MINISTRY OF FINANCE OF THE REPUBLIC OF LITHUANIA

STATE DEBT OF THE REPUBLIC OF LITHUANIA 2002

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2003

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INTRODUCTION

This bulletin about the public debt is an annual publication of the Ministry of Finance, which gives an overview of public debt developments over 2002, outlines the economic and financial situation of the country, presents statistical and analytical data about domestic and external state debt.

Overview of the Lithuanian economy. The macroeconomic situation in Lithuania in 2002 significantly improved thus retaining the tendencies of the recent several years. Upon assessment of Lithuania's macroeconomic indicators and tendencies of the economy, the Board of Directors of the International Monetary Fund recognised that Lithuania has made impressive progress over the year and forecasts a steady growth in 2003.

The growth of GDP driven by exports and increased domestic demand has surpassed even the most optimistic expectations. In 2002, GDP comprised LTL 50,678.6 million. GDP growth over the year amounted to 6.7%. The annual GDP per capita amounted to LTL 14,609. GDP deflator was at zero meaning the real and nominal GDP growth coincided.

Economic growth was driven by growing exports, recovering domestic demand and increase in the efficiency of work (processing industry, electricity, water and gas supply, construction) and the working hours (retail and wholesale trade, transportation and storage activities).

According to the Department of Statistics of the Republic of Lithuania, in 2002, exports of goods and services at constant prices of 2000 grew by 19.4%, while imports by 16.1%. Import of investment goods and increase of construction volumes resulted in growth of the gross principal capital formation.

In 2002, the largest portion of goods was exported to the EU states, i.e. 48.4% of the total Lithuania's exports (exports to CIS accounted for 19.2%, whereas exports to the EU and CIS states increased by 12% and 7.7%, respectively). Exports results of 2002 were mainly influenced by narrowed exports of mineral products and fast-growing exports of vehicles (export of repaired ships to the EU). The largest portion of imported goods was also from the EU states, i.e. 45% of the total Lithuania's import (imports from CIS accounted for 26.2%), whereas imports from EU states increased by 13.6%, and imports from CIS decreased by 0.9%. The annual import results were predetermined by a fast growth of the import of investment goods (45.9%).

In 2002, the flow of the international official reserves was positive (LTL 1.61 billion). Lithuania's official international reserves increased by 20% over 2002 and, according to the data of the Bank of Lithuania, amounted to LTL 8,012.7 million as of December 2002.

By preliminary data, the current account deficit comprised LTL 2.4 billion in 2002. As compared to 2001, it increased by LTL 118.4 million, however, like in 2001, it stood at a fairly moderate level, i.e. 4.8% of GDP.

In 2002, the increase of the current account deficit was caused by a 21% slump of the positive current transfers balance and a 2.9% increase of the negative foreign trade balance. An increase of the positive balance of services of 8.9% and a 8.7% decrease of the negative revenue balance were among the factors pushing the current account deficit down.

In 2002, the Government of the Republic of Lithuania further pursued tight fiscal policies, continued fiscal consolidation and implemented structural reforms. In 2001, the general government budget fiscal deficit accounted for 1.6% of GDP, whereas according to the data for 2002, it fell to 1.2% of GDP.

As of 31 December 2002, the flow of foreign direct investments in Lithuania amounted to LTL 2.67 billion. As compared to 2001, the investment flow increased by LTL 882.4 million, i.e. almost 50%. It is noteworthy that attraction of direct investments is associated with greenfield investments, unlike in previous years, when foreign investors would acquire assets in Lithuania through privatisation programmes.

Strong supply of consumer goods, competition between trading networks and appreciation of the Litas against the US dollar resulted in a decrease in prices of consumer goods and services by 1%, and this was the first annual deflation recorded within 12 years of independence.

Due to a deficit budget, an increase of the total public debt was observed in 2002, although in terms of its ratio against GDP, it decreased by 1.2% and that the foreign debt decrease was even 2.7%. The Government's position to expand Lithuania's capital market and the base of investors was further implemented. Comparatively low Government's borrowing needs and considerable liquidity of banks secured favourable conditions for borrowing in Lithuania's capital market in 2002. A further decrease of interest rates on the domestic capital market, including the Government securities market, was observed. The weighted average annual interest rate of issued GS, in comparison to that in 2001, decreased from 6.46% to 4.62%. The lowest official interest rate was 2.8% (on 6-month Treasury bills), whereas the highest one was 6.494% (on 10-year bonds). In 2002, the maturity of Government securities denominated in Litas was being further increased. For the first time ever, 10-year bonds were issued and 3-year saving notes were issued.

Commercial banks set their interest rates on loans on the basis of average interest rates on GS. In the end of 2002, the average annual interest rate on loans issued in Litas was 6.08% (8.13% in 2001), and 4.71% on loans in foreign currencies (5.66% in 2001).

Lithuania's economic progress and the financial system has been assessed favourably by all the three ratings agencies.

A report of the Fitch Ratings Services emphasises that Lithuania's financial system is stable and reliable, and that the country has made considerable progress. Tight fiscal policies pursued by the Government and consistent implementation of structural reforms has contributed to Lithuania's successful progress towards integration to the EU and the fact that the country has been invited to join the NATO alliance.

In 2002, the national borrowing ratings were reviewed. For long-term commitments in the national currency, Lithuania was attributed to the group of countries with the highest ratings, 'A'. Lithuania's long-term investment ratings for borrowing in foreign currencies was upgraded to 'BBB' from 'BBB-', whereas the long-term local currency ratings were raised to 'A-' from 'BBB+'.

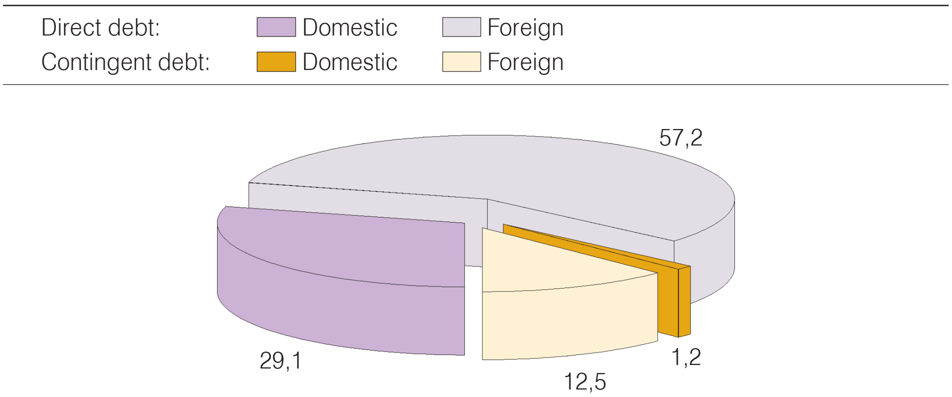
In November 2002, the international Moody's Ratings Services raised the country's foreign currency ratings by as many as three points to 'Baa1' (outlook stable) from 'Ba1' (outlook positive).

Lithuania's credit ratings received identical assessment by Standard & Poor's Ratings Services, which raised long-term ratings for borrowing in foreign currencies to 'BBB'from 'BBB-'. This was the first upgrade of the initial rating awarded to Lithuania by the aforementioned Agency in 1997.

The public debt is classified into the direct debt, i.e. liabilities taken on behalf of the government, and contingent, i.e. liabilities guaranteed by the government. The direct and contingent debt is further divided into domestic, i.e. liabilities denominated in Litas, and foreign, i.e. liabilities denominated in foreign currencies (Diagram 1).

Direct government liabilities (those taken on behalf of the government in Litas or foreign currencies) increased by LTL 642.7 million and amounted to LTL 11,366.5 million.

Structure of Public Debt as of 31.12.2002, percentage *Diagram 1*

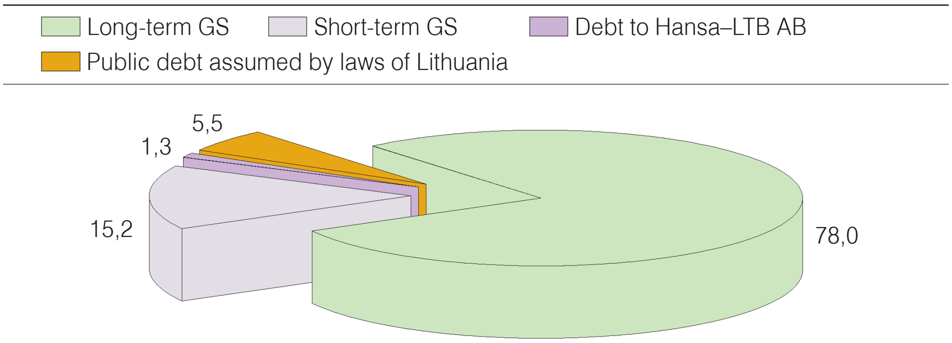


Direct domestic debt (government liabilities in Litas) as of end-2002 amounted to LTL 3,830.9 million, or 29.1% of the total public debt. The structure of the domestic debt was as follows: Government securities – LTL 3569 million, public debt assumed under laws of the Republic of Lithuania – LTL 211.3 million, and debt to the Public Limited Company Bank Hansa-LTB – LTL 50.6 million (Diagram 2).

In 2002, the government borrowed in Litas by issuing GS: T-bills in the amount of 659.6 million, saving notes in the amount of 398.5 million, bonds and special purpose GS in the amount of LTL 367.9 million.

As of end-year, the stock of short-term GS (T-bills and saving notes) was LTL 580.9 million, or 15.2% of the total direct domestic debt; long-term liabilities (saving notes, bonds, loans and other) accounted for LTL 3,250 million, or 84.8% of the total direct domestic debt.

Direct Domestic Debt by Instrument as of 31.12.2002, percentage *Diagram 2*



Direct foreign debt (government liabilities denominated in foreign currencies) decreased by LTL 260 million and as of 31 December 2002 amounted to LTL 7,535.6 million, or 57.2% of the total public debt.

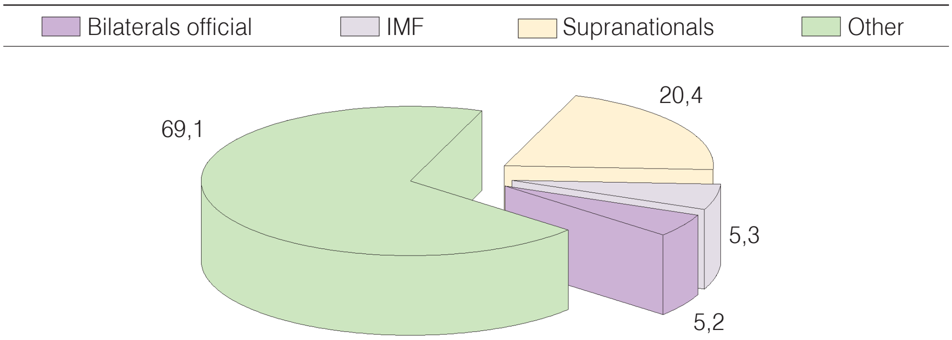
As of end-year, all direct liabilities of the government in foreign currencies were long-term.

In 2002, the government borrowing in foreign currencies amounted to almost LTL 1,645 million, and LTL 1303.5 million was repaid to foreign lenders. Bonds and long-term loans were main borrowing instruments used in 2002 to borrow in foreign markets and from foreign banks: the government borrowed LTL 1,381.1 million by issuing a eurobond issue of 400 million, and LTL 128.2 million by contracting long-term loans from international development organisations and foreign governments.

Over the year, the government redeemed short-term and long-term GS issued abroad in the amount of LTL 797.9 million, and repaid loans to the International Monetary Fund in the amount of LTL 138.9 million, to the World Bank in the amount of LTL 84.9 million, Norwegian credit organisation A/S Eksportfinans in the amount of LTL 28.3 million, and to other international organisations and commercial lenders in the amount of LTL 253.5 million.

As of end-year, the public debt in foreign currencies included: LTL 5,203.2 million to foreign commercial banks and financial institutions; LTL 1,538.4 million to the World Bank and the European Bank for Reconstruction and Development, to the European Investment Bank and the Nordic Investment Bank and other international institutions; LTL 399.5 million to the International Monetary Fund; LTL 394.5 million to foreign governments (Diagram 3).

Direct Foreign Debt by Lender as of 31.12.2002, percentage *Diagram 3*



Contingent government liabilities (loans guaranteed by the government in Litas and foreign currencies) decreased by LTL 384.8 million in 2002 and amounted to LTL 1,795 million.

Contingent domestic debt (government guarantees extended in Litas) as of end-December 2002 amounted to LTL 152.9 million, or 1.2 % of the total debt. Over the year, it increased by LTL 33.6 million due to guarantees on liabilities assumed by institutions and insurance companies.

Outstanding short-term loans amounted to LTL 77.1 million, or 50.4% of the total contingent domestic debt.

Contingent foreign debt (government guarantees extended in foreign currencies) decreased by LTL 418.4 million and as of 31 December 2002 amounted to LTL 1,642.2 million, or 12.5% of the total public debt. The short-term debt was LTL 54.5 million, i.e. 3.3% of the total liabilities in foreign currencies secured by government guarantees;

long-term debt amounted to LTL 1,587.7 million, or 96.7% of the total liabilities in foreign currencies secured by government guarantees.

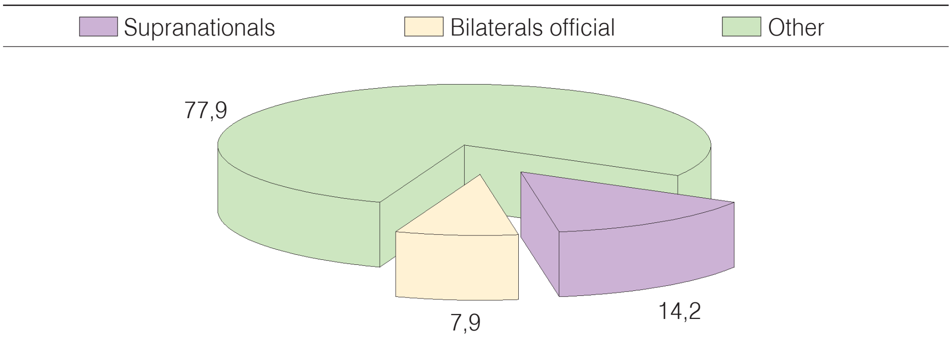
In 2002, the government extended only two new guarantees to creditors on loans in foreign currencies, namely, the Public Limited Company Yukos Oil Corporation of the Russian Federation on a loan extended to the Public Limited Company Mažeikių Nafta in the amount of USD 75 million (LTL 248.36 million), and the Nordic Investment Bank on a loan extended to the State Enterprise Klaipėda State Seaport Authority in the amount of EUR 4.34 (LTL 14.99 million).

In 2002, repayment to creditors of government guaranteed loans in foreign currencies was about LTL 406 million, of which LTL 10.3 million on short-term loans, LTL 18.1 million to international organisations, and LTL 41.3 million to foreign governments; and LTL 336.3 million to other creditors (foreign and Lithuanian commercial banks and organisations).

Enforcement of government guarantees in favour of the borrowers facing financial difficulties, namely, JSC Šiaulių Aerouostas, PLC Lietuvos Tara, PLC Oruva, resulted in the repayment of loans and payment of interest to foreign creditors in the amount of LTL 76.8 million out of LTL 98 million allocated in the national budget for defaulted loans.

As of end-year, the borrowers that had procured government guarantees on loans in foreign currencies were indebted: to foreign commercial banks, companies and financial institutions – LTL 1,309.3 million; to Lithuanian commercial banks – LTL 326.8 million; to foreign governments– LTL 196.9 million; to the European Bank for Reconstruction and Development – LTL 87.2 million, to the European Investment Bank – LTL 60.7 mill; to the World Bank – LTL 57.5 million, and to other international financial institutions – LTL 22.3 million (Diagram 4).

Contingent Foreign Debt by Lender as of 31.12.2002, percentage *Diagram 4*



GOVERNMENT BORROWING

3.1. Government Borrowing in Money and Capital Markets

Government borrowing in money and capital markets includes issuance of Government securities of the Republic of Lithuania (hereinafter referred to as GS) in domestic and foreign markets and borrowing from foreign commercial banks.

The key debt instrument used by the Government of the Republic of Lithuania is issuance of Government securities. As of 31 December 2002, debt in issued GS comprised 64.5% of the total public debt.

Securities of the Government of the Republic of Lithuania refer to the liabilities of the Government of the Republic of Lithuania issued in series on behalf of the Republic of Lithuania, confirming rights and obligations defined in the terms and conditions of the emission, and used as a means of borrowing in order to finance budget deficit of the State of the Republic of Lithuania and other needs stipulated in the laws, and able to serve as an item of secondary circulation of securities, unless it is otherwise provided for in the terms and conditions of the emission.

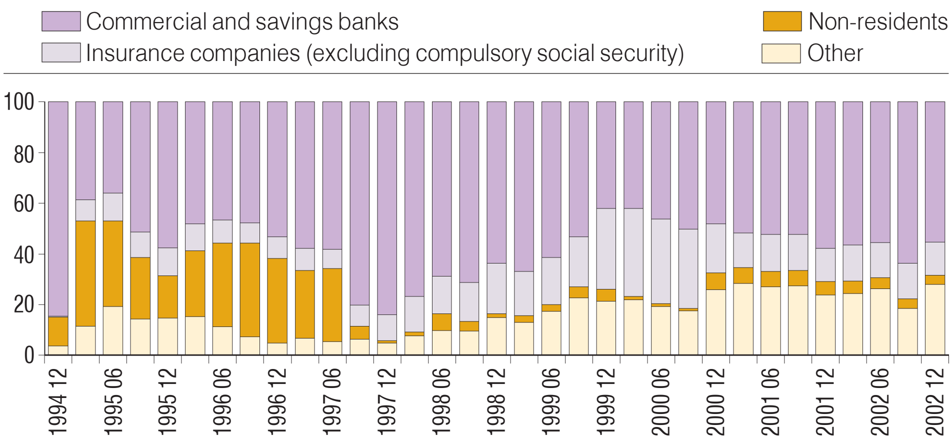
Government securities issued in Litas. **The following types of GS are issued in Lithuania:** *State Treasury bills of the Republic of Lithuania* – GS, the maturity of which at the time of issue does not exceed one year; *bonds of the Government of the Republic of Lithuania* – GS, the maturity of which at the time of issue is longer than one year; and *saving notes of the Government of the Republic of Lithuania* – GS issued through the network of commercial banks and finance brokerage companies and offered for sale in the primary market only to natural persons. In addition to the aforementioned GS, there are also *GS issued for special purposes (hereinafter referred to as special purpose GS)*, which were issued under special laws, without auctions.

As of end-2002, the stock of the public debt in GS (including special purpose GS) and saving notes issued in Litas amounted to LTL 3,569 million, of which debt in auctioned GS totalled LTL 2,467.8 million, debt in saving notes – LTL 476.7 million, debt in special purpose GS – LTL 524.5 million. LTL 100 million was the debt in Litas denominated five-year bonds issued abroad. The portion of the public debt in Litas denominated GS grew by LTL 912.5 million, or 34.35% compared to 2001.

The structure of investors in domestically issued GS has not changed significantly in 2002 in comparison with that in 2001. As of end-2002, the share in GS purchased by foreign investors has gone down from 5.2% of all circulating GS (including GS issued in Litas abroad, but excluding special purpose GS) to 3.7%. As of end-2002, the key foreign investors into Litas denominated GS were commercial banks of Estonia (LTL 10.6 million), whereas as of end-2001, the key foreign investors were commercial banks of Latvia (LTL 3.5 million). Natural persons of USA held GS worth LTL 1.2 million. Among local investors, the major part of the circulating GS, like in previous years, were owned by commercial banks and insurance companies. The share of GS owned by commercial banks went down from 57.9% in 2001 to 55.3% in 2002 and the share held by insurance companies fell from 13.1% to 13% (see Diagram 5). Natural persons' investment in GS increased from 7.8% to 14.7%.

Government Securities issued by auction. The major portion of GS issued in Litas is comprised of securities sold by auction – **State Treasury bills of the Republic of Lithuania** and **Government bonds of the Republic of Lithuania**. GS auctions are organised by the Bank of Lithuania. Auctions are open only to those Lithuanian and foreign commercial banks and brokerage companies, which have entered with the

Holders of Litas Denominated Government Securities *Diagram 5*



Bank of Lithuania into Auction Participant's Agreement and which meet the requirements applied by the Bank of Lithuania to auction participants.

In 2002, the Ministry of Finance launched 45 GS auctions, including 4 auctions for ten-year maturity bonds (including 3 due to an additional issue of GS of previous issue), 3 auctions for seven-year maturity bonds (including 2 due to an additional issue of GS of previous issue), 11 auctions for five-year maturity bonds (including 7 due to an additional issue of GS of previous issue), 12 auctions for three-year maturity bonds (including 8 due to an additional issue of GS of previous issue), 12 auctions for twelve-month maturity Treasury bills (including 6 due to an additional issue of GS of previous issue) and 3 auctions for six-month maturity Treasury bills.

In order to standardise the GS, less of seven-year bonds and no two-year bonds were issued in 2002.

In 2002, for the first time ever ten-year bonds were issued in the domestic market. The first auction for ten-year bonds in the domestic market (held on 18 March 2002) was successful, investors showed great interest in these GS. The highest average annual interest rate on ten-year bonds was recorded at the first auction and reached 6.150%; afterwards it constantly decreased and at the last auction for ten-year bonds reached the bottom, i.e. 5.871%.

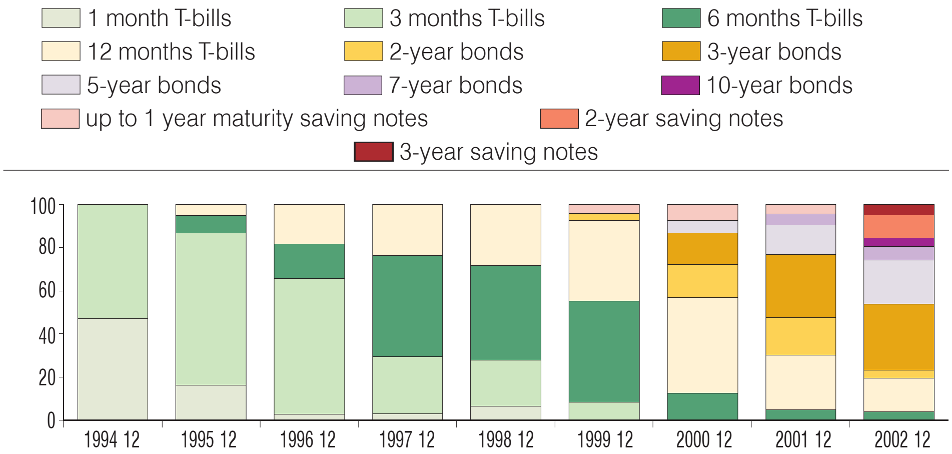
The stock of the public debt in Litas denominated GS sold by auction increased from LTL 1,719.1 million in 2001 to LTL 2,657.8 million in 2002 and accounted for 71.95% of the total issue of Litas denominated GS. As of the end of 2002, 3-year bonds accounted for the largest share of the nominal value of auctioned outstanding GS , i.e. LTL 941.0 million (or 36.65%). The share at the nominal value of outstanding Litas denominated bonds of any maturity was LTL 1,986.9 million (76.8%), 23.2% (LTL 600.3 million) being T-bills (see Diagram 6).

The weighted average annual interest rate on GS fell from 6.46% in 2001 to 4.62% in 2002. The aforementioned interest rate is 459 bps higher than the average annual inflation rate.

Chart 1 shows the dynamics of the weighted average annual interest rate on Litas denominated GS during 1998–2002.

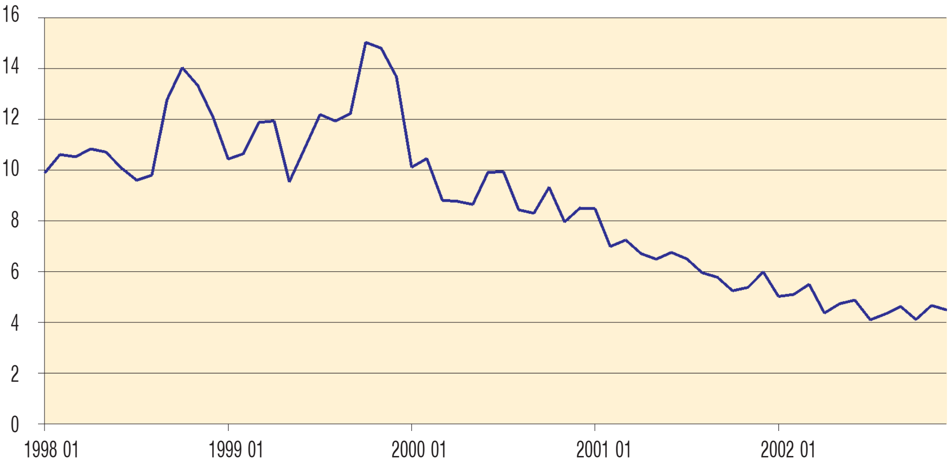
Distribution of Litas Denominated Government Securities by Maturity

Diagram 6



Average Yield of Litas Denominated Government Securities Issued in Market during 1998–2002

Chart 1



The weighted average annual interest rate on saving notes fell from 6.89% in 2001 to 4.84% in 2002, T-bills – from 5.67% to 3.69%, bonds – from 7.24% to 5.20%. The lowest interest rate established at auctions was that on six-month T-bills, i.e. 2.8% (recorded at the auction of 7 October 2002), and the highest on ten-year bonds, i.e. 6.494% (recorded at the auction of 18 March 2002). Lower borrowing costs reflect a change in the economic situation (larger surplus of free resources in the domestic market and increased investment needs of market participants), smaller sovereign's credit risk and higher market participants' confidence in the Government's policy.

The development of the weighted average annual interest rate on Litas denominated GS in the secondary market is presented in Table 1.

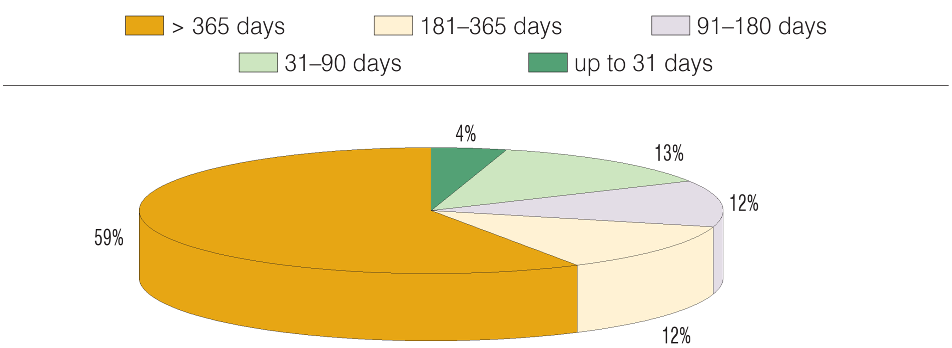
The weighted average original maturity of outstanding Litas denominated GS was 1,269 days as of end-2002 (in comparison to 951 days as of end-2001) and the remaining maturity was 896 days (in comparison to 674 days as of end-2001). The increase of these parameters was caused by, inter alia, introduction of ten-year bond issues, by increase of the share in volume of three-year and five-year bond issues, and by reduction of the volume of outstanding T-bills. During the forthcoming year it is intended to prolong further average maturity of Litas denominated GS by increasing volumes of longer maturity GS.

Weighted Average Yields (%) of Litas Denominated Government Securities Issued in Market in 1994–2002 *Table 1*

Period	Treasury bills					Bonds						T-bills and bonds	Saving notes				All GS
	up to 1 month	3 months	6 months	12 months	All T-bills	2 years	3 years	5 years	7 years	10 years	All bonds		up to 1 year	2 years	3 years	All saving notes	
1994, average	11,26	21,25	-	-	20,38							20,38					20,38
1995, average	27,55	26,09	27,22	20,15	26,65							26,65					26,65
1996, average	20,64	20,02	15,81	20,13	19,80							19,80					19,80
1997, average	6,83	8,79	9,20	9,25	8,90							8,90					8,90
1998, average	8,78	10,70	11,28	12,29	11,00							11,00					11,00
1999, average	8,12	10,33	12,25	13,65	11,40	13,73					13,73	11,43	10,45			10,45	11,39
2000, average	-	7,49	8,54	9,90	8,85	11,13	11,07	10,50			10,99	9,34	9,85			9,85	9,36
2001, average	-	-	5,67	5,67	5,67	7,78	7,07	7,04	7,52		7,24	6,41	7,65	6,27		6,89	6,46
2002, average	-	-	3,21	3,84	3,69	-	4,86	5,16	5,72	5,98	5,20	4,57	-	5,01	4,56	4,84	4,62

Secondary market of GS sold in auctions may be performed through the National Stock Exchange following the rules set by the Stock Exchange or outside the Stock Exchange. During 2002, the GS secondary market turnover in the National Stock Exchange was LTL 1,375.0 million compared to LTL 1,001.1 million during 2001 (see Diagram 7).

Secondary Market Data (by Remaining Maturity), 2002, percentage *Diagram 7*



Saving notes were launched in Lithuania's GS market in April 1999. These GS are not issued by auction and are offered only to natural persons and provide an opportunity to invest a smaller amount than in case of securities sold in auctions. Besides, they can be redeemed before their final maturity date without loosing interest due. Saving notes are offered for sale in commercial banks and brokerage companies, which have concluded agreements with the Ministry of Finance on release of GS.

Since the introduction of the saving notes, the total issue thereof has reached LTL 833.5 million at the nominal value. In the end of 2002, three-year saving notes were issued for the first time ever. Two issues (LTL 151.47 million at the nominal value) of these saving notes were sold and they accounted to 38% of the nominal value of all saving notes sold last year. Enormous popularity of the saving notes shows confidence in the Government's policy and the country's financial system.

Throughout 2002, five other issues of two-year saving notes (at the nominal value of LTL 240.37 million) were successfully completed. The sale of one issue of two-year saving notes (which was started to sell at the end of 2001) was finalised in 2002 (the nominal value of saving notes of the said issue sold during 2002 was LTL 6.71 million).

Stock of debt in saving notes as of end-2002 accounted for 13.36% of the total value of outstanding Litas denominated GS. In 2002, saving notes at the nominal value of LTL 95.59 million were redeemed, of which LTL 13.91 million (14.55%) was redeemed prematurely.

Government Securities issued for special purposes. The stock of the public debt in GS issued for restructuring of banks and settlements with creditors of the Joint Stock Company Lithuanian Stock Innovation Bank under liquidation, decreased from LTL 663.7 million in 2001 to LTL 524.54 million in the end of 2002 and accounted for 14.7% of all GS issued in Litas. The nominal value of GS for restructuring of banks totalled LTL 292.17 million as of end-2002, GS issued to settle accounts with creditors of the Joint Stock Company Lithuanian Stock Innovation Bank, i.e. legal persons and enterprises without the status of a legal person, totalled LTL 228.9 million, and GS issued to settle accounts with creditors of the Joint Stock Company Lithuanian Stock Innovation Bank, i.e. natural persons, totalled LTL 3.47 million.

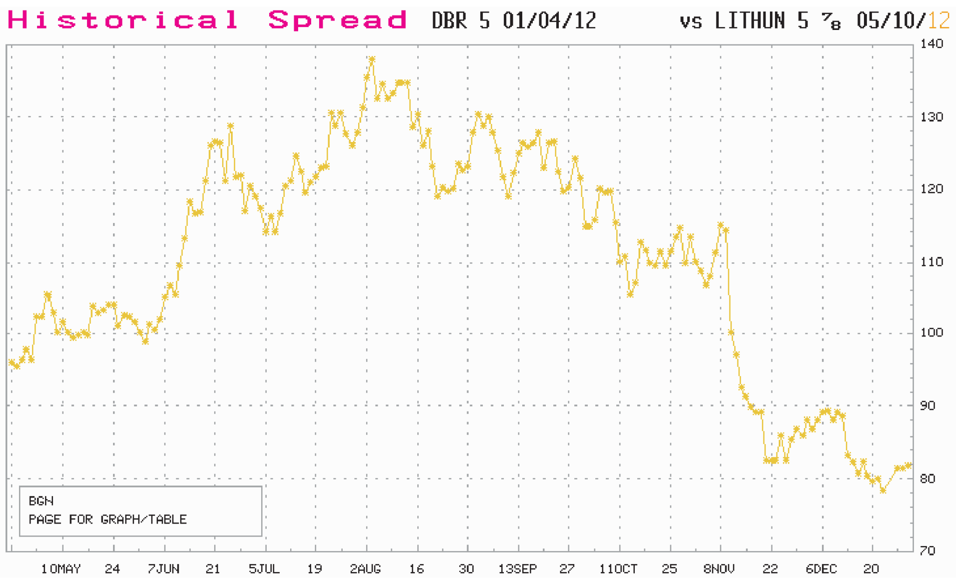
Borrowing in foreign markets. To issue foreign currency denominated Government securities in foreign financial markets, the Ministry of Finance uses services of foreign investment banks. The main instrument for borrowing in foreign markets is eurobonds.

Two eurobond issues were issued in international markets in 2002. On 24 January 2002, the Ministry of Finance through *BNP Paribas* as intermediary issued six-month T-bills in the amount of EUR 40 million and with a coupon of 3.62%. These T-bills were redeemed on 16 May.

On 8 May 2002, the Ministry of Finance through *UBS Warburg* and *JP Morgan* as intermediaries successfully issued ten-year eurobonds in the amount of EUR 400 million in international capital markets. These bonds bore a coupon of 5.875%, and a spread of 94 bps over the ten-year German Government securities. The raised funds were used to redeem the eurobond issue in the amount of USD 200 million (issued in 1997), to finance the State budget deficit and for other purposes established by the laws.

The development of the credit risk spread of the eurobond issue released in foreign markets in 2002 during the year is presented in Chart 2.

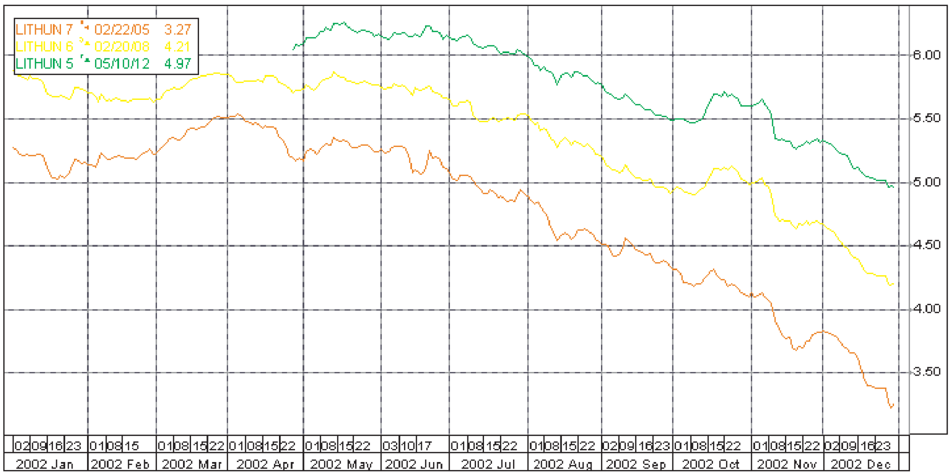
Chart 2



Source: Bloomberg

Data for the secondary market yield of the latest three eurobond issues during 2002 is given in Chart 3.

Chart 3



Source: Bloomberg

As of the end of 2002, the public debt for GS issued in the domestic and foreign markets totalled LTL 8,489.256 million (GS issued in foreign markets made up 57.96% of this debt). Compared to 2001, the share of the public debt for GS issued domestically and in foreign markets increased by LTL 1,417.334 million (20.04%).

3.2. Government Borrowing from International Financial Institutions

The Republic of Lithuania is a member of several large international financial organisations, such as the International Monetary Fund (IMF), the European Bank for Reconstruction and Development (EBRD), the Council of Europe Development Bank (CEB) and three institutions of the World Bank Group: the International Bank for Reconstruction and Development (IBRD), the International Finance Corporation (IFC) and the Multilateral Investment Guarantee Agency (MIGA).

Lithuania joined the World Bank Group in 1992 and currently holds 1,507 shares of the International Bank for Reconstruction and Development, 2,341 shares of the International Finance Corporation and 187 shares of the Multilateral Investment Guarantee Agency.

The International Bank for Reconstruction and Development is the largest lender to Lithuania among international financial organisations. Since 1992, the Bank has lent to Lithuania USD 455.4 million. By the end of 2002, USD 58.7 million of this amount has been repaid. The International Bank for Reconstruction and Development has extended loans for investment projects in environmental, energy, financial, transport, social, health care and education sectors. The IBRD has also extended two Structural Adjustment Loans (USD 80 million and EUR 108.29 million) to support structural reforms carried out by the Government. The second Structural Adjustment Loan (EUR 108.29 million) was extended in 2000. Half of this amount was disbursed in the same year. Due to the improved budget situation in 2002, the Government has decided not to proceed with the withdrawal of the second tranche of the Structural Adjustment Loan. In 2002, the IBRD extended a loan of EUR 29 million to finance Lithuania Education Project.

Since 1992, the Republic of Lithuania has been a member of the International Monetary Fund. Lithuania holds SDR 144.2 million quota of the IMF. The IMF has provided loans in total of USD 251.8 million[1] to Lithuania, of which USD 131.1 million has been repaid. No more loans have been taken from IMF since 1998, however, IMF has been providing advisory assistance to the Government of the Republic of Lithuania in the macroeconomic area and technical assistance in the areas of market operations, monetary policy, banking supervision, national accounts and adjustment of the balance of payments. In 2002, the co-operation with the IMF continued on the basis of the Memorandum of Economic Policies for the period up to 31 December 2002 signed by the Government of the Republic of Lithuania, the Bank of Lithuania and the IMF in 2001.

Lithuania has also subscribed for 2,000 shares of the European Bank for Reconstruction and Development. Since 1992, the EBRD has extended loans to Lithuania totalling USD 82.6 million. By the end of 2002, USD 45.9 million of this amount had been repaid. The EBRD loans have been used to finance projects in transport and energy sectors. In 2002, no loans from EBRD were received on behalf of the government.

In addition to the above-mentioned international financial institutions, the Republic of Lithuania has received loans from the European Investment Bank, the Nordic Investment Bank and the Council of Europe Development Bank.

Since 1994, the European Investment Bank (EIB) has extended loans to Lithuania in amount of USD 161.6 million, By the end of 2002, USD 12.4 million of this amount has been repaid. The EIB has mainly invested into transport and telecommunications, energy, industrial and environmental sectors. In 2002, no loans were extended by EIB.

Since 1996, the Nordic Investment Bank (NIB) has extended loans to Lithuania amounting to USD 37.98 million. In 2002, the NIB extended a loan of EUR 10 million to finance Lithuania's Public Institutions Buildings Energy Savings Investment Project.

Since 1997, the Council of Europe Development Bank (CEB) has extended loans in amount of USD 10.4 million to finance social projects. In 2002, the CEB extended a loan of EUR 2.9 million for financing of the Buildings Renovation of Science and Higher Education Establishments Project.

As of the end of 2002, Lithuania's debt to international financial institutions, i.e. the IMF, IBRD, EBRD, EIB, NIB, CEB and the European Union, totalled LTL 1.94 billion, or 25.7% of the total foreign debt. By the end of 2002, repayments to these international financial institutions totalled LTL 821.9 million, of which LTL 377.5 million was repaid in 2002.

3.3. Issuance of Government Guarantees

Government guarantees on loans were extended only for infrastructure investment projects of national significance that have been incorporated in the Public Investment Programme.

In 2002, the amount of government guarantees granted on foreign loans was reduced to LTL 263.35 million, or 61.9% less compared with 2000.

[1] Repaid loans that have been repaid are not included in this figure

In 2002, the State issued 2 guarantees in favour of the following creditors:

- the Nordic Investment Bank on a loan of EUR 4.344 million to the State Enterprise the Klaipėda State Seaport Authority to finance the seaport quays No 69, 70 reconstruction investment project;

- the Public Limited Company Yukos Oil Corporation of the Russian Federation on a long-term loan of USD 75 million to the Public Limited Company Mažeikių Nafta to finance the company's investment programme.

By implementing tight fiscal policies, the Government has since 2001 striven to reduce the government borrowing volumes as well as the number of government guarantees on loans and the limit thereof. In 2003, extension of new government guarantees is not envisaged.

IV. GOVERNMENT BORROWING POLICY IN 2002

In 2002, the borrowing policy objectives set by the Republic of Lithuania Government Resolution No 4 of 7 January 2002 On the Approval of the Directions for Medium-term Government Borrowing Policies were successfully met.

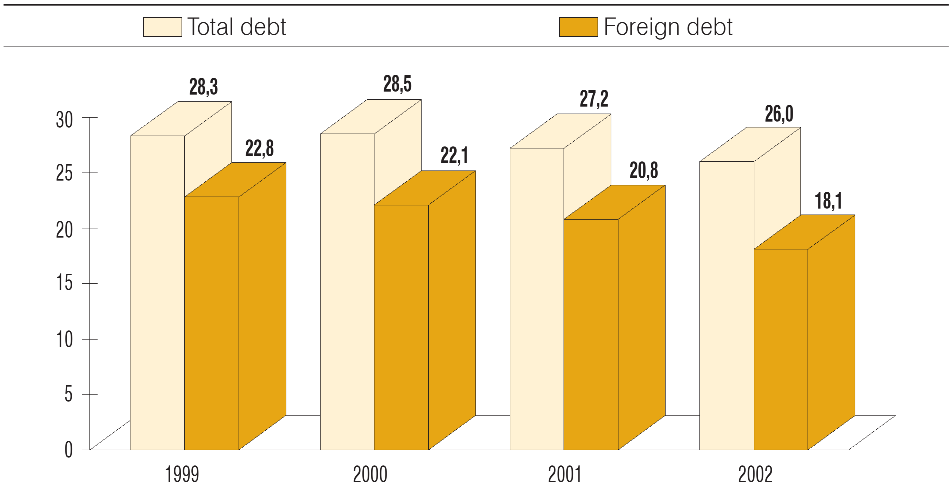
Due to a deficit national budget, a portion of the government expenditures had to be funded again from borrowed funds, and the the Law on the Approval of the Financial Indicators of the State Budget and Municipal Budgets for 2002 established a **net borrowing limit of LTL 1,100 million** (loans raised in that year minus the repaid loans). Compared to previous years (LTL 1,400 million in 2001, LTL 1,600 in 2000, LTL 2,900 million in 1999), this limit was reduced.

The actual net government borrowing volume did not exceed the established limit and comprised LTL 1,072.0 million.

By the end of 2002, the total public debt comprised LTL 13,161.5 million. Despite the fact that the total amount of the public debt increased by LTL 257.9 million, its relative amount, i.e. its proportion against the gross domestic product (GDP), decreased by 1,2 % over the year, while the amount of the foreign debt by as much as 2.7 per cent (Diagram 8).

Total Public Debt Relative to GDP in 1999–2002, percentage

Diagram 8



In 2002, debt management was performed strictly observing all debt limits established by legal acts of the Republic of Lithuania limiting government borrowing, extension of government guarantees, amount of debt and defining the structure of the total debt (Table 2).

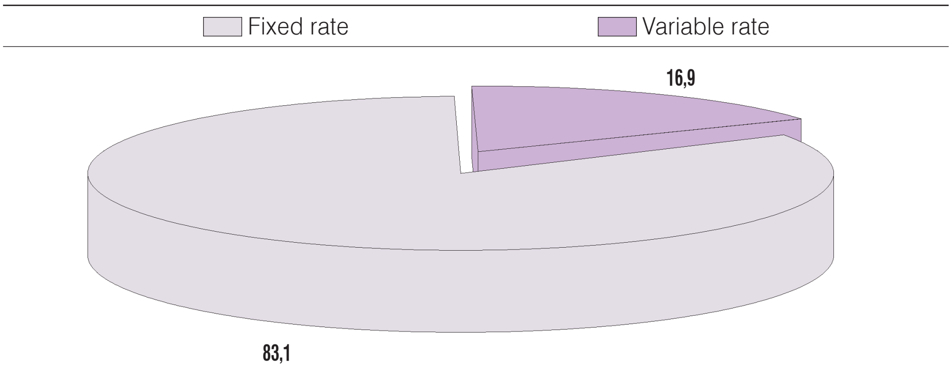
Debt Limits as of 31 December 2002

Table 2

Title	Fixed rate	Actual amount
Net borrowing, LTL million	1.100,0	1.072,0
Share of public debt in the gross domestic product (not more than), percentage	30,0	26,0
Share of foreign debt in the gross domestic product (not more than), percentage	25,0	18,1
Share of foreign debt in Euro assumed on behalf of the government in the total foreign debt (at least), percentage	75,0	76,0
Share of short-term debt in the total public debt (not more than), percentage	25,0	5,4
Share of government expenditure on interest on loans in the annual revenue of the State budget (not more than), percentage	15,0	7,5
Share of the direct government debt liabilities at a fixed interest rate in the total direct debt liabilities (at least), percentage	70,0	83,1
Liabilities of guarantee institutions and insurance companies, fulfilment whereof is guaranteed by the government, LTL million	250,0	166,7
New government guarantees signed in 2002, LTL million	400,0	263,3

To avoid the risk of exchange rate fluctuations and its impact on the stability of debt servicing costs, the government increasingly borrowed at a fixed interest rate and by the end of 2002 **the direct government liabilities at a fixed interest rate** comprised 83.1% of the total direct government liabilities (Diagram 9).

Direct Public Debt by Type of Interest Rate as of 31.12.2002, percentage *Diagram 9*



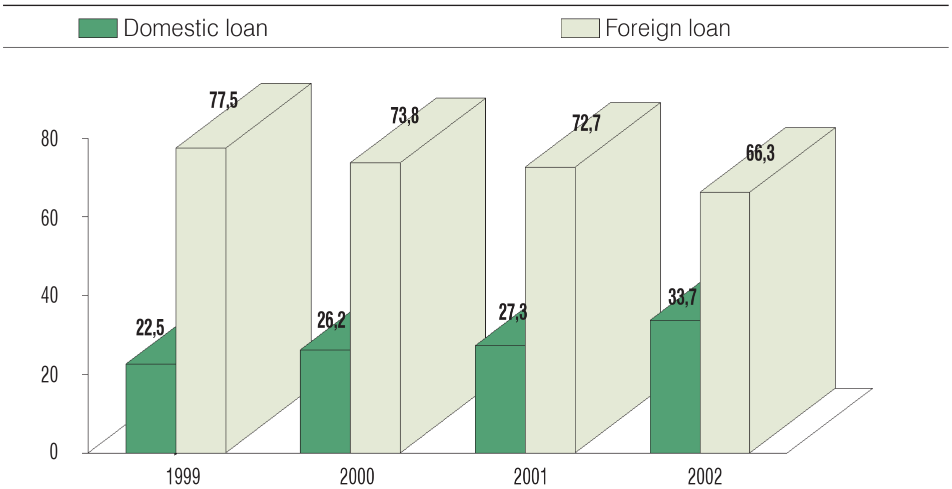
For several years already, the Government's strive for **promotion of the development of the domestic financial market** has been pursued resulting in increase of the borrowing in the domestic market.

Over the year, the direct domestic debt increased by LTL 902.7 million and amounted to LTL 3,830.9 million, or 33.7% of the total direct debt (compared to 27.3% in the end of 2001) (Diagram 3).

Due to the fact that the Government promotes the development of the domestic financial market, and at the same time respects the net borrowing limit, borrowing in foreign markets is restricted.

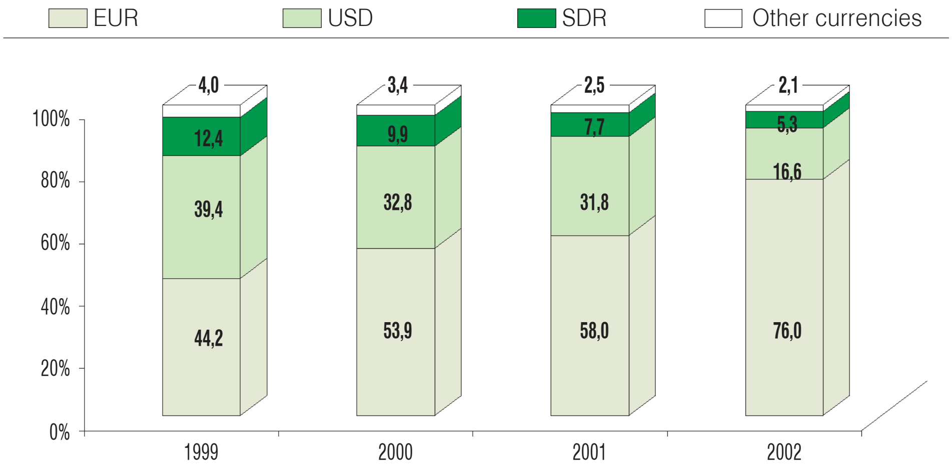
In 2002, the direct foreign debt decreased by LTL 260 million and amounted to LTL 7,535.6 million, or 66.3% of the total direct debt (compared to 72.7% in the end of 2001) (Diagram 10).

Proportions of the Direct Foreign and Domestic Debt in 1999–2002, percentage *Diagram 10*



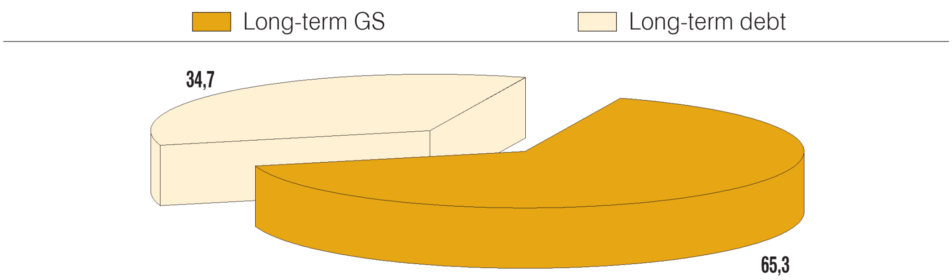
The structure of the foreign debt by currency has entirely transformed. Prior to pegging of the Litas to the Euro (on 2 February 2002), the currency used in most borrowing transactions had been the US dollar, and the dollar had accounted for a third of the total liabilities assumed on behalf of the government (31.8% in 2001). Afterwards, seeking to protect the foreign debt from exchange rate fluctuations, the government borrowed increasingly in Euro, and in 2002 almost all funds borrowed abroad (about LTL 1,615.6 million) were denominated in Euro. By the end of the year, this share of the foreign debt had increased to 76% of the total direct foreign debt, while the portion of the debt in US dollars decreased to 16.6% (Diagram 11).

Direct Foreign Debt by Currency in 1999–2002, percentage *Diagram 11*



In order to continually increase the share of GS issued in foreign markets in the total direct foreign debt, GS for LTL 1,381.1 million was issued in foreign markets in 2002, and in the end of the year they accounted for almost two thirds of the direct foreign debt, i.e. 65.3% (Diagram 12).

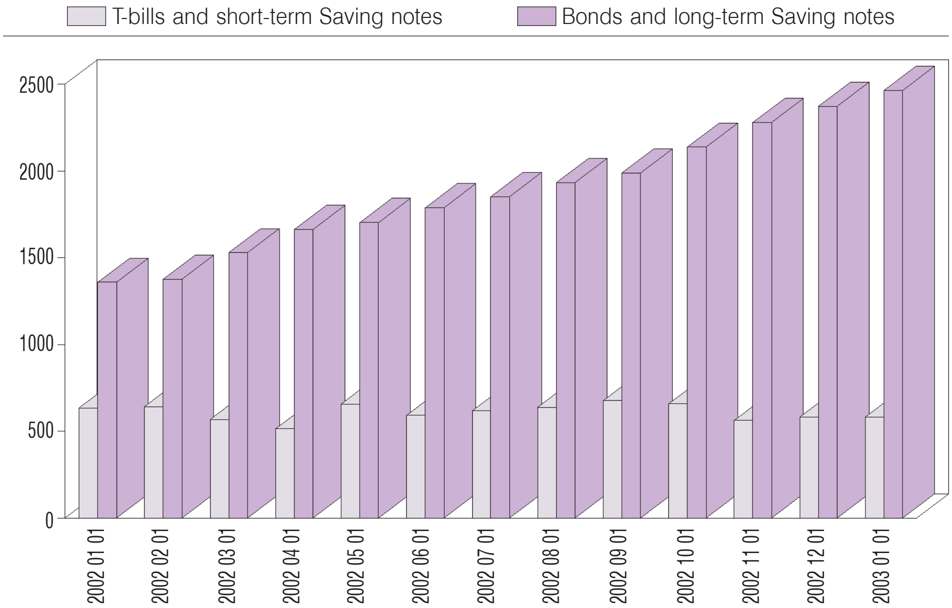
Direct Foreign Debt by Instrument as of 31.12.2002, percentage *Diagram 12*



To reduce the risk of re-financing in the domestic and foreign financial markets, **new long-term debt instruments were used**.

In 2002, the government borrowed in the domestic market almost exclusively by of issuing long-term Government securities (GS): three-year saving notes and ten-year bonds were launched for the first time in the domestic market. Thus, the volume of outstanding short-term GS remained almost unchanged in 2002, while the volume of long-term GS increased and in the end of the year exceeded the volume of short-term GS four times (long-term GS with the value of LTL 2,463.6 million and short-term GS worth LTL 580.9 million) (Diagram 13).

Change of Balance of Outstanding GS in 2002, LTL million *Diagram 13*

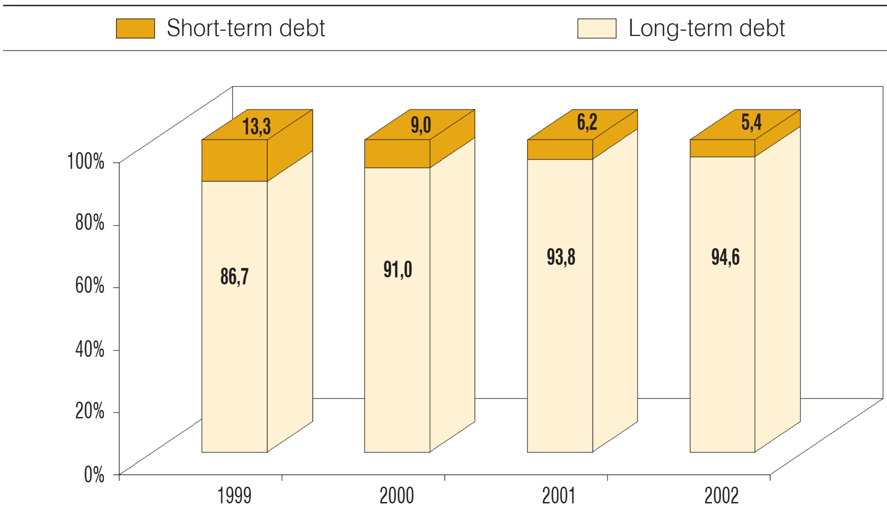


Ten-year bonds were issued in the foreign markets for the first time, namely, EUR 400 million eurobond issue, and all direct government liabilities in foreign currency (bonds and loans) were long-term and in the end of the year.

Contingent short-term liabilities of the government (liabilities of guarantee institutions and insurance companies, fulfilment whereof is guaranteed by the government) amounted to LTL 131.6 million, i.e. only 7.3% of the total government guarantees.

Thus, in the end of 2002, the total long-term public debt amounted to LTL 12,449.1 million, or 94.6% of the public debt, whereas the short-term debt (liabilities not exceeding one year) decreased to LTL 712.4 million and comprised 5.4% of the public debt (Diagram 14). The major share of the short-term debt, i.e. 81.5% was composed of T-bills issued in the domestic market in the amount of LTL 580.9 million.

Structure of Total Public Debt by Maturity in 1999–2002 *Diagram 14*



V. PUBLIC DEBT FORECAST

In the medium-term, the Government of the Republic of Lithuania intends to continue pursuing tight borrowing policies and secure the funding of the government expenditure from borrowed funds with minimum costs and risks.

The Medium-term Government Borrowing Policy approved by the Government of the Republic of Lithuania places a limit on debt as a percentage of GDP, i.e. as of December 2004, the public debt should not exceed 30%, and the foreign debt 25% of GDP.

The direct government borrowing need for 2003 is expected to amount to about LTL 4,300 million. The borrowed funds would be mostly used for funding of the State budget deficit and for repayment of the government foreign debt and the government domestic debt. It is envisaged to fund the borrowing needs by issuing GS domestically and by issuing a EUR 400 million eurobond issue in foreign markets.

The Republic of Lithuania Law on Approval of Financial Indicators of the State Budget and the Budgets of Municipalities for 2003 sets the net government borrowing limit of LTL 900 million (LTL 1,100 million in 2002). Government guarantees on new projects for 2003 will not be extended (LTL 400 million was the limit set for 2002).

Presuming that the Government will continue pursuing tight fiscal policies, in the end of 2003 the public debt (including guarantees extended by the government on domestic and foreign loans) should account for approximately 25,7 % of GDP (25.96% in the end of 2002), a subsequent gradual decrease of the aforementioned percentage is expected.

Provided a favourable situation is maintained, it is envisaged to further increase the share of debt liabilities in the domestic currency, increase the average maturity of issued borrowing instruments (bonds, saving notes) and to boost liquidity of Government securities in the secondary market. The aforementioned factors should even more markedly contribute to the promotion of the domestic and foreign investment into Government securities and expand the domestic financial market.

As concerns borrowing in foreign markets, it is envisaged to aim at continually increasing the share of GS denominated in foreign currencies in the total foreign debt, and to reduce borrowing from international financial organisations. It is also planned that the foreign debt denominated in Euro will augment and in the end of 2004 it should comprise more than 80% of the direct foreign debt assumed on behalf of the government.

Priority will be given to borrowing at fixed interest rates with the view to reduce interest risks and subdue fluctuations of debt servicing costs. The direct government debt liabilities at fixed interest rates should comprise at least 70% of the total debt liabilities assumed on behalf of the government.

The Short-term public debt, i.e. commitments of the initial maturity of up to 1 year, should not exceed 25% of the public debt.

It is expected that pursuance of stringent fiscal policies by the Government in the medium-term and improvement of Lithuania's macroeconomic indicators will lead to improvement of Lithuania's international credit rating, which would reduce borrowing costs and debt servicing costs. It is likely that within the EU pre-accession period, at least one international rating agency will upgrade the government's long- term foreign currency debt rating to A–.