

## Commission assesses the state of convergence in Lithuania

***The European Commission has assessed, at the request of the Lithuanian authorities, whether Lithuania is ready to adopt the euro and concluded that, at the present stage, there should be no change in its status as an EU Member State with a derogation<sup>1</sup>.***

*"Lithuania meets all the convergence criteria except the one on inflation. The average rate of inflation has been slightly above the reference value since April 2005 and is expected to rise gradually until the end of the year. I commend Lithuania for its strong economic performance and sincerely wish that it will soon be able to meet all conditions for euro area membership, a goal which the Commission supports not only for Lithuania but for all EU Member States,"* said Economic and Monetary Affairs Commissioner Joaquín Almunia.

Article 122(2) of the Treaty requires the Commission to assess the fulfilment of the conditions for full participation in the Economic and Monetary Union by Member States with a derogation at least once every two years or at the request of a Member State.

The Lithuanian authorities asked the Commission and the European Central Bank on 16 March to assess whether the country was meeting the necessary conditions for adopting the euro. Slovenia made a similar request on 2 March (see press release [IP/06/623](#) published today).

In its so-called Convergence Report, the Commission assesses whether Lithuania has achieved a high degree of sustainable convergence, measured against the criteria set out in Article 121(1) regarding the government budgetary position, price stability, exchange rate stability and convergence of long-term interest rates. Compatibility of the legal framework with the Treaty is also examined. The ECB also issued a Convergence Report today as envisaged by the Treaty.

### Results of the convergence examination

On the basis of the reports, the Commission concludes that there should be no change at present to Lithuania's status as a Member State with a derogation pursuant to Article 122(1).

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<sup>1</sup> The 10 countries that became members of the EU in May 2004 were given a derogation from adopting the euro as they were not yet meeting the necessary conditions.

## **Inflation**

The average inflation rate in Lithuania during the 12 months to March 2006 was 2.7 percent, just above the reference value of 2.6 percent. 12-month average inflation in Lithuania has been slightly above the reference value since April 2005 and, based on the present outlook for inflation, is likely to stay above until the end of the year. In a longer-term perspective, buoyant domestic demand, energy price increases and increases in indirect taxes represent risk factors for inflation. The achievement and maintenance of a low level of inflation in the medium-term will also depend on maintaining the appropriate fiscal policy and on keeping wage growth in line with productivity developments.

## **Government budgetary situation**

Since EU accession, Lithuania has never been subject to an Excessive Deficit Procedure. Its general government deficit declined from 1.5 percent in 2004 to 0.5 percent of GDP in 2005. General government debt has been on a declining trend and, at below 20 percent of GDP, remains well below the Treaty threshold. According to the Convergence Programme submitted by the Lithuanian government in December 2005, the budgetary strategy is to gradually reduce the general government deficit to 1 percent of GDP in 2008. The Ecofin Council has regarded the Lithuanian budgetary targets as plausible and the underlying risks balanced. However, it invited Lithuania to strengthen the effort in terms of structural budgetary adjustment.

## **Exchange rate**

The litas has participated in ERM II since 28 June 2004 and Lithuania has maintained its currency board arrangement as a unilateral commitment within ERM II. During the two years before the convergence examination, the litas has remained stable vis-à-vis its ERM II central rate.

## **Long-term interest rates**

Between ERM II entry in June 2004 and March 2006, the spread of long-term government bond yields vis-à-vis the euro area declined from some 55 basis points to around 25 basis points, reflecting the credibility of Lithuania's convergence process. The 12-month average of long-term interest rates showed a steady decline over the whole assessment period. In the year to March 2006, the average long-term interest rate in Lithuania stood at 3.7 percent, well below the reference value of 5.9 percent.

## **Legal convergence**

The remaining incompatibilities between the Lithuanian legislation and the statutes of the European System of Central Banks/ECB as regards the central bank integration into the ESCB have been addressed in three laws that are planned to enter into force on the day of the abrogation of Lithuania's derogation.