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## **International Competitiveness of Economies: The Baltic States**

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**Competitiveness is a key element of the European Union's development strategy. In all the Baltic states, a significant weakening of competitiveness is currently observed, primarily due to external factors over which these countries, as both small and open economies, have limited influence. At the same time, however, Lithuania, Latvia, and Estonia continue to invest in the long-term foundations of their development, which are already seen today as the strengths of these states: human capital and the level of education, innovation, and digitalisation.**

**The Imperative of Competitiveness.** Competitiveness remains one of the key priorities of the European Union's development strategy. The President of the European Commission, Ursula von der Leyen, in her State of the Union address delivered at the European Parliament in September 2023, emphasised the importance of competitiveness for strengthening the EU's position on the global economic stage. Earlier, in March of this year, on the occasion of the 30th anniversary of the founding of the single market, the European Commission prepared a communique presenting the current competitive position of the EU on the international stage and its prospects for the future<sup>1</sup>. The document noted that despite many achievements, the EU faces challenges in this area. These primarily include a slower rate of productivity growth compared to other economies, which, combined with demographic challenges, pose a threat to the EU's future ability to compete in global markets. Consequently, understanding and appropriately addressing these challenges becomes crucial at not only the EU level but also at the level of individual member states.

A significant role in assessing competitiveness is played by analyses conducted by international organizations. One such organization is the International Institute for Management Development (IMD), which publishes the comprehensive World Competitiveness Yearbook ranking. This ranking includes 64 economies (including nearly all EU countries except Malta) and is based on 336 competitiveness criteria selected based on a broad review of economic reports, international, national, and regional data sources as well as opinions from business representatives, the academic community, and government agencies. Moreover, these data include survey research of executive staff of companies operating in the studied countries regarding key indicators of investment attractiveness.

**Competitiveness of the Estonian Economy.** Among the Baltic states, Estonia holds the highest position in the IMD competitiveness ranking. However, according to its latest edition, it recently experienced a decline – from 22nd place in 2022 to 26th in 2023. Among the reasons for the deterioration in position, a decrease in the real growth of gross fixed capital formation can be pointed out, suggesting a slowdown in investments. Additionally, high inflation and weakened growth of both real GDP and real GDP per capita have contributed to this, indicating a slowdown in economic dynamics („Komentarze IES”, nr 878). Furthermore, a deterioration in the current account balance was noted, which reflects both a decline in external demand and signals a potential imbalance between savings and investments. Among the challenges for improving competitiveness, the need to minimize the gap between the skills sought by employers and the competencies of potential employees was highlighted, which could contribute to better utilization of labour resources. Attention was also drawn to the need to ensure energy security and to change the structure of electricity generation through the development of renewable energy sources (RES) as well as to strengthen defence capabilities.

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<sup>1</sup> [https://commission.europa.eu/system/files/2023-03/Communication\\_Long-term-competitiveness.pdf](https://commission.europa.eu/system/files/2023-03/Communication_Long-term-competitiveness.pdf)

At the same time, Estonia has made progress in several key areas of competitiveness. A positive trend is visible in terms of population growth, mainly due to immigration together with an increase in the workforce and employment, which can strengthen the human capital potential of the economy. Additionally, an improvement in the budget balance and an increase in the share of renewable energy sources in electricity consumption were noted. In survey research of executive staff, the dynamism of the Estonian economy (appreciated by 55.2% of respondents), a business-friendly environment (52.2%), a competitive tax system (50.7%), an efficient legal system (47.8%), and a high level of education (46.3%) were pointed out as assets for investment in Estonia.

**Competitiveness of the Lithuanian Economy.** According to the latest IMD competitiveness ranking, Lithuania fell from 29th place in 2022 to 32nd in 2023. Several factors contributed to this decline: an unfavourable current account balance, high inflation limiting household purchasing power, and a decrease in real GDP growth per capita, indicating a slowdown in economic activity ([„Komentarze IEŚ”, nr 902](#)). The analysis also pointed to challenges related to economic uncertainty caused by the Russian-Ukrainian war and the need to increase energy independence, accelerate the transformation of the economy towards high-tech sectors, and rising labour costs. In this context, a strategic opportunity for Lithuania could be to capitalize on the trend of shortening supply chains in Europe.

On the other hand, positive changes affecting an improvement in the competitiveness of the Lithuanian economy relate to the number of patents obtained, which may indicate its increasing innovativeness. Additionally, a favourable reduction in the budget deficit was observed, along with an increase in education spending, indicating a focus on the competitiveness of human capital. In this context, it is also worth emphasizing that there has been an increase in the population, partly due to refugee migration, which is particularly important in the face of demographic challenges facing Central European countries ([„Komentarze IEŚ”, nr 243](#)). Meanwhile, in the opinion of executive staff, the key indicators of the attractiveness of the Lithuanian economy for investment include a qualified workforce (noted by 76.2% of respondents) and a high level of education (61.4%), which also highlights the importance of human capital for Lithuania's economic development. Other important factors included reliable infrastructure (54.5%), economic dynamism (52.5%), and a business-friendly environment (39.6%).

**Competitiveness of the Latvian Economy.** Latvia's competitive position in the IMD ranking<sup>2</sup> significantly worsened – from 35th place in 2022 to 51st in 2023. This decline reflects a variety of problems faced by the Latvian economy. These include a significant increase in the prices of consumer goods and services, a deterioration in the current account balance, and a slowdown in the growth of gross fixed capital formation. Additionally, challenges for the Latvian economy remain in terms of economic security in light of the Russian-Ukrainian war and its consequences, including increased aversion to investment in Latvia. Moreover, inflation continues to be a challenge, putting pressure on wages and labour costs and posing a risk of recession ([„Komentarze IEŚ”, nr 887](#)).

On the positive side, Latvia recorded a reduction in the budget deficit, an increase in the export of commercial services, a rise in patent applications, and an increased influx of students. Similar to Lithuania, in the survey on investment attractiveness, a qualified workforce (70.8% of respondents) and a high level of education (50%) were identified as key assets of the Latvian economy. Additionally, reliable infrastructure was highlighted, which facilitates efficient business operations (41.7%), effective employee relations, suggesting a favourable environment for harmonious interactions between employer and employee (39.6%) as well as open and positive attitudes reflecting a potentially friendly and progressive social environment (37.5%).

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<sup>2</sup> <https://www.imd.org/centers/wcc/world-competitiveness-center/rankings/world-competitiveness-ranking/2023/>

## Conclusions

In the years 2022-2023, external conditions such as economic uncertainty resulting from Russia's war of aggression against Ukraine and the effects of the energy crisis, leading to rising inflation curbing consumption and investment, had a significant impact on the economies of the Baltic states. As a result, all Baltic countries recorded a decline in the latest IMD competitiveness ranking.

At the same time, however, the Baltic states show certain positive trends that may form the foundation for the long-term strengthening of their competitive position. A key role in this regard is played by the development of human capital, as evidenced both in data (increased spending on education, influx of students) and in surveys among executive staff (appreciation of a qualified workforce and high level of education). It is also worth emphasising the relatively high level of innovation (reflected in the number of patents), advancing digitalization, and adaptation of modern technologies in these countries ([„Komentarze IEŚ”, nr 209](#), [„Komentarze IEŚ”, nr 653](#)).

The analysis of the competitiveness of the Baltic states suggests that despite external difficulties, a key role in building a long-term competitive advantage is played by investing in human capital and promoting innovation and digitalization. These observations can be useful for the development strategy of Poland.