

PROJECT INFORMATION DOCUMENT (PID) APPRAISAL STAGE

Report No.: PIDA36448

Project Name	Local Economy and Infrastructure Development Project (P150327)
Region	EUROPE AND CENTRAL ASIA
Country	Armenia
Sector(s)	Sub-national government administration (20%), SME Finance (10%), Rural and Inter-Urban Roads and Highways (35%), General water, sanitation and flood protection sector (35%)
Theme(s)	Micro, Small and Medium Enterprise support (10%), Cultural Heritage (20%), Urban Economic Development (25%), City-wide Infrastructure and Service Delivery (35%), Infrastructure services for private sector development (10%)
Lending Instrument	Investment Project Financing
Project ID	P150327
Borrower(s)	REPUBLIC OF ARMENIA
Implementing Agency	Armenia Territorial Development Fund
Environmental Category	B-Partial Assessment
Date PID Prepared/Updated	20-Nov-2015
Date PID Approved/Disclosed	25-Nov-2015
Estimated Date of Appraisal Completion	10-Nov-2015
Estimated Date of Board Approval	22-Dec-2015
Appraisal Review Decision (from Decision Note)	The chair authorized the team to proceed with project appraisal subject to meeting all the recommendations of the Decision Review Meeting.

I. Project Context

Country Context

Armenia is a small (29,800 km²), landlocked lower-middle income country with a population of about 3 million, with a large diaspora population of around 7 million, and an average per capita Atlas Gross National Income (GNI) of US\$3,810 in 2014. In the decade preceding the global economic and financial crisis, real Gross Domestic Product (GDP) growth was more than 10 percent per annum, strongly fueled by remittances. In 2009, there was a substantial contraction of 14.1 percent. Growth has since resumed, although at a slower pace, averaging to 4.2 percent during 2010-2014. In 2014 the largest components of GDP (measured at factor costs) were services, including tourism and travel (51 percent); industry, including mining and energy (29 percent); and agriculture (21 percent). Inflation has dropped to about 4 percent at present from as high as 9 percent in 2010, but was less than 5 percent throughout most of the last decade.

Improved institutions and implemented structural reforms yet to result in poverty reduction gains. Armenia joined the World Trade Organization (WTO) in January 2003 and has put in place a favorable trade environment with low tariffs and some improvements in tax and customs administration. It is ranked 52nd in the Index of Economic Freedom and 35th in the 2016 Doing Business Index, with a major constraint identified as connection to the electricity grid. The population has declined in recent years mainly due to migration; about 64 percent of the population is urban. In the 1990s, more than 50 percent was classified as poor. This figure was reduced to 27.6 percent in 2008, but increased to around 36 percent in 2010 due to the economic and financial crises, before declining moderately to 32 percent in 2013. The level of poverty is the highest in cities other than Yerevan.

According to the Armenia Development Strategy (ADS), incoming tourism is Armenia's second export line item after the mining and metal industry and covers more than half of service exports. Tourism in Armenia has the potential to reduce poverty and improve living standards of the bottom 40 in tourist destination areas. As demonstrated around the world, with careful strategic planning and relatively modest public sector investments, this services sector activity can be nurtured into a critical source of economic and employment growth at a time when agriculture's share of GDP and employment is shrinking and manufacturing/mining cannot sufficiently absorb a large share of the labor force.

Despite economic downturns in key generating markets, especially in Europe, the outlook for Armenian tourism and its contribution to economic growth is cautiously optimistic. International tourist arrivals have been growing steadily in Armenia, well above the world average of 4 percent. During the period of 2010-2014, the number of international travelers visiting Armenia increased by more than 10 percent per annum reaching 1,203,746. The top generating markets, which account for approximately 71 percent of total international arrivals, include CIS (41.5 percent), Iran (18.4 percent) and USA (8.2 percent). Total share of visitors from EU approaches 10 percent. According of the World Tourism Organization (WTO), 34 percent of visitors came through organized tours (2012).

The bottom 40 percent of the income distribution enjoyed strong consumption growth prior to the global crisis. One of the Bank's indicators of shared prosperity, i.e., the growth rate of consumption per capita of the bottom 40 percent, demonstrates that economic growth in Armenia benefited the poor and vulnerable more than the overall population. From 2006-2008, growth in average real consumption per capita of the bottom 40 percent outpaced that of the population as a whole, 6.5 percent versus 5.2 percent. The 2008 crisis eroded the growth in average consumption that had been enjoyed by both the bottom 40 percent and the population as a whole. As a result, between 2006 and 2011, the consumption per capita of the bottom 40 percent grew only at 0.4 percent per year, while that of the population as a whole even stagnated.

The Government's strong counter-cyclical fiscal policy since the 2008 crisis has focused mainly on increased spending on infrastructure, social protection, and emergency financing for enterprises. While the fiscal expansion has helped protect the poor and maintain jobs, the pace of recovery has remained slow and prone to external downside risks with around 1.3 percent real growth expected for 2015.

Sectoral and institutional Context

According to the Armenia Development Strategy, incoming tourism is Armenia's second export line item after the mining and metal industry and covers more than half of service exports. Others include a limited range of food items and beverages. Exports are outweighed by imports of – among others – manufactured goods and food, resulting in a substantial trade deficit of around US\$2 billion annually. Remittances from the Armenian diaspora, amounting to more than US\$1.5 billion, limited foreign direct investment inflows, and donor funding help to close the gap. Tourism in Armenia has the potential to reduce poverty and improve living standards of the bottom 40 percent in tourist destination areas. As demonstrated around the world, with careful strategic planning and relatively modest public sector investments, this services sector activity can be nurtured into a critical source of economic and employment growth at a time when agriculture's share of GDP and employment is shrinking and manufacturing/mining cannot sufficiently absorb a large share of the labor force. Despite economic downturns in key generating markets, especially in Europe, the outlook for Armenian tourism and its contribution to economic growth is cautiously optimistic.

International tourist arrivals have been growing steadily in Armenia, well above the world average. During the period 2010-2011, the number of international travelers increased by more than 10 percent reaching 758,000. In 2012, the numbers reached 843,330; an 11.3 percent increase over 2011 and more than double the global tourism growth rate of 4 percent. In 2013, the number of travelers reached 924,965; an increase of 9.7 percent compared to 2012. This trend accelerated in 2014, with the National Statistics Service (NSS) reporting 1,203,746 travelers; 11.3 percent increase. The top generating markets, which account for approximately 71 percent of total international arrivals, include Commonwealth of Independent States (CIS) (41.5 percent), Iran (18.4 percent), United States of America (USA) (8.2 percent), Argentina (3 percent), France (3 percent), Lebanon (3 percent), Germany (2.7 percent), Greece (1.5 percent), United Kingdom (UK) and Italy (1 percent). According to the 2012 statistics of the World Tourism Organization, 34 percent of visitors came through organized tours. At least 51.2 percent of all visitors are believed to be coming to visit family or friends (VFF). According to the USAID International Visitor's Survey (2013), some 12.2 percent come for business or professional reasons. Tourists coming from the CIS (mostly Russia, Georgia and Ukraine), European Union (EU) (mostly Germany, France and Italy) and Iran, comprised 77.3 percent of total international arrivals in 2013. The visitors' receipts were US\$923 million in 2014.

With an increased number of visitors and spending, the benefits to Armenia's economy are also growing. According to the World Travel and Tourism Council (WTTC), the tourism and travel sector directly contributed 3.6 percent of the country's GDP (AMD163.1 billion in 2014). The total contribution was AMD578.5 billion (12.7 percent of GDP) and is expected to grow by 7.9 percent (AMD 532.6 billion, 11.3 percent of GDP) by the end of 2015. The tourism and travel sector generated 11.3 percent of total employment in 2014; 133,500 jobs (3.1 percent directly and 8.2 percent indirectly) and is expected to maintain employment at about 8.6 percent over the next decade. The industry accounts for nearly 32 percent of export earnings in 2014.

With over 4000 historical monuments throughout the country dating from pre-historic to Hellenistic and early Christian eras – three of which are United Nations Organization for Education, Science and Culture (UNESCO) World Heritage Sites – Armenia is often referred to as an open air museum. Yerevan alone hosts 40 art museums and galleries. Armenia offers multiple eco/nature and authentic cultural heritage experiences to travelers, summer and winter destinations, including

33 national parks and protected areas. In terms of geographical opportunities, the most visited destination and itineraries are the North tourism corridor (Gyumri – Vanadzor – Dilijan – Lake Sevan) and the South tourism corridor (Garni – Geghard -Khor Virap – Areni – Jermuk – Sisian – Goris – Tatev – Meghri). The World Bank assisted the Government of Armenia in 2014 to assess the regional development disparities (the Assessment) and opportunities and prepare a Tourism Strategy for the South Tourism Corridor. The regional analysis helped identify the opportunities for regional development and shared prosperity by analyzing the profile of each region (Marz) in Armenia and identifying key policy and investment needs in the most competitive sectors that drive private sector-led growth and job creation, most notably tourism, agro-tourism and agri-business.

The Assessment employed the framework of the World Development Report 2009 (WDR 2009) to analyze economic disparities of Armenian regions. According to the WDR, geographic transformations for economic development can be characterized in three dimensions – Density, Distance, and Division (the 3Ds). This concept was used to assess relative economic standing of the regions of Armenia, including disparities in productivity and well-being that exist between urban and rural areas, as well as the capital and the rest of the regions. According to the WDR framework the type of public policy intervention depends on the level of urbanization. Thus, given an overall urbanization rate of over 60 percent, Armenia needs to prioritize spatially blind and spatially connective policies. Continued strategic investments in transport infrastructure should be carried out with the aim of improving provision and access to basic services and optimizing connectivity between and throughout regions, which would allow for reducing distance and costs. The South Corridor Tourism Destination Strategy has focused on four regions (the Southern part of Kotayk, Ararat, Vayots Dzor and Syunik), which combine several scenic cultural and natural attractions; traditional farms, mountains including Mount Ararat, carpet production in Yeghegnadzor and Goris, wine tourism in Areni, and cultural heritage and traditional cuisine in Goris. The strategy found that the quality of roads and other municipal infrastructure ranges from poor to good along the Corridors but, overall, road and water improvements and urban regeneration are high priorities. This Corridor provides opportunities for many activities such as visits to natural areas, cultural heritage sights, and visits with carpet producers, traditional meals and community home stays. Many of these activities are offered by small and micro-enterprises. Hence, generating more tourism supports local businesses and spreads prosperity over a broader range of stakeholders.

The key conclusion of the South Corridor Tourism Destination Strategy is that corridor development requires several key interventions, such as tourism infrastructure improvements, especially through site management plans; improved and expanded product offers; and local capacity building and workforce development. It also highlighted Areni, Goris and Meghri as potential hub destinations that should be developed along with selected spoke destinations to realize the vision of the establishment of the Southern Corridor as a new tourism destination, and to achieve economic development objectives all along Corridor. The South Corridor Tourism Development Strategy has identified destination hubs along the Southern Corridor that are attractive to visitors, tour operators and investors. The "hubs" and corresponding 'spoke' destinations would serve as clusters and circuits. While it would be ideal to assist as many destinations as possible in each of the areas mentioned above – product offerings and marketing, infrastructure, private investment, and workforce development– resources are limited and must be allocated to those destinations where improvements could best attract more visitor spending, generate increased incomes and employment, and spur more investment. The Strategy revealed that the average tourism receipts earned per visitor have been steadily declining from 2005 to date, which suggests that the available tourism offers are somewhat static and not improving in quality and variety. It

also suggests that marketing efforts are not being directed to and not succeeding in capturing higher spending visitors. Lower spending from static tourism markets runs the risk of being less competitive and thus less able to sustain increased earnings. An integrated approach to development of tourism corridors and circuits should explicitly aim at diversifying and improving Armenia's tourism products, which could, in turn, increase spending and deliver a more robust tourism-led local economic development.

Focusing on tourism opportunities that enhance shared prosperity along the main Northern and Southern Corridors also supports the Government's ADS, which aims to triple per capita income to US\$10,000 and lift 800,000 people out of poverty by 2025. The Government of Armenia has requested World Bank financing under this Project to contribute to the implementation of an integrated tourism and regional development, especially in the south and the World Heritage Sites in the north. The World Bank's Country Partnership Strategy for 2014-2017 supports this focus by emphasizing the need of sharing prosperity and reducing poverty through accelerated economic growth and job creation.

With the implementation of the proposed integrated approach to tourism development, the following targets are set to be achieved by 2021: international arrivals to grow from 1,203,746 in 2014 to 1,806,498 in 2021; international tourist receipts to increase from US\$749.5 to US\$1,500; international receipts to grow from US\$923 million to US\$ 1,108 billion in 2021; and tourism employment to increase from 133,500 in 2014 to 147,070 in 2021.

Armenia faces major risks from earthquakes, drought, floods, hail, and landslides. The World Bank's recent risk profiling study revealed that 12 percent of the country's GDP would be affected by an earthquake with 25-years return period. Potential government revenue losses could amount to approximately 20 percent of the general total government revenues. In addition, Armenia is prone to flood risks. The same Bank study indicated that a flood with 25-years return period could affect six percent or more of the country's GDP with the government revenue losses and the public damage and losses potentially amounting to approximately 10 percent of the total general government revenues. In this context, disaster risk mitigation and preparedness is increasingly recognized as a priority consideration in the framework of country's development. This explains the rationale for introducing Component 3 under the Project.

II. Proposed Development Objectives

The Project Development Objective is to improve infrastructure services and institutional capacity for increased tourism contribution to local economy in selected regions of Armenia.

III. Project Description

Component Name

Heritage Hub Regeneration and Tourism Circuit Development

Comments (optional)

Sub-component 1.1: Heritage hub regeneration (US\$21.07 million) to finance urban regeneration activities in the old towns of Goris and Meghri, and the heritage villages Areni, Tatev and Tandzatatap.

Sub-component 1.2: Development of the tourism circuits (US\$16.8 million) to finance an integrated approach to cultural heritage preservation and improved site management plans of the most attractive cultural and natural heritage sites located along the main tourism circuit/route in Armenia.

Sub-component 1.3: Public-Private Investment (PPI) (US\$5.00 million) to provide public infrastructure to attract private investments.

Sub-component 1.4: Project management, designs and construction supervision (US\$4.74 million).

Component Name

Institutional Development

Comments (optional)

The component will increase the institutional capacity and performance of the Development Foundation Armenia (DFA), the Historical and Culture Heritage Protection Agency (HCHPA), Project implementing entity and other local and regional entities in order for them to carry out the following activities: setting up of destination management organization and offices in key regions; marketing and promotion; preparation of sustainable site management plans for selected Project's cultural heritage sites; training for skilled workforce development and capacity building; cultural heritage advisory service to improve capacity of protection and management of the World Heritage Sites; business start-up/expansion advisory service to tourism SMEs; and performance monitoring & evaluation activities.

Component Name

Contingent Emergency Response

Comments (optional)

This component is being introduced as a precautionary measure that would allow the GoA and the Bank to quickly channel the loan financing for emergency recovery efforts following an adverse natural or man-made disaster and declaration by the GoA of a State of Disaster and Emergency. The built-in CER with an associated new disbursement category would allow the GoA to request the Bank to reallocate loan proceeds to this sub-component towards an emergency response for the municipal infrastructure sector within the five regions targeted by this Project in the Borrower's territory. The new disbursement category will have a zero dollar allocation, with 100 percent IBRD financing.

IV. Financing (in USD Million)

Total Project Cost:	68.75	Total Bank Financing:	55.00
Financing Gap:	0.00		
For Loans/Credits/Others			Amount
Borrower			13.75
International Bank for Reconstruction and Development			55.00
Total			68.75

V. Implementation

The Armenia Territorial Development Fund (ATDF) will act as the Project implementation entity while the Ministry of Economy will be responsible for overall coordination and policy support of the Project. The ATDF will be supported by a consultative inter-agency Working Group (WG) and a high level Project Steering Committee (PSC). The WG will be composed by the technical representatives from the agencies concerned (Ministry of Economy, Ministry of Territorial Administration and Emergency Situations, Ministry of Culture, Ministry of Natural Protection, Ministry of Urban Development, Armenia Territorial Development Fund, Armenian Apostolic Church, Historical and Cultural Heritage Protection Agency, and local self-government (LSG) units

benefiting from the Project) to guarantee strong inter-agency communication. The DFA will serve as secretariat for the WG. The WG will review sub projects, monitor implementation progress, and address complex issues and concerns on time. The WG will issue technical recommendations to the PSC for high level decision-making matters. The PSC will be chaired by the Deputy Prime Minister and include all key participating institutions. The PSC will provide oversight and coordination of Project implementation and ensure high level inter-agency coordination.

ATDF will be responsible for the fiduciary implementation of the Project. This includes procurement and financial management (FM) functions. The FM function includes planning and budgeting, accounting, financial reporting, external auditing, funds flow, and internal controls. No significant weaknesses were identified at ATDF. It was agreed that prior to the Project implementation ATDF will (a) hire additional FM/accounting staff, acceptable to the Bank, to manage the increased workload; (b) develop the Project's Financial Management Manual (FMM), acceptable to the Bank, to reflect the FM arrangements and controls under the Project, and (c) finalize the upgrade of the accounting system. Those are capacity building actions but not conditions.

The ATDF will be responsible for monitoring and evaluation (M&E) of the Project outcomes against agreed indicators as presented in the Results Framework. In support of the M&E, the Project will contract international consulting firms to (a) assist in collection and analysis of baseline and progress data and monitor tourism and local economic development. The cost of these services, as well as raising the institutional capacity to sustain Project interventions, is built into the Project design under Component 2. The ATDF will produce biannual progress reports to assess implementation and suggest any need for adjustments.

VI. Safeguard Policies (including public consultation)

Safeguard Policies Triggered by the Project	Yes	No
Environmental Assessment OP/BP 4.01	x	
Natural Habitats OP/BP 4.04	x	
Forests OP/BP 4.36		x
Pest Management OP 4.09		x
Physical Cultural Resources OP/BP 4.11	x	
Indigenous Peoples OP/BP 4.10		x
Involuntary Resettlement OP/BP 4.12	x	
Safety of Dams OP/BP 4.37		x
Projects on International Waterways OP/BP 7.50	x	
Projects in Disputed Areas OP/BP 7.60		x

Comments (optional)

VII. Contact point

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Borrower/Client/Recipient

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VIII. For more information contact:

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