

**Document of  
The World Bank**

**Report No: ICR00001059**

**IMPLEMENTATION COMPLETION AND RESULTS REPORT**

**(IDA-39990 TF-54431)**

**(IDA-41440 TF- 54066,TF-56146)**

**(IDA-42660,TF-91270)**

**(IDA-43690,TF-57634)**

**ON A**

**POVERTY REDUCTION SUPPORT CREDITS**

**IN THE AMOUNT OF**

- 1. US\$20.0 MILLION EQUIVALENT**
- 2. US\$20.0 MILLION EQUIVALENT**
- 3. US\$28.0 MILLION EQUIVALENT**
- 4. US\$18.5 MILLION EQUIVALENT**

**TO THE**

**REPUBLIC OF ARMENIA**

**September 21, 2009**

**Poverty Reduction and Economic Management Department  
Europe and Central Asia Region**

## CURRENCY EQUIVALENTS

(Exchange Rate Effective August 24, 2009)

Currency Unit = Drams  
US\$ 1.00 = 375.28 drams

## FISCAL YEAR

January 1 – December 31

## ABBREVIATIONS AND ACRONYMS

ADC	Agriculture Development Centre
AR	Armenian Railways
ASC	Agriculture Support Centre
ASYCUDA	Automated System for Customs Data
BEEPS	Business Environment and Enterprise Performance Survey
CAS	Country Assistance Strategy
CFAA	Country Financial Accountability Assessment
CIS	Commonwealth of Independent States
COC	Chamber of Control
DTI	Direct Trade Input
IDA	International Development Association
IFRP	Integrated Financial Rehabilitation Plan
IPSAS	International Public Sector Accounting Standards
ITU	International Telecommunication Union
JSAN	Joint Staff Advisory Note
LDP	Letter of Development Policy
LTU	Large Taxpayer Unit
MCC	Millennium Challenge Corporation
MDGs	Millennium Development Goals
MTEF	Medium-Term Expenditure Framework
PCA	Post-clearance Audit
PHRD	Japan Policy and Human Resources Development Trust Fund
PRGF	Poverty Reduction and Growth Facility (of the IMF)
PRSC	Public Service Regulatory Commission
PRSP	Poverty Reduction Strategy Paper
PSRC	Public Services Regulatory Commission
ROSC	Reports on the Observance of Standards and Codes
SAC	Structural Adjustment Credit
SCC	State Customs Committee
SDP	Sustainable Development Program
SNCO	State Non-Commercial Organizations
STS	State Tax Services
UNDP	United Nations Development Program
USAID	US Agency for International Development
WRMC	Water Resources Management Committee
WUA	Water Users Association

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Task Team Leader:	Saumya Mitra

**REPUBLIC OF ARMENIA**  
**Poverty Reduction Support Credits I, II, III, and IV**

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<b>A. Basic Information</b>			
<b>Program 1</b>			
Country	Armenia	Program Name	Poverty Reduction Support Credit (PRSC)
Program ID	P078673	L/C/TF Number(s)	IDA-39990,TF-54431
ICR Date	09/29/2009	ICR Type	Core ICR
Lending Instrument	PRC	Borrower	GOVERNMENT OF ARMENIA
Original Total Commitment	XDR 13.7M	Disbursed Amount	XDR 13.7M
<b>Implementing Agencies</b>			
Ministry of Finance and Economy			
<b>Cofinanciers and Other External Partners</b>			
<b>Program 2</b>			
Country	Armenia	Program Name	Second Poverty Reduction Support Credit
Program ID	P093459	L/C/TF Number(s)	IDA-41440,TF-54066,TF-56146
ICR Date	09/29/2009	ICR Type	Core ICR
Lending Instrument	DPL	Borrower	GOVERNMENT OF ARMENIA
Original Total Commitment	XDR 14.1M	Disbursed Amount	XDR 14.1M
<b>Implementing Agencies</b>			
Ministry of Finance and Economy			
<b>Cofinanciers and Other External Partners</b>			
<b>Program 3</b>			
Country	Armenia	Program Name	PRSC3
Program ID	P093460	L/C/TF Number(s)	IDA-42660,TF-91270
ICR Date	09/29/2009	ICR Type	Core ICR
Lending Instrument	DPL	Borrower	REPUBLIC OF ARMENIA
Original Total Commitment	XDR 18.7M	Disbursed Amount	XDR 18.7M

<b>Implementing Agencies</b>			
Ministry of Finance and Economy			
<b>Cofinanciers and Other External Partners</b>			
<b>Program 4</b>			
Country	Armenia	Program Name	Fourth Poverty Reduction Support Credit
Program ID	P101486	L/C/TF Number(s)	IDA-43690,TF-57634
ICR Date	09/29/2009	ICR Type	Core ICR
Lending Instrument	DPL	Borrower	REPUBLIC OF ARMENIA
Original Total Commitment	USD 18.5M	Disbursed Amount	USD 19.7M
<b>Implementing Agencies</b>			
Ministry of Finance and Economy			
<b>Cofinanciers and Other External Partners</b>			

<b>B. Key Dates</b>				
<b>Poverty Reduction Support Credit (PRSC) - P078673</b>				
Process	Date	Process	Original Date	Revised / Actual Date(s)
Concept Review:	06/08/2004	Effectiveness:		12/23/2004
Appraisal:	09/20/2004	Restructuring(s):		
Approval:	11/18/2004	Mid-term Review:		
		Closing:	12/31/2005	12/31/2005

<b>Second Poverty Reduction Support Credit - P093459</b>				
Process	Date	Process	Original Date	Revised / Actual Date(s)
Concept Review:	11/08/2005	Effectiveness:		04/05/2006
Appraisal:	11/09/2005	Restructuring(s):		
Approval:	01/19/2006	Mid-term Review:		
		Closing:	06/30/2007	06/30/2007

<b>PRSC3 - P093460</b>				
Process	Date	Process	Original Date	Revised / Actual Date(s)
Concept Review:	12/12/2006	Effectiveness:		04/25/2007

Appraisal:	01/15/2007	Restructuring(s):		
Approval:	03/08/2007	Mid-term Review:		
		Closing:	06/30/2008	06/30/2008

Fourth Poverty Reduction Support Credit - P101486				
Process	Date	Process	Original Date	Revised / Actual Date(s)
Concept Review:	11/02/2006	Effectiveness:		03/05/2008
Appraisal:	10/10/2007	Restructuring(s):		
Approval:	11/27/2007	Mid-term Review:		
		Closing:	06/30/2008	06/30/2008

## C. Ratings Summary

### C.1 Performance Rating by ICR

#### Poverty Reduction Support Credit (PRSC) - P078673

Outcomes	Satisfactory
Risk to Development Outcome	Moderate
Bank Performance	Satisfactory
Borrower Performance	Satisfactory

#### Second Poverty Reduction Support Credit - P093459

Outcomes	Satisfactory
Risk to Development Outcome	Moderate
Bank Performance	Satisfactory
Borrower Performance	Satisfactory

#### PRSC3 - P093460

Outcomes	Satisfactory
Risk to Development Outcome	Moderate
Bank Performance	Satisfactory
Borrower Performance	Satisfactory

#### Fourth Poverty Reduction Support Credit - P101486

Outcomes	Satisfactory
Risk to Development Outcome	Moderate
Bank Performance	Satisfactory
Borrower Performance	Satisfactory

<b>C.2 Detailed Ratings of Bank and Borrower Performance (by ICR)</b>			
<b>Poverty Reduction Support Credit (PRSC) - P078673</b>			
<b>Bank</b>	<b>Ratings</b>	<b>Borrower</b>	<b>Ratings</b>
Quality at Entry	Satisfactory	Government:	Satisfactory
Quality of Supervision:	Satisfactory	Implementing Agency/Agencies:	Satisfactory
Overall Bank Performance	Satisfactory	Overall Borrower Performance	Satisfactory

<b>Second Poverty Reduction Support Credit - P093459</b>			
<b>Bank</b>	<b>Ratings</b>	<b>Borrower</b>	<b>Ratings</b>
Quality at Entry	Satisfactory	Government:	Satisfactory
Quality of Supervision:	Satisfactory	Implementing Agency/Agencies:	Satisfactory
Overall Bank Performance	Satisfactory	Overall Borrower Performance	Satisfactory

<b>PRSC3 - P093460</b>			
<b>Bank</b>	<b>Ratings</b>	<b>Borrower</b>	<b>Ratings</b>
Quality at Entry	Satisfactory	Government:	Satisfactory
Quality of Supervision:	Satisfactory	Implementing Agency/Agencies:	Satisfactory
Overall Bank Performance	Satisfactory	Overall Borrower Performance	Satisfactory

<b>Fourth Poverty Reduction Support Credit - P101486</b>			
<b>Bank</b>	<b>Ratings</b>	<b>Borrower</b>	<b>Ratings</b>
Quality at Entry	Satisfactory	Government:	Satisfactory
Quality of Supervision:	Satisfactory	Implementing Agency/Agencies:	Satisfactory
Overall Bank Performance	Satisfactory	Overall Borrower Performance	Satisfactory

<b>C.3 Quality at Entry and Implementation Performance Indicators</b>			
<b>Poverty Reduction Support Credit (PRSC) - P078673</b>			
<b>Implementation Performance</b>	<b>Indicators</b>	<b>QAG Assessments (if any)</b>	<b>Rating:</b>
Potential Problem Program at any time (Yes/No):	No	Quality at Entry (QEA)	None
Problem Program at any time (Yes/No):	No	Quality of Supervision (QSA)	None
DO rating before Closing/Inactive status			

<b>Second Poverty Reduction Support Credit - P093459</b>			
<b>Implementation Performance</b>	<b>Indicators</b>	<b>QAG Assessments (if any)</b>	<b>Rating:</b>
Potential Problem Program at any time (Yes/No):	No	Quality at Entry (QEA)	None
Problem Program at any time (Yes/No):	No	Quality of Supervision (QSA)	None
DO rating before Closing/Inactive status	Satisfactory		

<b>PRSC3 - P093460</b>			
<b>Implementation Performance</b>	<b>Indicators</b>	<b>QAG Assessments (if any)</b>	<b>Rating:</b>
Potential Problem Program at any time (Yes/No):	No	Quality at Entry (QEA)	None
Problem Program at any time (Yes/No):	No	Quality of Supervision (QSA)	None
DO rating before Closing/Inactive status			

<b>Fourth Poverty Reduction Support Credit - P101486</b>			
<b>Implementation Performance</b>	<b>Indicators</b>	<b>QAG Assessments (if any)</b>	<b>Rating:</b>
Potential Problem Program at any time (Yes/No):	No	Quality at Entry (QEA)	None
Problem Program at any time (Yes/No):	No	Quality of Supervision (QSA)	None
DO rating before Closing/Inactive status			



<b>D. Sector and Theme Codes</b>		
<b>Poverty Reduction Support Credit (PRSC) - P078673</b>		
	<b>Original</b>	<b>Actual</b>
<b>Sector Code (as % of total Bank financing)</b>		
General agriculture, fishing and forestry sector	20	10
General education sector	10	20
General finance sector	20	30
General public administration sector	40	30
Health	10	10
<b>Theme Code (as % of total Bank financing)</b>		
Environmental policies and institutions	20	25
Public expenditure, financial management and procurement	20	25
Regulation and competition policy	20	15
Rural services and infrastructure	20	15
Tax policy and administration	20	20

<b>Second Poverty Reduction Support Credit - P093459</b>		
	<b>Original</b>	<b>Actual</b>
<b>Sector Code (as % of total Bank financing)</b>		
General agriculture, fishing and forestry sector	25	20
General finance sector	10	15
General industry and trade sector	20	15
General public administration sector	25	25
Other social services	20	25
<b>Theme Code (as % of total Bank financing)</b>		
Other environment and natural resources management	14	15
Public expenditure, financial management and procurement	29	30
Regulation and competition policy	29	25
Rural services and infrastructure	14	15
Trade facilitation and market access	14	15

PRSC3 - P093460		
	Original	Actual
<b>Sector Code (as % of total Bank financing)</b>		
Central government administration	30	30
General agriculture, fishing and forestry sector	25	20
General industry and trade sector	23	25
Health	12	13
Non-compulsory pensions, insurance and contractual savings	10	12
<b>Theme Code (as % of total Bank financing)</b>		
Health system performance	16	15
Regulation and competition policy	33	30
Rural services and infrastructure	17	15
Social risk mitigation	17	20
Tax policy and administration	17	20

Fourth Poverty Reduction Support Credit - P101486		
	Original	Actual
<b>Sector Code (as % of total Bank financing)</b>		
Aviation	14	15
Central government administration	29	30
Forestry	14	15
General industry and trade sector	29	20
Telecommunications	14	20
<b>Theme Code (as % of total Bank financing)</b>		
Corporate governance	14	15
Debt management and fiscal sustainability	14	15
Environmental policies and institutions	14	15
Regulation and competition policy	29	30
Tax policy and administration	29	25

<b>E. Bank Staff</b>		
<b>Poverty Reduction Support Credit (PRSC) - P078673</b>		
<b>Positions</b>	<b>At ICR</b>	<b>At Approval</b>
Vice President:	Philippe H. Le Houerou	Shigeo Katsu
Country Director:	Asad Alam	D-M Dowsett-Coirolo
Sector Manager:	Kazi Mahbub-Al Matin	Carlos Felipe Jaramillo
Task Team Leader:	Saumya Mitra	Saumya Mitra
ICR Team Leader:	Saumya Mitra	
ICR Primary Author:	Daniel Morrow	

<b>Second Poverty Reduction Support Credit - P093459</b>		
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Vice President:	Philippe H. Le Houerou	Shigeo Katsu
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ICR Team Leader:	Saumya Mitra	
ICR Primary Author:	Daniel Morrow	

## F. Results Framework Analysis

### Program Development Objectives (from Program Document)

The proposed series of three annual single tranche Poverty Reduction Support Credit (PRSCs) is intended to support policy and institutional reforms in furtherance of the official Poverty Reduction Strategy Paper (PRSP). The PRSCs focus on four critical reform themes: (i) consolidating macroeconomic discipline and strengthening of governance; (ii) sharpening competition and entrenching property rights; (iii) mitigating social and environmental risks, and (iv) modernizing the rural economy.

### Revised Program Development Objectives (as approved by original approving authority)

#### (a) PDO Indicator(s)

Poverty Reduction Support Credit (PRSC) - P078673				
Indicator	Baseline Value	Original Target Values (from approval documents)	Formally Revised Target Values	Actual Value Achieved at Completion or Target Years
<b>Indicator 1 :</b>	Tax to GDP ratio to increase from 14% in the base year (2003) to 16.4 percent by the end of the program. The actual outcome of this indicator for 2008 was 17 percent.			
Value (quantitative or Qualitative)				
Date achieved				
Comments (incl. % achievement)				
<b>Indicator 2 :</b>	share of taxpayers using self-assessment tax system. The system was non-existent in 2003 but in 2008 almost 30 percent of tax returns were submitted via postal service relying on self-assessment practice.			
Value (quantitative or Qualitative)				
Date achieved				
Comments (incl. % achievement)				

Second Poverty Reduction Support Credit - P093459				
Indicator	Baseline Value	Original Target Values (from approval documents)	Formally Revised Target Values	Actual Value Achieved at Completion or Target Years
<b>Indicator 1 :</b>	Real GDP growth (%)			
Value (quantitative or Qualitative)	13.9	7.5		
Date achieved	12/31/2005	12/31/2007		
Comments (incl. % achievement)				
<b>Indicator 2 :</b>	Inflation (%)			
Value (quantitative or Qualitative)	0.6	3.0		
Date achieved	12/31/2005	12/31/2007		
Comments (incl. % achievement)				
<b>Indicator 3 :</b>	Fiscal deficit (% of GDP)			
Value (quantitative or Qualitative)	2.6	2.9		
Date achieved	12/31/2005	12/31/2007		
Comments (incl. % achievement)				
<b>Indicator 4 :</b>	Tax revenues (% of GDP)			
Value (quantitative or Qualitative)	14%	16%		
Date achieved	12/31/2003	12/31/2007		
Comments (incl. % achievement)				
<b>Indicator 5 :</b>	Private sector deposits (% of GDP)			
Value (quantitative or Qualitative)	9.8%	11%		
Date achieved	12/31/2004	12/31/2007		
Comments (incl. % achievement)				

<b>Indicator 6 :</b>	Share of poor households receiving family poverty benefits			
Value (quantitative or Qualitative)	40%	70%		
Date achieved	12/31/2005	06/30/2008		
Comments (incl. % achievement)				
<b>Indicator 7 :</b>	Weighted average water supply duration (hours per day)			
Value (quantitative or Qualitative)	18 hours for Yerevan Water Supply Company 5.07 hours for Armenia Water Supply Company	18.5 hours for Yerevan Water Supply Company 5.6 hours for Armenia Water Supply Company		
Date achieved	12/31/2005	12/31/2007		
Comments (incl. % achievement)				
<b>Indicator 8 :</b>	Commercial bank loans to private sector (%GDP)			
Value (quantitative or Qualitative)	8.0%	10.0%		
Date achieved	12/31/2005	12/31/2007		
Comments (incl. % achievement)				
<b>Indicator 9 :</b>	Share of farmer-respondents reporting access to advisory services			
Value (quantitative or Qualitative)	32%	50%		
Date achieved	12/31/2005	06/30/2008		
Comments (incl. % achievement)				
<b>Indicator 10 :</b>	Insurance premiums US\$m			
Value (quantitative or Qualitative)	US\$4.5m	US\$15m		
Date achieved	12/31/2003	12/31/2007		
Comments (incl. % achievement)				

<b>Indicator 11 :</b>	Utilization rate of hospital and PHC services by bottom two quintiles			
Value (quantitative or Qualitative)	22%	33%		
Date achieved	12/31/2003	12/31/2007		
Comments (incl. % achievement)				

PRSC3 - P093460				
Indicator	Baseline Value	Original Target Values (from approval documents)	Formally Revised Target Values	Actual Value Achieved at Completion or Target Years
<b>Indicator 1 :</b>	Staff performance appraisal system in implementation			
Value (quantitative or Qualitative)	None of the ministries used performance appraisal systems	have successful pilots		By end-2007 the system was successfully piloted in the MoE, MoF and Central Government apparatus
Date achieved	04/01/2003	12/31/2007		12/31/2007
Comments (incl. % achievement)				
<b>Indicator 2 :</b>	Share of ministries using GFS 2001 budget classifications			
Value (quantitative or Qualitative)				
Date achieved				
Comments (incl. % achievement)				
<b>Indicator 3 :</b>	Electricity service monitoring system functional and data published			
Value (quantitative or Qualitative)				
Date achieved				
Comments (incl. % achievement)				

Fourth Poverty Reduction Support Credit - P101486				
Indicator	Baseline Value	Original Target Values (from approval documents)	Formally Revised Target Values	Actual Value Achieved at Completion or Target Years
<b>Indicator 1 :</b>	Illegal logging monitored and controlled			
Value (quantitative or Qualitative)	the forest monitoring system was completely non-existent	To have a fully functional monitoring system in place		monitoring system introduced
Date achieved	01/01/2003	12/31/2007		12/31/2007
Comments (incl. % achievement)				
<b>Indicator 2 :</b>	the share of discretionary customs inspections decreased			
Value (quantitative or Qualitative)				
Date achieved				
Comments (incl. % achievement)				

**(b) Intermediate Outcome Indicator(s)**

Poverty Reduction Support Credit (PRSC) - P078673				
Indicator	Baseline Value	Original Target Values (from approval documents)	Formally Revised Target Values	Actual Value Achieved at Completion or Target Years
<b>Indicator 1 :</b>	student to full-time teacher ratio was expected to increase from 9:1 ratio in the base (2003) year to 16:1 by the end of program with 14:1 intermediate ratio during the project implementation period			
Value (quantitative or Qualitative)				
Date achieved				
Comments (incl. % achievement)				



Second Poverty Reduction Support Credit - P093459				
Indicator	Baseline Value	Original Target Values (from approval documents)	Formally Revised Target Values	Actual Value Achieved at Completion or Target Years
<b>Indicator 1 :</b>	Single source open procurements as share of number of procurements (outside natural monopoly sectors)			
Value (quantitative or Qualitative)	Awaiting baseline information	20%		
Date achieved	12/31/2005	12/31/2006		
Comments (incl. % achievement)				
<b>Indicator 2 :</b>	% of SNCOs in compliance with financial reporting rules			
Value (quantitative or Qualitative)	0	80		
Date achieved	12/31/2005	12/31/2007		
Comments (incl. % achievement)				
<b>Indicator 3 :</b>	Spending on education (% of GDP)			
Value (quantitative or Qualitative)	2.7	3.15		
Date achieved	12/31/2005	06/30/2007		
Comments (incl. % achievement)				
<b>Indicator 4 :</b>	Irrigation cost recovery rate			
Value (quantitative or Qualitative)	30%	56%		
Date achieved	12/31/2004	06/30/2007		
Comments (incl. % achievement)				

PRSC3 - P093460				
Indicator	Baseline Value	Original Target Values (from approval documents)	Formally Revised Target Values	Actual Value Achieved at Completion or Target Years
<b>Indicator 1 :</b>	Share of single source open procurement (outside natural monopolies)			
Value (quantitative or Qualitative)	80 percent	20 percent		20
Date achieved	01/01/2004	12/31/2007		01/01/2008
Comments (incl. % achievement)				

<b>Indicator 2 :</b>	Weighted average water supply duration for Yerevan			
Value (quantitative or Qualitative)				
Date achieved				
Comments (incl. % achievement)				

Second Poverty Reduction Support Credit - P093459				
Indicator	Baseline Value	Original Target Values (from approval documents)	Formally Revised Target Values	Actual Value Achieved at Completion or Target Years
<b>Indicator 1 :</b>	Leakage from family poverty benefit program			
Value (quantitative or Qualitative)	27 percent	25		29.4
Date achieved	03/31/2003	12/31/2007		12/31/2007
Comments (incl. % achievement)	Administrative capacities of the Ministry of Social and labor issues was weak			

## G. Ratings of Program Performance in ISRs

Poverty Reduction Support Credit (PRSC) - P078673				
No.	Date ISR Archived	DO	IP	Actual Disbursements (USD millions)
1	12/21/2004	Satisfactory	Satisfactory	0.00

Fourth Poverty Reduction Support Credit - P101486				
No.	Date ISR Archived	DO	IP	Actual Disbursements (USD millions)
1	10/06/2006	Satisfactory	Satisfactory	20.32

## H. Restructuring (if any)

# 1. Program Context, Development Objectives and Design

## 1.1 Context at Appraisal

*Political background.* Armenia's birth from the dissolution of the Soviet Union in 1991 took place at a time of severe economic difficulty exacerbated by natural disasters and energy shortages as well as by an armed conflict with neighboring Azerbaijan over the territory of Nagorno-Karabakh. Over the past decade, Armenia has maintained political stability. Presidential and national assembly elections took place about a year before credit appraisal in early 2003 with the emergence of a coalition government. However, opposition parties boycotted parliament following the 2003 elections, alleging electoral fraud. Since 2002, Armenia's rating on political rights by Freedom House has declined somewhat. Surveys indicated that corruption remained and remains a serious problem.

*Economic background.* Following a period of hyperinflation, fiscal crisis and severe economic contraction after independence in 1991-93, the Armenian authorities carried out a successful stabilization and structural reform program. Trade and prices were liberalized, the legal framework for a market economy was established, most small- and medium-sized enterprises were privatized, and the government intervention in the economy was considerably reduced. Economic growth averaged 5.5% per year during 1994-2000, one of the highest among the CIS countries. Growth accelerated to an annual average of 12% in the 2001-03 period, driven by export expansion and significant contributions from the construction, industry and service sectors. While the diaspora and official donors financed much of the construction through grants, investment in tradable goods contributed increasingly to growth during this period. Fiscal deficits fell in the early years of the decade, and inflation was confined to 2-3% in 2001-02 but flared to 8.6% in 2003. Aided by rapid growth, strong inflow of remittances, and an expanding social assistance program, the rate of poverty had begun to fall sharply, but the overall level of poverty remained high and there was particular concern at the concentration of poverty in urban centers outside the capital.

*Other developments prior to appraisal of the first PRSC.* In late 2003, the Armenian authorities published an ambitious Poverty Reduction Strategy Paper (PRSP), laying out a comprehensive program stretched over a decade for sustaining high rates of growth and directing public resources sharply towards fighting poverty. From the range of interventions proposed in the PRSP, the Bank's Country Assistance Strategy (CAS), endorsed by the Bank's Board of Executive Directors in June 2004, focused on three areas that best fit the Group's comparative advantage and complement the activities of other donors: (i) promotion of private sector led growth, through increased efficiency in public services and strengthened competition; (ii) re-orientation of growth to fighting poverty, through accelerated job creation in the private economy, modernization of the rural economy, and effective social protection systems; and (iii) reduction of non-income poverty, through education, health and infrastructure reforms. The PRSC series followed a set of five Structural Adjustment Credits that had supported the initiation of deep market-oriented reforms in the country over the 1996-2003 period and which had been strikingly successful in its broad objectives.

## 1.2 Original Program Development Objectives (PDO) and Key Indicators

**Program Development Objectives.** Within the framework of the country's PRSP and the Bank's CAS, the Program Document of PRSC I outlined the overall development objectives for the proposed series of PRSCs in terms of four themes as follows:

1. *Consolidating macroeconomic discipline and strengthening governance.* The first theme of consolidating macroeconomic discipline and strengthening governance recognizes that a

continuation of Armenia's exemplary macroeconomic performance over the past five years is necessary to underpin high rates of growth. Moreover, governance reforms that cut across budget, fiduciary, revenue raising (customs and tax), and public administration institutions and sectors will improve the climate for private sector investment, remove important opportunities for corruption, and enhance revenue mobilization.

2. *Sharpening competition and entrenching property rights.* The second theme of sharpening competition and entrenching property rights - -cutting across trade, utilities regulation, property and contract law, banking and capital markets, and rural sectors -- addresses the key weaknesses in the competition environment. Armenia needs to reduce costs and sharpen its competitive edge by complementing its highly liberal regime in trade in goods with liberalization in key services and by consolidating its impressive reforms in state owned utilities. In addition, entrenching property rights through provision of a legal framework for secured transactions, by instilling confidence in the banking sector, and by developing insurance markets is essential to secure growing rates of private investment.

3. *Mitigating social and environmental risks.* Social and environmental risks - the third theme - that cuts across education, health, social risk management and environmental protection sectors - are designed to be mitigated by a program of reforms directed at raising both the share of public spending devoted to these sectors and the quality of spending through changes in their composition and institutional reforms, notably in the private provision of health and pension services. The resulting strengthening of human capital and reduced risks for sustainable livelihoods in natural resource use will greatly assist in the reduction of poverty.

4. *Modernizing the rural economy.* Interventions in the rural economy -- the final theme - that cut across the agriculture, non-farm incomes, and infrastructure sectors - are intended to modernize a lagging sector of the economy and one in which the impact of growth on poverty needs to be further strengthened. Greater predictability and sustainability in public services in rural Armenia is expected to strongly benefit the fight against poverty.

**Specific Measures and Key Indicators.** The specific measures associated with each of these themes are described in sections 2.1 and 3.2 below. The expected outcomes associated with these program development objectives are presented in Annex 1.

### **1.3 Revised Program Development Objectives and Key Indicators**

The original Program Development Objectives within these four themes were maintained throughout the first three PRSCs of the series with only marginal changes in program elements. Specifically, under the theme of Consolidating macroeconomic discipline and strengthening governance, (i) measures to improve external auditing were dropped after PRSC I because the government decided to give priority to internal auditing; (ii) measures to introduce a system of staff performance appraisal for the civil service were added in PRSC III; and (iii) measures to strengthen corporate governance by requiring public disclosure of beneficial owners of traded companies were added to PRSC III. The latter two measures were introduced following Bank-supported analytical work and the government's interest in implementing some of the associated recommendations. Key indicators associated with these new PDOs are presented in Annex 1. In the PRSC IV, the scope of the Policy Matrix was somewhat reduced, and the themes were refocused to Strengthening Public and Corporate Governance, Strengthening Competition, and Mitigating Environmental Risks.

## **1.4 Original Design and Revisions**

The PRSC series was initially designed in mid-2004 as a series of three single tranche credits of US\$20 million equivalent each that would support the government's reform program and provide predictable budget support on an annual cycle. Based on the 2004 CAS, the financing provided through the PRSCs amounted to about 33% of the total lending program to Armenia during this period. This design was implemented as planned except that, following approval by Bank Management and Board: (a) the credit amount for PRSC III was increased to US\$28 million equivalent in order to provide financial resources for the government to procure equipment needed for the reform of its customs and tax administration; (b) approval of PRSC III was somewhat delayed from late 2006 to early 2007 so that the government had additional time to complete agreed measures; (c) beginning with PRSC III, the final maturity of the IDA credit was reduced from 40 years to 20 years in light of Armenia's increasing per capita income and improving external position; and (d) prior to approval of PRSC III, given Armenia's continued strong reform performance, which qualified it for the CAS "high case," it was agreed that the series would be extended to include a PRSC IV, for which the credit amount was set at US\$18.5 million within the overall IDA allocation to Armenia.

## **2. Key Factors Affecting Implementation and Outcomes**

### **2.1 Program Performance**

Over the PRSC period, macroeconomic stability was maintained with fiscal deficits being small in relation to GDP, a flexible exchange rate policy led to substantial nominal and real appreciation of the dram, monetary policy was geared to securing low inflation, and highly cautious external borrowing policy led to a sharp fall in the debt to GDP ratio. Growth averaged double digit rates annually and poverty plunged.

Impressive progress was achieved across the structural reform agenda. Improvements in customs and tax administration helped to raise the tax to GDP ratio – a critical objective in light of the need to enhance revenue mobilization. Public management reforms centered on budget decentralization, progress towards program budgeting, and the implementation of devolved authority to schools, hospitals and other public entities. Business conditions were improved through legal improvements in secured transactions and in corporate governance. Regulatory reforms led to improvements in the quality of utility services, notably telecommunications and some liberalization in civil aviation was achieved. The social sectors saw a re-dimensioning of the teaching force and of hospitals to better reflect needs and improvements in social protection. The rural economy benefitted from strengthened extension services and environmental protection.

The PRSC framework helped discipline the budget to the MTEF and PRSP priorities. It also fostered closer cooperation between the ministry of finance and the line ministries in allocating resources as well as reaching decisions on reform priorities.

The following table lists the Prior Actions, as specified in the associated financing or credit agreements that were taken by the government as the basis for the approval of each of the four credits in the series. Given the nature of programmatic operations, these actions were by definition fulfilled by the time of Board approval.

**Table 1: PRSC Core Reforms**

	PRSC I	PRSC II	PRSC III	PRSC IV
<b>1. Consolidating macroeconomic discipline and strengthening governance</b>	Maintained a satisfactory macroeconomic framework.			
	<ul style="list-style-type: none"> <li>Submitted satisfactory quantitative schedule for reduction in outstanding VAT refund claims to exporters and for reduction in tax arrears.</li> <li>Initiated the use of a self-declaration system at all Customs houses and extended access to DTI [Direct Trade Input] facilities at all of its customs houses to importers and customs brokers.</li> </ul>	<ul style="list-style-type: none"> <li>Strengthened the operations of the Large Tax Payers Unit at the State Tax Service, especially audit, collection and enforcement.</li> <li>Implemented a pilot for full access to DTI Facilities.</li> <li>Developed a strategy to apply sanctions for non-compliance with financial reporting for SNCOs.</li> </ul>	<ul style="list-style-type: none"> <li>State Tax Service has made satisfactory progress in implementing its self-assessment system, and has adhered to a satisfactory reform program for its Large Taxpayers Unit.</li> <li>Completed the implementation of the DTI facilities in two major customs houses acceptable to the Association.</li> </ul>	<ul style="list-style-type: none"> <li>The State Tax Service has implemented self-assessment and has adhered to a satisfactory reform plan for its Large Taxpayer Unit.</li> <li>Made satisfactory progress in implementing its comprehensive post-release review program to support the implementation of direct trader input in customs; and developed a satisfactory guarantee mechanism scheme for approved importers.</li> </ul>
<b>Sharpening competition and entrenching property rights</b>	<ul style="list-style-type: none"> <li>Adopted a resolution: (a) widening participation in the provision of international civil aviation services, without prejudice to the existing obligations of the government; and (b) enabling managerial and operational autonomy in the Armenian Railway CJSC to constitute an independent board and reform its tariff-setting procedure.</li> <li>Established plan aimed at strengthen creditor rights and encompassing (a) improvement of civil procedures for debt recovery, and (b) simplification of procedures for certification</li> </ul>	<ul style="list-style-type: none"> <li>Adopted a policy statement incorporating a more liberal and flexible stance to civil aviation and indicating a simplification of procedures.</li> <li>Initiated railway company reforms.</li> <li>Strengthened its utilities regulatory framework through the following actions: (a) adoption of rules for services provision and procedures for monitoring quality in energy and drinking water; (b) publication of performance-monitoring data for energy and water sectors; (c) publication of results of financial performance of irrigation companies; and (d) adoption of power market rules for trade,</li> </ul>	<ul style="list-style-type: none"> <li>Satisfactory progress in implementing its civil aviation regime with the publication of a declaration of developments and intentions in the field of air services.</li> <li>The Public Service Regulatory Commission has developed a telecommunications regulatory policy and a related time-bound action plan in line with international best practice.</li> <li>Strengthened the secured transactions framework through the implementation of the amendments to the Civil Code and related procedures and regulations on secured</li> </ul>	<ul style="list-style-type: none"> <li>Decree has been issued for the revision of the Law on Registration of Legal Entities in order to provide public access to key company records, including internet access to business registry.</li> <li>Submitted to Parliament a revision of the Recipient's Securities Law, which includes a requirement of public disclosure of owners of publicly traded companies.</li> <li>Made satisfactory progress in the reform of its civil aviation regime to open reciprocal access to major partners in aviation services, in line with</li> </ul>

	PRSC I	PRSC II	PRSC III	PRSC IV
	for property sales and registration of secured credit.	<p>dispatching, and safety of the grid.</p> <ul style="list-style-type: none"> <li>Amended its Civil Code and related procedures and regulations on secured credit, and has streamlined civil court procedures and court decision enforcement.</li> </ul>	credit.	<p>its Policy Statement.</p> <ul style="list-style-type: none"> <li>Issued an order to adapt the Armenian table of frequency allocations to conform to the ITU Table of Frequency Allocations.</li> </ul>
<b>Mitigating social and environmental risks</b>	<ul style="list-style-type: none"> <li>Improved targeting of beneficiaries within the family poverty benefit system.</li> </ul>	<ul style="list-style-type: none"> <li>Prepared a draft law on private pension insurance, and has developed an action plan on supervisory and regulatory capacity for private pension services.</li> <li>Continued to implement its school rationalization program, and has raised teacher salaries by sixteen percent (16%).</li> <li>Made progress in implementing its hospital rationalization program.</li> </ul>	<ul style="list-style-type: none"> <li>Satisfactory progress in determining the overall structure of the reformed pension system.</li> <li>Satisfactory progress in implementing its hospital rationalization program.</li> </ul>	
<b>Modernizing the rural economy</b>	<ul style="list-style-type: none"> <li>Established a task force to develop plan aimed at (a) strengthening the applied research and agriculture extension delivery system, (b) improving the links and information transfers between research and extension services, c) increasing the domestic financing of the public extension system; and (d) augmenting the role of private advisory services through, among others: (i) increased utilization of fee-for-services; and (ii) promotion of the involvement of private agri-food marketing and agricultural input companies.</li> </ul>	<ul style="list-style-type: none"> <li>Submitted the Forest Code to its Parliament, and has made significant progress in developing a restructuring plan for the sector.</li> <li>Adopted a framework for agricultural extension, research and education.</li> <li>Established an inter-ministerial working group and has started to implement a time-bound action plan of reforms in rural roads, water, energy and telecommunications sectors to encompass universal access to services and to pave the way for private-public partnership.</li> </ul>	<ul style="list-style-type: none"> <li>Satisfactory progress in implementing its plan to strengthen agricultural extension, research and education.</li> <li>Implemented its rural infrastructure action plan encompassing: (a) classification of communities according to clearly defined criteria; (b) definition of the universal access concept and development of an adequate financing mechanism; (c) delineation of ownership and operational responsibilities; and (d) introduction of simplified standards and new technologies.</li> </ul>	<ul style="list-style-type: none"> <li>Implemented an acceptable illegal logging monitoring system, with autonomy built into the operations of its monitoring institution.</li> </ul>

These Prior Actions were consistent with the Triggers that had been specified in the preceding operation. However, in some areas, the time period for implementing desired reforms was extended. As detailed in section 3.2 below, these areas were: reforms in tax and customs administration, liberalization of air services, development of a multi-pillar pension system, development of a private health insurance system, and monitoring and control over illegal logging. In these areas, it was a common pattern that the Prior Actions were less specific than the corresponding Triggers. For example, PRSC II included a Trigger for PRSC III indicating that the government would “implement a more liberal civil aviation regime in line with policy statement and market potential;” but the formal Prior Action for PRSC III involved only publication by the government of a declaration of developments and intentions. Similarly, the PRSC II Policy Matrix envisioned that, as a Trigger for PRSC III, the government would “adopt the law on private pension insurance,” but the formal Prior Action for PRSC III was “satisfactory progress in determining the overall structure of the reformed pension system.”

In two cases, there was no Prior Action corresponding to a Trigger in the preceding PRSC, indicating that no significant action had been taken in that domain. Specifically:

- A PRSC II Trigger related to customs administration required the government to “complete and implement intelligence-based system based on risk assessment in line with program agreed with IDA.” For PRSC III, this measure was changed to a milestone and not listed as a Prior Action. This action took place in the context of a re-programming of the reforms.
- The Trigger in PRSC II with respect to illegal logging was “Control illegal logging and forest removals within targets to be agreed by IDA by March 2006.” However, the formal Prior Actions for PRSC III did not include any measures related to illegal logging. Instead, the Policy Matrix in PRSC III included a milestone “Developed plan for implementation of the illegal monitoring system.” The complete fulfillment of this reform action was delayed to PRSC IV given the complexity of the institutional arrangements necessary, and it was achieved a year later than originally intended.

The Policy Matrices for PRSC I, II, and III included a large number of “milestones” that were fully consistent with the overall program development objectives. (For PRSC IV, the Policy Matrix included only measures related to the Triggers specified at the time of PRSC III.) In some cases, these milestones involved details that were directly associated with the reform measures that were Triggers and subsequent Prior Actions, but other milestones expanded the scope of measures into areas that were not covered by Triggers/Prior Actions. In particular, milestones were established related to the management of irrigation and drainage, the budget management system, internal auditing, procurement, bank regulations, insurance markets, early childhood education, higher education, prevention of non-communicable diseases, private health insurance, seed certification, and food safety and phytosanitary standards. Achievements with respect to these milestones are discussed in section 3.2.

## 2.2 Major Factors Affecting Implementation

The implementation of the program of policy and institutional reforms supported by this PRSC series benefited from these factors:

- Since the late-1990s, the Armenian government has had a strikingly constructive and successful *relationship with the World Bank*. Even before the PRSC series, the country’s economic reform programs had received substantial support from the Bank and had been successful at triggering rapid economic growth and significant poverty reduction. Hence, the Bank now enjoys substantial credibility in Armenia, and the Bank’s overt



endorsement of any particular reform, *ceteris paribus*, is likely to be politically helpful to domestic champions of that reform. Furthermore, the Bank had provided a series of five Structural Adjustment Credits (SACs) (spanning 1996-2003) prior to the PRSCs, and the government was familiar and comfortable with this modality of engagement with the Bank. In addition, several components of the PRSC program were continuations of reform efforts that had started under SAC IV and V.

- The *Armenian government has been seriously reformist* in orientation. Throughout the PRSC period, Armenia stood at the top of CPIA ratings for IDA countries. The government took the PRSP process and product seriously and invested considerable effort in the associated analysis, policy formulation and public consultation. The PRSP in 2003 set broad priorities for the reform agenda, which were captured in a medium-term program for public expenditures, and then translated by the government into a Medium-Term Expenditure Framework (MTEF). The MTEF was a critical determinant of over subsequent annual budget decisions. In short, country ownership of the PRSP was high, and, to the extent that the PRSC program was grounded in the PRSP, it also enjoyed substantial country ownership.
- The authorities took the *objectives and the specific reform programs of the PRSP* as constituting the government's overall reform program in a disciplined way; thus, only economic and social priorities that had been specified in the PRSP were allowed to be financed by the budget. The medium term expenditure framework was derived exclusively from the PRSP and the annual budgets were, in turn, based on the MTEF. In this way, the government exercised firm control over the reform and budget processes; and the ministry of finance imposed discipline on the line ministries. This observation does not apply to those expenditures not covered by the PRSP, chiefly security related expenditures.
- In part because of their experience with SACs and because of their PRSP and associated planning processes, senior government officials had become more confident in their relationship with the Bank and in their use of development policy operations. In particular, senior officials perceived the *PRSCs as useful vehicles for making commitments within the government* and setting deadlines. For example, line ministers sought to include their reform agendas within the PRSCs in order to ensure that these agendas would receive adequate support from the prime minister and the finance minister. In turn, the ministry of finance regarded the PRSCs as means to exercise discipline on line ministries to undertake reforms and live within spending allocations.
- Throughout PRSC implementation, there was a single government in place; moreover, there was *stability among ministers* and senior government officials involved with the PRSCs. At the beginning of the series, the government created a committee to oversee the process, headed by the Deputy Minister of Finance, who had been deeply involved in the PRSP process. That committee remained in place throughout the PRSC series. In addition, the senior economic adviser to the president, who was also the Governor of Armenia for the Bank, throughout this period was a former Bank staff, and his involvement contributed substantially to achieving understandings between the Bank and the government. This continuity contributed in large measure to both the seriousness of purpose within the government and to the high quality of dialogue between the government and the Bank related to the PRSCs.
- During the PRSCs, there was also substantial *continuity among the Bank staff* involved. The Task Manager for the PRSCs (also the lead economist for Armenia) and the Country Director remained unchanged throughout the PRSC series; the Country Manager in

Armenia at the beginning of the series continued in that role through PRSC III; and there was substantial continuity among the key sector staff both in Washington and in the Armenian office. The PRSC team was concurrently responsible for analytical and policy advisory work and produced three major policy-oriented reports: *The Caucasian Tiger: Sustaining Economic Growth in Armenia*, annual *Poverty Assessments* and annual *Programmatic Public Expenditure Reviews*. These factors contributed significantly both to the quality of the analytical work underpinning the PRSCs and to the richness of the dialogue with the government.

- Armenia enjoyed rapid ***economic growth*** during the period of the PRSCs, building upon its earlier reforms and benefiting substantially from accelerating inflows of private capital from the Armenian diaspora, including Armenian workers in Russia during that country's oil boom in the middle of this decade. This rapid economic growth generated increasing fiscal resources and made it relatively easy for the government to carry through with many of the policy directions set forth in the PRSP.
- In parallel with the PRSCs, the Bank had a wide-ranging program of ***investment operations and AAA*** in Armenia that complemented strongly the areas covered by the PRSC policy matrices. Furthermore, the Bank had access to large trust fund resources, especially from PHRD, that could be used to finance consultants to do technical assistance and analytical work associated with the PRSC-supported reforms.

Taken together, these factors created unusually favorable circumstances for the design and implementation of the PRSC-supported program. There were, nevertheless, some factors that worked against the PRSC program. In particular, there has been increasing concern that ***a small set of business groups*** have expanded their influence within the government, including in the parliament, and that they have been able to use this influence to maintain favorable, discretionary treatment in many domains of public policy. Furthermore, there is still a widespread realization within Armenia that ***corruption*** within the government, and even at the lowest level of public service delivery, is not being reduced. The failure to resolve the dispute with Azerbaijan over Nagorno-Karabakh resulted in large budget outlays for defense as well as the continuation of the closure of borders with Azerbaijan and Turkey. Thus, economic growth was being constrained and fiscal resources diverted from high return activities, which dampened the impact of reforms. The possible impacts of these negative factors on implementation of some elements of the program are discussed in section 3.2.

### **2.3 Monitoring and Evaluation (M&E) Design, Implementation and Utilization**

Building on the very extensive set of monitoring indicators in the 2003 Armenian PRSP, the PRSC documents included a broad set of outcome indicators. The set of monitoring indicators initially set forth in Annex III of PRSC I (and included as Annex 1 in this document) was maintained with some changes throughout the series.

The choice of indicators was, for the most part, reasonable. In a few cases the causal linkages between policy measures to be taken and the indicators chosen to monitor their impacts was conceptually weak. For example, the overall indicator of progress on "sharpening competition" was the share of the private sector in GDP. In a few cases, the quantitative targets associated with indicators lacked clarity. For example, the target for the share of rural households with gas was defined in terms of a percentage increase from the base year but the value for that base year is not provided. In some cases, such as education spending, indicators were defined as a share of GDP, and the associated targets became questionable or inadequate because GDP growth was so much faster than projected. Finally, there were a few instances in which there was inconsistency between indicators and targets cited in the policy matrices and those included in the annex tables

on monitoring indicators. For example, with respect to the hospital rationalization program, the matrix refers to targets for beds and physicians, but these indicators are not included in the table of monitoring indicators.

For the most part, data on the selected indicators could be gathered by relevant agencies. The National Statistical Service, which had become an increasingly engaged partner of the Bank and whose capacity had been much strengthened by joint work on poverty and social monitoring and analysis, conducted an annual household survey (the Integrated Living Conditions Survey) that provided much of the information about poverty and utilization of social services. However, data on outcome indicators tend to be less willingly supplied from the two agencies that were reluctant reformers: the civil aviation department and customs and tax administration. Data was supplied but with delays.

A key instrument for monitoring progress with respect to the PRSP was the annual report on the PRSP produced by the government; and as the PRSC program content was derived as a selective sub-set of the PRSP, these reports provided monitoring of the PRSC itself. The Bank provided Trust Fund resources to help the government improve its M&E capacities and program within this context. Capacity to undertake this task has grown steadily, in part as a result of the dialogue with the Bank. The government's move toward program budgeting will likely encourage it to further improve M&E.

## **2.4 Expected Next Phase/Follow-up Operation**

Subsequent to the government's completion of its second PRSP, entitled its Sustainable Development Program (SDP), in autumn 2008, the government and the Bank began to work on a new series of development policy operations. The onset of the international economic crisis lent urgency to this joint work, but also shifted its orientation towards reassertion of growth and fighting the social effects of the crisis. The government began a process of revision of its SDP to take account of the new international economic realities, whilst reaffirming the medium term structural reformist thrust of its approach. The new development policy operation series was built upon providing urgent budget support to finance counter-cyclical fiscal spending, support output and employment and tilt expenditures towards social protection; at the same time, the program sought to consolidate the reform gains of the PRSC series (such as in advancing reforms in customs and tax administrations or in social protection or telecommunications regulation) and to initiate reforms in new areas (such as in the fiscal regime for mining operations). The first of such operations was approved by the Bank's Board of Executive Directors in July 2009.

## **3. Assessment of Outcomes**

### **3.1 Relevance of Objectives, Design and Implementation**

Even in retrospect, the overall reform program supported by *the PRSCs was highly relevant to the development challenges* facing Armenia during this period. Having substantially completed the first generation reforms for a transition economy during the 1990s, the PRSCs appropriately focused on further improvements in public sector management, in the environment for private sector development, in the social sectors and social safety nets, and in the rural economy. The elements of the PRSC program were consistent with the 2003 PRSP, enjoyed country ownership, and were largely oriented toward poverty reduction.

Furthermore, *the broad agenda of the PRSCs was consistent with and supportive of the Bank's wide-ranging Country Assistance Strategy*. It took advantage of synergies across the Bank's program. The complementarity of the PRSCs and investment operations was notable: in many areas such as education, health, irrigation, utilities, the PRSCs provided support for policy

changes and institution building, whilst the investment operations in these areas provided financing for infrastructure and technical assistance. The design of the series of four annual single-tranche operations was well suited to the political circumstances because they spanned the tenure of a single administration. Finally, given that the Bank had opportunities for financing well-designed investment operations in a number of sectors, the amounts of IDA resources committed to the PRSCs seems appropriate: sufficiently large to attract the serious attention of the government but not so large as to crowd out other good uses of Armenia's IDA allocation.

However, there were several elements of the PRSCs that were driven by the Bank's diagnostics of the binding constraints to growth in Armenia and enjoyed *ambiguous support within the government*. First, reform of tax and customs administration. This was recognized by the government to be important for attaining the priority medium term goal of raising the tax to GDP ratio and for fighting corruption, thereby improving the conditions for business investment, domestic and foreign. However, there were clearly powerful vested interests within the oligarchs as well as within the revenue agencies that resisted reforms and the government's preferred approach tended to be gradualistic and weak. Bank staff spent large efforts in fortifying the content and pace of reforms in this area and the reform program adopted by the government eventually was reasonable, but implementation continued to face opposition.

Second, the liberalization of air services. Bank analysis (detailed in the *Caucasian Tiger*) showed convincingly the large costs imposed on a landlocked economy such as Armenia's and one that faced closed borders with its two important neighbors of restricting competition in international civil aviation. Reforms in civil aviation were not a part of the PRSP but Bank staff insisted that a beginning be made with the PRSC series. Again the dominance of vested interests in maintaining a monopoly in air services influenced the government.

Finally, in two other areas, institutional complexities and the need to coordinate closely across a range of ministries and agencies – with mechanisms and the political will for coordination being weak – meant that reforms had to be re-programmed to take place with one additional year: controlling illegal logging and introducing food safety and phyto-sanitary standards. There were areas where coordination across a number of ministries and agencies was required. In each of these areas, the pace of implementation was slower than initially programmed, as discussed in section 3.2 below. Bank staff responded with commendable flexibility to the institutional constraints observed in the implementation of these reforms and re-programmed the pace of implementation.

The PRSC series provided focused support to the government's efforts to combat *corruption*. The IEG's Country Assistance Evaluation (CAE) for Armenia in 2002 recommended that the Bank should help Armenia formulate and implement an anti-corruption strategy. In response to the CAE, the Regional Management noted that the government just published an anti-corruption strategy with support from the Bank and that the Bank would attempt to do support its implementation through the forthcoming PRSCs. The PRSC team judged that the client interest in and commitment to implementing a broad-based reform effort was weak and, moreover, there was little institutional capacity to undertake a broad-based agenda. No implementing body could be expected to enjoy the independence and the support necessary for success at this stage. In agreement with the government, the Bank team judged it important to proceed in a modular fashion, focusing on key reform elements. Given the comparative advantage of the Bank, it was decided to orient the PRSCs to reforms of the tax and customs administration, with the purpose of fighting corruption, whilst improving the business climate. It was expected that with demonstrated success with a modular approach, a holistic approach could be taken over a future CAS period. In view of the difficulty encountered with this reform step, it appears appropriate to have eschewed a more ambitious reform agenda in governance.

*Overall, the relevance of the PRSCs is rated as highly satisfactory.*

### **3.2 Achievement of Program Development Objectives**

*Overall achievement of objectives*

***Rating: Satisfactory***

On balance, the achievement of objectives of the PRSC program was satisfactory. In each of the four thematic areas, Armenia made substantial progress. As detailed in Annex 1 and in the discussion below, most of the specific PRSC objectives and expected outcomes were substantially and a few were partially achieved. Probably the most noteworthy successes were improving telecommunication services, consolidating reforms in the management of public utilities, improving property rights and taking other measures to strengthen financial intermediation, greatly expanding real spending while improving efficiency in the education and health sectors, increasing pension payments, and expanding agriculture extension services. By any standards, this is a large and impressive body of reforms to have achieved in a four year period.

Significant progress was also made in various aspects of budget management, financial accountability and procurement, corporate governance, tertiary education, rural infrastructure, and in railway services and early childhood education. Areas in which there was progress but achievements fell below initial expectations were: reforms in tax and customs administrative and the liberalization of air services, programs to control non-communicable diseases, development of private health insurance, and monitoring and control of illegal logging. On balance, an overall rating of satisfactory is justified.

*Consolidating Macroeconomic Discipline and Strengthening Governance*

#### **1.1 Maintaining macroeconomic stability.**

During the period of the PRSCs (2004-2007), economic growth averaged about 13% per annum, fiscal deficits were less than 3 percent of GDP, annual inflation averaged 3.4%, and foreign reserves were maintained above the equivalent of 3 months of imports. The very rapid economic growth—well above the 6% per annum rate anticipated at the time of PRSC I—was driven in large measure by a dramatic increase in remittances: recorded remittances (which probably understate actual remittances) grew from about US\$220 m (about 8% of GDP) in 2003 to over US\$1,200 m. (13% of GDP) in 2007.<sup>1</sup> This large inflow financed a major expansion of new construction of both residential and commercial property, and the construction sector contributed at least one third of total GDP growth over the period.<sup>2</sup>

During this construction boom, the government was able to increase tax revenue as a share of GDP (from 14% in 2003 to 17% in 2008) and thereby to increase real public sector expenditures significantly while keeping the fiscal deficits below 3% of GDP and reducing the external debt-to-GDP ratio. Financed by the significant capital inflows mentioned above, the current account deficit grew sharply from under 1% of GDP in 2003 to about 8% in 2008. Inflation accelerated modestly from 2% in 2004 to over 5% in 2006, 2007 and 2008—above the PRSC target of less than 3% per annum.

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<sup>1</sup> IMF Staff Report, Oct. 31, 2008.

<sup>2</sup> Figure 1 in IMF Staff Report, Oct. 31, 2008

Overall, Armenia maintained adequate macroeconomic discipline during this period that was dominated by an externally-financed construction boom. It met the targets of the IMF's PRGF covering 2005-08.

As noted, the economy went through several structural transformations throughout the PRSC period. One of the most pronounced changes was the dramatic shift in the growth structure driven by a dramatic increase in the share of non-tradable sectors, namely by the construction sector, moving out resources from tradable sectors of the economy. The construction sector had nearly doubled its share in GDP generating almost 40 percent of the above mentioned average 13 percent annual growth in 2004-07 period. However, the rapid increase in externally-financed housing construction contributed to structural vulnerabilities of the Armenian economy and led to a disappointing export performance.

Economic growth was driven by productivity gains and accompanied with structural changes in the sectoral composition of employment, but with weak job creation until the middle of the PRSC period. However starting from 2006 the employment response to growth became positive, led to a net job creation in the economy and reduction in unemployment rates both in rural and urban settlements.

### *1.2 Public administration reforms.*

Although the overall target for increasing the tax revenue/GDP ratio from 14% to 16% by 2008 has been achieved, the efforts to strengthen tax administration (which the Bank had initially supported beginning with SAC IV in 2001) have proceeded slowly and with partial success. Regarding the introduction of self-assessment systems, since mid-2006, taxpayers have been provided the option to send tax declarations by post. The process of accepting returns has been simplified, returns may be accepted through mail boxes placed in tax offices and the basis for implementing electronic filing is being put in place. However, implementation of this measure has not been encouraging mainly because administrative practices, such as the examination of declarations by the recording commissions, had not been improved.<sup>3</sup> Most returns are still submitted manually.

The Large Taxpayers Unit (LTU) has taken some positive steps, such as periodic publication of the list of 300 large taxpayers, but its organization remains inefficient and the share of total revenues contributed by large taxpayers has declined.<sup>4</sup> From 2009 steps have been taken to improve LTU administration: there has been a pooling of efforts within one office, and selection criteria have been strengthened. The goal of accelerating VAT refunds has been somewhat thwarted by the continuing prevalence of apparently bogus invoices that require careful review.<sup>5</sup> Clearing the backlog of VAT refund claims therefore has been retained as a structural measure in the new IMF PRGF for 2008-09.<sup>6</sup>

Overall, the common perception is that tax administration has improved—but not significantly. In the 2009 World Bank's Doing Business Report, Armenia's score on "ease of paying taxes" was

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<sup>3</sup> Policy Notes 2008 p. 103. According to the State Revenue Commission, the practice of sending all returns to the Recording Commission was eliminated in late 2008.

<sup>4</sup> Policy Notes 2008 p. 103.

<sup>5</sup> Policy Notes 2008, p. 111.

<sup>6</sup> IMF Art. IV, p.22.

unchanged between 2005 and 2008.<sup>7</sup> New results from the Business Environment and Enterprise Performance Survey (BEEPS)—which indicated in 2005 that 63% of firms reported that tax administration was a problem in doing business in Armenia—are not yet available. Tax administration will benefit from the adoption of a three year integrated strategic reform program adopted in 2008, which is the basis for continued Bank policy support.

Sound progress was made with reforms intended to strengthen customs administration (which the Bank had also initially supported beginning with SAC IV in 2001), though implementation was slower than initially programmed. A modern system for Direct Trader Input was established, thereby reducing the interaction between importers and customs agents and hence opportunities for corruption; this system is available in customs houses and offices, but not as yet in customs warehouses. Moreover, the use of “green channels” based on risk assessment systems has significantly increased. However, the imposition of revenue targets on the Customs Administration by the government led to a cautious attitude on the part of Customs in implementing reforms. Reportedly one element of the agreed reform program—reducing the role of reference prices in valuing imports—was pursued briefly in order to win approval of the next PRSC but was subsequently reversed. Overall, during the period of the PRSCs, the customs administration has greatly improved its technical capacities for better, less corrupt performance, using funds for computers and software provided indirectly through PRSC III, and the political will to eliminate discretionary behavior has been fortified, but implementation will continue to require strong political support.<sup>8</sup> Recent BEEPS data (August 2009) show that complaints about unofficial payments to customs have fallen significantly; however, overall customs regulations continue to pose a serious barrier to businesses.

Prior actions for PRSC I and II included merging responsibilities for *irrigation and drainage* under the Water Resources Management Committee (WRMC). This was a step toward a medium-term goal of increasing irrigation cost recovery. The lead responsibility for supporting institutional reforms was taken by the Millennium Challenge Corporation (MCC) from 2006 and the Bank team assisted the MCC in this area.

### 1.3 Public Management Reforms.

The measures designed to advance the *budget management system and financial reporting* during the period of the PRSCs have been largely implemented, although the quality of that implementation must still be substantially improved. The budget in all ministries is prepared on the basis of GFS 2001 classifications, program budgeting is used in 14 state budget agencies; an internal audit office has been set up in all ministries and in the majority of central government entities;<sup>9</sup> IPSAS cash basis standard have been implemented in all ministries; and all State Non-Commercial Organizations are submitting financial reports. The quality standards achieved so far are uncertain and likely to be low. In particular, internal audit offices are quite new: pilots in two agencies were started a few years ago and the expansion to all ministries took place only in 2008. Hence, their technical capacities and authority (*vis a vis* other financial review offices from the Soviet days that still exist) have yet to be developed, and their audits do not conform to international standards.<sup>10</sup> With respect to SNCO reporting, under current legislation, there is no

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<sup>7</sup> IMF Art IV, p. 20.

<sup>8</sup> The new administration that took office in early 2008 seems to be more determined to reduce corruption in customs administration. See Policy Notes 2008 p. 69.

<sup>9</sup> Policy Notes 2008, p. 150.

<sup>10</sup> PEFA 2008 p. 53.

requirement for auditing SNCO statements, and information on receipt and use of funds is thus not effectively verified.<sup>11</sup> In short, positive steps have been taken during the PRSC period, and the government has demonstrated serious intent to improve public expenditure management, but sustained attention to improving capacities and standards is still needed.

With respect to *external audit*, PRSC I had included measures to create a new system. But, prior to PRSC II, the Bank Government decided that this was too ambitious and dropped any reference to external audit functions. Nevertheless, the Armenian government did begin to move forward to strengthen its external audit function in 2007.<sup>12</sup>

On *procurement*, work began in 2004 on introducing an electronic system, and the government approved a “Strategy for Introducing the System of Electronic Procurement” in January 2006. However, the implementation of system has been delayed, mainly due to political change, lack of capacity, an overambitious implementation approach, and the absence of a detailed action plan.<sup>13</sup> Although data on the use of the Single Source method of procurement in Armenia is not available, it appears that it has been reduced but is still higher than the international norms (5% of the total procurement expenditure).<sup>14</sup>

Following initial work under the IDA Public Sector Modernization Project, a milestone was introduced in PRSC III calling for the preparation of a strategy to introduce a system of *staff performance appraisal* to support a merit based basic wage and bonus system. As expected, by 2008, this staff performance appraisal system is being piloted in three key ministries.

Following implementation of surveys in Armenia during 2006 under the Reports on Observance of Standards and Codes (ROSC), the government became interested in taking steps to *improve corporate governance*, especially with respect to disclosure of the ultimate beneficial shareholders of banks and public access to key company records. In response, milestones were included in PRSC III and IV regarding necessary revisions in the banking law and registration law. These steps were completed. As very imperfect indicator on confidence in publicly-listed companies, market capitalization of quoted companies has increased from 0.8% of GDP in 2005 to 1.5% of GDP in 2008. This is well below the target outcome of 12% due largely to various changes in securities laws.

### *Sharpening Competition and Entrenching Property Rights*

#### *2.1 (a) Liberalization of key services.*

The PRSC goal of establishing a competitive telecommunication sector has been achieved. The PRSC supported the modernizing of the *telecommunications* law and the expansion of telecommunications services. In conjunction with its privatization of the telephone company in the 1990s, the government had granted a 15 year monopoly to the private investor, Armentel. However, without changing that monopoly over land lines, the government passed a new telecommunications law in 2005 that opened mobile telephony and internet services to competition. Based on that law, the government defined a new regulatory policy and has since licensed three mobile telephone companies and about 40 Internet service providers. The number

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<sup>11</sup> PEFA 2008 p. 55.

<sup>12</sup> Policy Notes p. 150.

<sup>13</sup> Draft CPPR 2009 p. 32 and Policy Notes 2008, p. 150.

<sup>14</sup> Draft CPPR 2009, p. 11 and p. 15.



of mobile phone subscriber has jumped from about 200,000 in 2004 to about 1.6 million in 2008, and Internet services are now widely available. Also, as a milestone for PRSC IV, the government has taken steps to modernize its procedures for allocating radio frequencies among commercial uses, although the transparency and efficacy of these new procedures have not yet been established.

The policy and legal regime governing *air services*, and the price and quality of those services, have not improved to the extent expected under the PRSCs, though there has been a substantial rise in the range and quality of air services (passenger and cargo) to the country. Before PRSC I, the government had given exclusive rights through 2013 to Armenia's international air services to a private airline, Armavia, in exchange for an up-front payment and an annual payment of US\$1 million for the life of the agreement. Beginning with PRSC I, the government announced its intention to liberalize the air services regime—but always with the caveat that this must be “without prejudice to the implementation of already existing commercial agreements with private carriers.” In December 2006, the government issued a policy note stating: “The government considers it appropriate to work with Armavia to achieve a more normal and flexible relationship between the government as policy maker and Armavia as a private airline. The aim would be the earliest possible negotiated removal of contractual limitations on the government's ability to make and implement air services policy in the overall interest of the nation, customers and airlines.”

Two important reform steps were taken by the authorities with the support of the PRSCs. Armenia concluded on “Open Skies” agreement with the US, which made possible direct flights to the US without any restrictions and under conditions of liberal competition. Second, Armenia negotiated a horizontal air services agreement with the European Union that permits the designation of any EU carrier – this is a first step towards a fully liberal regime for the future. To date, however, no modification of the contract with Armavia has been negotiated, and Armavia retains an effective veto on any additional airline services. As a consequence, the flight frequencies continue to be at sub-optimal levels, connections limited, and the services prices are high,<sup>15</sup> despite the entrance of new carriers to the market, especially on routes to central and Western Europe.

With respect to *railway services*, the PRSC objective was to ensure that the Armenia Railways would operate on a commercial basis with transparent rate setting. PRSCs I and II supported the objective of setting up effective public regulation of an autonomous state-owned railway. At the same time, the Bank provided technical assistance to the government on the design of a private sector partnership. This came to fruition in 2006 with the government decision to concession the railway operation and infrastructure through an international tender to a private operator. The Bank provided technical assistance to prepare that tender. The concession agreement establishes levels of investments and provides a framework for performance monitoring. But performance standards and the rules and regulations to govern the relations between the government and the concessionaire and for tariff setting are yet to be defined.<sup>16</sup> The concession agreement requires the railways—now renamed the South Caucasus Railway (SCR) — to be run on a commercial basis with transparent rate setting.

## 2.1 (b) *Regulatory reform of state-owned utilities.*

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<sup>15</sup> PRSC IV Program Document, p. 27.

<sup>16</sup> Transport Policy Note 2008 pp. 10-11.

The broad objective of the PRSCs was to further strengthen the regulation of *public utilities* (energy, irrigation, drinking water, and telecommunications) by the Armenia Public Services Regulatory Commission (PSRC) and to raise the quality of service provision. This involved implementation of an Integrated Financial Rehabilitation Plan and improved monitoring of performance data. The PSRC, which was established in 1998 and with whom the Bank has worked closely through a number of investment projects, has proven to be a very capable organization and has kept the reform agenda on track. The envisioned reforms associated with the PRSCs, including improvements in the operation of the electricity markets, have been completed. The newly established monitoring system is functional and indicates that performance standards for electricity and drinking water have improved steadily, as indicated in Annex 1.

## 2.2 Entrenching property rights

Under the leadership of the Armenian Central Bank and in cooperation with private banks, the regulatory and institutional arrangements for *secured transactions* were significantly improved during the PRSC period. In order to enhance *confidence in the banking system*, the Central Bank also modernized corporate governance laws for banking and established a unified supervision regime for the banking sector. Finally, the government improved regulation and supervision of the insurance industry. These reforms almost certainly contributed to a rapid increase in bank loans to the private sector, an increase in private sector deposits relative to GDP, and an expansion of the insurance industry. As detailed in Annex 1, all of the 2008 expected outcomes for these indicators have been realized. Much of the expansion of lending was probably associated with the real estate boom during these years. Furthermore, Armenia's score on the "Ease of getting credit" as measured by the World Bank Doing Business Report 2009 improved significantly between 2005 and 2008.<sup>17</sup>

## Mitigating Social and Environmental Risks

### 3.1 Improving social protection and social risk management.

Important objectives of the PRSCs were to increase the share of poor families who receive support under the *family benefit program*, which had been initiated in 1999, to differentiate the amount of the benefit according to family characteristics, and to decrease leakage of funds to non-poor families (i.e. to improve targeting). Based on the latest available data from the 2006 and 2007 Integrated Living Conditions Survey (ILCS),<sup>18</sup> there were substantial improvements in these dimensions. The data for 2006 show significant improvements; the data for 2007 less so, but there are reasons to believe that distortions are reflected in the 2007 data that understate the improvement.

In evaluating the impacts of social protection programs, it is important to keep in mind that poverty has fallen significantly in Armenia in recent years. The share of the population living below the official poverty line fell from 34.6% in 2004 to 25.0% in 2007, and the share of the very poor fell from 6.4% to 3.8% over the same period.<sup>19</sup> The impressive reduction in poverty was achieved by high rates of sustained economic growth that led to increases in labor income and

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<sup>17</sup> IMF Art. IV, p. 20.

<sup>18</sup> All data based on 2007 outcomes are from the Social Snapshot and Poverty in Armenia 2008.

<sup>19</sup> Social Snapshot 2008, Table 3.1, p. 28.

growth in remittances also played an important role.<sup>20</sup> Pension payments and social assistance payments (mostly from the family benefit program) also made a significant contribution. Pensions have kept poverty headcount much lower than what it would have been without the social transfers. The family benefit, which is targeted at the very poor, has less of an impact on the headcount but has a large effect on decreasing the poverty gap and poverty severity. There is firm and robust empirical evidence on this.

Given the significant decline in the absolute number of poor, the number of individuals that receive payments under the family benefit program has fallen slightly in absolute terms (from 476,495 in 2004 to 470,078 in 2007).<sup>21</sup> However, the *share* of the poor that have received payments from the family benefit program has fluctuated in the range of 25-30%, as shown in the table below. The share of the very poor receiving such benefits increased steadily from 40.6% to 64.6% over the same period; hence, in terms of errors of exclusion of the very poor, targeting have improved impressively. This is important because the benefit targets the very poor. Even though there was a very significant movement out of poverty, the coverage of the poor remained constant over time, indicating a good targeting performance (obviously, those who moved out of poverty were excluded from the benefit).

Finally, a comment on the original target of 70 percent coverage of the overall poor. This can be judged to have been overambitious as resources allocated would have to be 2.5-fold higher. This would be fiscally unaffordable and unsustainable.

**Table 2: Coverage of the family benefit program: percent of the “pre-transfer poor” who received family benefit payments<sup>22</sup>**

	2004	2005	2006	2007
Poor	25.1	26.5	31.9	28.6
Very Poor	40.6	50.8	60.2	64.6

In terms of errors of inclusion, performance remained impressive by international standards, even if the ambitious goals set by the government for itself were not reached. The share of the bottom two quintiles remained consistent over time at 70 per cent.

With regard to *pensions*, the objectives of the PRSCs were to increase the average pension paid under the pre-existing pension system and to develop and begin to put in place the foundations for a new multi-pillar pension system. These objectives were achieved.

The existing pension system is the broadest social protection program in Armenia: during 2004-2007 about 48% of Armenian households reported receiving pension payments.<sup>23</sup> The average pension payment has been increased significantly: it almost doubled in real terms between 2003

<sup>20</sup> For analysis of 1999-2005 poverty dynamics, see the 2008 Sustainable Development Program, Table 2.2, p. 43, and Figure 2.6, p. 57.

<sup>21</sup> Social Snapshot 2008, Table 9.8, p. 108.

<sup>22</sup> Social Snapshot 2008, Table 96, p. 108. The figure cited in the 2008 Policy Notes is slightly higher: the share of the poor receiving the family benefit was estimated at 34% in 2006 (p. 191, para. 13.43).

<sup>23</sup> Social Snapshot p. 104.

and 2006,<sup>24</sup> increased slightly in 2007,<sup>25</sup> and then increased 62% for 2008 and 16% for 2009.<sup>26</sup> Cumulatively, this will achieve the target of a three-fold increase over 2003 as established in PRSC IV.<sup>27</sup> Within the government's rapidly growing budget, the *share* allocated for pensions remained flat at around 14% during 2005-2007 and then jumped to over 19% in 2008.<sup>28</sup> Despite the fact that average pension payments still remain low relative to average salaries, pension payments have contributed significantly to poverty reduction: in the absence of pension payments, the share of poor households in 2007 would have been 31.2% compared to the actual 25%, and the share of very poor households would have been 11.7% compared to the actual 3.8%.<sup>29</sup>

While increasing payments under the pre-existing pension system, the government has also moved forward in designing a new, multi-pillar system. It has set a target date of January 2010 to begin implementation. However, the feasibility of the new system in terms of fiscal resources and institutional capacity is uncertain, especially in light of the current economic downturn, and merits further consideration.<sup>30</sup>

Overall, the social transfers have played an important role in poverty reduction and keeping living standards of the poor and vulnerable improved. The table below illustrates what will happen to poverty among pension recipients and beneficiaries of family benefit, if they were reduced or eliminated. The rate of extreme poverty among the FPB recipients would go up from 8.5 to 28 percent.

Finally, without the constant support of the PRSCs series, it would have been difficult to protect the allocation of resources to FPB (and to pensions) as the government had shown clear intentions to reduce outlays. The clear empirical evidence of the effectiveness of these programs in fighting poverty helped to convince the government as to their value.

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<sup>24</sup> PRSC IV, Annex III, p. 1.

<sup>25</sup> Based on Policy Notes p. 182 and assuming relatively constant number of total beneficiaries.

<sup>26</sup> EIU p. 19.

<sup>27</sup> In PRSC I, the target was defined as a pension/average wage ratio of 27.5%. Given the significant increase in average salaries during the period of rapid economic growth, the average pension relative to average salary fell from 21% in 2002 to 17% in 2006.<sup>27</sup> By 2007 this ratio remained below the target of 27.5% established in PRSC I.

<sup>28</sup> Policy Notes p. 181.

<sup>29</sup> Social Snapshot p. 105.

<sup>30</sup> Joint Staff Advisory Note, SDP 2008 p. 8 and 11.

**Table 3: Changes in Pensioners' Poverty with Declining Pensions**

	Base	Poverty with declining pensions				Corresponding increase in poverty (percent)			
<i>Overall poverty</i>		-25%	-50%	-75%	-100%	-25%	-50%	-75%	-100%
Headcount	29.3	30.6	33.2	35.8	39.0	4.4	13.5	22.5	33.4
Gap	4.3	5.8	7.5	9.5	11.8	35.4	75.6	122.2	175.6
Severity	1.2	1.8	2.6	3.7	5.3	41.3	105.5	198.6	327.3
<i>Extreme poverty</i>									
Headcount	4.9	5.7	7.6	10.4	14.0	15.1	54.0	111.0	183.5
Gap	0.6	1.0	1.6	2.6	4.1	72.1	180.1	363.1	635.2
Severity	0.1	0.2	0.5	1.1	2.2	85.3	292.0	734.1	1,575.0

Source: ILCS 2007.

**Table 4: Changes in Beneficiary Poverty with Declining Targeted Family Benefit**

	Base	Poverty with declining family benefits				Corresponding increase in poverty (percent)			
<i>Overall poverty</i>		-25%	-50%	-75%	-100%	-25%	-50%	-75%	-100%
Headcount	47.5	48.9	50.6	53.0	56.0	3.1	6.7	11.6	18.1
Gap	8.4	11.0	13.8	16.7	19.8	31.5	64.7	99.3	136.1
Severity	2.5	3.6	5.0	6.9	9.1	45.0	103.9	177.4	266.5
<i>Extreme Poverty</i>									
Headcount	8.5	11.8	16.9	22.4	28.0	39.2	99.4	163.8	229.9
Gap	1.0	1.8	3.2	4.9	7.3	92.0	227.8	413.5	660.5
Severity	0.2	0.5	0.9	1.7	2.9	114.5	325.7	675.2	1217.5

Source: ILCS 2007.

**Table 5: Changes in Beneficiary Poverty with Declining Government Transfers (Pensions plus FB)**

	Base	Poverty with declining combined transfers				Corresponding increase in poverty (percent)			
<i>Overall poverty</i>		-25%	-50%	-75%	-100%	-25%	-50%	-75%	-100%
Headcount	31.6	33.3	36.1	39.2	43.7	5.4	14.0	24.0	38.1
Gap	4.9	7.0	9.4	12.1	15.2	43.3	92.0	147.3	210.2
Severity	1.4	2.3	3.5	5.3	7.7	56.5	143.4	267.2	434.9
<i>Extreme poverty</i>									
Headcount	5.5	7.6	10.8	15.2	20.8	37.7	96.0	177.3	278.6
Gap	0.6	1.3	2.3	4.0	6.5	102.3	270.8	546.1	945.6
Severity	0.1	0.3	0.8	1.8	3.5	130.6	446.1	1109.4	2327.5

Source: ILCS 2007.

### 3.2 *Raising the quality of education*

Within the framework of increasing budget allocations to the education sector, the specific goals under the PRSCs were: (a) to increase the efficiency and quality of education by decreasing the number of teachers and increasing average teacher salaries; and (b) to define a strategy for early childhood education and initiate pilot programs. Other goals were to consolidate high schools, improve the per capita financing formula, and begin implementation of selected reforms in higher education. All of these goals have been substantially achieved. Moreover, Armenia implemented a radical decentralization in education, whereby authority was shifted from the line ministry to be devolved to schools through the allocation of block grants and greater authority for school administrations and boards. Schools were established as state non-commercial entities following the New Zealand model.

Recognizing that the existing educational establishment was over-dimensioned, the government initiated its program to enhance system efficiency by reducing the ratio of students to teachers (on a full-time equivalent basis) in 1998, when the ratio was about 8. At the time of PRSC I, the ratio was about 14, and the goal was to increase that ratio to over 16 by 2007 by dismissing over 6,000 teachers. Over this period, the government did take the politically difficult step of dismissing teachers. The total number of teachers (not full-time equivalents) fell from 60,000 in 2000 to 42,000 in 2008. However, as of 2007, the ratio of student to full-time equivalent teachers remained at 14.0, and the plan for 2008 was to increase this ratio to 14.8. This is below the original target for several valid reasons. In 2006, the government increased the standard program from 10 to 12 years of schooling, and this necessarily involved lower student-teacher ratios in the newly added grades. Also, the original target had not taken into account either the need to have lower student-teacher ratios in relatively isolated rural schools or the absolute decline in the number of the student population.

Given its increased budget allocations to the sector (from 2.0% of GDP in 2002 to about 3% in 2007 and 2008) and the decreasing number of teachers, the government was able to increase average teacher salaries steadily from Dr50,500 in 2005 to Dr90,000 in 2008 (in nominal terms), thus substantially exceeding the annual targets initially established in PRSC I.

For *early childhood education* (ECE), the milestones included in the PRSC matrices were rather modest: initiating and then adopting a strategy for ECE and then launching pilot programs consistent with that strategy. Despite a slow start, the government did put forward a strategy, embodied in a law approved by Parliament, during 2006, but this was more of a wish list than a well-articulated strategy. Despite prodding from the Ministry of Education, UNICEF and the Bank, the Ministry of Finance has not allocated any significant funding for an ECE program. Twenty pilot projects involving about 500 children have been launched primarily with funding from IDA, UNICEF, and local communities, and it is intended to expand these pilots to about 150 students soon. However, the targets for significantly increasing the proportion of poor children participating in pre-school institutions, which were put forward in the PRSC policy matrices and tables of expected outcomes, were unrealistic in light of the measures contemplated in the policy matrices and have not been realized.

All of the other objectives for education envisioned in the PRSCs have been achieved. In particular, as part of the strategy to improve higher education and consistent with Armenia's undertakings in the 2005 Bologna Declaration, more than two state-run universities have met the

standards so that their courses will be credited throughout the European system. However, the amount of financing for stipends and scholarships remains extremely limited.<sup>31</sup>

### 3.3 *Controlling health risks*

The primary objectives for the health sector associated with the PRSCs were: (a) to improve efficiency in the hospital sector by implementation of a hospital rationalization program; (b) to increase the share of the health budget allocated to of Primary Health Care (PHC); (c) to develop and put in place a framework for private health insurance; and (d) to develop and implement a program for control of non-communicable diseases. These goals were to be pursued within the context of increased budget allocations to the health sector. The measures taken under the PRSC were expected to contribute to reductions in infant and maternal mortality and to higher utilization rates for hospitals and PHC by the poor. Hospitals were transformed into state non-commercial entities along a decentralized reform model.

During the period of the PRSCs, the budget allocations to the health sector increased substantially from Dr16 b. (1.2% of GDP) in 2002<sup>32</sup> to about DR54 b. (1.5% of GDP) in 2008.<sup>33</sup> This represents a high rate of increase in real terms – about 15 per cent per year – or what could be absorbed by the health sector efficiently. The PRSC targets were, however, set as shares of GDP and on the assumption of GDP growth of 6 per cent annually. With real growth being nearly twice the target, and despite a strong real rise in health spending, PRSC targets of 1.8% and 1.9% of health expenditures as a share of GDP as set forth in PRSC I and II proved to be no longer relevant. Within this sharply expanding real budget, the share allocation to Primary Health Care services increased from 33.4% in 2003<sup>34</sup> to 35.6% in 2007.<sup>35</sup> This fell somewhat below the target for the PHC share of 38.5% first set in PRSC II and remains below the target of 45% for 2009 as set in PRSC III and IV – again in line with the absorptive capacity of the PHC sector. In the 2008 Sustainable Development Program, the government indicates that the allocation to primary health care through 2015 will be in the range of 40-45%.<sup>36</sup>

The hospital rationalization plan has moved substantially forward in Yerevan, although more slowly than anticipated as measured by the number of hospital contracts issued by the State Health Agency. This figure had been reduced to only 115 in 2006 compared to the initial target of 100.<sup>37</sup> For the regional hospitals, by the time of PRSC IV, the government had prepared rationalization plans, and the 2008 SDP indicates that these plans would be implemented over a 7-8 year period.<sup>38</sup> Although all of the PRSC Policy Matrices (but not the Expected Outcome tables) stated that progress in the hospital rationalization program would be measured by bed and physician ratios, it was subsequently decided that these would not be appropriate indicators for measuring efficiency in the system and, in the context of the IDA-financed Health System Modernization Project, other indicators have been used.

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<sup>31</sup> Policy Notes p. 156 and p. 159.

<sup>32</sup> PRSP 2003, p. 70. These figures are in nominal drams.

<sup>33</sup> SDP 2008, p. 238.

<sup>34</sup> PRSC II PD, Annex III, p. 4. The Health Sector Aide Memoire 2005, p. 22, gives a lower figure of 29% (assuming 2003 is baseline year).

<sup>35</sup> Health Project Aide Memoire Results Matrix Nov. 2008, p 8.

<sup>36</sup> SDP 2008 p. 239.

<sup>37</sup> See PRSC I Annex III, p. 3 and Health Sector Aide Memoire Oct. 2007 p. 23.

<sup>38</sup> PRSC IV p. 34 and SDP p. 239.

The goal of developing and putting in place a framework for private health insurance, which had been first included in PRSC I as a trigger for PRSC III, was overtaken by government decision to institute ambitious reforms in pension insurance and, hence, the concentration of government capacity on these reforms meant that private health insurance reforms were to be worked on at a later stage.

As the government focused its reform efforts and capacity on hospital rationalization and PHC reforms, the objective to develop and implement a program for control of non-communicable diseases (NCD), was postponed. In 2007, the State Health Agency provided the Bank with a strategy for NCD-related activities.<sup>39</sup> In 2008 the SDP states that “the government in the long and medium term perspective intends to...develop and continuously improve the national policy and plan for prevention and control over non-communicable diseases.”<sup>40</sup>

Among the health indicators included the PRSC Expected Outcome tables, the infant mortality rate has improved modestly from 12.1 per 1000 live births in 2002 to 10.8 in 2008 but remains far above the target of OECD rate of 5-6. Despite substantial improvements during the 1990s, the maternal mortality rate has not improved on a sustained basis in recent years, as shown in Annex 1. Although it is better than in most CIS countries, it remains far above the OECD average of about 9. Finally, the utilization rate of health care services (PHC) by the bottom two quintiles was targeted to increase from 3.5% in 2003 to 10% by 2007 and 15% by 2009.<sup>41</sup> As shown in Annex 1, the actual rate increased initially in 2004 but fell back to 3.5% in 2006.<sup>42</sup> In January 2006 the government eliminated fees on PHC services and so this utilization rate has probably increased in 2007 and 2008.

### *3.4 Reducing risks in natural resource management for sustainable livelihoods*

In the realm of environmental management, the primary objective of the PRSCs was to establish a national forestry policy and the institutions required to monitor and control illegal logging. This plan included the establishment of community-managed forest areas. PRSC I had also established the goal of expanding the use of Environmental Impact Assessments, but this was abandoned by the time of PRSC II due to lack of government commitment.

During the course of the PRSCs, the government adopted a National Forestry Action Plan and a National Action Plan to combat illegal logging, and, after much internal debate about its location within the government and its responsibilities, it established the multi-agency State Forest Monitoring Center to monitor and control illegal logging, a highly profitable activity, involving not only poor villagers but also well-organized and politically connected groups. Through this process, the public awareness of the issues of forestry management and illegal logging was increased. The monitoring committee, under the chairmanship of a senior minister, has representation from various ministries and agencies (such as customs and tax and the police) and the political authority to monitor illegal logging. In addition, the legal basis has been put in place

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<sup>39</sup> The November 2008 Results Matrix from the supervision mission for the health project indicates that a baseline budget for NCD activities has yet to be established but will be estimated by the Bank in the course of its PER work in the sector. See footnote 7, p. 31.

<sup>40</sup> SDP 2008 p. 241.

<sup>41</sup> These are the targets indicated in PRSC, Annex III, p. 2. These utilization targets were expressed in two ways: number of users as a percentage of total number of individuals in the bottom two quintiles (which is cited here), and number of users as a percentage of the estimated number of *ill* individuals in the bottom two quintiles. Recent data on the latter is not available.

<sup>42</sup> Social Snapshot 2008, p. 87.



for community forest management, which will likely lead to better control over use of forest resources. But such community forest management is only in the pilot stage, and the authority and capacities of this system remain to be established. It will likely take several years, at least, for these positive steps to bear fruit in terms of better forest management.

### *Modernizing the Rural Economy*

#### *4.1 Stimulating farm incomes*

As part of a broader program to increase agricultural sector production and incomes, the PRSC objectives were: (a) to strengthen and expand use of the agricultural extension services; (b) approve a new legal regime for the production of certified seeds and increase their use; and (c) establish and stimulate the use of modern food safety and phytosanitary standards. The first two of these objectives—expanding extension services and producing certified seeds—which were core conditions have been achieved, but there has been limited progress on the third objective regarding food safety and phytosanitary standards, which were milestones in the PRSC program.

The national agricultural service had been established with IDA and USAID support in 1996, but it had not received financing from the government budget and its capacity was limited. With strong leadership from the Ministry of Agriculture, the government began to expand financing for the service in 2006. Based on an independent survey, the percentage of farmers using the advisory services grew from 29% in 2004 to 61% in 2008. Cost recovery from users of the agriculture extension services has increased significantly, although in 2008 the 22% cost recovery rate remained somewhat below the target of 30%.

At the beginning of the PRSCs, Armenia had no legal or institutional system for certification of seed quality. Before PRSC II, a new seeds law was approved by Parliament, and procedures for seed certification are now in force. Implementation has been good but somewhat slower than anticipated, in part to allow existing seed producers to adjust to the new requirements. By 2008, only 10% of seeds sold were certified, compared to the PRSC target of 30%, but this percentage is expected to increase sharply in the coming years.

Progress toward putting in place new food safety and phytosanitary standards consistent with international norms has been slow for several reasons. There had been no rigorous analytical work on these issues prior to PRSC I; there has been lack of clarity within the government about the relative importance of food safety standards for the sake of public health and phytosanitary standards for the sake of promoting exports; and progress requires collaboration among three ministries—Health, Agriculture, and Trade and Economic Development. The government was able to mobilize technical assistance on these issues from the US Department of Agriculture, FAO, the EC, as well as the Bank. Work toward approval and implementation of these standards is continuing. The targets established in the PRSCs for a significant increase in the share of agricultural products being tested and certified by 2008 was never realistic in light of the challenges involved in setting up such a system.

#### *4.2 Developing rural infrastructure.*

The PRSCs supported completion of a diagnostic study covering all rural infrastructure services, the establishment of an inter-ministerial working group to define and pursue an action plan for improving these services, and the creation and monitoring by PSRC of rural infrastructure service standards. Priority within the PRSCs was given to (a) clarifying responsibility for each part of the rural road infrastructure in order to accelerate rural road reconstruction and (b) expanding use of natural gas by rural households.

The diagnostic and planning work has been done, including clarification of responsibilities for roads, and an ambitious reconstruction/rehabilitation of the rural road system is under implementation. The Bank has stepped up investment support in this area, partly as an emergency response to the global economic crisis. The government had also relied on financing from the US Millennium Challenge Corporation (MCC) for its rural roads program, but the MCC financing has been put on hold due to MCC's re-evaluation of Armenia's eligibility. The weighted average of over 60% of roads needing reconstruction falls short of the PRSC target of below 50% by 2008.<sup>43</sup> In 2009, the World Bank and the Asian Development Bank have approved an investment project that will finance rural road reconstruction.

The share of rural households using gas has increased steadily from about 35% in 2005 to 49% in 2007. Gas distribution is provided by private companies, but the government has subsidized construction of supply lines to villages. This expansion of gas service is only slightly below the pace envisioned by the PRSCs: the target was defined as a 50% increase in the share of rural households using gas between 2005 and 2008; and the actual increase through 2007 was 40% (49/35).

With some technical assistance from the Bank, PSRC has defined rural infrastructure service standards and is also monitoring those services.

### **3.3 Justification of Overall Outcome Rating**

Given that relevance of the program supported by the PRSCs is rated as highly satisfactory and the achievement of program development objectives is rated as satisfactory, *the overall outcome rating is rated as satisfactory.*

### **3.4 Overarching Themes, Other Outcomes and Impacts**

#### **(a) Poverty Impacts, Gender Aspects, and Social Development**

The rapid reduction in poverty in Armenia in recent years has been driven primarily by increased wages reflecting the productivity gains in the economy against a background of rapid and sustained economic growth – clearly, the PRSC-supported reforms contributed to this result. Poverty assessments prepared jointly by the Bank and the authorities show a marked disproportionate rise in the income of the bottom quintile and the bottom two quintiles as a result of growth. The PRSC-supported program contributed in several other important ways: supporting the design and the focusing of family benefit payments to the very poor; increasing pension payments; and stimulating the farm economy on which many poor people depend. Conditions for increased investment and job creation were clearly greatly enhanced. Over a longer time horizon, the expansion and improvements in the public education and health systems should lead to other improvements in social indicators. None of the PRSC-supported programs were specifically directed toward gender issues.

#### **(b) Institutional Change/Strengthening**

The PRSC program included many elements of far-reaching institutional reform and strengthening, as detailed above, in areas of budget management, civil service management, tax and customs administration, financial accountability, procurement, establishment of schools and hospitals as highly decentralized and autonomous non-commercial entities following the New

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<sup>43</sup> Republican roads include 4087 kms and local roads, 1962 kms, according to data in the Bank's 2008 Transport Policy Note. On this basis, the weighted average of the share of roads needing reconstruction is 60% compared to the target of 50%.

Zealand model, regulation of banks and other financial institutions, regulation of public utilities, and corporate governance, creation of forest management and illegal logging bodies. These deep institutional changes have to be followed up with sustained implementation and supporting reforms for them to take root.

**(c) Other Unintended Outcomes and Impacts**

None.

**4. Assessment of Risk to Development Outcome**

Armenia's prospects for sustained economic growth and further poverty reduction face increased risk due to the unfolding global economic crisis, the emergence of political tensions as a result of electoral unfairness (as noted by the OSCE), and the continued strength of dominant business groups that distort competition seriously.

Already the sharp reduction in remittances and other capital inflows from late 2008 to date has led to a dramatic slowdown in the construction sector. Prices of and demand for Armenia's mineral exports have declined sharply, leading to some mine closures. The economy is projected to contract by 15 per cent in 2009, and this will likely reverse temporarily the decline in poverty rates. The fiscal resources that the government has counted on to continue expansion and improvements in the education and health sectors and in its social safety nets have come under severe pressure.

Coping with these economic challenges might be complicated by on-going struggles between the major political parties, which became more intense following the disputed elections and related protests in early 2008. The consequent issues regarding political rights have already led to delays in financial support from major donors and could potentially lead to significant reductions in bilateral development assistance.

Finally, further consolidation of influence by major business groups, which have extensive ties within the government, might stall reforms that are designed to reduce discretion and increase the rules-based character in public policies and strengthen competition in key sectors and services.

However, the government has responded with vigor to the economic downturn through counter-cyclical policies aided by greatly increased external support. It is adhering to the underlying philosophy and thrust of its reform program, even if specific reform measures have to be re-programmed in the light of new fiscal realities.

In summary, the near-term risk to sustained economic growth and poverty reduction in Armenia is rated as "significant." However, the medium and long-term risk is judged to be "low", given the capacity within the country in the public and private sectors, the record of sustaining a reform program over more than a decade, political stability and a clear vision for reform aided by specific reform programs and measures, and the growing integration via trade, investment, technology and above all in the realm of ideas and experiences with the rest of the world.

Highly responsible macroeconomic policies over the past decade have created the fiscal and debt space for counter-cyclical policies that are now being pursued to support output and employment. Moreover, the authorities have mobilized large scale external support from the Bank and the Fund as well as bilateral. They are adhering to the reform course, maintaining an open trade and investment system, and have redoubled efforts to build a knowledge-based economy. With an equal effort on liberalizing air services and reforming customs and tax agency, the country would be well placed to seize opportunities as the international economy recovers. The priority in Armenia in the near-term must lie in maintaining the strong policy framework that it has put in place and consolidating institutional reforms already started.

## **5. Assessment of Bank and Borrower Performance**

### **5.1 Bank Performance**

#### **(a) Bank Performance in Ensuring Quality at Entry**

In the initial design of the PRSC series, the Bank's performance was satisfactory in terms of adjusting its own behaviors to the new guidelines for development policy operations within the framework of the PRSP approach. The Bank made a serious effort to "put the country in the driver's seat." Whereas previous SACs had primarily been designed by the Bank staff and presented to the government, at the beginning of the PRSC series the Bank invited the government to present its own program as the basis for dialogue and negotiation. In that spirit, the Bank also tried to align the PRSC with the priorities established in the 2003 PRSP, recognizing that the government had taken the PRSP process seriously and regarded it as a relevant strategic document.

However, as noted, the Bank staff pressed for a vigorous approach to customs and tax reforms than envisaged by the authorities and for a high priority for reforms in certain areas that went beyond the PRSP: the liberalization of the air services and telecommunications regimes, the expansion of early childhood education, and monitoring and control of illegal logging. Bank analysis showed the criticality of these reforms for sustaining growth and staff believed that their inclusion in the PRSCs would provide a vehicle for building country ownership over time.

The Bank's performance was also satisfactory in terms of aligning components of the PRSC with its broader country assistance program in order to maximize synergies and complementarities. The coverage of PRSCs I-III was quite broad, and the Bank's active engagement on so many policy areas would not have been feasible in the absence of complementary activities in its investment lending and AAA program. In this context, the Bank also ensured engagement by sectoral staff in the PRSCs, which had not always been the case for the earlier SACs.

The Bank performed well in terms of synchronizing its appraisal and approval of the PRSCs with the government's budget cycle so that the flow of Bank's resources could be taken into account in the government's fiscal plans. However, from the government's perspective, it might have been even better if appraisals had been consistently undertaken prior to September in each year, when the government sets its budget for the following year.

#### **(b) Quality of Supervision**

Throughout PRSC implementation, the quality of Bank supervision was satisfactory in two respects. First, the Bank maintained an active dialogue with the government on all key dimensions of the PRSC, and that dialogue was conducted not only with the Ministry of Finance by the PRSC team but also with line ministries by the Bank's sectoral staff. The integrated approach taken by PREM and sectoral staff was impressive. The concluding statements of Bank supervision missions and follow-up technical notes provided to the authorities was succinct, strategic and provided clear guidance as to resolving implementation problems.

Second, the Bank mobilized substantial resources through its administrative budget, trust funds (especially PHRD), and other sources to provide analytic work and technical assistance as needed during implementation. These inputs, including numerous "just-in-time" activities, were greatly appreciated by government staff involved. Examples of the Bank's efforts in this way include financing for study tours by government officials in tax administration and in bank supervision to Estonia and elsewhere, and mobilizing financial support from the FIRST International program in London to provide technical assistance to the superintendency of financial institutions within the Central Bank.

Third, the Bank undertook significant AAA work, especially the 2003 PER and subsequent sectoral PERs, that directly or indirectly supported the objectives of the PRSC. The PERs, and some other AAA, were undertaken jointly with the government, which proved effective. Finally, the Bank maintained a high degree of continuity among staff engaged on the PRSCs, especially among the core PREM and country office staff, although there may have been exceptions to this continuity in the education sector.

### **(c) Justification of Rating for Overall Bank Performance**

Given the ways in which the Bank conducted the dialogue regarding the design and implementation of the PRSCs and mobilized support for implementation, its performance is evaluated as satisfactory. Senior officials within the government commented that they regarded the Bank as fast and responsive and that they certainly had the feeling that the Bank was “working for us and the interests of the country.”

## **5.2 Borrower Performance**

### **(a) Government Performance**

Overall the government’s performance was satisfactory. Prior to PRSC design, the government had taken the PRSP process very seriously. That process was conducted under the responsibility of an inter-agency committee that reported to the Prime Minister, and on occasion to the President, and that was managed strategically by the Finance Minister (who held frequent meetings with the PRSC team) and on a day-to-day-basis by the Deputy Minister of Finance and Economy. At the beginning of the PRSC, the government established a similar inter-agency committee, and the same Deputy Minister was the operative head of that committee. This helped to ensure that the PRSC was regarded within the government as serving implementation of the country’s PRSP strategy. It also ensured high level and inter-agency attention to PRSC implementation.

The government also made significant efforts to identify its needs for analytical work and technical assistance and to work with the Bank, and in many instances with other donor agencies, to mobilize that support.

The government’s supervision might have been strengthened by greater attention to monitoring of outcome indicators, as discussed above under Monitoring and Evaluation.

### **(b) Implementing Agency or Agencies Performance**

There is no reason to distinguish between overall government performance and the performance of the implementing agency.

### **(c) Justification of Rating for Overall Borrower Performance**

In light of its excellent internal organization for designing and implementing the PRSCs and its willingness to use the PRSC process as a means for mutual accountability and deadline setting within the government, the borrower’s performance is evaluated as satisfactory.

## **6. Lessons Learned**

The experience with the Armenia PRSC series suggests the following lessons that should be taken into consideration in designing future development policy operations in Armenia and elsewhere:

1. *A sound PRSP with supporting MTEF and a set of government-determined priorities were crucial to success.* The broad coverage of policy issues and sectors within a DPO series, given the right circumstances, can be appropriate and useful. The first three PRSCs had such broad coverage, while the fourth PRSC focused on a narrow set of critical

reforms towards the end of a parliamentary period. Factors behind the successful PRSCs were: a long-standing relationship of trust between the government and the Bank; strong country ownership of most of the elements of the PRSC program; substantial complementarity between the PRSC program and the Bank's on-going investment operations and its AAA; and ample Bank resources, through the administrative budget and trust funds, to provide technical assistance as needed during PRSC implementation. In particular, the availability of Japanese financed PHRD grants for policy analysis and design, proved to be invaluable and essential to the success of the PRSC-supported reforms. When most or all these factors are present, broad coverage of DPOs can work; to the extent that they are not, coverage should be reduced.

In this connection, as a country's own processes for strategic planning improve, future DPOs should continue to be based on the country's own strategy, but reflect rapidly changing world economic conditions. In the case of Armenia, the second PRSP that was drawn up just before the global economic crisis – the SDP -- and, perhaps more importantly, the MTEFs reflect increasingly strong government policy formulation and analysis processes. However, one problem in using the existing SDP and MTEF for designing new DPOs is that the global economic crisis has compelled major changes in the government's fiscal program and in the pacing of its reform agenda. With this in mind, the Bank will need to help the government revise its strategy in response to rapidly changing circumstances. Depending on the severity of Armenia's economic problems in the coming year, it may be appropriate to focus DPOs on maintenance of the policy framework already in place and fuller implementation of institutional changes already taken than to pursue new reforms.

2. The Armenia experience shows the value of including measures in the PRSC where the *support of the government is nascent or mixed* and where the potential exists to build support through the PRSC. Such support can be built through demonstrated persistence, the importance of careful underlying analysis, the use of international best practice examples and the importance of trust in relations with the client. The Armenia example shows that (i) such measures should be limited to those that have been demonstrated through robust analysis to be critical for sustained growth; (ii) inclusion of such measures should help build support while providing lessons; (iii) and implementation will be difficult and will have to be flexibly tailored in the light of experience. In view of Armenia's weakness in governance and severe problems with corruption and anti-competitive behavior, the Bank insisted on a strong program of reforms in customs and tax administration. Similarly, reforms towards liberalization of civil aviation had a sound analytical basis. The intellectual case for such reforms was easy to establish, and the Bank engaged in intensive advocacy, but implementation proved to be difficult and re-programming of sequenced reform steps had to be undertaken. Today it can be confidently said that the awareness of the need for customs and tax reforms is widespread, deeper measures are being taken, and initial important steps towards aviation reforms have been agreed. Thus, nascent ownership within important parts of the government for reforms that the Bank believes are critically important for the country was strengthened – and in this connection, the high degree of trust between the Bank and its client played a vital role. In building support for reforms, the Bank should routinely undertake major **AAA work** that underpins DPOs as joint exercises with the government and, whenever possible, give the government the leading role in such exercises. In the case of Armenia, this was done, *inter alia*, for PERs and the PEFA, and this contributed both to the quality of the analysis and the ownership of the results within the government.

3. The PRSC experience also illustrated well the ***long term nature*** of implementation efforts, especially in complex second generation reform areas, the need to re-prioritize in the light of implementation experiences, the need for the Bank to be flexible with policy advice, whilst assisting the government to keep its focus on key PRSP goals. Pragmatic re-programming of steps in customs reforms or in health reforms proved to be necessary and wise. The PRSC proved to be a sound instrument for cross-sector work with the government as well as the Bank. Flexibility should extend to willingness to introduce ***new elements*** when doing so will likely facilitate their implementation. In the case of the Armenian PRSCs, analytical work on corporate governance and on a performance appraisal system, completed after the initial design of the series, gave rise to milestones included in PRSC III and IV. This proved useful in bringing broader attention to these measures across and the government and setting deadlines for implementation. Similarly, the Bank and the government should be flexible and willing to drop measures that no longer seem appropriate.
4. The ***amount of a DPO*** need not be large relative to the fiscal program of the government in order for it to provide a useful vehicle for the dialogue between the Bank and the government and for facilitating implementation of the government's program. In the case of the Armenian PRSCs, they were very useful for these purposes even though the credit amounts were only about 2% of overall government expenditures. Indeed, some Armenian observers of the PRSC process commented that the dialogue related to the PRSC was more "honest and productive" than the previous SAC dialogue simply because the government had much less need for the money. Hence, the amounts of DPOs should be based on judgments about the relative efficacy of this form of budget support versus investment lending by the Bank.
5. The Bank should encourage governments to assume full responsibility for ***M&E*** for DPO outcomes as an integrated part of its overall M&E system. This would enhance the understanding that the DPOs are the government's program, not the Bank's. In the case of the Armenia PRSCs, the Bank did this to some extent but perhaps could have done so more effectively.
6. The timing of DPO appraisals and approvals need to be usefully synchronized with the government's ***budget cycle***. In the case of Armenia, this means appraisal before September, when the government needs to know its likely revenues.

## 7. Comments on Issues Raised by Borrower/Implementing Agencies

The Armenian authorities provided written comments of a factual nature largely to update data, clarify the language in several places and to add explanations in several other places. Bank staff found these comments to be helpful and fully acceptable and have reflected them in the text of the ICR.

## Annex 1: Priority Outcome Indicators<sup>44</sup> as of September 10, 2009

### 1.1 Maintaining macroeconomic stability

Outcome Indicator	Base Year	Expected Outcome	Actual Outcome	Source and Comments
GDP growth	2003: 14.0	Expands 30% 2004-2007 I, II Expands 65% 2004-2010 III	2003 14.0 2007 13.8 2004 10.5 2008 6.8 2005 13.9 2006 13.3	NSS, 2008 preliminary data. Cumulative growth: 2004-07, 62%.
Inflation rate	2003: 8.6	Below 5%	2004 2.0 2007 6.6 2005 -0.2 2008 5.2 2006 5.2	NSS, CPI, eop
Fiscal deficit	2003: -1.3	2009 -7.0 %	2003 -1.3 2006 -1.5 2004 -1.7 2007 -1.5 2005 -1.9 2008 -0.7	MoFE
External debt/GDP	2003: 39.1	2009: 39.1%	2003 39.1 2007 15.8 2004 33.1 2008 13.2 2005 22.4 2009 39.1 2006 18.9	NSS, MoFE Public debt, eop 2008 preliminary 2009 projection

### 1.2 Public administration reforms 1.3 Public Management, and 1.4 Corporate Governance

Outcome Indicator	Base Year	Expected Outcome	Actual Outcome	Source and Comment
Tax revenue/GDP ratio	2003: 14%	2009: 16.4%	2003 14.0 2006 14.5 2004 14.0 2007 16.0 2005 14.4 2008 17.0	MoFE, State Budget (incl. State duties)
Share of taxpayers using self-assessment	2003: None	2007: 25% I 2008: Surveys show indicators of mis-governance in tax administration close to central Europe/Baltic levels: III, IV	See text	
Discretionary	2003:	2007: Reduce by 80% I	See text	

<sup>44</sup> These expected outcome indicators are a combination of those included in Annex III in each of the PRSC Program Documents and those included in the four policy matrices. When expected outcome varied among the four PRSCs, the corresponding target is denoted by I, II, III, or IV to indicate in which PRSC that target appeared.



<b>Outcome Indicator</b>	<b>Base Year</b>	<b>Expected Outcome</b>	<b>Actual Outcome</b>	<b>Source and Comment</b>
customs inspections	100%	2008: Reduce by 80% II 2008: Survey shows mis-governance in customs close to central Europe/Baltic levels III, IV 2008: discretionary inspections reduced to 25% of total IV		
Share of ministries using GFS 2001 budget classifications	2003: none	2007: All	100% (further improvement to bring to international best standard is required)	
Share of ministries with functional internal audit system	2003: Few	2007: 100% I 2008: in pilots II, III, IV	100% (further improvement to bring to international best standard is required)	
Staff performance appraisal system in implementation	2004: none	2007/8: in pilot ministries	The system is being piloted in the Government Staff, Ministry of Economy and Ministry of Finance	
Share of SNCOs in compliance with financial reporting	2003: 20%	2007: 80% accounting for 75% of aggregate income I, II 2008: same III, IV	100% (further improvement to bring to international best standard is required)	
Share of single source open procurement (outside natural monopolies)	2003: 80%	2006: 20% I 2008: 20% II, III, IV	See text	

## 2. Sharpening Competition and Entrenching Property Rights

Outcome Indicator	Base Year	Expected Outcome	Actual Outcome	Source and Comment
Air services (connections, frequency, pricing) approaching European levels	Exclusive rights to the national carrier, high cost of air services	Not quantified	See text	
Railways operating on commercial basis	2003: completely absent	Not quantified	See text	
Quality monitoring system for water sector established and service quality data available	Quality monitoring system non-existent	2008: II, III, IV	Water utilities carry out daily monitoring and results published by PSRC. State anti-epidemic department conducts regular monitoring.	PSRC
Weighted average water supply duration for Yerevan	2003: ~ 9 hours	2008: 18.5 hours	Yerevan 18.7 (2007)	Sustainable Development program report
Weighted average water supply duration AWSC		2008: 5.6 hours	AWSC 2004=6.0, 2005=7.4, 2006=9.6, 2007=11.9	Sustainable Development program report
Electricity service monitoring system functional and data published	2003: 5.07 hours	2008: II, III, IV	Done by PSRC	
Fully liberal regime for telecomm with reliance on competition law	Non-liberal, state controlled telecom system	2008: III, IV	See text	
Commercial bank loans to private sector as share of GDP	2003: 6% I	2007: 10% I 2008: 15% IV 2009: 20% III	2003 6.3% 2006 9.1% 2004 7.3% 2007 13.5% 2005 8.4% 2008 17.4%	Sustainable Development program report, CBA eop
Volume of private sector deposits as a share of GDP	2003: 9% I	2007: 11% I, II, III 2008: 11.5% IV	2003 11.4% 2006 11.6% 2004 12.1% 2007 13.1% 2005 11.8% 2008 12.8%	CBA, eop, Commercial bank deposits
Level of insurance premiums	2003: US\$4.5m	2008: US\$15 m.	2008: US\$15.2 m	CBA

## Annex 2. Matrix of Policy and Institutional Actions and Expected Outcomes

Goals	PRSC1 (Actions Taken)	PRSC2 (Actions Taken)	PRSC3 (Actions Taken)	PRSC4 (Actions Taken)	Outcomes and Impact
<i><b>THEME I: Consolidating Macroeconomic Discipline and Strengthening Governance</b></i>					
<b>1. Maintaining macroeconomic stability.</b>	Falling inflation, fiscal deficits below 2.5 percent of GDP and satisfactory budget for 2005.	In 2005, growth was 14.0 percent; inflation was minus 0.2 percent and the fiscal deficit 2.6 percent of GDP.	In 2006, growth is estimated at 13.4 percent; inflation at 5.2 percent and the fiscal deficit at 1.1 percent of GDP.	In 2007, growth is projected at 11 per cent, inflation at 4 per cent and the fiscal deficit at 2.3 per cent of GDP –continued strong improvement in sustainability.	GDP expands by 58 percent over 2004-08 to \$2200 per head (in 2004 dollars); inflation kept at 3 percent and fiscal deficit in 2-3 percent range. External debt falls to 14.5 percent of GDP.
<b>1.2 Public administration reforms.</b>  <b>(a) Strengthening tax administration.</b>	Submitted to Parliament a Law on Electronic (digital) Signature and Electronic Document.  Adopted a strategy to introduce self-assessment in tax returns.  Adopted a quantitative schedule for reduction of outstanding VAT refund claims to exporters and for reduction of tax arrears.	Law approved and under implementation.  Satisfactory progress made in strengthening the operation of the Large Tax Payers Unit at the State Tax Service, especially in audit, collection, and enforcement.  Outstanding VAT refund claims to exporters and tax arrears reduced in accordance with the	Start implementation of self-assessment systems; adhere to reform plan for the Large Taxpayer Unit.  Continue adherence to good practices on VAT refunds and tax arrears.	Implement self-assessment in tax administration and implement institutional reforms of the large taxpayer units in line with action plan.	Tax to GDP ratio rises from 14 percent in 2003 to 16.3 percent in 2008. Tax evasion substantially reduced. Surveys of business climate show indicators of mis-governance in tax administration to be approaching those in central Europe/Baltics.  Discretionary inspections

Goals	PRSC1 (Actions Taken)	PRSC2 (Actions Taken)	PRSC3 (Actions Taken)	PRSC4 (Actions Taken)	Outcomes and Impact
<p><b>(b) Strengthening customs administration.</b></p>	<p>Adopted decision to introduce a self declaration system at all Customs houses and extend Direct Trader Input (DTI) facilities to importers and custom brokers.</p>	<p>quantitative schedule. Implemented a pilot for access to DTI facilities.</p>	<p>Complete and implement DTI facilities in major customs houses in line with program agreed with IDA.</p>	<p>Implement comprehensive post-release review program to support full scale implementation of direct trader input in customs and develop a guarantee mechanism supporting an approved importer scheme.</p>	<p>reduced to 25 percent of total inspections by 2008. Risk based systems functioning to high international standards.</p>
<p><b>(c) Improving governance in irrigation and drainage.</b></p>	<p>Improved selectivity of customs control based on risk criteria and of green channel; and established a risk management unit.</p> <p>Established a quantitative program for reducing the role of reference prices.</p> <p>Strengthened Post Clearance Audit (PCA) unit.</p> <p>Decision taken to merge state-level</p>	<p>Role of reference prices reduced consistent with WTO undertakings.</p> <p>Further progress made in strengthening PCA unit.</p> <p>Irrigation and drainage merged and functioning satisfactorily.</p>	<p>Complete and implement intelligence-based system based on risk assessment in line with program agreed with IDA.</p>		<p>Duties evasion substantially reduced. Surveys of business climate show that indicators of mis-governance in customs administration approaching those in central Europe/Baltics.</p>

Goals	PRSC1 (Actions Taken)	PRSC2 (Actions Taken)	PRSC3 (Actions Taken)	PRSC4 (Actions Taken)	Outcomes and Impact
	responsibilities for irrigation and drainage within WRMC.				
<b>1.3 Public Management (a) Advancing budget management system and financial reporting.</b>	<p>Approved new budget classifications along GFS 2001 principles.</p> <p>Adopted a strategy to develop internal audit functions within Government.</p>	<p>Developed public sector integrated chart of accounts, accounting and reporting standards.</p> <p>Detailed implementation action plan for internal audit strategy for 2005-2008 developed. New Department for Internal Audit Assessment and Financial Supervision operational.</p>	<p>Satisfactory progress toward ensuring that the 2008 budget fully adheres to GFS classification and chart of accounts.</p> <p>Ensure budget reporting and execution practices in pilot ministries to comply with program budgeting requirements.</p> <p>Prepare strategy to introduce system of staff performance appraisal to support a merit based basic wage and bonus system.</p> <p>Implement agreed actions on internal audit functions.</p> <p>IPSAS Cash Basis Standards for accounting approved and under implementation in line</p>		<p>The state budget from 2008 is prepared and approved in accordance with GFS 2001 classification for all line ministries.</p> <p>Quarterly and annual budget execution reports contain both financial and non-financial performance indicators.</p> <p>Staff performance appraisal system in implementation in pilot ministries.</p> <p>Internal audit system fully functional in pilot ministries.</p> <p>IPSAS cash basis standards implemented in all line ministries.</p> <p>Eighty percent of SNCOs accounting for not less than 75 percent of aggregate income of</p>

Goals	PRSC1 (Actions Taken)	PRSC2 (Actions Taken)	PRSC3 (Actions Taken)	PRSC4 (Actions Taken)	Outcomes and Impact
(b) Improving Public Procurement System.	<p>Implemented financial reporting by state Non-Commercial Organizations (SNCOs).</p> <p>Prepared an action plan and cost estimates for introduction of an electronic procurement system.</p>	<p>Developed strategy to apply sanctions for non-compliance with financial reporting for SNCOs.</p> <p>Prepared catalogues for procuring entities on technical specifications for goods and services of common use and catalogues published on website.</p>	<p>ministries.</p> <p>Make legislative changes to clarify definition of SNCOs and establish an appropriate SNCO reporting framework and consolidated quarterly reports from Min of Finance to Parliament and Chamber of Control, and ensure compliance with the law.</p> <p>Adopt methodological guidelines on appropriate fiduciary controls in SNCOs.</p>		<p>SNCOs in compliance. 2007 onwards State Budget accurately reflecting SNCO allocations.</p> <p>Regular submission of SNCO consolidated reports to Parliament and Chamber of Control.</p> <p>Electronic e-tendering system operational in the public sector. Single source open procurement (outside the natural monopoly sector) reduced to 20 percent.</p>
1.4 Strengthening corporate governance			<p>Corporate Governance ROSC conducted and workshops held.</p> <p>Revised banking law to</p>	<p>Registration law revised to provide for public access to key company records,</p>	<p>Substantially greater information flow to investors leading to gains in confidence in capital</p>

Goals	PRSC1 (Actions Taken)	PRSC2 (Actions Taken)	PRSC3 (Actions Taken)	PRSC4 (Actions Taken)	Outcomes and Impact
			require disclosure of ultimate beneficial shareholders of banks.	including company charters and revised securities law to require public disclosure of ultimate beneficial owners of traded companies.	markets and reduction in risk premium in the cost of raising finance for investment through securities. Market capitalization of quoted companies rise from 0.8 percent of GDP in 2005 to 12 percent of GDP.
<b>THEME II: Sharpening Competition and Entrenching Property Rights</b>					
<b>2.1 Competition</b>  <b>(a) Liberalization in key services.</b>	Decision taken and policy work initiated to widen participation in the provision of international civil aviation services, raise efficiency and cut costs (without prejudice to existing commercial agreements with private carriers). Decision taken to accord managerial and operational autonomy to the railway company, to constitute an independent board, and to reform tariff-setting.	Adopted a policy statement incorporating a more liberal and flexible stance to civil aviation and indicating a simplification of procedures.  Initiated railway company reforms.	Implement a more liberal civil aviation regime in line with policy statement and market potential.  Adopt a railway restructuring plan satisfactory to the Bank that improves commercialization, transparency and accountability and	Sound progress towards meeting the end-2007 target of amending all air service agreements with EU nations to replace "national" airlines with "EU" airlines and with implementation of all actions necessary to signing a new air services agreement with the US, consistent with Armenian legislation.  Adapt the Armenian Table of Frequency	Air services in terms of connections, frequencies and prices improving towards European levels. Policy monitored and improved.  Railways operating on a commercial basis.  Fully liberal regime in operation, with reliance on

Goals	PRSC1 (Actions Taken)	PRSC2 (Actions Taken)	PRSC3 (Actions Taken)	PRSC4 (Actions Taken)	Outcomes and Impact
(b) Regulatory reform in state owned utilities.	Implemented Integrated Financial Rehabilitation Plan (IFRP) for <i>state owned utilities</i> (including energy, irrigation, drinking water companies, and Yerevan Metro), with strengthened corporate governance, creation of electricity market, and cessation of operations of the state electricity wholesale company.	<p>Parliament enacted a new telecommunications law and a modern regulatory framework is being drafted that would allow for progressive licensing of additional service providers.</p> <p>Strengthened utilities regulatory framework: (a) adopted rules for service provision and procedures for monitoring quality in energy and drinking water, (b) performance-monitoring data for</p>	<p>supports private sector participation.</p> <p>Develop telecommunications regulatory policy and time-bound action plan conducive to the maximum possible competition permitted under current commercial arrangements and subsequently, with the arrangement's expiration. Regulation to be in line with international best practice.</p>	<p>Allocations to conform to the International Telecommunications Union Table of Frequency Allocations.</p>	<p>competition law to regulate markets.</p> <p>A functional quality monitoring system for the water sector established and service quality data available to the public.</p> <p>Weighted average water supply duration improved from 18 hours to 18.5 hours (3 percent) for</p>



Goals	PRSC1 (Actions Taken)	PRSC2 (Actions Taken)	PRSC3 (Actions Taken)	PRSC4 (Actions Taken)	Outcomes and Impact
		energy and water sectors published, (c) results of financial performance of PSRC-regulated irrigation companies published (d) adopted power market rules for trade, dispatching, safety of the grid.	Maintain these actions; introduce forms and registers for collection of service quality data for drinking water companies; publish data.  Implement service quality monitoring system in the electricity sector; publish quarterly data; establish baseline service quality indicators, and set minimum service quality standards for frequency and duration of outages.		Yerevan Water Supply Company; and from 5.07 hours to 5.6 hours (10 percent) for Armenia Water Supply Company.  Electricity service quality monitoring system fully functional and data published.
<b>2.2 Entrenching property rights (a) Secured transactions.</b>	Established plan to (i) strengthen creditor rights, (ii) improve civil procedures for debt recovery, and (iii) simplify procedures for certification for property sales and registration of secured credit.  Prepared collateral registry guide and software. Initiated a review of offsite monitoring	Amended civil code and related procedures and regulations on secured credit and streamlined civil court procedures and court decision enforcement.  Action plan to implement FSAP recommendations prepared.	Sustain improvements in secured transactions conditions.  Implement the unified supervision regime in banking sector.		Commercial bank loans to private sector increase from 6 percent of GDP in 2003 to 15 percent of GDP by 2008.  Volume of private sector deposits rises from 9 percent of GDP in 2003 to

Goals	PRSC1 (Actions Taken)	PRSC2 (Actions Taken)	PRSC3 (Actions Taken)	PRSC4 (Actions Taken)	Outcomes and Impact
(b) Confidence in the banking system.	systems and on site supervision systems, procedures and practices.	Approved draft amendments to law on banks and banking which include regulations to improve corporate governance for banks in consultation with commercial banks.			11.5 percent of GDP in 2008.
(c) Insurance markets.	Developed prudential standards, acceptable to IDA, in line with the new law on insurance and set minimum capital requirements for insurance companies at AMD 100 Million.	Adopted prudential regulations and reporting forms and guidelines for insurance companies.	Establish: (i) an independent inspectorate, (ii) increase the minimum capital requirement for companies to AMD 350 Million and (iii) establish an appropriate actuarial system.		Level of premiums increases from US\$4.5 million in 2003 to US\$15 million in 2008.
<b>THEME III: Mitigating Social and Environmental Risks</b>					
<b>3.1 Improving social protection and social risk management.</b>	Introduced differentiation of benefits within the family poverty benefit.	Effectiveness of the family poverty benefit, (including the targeting formula) evaluated based on 2004 data and corresponding policy changes made.			At least 70 percent of poor households receive family poverty benefit.  Leakage of resources allocated to the poverty benefit (i.e. diversion to

Goals	PRSC1 (Actions Taken)	PRSC2 (Actions Taken)	PRSC3 (Actions Taken)	PRSC4 (Actions Taken)	Outcomes and Impact
	Implemented Public Pensions Law in accordance with timeline.	Developed draft law on private pension insurance and action plan on supervisory and regulatory capacity for private pension services.	Design reform of pensions system under a multi-pillar framework and placed pension supervision within the unified supervision institution.		non-poor) falls from 27 percent in 2003 to 25 percent from 2007 onwards.  Diversified system designed and agreed on. An action plan for its implementation in place and its implementation launched.
<b>3.2 Raising the quality of education.</b>	Made satisfactory progress in the school rationalization program, raising the ratio of pupils to full-time equivalent teachers to 13.8 and raising 2005 teacher salaries by 65 percent.  Initiated policy formulation on early childhood education (ECE) with wide	Continued satisfactory progress on school rationalization program and teacher salaries raised by 16 percent.  Adopted a 3-year implementation plan for tertiary education, including sustainable financing and piloting.  Strategy and supporting new law on ECE adopted,	Continue improvements in system efficiency through a) consolidating high schools; b) reviewing the per capita financing formula; c) raising the ratio of pupils to full-time equivalent teachers to 16:1 (excluding small schools protected by GoA); and d) raising teacher salaries by a further 19.5 percent.  Begin implementation of higher education		Public spending on general education continues to increase over the PRSC period to reach 2.0 percent of GDP by 2008 from 1.4 percent in 2003.  Implementation of course credit system commenced

Goals	PRSC1 (Actions Taken)	PRSC2 (Actions Taken)	PRSC3 (Actions Taken)	PRSC4 (Actions Taken)	Outcomes and Impact
	participation.	standards developed and designs for piloting strategy in two communities developed.	reforms, including sustainable financing and piloting, and then expand the course credit system.  Approve “Strategy of ECD and Pre-school Education for 2007-2010” and standards for ECE institutional services.  Approve and start implementation of the “Pilot Project in two regions for introduction of the Strategy and piloting of the ECE standards.”		in at least two state run universities.  The proportion of children participating in pre-school institutions and the proportion of those from the poorest quintile of families increased from 16% and 19% respectively in 2003 to 30% and 50% in 2009.  .
<b>3.3 Controlling risks in health.</b>	Adopted an action plan on hospital governance.  Undertook measures for secured financing and management of Primary Health Care departments of polyclinics that are included in the hospital networks.	Satisfactory progress made in hospital rationalization program.  Prepared draft options for private insurance to cover certain health risks and/or population pools.	Adhere to the rationalization program in the hospital sector as measured by target bed ratio and physician ratio.  Adopt policies to define the scope of publicly-funded healthcare services and define a regulatory		Infant mortality rate to decline from 12 per 1000 live births in 2003 to approach mean OECD levels or MDGs. Maternal mortality rate to decline from 18 per 100,000 live births in 2003 to approach mean OECD levels or MDGs.  Utilization rate of hospital and PHC by bottom two

Goals	PRSC1 (Actions Taken)	PRSC2 (Actions Taken)	PRSC3 (Actions Taken)	PRSC4 (Actions Taken)	Outcomes and Impact
		Prepared a draft program on the prevention and control of non-communicable diseases (NCDs).	framework for voluntary health insurance. Begin implementing the program on the prevention and control of NCDs.		quintiles to rise from 22 percent in 2003 to 30 percent in 2008.  A gradual increase in the funding for and utilization of preventive services for the control of NCDs (e.g., tobacco control, mammography, high blood pressure, diabetes, pap smear).
<b>3.4 Reducing risks in natural resource management for sustainable livelihoods</b>	<p>Adopted a schedule for strengthened Environmental Impact Assessment and Supervision.</p> <p>Adopted a National Forestry Policy satisfactory to IDA.</p> <p>Adopted a National Action Plan to combat illegal logging.</p>	<p>Submitted forest code to Parliament and satisfactory progress made in developing the restructuring plan for the forest company.</p> <p>Established system for monitoring of (i) illegal logging and (ii) forest removal/exploitation.</p> <p>Developed supporting regulations on forest management planning and community forest management.</p>	Developed plan for implementation of the illegal monitoring system.	Implement the illegal logging monitoring system with autonomy built into the operations of the monitoring institution.	Illegal logging is monitored and controlled on all forest in Armenia through an autonomous and effective monitoring institution.

Goals	PRSC1 (Actions Taken)	PRSC2 (Actions Taken)	PRSC3 (Actions Taken)	PRSC4 (Actions Taken)	Outcomes and Impact
<b>THEME IV: Modernizing the Rural Economy</b>					
<b>4.1 Stimulating farm incomes.</b>	<p>Task force established to develop plan to (a) strengthen applied research and agriculture extension delivery system, (b) improve the links and information transfers between research and extension services, (c) augment the role of private advisory services and (d) make viable the official extension system.</p> <p>Government submitted seeds law to Parliament.</p> <p>Task force formed to develop action plan for (a) harmonizing food safety and phytosanitary standards with relevant chapters of the Codex Alimentarius and (b) to stimulate the use of internationally recognized certificates of conformance (e.g., with ISO 1700 standards).</p>	<p>Framework for agricultural extension, research and education adopted.</p> <p>Approved seeds law, seeds certification procedures adopted. Action plan developed for harmonization of legislation and developing standards; established working group to implement action plan.</p>	<p>Satisfactory progress with implementation of the plan.</p> <p>Seeds law and seeds certification procedures fully in force. Harmonize food safety legislation with EU directives; adopt new food safety law; establish clear timeline for adoption of supporting regulations.</p>		<p>Percentage of farmer respondents accessing advisory services and using recommended practices to increase from 29 percent in 2004 to 45 percent in 2008.</p> <p>Cost recovery by Marz Agricultural Support Centers rises from 5 percent in 2003 to on average 14 percent in 2007. The cost recovery is expected to reach 30 percent in 2008.</p> <p>Share of certified seeds sold to farmers rises from nil in 2003 to 30 percent in 2008.</p> <p>Share of agricultural products being tested and certified rises from nil in 2003 to 13 percent in 2008.</p>
<b>4.2 Developing Rural Infrastructure</b>	<p>Completed a diagnostic study on a set of rural infrastructure services (drinking water, roads, gas, electricity,</p>	<p>Established inter-ministerial working group and begun implementation of a</p>	<p>Implement rural infrastructure action plan that encompasses: (i) classification of</p>		<p>Share of rural households with gas rises by 50 percent over 2005 figure.</p>

Goals	PRSC1 (Actions Taken)	PRSC2 (Actions Taken)	PRSC3 (Actions Taken)	PRSC4 (Actions Taken)	Outcomes and Impact
	and telecommunication).	time-bound action plan of reforms in rural roads, water, energy and telecom sectors that encompass universal access, clarify ownership and pave the way for private-public partnerships.  Public Service Regulatory Commission (PSRC) developed quality standards for rural infrastructure services and mechanisms for monitoring their quality.	communities according to clearly defined criteria; (ii) definition of the universal access concept and development of an adequate financing mechanism; (iii) delineation of ownership and operational responsibilities; and (iv) introduction of simplified standards and new technologies. Fully apply PSRC standards.		Share of local and republic roads serving rural Armenia needing reconstruction reduced from 65 percent in 2003 to below 50 percent.

### Annex 3: Bank Lending and Implementation Support/Supervision Processes

#### (a) Task Team members

Names	Title	Unit
<b>Lending</b>		
Saumya Mitra	Lead Economist	ECSPE
Gohar Gyulumyan	Economist	ECSPE
Karen Grigorian	Sr. Economist	ECSPF
Matin Kholmatov	Consultant	ECSPE
Mohammad Reza Ghasimi	Sr. Economist	ECSPE
<b>Supervision</b>		
Adriana Damianova	Lead Environmental Specialist	ECSS3
Afsaneh Sedghi	Economist	ECSPE
Aghassi Mkrtchyan	Economist	ECSPE
Aleksandra Posarac	Lead Human Development Economist	HDNSP
Andrina A. Ambrose-Gardiner	Senior Operations Officer	OPCCS
Ani Balabanyan	Operations Officer	ECSSD
Anthony Cholst	Lead Country Officer	ECCU3
Aristomene Varoudakis	Country Manager	ECCAR
Arman Vatyan	Sr. Financial Mgmt. Specialist	ECSPS
Artavazd Hakobian	Operations Officer	ECSSD
Arusyak Alaverdyan	Operations Officer	ECSS1
Asita De Silva	Sr. Evaluation Officer	CEXEG
Bartek Kaminski	Consultant	ECSPE
Christian Petersen	Lead Economist	ECSPE
Craig Jenks	Consultant	ECSPE
Davit Melikyan	Public Sector Mgmt. Specialist	ECSPE
Douglas R. Andrew	Consultant	ECSPE
Ekaterina Vashakmadze	Sr. Economist	ECSPE
Eluned Roberts-Schweitzer	Sr. Education Specialist	ECSH2
Enis Baris	Sr. Public Health Specialist	MNSHD
Frauke Jungbluth	Senior Rural Development Economist	AFTEN
Gayane Minasyan	Environmental Econ.	EASER
Gerard McLinden	Sr. Trade Facilitation Specialist	PRMTR
Gevorg Sargsyan	Sr. Infrastructure Specialist	SASDE
Giuseppe Fantozzi	Sr. Operations Officer	ECSS1
Harold Bedoya	Operations Officer	AFRVP
Hormoz Aghdaey	Lead Financial Sector Specialist	EASFP
Irina Tratch	Consultant	ECSPE
Jean-Charles De Daruvar	Sr. Counsel	LEGEM
Juan Manuel Moreno	Sr. Education Specialist	MNSHD
Junko Funahashi	Sr. Counsel	LEGCF
Kathy Lalazarian	Sr. Public Sector Specialist	ECSPE
Martha Lawrence	Sr. Transport Specialist	ECSS5
Matin Kholmatov	Consultant	ECSPE
Matthew Andrews	Economist	ECSPE
Michel Zarnowiecki	Consultant	ECSPS
Munawer Khwaja	Sr. Public Sector Specialist	ECSPE



Names	Title	Unit
Naira Melkumyan	Sr. Operations Officer	ECCAR
Nvard Manasian	Education Specialist	ECSH2
Oliver Le Ber	Lead Transport Specialist	MNSTR
Panagiota Panopoulou	Health Specialist	ECSH2
Paul Holden	Consultant	ECSPE
Peter Nicholas	Sr. Country Officer	ECCU3
Ramin Shojai	Sr. Private Sector Development	ECSPF
Roger Robinson	Country Manager	ECCKG
Richard Burcroff	Consultant	MNSSD
Sarosh Sattar	Sr. Economist	ECSP3
Sue Rutledge	R. Private Sector Development Specialist	ECSPF
Susanna Hayrapetyan	Sr. Health Specialist	ECSHD
Toby Linden	Sr. Education Specialist	ECSHD
Toomas Palu	Lead Health Specialist	EASHH
Vahram Stepanyan	Economist	ECSPE

**(b) Staff Time and Cost**

<b>P078673 - Poverty Reduction Support Credit (PRSC)</b>		
Stage	Staff Time and Cost (Bank Budget Only)	
	No. of staff weeks	USD Thousands (including travel and consultant costs)
<b>Lending</b>		
FY04	35	252.08
FY05	71	348.69
FY06		0.00
<b>Total:</b>	106	600.77
<b>Supervision</b>		
FY04		0.00
FY05	15	65.63
FY06	25	57.64
<b>Total:</b>	40	123.27

<b>P093459 - Second Poverty Reduction Support Credit</b>		
Stage	Staff Time and Cost (Bank Budget Only)	
	No. of staff weeks	USD Thousands (including travel and consultant costs)
<b>Lending</b>		
FY05	27	198.66
FY06	48	294.23
FY07		0.00
<b>Total:</b>	75	492.89
<b>Supervision</b>		
FY05		0.00
FY06	5	18.13
FY07	6	7.83
<b>Total:</b>	11	25.96

<b>P093460 - PRSC3</b>		
Stage	Staff Time and Cost (Bank Budget Only)	
	No. of staff weeks	USD Thousands (including travel and consultant costs)
<b>Lending</b>		
FY06	20	148.35
FY07	48	300.46
<b>Total:</b>	68	448.81
<b>Supervision</b>		
<b>Total:</b>		0.00

<b>P101486 - Fourth Poverty Reduction Support Credit</b>		
Stage	Staff Time and Cost (Bank Budget Only)	
	No. of staff weeks	USD Thousands (including travel and consultant costs)
<b>Lending</b>		
FY07	58	263.25
FY08	60	273.65
<b>Total:</b>	118	536.90
<b>Supervision</b>		
FY07		0.00
FY08	3	65.30
FY09		56.70
<b>Total:</b>	3	122.00

#### **Annex 4. Summary of Borrower's ICR and/or Comments on Draft ICR**

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No. 12.1-31374809

Date: 06.07.09

THE WORLD BANK YEREVAN OFFICE

In respect of the draft Report on Progress and Outcomes of Poverty Reduction Support Credit Programs presented to the Ministry of Finance of the Republic of Armenia on June 16, 2009, we would like to note that some of the macro-economic indicators reflected therein, namely, indicators on private sector lending by commercial banks, and deposits, need to be adjusted (Annex 1).

Sincerely,

T. DAVTYAN (signature)

## **Annex 5. List of Supporting Documents**

### **Internal World Bank Documents**

Armenia PRSC I: Concluding Notes of Identification Mission, April 14, 2004.  
Armenia PRSC I: Armenia Fiscal Review Mission, May 17, 2004.  
Armenia PRSC I: Concluding Notes of Pre-Appraisal Mission, June 25, 2004.  
Armenia PRSC I: Concluding Notes of the PRSC Review Mission, December 1, 2004.  
Armenia PRSC I: Concluding Notes of the Mission, February 3, 2005.  
Armenia PRSC II: Concluding Notes of the Pre-Appraisal Mission, September 15, 2005.  
Armenia PRSC II: Concluding Notes of Appraisal Mission, November 18, 2005.  
Armenia PRSC II: Concluding Notes of the Review Mission, February 14, 2006.  
Armenia PRSC III: Concluding Notes of the Mission, April 13, 2006.  
Armenia PRSC III: Concluding Notes of the Mission (Custom Reforms), May 18, 2006.  
Armenia PRSC III: Concluding Notes on Custom Reforms: Briefing Note for the Armenian President's Office, May 23, 2006.  
Armenia PRSC III: Concluding Notes of the Mission, July 12, 2006.  
Armenia PRSC III: Concluding Notes of the Mission, September 29, 2006.  
Armenia PRSC IV: Mission Concluding Note, August 1, 2007.  
Armenia PRSC IV: Concluding Statement of the Economic Mission, May 2, 2008.

### **Publicly Available World Bank Documents Related to this Report**

Program Document for A Proposed First Poverty Reduction Support Credit In the Amount of SDR 13.7 Million (US\$20 Million Equivalent) to the Republic of Armenia, October 2004.

Program Document for A Proposed Second Poverty Reduction Support Credit In the Amount of SDR 14.1 Million (US\$20 Million Equivalent) to the Republic of Armenia, December 2005.

Program Document for A Proposed Third Poverty Reduction Support Credit In the Amount of SDR 18.7 Million (US\$28 Million Equivalent) to the Republic of Armenia, February 2007.

Program Document for A Proposed Fourth Poverty Reduction Support Credit In the Amount of SDR 12.0 Million (US\$18.5 Million Equivalent) to the Republic of Armenia, October 2007.

### **Other World Bank Reports**

The Caucasian Tiger: Sustaining Economic Growth in Armenia, 2007.  
Armenia: Choices in Development Policy, in two Volumes, June 2008.  
Armenia: Poverty Assessment, in three Volumes, November 2003.  
Armenia: Poverty Assessment TA, June 2004.  
Armenia: Programmatic Poverty Assessment, May 2005.  
Armenia: Programmatic Poverty Assessment – Policy Note, March 2006.  
Armenia: Poverty Assessment, June 2008.  
Armenia: Programmatic Public Expenditure Report, June 2005.  
Armenia: Programmatic Public Expenditure Report, May 2007.  
Armenia: Programmatic Public Expenditure Report (series 4), June 2008.