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LITHUANIAN ECONOMIC  
AND RE-MARKET REPORT

**2020 H1**

WITH PARTNERS: ŠIAULIŲ BANKAS AND LAW FIRM COBALT

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## **OVERVIEW OF ECONOMICS**

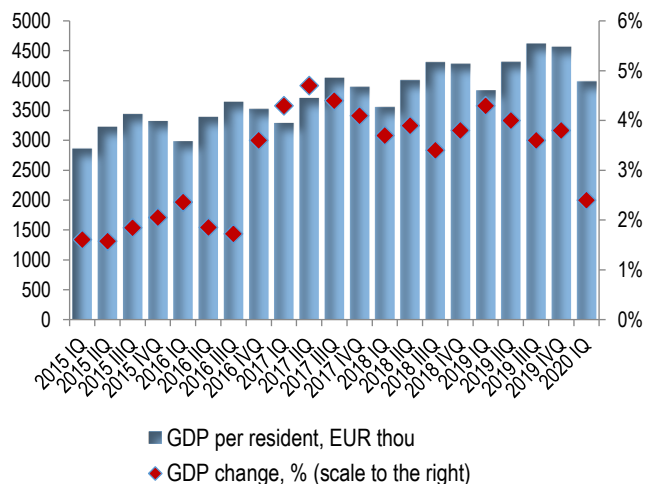
The Lithuanian economy ended 2019 with a boom: the country's GDP grew by 3.8 per cent, and at that pace we were once again one of the EU leaders. But that is history. The unexpectedly strong wave of quarantine caused by the COVID-19 pandemic, which went round the world this year, has brought a great deal of uncertainty. Small businesses tackled survival issues: lacked of working capital, cut jobs. In fact, unlike in 2008, this time the country's business has a bigger cushion. According to the Bank of Lithuania, government measures and accumulated corporate reserves helped businesses to withstand the liquidity shock: the share of companies with financial problems in April increased relatively little and remained unchanged in early May. In response to the shock of the pandemic and in order to

mitigate its effects on the Lithuanian economy, the country's government rushed to implement a plan of economic stimulus measures, which focuses on preserving the liquidity of companies and jobs. Up to 5 billion EUR, or 10 per cent of country's GDP, has been allocated for the implementation of all measures.

The withdrawal of isolation has significantly eased tensions and the economy is gradually returning to its normal pace, with the trade and industry sectors stabilizing after 12-15 per cent recession in April, the number of employees is no longer declining, population mobility and domestic demand are recovering, and energy consumption is no longer declining. The country's GDP growth slowed, compared with the similar period one year ago, to 2.4 per cent in the first quarter of this year, but remained solid. Compared to the last quarter of 2019, the economy shrank by 0.2 per cent. Manifestations of the slowdown were already visible at the end of 2019, when the prices of Lithuanian industrial exports fell, and the transport sector grew more slowly. Transport services account for the largest share of exports and imports of services: 60 and 50 per cent, respectively. During the first quarter of this year, Klaipėda Seaport companies handled 8

per cent less freight than a year ago, rail traffic shrank by 12 per cent, airports handled by 16 per cent fewer passengers. Carrier revenues were further reduced by the declining number of new lorry registrations due to the forthcoming entry into force of the Mobility Package. While it is clear that the onset of quarantine which started on 16 of March has not managed to cause very significant damage, but the true extent will be seen when the second quarter data is released.

### Lithuanian GDP

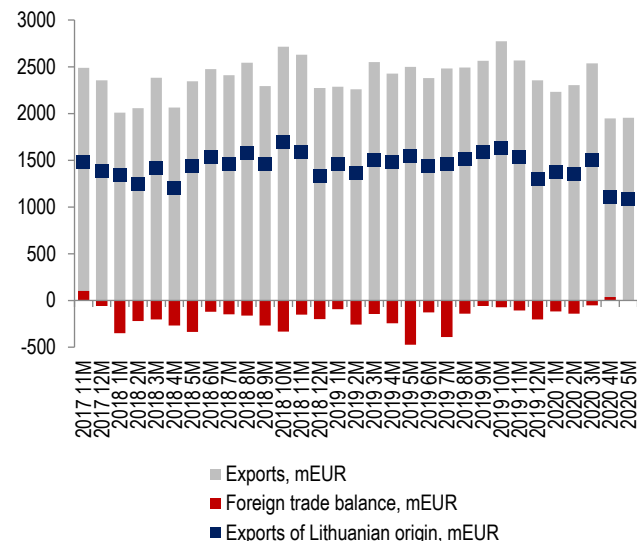


Source: Lithuanian Department of Statistics, calculations of Šiaulių Bankas

Lithuania's economic growth remains sufficiently balanced as the country's economy is driven not only by strong domestic sectors, but also by sufficiently resilient exports. The annual growth of exports, excluding oil products, remained virtually unchanged in the first quarter of this year (-0.4 per cent). Exports of Lithuanian origin decreased by 2.3 per cent. A significant decline in exports was recorded already in April-May, after the introduction of quarantine (-21 per cent). Exports of Lithuanian origin suffered 27 per cent fall. Due to uneven recovery of the world's countries after isolation, Lithuania's export activity is likely to remain lower

and more constrained for some time than domestic consumption, which has stabilized in recent months. Export losses could be somewhat reduced by the good performance of the country's business in recent years in foreign markets. As competitors in Western countries slipped, Lithuanian producers took over a number of orders due to higher productivity progress and lower production costs in recent years. As the growth rate of Westerners' income slows down, some of them may choose cheaper Lithuanian goods. However, the further development of exports will largely depend on the economic development of Western and Northern European countries. Germany, Poland, Sweden and Latvia are the most important foreign trade partners of Lithuania, to which a third of Lithuanian production goes. According to the forecast of the Bank of Lithuania, Lithuanian exports will shrink by 14 per cent this year.

### Foreign trade

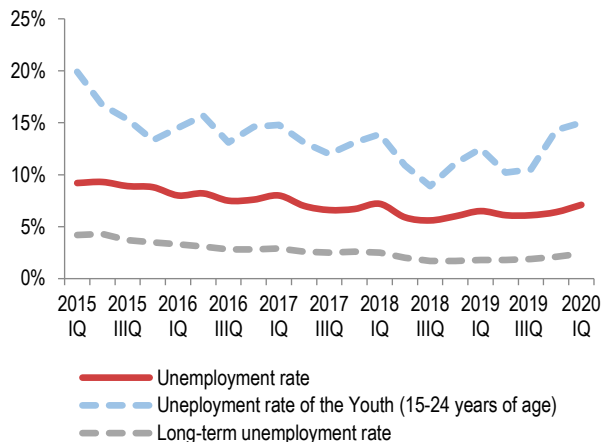


Source: Lithuanian Department of Statistics

Trends in world goods imports seem even worse. The decline continues since the peak reached in 2018. At the end

of 2019, growing concerns about a possible recession in major economies were not without reason. This year's pandemic has acted as a sharp catalyst, plunging world trade into unprecedented lows. Lithuanian imports shrank by 15 per cent in the first five months of this year (2.9 per cent during the first quarter).

### Unemployment rate



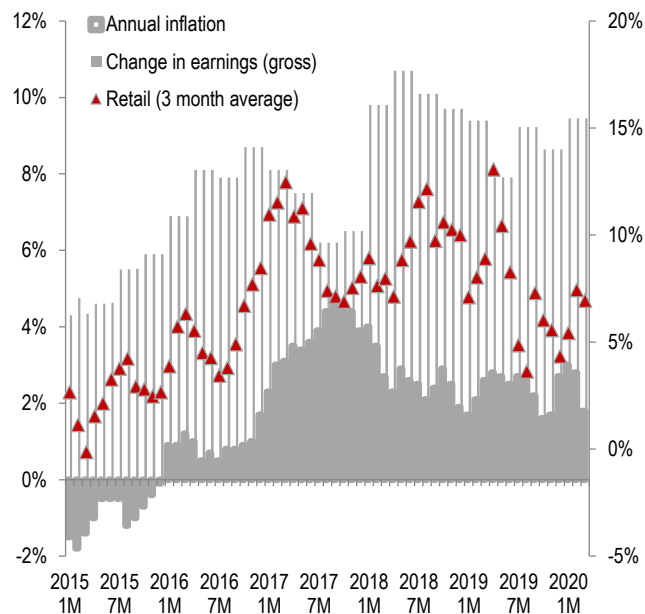
Source: Lithuanian Department of Statistics

The country's consumer expectations and revenues did not show any tensions when assessing data for the first quarter of 2020. The income of the population continued to grow strongly due to rising wages. In fact, the unemployment rate rose to 2-year highs in the first quarter (to 7.1 per cent). Due to the impact of the pandemic, the unemployment rate is expected to rise to 10-12 per cent this year. (EC forecast is 9.7 per cent), and the average wage will decrease by 2.6 per cent. Quarantine and increased uncertainty will have a major impact on workers in the service sector. To preserve jobs, the Government pays subsidies to companies that have retained their employees during and after quarantine. The pace of price growth in the country will be slowed by lower pressure on wages and cheapening energy sources. This

year, inflation of 0.6-0.8 per cent and next year 1.5 per cent is forecasted.

After the sluggish end of 2019, the country's retail trade intensified again in the first quarter of this year (+ 6.9 per cent). A good start of the year can be attributed to the continued rapid rise in wages. In the first quarter of this year, wages grew by as much as 9.4 per cent, as they have increased on average since the beginning of 2018. The share of wages in the structure of GDP is likely to increase further and that of capital to decline. In fact, in April, retail sales shrank by as much as 18 per cent. Uncertainty is still too high, so domestic demand this year will be negatively affected by melted household income, limited borrowing opportunities and increased level of savings.

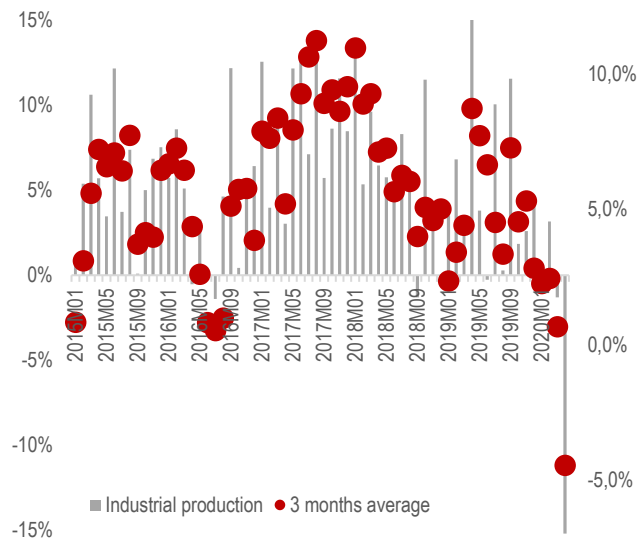
### Changes in consumer prices (according to the consumer price index)



Source: Lithuanian Department of Statistics, calculations of Šiaulių Bankas

Growth in non-petroleum industrial production continues to slow markedly. In the first quarter of this year, growth was only 1.8 per cent, while in previous periods it was 5-7 per cent. Still, it is a good enough result, and one of the best among all EU countries.

### Industrial production (annual change)

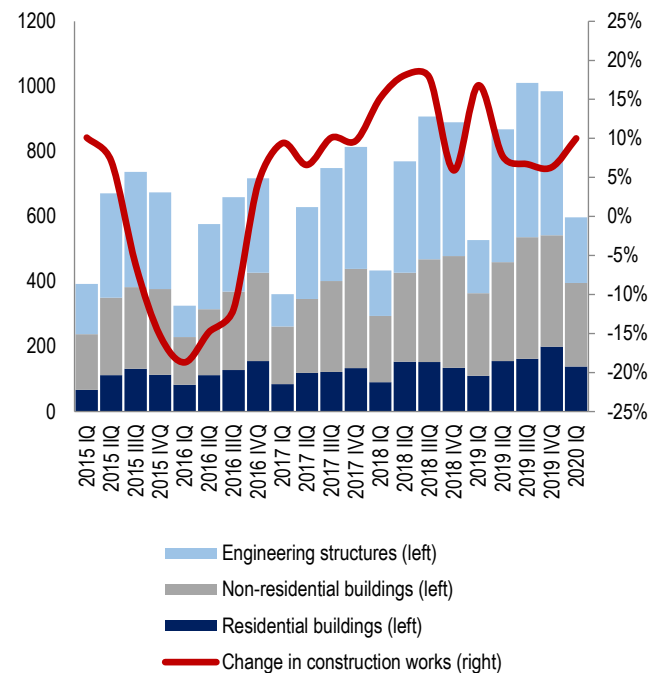


Source: Lithuanian Department of Statistics, calculations of Šiaulių Bankas

The production of food and tobacco products stood out with strong growth (+8 per cent), the furniture sector looked quite good, which, despite 0.8 per cent decline in the first two months of this year, grew by about 5 per cent. The largest losses were suffered by oil refining production, which fell by more than 20 per cent. Taking into account that industry and retail trade are the two largest sectors of the Lithuanian economy, which account for about 40 per cent of the GDP structure, the results of this year's economic development will largely depend on further dynamics of these sectors.

The construction sector did not respond to the pandemic and achieved the best result in the first quarter since 2008. Companies continued to actively engage in capital investments. Investments in the construction of infrastructure and engineering facilities grew by 23 per cent, construction of residential buildings by 26 per cent. According to the Bank of Lithuania, the liquidity situation of real estate (RE) developers is certainly not bad, their loan portfolio in banks is about 30 per cent. Real estate prices remained stable. The commercial real estate market, which has experienced a period of high growth in recent years and which is characterized by a stronger correlation with the dynamics of the country's business activity, may experience a greater shock.

### Construction activity in Lithuania (mEUR/percent)

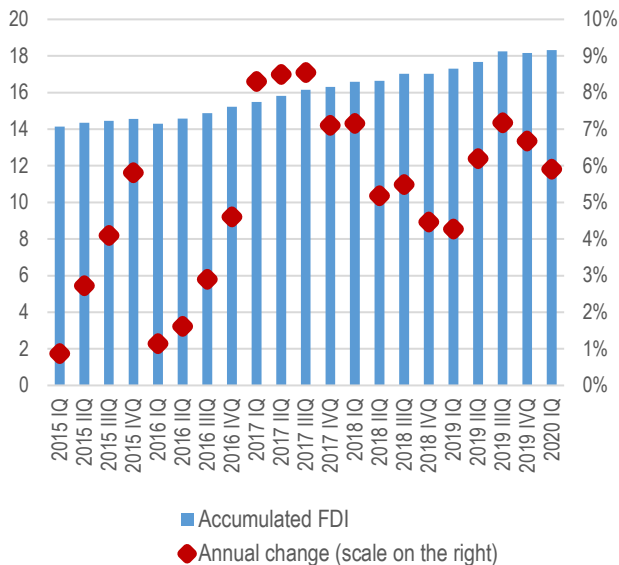


Source: Lithuanian Department of Statistics

Foreign direct investment (FDI), an important component of the country's export growth, continues to maintain the pace. FDI growth in the first quarter was 5.9 per cent and reached record highs. The growing share of investments in high value-added products strengthens the country's competitive opportunities and will be a very important component of Lithuania's future.

development (avoiding the second wave of the virus and estimating a possible second wave of the virus), Lithuania's GDP may shrink by 8.1–10.4 per cent this year (EU forecast 9.1-11.5 per cent), and the recovery is expected in 2021, the country's GDP should grow by 3.4-6.4 per cent.

**Foreign direct investment in Lithuania, billion EUR**



Source: Bank of Lithuania, calculations of Šiaulių Bankas

The time of great challenges has come for the country's economy, which has been growing at an impressive pace over the past few years. Force majeure has forced many to tighten their belts and even rethink their operational strategy. With the disruption of the supply chain in world trade, a significant decline in the country's exports is expected. The first quarter of this year has not yet shown a major heat, but the real picture will become clear with the release of data for the second quarter. According to forecasts published by the OECD, which envisage two scenarios of economic





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## **REAL ESTATE MARKET OVERVIEW**

The first half of year 2020 could be easily divided into two parts by drawing a red line at the 16<sup>th</sup> of March, i.e., the day when the quarantine was declared in Lithuania. January and February signalled potentially another record year for the RE market, however, the business activities paralysed by the pandemic and the quarantine for a period of three months, limited social contacts, and disappearance of the foreign tourist traffic have erased any achievements of the beginning of the year in a flash.

Hotels have been hit hardest by the crisis. There is no point in talking about any income at the moment: all they have left is expenditure lines on their balance sheets. Sports clubs, concert halls, catering and entertainment establishments continue the ranking along the line in terms of losses. All these activities require premises and their employees are a

part of all consumers in the country participating in other segments of the RE market as well.

The primary housing market is typically dominated by transactions involving residential buildings still under construction. However, in the face of uncertainty about the future, a significant number of buyers have decided to postpone signing of preliminary contracts. This led to almost non-existent sales of new construction apartments in major cities in Lithuania in April – May. Buyers also faced financing challenges due to the declared downtime while changes in the rent market discouraged investors as well. Probably the only exception in the housing market is “the second home” in the coastal region. The opportunity to relax by the sea became an incentive for buying “the second home” as the quarantine confined people to the walls of their own homes and restricted any foreign travel.

Business centres also have faced challenges during the quarantine period despite of their enviable development rates demonstrated over the several past years. Potential tenants were willing to reconsider their plans for renting premises due to increased work from home during the quarantine and prevailing uncertainty about the future. Mass termination of long-term lease contracts was prevented because both the



lessors and the State contributed to the support to tenants.

E-commerce has been a major challenge to operators of commercial premises for several years already and the quarantine triggered a cardinal break in customer behaviour. On the other hand, this did not have a major impact on the market of storage premises, because in this case the seller of the goods is a less important factor than the buyer.

## APARTMENT MARKET IN VILNIUS

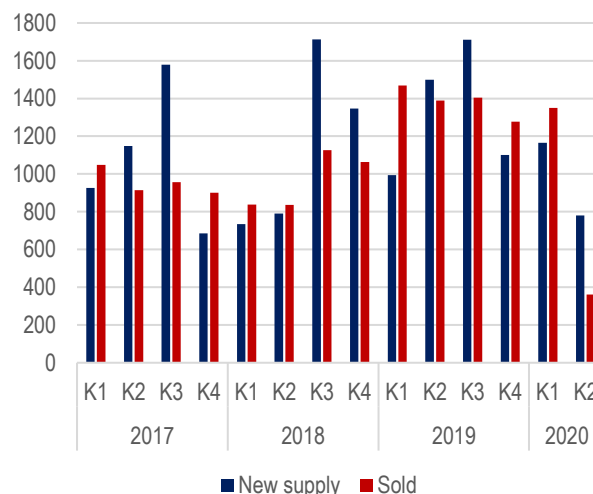
The first half of year 2020 was full of contrasts in the capital's primary apartment market. The year started with record numbers of new supply and sales, however, in spring the pandemic sent all RE developers to "vacation". June was not very successful in terms of housing sales in comparison to the beginning of summer in 2019, but it was much more favourable than the previous couple of months.

The first quarter of 2020 (prior to declaration of the quarantine) maintained the "record braking" trend of the previous years. 1166 new apartments were offered to the RE market, which is more than during any previous first quarter of the year since 2012<sup>1</sup>. The onset of the pandemic had a negative impact on the sales rates in the primary housing market. Only 190 new apartments were sold, which is three times less than a month earlier or a year ago (in March 2019). On the other hand, record results of January (526 units) and February (634 units) contributed to exceptionally good overall sales in the first quarter.

The second quarter demonstrated that housing development is a long-term and inert process, thus offers of new products may not always be postponed. 781 newly offered apartments seem like a small number in comparison to the supply of new apartments in the beginning of 2020 or the second quarter of

2019, however, similar rates were also recorded in 2016 – 2018. Buyers' intentions to purchase new construction housing were less sustainable than developers' plans for development of new projects. Developers managed to sell less than 100 new construction apartments (including agreements terminated later) in April and May. This shows that less than a half of the apartments newly offered to the market were sold during the second quarter of this year even with the figures of the much more active month of June (262 units) added to the total number.

**Dynamics of the new supply and sales of apartments in Vilnius (units)**



Source: INREAL

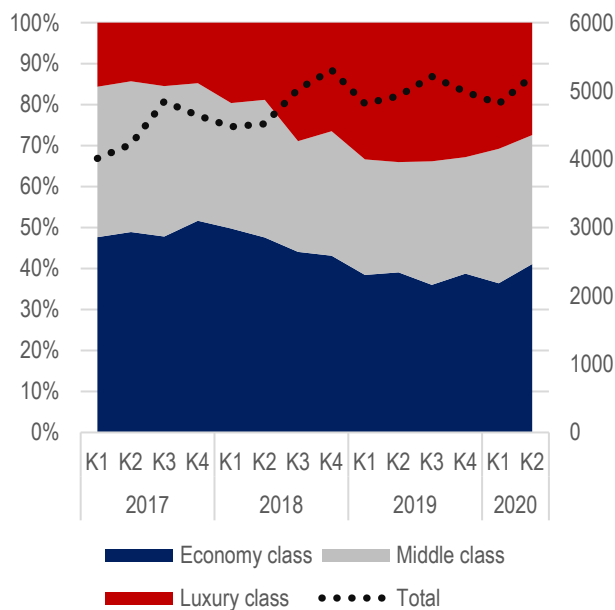
Despite of a large new supply, the stock of unsold housing in the capital during the first quarter this year decreased to approximately 4800 apartments. This was due to the months of January and February with record sales. Truth be told, this decrease was short-term, because the stock at the end the first half of the year was over 5200 new apartments again.

<sup>1</sup> Year 2012 is considered as the reference point marking the time when INREAL started compilation of the primary housing market database.

Considering the shrunken sales and still uncertain market recovery prospects, the increased stock of unsold housing could have a negative impact on RE developers' plans for development in the near future. It is likely that the new supply during the third quarter this year would be much smaller.

Changes in the stock structure are also noticeable in terms of classes. A surplus of luxury housing started forming in 2019. On the other hand, this segment survives turmoil on the market much easier than the economy class market and the spring of 2020 has proven just that. Luxury housing made approximately one third of all unsold apartments in the end of 2019, however, at the end of this half-year such apartments made merely 27 percent. Meanwhile the share of the economy-class housing increased from 39 percent to 41 percent and from 28 percent to 32 percent in case of the middle-class housing.

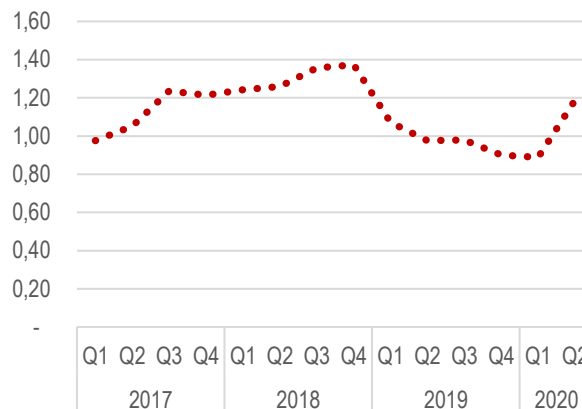
**New construction apartments, unsold in Vilnius (% / units)**



Source: INREAL

Declining market activity also affected the housing liquidity ratio. The liquidity ratio predicts the period during which the existing stock of new construction housing would be sold if the sales rates matched the results of the last 12 months. Back in March 2020 the housing liquidity ratio was only 0.89 (which meant that the unsold apartments could be sold in less than 11 months). This ratio increased to 1.19 (13-14 months) at the end of the half-year.

**Liquidity rate of new apartments in Vilnius**



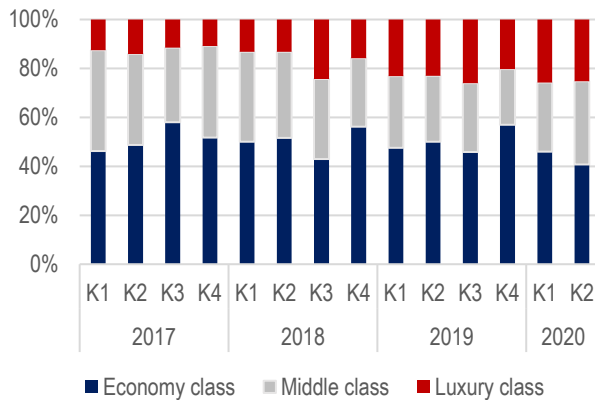
Source: INREAL

The current value of the ratio is not so bad (it was worse in 2012 – 2013, 2015, 2018), however, the sudden change of it and the existing scope of the unsold housing stock indicates that the RE market suffered a negative impact and the future situation will depend on the pace of economic recovery.

The sales volumes declined in all segments, however, the assessment of the proportions of different classes shows that there were less cheaper housing units bought. We may assume that this was affected by both the restrictions applicable during the quarantine resulting in reduced income for some buyers and the oversupply in the housing rent market. The share of the demand for luxury housing essentially has not changed while the demand for middle-

class housing has increased from a quarter to one-third of all purchased new construction apartments.

#### Apartment sales in Vilnius by class (percent)



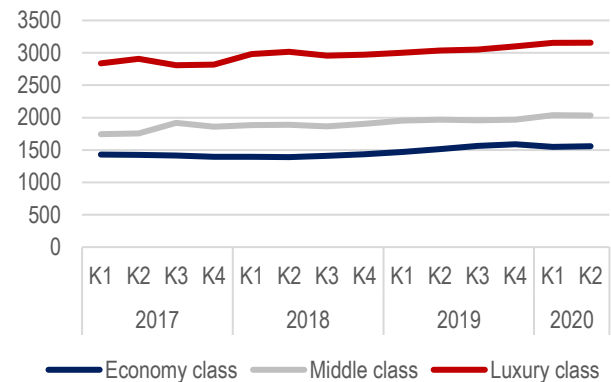
Source: INREAL

A minor drop in prices in the economy-class housing segment and minor increases in middle-class and luxury-class segments were recorded during the first quarter of 2020. Meanwhile essentially the prices have not changed during the second quarter. Stable prices reflect the mood of the market participants both prior to the quarantine and during it. Even though some buyers expected a drop in prices due to the pandemic, both the individual financial situation of the developers and the willingness of credit institutions to defer payment of instalments as well as support by the State enabled to prevent a price war. The buyers were offered indirect concessions: price adjustment (in the event of declining prices on the market), insurance of mortgage payments, more flexible conditions of preliminary purchase – sale agreements, reimbursement of utility bills or household appliances as gifts.

An economy-class apartment cost approximately 1558 EUR/ sq. m, the price of a middle-class apartment amounted to 2033 EUR/ sq. m, and the price of a luxury-class apartment

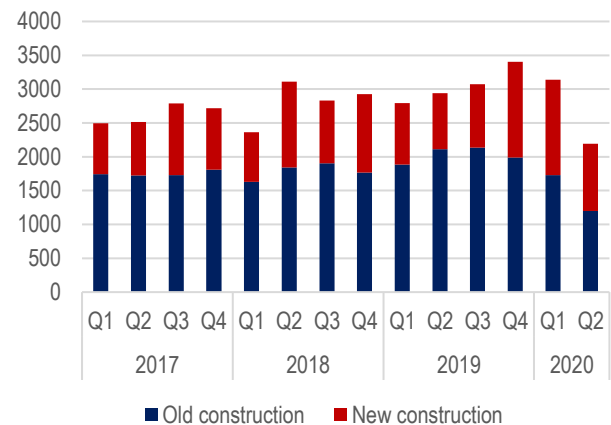
amounted to 3156 EUR/ sq. m in Vilnius at the end of the first half of 2020.

#### Average prices of apartments under classes in Vilnius (EUR/ sq. m)



Source: INREAL

#### SE Center of Registers registered apartment transactions in Vilnius (units)



Source: SE Centre of Registers, 07-2020

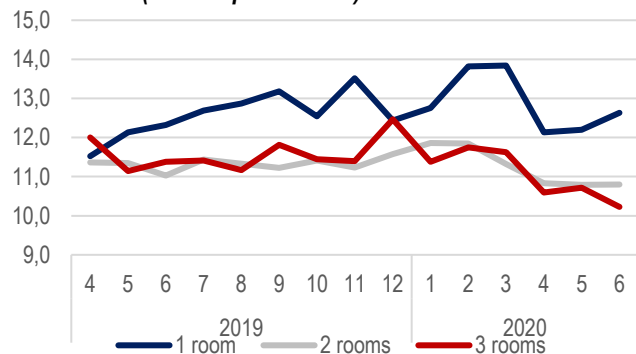
Even though the primary housing market essentially came to a standstill during the second quarter this year, the records of SE “Centre of Registers” showing almost 1000 transactions for new construction housing indicate that the market turmoil

was not strong enough to make buyers to withdraw from previously concluded preliminary agreements en masse.

The numbers of transactions for old construction apartments were particularly bad during the second quarter this year. Similar results were recorded only at the turn of 2008 – 2009. The situation now and the one almost a decade ago is fundamentally different both in terms of the nature and the duration of the problems as well as the response of the market participants, which gives hope that the worst is over. On the other hand, the pandemic is far from over and the market could still face a number of challenges.

The declaration of the quarantine also sent shockwaves across the housing rent market. The impact on the rental housing prices varied in different neighbourhoods of the Capital. The central part of the city was hit hardest. The supply of housing for long-term rent has increased significantly in Naujamiestis and in the Old Town following disappearance of demand for housing for short-term rent, therefore the rent of 2-3-room apartments decreased by approximately 10 percent in comparison to 2019. The housing rental prices in dormitory suburbs changed insignificantly, i.e., by approximately 5 percent.

**Average apartment rental prices in Vilnius Naujamiestis and Senamiestis (EUR / sq. M / month)**



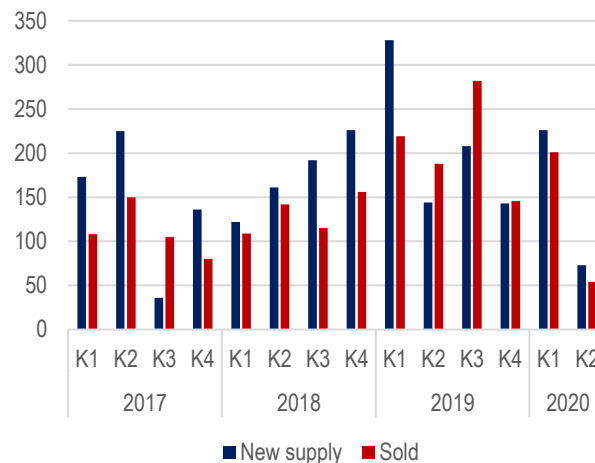
Source: INREAL

## APARTMENT MARKET IN KAUNAS

Like in Vilnius, the beginning of 2020 seemed promising to for Kaunas as well. Sales in January were better than in December last year and equalled to the result recorded in January in 2019. The sales in February surpassed the historical data over a period of several years. Even the month of March was relatively good with a total of 58 sold apartments, however, April and May turned out to be the worst months among all major cities in Lithuania with 5 and 0 sold apartments (upon assessment of returns) respectively. The market hit the rock bottom and started rising up in June when 49 apartments were sold, which sparked hope that the second half of the year would be better: the annual results could hardly reach the level of year 2019, but they could still surpass year 2018.

RE developers offered 226 new apartments during the first quarter and only 73 apartments during the second quarter of the year.

**Dynamics of the new supply and sales of apartments in Kaunas (units)**

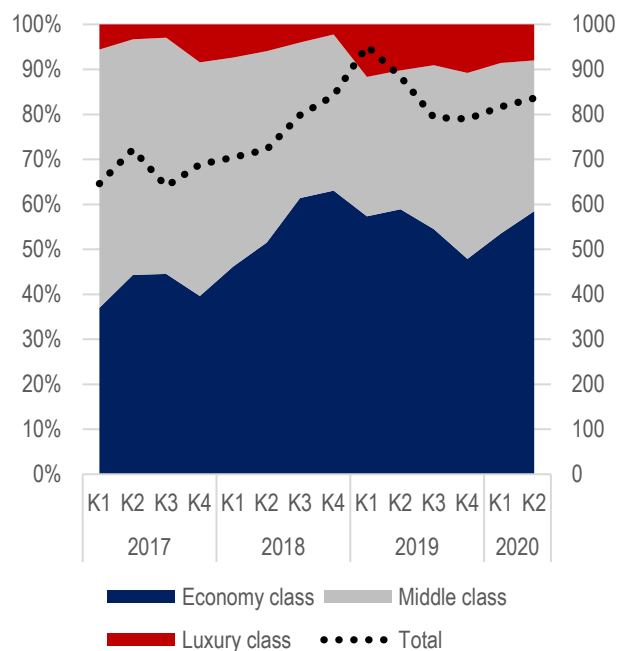


Source: INREAL



The drop in sales due to the pandemic caused the stock of unsold new housing to slightly increase in Kaunas from 790 (at the end of 2019) to 836 (in June 2020). However, this increase is not cardinal and the choice of apartments in Kaunas remains smaller than 12 months ago. Given the population of Kaunas, the City is not expected to encounter major difficulties in selling this quantity. The share of unsold economy-class housing increased just like in case of Vilnius.

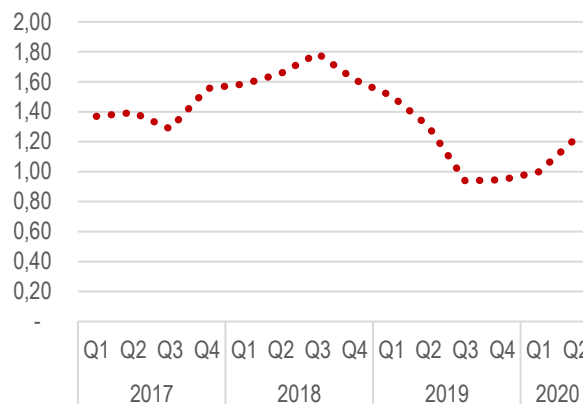
#### New construction apartments, unsold in Kaunas (% / units)



Source: INREAL

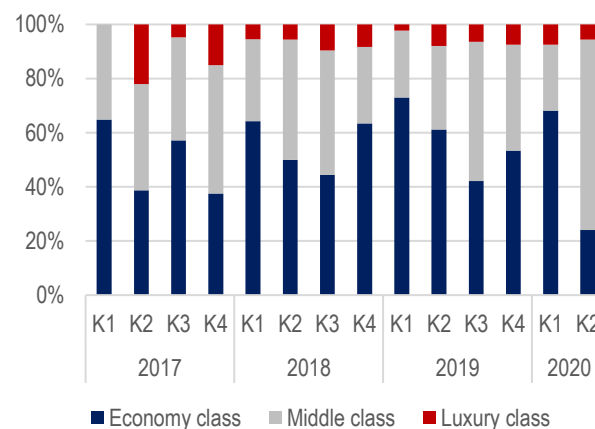
Decreased sales and increased housing stock also affected the housing liquidity ratio, which increased from 0.95 at the end of 2019 to 1.22. On the other hand, it is still a good ratio, which means that all available supply could be sold within approximately 14-15 months. With the exclusion of the 2<sup>nd</sup> quarter of 2019, when the liquidity ratio in Kaunas was record good, this value is the best since 2012.

#### Liquidity rate of new apartments in Kaunas



Source: INREAL

#### Apartment sales in Kaunas by class (percent)



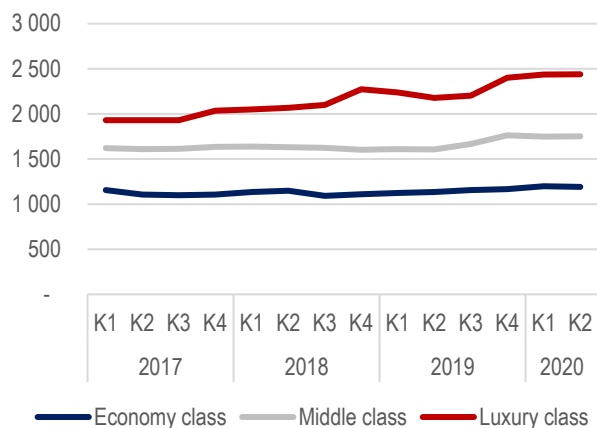
Source: INREAL

A significant decrease in demand in the economy-class segment was recorded in Kaunas during the first half of 2020, just like in the Capital. This share dropped from almost 70 percent during the first quarter this year to 24 percent at the end of the half-year. It is a particularly bad result: it is twice less than the historical average. It is likely that this change was caused by deteriorating expectations for the future of the

buyers of the economy-class housing and stricter financing conditions set by the banks, just like in case of the Capital.

There were no significant changes in the housing prices during the 1<sup>st</sup> half of 2020. The developers offered indirect concessions just like in the Capital. The economy-class housing unit cost 1191 EUR/ sq. m on average, the middle-class housing could be bought for 753 EUR/ sq. m and the luxury-class housing could be bought for 2439 EUR/ sq. m on average in Kaunas City at the end of the 1<sup>st</sup> half of 2020.

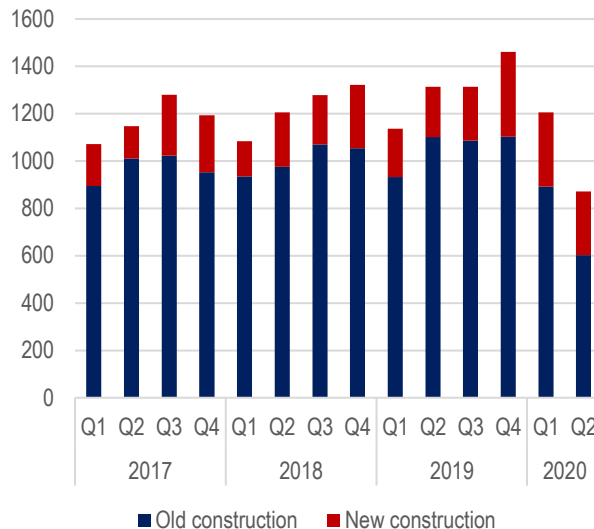
**Average prices of apartments under classes in Kaunas (EUR/ sq. m)**



Source: INREAL

Based on the data of the information recorded by SE “Centre of Registers”, the contraction of the secondary apartment market in Kaunas was not as significant as in case of the primary one. There are no grounds for talking about the market stagnation despite that the results of the second quarter are even one and a half times worse than ones before the quarantine. The scale of transactions for new construction apartments have essentially remained unchanged, which indicates that the buyers have not withdrawn from the preliminary purchase – sale agreements.

**SE Center of Registers registered apartment transactions in Kaunas (units)**



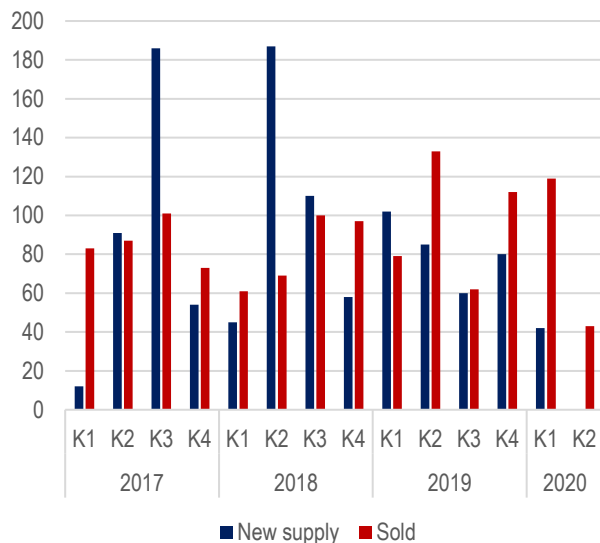
Source: SE Centre of Registers, 07-2020

## APARTMENT MARKET IN KLAIPĖDA

It would not be fair to claim that the Port City did not suffer from the pandemic and the quarantine, but the consequences for the RE market in Klaipėda were milder than in Vilnius or Kaunas. The sales results of the first quarter were only surpassed by the record-breaking second quarter of 2019 and they have been the best ones since 2014. Although the second quarter was much worse, similar sales results occurred earlier in the relatively small market in Klaipėda.

An opposite situation developed in respect of supply of new housing in the Port City. Only 42 offers for new apartments have been recorded here since the beginning of the year, and due to uncertainty of the future it is much likely that we might have to wait for new apartment projects.

### Dynamics of the new supply and sales of apartments in Vilnius (units)

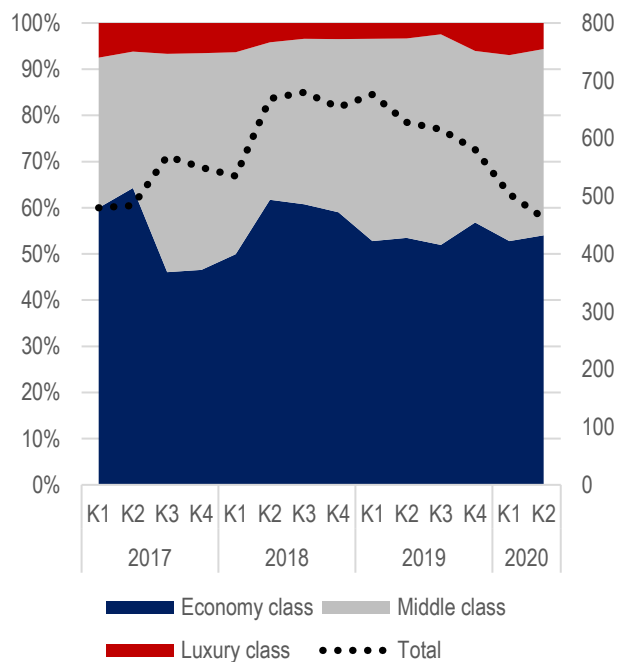


Source: INREAL

The low supply of new construction objects led to the fact that the stock of unsold housing in Klaipėda kept decreasing

steadily unlike in Vilnius and Kaunas. At the end of the 1<sup>st</sup> half of 2020 it had 448 apartments, and this was the lowest number since the beginning of 2017. Although the RE developers in the Port City are rather passive, this does not mean that this City has no need for new housing. Relatively slow pace of housing sales indicates not only market saturation, but also the possibility that potentially the existing supply does not meet buyers' needs and a new exceptional project could be met favourably.

### New construction apartments, unsold in Klaipėda (% / units)



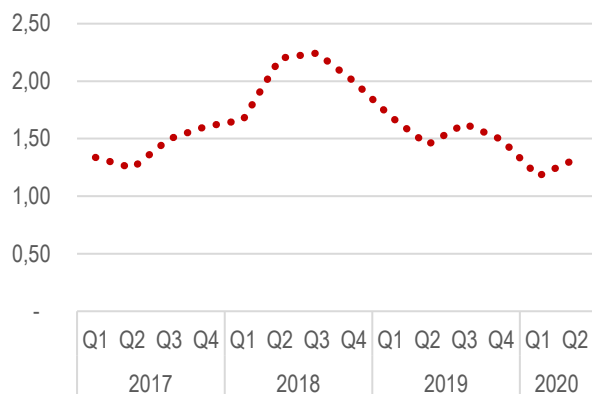
Source: INREAL

The housing liquidity ratio in Klaipėda balances at the rate of 1.32, which means that the existing stock could be sold during the next 16 months, if there are no changes in the supply.

There were no significant changes in the structure of the housing classes in Klaipėda, however, the sales in the

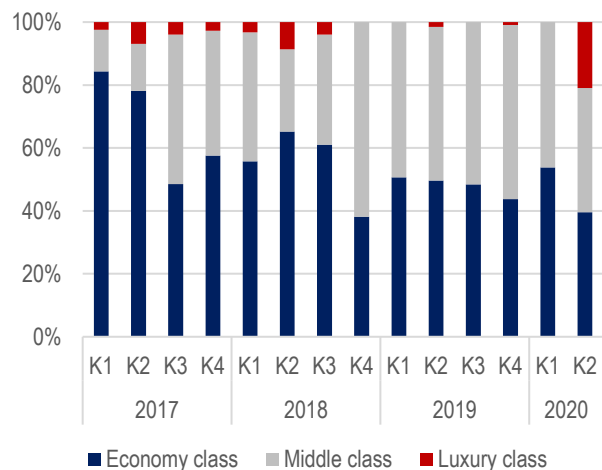
luxury-class segment increased during the quarter in 2020 both as part of all sales and in absolute numbers.

### Liquidity rate of new apartments in Klaipėda



Source: INREAL

### Apartment sales in Klaipėda by class (percent)



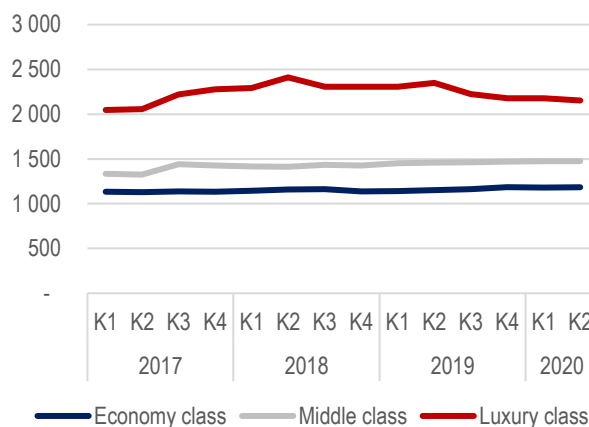
Source: INREAL

There were no changes in the housing prices in Klaipėda during the first half of the year, all adjustments were only symbolic in nature.

The economy-class housing unit cost approximately 1184

EUR/ sq. m, the middle-class housing cost 1475 EUR/ sq. m, and the luxury-class housing cost approximately 2152 EUR/ sq. m in Klaipėda City at the end of the 1<sup>st</sup> half of 2020. Taking into account the wage gap between the municipalities, new construction housing units in Klaipėda are the cheapest one among the three major cities in Lithuania. On the other hand, the low price of housing is one of the factors leading to a smaller supply of new construction housing in Klaipėda. The economy-class housing units on relatively inexpensive land plots in Vilnius City only cost one-third more, so it is likely that the prices of new apartments in Klaipėda City could increase in the future. The apartments in this City also compete with small individual houses, so the price ceiling exists as well.

### Average prices of apartments under classes in Klaipėda (EUR/ sq. m)



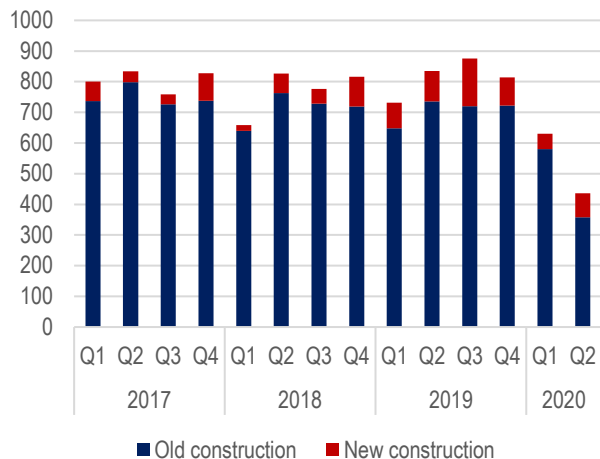
Source: INREAL

According to the data of SE “Centre of Registers”, the transactions for purchase – sale of old construction apartments have been gradually declining both during the first and the second quarters this year. This rate at the end of the first-half year in 2020 was among some of the worst ones over the last ten years. On the other hand, the biggest decline was recorded back in March while the results in June are the



best ones since the beginning of the second quarter.

**SE Center of Registers registered apartment transactions in Klaipėda (units)**



Source: SE Centre of Registers, 07-2020

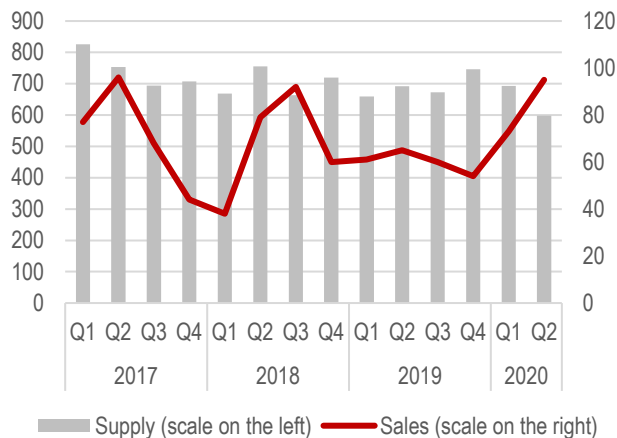
**PALANGA AND NERINGA**

The recreational real estate market on the seaside did not succumb to the slowdown trends, which dominated the first half of 2020. The coastal RE market experienced one of the most active periods during the first half of this year while a significant or even critical drop in both in housing sales and rental markets was observed throughout Lithuania.

The market seasonality is a common phenomenon for recreational housing. Typically RE sales in the coastal zone reach the peak in the middle of the year. Year 2020 turned into a pleasant exception for RE developers in Palanga and Šventoji. The quarantine restricted foreign travel and the psychological impact of the pandemic increased buyers' attention to the coastal market, therefore the sales both during the first quarter (73 units) and the second quarter (95 units) exceeded the rates of the respective periods in 2018–2019 by 20 – 90 percent. The increased market activity also led to a steady decline of the available stock of new construction housing in Palanga and it currently consists of 598 objects, which is the lowest number since the end of 2016 when 591 housing units were offered to the market.

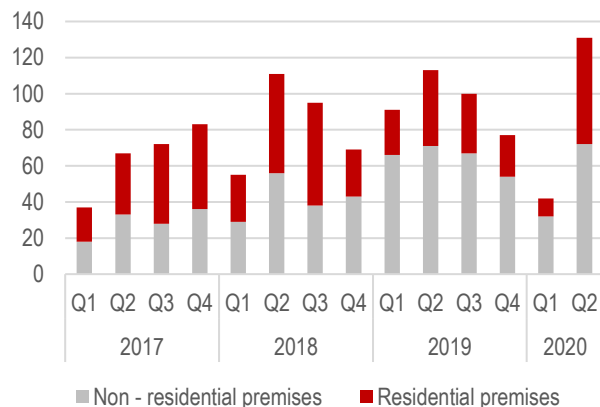
Increased activity was also recorded on the database of SE “Centre of Registers”. The sales of new construction objects were exceptional during the second quarter this year. A total of 59 units of residential premises (apartments) were sold, which is the highest result since the fourth quarter in 2013 when the buyers bought 87 objects. Non-residential premises, which include non-typical housing, e.g., hotel apartments, made a half of all sales. The sales (32 units) were normal during the first quarter, however, the 72 units of premises sold during the second quarter this year is a record result since the third quarter in 2015 when even 112 units of non-residential premises were sold.

### Supply and demand of the primary housing market in Palanga and Šventoji (units)



Source: INREAL

### SE Center of Registers registered sales transactions of new construction premises in Palanga (units)

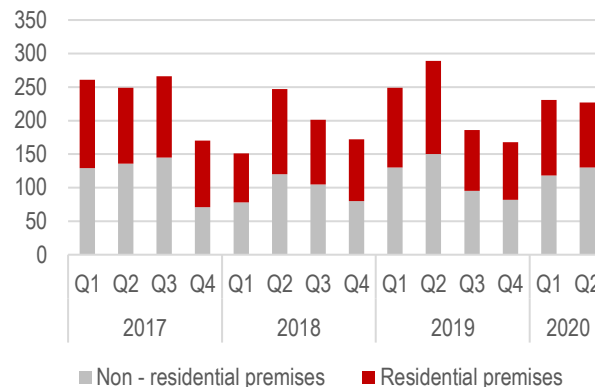


Source: SE Centre of Registers, 07-2020

However, not all housing segments in Palanga could enjoy the increase in buyers' interest. Despite that sales of old construction premises exceeded the long-term average rates (100 premises per segment in a quarter on average), the results were worse in comparison to analogous periods in 2017 – 2018. There are several assumptions, which could

explain lower activity involving old construction premises. Firstly, the pandemic affected the primary (main) housing market in Palanga just like in the biggest cities of the country, secondly, currently the sellers are not willing to sell their existing housing, because they do not see more attractive alternatives or they expect some increase in prices.

### SE Center of Registers registered sales transactions of old construction premises in Palanga (units)



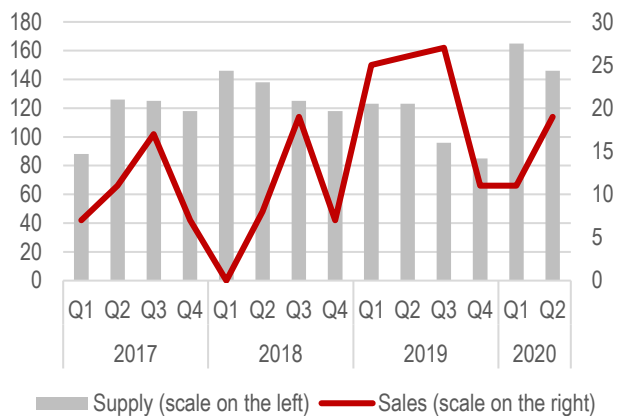
Source: SE Centre of Registers, 07-2020

The real estate market in Neringa is exceptional. Limited development opportunities lead to a particularly small and uneven change in supply, therefore, the sales are associated not only with seasonality, but with the choice options as well. The supply of new housing in Neringa increased by approximately one and a half times at the beginning of this year, while the sales declined significantly at the end of 2019 already. Normally this scenario would be particularly unfavourable for developers, however, sales growth was recorded during the second quarter already due to the specifics of the market. Considering the trends in Palanga and Šventoji, there is still a lot of potential for sales growth.

Historically the biggest challenge for developers in Neringa was sale of the largest and the most expensive housing projects. Comparison of the project structure at the beginning

and during the sale period showed that specifically these apartments dominated among the less attractive ones and the cheaper alternatives used to be sold out soon after developers offer them. On the other hand, due to the limited supply and the increased buyers' interest, even larger housing units have a potential for sale in the near future, especially if new and cheaper projects would not increase in supply.

**Supply and demand of the primary housing market in Neringa (units)**

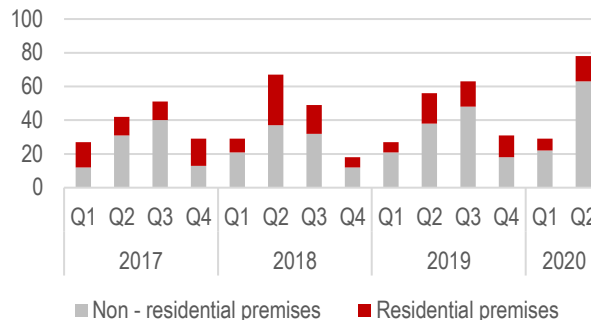


Source: INREAL

Due to the exclusive rights to the land on the Curonian Spit retained by the Republic of Lithuania, essentially there are no new construction objects in Neringa Municipality, so the market is dominated by reconstruction of old objects.

Based on the data of SE “Centre of Registers”, increased activity in Neringa was also recorded in terms of registered RE transactions as well. The sales during the first quarter (29 units) are analogous to the results of the first quarters in 2017 – 2019, whereas the second quarter (78 units) supersedes the period of 2018-2019 by respectively 15 and 40 percent. The difference in comparison to even earlier periods is measured in times.

**SE Center of Registers registered sales transactions of premises in Neringa (units)**

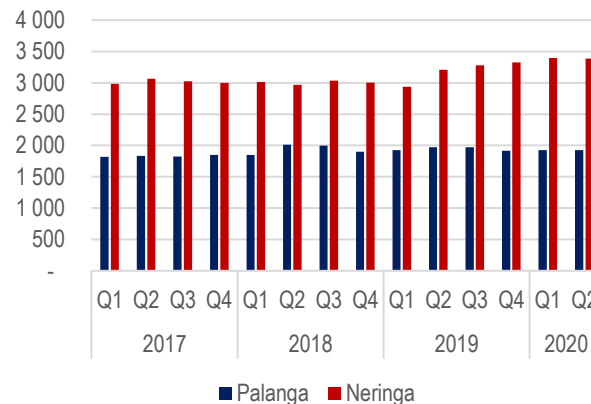


Source: SE Centre of Registers, 07-2020

The housing prices on the primary market in Palanga and Šventoji are characterized by continuity and amount to approximately to 1900 – 2000 EUR/sq. m for the third year already.

No significant changes in prices were recorded in Neringa either. The average housing price on the primary market in Neringa increased from approximately 3200 EUR/sq. m to almost 3400 EUR/sq. m over the last twelve months.

**Average housing prices in the coastal primary market (EUR / sq. M)**



Source: INREAL

## LAND PLOT MARKET

The impact of the pandemic on the land plot market was significantly smaller during the first half of 2020 than it was on the primary housing market. On the other hand, it would not be fair claiming that this segment was not affected by the pandemic.

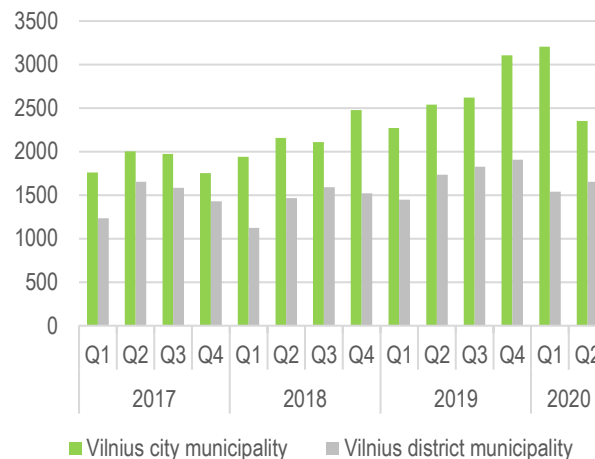
With the ongoing intense development of apartment buildings, considering the population density, the vacant land area in the Capital is larger than in other major cities, so it is not surprising that the land plot market in the City municipality than in the surrounding area. The first quarter this year was particularly successful to the Capital's land plot market. A record number of land plots (since 2012), i.e., over 3200 land plots, was sold in the City. The results of the second quarter in Vilnius shrank by one-fourth, however, the drop in sales was not as dramatic as it was in the apartment segment. The seasonal decrease in the number of transactions in Vilnius District could be felt during the first quarter this year, however, further decrease in the middle of the year was avoided.

There was less vacant land in Kaunas City than in the Capital, thus resulting in higher activity observed in the surrounding areas rather than the City itself. The results of the first quarter (1001 units) in the City were particularly good, the growth continuing over a period of several years was maintained, however, due to the effect of the pandemic, the second quarter was less active (858 units) even than the second quarter of 2019 (991 units). The situation in the District was similar. Growth was recorded during first quarter (1070 units) and despite that the second quarter was better (1092 units), it was still not as active as it was a year ago (1354 units).

It is likely that the land plot market in Klaipėda suffered significantly smaller turmoil due to the shortage of new construction apartments. The trends of the first quarter in

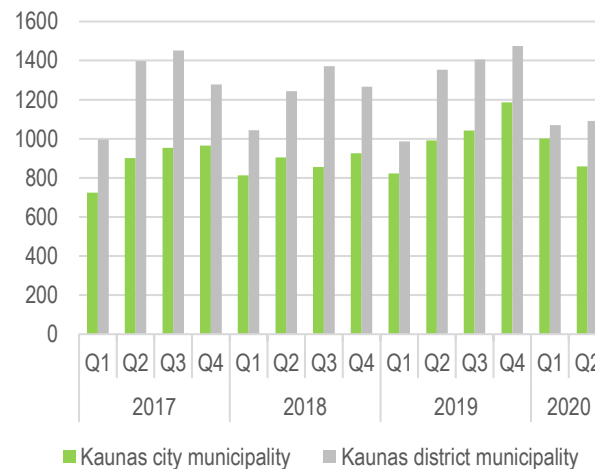
2020 are consistent with the situation in major cities and the decline in the number of transactions during the second quarter was much milder.

### **Land transactions in Vilnius city. and district municipalities (units)**



Source: SE Centre of Registers, 07-2020

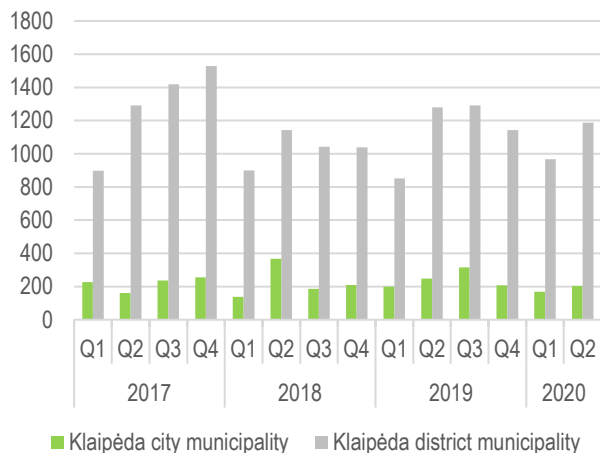
### **Land transactions in Kaunas city. and district municipalities (units)**



Source: SE Centre of Registers, 07-2020



### Land transactions in Klaipėda city. and district municipalities (units)

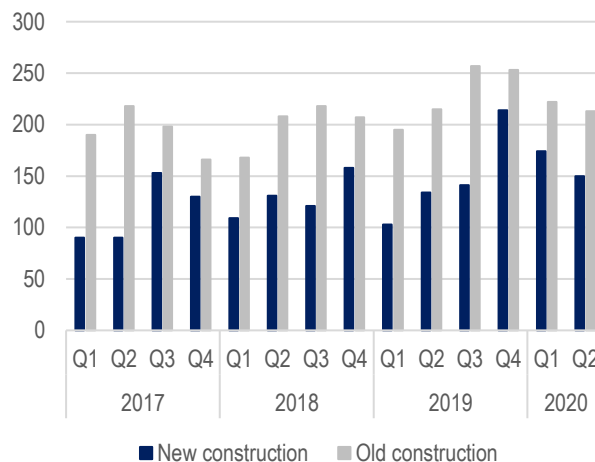


Source: SE Centre of Registers, 07-2020

## RESIDENTIAL BUILDING MARKET

The general decline in the RE market activity did not leave the individual house and cottage segment behind. A steady decline in the number of transactions was recorded here since the end of 2019. On the other hand, the situation on the residential building market was evolving differently than on the apartment market during the first half of 2020. Just like the land plot market, this segment is characterized by major seasonality. The second quarter of the year always used to grow by 20-50 percent (this increase used to reach even 60 percent in the new house segment) in comparison to the first quarter. However, this year the case was quite different: the number of transaction for residential buildings dropped by approximately 10 percent (by approximately 9 percent in case of new houses) in all three major cities during the second quarter. The market of new construction houses remained stable in comparison to the last year, however, the number of transactions for old construction houses decreased.

### Residential buildings transactions in Vilnius city. and district municipalities (units)

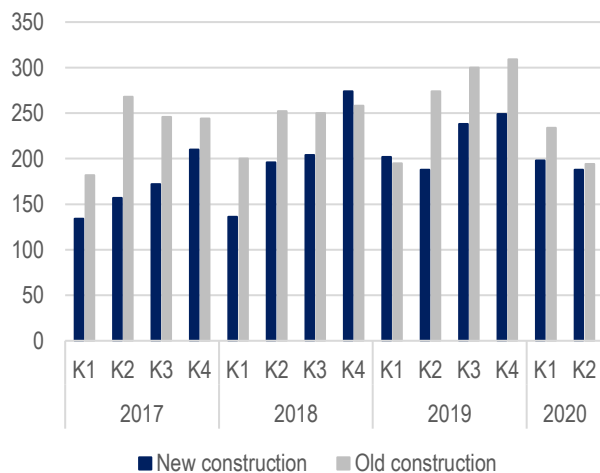


Source: SE Centre of Registers, 07-2020

The number of transactions for new construction residential buildings in Vilnius City and in the surrounding areas kept increasing in comparison to the last year. 69 percent more transactions (174) were made during the first quarter and 12 percent more (150) were made during the second quarter. The market of old construction houses respectively increased by 14 percent (222 transactions) and decreased by 1 percent (213 transactions).

Kaunas and the areas around the City remain a clear leader and more transactions were recorded both before the pandemic and after the quarantine, in comparison to other cities in the country. On the other hand, the market dynamics was worse. 2 percent fewer transactions (198) were made in the new construction house segment during the first quarter than a year ago, the same applies to the second quarter (188). The market of old construction houses respectively increased by 20 percent (234 transactions) and decreased by 29 percent (194 transactions).

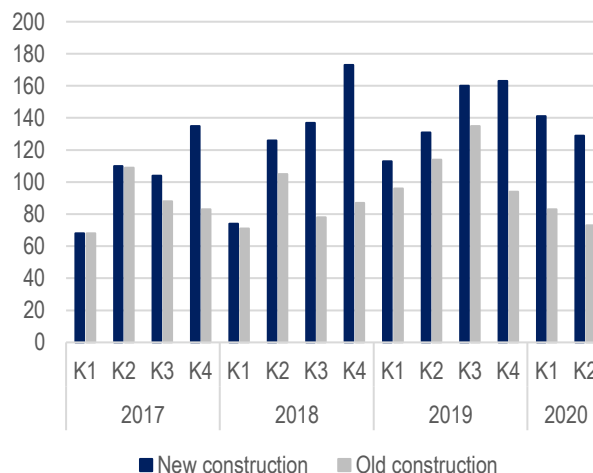
**Residential buildings transactions in Kaunas city. and district municipalities (units)**



Source: SE Centre of Registers, 07-2020

In Klaipėda the market of new construction houses grew by 25 percent (141 transactions) during the first quarter and declined by 2 percent (129 transactions) during the second quarter in comparison to 2020 and 2019. The old construction segment dropped by 14 percent (83 transactions) during the first quarter and by 36 percent (73 transactions) during the second quarter. It should be noted that Klaipėda (including the surrounding areas) is the only major city with a recorded larger number of transactions for new construction residential buildings in comparison to the old ones.

**Residential buildings transactions in Klaipėda city. and district municipalities (units)**



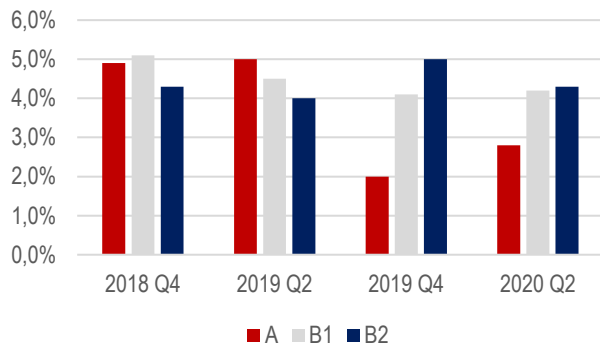
Source: SE Centre of Registers, 07-2020

## VILNIUS BUSINESS CENTRES

There were some minor changes in the occupancy of business centres in the middle of 2020. They were caused by the development of new objects, the migration of tenants, the pandemic and its management measures. Currently vacant Class A premises in business centres make approximately 2.8 percent of the premises, in case of Class B1 this rate is approximately 4.2 percent, and in case of Class B2 it is approximately 4.3 percent. A common challenge encountered by all segments is an increased number of employees working from home. It is likely that tenants will take this opportunity to save some money if this trend prevails in the future.

The competition between the segments will keep rising as the supply on the market keeps increasing each year. Having reduced the space of rented premises, the resulting difference in funds could be used for a better location of the office, and it is likely that tenants of particularly small premises would make arrangements for work from home and co-working spaces.

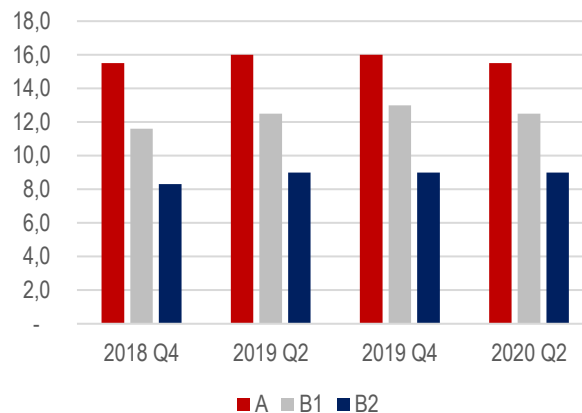
### **Dynamics of vacancies in Vilnius business centres under classes**



Source: INREAL

The ranges of the rental prices have not changed over the period of six months. The price of Class A office premises amounted to 14–17 EUR/sq. m, the rate in case of Class B1 is 11–14 EUR/sq. m and in case of Class B2 it is 7–10 EUR/sq. m. The rental prices decreased in individual cases due to the pandemic and particularly rapid development of business centres, however, these concessions are mostly related to the relationship between the tenant and the lessor, the size of the rented premises, the duration of agreements and additional rent costs.

### **Dynamics of lease prices in Vilnius business centres under classes**

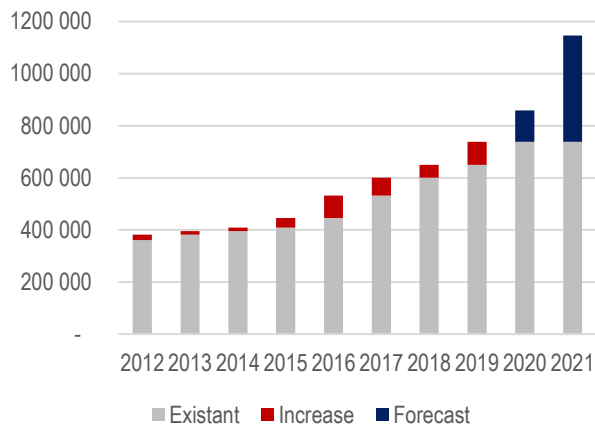


Source: INREAL

High occupancy of Vilnius business centres, stable rental prices, and appealing sales conditions contribute to a steady growth of the Capital's office market. 12 objects (approximately 120 000 sq. m) are expected to be completed this year, provided that any delay in the construction due to the pandemic is prevented. The figures for the planned development next year are even more impressive with twice as many objects (almost 300 000 sq. m). On the other hand, some of these objects are still in the drawing phase, so there is a chance that their implementation could be postponed.

Continued existence of remote work and such sudden increase in new space could lead to a significant increase in vacant premises and lower rental prices, which could plunge the office market into several-year-long stagnation.

#### Development of modern business centres in Vilnius (sq.m)



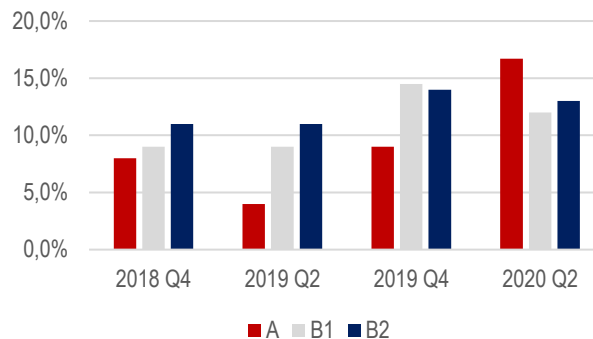
Source: INREAL

## KAUNAS BUSINESS CENTRES

The main factors having shaped Kaunas office market this year include increased supply of offices and the COVID-19 pandemic. These circumstances gave a little more bargaining power to tenants allowing them to negotiate both the rental prices and the conditions of agreements.

The business centres opened at the end of 2019 significantly increased the vacancy rate of Class A business centres. Approximately 9 percent of all top class premises were offered to tenants last year, but in the middle of 2020 the vacancy rate increased to 16.7 percent. Vacant Class B1 premises made approximately 12 percent in Kaunas during the second quarter this year (which is slightly less than 14.5 percent last year), and in case of Class B2 this rate was 13.0 percent (14.0 percent).

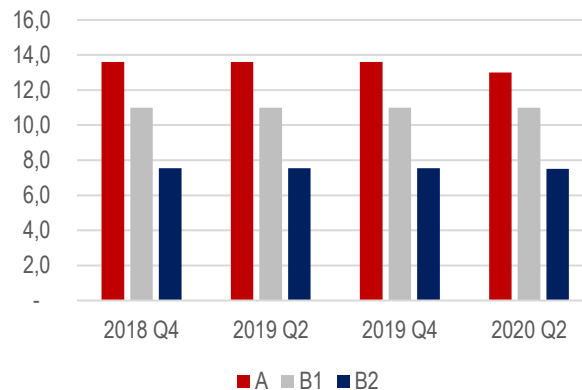
#### Dynamics of vacancies in Kaunas business centres under classes



Source: INREAL

There have been no essential changes in the office rental prices during the first half of this year, but the tenants may expect minor concession due to the pandemic as well as slightly more relaxed conditions applicable to the rent. The price range of newly concluded contracts for Class A centres is 12-13 EUR/sq. m, in case of Class B1 this rate is 9-11 EUR/sq. m, and in case of Class B2 business centres it is 6-9 EUR/sq. m.

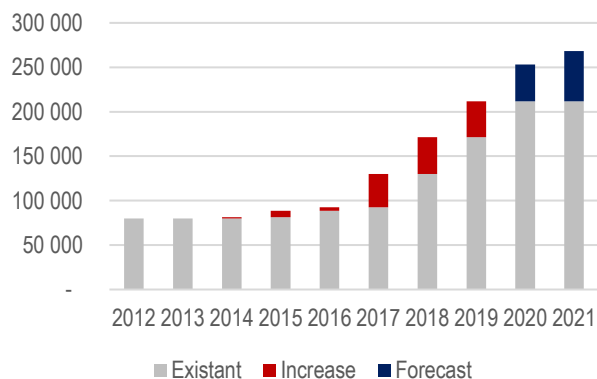
#### Dynamics of lease prices in Kaunas business centres under classes



Source: INREAL

The development plans for Kaunas in 2020 have remained unchanged. 6 business centres are expected to be built this year, thus providing more than 40 000 sq. m additional premises to the market. The development plans for year 2021 remain vague. There is some information about the intention to develop 3 new projects for 15 000 sq. m of premises. The slightly slower development was determined by not only the new areas to be utilised, but also by still undetermined impact of the pandemic on the RE market as well as the national and global economy. On the other hand, slower development will enable to ensure sustainability of this market segment.

#### Development of modern business centres in Kaunas (sq.m)



Source: INREAL

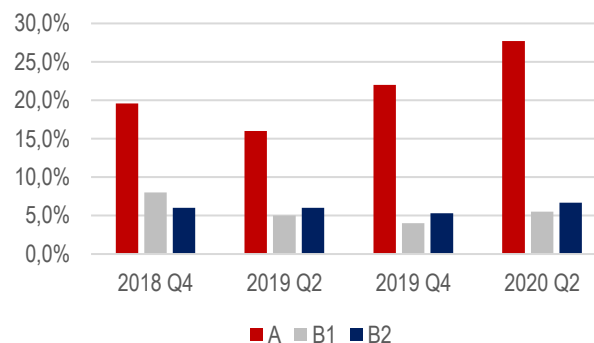
## KLAIPĖDA BUSINESS CENTRES

Regardless of particularly restrained office development, Klaipėda still faces difficulties in terms of occupation of vacant premises, despite of the relatively numerous options in terms of available premises and the rental prices being lower than in Vilnius and Kaunas.

The vacancies in Class A business centres increased from 22.0 percent at the end of 2019 to 27.7 percent in the middle of this year, this rate increased from 4.0 percent to 5.5

percent in case of vacancies on Class B1 premises, and from 5.3 percent to 6.7 percent in case of Class B2 premises.

#### Dynamics of lease prices in Vilnius business centres under classes



Source: INREAL

There were no changes in rental prices. Class A premises could still be rented for 9–12 EUR/sq. m, the rental price of Class B1 premises amount to 7–11 EUR/sq. m, while premises in segment B2 currently could be rented for 5–7 EUR/sq. m.

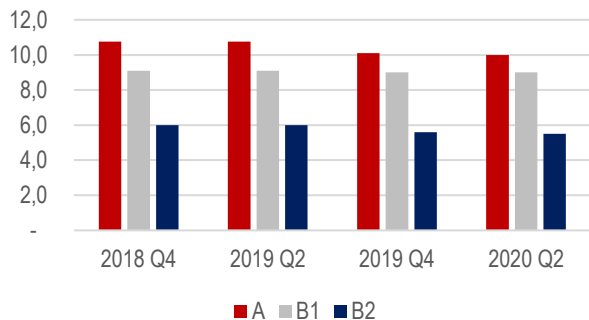
It is likely that the steady low occupancy of Class A business centres could lead to a minor price war. On the other hand, the rental prices in segment B are not high altogether, so it is likely that the differences in occupation of premises of different classes could decrease in the future.

The office market in Klaipėda is not very attractive to RE developers, just like in case of the primary apartment market. Despite that the relative office space per capita here is smaller than in Vilnius or Kaunas, even individual new objects increase vacancy of premises for a long time.

4 objects are planned to be built in 2020 with a total space available for rent amounting to approximately 10 000 sq. m. The plans for year 2021 are much more modest with only one business centre of 2500 sq. m in the works.



### Dynamics of vacancies in Klaipėda business centres under classes

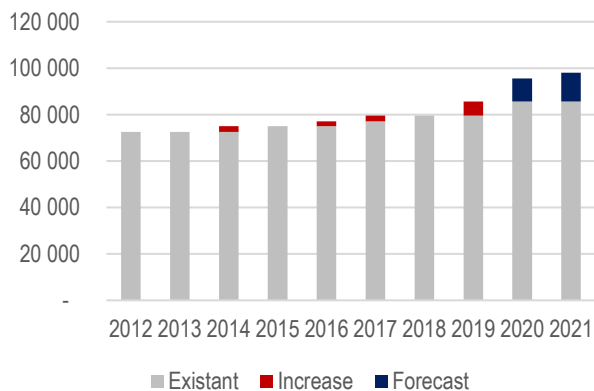


Source: INREAL

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### Development of modern business centres in Klaipėda (sq.m)



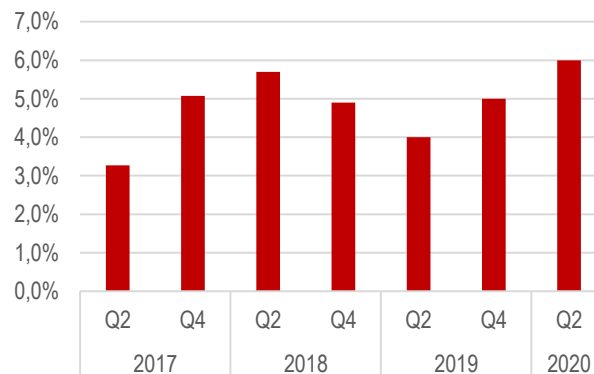
Source: INREAL

## INDUSTRIAL AND STORAGE PREMISES

The first half of the year also had some negative impact on logistics centres and storage premises both in terms of vacant space and prices.

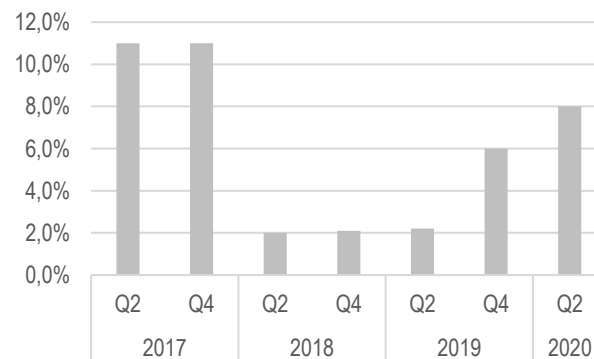
Vacant space in logistics centres and warehouses in Vilnius increased from 5.0 percent at the end of 2019 to 6.0 percent this year.

### Dynamics of vacancies in modern logistics centres in Vilnius (percent)



Source: INREAL

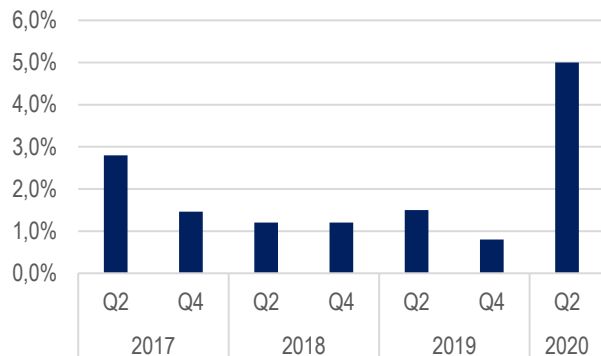
### Dynamics of vacancies in modern logistics centres in Kaunas (percent)



Source: INREAL

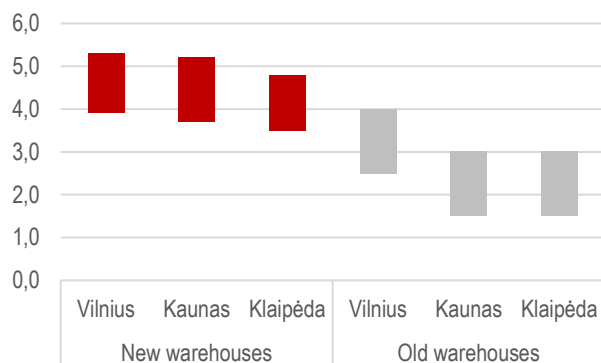
The increase in vacant spaces on the premises is even more significant in Kaunas. The vacancy rate of the premises of approximately 2.2 percent at the end of 2019 reached approximately 8.0 percent at the end of June.

**Dynamics of vacancies in modern logistics centres in Klaipėda (percent)**



Source: INREAL

**Lease prices of logistics centres in Lithuania (EUR/ sq. m)**



Source: INREAL

The increased space of vacant premises and the pandemic also had a negative impact on the rental prices in the segment of logistics centres and storage premises.

The rental price of new construction logistics centres in the Capital region amounted from 3.9 EUR/sq. m to 5.3 EUR/sq.

m, the price rate in Kaunas and the surrounding areas amounted to approximately 3.7–5.2 EUR/sq. m, and the price rate in the coastal region amounted to 3.5–4.8 EUR/sq. m.

Old construction warehouses currently cost 2.5-4.0 EUR/sq. m in Vilnius and approximately 1.5–3.0 EUR/sq. m. in Kaunas and Klaipėda.



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*Ms Bitinaitė's specialisation is real estate, construction law, infrastructure and public-private partnerships. She advises clients on real estate development, sales and acquisitions, leasing and other related matters.*

## **REAL ESTATE LAW AND TAX NEWS**

The first half of this year did not bring significant changes in the field of real estate law for the reasons that are probably well known to everybody. The spread of the COVID-19 virus and the related restrictions, which stopped the daily rhythm around the world, did not escape Lithuania either. The main focus of the legislation has been on drafting and adopting legislation on preventive measures to stop the spread of the COVID-19 virus and on reducing the negative consequences of the business most affected by COVID-19. Among other things, **the description of the state aid scheme and conditions of the measure “Partial rent compensation to the companies most affected by COVID-19”** approved by the Minister of Economy and Innovation of the Republic of Lithuania is relevant for real

estate market participants. The description provides for state aid to legal entities and entrepreneurs by compensating up to 50% rent to tenants during the quarantine period and for two months thereafter. The essential conditions for receiving state support are that the tenants' main activities during the quarantine period were banned or restricted by a Government resolution and they did not carry out such activities during the restriction period, and that the landlords had provided tenants with at least 30% discount on rent after the declaration of quarantine. The description also covers other requirements, including the much-discussed, labour-intensive and troubling requirement for tenants and landlords to register rent agreements in the Public Real Estate Register. Thus, if all conditions and requirements set out in the description are met, applications for the state aid can still be submitted until 1 December 2020.

In the light of recent events, the construction technical regulation STR 1.05.01:2017 “Construction permits. Completion of construction. Suspension of construction. Elimination of the consequences of arbitrary

construction. Elimination of the consequences of construction under an illegally issued building permit” has been adjusted since 2 April 2020. Together with amendments adopted by the order of the Minister of the Environment, a new annex to the Construction Technical Regulation “Description of the procedure for carrying out construction completion procedures during global quarantine” has been prepared, which slightly changes the construction completion process during global quarantine allowing more actions to be performed remotely. It is worth mentioning such changes as the possibility to submit a request for the completion of the construction certificate remotely (using IS Infostatyba) or the possibility for the commission members to perform the construction completion procedures separately (in order to maximally protect the health of the construction commission members and the builder). However, the most noteworthy change is the ability for all members of the construction completion commission to participate in a remote inspection of the building, submit questions, comments, and receive answers, provided that the builder ensures live streaming of the high-definition video.

On May 7, 2020, an important and long-awaited law was adopted for both real estate developers and real estate users – **the Law on Municipal Infrastructure Development, which will enter into force on 1 January 2021**. The law eliminates the existing legal gaps regarding the development of municipal infrastructure and its organization. Prior to the entry into force of the said law, legal acts regulated only individual stages of the municipal infrastructure development, did not establish a clear and uniform procedure for the compensation for

investments in infrastructure development, and infrastructure development was chaotic, applying different rules each time.

The new legal regulation brings clarity to the determination of the entities responsible for infrastructure development planning and organization (municipal administration or public legal entity established and / or appointed by the decision of the municipal council), municipal infrastructure development financing procedure (introduces a new measure – municipal infrastructure development support program aimed at financing the development of municipal infrastructure), the division of responsibilities between entities in the implementation of municipal infrastructure development, including a clear mechanism for real estate developers and / or users how to contribute to the implementation of the relevant infrastructure development (by paying a fee calculated in accordance with the established procedure or participating in the infrastructure development process). In addition, the law provides for the establishment of a new position – the chief engineer of the municipality whose main function will be to ensure the compatibility and compliance of engineering infrastructure solutions with approved territorial planning documents and construction legislation. By-laws are currently being drafted, such as the procedure for calculating compensation prepared by the Government for infrastructure development initiators for the municipal costs incurred in the infrastructure development agreement and the methodology for determining the municipal infrastructure development fee, which will ensure proper implementation of the law from 2021.

Respectively, after the adoption of the Law on Municipal Infrastructure Development, amendments to **the Law on Construction, the Law on Territorial Planning and the Law on Local Self-Government** were adopted, harmonizing the provisions of the said laws with the provisions of the Law on Municipal Infrastructure Development. One of the key amendments to the Law on Construction that should be noted is the moment of amendment of the municipal infrastructure development contract concluded by the builder (concluded before the issuance of the construction permit) after the change of the builder to whom the construction permit was issued (this contract must be amended before the start of construction and / or completion procedures in accordance with the issued building permit). Amendments to the Law on Territorial Planning determine when the initiator of planning must conclude municipal infrastructure development agreements (when the implementation of the decisions of the territorial planning document requires the development of engineering and / or social infrastructure), specify the deadlines for coordination of integrated territorial planning documents at the municipal level. Amendments to these laws will enter into force together with the Law on Municipal Infrastructure Development, i. e. from 1 January 2021.

Although we have already discussed the legislation and its amendments that came into force on 1 January 2020 in the previous review, once again we briefly recall the most important legislation that came into force with the beginning of 2020:

- **Law on Special Land Use Conditions.** The law sets out the conditions for the establishment, amendment and cancellation of special land use conditions, their

legal force and the procedure for compensation for losses incurred due to the established conditions. Significant innovations are envisaged – special land use conditions can be established in unformed land plots, the moment of application of special land use conditions is related to the categories of land plots (newly formed land plots, land plots registered in the Real Estate Register and areas where no land plots are formed). The terms and procedure for the issuance of consents by the owner of the land plot, the state or municipal trustee, as well as the obligation to indicate the relevant data to the manager of the public register is specified;

- Amendments to **the Law on Land**, which stipulate that all land formation and redevelopment projects are organized by the director of the administration of the respective municipality, regardless of whether the project is prepared in urban and township areas or in rural residential areas;
- Amendments to **the Law on Acquisition of Agricultural Land**, which establishes the right of private landowners to purchase intervening plots of land not exceeding 3 ha without an auction, and the priority right to purchase the intervening state agricultural land to the owner of the adjacent land plot who rents or temporarily uses it;
- Amendments to **the Law on Protected Areas and the Law on the Coastal Zone**, which specify the conditions for activities in protected areas and the coastal zone, as well as the provisions of these laws have been harmonized with the new Law on Special Conditions of Land Use;



- Amendments to **the Forest Law**, which provide that persons or related persons may acquire a maximum of 1,500 ha of forestry land. It is also provided that persons will be able to acquire a forestry land plot or more than 20% of the shares of a legal entity owning more than 400 ha of forestry land in the territory of Lithuania only with the consent of the National Land Service;
- **STR 2.03.01: 2019 “Accessibility of buildings”**, which sets out the requirements to be met during the construction, reconstruction, renovation (modernization) and overhaul of buildings to be adapted to the special needs of the disabled;
- **The Law on Metropolitan**, which establishes the foundations for the implementation of the metro as a new mode of transport.
- The amendments to **the Law on Land Tax** provide for a new exemption for the calculation of land tax for 2020 and subsequent tax periods – land tax will not be levied on land included in the areas specified in the Special Land Use Law established in the public interest when due to the application of special land use conditions in these territories, the land owner loses the possibility to use the land plot in accordance with the established main land use purpose and / or the land use method(s), except in cases when the land owner could use the land plot in accordance with the newly determined main land use purpose and / or land plot method of use;
- Amendments to **the Law on Real Estate Tax** have reduced the tax-free amount of real estate owned by natural persons (to EUR 150,000 (previously EUR 220,000)), as well as by families raising three or more natural children (adopted children) or a disabled child (to EUR 200,000 (previously EUR 286,000)). The minimum real estate tax rate has also been harmonized for all taxable real estate of natural and legal persons, increasing it from 0.3% to 0.5%.

During the first half of the year, no new amendments to real estate-related tax laws were adopted.

Relevant amendments to **the Law on Land Tax** and **the Law on Real Estate Tax**, which entered into force on **1 January 2020**. They changed the procedure for setting the rates of land tax and, accordingly, real estate tax (municipal councils are no longer obliged to set rates for these taxes annually, but have the right to choose whether to set a new rate for these taxes or to maintain and apply specific rates for the previous tax period). Both laws also specify that the fees of a collective investment undertaking, that is not a legal person, are paid by the management company of the collective investment undertaking.

At the same time, other amendments to these laws came into force:

As of **January 1, 2020**, amendments to **the Law on Tax Administration** came into force, which changed the statute of limitations for tax calculation or recalculation – both the taxpayer and the tax administrator may calculate or recalculate the tax for no more than the current and 3 previous calendar years. There are several exceptions when the tax administrator will have the right to recalculate taxes for a longer period than provided (5 or 10 years).

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