DOCUMENT OF THE EUROPEAN BANK
FOR RECONSTRUCTION AND DEVELOPMENT

STRATEGY FOR LITHUANIA

As approved by the Board of Directors at its meeting on 23 March 2006

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ABBREVIATIONS and CURRENCY EXCHANGE RATES

CAP	Common Agricultural Policy
CEB	Central Europe and the Baltics
CIS	Commonwealth of Independent States
EC	European Commission
ECB	European Central Bank
EIB	European Investment Bank
EMU	European Monetary Union
ERM II	Exchange Rate Mechanism II.
ESCO	Energy Saving Company
EU	European Union
FDI	Foreign Direct Investment
FI	Financial Institutions
GDP	Gross Domestic Product
IAIS	International Association of Insurance Supervisors
IFC	International Finance Corporation
IFI	International Financial Institutions
IIDSF	Ignalina International Decommissioning Support Fund
IMF	International Monetary Fund
INPP	Ignalina Nuclear Power Plant
IPO	Initial Public Offering
IOSCO	International Organisation of Securities Commissions
ISPA	Instrument for Structural Policies for Pre-Accession
IT	Information Technology
KfW	Kreditanstalt für Wiederaufbau
LTL	Lithuanian litas
MEI	Municipal and Environmental Infrastructure
NATO	North Atlantic Treaty Organisation
NBFI	Non Bank Financial Institution
NIB	Nordic Investment Bank
OECD	Organization for Economic Co-operation and Development
PET	Polyethylene terephthalate
PPP	Public Private Partnership
SDR	Special Drawing Rights
SME	Small and Medium Enterprises
TC	Technical Cooperation
UNCITRAL	United Nations Commission on International Trade Law
US$	United States Dollar
WHO	World Health Organisation

EXCHANGE RATES

€1.0	LTL 3.4528
€1.0	US$ 1.24

EXECUTIVE SUMMARY

Lithuania continues to meet the conditions specified in Article 1 of the Agreement Establishing the Bank. In recent years the country has made substantial progress in transition and this Strategy document recognises the laudable success of Lithuania and its economy. Some 75 per cent of economic activity is in the private sector and price and trade liberalisation, enterprise privatisation and effective financial sector reforms have taken place. There is an open foreign trade regime and no major constraints to foreign investment.

The macroeconomic environment remains generally favourable. The impact of EU accession has been positive in terms of trade and enterprise investment. The economy grew by 7.5 per cent in 2005 and has averaged annual growth in excess of 7 per cent since 2000. Strong domestic consumption and investment demand were major contributors to growth. However, raising expenditures contributed to a loosening of the fiscal stance in 2004 when the general government deficit widened to 1.4 per cent of GDP. The economic stimulus continued in 2005. Following an increase in 2004, the current account deficit stabilised at just over 7 per cent of GDP in 2005 as a result of an improved trade account performance. Unemployment is declining rapidly while the labour force is shrinking due to emigration. The currency board continues to enjoy broad support and Lithuania was admitted to the European Exchange Rate Mechanism (ERM II) in 2004. However, annual average inflation accelerated in the course of 2005. The authorities are aware of the risk to EU convergence that this poses but remain convinced that inflation can be contained within the Maastricht limit.

Since the last strategy, progress has continued on the reform front, and a number of high-profile companies have been privatised, including the national carrier Lithuanian Airlines, power line construction company Elektros Tinklu Statyba, gas utility Lietuvos Dujos and the National Stock Exchange of Lithuania. The business environment is becoming more dynamic and local banks and leasing companies have started to extend loans and leases to smaller companies, often supported through credit lines from international financial institutions. Foreign ownership of the banking sector has led to the restructuring and recapitalization of the system, the introduction of a wider array of products and services and improved corporate governance and transparency.

However, with respect to the Bank’s mandate, a number of remaining transition challenges in Lithuania have been identified and this strategy aims to address those challenges in order to further increase the competitiveness of the Lithuanian economy. The priority transition challenges for Lithuania are as follows:

Infrastructure, environment and energy

With extensive investment and operational needs, there is limited private sector participation in municipal sectors including water and sewage, urban transport and in the development of state transport infrastructure. Energy efficiency is a concern. There are significant costs related to heat losses from municipal-owned heating networks and buildings and privatised industrial enterprises. The closure of Ignalina Nuclear Power

Plant is a key challenge. After the closure Lithuania will be reliant on natural resources imported mainly from Russia for most of its energy generation needs.

Enterprise sector

Further improvements in the business environment are needed, including more extensive and consistent enforcement of laws, reduction in corruption and improved transparency in public procurement. Expansion of private enterprises and completion of restructuring of former state owned companies, particularly in less developed regions, are important.

Financial sector

Financial intermediation remains low, particularly to the SME sector and there is a lack of equity and mezzanine capital to support economic growth.

As of 30 November 2005 the Bank had signed a cumulative total of 31 projects for Lithuania with a total project cost of €1.1 billion, including Bank financing of €475 million, or 43 per cent. The private/state sector portfolio ratio stood at 61/39.

While new business in 2005 is modest, the Bank can continue to play a role over the strategy period by focusing selectively on areas where it is additional and where it can address the remaining transition challenges, particularly in providing equity and cross-border financing, promote public private partnerships and strengthen corporate governance and good business practice.

In addressing the transition challenges, the Bank's activities in Lithuania will be based on the following operational objectives:

- Support large, complex or sensitive transactions that would benefit from the Bank's expertise in project structuring, corporate governance and mobilising co-financing;
- Support the expansion of local companies, particularly in cross-border projects, for example into or from Russia or other CIS countries;
- Promote SME and municipal financing and energy efficiency through financial intermediaries, enhanced where appropriate with EU or other donor support;
- Encourage the development of local capital markets, for example in investing in the local securitisation of mortgage loans.

The Bank will continue to ensure that all EBRD operations in Lithuania meet sound banking principles, have transition impact, are additional and are subject to the Bank's Environmental Procedures and incorporate, where appropriate, Environmental Action Plans.

1. THE BANK'S PORTFOLIO

1.1 Overview of activities to date

As of the end of November 2005, the Bank's cumulative commitments in the Republic of Lithuania (including regional projects) had reached €475 million representing 1.7 per cent of the Bank's net cumulative commitment volume. The Bank helped to mobilise a further €643 million of co-investment, representing a multiplier of 1.4.

The table below gives an overview of the Bank's current portfolio in Lithuania by sector as of end of November 2005. Totalling €204 million, it represented 1.3 per cent of the overall Bank portfolio. The private/state ratio stood at 61/39 and the non-sovereign/sovereign ratio stood at 75/25. The non-sovereign ratio was higher than the private sector ratio because some of the municipal projects have been executed as corporate loans without state or municipal guarantees.

Table 1: Current portfolio by industry (including regional projects) (as of 30 November 2005)

Sector	No of Projects	EBRD finance (€ million)	Portfolio share (%)
Industry and Commerce	**3.1**	**62.1**	**30%**
Agribusiness	1.1	49.8	
Property Tourism and Shipping	0.0	3.3	
Telecom Informatics & Media	1.0	2.8	
General Industry	1.0	6.2	
Financial Institutions	**6.0**	**56.2**	**28%**
Bank Equity	0.5	5.9	
Bank Lending	2.1	17.3	
Non Banking Financial Institutions	1.7	15.5	
Equity Funds	1.7	17.6	
Infrastructure	**5.2**	**85.7**	**42%**
Transport	1.0	43.0	
Municipal & Environment Infrastructure	4.0	36.7	
Energy Efficiency	0.2	6.0	
Power & Energy	0.0	0.0	
TOTAL	**14.2**	**204.0**	**100%**
of which debt	10.0	152.2	75%
of which equity	4.2	51.8	25%
of which guarantee	0	0.0	0%
of which private	8.2	124.3	61%
of which state	6.0	79.7	39%
of which direct	12.1	173.3	85%
of which regional	2.1	30.7	15%
of which non-sovereign	12.2	153.2	75%
of which sovereign	2.0	50.8	25%

The largest portion of the portfolio (42 per cent) relates to infrastructure, with municipal and environmental infrastructure representing approximately half of this and the loan to Lithuanian Railways being the largest single exposure. A significant portion, 28 per cent, of the portfolio relates to FI, a reflection of the structure of the Lithuanian economy and the EBRD's significant role in the support of SMEs through credit lines, equity funds and insurance. A similar portion (30 per cent) relates to Industry and Commerce dominated by the Agribusiness sub-sector.

1.2 Implementation of the previous country strategy

The previous Lithuania strategy has been implemented in an increasingly competitive environment with term credit liquidity readily available from local banks and country risk improving with Lithuania's accession to the EU. The Bank has had to be innovative in identifying market niches that satisfy the Bank's mission. Financing SMEs through financial intermediaries, upgrading municipal infrastructure and supporting cross-border investments of Lithuanian companies have continued to be core areas for the Bank in Lithuania. The 2004 country strategy outlined the following strategic priorities for the Bank in Lithuania:

Private enterprise sector: seek to support larger industrial, manufacturing and service enterprises with a view to facilitating the expansion of Lithuanian companies in the region and improving local corporate governance standards and SMEs through operations in the financial sector and through equity funds.

Energy: seek to promote development of a Baltic energy market among the three Baltic States as well as the Polish-Lithuanian Interconnector and to support projects consequential to the decommissioning the Ignalina Nuclear Power Plant.

Infrastructure: seek to support the further development of infrastructure including in the transport and municipal infrastructure sectors.

During 2004-05 five direct operations were signed in Lithuania with a total volume of €59 million. Also in October 2005 the Bank signed a syndicated loan for the Belarusian subsidiary of a Lithuanian company. Total loan size was €14 million and the Bank's share was €7 million. EBRD's investment in various regional funds has in the same period resulted in an allocation of €7 million.

1.3 Transition impact of the Bank's portfolio and lessons learnt

1.3.1 Relevance and transition impact of previous country strategies

Infrastructure and environment

The Bank's involvement in the transport sector has been through a loan to Lithuanian Railways, which has been successful in moving transition forward. During 2000-05 the Bank's transition impact in the transport sector has been *moderate*.

The Bank has had three projects in the last five years in the MEI sector. The Kaunas Water and Environment Project, a follow-up to an earlier transaction, targets private sector participation, improvements in the regulatory framework and demonstration effects of a loan without municipal guarantee. A second project, signed in 2003, aims to assist the municipality of Vilnius in enhancing its budgeting process related to urban infrastructure. More recently, in 2004, the Bank signed a corporate loan to the Kaunas Public Transport Company, targeting commercialisation, tariff reform and regulatory reform of municipal transport. Overall *significant* transition impact in the MEI sector since 2000.

Energy

The Bank has had a wide-ranging involvement in the Lithuanian energy sector. Early on, the Bank has had one project in the Lithuanian power sector, an emergency rehabilitation loan in 1992. The Bank played a leading role in the establishment of the Ignalina Decommissioning Fund and continues its active role in its administration.

In the Energy Efficiency sub-sector the Bank has been involved in one ESCO operation in Lithuania. Overall *moderate* transition impact in the Energy sector since 2000.

Enterprise

The Bank made four agribusiness investments in Lithuania, aimed at restructuring key companies, providing positive examples of corporate governance, attracting strong strategic investors and enhancing competition.

The Bank supported two industrial companies, Paroc Silikatas - an insulation material manufacturer- with a loan in the mid 90's, and Drobe Wool - one of the largest Eastern European manufacturers of pure wool and wool blend fabrics - with equity and debt in early 2000.

The Bank has been involved in the early stage of privatisation of Lietuvos Telekomas through a loan aimed at restructuring the state-owned enterprise. The Bank also participated in the second stage of LT’s privatisation, when it underwrote a number of shares of the company during its IPO and provided assistance on the redrafting of the legal framework for telecommunications.

The provision of finance to SMEs has progressed much more slowly than in the other new EU members. In Lithuania the SME sector was reached through a credit line under the EU SME Facility to Siauliu Bankas. Given the structure of Lithuania’s economy, in which the vast majority of enterprises are SMEs, the Bank’s contribution as a core investor in private equity funds has enabled equity investments in a number of SMEs in Lithuania. The Bank has invested in seven equity funds in the Baltics which have invested €51 million in 24 companies in Lithuania. Other companies in Estonia and Latvia in which the EBRD-supported equity funds have invested have themselves established subsidiaries or acquired companies in Lithuania.

Overall *minimal* transition impact since 2000 in the Agribusiness sub-sector, *significant* in the Telecoms sub-sector.

Financial sector

The Bank helped to facilitate the privatisation of LZUB's, the third largest bank in the country, to a foreign investor through a swap of shares in LDB for shares in LZUB. In August 2004 a €11 million subordinated loan was provided to Nord LB Lietuva (formerly LZUB) to support the growth of the bank, particularly in the areas of corporate and mortgage lending. As a result of the successful relationship (SME and Warehouse Receipts) and transition achieved by Siauliu Bankas, the EBRD made an equity investment in such bank in June 2005, acquiring a 16 per cent stake. The EBRD also arranged in September 2005 a €12 million medium-term syndicated loan for Siauliu Bankas.

In the non-bank financial sector, the EBRD participated in the successful privatisation of the dominant state-owned insurance company - Lietuvos Draudimas - to Codan (Denmark) as a foreign strategic investor. Through its involvement the Bank contributed to the introduction of new products in the life and non-life insurance sector, and to the dissemination of critical skills in the sector.

Equity funds targeted the Baltics later than Central Europe, and the Bank has been active in the Baltics since the late 1990s through a number of regional pan-Baltic private equity funds. Of these funds' total of over 70 investee companies, 24 are in Lithuania.

Overall *moderate/significant transition* impact in the financial sector since 2000.

Overall assessment

The Bank's strategies for Lithuania from 2000 addressed the evolving needs of the Lithuanian economy, which is characterised by the high proportion of SMEs among corporate entities and by under-developed municipal infrastructure throughout the country, as well as the increasing interest of Lithuanian enterprises to invest abroad.

Since 2000 out of the Bank's over €230 million investments in Lithuania (including regional), 39 per cent have been in the private enterprise sector, 32 per cent in infrastructure and MEI, 17 per cent in the financial sector and 12 per cent in equity funds.

Policy dialogue

In preparation of the liberalisation of the energy market in Lithuania the Bank maintained effective policy dialogue with the authorities relating to the setting up and strengthening of the Energy and Price Commission. The telecommunications market was fully liberalised on 1 January 2003.

In 2002 the Bank provided support and comments when changes to the procurement law were being prepared.

In 2002 and 2003 legal technical assistance was provided by the EBRD for the development of Lithuania's concession law and in 2003 a new Concessions Law was enacted (with effect on 1 October 2003).

The policy dialogue initiated by the Bank eventually led to the approval and implementation of the warehouse receipt law in July 2002.

1.3.2 Selected lessons learned

The Bank's experience in Lithuania in recent years has resulted in a variety of lessons learned, the most important of which are the following:

Well structured **non-sovereign financing to state or municipal-owned companies**, including private sector participation where appropriate, helps to apply commercial discipline to the borrowers and to reduce budget pressures in the public sector. The success of **concession** will be dependent on the reliability of implementation of negotiated tariff and of their ongoing regulation.

Early equity investments and credit lines to the **financial sector** strengthen corporate governance and enable growth of the corporate sector. A key rationale of Bank operations in the financial sector is to increase the confidence of international markets in banks and the banking sector of countries of operation. Faced with forceful demands to match the market terms for a good client, the Bank should be willing to consider re-pricing its credit line.

By agreeing to amendments of the credit line to allow on-lending of the client bank's leasing subsidiary, the Bank facilitated the development of the **leasing sector** in Lithuania while at the same time increasing penetration of the **SME sector**. The Bank should be responsive to positive market developments and be prepared to agree changes to project conditions where these contribute to achieving Bank objectives.

The Bank should investigate cautiously the prospect for managerial and **corporate governance** changes before engaging in serious negotiation with a company. The Bank's role and objectives as well as the terms and conditions of its financing should be communicated clearly and early to all parties involved in a project.

The level of work involved in the appraisal and execution of a **Multi Project Facility** will only be fully justified when there is a strong pipeline of projects with a high degree of certainty. However, changes in the markets or strategy of the Sponsor are unforeseen events and the Bank's ability and willingness to extend an MPF to a dedicated Sponsor have to be judged with a long-term perspective in mind.

1.4 Financial performance of the existing portfolio

During the last two years the quality of the Lithuanian portfolio measured by the overall portfolio risk category improved markedly from 5.9 in December 2003 to 4.8 in

November 2005. This compares with a risk rating of 5.4 for the Bank as a whole and 4.8 for Central Europe.

1.5 Mobilisation of co-financing

Overall mobilisation ratio (total project cost/EBRD financing) is 2.4. In 2005 the Bank arranged a syndicate of €12 million to Siauliu Bankas with commercial banks taking up €7 million. The Bank's continuing support to the private equity industry focusing on SMEs is essential for raising second generation funds with majority private capital.

2. OPERATIONAL ENVIRONMENT

2.1 General reform environment

2.1.1 Political environment

Lithuania continues to meet the conditions specified in Article I of the Agreement Establishing the Bank. Since independence, Lithuania has been a constitutional parliamentary democracy, with a 141-member single-chamber Parliament; a directly elected President; and a government whose ministers are nominated by the Prime Minister, appointed by the President, and approved by Parliament. The government respects human rights, the judiciary is independent and the Ministry of the Interior oversees the police force. Civil and political society in Lithuania is vibrant, although there are some concerns about media independence. Lithuania acceded to both the EU and NATO in 2004.

The parliamentary elections in October 2004 produced no outright victor. Prolonged post-election negotiations resulted in a centre-left government under Prime Minister Algirdas Brazauskas, veteran leader of the Social Democratic Party (SDP) and former President. The coalition includes Brazauskas' SDP; the recently-established Labour Party headed by the controversial Russian-born businessman Viktor Uspaskich; the New Union-Social Liberals (NU) led by Arturas Paulauskas; and the Union of Farmers/New Democracy Party of Kazimiera Prunskiene. Brazauskas's reform-oriented SDP secured control of the premiership and the powerful Finance Ministry, but infighting within the coalition broke out almost immediately, arising in part from opposition within the SDP to the coalition with Uspaskich and the possible conflicts of interest involving the Labour Party, many of whose deputies are businessmen.

Tensions within the governing coalition have increased significantly since Uspaskich resigned from the post of Economy Minister in June 2005 in the wake of allegations of conflict of interest. Since Uspaskich's resignation, several Labour Party-supporting media outlets have launched a series of attacks on both Brazauskas and civil society organisations with ties to the George Soros-financed Open Society Fund. During this period Brazauskas' popularity has declined sharply while Uspaskich's popular support has recovered close to the level he enjoyed prior to his resignation. New parliamentary elections are not officially due until 2008 but could take place sooner, chiefly because of the fragility of the coalition. A more detailed political and social assessment is provided in Annex 7.

The far-reaching implementation of structural reforms and sound policies in the decade since independence allowed Lithuania to progress significantly on the transition to a functioning market economy. By the end of the 1990s, Lithuania was a successful open economy with a thriving private sector. In recent years, the reform agenda has focused on the adoption of the EU *acquis communautaire*. Since the last strategy, progress has continued on the reform front, and a number of high-profile companies have recently been privatised, including the national carrier Lithuanian Airlines, gas utility Lietuvos Dujos and the National Stock Exchange of Lithuania.

Accession to the European Union and entry into ERM II have further reduced the distance with the more advanced European economies. Although much has been achieved, challenges remain. Further improvements to public administration and the judiciary, as well as investments in the less developed regions of the country, are needed to support private sector growth and sustain productivity increases across the country. With the labour supply shrinking as a result of migration to neighbouring EU countries, further employment growth depends on sustained labour market flexibility and improvements to the vocational education and training system. This will contribute to shift the basis of the country's competitiveness from cheap labour to value added. Most importantly, the recent record of fiscal discipline needs to be maintained to keep the external position under control and to allow for EMU membership in the agreed timetable.

2.1.2 Macroeconomic conditions relevant for Bank operations

Real GDP grew by 7.5 per cent in 2005. The economy's performance was supported by favourable external conditions, which helped to bring about low interest rates and declining unemployment. This in turn resulted in strong growth in domestic consumption and investment demand. Following a slowdown in the first months of 2005, partly the consequence of the shutdown of the first block of the Ignalina Nuclear Power Plant, economic growth picked up again in the course of the year on the back of investment-led productivity increases. In the first half of 2005, value added growth was highest in market services, notably in hotels and restaurants, transport and communications and trade, followed by the manufacturing and construction sectors. Internal demand remains strong, especially among consumers, and the recent flow of EU funds results in increased production and higher competitiveness. In the medium term, growth is expected to drift down toward its potential, currently assessed at around 6 per cent as external conditions deteriorate. Real convergence is still a long way away, as Lithuania's GDP per capita stands at about 40 per cent of the EU average. Furthermore, growth composition indicates that the distribution of activity across sectors and geographic regions remains uneven.

Unemployment is rapidly falling on the back of the fast pace of economic growth. In 2004 unemployment declined to 11.4 per cent from over 16 per cent in 2000. The rate fell further in 2005 and reached 7.2 per cent in the third quarter. Long-term unemployment accounts for almost 60 per cent of total unemployment, with the elderly being worse off as they find it increasingly difficult to adapt to the needs of the labour market. Regional differences in unemployment and shortages of skilled labour remain. Vocational education and training systems need updating in order to equip the workforce with skills relevant to the private sector needs. Furthermore, demographic developments are not favourable and the size of the labour force has been shrinking since 2003. Labour supply and the structure of the labour force are significantly affected by the continuing process of migration to other European countries, particularly among young people. As the labour supply shrinks, real wages increase. According to Statistics Lithuania, average monthly real gross earnings grew by 7.2 per cent in 2004 and by 8.3 per cent year-on-year in the first quarter of 2005. Unless matched by productivity gains, these increases may affect the country's competitiveness in the long run.

Annual average inflation was moderate in 2004, reaching 1.2 per cent by year-end, but it has been accelerating in the course of 2005. In the period August 2004 – July 2005, average annual inflation amounted to 2.7 per cent. Upward pressures on prices have materialised through rising excise taxes, administered prices and oil and gas price increases. The inflationary trend is expected to continue in the near future as commodity prices remain high. The State Control Commission for Prices and Energy has recently announced that natural gas prices for Lithuanian consumers will rise by 29 percent on average in 2006 as a result of Gazprom's decision to increase the prices of gas for Lietuvos Dujos, the Lithuanian distributor. Wage growth has also been accelerating since EU membership last year, and salaries grow faster than productivity in most sectors of the economy. The authorities are aware of the risk to EU convergence that increasing inflation entails. However, they remain convinced that inflation can be contained within the Maastricht limit.

Following an uneventful transition from the US dollar peg to the euro peg in 2002, Lithuania joined ERM II in June 2004 with its existing currency board arrangement. The litas is pegged to the anchor currency euro at a fixed exchange rate of 3.4528 litas per euro without fluctuation band (a commission fee charged by the central bank for exchanging the anchor currency is LTL 50, irrespective of the amount exchanged). The amount of litas in circulation is fully backed with gold and convertible foreign currency reserves. This system's decade-long track record, the clear exit strategy into EMU and the significant excess reserve coverage make the currency board credible, as indicated by the low spreads on euro-denominated bonds. In addition, a considerable amount of political capital has been spent on EMU membership by January 1, 2007. While recognising the risks coming from inflation, the IMF, in its last Article IV Consultation, has confirmed that the country is on course to make that deadline. Despite some degree of attachment to the litas as a symbol of the country's independence, political support for adopting a single currency continues to be strong across the political spectrum.

Raising expenditures contributed to a slight loosening of Lithuania's fiscal stance in 2004, although methodological changes in fiscal statistics resulted in a downward revision of the government deficits numbers since 2000. The general government deficit accounted for 1.4 per cent of GDP in 2004, up from 1.2 per cent the year before. In spite of better then expected revenues on the back of economic growth and improved tax collection, in 2005 Lithuania's economy has continued to receive stimulus from public salary increases, higher pension benefits and increasing co-financing obligations. In 2005, the Parliament approved a decrease in the personal income tax from the current 33 per cent down to 27 per cent starting from July 2006 and then down to 24 per cent in 2008. To compensate for the loss in revenues, additional taxes on profits and residential property used for commercial purposes will be introduced in 2006. The government introduced a temporal increase in the corporate profits tax rate to 19 per cent for 2006 and 2007, before returning to the current 15 per cent in 2008. The general government debt fell below 20 per cent of GDP in 2004, well below the 60 per cent Maastricht requirement. Foreign debt accounts for about two thirds of it, while short-term debt is some 5 per cent of total debt.

The current account deficit increased in 2004. Following EU membership and expectations of strong future growth, investment rates continued to increase while the savings rate fell. As a result, the current account deficit widened to 7.7 per cent of GDP in 2004 up from 6.9 the year before. This increase reflects changes in the trade and income balances, as imports grew faster than exports and profits on FDI were repatriated. The trade deficit has improved over the course of 2005, when export growth picked up significantly. In the first half of 2005, export growth was highest in mineral products and re-export of food product and chemical goods. Foreign trade trends are expected to continue on the back of high import growth in some of Lithuania's main trading partners, notably the CIS and neighbouring EU members. As a result, the current account deficit is expected to stabilise at about 7 per cent in the near future. FDI financing accounted for only one third of the current account deficit in 2004 but is expected to increase in 2005 as a result of a green-field investment in the PET plant in Klaipeda.

The banking system is wholly privatized and very competitive. The sector is highly concentrated, with the top 3 banks – Vilniaus Bankas, Hansabankas and Nord/LB – accounting for 68 per cent of the banking assets. Despite fierce competition and decreasing margins, the sector continues to be profitable. Foreign ownership, mostly from Nordic countries, is widespread and accounts for 87 per cent of the capital of commercial banks. This led to managerial and operational skill transfer that resulted in the restructuring and recapitalization of the system, the introduction of a wider array of products and services and improved corporate governance and transparency. The harmonization with EU directives has been the main driver in legislative reforms in the field of banking supervision. Financial supervision has been stepped up both on- and off-site and benefits from close cooperation with Nordic peers.

2.1.3 Transition success and transition challenges

Lithuania has made remarkable progress in transition in the last decade. In many areas of structural reforms the country took the lead among the transition economies. The transition indicator scores published in the 2005 Transition Report indicate that Lithuania is, on average, among the most advanced in transition in the new EU member states under the seven categories measured. In three categories – price liberalisation, trade and foreign exchange liberalisation and small-scale privatisation – Lithuania has already achieved standards of a well functioning market economy.

Nevertheless, a number of transition challenges remain. The 2005 Assessment of Transition Challenges highlighted the following challenges for Lithuania. Please refer to the snapshot table in Annex 5 for individual sector-by-sector ratings and to the table on comparative Structural Change Indicators in Annex 6 for more detailed transition indicators.

Infrastructure, environment and energy

Following the unbundling of Lietuvos Energija in 2002, remaining challenges in the **power** sector relate to energy generation and distribution. As for the former, Lithuania closed Unit 1 of Ignalina at the end of 2004 as agreed during the EU accession process, and is committed to close Unit 2 by 2009. By then Lithuania will become a net importer of power from Russia, on which it already relies for natural gas. To reduce this dependence, the 1,800-MW Lithuanian Power Plant is being upgraded, a power link with Poland is being discussed, and a sea cable between Sweden and Lithuania is being studied. On 27 February 2006 the Prime Ministers of Lithuania, Latvia and Estonia signed a declaration in which they support the objective aimed at reducing the dependency of the Baltic States on one dominant supplier of energy resources and invite energy enterprises to participate in the construction of a new nuclear power plant in Lithuania. This, however, would be a costly and long-term option. As for energy distribution, the privatisation of one regional company (Rytu Skirstomieji Tinklai) is still on hold. There has been progress in adjusting electricity tariffs to reflect long run marginal cost. Market opening is taking place in line with the new electricity law and commitments made under the EU negotiations.

As for the **MEI** sector, municipal infrastructure is decentralised and commercialised. There is significant private sector participation in district heating and to a lesser extent in urban transport. Remaining challenges concentrate in the water services, which are still operated by publicly owned companies.

As an EU member state and Kyoto protocol member, Lithuania is in the process of implementing a comprehensive set of institutions and incentives to deal with **energy efficiency**. A market has been created and a few ESCOs are active.

In the **telecommunication** sector, the dominant fixed line incumbent has been fully privatised through sale to a strategic investor and an IPO. The Lithuanian telecoms market was fully liberalised in January 2003. However, effective competition has been hindered by ongoing negotiations with the dominant operator as to interconnection.

In the **railways** sector, operating and policy setting functions have been separated, but core railway businesses are operated by the same entity. There is an independent regulator. Infrastructure access is granted legally but is not fully working in practice yet.

In **roads**, all construction entities have been divested and privatised. The road fund was established in 1996.

Enterprise sector

Since the last strategy period, there has been significant progress in the **general industry** sector with the recent privatisation of national carrier Lithuanian Airlines, power line construction company Elektros Tinklu Statyba, gas utility Lietuvos Dujos and the National Stock Exchange of Lithuania. However, improvements in public administration and judiciary are paramount to strengthening the sector. Although lower than in most transition countries, corruption is still relatively high compared to standard developed market economies. Expansion of private enterprises and completion of restructuring of former state owned companies, particularly in less developed regions, remain key issues.

In **agribusiness**, Lithuania maintained a system of price supports throughout the transition and is now integrating into the EU's CAP. Land ownership rights have been restored to almost all claimants, but obtaining titles has been cumbersome. Ownership by foreigners and legal entities is being phased in. Privatisations of agribusinesses is essentially completed, but as in other accession countries new owners still have to reduce costs, improve efficiency and upgrade hygiene standards in order to become internationally competitive. Transport, storage, marketing and retail facilities need to be modernised further. Credit to the agricultural sector is increasing and a functioning warehouse receipts system exists.

With minimal natural gas reserves and no natural gas production, Lithuania is completely reliant on **natural resources** imports. The privatisation of the country's gas transmission and distribution monopoly Lietuvos Dujos (Lithuanian Gas) was finalised in 2004 with the sale of 34 per cent stake to Russia's Gazprom (another 34 per cent stake in the company was sold to a German consortium in 2002). Russia's Yukos is currently holding some 53.7 per cent stake in the country's only refinery Mazeikiu Nafta. However, the government is considering buying Yukos'shares and sell them to another investor, to which it could offer 20 per cent from its 40.66 per cent holding.

The **property** sector is developing fast, including new types of real estate as well as financing instruments. There is little state interference in the sector. Land is fully tradable except for foreigners.

Lithuanian enterprise sector faces the challenge of meeting more stringent environmental requirements through the implementation of EU environmental legislation, particularly the Integrated Pollution Prevention and Control Directive, requiring them to meet the environmental standards that can be achieved with the use of Best Available Techniques.

Financial sector

The basic regulatory framework in the **banking sector** is in place but financial sector supervision requires better coordination between the institutions responsible for banks and non-bank institutions. The number of banks is stable and a majority is foreign-owned. Regarding market institutions and policies, privatisation has been finished, with state-owned banks having no significant asset share. Market-based conduct, approached through the domestic credit to private sector/ GDP ratio, is low.

In the **non-bank financial sector**, **s**ecurities markets legislation and regulation almost fully meet IOSCO standards. Insurance legislation and regulation almost meet IAIS standards but the capacity of the regulator should be further enhanced. The size of capital markets is comparable to other EU members in CEB but insurance penetration is low. There are both mandatory and voluntary privately managed pension funds. The leasing sector is thriving.

Although the **private equity fund** sector remains small, there has been a renewed interest by private investors from Scandinavian countries who appear increasingly committed to private equity investments in the Baltic States. Increased business activity by equity funds, including offering a broader range of financial instruments, is needed to improve the visibility of the sector.

As for the **SME** sector, the business environment is becoming more dynamic. According to the World Bank's "Doing Business" report, starting a business requires eight different procedures and takes an average of 26 days, at a cost equal to 3.3 per cent of gross national income (GNI) per capita, lower than the average cost for OECD countries (6.5 per cent). There is no credit registry, but a private credit information bureau provides information on 4.4 per cent of the population. The cost of registering collateral is lower than in OECD countries. Local banks and leasing companies have started to extend loans and leases to smaller companies, often under IFI-supported credit lines.

2.2 Access to capital

Domestic credit

Financial intermediation remains moderate, with domestic credit expected to exceed 30 per cent of GDP in 2005, amongst the lowest levels in new EU member states. However, a combination of low interest rates and robust economic growth resulted in a significant expansion of domestic credit in 2004 and the first half of 2005. Credit to households expanded at an especially fast pace, notably for real estate purchases. However, such an expansion has not undermined the quality of the loan portfolio, which remains high with non performing loan ratios at about 2 per cent of total loans. As private activities thrive, the composition of the loan portfolio of commercial banks is shifting away from the public sector towards private enterprises and households. Although specific loan provisioning has not grown in line with credit expansion, capital adequacy is above the required level. Leasing and factoring have also increased rapidly in importance in the past years to the advantage of SME financing.

Capital market

Capital markets are developing slowly and remain dominated by central government securities with maturities extending to 10 years. The Lithuanian Securities Commission and the National Stock Exchange of Lithuania – currently renamed Vilnius Stock Exchange (VSE) – were established in 1992. Market capitalisation and turnover have since risen, as have the number of financial intermediaries. At the end of 2004, some 40 companies were listed on the VSE and the overall capitalisation amounted to LTL 24.601 billion (€7.1 billion). The VSE is the only regulated secondary securities market in Lithuania, offering trading, listing and information services. It is part of OMX Exchanges which also operates exchanges in Copenhagen, Stockholm, Helsinki, Tallinn and Riga and offers access to 80 per cent of all securities trading in the Nordic and Baltic marketplace. In the future, regional integration and cross-border transactions will play an increasingly important role in the development of Lithuania's capital market.

Foreign direct investment

While robust economic performance and low overall wages make Lithuania an attractive destination for investment, levels of FDI per capita remain the lowest in the EU. According to the Central Bank, accumulated foreign direct investment in Lithuania stood at LTL 17.53 billion (€5.08 billion), or LTL 5,128 (€1,485) per capita in the first quarter of 2005. FDI inflows were particularly large in 1998 and 2002, following the privatisation of Lietuvos Telekomas and Mazeiku Nafta. Net FDI inflows increased sharply again in 2004 (to reach €423 million) and are expected to increased further (to around €550 million) in 2005 as a result of a green-field investment in the PET plant in Klaipeda. The largest foreign direct investment flow in Q1 2005 was recorded in the manufacturing industry (LTL 234.2 million), electricity, gas and water supply activities (LTL 178.4 million), and financial intermediation (LTL 174.4 million). On 31 March 2005, investment in the manufacturing industry accounted for 32.8 per cent of total foreign direct investment in Lithuania, retail and wholesale trade for 14.7 per cent, financial intermediation for 14.4 per cent, and transport, storage and telecommunications for 13.3 per cent. The largest investors by country were Sweden (14.2 per cent), Denmark (13.7 per cent), Germany (12.9 per cent), Russia (12.6 per cent), Finland (7.6 per cent), and Estonia (7.1 per cent). Investment from the EU (25 Member States) accounted for 72.7 per cent of total investment, of which investment of old EU Member States (15 countries) accounted for 61.7 per cent, while investment of the CIS countries made up 12.9 per cent.

2.3 Legal environment

Over the past years, Lithuania has achieved substantial progress in the transition process and the EU accession in May 2004 has further contributed to the transition to a market-oriented economy. In most areas related to investment activities, Lithuania has overall reached a fairly high level of compliance with international standards. Thus, the assessment conducted by the EBRD (as detailed in Annex 10) shows that generally the legislation with respect to corporate governance is quite effective and highly compliant with the OECD Principles of Corporate Governance. Likewise, over the past years, Lithuania has continued to supplement or amend its laws and regulations with respect to capital markets to address previous shortfalls and has now achieved high compliance with international standards. The concessions law adopted in 2003 (with the EBRD's technical assistance), which is based (among other things) on the UNCITRAL Legislative Guide on Privately Financed Infrastructure Projects, is a comprehensive law in line with the EU recommendations and in very high compliance with internationally accepted good standards. In terms of secured transactions, although some improvements may be advisable as described in Annex 10, there have been no significant changes over the past two years to the legislation in place, and this legislation is generally well implemented and enforcement of security seems to be efficient. Among the areas where improvements are needed are the insolvency laws: the assessment conducted by the EBRD (see Annex 10) shows that such laws are not efficient in practice and that there are still key issues that need to be addressed in such area, such as the failure to establish clear balance sheet tests for insolvency, the lack of specific qualifications or requirements for insolvency administrators or the failure to address adequately the possible reorganisation of insolvent companies.

3. STRATEGIC ORIENTATIONS

3.1 Bank's priorities for the strategy period

Given the success of the transition in Lithuania to date, in response to the few remaining transition challenges identified, and considering the Bank's ability to address them, the main focus of the Bank's activities during the strategy period will be the following:

- In the infrastructure sector the Bank will support the upgrade of state transport infrastructure and municipal infrastructure, particularly in regional cities and towns, while actively promoting energy efficiency and the use of renewable energy. The Bank will seek to promote development of a Baltic energy market among the three Baltic States as well as the Polish-Lithuanian Interconnector. The decommissioning of INPP will translate into energy projects eligible for IIDSF support with co-financing from the Bank.

- In the enterprise sector the Bank will provide primarily equity investments and other intermediate capital to companies with projects requiring extensive restructuring or corporate governance support, or cross-border investments, for example into or from Russia or other CIS countries.

- Where appropriate, the Bank will support the privatisation of remaining partially state-owned enterprises as well as the development of Private Public Partnerships.

- In the financial sector the Bank will continue to work with selected financial intermediaries on providing equity and debt funding primarily to the SME sector.

- Encourage the development of local capital markets, for example in investing in the local securitisation of mortgage loans.

- Support enterprise sector in meeting EU environmental requirements based on the use of Best Available Techniques

The Bank will be responsive to other opportunities that may arise, but will concentrate on the priorities outlined above.

3.2 Sectoral challenges and Bank objectives

In line with the transition challenges identified above and in Annex 5, the EBRD will focus on the following sectoral priorities.

3.2.1 Infrastructure, environment and energy

Transition challenges

There is limited private sector participation in municipal sectors particularly water and sewage, urban transport and in state transport infrastructure. There are significant unnecessary operating costs due to heat losses from municipal-owned heating networks and buildings and privatised industrial enterprises. The privatisation of one of the two electricity distribution companies is on hold. The closure of INPP is a key challenge and after closure Lithuania will be reliant on natural resources imported from Russia for most of its energy generation needs.

Operational priorities

- Encourage and support private sector participation in the financing of municipal infrastructure and in state transport infrastructure. This could be achieved with a variety of private public partnerships, possibly complemented with EU funding.
- Include greater energy efficiencies in project design, implementation and operations.
- Support the development of alternative energy sources and of the Baltic power ring as well as the Polish-Lithuanian Interconnector

3.2.2 The enterprise sector

Transition challenges

Improvements in public administration and judiciary are key remaining issues in the enterprise sector and corruption is still relatively high. Increased business activity by equity funds, including offering a broader range of financing instruments, is needed. Expansion of private enterprises and completion of restructuring of former state owned or still partially state owned companies, particularly in less developed regions, are important.

Operational priorities

- Provide primarily equity and mezzanine investments to companies with potential but that require restructuring or corporate governance support, or cross-border investments, for example into or from Russia or other CIS countries.
- Support the privatisation where appropriate of remaining partially state-owned enterprises.

3.2.3 The financial sector

Transition challenges

Financial intermediation in Lithuania remains low, particularly to the SME sector. There is a lack of equity and mezzanine capital to support economic growth.

Operational priorities

- Provide funding and subordinated financing to selected financial institutions to support funding primarily for corporate lending, also in the less developed regions.
- Selectively commit capital to new equity funds, particularly those which focus on SMEs.

4. CO-OPERATIONS WITH OTHER IFIS

European Union (EU) – The EU committed a total of €1,503 million in Structural and Cohesion Funds for the period 2004-06. Structural funds amount to €895 million and are allocated to the following priority areas: social and economic infrastructure (€347 million), human resources development (€164 million), development of productive sector (€222 million); rural development, agriculture and fisheries (€135 million); and technical assistance (€27 million). The total Cohesion Funds in the period 2004-2006 attributable to Lithuania amounts to €608 million to co-finance infrastructures in the environment and transport sectors. The Bank has worked with the EU in relation to the SME Finance Facility which the EU has supported and the Bank has implemented as a SME credit line to Siauliu Bankas. The Bank has co-financed together with ISPA two projects, Kaunas Water Phase II and Lithuanian Railways Corridor IX. In addition, the Bank will participate in the Jasper and Jeremie initiatives aimed at improving the use of available resources in line with the Lisbon agenda.

International Monetary Fund (IMF) – Lithuania joined the IMF in May 1992. Throughout the course of the 1990s and until last year, Lithuania requested from the IMF one Extended Fund Facility (from 1994-97) and 2 Stand-By Arrangements as a precautionary measure. The latest SBA was approved in August 2001 for the amount of SDR 86.5 million and expired successfully in March 2003 with all performance criteria met. Lithuania has not had financial obligations to the IMF since February 2005. The Article IV consultations are held on the standard 12-month cycle.

World Bank – Lithuania joined the World Bank in 1992. Since then, the World Bank support has helped the government implement structural reforms and build capacity at the sector and local levels, improve SME access to finance, and tackle the cleaning up of the Baltic Sea. To date, World Bank's commitments have totalled US$ 490.8 million for 17 operations. The World Bank is still active in the country and three projects are currently under implementation (health, education and infrastructure). As in other new member states of the EU, the partnership between Lithuania and the World Bank is now focused on supporting institutional development for rapid convergence to EU levels of income and for effective use of EU structural funds, and no new projects are currently envisaged. Given the differing objectives and sectoral priorities of the respective institutions, the Bank has not collaborated on any concrete projects with the World Bank in Lithuania.

International Finance Corporation (IFC) – Lithuania joined the IFC in 1993. Since then, the IFC has invested US$ 58 million from its own account and mobilized US$ 9 million in syndications from other banks in five projects in the food processing, textile, finance, construction materials, and electronics industries. In addition, the IFC completed a number of donor-funded technical assistance projects, focused on improving the investment climate, developing small and medium enterprises, and helping with the leasing sector and privatization. Following Lithuania's accession to the EU, IFC's role in the country is changing and its focus will shift to the regions, sectors, and projects where private financing remains limited, emphasizing socially and environmentally sensitive sectors. The Bank has co-invested with IFC in Drobe Wool, a Lithuanian textile company.

European Investment Bank (EIB) – Since 1992, the EIB has committed a total of €455 million for projects in Lithuania, mainly for infrastructure (energy, roads, rail-corridors, airport, water systems) and small and medium-sized enterprises (SMEs) through global loans to banking intermediaries. EIB's priorities in Lithuania are to support projects that help integrate the economy into the EU Single Market and contribute to the application of European standards as developed in the *acquis communautaire*. The Bank has collaborated on the Lithuanian Railways Corridor IX project with EIB.

Nordic Investment Bank (NIB) – Lithuania became a member of the Nordic Investment Bank in January 2005. However, the NIB has been active in the country since its independence through the Baltic Investment Programme (BIP). Later, the NIB financed investment loans for major individual projects in energy efficiency, water utility and power generation sectors. The Bank has not collaborated on any concrete projects with NIB in Lithuania since the co-investment into the Lithuanian Development Bank in 1994.

Kreditanstalt für Wiederaufbau (KfW) – KfW has provided financing to support the private enterprise sector through SME development. In addition, KfW has financed projects for improving energy efficiency through building rehabilitation. KfW is currently financing part of the €90 million project to develop a new PET production plant in Klaipeda. The Bank has not collaborated on any concrete projects with KfW in Lithuania.

ANNEX 1: COMMITTED PROJECTS PER YEAR

Year	Op Name	Regional/Direct	Total Project Value	EBRD Finance	Debt	Equity
	Lithuania Energy Sector Emergency Investment Project	Direct	33.0	33.0	33.0	0.0
1992	1		33.0	33.0	33.0	0.0
	Lithuanian Development Bank Capital Investment	Direct	5.0	0.9	0.0	0.9
	Transport Project	Direct	39.4	16.0	16.0	0.0
	First NIS Regional Fund	Regional	0.6	0.3	0.0	0.3
	Telecom Development International	Direct	50.2	21.2	21.2	0.0
1994	4		95.2	38.4	37.2	1.2
	East European Food Fund	Regional	4.8	1.0	0.0	1.0
	Paroc Silikatas	Direct	19.6	5.4	5.4	0.0
	Vilniaus Bankas (credit line)	Direct	7.9	6.9	6.9	0.0
	Baltic Investment Fund	Regional	5.8	1.6	0.0	1.6
	Kaunas Water and Environment	Direct	79.3	12.7	12.7	0.0
	Vilniaus Bankas (Lines of Credit)	Direct	6.4	6.4	6.4	0.0
	Vilniaus Bankas (Equity)	Direct	2.5	2.5	0.0	2.5
1995	7		126.3	36.5	31.4	5.1
	Sampo Bankas (formerly LDB) (credit line)	Direct	8.0	2.8	2.8	0.0
	Via Baltica and Lithuania Road Project	Direct	102.2	19.7	19.7	0.0
	New Europe Insurance Ventures	Regional	1.5	0.1	0.0	0.1
	Lithuanian Development Bank Capital Increase	Direct	5.8	0.7	0.0	0.7
1996	4		117.5	23.2	22.4	0.8
	IO Fund - Wood Team Production	Direct	0.3	0.3	0.0	0.3
	PPF - Baltic - Vilkma	Direct	0.7	0.7	0.0	0.7
	Baring Communications Equity	Regional	1.9	0.4	0.0	0.4
	Baltic Small Equity Fund	Regional	4.2	1.9	0.0	1.9
1997	4		7.2	3.4	0.0	3.4
	Innova/98 LP	Regional	2.0	0.4	0.0	0.4
	PPF - Baltic - Trinyciai	Direct	0.9	0.9	0.0	0.9
	PPF - Baltic - Utenos Trikotazas	Direct	3.9	3.9	0.0	3.9
	Vilniaus Bankas Subordinated Loan	Direct	9.2	9.2	9.2	0.0
	Nord/LB Lietuva (formerly LZUB) Subord Loan	Direct	13.6	11.0	11.0	0.0
	Vilniaus Bankas Subordinated Loan	Direct	10.2	10.2	10.2	0.0
	PPF - Baltic - Kauno Pieno Centras	Direct	8.1	8.1	0.0	8.1
	Dalkia - Litesko	Direct	12.8	4.4	3.5	1.0
1998	8		60.7	48.1	33.9	14.2
	Rokiskio Suris	Direct	10.0	8.7	0.0	8.7
	Vilniaus Bankas	Direct	75.0	25.0	25.0	0.0
	Carlsberg MPF - Svyturys	Direct	41.5	9.5	0.0	9.5
	Nord/LB Lietuva (formerly LZUB) Syndicated Loan	Direct	12.7	4.2	4.2	0.0
	Emerging Europe Capital Investors LDC	Regional	8.3	2.2	0.0	2.2
	Drobe Wool	Direct	23.7	8.1	7.0	1.1

Year	Op Name	Regional/Direct	Total Project Value	EBRD Finance	Debt	Equity
	LDB/LZUB Share Swap	Direct	4.8	1.6	0.0	1.6
	IO Fund - Lietuvos Draudimas (equity)	Direct	8.4	8.4	0.0	8.4
	Lietuvos Telekomas IPO	Direct	146.3	51.8	0.0	51.8
	PPF - Baltic - Sonex	Direct	3.5	3.0	0.0	3.0
	PPF - Baltic - Alna	Direct	1.6	1.5	0.0	1.5
	Baltic Investment Fund III	Regional	18.0	3.3	0.0	3.3
	TBIH Financial Services Group N.V. (debt & equity)	Regional	1.3	0.8	0.1	0.6
	EU/EBRD Phase I - Ext. - Siauliu Bankas	Direct	5.0	5.0	5.0	0.0
2000	8		189.0	75.3	5.1	70.2
	DVI, Inc. (debt)	Regional	1.1	0.3	0.3	0.0
	Kaunas Water and Environment Project - Phase II	Direct	73.6	14.7	14.7	0.0
	Lithuania/Warehouse Receipt Programme-Siauliu Bankas	Direct	1.6	1.6	1.6	0.0
	Lietuvos Draudimas	Direct	16.0	5.3	0.0	5.3
	EU/EBRD Phase I - Baltic SME Fund	Regional	5.7	1.0	0.0	1.0
	Lithuania Railways (LG) Corridor IX Project	Direct	94.4	45.8	45.8	0.0
2001	6		192.3	68.7	62.4	6.4
	Askembla Growth Fund	Regional	17.5	6.0	0.0	6.0
	Heitman Central Europe Property Partners Fund II	Regional	3.8	1.1	0.0	1.1
	Danfoss Debt Facility for Industrial Energy Projects	Regional	0.3	0.1	0.1	0.0
2002	3		21.6	7.2	0.1	7.1
	City of Vilnius Municipal Infrastructure Project	Direct	8.5	7.0	7.0	0.0
	EU/EBRD Extension 4 - Hansa Capital	Regional	9.9	5.0	5.0	0.0
	Dalkia Litesko II	Direct	3.8	3.8	0.0	3.8
2003	3		22.2	15.8	12.0	3.8
	VP Market *)	Direct	35.0	35.0	35.0	0.0
	Polish Enterprise Fund V	Regional	0.9	0.9	0.0	0.9
	Kauno Autobusai	Direct	10.0	10.0	10.0	0.0
	NordLB Lietuva	Direct	3.3	3.3	3.3	0.0
	Europolis II	Regional	9.0	2.3	1.7	0.6
2004	5		58.2	51.5	50.0	1.5
	Siauliu Bankas equity	Direct	5.9	5.9	0.0	5.9
	Emerging Europe Convergence Fund II	Regional	3.6	3.6	0.0	3.6
	Siauliu Bankas credit line	Direct	12.0	5.0	5.0	0.0
	Minsk Retail Network	Regional	12.5	5.4	5.4	0.0
2005	4		34.0	19.9	10.4	9.5
TOTAL	**63**		**1,128.3**	**478.7**	**334.0**	**144.7**

*) corporate loan, up to 30% of the total financing plan

ANNEX 2: NET CUMULATIVE BUSINESS BY INDUSTRY

Sector Business Group (SIC)	Sector Team (SIC)	No. of Projects	Total Project Value	EBRD Finance	Debt	Equity	% Share of Commit-ments
Energy	Energy Efficiency	0.2	17	8	4	5	2%
	Power and Energy	1.0	33	33	33	0	7%
Sub-total Energy		**1.2**	**50**	**41**	**37**	**5**	**9%**
Financial Institutions	Bank Equity	3.0	21	12	0	12	2%
	Bank Lending	9.6	162	87	87	0	18%
	Equity Funds	2.2	86	40	0	40	8%
	Non Bank Financial Institutions	1.7	38	20	5	15	4%
Sub-total Financial Institutions		**16.5**	**307**	**158**	**93**	**66**	**33%**
General Industry	General Industry	2.0	43	14	12	1	3%
Sub-total General Industry		**2.0**	**43**	**14**	**12**	**1**	**3%**
Infrastructure	Municipal & Env Inf	4.0	171	44	44	0	9%
	Transport	3.0	236	81	81	0	17%
Sub-total Infrastructure		**7.0**	**407**	**126**	**126**	**0**	**26%**
Specialised Industries	Agribusiness	2.1	99	59	40	19	13%
	Property and Tourism	0.1	13	3	2	2	1%
	Telecoms Informatics & Media	2.0	198	73	21	52	15%
Sub-total Specialised Industries		**4.2**	**310**	**136**	**63**	**73**	**29%**
LITHUANIA TOTAL		**30.9**	**1,117**	**475**	**331**	**145**	**100%**

	No. of Projects	Total Project Value	EBRD Finance	Debt	Equity
Direct	28.6	1,005	438	318	120
Regional	2.4	113	38	12	25
Non-Sovereign	24.9	719	327	182	145
Sovereign	6.0	398	148	148	0
PRIVATE	22.9	677	317	172	145
STATE	8.0	440	159	159	0
DEBT	20.6	760	331	331	0
EQUITY	9.4	358	145	0	145
GUARANTEE	1.0	0	0	0	0

ANNEX 3: SELECTED ECONOMIC INDICATORS

	2000	2001	2002	2003	2004	2005 Estimate	2006 Projection
Output and expenditure				*(Percentage change in real terms)*			
GDP	4.7	6.4	6.8	10.5	7.0	7.5	6.2
Private consumption	5.9	3.7	5.8	11.1	9.7	na	na
Public consumption	4.5	0.7	1.4	3.8	7.5	na	na
Gross fixed capital formation	-9.0	13.5	8.7	11.4	12.3	13.0	na
Exports of goods and services	9.9	21.2	19.5	6.9	4.2	13.0	na
Imports of goods and services	4.8	17.6	17.7	10.3	14.8	11.0	na
Industrial gross output	5.3	15.9	4.6	15.8	9.3	10.4	na
Agricultural gross output	0.9	-5.0	7.9	7.7	-0.8	na	na
Employment[1]				*(Percentage change)*			
Labour force (end-year)	-2.0	-2.1	-0.3	0.7	-1.3	na	na
Employment (end-year)	-4.0	-3.3	4.0	2.3	-0.1	3.9	na
				(In per cent of labour force)			
Unemployment (end-year)	16.4	17.4	13.8	12.4	11.4	7.2	na
Prices and wages				*(Percentage change)*			
Consumer prices (annual average)	1.0	1.5	0.3	-1.2	1.2	2.7	2.8
Consumer prices (end-year)	1.5	2.1	-1.0	-1.3	2.9	3.5	2.5
Producer prices (annual average)	16.0	-3.0	-2.8	-0.5	6.0	na	na
Producer prices (end-year)	2.6	-7.8	1.9	-0.2	6.8	13.5	na
Gross average monthly earnings in economy (annual average)	-1.5	1.4	3.2	4.1	8.5	15.8	na
Government sector				*(In per cent of GDP)*			
General government balance	-2.5	-2.0	-1.4	-1.2	-1.4	-2.0	-1.8
General government expenditure[2]	39.2	35.0	34.2	33.1	33.2	30.5	na
General government debt	23.6	22.9	22.3	21.2	19.5	18.7	na
Monetary sector				*(Percentage change)*			
Broad money (M2, end-year)	16.5	21.4	16.9	18.2	24.1	32.9	na
Domestic credit (end-year)	1.7	13.7	22.3	42.4	41.0	61.6	na
				(In per cent of GDP)			
Broad money (M2, end-year)	22.8	26.1	28.6	30.9	34.9	40.9	na
Interest and exchange rates				*(In per cent per annum, end-year)*			
Interbank interest rate	10.4	5.5	10.0	4.3	3.0	3.3	na
Treasury bill rate (3-month maturity)	5.9	4.8	3.3	2.5	2.1	2.4	na
Deposit rate[3]	1.0	0.8	0.3	0.2	0.2	na	na
Lending rate[4]	10.7	8.1	6.1	5.1	5.6	4.7	na
				(Litai per US dollar)			
Exchange rate (end-year)	4.0	4.0	3.3	2.7	2.5	2.8	na
Exchange rate (annual average)	4.0	4.0	3.7	3.1	2.8	2.7	na
External sector				*(In millions of US dollars)*			
Current account	-675	-574	-734	-1,278	-1,724	-1,875	-1,957
Trade balance	-1,104	-1,108	-1,337	-1,704	-2,382	-2,421	-2,758
Merchandise exports	4,050	4,889	6,031	7,658	9,305	11,056	11,015
Merchandise imports	5,154	5,997	7,368	9,363	11,688	13,477	13,773
Foreign direct investment, net[5]	375	439	714	142	510	655	667
Gross reserves, excluding gold (end-year)	1,359	1,669	2,413	3,450	3,594	3,816	na
External debt stock[6]	4,857	5,268	6,199	8,338	10,472	11,409	na
				(In months of imports of goods and services)			
Gross reserves, excluding gold (end-year)	2.8	3.0	3.5	3.9	3.2	3.0	na
				(In per cent of exports of goods and services)			
Debt service	20.5	15.5	39.1	19.6	16.6	16.5	na
Memorandum items				*(Denominations as indicated)*			
Population (end-year, million)	3.5	3.5	3.5	3.5	3.4	3.4	na
GDP (in millions of litai)	45,848	48,563	51,948	56,772	62,440	70,763	77,255
GDP per capita (in US dollar)	3,260	3,478	4,068	5,360	6,518	7,568	na
Share of industry in GDP (in per cent)	26.3	27.3	26.4	28.3	29.4	na	na
Share of agriculture in GDP (in per cent)	7.0	6.3	6.3	5.8	5.3	na	na
Current account/GDP (in per cent)	-5.9	-4.7	-5.2	-6.9	-7.7	-7.2	-7.0
External debt - reserves (in US$ million)	3,498	3,599	3,786	4,888	6,878	7,593	na
External debt/GDP (in per cent)	42.4	43.4	43.8	44.9	46.6	44.0	na
External debt/exports of goods and services (in per cent)	95.1	87.1	82.5	87.4	89.1	82.9	na

[1] Data from 2000 based on the population census. Previous data from the labour force survey have not been recalculated.
[2] General government expenditure includes net lending.
[3] Average interest rate on demand deposits in litai.
[4] Average interest rate on loans in litai.
[5] Covers equity capital and reinvested earnings.
[6] Includes non-resident currency and deposits and loans to foreign subsidiaries.

ANNEX 4: RATINGS FROM THE 2005 ASSESMENT OF TRANSITION CHALLENGES

LITHUANIA	Structure	Institutions	Conduct	Comments
Agribusiness	*Small*	*Small*	*Small*	Poorly functioning land market. Agroprocessors still need to improve efficiency and standards. Improvements to distribution and traceability are necessary. Credit to the sector is increasing and functioning warehouse receipt system exists.
Banking	*Negligible*	*Small*	*Small*	Basic regulatory framework in place, but supervision requires additional coordination. The number of banks is stable and majority foreign-owned. Domestic credit to the private sector (as % of GDP) is, however, the lowest in the region.
Energy Efficiency	*Medium*	*Medium*	*Medium*	As an EU member state and Kyoto Protocol signatory, Lithuania is in the process of implementing a comprehensive set of institutions and incentives to deal with energy efficiency. A market has been created and a few ESCOs are active.
General Industry	*Small*	*Small*	*Small*	Improvements in public administration and judiciary are key remaining issues in the enterprise sector. Corruption is still relatively high. Expansion of private enterprises and completion of restructuring of former state owned companies, particularly in less developed regions, are key.
MEI	*Small*	*Medium*	*Medium*	Municipal infrastructure decentralised and commercialised. Significant private sector participation in district heating and some in urban transport, while water services still operated by publicly owned companies.
MSMEs	*Medium*	*Medium*	*Medium*	Starting a business carries medium costs. No credit registry is in place but a private credit information bureau exists. Collateral and bankruptcy legislation are moderately supportive of MSME lending. The cost of registering collateral is lower than in many OECD countries.

Natural Resources	*Small*	*Small*	*Small*	The country's gas transmission and distribution monopoly Lietuvos Dujos has been privatised. Following the controversial sale of the country's only refinery Mazeikiu Nafta to Williams Intl in 1999, Yukos acquired a 53.7% stake in the company in 2002, buying out Williams' stake
NBFIs	*Negligible*	*Small*	*Medium*	Securities and insurance markets legislation and regulation almost fully meet IOSCO / IAIS standards but the capacity of the regulator should be further enhanced. The size of capital markets is comparable to other EU members in CEB but insurance penetration is low. There are both mandatory and voluntary privately managed pension funds. Leasing sector is thriving.
Power	*Small*	*Medium*	*Small*	Sector is the only unbundled power market in the Baltic countries. The closure of Ignalina is a key challenge. Privatisation of one regional distribution companies was completed, but the other one is on hold. There has been progress in adjusting electricity tariffs to reflect long run marginal cost. Market opening is taking place in line with the new electricity law and commitments made under the EU negotiations.
Private Equity Funds	*Medium*	*Small*	*Medium*	Although the private equity fund sector remains small, there has been renewed interest by private investor from Scandinavian countries. Increased business activity by equity funds, including offering a broader range of financial instruments, is needed to improve the visibility of the sector.
Property + Tourism	*Small*	*Small*	*Negligible*	Full tradability of land except foreigners. The real estate sector is developing fast, including new types property as well as financing instruments. There is little state interference in the sector.
Telecoms	*Small*	*Small*	*Small*	The dominant fixed line incumbent has been fully privatised, through sale to a strategic investor and an IPO. The Lithuanian telecoms market was fully liberalised in January 2003. However, effective competition has been hindered by ongoing negotiations with the dominant operator as to interconnection.

Transport	*Medium*	*Medium*	*Medium*	In railways, operating and policy setting functions have been separated, but core railway businesses are operated by the same entity. An independent regulator was established. Infrastructure access is granted legally but not fully working in practice yet. In roads, all construction entities have been divested and privatised. The road fund was established in 1996.

ANNEX 5: COMPARATIVE STRUCTURAL CHANGE INDICATORS

	Czech Republic	Estonia	Hungary	Latvia	Lithuania	Poland	Slovakia	Slovenia
Liberalisation								
Share of administered prices in CPI (in per cent)	10.9	26.9	17°	14.3°	19.8	1.2°	19.9	16.7°
Number of goods with administered prices in EBRD-15 basket	1.0	3.0	2.0	2.0	1.0	0.0	2.0	1.0
Share of trade with non-transition countries (in per cent)	80.6*	72*	84*	65.5	63.6	81.7	66.1	77.7
Share of trade in GDP (in per cent)	125.4	125.8	113.9	82.3	93.7	69.8	138.6	100.2
Tariff revenues (in per cent of imports)	0.2°	0.1*	na	0.4°	0.5	1.5*	0.5*	na
EBRD index of price liberalisation	4.3	4.3	4.3	4.3	4.3	4.3	4.3	4.0
EBRD index of forex and trade liberalisation	4.3	4.3	4.3	4.3	4.3	4.3	4.3	4.3
Privatisation								
Privatisation revenues (cumulative, in per cent of GDP)	21.9	7.5	31.1	5.3	13.4	14.5	35.0	4.7
Private sector share in GDP (in per cent)	80.0	80.0	80.0	70.0	75.0	75.0	80.0	65.0
Private sector share in employment (in per cent)	70*	na	na	76.0	na	72*	na	na
EBRD index of small-scale privatisation	4.3	4.3	4.3	4.3	4.3	4.3	4.3	4.3
EBRD index of large-scale privatisation	4.0	4.0	4.0	3.7	4.0	3.3	4.0	3.0
Enterprise and markets								
Budgetary subsidies and current transfers (in per cent of GDP)[1]	9.3	1.8	20.2	5.1	0.4	2.5	1.6	1.5*
Share of industry in total employment (in per cent)	29.7	25.2	33.3*	19.7	20.7*	22.3	29.2	36.3*
Change in labour productivity in industry (in per cent)	10.8	3.9*	7.6*	8.2	14.1*	11.9	2.9	8.8*
Investment/GDP (in per cent)	35.7	29.3	22.5	32.6	21.9*	22.0	na	25.3*
EBRD index of enterprise reform	3.3	3.7	3.7	3.0	3.0	3.7	3.7	3.0
EBRD index of competition policy	3.0	2.7	3.0	2.7	3.0	3.0	3.0	2.7
Infrastructure								
Fixed-line (mobile) penetration rate (per 100 inhabitants)	36.0 (96.5)*	33.9 (72.3)*	33.4 (78.3)	28.3 (52.9)*	25.3 (66.6)	31.9 (45.1)*	24.1 (68.4)*	40.7 (87.1)*
Internet penetration rate (per 10,000 inhabitants)	274.4*	498.9*	357.8*	178.8*	203.8*	203.8*	212.2*	214.8*
Railway labour productivity (1989=100)	69.9*	267.3*	133.9*	129.9*	67.8*	106*	60.5*	150.3*
Electricity tariffs, USc kWh (collection rate in per cent)	8.4 (na)*	6.5 (na)*	11.4 (99)*	7.1 (99)*	9.4 (90)*	9.8 (na)*	10.9 (na)*	na
GDP per unit of energy use (PPP in US dollars per kgoe)	3.2**	2.8**	4.7**	4.1**	3.7**	3.9**	3.1**	4.5**
EBRD index of infrastructure reform	3.3	3.3	3.7	3.0	2.7	3.3	3.0	3.0
Electric power	3.3	3.0	4.0	3.3	3.3	3.3	4.0	3.0
Railways	3.0	4.3	3.3	3.3	2.3	4.0	3.0	3.0
Roads	2.3	2.3	3.3	2.3	2.3	3.0	2.3	3.0
Telecommunications	4.3	4.0	4.0	3.0	3.3	4.0	3.3	3.0
Water and waste water	4.0	4.0	4.0	3.3	3.3	3.3	2.7	3.3
Financial sector								
Number of banks (foreign-owned)	35 (26)*	7 (4)*	39 (29)	23 (10)*	13 (7)*	58 (46)*	21 (16)*	22 (6)*
Asset share of state-owned banks (in per cent)	3*	0*	7.4*	4.1*	0*	25.7*	1.5*	12.8*
Non-performing loans (in per cent of total loans)[2]	5*	0.5*	3.8*	1.5*	2.6*	25.1*	9.1*	9.4*
Domestic credit to private sector (in per cent of GDP)	17.7*	33.7*	42.3*	38.8*	19.9*	17.8*	25*	43.2*
Stock market capitalisation (in per cent of GDP)	17.8*	41.5*	18.7*	9.6*	17.2*	17.3*	7.6*	17*
EBRD index of banking sector reform	4.0	4.0	4.0	3.7	3.7	3.7	3.7	3.3
EBRD index of reform of non-bank financial institutions	3.7	3.3	4.0	3.0	3.0	3.7	2.7	2.7

[1] Subsidies to enterprises and financial institutions, including the Czech Consolidation Agency.

EBRD rates as of mid 2005. Remaining data is for 2004, unless otherwise specified.
°Data for 2005
*Data for 2003.
**Data for 2001

ANNEX 6: POLITICAL AND SOCIAL ASSESMENT

Political context

On regaining independence in 1991, Lithuania established a multiparty, parliamentary democracy. Executive power is vested in the president, who is directly elected for 5 years. The president is responsible for foreign and security policy, and nominates the prime minister, the cabinet and a number of other top civil servants. The parliament (Seimas) has 141 deputies elected for a 4-year term, 71 of whom are elected in single constituencies and 70 from national party lists, with a minimal threshold of 5 per cent for parties and 7 per cent for coalitions. Independent Lithuania has held four presidential and four parliamentary elections, all of which have been deemed free and fair by the international community.

Since 1991, Lithuanian voters have alternated in their support between conservative parties and social democratic parties, particularly the Social Democratic Party led by the current Prime Minister Algirdas Brazauskas. This pattern was interrupted in the October 2000 parliamentary elections in which the Liberal Union and New Union parties won a plurality and were able to form a centrist ruling coalition with minor partners. The leader of the centre-left New Union, Artūras Paulauskas, became the Chairman of the Seimas. However, the government of Prime Minister Rolandas Paksas got off to a rocky start and collapsed within seven months. In July 2001, the centre-left New Union party forged an alliance with the Social Democratic Party (SDP) and formed a new cabinet under Brazauskas. Shortly after his resignation as prime minister, Paksas formed a new party, the Liberal Democrats, and he was elected president in January 2003. However, Paksas was impeached and removed from office in May 2004, following accusations of violating the constitution. Fresh elections in June 2004 returned the popular conservative, Valdas Adamkus, to the presidency.

A new political actor, the Labour Party, appeared on Lithuania’s political scene in late 2003. Led by the Russian-born Viktor Uspaskich, the Labour Party adopted a centre-left populist platform and succeeded in winning the largest share of seats in the October 2004 parliamentary elections. Prolonged coalition talks eventually resulted in a four-party coalition government, comprising Brazauskas’ SDP, New Union-Social Liberals, the Labour Party and the Union of Farmers/New Democracy party. Brazauskas was appointed Prime Minister. Since its formation, the coalition government has been riven by internal tensions and frequent speculation about Uspaskich challenging for the premiership, although the government has been able to maintain a certain degree of reform momentum.

International relations

The priorities of Lithuania’s foreign relations since independence have been integration into Western European security and economic institutions, while maintaining good relations with the Russian Federation, with which Lithuania shares a common border (Kaliningrad) and which remains an important economic partner for Lithuania. In pursuit of the latter objective, Lithuania did not impose ethnic criteria in its citizenship policy in the early 1990s, unlike its other two Baltic neighbours. In pursuit of European integration, successive Lithuanian governments implemented far-reaching reforms to the military, legal and economic systems.

Lithuania succeeded in joining NATO in April 2004 and the EU in May 2004, following a referendum in which 91 per cent of the electorate overwhelmingly backed EU accession. Lithuania was also the first country to ratify the proposed EU constitution, in November 2004. Although the rejection of the constitution by French and Dutch voters has tempered the pace of European integration, the Lithuanian populace remains firmly committed to deepening integration, and Lithuania is currently the only new EU member state likely to join the eurozone on schedule, in January 2007. Under the British presidency, Lithuania has lobbied aggressively, with Poland and the other Baltic States, to retain the relatively high levels of structural funds previously agreed.

Integrity issues

In relative terms, corruption in Lithuania is not a severe problem. According to Transparency International's Corruption Perceptions Index (CPI) – an 'index of corruption indices' – in 2005 Lithuania scored 4.8 out of 10 (with 10 representing the lowest level of corruption). This marked a slight improvement from Lithuania's score of 4.6 in 2004. Furthermore, the increasing number of countries in the 2005 CPI has meant that Lithuania's global ranking improved from the 42nd percentile in 2001 to the 28th percentile in 2005. Since 2001, Lithuania has consistently ranked fourth among the transition countries, behind Estonia, Slovenia and Hungary.

The more detailed 2005 EBRD-World Bank Business Environment and Enterprise Performance Survey (BEEPS) painted a mixed picture of the Lithuanian business environment. Although firm managers reported a general reduction in the obstacles to the operation and growth of their firms across most aspects of the business environment, they also reported a worrying increase in some aspects of corruption, particularly in public procurement. These findings echo the survey-based findings of the non-governmental sector, in particularly Transparency International-Lithuania. TI-Lithuania has recently conducted extensive surveys of public procurement practices which confirmed that bribery of public officials is relatively widespread.

However, some observers argue that the much higher profile accorded to corruption in the media in the past two years – particularly since the impeachment of President Paksas in April 2004 – has raised public awareness of the issue, leading firms to report higher levels of corruption even though objective levels are constant or falling. Furthermore, Lithuania's Special Investigation Service, which was established in 1999 to investigate and prosecute cases of corruption, had its powers significantly strengthened in early 2004. Since then, the annual number of successful prosecutions has doubled, leading both to a further increase in the public awareness of corruption-related issues, and the perception that the government is seriously tackling the issue.

According to the US State Department's Bureau of Democracy, Human Rights and Labor, the Lithuanian government complies with the minimum standards for the elimination of trafficking and Lithuanian law prohibits all forms of trafficking in persons.[1] During 2005, the number of trafficking-related convictions in Lithuania increased and the government expanded funding for anti-trafficking programmes. In June 2005 new amendments to the law on trafficking strengthened penalties for trafficking in persons, including increasing prison sentences for convicted traffickers and exempting victims of trafficking from prosecution. However, human trafficking, particularly in women and girls for the purpose of sexual exploitation, remains a serious problem in Lithuania. The country is a source, transit point, and destination for trafficking in women and girls. Europol estimates that more than 1,200 women and girls in Lithuania are victims of trafficking every year. Lithuanian women were primarily trafficked to Western Europe, while most women trafficked into or transiting the country originated from Eastern Europe. Despite the government's efforts, trafficking convictions and sentences remained low by regional standards. Moreover, both international and local NGOs concerned with human trafficking claim that the problem has increased in Lithuania since accession to the EU.

Social conditions

Population

According to Statistics Lithuania, Lithuania's population was 3.43 million at the beginning of 2004, down approximately 7.1 per cent since 1990. The population decline is attributable to a combination of natural decrease – owing in part to the deterioration in living conditions in the early 1990s – and net migration outflows. Emigration from Lithuania has increased sharply in recent years, from 7,000 in 2002 to more than 15,000 in 2004, and is forecast to remain around 15,000 per year until 2010. Statistics Lithuania estimate that as many as 400,000 mostly young Lithuanians currently reside abroad, while another 300,000 are forecast to emigrate by 2030. The government has responded to increasing migration outflows by authorising a programme "To Encourage Young Emigrants to Return to Lithuania," and the parliament has recently proposed a dedicated Committee to address the issue. Like most EU member countries, Lithuania has an ageing population demographic, which has led the government to raise the retirement age twice; from 2006 the retirement age is 65 for men and 60 for women.

Minorities

Lithuania is the most ethnically homogeneous of the Baltic countries: according to the 2001 census, 83.5 per cent of the population was ethnically Lithuanian. In addition there are 115 nationalities in Lithuania, of which the largest are the Poles (6.7 per cent), Russians (6.3 per cent), Belarussians (1.2 per cent) and Ukrainians (0.7 per cent). There is

[1] US Department of State, Bureau of Democracy, Human Rights and Labor, *Country Report on Human Rights Practices 2005 – Lithuania* (released 8 March 2006). Available at http://www.state.gov/g/drl/rls/hrrpt/2005/61660.htm.

also a small Roma population in Lithuania (approximately 2,600), who continue to live in poor conditions.

Lithuania's legal framework for the protection of minority rights is well developed. Lithuania's citizenship law of 1989 allowed all residents to apply for naturalisation, regardless of ethnicity. Important amendments to a number of laws – including the Penal Code, the Civil Code, the Labour Code and the Law on Education – were undertaken in the early 2000s to comply with relevant EU legislation as well as the UN Convention on Elimination of All Forms of Racial Discrimination. In early 2002 the Ministry of Education approved new regulations permitting the use of minority languages as the primary language of education in compulsory education, and there is an expansive network of state-funded Polish- and Russian-language primary and secondary schools. In 2003, the Seimas Commission for Human Rights prepared a Programme to Combat Intolerance, Racism, Xenophobia and Homophobia as part of the government's National Action Plan for the Protection and Promotion of Human Rights. Providing access to education for Lithuania's Roma population was prioritised within the government's Programme for the Integration of Roma into Lithuanian Society. However, the European Roma Rights Centre has repeatedly criticised many aspects of the governments' policy on the Roma.

Poverty

Strong economic growth and relatively low levels of income inequality in Lithuania have resulted in comparatively low levels of poverty. According to the World Bank's survey-based estimates, less than 3 per cent lives on less than US$ 2.15 per day (calculated in US$ purchasing power parity terms) while approximately 24 per cent of Lithuania's population lives on less than US$ 4.30 per day ($PPP). While income inequality is increasing, poverty is not anticipated to become a significant problem in Lithuania. However, rural poverty remains an issue of concern, particularly as the growth in disposable income is higher in urban than rural areas.

Education

Education in Lithuania is compulsory from the age of six to 16, and more than 50 per cent of Lithuanian children attend pre-school before the age of six. From 16 onwards children in Lithuania can attend either vocational or comprehensive upper secondary schools, and vocational education has been restructured to more flexibly meet the needs of the labour market. Educational enrolment hit a low of 633,000 in 1993, but has since recovered to 810,000 in 2004, in part due to a baby boom in the early 1980s and in part to the growing importance of educational qualifications for the labour market. Continuation to tertiary education has increased almost 120 per cent since 1996, to 183,000 students, although the lack of commensurate increases in tertiary education spending (from a low base) has also led to low wages and a significant increase in corruption in Lithuanian universities. Tuition-based universities now account for approximately 7 per cent of higher education places and the private sector provides virtually all adult further education.

Health

Health indicators declined precipitously in the early 1990s, in the wake of Lithuania's economic collapse. Infant mortality reached a peak of 16.3 deaths per 1,000 live births in 1992, before declining to 7.9 in 2004, according to the World Health Organisation (WHO). Life expectancy also fell sharply in the early 1990s but has since recovered: life expectancy for women, currently 77.8 years, is converging toward the EU mean, although for men it remains low, at 66.5 years. This is largely attributable to continued high levels of alcohol consumption, which was higher in 2004 than in 1986. High levels of alcohol consumption are also correlated with the suicide rate in Lithuania, which is the highest in the world. According to the WHO, the suicide rate among Lithuanian males was 76.5 per 100,000 in 2003, almost five times the EU average.

Health system reforms were implemented in the mid-1990s, including a move away from the highly centralised Soviet system of tertiary care specialists toward greater emphasis on primary care and general practitioners. However, the number of general practitioners remains low by EU standards. The financing of the national health system was overhauled in 1997, with the introduction of employed-funded compulsory health insurance, administered by the State Patients' Fund independently from the Social Security Agency. Private sector healthcare has had little take up. The government remains committed to deepening the provision of primary care. However, as with higher education, the low wages in the health sector have led to high levels of emigration of professionally qualified medical staff (particularly doctors), and corruption in the state-run health system remains an endemic problem.

Labour issues

Unemployment in Lithuania reached its post-independence high of 17.9 per cent (according to ILO methodology) in H2 2001. The unemployment rate fell steadily, to approximately 11 per cent at the end of 2004, and then dropped rapidly to 7.8 per cent at the start of Q4 2005. This steady decline and then rapid drop has been attributed to a combination of increasing employment opportunities presented by Lithuania's rapid growth rate, and the high level of emigration of unemployed younger members of the workforce, particularly following Lithuania's accession to the EU. The pressures on the young to emigrate come in part from the high level of youth unemployment, with unemployment running at 22.7 per cent of those aged 15-24 for the full-year 2004, falling to 12.8 per cent at the beginning of Q4 2005. The labour market continues to suffer from structural imbalances, with falling demand for unskilled labour and increasing demand for highly skilled labour and professionals, while concerns remain about the ability of the Lithuanian educational system to supply the labour market's demands. Although gradually being displaced by increasing employment in the services sector, a disproportionally high percentage of the workforce (15.7 per cent) is still employed in the agricultural sector, while the industrial sector has remained constant at around 28 per cent of the workforce. Trade unions in Lithuania are relatively weak, with a membership of approximately 200,000, or 14 per cent of the workforce. Lithuania's 2003 Labour Law established collective bargaining as the main tool to regulate labour relations and gives employees the right to be represented in collective bargaining by unions or by a work council elected by a secret ballot. However, the US State Department concluded that Lithuanian managers often determined wages without regard to union preferences, except in larger factories with well-organised unions.

ANNEX 7: ENVIRONMENT

The objectives of environment and sustainable development of Lithuania are defined in the National Strategy for Sustainable Development (2003), the implementation period of which extends to 2020. The Strategy, which takes into consideration EU's Sixth European Community Environment Action Programme for 2001-10, formulates Lithuanian sustainable development priorities as follows:

- Moderate economic growth balanced between economic branches and regions;
- Minimization of social and economic differences between regions and within regions by preserving their identity;
- Minimization of the impact from the main sectors (transport, industry, energy, agriculture, housing, tourism) on the environment;
- More efficient use of natural resources and waste management;
- Minimization of impact on human health;
- Mitigation of global climate change and its consequences;
- More effective protection of biodiversity;
- More effective protection of the landscape and rational landscape management;
- Decrease of unemployment, poverty and social exclusion;
- Enhancement of education and science roles; and
- Preservation of Lithuanian cultural identity.

The sustainable development strategy is realised with help of legislation system and institutional framework and balanced environmental, economic and social development.

During Lithuania's EU accession process the national legislation has been harmonised with environmental legislation of European Union, and specific tasks in environmental protection have been defined. Lithuania essentially had implemented the *acquis* in all areas of environment policy by its accession in May 2004. Certain transitional arrangements have been agreed in Lithuania's EU Accession Treaty regarding implementation of EU environmental legislation and standards up to 2015.

Ensuring compliance with the *acquis* requires significant investments, but also brings significant benefits in all priority areas of Lithuania's National Sustainable Development Strategy.

Conclusion

Environmental legislation has been harmonised with that of European Union. The sustainable development (environmental, social and economic) objectives have been established and these are being integrated into national and regional development plans. Achievement of the sustainable development goals require for significant additional investment from public and private sector.

ANNEX 8: BILATERAL ASSISTANCE

Commitment Number	TC OPID	Commitment Name	Fund Short Code	Euro Committed	Euro Disbursed	Fund Approved Date	Commit. Stage Name	Operation Leader	Sector	Team Name	Business Group	Linked to Inv.
LITHUANIA												
ATR-93-10-01PS	1421	Drobe Wool Company	ATR	80,089	80,089	20/03/93	Closed	Riley-Pitt J.	Manufacturing	BG/Op. Teams/Central Europe Front Office	Central Europe	N
AUS-1996-01-01	5242	Development of small hydro power plants	AUS	56,010	56,010	29/01/96	Closed	Chabrier L.	Energy	BG/Op. Teams/Power and Energy	Energy	N
BTAF-1994-02-05	5319	Post-privatisation Fund - project screening	BTAF	99,924	99,924	01/02/94	Closed	Tangen H.	Finance, Business	BG/Op. Teams/Natural Resources	Energy	N
BTAF-1994-04-08	1345	Financial Institution initiatives - due diligence	BTAF	79,010	79,010	15/04/94	Closed	Marzanati R.	Finance, Business	BG/Op. Teams/Financial InstitutionsA	Financial Institutions	N
BTAF-1994-06-16	1628	Lithuanian Development Bank - board representation	BTAF	246,798	246,798	15/06/94	Closed	Cicognani M.	Finance, Business	BG/Op. Teams/Financial InstitutionsA	Financial Institutions	N
BTAF-1994-08-21	1680	TurnAround Management Programme - MEDIENOS PLAUSAS	BTAF	43,141	43,141	20/08/94	Closed	McAlister M.	Community/Social Services	PE/ESE/TurnAround Management Group	SEEC	N
BTAF-1994-08-22	1680	TurnAround Management Programme - ASTRA	BTAF	44,516	44,516	20/08/94	Closed	McAlister M.	Community/Social Services	PE/ESE/TurnAround Management Group	SEEC	N
BTAF-1994-08-23	1680	TurnAround Management Programme - Jonavas Baldai	BTAF	23,894	23,894	20/08/94	Closed	McAlister M.	Manufacturing	PE/ESE/TurnAround Management Group	SEEC	N
BTAF-1995-04-11	1381	Business Advisory Services - regional project manager	BTAF	193,654	193,654	02/04/95	Closed	McPhee J.	Manufacturing	PE/ESE/TurnAround Management Group	SEEC	N
BTAF-1995-04-12	1680	TurnAround Management Programme - Taurages Maistras	BTAF	39,256	39,256	02/04/95	Closed	McPhee J.	Manufacturing	PE/ESE/TurnAround Management Group	SEEC	N
BTAF-1995-04-14	1381	Business Advisory Services - operating expenses for Vilnius	BTAF	75,904	75,904	02/04/95	Closed	McPhee J.	Manufacturing	PE/ESE/TurnAround Management Group	SEEC	N
BTAF-1995-04-16	1680	TurnAround Management Programme - Laima	BTAF	46,760	46,760	02/04/95	Closed	McPhee J.	Manufacturing	PE/ESE/TurnAround Management Group	SEEC	N
BTAF-1995-04-17	1381	Business Advisory Services - local fund director	BTAF	37,358	37,358	02/04/95	Closed	McPhee J.	Manufacturing	PE/ESE/TurnAround Management Group	SEEC	N
BTAF-1995-05-19	1381	Business Advisory Services - local project officer	BTAF	6,336	6,336	04/05/95	Closed	Cicognani M.	Manufacturing	BG/Op. Teams/Financial InstitutionsA	Financial Institutions	N
BTAF-1995-06-22	1381	Business Advisory Services - subsidies dusbursement	BTAF	825,323	825,323	20/06/95	Closed	McPhee J.	Manufacturing	PE/ESE/TurnAround Management Group	SEEC	N
BTAF-1995-07-24	1680	TurnAround Management Programme - Snaige	BTAF	49,300	49,300	20/07/95	Closed	White J.	Manufacturing	BG/Op. Teams/Early Stage Equity	Financial Institutions	N
BTAF-1995-08-27	1680	TurnAround Management Programme - Daugeliu	BTAF	48,650	48,650	25/08/95	Closed	McPhee J.	Manufacturing	PE/ESE/TurnAround Management Group	SEEC	N
BTAF-1995-08-29	2380	Vilniaus Bankas	BTAF	145,000	145,000	25/08/95	Closed	Marzanati R.	Finance, Business	BG/Op. Teams/Financial InstitutionsA	Financial Institutions	N

Commitment Number	TC OPID	Commitment Name	Fund Short Code	Euro Committed	Euro Disbursed	Fund Approved Date	Commit. Stage Name	Operation Leader	Sector	Team Name	Business Group	Linked to Inv.
BTAF-1998-03-09	4773	Business Advisory Services - Regional Fund Director	BTAF	16,200	16,200	10/03/98	Closed	McPhee J.	Manufacturing	PE/ESE/TurnAround Management Group	SEEC	N
BTAF-1998-03-10	4773	Business Advisory Services - National Fund Director	BTAF	6,930	6,930	10/03/98	Closed	McPhee J.	Manufacturing	PE/ESE/TurnAround Management Group	SEEC	N
BTAF-1998-03-11	4773	Business Advisory Services - project officer	BTAF	2,970	2,970	10/03/98	Closed	McPhee J.	Manufacturing	PE/ESE/TurnAround Management Group	SEEC	N
BTAF-1998-03-12	4773	Business Advisory Services - Assistant to National Fund Director	BTAF	1,180	1,180	10/03/98	Closed	McPhee J.	Manufacturing	PE/ESE/TurnAround Management Group	SEEC	N
BTAF-1998-06-19	5743	Baltic Micro Business Advisory Services Programme project officer	BTAF	9,030	9,030	30/06/98	Closed	McPhee J.	Manufacturing	PE/ESE/TurnAround Management Group	SEEC	N
BTAF-1998-07-22	5743	Baltic Micro Business Advisory Services Programme subsidy account	BTAF	413,024	413,024	23/07/98	Closed	McPhee J.	Manufacturing	PE/ESE/TurnAround Management Group	SEEC	N
BTAF-1998-07-27	5743	Baltic Micro Business Advisory Services Programme operating expenses	BTAF	14,769	14,769	23/07/98	Closed	McPhee J.	Manufacturing	PE/ESE/TurnAround Management Group	SEEC	N
BTAF-1998-08-28	5134	TurnAround Management Programme - post-investment support - Interfarma	BTAF	55,161	55,161	03/08/98	Closed	McPhee J.	Community/Social Services	PE/ESE/TurnAround Management Group	SEEC	N
BTAF-1998-12-30	5744	TurnAround Management Programme - Drobe Worsteds II	BTAF	50,535	50,535	02/12/98	Closed	McPhee J.	Manufacturing	PE/ESE/TurnAround Management Group	SEEC	N
BTAF-1999-01-01	5744	TurnAround Management Programme - Trinyciai II	BTAF	59,143	59,143	26/01/99	Closed	McPhee J.	Manufacturing	PE/ESE/TurnAround Management Group	SEEC	N
BTAF-1999-04-08	5744	TAM Programme - Kauno Pieno Centras II	BTAF	54,186	54,186	15/04/99	Closed	McPhee J.	Manufacturing	PE/ESE/TurnAround Management Group	SEEC	N
BTAF-1999-05-09	5744	TurnAround Management Programme - Vilma II	BTAF	59,544	59,544	24/05/99	Closed	McPhee J.	Manufacturing	PE/ESE/TurnAround Management Group	SEEC	N
BTAF-1999-07-10	5133	Turnaround Management Programme - Lietuvos Draudimas II	BTAF	28,219	28,219	01/07/99	Closed	McPhee J.	Manufacturing	PE/ESE/TurnAround Management Group	SEEC	N
BTAF-1999-07-12	5744	Turnaround Management Programme - AB Kauno Audiniai	BTAF	58,953	58,953	20/07/99	Closed	McPhee J.	Manufacturing	PE/ESE/TurnAround Management Group	SEEC	N
BTAF-1999-11-20	5744	TurnAround Management Programme (TAM) - Litekas & Calw AB	BTAF	32,342	32,342	24/11/99	Closed	McPhee J.	Manufacturing	PE/ESE/TurnAround Management Group	SEEC	N
BTAF-1999-12-21	5743	Micro-BAS Programme - Project Officer	BTAF	14,119	14,119	16/12/99	Closed	McPhee J.	Manufacturing	PE/ESE/TurnAround Management Group	SEEC	N
BTAF-2000-02-01	6964	Business Advisory Services (BAS) Programme - Subsidies	BTAF	1,025,798	1,025,798	07/02/00	Closed	McPhee J.	Manufacturing	PE/ESE/TurnAround Management Group	SEEC	N
BTAF-2000-02-05	5744	TurnAround Management Programme - Senukai II	BTAF	55,038	55,038	22/02/00	Closed	McPhee J.	Manufacturing	PE/ESE/TurnAround Management Group	SEEC	N
BTAF-2000-03-07	5744	TurnAround Management Programme (TAM) - Vilniaus Prekybos	BTAF	58,423	58,423	09/03/00	Closed	McPhee J.	Manufacturing	PE/ESE/TurnAround Management Group	SEEC	N

Commitment Number	TC OPID	Commitment Name	Fund Short Code	Euro Committed	Euro Disbursed	Fund Approved Date	Commit. Stage Name	Operation Leader	Sector	Team Name	Business Group	Linked to Inv.
BTAF-2000-05-08	5744	TurnAround Management Programme (TAM) - Sparta Wool	BTAF	59,581	59,581	15/05/00	Closed	McPhee J.	Manufacturing	PE/ESE/TurnAround Management Group	SEEC	N
BTAF-2000-05-11	5744	TurnAround Management Programme (TAM) - Savy	BTAF	55,801	55,801	30/05/00	Closed	McPhee J.	Manufacturing	PE/ESE/TurnAround Management Group	SEEC	N
BTAF-2000-06-12	5744	TurnAround Management Programme (TAM) - Klaipedos Pienas	BTAF	54,691	54,691	16/06/00	Closed	McPhee J.	Manufacturing	PE/ESE/TurnAround Management Group	SEEC	N
BTAF-2000-06-13	5744	TurnAround Management Programme (TAM) - Kauno Platanas	BTAF	55,871	55,871	16/06/00	Closed	McPhee J.	Manufacturing	PE/ESE/TurnAround Management Group	SEEC	N
BTAF-2000-07-16	5744	TurnAround Management Programme (TAM) - Kanta	BTAF	60,000	60,000	11/07/00	Closed	McPhee J.	Manufacturing	PE/ESE/TurnAround Management Group	SEEC	N
BTAF-2000-07-18	5744	TurnAround Management Programme (TAM) - Kauno Audiniai II	BTAF	53,307	53,307	27/07/00	Closed	McPhee J.	Manufacturing	PE/ESE/TurnAround Management Group	SEEC	N
BTAF-2000-10-25	5744	TurnAround Management Programme (TAM) - Vilsota AB	BTAF	51,293	51,293	18/10/00	Closed	McPhee J.	Manufacturing	PE/ESE/TurnAround Management Group	SEEC	N
BTAF-2000-10-27	5744	TurnAround Management Programme (TAM) - Aukmerges Baldai	BTAF	58,605	58,605	31/10/00	Closed	McPhee J.	Manufacturing	PE/ESE/TurnAround Management Group	SEEC	N
BTAF-2000-12-29	5743	Business Advisory Services Programme - Robertas Ivanauskas, Project Officer	BTAF	16,055	16,055	07/12/00	Closed	McPhee J.	Manufacturing	PE/ESE/TurnAround Management Group	SEEC	N
BTAF-2001-02-03	5744	TurnAround Management Programme (TAM) - Lithuanian Airline	BTAF	56,667	56,667	13/02/01	Closed	Walker C.	Manufacturing	PE/ESE/TurnAround Management Group	SEEC	N
BTAF-2001-04-08	5744	TurnAround Management Programme (TAM) - AB Vilniaus Mesos Kombinatas	BTAF	58,548	58,548	19/04/01	Closed	McPhee J.	Manufacturing	PE/ESE/TurnAround Management Group	SEEC	N
BTAF-2001-08-10	5744	TurnAround Management Programme (TAM) - Baldai Jums	BTAF	50,705	50,705	21/08/01	Closed	McPhee J.	Manufacturing	PE/ESE/TurnAround Management Group	SEEC	N
CA3F-2002-11-09	26593	City of Vilnius - Municipal Capital Development Programme	CA3F	275,000	235,041	13/11/02	Disbursing	Covenden P.	Community/Social Services	BG/Op. Teams/Municipal & Environmental Infrastructure	Infrastructure	N
CAN-1995-01-01	1667	Klaipeda Port rail interface study	CAN2	66,663	66,663	31/01/95	Closed	Smith I.	Transport, Storage	BG/Op. Teams/Transport	Infrastructure	N
DEN-1992-09-05	627	Telecommunications programme - strategy study	DEN	294,600	294,600	14/09/92	Closed	Haugan O.	Telecommunications	BG/Op. Teams/Telecommunications, Informatics and Media	Specialised Industries	N
DEN-1992-11-08	621	Telecommunications programme - regulatory study	DEN	157,624	157,624	19/11/92	Closed	Haugan O.	Telecommunications	BG/Op. Teams/Telecommunications, Informatics and Media	Specialised Industries	N
DEN-1998-10-07	6006	Drobe Wool Energy Audit	DEN	22,458	22,458	05/10/98	Closed	Herman E.	Manufacturing	BG/Op. Teams/Energy Efficiency	Energy	N
EC-1992-12-69	954	Energy sector emergency investment programme - project management unit	ECP	362,766	362,766	20/12/92	Closed	Dyvik E.	Energy	BG/Op. Teams/Central Europe Front Office	Central Europe	N
EC-1992-12-70	943	Energy sector emergency investment programme - energy emergency planning group	ECP	178,354	178,354	20/12/92	Closed	Dyvik E.	Energy	BG/Op. Teams/Central Europe Front Office	Central Europe	N

Commitment Number	TC OPID	Commitment Name	Fund Short Code	Euro Committed	Euro Disbursed	Fund Approved Date	Commit. Stage Name	Operation Leader	Sector	Team Name	Business Group	Linked to Inv.
EC-1992-12-71	992	Energy sector emergency investment programme - commercial accounting systems for main energy utilities	ECP	475,627	475,627	20/12/92	Closed	Dyvik E.	Energy	BG/Op. Teams/Central Europe Front Office	Central Europe	N
EC-1992-12-72	968	Energy sector emergency investment programme - energy conservation awareness campaign	ECP	189,000	189,000	20/12/92	Closed	Dyvik E.	Energy	BG/Op. Teams/Central Europe Front Office	Central Europe	N
EC-1992-12-73	978	Energy sector emergency investment programme - wood harvest, distribution and conversion study	ECP	188,926	188,926	20/12/92	Closed	Noro H.	Energy	BG/Op. Teams/Russia HQ	Russia & Central Asia	N
EC-1992-12-74	972	Energy sector emergency investment programme - crude supply study and training	ECP	182,876	182,876	20/12/92	Closed	Dyvik E.	Energy	BG/Op. Teams/Central Europe Front Office	Central Europe	N
EC-1994-11-51	1820	Post-privatisation assistance - financial advice	ECP	367,888	367,888	04/11/94	Closed	Krivicky G.	Finance, Business	BG/Op. Teams/Central Europe Front Office	Central Europe	N
ECP-1995-12-42F	2150	Post-privatisation Fund (Latvia / Lithuania) - pre-investment support, accounting and technical advice	ECP	705,778	705,778	02/01/96	Closed	Moore T.	Finance, Business	BG/Op. Teams/Financial InstitutionsA	Financial Institutions	N
ECP-1995-12-43F	2154	Post-privatisation Fund (Latvia / Lithuania) - investment, legal and environmental support to enterprises	ECP	258,821	258,821	02/01/96	Closed	Moore T.	Finance, Business	BG/Op. Teams/Financial InstitutionsA	Financial Institutions	N
ECP98-2000-12-76	16241	Business Advisory Programme	ECP	248,818	248,818	08/12/00	Closed	McPhee J.	Manufacturing	PE/ESE/TurnAround Management Group	SEEC	N
FIN-1998-12-04	6109	Rokiskio Suris	FIN	77,055	77,055	21/12/98	Closed	Campbell D.	Manufacturing	BG/Op. Teams/Agribusiness	Specialised Industries	N
FIN-2000-10-05	12350	Development of Alternative Energy for Ignalina NPP Closure	FIN	199,215	199,215	09/10/00	Closed	Stanaro R.	Energy	BG/Op. Teams/Power and Energy	Energy	N
FRA-1997-11-05	3985	Kaunas energy sector and modernisation project	FRA	106,646	106,646	17/11/97	Closed	Chabrier L.	Energy	BG/Op. Teams/Power and Energy	Energy	N
GER-1993-01-01	614	Telecommunications programme - Master Plan	GER	292,970	292,970	15/01/93	Closed	Haugan O.	Telecommunications	BG/Op. Teams/Telecommunications, Informatics and Media	Specialised Industries	N
GER-1994-12-14	1820	Post-privatisation Fund - legal advice	GER	77,826	77,826	02/12/94	Closed	Krivicky G.	Finance, Business	BG/Op. Teams/Central Europe Front Office	Central Europe	N
GERK-1997-10-04	3985	Kaunas energy sector and modernisation project	GERK	24,368	24,368	17/10/97	Closed	Chabrier L.	Energy	BG/Op. Teams/Power and Energy	Energy	N
GERK-1997-10-05	3985	Kaunas energy sector reorganisation study	GERK	69,024	69,024	17/10/97	Closed	Chabrier L.	Energy	BG/Op. Teams/Power and Energy	Energy	N
HOL-1997-03-01	3985	Kaunas energy sector reorganisation study	HOL	192,527	192,527	06/03/97	Closed	Chabrier L.	Energy	BG/Op. Teams/Power and Energy	Energy	N
IRL-1994-10-04	1821	Follow-up of corporate strategy	IRL	38,341	38,341	11/11/94	Closed	Cooper D.	Telecommunications	BG/Op. Teams/Telecommunications, Informatics and Media	Specialised Industries	N
ITA-1999-03-01	6290	Drobe Wool Project Preparation	ITA	9,260	9,260	15/03/99	Closed	Gutnik S.	Manufacturing	BG/Op. Teams/Central Europe Front Office	Central Europe	N
JAP-1993-08-34	1030	Energy emergency investment programme - procurement adviser	JAP	140,260	140,260	01/08/93	Closed	Dyvik E.	Energy	BG/Op. Teams/Central Europe Front Office	Central Europe	N

Commitment Number	TC OPID	Commitment Name	Fund Short Code	Euro Committed	Euro Disbursed	Fund Approved Date	Commit. Stage Name	Operation Leader	Sector	Team Name	Business Group	Linked to Inv.
JAP-1994-02-06	761	Telecommunications projects - tender documentation preparation	JAP	144,987	144,987	08/02/94	Closed	Haugan O.	Telecommunications	BG/Op. Teams/Telecommunications, Informatics and Media	Specialised Industries	N
JAP-1994-03-08	761	Telecommunications project - corporate strategy	JAP	114,522	114,522	01/03/94	Closed	Haugan O.	Telecommunications	BG/Op. Teams/Telecommunications, Informatics and Media	Specialised Industries	N
JAP-1994-03-09	761	Telecommunications project - accounting and billing systems	JAP	120,000	120,000	08/02/94	Closed	Cooper D.	Telecommunications	BG/Op. Teams/Telecommunications, Informatics and Media	Specialised Industries	N
JAP-1996-11-29	3214	Telecommunications regulatory development licensing for privatisation and liberalisation	JAP	289,113	289,113	25/11/96	Closed	Styliadou M.	Telecommunications	GC/General Counsel/Legal Transition	Non-Banking	N
LUX-2001-09-01	21702	Lithuania: Public Sector Energy Management Programme, Technical Preparation	LUX	26,996	26,996	17/09/01	Closed	McCallion T.	Energy	BG/Op. Teams/Energy Efficiency	Energy	N
NOR-1993-10-06	1002	Hydrocarbons sector advice - environmental specialist	NOR	99,847	99,847	01/10/93	Closed	Sholem W.	Manufacturing	BG/Op. Teams/Central Europe Front Office	Central Europe	N
NOR-1994-07-01	1629	Oil port pipeline - environmental consultant	NOR	123,017	123,017	01/07/94	Closed	Sholem W.	Transport, Storage	BG/Op. Teams/Central Europe Front Office	Central Europe	N
NORG-1995-03-01	2371	Bankas Hermis - institutional strengthening	NORG	239,286	239,286	01/03/95	Closed	Marzanati R.	Finance, Business	BG/Op. Teams/Financial InstitutionsA	Financial Institutions	N
SWE-1993-05-07	584	Baltic sea environmental programme - wastewater treatment plant, Kaunas - feasibility study	SWE	156,400	156,400	21/05/93	Closed	Holm N.	Local Authority Services	BG/Op. Teams/Municipal & Environmental Infrastructure	Infrastructure	N
SWE2-2005-05-03	35051	Kaunas Public Transport Project Transport Restructuring	SWE2	168,280	0	12/05/05	Committed	Bruggeman G.	CEALs,CoFinancing Lines & RVF's	BG/Op. Teams/Municipal & Environmental Infrastructure	Infrastructure	N
SWE2-2005-12-08	36685	Kaunas Consultancy Services for Procurement of Trolleybuses	SWE2	40,000	0	05/12/05	Committed	Forsberg J.	CEALs,CoFinancing Lines & RVF's	BG/Op. Teams/Municipal & Environmental Infrastructure	Infrastructure	N
SWEF-2003-11-01	34745	Kaunas Public Transport - Project Preparation	SWE2	49,438	49,438	06/11/03	Closed	Bruggeman G.	CEALs,CoFinancing Lines & RVF's	BG/Op. Teams/Municipal & Environmental Infrastructure	Infrastructure	N
SWEF-2003-12-02	34748	Kaunas Public Transport Project - Consultancy Services for the Procurement of Buses	SWE2	26,879	26,879	08/12/03	Closed	Bruggeman G.	Transport, Storage	BG/Op. Teams/Municipal & Environmental Infrastructure	Infrastructure	N
TAI-1992-01-11	5343	Banking training	TAI	4,498	4,498	01/01/92	Closed	Pilipovic-Chaffey D.	Local Authority Services	BG/Op. Teams/Financial InstitutionsA	Financial Institutions	N
TAI-2002-03-07	4526	Regional Warehouse Receipts Programme	TAI	24,822	21,487	06/03/02	Disbursing	Bryde P.	Manufacturing	BG/Op. Teams/Agribusiness	Specialised Industries	N
TAMEC-95-10-10	5144	TurnAround Management Programme - Drobe Wool	TAMEC	49,693	49,693	01/10/95	Closed	McAlister M.	Manufacturing	PE/ESE/TurnAround Management Group	SEEC	N
TAMEC-95-10-15	5144	TurnAround Management Programme - advisory services contract - Nemunas	TAMEC	49,229	49,229	01/10/95	Closed	McPhee J.	Manufacturing	PE/ESE/TurnAround Management Group	SEEC	N
TAMEC-95-11-17	5144	TurnAround Management Programme - advisory services contract - Vilniaus Vingis	TAMEC	49,711	49,711	01/11/95	Closed	McPhee J.	Community/Social Services	PE/ESE/TurnAround Management Group	SEEC	N
TAMEC-95-11-18	5144	TurnAround Management Programme - advisory services contract - Ekranas	TAMEC	49,458	49,458	01/11/95	Closed	McPhee J.	Manufacturing	PE/ESE/TurnAround Management Group	SEEC	N

Commitment Number	TC OPID	Commitment Name	Fund Short Code	Euro Committed	Euro Disbursed	Fund Approved Date	Commit. Stage Name	Operation Leader	Sector	Team Name	Business Group	Linked to Inv.
TAMEC-95-11-21	5144	TurnAround Management Programme - advisory services contract - Astra	TAMEC	49,497	49,497	01/11/95	Closed	McPhee J.	Manufacturing	PE/ESE/TurnAround Management Group	SEEC	N
TAMEC-95-11-22	5144	TurnAround Management Programme - advisory services contract - Kauno Flektra	TAMEC	49,370	49,370	01/11/95	Closed	McPhee J.	Manufacturing	PE/ESE/TurnAround Management Group	SEEC	N
TAMEC-95-11-23	5144	TurnAround Management Programme - Linas	TAMEC	49,625	49,625	01/11/95	Closed	McPhee J.	Manufacturing	PE/ESE/TurnAround Management Group	SEEC	N
TAMEC-95-12-29	5144	TurnAround Management Programme - advisory services contract - Snaige	TAMEC	49,757	49,757	01/11/95	Closed	McPhee J.	Manufacturing	PE/ESE/TurnAround Management Group	SEEC	N
TAMEC-96-01-01	5144	TurnAround Management Programme - advisory services contract - Endokrininiai Preparati	TAMEC	42,792	42,792	01/01/96	Closed	McPhee J.	Manufacturing	PE/ESE/TurnAround Management Group	SEEC	N
TAMEC-96-01-02	5144	TurnAround Management Programme - advisory services contract - Klaipeda Svyturys	TAMEC	48,253	48,253	01/01/96	Closed	McPhee J.	Manufacturing	PE/ESE/TurnAround Management Group	SEEC	N
TAMEC-96-01-03	5144	TurnAround Management Programme - advisory services contract - Klaipedos Baldai	TAMEC	45,829	45,829	01/01/96	Closed	McPhee J.	Manufacturing	PE/ESE/TurnAround Management Group	SEEC	N
TAMEC-96-01-06	5144	TurnAround Management Programme - advisory services contract - Vilkma	TAMEC	42,000	42,000	01/01/96	Closed	McPhee J.	Manufacturing	PE/ESE/TurnAround Management Group	SEEC	N
TAMEC-96-03-13	5144	TurnAround Management Programme - advisory services contract - Vilkas	TAMEC	38,968	38,968	01/03/96	Closed	McPhee J.	Community/Social Services	PE/ESE/TurnAround Management Group	SEEC	N
TAMEC-96-03-14	5144	TurnAround Management Programme - advisory services contract - Audimas JSC	TAMEC	33,037	33,037	01/03/96	Closed	McPhee J.	Community/Social Services	PE/ESE/TurnAround Management Group	SEEC	N
TAMEC-96-03-15	5144	TurnAround Management Programme - advisory services contract - Neris	TAMEC	26,412	26,412	01/03/96	Closed	McPhee J.	Community/Social Services	PE/ESE/TurnAround Management Group	SEEC	N
TAMEC-96-03-16	5144	TurnAround Management Programme - advisory services contract - Poslovni Sistem Mercator	TAMEC	46,888	46,888	01/03/96	Closed	McPhee J.	Community/Social Services	PE/ESE/TurnAround Management Group	SEEC	N
TAMEC-96-04-20	5144	TurnAround Management Programme - advisory services contract - Panevezys Glass Works	TAMEC	49,567	49,567	01/04/96	Closed	McPhee J.	Manufacturing	PE/ESE/TurnAround Management Group	SEEC	N
TAMEC-96-04-24	5144	TurnAround Management Programme - advisory services contract - Alpina	TAMEC	48,237	48,237	01/04/96	Closed	McPhee J.	Community/Social Services	PE/ESE/TurnAround Management Group	SEEC	N
TAMEC-96-06-28	5144	TurnAround Management Programme - advisory services contract - Medienos Plausas training	TAMEC	40,449	40,449	01/06/96	Closed	McPhee J.	Manufacturing	PE/ESE/TurnAround Management Group	SEEC	N
TAMEC-96-10-45	5144	TurnAround Management Programme - advisory services contract - Vilnius Venta	TAMEC	28,193	28,193	01/10/96	Closed	McPhee J.	Manufacturing	PE/ESE/TurnAround Management Group	SEEC	N
TAMEC-97-01-07	5144	TurnAround Management Programme - Klaipeda Svyturys	TAMEC	41,987	41,987	01/01/97	Closed	McPhee J.	Community/Social Services	PE/ESE/TurnAround Management Group	SEEC	N
TAMEC-97-01-08	5144	TurnAround Management Programme - advisory services contract - Nemunas training	TAMEC	49,963	49,963	01/01/97	Closed	McPhee J.	Community/Social Services	PE/ESE/TurnAround Management Group	SEEC	N
TAMEC-97-01-09	5144	TurnAround Management Programme - Siauliu Vairas	TAMEC	42,044	42,044	01/01/97	Closed	McPhee J.	Community/Social Services	PE/ESE/TurnAround Management Group	SEEC	N

Commitment Number	TC OPID	Commitment Name	Fund Short Code	Euro Committed	Euro Disbursed	Fund Approved Date	Commit. Stage Name	Operation Leader	Sector	Team Name	Business Group	Linked to Inv.
TAMEC-97-01-10	5144	TurnAround Management Programme - advisory services contract - Vilniaus Vingis	TAMEC	49,695	49,695	01/01/97	Closed	McPhee J.	Community/Social Services	PE/ESE/TurnAround Management Group	SEEC	N
TAMEC-97-04-24	5144	TurnAround Management Programme - advisory services contract - AB Audejas	TAMEC	49,941	49,941	01/04/97	Closed	McPhee J.	Community/Social Services	PE/ESE/TurnAround Management Group	SEEC	N
TAMEC-97-04-26	5144	TurnAround Management Programme - advisory services contract - Ekranas II	TAMEC	20,000	20,000	01/04/97	Closed	McPhee J.	Community/Social Services	PE/ESE/TurnAround Management Group	SEEC	N
TAMEC-97-05-29	5144	TurnAround Management Programme - advisory services contract - Linas (Phase III) training	TAMEC	21,312	21,312	01/05/97	Closed	McPhee J.	Community/Social Services	PE/ESE/TurnAround Management Group	SEEC	N
TAMEC-97-06-32	5144	TurnAround Management Programme - AB Sparta	TAMEC	57,575	57,575	20/06/97	Closed	McPhee J.	Community/Social Services	PE/ESE/TurnAround Management Group	SEEC	N
TAMEC-97-06-37	5144	TurnAround Management Programme - Rokiskio Suris	TAMEC	43,531	43,531	24/06/97	Closed	McPhee J.	Community/Social Services	PE/ESE/TurnAround Management Group	SEEC	N
TAMEC-97-07-39	5144	TurnAround Management Programme - advisory services contract - Snaige II training	TAMEC	19,701	19,701	03/07/97	Closed	McPhee J.	Community/Social Services	PE/ESE/TurnAround Management Group	SEEC	N
TAMEC-97-07-41	5144	TurnAround Management Programme - Achema	TAMEC	49,857	49,857	18/07/97	Closed	McPhee J.	Community/Social Services	PE/ESE/TurnAround Management Group	SEEC	N
UK-93-08-12PS	1002	Hydrocarbons sector advice - financial advice / petroleum industry economic advice	UK9312	581,660	581,660	04/08/93	Closed	Sholem W.	Manufacturing	BG/Op. Teams/Central Europe Front Office	Central Europe	N
UKB-1994-05-03	1421	Drobe Wool Company - financial and legal advice	UKB	20,027	20,027	13/05/94	Closed	Riley-Pitt J.	Manufacturing	BG/Op. Teams/Central Europe Front Office	Central Europe	N
UKB-1999-03-01	6290	Drobe Wool project preparation	UKB	5,071	5,071	11/03/99	Closed	Gutnik S.	Manufacturing	BG/Op. Teams/Central Europe Front Office	Central Europe	N
UKB-1999-07-02	6290	Drobe Wool Project Preparation	UKB	11,859	11,859	07/07/99	Closed	Gutnik S.	Manufacturing	BG/Op. Teams/Central Europe Front Office	Central Europe	N
UKC-1997-04-05	4267	Power sector least cost plan follow on study	UKC	25,164	25,164	01/04/97	Closed	Chabrier L.	Energy	BG/Op. Teams/Power and Energy	Energy	N
UKE-2000-06-08	4526	FAO Framework Agreement - Dairy Sector Analysis in Lithuania	UKE	34,564	34,564	14/06/00	Closed	Campbell D.	Manufacturing	BG/Op. Teams/Agribusiness	Specialised Industries	N
UKE-2001-07-24	18469	Lithuania Concessions Law Development	UKE	184,506	184,506	24/07/01	Closed	Zverev A.	Community/Social Services	GC/General Counsel/Legal Transition	Non-Banking	N
		Country Total Euro Amount:		**14,438,415**	**14,186,841**							
		Report Total Euro Amount:		**14,438,415**	**14,186,841**							
		No of Commitments:		**147**								

ANNEX 9: ASSESSMENT OF LITHUANIA'S COMMERCIAL LAWS

The EBRD has developed and regularly updates a series of assessments of legal transition in its countries of operations, with a focus on selected areas relevant to investment activities: capital markets, company law and corporate governance, concessions, insolvency, secured transactions and telecommunications. The existing tools assess both the quality of the laws "on the books" (also referred to as "extensiveness") and the actual implementation of laws (also referred to as "effectiveness"). All available results of these assessments can be found at www.ebrd.com/law. This annex presents a summary of the results for Lithuania, accompanied by critical comments of the Bank's legal experts who have conducted the assessments.

Capital markets

The primary legislation governing the securities market in Lithuania includes the Law on Securities Market, the Law on Collective Investment Undertakings and the Law on Companies.

The Law on Securities Market was originally enacted in 1996 and then amended several times, most recently in June 2005 in order to bring it in line with the EU Directive 2003/71 on the prospectus to be published when securities are offered to public or admitted to trading. The Law on Collective Investment Undertakings was adopted in July 2003 and aims at harmonising the regulation of collective investment undertakings with EU legislation. The Law on Companies entered into force on 1 January 2001, with the most recent amendments made in June 2005, in order to harmonise its wording with the new regulations regarding the securities market.

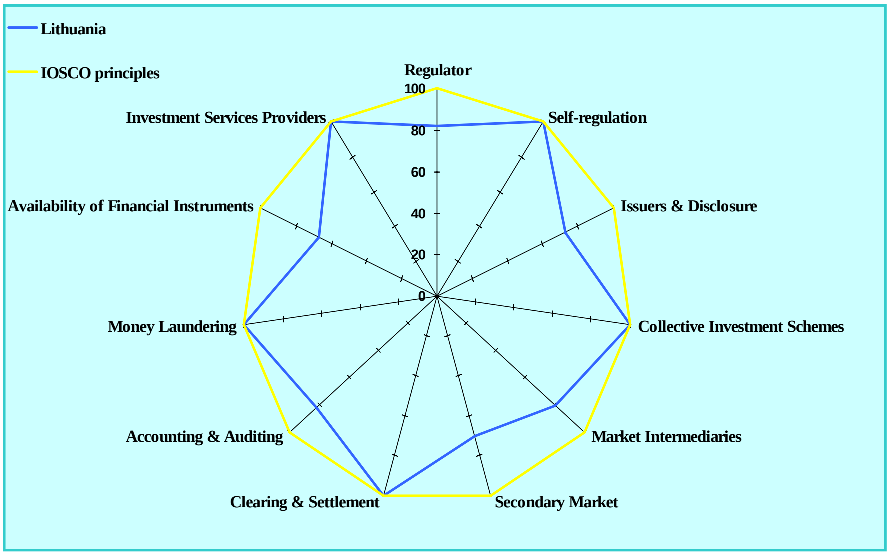
The Securities Commission of the Republic of Lithuania (the "LSC") is the supervisory authority of the securities market. The LSC was established in September 1992 and is funded by the state budget. In September 1996 the LSC joined the International Organisation of Securities Commissions (IOSCO) and in 2004 became a full member of the Committee of European Securities Regulators (CESR), enjoying wider possibilities for the exchange of information with its counterparts on issues related to securities market surveillance.

Following its accession to the EU, in June 2004 Lithuania joined the Exchange Rate Mechanism 2 (ERM II), the obligatory waiting room for the eurozone, while its scheduled date for joining the European currency is January 2007. In 2004, the Vilnius Stock Exchange was privatised and integrated into the OMX group, a common Nordic and Baltic trading system with harmonised trading rules, securities listing and stock exchange's membership principles, providing members of the stock exchange access to the common trading platform through a single access point.[2]

[2] The OMX group includes the Copenhagen, Stockholm, Helsinki, Riga, Tallinn and Vilnius stock exchanges

According to the EBRD Securities Markets Legislation Assessment conducted in 2004, the country was found to be in "*high compliance*" with the Objectives and Principles of Securities Regulation published by the IOSCO – see above chart - showing only minor flaws in the "issuers and disclosure", "market intermediary", "secondary market" and "availability of security instruments" sections. Among those, the lack of adequate legislation on prospectuses was evidenced as the major weakness.

Quality of securities market legislation – Lithuania (2004)



Note: The extremity of each axis represents an ideal score, i.e., corresponding to the standards set forth in IOSCO's *Objectives and Principles for Securities Regulations*. The fuller the 'web', the closer the relevant securities market legislation of the country approximates these principles.

Source: EBRD Securities Market Legislation Assessment 2004

The assessment was updated in 2005 and the results confirmed the high compliance rating. In 2005 new legislation on listing documents and prospectuses was issued. The possibility for a public offer of securities and their listing in a regulated market is now associated with the publication of a prospectus rather than with registration of the securities with the Securities Commission. Other regulations issued in 2005 set additional requirements for auditors of listed companies and improve the disclosure of the identity of major shareholders and the mandatory disclosure after certain thresholds are reached.

Company law and corporate governance

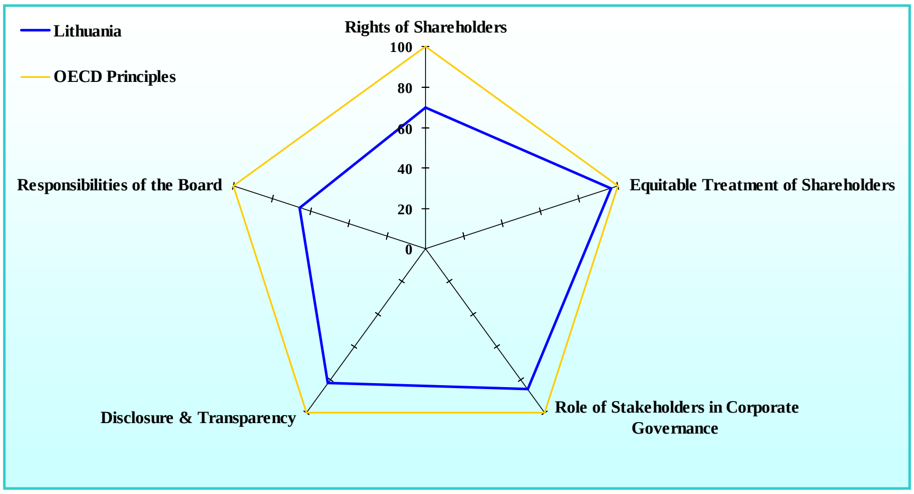
The Law on Companies is the most important legislative document dealing with corporate governance in Lithuania. In April 2004 the Vilnius Stock Exchange approved a Corporate Governance Code[3] and the LSC endorsed it. The Code includes a set of requirements that listed companies are invited to observe on a purely voluntary basis. A new version of the Code is being drafted to incorporate a new "comply or explain" approach.

Joint stock companies can be incorporated in private or public form. Private companies cannot have more than 100 shareholders and the amount of the authorised capital cannot

[3] The Code is available in English on the Vilnius Stock Exchange webpage http://www.lt.omxgroup.com

be less than LTL 10,000. The shares of a private company cannot generally be offered for sale or traded in publicly. The amount of authorised capital of a public company cannot be less than LTL 150,000 while shares can be offered for sale and traded in publicly. All companies are subject to registration in the Register of Enterprises of the Republic of Lithuania. The company is deemed incorporated and acquires the rights of a legal person as from the day of its registration.

Quality of corporate governance legislation – Lithuania (2004)



Note: The extremity of each axis represents an ideal score, i.e., corresponding to OECD Principles of Corporate Governance. The fuller the 'web', the more closely the corporate governance laws of the country approximate these principles

Source: EBRD Corporate Governance Sector Assessment, 2004 assessment

According to the results of the EBRD's 2004 Corporate Governance Sector Assessment, under which the quality of corporate governance related "laws on the books" was assessed, Lithuania was rated as having achieved "high compliance", when compared to the OECD Principles of Corporate Governance. As shown in the chart above only minor shortcomings were found in the "responsibilities of the board" and "rights of shareholders" sections. Among those, the assessment evidenced that the law is silent on board's functions as ensuring the integrity of the corporation's accounting and financial reporting systems and does not require the board to include a sufficient number of non-executive and independent directors.

In 2005, the EBRD launched a survey for testing the effectiveness of corporate governance (how the law works in practice). A case study dealing with related-party transactions was designed. The case study investigated the position of a minority shareholder seeking to access corporate information in order to understand if a related-party transaction has indeed been entered into by the company and on how it was possible to obtain compensation in case damage was suffered. The effectiveness of legislation was then measured according to four principal variables: complexity, speed, enforceability and institutional environment. The survey revealed that legislation in Lithuania is quite effective and only minor problems have been evidenced. Related-party transactions are however not well detailed in the legislation and this might render the procedures complex and the burden of proof heavy. The time needed to conclude the proceedings is usually under 6 months when seeking disclosure although in case of appeal the time needed to obtain an executable judgement can exceed two years.[4] Enforceability of judgements is not considered to be a problem. Turning to the institutional environment, the survey evidenced that company information is considered generally reliable, which enhances the possibility to obtain disclosure. When considering redress, the survey reported a lack of experience of the lower courts in corporate law cases.

Concessions

Lithuania has a modern Concessions Law (the "Concessions Law") developed with the EBRD's technical assistance and enacted in 2003. The Concessions Law is based on best international standards and practices, particularly, the UNCITRAL Legislative Guide on Privately Financed Infrastructure Projects and is in line with EU recommendations and standards. At the same time the Concessions Law is consistent with other Lithuanian laws, being based on and taking into account specificities of the local legal and judicial systems as well as the Civil Code.

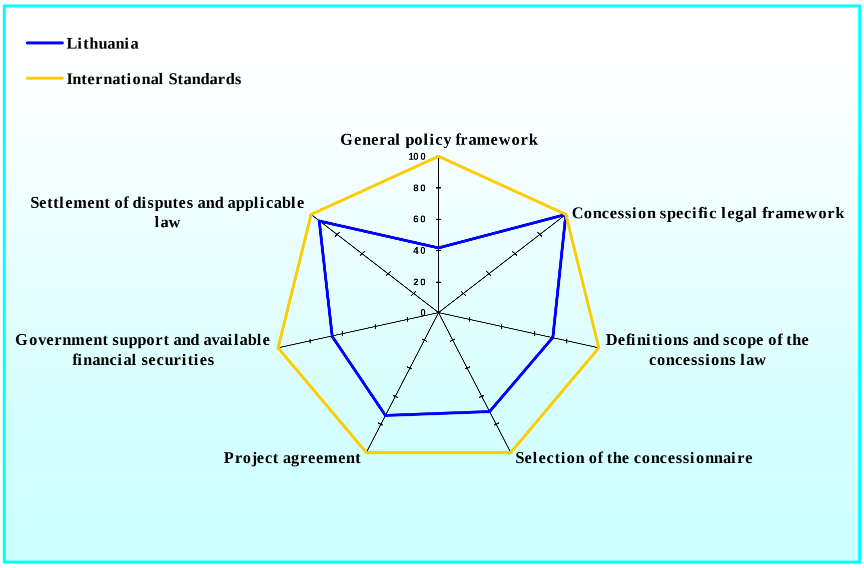
The definition of a concession under the Concessions Law covers a full range of activities, assets and services. Eligible bidders and sectors concerned are clearly identified. Under the Concessions Law, any domestic or foreign entity including consortia and joint ventures may bid for and be granted concession contracts. Remarkably, it is one of the few concession laws in the region that expressly refers to the commercial value of concessions, including risk-taking, in the definition of a concession. It is also one of the few laws in the region stating that a concessionaire has the right to create security over its property, rights and assets and that the parties are free to agree (subject to the Lithuanian Civil Code) on the governing law applicable to the project agreement. According to the Concessions Law parties have a choice of dispute resolution procedure and forum, including domestic or international arbitration.

The provisions regulating the project agreement give clear guidance on the main issues to be covered yet remain sufficiently flexible, thus allowing the parties to freely negotiate its terms and the arrangements' structure, which brings desirable flexibility to both investors and the authorities. The tendering rules are sufficiently simple and clear. The Concessions Law contains provisions assuring fair and transparent selection process (pre-selection of bidders, procedure for requesting proposals - with a distinction drawn between technical and financial proposals-, possibility of two-stage procedure, publication of concession award, limited exceptions to concession award without competitive procedure, existence of review procedures, parameters for the negotiation process, etc.).

In line with best international practices, direct selection of the concessionaire is allowed by the Concessions Law in specific cases.

[4] The new Code of Civil Procedure – in force since 2003 – has introduced certain effective measures to avoid unfair delay of the process.

Quality of concession legislation –Lithuania (2005)



Note: the extremity of each axis represents an ideal score in line with international standards such as the UNCITRAL Legislative Guide for Privately Financed Infrastructure projects. The fuller the 'web', the more closely concessions laws of the country approximate these standards.

Source: EBRD Concessions Sector Assessment 2005

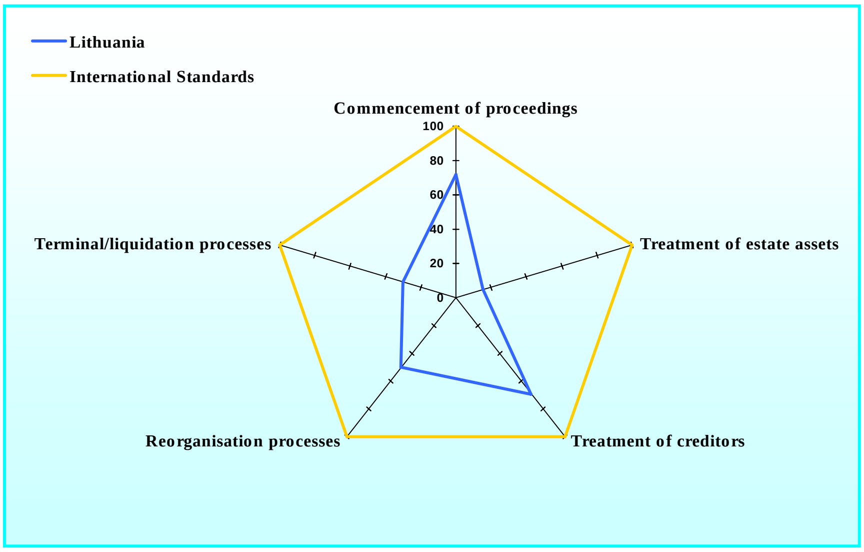
The recent EBRD Concession Laws Assessment project undertaken to evaluate applicable regime throughout the 27 countries of EBRD operations (the laws on the books only rather than how they work in practice), revealed that Lithuanian laws had "very high compliance" with internationally accepted good standards in this sector of law. In fact, Lithuania became the only country scoring that high. As can be seen from the above graph, while nearly all core dimensions of legal concession framework are regarded as regulated fairly extensively, there is still some room for improvement in terms of 'availability of financial instruments and state support' rules.

The area most in need of further improvement however is PPP policy framework. The absence of a clearly spelled out policy may become a significant factor preventing investors from being attracted to infrastructure and municipal programmes. The EBRD is developing a project to follow up with the authorities, building on the success of an earlier technical assistance, aimed at defining further needs, including policy, institutional, training, and advising on practical steps to translate the good quality comprehensive legal framework into practical implementation.

Insolvency

Bankruptcy and insolvency are governed by the Enterprise Bankruptcy Law (as amended, 2003) (the "Insolvency Law"). The Insolvency Law scored "very low compliance" when compared with international standards in the EBRD's 2003 Sector Assessment Survey and is one of the least extensive insolvency laws in the EBRD's countries of operations. The graph below displays the data collected in this project and shows levels of compliance of the Insolvency Law with international standards in five core areas, as specified in the graph:

Compliance of the Lithuania's insolvency law with international standards
Quality of insolvency legislation – Lithuania (2004)



Note: The extremity of each axis represents an ideal score, i.e., corresponding to the international standards such as the World Bank's Principles and guidelines for Effective Insolvency and Creditor Rights Systems, the UNCITRAL Working Group on "Legislative Guidelines for Insolvency Law", and others. The fuller the 'web', the more closely insolvency laws of the country approximate these standards.

Source: EBRD Insolvency Sector Assessment Project, 2003/4

As the above graph reveals, this law is deficient in many key areas of insolvency. Specifically, the Insolvency Law does not recognise debts owed to creditors (for the purposes of commencing insolvency proceedings) until those debts are three months overdue. This is a timeline that is far too long and is inconsistent with the leading international standards on the topic. In addition, the law does not contain a 'balance sheet' test for insolvency. This law also fails to provide any qualifications or requirements for insolvency administrators. Insolvency administrators are the central actors in organising insolvency proceedings and, as such, should be professionally trained in the field of law or accounting and, preferably, should be licensed by some sort of governmental or quasi-governmental authority.

As is common in insolvency legislation in EBRD countries of operations, the Insolvency Law is particularly deficient in addressing the issue of reorganisation. A meaningful reorganisation scheme should allow for the compromising of obligations, in a timely fashion, to facilitate recovery. Under the current Lithuanian scheme, virtually no ongoing financing during restructuring will be available and there are no provisions for set-off. Both of these issues must be addressed. Finally, given Lithuania's increasing business relationships with foreign countries, it would be worthwhile for the law to address the issue of cross-border insolvency proceedings (although, admittedly, this is not as pressing an issue as the other deficiencies discussed herein).

Other concerns appear when one looks at the practical implementation of Lithuania's insolvency legislation. The EBRD 2004 Legal Indicator Survey on Insolvency, which examined the 'effectiveness' (or how the law works in practice) of insolvency regimes in both creditor-initiated insolvencies and debtor-initiated insolvencies, revealed that Lithuania's insolvency system does not operate effectively in practice. In particular, access to the system for both debtors and creditors is unduly formal and difficult. Cases are not handled by specialised courts and the confidence of users of the insolvency system in the competence of judges and insolvency administrators is not high.

The poor access for debtors, in particular, suggests not only weakness in the legislation but also an unduly slow and complex legal regime that makes reorganisation (and therefore business continuity) extremely unlikely.

All of these factors, together with the law's deficiencies, militate against the insolvency regime functioning properly as a 'stick' to induce debtors to act in good faith and as a 'carrot' to induce insolvency debtors, with businesses that are fundamentally viable, to try to promote the rescue of such businesses.

Secured transactions

No significant changes have taken place since the preparation of the last EBRD strategy for Lithuania and the regime applicable to taking security over movable property has preserved its strengths and minor weaknesses.

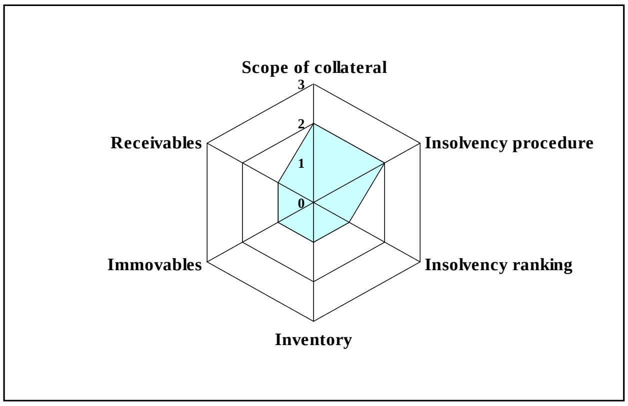
Secured transactions over movable assets are governed by Articles 4.198-4.228 of the Civil Code of the Republic of Lithuania; The Law on Establishment of the Hypothec Register adopted in June 1997; Instruction on Filling in the Mortgage, Compulsory Mortgage, Pledge and Compulsory Pledge Bonds, approved by Order no. 46 of the Minister of Justice of the Republic of Lithuania on 20 February 2002; and Regulations of the Hypothec Register of the Republic of Lithuania, adopted by Resolution no. 1246 of the Government of Lithuania on 18 October 2001.

All charges over movable property (except possessory charges) and a number of other transactions which are "quasi" security interests (sales with the right of redemption, leasing agreements, and sales with reservation of title) must be registered with the Hypothec Register. The Register also records mortgages over immovable assets. The system is centralised, fully computerised and easily accessible through the Internet. All interested persons can search the data electronically, including the particulars of a charge.

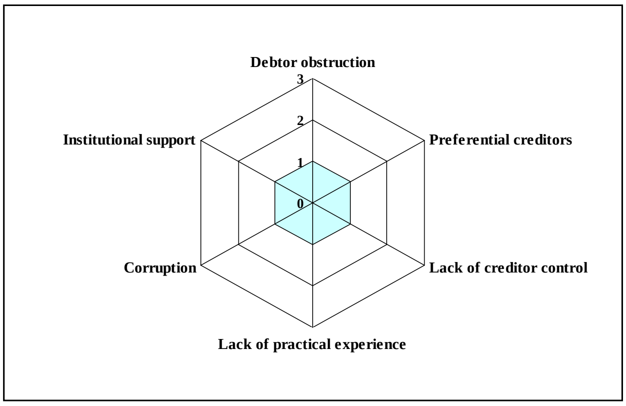
Generally, the system for taking, perfecting and enforcing security over movable and immovable property has been carefully and thoroughly implemented and is working well. This is confirmed in all EBRD surveys. In particular, enforcement of a charge seems to be very efficient (see EBRD Legal Indicator Survey, 2003).

Obstacles to charge enforcement process – Lithuania (2003)

Scope



Process



Note: The fuller the web, the more serious the problems are in each of the respective categories. "Process" factors measure the impact that specific obstacles would have on the enforcement proceedings. "Scope" factors give an indication of how effective enforcement would be when conducted on various types of collateral and in the case of debtor insolvency.

Source: EBRD Legal Indicator Survey 2003

However, further improvements could be made to the regime.

1. There is uncertainty about charging assets that would be described generally in the collateral bond. Although the Civil Code provides that the charge can cover all types of movable assets, both present and future to secure all types of debts, including future debts, so that in theory it would be perfectly possible to create a charge encompassing fluctuating pools of assets, and even the whole of the enterprise, it seems that in practice the procedure specifically requires that all assets given as collateral be described and identified. Local practitioners report that the only charge over fluctuating assets which could be taken is a charge over stock-in-trade – ambiguously, the Civil Code provides a special charge over stock in trade, encumbering only goods and raw materials owned by an enterprise.

2. The registration procedure could be streamlined and simplified. Currently, in order to register a charge with the Register, all transaction documents must be filed at the Register and reviewed, in addition to being previously certified by a public notary. In contrast, in order to register a quasi security interest, it is sufficient to give a simple notice to the Hypothec Register. A term of five working days is usually sufficient to carry out the entire process. It may be that this time could be significantly reduced. This could have an impact on the costs too: currently, fees for registering a charge can amount to LTL 700 (approximately €200, this includes stamp duty and notary fees). The filing of a quasi security interest, in contrast, is only LTL 20.

Telecommunications

The telecommunications sector in Lithuania is currently regulated by the Communications Regulatory Authority (“RRT”) and is governed by the Law on Electronic Communications 2004. This 2004 Law transposed the 2002 European Union (EU) regulatory framework on electronic communications and came into force on 1 May 2004 upon accession to the EU.

The RRT is an independent institution, formed in May 2001 in accordance with the then Law on Telecommunications, 1998, as part of Lithuania’s efforts to harmonise with European Union Telecom *Acquis*. The 1998 Act defines the responsibilities of the RRT as including supervision of licences; setting requirements for and monitoring interconnection; setting tariff limits in fixed-line telecoms and any other area where there is market dominance or cross-subsidisation; administering the national numbering plan; approving customer contracts; and, examining disputes between operators over interconnection and the joint use of conduits, cable ducts, towers and poles. The RRT’s responsibilities will have been appropriately redefined in accordance with the transposition of the EU 2002 regulatory framework.

The telecoms market was formally fully liberalised on 1 January 2003 when local, domestic and international long-distance telephony were opened up to competition. By the end of Q3 of 2005, 41 companies were reportedly active in the provision of fixed line communications services. However, meaningful competition in the fixed sector appears to be taking longer to emerge, with Lietuvos Telekomas (“LT”), the incumbent operator, still controlling about 95 per cent of the fixed telecommunications market. Fixed line penetration stood at 23.5 per cent at the end of Q3 of 2005 but has been decreasing in recent years mainly due to the entrance of various new technologies to the market place, particularly mobile.

LT was partly privatised in June 1998 with the sale of a 60 per cent controlling stake by international tender. A further 25 per cent was sold by Initial Public Offering (IPO) in June 2000 and 5 per cent sold to former and current employees. The state retains a 10 per cent share. The European Bank for Reconstruction and Development (EBRD) acquired a 7.73 per cent shareholding in LT as part of the June 2000 IPO and sold its stake in July 2005.

There are three GSM mobile network operators in Lithuania (TeliaSonera-owned Omnitel, TDC-owned Bite and Tele2), all of whom are privately owned. GSM Mobile penetration stood at an impressive 135% (118% active subscribers) at and of Q3 o f 2005, reflecting vigorous competition between mobile market players. All existing GSM operators were recently granted 3G licences by RRT following a tender process completed in February 2006, with Omnitel being first to launch an initial 3G service offering the same month. It is understood that mobile number portability went live on 1st January 2006.

There have been significant advances in the implementation of modern, EU compliant, regulatory standards for telecoms in Lithuania and the resulting development of certain sector markets has been impressive. However, there are currently a number of outstanding issues. Particularly, it is notable that meaningful competition has yet to occur in the fixed market, with LT maintaining overwhelming dominance in that market. Accordingly, RRT should prioritise intervention in this area of the market through full implementation of all relevant regulatory tools at its disposal, including swift resolution by RRT of interconnection issues between LT and alternative operators, noted by many as an issue on the Lithuanian market.

ANNEX 10: THE NUCLEAR SAFETY ACCOUNT AND THE IGNALINA INTERNATIONAL DECOMMISSIONING SUPPORT FUND

The Ignalina Nuclear Power Plant (INPP) is a legacy from the former Soviet Union. INPP's two 1500 MWe RBMK reactors are of the same basic design as those at Chernobyl Nuclear Power Plant.

In an Agreement signed in 1994 with EBRD under the EBRD-managed Nuclear Safety Account (NSA), the Government of Lithuania committed itself to (i) to submit INPP to an in-depth safety assessment for the purpose of nuclear licensing process and to implement safety improvement measures for INPP; (ii) not to extend the lifetime of either of the two nuclear reactors beyond the time at which their fuel channels should be replaced. (Lifetime extension of the reactors through re-channelling is thus excluded.); and (iii) to develop and implement a programme for rehabilitation in the power sector and for demand-side management, improvements in energy efficiency, further reform of pricing policy and the assessment of the need for additional power generating capacity. The 1994 NSA Agreement provided a grant of €34 million to INPP to support enhancement of the short-term safety of the plant. The short-term safety enhancement project was successfully completed in 1999. An in-depth safety assessment of INPP, also funded by the NSA, was completed in December 1996 and established a safety case for the remaining limited service life of the plant until permanent shutdown. A similar licensing process was implemented for Unit 2. This was supported by a number of bilateral co-operation agencies.

International experts stated that implementation of short-term safety upgrading programmes has reduced some of the serious deficiencies in design, quality and safety culture and brought the plant to a level of safety tolerable only for a limited period of operation. The Council of the European Union Report on Nuclear Safety in the Context of Enlargement of 27 May 2001 states that in spite of the short-term safety improvements achieved, there remain substantial deviations from widely applied requirements within the EU, mainly with respect to the last barrier for protection of the environment, the confinement system. It is not technically realistic to eliminate these deviations to the extent necessary to achieve the high level of nuclear safety expected within the EU.

Lithuania has closed INPP Unit 1 in December 2004 and committed to close Unit 2 by 31 December 2009 at the latest. These commitments were made with Government and Seimas approval of the National Energy Strategy in 1999 and in 2002 and reconfirmed the early closure of INPP Units 1 and 2 in accordance with the covenants of the NSA Agreement.

It is, however, essential that INPP implements additional short-term safety upgrades at the plant including an independent and diverse reactor shutdown system at Unit 2, and measures to ensure continued high motivation and safety awareness of the operating staff.

The INPP decommissioning work is a long-term process, which is divided in several phases. The initial programme focuses on preparatory activities following the closure of Unit 1. It also includes removal and intermediate storage of fuel and the processing and intermediate storage of operational radioactive wastes from Units 1 and 2. The

Lithuanian Government invited concerted and well co-ordinated national and international effort for implementation of this programme.

On the initiative of the European Commission, the EBRD established in June 2000 the new multilateral grant facility Ignalina International Decommissioning Support Fund (IIDSF). IIDSF activities are being implemented under a Framework Agreement dated 5 April 2001 between the Republic of Lithuania and the EBRD, which was ratified by the Seimas in July 2001.

To date the European Community and 15 additional countries contributed €433.325 million to the IIDSF. On 13 December 2002, at the Copenhagen European Council the EU finalised accession negotiations with ten candidate countries including Lithuania. On 16 April 2003, at the Athens EU Summit, the Accession Treaty was signed. The Treaty contains specific provisions relating to the closure and decommissioning of INPP. It also contains a financial package to address these matters. The Treaty furthermore provides for the possibility of making EU assistance or part thereof available to the IIDSF. The Lithuanian financial package includes: (i) €285 million (based on 1999 prices) additional Community financial assistance for the period 2004 - 2006; and (ii) prolonged Community assistance beyond 2006. The amount of the Community assistance for the period 2007-2013 is being finalised. The December 2005 European Council conclusions mentioned a figure of €865 million (in 2004 prices).

The purpose of the IIDSF is to finance or co-finance the provision of goods, works and services necessary:

(i) to support the decommissioning work at INPP

The overall INPP decommissioning should be done in a safe and efficient manner in order to ultimately reduce the INPP hazards and in the long term to release the site for other uses. Decommissioning is a long-term process of high technical complexity. It includes all the administrative and technical operations necessary to withdraw INPP from the list of licensed facilities. Therefore it is important to bring an integrated approach to the decommissioning process, so that design, engineering, management of investments in pre-decommissioning facilities, licensing and technical support issues are optimised. The main activities during the first phase following closure are the removal and intermediate storage of spent fuel, the processing of liquid and solid radioactive waste, and preparations for intermediate storage, as well as decontamination of systems and components, systems modifications and systems separations. Lithuania decided to apply the strategy of Immediate Dismantling for decommissioning of INPP.

The current commitments of the IIDSF relating to the INPP nuclear decommissioning support under Grant Agreements cover:

- Project management and engineering services (DPMU) phase 1 project from 2001 onwards. The onsite DPMU ensures an integrated approach to the decommissioning and waste management of INPP and is responsible for ensuring that these Lithuanian resources will be implemented to meet requirements with respect to scope and quality, time schedule and cost.
- Design and construction of a new interim storage facility for 18,000 RBMK spent nuclear fuel assemblies from Units 1 and 2.

- Design and construction of a new solid waste management and storage facility (SWMSF) for 120,000 m^3 short- and long-lived low and intermediate level radioactive waste.
- Design and construction of a reliable replacement environmentally friendly heat and steam source for INPP and Visaginas (completed in 2005).
- Modernisation of INPP technical documentation archive (completed in 2005).
- Pilot decommissioning project for engineering, planning and licensing of dismantling activities at Unit 1 building 117/1 of the high pressure emergency core cooling system.
- Free release measurement facility.
- Tools and equipment for radiological characterisation.
- Reactive power compensation at INPP power junction.

(ii) to implement measures in the energy sector of Lithuania which are consequential to the closure and decommissioning of INPP and which would assist the necessary restructuring, upgrading and modernisation of the energy production, transmission and distribution sectors as well as to improve energy efficiency

In 2003, INPP produced approx. 73 per cent of Lithuania's electricity. The closure of INPP impacts on the development of the energy sectors of the country. Therefore implementation of measures to facilitate the necessary restructuring, upgrading and modernisation of the energy production, transmission and distribution sectors, as well as to improve energy efficiency, is becoming increasingly important.

In order to support the development of relevant projects, in March 2003 the EBRD commissioned with IIDSF grant financing the following two studies:

- "Lithuania – Power Sector Least Cost Expansion Plan Update"; and
- "Updating of the Gas Sector Development Plan in Lithuania and its Interface with the Gas Sector Development in Latvia, Estonia, NW Russia, Belarus and Poland".

According to the Lithuanian power sector least-cost expansion plan update, the upgrading of the environment protection (fulfilment of EU environment regulations), reliability and energy efficiency of the existing 1800 MW_e multi-fuel Lithuanian Power Plant (LPP) is of the highest priority for expedited project development and implementation from 2005-2011. LPP will become the major Lithuanian power generator after closure of INPP. The LPP project could become the first future EBRD-loan/IIDSF-grant co-financed investment project.

The current commitments of the IIDSF relating to the development of the Lithuanian energy sector under Grant Agreements cover:

- Construction of a new 100 km gas pipeline from Pabrade to INPP and Visaginas (completed in 2005).
- Design and construction of new flue gas desulphurisation and dust collection plants and related project management consultancy services.

The EBRD and Lithuania have developed a strong relationship in the implementation of the INPP decommissioning process. Subject to additional contributions to the IIDSF and approval at the Assembly of Contributors, the EBRD intends to define with INPP and the energy sector companies for the period 2007-13 additional project proposals.

The new project INPP decommissioning support project proposals may include: (i) engineering, tools and equipment for decontamination and dismantling of remaining systems and components; (ii) a melting unit; (iii) a near surface repository for short-lived low- and intermediate level waste; and (iv) upgrading of the existing INPP training centre.