid19/the_strategy_for_exiting_the_situation_caused_by_the_spread_of_covid-19.pdf)

measures to prevent unemployment in a form of subsidies to cover wage costs for employers. Despite the specific requirements being slightly different between the states, this has helped to keep workers employed during the months when the firms' revenues were cut due to the lockdown. From other specific measures, reducing excises on diesel fuel, gas, and electricity were also used with the purpose of supporting the recovery of firms in case of Estonia. Latvian government has approved a special support program for tourism industry, which will provide 19.2 million EUR to 7,156 companies with a total of 69,988 employees.<sup>14</sup> Similarly, in autumn a special programme "vacation for doctors" was launched which would allow a total of 54,000 medical staff to use various recreational, entertainment, cultural, health services in Lithuania (compensation of up to 200 EUR for each) - a total of 10 million EUR is foreseen.

In Latvia, discussions took place to reduce VAT on catering services, but the proposal was declined and replaced by extensions of tax payments periods. Latvia seems to have the largest share of shadow economy among the Baltic states; in addition large share of employees in alternative regimes pay very little social contributions. Public opinion polls show that the population supports government's tougher action on the former and also supports government's efforts to equalize tax regimes for all taxpayers. As a part of budget package for year 2021, the government is trying to implement social tax reform by increasing social tax payments for groups that so far had to pay little in social contributions. It encountered fierce resistance from the groups affected: it remains to be seen if the proposal will be approved by the parliament.

Important strategic decisions with a long-term effect have been related to transportation sector. Latvian government has decided to allocate the massive state aid to the national aircarrier Airbaltic. Since air traffic industry is one of the most hit industries, the Latvian government promptly injected more than 310 million euros into air traffic related companies (Airbaltic, Riga Airport, Traffic control) ensuring continuity of reliable airtraffic connections from the Baltic countries. Similarly, Estonian government decided to provide a working capital loan of 100 million to Tallink, the major ferry company in Baltics. The loan will be used for ensuring longer-term stability and restoration of freight and passenger transport services with neighboring countries, which are important on supporting the recovery of the Estonian tourism sector and the wider economy.

Implementation of support measures has been a challenge in all three states due to the very limited period and coordination issues. The crisis has also highlighted the need for reduction of bureaucracy and the digital transformation, which has been a bottleneck for several support measures.

### *Business response*

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<sup>14</sup> <https://em.gov.lv/lv/jaunumi/28567-turisma-uznemumiem-pieejama-atbalsta-programma-nodarbinatibas-sekmesanai>

COVID-19 related lockdown and safety restrictions imposed requirements entailed rapid business response in order to radically change their business models and operations management. For many, it was a push towards e-commerce, expanding opportunities of existing e-sales platforms and sharing them with other vendors. Firms have had to cope with the social distancing requirements and restricted travelling. The latter has been especially serious issue in case of Estonia and Latvia where the primary sector is very dependent on seasonal migrant workers and some agricultural niches such as strawberry farming have lost a significant share of output due to the travel restrictions.

For some, the new requirements represented new business opportunities: media was full of accounts of companies reacting quickly and flexibly, especially those that reoriented their production to COVID-19 related needs offering to the market the necessary medical equipment, for instance, respirators, test reagents, transport of vital goods etc.

As a response to the lockdown situation, many companies encouraged remote work and virtual communication. Sudden increase in the intensity of remote work highlighted challenges such as securing work-life balance and ensuring effective internal communication. Lack of communication and blurred boundaries between work and leisure could result in longer working hours, which may lead to overworked employees, drop in motivation to continue working.<sup>15</sup> This also relates to the mental well-being of people that has been a subject of increased concern in all three states. Despite high level of concerns about the impact of pandemic, too often employers do not consider health and mental wellbeing of their employees to be their responsibility.

A number of inspiring, collaborative and innovative transformations have taken place in order to mitigate the impact of lockdown. For instance, open-air movie screenings, drive-in theaters and concerts were held in order to replace the closures of entertainment facilities. City of Vilnius was practically turned into the biggest open-air cafe<sup>16</sup> as the municipality decided to give much of the public space to hard-hit bars and restaurants to be able to follow the requirements and to keep alive.

### *Social response*

From the societal and people's perspective, the effects of the virus, lockdown and the resulting economic shrinkage have been severe. During this experience, society was mobilized and multiple private initiatives were inspired often filling the gaps where governmental action was not sufficient.

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<sup>15</sup> <https://www.diena.lt/naujienos/verslas/ekonomika/karantino-itaka-verslui-iki-20-proc-mazesni-atlyginimai-ir-darbuotoju-atleidimas-965785>

<sup>16</sup> <https://www.theguardian.com/world/2020/apr/28/lithuanian-capital-to-be-turned-into-vast-open-air-cafe-vilnius>

The extraordinary nature of pandemics led to earlier unseen mobilization of intellectual capital. Examples of collective interaction include virtual hackathons in Estonia, Latvia and Lithuania. In Estonia, the purpose of the event was tackle the Coronavirus pandemic crisis and emerge from the crisis stronger than ever. Five winners were selected who will get full support and a 5 000 euros from Accelerate Estonia to use for further development during the emergency situation: 1) Zelos – connecting people at risk with volunteers via call center, 2) Ventit Breathing apparatus, 3) Vanemuine – medical volunteer management database, 4) Share Force One – workforce sharing platform that connects B2B sides for temporary workforce Exchange, 5) Corona-tracker by Velmio. In Latvia, the event was aimed at finding agile solutions to pertinent challenges posed by pandemics like shortage of medical equipment, fostering distance learning, and providing relief to businesses suffering from lock-downs. The grand prize was awarded to the company "Baltic3D" for the idea to use 3D printing in production of face shields suitable to people exposed to regular contact with potentially infected people. In the aftermath, the company produced 20 000 prototypes of these face masks within a time span of 17 days and delivered them to hospitals and practicing doctors whose work without these masks would have been severely hampered. Hackaton held in Lithuania was inspired by Estonia & the community of Garage48. Over 1,300 technology enthusiasts and start-ups in Lithuania gathered for a remote programming marathon ("hackaton") "Hack the Crisis". There are a plethora of challenges facing every citizen of a quarantine country, from the stagnant delivery of products to the home, to helping the education system organize distance learning or ideas for occupying children who remain at home. The participants of the programming marathon were offered 54 challenges, which they will later be able to develop and adapt to the market. In addition, in the international hackathon held on Easter weekend, where participated remotely about 15,000 people from 100 countries and were provided a total of over 1,000 ideas for tackling the COVID19 pandemic, a program created by Lithuanians "Act On Crisis" (AOC) won the second place and a total of 10,000 Eur.

Support for medical doctors boomed by raising funds and bringing necessary aid measures, various initiatives to address the challenges of mental health were launched. The workload in the system of social protection has increased considerably across the Baltic States. As expected, the need for retraining was put in the spotlight. Some novel approaches were also applied in this regard. For instance, Lithuanian Employment Service in collaboration with the online training platform Coursera has offered an opportunity for up to 50 000 residents to improve qualification or learn new subjects<sup>17</sup>. Exactly the same was done in Estonia. As a universal remedy, suspension of mortgage payments was offered by commercial banks in all three states, which has reduced the financial stress of those most affected. In Lithuania, one-time support (120-200 euros) for pensioners, and low-income families were allocated.

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<sup>17</sup> <https://www.delfi.lt/darbas/darbo-rinka/uzimtum-tarnyba-siulo-buda-nemokamai-igyti-paklausia-profesija-iki-rugsejo-pabaigos-prieinama-visiems.d?id=85125569>

Another important development brought by the experience of the pandemic was that all institutions of primary, secondary, and higher education had to go to the e-space and to carry out activities remotely. On the one hand, there were voices welcoming this “long-awaited” transformation, on the other hand, the preliminary indicators suggest that the quality of education might be deteriorating and e-learning might increase educational inequality. This could be partly explained by the unpreparedness of institutions to deliver a quality remote education, including availability of necessary equipment and readiness of teachers, etc. It also highlighted the value of personal teacher-to-student contact in education, leading to thoughts about possible over-exaggeration of benefits of virtual education, as having its own limits, especially in schools.

### *Long-term effects*

In terms of long-term effects, there seems to be a common debate in Baltic States if and how the crisis should be used as an incentive for introducing major structural reforms and restructuring of the economy. All states have declared to significantly increase public sector investments, but the question remains how to allocate this. Restructuring approach has been especially highlighted in Lithuania as the economic support package 'Future Economy DNA' directly aims at “promoting conditions for qualitative transformation of Lithuanian economy, sustainable development and development of innovative, high value-added business”<sup>18</sup>. The support package totals €6.3 bn and it is estimated that one Euro invested will bring a return of 1.88 Euros in the long run. While some see it as a possibility of a turning point in the development of Lithuania’s economy, some criticize that this plan was prepared with urgency and risks not to bear the fruits it promised: possibly, funds could be allocated for poorly designed investment- therefore their benefits for the country's economic transformation are questionable. Similar concerns are raised in Latvia and Estonia. Debates are ongoing in all three countries.

COVID-19 has also brought the resilience of the state into the public discourse and political agenda: a necessity to have enough essential resources within the society to ensure a secure livelihood (food, medicine and other medical supplies), for the governing structures – of building a capacity for agile and flexible governance, for expanding cooperation between public and private sectors in times of crisis. For those who are pre-occupied with questions of the future of governance and democracy– the pandemic has also brought questions on finding the right balance between the need to make speedy effective decisions in the face of crisis and the need for deliberations, involving interested parties, the possibilities being opened by new technologies of detecting contacts (and preventing the spread of disease) – by a need to protect one’s privacy, authoritative measures to ensure the health and safety of society – by trusting citizens to behave responsibly.

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<sup>18</sup> <https://finmin.lrv.lt/lt/naujienos/vyriausybeje-patvirtintas-ateities-ekonomikos-dnr-planas>

### **3. The bright side: opportunities arising from the crisis**

As with any crises, there is creative destruction in the markets, both locally and globally. Strong focus on the new and emerging business opportunities both by companies (often as a necessity to survive), and by the states might give remarkable impetus to positive structural changes in the economy.

In the shorter time horizon, the medical crises itself represented new business opportunities as many companies reorientated their production to COVID-19 related needs offering to the market the necessary medical equipment, for instance, respirators, test reagents, transport of vital goods etc. In the medium and long-term perspective, opportunities arising from the crisis can be described in the context of emerging and intensifying trends such as emphasizing the resilience of supply chains, social distancing, digitalisation and green restructuring.

#### *Supply chain resilience*

As a result of the crisis several changes are expected in the regional distribution of goods and services markets, stimulated by the firms seeking to improve their supply chain resilience – sudden need to keep more reserves, source from many suppliers instead of just one, and preferably closer to home. Diversification of suppliers also means, that suppliers with smaller production volumes might start having a chance, and this might open up new opportunities for Baltic companies to integrate to regional value chains.

The shortening of production chains would improve the safety of the production cycle and potentially shorten delivery times, but at the same time it would also reduce the division of labour between countries, limit globalization and push up prices for intermediary and final products. Localization could boost investment in the local market. Even before the COVID-19 crisis, more and more companies were introducing automation-based localization to shorten the global value-added chains. With the development of integrated technology solutions, (including IoT), the so-called additive manufacturing would spread through the manifestations of 3D processes, and the growing need for smart and flexible automation. This should foster the transition from traditional production models to adaptive solutions (small volume; higher prices or the development of customer-specific solutions).

A positive side effect of governments resilience seeking behaviour in terms of securing the essential supplies would be a switch from Chinese products and contractors to domestically produced substitutes in Baltics and other EU member states. This would create opportunities for Baltic companies to expand production in new niches.

#### *Social distancing, triggering e-services, e-governance and new business models*

COVID-19 related lockdown has been a strong incentive for firms to push towards e-commerce. In the long term, this could help firms reaching a larger target market and increasing exports. Changes in public behaviour patterns triggered remote work expansion and wider use of e-services, including e-health and e-education solutions. Since the surge in e-health solutions is expected to be enduring<sup>19</sup> this could create new business opportunities such as e-pharmacy and e-doctor services as well as more sophisticated personalized healthcare applications.

Even post crises, it is probable that market for digital interaction platforms continues to grow. This creates ground for new technologies such as virtual reality, applied for example to offer a tourism experience. People's reluctance to leave home might be sustained for longer, including new VR-based socialisation options, especially among young people. The new forms of work would also promote a comprehensive digital transformation of the public and private sectors, as well as the processing and use of big data to meet the needs of society.

### *Industry digitalisation*

The pandemic is accelerating automation and use of digital solutions in the industry, first as the cost pressures increase due to weakening demand in the market, and also because it turned out that the presence of many people in factory might be a risk factor.

The pandemic provided excellent data for analysis regarding operation of companies in a situation of increased stress. Superficial estimates suggest that the pandemic indeed forced companies to focus more on digitalization of business processes and remote staff management, which might lead to new forms of outsourcing and other cost optimization.

Teleworking might reduce demand (and prices) for offices, transport services, etc. At the same time, the replacement of existing infrastructure with intelligent industrial ecosystem solutions would encourage the creation of new, indirectly related jobs, such as those that will ensure the operation and maintenance of these facilities.

### *Stimulus for restructuring and green deal*

The current crisis and the means to manage it are significantly different from the previous financial crisis of 2008-2009 when measures of austerity were applied, and borrowing in foreign financial markets was a challenge. This time, generous support budgets are promised by European Recovery and Resilience Facility. Thus, the biggest opportunity provided by the crises seems to be "the [unexpected] money rain from Brussels" which would complement the EU Long-term Budget/ Multi-annual Financial Framework 2021-2027.

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<sup>19</sup> McKinsey 2020, Covid-19-implications-for-business

The European Commission wants the EU countries in their recovery strategies to address the main challenges they are facing as identified in the European Semester, in areas such as competitiveness, productivity, education and skills, health, employment, and economic, social and territorial cohesion. However, strongest emphasis while using these funds should be put on addressing climate change and energy issues, in accordance with the Green Deal announced by European Commission.

In society, the fears have grown that in times of economic difficulties, the environmental goals may easily get neglected. Societies might start seeking more balance in environmental, economic and social priorities, as COVID-19 demonstrated, how delaying necessary preventive action can result in far greater costs. Stronger public support for climate action together with support for investments from EU funds might represent a once-in-a-lifetime opportunity for Baltic countries to take big steps in green regulation and investments, thus benefitting respective parts of the economy. However, it has to be said that using the stimulus money might be a challenge, given the short periods of implementation and restricted administrative capacities.

#### **4. Possible coordinated actions of the three Baltic States to build back better**

Societal and economic relatedness, similar export markets and shared geopolitical position mean that the Baltic States are often seen as a unified region. On the one hand, this provides a unique opportunity to benefit from the previous success in managing the first wave of the virus crises in order to foster long-term growth. On the other hand, policy coordination seems to be the most difficult in turbulent times, which means that joint efforts might fade in individualistic policy actions. One possibility to frame this section is using scenarios, which is an effective tool in case of a high level of uncertainties.

Baltic States have managed to pursue common interest so far, the EU co-financed large-scale infrastructure projects like “Rail Baltica” continue to bring our economies closer to each other. Most importantly, in May 2020, three Baltic governments decided to uplift travel restrictions between the three states, thus creating a “Baltic travel bubble”<sup>20</sup>. Due to increased virus infection rate in Estonia, Latvia on September 11 restricted the entry conditions applying to people coming from this neighbouring country, thus bursting a travel bubble.

So far, free people movement between the states in holidays season had a very positive implication to the tourism sector – as travels to many European countries and popular

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<sup>20</sup> <https://www.weforum.org/agenda/2020/05/baltic-states-to-create-travel-bubble-as-pandemic-curbs-eased/>

holiday destinations were still restricted, there was an increase of short-term travels between the Baltic States in summer<sup>21</sup>.

However, more can be done. The Nordic experience can serve as an example of excellent regional cooperation. The prime ministers of the five Nordic countries have announced that their objective is to transform the Nordic region into the world's most integrated region. The Nordic Council of Ministers serves as an essential instrument in achieving this ambitious goal.

The Baltic states, because of common past, similar level of economic development as well as similar foreign and economic policy orientation, have equal or even much better chance to become the world's most integrated region.

As noted by the respectable journal "The Economist", the EU's internal market, originally devised to break down trade barriers in the era of coal and steel, has not adapted fast enough to the era of digital services.

Today the geopolitical and economic realities are such, that distortion of global supply chains open-up opportunities for attracting more industrial investments to Europe. It presents a unique opportunity for the Baltic states. As size matters, by acting alone the Baltic states will achieve little. In order to win place among the most developed nations of the world, our markets need to be more integrated. Ideally, there should be no difference between the three Baltic markets from the perspective of labor and companies. A registration in one country should be sufficient for activity in all three markets, including access to banking services. Likewise, the supervision of market participants in the future should be carried out jointly not separately.

We need to act fast. In order to move towards closer mutual integration, a fresh impetus must be given to the Baltic Council of Ministers. Like within the Nordic Council of Ministers, each government would need to appoint a minister responsible for cooperation with the other Baltic states. More regular meetings among all governmental ministers is also required. The work of ministers should be aided by joint working groups on different subject matters.

In a longer perspective the Recovery and Resilience Facility, aimed at making the EU economies more sustainable, resilient and better prepared for the challenges posed by the green and digital transitions<sup>22</sup> creates a common ground for fostering transformation of the whole Baltic region. Practical examples of joint actions could include creation on common e-residency programme, joint green energy initiatives (e.g. windfarm in Baltic Sea) or perhaps creation of joint VR tourism programs.

Considering various opportunities and threats described in this paper, different scenarios or trajectories for coordinated actions can be drawn:

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<sup>21</sup> <http://alkas.lt/2020/08/01/atslugus-karantinui-baltijos-saliu-gyventojai-puole-keliauti-ir-pramogauti-restoranuose/>

<sup>22</sup> [https://ec.europa.eu/commission/presscorner/detail/en/QANDA\\_20\\_949](https://ec.europa.eu/commission/presscorner/detail/en/QANDA_20_949)

- **“DigiGreen bubble”**. In 2030, the Baltic states become the “centre of excellence” for the rest of EU in areas of digital and green transformation by incorporating newest IT, development of biotechnologies and applying them widely without borders in all major policy areas, by attracting EU funds, exploring opportunities of expanding collaboration between the Baltic and leading Nordic, UK and other countries research and industry. The three Governments have made a joint proposal to EC to become a “testbed”/ sandbox for development of new digital and biotechnologies and testing them in practice. Experimental laws enabling testing were passed in the three states, e-residence model was expanded to all the Baltic states, thus allowing to establish business, live and get educated anywhere, as a result, investments flood and the Baltic states get a quick uplift in living standards, income to Treasuries, positive image for the states, etc. All three Baltic states become the most popular holiday travel destination as it is safe and clean here (health conditions can be tested and verified easily), and due to climate change the north becomes “new south”.
- **“The Bubble burst”**. As EU has managed quickly to provide a new anti-COVID vaccine for its member states, since 2021 the three Baltic states each further built on their own alternative ideas and current strengths: further advancement e-Stonia lead to the expanded digital nation (biggest among the three); development of life sciences in Lithuania lead to development of “Green Lithuania”, Latvia – becoming the gateway for the “Baltic bubble” to Europe, etc. The three countries are finally connected by Rail Baltica, thus, advantages of each country can be partly extended and shared to the other countries (some bits of e-residence programme available for Latvia and Lithuania, every third flight of Air Baltic is operated from Vilnius and Tallinn, respectively, etc.).
- **“Piecemeal upgrade”**. By 2030, each of the three Baltic states have developed bits of digital and green transformations after negotiations for EU Recovery and Resilience Facility. The Brussels provided the “Baltic bubble” as an outstanding example of trilateral cooperation and advised the three governments to bring more of joint proposals (for the reasons of diminishing administrative burden for national as well as EU agencies, inter alia), especially as development of modern technologies allow them to be better connected. As a result, projects of digital and green transformations are implemented by means of trilateral consortiums where research institutions, business, and governmental agencies from three countries are involved. However, due to some inner considerations prevailing (“who gets what?”) and other obstacles to cooperation, the real progress in implementation of big projects remains negligent.
- **„Nothing ever happens”**. The Baltic Assembly in 2030 meets virtually (by means of augmented reality) to discuss potential areas of further Baltic States cooperation.