

## Lithuania: One foot in the eurozone already

### Summary

- Lithuania met all the euro convergence criteria and will almost surely become the 19<sup>th</sup> member of the euro zone in 2015
- Final decision on Lithuania's accession to the euro zone will be made on July 22, 2014
- Lithuanian credit rating was raised by two notches by S&P in April 2014 based on the expectation that Lithuania will join eurozone in 2015
- However, a number of structural reforms still needs to be implemented to ensure the continuation of the real economic convergence

**Maastricht criteria:** Lithuania met all the euro convergence criteria and will almost surely become the 19<sup>th</sup> member of the euro-zone in 2015. Budget deficit was significantly lower than expected falling to just 2.2% of GDP in 2013. Better than expected result was achieved primarily due to lower than planned budget expenditures and to a lesser degree – higher than expected tax revenues. Favourable developments of global energy and food prices as well as meagre domestic inflationary pressures kept inflation at bay with average annual inflation falling to 0.6% in April 2014.

**Final decision:** Final decision on Lithuania's accession to the euro zone will be made by the ECOFIN council on July 22, 2014. The decision is highly expected to be positive, since Lithuania not only meets all the euro convergence criteria, but also shows strong commitment to sustain prudent fiscal and economic policies in the future. Contrary to pre-crisis period, Lithuania is among the most stable and fastest growing EU countries with no major macroeconomic imbalances. Geopolitical tensions in Ukraine also help supporting Lithuanian case.

**Credit ratings:** Acknowledging the improved fiscal situation, healthy economic growth and increased likelihood of joining euro in 2015, S&P raised Lithuanian credit rating by two notches in April 2014: from BBB to A-. As a consequence, Lithuanian long-term borrowing costs fell to record-low levels. It is expected that other credit agencies will follow shortly.

**Real convergence:** The greatest challenge, however, is to ensure the real economic convergence in post-eurozone period. Examples of Portugal, Italy or Greece show that without institutional and economic reforms, there is no guarantee that economic convergence will continue. Hence, Lithuania will face many challenges in trying to improve business, economic and institutional framework, the success of which is not guaranteed.

### Lithuania meets all the Euro convergence criteria

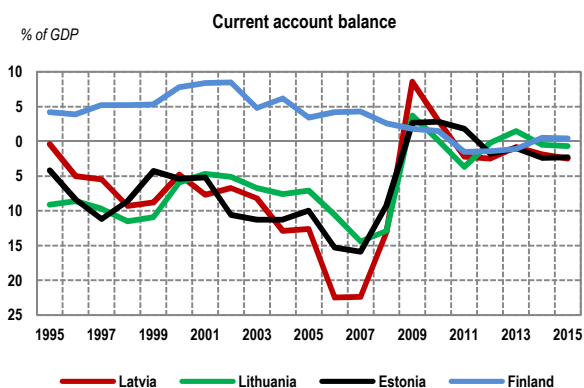
Criteria	Lithuania	Reference
HICP inflation (12 month m.a.)	0.6%	0.7-1.7%*
Budget deficit (% of GDP)	2.2%	3.0%
Public debt (% of GDP)	39.4%	60%
Long-term interest rates	3.6%	5.4-6.5%*
Exchange rate	3.4528	3.4528±15%

\*Countries with negative inflation rate may be excluded from the estimation of reference value (Greece, Bulgaria, Cyprus)

### Credit ratings are expected to improve

Criteria	S&P	Moody's	Fitch
Lithuania	A-	Baa1	BBB+
Latvia	BBB+	Baa2	BBB+
Estonia	AA-	A1	A+
Sweden	AAA	Aaa	AAA
Finland	AAA	Aaa	AAA
Poland	A-	A2	A-
Russia	BBB-	Baa1	BBB

### Sustainability should be maintained



Source: Eurostat

### Real economic convergence remains a challenge

Ranking	Global competitiveness index	Ease of doing business	Corruption perception index
Lithuania	48	17	43
Latvia	52	24	49
Estonia	32	22	28
Sweden	6	12	3
Finland	3	14	3
Poland	42	45	38
Russia	64	92	127