

## INTERNATIONAL MONETARY FUND ASSESSMENT LETTER



INTERNATIONAL MONETARY FUND



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May 17, 2019

International Monetary Fund  
Washington, D.C. 20431 USA

### **IMF Executive Board Approves US\$248.2 Million Stand-By Arrangement for Armenia**

- The IMF approved a 36-month Stand-By Arrangement (SBA) for Armenia amounting to about US\$248.2 million. The Armenian authorities have indicated that they will treat the arrangement as precautionary, and do not intend to draw on the new SBA unless shocks generate balance of payments needs.
- The SBA will support the authorities' efforts to strengthen the economic fundamentals and policy frameworks. It will also help effective implementation of structural reforms, particularly relating to governance and improving business climate.
- The authorities are committed to a sustainable fiscal path, supported by the fiscal rule, while creating space for critical spending in enhancing infrastructure and social spending.

The Executive Board of the International Monetary Fund (IMF) today approved a 36-month Stand-By Arrangement (SBA) for Armenia amounting to SDR 180 million (about US\$248.2 million or about 139.75 percent of Armenia's quota in the IMF).

Upon the Board's approval, an amount equivalent to SDR 25.714 million (about US\$35.5 million) becomes immediately available to Armenia, and the remaining amount will be made available, subject to six semi-annual reviews.

The Armenian authorities have indicated that they will treat the arrangement as precautionary, and do not intend to draw on the new SBA unless shocks generate balance of payments needs. In addition to providing insurance against shocks, the arrangement will support the authorities' efforts to strengthen the economic fundamentals and policy frameworks. It will also help effective implementation of structural reforms, particularly relating to governance and improving business climate.

Following the Executive Board discussion, Mr. Mitsuhiro Furusawa, Deputy Managing Director and Acting Chairman, issued the following statement:

"Armenia has continued to make progress in recent years in maintaining macroeconomic and financial stability and in implementing structural reforms to promote growth. Economic

activity has strengthened, and public debt has started to decline. Inflation is under control, the financial system remains stable, and international reserves are assessed to be adequate. Nonetheless, continuing reform efforts are needed to support a more balanced and inclusive growth, by reducing imbalances, improving the business climate and strengthening governance, and advancing measures to reduce poverty and unemployment.

“The three-year Stand-By Arrangement will support the authorities’ objective of moving toward a more dynamic, sustainable, and inclusive economy. The precautionary nature of the arrangement will provide insurance against external shocks. The authorities are committed to a sustainable fiscal path, supported by the fiscal rule, while creating space for critical spending in enhancing infrastructure and social spending. These objectives need to be accompanied by measures to improve tax administration and modernize property taxation.

“Further strengthening of the monetary policy framework will improve the effectiveness of monetary policy and help bring inflation back to its medium-term target. Measures will also be taken to safeguard the financial system, further develop capital markets, and improve access to finance.

“The decisive implementation of a strong package of structural reforms will help foster sustainable and inclusive growth through measures that promote private sector development, attract more FDI, and increase diversification. Steps to enhance human capital and increase female labor force participation will also be helpful.”

## **Annex**

Since the completion of the 2014–17 IMF-supported program ([See Press release No. 14/88](#)), economic and financial stability has been maintained and macroeconomic policy implementation has been sound. Despite gradual improvements, poverty and unemployment remain relatively high, causing migration and a shrinking labor force.

Against this backdrop, the newly formed government, which took office after the 2018 peaceful political transition, launched a five-year economic program in February 2019. This watershed moment created a new opportunity for Armenia to deal with the oligarchical economic system and combat corruption. The government program is centered on advancing structural reforms to generate a broad-based inclusive growth and strong policies to maintain macroeconomic stability. To support this program, the authorities have requested a Stand-By Arrangement (SBA) with the Fund.

## Program Summary

The government's program for 2019-23, supported by the SBA aims to maintain macroeconomic stability and promote higher and more inclusive growth. It is based on four pillars: (i) anchoring fiscal policy on the fiscal rule to maintain debt sustainability, and creating space for priority (social and capital) spending; (ii) further strengthening of the monetary policy framework and maintaining a flexible exchange rate system; (iii) safeguarding the financial system and improving access to finance; and (v) implementing a strong package of structural reforms, with renewed emphasis on inclusiveness and governance.

**Promoting Growth-friendly Fiscal Consolidation.** The new arrangement will support the authorities' prudent fiscal consolidation plan, guided by the fiscal rule, to bring central government debt to below 50 percent of GDP in the medium term. This will be accompanied by strong efforts to enhance revenue mobilization to help create space to boost growth-enhancing infrastructure and social spending. In addition, the authorities' tax reform plans will be accompanied by sustainable compensating measures to offset expected revenue shortfalls, and more targeted measures toward the poor to make the tax system more progressive. Meanwhile, structural fiscal reforms will aim to strengthen public financial management to buttress fiscal discipline and protect essential expenditure, including foreign-financed capital spending.

**Enhancing Resilience and Promoting Deepening of the Financial Sector.** Drawing on the 2018 financial sector assessment program, the Central Bank of Armenia will aim to (i) safeguard financial stability by improving the risk-based supervision framework; (ii) strengthen macroprudential measures in light of high levels of dollarization; (iii) enhance banks' foreign currency liquidity buffers; and (iv) further develop capital market to mobilize a growing supply of long-term domestic capital to fund economic developments and channeling it to the economy.

**Reinvigorating Structural Reforms.** The new program aims to help the authorities: (i) strengthen governance and institutions, which has been a long-standing issue; (ii) improve the business environment to attract investment and ignite more inclusive and durable growth; and (iii) enhance social safety net programs to include better education and health care access for the most vulnerable.

Table 1. Armenia: Selected Economic and Financial Indicators, 2016–23

	2016	2017	2018	2019	2020	2021	2022	2023
	Act.	Act.	Act.			Projections		
National income and prices:								
Real GDP (percent change)	0.2	7.5	5.2	4.6	4.5	4.5	4.5	4.5
Final consumption expenditure, Contrib. to Growth	-0.9	7.4	2.7	3.3	3.4	2.7	3.5	2.1
Gross fixed capital formation, Contrib. to Growth	-2.4	1.5	0.8	6.8	4.6	5.0	4.2	3.1
Changes in inventories, Contrib. to Growth	0.7	1.1	4.0	-4.6	0.0	0.0	0.0	0.0
Net exports of goods and services, Contrib. to Growth	3.1	-1.2	-1.8	-1.2	-3.4	-3.1	-3.2	-0.6
Gross domestic product (in billions of drams)	5,067	5,569	6,003	6,549	7,102	7,745	8,437	9,169
Gross domestic product per capita (in U.S. dollars)	3,524	3,872	4,186	4,533	4,764	5,068	5,386	5,710
CPI (period average; percent change)	-1.4	1.0	2.5	2.1	3.0	3.7	4.0	4.1
CPI (end of period; percent change)	-1.1	2.6	1.8	2.5	3.3	3.8	4.1	4.3
GDP deflator (percent change)	0.3	2.2	2.5	4.3	3.8	4.4	4.2	4.0
Unemployment rate (in percent)	20.2	18.6	18.1	17.9	17.7	17.8	17.7	17.6
Investment and saving (in percent of GDP)								
Investment	18.0	19.0	22.4	23.6	24.1	24.4	24.9	25.6
National savings	15.8	16.6	13.3	16.3	16.8	17.5	18.4	19.4
Money and credit (end of period)								
Reserve money (percent change)	13.1	-1.0	17.8	9.0	9.5	8.5	8.5	8.5
Broad money (percent change)	16.6	17.7	8.1	7.0	9.5	8.5	8.5	8.5
Private sector credit growth (percent change)	14.4	16.9	16.4	16.0	15.5	13.0	12.5	11.0
Central government operations (in percent of GDP)								
Revenue and grants	21.4	21.2	21.7	22.6	22.8	22.8	22.9	23.2
Of which: tax revenue	20.1	20.2	20.6	21.0	21.3	21.5	21.7	21.9
Expenditure	27.0	26.0	23.5	25.2	24.9	24.7	24.7	25.0
Overall balance on a cash basis	-5.6	-4.8	-1.8	-2.5	-2.1	-1.9	-1.8	-1.8
Public and publicly-guaranteed (PPG) debt	56.7	58.9	55.8	54.6	53.7	52.3	51.1	50.1
Central Government's PPG debt (in percent)	52.0	53.7	51.4	51.0	50.8	50.2	49.5	49.0
Share of foreign currency debt (in percent)	80.9	81.1	77.5	77.6	76.5	75.4	73.9	74.3
External sector								
Exports of goods and services (in millions of U.S. dollars)	3,500	4,307	4,669	5,074	5,361	5,744	6,137	6,625
Imports of goods and services (in millions of U.S. dollars)	-4,516	-5,710	-6,583	-7,132	-7,467	-7,892	-8,371	-8,875
Exports of goods and services (percent change)	11.6	23.0	8.4	8.7	5.7	7.2	6.8	7.9
Imports of goods and services (percent change)	2.2	26.4	15.3	8.3	4.7	5.7	6.1	6.0
Current account balance (in percent of GDP)	-2.3	-2.4	-9.1	-7.3	-7.3	-6.9	-6.5	-6.2
FDI (net, in millions of U.S. dollars)	272	228	266	296	318	346	376	407
Gross international reserves (in millions of U.S. dollars)	2,204	2,314	2,249	2,284	2,373	2,418	2,468	2,633
Import cover 1/	4.6	4.2	3.8	3.7	3.8	3.5	3.3	3.4
End-of-period exchange rate (dram per U.S. dollar)	484	484	484	...	...	...	...	...
Average exchange rate (dram per U.S. dollar)	480	483	483	...	...	...	...	...

Sources: Armenian authorities; and Fund staff estimates and projections.

1/ Gross international reserves in months of next year's imports of goods and services, including the SDR holdings.



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May 31, 2019

International Monetary Fund  
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Washington, D. C. 20431 USA

### **IMF Executive Board Concludes 2019 Article IV Consultation with the Republic of Armenia**

On May 17, 2019, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation<sup>1</sup> with the Republic of Armenia.

Armenia's economy continues to perform well. Activity expanded by 5.2 percent in 2018, aided by a pickup in private investment and continued recovery in remittances, and annual consumer price index (CPI) inflation fell to 1.9 percent in March. The current account deficit widened to 9.1 percent of GDP in 2018, primarily owing to stronger capital goods imports, weaker primary income, and some measurement issues. Fiscal consolidation is on track, supported by strong tax administration efforts, with public debt as a share of GDP declining in 2018. Monetary and financial conditions remain stable with limited pressure on the exchange rate. The banking sector is well-capitalized, and credit growth has been supporting economic activity. On the structural front, the fiscal rule was redesigned and improved in December 2017. A full-fledged pension reform came into effect in July 2018. A draft public-private partnership law has been prepared in consultation with international development partners, including the IMF. The new government has pledged to speed up reform, in particular to decisively combat corruption and improve governance, with a view to promoting inclusive and sustainable growth.

Looking ahead, growth is expected to moderate to a more sustainable level of 4.6 percent in 2019 and stabilize at 4.5 percent over the medium term. The authorities are aiming for higher medium-term growth supported by reform. CPI inflation is projected to converge to the Central Bank of Armenia's (CBA's) medium-term target of 4 percent over the next two years. The current account deficit is expected to improve to 7.3 percent of GDP in 2019, as transitory factors begin to fade, and gradually fall to a more sustainable level of around 6 percent of GDP, as exports continue to grow and imports moderate somewhat.

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<sup>1</sup> Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board.



Downside risks to growth are mostly external. They include increased global trade tensions and turbulence in global financial markets, both of which could lower trading partners' growth, remittances, and commodity prices. On the upside, faster progress on the reform agenda could boost potential growth.

### **Executive Board Assessment<sup>2</sup>**

Executive Directors agreed with the thrust of the staff appraisal. They commended the authorities' efforts in recent years to maintain macroeconomic stability and strengthen policy frameworks. Directors noted that Armenia remains vulnerable to external shocks and faces structural challenges in its transition toward a dynamic, private-sector led emerging market economy. In this context, they welcomed the new government's reform agenda, particularly anti-corruption efforts to improve governance and the business environment, to foster sustainable and inclusive growth. Directors emphasized that ownership and resolute implementation are key to the success of the reforms.

Directors supported the authorities' fiscal consolidation plans, guided by the fiscal rule, aiming to bring central government debt to below 50 percent of GDP in the medium term, while leaving adequate fiscal space for critical spending. They noted that the authorities' tax reform, including the simplification of the personal income tax system, is aimed at improving compliance and supporting economic activity. However, they cautioned that careful monitoring is needed to avoid a fall in revenues and a worsening of income distribution. Directors also underscored the need for accompanying sustainable compensating measures and strong tax administration efforts. Strengthening revenue mobilization would help preserve debt sustainability while also creating needed space for growth-enhancing infrastructure and social spending. In this regard, further efforts to improve public investment management were encouraged.

Directors considered that the current monetary policy stance remains appropriate and that policy should remain focused on bringing inflation back to its medium-term target. At the same time, they underscored the importance of continued exchange rate flexibility in responding to external shocks, maintaining foreign exchange reserves at an adequate level, and protecting competitiveness. Foreign exchange market interventions should be limited to preventing disorderly market fluctuations.

Directors encouraged further strengthening of the monetary and financial sector policy frameworks. To increase the effectiveness of inflation targeting and monetary transmission mechanism, they noted the need to develop a well-functioning interbank market, enhance communication, and promote de-dollarization. In supporting a more resilient financial sector and strengthening the macroprudential framework, Directors welcomed the authorities' commitment

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<sup>2</sup> At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. An explanation of any qualifiers used in summings up can be found here: <http://www.imf.org/external/np/sec/misc/qualifiers.htm>.

to bolstering banks' foreign exchange liquidity buffers, and encouraged measures to develop capital markets further and increase access to finance.

Directors noted the importance of advancing structural reforms to foster sustainable and inclusive growth through measures that promote private sector development, attract more FDI, and increase diversification. They welcomed the government's strong commitment through its five-year program to strengthen governance, enhance competition, and improve the business climate. Measures to enhance human capital and foster female labor market participation were also encouraged.

It is expected that the next Article IV consultation with the Republic of Armenia will be held in accordance with the Executive Board decision on consultation cycles for members with Fund arrangements.

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Broad money (percent change)	17.5	18.5	7.4	7.0	9.5	8.5	8.5	8.5
Private sector credit growth (percent change)	6.0	16.5	17.2	16.0	15.5	13.0	12.5	11.0
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Sources: Armenian authorities; and Fund staff estimates and projections.

1/Gross international reserves in months of next year's imports of goods and services, including the SDR holdings.