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November 29, 1995

To: Members of the Executive Board

From: The Secretary

Subject: Republic of Lithuania - Second Review Under the Extended Fund Facility

Attached for consideration by the Executive Directors is a paper on the second review under the extended Fund facility for the Republic of Lithuania, which is tentatively scheduled for discussion on Wednesday, December 20, 1995. A draft decision appears on pages 15-17.

Mr. Berengaut (ext. 38773), Mr. Brekk (ext. 38754), or Ms. Psalida (ext. 35360) is available to answer technical or factual questions relating to this paper prior to the Board discussion.

Unless the Documents Preparation Section (ext. 36760) is otherwise notified, the document will be transmitted, in accordance with the procedures approved by the Executive Board and with the appropriate deletions, to the European Bank for Reconstruction and Development (EBRD), the European Commission (EC), the European Investment Bank (EIB), and the Organisation for Economic Cooperation and Development (OECD), following its consideration by the Executive Board.

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REPUBLIC OF LITHUANIA

Staff Report for Second Review Under Extended Fund Facility

Prepared by the European II and Policy Development and Review Departments

Approved by John Odling-Smee and Susan Schadler

November 28, 1995

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I. Introduction

The discussions for the second review under the EFF arrangement for Lithuania were held during October 23-November 3, 1995. 1/ The Lithuanian representatives included President Brazauskas, Prime Minister Šleževičius, Minister of Finance Šarkinas, Governor Ratkevičius of the Bank of Lithuania (BOL), and other officials engaged in economic and financial matters.

The EFF arrangement supports a program covering October 1, 1994-September 30, 1997, described in the Government's Memorandum of Economic Policies, and was approved by the Executive Board on October 24, 1994 (EBS/94/199, 10/3/94, and Supplement 1). The first EFF review was completed on July 14, 1995, in conjunction with the 1995 Article IV consultation (EBS/95/106, 6/23/95, and Supplement 1). Access under the EFF arrangement is SDR 135 million, or 130 percent of quota; Table 1 shows use of Fund resources while Table 2 shows the schedule of purchases under the second annual program. In a letter dated November 28, 1995 (Appendix I), the authorities review economic developments and policies in the period since the first EFF review, and describe in detail economic objectives and policies for the second annual program.

Appendix II summarizes Lithuania's relations with the Fund, and Appendix III lists Fund technical assistance. Appendix IV shows the status of economic data. 2/ Appendix V summarizes World Bank Group operations.

II. Economic Developments under the EFF-Supported Program 3/

Since independence was regained, Lithuania has established a solid record in attaining macroeconomic stability and making the transition to a market economy. This progress has continued under the EFF-supported program; all end-September 1995 performance criteria were observed

1/ The mission consisted of Mr. Berengaut (head), Mr. Brekk, Ms. Psalida (all EUR II), Mr. Josefsson (MAE), Mr. Shiells (PDR), Mr. Platais (special appointee-ADM), and Ms. Coles (assistant-EUR II), and was assisted by Mr. Fanizza, the resident representative. Mr. Giugale of the World Bank also participated. Ms. Srejber, Alternate Executive Director for Lithuania, took part in the latter part of the discussions.

2/ The staff report for the 1995 Article IV consultation and first EFF review contains a detailed discussion of the economic data base. Fund staff estimates make adjustments for under-recording in the official national accounts and balance of payments data.

3/ This chapter mainly describes economic developments during the second half of the first annual program (i.e., April-September 1995). Developments through early 1995 are described in the staff report for the 1995 Article IV consultation and first review under the EFF arrangement, and in the accompanying Recent Economic Developments report (SM/95/161, 7/6/95).

(Table 3), and headway has been made essentially as envisaged in structural reform (Table 4). However, weaknesses in the banking system have started to surface and the financial position of the energy sector remains fragile.

1. Growth, inflation, and the balance of payments

Economic activity has continued to recover. In 1995, the industrial, construction, and retail trade sectors have recorded large increases in output. Staff projections suggest that real GDP growth will be 4 percent in 1995 (Table 5). This is somewhat lower growth than earlier projected; the downward revision mainly reflects weaker-than-expected domestic demand.

Inflation has remained relatively low, at 1.5-2 percent monthly average during April-October 1995, although there has been a sharp increase in sugar prices, as well as an increase in excise taxes (Chart 1). 1/ Inflation is expected to accelerate toward the end of 1995, reflecting normal seasonal variations, the doubling of heating prices at the start of the heating season, and public sector wage increases effective October 1.

The measured current account deficit in 1995 is projected to be lower than earlier expected, mainly reflecting higher net services inflows. 2/ External competitiveness appears adequate; export growth--in particular to the West--has continued to be robust, the real exchange rate of the litas has remained broadly unchanged during 1995 (Chart 2), and Lithuanian wages in U.S. dollar terms have remained low compared with those in economies at a similar stage of transition (Chart 3); however, a somewhat higher inflation than among trading partners could be expected as a reflection of the initial undervaluation of the litas, as well as differential productivity growth in the traded and non-traded goods sectors.

2. Budgetary policy

Fiscal restraint has been maintained, and the general government financial deficit has remained well below the program ceilings. In contrast to the situation in early 1995, fiscal restraint recently has been achieved chiefly through improved revenue collection rather than expenditure cuts. Indeed, the better revenue performance has allowed some reduction in government arrears to suppliers and in salary arrears.

The revenue performance reflects improvements in the administrative and legal framework for tax collection. The new Law on Tax Administration has provided the legal basis for stricter tax enforcement. The head office and the staff of the State Tax Inspectorate have been strengthened. Legal action has been taken against customs officers involved in corrupt practices and against tax delinquents. Finally, excise taxes on alcohol and tobacco

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1/ The excise tax increase had not been factored into the projections prepared for the first EFF review.

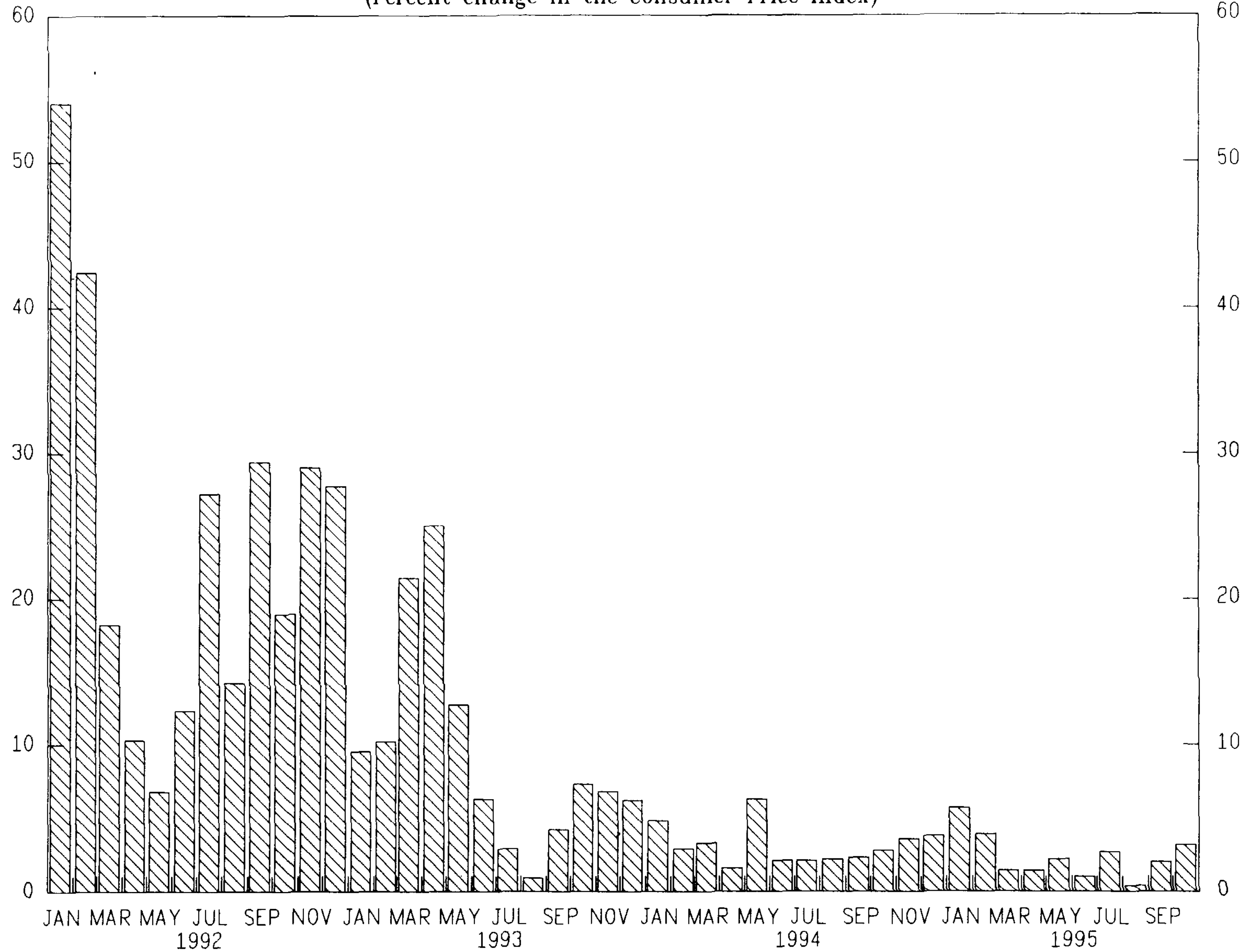
2/ Due to improved coverage in the data.

CHART 1

LITHUANIA

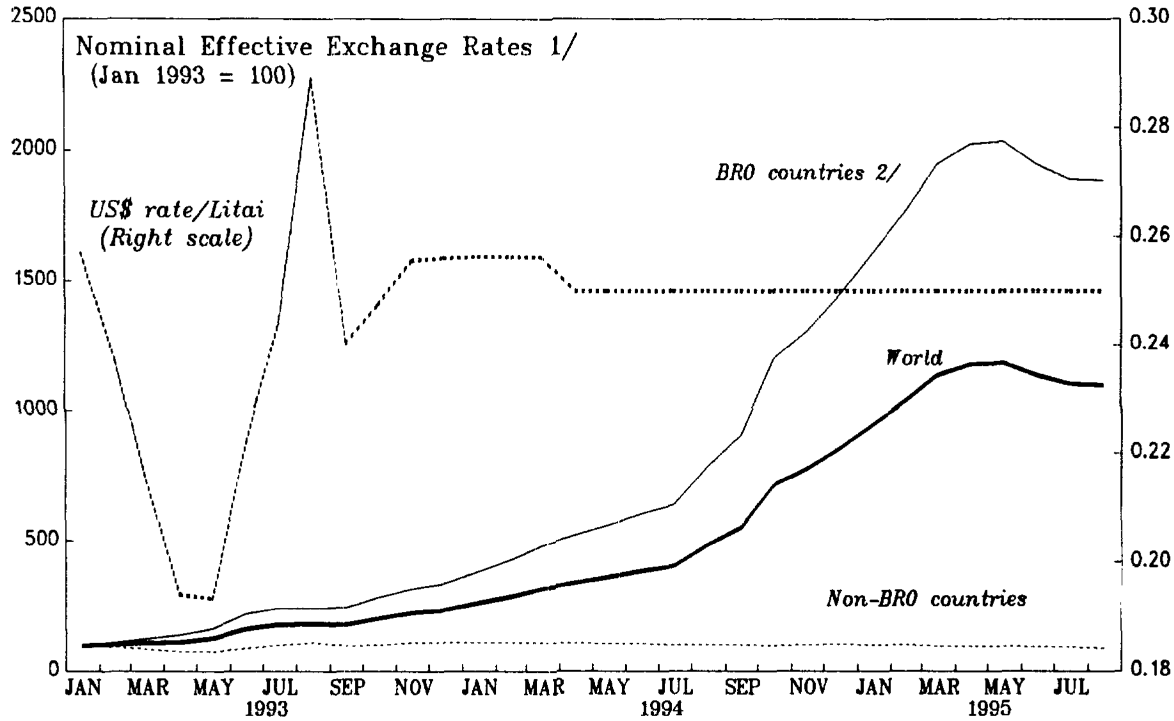
MONTHLY INFLATION

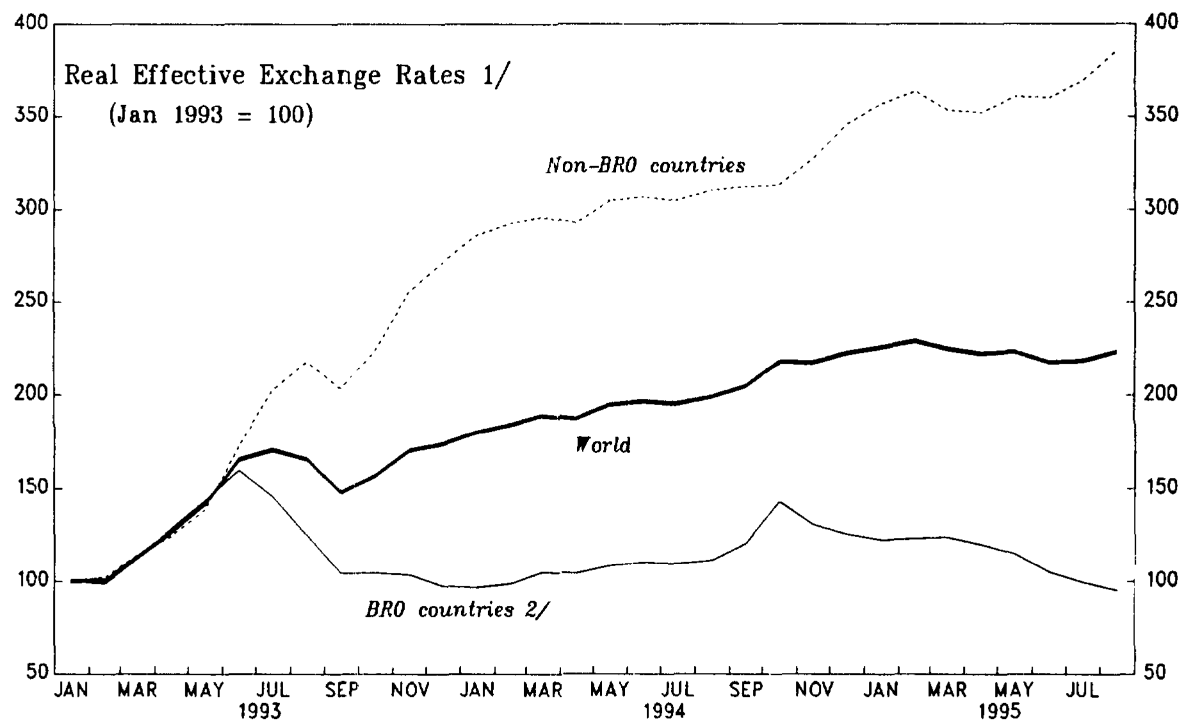
(Percent change in the Consumer Price Index)



Source: Data provided by the Lithuanian authorities.

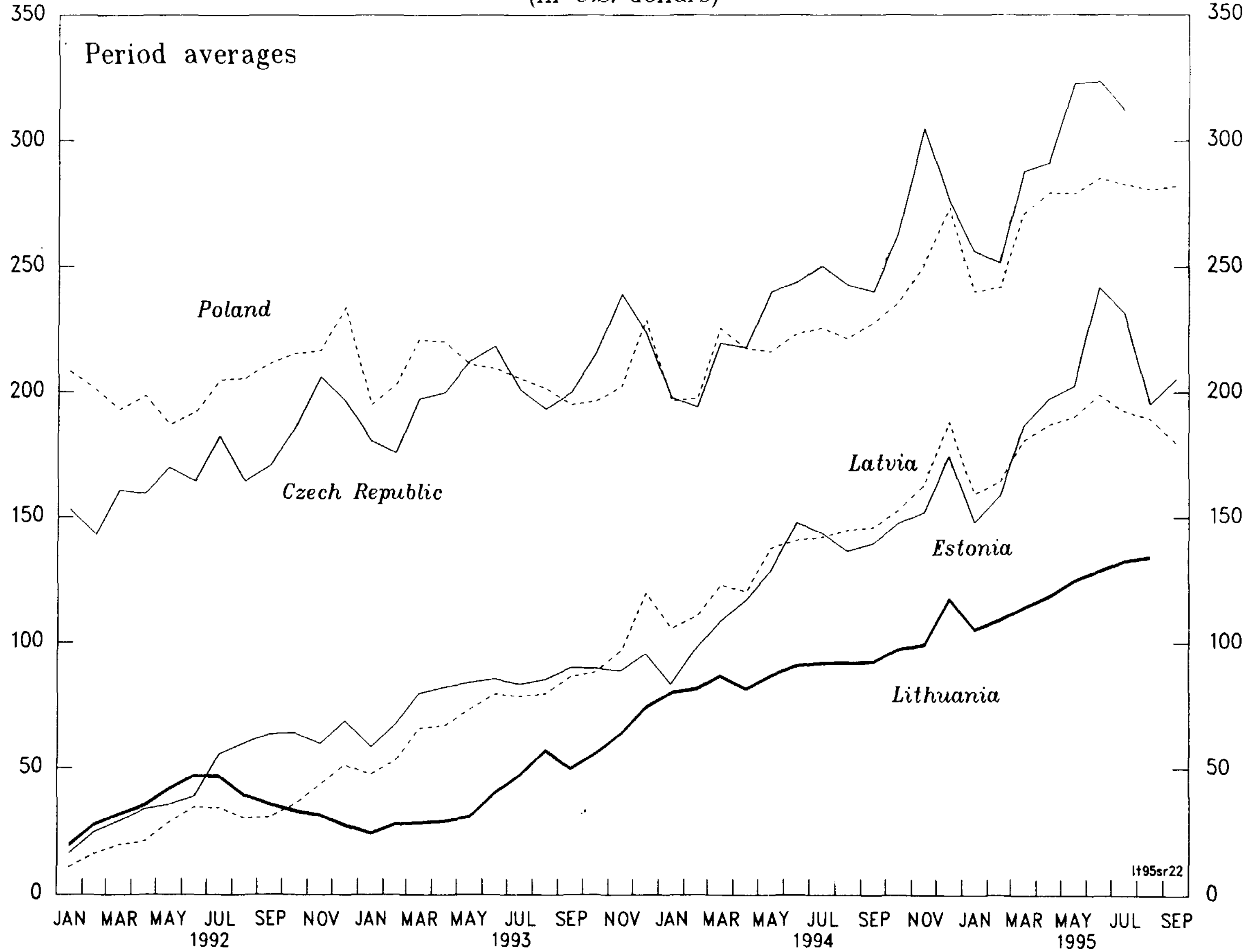
CHART 2
LITHUANIA
EFFECTIVE EXCHANGE RATES (1/93-8/95)
[Trade Weights]





Sources: IMF, International Financial Statistics, staff reports on Belarus, Lithuania, the Russian Federation, Ukraine, and staff estimates.
1/ Increase implies an appreciation.
2/ Baltics, Russia, and other FSU republics.

CHART 3
LITHUANIA
AVERAGE MONTHLY WAGES
(In U.S. dollars)



Sources: Country authorities.

(specific rates) have been increased at a faster pace than inflation. Overall, it is now expected that revenue in 1995 will amount to 24 percent of GDP, about 1/2 percent of GDP above the earlier projection (Table 6).

Progress in strengthening expenditure management and improving the composition of expenditure has been mixed. On the positive side, the structure of social expenditures has been improved (through rationalization of unemployment benefits and sick pay and streamlining of social assistance), and expenditure arrears have declined. On the other hand, cash rationing remains the basis for expenditure control, as the treasury system is still being developed. Moreover, investment expenditure has been lower than planned, while the wage bill has been higher.

3. Monetary developments

Confidence in the currency board arrangement and the exchange rate remains strong. Following the foreign exchange outflows, which occurred amidst devaluation rumors in late 1994 and early 1995, large foreign exchange inflows have resumed (Chart 4). The foreign exchange inflows have resulted in a significant monetary expansion (Table 7); in the six-month period ended September 1995, reserve money and broad money both increased by close to 20 percent (seasonally adjusted). After some increase in early 1995, interest rates again are on a declining trend, although they remain high relative to U.S. dollar rates because of residual uncertainties with respect to the exchange rate, and weaknesses in the banking system (through which transactions in securities take place). The authorities have moved to reverse the pledge (of US$30 million) of BOL foreign reserves that was made in early 1995 as collateral for external borrowing by the energy system; 1/ no other official foreign reserve pledges are currently in effect.

4. Banking sector

The underlying position of the banking sector remains weak. Bank capital has been eroded further. The number of smaller banks under bankruptcy proceedings increased to a total of 11 by October 1995 (these banks represented about 2 percent of total bank deposits). The BOL and the Government have provided liquidity support for two medium-sized banks. 2/ Most banks have yet to achieve full compliance with the prudential standards under the Commercial Bank Law enacted in December 1994, especially with respect to capital adequacy and limits on insider lending. Finally, no progress has been made towards privatizing the three dominant state-

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1/ The exchange rate pressures during the winter of 1994/95 were caused in part by this pledge.

2/ The program floors for net international reserves of the BOL incorporate a buffer of US$15 million to allow a limited lender-of-last-resort function for the BOL, consistent with the integrity of the currency board arrangement.

controlled banks. On the positive side, the liquidity situation of banks has improved since the summer of 1995, and almost all banks currently observe the reserve requirement.

After some initial hesitation when the banking sector problems emerged, the authorities recently have taken a more active stance. Since mid-1995, they have: (i) reached agreements on bank-by-bank plans for full compliance by all banks with prudential standards within given time frames; 1/ if a bank does not meet these standards as scheduled, it would be subject to sanctions (such as fines, dismissal of managers, and restrictions on operations); (ii) developed a contingency plan for intervention in the event of bank failures; under this plan, problem banks would be required to cease all operations with immediate effect; banks that are later allowed to resume operations would--to protect the integrity of the currency board arrangement--be supported by the Government rather than the BOL; (iii) imposed sanctions on several banks for non-compliance with prudential standards; (iv) formulated a bank merger policy, which prevents banks from merging unless the merged bank meets prudential regulations; (v) presented to Parliament legislation for a deposit protection scheme, to become effective on January 1, 1996, and for partial compensation for depositors in banks that will have been closed by that time; 2/ and (vi) strengthened banking supervision.

5. Other structural policies

Concerning agriculture, the average tariff on agricultural imports was reduced from 35 percent to 27 1/2 percent effective October 1, 1995, as envisaged. The tariff reduction was achieved through a broad-based reduction in the relevant rates (Table 8). When announcing this reduction, the Government expressed an intention to support agriculture through other means, and the 1996 budget proposal provides for unchanged direct budgetary

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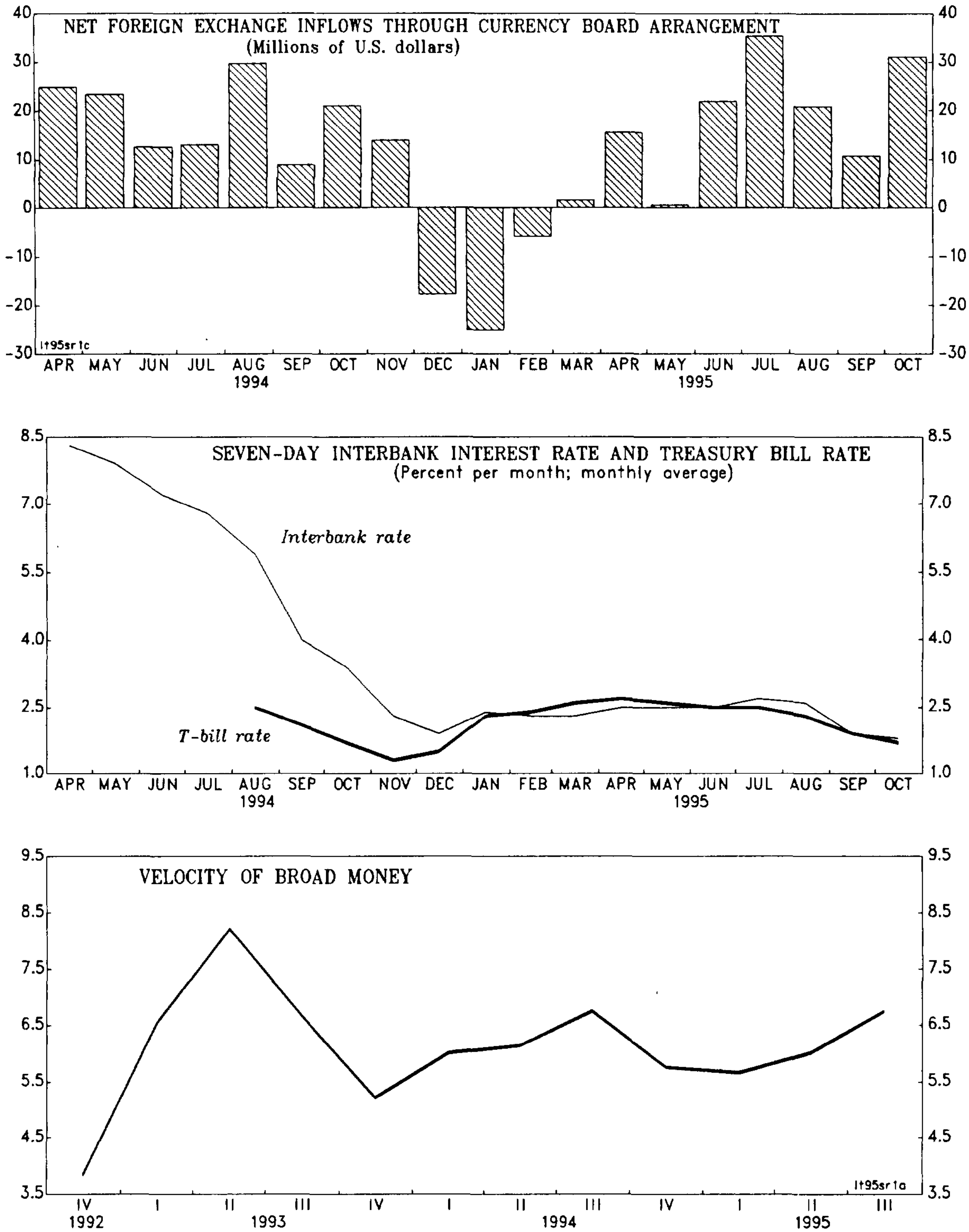
1/ Under these plans, all banks will satisfy prudential ratios in accordance with the Commercial Bank Law, as follows (percentages of capital): (a) maximum connected lending, 10 percent; (b) minimum capital adequacy ratio, 13 percent; (c) minimum liquidity ratio, 30 percent (of liabilities); (d) maximum overall open position in foreign currencies, 30 percent, and in individual currencies (except U.S. dollars), 20 percent; (e) maximum lending to a single borrower, 30 percent; and (f) minimum amount of share capital (as of July 1, 1995), equivalent to ECU 1.9 million.

2/ There is already a degree of deposit protection in Lithuania. First, deposits at the three state-controlled banks (which together account for almost half of bank deposits) are fully guaranteed by the Government under the Civil Code. Second, the Commercial Bank Law gives individual depositors claims on proceeds from liquidation of a bank--after first priority claims, including secured creditor claims, have been settled--of up to Llt 5,000.

CHART 4

LITHUANIA

MONEY, INTEREST RATES AND VELOCITY



Sources: Data provided by the Lithuanian authorities; and staff estimates.

subsidies for agriculture in relation to GDP; however, few provisions of the interventionist Agricultural Law of December 1994 have been implemented. 1/

Some headway has been made in enforcing payments discipline among energy customers. 2/ Consumer indebtedness of energy customers declined from a peak of Llt 500 million (1 1/2 percent of GDP) in April 1995 to Llt 300 million in October. This improvement reflected an intensified effort to improve payments discipline, but was helped also by seasonal factors. Payments discipline has been enforced through cut-offs and rationing of energy; in 1995, 10,000 households and 1,500 other energy customers have been subject to such sanctions. Also, the energy companies have initiated court injunctions and levied penalties on late payers.

Voucher privatization was essentially completed on July 1, 1995 (vouchers may be used for purchasing a few types of non-enterprise state assets through 1996). About one third of state assets were divested through voucher privatization. The Law on Cash Privatization, enacted in July 1995, provides for an independent privatization agency, as envisaged in the program.

Some progress has been made in legal reform. A new Bankruptcy Law is being prepared. The cumulative number of bankruptcy cases had risen to about 100 by October 1995. However, limited progress has been made in expanding the capacity of the court system, and there remains a strong emphasis on restructuring even of companies with questionable viability; in effect, by October 1995, only 6 bankruptcy cases had been completed. A new law on foreign direct investment came into effect in August 1995, allowing foreign investment in virtually all sectors. Constitutional amendments to lift the ban on foreign ownership of non-agricultural land are currently before Parliament.

1/ The Law calls for--inter alia--binding threshold prices on agricultural imports based on domestic prices (akin to import levies), credit subsidies, and guaranteed minimum prices.

2/ The lack of such discipline undermined macroeconomic stability in the 1994/95 winter season, as the non-payment of energy bills left the energy companies short of funds to pay for energy imports. The authorities' actions to ensure such imports undermined confidence in the currency board, as BOL foreign exchange reserves were pledged as collateral for foreign borrowing by energy companies, and one commercial bank was exempted from the reserve requirement to allow extension of a loan to the nuclear power plant.

III. Report on Discussions and Program for 1995/96 (October-September)

The discussions took place against the background of continued recovery, relatively low inflation, and a strong balance of payments. At the same time, the problems in the banking sector had become more acute and the energy companies' finances remained fragile. These problems have the potential to derail the recovery and lead to macroeconomic instability, and the discussions focussed on the measures needed to address the issues.

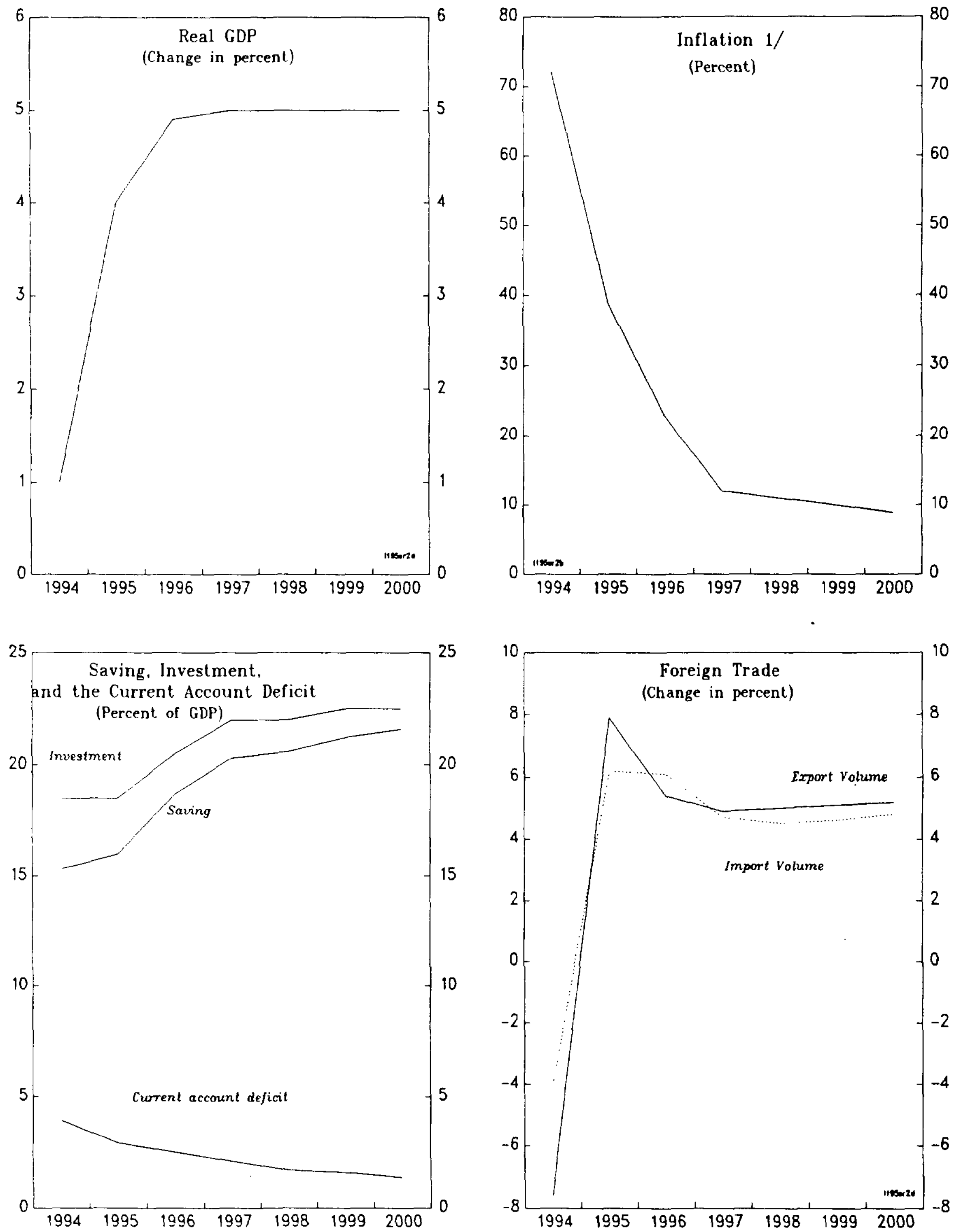
Beyond the intensified efforts to address the banking and energy sector problems, the basic stabilization and reform strategy will remain unchanged in 1995/96. The authorities have completed all preparatory steps for the key actions envisaged for implementation prior to completion of the second EFF review (Table 9). Specifically, they have taken the necessary preparatory steps to reverse the foreign exchange pledge (by end-September, they had raised US$20 million and notified the foreign bank of their intention to reverse the pledge), and have initiated cash privatization following the passing of the cash privatization law (by establishing the privatization agency and starting preparation of the list of assets to be privatized in 1996).

The targets under the program assume that a full-fledged banking crisis will be avoided; if such a crisis were to occur, its consequences for the program--including the budgetary implications--would be dealt with in consultation with the Fund. General elections are scheduled for late 1996; during the second program year, the Government will thus face political challenges in maintaining financial discipline and moving forward with structural reforms.

1. Macroeconomic outlook, 1996-2000

The macroeconomic outlook remains essentially unchanged from that expected at the time of the first EFF review. Real GDP growth is projected to increase to about 5 percent in 1996, driven in particular by a pick-up in investment, and to remain at that rate over the medium term (Chart 5). While structural reforms are expected to help increase capital productivity, the growth objectives would require some increase in the share of investment in GDP, from 20 1/2 percent of GDP in 1996 to 22-23 percent in 1997-2000. Investment would be financed increasingly from domestic resources, and the current account deficit would decline gradually as a share of GDP. Fiscal policy will play a major role in the domestic saving mobilization; while the financial deficit would decline only moderately, from 2 percent of GDP in 1996 to 1 1/2 percent of GDP in 2000, expenditure would be shifted towards investment and government saving would increase by 2 percentage points of GDP.

CHART 5
LITHUANIA
MEDIUM-TERM ADJUSTMENT FRAMEWORK, 1994-2000



Sources: Data provided by the Lithuanian authorities; and staff estimates.

Inflation in 1996 is projected at about 17 percent on an end-period basis, broadly the same as earlier expected. In the following years, inflation is projected to fall further as the initial undervaluation of the litas dissipates.

The balance of payments is projected to strengthen in 1996, owing mainly to an improvement in the capital account; the program for 1995/96 is fully financed (Table 10). The current account is projected to decline from 2 percent of GDP in 1996 to less than 1 percent of GDP in 2000. While export and import volume growth are both projected at about 5 percent per year during the period, 1/ the improvement in the overall current account deficit would stem from an increase in the surplus on the net services balance in line with the growth in trade and economic activity. The capital account is projected to show an increasing surplus, driven by foreign direct investment and private capital inflows, reflecting deepening economic integration with the EU, the forthcoming WTO membership, and an improved macroeconomic climate coupled with structural reforms (including cash privatization). Lithuania has a record of sound economic policies, a low external debt burden, and comfortable Fund debt indicators (Table 11); therefore, it can be assumed that the prospective obligations to the Fund will be fully met.

2. Monetary and fiscal policy

The authorities are committed to maintaining the currency board, at the current exchange rate peg, as the cornerstone of their stabilization strategy (paragraph 8). 2/ They indicated their determination to avoid any measures that could undermine the currency board's credibility. The reserve requirement will be enforced firmly and evenly, through strict application of penalties against banks that register shortfalls, and the definition and ratio of required reserves will remain unchanged. The authorities also indicated that they will not enter into any new foreign exchange reserve pledges.

The currency board will be supported by continued fiscal restraint. The program envisages a modest increase in the general government financial deficit (i.e., excluding net lending), from 1 1/2 percent of GDP in 1995 to about 2 percent in 1996 (paragraph 9). Combined with the planned scaling back of net lending activities as foreign assistance is channelled through the banking system, this would entail a reduction in the fiscal deficit from 3 1/2 percent of GDP in 1995 to less than 3 percent in 1996. An intensified revenue effort is projected to help increase revenue by close to 1 percent of GDP, effectively ending the declining trend in revenue which has

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1/ In the medium term, the volume of exports to other than BRO countries, which does not include energy exports, is projected to grow by 8 percent annually.

2/ In the following, all paragraph references relate to the letter for the second EFF review (Appendix I of this report).

complicated budget execution in recent years. The higher financial deficit and revenue would allow an expansion in expenditure (excluding net lending) of about 1 1/2 percent of GDP. The Government has presented to Parliament a budget for 1996 with overall parameters consistent with these objectives.

To increase tax revenue as targeted, the Government plans to introduce a number of measures centered on improvements in tax administration and broadening of tax bases, including widening of tax collection from the private sector (paragraph 10). As a result, tax revenue is expected to increase for all tax categories in 1996 (except for taxes on foreign trade, which will be affected by the lowering of import tariffs, and VAT--see below). While agreeing with the focus of the authorities' revenue effort, the staff expressed its concern about the revenue loss resulting from the Parliament's recent decision to extend the VAT exemptions for food and energy through end-1996 (these exemptions were to expire in mid-1995); the continuation of this exemption will entail a direct revenue loss equivalent to about 1/2 percent of GDP in 1996. Also worrisome is the delay in the removal of profit tax exemptions, pending decision on a narrower set of priority sectors which will continue to enjoy this tax break. Finally, the targets for wage taxes (i.e., income and profit tax, and payroll tax) are ambitious.

The planned increase in expenditure would be directed primarily towards government investment and reduction in arrears of budgetary organizations to suppliers as planned (paragraph 11). The staff noted that, to make room for these outlays, the wage bill will need to be limited through wage restraint, and that the Government should assess the scope for reduction in civil service employment as a means to limit the wage bill and restrain other current expenditure. The Lithuanian representatives concurred, but noted that the expansion in government investment would be hampered by the difficulties in preparing and managing high-quality investment projects. Also, they indicated that while the 1996 budget proposal includes a salary increase for the public sector of 11 percent (following an increase of 14 percent effective October 1, 1995), wages might increase by more as a result of the ongoing parliamentary deliberations; they committed themselves to start a review of the civil service structure by January 1996.

The authorities were mindful of the need to avoid future deficits in the social insurance fund. They pointed to the important progress already made in containing social benefits, and indicated their commitment to taking further action (paragraph 13). The budgeted increase in transfers to households--which reflects higher pensions--is expected to be fully financed through better payroll tax collection. The authorities were not willing, however, to accelerate increases in the pension age relative to the agreed schedule, citing lack of political consensus, but indicated that they would keep the issue under review.

The authorities acknowledged that the ambitious targets for wage taxes, and the banking problems, had made it pressing to identify contingency measures to protect the budget. Large additional budgetary resources might be needed to put the banking system on a sound footing. The outlays already included in the 1996 budget proposal--i.e., for the deposit protection scheme, the bank restructuring fund, and for compensation of depositors of the smaller banks that have been closed already--are modest, since it is assumed that a full-fledged banking crisis will be avoided. A recapitalization/restructuring of the banking system, which could only proceed once the overall strategy has been agreed, would likely require much larger amounts, to be mobilized through bond issues; the Government would then need to assume the interest costs on the additional debt. The Lithuanian representatives indicated that contingency measures would include cuts in lower-priority expenditure, adjustments in excise taxes, and early elimination of VAT exemptions (paragraph 12). The staff emphasized that contingency measures should be designed for implementation on short notice; in this regard, increases in excise tax rates on petrol and alcohol would be suitable. The Government would be well advised to restrain expenditure in the early part of the year, as concrete contingency measures are being decided upon.

The authorities shared the mission's concern about weaknesses in the budgeting framework, and noted their ongoing efforts to upgrade the capacity for budget preparation and implementation, including current reporting of expenditure arrears (paragraph 14).

3. Banking sector and financial reform

The authorities and the staff agreed that an urgent task in the year ahead will be to address the problems in the banking sector. To this end, the authorities will take a range of additional measures. Particularly important will be the development and implementation of a plan for a fundamental and orderly restructuring of the banking sector (paragraph 16). The authorities intend to develop this plan by March 1996 in consultation with the World Bank, the Fund, and other multilateral agencies. The plan will include a schedule for the restructuring and privatization of the state-controlled banks, restructuring or liquidation of insolvent private banks or mergers of such banks with other banks to establish viable banks, and strengthening of management capabilities of banks under the institutional development programs. The staff emphasized the need to move ahead swiftly to privatize the state-controlled banks, as soon as possible after the restructuring. Recapitalization would take place only as a last resort, be financed by the Government in order to protect the principles of the currency board, and be designed with concern for the signals sent to banks. Additional actions will include formalization of the bank merger policy, further inspection of the larger banks, reinforcement of prudential regulations (including moving as soon as possible to adopt Basle standards for capital adequacy requirements), and strengthening of the efforts to complete the ongoing bank bankruptcy proceedings.

4. Agriculture and external trade

The Lithuanian representatives reiterated their commitment to continued trade liberalization. Lithuania has started WTO membership discussions; several free trade agreements are already in place, including with the EU. The program for 1995/96 incorporates further trade reform as planned in the original program, importantly an additional reduction in agricultural import tariffs (paragraph 17). Nevertheless, the authorities expressed their general reservations about the speed of trade liberalization, noting the slower pace adopted in several neighboring countries. Also, they stressed that export bans and export tariffs only apply to five product categories which are important for environmental and health reasons, and that the restrictions could be lifted only in May 1996, after alternative mechanisms for these items--that do not distort international trade--are in place. Finally, they stressed that threshold prices for agricultural imports will not be introduced, and that they would consult with the WTO to ensure that reference prices, if introduced, would be consistent with WTO rules. The authorities also agreed to eliminate the remaining specific elements of the mixed import duties (on alcohol, sugar, and tobacco by May 1996), noting, however, the political difficulties involved. 1/

5. Energy sector

The program for 1995/96 envisages a considerable strengthening of the endeavor to address the financial problems of the energy sector (paragraph 18). First, the authorities will address the energy companies' problems of underpricing and poor revenue collection. The prices charged at the various stages of energy production and distribution will be set on a cost-recovery basis. 2/ Preliminary estimates suggest that for 1996 prices on electricity and heating would need to be increased by about 25 percent on this basis; the authorities noted that the increase would be smaller, the larger the capacity utilization at the nuclear power plant, and that they were actively seeking export markets for electricity.

The strategy for enforcing payments of energy bills and reducing consumer indebtedness to energy companies will be bolstered. Energy companies will be given the authority to cut off energy supply to delinquent customers, with the exception of a narrowly defined list of essential institutions and enterprises (such as hospitals and schools). 3/ Also, the Government will end the practice of granting exemptions from payment of

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1/ For the three products with "mixed" duties, both ad valorem and specific duties apply, with the highest of the two being the binding one.

2/ The prices charged by the Lithuanian State Power System (LSPS) were adjusted to full cost recovery in June 1995, based on the actual electricity prices charged to LSPS by the nuclear power plant at that time (which, however, did not cover costs fully).

3/ Hitherto, the decision to cut off energy supply to delinquent customers rested with a government commission.

energy bills, and budgetary organizations will avoid new energy arrears and completely eliminate their existing arrears by mid-1996. On this basis, consumer indebtedness to energy companies will be reduced to Llt 250 million by end-1995 (or half of their July 1995 level), to Llt 100 million by end-March 1996, and stay below that level thereafter. Second, the program provides for more fundamental restructuring of the energy companies, with the support of international donors, including the World Bank.

Improved payments discipline and cost recovery in the energy sector will be combined with a continued effort to protect the truly needy. Households will receive full compensation for energy outlays in excess of 20 percent of their income; the 1996 budget proposal incorporates about Llt 100 million for this purpose.

6. Privatization

The Lithuanian representatives stressed that preparations for the start of cash privatization were well underway, although the start of cash privatization had been delayed because of the practical difficulties involved. The Government will approve and publish by end-1995 the list of assets to be privatized in 1996; it was expected that the first cash sales would take place in the first quarter of 1996 (paragraph 19). In line with the program, cash privatization over the coming years will cover all assets (including the remaining state ownership in enterprises partly privatized through vouchers), except the list of strategic enterprises that will remain in government hands through 2000. The authorities stressed that this list had been reduced in February 1995, and indicated their intention to seek further reduction by March 1996 (reductions require parliamentary approval).

The staff expressed concern that the cash privatization law--which gives municipalities and ministries continued responsibility for managing public assets, and municipalities a potentially large role in privatization--could create disincentives to privatization. The Lithuanian representatives responded that they intended to review the cash privatization law in consultation with the World Bank by March 1996. This review will focus in particular on the need to consolidate the responsibility for privatization. Also, the review will seek to establish concrete privatization targets for the period through end-1997 (i.e., beyond the period of the EFF-supported program).

7. Institutional reform, legal reform, and economic management and data

While Lithuania has made rapid progress in transferring ownership to the private sector, the change in ownership has not been supplemented to a sufficient degree by policies to promote hard budget constraints and economic restructuring. To this end, the authorities plan further progress in adjusting laws and regulations to the requirements of a market economy (paragraph 20). A broad-based program has been started, following the signing of the EU Association Agreement in June this year, to harmonize the legal framework with those of EU countries. In 1995/96, specific initiatives in the area of legal and institutional reform will include: (i) introduction of a new system of enterprise accounting, consistent with international standards; (ii) establishment of a system for registration of property rights and loan collateral; (iii) introduction of new bankruptcy legislation by early 1996 to speed up bankruptcy proceedings, inter alia, through better prioritization of creditors, and further strengthening of the court system; and (iv) amendments to the competition legislation, to allow the State Price and Competition Office to focus on the more important cases. Finally, the improvements in the economic data base are ongoing, with technical assistance from the Fund and other bilateral and multilateral donors; future efforts should concentrate on improving customs data collection and further strengthening the enterprise survey.

8. Program monitoring

The performance criteria relating to the maintenance of the currency board arrangement and no accumulation of external payments arrears by the Government have been retained (paragraph 21 and Appendix Table 1). Also, the second annual arrangement includes a performance criterion on the reduction of agricultural import tariffs to at most 20 percent by end-September 1996. Quantitative performance criteria for end-December 1995 and end-March 1996, as well as indicative targets for end-June 1996 and end-September 1996, have been set for the same variables as in the original program. The external borrowing ceilings have been rebased to take account of developments through end-September 1995. For the purpose of program monitoring, the definition of general government net lending has been broadened to include, as provisioning, 25 percent of government guarantees of domestic bank lending up to a total of Llt 100 million, and 100 percent of guarantees in excess of that amount, as well as government deposits placed with illiquid banks as part of rescue operations. Finally, in light of the importance of addressing the financial difficulties of the energy sector, new benchmarks have been added in the form of ceilings on consumer indebtedness for electricity, heating, and gas. The third review is scheduled for completion in June 1996; in the context of that review, understandings will be reached on performance criteria for end-June and end-September 1996 and on specification of the fourth review under the EFF arrangement. Table 12 summarizes structural policies under the 1995/96 program.

IV. Staff Appraisal

Since independence was regained, Lithuania has moved ahead swiftly to establish a market-based economy. The first phase of stabilization and liberalization has now been completed: inflation has remained relatively low since mid-1993 and economic recovery began in 1994; privatization has moved forward faster than in neighboring countries; domestic prices have been virtually fully decontrolled; and external trade has been liberalized. This progress has provided a sound basis for sustained economic growth in the years ahead.

While the basic macroeconomic outlook is favorable, downside risks are considerable. In 1996, the Government will face a mounting challenge in protecting the stabilization gains and safeguarding the recovery. The upcoming elections, the potential banking crisis, and the fragile finances of the energy sector will all compound this challenge. Every effort will be required to keep the economic program on course.

The currency board arrangement, at the current exchange rate, should remain in place. Its simplicity and transparency serve as important underpinnings of financial stability. To continue to realize fully these benefits, the reserve requirement should remain unchanged and be enforced consistently, and no new pledges of central bank foreign exchange reserves as collateral for external borrowing should be made.

The maintenance of fiscal restraint is critical in supporting financial stabilization and private-sector development. To this end, the program rightly emphasizes improved tax collection. The revenue target for 1996 envisions an end to the decline in the revenue-to-GDP ratio that has complicated fiscal policy implementation over the last several years. Higher revenue should be utilized to expand government investment in infrastructure and settle arrears to suppliers by budgetary organizations. A more comfortable revenue situation must not be used to expand the public sector wage bill. The authorities should complete their work on identifying concrete budgetary contingency measures and, in the meantime, restrain expenditure as a safeguard against higher outlays relating to the banking sector.

The authorities must press ahead to address the banking problems. In this regard, the staff is encouraged that broadly appropriate prudential standards have been put in place, and that bank-by-bank plans for compliance with these standards have been established; the prudential standards must now be strictly enforced in line with these plans. Looking further ahead, the underlying weaknesses of the banking system need to be addressed; as a first step, Lithuania should develop rapidly, in cooperation with the World Bank and the Fund, a bank restructuring plan. The authorities will need to take a firm approach towards dealing with banks that fail, with due concern for the signals that are sent to the banking community; public funds should be used to recapitalize banks only as a last resort. The staff would encourage the authorities to move towards Basle standards for capital adequacy requirements as the situation in the banking system stabilizes.

The momentum in trade reform must not be lost in the period up to the elections. Agricultural policy should aim to facilitate the restructuring of the economy; any measures to support agriculture that distort relative prices or undermine budgetary targets should be avoided. Further slippage in removing export bans and tariffs should not be allowed, and the authorities should refrain from introducing threshold prices or reference prices for agricultural imports in a manner that distort international trade, and should eliminate the specific element of the mixed import duties as planned.

The strengthened effort to improve the finances of the energy companies is a key element of the program. The staff supports the general strategy adopted, which focusses on cost recovery and revenue collection for the energy companies (including from government agencies) as short-term measures, combined with fundamental improvements in efficiency over the medium term. The staff endorses the planned measures to alleviate the impact of these actions on the poor.

The pace of privatization must not be allowed to decelerate. The Government should set an ambitious timetable for completion of cash-based privatization, and develop laws and institutions to facilitate privatization. Except for narrowly defined strategic enterprises, all government assets--including holdings in commercial banks and energy companies--should be divested.

The continued privatization needs to be complemented by actions to further strengthen the institutions and laws necessary for the effective functioning of a market economy. The recently enacted law on foreign direct investment is a welcome step in this direction. Firm application of such laws and regulations will be critical to foster restructuring and growth. The efforts to improve economic management and data should continue.

The staff believes that the proposed program for 1995/96 addresses appropriately the key problems facing Lithuania. Undoubtedly, risks exist for the year ahead; the course of events in the banking sector is uncertain, even with the efforts being made to minimize the potential for a full-fledged crisis, and this year's heating season will again pose a challenge to the Government's resolve to strengthen payments discipline among energy customers. Nevertheless, the program, if fully implemented, would help complete another stage in the transition to a stable market economy. The authorities' commitment to the reforms remains firm, and they have amply demonstrated, on earlier occasions, an ability to take politically difficult action. The staff will remain in close contact with the authorities concerning the implementation of the program, in particular as regards the efforts to address the banking sector problems. On this basis, the staff recommends that the second review under the EFF arrangement be completed.

V. Proposed Decision

The following draft decision is proposed for adoption by the Executive Board:

Second Review Under the Extended Arrangement

1. The Republic of Lithuania has consulted with the Fund in accordance with paragraph 3(d) of the extended arrangement for the Republic of Lithuania (EBS/94/199, Supplement 2) and paragraph 4 of the letter dated September 29, 1994 from the Prime Minister and the Governor of the Bank of Lithuania to which the Memorandum on Economic Policies of the Government of the Republic of Lithuania is attached, in order to review progress made in the implementation of the policies and measures described in that letter and the attached Memorandum, as supplemented and modified by the letter of June 22, 1995, and to reach understandings on the phasing of purchases and the frequency of reviews for the second year of the arrangement.

2. The letter from the Prime Minister and the Governor of the Bank of Lithuania dated November 28, 1995 shall be attached to the extended arrangement for the Republic of Lithuania, and the letter of September 29, 1994 and the attached Memorandum, as amended, shall be read as supplemented and modified by the letter of November 28, 1995 and the attached Table 1.

3. Accordingly:

(i) paragraph 2(a) of the extended arrangement shall read as follows:

"(a) Purchases under this extended arrangement shall not, without the consent of the Fund, exceed the equivalent of SDR 20.70 million until February 15, 1995, the equivalent of SDR 31.05 million until May 15, 1995, the equivalent of SDR 41.40 million until August 15, 1995, the equivalent of SDR 51.75 million until November 15, 1995, the equivalent of SDR 62.10 million until February 15, 1996, the equivalent of SDR 72.45 million until May 15, 1996, the equivalent of SDR 82.8 million until August 15, 1996, and the equivalent of SDR 93.15 million until November 15, 1996."

(ii) paragraphs 2(b) and 2(c) shall be deleted and a new paragraph 2(b) shall be added as follows:

"(b) The right of the Republic of Lithuania to make purchases during the third year shall be subject to such phasing as shall be determined."

(iii) the word "or" shall be inserted at the end of paragraph 3 (a)(v).

(iv) a new paragraph 3(a)(vi) shall be added as follows:

"(vi) the limit on the stock of consumer indebtedness for electricity, heating, and gas described in paragraph 18 of the letter of November 28, 1995 and the attached Table 1".

(v) paragraph 3(c) shall be supplemented as follows:

"(c) after September 30, 1995, if the limit on the weighted average tariff rate described in paragraph 46 and in Annex V of the

Memorandum is not observed and after September 30, 1996, if the limit on the weighted average tariff rate described in paragraph 17 of the letter of November 28, 1995 and the attached Table 1 is not observed."

(vi) paragraph 3(d) of the extended arrangement shall be amended to read as follows:

"(d) After May 14, 1995, November 14, 1995, and May 14, 1996, until the reviews contemplated in the letter of September 29, 1994, as amended, and the letter of November 28, 1995 are completed."

(vii) the performance criteria referred to in paragraphs 3(a)(i) to 3(a)(v) for December 31, 1995 and March 31, 1996 shall be, with respect to the second year of the arrangement, as specified in the letter of November 28, 1995 and the attached Table 1;

4. The Fund decides that the second review contemplated in paragraph 3(d) of the extended arrangement for the Republic of Lithuania is completed.

Table 1. Lithuania: Fund Transactions During Period of EFF Arrangement

	1994	1995		1996				1997		
	Oct.-Dec.	Jan.-Sept.	Oct.-Dec.	Jan.-Mar.	Apr.-Jun.	Jul.-Sep.	Oct.-Dec.	Jan.-Mar.	Apr.-Jun.	Jul.-Sep.
	(In millions of SDRs)									
Purchases	20.70	31.05	10.35	10.35	10.35	10.35	10.35	10.35	10.35	10.35
Ordinary resources										
Tranche policies	--	--	--	--	--	--	--	--	--	--
Special facilities	20.70	31.05	10.35	10.35	10.35	10.35	10.35	10.35	10.35	10.35
Repurchases	--	--	--	2.16	2.16	5.46	7.12	7.76	7.76	7.76
Total Fund credit outstanding (end of period)	134.55	165.60	175.95	184.14	192.33	197.22	200.45	203.04	205.63	208.22
Tranche policies	62.10	62.10	62.10	59.94	57.78	52.32	45.20	37.44	29.68	21.92
Special facilities	72.45	103.50	113.85	124.20	134.55	144.90	155.25	165.60	175.95	186.30
	(In percent of quota)									
Total Fund credit outstanding (end of period)	130.0	160.0	170.0	177.9	185.8	190.6	193.7	196.2	198.7	201.1
Tranche policies	60.0	60.0	60.0	57.9	55.8	50.6	43.7	36.2	28.7	21.1
Special facilities	70.0	100.0	110.0	120.0	130.0	140.0	150.0	160.0	170.0	180.0

Source: IMF, Treasurer's Department.

Table 2. Lithuania: Schedule of Purchases for 1995/96
Under Extended Arrangement

Amount	Scheduled availability date	Conditions
SDR 10.35 million	On or after February 15, 1996	Observance of end-December 1995 performance criteria
SDR 10.35 million	On or after, May 15, 1996	Observance of end-March 1996 performance criteria and completion of third EFF review
SDR 10.35 million	On or after August 15, 1996	Observance of end-June 1996 performance criteria
SDR 10.35 million	On or after November 15, 1996	Observance of end-September 1996 performance criteria and completion of fourth EFF review 1/

1/ In consultation with the authorities, the deadline for the fourth EFF review will be specified in the context of the third EFF review.

Table 3. Lithuania: Outcomes in Relation to Performance Criteria During First Annual EFF-Supported Program, October 1994 - September 1995 1/

Variable and Periods	Performance Criteria/ Indicative Targets		Outcome	
I. Maintenance of exchange rate under currency board arrangement; Duration of the extended arrangement			Observed	
II. Full foreign exchange cover for currency board liabilities; Duration of the extended arrangement			Observed	
III. Minimum levels for total reserve deposits of banks with the Bank of Lithuania, calculated as for the reserve maintenance period and expressed as a percentage of eligible commercial bank liabilities:	9		Observed	
IV. Limit on tariff rates for major agricultural goods; September 30, 1995 (in percent):	27 1/2		Observed	
V. No accumulation of external payments arrears by the Government			Observed	
	(In millions of Litai)			
VI. Limits on the general government financial balance; from July 1, 1994 to:				
December 31, 1994	-110		-157	
March 31, 1995	-275		-166	
June 30, 1995	-400		-264	
September 30, 1995	-545		-407	
VII. Limits on general government net lending; from July 1, 1994 to:				
December 31, 1994	500		384	
March 31, 1995	900		373	
June 30, 1995	930		495	
September 30, 1995	1,080		709	
	(In millions of U.S. Dollars)			
	Minimum limits			
VIII. Minimum net international reserves of the Bank of Lithuania				
December 31, 1994	-112		-70	
March 31, 1995	-118		-77	
June 30, 1995	-111		-105	
September 30, 1995	-123		-119	
	Maximum limits			
IX. Limits on contracted public and publicly guaranteed medium- and long-term external debt; from June 30, 1994 to:	1-12 yr maturity	1-5 yr maturity	1-12 yr maturity	1-5 yr maturity
December 31, 1994	165	50	51	14
March 31, 1995	200	75	94	45
June 30, 1995	250	100	158	53
September 30, 1995	275	125	160	59
X. Limit on government debt of up to one year; Duration of the extended arrangement	--		--	

Sources: Memorandum of Economic Policies (MEP) of September 29, 1994; Letter for First EFF Review of June 22, 1995; and data and information provided by the authorities.

1/ Performance criteria for end-December 1994 and end-March 1995 are those included in the MEP of September 29, 1994, and performance criteria for end-June 1995 and end-September 1995 are those included in the Letter for First EFF Review of June 22, 1995. Detailed definitions are included in the Annexes to the MEP.

Table 4. Lithuania: Status of Structural Policies Under First Annual EFF-Supported Program, October 1994 - September 1995. 1/

Measure	Date/period of implementation	Status September 1995
I. Financial sector		
Further strengthening of bank regulation and supervision	Throughout 1994/95	Legislation adopted; efforts underway to strengthen regulation and supervision
Training of commercial bank staff; institutional development	Throughout 1994/95	Ongoing
Increase of minimum bank capital	Beginning 1995	Done
Redefine bank capital to include retained earnings as capital	End-1994	Done
Passage of Commercial Bank Law	Fall 1994	Done
Government to pay the remainder of its capital subscription for shares in state-controlled banks	1994/95	Done
II. Budgetary policies		
Implementation of Treasury project	Throughout 1994/95	On schedule
Strengthening of tax administration	Throughout 1994/95	Done
Introduction of tax deductibility of loan loss provisions of commercial banks	Fall 1994	Done
Improved collection of payroll taxes	Fall 1994	Done
All import duties and taxes to be paid in full before Customs Administration releases goods	Beginning 1995	Done
Preparation of three-year public investment program	Beginning 1995	Done
Strengthening of budget procedures; development of three-year budget outlook	Beginning 1995	In progress; fiscal policy unit formed at the Ministry of Finance
Further reform of profit and income tax regimes	Beginning 1995	Underway; profit tax regime remains unchanged
Remove remaining temporary VAT exemptions	June 1995	Exemptions extended through end-1996
Amendment of pension law, accelerated increase in pension age, and revised pension formula	Fall 1994	Pension law amended, pension age increased, and pension formula revised

Table 4. (continued). Lithuania: Status of Structural Policies Under First Annual EFF-Supported Program, October 1994 - September 1995. 1/

Measure	Date/period of implementation	Status September 1995
Introduction of flat-rate unemployment benefit unrelated to past earnings	Fall 1994	Done
Reform of social assistance benefits; reduction of number of benefits and introduction of means-testing	Fall 1994	Done
Improve system of sick pay	June 1995	Done
III. Privatization		
Evaluation of remaining state ownership and the scope for further privatization	Fall 1994	List of enterprises that will remain in governments hands until year 2000 shortened in February 1995
Conclude voucher-based privatization	End-1994	Completed on July 1, 1995, with the exception of a limited set of non-enterprise objects
Introduction of legislation allowing for second round of privatization based on cash payments	Fall 1994	Legislation presented in May 1995
Passage of new privatization legislation	Fall 1994	Passed in July 1995
Passage of revised direct foreign investment law	Fall 1994	Passed in August 1995
Initiation of cash-based program to privatize remaining state property	Beginning 1995	Initiated
IV. Other legal, institutional, and sectoral reforms		
Continued land restitution	Throughout 1994/95	Land registers being established as a preparatory step.
Corporatization of remaining state enterprises	Fall 1994	Done in part
Abolish state stock enterprise as legal enterprise form	March 1995	Done
Reform of mortgage legislation and establishment of land registry	June 1995	Underway
Further amendments to the Bankruptcy Law	End-1994	Full revision of Bankruptcy Law underway; expected for completion by early 1996
Introduction of amended law on competition policy, allowing for breaking up enterprises with excessive market power	June 1995	Underway; focus on harmonization with EU standards
Continuation of work to restructure the energy sector	Throughout 1994/95	Underway

Table 4. (concluded). Lithuania: Status of Structural Policies Under First Annual EFF-Supported Program, October 1994 - September 1995. 1/

Measure	Date/period of implementation	Status September 1995
Discontinue all subsidies on energy, except for household heating	End-1994	Done; in addition, household heating prices increased to full cost recovery effective June 1995 2/ (compared to program target of June 1996)
Continuation of work to restructure the agricultural sector	Throughout 1994/95	Discussion on World Bank Agricultural Project underway
Initiation of program to restructure the housing and transportation sectors	Beginning 1995	Legislation amended to facilitate private home-ownership; virtually full privatization of housing undertaken. Limited progress in transport sector reform
Remove all remaining export tariffs and QRs	End 1994	Done in part; export bans on five product categories and some export taxes remain
Production of trade statistics based on customs data; transfer of responsibility for balance of payments data from MOE to BOL; strengthening of procedures to produce national accounts data		Done

Source: Memorandum of Economic Policies of September 29, 1994; and information provided by the Lithuanian authorities.

1/ Includes key actions, other than performance criteria and benchmarks.
2/ Based on electricity prices charged by the nuclear power plant to Lithuania State Power System at that time.

Table 5. Lithuania: Key Economic and Financial Indicators

	1993	1994	1995		1996		1997	1998	1999	2000
			First Review	Second Review	First Review	Second Review		Projections		
					(Percentage changes from previous period)					
Real GDP	−24.2	1.0	5.3	4.0	5.0	4.9	5.0	5.0	5.0	5.0
Real domestic demand	...	0.7	4.3	3.1	4.3	5.4	4.6	5.1	4.8	4.7
Consumer prices										
Period average	410.4	72.1	36.5	38.8	18.5	22.7	12.0	11.0	10.0	9.0
End of period	188.8	45.0	26.0	32.6	17.7	17.1	...	...	...	...
Broad money	...	63.6	23.3	32.6	26.6	38.8	...	...	...	...
Reserve money	...	61.9	10.1	28.6	22.7	25.4	...	...	...	...
Currency in circulation	...	69.0	10.2	34.2	24.8	22.5	...	...	...	...
Velocity of broad money 1/	...	5.8	6.7	6.2	6.5	5.8	...	...	...	...
Money multiplier 1/	2.4	2.4	2.7	2.5	2.8	2.8	...	...	...	...
Deposit interest rate 2/	77.6	19.4	...	...	...	...	...	...	...	...
Lending interest rate 2/	91.4	33.0	...	...	...	...	...	...	...	...
Real merchandise exports	31.4	−7.6	12.9	7.9	6.1	5.4	4.9	5.0	5.1	5.2
Real merchandise imports	−17.1	−4.1	9.6	6.2	4.7	6.1	4.7	4.5	4.6	4.8
Merchandise terms of trade	−47.6	4.0	−0.7	−1.7	0.2	2.5	−0.1	0.7	−0.2	0.9
					(Percent of GDP)					
Gross national saving	18.1	15.3	16.6	16.0	17.5	18.7	20.3	20.6	21.2	21.6
General Government	3.8	1.0	2.3	2.0	2.4	2.3	3.5	4.0	4.5	4.5
Other	14.3	14.3	14.3	14.0	15.1	16.4	16.8	16.6	16.7	17.1
Gross investment	22.7	18.5	19.5	18.5	20.0	20.5	22.0	22.0	22.5	22.5
General Government	3.2	3.0	3.7	3.1	4.4	4.2	5.2	5.7	6.2	6.2
Other	19.5	15.5	15.8	15.4	15.6	16.3	16.8	16.3	16.3	16.3
External current account (incl transfers)	−4.6	−3.2	−2.9	−2.5	−2.5	−1.8	−1.8	−1.4	−1.3	−0.9
General Government financial balance	2.4	−1.5	−1.3	−1.5	−1.9	−1.9	−1.7	−1.6	−1.6	−1.6
General Government net lending	5.5	2.6	2.1	1.8	1.0	0.9	0.6	0.6	0.4	0.3
General Government borrowing requirement	3.1	4.2	3.4	3.4	2.9	2.9	2.4	2.2	2.0	1.9
					(In millions of litai at current prices)					
Gross domestic product	12,219	22,214	32,243	31,869	40,123	41,438	49,144	57,974	67,498	78,279
					(In millions of U.S. dollars)					
Gross domestic product	2,863	5,588	8,061	7,967	10,031	10,359	12,286	14,494	16,875	19,570
Current account (incl transfers)	−131	−178	−232	−198	−255	−189	−216	−201	−214	−183

Sources: Staff estimates; and projections.

1/ Level in final quarter of calendar year.
2/ In percent; weighted average of rates at commercial banks in December; 1−3 months' maturity.

Table 6. Lithuania: Summary of General Government Operations 1/

	1993	1994	1995		1996		1997	
	Actual	Actual	EFF 2/	Revised	EFF 2/	Revised	EFF 2/	Revised
				(In millions of Litai)				
Total revenue	3,473	5,472	7,560	7,655	10,000	10,225	12,563	12,789
Tax revenue	3,222	5,315	7,464	7,550	9,879	10,136	12,420	12,627
Income and profits	1,257	1,742	2,368	2,252	3,170	3,171	4,102	4,053
Payroll tax	774	1,481	1,839	1,947	2,386	2,783	2,826	3,296
GET/VAT & excises	972	1,578	2,642	2,788	3,562	3,537	4,590	4,519
Other taxes	219	514	615	563	760	645	903	758
Nontax revenue	251	157	97	105	120	89	143	162
Expenditure and net lending	4,070	6,508	8,675	8,602	11,172	11,416	13,675	13,948
Expenditure	3,402	5,920	7,986	8,022	10,766	11,024	13,358	13,638
Current expenditure	3,011	5,252	6,806	7,024	9,014	9,263	10,861	11,086
Wages and Salaries	683	1,468	1,861	2,271	2,646	2,999	3,289	3,580
Transfers	1,109	1,829	2,735	2,372	3,629	3,375	4,326	4,027
Subsidies	163	293	213	257	239	272	255	281
Other	1,052	1,641	1,883	2,040	2,328	2,439	2,766	2,951
Interest	3	23	115	83	172	178	224	248
Investment	392	668	1,179	998	1,752	1,761	2,498	2,552
Other Balances 3/	...	61	21	--	--	--	--	--
Discrepancy 4/	-110	-53	--	121	--	--	--	--
Financial balance	291	-334	-404	-488	-766	-799	-795	-850
Net Lending	668	588	689	580	406	392	317	310
Fiscal balance	-377	-922	-1,094	-1,068	-1,172	-1,191	-1,112	-1,160
Borrowing requirement	377	922	1,094	1,068	1,172	1,191	1,112	1,160
Foreign financing	841	482	680	867	436	430	342	342
Domestic financing	-464	440	414	201	736	761	770	818
Bank financing 5/	-563	329	47	-139	285	365	321	321
Of which: Treasury Bills	--	206	206	164	285	196	321	321
Privatization receipts	99	67	92	52	150	142	70	118
Treasury Bills (nonbanks)	--	44	275	288	301	254	380	380
				(In percent of GDP)				
Total revenue	28.4	24.6	23.4	24.0	24.9	24.7	26.4	26.0
Tax revenue	26.4	23.9	23.1	23.7	24.6	24.5	26.1	25.7
Income and profits	10.3	7.8	7.3	7.1	7.9	7.7	8.6	8.2
Payroll tax	6.3	6.7	5.7	6.1	5.9	6.7	5.9	6.7
GET/VAT & excises	8.0	7.1	8.2	8.7	8.9	8.5	9.6	9.2
Other taxes	1.8	2.3	1.9	1.8	1.9	1.6	1.9	1.5
Non-tax revenue	2.1	0.7	0.3	0.3	0.3	0.2	0.3	0.3
Expenditure and net lending	33.3	29.3	26.9	27.0	27.8	27.5	28.7	28.4
Expenditure	27.8	26.7	24.8	25.2	26.8	26.6	28.0	27.8
Current expenditure	24.6	23.6	21.1	22.0	22.5	22.4	22.8	22.6
Wages and Salaries	5.6	6.6	5.8	7.1	6.6	7.2	6.9	7.3
Transfers	9.1	8.2	8.5	7.4	9.0	8.1	9.1	8.2
Subsidies	1.3	1.3	0.7	0.8	0.6	0.7	0.5	0.6
Other	8.6	7.4	5.8	6.4	5.8	5.9	5.8	6.0
Interest	--	0.1	0.4	0.3	0.4	0.4	0.5	0.5
Investment	3.2	3.0	3.7	3.1	4.4	4.2	5.2	5.2
Other Balances 3/	--	0.3	0.1	--	--	--	--	--
Discrepancy 4/	-0.9	-0.2	--	0.4	--	--	--	--
Financial balance	2.4	-1.5	-1.3	-1.5	-1.9	-1.9	-1.7	-1.7
Net Lending	5.5	2.6	2.1	1.8	1.0	0.9	0.7	0.6
Fiscal balance	-3.1	-4.2	-3.4	-3.4	-2.9	-2.9	-2.3	-2.4
Borrowing requirement	3.1	4.2	3.4	3.4	2.9	2.9	2.3	2.4
Foreign financing	6.9	2.2	2.1	2.7	1.1	1.0	0.7	0.7
Domestic financing	-3.8	2.0	1.3	0.6	1.8	1.8	1.6	1.7

Sources: Data provided by Lithuanian Authorities and Staff Projections.

1/ Includes the State Budget, Municipal Budgets, Privatization Funds, and the Social Security Fund.

2/ First EFF review.

3/ Balances of budgetary organizations not recorded in the above the line numbers, but reflected in below the line estimates.

4/ Discrepancy between above and below the line estimates of the financial balance.

5/ Differs from the definition of net credit to Government in the monetary accounts.

Table 7. Summary Monetary Accounts, December 1993–September 1996
(In millions of litai, end of period)

	1993 Dec.	1994 Dec.	1995 Mar.	1995 June	1995 Sep.	1996 Sep.
		Monetary authorities				
Net Foreign Assets 1/	1,320	2,091	2,001	1,975	2,422	3,177
Gold	241	248	248	248	248	248
Convertible currencies	885	1,676	1,585	1,728	2,174	2,929
Nonconvertible currencies	194	168	168	--	--	--
Net Domestic Assets	-203	-285	-272	-109	-251	-537
Net credit to Government	-93	-60	-42	-39	-118	-118
Credit to banks	292	157	147	153	168	193
Credit to private sector	1	6	6	7	12	12
Other items, net	-404	-388	-383	-229	-312	-624
Reserve Money	1,116	1,807	1,729	1,867	2,171	2,640
Currency outside the central bank	835	1,411	1,300	1,525	1,728	2,108
Deposit money banks' deposits	281	391	423	335	434	523
Reserves in litai	198	259	254	182	269	324
Required reserves in foreign currency	84	132	169	153	165	199
Private deposits	--	5	6	7	9	9
		Monetary survey				
Net Foreign Assets	1,586	2,148	1,981	1,960	2,606	3,273
Net Domestic Assets	1,087	2,224	2,512	2,903	2,833	3,903
Net claims on Government	-407	-541	-684	-737	-915	-640
Credit to nonfinancial public enterprises	409	399	346	291	195	195
Credit to private sector	1,394	3,016	3,446	3,731	3,914	5,211
Other items, net	-310	-649	-594	-381	-361	-862
Broad Money	2,673	4,373	4,493	4,863	5,439	7,176
Currency outside banks	791	1,334	1,251	1,468	1,668	2,096
Deposits	1,881	3,039	3,242	3,395	3,771	5,080
Memorandum items:						
Reserve money (quarterly percent change)	...	6.5	-4.3	8.0	16.3	...
Broad money (quarterly percent change)	...	13.2	2.7	8.2	11.8	...
Money multiplier	2.4	2.4	2.6	2.6	2.5	2.7
Reserve ratio (percent, end of month)	15.0	12.9	13.1	9.9	11.5	10.3
Quarterly inflation rate (CPI, end of period)	21.7	10.5	11.4	4.8	5.2	3.0
Velocity of broad money	...	5.8	5.7	6.0	6.7	6.6
Derivation of NIR under the EFF program (in millions of US$) 1/						
Net international reserves	...	-70	-77	-105	-119	...
Gross foreign assets (GFA)	...	588	572	609	739	...
Litai liabilities	...	425	392	431	517	...
Foreign exchange liabilities	...	233	257	253	311	...
Of which, use of Fund credit	...	195	210	211	249	...
Encumbered assets (EA)	...	...	...	30	30	...
Currency board cover ratio ((GFA–EA)/litai liabilities)	...	...	1.46	1.34	1.37	...

Source: Bank of Lithuania; and staff projections.

1/ Program definitions for net foreign assets (NFA) and net international reserves (NIR) of the Bank of Lithuania differ in that NFA exclude the portion of Fund drawings which is allocated towards import financing through the State Liabilities Commission (see Annex II of the MEP, EBS/94/199, for the detailed definition of NIR).

Table 8. Lithuania: Agricultural Import Tariffs

Product group	HS codes	Weight 1/	Previous Tariffs 2/	Current Tariffs 3/
Sausages	1601	22	15	14
Meat	0201–0205, 0209–0210	20	30	30
Milk and dairy products	0401–0404	16	30	20
Butter	0405	16	50	45
Sugar	1701–1702	13	70 4/	35 5/
Eggs	0407–0408	7	35	30
Potatoes	0701	3	25	20
Poultry	0207	3	25	20
Weighted Average		100	35	27 1/2

Sources: Information provided by the authorities; and staff calculations.
1/ Normalized weights derived from the consumer price index, as specified in the performance criterion on agricultural tariffs (Attachment II, Annex V, EBS/94/199, 10/3/94).
2/ These tariff rates were in effect prior to October 1, 1995.
3/ These tariff rates entered into force on October 1, 1995.
4/ The tariff rate for sugar was 70 percent ad valorem, but not less than 0.8 Llt per kg.
5/ The tariff rate for sugar is 35 percent ad valorem, but not less than 0.75 Llt per kg.

Table 9. Lithuania: Status of Key Actions Planned for Implementation Before Second EFF Review

Action		Status September 1995
(i)	Implement plan to reduce arrears of energy consumers, and confirm that no new energy arrears of budgetary organizations have arisen.	Done. A Government commission has established targets for reduction in arrears, as well as enforcement mechanisms. No new arrears of budgetary organizations have arisen.
(ii)	Reversal of US$20 million (cumulative) of the pledge of US$30 million of central bank reserves (made as collateral for foreign bank borrowing by the energy sector) by end-September 1995	The Government had taken the necessary preparatory steps within its purview; i.e., raising US$20 million and notifying the foreign bank of its intention to reverse the pledge.
(iii)	Initiate cash privatization, provided that the requisite legislation is passed by Parliament	Preparatory steps taken: law passed in July 1995; separate privatization agency has been established; and the privatization list for 1996 is being prepared.
(iv)	Review, in consultation with Fund staff, the operation of the system of non-binding reference prices for agricultural imports, based on international prices.	Done. The amendment of the Agricultural law to provide for reference prices (replacing the planned binding threshold prices based on domestic prices) still before Parliament.

Sources: Letter of the Government of Lithuania for the First EFF Review, dated June 22, 1995; and information provided by the authorities.

Table 10. Lithuania: Balance of Payments, 1993–2000

	1993	1994	1995 First Review	1995 Proj.	1996 First Review	1996 Proj.	1997	1998	1999	2000
	(In millions of U.S. dollars)									
Trade balance	–283	–307	–329	–358	–329	–358	–390	–382	–406	–387
Exports	1,709	1,930	2,331	2,249	2,659	2,577	2,837	3,098	3,377	3,685
East 1/	993	1,067	1,293	1,195	1,505	1,331	1,451	1,556	1,660	1,771
Of which: energy	337	242	345	283	436	305	321	338	357	376
West 1/	716	863	1,038	1,054	1,154	1,246	1,386	1,542	1,717	1,914
Imports	1,992	2,238	2,661	2,608	2,987	2,935	3,226	3,479	3,783	4,072
East	1,472	1,513	1,783	1,710	2,020	1,877	2,047	2,186	2,326	2,476
Of which: energy	901	664	826	746	941	768	826	871	918	969
West	520	725	877	898	967	1,058	1,179	1,293	1,457	1,596
Services (Net)	31	55	16	69	11	70	76	82	93	103
Of which: interest	10	–2	–1	5	–10	–2	–1	1	6	11
Transfers	120	74	82	91	63	97	98	99	100	101
Official	108	60	66	75	46	80	80	80	80	80
Private	12	14	16	16	17	17	18	19	20	21
Current account	–131	–178	–232	–198	–255	–189	–216	–201	–214	–183
(Without official transfers)	–239	–238	–298	–273	–301	–271	–296	–281	–294	–263
Capital account	215	202	281	307	375	355	382	397	418	411
Foreign direct investment	23	60	60	55	106	101	115	125	135	145
Other private capital	95	125	90	80	145	135	145	155	165	195
Short–term credits (net)	–15	–81	–62	–79	––	–22	–11	–22	–25	–42
Medium– and long–term loans	112	98	193	252	124	141	133	139	143	113
Disbursements	112	98	232	290	130	147	200	150	220	170
Amortization	––	––	38	38	6	6	67	11	77	57
Other capital movements (net)	––	––	––	––	––	––	––	––	––	––
Errors and omissions	72	116	––	––	––	––	––	––	––	––
Overall balance	156	141	49	109	120	167	166	196	205	228
Financing	–156	–141	–49	–109	–120	–167	–166	–196	–205	–228
NFA of banking system 2/	–156	–141	–49	–109	–120	–167	–166	–196	–205	–228
Central Bank 2/	–206	–193	–34	–86	–113	–156	–154	–180	–185	–204
Fund financing	98	67	58	63	34	37	––	–31	–18	–31
Purchases	98	67	58	63	58	63	47	––	––	––
Repurchases	––	––	––	––	24	26	47	31	18	31
Reserves (–=increase)	–304	–260	–92	–149	–147	–193	–154	–149	–167	–173
Foreign exchange	–310	–260	–92	–149	–147	–193	–154	–149	–167	–173
Issue Department	...	...	–57	–138	–103	–153	–140	–131	–145	–148
Banking Department	...	...	–35	–11	–44	–39	–14	–18	–22	–25
Deposit Money Banks	51	52	–15	–23	–7	–11	–12	–16	–20	–24
Memorandum items:										
Export volume (change in percent)	31.4	–7.6	12.9	7.9	6.1	5.4	4.9	5.0	5.1	5.2
Of which: West	21.1	7.9	9.5	9.6	8.0	8.8	8.0	8.0	8.1	8.1
Import volume (change in percent)	–17.1	–4.1	9.6	6.2	4.7	6.1	4.7	4.5	4.6	4.8
Of which: West	40.8	19.2	9.3	10.1	7.1	8.5	7.3	7.5	7.7	7.9
Current account balance (incl. trans.) (In percent of GDP)	–4.6	–3.2	–2.9	–2.5	–2.5	–1.8	–1.8	–1.4	–1.3	–0.9
Terms of trade	–47.6	4.0	–0.7	–1.7	0.2	2.5	–0.1	0.7	–0.2	0.9
Gross official reserves (In months of imports)	1.8	3.0	2.7	3.3	3.0	3.3	3.6	3.8	4.0	4.3
Debt service (In percent of exports to the West)	1.6	2.2	6.2	6.3	3.9	3.9	8.6	4.7	8.5	7.1
External Debt (In percent of GDP)	9.8	8.0	9.0	10.1	8.8	9.5	9.6	8.8	8.7	8.1

Sources: Information provided by the Lithuanian authorities; and staff estimates and projections.

1/ "East" includes Estonia, Latvia, Russia and other FSU countries. "West" includes all others.
2/ The change in net foreign assets from the Bank of Lithuania's (BoL) balance sheet has been reduced for presentation in the balance of payments by 50 percent of the amount of Fund purchases during 1995 and 1996. The BoL does not include the 50 percent of a Fund purchase that goes to finance imports, in either its foreign assets or its foreign liabilities.

Table 11. Lithuania: Indicators of Capacity to Repay the Fund

	1993	1994	1995	1996	1997	1998	1999	2000
				(In millions of SDRs)				
Outstanding use of Fund credit	88.0	134.6	176.0	200.5	200.5	179.9	167.8	147.1
IMF Obligations	0.7	1.6	8.7	25.4	40.5	29.4	20.2	28.1
Purchases	70.7	46.6	41.4	41.4	31.1	--	--	--
Repurchases	--	--	--	16.9	31.1	20.6	12.1	20.7
Charges	0.7	1.6	8.7	8.5	9.4	8.8	8.1	7.4
				(In percent)				
Outstanding use of Fund credit as a ratio of								
GDP	4.3	3.4	3.4	2.9	2.5	1.9	1.5	1.1
Exports of goods and non-factor services								
Total exports	6.2	8.5	10.3	10.2	9.3	7.7	6.6	5.4
Exports to non-FSU	12.4	15.9	18.9	18.5	16.8	13.7	11.6	9.3
External debt	43.7	43.0	33.3	30.9	25.8	21.3	17.4	14.1
Net official international reserves 1/	41.1	39.2	46.5	41.4	34.1	25.4	20.3	15.3
Quota (new)	85.0	130.0	170.0	193.7	193.7	173.8	162.1	142.1
Debt service obligations to IMF as a ratio of								
GDP	--	--	0.2	0.4	0.5	0.3	0.2	0.2
Exports of goods and non-factor services								
Total exports	--	0.1	0.5	1.3	1.9	1.3	0.8	1.0
Exports to non-FSU	0.1	0.2	0.9	2.3	3.4	2.2	1.4	1.8
Total debt service	3.7	2.3	20.0	51.4	36.7	42.5	18.5	25.6
Net official international reserves 1/	0.3	0.5	2.3	5.2	6.9	4.2	2.4	2.9
Memorandum Items:								
Debt to international financial institutions								
(In millions of U.S. dollars)	177.2	298.3	457.7	618.2	707.1	761.7	825.3	869.1
(In percent of total external debt)	63.1	66.6	56.8	63.1	60.4	59.6	56.6	54.9

Sources: Data provided by the Lithuanian authorities; and staff estimates and projections.

1/ Convertible currencies.

Table 12. Lithuania: Summary of Structural Policies Under Second Annual EFF-Supported Program, October 1995-September 1996 1/

Measure	Date/Period of Implementation
I. Financial sector	
Further strengthening of bank regulation and supervision.	Throughout 1995/96
Conclusion of plans to bring banks in compliance with prudential regulations.	End-1995
Development of contingency plan to deal with bank failures.	Fall 1995
Introduction of bank merger policy.	Fall 1995
Development of restructuring plan for the banking sector.	End-March 1996
Development of money market.	Throughout 1995/96
Training of commercial bank staff; institutional development.	Throughout 1995/96
Increase of minimum bank capital.	Beginning 1996
II. Budgetary policies	
Implementation of Treasury project.	Throughout 1995/96; to be operational by mid-1996
Strengthening of tax administration.	Throughout 1995/96
Unification of personal income tax system.	1995/96
Strengthening of framework for fiscal policy implementation.	1995/96
Evaluation and revision of three-year public investment program.	Fall 1995
Preparation of three-year budget outlook.	Fall 1995
Increase in retirement age.	Beginning 1996
III. Other structural reforms	
Continued privatization of remaining state property.	Throughout 1995/96
Continued land restitution.	Throughout 1995/96
Continuation of work to restructure the energy sector and strengthening its financial performance	Throughout 1995/96
Further reductions in import tariffs	Fall 1996

Table 12 (Concluded). Lithuania: Summary of Structural Policies Under Second Annual EFF-Supported Program, October 1995-September 1996 1/

Measure	Date/Period of implementation
Eliminate all specific import tariffs	May 1996
Eliminate all bans and tariffs on exports	May 1996
Continuation of work to restructure agricultural sector	Throughout 1995/96
Continuation of work to restructure the housing and transportation sectors.	Throughout 1995/96
Introduction of new bankruptcy law.	Early 1996
Introduction of amended law on competition policy	1995/96
Introduction of new system of enterprise accounting.	1995/96
Establishment of system for registration of property rights and loan collateral.	1995/96

Sources: Memorandum of Economic Policies of September 29, 1994; Letter for First EFF Review of June 22, 1995; and Letter for Second EFF Review of November 1995.

1/ Excludes actions that constitute performance criteria or benchmarks.

Vilnius, November 28, 1995

Dear Mr. Camdessus:

1. The Memorandum of Economic Policies (MEP) attached to our letter of September 29, 1994 described our general policy objectives for the period October 1994-September 1997, and set out in detail the economic program covering October 1994-September 1995. On October 29, 1994, the Executive Board of the IMF approved our request for use of Fund resources under the extended Fund facility (EFF) in support of our policies. Our letter of June 22, 1995--for the first review under the EFF arrangement--described developments during the first six months of the program, as well as economic objectives and policies for the remainder of 1995. The program had been implemented as scheduled and its objectives broadly attained. The present letter updates and supplements our earlier letters, outlining developments since the first review and describing economic objectives and policies for the second-year program, covering October 1995-September 1996. On the basis of our record of cooperation with the Fund and our policy objectives set forth below, we request the completion of the second review under the EFF arrangement.

I. Recent Economic Developments and Policies

2. The progress in stabilizing the economy and moving to a market system has continued under the EFF-supported program. All end-September 1995 performance criteria were met, and structural reforms have been implemented as planned. We are mindful, nevertheless, that underlying weaknesses remain in some key sectors, in particular banking and energy, and that these could pose a threat to macroeconomic stability. To protect the objectives of the program, we have taken a number of actions to strengthen economic policy implementation, including all those specified in the letter for the first EFF review. The program described below is based on the assumption that the measures that have been or are being implemented are sufficient to avoid a deterioration in the banking sector. However, as the situation is evolving, we realize that additional measures may be necessary, on which we intend to consult with the Fund.

3. Sound macroeconomic policies have continued, and macroeconomic trends have been favorable overall. Real GDP is projected to increase by about 4 percent in 1995, somewhat lower than the program projection. Inflation has remained low, but is expected to pick up in the last quarter of 1995, as the doubling of heating prices takes effect. For 1995 as a whole, inflation is expected to be somewhat higher than earlier forecast because of relative price changes including the effects of higher excises; the rate of inflation is projected at 39 percent (annual average), compared with a program projection of 36 1/2 percent. Developments under the currency board arrangement have been favorable. We have increased the foreign currency

backing of the currency board's litas liabilities on a net basis, through a reversal of the pledge of US$30 million of central bank foreign reserves made as collateral for foreign bank borrowing by the energy sector. Moreover, following the foreign exchange outflows that occurred amidst devaluation rumors in late 1994 and early 1995, we have again experienced large inflows and interest rates have been declining. The external current account is expected to register a somewhat smaller deficit in 1995 than earlier projected, while the capital account has been stronger due to a catchup in G-24 official loan disbursements.

4. In April-September 1995, the general government budget registered a financial deficit of Llt 241 million, well below the program projection of Llt 270 million for that period. In contrast to the first quarter of 1995, when expenditure was compressed strongly, the favorable fiscal outturn reflected an improvement in revenue collection. Revenue collection was improved through the adoption of the General Law on Tax Administration, strengthened oversight and coordination capabilities of the head office of the State Tax Inspectorate, better enforcement and higher rates for excises, and the initiation of VAT and excise tax collection on imported goods at the border. The strong revenue performance has allowed the Government to move forward the increase in public sector salaries, which had been lagging behind inflation.

5. In the process of transition to a market economy, strains have developed in the banking system. This year, an increasing number of banks have been experiencing liquidity and solvency problems. We recognize that financial sector stability is very important for the stability of the overall economy. We have already implemented the following measures to address the weak position of the banking system: (i) on the basis of the Commercial Bank Law adopted in late 1994, prudential regulations have been established by the Bank of Lithuania (BOL), and bank-by-bank plans have been worked out in which each bank will sign by end-1995 an agreement with the BOL to come into compliance with these regulations within a given timetable; the plans will include sanctions (such as fines, restrictions on operations, and suspension of license), in accordance with the Commercial Bank Law, on banks that do not observe their individual commitments; such action has already been taken on 22 occasions against 11 banks; (ii) to protect the integrity of the currency board arrangement, a contingency plan has been worked out, which would allow a rapid and appropriate response in the event of a bank failure; the burden of any need to restore the solvency of banks would be borne by the Government; (iii) bankruptcy proceedings have been initiated for 11 small banks, reducing the number of banks in operation from 27 in early 1994 to 16 at present (the 11 failed banks constituted less than four percent of total assets of the banking system); (iv) we have presented to Parliament legislation that provides for a limited deposit protection scheme; (v) we have decided to compensate in part individual depositors of banks that will be closed prior to January 1, 1996, with modest fiscal outlays; and (vi) on-site banking supervision has been strengthened by introducing a new inspection manual and by expanding the number of inspections, and off-site supervision has been improved by the introduction of a new reporting system aimed at providing early warning.

6. Structural reforms have progressed largely as planned. The average tariff on selected agricultural imports was reduced from 35 percent to 27 1/2 percent effective October 1, 1995; this reduction was achieved through a broad-based reduction in the relevant tariff rates. However, tariffs on three products (alcohol, tobacco, and sugar) still include both specific and ad valorem rates. Reference prices or threshold prices for agricultural imports have not been introduced. We have started to implement a plan for reduction in arrears of energy consumers, including cut-offs of energy supply and penalties for delinquent customers; consumer arrears for electricity, heating, and gas declined from their peak of Llt 500 million (1/2 percent of GDP) in April 1995 to Llt 300 million in October. Voucher privatization was completed on July 1, 1995 (remaining vouchers may be used for purchasing apartments and a few other types of assets through end-1996). The Law on Cash Privatization was enacted in July 1995, providing for an independent privatization agency overseen by a Privatization Commission; the Agency and the Commission have already been established, and are ready to initiate operations. The number of bankruptcy cases has been rising, although only a small number of cases has been completed yet; an important constraint in this regard is that we have been able to make only limited progress in expanding the capacity of the court system. A new law on foreign direct investment came into effect in August 1995, allowing foreign investment in virtually all sectors; a constitutional amendment to lift the ban on foreign ownership of land is currently before Parliament.

II. Economic Objectives and Policies for October 1995-September 1996

7. The overall strategy--the currency board arrangement, tight fiscal policy, and structural reforms--will continue. The main challenge in the period ahead will be to protect the stabilization gains by addressing, in particular, the problems in the banking and energy sectors. We are confident that this effort will be successful, and therefore have kept our macroeconomic objectives for 1996 and the medium term broadly unchanged. Specifically, real GDP is projected to increase by about 5 percent in 1996, spurred by continued strong growth in the services sectors, an expansion in agriculture, as well as a turnaround in manufacturing. Inflation in 1996 is now projected at 23 percent, compared with a program projection of 19 percent; the higher inflation reflects the carry-over from higher inflation in 1995. The external position is expected to remain strong in 1996, due to continued high export growth and capital inflows.

Macroeconomic policies

8. The currency board arrangement, at the current exchange rate, will continue to govern monetary policy. To maintain credibility, the BOL will enforce, firmly and uniformly, the reserve requirement through strict application of penalties against banks that register shortfalls, and the definition and ratio of required reserves will remain unchanged. Moreover, we shall not enter into any new pledges of BOL foreign exchange reserves.

9. The proposed program includes quarterly ceilings for the general government financial deficit and net lending, consistent with containing the financial deficit to about 2 percent of GDP in 1996. The fiscal strategy centers on an intensified revenue effort based on improvements in tax administration and broadening of tax bases, with a view to allowing an expansion in government infrastructure investment and some reversal of the compression in current expenditure. The Government has presented to Parliament a state budget for 1996 which is consistent with the above objectives.

10. To improve revenue performance, we intend to take the following measures in 1995/96: (i) strengthening of customs collection, by increasing the number of border posts and computerization, with continued technical assistance from the EU; (ii) full implementation of the General Law on Tax Administration, and completion of the reorganization of the State Tax Inspectorate; (iii) discontinuation of the granting of tax deferments, and collection of taxes in arrears through administratively authorized seizure of assets of delinquents, court actions, and bankruptcies; (iv) simplification of the personal income tax through unification of rates for income from different sources; (v) elimination of exemptions from the profit tax; (vi) improvement of invoicing regulations for VAT and excise tax; (vii) introduction by end-1995 of new tax-payer registration requirements; and (viii) establishment of new regulations concerning cash transactions and tax liabilities for companies that split into smaller units. Parliament has decided to extend the VAT exemptions for food and energy through end-1996; to offset the revenue loss from the continued exemption, we will increase excises on petrol and undertake further expenditure cuts. The increases in excise tax rates effected in July and November 1995 will also help raise revenue in 1996.

11. Strong revenue performance will permit a reduction in arrears of budgetary organizations to suppliers as planned, while avoiding accumulation of new arrears. Current expenditure will be covered by current revenue in the remainder of 1995 and in 1996; government domestic and foreign borrowing will not exceed the amounts needed for investment and net lending. Also, the share of government investment in total government expenditure will increase; the investments would be based on our public investment program (PIP) prepared in early 1995. Following the large public sector salary increases in October 1995, the growth of the wage bill of budgetary organizations will be limited in 1996. By January 1996, we will start a review of the scope for reduction in civil service employment as a means to improve efficiency and limit the wage bill. The draft 1996 budget provides Llt 30 million for the deposit protection scheme, Llt 15 million for capital injection in state-controlled banks, and about Llt 20 million for partial compensation for depositors of banks that will have been closed before the introduction of the deposit protection scheme; any fiscal outlays to deal with bank failures will be consistent with the budget ceilings.

12. In light of the situation in the banking sector--as well as the downside risks in the revenue targets--we have identified contingency measures that would be taken to protect the deficit targets; these measures would include elimination of VAT exemptions, introduction of new excise taxes, and cuts in low-priority expenditure.

13. The operations of the social insurance fund will continue to be balanced. To achieve this objective in the short run, payroll tax collection will be strengthened (including through improved cooperation with the labor inspectorate and the State Tax Inspectorate in cross-checking employment and salaries) and arrears cleared. The medium-term viability of the social insurance fund will be sought through an increase in the retirement age (by at least 2 and 4 months per year for men and women, respectively), a streamlining of social security benefits, and the development of privately managed pension schemes. The Government will keep under review the advisability of accelerating the increases in the retirement age.

14. While overall fiscal restraint has been maintained through cash rationing, weaknesses in the budgeting framework have contributed in the past to expenditure instability, accumulation of expenditure arrears, and excessive expenditure compression. Accordingly, budget preparation and implementation will be strengthened in 1995/96, by establishing a fiscal policy department at the Ministry of Finance and by consolidating expenditure management under the state treasury. Also, we are moving ahead swiftly to make the treasury system (including the consolidation of all government funds under the authority of the state treasury) fully operational by mid-1996, as earlier planned. In the meantime, government deposits placed with illiquid banks as part of rescue operations shall be treated as net lending. In regard to government guarantees of domestic lending by the banking system, the Government will start provisioning by setting aside amounts equivalent to 25 percent of guarantees up to Llt 100 million and 100 percent of guarantees above this amount, with such set-asides treated as government net lending. We intend to introduce quarterly reporting on payments arrears by spending units of the state and municipal budgets, starting January 1, 1996. Finally, to improve government debt management, we will introduce a rolling four-quarter borrowing plan.

Structural policies

15. During 1995/96, we will move ahead with structural reforms as outlined in the MEP, and catch up in areas where progress has been slower than planned. The second-year program will focus in particular on continued reforms in the banking sector, progress in liberalizing agriculture and external trade, strengthening of the operations and financial performance of the energy sector, and development of the legal and institutional foundations of a market economy.

16. As noted above, we have already started to implement measures to strengthen the banking sector. Further steps in this area will include: (i) issuing regulations, by end-December 1995, setting out the new bank reorganization policy, such that no bank reorganizations (including mergers) will be approved unless the reorganized bank would meet prudential rules; excessive concentration in the banking sector will be avoided; (ii) completing, by end-November 1995, on-site inspection of the largest private bank, as well as initiating, by end-March 1996, on-site inspections of the state-controlled banks; (iii) maintaining the present definition of capital until Basle rules for capital adequacy have been introduced; (iv) adopting, by March 1996, a BOL resolution that provides for the inclusion of interbank lending in the overall exposure limits to a single borrower; (v) strengthening of efforts to complete bankruptcy proceedings for banks currently under such proceedings; and (vi) developing a plan, by end-March 1996, in consultation with the World Bank and other multi-lateral agencies, to restructure the banking system. This plan will include a schedule for privatization of the three dominant state-controlled banks. As a first step, a plan will the developed, with the help of the U.S. Treasury-sponsored advisor, to strengthen corporate governance of the state-controlled banks. As regards restructuring of the banking system, recapitalization with public funds will take place only as a last resort and only in appropriate cases. Any such operation will be subject to proper corporate governance and adequate safeguards for providers of additional capital. The responsibility for bank supervision will remain fully with the BOL, which will coordinate with the Government and its agencies.

17. The reform of the external trade system will be continued in 1995/96, in particular through: (i) further lowering of the weighted average import tariff rate for major agricultural products to at most 20 percent; (ii) elimination of all "exceptional" import tariffs (i.e., rates in excess of 30 percent); (iii) further reduction in other import tariff rates that are currently above 10 percent, consistent with the reduction in the maximum rate to 10 percent by September 1997; and (iv) elimination of remaining export bans and export tariffs by May 1996. Also, all remaining specific import duties (including on those items where ad valorem tariffs are combined with specific tariffs) will be abolished by May 1996. Threshold prices for agricultural imports will not be introduced, and a system of reference prices--if introduced--would be developed in consultation with the WTO, and be based on international prices and be non-binding. The need for reference prices will be eliminated through a strengthening of customs procedures.

18. The second-year program aims to reduce consumer indebtedness for electricity, heating, and gas to Llt 250 million (or one half of their July 1995 level) by end-1995 and Llt 100 million by end-March 1996, and to remain below Llt 100 million thereafter. To this end, we will allow energy suppliers to cut off the energy supply to all delinquent customers except for a narrowly defined list of essential customers (defined in consultation with the World Bank), apply penalties for late payment, and pursue cases in court; we will not grant exemptions from payment of energy bills. Also, budgetary organizations including municipalities will avoid new energy

arrears, and completely eliminate their existing arrears by mid-1996. The monitoring of the energy companies' finances will be strengthened. For this purpose, the audit of the Lithuanian State Power System (LSPS) was completed in mid-October 1995; on the basis of this audit, we have established a financial action plan for LSPS. To address the more fundamental problems in the energy sector, and in consultation with the World Bank, we will take the following steps: (i) complete, by June 1996, preparatory work and take first steps to transfer district heating ownership and operational responsibilities--including tariff setting--from the LSPS to local municipalities; (ii) allow Ignalina Nuclear Power Company to charge cost-recovering tariffs--including provisions for de-commissioning and fuel disposal costs--for its sales of power to LSPS by January 1, 1996; (iii) allow LSPS to set cost-recovering tariffs for its power deliveries to customers by January 1, 1996 to address both increased costs from Ignalina and provisions for uncollectible customer debts; (iv) begin implementation of a cost-cutting program at LSPS (including, inter alia, independent supervision of fuel procurement, delivery, and stock-taking) by January 1, 1996, with penalties applied to LSPS management if the targets of this program are not observed; and (v) complete preparatory work for introducing a proper regulatory framework for energy pricing and establish the framework by end-March 1996. Privatization of the energy sector is retained as a medium-term goal.

19. We are moving ahead with divestiture of state assets for cash. The list of enterprises to be offered for sale in 1996 is under preparation, and is planned to be approved by the Government and published by end-1995; actual sales are expected to commence in early 1996. Cash privatization will include all state assets (including the remaining state ownership in enterprises partly privatized through vouchers), except for the list of strategic enterprises that will remain in government hands at least through 2000; we will seek to reduce this list further by March 1996. Also by March 1996, we will review the Law on Cash Privatization, in consultation with the World Bank, with a view to propose amendments to the Law that would facilitate the privatization process. This review will focus in particular on the centralization of privatization responsibilities--including for municipal property--under the Privatization Agency, and will establish targets for privatizations through end-1997.

20. During the second annual program, further progress in adjusting laws and regulations to the requirements of a market economy is planned. To facilitate bankruptcy proceedings, the capacity of the court system is being increased, and a new Bankruptcy Law is being prepared; it is expected that this Law will be presented to Parliament in early 1996. Moreover, a new Law on Competition has been drafted; this Law will strengthen the State Price and Competition Office's power to collect information, provide the basis for breaking up large companies that abuse their market power, and harmonize Lithuania's competition legislation with that of the EU. The new Competition Law is expected to be presented to Parliament in the second half of 1996, following the necessary reviews to ensure EU harmonization. The Government will also introduce a new system of enterprise accounting consistent with international standards, and establish an improved system

for registration of property rights and loan collateral. Finally, we will continue our efforts, with assistance from the international donor community, to improve the statistics, in particular for national accounts and balance of payments.

III. Program Monitoring

21. The performance criteria relating to the maintenance of the exchange rate under the currency board arrangement, the full foreign exchange cover for currency board liabilities, the minimum levels for total reserve deposits of banks with the BOL, and no accumulation of external payments arrears by the Government have been retained. Also, the proposed second annual arrangement includes a performance criterion on the reduction of the weighted average import tariff rate for major agricultural products 1/ to at most 20 percent by end-September 1996. Quantitative performance criteria for end-December 1995 and end-March 1996, and indicative targets for end-June 1996 and end-September 1996, have been set for the same variables as in the original program (Table 1). New quarterly benchmarks have been established for consumer indebtedness for electricity, heating, and gas. Also, government deposits placed with illiquid banks as part of rescue operations and a specified proportion of government guarantees on domestic borrowing will be included in the definition of net lending. The third EFF review, expected for completion by June 1996, will focus on the plan for banking system restructuring, the adequacy of energy prices, progress in cash privatization, presentation of the new bankruptcy law to Parliament, the elimination of export tariffs and restrictions, and developments in current government expenditure, especially wage payments.

Yours sincerely,

/S/
Adolfas Šleževičius
Prime Minister

/S/
Kazys Ratkevičius
Governor, Bank of Lithuania

Mr. Michel Camdessus
Managing Director
International Monetary Fund
Washington, D.C., 20431

1/ As defined in Annex V of the MEP of September 29, 1994.

Table 1. Lithuania: Performance Criteria, Benchmarks, and Indicative Targets for Second Annual Program, October 1995 - September 1996 1/

Variable and Periods		Performance Criteria/ Indicative Targets	
I.	Maintenance of exchange rate under currency board arrangement Duration of the extended arrangement		
II.	Full foreign exchange cover for currency board liabilities Duration of the extended arrangement		
III.	Minimum levels for total reserve deposits of banks with the Bank of Lithuania, calculated as for the reserve maintenance period and expressed as a percentage of eligible commercial bank liabilities:	9	
IV.	Limit on tariff rates for major agricultural goods; September 30, 1996 (in percent)	20	
V.	No accumulation of external payments arrears by the Government		
VI.	Limits on the general government financial balance; cumulative from October 1, 1995 to:	(In millions of Litai)	
	December 31, 1995	-240	
	March 31, 1996	-480	
	June 30, 1996	-700	
	September 30, 1996	-920	
VII.	Limits on net lending by the general government; 2/3/ cumulative from October 1, 1995 to:		
	December 31, 1995	280	
	March 31, 1996	430	
	June 30, 1996	530	
	September 30, 1996	630	
		(In millions of U.S. Dollars)	
		Minimum limits	
VIII.	Minimum net international reserves of the Bank of Lithuania 4/		
	September 30, 1995 (actual)	-119	
	December 31, 1995	-114	
	March 31, 1996	-125	
	June 30, 1996	-131	
	September 30, 1996	-137	
IX.	Limits on contracted public and publicly guaranteed medium- and long-term external debt; cumulative from October 1, 1995, until	Maximum limits	
		1-12 yr maturity	1-5 yr maturity
	December 31, 1995	140	90
	March 31, 1996	165	115
	June 30, 1996	190	140
	September 30, 1996	215	165
X.	Limit on government debt of up to one year; duration of the extended arrangement	--	
		(In millions of Litai)	
XI.	Limit on consumer indebtedness for electricity, heating, and gas (stocks)		
	End-December 1995	250	
	End-March 1996	100	
	End-June 1996	100	
	End-September 1996	100	

1/ Items I, II, III, and quantitative target figures for end-December 1995 and end-March 1996 are performance criteria; target figures for end-June 1996 and end-September 1996 are indicative targets. Target figures for consumer indebtedness for electricity, heating, and gas are benchmarks. Detailed definitions are included in the Annexes to the MEP. Net international reserves are defined as BOL's gross reserves minus foreign reserve liabilities and domestic liabilities.

2/ The definition of net lending includes 25 percent of government guarantees for domestic bank lending up to Llt 100 million and 100 percent of such guarantees above Llt 100 million, and government deposits placed with illiquid banks as part of rescue operations.

3/ Excludes the counterpart of borrowing from the EU on-lent through domestic commercial banks.

4/ The performance criteria would be adjusted upwards by 50 percent of any shortfall in purchases from the Fund.

LITHUANIA: Fund Relations
(As of October 31, 1995)

I. Membership Status: Joined 4/29/92; Article VIII

II. General Resources Account:	SDR Million	% Quota
Quota	103.50	100.0
Fund holdings of currency	269.10	260.0
Reserve position in Fund	0.01	--

III. SDR Department:	SDR Million	% Allocation
Holdings	13.14	--

IV. Outstanding Purchases and Loans:	SDR Million	% Quota
Stand-by arrangements	62.10	60.0
Extended arrangements	51.75	50.0
Systemic Transformation	51.75	50.0

V. Financial Arrangements:

Type	Approval Date	Expiration Date	Amount Approved (SDR Million)	Amount Drawn (SDR Million)
EFF	10/24/94	10/23/97	134.55	51.75
Stand-by	10/22/93	10/24/94	25.88	5.18
Stand-by	10/21/92	9/20/93	56.93	56.93

VI. Projected Obligations to Fund (SDR Million; based on existing use of resources and present holdings of SDRs):

	Overdue	Forthcoming				
	4/30/95	1995	1996	1997	1998	1999
Principal	--	--	16.9	31.1	20.6	12.1
Charges/Interest	--	1.9	7.8	6.7	5.3	4.5
Total	--	1.9	24.7	37.8	25.9	16.6

VII. Exchange Arrangements

The currency of Lithuania is the litas. Since April 1, 1994, the litas has been pegged to the U.S. dollar at Llt 4 per U.S. dollar under a currency board arrangement.

VIII. Resident Representative

The Resident Representative of the Fund in Lithuania is Mr. Domenico Fanizza, who took up his post in October 1995.

IX. Consultation Cycle

Lithuania is on the 12-month consultation cycle.

Lithuania: Technical Assistance from the Fund, 1991-95

Department	Issue	Action	Date	Counterpart
MAE	Multi-topic mission	Mission	December 91	Bank of Lithuania
MAE	Multi-topic mission	Mission	March 92	Bank of Lithuania
FAD	Multi-topic mission	Mission	March 92	Ministry of Finance
STA	Price statistics	Expert visit	March 92	Department of Statistics
STA	Diagnostic mission	Mission	March/ April 92	Bank of Lithuania Ministry of Finance
STA	Balance of payments statistics	Mission	May 92	Ministry of Economy Department of Statistics
MAE	Multi-topic mission	Mission	June 92	Bank of Lithuania
STA	Government finance statistics	Mission	June/ July 92	Ministry of Finance Bank of Lithuania
STA	Follow-up to March 92 mission on price statistics	Expert visit	July 92	Department of Statistics
STA	Balance of payments statistics	Mission	September 92 Statistics	Ministry of Economy Department of
TRE	Quota payment	Mission	October 92	Bank of Lithuania Ministry of Economy
MAE, LEG	Financial legislation	Mission	November 92	Bank of Lithuania Ministry of Economy Ministry of Finance
MAE	Multi-topic mission	Mission	December 92	Bank of Lithuania
EXR	Seminars on Fund, press interviews	Mission	November 92	Ministry of Foreign Affairs Bank of Lithuania
FAD	Expenditure management	Mission	December 92	Ministry of Finance
STA	Balance of payments statistics	Mission	December 92	Ministry of Economy Department of Statistics
STA	Assessment of TA needs	Mission	March 93	Department of Statistics
MAE	Foreign exchange operations	Advisor	March 93 onward	Bank of Lithuania
MAE	Central Bank accounting	Expert visits	March/Aug. 93	Bank of Lithuania
MAE	Banking supervision	Expert visits	March/Dec. 93	Bank of Lithuania
STA	Money and banking statistics	Mission	April 93	Bank of Lithuania

Lithuania: Technical Assistance from the Fund, 1991-95 (cont'd)

Department	Topic	Action	Date	Counterpart
STA	Balance of payments statistics	Expert visit	April/May 93	Ministry of Economy Department of Statistics
MAE	Banking supervision	Expert visits	March/Dec. 93	Bank of Lithuania
STA	Money and banking statistics	Mission	April 93	Bank of Lithuania
STA	Balance of payments statistics	Expert visit	April/May 93	Ministry of Economy Department of Statistics
MAE	Monetary operations, bank supervision, payments system improvement, central bank accounting, foreign exchange operations	Mission	May/June 93	Bank of Lithuania
MAE	Central bank accounting	Expert visit	August 93	Bank of Lithuania
MAE	Monetary operations	Expert visit	Aug./Sep. 93	Bank of Lithuania
STA	Balance of payments	Expert visit	Sep./Oct. 93	Department of Statistics
STA	Price statistics	Expert visit	September 93	Department of Statistics
FAD	Treasury operations, revenue and expenditure projections, control of cash disbursements to line ministries, financial control system	Mission	November 93	Ministry of Finance
MAE, LEG	Monetary operations, payments system, bank supervision, banking legislation	Mission	November 93	Bank of Lithuania
STA	Monetary statistics	Mission	December 93	Bank of Lithuania
MAE	Bank supervision	Expert visit	Jan./Feb./July Oct. 94	Bank of Lithuania
MAE	Central Bank accounting	Expert visit	Feb./Apr./June/ Aug. 94	Bank of Lithuania
STA	National accounts	Expert visit	Feb./June 94	Department of Statistics
FAD	Tax policy	Mission	March 94	Ministry of Finance
MAE	Assessment of technical assistance needs	Mission	July 94	Bank of Lithuania
STA	Balance of payments statistics	Expert visit	Apr./Aug./ Sep. 94/ Sep. 95	Department of Statistics
MAE	Payments system, research activities of BOL	Mission	December 94	Bank of Lithuania
MAE	Central bank accounting	Expert visit	Jan./Feb. 95	Bank of Lithuania
FAD	Budget Framework	Mission	July 1995	Ministry of Finance

Resident Advisors

Department	Issues	Advisor	Dates
MAE	Monetary Operations	Mr. Selnes	March 1994- June 1995
FAD	Treasury Operations	Mr. Ramachandran	July 1994- July 1996
	Tax Policy and Administration	Mr. Hart	August 1994- March 1995
STA	Statistical Systems	Mr. Saunders	November 1993- April 1996

Statistical Data Matrix

(as of early November 1995)

	Exchange rates 1/	International reserves	Reserve/ base money	Central Bank balance sheet	Broad money	Interest rates	Consumer price index	Exports/ Imports	Current account balance	Overall government balance	GDP/GNP
Date of latest observation	...	Sept. 30	Sept. 30	Sept. 30	Sept. 30	end-Oct.	Oct. 1995	Q3:95	Q3:95	Q3:95	Q3:95
Date received	...	Oct. 10	Aug.10	Aug. 10	Aug. 23	early Nov.	early Nov.	October	October	Nov. 3/	Oct. 24
Frequency of data	...	M	D	M	M	W	M	Q	Q	M	Q
Frequency of reporting	...	M	M	M	M	W	M	V	V	M	Q
Source of data	...	A 2/	A 2/	A 2/	A 2/	A 2/	A,N 2/	A	A	A 2/	A,N 2/
Mode of reporting	...	C	C	C	C	C	C	V	V	C	X
Confidentiality	...	B	C	C	C	C	C	C	C	C	C

1/ Lithuania has a currency board arrangement, under which the litas is pegged at Llt 4 to the U.S. dollar.
2/ Through the resident representative's office
3/ General government balance computed by staff based on separate data provided by the Ministry of Finance.

Explanatory Notes

Frequency of data: D-daily, W-weekly, M-monthly, Q-quarterly.
Frequency of reporting: M-monthly, Q-quarterly, V-irregularly in conjunction with staff visits.
Source of data: A-direct reporting by central bank, ministry of finance, or other official agency, N-official publication or press release.
Mode of reporting C-cable or facsimile, V-staff visits, or O-other.
Confidentiality: (B) for use by the staff and the Executive Board, (C) for unrestricted use.

Lithuania: World Bank Group Relations

Lithuania became a member of the World Bank on July 6, 1992. On October 22, 1992, the World Bank approved the first loan to Lithuania, a Rehabilitation Loan in the amount of US$60 million. This loan was designed to assist the Government in the implementation of its economic reform program and to support economic activity through the importation of essential goods for high-priority sectors. As of end-September 1995, the loan was essentially fully committed, and US$58.5 million had been disbursed. On May 24, 1994, the Bank approved the first investment loan to Lithuania for Power Rehabilitation and Restructuring in the amount of US$26.4 million. The objectives of this loan are to improve the operating efficiency, safety, reliability, and flexibility of the electricity system. The loan will also provide support for the restructuring and commercialization of the national electricity agency. A loan of US$7 million to support an environment project in Klaipeda was approved on December 8, 1994; disbursements have begun, and had reached US$0.12 million by end-September 1995. On April 13, 1995, the Bank approved the Enterprise and Financial Sector Assistance Loan for a total amount of US$25 million. The objective of the loan is to support and help accelerate the Government's reform efforts in the enterprise and financial sectors. It focuses in particular on delivering financial and technical assistance to private banks and privatized enterprises to help them adjust to the new economic system in Lithuania, and provides some technical pre-privatization assistance to large state enterprises.

The first World Bank Country Economic Memorandum (CEM) was published in April 1993. A Public Expenditure Review was conducted in 1993/1994 and was the basis for a donors' meeting on public investments in May 1994. The Bank also has prepared an informal enterprise and financial sector study, an assessment of private sector development, a comprehensive energy sector review, a study of nuclear energy alternatives commissioned by the G7, an agricultural review, a municipal finance study, a social insurance/social policy note, and a transport study. Future studies may include an economic report on foundations of a sustainable macro-framework, a health sector note, and a poverty assessment.

Work is proceeding on three operations covering the environment, energy/geothermal, and agricultural sectors. World Bank lending to Lithuania may range from two to three lending operations per year over the Bank fiscal years 1995-98.

FOR AGENDA

EBS/95/199
Corrected: 12/15/95

CONFIDENTIAL

November 29, 1995

To: Members of the Executive Board

From: The Secretary

Subject: Republic of Lithuania - Second Review Under the Extended Arrangement

Attached for consideration by the Executive Directors is a paper on the second review under the extended arrangement for the Republic of Lithuania, which is tentatively scheduled for discussion on Wednesday, December 20, 1995. A draft decision appears on pages 15-17.

Mr. Berengaut (ext. 38773), Mr. Brekk (ext. 38754), or Ms. Psalida (ext. 35360) is available to answer technical or factual questions relating to this paper prior to the Board discussion.

Unless the Documents Preparation Section (ext. 36760) is otherwise notified, the document will be transmitted, in accordance with the procedures approved by the Executive Board and with the appropriate deletions, to the European Bank for Reconstruction and Development (EBRD), the European Commission (EC), the European Investment Bank (EIB), and the Organisation for Economic Cooperation and Development (OECD), following its consideration by the Executive Board.

Att: (1)

Other Distribution:
Department Heads

EBS/95/199
Corrected: 12/15/95

CONFIDENTIAL

INTERNATIONAL MONETARY FUND

REPUBLIC OF LITHUANIA

Staff Report for Second Review Under Extended Arrangement

Prepared by the European II and Policy Development and Review Departments

Approved by John Odling-Smee and Susan Schadler

November 28, 1995

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