CONTEXT AND RECENT DEVELOPMENTS

1. **Prime Minister Pashinyan's party won the June 20 elections, lifting much of the political uncertainty seen after the ceasefire, but the geopolitical situation remains tense.** The PM's Party secured two-thirds of parliamentary seats, and the new cabinet was appointed in mid-August. The cabinet quickly formulated a new economic program, which was approved by parliament on August 27 (Box 1). The security situation has improved considerably since the ceasefire in November 2020 and the deployment of Russian peacekeepers in Nagorno-Karabakh. Yet, geopolitical tensions fester over the exchange of prisoners, road blockages, and border demarcation. While discussions over these topics and an easing of restrictions on regional transportation are ongoing, there is uncertainty over their prospects.

Box 1. Summary of the 2021–26 Government Program

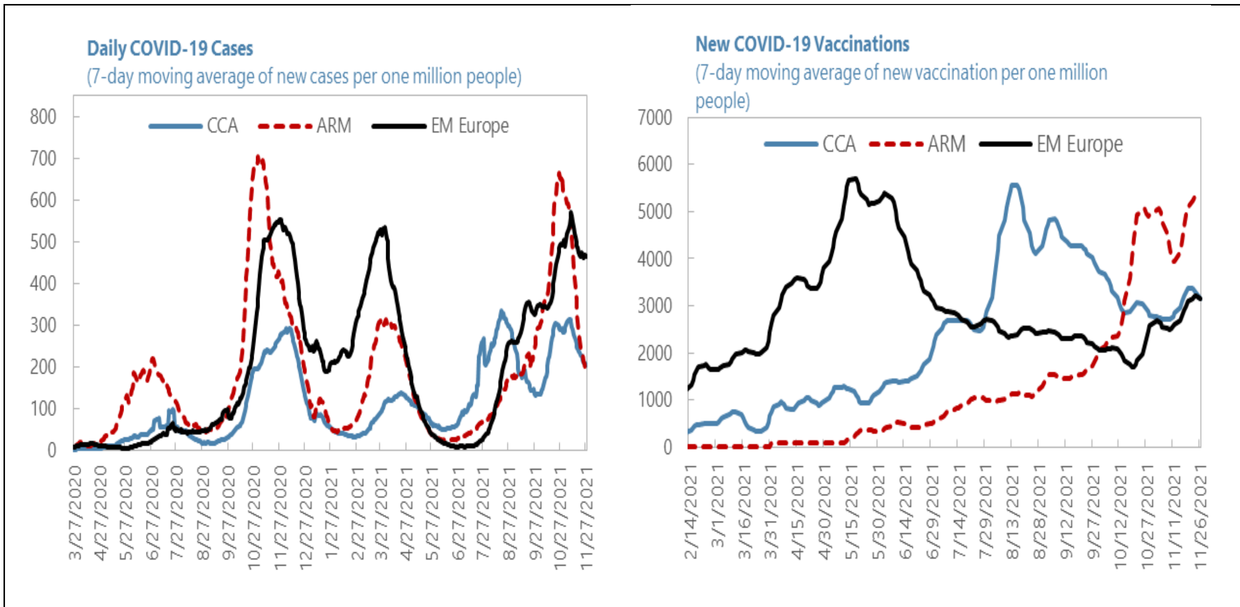
The government's five-year program seeks to advance a knowledge-based, export-oriented, investment-driven growth model, aimed at reducing poverty (Annex V). It anticipates growth in the range of 7–9 percent, with productivity growing at 5 percent a year, investment reaching 25 percent of GDP (with a higher share of FDI) and the unemployment rate falling to 10 percent. The program envisages support to SMEs and increase their share to over half of GDP, pensions to be increased to cover minimum consumption needs, and a 25 percent increase in the minimum wage.

While some of these targets are perhaps overly optimistic for a 5-year plan, the program's structural reform agenda revolves around some important priorities:

- Infrastructure development aimed at improved connectivity, water management, and green energy. SME support, land reforms, and digitalization aiming to expand economic opportunities.
- Stronger trade links, with more diversified export basket, markets, and higher tourism.
- Human capital development, enhanced flexibility in employer-employee relationships, greater social assistance targeting, and increased female labor force participation (childcare support).
- Capital market development.
- Improved corporate governance as well as judicial and anti-corruption reforms.
- Public administration reforms to improve service delivery.

To support their structural agenda, the government aims to **create space through growth-friendly revenue-enhancing tax policies, spending prioritization, and higher quality investment.** It has committed to medium-term sustainability and full compliance with fiscal rules.

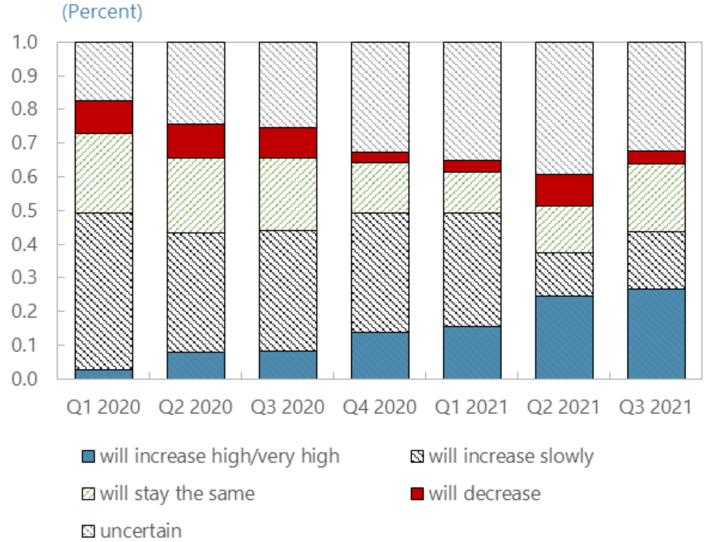
2. **COVID cases remain elevated, but vaccination efforts are accelerating**. The country is experiencing a fourth wave of infections with high numbers of fatalities. While the seven-day case average is trending downward, it remains high (currently with a 7-day average around 539, 18 cases per 100,000 people). Meanwhile, the pace of vaccination has accelerated, with around 11 percent of Armenia's population fully vaccinated and 25 percent having received their first dose as of November 21, 2021. The government is managing the situation through administrative measures including masking, testing and vaccination mandates. With 1.88 million complete vaccine doses procured or contracted, Armenia has sufficient supply to cover all adults and around 63 percent of the population, and an Armenian pharmaceutical firm has been licensed to produce the Sputnik V vaccine domestically.



Source: Haver, Oxford University.

3. A strong recovery is underway with inflation pressures persisting. After GDP contracted by 7.4 percent in 2020, activity has rebounded strongly this year, with growth of almost 5 percent in 2021H1, although poverty and unemployment remain elevated. This recovery reflects strong construction, trade, and service activity and significant base effects. Inflation accelerated to 9.1 percent in October, reflecting pent-up consumption, domestic supply constraints, external food inflation, as well as pressures from global supply chain disruptions. While there have been many drivers, and prices have risen across the most categories (services being an exception), imported prices have been a major impulse since the beginning of the year (Box 2). The CBA's most recent inflation expectations survey suggests that expectations show some tentative signs of stabilization, while the ongoing strengthening of the dram and low level of inflation in some categories (notably services) seem consistent with relatively stable expectations.[1]

Inflation expectations since COVID-19
(Percent)



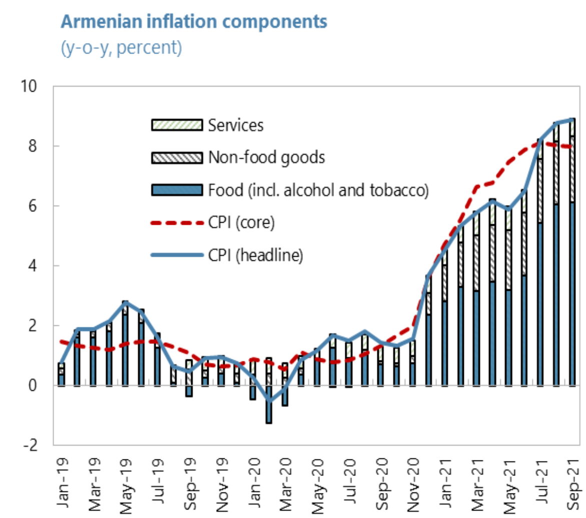
Source: National Authorities and IMF staff calculations.

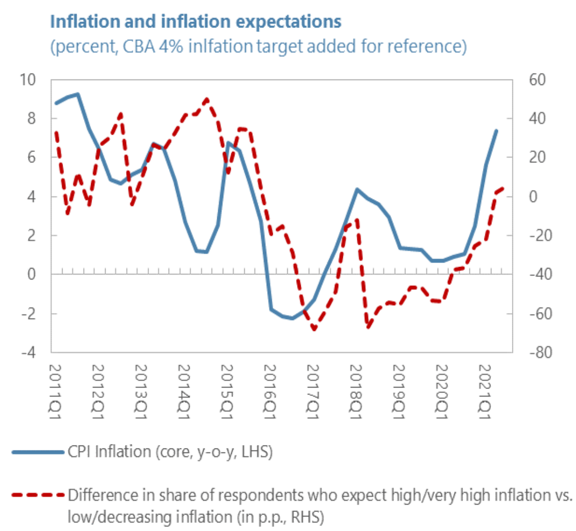
[1] An improved survey methodology, aimed at better gauging the perceived and expected numerical level of inflation expectations, is currently under development by the CBA.

Box 2. Inflation Drivers in Armenia

The recent uptick in inflation has primarily been driven by a rise in import prices, reflecting global supply chain disruptions and higher commodity prices. While inflation expectations increased in the first half of 2021 and become more dispersed, they have not significantly contributed to the recent rise in inflation.

After years of remaining subdued and below-target, inflation has picked up strongly in recent months. Beyond a base effect, a mix of external and domestic factors has contributed to this rise. A composite measure of the qualitative expectation based on answers to the CBA survey—calculated as the difference in the share of respondents who expect high or very high inflation and those that expect low or decreasing inflation over the next 12 months—indicates a close co-movement with recent trends in actual inflation and a moderation in recent months.

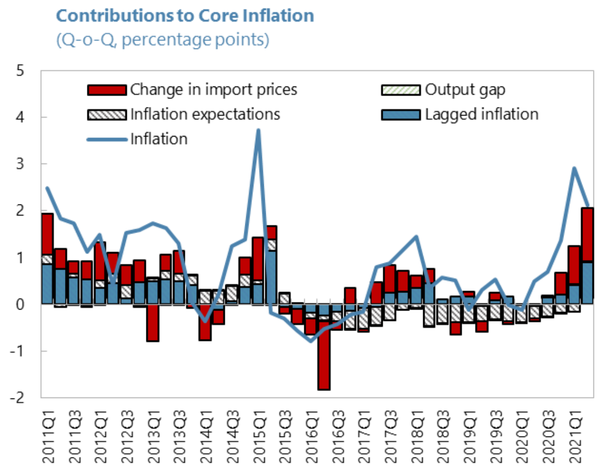


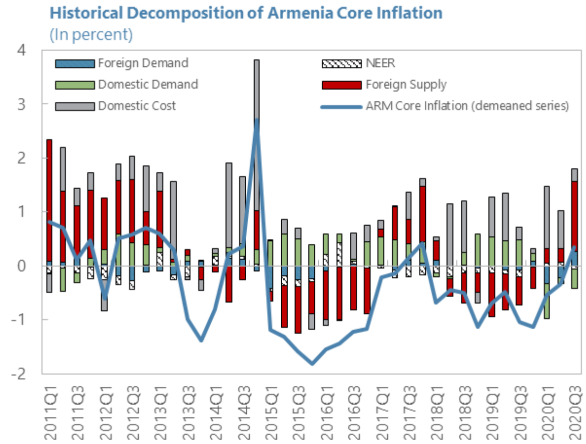


Source: National Authorities and IMF staff estimates

An econometric analysis suggests that import prices (including through the exchange rate) are a key driver of the recent rise in inflation. To better understand the role of various inflationary drivers, we estimate a reduced-form Phillips curve for Armenia (Annex VI).[1] The results (LHS chart below) indicate a strong role for lagged inflation (coefficient of 0.31), attesting to the inertia in price dynamics, as well as changes in import prices (coefficient of 0.21). These two factors account for most of the large increase in overall core inflation seen since 2020Q4. While inflation expectations have played a role in the past, they do not currently show up as empirically important. The domestic output gap appears to play a more limited role in driving core inflation.

An alternative decomposition of core inflation, using a structural vector autoregression (VAR) methodology, highlights the importance of foreign supply and domestic cost shocks as well as some emerging influence from domestic demand shock for current inflation. This structural VAR approach decomposes the movements of Armenian core inflation into the effects from foreign demand, foreign supply, exchange rate (NEER), domestic cost, and domestic demand (Annex VI). This analysis (RHS chart below) also suggests that foreign cost pressures play a major role in recent inflation.

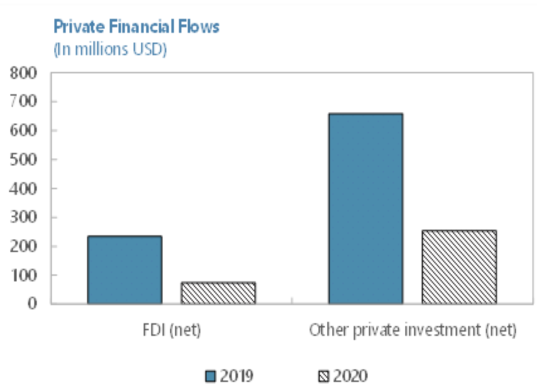


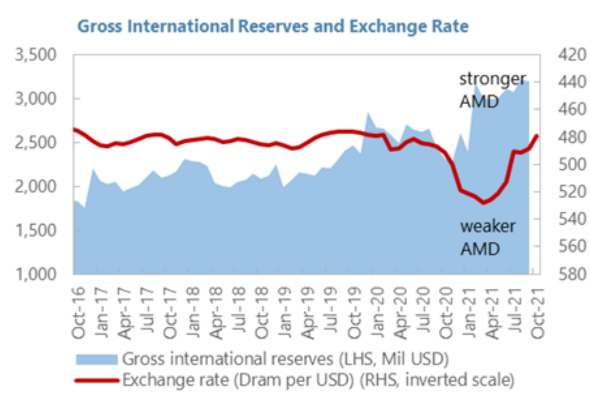


Sources: Haver, National Authorities, IMF World Economic Outlook, IMF International Financial Statistics and IMF staff estimates.

1/ The approach follows Chapter 2 from the October 2021 WEO, adapted for Armenia.

4. External pressures have gradually eased. Although tourism receipts and remittances declined sharply during the pandemic, the 2020 current account deficit narrowed to 3.8 percent of GDP, principally reflecting import compression. At the same time private financial inflows declined by around $550 million placing pressure on the dram and gross reserves. The dram depreciated by 10 percent against the US dollar (at its trough) between the outbreak of the military conflict in late-September and the general elections in June 2021. Since then, external conditions have become more favorable, and the dram has appreciated beyond pre-conflict levels. Remittances and exports have also recovered robustly in 2021, with the current account deficit projected to remain modest given the strength of the recent export recovery (the deficit was 2.2 percent of GDP in 2021H1). At $3,201 million (about 143 percent of the ARA metric), end-October reserves were adequate and, using the current account approach, the external position for 2020 is assessed as broadly consistent with fundamentals and desirable policies (Annex III).





Sources: National authorities, Haver, and IMF staff calculations.

5. The headline fiscal deficit widened to 5.4 percent of GDP in 2020, reflecting economic support measures and increased health spending, but has fallen in 2021.[2] Tax collection and social contributions relative to GDP held-up in 2020. Capital expenditure increased by around ¾ ppts to 3¾ percent of GDP, while current spending—including health (0.5 percent of GDP) and economic and social support measures (0.7 percent of GDP)—increased to 27 percent of GDP. Central government debt reached 63½ percent of GDP by end-2020. Preliminary 2021H1 data point to a deficit around 1½ ppts smaller than program target. This reduction reflects stronger revenue collection on the back of higher-than-expected growth, with nominal spending remaining at its programmed level so far.

Anti-crisis Support 2020, in billions of AMD and (percent of GDP)

	Above-the-line		Below-the-line		Commerical Bank Support	
Liquidity Provision to Business	9.2	*(0.1%)*	15.4	*(0.2%)*	157.5	*(2.5%)*
Direct Labor Subsidies	16.0	*(0.3%)*	0.0	*(0.0%)*		*(0.0%)*
Lump sum transfers to vulnerable individuals	17.2	*(0.3%)*	0.2	*(0.0%)*		*(0.0%)*
Utility Support	4.8	*(0.1%)*	0.0	*(0.0%)*		*(0.0%)*
Transfer to families	7.4	*(0.1%)*	0.0	*(0.0%)*		*(0.0%)*
Transfer to the unemployed or workers heavily affected by the pandemic	4.3	*(0.1%)*	0.0	*(0.0%)*		*(0.0%)*
Educational support	0.8	*(0.0%)*	0.2	*(0.0%)*		*(0.0%)*
Total	42.4	*(0.7%)*	15.6	*(0.3%)*	157.5	*(2.5%)*
COVID-19 related Heath Spending	31.8	*(0.5%)*				

Source: *National authorities, and IMF staff calculations. Note: "Commercial bank support" corresponds to commercial loans supported by the interest subsidies included in the government liquidity support to businesses.*

6. Conditions across domestic banks have deteriorated during the pandemic but there are solid signs of recovery. FSIs deteriorated somewhat during 2020 and 2021Q1, showing tighter liquidity, weaker profitability, and deteriorating asset quality. Since May these trends have reversed, with most FSIs improving towards their pre-COVID level (Table 5). Bank capital remains well above the 12 percent minimum capital adequacy ratio (CAR), liquidity is ample, dollarization is declining, and NPLs have since fallen from their 7.4 percent February peak to 5.1 percent in September.[3] Notwithstanding the deep recession, credit expanded by about 14.3 percent in 2020, principally reflecting demand for mortgage and consumer credit, although credit growth has reversed in 2021 as banks have become more conservative due to heightened economic uncertainty with loans declining by 6.7 percent in September (e-o-p). Deposits increased by about 4 percent in 2020 and 3.9 percent (e-o-p) through September 2021, with rising resident deposits offsetting declining nonresident deposits.

[2] The government has been closely monitoring the implementation of COVID-related spending programs and regularly publishes a list of beneficiaries receiving support under these measures. See link on support programs to address the economic impact of COVID-19 and link on support programs to address the social impact of COVID-19. The authorities reiterated their (Second Review) commitment to conduct an ex-post audit by mid-2023 of their COVID-19 on-lending business support scheme and publish the results. Also, the authorities publish crisis-related procurement contracts—including information on the companies awarded contracts and their beneficial owners (see link).

[3] In July, the Central Bank of Armenia aligned the NPL definition with the BCBS regulation identified in the 2019 FSAP recommendation. The new NPL definition only considers exposures more than 90 days past due (doubtful and substandard loans). On this definition, September NPLs are 2.9 percent of loans.

OUTLOOK AND RISKS

7. The economic recovery is projected to strengthen through 2021 and 2022 and taper off to its potential growth rate thereafter, although significant uncertainty remains.

- *Near-term growth* of around 5½ and 5¼ percent is expected in 2021 and 2022, respectively, with nominal GDP expected to surpass its 2019 level this year, although the output gap is only expected to close in 2022.

- *Inflation* is expected to moderate to 8.5 percent by end-2021 and around 5.5 percent by end-2022, as the temporary impact of imported food inflation and supply disruption dissipate. Provided the recent upward price pressures do not feed into higher expectations (Box 2), inflation is expected to gradually converge to the CBA target of 4 percent over the medium term.

- As elaborated below (¶14), *medium-term (MT) growth* is likely to fall in the 4½–5 percent range depending on the authorities' implementation of their reform program.

- *External position*. Despite the recovery in domestic activity, robust exports—which reflect higher commodity prices and remittances—are expected to narrow the current account deficit in 2021 further to 2.1 percent of GDP. In the meantime, private capital inflows are expected to remain weak. NIR at end-2021 is projected to fall short of the level projected at the Third Review, reflecting higher than expected government conversions, and would decline modestly through early 2022 given elevated near-term external debt service (December 2021 QPC proposed accordingly). However, end-2021 gross reserves are projected at about $3,101 million (138 percent of ARA metric) up from $2,616 million at end-2020, reflecting the successful 10-year Euro bonds issuance ($750 million) in January, some buy-side intervention, and the SDR allocation (about $175 million) in August.

8. Risks to the outlook are relatively balanced, although uncertainty remains high (Annex II). The June elections lifted much of the political uncertainty hanging over Armenia since late-2020, creating upside risks, including by providing a renewed focus on infrastructure investment and reinvigorating the government's reform agenda under its 2021-26 program. Vaccination efforts have also been accelerated. However, with the vaccination rate still low, a prolonged wave of infections or new COVID-19 variants could hamper the recovery through lower mobility and external demand. Risks that inflation will remain high are non-negligible, particularly if global commodity prices and supply chain disruptions continue to exert upwards pressure on prices. Additional near-term risks include renewed regional tensions (notably with Azerbaijan over their border), a slowdown in major trading partners, and stress from global financial volatility and/or trade tensions.

Authorities' Views

9. The authorities broadly agreed with the staff's assessment of near-term outlook but are optimistic about medium-term growth given their new economic program. They expect growth of 6½ percent in 2021 and 7 percent in 2022 and over the medium term. They argue that the quarantine measures are less restrictive than those applied in 2020 and that consumption demand will be

maintained. The CBA expects inflation to remain elevated in the first half of 2022 and to converge to the 4 percent target, partly due to base effects and as temporary supply factors ease by the end of 2022. They see risks to the economic outlook as broadly balanced and shared concerns about renewed virus resurgence and noted that they have secured sufficient vaccines to cover almost all of adult population.

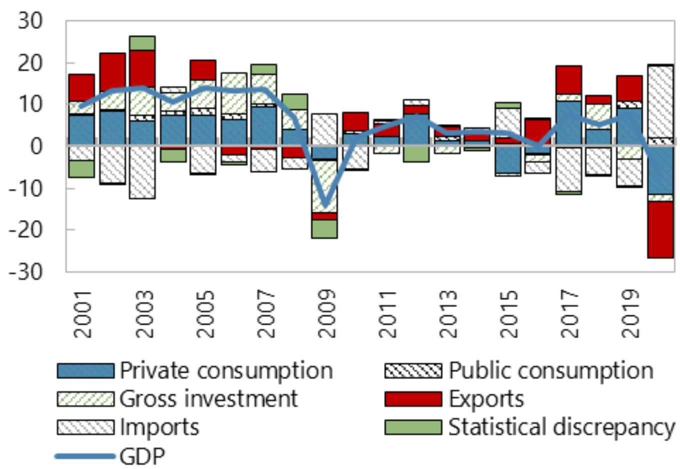
POLICY DISCUSSIONS

Discussions focused on both near-term policies under the program as well as policies to improve medium-term prospects. Near-term discussions addressed (i) balancing fiscal support with MT sustainability; (ii) monetary policy to manage inflation; and (iii) the maintenance of financial stability. Medium-term discussions considered three interconnected agendas: (i) boosting export-led growth; (ii) attracting greater FDI while strengthening financial development; and (iii) fostering inclusion and enhanced governance and anti-corruption.

A. Rebalancing the Armenian Growth Model

10. Although Armenia successfully navigated two difficult shocks in 2020–21, it needs to reinvigorate its growth model. Over the past two decades, the quality (sophistication, complexity, and value-added) of Armenia's exports has declined, and there has been a shift from FDI towards external debt-based financing. At the same time, growth has been largely driven by consumption and non-tradeables. Until the global financial crisis (GFC) in 2008, growth was principally driven by private consumption and investment, where the latter was mostly channeled to residential construction, providing limited support for potential growth. In the post-GFC period, services, agriculture, mining, and industry became the drivers of slower, but generally more balanced, growth. On the demand side, net exports contributions generally turned positive during this period. Yet two-thirds of the average annual 4.5 percent growth over 2010-19 came from private consumption. Given the small size of its domestic market, there are limits to sustainable growth from focusing on non-tradable activity. Thus, to sustainably raise Armenia's growth rate there will be a need to rebalance its economy from

Growth Decomposition by Expenditure
(Percentage points)

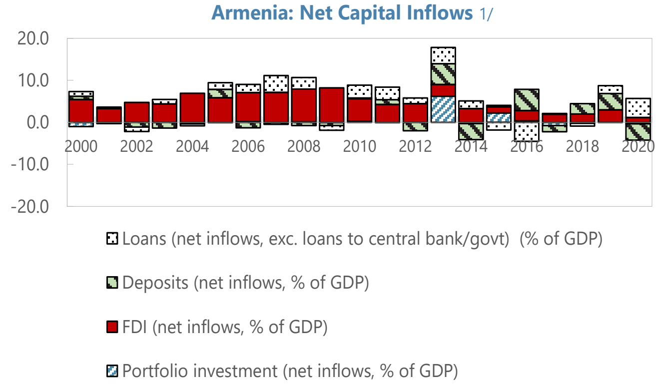


Source: Armstat and IMF staff calculations.

domestic to external demand by removing impediments affecting the potential growth of the tradable sector.[4]

11. At the same time, the share of foreign direct investment (FDI) in private external financing has declined significantly over the past decade. While the decline in FDI following the GFC was a global pattern, driven by the narrowing growth differential between emerging and advanced economies, for Armenia, inward FDI continued to decline even after the mid-2010s. In recent years, net FDI relative to GDP has remained at most around one-third of its pre-GFC levels. The decline in inward FDI means a loss of the benefits associated with this type of investment, including spillovers to productivity through knowledge and skill transfers in addition to the direct financing of productive capital. As equity investment, FDI typically contributes more to financial and external stability than either debt-based portfolio or other investment.[5]

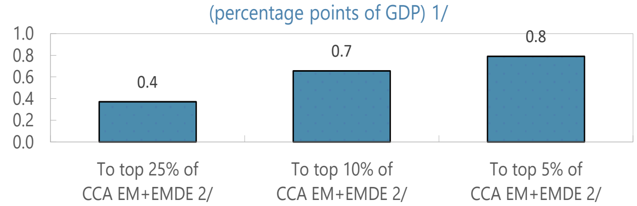
Armenia: Net Capital Inflows 1/



1/ Net capital inflows are calculated by net inflows by non-residents minus net outflows by residents.
Sources: National authorities, IMF WEO

12. Rebalancing Armenia's growth drivers from domestic to external demand, and financing towards long-term equity, will require a broad set of structural reforms. Panel data analysis for CCA countries and peer European countries suggest that, in addition to the maintenance of macroeconomic and financial stability and sound policies, improving the quality of its tradable production requires strengthening:[6] (i) <u>for goods</u>: the quality of physical infrastructure and education, reducing export costs, and lowering income inequality; and (ii) <u>for services</u>: the quality of digital infrastructure, R&D expenditure, REER, and lowering income inequality. Focusing on upgrading export services could be particularly promising considering Armenia's relative geographical isolation. Similar structural factors also significantly impact the ability to attract inward FDI. Specifically, for Armenia, improving core governance and business environment to the levels of good performers among peer (CCA and EMDE) countries—including by

Estimated Impact on Armenia's Inward FDI of Improvement in Structural Variables
(percentage points of GDP) 1/



1/ Improvement of each of five structural variables (control of corruption, government effectiveness, regulatory quality, rule of law, voice and accountability) are assumed. The results shouold be interpreted carefully, as these indicators are derived from perceptions-based data.
2/ CCA EM consists of Azerbaijan, Georgia, Kazakhstan, and Turkmenistan. EMDE is Emerging and Developing Europe.
Sources: IMF WEO; World Bank WDI; Worldwide Governance Indicators (WGI): D. Kaufmann (Natural Resource Governance Institute and Brookings Institution) and A. Kraay (World Bank)

[4] Selected Issues Paper, Chapter 1, "Promoting Export-Led Growth."

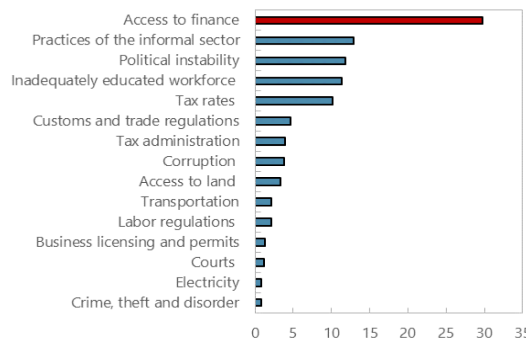
[5] Selected Issues Paper, Chapter 2, "Sustainable Financing for the Recovery in Armenia."

[6] Peer European countries are Albania, Belarus, Bosnia and Herzegovina, Bulgaria, Moldova, North Macedonia, Serbia, Ukraine.

continuing efforts to build on achievements like establishing the single anti-corruption entity—could be associated with an increase in FDI inflows.[7]

13. Reducing informality and improving access to finance should also help raise productivity and promote inclusion. Identifying the factors behind the supply of, and demand for, formal and informal sector workers in Armenia, and what governs upward mobility in the Armenian labor market is a first step towards designing policies to reduce informality.[8] Factors include reducing the complexities of regulatory compliance, strengthening the business environment, and improving access to finance. While financial inclusion has improved in recent years, rural areas remain relatively disadvantaged and firms' access to finance, especially for micro and small and medium enterprises, is cited by Armenian entrepreneurs as one of the main challenges affecting the business environment. This could be facilitated by improving corporate governance and transparency, including the relative roles of management, the board of directors, and shareholders; the clarity and readability of financial reports; and promoting financial literacy and education will facilitate this development.[9]

Armenia: Factors Impeding Business Activity
(Percent of firms choosing this factor as their biggest obstacle)



Source: Enterprise Surveys (http://www.enterprisesurveys.org), The World Bank, Armenia (2020).
Note: use of these indicators should be considered carefully, as they are derived from perceptions-based data.

14. The government's 2021-26 program outlines an agenda which could facilitate the rebalancing of Armenia's economy, although the growth impact of planned reforms will only be realized over time. This program seeks to address many of the challenges identified above, and if fully implemented could durably raise growth and living standards (Box 3). The specific impact of the reform program will crucially depend on both the depth and breadth (complementarity) of reforms as well as the timing of implementation. While there is increasing clarity on some key policy initiatives (and plans to create fiscal space), such as renewed effort to strengthen public investment management and execution as well as financial market infrastructure (as elaborated in the following sections), specific details on planned reforms in other areas are still forthcoming. As additional details of the authorities' implementation plans become clearer, staff will be able to come to a firmer view of the impact on growth (as noted above, currently medium-term growth is expected in the range of 4½-5 percent).

Authorities' Views

15. The authorities noted important reform efforts already underway, including the adoption of the law on a single autonomous anti-corruption entity (which should contribute to an

[7] Control of corruption, government effectiveness, regulatory quality, rule of law, and voice and accountability.

[8] Selected Issues Paper, Chapter 4, "Reducing Informality to Raise Productivity and Promote Inclusion."

[9] Selected Issues Paper, Chapter 3, "Increasing Access to Finance in Armenia."

improved business environment), and various initiatives to increase access to finance over the past few years (including establishment of a movable collateral registry, adoption of the National Strategy of Financial Education for 2014-2019, followed by the 2021-25 program). To further facilitate financial inclusion, the CBA is planning the digital transformation of financial services. Further efforts will be made to ensure the smooth functioning of the labor market, specifically in education and training to facilitate the transition from school to work and decrease structural unemployment, also in childcare support to encourage female labor force participation.

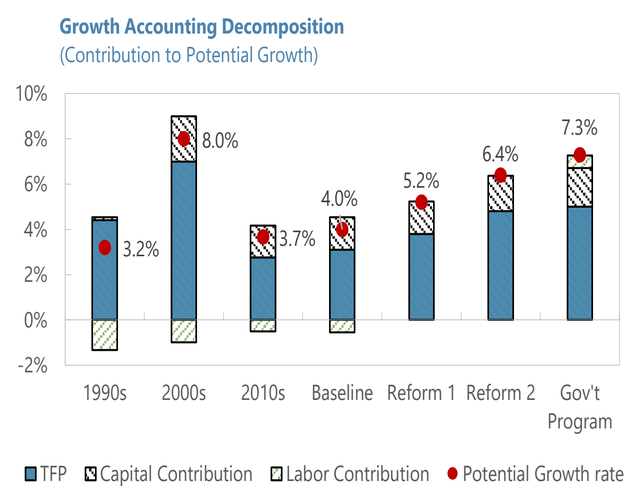
Box 3. The Armenian Economy's Growth Potential and Structural Reforms

Implementation of the government's ambitious structural reform program (Box 1) will influence Armenia's medium-term growth prospects. Our analysis suggests that potential growth could accelerate considerably if core elements embedded in the government program are comprehensively implemented as a package swiftly.

The experience with the growth impact of reform implementation across emerging market and developing economies is mixed, although empirical analysis suggests that comprehensive reforms encompassing key areas (governance, domestic and external finance, trade, and labor and product markets) can raise annual growth by about 1 ppt over the medium term (with output gains potentially even larger in the longer term).[1]

At the same time, reforms take time to implement, tend to deliver larger gains when macroeconomic conditions are favorable and with proper sequencing, and where informality is high. This highlights the need for careful design and prioritization, clear communication and transparency to ensure broad-based support, as well as coordination and swift action when conditions are ripe. Lastly, it is important to mitigate any adverse distributional effects on incomes and the vulnerable. Enhanced social safety nets can augment the impact.

For Armenia, historical trends of productivity growth, capital and labor accumulation suggest a baseline medium-term economic growth of 4 percent (text figure). Should Armenia follow through on the implementation of core elements of its government program (Box 1) and assuming an average estimated yield from structural reforms (cited above), potential growth could increase to around 5-5½ percent (Reform 1). Assuming a more ambitious reform package where policy actions are taken swiftly, reforms could raise potential growth even higher to around 6½ percent (Reform 2).



[1] IMF, "Reigniting Growth in Low-Income and Emerging Market Economies: What Role Can Structural Reforms Play?," October 2019 WEO.

B. Fiscal Policy: Promoting Growth-Friendly Fiscal Consolidation and Debt Sustainability

Near-Term Issues

16. Given the need to respond to the consequences of the twin shocks, continued targeted and temporary fiscal flexibility has been necessary in 2021. The headline fiscal deficit is expected to reach 4.7 percent of GDP in 2021 but stay well below the program target. However, in nominal terms, the headline deficit plus net lending is expected to exceed the level anticipated in the Third Review by about AMD 58 billion or ¾ percent of GDP (December 2021 QPC proposed accordingly). In addition to COVID-related spending, this reflects immediate needs for humanitarian relief and reconstruction following the Nagorno-Karabakh conflict zone ceasefire in November 2020.[10] The fiscal impact was partially offset by an increase in duties on mineral commodity (estimated at AMD20 billion) and increased social contributions (AMD 21billion), revenue administration gains and some spending re-prioritization.

17. The 2022 budget deficit target is consistent with a gradual return to the authorities' deficit and debt objectives, while maintaining adequate support. The authorities' planned budget seeks to accelerate social spending under their new program as well as critical infrastructure projects (including to ensure secure internal mobility). With projected revenue increases (increased mining sector duties, increased VAT coverage, micro-enterprises taxation reform, revenue administration improvement), the authorities' budget deficit of around 3.1 percent of GDP would imply a decline of 0.8 ppts in cyclically adjusted primary terms, with debt, assessed as sustainable (Annex I), declining to 61.1 percent of GDP.

18. Financing of the 2022 budget will come from IFIs as well as domestic and international markets. The authorities expect $200 million of budget support from development partners, including ADB, European Banks, and the European Union. In particular, the authorities are working with the EU, including to develop mature project proposals, on the specifics of a recently announced €2.6 billion multi-year package of support. The authorities also plan to use SDR 51.428 million that would be made available upon the completion of the fourth and fifth reviews for budget purposes, as the domestic absorption capacity is constrained due to the large issuances of t-bills to finance the COVID response measures.[11] They intend to meet the remainder of their financing needs by raising at least AMD250 billion on domestic markets and to use the proceeds of the 2021 $750 million Eurobond that were initially saved.

[10] In the course of 2021, the government put together a support package of AMD135 billion. The authorities regularly assess support to Nagorno-Karabakh before approval and intend to evaluate the nature, efficiency and effectiveness of future support and, as conditions permit, phase-out such support (MEFP, ¶11).

[11] The MoF and CBA will update their exiting MOU as necessary.

Medium-Term Issues

19. The authorities are committed to ensuring medium-term fiscal sustainability, rebuilding buffers, and creating fiscal space through growth-oriented spending and revenue reforms. The new government's program focuses on scaling up investment in human and physical capital to raise potential growth, and it will be essential to incorporate this cost into the Medium-term Expenditure Framework and maintain efforts to strengthen PFM. In addition to creating space for these priorities, it is essential to rebuild buffers as a guard against future shocks. Staff expects that the authorities' tax policy and administration measures, elaborated below, could raise the tax-to-GDP ratio (including social contributions) by around 2 ppts above pre-COVID levels, with a debt-to-GDP ratio declining to below 60 percent by end-2023 and further down to 50 thereafter, in line with the authorities' fiscal rule.[12] Achieving these objectives will require steadfast action to raise revenue and prioritize spending.

- *Implementation of planned tax policy and revenue administration reforms is critical* to broaden the tax base and, in this regard, the authorities' plans to review and consolidate existing efforts are very welcome (MEFP ¶10). In particular, they are pursuing wide-ranging measures to: (i) <u>reduce distortions</u> (harmonizing the tax burden across firms of difference size and addressing issues with micro-enterprises taxation); (ii) <u>expand the tax base</u> (collecting VAT on electronic services, removing VAT exemptions and PIT deductions, reforming securities taxation); and (iii) <u>improve tax compliance</u> (introducing broad-based individual income declarations with appropriate compliance safeguards, strengthening the tax audit legislation and methods, bring electronic services under the VAT net). A careful review of mining sector taxation (February 2022 SB), including the recent ad hoc temporary changes to the regime, is needed to move the legislation towards a permanent system that balances the government's objectives of capturing a fair share of the extra-profits generated by high international commodity prices, while also providing a stable tax environment and equitable treatment across firms to allow for future investment in the sector.

- *Strengthening of the MoF's capacity to prioritize and assess the efficiency and effectiveness of public spending is equally critical*. The government's plans include the objectives of upgrading the social pensions and raising the minimum wage. The timing and implementation modalities of these reforms should be considered carefully, with the impact on the budget largely met through a re-prioritization of current expenditure. As part of the broader effort to ensure current spending is carefully prioritized, the pilot review of central government compensation (supported by IMF TA) is a welcomed first step (April 2022 SB).

Estimated Tax Collection Gains from Selected Reforms

(Potential yield per year)	AMD bln.	(% GDP)
Harmonizing tax burden across firm sizes	15	0.2
Phase out mortgage interest PIT deductions	20	0.3
Bring micro-entrepreneur to general PIT regime	5	0.1
Eliminate CIT deductions for large firms buying from micro-enterprises	10	0.1

Source: IMF estimates.

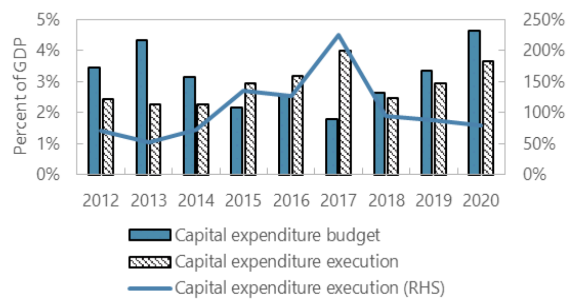
[12] This is slightly below the authorities' plans to raise tax revenue (including social contributions) by 2.5 ppts by 2026.

20. The authorities should continue advancing other critical reforms (MEFP ¶11):

- *Steady efforts to strengthen the budget process are warranted*. Improving and institutionalizing program evaluation with better performance indicators, contract management, and costings, as well as the identification of potential savings are necessary to implement the government's plans in a sustainable manner. The strengthening of financial management information systems in general, and the use of an economic classification for planning and analyzing expenditure in particular, should help identify efficiencies in government spending.

- *The authorities' renewed focus on strengthening public investment management (PIM), is also timely*. Capital expenditure execution has declined in recent years and strengthening the PIM function is critical to achieving the government's economic priorities. The recently upgraded PIM procedures contribute to this goal and it is essential that capacity and resources are mobilized to apply and mainstream these procedures. Specifically, the authorities should subject all substantial new investment projects to the examination of the government's newly established investment committee.

Capital Expenditure Budget Execution



Source: National authorities and IMF staff calculations.

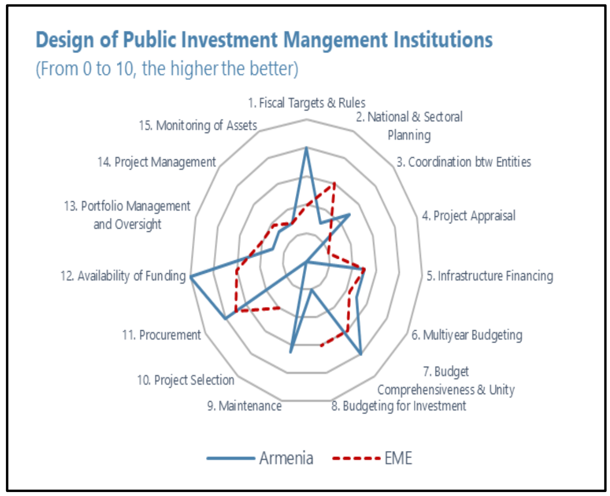
- *Institutional arrangements for Public-Private Partnerships (PPPs) continue to require attention.* Amendments to Armenia's PPP law in July paved the way for better risk management, strengthening the MoF's key gatekeeping role. The MoF will assess the affordability of PPP projects in line with two new limits, a recently approved stock limit (3 percent of GDP) and a future flow limit. The latter still needs to be set (March 2022 SB) and should be calibrated in line with experience in comparator countries (between 3 and 7 percent of current spending). The legislated amendments also clarified that the PIM process is neutral between private-public and government-financed investment but allowed for unsolicited PPPs (UPPP) and delayed the effective start date of the law. Given this, heightened scrutiny and transparency (including publication of contracts, analysis of fiscal risks and lifetime fiscal implications) should apply to all recent PPP projects approved before the current law became effective. Finally, the authorities should work to finalize the new framework, including the strengthening of procurement, and the build-up of risk assessment capacity before contracting new PPPs.

- *The authorities' intention to enhance the monitoring, reporting, and management of fiscal risks is welcome*. Improvement of fiscal transparency is a prerequisite and includes enhancing the quality of existing reporting as well as expanding government statistics to all public sector entities. Specifically, this implies transparent reporting on the use of all public funds, including those channeled through SOEs and in the context of emergency COVID response. Progress made in recent budget documents on the analysis, summary and management of fiscal risks should be continued by expanding and mainstreaming the coverage of risks being monitored, which could benefit from further capacity development.

- *The government and central bank have further moved government FX transactions towards the market.* The MoF will continue to use market-determined exchange rates for all budget transactions and for transactions by project implementation units, while also managing exchange rate risks in a transparent and cost-effective manner. In line with the new agreement between the CBA and MoF—which will become effective from January 1, 2022—it is envisaged that transactions will take place at the market-determined reference bid/ask exchange rate set by the CBA. Under the agreement, the difference between the buying and selling exchange rates set and used by the Central Bank for government FX transactions and the prevailing market buy/sell rates may not be greater than 2 percent (MEFP, ¶11).

Highlights from Recent 2018 and 2019 PIMA Reports

December 2019 PIMA recommendations
» Clarify roles and responsibilities in the PIM process
Determine responsible stakeholders for all PIM functions
Allocate clear responsibilities to different government agencies
» Strengthen the apraisal and selection of projects
Finalize, approve and implement a PIM manual following best practices
Strengthen government officials capacity in project preparation and appraisal
» Improve the budgeting and monitoring of projects
Build portfolio of projects in Line Ministries linked to strategic objectives and sectoral targets
Build a database of externally and domestically-funded projects throughout their life-cycle
Monitor project execution to identify and possibly reformulate poorly-performing projects
Improve expenditure projections in the MTEF and annual budget



21. Implementation of the government's program should improve inclusion. Reforms under the program aimed at removing tax policy distortions and strengthening compliance, improving corporate transparency and financial inclusion, and developing human capital should strengthen inclusion both directly and through reduced informality. Staff welcomes the introduction of an integrated social services system that unifies the provision of services and improves the targeting of support to vulnerable households. Plans to increase social pensions and the minimum wage should aim to meet social needs while limiting macro-fiscal consequences (e.g., by improved targeting and linking minimum wage changes to productivity) and be guided by the expenditure review mission findings.

Authorities' Views

22. The authorities concurred with staff on key fiscal reform priorities and the need to implement their program in a manner consistent with fiscal sustainability. They agreed that revenue mobilization was essential to create space for investment in physical and human capital and the social protection objectives envisaged under the government plans. They also stressed the need to reformulate the structure and functions of the Budget Department to strengthen program-based budgeting and spending reprioritization and carefully control current spending. However, they were of the view that the growth dividends of the government plans may, particularly in the face of renewed shocks, warrant a slower reduction in the debt-to-GDP ratio. They noted that in the

aftermath of the twin shocks, social needs remain elevated while the government's renewed efforts on structural reform and capital investment should boost growth potential and thereby improve long-term debt sustainability.

C. Monetary Policy: Curbing Inflation and Strengthening the Inflation Targeting Framework

23. Monetary policy should continue to focus on returning inflation to target and limiting the risk that transitory, external, and supply pressures dislodge expectations. The CBA has proactively raised rates (cumulatively 300 bps since December 2020) to 7.25 percent in September. Staff supports the policy tightening which signaled the CBA's commitment to inflation targeting and helped anchor inflation expectations. Despite current above-target inflation, the CBA's close to neutral monetary policy stance is justifiable given the importance of exogenous inflation drivers which are expected to moderate in 2022, indications of stabilizing pressures on expectations, and to limit the potential risks to the nascent recovery. However, given the elevated uncertainty and the anticipated closing of the output gap in 2022, the CBA should stand ready to raise the policy rate further as demand factors come more to the fore and if pressures on inflationary expectations become more protracted. Staff also emphasized that the CBA should allow exchange rate flexibility, intervening only to counter disorderly market conditions and to build up reserves in an opportunistic manner to ensure a strong NIR position.

24. The ongoing improvements in the CBA's communication strategy are welcome. Communication between the CBA, banks, and the public has been enhanced, and is perceived to work well overall by market participants. Key steps in this process include regular press conferences by the CBA Governor, the publication of financial stability reports with stress-test results, and the development of a new inflation expectations survey (MEFP, para 13).

25. The authorities have indicated that they plan to save the SDR allocation to bolster reserves. They have requested the exchange of SDRs to USD (around $114 million).

Authorities' Views

26. The CBA noted that it is proactively managing the challenges posed by above-target inflation, which it views as driven by multiple factors. In particular, the CBA continues to closely monitor inflation expectations, inflation developments, and drivers. It sees the recent policy tightening as an effective step to manage inflation dynamics and stands ready to adjust monetary policy as needed in response to changes in the economic outlook and inflation expectations. The CBA projects inflation to start slowing by end-2021 and return to the four percent target in the second half of 2022. The CBA also underlined the importance of its improved communication strategy to strengthen monetary policy implementation and help anchor inflation expectations.

D. Financial Sector Policy: Enhancing Resilience and Promoting Deepening

Near-Term Issues

27. The financial sector weathered the pandemic relatively well, although vulnerabilities remain. Despite the severe 2020 recession, the financial sector has strengthened in recent months (¶6). The capital position of the banking system remains well above the current minimum requirement of 12 percent of risk weighted assets due partly to the measures that were introduced by the CBA to preserve capital in the face of the economic slowdown. Banks responded to rising risks by tightening lending standards and increasing their holdings of government securities, which helped reduce the risk profile of their balance sheets. Banks' profitability, however, continues to be weak mainly due to the recognition of credit losses. Given declining uncertainty over the pandemic impact and to improve the resilience of financial institutions against potential new shocks, the CBA has required all banks to maintain a Capital Conservation Buffer (CCB) of 1.5 percent. In addition, systemically important banks will be required to maintain an additional 1.0 percent buffer above the minimum requirements from January 2022. These buffers will be increased to 2.5 percent by January 2024 and 1.5 percent, respectively, by January 2023. Banks are also required to maintain a minimum Liquidity Coverage Ratio (LCR) level of 100 percent for each significant currency starting from January 2022. Considering remaining vulnerabilities, the CBA should continue monitoring capital and liquidity buffers, perform regular stress tests, and enforce the newly introduced asset classification and provisioning rules.

28. Most of the measures introduced by the CBA to support the financial sector during the pandemic have either expired or been withdrawn. These measures slowed the crystallization of losses, improved the capacity of banks to absorb losses and ensured continued flow of credit to the real sector. They included (i) encouraging voluntary prudent loan restructuring where necessary, (ii) permission to utilize banks' usable capital buffers at the cost of restrictions on dividend distribution, i.e., the CCB and the buffer for domestic systemically important banks; and (iii) other targeted relief measures including subsidized loans by commercial banks. Loan restructuring options were available for a limited period until June 2020 while government-subsidized loans will be available until February 2022.

Medium-Term Issues

29. The authorities are keen to continue developing their capital market and expanding access to finance.

- *Financial markets.* The CBA is finalizing the 2021 capital market development action plan that builds on IMF TA. The plan proposes reforms, including deepening FX, money, and sovereign markets, strengthening the primary dealer network, developing an electronic platform for FX trading, improving market information, and removing regulatory obstacles to forward market development. The authorities are committed to creating centralized platforms for overnight repo market and for the FX market (March 2022 SB) and developing improved money market reference rates.

- *Financial inclusion*. Staff looked at major bottlenecks to financial inclusion for corporates and households in Armenia.[13] While the authorities have been implementing various initiatives to increase access to finance over the past few years, the CBA's recent agenda on digitalization to facilitate the digital transformation of financial services could assist progress in this area particularly given the planned development of the infrastructure, standards and ecosystem to drive the adoption of electronic services provided the platform is open to competition and adequate consumer protection and privacy safeguards are put in place.

30. Staff welcomed initiatives to enhance the assessment of banks' Internal Capital Adequacy Assessment Process (ICAAP) and to introduce Pillar 2 buffers in the next few years. The current capital adequacy requirement is based on the standardized approach of the Basel Framework with a minimum CAR of 12 percent. To address FX risks, the adopted approach applies higher risk-weights (of 150-200 percent) to exposures denominated in foreign currency. The CBA recognizes the need to align individual banks' minimum capital requirements with their risk profile through the introduction of Pillar 2 capital buffers and is currently building their capacity to effectively assess banks' ICAAP with support from the World Bank. Staff welcomed the plan to introduce Pillar 2 capital as it will ensure that each individual bank's capital requirements will be commensurate with their risk profile. The CBA can also incentivize improvements in banks' risk management capacity by imposing additional capital requirements on banks with significant risk management and governance weaknesses.

31. The CBA should continue enhancing its supervisory and macroprudential toolkits. In line with the 2018 FSAP recommendations, the CBA aligned its NPL definition with international standards, continued with FX reserve requirement redenomination per their action plan, and has already decided to introduce Loan-to-Value (LTV) limits on new mortgages from April 2022 (90 percent for LC loans and 70 percent for FX loans). The CBA also plans to introduce debt-service-to-income (DSTI) limits to complement the LTV limits. These measures will help address risks from mortgage lending, which has grown rapidly in recent years. There are also plans to phase out fiscal incentives for mortgages. Staff welcome the ongoing initiatives, supported by Technical Assistance from the World Bank, to enhance the resolution framework, assessment of banks' business model, and supervisory review of banks' ICAAP.

32. The CBA is working on monitoring risks from increased digitization of financial services and climate-related shocks. The pandemic has accelerated the adoption of digital channels by financial institutions resulting in new risks including those related to cyber security, data privacy, outsourcing, third-party dependency and concentration risk.[14] Further, an increase in the frequency and severity of climate-related events (physical risks) and transition to a low-carbon economy (transition risks) could potentially impact economic activities, assets classes and, consequently, the stability of the banking sector.[15] The authorities have established a Working

[13] Selected Issues Paper, Chapter 3, "Increasing access to Finance in Armenia".

[14] This could arise if several banks were to rely on the same service provider.

[15] For example, falling asset values due to climate-related events (e.g., real estate in flood or landslide prone areas) or adjustments to firms' business models in response to climate change mitigation policies could result in substantial losses to the financial sector.

Group on Environmental, Social and Governance risks, and plan to review the regulatory and supervisory framework to capture specific risks from digitization of financial services and introduction of new products.

33. In view of the new risks posed by digitalization of financial services, staff also recommends that the authorities introduce appropriate consumer protection safeguards. This includes enhancements to the data protection and governance frameworks with the aim of: (i) protecting the privacy and integrity of consumer data; (ii) addressing the issues related to collection, access, use and sharing of customer information; (iii) clarifying on ownership of, and control over, customer data; and (iv) enhancing fairness, accountability and transparency in the provision of digital financial services.

34. The latest Safeguards Assessment found that the CBA continued to maintain a strong safeguards framework, including well established audit (internal and external) arrangements and financial reporting practices. In addition, amendments to the CBA law and internal regulations were implemented to address previous safeguards concerns, although there may be scope for further legislative and operational refinements to reinforce the CBA's autonomy and governance arrangements, including by establishing a risk management function and further enhancing the oversight role of the Board. The authorities have finalized a medium-term exit strategy to reduce and, in an orderly manner, phase-out its involvement in non-core central banking activities (April 2021 SB; MEFP ¶16), which should be adopted by the CBA Board shortly. Staff strongly support the planned diversification of the Board composition in subsidiary companies to enhance independence and effectiveness, as well as the phasing out of CBA involvement in the Boards of subsidiaries.

Authorities' Views

35. The authorities continue working to promote capital market development, digitalization, and further enhancing their supervisory framework. As part of the capital market development action plan, the CBA has finalized the framework and rules for a centralized foreign exchange trading platform that should result in a more liquid market. The CBA is also working on a plan to facilitate the digital transformation of financial services. The CBA concurred with staff on the importance of introducing Pillar 2 charges as they will be instrumental in addressing additional risks, and in aligning capital requirements with risk profile of bank's balance sheets.

E. Structural Reforms: Advancing Sustainable and Inclusive Growth

36. The authorities' economic program appropriately focuses on boosting long-term tradeables-led and inclusive growth and increasing public and private investment. As outlined above, Armenia would benefit from improved export quality and potential, further integration into global value chains, and transitioning the sources of external financing from debt (largely deposits) to equity (FDI). Key priorities to bring this about include: (i) better infrastructure and improved public service delivery through public administration reforms; (ii) human capital development through improved education, healthcare, and social protection; (iii) a stronger business environment with improved transparency and governance; (iv) reduced informality and income inequality through reforms and redistributive policies; and (v) expanded economic opportunities through SME support,

capital markets development and improved access to finance. While the government's program outlines reforms across all these areas, the key near-term task is to elaborate the specific actions plans and policies (and associated costing and performance indicators) underpinning progress in each of these areas, and expeditiously commence implementation of these actions plans. Releasing detailed implementation plans, and key performance indicators, will help clarify the likely impact of the government's program on the growth potential and provide critical guidance for private decision makers.

37. Reopening regional transport and trade links could enhance connectivity and contribute to Armenia's economic development. Ongoing trilateral discussions, under the framework agreed between the leaders of Armenia, Azerbaijan, and Russia in January 2021, are aimed at restoring regional (road and rail) transport routes, while respecting countries' sovereignty over railway and road links. Success in these efforts could bring long-term benefits to Armenia, offering it both access to larger and more diverse export markets as well as likely lower transportation costs and the prices of its imports.

38. Education, employment, and social assistance reforms are critically interconnected. If successfully implemented, the economic transformation envisioned in the government program could lead to a reallocation of resources from lower to higher productivity firms and sectors. Ensuring that the institutions across social sectors can respond—through retraining, reintegration of displaced workers to the labor market, and targeted temporary income support—would facilitate this transition and limit the unintended impact on the most vulnerable.

- Education reforms should build upon a well-designed strategy and focus on modernizing the curricula, improving infrastructure, reducing skill mismatches, and improving vocational training.
- Building on the network of unified social services and assessments of multidimensional poverty, the social safety nets should be enhanced to increase the coverage of beneficiaries and adequacy of benefits in a targeted and cost-effective way.
- Labor market reforms are required to durably reduce informality, improve inclusion, and foster sustainable economic growth. Childcare support (e.g., to enhance female labor force participation) should be complemented with active labor market policies to ease the transition to new employment opportunities. This includes both school- and unemployment-to-job transitions, as well as internship programs and reskilling.

39. New economic opportunities should be created through appropriately targeted SME support and a favorable business environment. SMEs are critical in creating employment opportunities and promoting inclusive growth in Armenia. They should be supported through improved access to finance, land, water management, labor (e.g., childcare support), and transportation reforms, as well as digitalization and by addressing gaps in the legal and institutional framework. Improving the business environment and strengthening corporate governance and transparency should facilitate access to financing, while the authorities should complete their efforts in assessing the effectiveness of existing SME support schemes to inform their reforms to SME support.

40. Efforts to address gaps in the AML/CFT legal framework should continue, and its implementation should be enhanced, also to address corruption risks. The authorities noted that a national money laundering/terrorism financing (ML/TF) risk assessment was conducted for 2017-2020, and efforts are being made to align the legal framework for domestic politically exposed persons (PEPs) and banking secrecy to the FATF standard, and that a law introducing civil forfeiture for seizure of illegal assets was passed. These are welcome developments addressing intrinsic ML/TF risks that are important to mitigate. A public beneficial ownership register (www.e-register.am) is being phased in, initially only to include mining companies. It is recommended to increase the scope of the register to all types of legal persons, in line with recommendations made by MONEYVAL, and to prioritize measures that would have a positive impact as well on beneficial ownership transparency of companies that are awarded public procurement contracts related to Covid-19 spending. Tax evasion was identified as a high-risk area for ML/TF, reporting of suspicious transactions related to tax evasion is another priority for authorities.

41. With the right mix of policies, Armenia can enhance its mitigation and adaptation efforts and lower the adverse impact of climate change. Armenia's average temperature has been on an increasing trend, and average annual precipitation has declined by 10 percent (1935-2012) (Box 4).[16] Under a global emissions scenario without mitigation, per capita GDP of Armenia would be 11 percent lower by the end of this century.[17] Cognizant of these effects, Armenia has adopted a series of climate change mitigation and adaptation targets in its government program and codified them in legislation (decree N 610-L). To achieve these targets, a mix of policies will be needed such as environmental taxes, investment for transitioning to cleaner energy systems, retrofitting of buildings and other measures to promote energy efficiency, a coherent regulatory framework (e.g., to avoid cross subsidization), improved water and waste management systems, and other adaptation measures outlined in the government program. The success of these efforts will also depend on the adequacy of international financial, technological, and capacity-building support.

Authorities' Views

42. The authorities are keen to implement their government program to promote equitable and sustainable growth. This will be through developing key performance indicators over major reform areas and in state bodies with the expectation of attracting the best specialists. The government's vision is to create a knowledge-based economy driven by innovation as the main source of development. This in turn will help create competitive conditions in the labor market, attract talent, specifically women and youth, and prevent brain drain. In addition, encouraging the upward transition of products through value chains which lead to higher export potential in particular agricultural production. Also, priority reforms will focus on Land Code for increasing the productivity of the agricultural sector, water sector reforms and urban development.

---

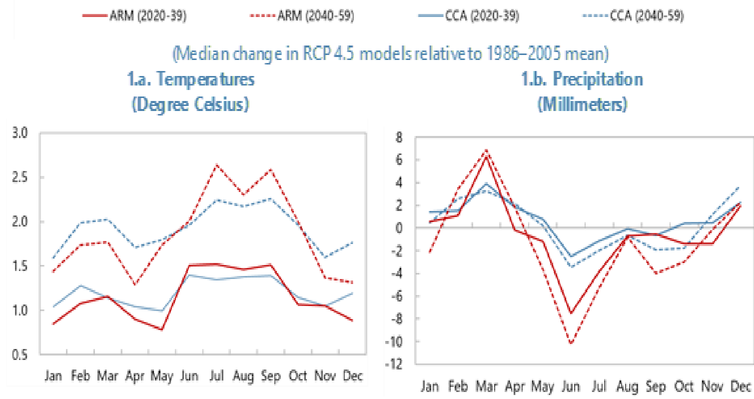
[16] World Bank Climate Change Knowledge Portal.

[17] Kahn and others (2021), Long-Term Macroeconomic Effects of Climate Change: A Cross-Country Analysis. *Energy Economics*.

Box 4. Armenia's Climate Change Risk Profile

- Armenia could experience a potential warming of around 3°C by 2040-59s above the 1986–2005 baseline, a much larger increase than the global average. In addition, precipitation has become more irregular across parts of Armenia, with the northeast and central regions becoming more arid while the southern and northwestern regions face higher precipitation.

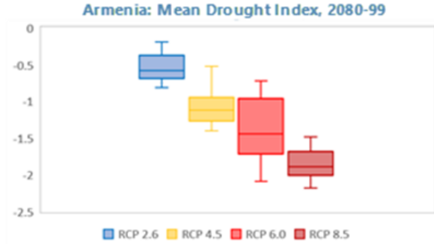
Armenia: Projected Change in Weather Patterns, 2020–59



Sources: World Bank Climate Change Knowledge Portal and IMF staff calculations.

- Increased drought, flood and landslide risks will affect the poorer rural communities that depend heavily on agriculture. Higher temperatures and a higher incidence of drought will lead to forest loss, dryland expansion and more dependence on water.

Armenia: Mean Drought Index, 2080-99



Note: RCP stands for Representative Concentration Pathways. Reference Period: 1986-2005. Positive values indicate positive water balance (or wet) conditions and negative values indicate negative water balance (or dry) conditions.
Sources: World Bank Climate Change Knowledge Portal and IMF staff calculations.

PROGRAM IMPLEMENTATION

43. The program remains broadly on track, although the snap elections in late-June and data limitations delayed the implementation of some measures. All quantitative performance criteria (QPCs) and ITs for end-December and end-March (except for end-March NIR IT) have been met. The end-June 2021 QPCs are controlling for the combined fourth and fifth reviews, and all but the NIR QPC for end-June 2021 were also met. NIR fell below the June (adjusted) target by $144 million, reflecting larger-than-projected government foreign exchange conversions and sell-side intervention in Q1–Q2 2021 to counter disorderly market conditions in the period of heightened political uncertainty between the November ceasefire over the Nagorno-Karabakh conflict zone and the June 2021 elections. The authorities remain committed to the underlying reform actions in the program and are intent to correct delays and slippages on quantitative conditionality. Preliminary data indicate that the end-September NIR, program fiscal balance, budget domestic lending, external public debt arrears, new government guaranteed debt, and social spending ITs were likely met. QPCs for end-December 2021 and ITs for end-March 2022 have been proposed (MEFP Table 1). The revised end-December IT on net domestic assets of the CBA reflects anticipated use of government deposits.

Armenia: Quantitative Performance Criteria, Indicative Targets and Consultation Clause 1/

(In billions of drams, at program exchange rates, unless otherwise specified)

	Sep. 3/	Dec. 2/				2021						
						Mar. 3/			Jun. 2/			
	Act.	EBS 20/178	Adjusted Target	Act.	Status	EBS 20/178	Adjusted Target	Act.	EBS 20/178	Adjusted Target	Act.	Status
Performance Criteria												
Net official international reserves (stock, floor, in millions of U.S. dollars)	1,332	1,348	1,099	1,131	Met	1,474	1,735	1,695	1,464	1,610	1,475	Not met
Program fiscal balance (flow, floor) 4/	-240	-517	-443	-421	Met	-181		-72	-253		-127	Met
Budget domestic lending (cumulative flow, ceiling)	40	115		41	Met	45		0	45		31	Met
External public debt arrears (stock, ceiling, continuous criterion)	0	0		0	Met	0		0	0		0	Met
MPCC 5/												
Inflation (upper-outer band, inflation consultation, percent)	4.3	4.5		4.5		5.0			5.1			
Inflation (upper-inner band, percent)	3.3	3.5		3.5		4.0			4.1			
Inflation (mid-point, percent)	1.4	1.5		3.8	Met	2.0		5.8	2.1		6.5	Not met
inflation (lower-inner band, percent)	0.0	0.0		0.0		0.0			0.1			
Inflation (lower-outer band, inflation consultation, percent)	0.0	0.0		0.0		0.0			0.0			
Indicative Targets												
Net domestic assets of the CBA (stock, ceiling)	390	622		598	Met	605		348	589		464	Met
Avg. concessionality of newly contracted ext. debt (flow, floor, in percent) 6/	...	30		43	Met	...		...	...		...	...
New government guaranteed external debt (stock, ceiling, in millions of USD) 7/	0	100		0	Met	100		0	100		0	Met
Social spending of the government (flow, floor) 8/	44	58		62	Met	16		17	32		33	Met

Sources: Armenian authorities; and Fund staff estimates.

1/ All items as defined in the TMU, based on program exchange rates in the TMU.

2/ Quantitative performance criteria at test dates.

3/ Indicative target.

4/ Below-the-line overall balance excluding net lending.

5/ If the end of period year-on-year headline inflation is outside the upper/lower bound, a formal consultation with the Executive Board as part of program reviews would be triggered.

6/ Assessed on a calendar year basis, excluding the Eurobond and any similar refinancing instruments.

7/ Includes both concessional and non-concessional debt, excluding the Eurobond and any simliar refinancing instruments.

8/ Defined as spending on the family benefit program and lump-sum financial aid, one-time childbirth benefits, and childcare benefits for children less than two years of age.

44. The authorities have requested a waiver of nonobservance for the June NIR QPC, which staff assesses as appropriate based on corrective actions: (i) the establishment of a committee in September 2021, which comprises the CBA and MoF, to improve projections for government conversions, and the MoF's ongoing efforts to strengthening its capacity to collect data from line ministries on demand for FX conversions; (ii) implementation of measures to improve FX market functioning and depth (¶29); and (iii) the purchase of US$ 22 million since June 2021. The authorities remain committed to strengthening reserve buffers in an opportunistic manner when market conditions are favorable.

45. End-June inflation (6.5 percent) breached the upper-bound of the MPCC, triggering a Board consultation (Attachment III). Going forward, the end-December MPCC is set with the midpoint based on projected inflation (8.5 percent), and a narrower inner upper band margin, and the same outer upper band margins (which reflects historical inflation volatility), relative to the end-June MPCC (MEFP Table 1). The lower bands are set at 3.5 percent and 2.5 percent, respectively, so that a Board consultation is triggered if inflation falls below the lower bound of the CBA's own inflation target range (2.5 percent), and a staff consultation if inflation is between 2.5 and 3.5 percent.

46. Progress on the structural benchmarks was mixed. The pre-election period has delayed completion of some SBs (MEFP Table 2), however, the government remains committed to their implementation. Since the third review, 3 SBs were met, 6 were not met but implemented with delay with another one also expected to be implemented with delay by the time of the Board discussion, one was not met but replaced by a new SB (¶47), and 3 not met but where the authorities remain committed to the underlying action (MEFP ¶¶10,11), but where implementation may fall outside the timeframe of this SBA. The CBA presented staff with, and incorporated staff's comments on, a time-

bound medium-term exit strategy to phase out the CBA's involvement in non-core activities (April 2021 SB). Loan-to-Value (LTV) limits on new mortgages are scheduled to be introduced in April 2022 with 90 percent for LC loans and 70 percent for FX loans (March 2021 SB).

Armenia: Structural Benchmarks for the Fourth and Fifth Reviews

Measures	**Time Frame**	**Status**
Fiscal		
Conduct a study identifying tax potential and factors preventing tax collection reaching its potential.	October 2020	Not met, implemented with delay
Design an action plan to reduce the tax policy gap identified in the study.	December 2020	Not met, implemented with delay
Compile a comprehensive sectorized list of all public sector entities, with IMF TA support.	March 2021	Met
Compile and estimate all the existing and future contingent liabilities associated with implemented and approved PPPs	January 2021	Met
Approve and publish a decree setting a cap to the total contingent liabilities contracted from PPPs.	February 2021	Not met, implemented with delay
Build a database of projects covering both externally and domestically funded projects that provides information on projects throughout their lifecycle.	December 2020	Not Met MEFP commitment (¶11), May 2022
Revise the turnover tax legislation by reducing the VAT registration threshold to AMD 60.00 million and adjusting tax rates to equalize the tax-burden across the turnover and general taxation regimes, effective from January 1, 2022.	May 2021	Not Met MEFP commitment (¶10) to revise the turnover tax legislation to take effect from January 1, 2023
Undertake a public expenditure review, with a view to identifying options for efficiency gains and improving the social protection system.	May 2021	Not Met MEFP commitment (¶11), with a new SB for April 2022
Conduct the review of securities' taxation to ensure appropriate taxation in this area and identify possible distortions and impediments to capital market development.	June 2021	Met
Include in the 2022 budget documentation a comprehensive list with all ongoing public investment projects and new public investment projects starting in the budget year, including PPPs, providing comprehensive information on lifetime fiscal implications, including project by project information for all externally financed projects and large domestically financed projects (at least 50 percent of investment volume from domestic financing).	October 2021	Not Met MEFP commitment (¶11) to improve transparency around the PIM process
Undertake a public expenditure review of civil service compensation.	April 2022	Improve the analytical capacity of the Ministry of Finance to increase the efficiency and effectiveness of current spending
Monetary and Financial		
Prepare a medium-term exit strategy to phase out the CBA involvement in non-core central bank activities (i.e. development lending and subsidiaries)	April 2021	Not Met, Implementation pending
Introduce limits to stressed Loan-to-Value (LTV) ratio	March 2021	Not Met, implemented with delay
Structural		
Submit to the National Assembly a draft law on a single autonomous anti-corruption entity in line with international standards, which combines all detection and investigative functions	September 2020	Not met, implemented with delay
Submit to the National Assembly a draft law on Higher Education and Science which sets the legal ground for (i) reforming the tertiary education management system; (ii) upgrading licensing and accreditation requirements, state financing principles, supervision mechanisms for quality of education services.	June 2020	Not met, implemented with delay

47. The authorities propose four SBs for the sixth and final program review (MEFP Table 2)**:**

- Undertake a review of mining sector taxation (February 2022).
- Approving a decree establishing a cap on direct PPP-related liabilities (March 2022).
- Creating a centralized platform for the overnight repo market and for the FX market (March 2022).
- Undertake a public expenditure review of civil service compensation (April 2022).

48. The program is fully financed, and Armenia's capacity to repay remains adequate. There is currently no estimated financing gap through the program, and Armenia's capacity to repay is supported by the downward trajectory of debt, the authorities' track-record of reforms and sound macroeconomic management. Financing support from the EU is under negotiation but its timing and composition remain unclear.

STAFF APPRAISAL

49. The Armenian economy is recovering strongly, but inflationary pressures have emerged as a key challenge. The economy posted 5 percent growth in 2021H1 after contracting by 7.4 percent in 2020, supported by recovering external and domestic demand. Inflation further accelerated in October, reflecting pent-up consumption, supply constraints, global and domestic food inflation, and pass-through from dram depreciation in early 2021.

50. The external position has improved, but vulnerabilities remain. Despite a decline in tourism receipts and remittances, the current account balance narrowed, mainly due to import compression. Reserves remain adequate and the external position for 2020 is assessed as broadly consistent with fundamentals and desirable policies.

51. The authorities need to quickly develop appropriate action plans to implement the government program, strengthening growth prospects while preserving economic and financial stability. The government should accelerate the costing of actions implementing its new program and integrate them into a revised medium-term expenditure framework. The new medium-term framework would clarify the government's commitment to fiscal sustainability and should underscore that public policies are meant to support, and be complementary to, private investment. In this regard, the pace of public spending will need to be aligned with growth developments to avoid crowding out private investments, with the transparency in the use of public funds and the creation of contingent liabilities should be improved, including for SOEs and when engaged in PPP contracts. At the same time, the government should finalize and circulate its action plans to strengthen the business environment and reiterate its commitment to a fair, modern, and transparent tax regime as these would help attract private sector and foreign investors.

52. A more revenue-based and growth-friendly fiscal consolidation is needed. While Armenia’s debt is assessed as sustainable and as the impact of the twin shocks dissipate, the government should focus on rebuilding buffers while adjusting the fiscal policy mix to support growth. In this respect, the government’s plans to steadily increase tax revenue with a quality package of tax policy and tax administration measures is welcome. As this package is being fine-tuned, it is essential to carefully review plans to review mining sector taxation to ensure a new regime will achieve the government’s objective of a fairer revenue share while not jeopardizing the ongoing development of the sector. The government also needs to accelerate the review of current expenditures with the objective of identifying efficiency gains and of redeploying resources towards its priorities, including social protection priorities.

53. Improving the efficiency of public investment is critical for future growth. The new government’s plan envisages a scaling up of public investment to address Armenia’s infrastructure gaps. The sustainability and growth impact of this scaling-up crucially hinge on the government’s capacity to develop, appraise, prioritize, and manage public investment projects. While some progress in strengthening PIM regulations has been achieved, it is now essential that the government firmly applies the new rules to build credibility of the new system and ensure only well-developed projects are considered, even if this entails some implementation delays that are inherent to the use of new

systems. In this regard, the priority should be to ramp up the capacity needed to operationalize the rules and fine-tune their application with the goal of ensuring the most efficient use of investment resources.

54. Staff welcomes the CBA's efforts to strengthen the inflation targeting framework as monetary policy continues aiming at returning inflation to the target. Staff supports the policy tightening that the CBA has been implementing over the past year which signaled its commitment to inflation targeting and helped with anchoring inflation expectations. Improvements in the CBA's communication strategy, including the development of a new inflation expectations survey, are major steps in this area. The CBA closely monitors the impact of various factors on risks to inflation and expectations and stands ready to further tighten policy if needed. The CBA should allow the exchange rate to move flexibly, intervening only to counter disorderly market conditions and to build up reserves in an opportunistic manner to ensure a strong NIR position.

55. Improving intermediation and the capacity of banks to lend to the real economy should be a priority. This includes removing bottlenecks of financial inclusion for corporates and households and facilitating the digital transformation of financial services. In parallel, the CBA should maintain its current policy, which require banks to seek regulatory approval before they can distribute dividends until the uncertainty about credit quality and the impact of the Covid crisis on borrowers' balance sheets is significantly reduced. Banks with limited capital buffers should also be encouraged to raise capital from the market once the conditions are favorable so as to enhance their capacity to lend and improve their resilience to potential additional shocks. Staff also particularly welcome the authorities' enhanced action plan to develop capital markets.

56. Staff welcomes the CBA initiatives to strengthen its supervisory toolkit. The CBA has improved its supervisory toolkit through implementation of Basel III standards, enhancement to its risk-based supervision framework, and introduction of macroprudential measures. The planned introduction of a supervisory reporting platform will further strengthen the supervisory toolkit by ensuring that supervisors have granular and validated data to facilitate timely identification and monitoring of risks and vulnerabilities. The CBA should accelerate plans to introduce Pillar 2 capital add-ons to ensure that banks maintain adequate capital buffers. In the meantime, banks should be required to maintain minimum capital above those required under the Basel framework to reflect additional risks that are currently not adequately captured.

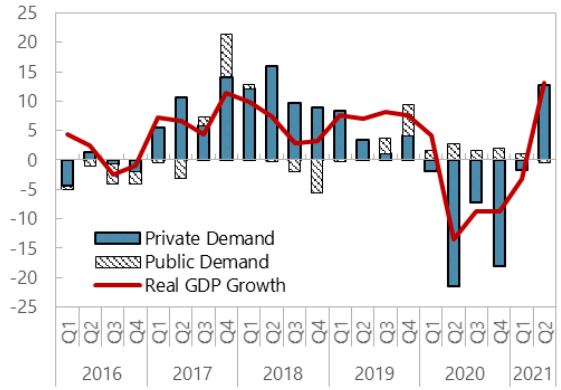
57. Staff supports the authorities' request for completion of the fourth and fifth reviews. In view of the authorities' performance under the program and commitments as described in the MEFP to implement fully the actions under their Fund-supported program, staff recommends completion of the fourth and fifth reviews. Staff supports the authorities' request for a waiver of nonobservance for the end-June performance criterion on net international reserves given the correction actions taken by the authorities. Staff also supports the completion of the consultation under the MPCC. Upon completion of the review, an additional SDR 51.428 million would be made available to Armenia.

58. Staff recommends that the next Article IV Consultation be held on the 24-month cycle, in accordance with Decision No. 14747-(10/96).

Figure 1. Armenia: Real Sector Developments

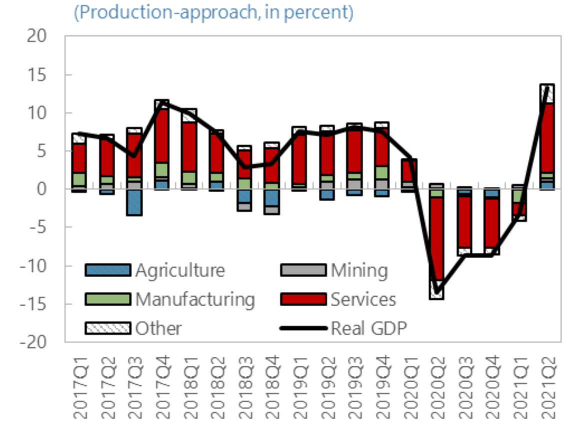
Growth in 2021 Q2 was mainly driven by private consumption.

Contributions to Real GDP Growth
(Expenditure-approach, in percent)



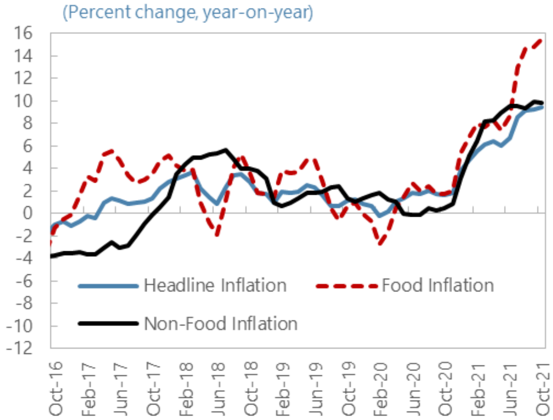
2021 Q2 shows a strong recovery with growth performance mainly driven by services sector.

Contributions to Real GDP Growth
(Production-approach, in percent)



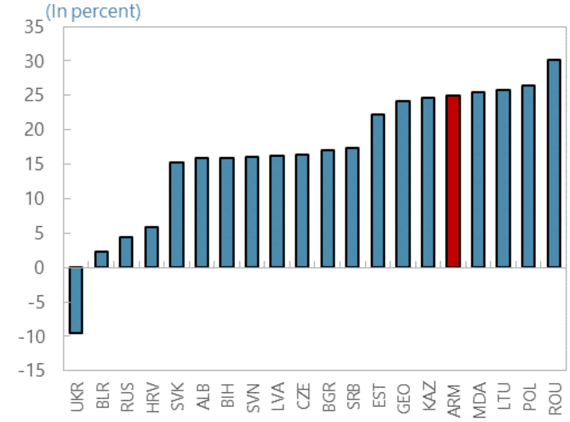
Both food and non-food inflation are above expectations

Consumer Price Inflation, SA
(Percent change, year-on-year)



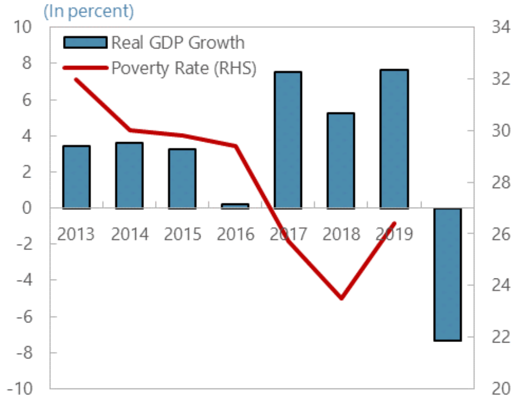
Armenia's per capita income growth is high, compared with peers.

Growth in Real GDP per capita between 2012 and 2020
(In percent)



Pre-pandemic, robust GDP growth helped poverty rates fall significantly.

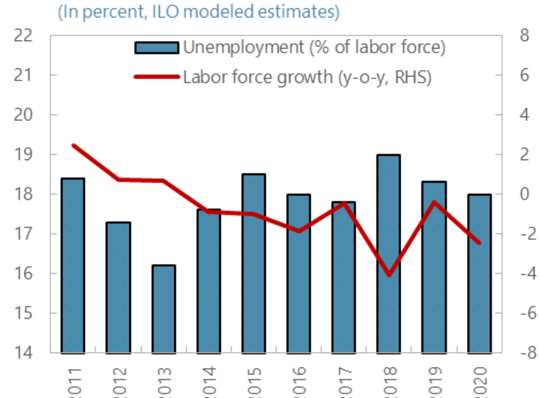
Real GDP Growth Rate and Poverty Rate
(In percent)



Note: Data on poverty rate available up to 2019.

Employment growth increased in recent years, and unemployment rates decreased slightly by end of 2020.

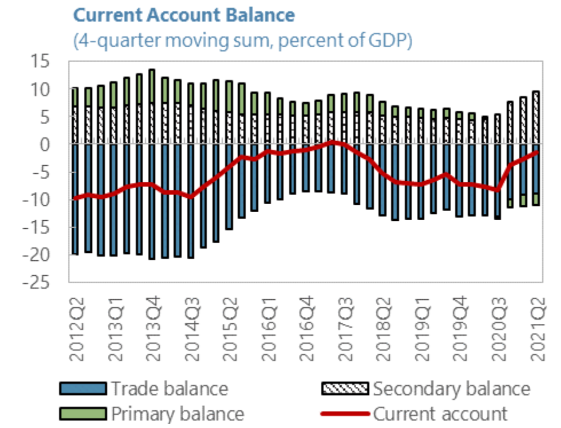
Labor Market Indicators
(In percent, ILO modeled estimates)



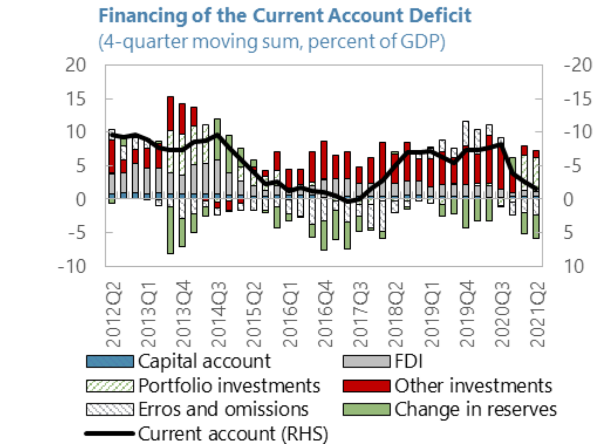
Sources: National authorities, Haver, IMF World Economic Outlook, and IMF staff calculations.

Figure 2. Armenia: External Developments

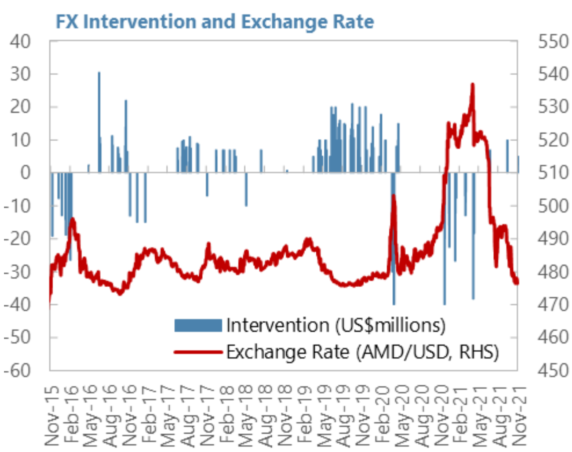
After a widening in 2019, the current account deficit narrowed toward end-2020.



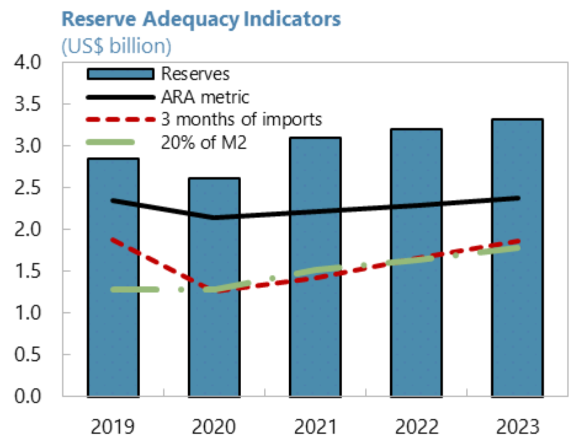
In recent years, current account has been financed mainly by private inflows.



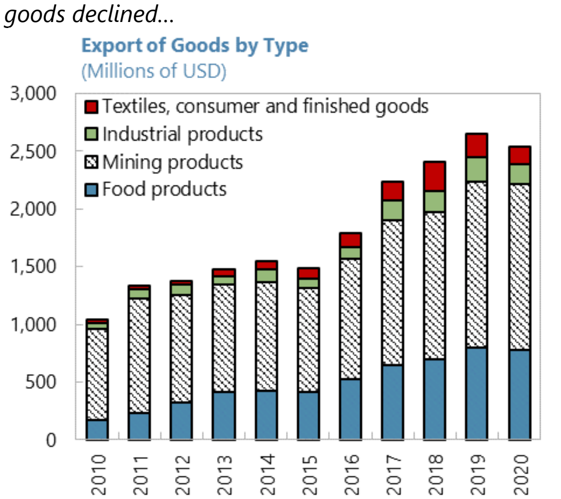
Dram depreciated through April-2021 but since then it has returned to pre-conflict levels.



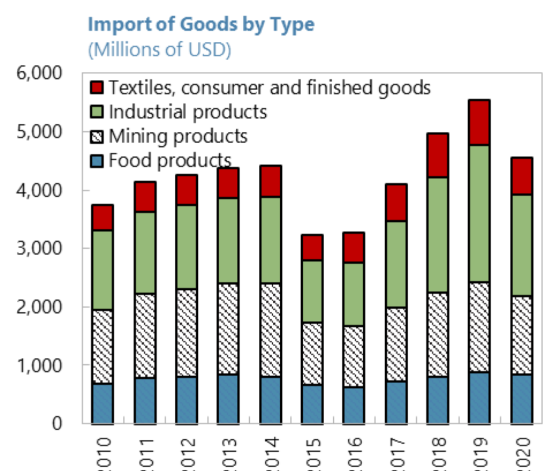
Thanks to IMF financing, Eurobond issuance and SDR allocation, reserves remain adequate.



In 2020, exports of textile, consumer and finished goods declined…



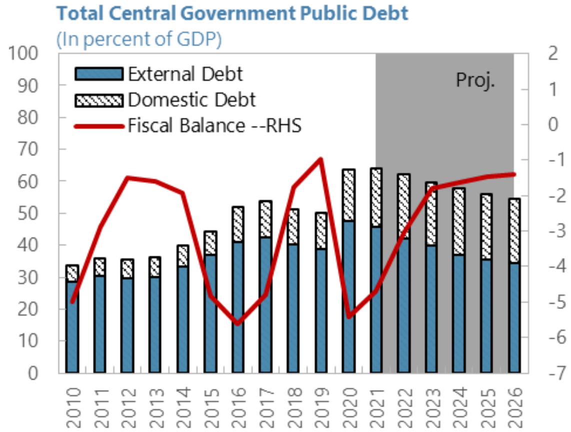
…and the imports of capital goods fell sharply.



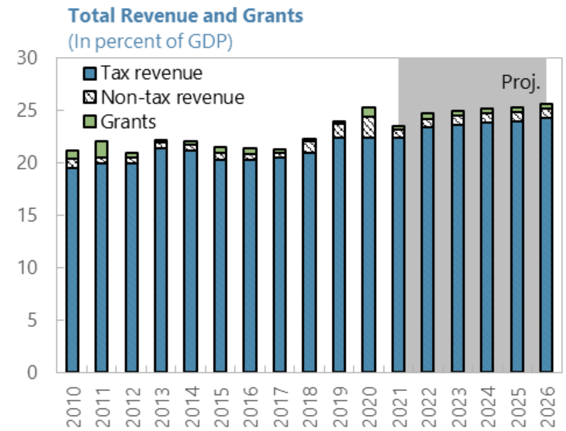
Sources: National authorities, IMF Information Notice Systems Database, and IMF staff calculations.

Figure 3. Armenia: Fiscal Developments

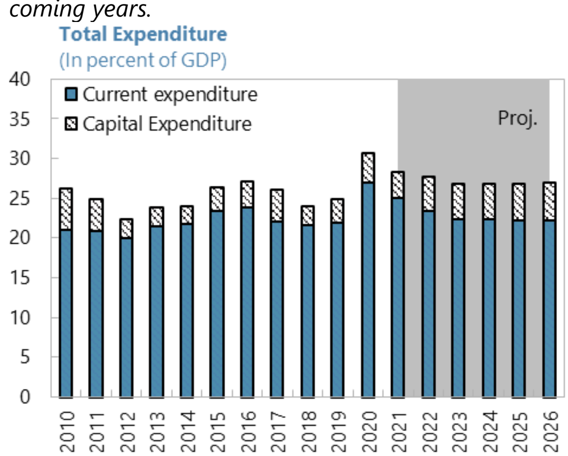
Following the twin shock, central government public debt peaked in 2020–21 and is projected to decline in line with the fiscal rule.



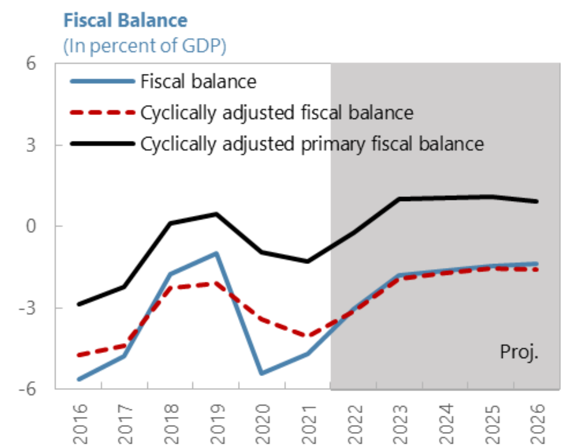
Revenues had been stable but is expected to decrease in 2021 following the twin shocks but projected to increase again in 2022–23.



Current and capital expenditures had increased significantly in 2020 but expected to decline in the coming years.



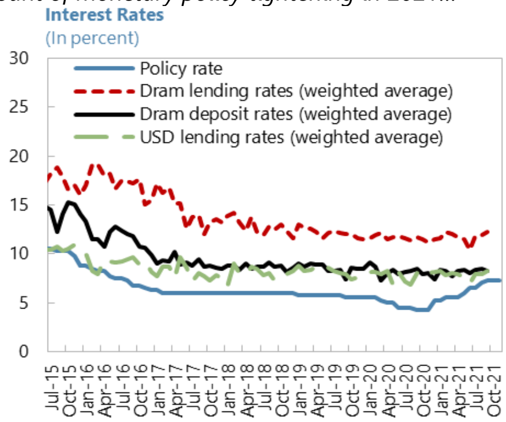
Cyclically adjusted deficit peaked as a result of the recent pandemic and political conflict.



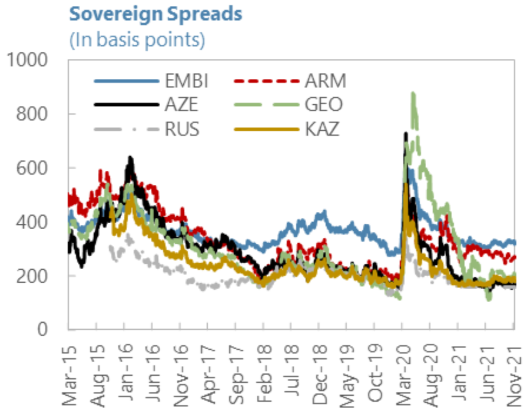
Sources: National authorities and IMF staff calculations.

Figure 4. Armenia: Monetary Developments

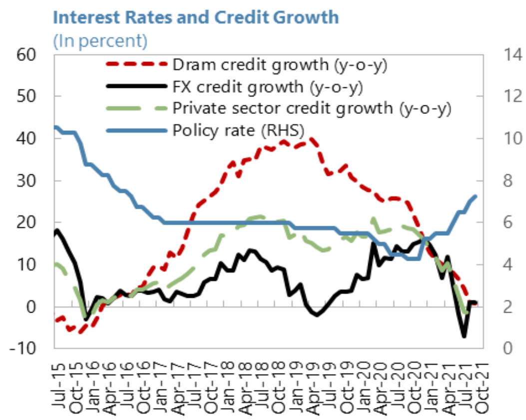
Short-term interest rates have somewhat increased on account of monetary policy tightening in 2021…



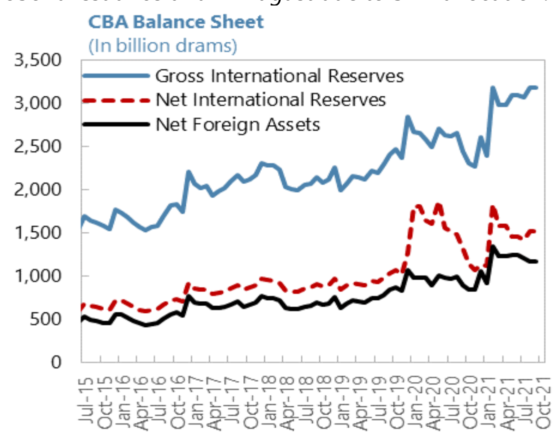
… while sovereign spreads have been volatile on account of economic and political developments.



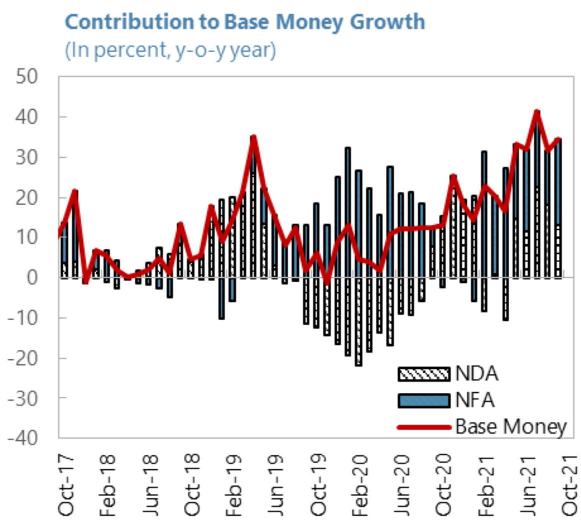
Credit growth is on a sharp declining path in 2021 as banks are becoming more risk averse.



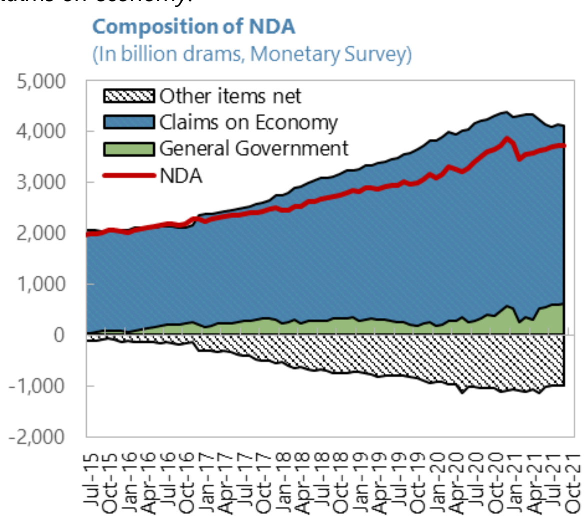
The CBA's net foreign assets increased in January due to the Eurobond issuance and in August due to SDR allocation.



Base money growth in 2021 was driven both by NDA and NFA increase.



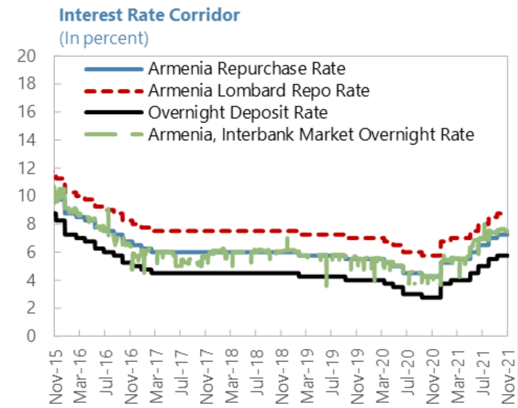
The main component in the rise of NDA remains growth in claims on economy.



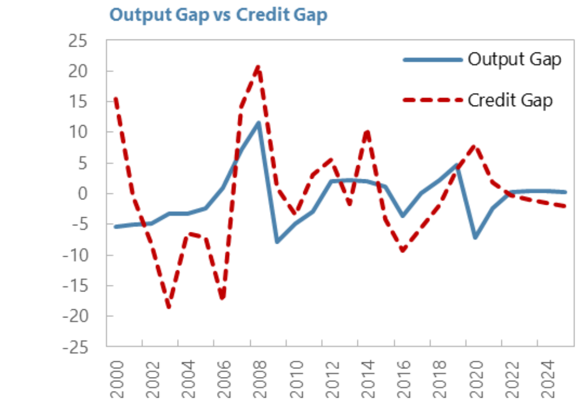
Source: Central Bank of Armenia, Bloomberg, JPMorgan EMBIG Diversified Index, and IMF Staff Calculations.

Figure 5. Armenia: Financial Developments

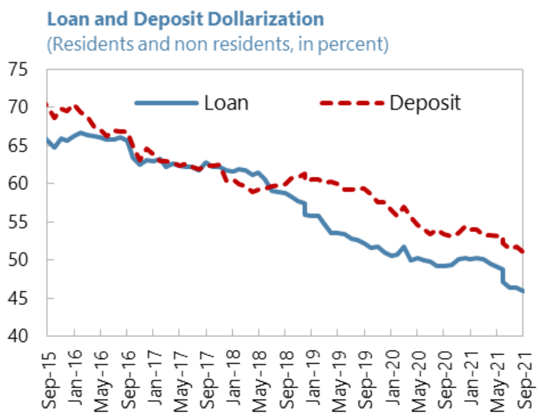
The CBA started increasing the policy rate in end-2020, with a cumulative raise of 300 bps. through September.



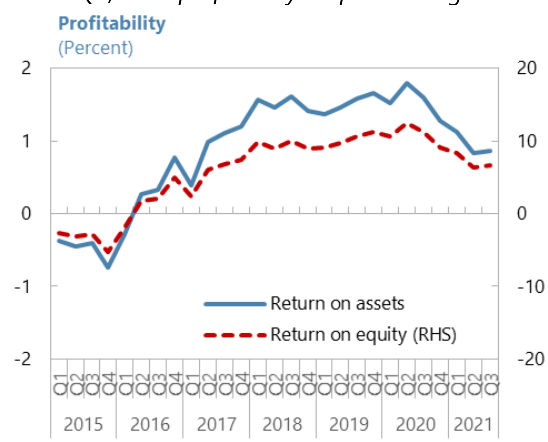
The credit-to-GDP gap is estimated to be marginally negative.



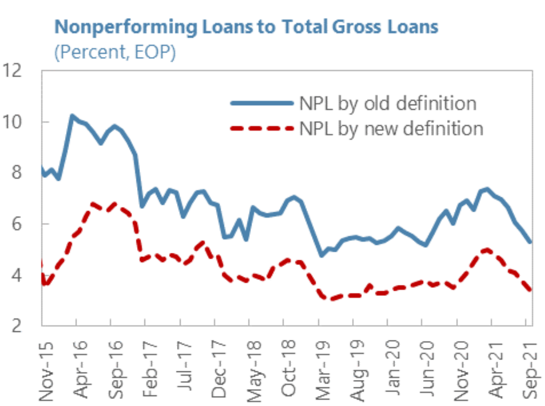
Credit and deposit dollarization, although somewhat moderated, remain significant.



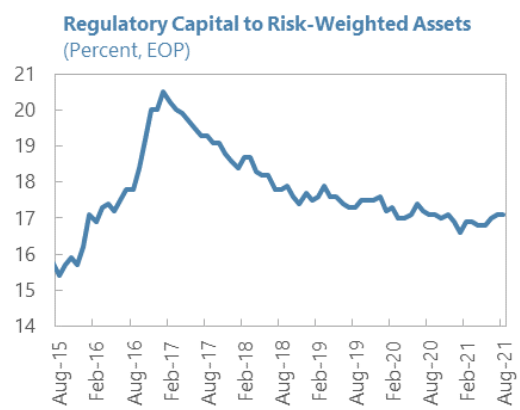
With most FSIs improving towards their pre-COVID level since 2021Q2, bank profitability keeps declining.



Non-performing loans have been declining after a sharp jump during the pandemic…



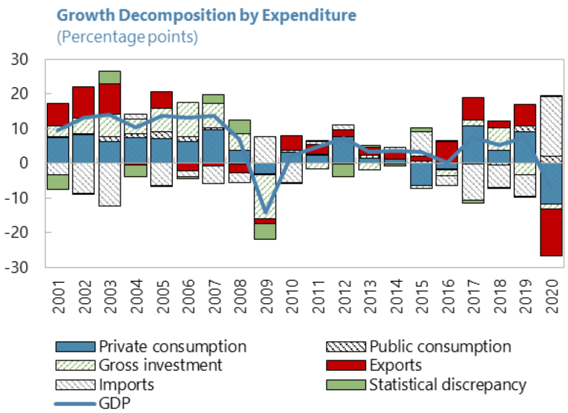
…while bank capital remained well above the minimum CAR.



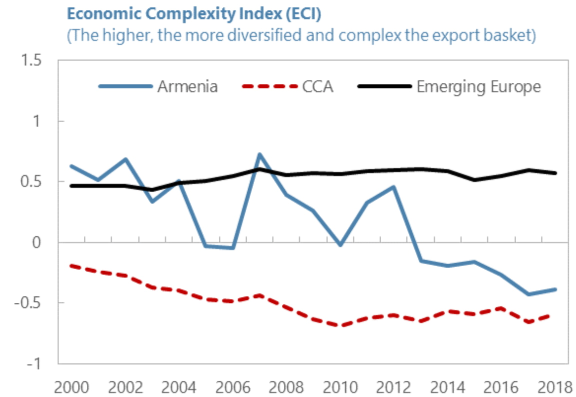
Sources: Haver, National authorities, Central Bank of Armenia, Bloomberg, and IMF staff calculations.
Note: In July 2021, the Central Bank of Armenia aligned the NPL definition with the BCBS regulation identified in the 2019 FSAP recommendation. New NPL definition only considers exposures which are more than 90 days past due (doubtful and substandard loans). On this definition, August NPLs are 3.4 percent of loans (vs 5.3 percent on old definition).

Figure 6. Armenia: Challenges to Boost Long-term Tradables-led and Inclusive Growth

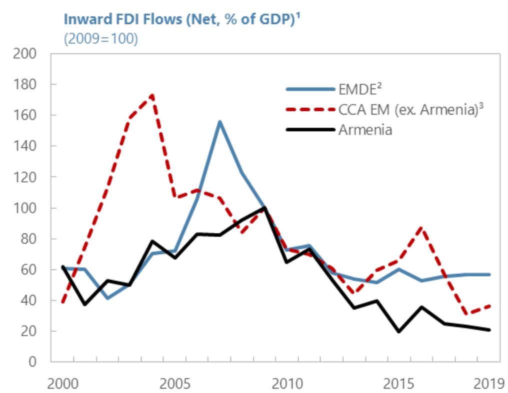
The role of exports as a driver of economic growth has been uneven over the past decades.



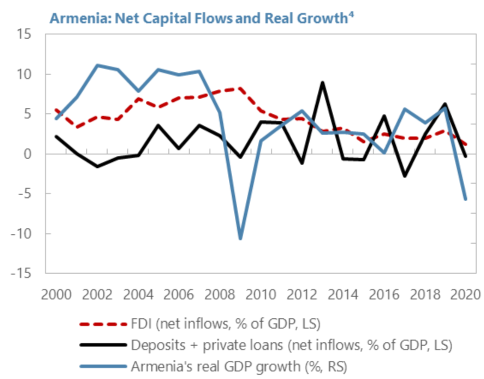
Armenia has been losing positions in export complexity ranking, both in goods and services.



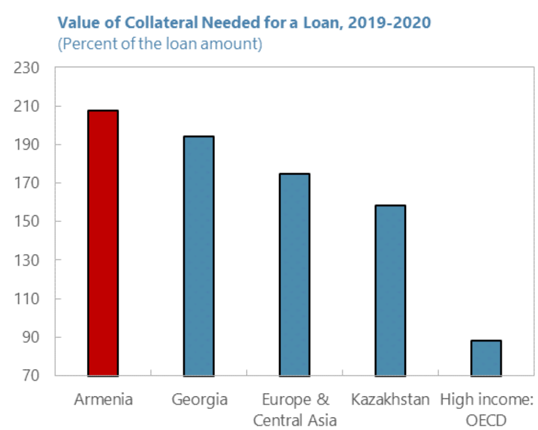
...and the decline in inward FDI sharper than in peer countries...



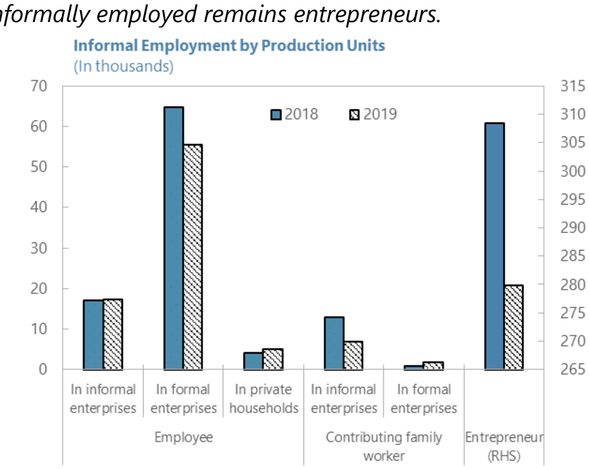
...has led to greater reliance on less stable debt-based external financing, necessitating reforms to support export-led growth and sustainable financing.



Improving financial inclusion and lowering collateral requirements will help facilitate access to financing.



Despite a sizable decline in the number of informal self-employed in 2019 (vs 2018), the largest share of the informally employed remains entrepreneurs.



Sources: National authorities, Armstat, Armenian Labor Force Surveys 2018-20, UNCTADstat, The WB World Development Indicators, IMF World Economic Outlook, and IMF staff calculations.

Note: [1]Net inward FDI flows by non-residents. [2]EMDE is Emerging and Developing Europe. Hungary excluded given the high volatility of inward FDI. [3]CCA EM are Azerbaijan, Georgia, Kazakhstan, and Turkmenistan. [4]Net capital inflows are calculated by net inflows by non-residents minus net outflows by residents.

Table 1. Armenia: Selected Economic and Financial Indicators, 2018–26

	2018	2019	2020	2021		2022	2023	2024	2025	2026
	Act.	Act.	Act.	EBS 20/178	Proj.			Proj.		
National income and prices:										
Real GDP (percent change)	5.2	7.6	-7.4	1.0	5.5	5.3	5.0	4.8	4.8	4.8
Final consumption expenditure, Contrib. to Growth	3.5	10.7	-9.7	2.5	5.5	4.4	3.8	2.7	2.3	2.2
Gross fixed capital formation, Contrib. to Growth	0.8	0.7	-1.4	-1.0	1.3	1.4	1.9	2.1	2.5	2.6
Changes in inventories, Contrib. to Growth	5.5	-3.9	0.4	0.0	-1.8	0.0	0.0	0.0	0.0	0.0
Net exports of goods and services, Contrib. to Growth	-4.6	0.2	3.4	-0.5	0.5	-0.5	-0.7	-0.1	-0.1	-0.1
Gross domestic product (in billions of drams)	6,017	6,543	6,182	6,344	7,031	7,869	8,639	9,420	10,243	11,121
Gross domestic product (in millions of U.S. dollars)	12,458	13,619	12,641	12,819	13,888	15,729	16,671	17,823	19,217	20,732
Gross domestic product per capita (in U.S. dollars)	4,196	4,597	4,267	4,317	4,688	5,309	5,627	6,015	6,485	6,995
CPI (period average; percent change)	2.5	1.4	1.2	2.1	7.2	6.6	5.1	4.5	4.2	4.1
CPI (end of period; percent change)	1.8	0.7	3.7	2.3	8.5	5.5	4.5	4.0	4.0	4.0
GDP deflator (percent change)	2.8	1.0	2.0	2.3	7.8	6.3	4.5	4.1	3.8	3.6
Unemployment rate (in percent)	19.0	18.3	18.1	24.3	18.5	18.3	17.8	17.5	17.3	17.0
Investment and saving (in percent of GDP)										
Investment	22.4	17.4	18.5	16.4	16.7	17.5	18.0	18.4	18.9	19.5
National savings	15.4	10.0	14.7	9.9	14.6	14.0	13.3	12.9	13.2	13.8
Money and credit (end of period)										
Reserve money (percent change)	17.8	8.8	18.3	7.3	19.3	5.5	7.2	7.3	7.6	7.7
Broad money (percent change)	7.4	11.2	9.0	12.6	16.3	9.8	14.3	9.7	8.1	8.0
Private sector credit growth (percent change)	17.2	18.5	14.3	6.0	0.0	4.5	7.2	7.0	7.2	7.2
Central government operations (in percent of GDP)										
Revenue and grants	22.3	23.9	25.2	23.6	23.6	24.7	25.0	25.2	25.3	25.6
Of which : tax revenue	20.6	22.1	22.0	22.1	21.8	22.6	22.7	22.9	23.1	23.4
Expenditure	24.0	24.9	30.6	29.2	28.2	27.8	26.7	26.7	26.6	26.8
Overall balance on a cash basis	-1.8	-1.0	-5.4	-5.6	-4.7	-3.1	-1.8	-1.5	-1.3	-1.2
Public and publicly-guaranteed (PPG) debt (in percent of GDP)	55.7	53.7	67.4	72.5	64.6	63.6	61.2	58.9	56.5	54.4
Central Government's PPG debt (in percent)	51.2	50.1	63.5	69.4	61.5	61.6	59.6	57.7	55.7	53.8
Share of foreign currency debt (in percent)	80.0	80.6	76.0	72.3	72.6	70.6	70.3	68.5	67.7	67.6
External sector										
Exports of goods and services (in millions of U.S. dollars)	4,942	5,718	3,763	4,078	4,559	5,295	5,816	6,381	6,807	7,262
Imports of goods and services (in millions of U.S. dollars)	-6,642	-7,513	-5,019	-5,780	-5,730	-6,672	-7,459	-8,197	-8,735	-9,303
Exports of goods and services (percent change)	12.1	15.7	-34.2	8.8	21.2	16.1	9.8	9.7	6.7	6.7
Imports of goods and services (percent change)	17.5	13.1	-33.2	7.6	14.2	16.4	11.8	9.9	6.6	6.5
Current account balance (in percent of GDP)	-7.0	-7.4	-3.8	-6.5	-2.1	-3.5	-4.8	-5.4	-5.6	-5.7
FDI (net, in millions of U.S. dollars)	260	234	74	196	223	259	337	421	467	481
Gross international reserves (in millions of U.S. dollars)	2,259	2,850	2,616	2,534	3,101	3,207	3,320	3,377	3,394	3,402
Import cover 1/	3.6	6.8	5.5	4.6	5.6	5.2	4.9	4.6	4.4	4.1
End-of-period exchange rate (dram per U.S. dollar)	484	480	523	…	…	…	…	…	…	…
Average exchange rate (dram per U.S. dollar)	483	480	489	…	…	…	…	…	…	…

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

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

Table 2. Armenia: Balance of Payments, 2018–26
(In millions of U.S. dollars, unless otherwise indicated)

	2018	2019	2020	2021	2022	2023	2024	2025	2026
	Act.	Act.	Act.			Proj.			
Current account	-876	-1,002	-479	-291	-553	-796	-969	-1,078	-1,182
Trade balance	-1,724	-1,728	-1,356	-1,308	-1,494	-1,673	-1,773	-1,879	-1,985
Exports	2,724	3,288	2,658	3,062	3,258	3,455	3,663	3,879	4,107
Imports	-4,448	-5,015	-4,014	-4,369	-4,752	-5,128	-5,436	-5,759	-6,092
Services (net)	25	-67	100	137	117	31	-43	-49	-55
Credits	2,218	2,431	1,105	1,498	2,037	2,361	2,718	2,928	3,156
Debits	-2,194	-2,497	-1,005	-1,361	-1,920	-2,330	-2,761	-2,976	-3,211
Income (net)	200	179	-196	-187	-140	-85	-54	-19	18
Transfers (net)	624	614	974	1,067	965	932	900	870	841
Private	479	468	754	920	819	786	755	725	696
Official	144	145	220	146	146	145	145	145	145
Capital and financial account	773	1,164	569	594	666	1,016	1,215	1,252	1,257
Capital transfers (net)	68	54	45	58	53	53	53	53	53
Foreign direct investment (net)	260	234	74	223	259	337	421	467	481
Portfolio investment (net)	-33	8	-49	0	0	0	0	0	0
Public sector borrowing (net)	168	292	-212	670	202	244	276	288	286
Disbursements	320	859	100	912	464	527	565	1,088	683
Amortization	-152	-567	-312	-242	-263	-282	-289	-800	-398
Other capital (net)	311	575	378	-357	152	382	465	444	438
Errors and omissions	113	502	-255	0	0	0	0	0	0
Overall balance	10	663	-497	303	113	219	245	175	75
Financing	-10	-663	497	-377	-150	-219	-245	-175	-75
Gross international reserves (increase: -)	55	-590	234	-486	-106	-113	-56	-17	-8
Use of Fund credit, net	-65	-73	263	-67	-44	-106	-189	-157	-67
Of which: IMF (SBA) budget support	0	0	332	0	0	0	0	0	0
SDR allocation	0	0	0	176	0	0	0	0	0
Financing needs	0	0	0	74	37	0	0	0	0
IMF (SBA) budget support	0	0	0	74	0	0	0	0	0
IMF (SBA) BOP support	0	0	0	0	37	0	0	0	0
Memorandum items:									
Current account (in percent of GDP)	-7.0	-7.4	-3.8	-2.1	-3.5	-4.8	-5.4	-5.6	-5.7
Trade balance (in percent of GDP)	-13.8	-12.7	-10.7	-9.4	-9.5	-10.0	-9.9	-9.8	-9.6
Gross international reserves (end of period)	2,259	2,850	2,616	3,101	3,207	3,320	3,377	3,394	3,402
In months of next year's imports	3.6	6.8	5.5	5.6	5.2	4.9	4.6	4.4	4.1
In percent of IMF's Reserve Adqeuacy Metric (ARA)	96	121	122	139	140	138	135	132	129
Goods export growth, percent change	14.1	20.7	-19.2	15.2	6.4	6.1	6.0	5.9	5.9
Goods import growth, percent change	17.4	12.8	-20.0	8.9	8.8	7.9	6.0	5.9	5.8
Nominal external debt	10,697	12,121	12,652	13,393	13,849	14,274	14,783	15,370	16,035
o.w. public external debt	5,536	5,785	6,053	6,728	6,924	7,064	7,156	7,331	7,594
Nominal external debt stock (in percent of GDP)	85.9	89.0	100.1	96.4	88.0	85.6	82.9	80.0	77.3
External public debt-to-exports ratio (in percent)	112.0	101.2	160.9	147.6	130.8	121.5	112.1	107.7	104.6
External public debt service (in percent of exports)	7.5	14.5	15.1	10.4	8.7	9.2	9.6	15.1	7.0

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

Table 3a. Armenia: Central Government Operations, 2018–26
(In billions of Armenian drams)

	2018	2019	2020	2021	2022	2023	2024	2025	2026
	Act.	Act.	Act.			Proj.			
Total revenue and grants	1,341.7	1,565.5	1,560.7	1,656.3	1,943.2	2,155.4	2,371.5	2,591.3	2,843.3
Total revenue	1,330.5	1,553.1	1,507.5	1,631.9	1,902.4	2,114.6	2,330.7	2,550.4	2,802.4
Tax revenues 1/	1,240.7	1,445.6	1,360.5	1,532.3	1,781.2	1,965.1	2,161.1	2,366.1	2,602.3
VAT	438.2	506.5	471.6	531.2	621.7	691.1	763.0	834.8	923.0
Profits, simplified and presumptive	170.4	234.0	148.8	219.8	251.8	285.1	310.9	338.0	367.0
Personal income tax	356.6	440.8	411.5	421.8	427.7	454.1	499.3	542.9	589.4
Customs duties	80.2	95.1	68.3	98.7	110.2	116.6	127.2	138.3	150.1
Other	195.3	169.2	260.3	280.9	369.9	418.2	460.8	512.1	572.7
Social contributions	17.4	18.7	24.7	46.7	59.0	71.7	84.8	92.2	100.1
Other revenue	72.3	88.8	122.2	52.9	62.2	77.7	84.8	92.2	100.1
Grants	11.2	12.4	53.2	24.4	40.8	40.8	40.8	40.8	40.8
Total expenditure	1,447.1	1,629.4	1,894.6	1,986.0	2,184.9	2,310.4	2,516.7	2,725.7	2,982.2
Expenses	1,299.0	1,437.1	1,668.5	1,762.2	1,843.3	1,934.6	2,097.5	2,259.7	2,448.4
Wages	304.4	327.0	380.8	414.1	443.0	475.1	518.1	563.3	611.6
Payments to individual pension accts.	29.0	49.4	59.9	52.4	55.1	63.9	69.7	75.8	82.3
Subsidies	4.3	4.4	1.7	5.2	7.9	8.6	9.4	10.2	11.1
Interest	139.0	157.6	164.6	197.1	221.3	234.4	242.7	253.1	258.7
Social allowances and pensions	396.5	403.9	499.9	489.0	516.8	591.8	678.3	737.5	811.8
Pensions/social security benefits	265.7	269.9	297.1	299.2	328.4	384.4	442.8	481.4	533.8
Social assistance benefits	130.8	134.0	202.9	189.8	188.3	207.3	235.5	256.1	278.0
Goods and services	98.6	128.1	114.1	127.7	137.7	151.2	164.9	179.2	194.6
Grants	126.3	150.0	185.5	175.8	228.3	224.6	216.7	235.6	255.8
Other expenditure 2/	200.8	216.8	261.9	301.0	233.3	184.9	197.8	204.9	222.4
Transactions in nonfinancial assets	148.1	192.3	226.2	223.8	341.5	375.8	419.2	466.0	533.8
Acquisition of nonfinancial assets	152.0	193.0	227.7	223.8	341.5	375.8	419.2	466.0	533.8
Disposals of nonfinancial assets	3.9	0.7	1.5	0.0	0.0	0.0	0.0	0.0	0.0
Overall balance (above-the-line)	-105.4	-63.9	-334.0	-329.7	-241.6	-154.9	-145.2	-134.4	-138.9
Statistical discrepancy	0.8	-4.3	14.7	0.0	0.0	0.0	0.0	0.0	0.0
Overall balance (below-the-line)	-104.6	-68.2	-319.2	-329.7	-241.6	-154.9	-145.2	-134.4	-138.9
Financing	104.6	68.2	319.2	329.7	241.6	154.9	145.2	134.4	138.9
Domestic financing	69.4	-13.3	342.3	73.1	271.8	160.1	236.6	191.1	102.6
Banking system	109.8	-39.1	306.7	146.1	254.9	85.6	193.5	156.2	83.9
CBA	43.4	-96.5	59.2	-60.5	61.0	0.0	0.0	0.0	0.0
Commercial Banks	66.4	57.5	247.5	206.6	193.9	85.6	193.5	156.2	83.9
Nonbanks	-40.4	25.7	35.7	-73.0	16.9	74.4	43.2	34.9	18.7
T-Bills/other	-13.5	41.5	55.2	-27.9	43.3	19.1	43.2	34.9	18.7
Promissory note/other	0.0	0.0	0.0	-0.1	0.0	0.0	0.0	0.0	0.0
Net lending	-26.9	-15.8	-19.6	-45.0	-26.4	55.3	0.0	0.0	0.0
External financing	35.2	81.6	-23.1	256.6	-30.2	-5.1	-91.4	-56.6	36.3
Gross disbursement	154.4	412.8	211.2	499.1	232.2	234.2	210.8	511.1	346.6
of which : IMF budget support	0.0	0.0	162.5	37.4	0.0	0.0	0.0	0.0	0.0
Amortization due	-68.5	-274.2	-152.4	-114.5	-117.9	-167.9	-224.4	-483.0	-218.4
Net lending	-50.8	-57.1	-81.8	-128.0	-144.5	-71.4	-77.9	-84.7	-91.9
Memorandum items:									
Nominal GDP (in billion of drams)	6,017.0	6,543.3	6,181.7	7,031.2	7,869.4	8,638.9	9,420.2	10,242.7	11,120.8
Program balance 3/	-155.7	-90.1	-401.9	-477.7	-393.0	-171.0	-223.1	-219.1	-230.8
Primary balance 4/	-44.1	20.7	-270.8	-305.6	-191.2	63.4	19.6	34.0	27.9

Sources: Ministry of Finance, Central Bank of Armenia, and Fund staff estimates and projections.

1/ From 2018, the temporary tax credits used to cover tax obligations are not included in total tax revenues and are also not netted out from individual tax categories.

2/ Includes acquisition of military equipment.

3/ The program balance is measured as below-the-line balance minus net lending.

4/ Sum of overall balance (above the line), interest expense, and domestic and external net lending.

Table 3b. Armenia: Central Government Operations, 2018–26

(In percent of GDP, unless otherwise specified)

	2018	2019	2020	2021	2022	2023	2024	2025	2026
	Act.	Act.	Act.			Proj.			
Total revenue and grants	22.3	23.9	25.2	23.6	24.7	25.0	25.2	25.3	25.6
Total revenue	22.1	23.7	24.4	23.2	24.2	24.5	24.7	24.9	25.2
Tax revenues 1/	20.6	22.1	22.0	21.8	22.6	22.7	22.9	23.1	23.4
VAT	7.3	7.7	7.6	7.6	7.9	8.0	8.1	8.2	8.3
Profits, simplified and presumptive	2.8	3.6	2.4	3.1	3.2	3.3	3.3	3.3	3.3
Personal income tax	5.9	6.7	6.7	6.0	5.4	5.3	5.3	5.3	5.3
Customs duties	1.3	1.5	1.1	1.4	1.4	1.4	1.4	1.4	1.4
Other	3.2	2.6	4.2	4.0	4.7	4.8	4.9	5.0	5.2
Social contributions	0.3	0.3	0.4	0.7	0.8	0.8	0.9	0.9	0.9
Other revenue	1.2	1.4	2.0	0.8	0.8	0.9	0.9	0.9	0.9
Grants	0.2	0.2	0.9	0.3	0.5	0.5	0.4	0.4	0.4
Total expenditure	24.0	24.9	30.6	28.2	27.8	26.7	26.7	26.6	26.8
Expense	21.6	22.0	27.0	25.1	23.4	22.4	22.3	22.1	22.0
Wages	5.1	5.0	6.2	5.9	5.6	5.5	5.5	5.5	5.5
Payments to individual pension accts.	0.5	0.8	1.0	0.7	0.7	0.7	0.7	0.7	0.7
Subsidies	0.1	0.1	0.0	0.1	0.1	0.1	0.1	0.1	0.1
Interest	2.3	2.4	2.7	2.8	2.8	2.7	2.6	2.5	2.3
Social allowances and pensions	6.6	6.2	8.1	7.0	6.6	6.9	7.2	7.2	7.3
Pensions/social security benefits	4.4	4.1	4.8	4.3	4.2	4.5	4.7	4.7	4.8
Social assistance benefits	2.2	2.0	3.3	2.7	2.4	2.4	2.5	2.5	2.5
Goods and services	1.6	2.0	1.8	1.8	1.8	1.8	1.8	1.8	1.8
Grants	2.1	2.3	3.0	2.5	2.9	2.6	2.3	2.3	2.3
Other expenditure 2/	3.3	3.3	4.2	4.3	3.0	2.1	2.1	2.0	2.0
Transactions in nonfinancial assets	2.5	2.9	3.7	3.2	4.3	4.4	4.5	4.6	4.8
Acquisition of nonfinancial assets	2.5	2.9	3.7	3.2	4.3	4.4	4.5	4.6	4.8
Disposals of nonfinancial assets	0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Overall balance (above-the-line)	-1.8	-1.0	-5.4	-4.7	-3.1	-1.8	-1.5	-1.3	-1.2
Statistical discrepancy	0.0	-0.1	0.2	0.0	0.0	0.0	0.0	0.0	0.0
Overall balance (below-the-line)	-1.7	-1.0	-5.2	-4.7	-3.1	-1.8	-1.5	-1.3	-1.2
Financing	1.7	1.0	5.2	4.7	3.1	1.8	1.5	1.3	1.2
Domestic financing	1.2	-0.2	5.5	1.0	3.5	1.9	2.5	1.9	0.9
Banking system	1.8	-0.6	5.0	2.1	3.2	1.0	2.1	1.5	0.8
CBA	0.7	-1.5	1.0	-0.9	0.8	0.0	0.0	0.0	0.0
Commercial Banks	1.1	0.9	4.0	2.9	2.5	1.0	2.1	1.5	0.8
Nonbanks	-0.7	0.4	0.6	-1.0	0.2	0.9	0.5	0.3	0.2
T-Bills/other	-0.2	0.6	0.9	-0.4	0.6	0.2	0.5	0.3	0.2
Promissory note/other	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Net lending	-0.4	-0.2	-0.3	-0.6	-0.3	0.6	0.0	0.0	0.0
External financing	0.6	1.2	-0.4	3.6	-0.4	-0.1	-1.0	-0.6	0.3
Gross disbursement	2.6	6.3	3.4	7.1	3.0	2.7	2.2	5.0	3.1
Amortization due	-1.1	-4.2	-2.5	-1.6	-1.5	-1.9	-2.4	-4.7	-2.0
Net lending	-0.8	-0.9	-1.3	-1.8	-1.8	-0.8	-0.8	-0.8	-0.8
Memorandum items:									
Nominal GDP (in billion of drams)	6,017	6,543	6,182	7,031	7,869	8,639	9,420	10,243	11,121
Program balance 3/	-2.6	-1.4	-6.5	-6.8	-5.0	-2.0	-2.4	-2.1	-2.1
Primary balance 4/	-0.7	0.3	-4.4	-4.3	-2.4	0.7	0.2	0.3	0.3

Sources: Ministry of Finance, Central Bank of Armenia, and Fund staff estimates and projections.

1/ From 2018, the temporary tax credits used to cover tax obligations are not included in total tax revenues and are also not netted out from individual tax categories.

2/ Includes acquisition of military equipment.

3/ The program balance is measured as below-the-line balance minus net lending.

4/ Sum of overall balance (above the line), interest expense, and domestic and external net lending.

Table 4. Armenia: Monetary Accounts, 2018–22
(In billions of drams, unless otherwise indicated)

	2018	2019	2020				2021				2022			
	Act.	Act.	Mar.	Jun.	Sep.	Dec.	Mar.	Jun.	Sep.	Dec.	Mar.	Jun.	Sep.	Dec.
			Act.				Act.				Proj.			
Central Bank of Armenia														
Net foreign assets	765.8	1071.8	988.2	988.6	899.5	1058.3	1267.7	1247.8	1169.5	1176.5	1114.5	1111.5	1111.5	1108.8
Net international reserves 1/	679.6	865.4	820.2	745.9	655.9	603.9	903.5	736.7	739.9	681.1	620.3	620.4	621.6	622.1
Other	86.2	206.3	168.0	242.7	243.6	454.4	364.2	511.1	429.6	495.4	494.1	491.1	489.8	486.8
Net domestic assets	449.8	250.5	255.6	277.3	373.4	505.3	229.9	424.2	542.3	688.3	753.6	778.8	804.1	859.3
Claims on general government (net)	-172.3	-314.1	-349.7	-418.8	-332.3	-254.9	-555.0	-524.2	-492.5	-328.0	-312.7	-297.5	-282.2	-267.0
Of which : central government (net)	-124.5	-252.8	-291.3	-354.7	-260.7	-189.6	-482.1	-450.9	-414.6	-250.1	-234.8	-219.6	-204.3	-189.1
central government deposits	186.0	327.3	362.9	432.3	345.8	266.5	565.3	534.4	502.3	259.9	244.6	229.4	214.1	198.8
Claims on banks	299.1	231.7	275.1	364.1	390.1	467.9	502.5	627.9	694.9	694.9	704.9	714.9	714.9	714.9
Other items (net)	323.0	332.9	330.2	331.9	315.6	292.3	282.4	320.4	339.9	321.4	361.4	361.4	371.4	411.4
Reserve money	1,215.6	1,322.2	1,243.8	1,265.9	1,272.8	1,563.7	1,497.5	1,672.0	1,711.8	1,864.8	1,868.0	1,890.3	1,915.5	1,968.1
Currency issue	566.7	607.2	554.4	589.0	633.2	751.5	680.9	709.3	712.3	733.9	700.4	722.5	737.0	763.8
Banks' reserves	596.7	674.3	649.6	639.9	602.1	758.7	760.2	910.1	952.2	1,083.4	1,120.3	1,120.4	1,131.2	1,156.9
In drams	351.9	304.8	301.3	366.9	316.0	275.4	343.6	354.0	385.5	466.7	503.6	503.7	514.5	540.2
In foreign currency	244.8	369.4	348.3	273.0	286.2	483.3	416.6	556.1	566.7	616.7	616.7	616.7	616.7	616.7
Other accounts	52.2	40.8	39.7	37.0	37.5	53.6	56.4	52.6	47.4	47.4	47.4	47.4	47.4	47.4
Banking system														
Net foreign assets	-78.7	-70.0	-241.1	-201.9	-380.1	-504.3	-139.8	-167.3	-132.0	-175.1	-237.1	-240.1	-240.1	-242.7
Net domestic assets	2,853.8	3,155.5	3,316.1	3,291.5	3,614.6	3,866.4	3,564.8	3,658.5	3,737.6	4,086.4	4,175.9	4,303.5	4,384.7	4,538.4
Claims on government (net)	343.8	259.3	275.7	263.6	402.0	565.7	344.1	544.8	612.4	699.3	763.0	826.8	890.5	954.2
Of which : claims on central government (net)	381.4	342.0	350.6	348.5	473.6	631.0	417.0	618.0	690.2	777.2	840.9	904.6	968.4	1,032.1
Claims on rest of the economy	3,232.0	3,830.6	4,006.1	4,051.9	4,254.2	4,378.5	4,339.1	4,137.1	4,115.2	4,378.5	4,404.2	4,468.1	4,485.6	4,575.5
Other items (net)	-722.0	-934.5	-965.7	-1,024.0	-1,041.5	-1,077.8	-1,118.4	-1,023.4	-990.0	-991.3	-991.3	-991.3	-991.3	-991.3
Broad money	2,775.1	3,085.5	3,075.0	3,089.6	3,234.5	3,362.0	3,425.0	3,491.1	3,605.5	3,911.3	3,938.8	4,063.4	4,144.6	4,295.6
Currency in circulation	477.0	502.3	474.8	508.7	550.2	648.4	596.2	623.1	617.5	629.9	594.3	613.1	625.3	648.1
Deposits	2,298.1	2,583.2	2,600.2	2,580.9	2,684.4	2,713.6	2,828.7	2,868.0	2,988.1	3,281.5	3,344.5	3,450.3	3,519.3	3,647.5
Domestic currency	1,089.8	1,400.8	1,390.2	1,450.7	1,531.7	1,535.5	1,560.1	1,622.0	1,698.1	1,944.3	1,973.5	2,059.9	2,095.0	2,189.4
Foreign currency	1,208.3	1,182.3	1,210.0	1,130.2	1,152.7	1,178.1	1,268.6	1,246.1	1,290.0	1,337.2	1,371.0	1,390.4	1,424.3	1,458.1
Memorandum items:														
Exchange rate (drams per U.S. dollar, end of period)	483.8	479.7	504.5	482.4	488.4	522.6	531.2	495.9	484.2	...	...	...	...	...
12-month change in reserve money (in percent)	17.8	8.8	4.0	12.1	12.6	18.3	20.4	32.1	34.5	19.3	24.7	13.1	11.9	5.5
12-month change in broad money (in percent)	7.4	11.2	11.8	10.6	11.9	9.0	11.4	13.0	11.5	16.3	15.0	16.4	15.0	9.8
12-month change in dram broad money (in percent)	14.7	21.5	19.2	21.7	22.6	14.8	15.6	14.6	11.2	17.9	19.1	19.1	17.5	10.2
12-month change in private sector credit (in percent)	17.2	18.5	19.7	17.5	18.4	14.3	8.3	2.1	-3.3	0.0	1.5	8.0	9.0	4.5
Velocity of broad money (end of period)	2.2	2.1	2.1	2.1	1.9	1.8	1.8	1.9	1.9	1.8	1.8	1.8	1.8	1.8
Money multiplier	2.3	2.3	2.5	2.4	2.5	2.2	2.3	2.1	2.1	2.1	2.1	2.1	2.2	2.2
Private sector credit (in percent of GDP)	53.7	58.5	64.8	65.5	68.8	70.8	61.7	58.8	58.5	62.3	62.6	63.5	63.8	65.1
Dollarization in bank deposits 2/	52.6	45.8	46.5	43.8	42.9	43.4	44.8	43.4	43.2	40.7	41.0	40.3	40.5	40.0
Dollarization in broad money 3/	43.5	38.3	39.3	36.6	35.6	35.0	37.0	35.7	35.8	34.2	34.8	34.2	34.4	33.9
Currency in circulation in percent of deposits	20.8	19.4	18.3	19.7	20.5	23.9	21.1	21.7	20.7	19.2	17.8	17.8	17.8	17.8
NIR (U.S. dollars, program exchange rate)	1,405.4	1,811.5	1,645.9	1,554.9	1,332.1	1,131.2	1,693.9	1,474.6	1,525.0	1,407.9	1,282.4	1,282.5	1,285.1	1,285.9
NIR (U.S. dollars, actual exchange rate)	1,404.9	1,804.1	1,625.9	1,546.4	1,342.3	1,155.6	1,700.9	1,485.8	1,528.1	1,407.9	1,282.4	1,282.5	1,285.1	1,285.9

Sources: Central Bank of Armenia; and Fund staff estimates and projections.

1/ In line with the TMU definition.
2/ Ratio of foreign currency deposits to total deposits (in percent).
3/ Ratio of foreign currency deposits to broad money (in percent).

Table 5. Armenia: Financial Soundness Indicators for the Banking Sector, 2018–21
(In percent, unless otherwise indicated)

	2018	2019				2020				2021		
	Dec	Mar	June	Sept	Dec	Mar	Jun	Sept	Dec	Mar	Jun	Sep
Capital adequacy												
Total regulatory capital to risk-weighted assets	17.7	17.9	17.4	17.5	17.6	17.0	17.4	17.1	16.9	17.0	17.0	17.2
Capital (net worth) to assets	15.0	15.0	14.7	14.8	14.1	14.1	14.6	14.0	13.1	13.3	13.0	12.8
Asset composition												
Sectoral distribution of loans (in billions of drams)												
Industry (excluding energy sector)	327.9	337.7	340.5	345.2	357.4	375.2	371.8	404.5	436.3	435.2	418.2	389.3
Energy sector	182.2	158.3	130.8	143.0	134.0	153.5	154.0	180.8	209.0	195.9	127.5	136.5
Agriculture	143.3	146.6	155.1	154.6	161.4	171.6	177.7	189.4	198.0	200.6	190.6	196.3
Construction	161.2	170.8	172.6	182.0	192.7	213.8	225.1	247.6	269.1	275.0	304.2	325.1
Transport and communication	106.4	105.4	102.9	105.5	101.7	114.7	108.4	110.4	141.8	139.8	129.6	121.8
Trade/commerce	441.1	443.5	460.9	467.5	508.6	501.1	513.4	537.7	533.9	532.8	501.3	481.0
Consumer credits	701.1	744.4	795.4	846.0	915.9	951.9	955.5	960.9	929.0	915.6	871.2	833.2
Mortgage loans	255.2	270.2	295.3	321.6	358.8	395.0	404.6	441.2	481.2	517.2	551.5	587.3
Sectoral distribution of loans to total loans (percent of total)												
Industry (excluding energy sector)	11.1	11.2	10.8	10.6	10.1	10.3	10.0	10.4	10.8	11.0	11.2	10.5
Energy sector	6.3	5.2	4.2	4.4	3.8	4.2	4.1	4.6	5.2	4.9	3.4	3.7
Agriculture	4.8	4.8	4.9	4.7	4.6	4.7	4.8	4.9	4.9	5.1	5.1	5.3
Construction	5.6	5.6	5.9	5.6	5.5	5.9	6.1	6.3	6.7	6.9	8.1	8.8
Transport and communication	3.6	3.5	3.3	3.2	2.9	3.2	2.9	2.8	3.5	3.5	3.5	3.3
Trade/commerce	14.7	14.7	14.7	14.3	14.4	13.8	13.8	13.8	13.2	13.4	13.4	13.0
Mortgage loans	8.7	8.9	9.4	9.8	10.2	10.8	10.9	11.3	11.9	13.0	14.8	15.8
Consumer credits	24.1	24.6	25.3	25.9	26.0	26.2	25.7	24.6	23.0	23.1	23.3	22.4
Other sectors	21.1	21.4	21.5	21.6	22.5	21.0	21.7	21.3	20.8	19.1	17.1	17.3
Foreign exchange loans to total loans	57.1	55.8	54.5	53.5	52.4	53.1	51.4	50.6	51.7	51.5	48.4	47.3
Asset quality												
Nonperforming loans (in billions of drams)	146.4	158.5	177.7	186.2	200.0	211.0	217.8	241.7	272.1	290.0	236.8	113.6
Watch (up to 90 days past due)	48.0	64.5	71.6	64.3	75.1	73.9	81.6	100.6	84.0	95.2	75.4	82.6
Substandard (91-180 days past due)	40.9	42.5	49.0	67.2	68.3	79.9	85.3	89.6	129.0	121.5	90.4	66.7
Doubtful (181-270 days past due)	57.5	51.6	57.1	54.7	56.6	57.2	50.8	51.4	59.1	73.3	71.0	46.9
Loss (>270 days past due, in billions of drams)	272.0	278.4	278.4	285.4	286.5	313.5	315.5	328.5	360.1	357.8	394.0	428.8
Nonperforming loans to gross loans	4.8	5.0	5.4	5.5	5.5	5.5	5.7	6.0	6.6	7.1	6.1	2.9
Provisions to nonperforming loans	56.6	52.1	50.9	51.1	49.9	48.7	46.2	41.8	45.0	45.2	49.4	84.1
Spread between highest and lowest rates of interbank borrowing in AMD	1.5	0.9	0.4	0.6	0.9	0.9	0.9	1.1	2.5	0.9	1.8	0.3
Spread between highest and lowest rates of interbank borrowing in FX	3.8	1.3	1.0	0.4	1.7	0.6	0.1	1.5	2.1	0.4	0.3	0.0
Earnings and profitability												
ROA (profits to period average assets)	1.2	1.6	1.4	1.6	1.7	1.52	1.79	1.60	1.28	1.12	0.84	0.9
ROE (profits to period average equity)	7.6	10.4	9.6	10.7	11.2	10.6	12.4	11.3	9.0	8.3	6.3	6.6
Interest margin to gross income	32.1	32.1	31.8	31.9	31.8	33.3	33.7	33.6	33.7	35.2	34.5	33.5
Interest income to gross income	75.1	75.7	75.2	74.3	73.4	74.7	75.5	75.4	74.7	76.7	76.5	76.3
Noninterest expenses to gross income	33.4	30.9	30.0	29.8	30.6	28.8	27.6	27.1	27.1	26.7	28.7	28.6
Liquidity												
Liquid assets to total assets	27.3	27.2	27.2	27.6	27.1	27.0	26.9	27.7	25.6	28.1	30.8	31.7
Liquid assets to total short-term liabilities	116.6	116.0	111.4	108.2	111.7	118.5	119.3	117.0	108.8	117.6	122.1	120.1
Customer deposits to total (non-interbank) loans	111.9	110.4	109.3	109.5	112.1	109.7	107.1	105.2	106.9	108.7	115.3	117.3
Foreign exchange liabilities to total liabilities	58.3	56.9	56.6	56.6	55.4	56.0	52.6	52.5	52.8	52.1	49.8	48.4
Sensitivity to market risk												
Gross open positions in foreign exchange to capital	6.1	3.7	3.7	4.6	4.0	4.3	3.1	3.1	4.5	4.2	3.6	5.5
Net open position in FX to capital	-3.2	-0.1	0.5	-2.0	0.3	-3.6	0.3	1.1	1.3	-2.1	-0.1	1.5

Source: Central Bank of Armenia.

Note: In July 2021, the CBA aligned the NPL definition with the BCBS regulation. New NPL definition only takes into account exposures that are more than 90 days past due (doubtful and substandard loans)

Table 6. Armenia: Fund Credit Available and Timing of Reviews Under the Standby Arrangement

Date of Availability[1/]	Conditions	Amount (millions of SDRs)	Percent of Quota	Percent of Quota (cumulative)
May 17, 2019	Board approval of the arrangement	25.714	19.96	19.96
September 30, 2019	Observance of end-June 2019 performance criteria and continuous performance criteria, and completion of first review	25.714	19.96	39.93
May 18, 2020	Observance of end-December 2019 performance criteria and continuous performance criteria, and completion of second review	154.514	119.96	159.89
October 15, 2020	Observance of end-June 2020 performance criteria and continuous performance criteria, and completion of third review	25.714	19.96	179.86
May 20, 2021	Observance of end-December 2020 performance criteria and continuous performance criteria, and completion of fourth review	25.714	19.96	199.82
October 15, 2021	Observance of end-June 2021 performance criteria and continuous performance criteria, and completion of fifth review	25.714	19.96	219.79
April 15, 2022	Observance of end-December 2021 performance criteria and continuous performance criteria, and completion of sixth review	25.716	19.97	239.75
	Total	308.8	239.75	239.75

Sources: Fund staff estimates and projections.

1/ The fourth review was delayed because of elections. The fourth and fifth reviews will be combined.

Table 7. Armenia: Indicators of Capacity to Repay the Fund, 2020–26

	2020	2021	2022	2023	2024	2025	2026
		Projections					
Fund obligations based on existing and prospective credit (in millions of SDRs)							
Principal	49.9	46.5	30.3	72.9	135.0	106.3	38.7
Charges and interest	4.7	5.6	5.8	5.6	3.0	1.2	0.4
Fund obligations based on existing and prospective credit							
In millions of SDRs	54.6	52.2	36.1	78.5	137.9	107.4	39.1
In millions of US$	76.1	74.6	52.1	114.5	202.9	159.2	58.3
In percent of Gross International Reserves	2.9	2.4	1.6	3.4	6.0	4.7	1.7
In percent of exports of goods and services	2.0	1.6	1.0	2.0	3.2	2.3	0.8
In percent of debt service	13.4	15.8	11.3	21.4	32.6	15.1	11.0
In percent of GDP	0.6	0.5	0.3	0.7	1.1	0.8	0.3
In percent of quota	42.4	40.5	28.0	60.9	107.1	83.4	30.4
Outstanding Fund credit based on existing and prospective drawings							
In millions of SDRs	360.2	365.1	360.5	287.7	159.1	52.8	7.7
In billions of US$	0.50	0.52	0.52	0.42	0.23	0.08	0.01
In percent of Gross International Reserves	19.2	16.8	16.2	12.6	6.9	2.3	0.3
In percent of exports of goods and services	13.3	11.5	9.8	7.2	3.7	1.2	0.2
In percent of debt service	88.5	110.5	113.0	78.4	37.6	7.4	2.2
In percent of GDP	4.0	3.8	3.3	2.5	1.3	0.4	0.1
In percent of quota	279.7	283.5	279.9	223.3	123.5	41.0	6.0
Net use of Fund credit (millions of SDRs) existing and prospective	181.7	4.9	-4.6	-72.9	-135.0	-106.3	-38.7
Disbursements	231.7	51.4	25.7	0.0	0.0	0.0	0.0
Repayments and Repurchases	49.9	46.5	30.3	72.9	135.0	106.3	38.7

Sources: IMF staff estimates and projections.

Table 8. Armenia: External Financing Requirements and Sources, 2020–26
(In millions of U.S. dollars, unless otherwise indicated)

	2020	2021	2022	2023	2024	2025	2026
		Proj.					
Gross Financing Requirements	1,599	2,153	1,930	2,230	2,404	2,922	2,496
External current account deficit (excl. transfers)	1,452	1,358	1,518	1,728	1,870	1,947	2,022
Debt amortization and Fund repurchases	381	309	306	389	478	957	465
Gross international reserve accumulation 1/	-234	486	106	113	56	17	8
Of which: IMF repurchases and repayments	70	67	44	106	189	157	67
Available financing	1,599	2,079	1,893	2,230	2,404	2,922	2,496
Capital and Financial Account and Current Transfers	1,599	2,079	1,893	2,230	2,404	2,922	2,496
of which: Capital transfers (net)	45	58	53	53	53	53	53
Foreign Direct Investment (net)	74	223	259	337	421	467	481
Public Borrowing (net)	120	670	202	244	276	288	285
Disbursements	432	912	464	527	565	1,088	683
Amortization	-312	-242	-263	-282	-289	-800	-398
SDR allocation	0	176	0	0	0	0	0
Private transfers (net)	754	920	819	786	755	725	696
Other private capital (net)	379	-357	152	382	465	444	438
Financing needs	0	74	37	0	0	0	0
IMF (SBA) budget support	0	74	0	0	0	0	0
IMF (SBA) BOP support	0	0	37	0	0	0	0
Memorandum item:							
Current Account deficit, percent of GDP	-3.8	-2.1	-3.5	-4.8	-5.4	-5.6	-5.7
Gross Reserves	2,616	3,101	3,207	3,320	3,377	3,394	3,402
In percent of ARA metric 1/	122	138	139	138	135	132	129
In months of prospective imports	5.5	5.6	5.2	4.9	4.6	4.4	4.1

1/ ARA metric for Assesing Reservers Adequacy (floating)

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

Annex I. Public Debt Sustainability Analysis[1]

Results from an updated DSA using the staff's baseline projections indicate that, due to a strong recovery in GDP growth compared to previous DSA (December 2020), Armenia's public debt remains sustainable, but both the high share of foreign currency debt and a sharp rise in the debt level are important sources of vulnerability. Alternative scenarios and stress tests suggest that shocks to growth and the exchange rate would have the largest impact on debt dynamics and government financing needs.

1. Debt increased substantially in 2020 due to higher spending related to the twin shocks, although reflecting measures starting in 2022, it is projected to decline to around 54.4 percent over the medium-term. The fiscal deficit turns out to be 5.4 percent of GDP in 2020. In 2021, the budget envisages a deficit of 4.7 percent of GDP, which the government financed from international markets by issuing 10 years Eurobond worth $750 million at favorable 3.9 percent interest rate. As a result, the end-2021 central government debt will be around 61.5 percent of GDP reflecting the issuance of Eurobond. After 2021, gross financing needs are estimated to revert to the norm—around 7–8 percent of GDP in the medium term except in 2025 due to expected repayments on existing Eurobonds. After using the fiscal rule's escape clause during 2020–21, the authorities are committed to bringing the central government debt below 60 percent of GDP by 2026. The baseline scenario shows this goal is achievable given planned revenue measures and current spending restraint. The share of FX-denominated debt is projected to be around 68 percent in 2026, due to sizable planned external financing in 2021. The large residuals in 2021 reflect the large appreciation which has occurred this year.

2. Baseline projections are subject to significant uncertainty. Historically, Armenian growth, primary balance, and inflation have all been volatile, which implies potential uncertainty in the baseline projections. Assuming the symmetric distribution of shocks, a fan chart for the public debt-to-GDP ratio—corresponding to the range between the 10th and 90th percentiles—points to a range between 59 and 75 percent in 2021 and between 39 and 71 percent in 2026. An asymmetric fan chart, which rules out real exchange rate depreciation, suggests that debt could range between 48 and 79 percent of GDP at the end of the projection horizon.

3. The heat map highlights vulnerabilities stemming from debt level, and residency and currency composition. The rise in public debt poses sustainability risks, especially if Armenia faces deeper macroeconomic shocks. FX-denominated debt and debt held by non-residents remain important risk factors for debt sustainability. A depreciation of the exchange rate would worsen the debt outlook as indicated by the relevant stress test (see Figure A4). Overall, risks associated with public external debt are modest. External public debt stood about US$ 6 billion at end-2020, of which US$ 4 billion was owed to multilateral official creditors and US$ 1 billion to (Paris club) bilateral official creditors. The outstanding of Euro bonds at end-2020 was US$ 1 billion (0.5 billion

[1] The coverage of public debt is general government debt and debt of the CBA.

each will be maturing in 2025 and 2029). Thanks to the high share of debt to multilateral official creditors, the average interest rate of the external public debt is relatively low at 3 percent.

4. Scenarios assuming key variables at their historical averages underscore the need for consolidation. The paths of public debt and gross financing needs deviate significantly from the baseline under the historical scenario; the debt ratio would be slightly over 70 percent in 2026. This would place debt sustainability at risk and increase financing needs to around 15 percent of GDP in 2026. This implies that without active policy measures aimed at reducing the fiscal deficit, debt sustainability would be jeopardized.

5. Stress tests suggest that shocks to growth have the largest impact on debt indicators. A combined macro-fiscal shock, whereby real GDP contracts by another 4.5 percent in 2022–23 in each year together with worsening primary balance, can cause public debt to increase to around 70 percent of GDP, and for public gross financing needs to remain around 10 percent of GDP in 2026. Given the twin shocks of 2020, the government is committed to conduct an expenditure review in FY2022 to reduce current expenditure and implement quality revenue measures over the medium term starting in 2022. These are important to mitigating risks which could come from higher primary balances and macroeconomic shocks. In isolation, shocks to growth, followed by shocks to the real exchange rate, have the most sizable adverse impact on the public debt path, relative to the baseline.

Figure A1. Armenia Public Sector Debt Sustainability Analysis (DSA) - Baseline Scenario

(in percent of GDP unless otherwise indicated)

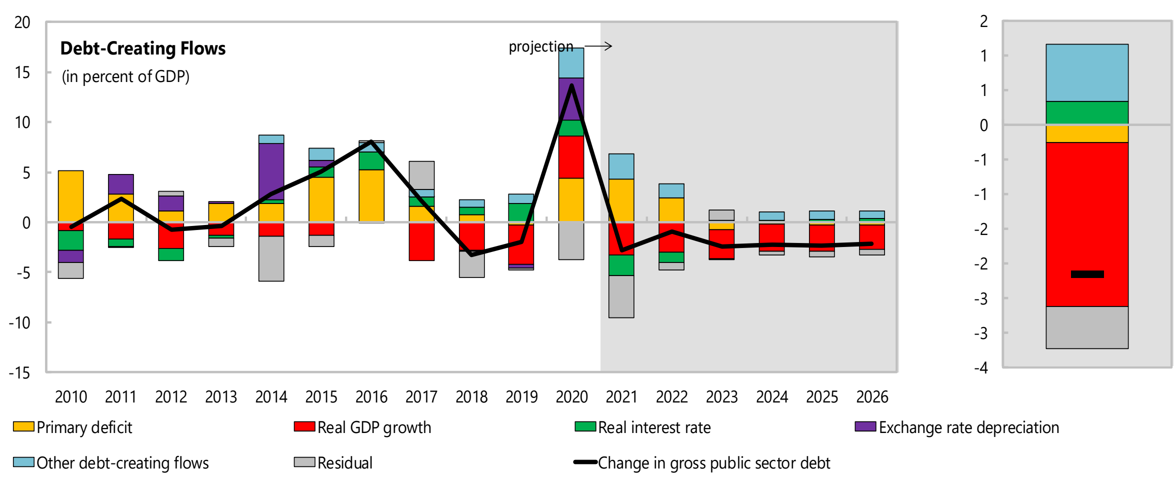
Debt, Economic and Market Indicators [1]

	Actual			Projections					
	2010-2018 [3]	2019	2020	2021	2022	2023	2024	2025	2026
Nominal gross public debt	47.5	53.7	67.4	64.6	63.6	61.2	58.9	56.5	54.4
Public gross financing needs	7.4	8.6	11.5	12.2	10.2	7.5	8.2	10.2	7.5
Net public debt 2/		48.1	61.0	58.4	57.8	56.5	54.6	52.6	50.7
Real GDP growth (in percent)	4.1	7.6	-7.4	5.5	5.3	5.0	4.8	4.7	4.8
Inflation (GDP deflator, in percent)	3.3	1.0	2.0	7.8	6.3	4.5	4.1	3.8	3.6
Nominal GDP growth (in percent)	7.5	8.7	-5.5	13.7	11.9	9.8	9.0	8.7	8.6
Effective interest rate (in percent) [5]	3.3	4.7	4.7	4.7	4.9	4.7	4.6	4.6	4.5

As of November 07, 2021		
Sovereign Spreads		
Spread (bp) 4/		276
CDS (bp)		n.a.
Ratings	Foreign	Local
Moody's	Ba3	n.a.
S&Ps	B+ (LT)/B (ST)	B+ (LT)/B (ST)
Fitch	B+	n.a.

Contribution to Changes in Public Debt

	Actual			Projections							
	2010-2018	2019	2020	2021	2022	2023	2024	2025	2026	cumulative	debt-stabilizing primary balance [10]
Change in gross public sector debt	1.7	-2.0	13.7	-2.8	-0.9	-2.5	-2.3	-2.3	-2.2	-13.0	
Identified debt-creating flows	2.5	-1.8	17.4	-1.4	1.6	-2.3	-1.5	-1.5	-1.3	-6.4	
Primary deficit	2.8	-0.3	4.4	4.3	2.4	-0.7	-0.2	-0.3	-0.3	5.3	-1.1
Primary (noninterest) revenue and grants	21.7	23.9	25.2	23.6	24.7	25.0	25.2	25.3	25.6	149.2	
Primary (noninterest) expenditure	24.4	23.6	29.6	27.9	27.1	24.2	25.0	25.0	25.3	154.5	
Automatic debt dynamics [6]	-0.7	-2.4	10.0	-8.2	-2.3	-1.7	-2.1	-2.0	-1.9	-18.2	
Interest rate/growth differential [7]	-1.7	-2.1	5.8	-5.3	-4.1	-3.0	-2.5	-2.3	-2.1	-19.2	
Of which: real interest rate	0.1	1.8	1.6	-2.1	-1.0	-0.1	0.2	0.3	0.3	-2.3	
Of which: real GDP growth	-1.8	-3.9	4.2	-3.2	-3.0	-2.9	-2.7	-2.6	-2.5	-16.9	
Exchange rate depreciation [8]	1.0	-0.4	4.2	…	…	…	…	…	…	…	
Other identified debt-creating flows	0.5	0.9	3.0	2.5	1.4	0.2	0.8	0.8	0.8	6.5	
Domestic net lend./drawdown of gov. dep. (	0.0	0.0	1.9	0.6	-0.4	-0.6	0.0	0.0	0.0	-0.4	
Contingent liabilities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
External net lending	0.5	0.9	1.2	1.8	1.8	0.8	0.8	0.8	0.8	7.0	
Residual, including asset changes [9]	-0.8	-0.2	-3.7	-4.3	-0.7	1.0	-0.4	-0.6	-0.6	-5.5	



Source: IMF staff.

1/ Public sector is defined as general government.

2/ Net public debt is defined as gross debt minus financial assets corresponding to debt instruments.

3/ Based on available data.

4/ Bond Spread over U.S. Bonds.

5/ Defined as interest payments divided by debt stock at the end of previous year.

6/ Derived as [(r - p(1+g) - g + ae(1+r)]/(1+g+p+gp)) times previous period debt ratio, with r = interest rate; p = growth rate of GDP deflator; g = real GDP growth rate; a = share of foreign-currency denominated debt; and e = nominal exchange rate depreciation (measured by increase in local currency value of U.S. dollar).

7/ The real interest rate contribution is derived from the denominator in footnote 4 as r - π (1+g) and the real growth contribution as -g.

8/ The exchange rate contribution is derived from the numerator in footnote 2/ as ae(1+r).

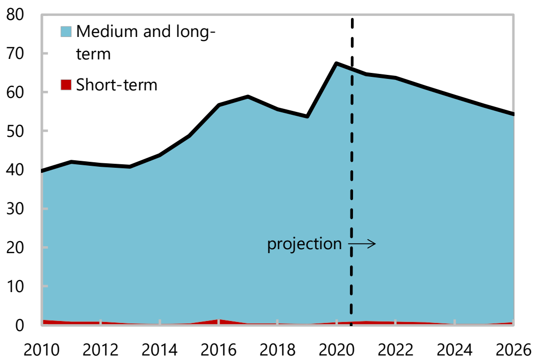
9/ Includes asset changes and interest revenues (if any). For projections, includes exchange rate changes during the projection period.

10/ Assumes that key variables (real GDP growth, real interest rate, and other identified debt-creating flows) remain at the level of the last projection year.

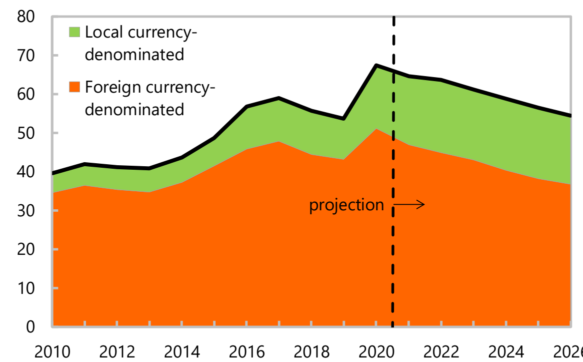
Figure A2. Armenia Public DSA - Composition of Public Debt and Alternative Scenarios

Composition of Public Debt

By Maturity
(in percent of GDP)



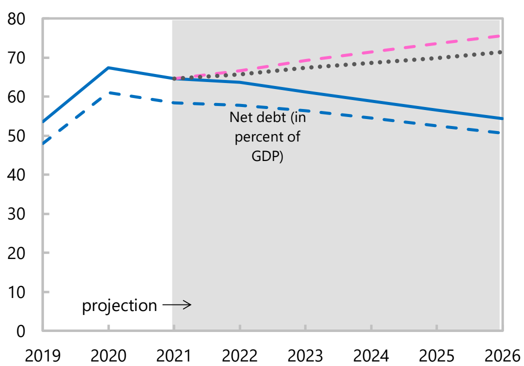
By Currency
(in percent of GDP)



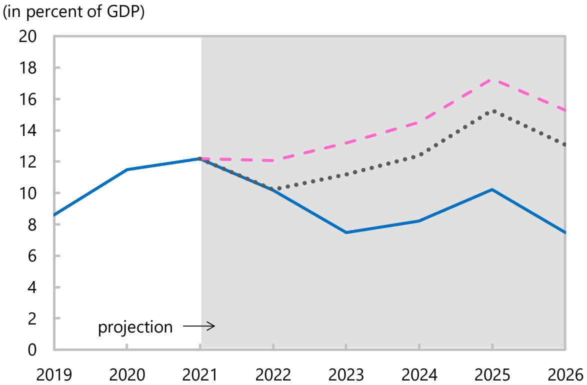
Alternative Scenarios

Baseline   Historical   Constant Primary Balance

Gross Nominal Public Debt
(in percent of GDP)



Public Gross Financing Needs
(in percent of GDP)



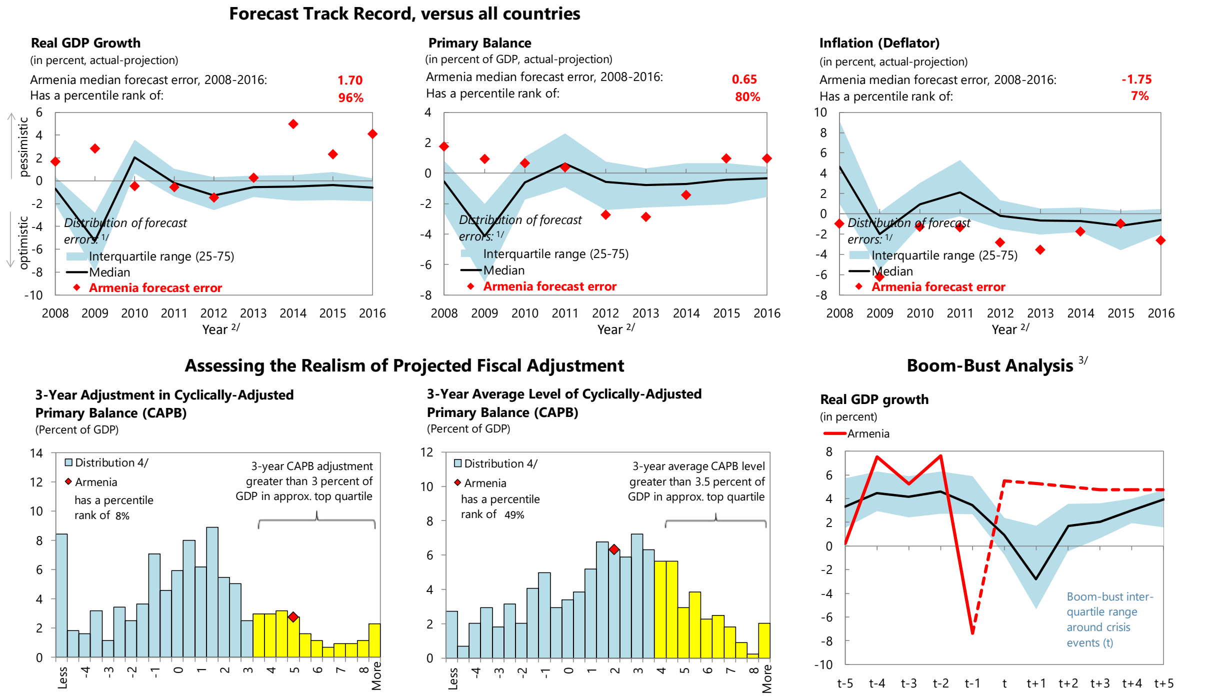
Underlying Assumptions
(in percent)

Baseline Scenario	2021	2022	2023	2024	2025	2026
Real GDP growth	5.5	5.3	5.0	4.8	4.7	4.8
Inflation	7.8	6.3	4.5	4.1	3.8	3.6
Primary Balance	-4.3	-2.4	0.7	0.2	0.3	0.3
Effective interest rate	4.7	4.9	4.7	4.6	4.6	4.5
Constant Primary Balance Scenario						
Real GDP growth	5.5	5.3	5.0	4.8	4.7	4.8
Inflation	7.8	6.3	4.5	4.1	3.8	3.6
Primary Balance	-4.3	-4.3	-4.3	-4.3	-4.3	-4.3
Effective interest rate	4.7	4.9	4.8	4.8	5.0	4.9

Historical Scenario	2021	2022	2023	2024	2025	2026
Real GDP growth	5.5	3.5	3.5	3.5	3.5	3.5
Inflation	7.8	6.3	4.5	4.1	3.8	3.6
Primary Balance	-4.3	-2.4	-2.4	-2.4	-2.4	-2.4
Effective interest rate	4.7	4.9	5.0	5.2	5.4	5.5

Source: IMF staff.

Figure A3. Armenia Public DSA - Realism of Baseline Assumptions (concluded)



Source : IMF Staff.

1/ Plotted distribution includes all countries, percentile rank refers to all countries.

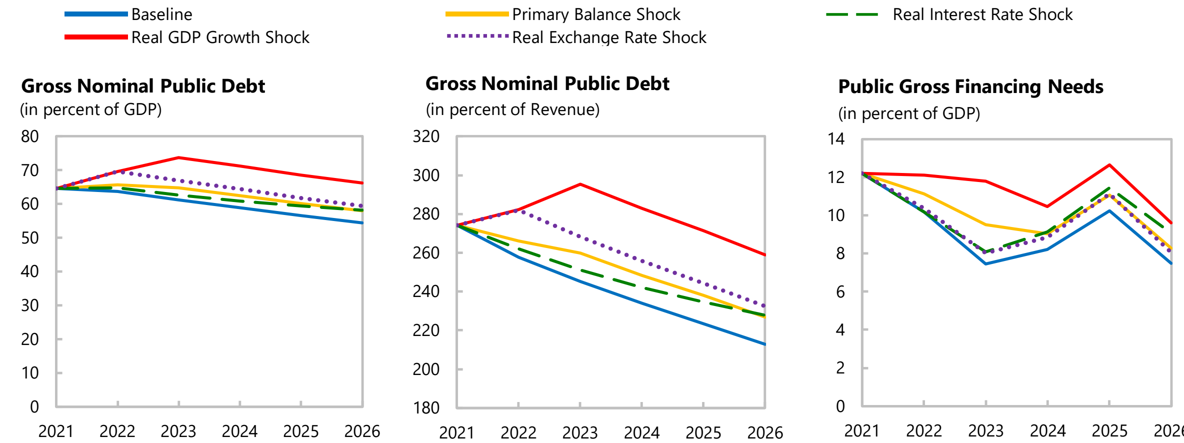
2/ Projections made in the spring WEO vintage of the preceding year.

3/ Armenia has had a positive output gap for 3 consecutive years, 2018-2020 and a cumulative increase in private sector credit of 21 percent of GDP, 2017-2020. For Armenia, t corresponds to 2021; for the distribution, t corresponds to the first year of the crisis.

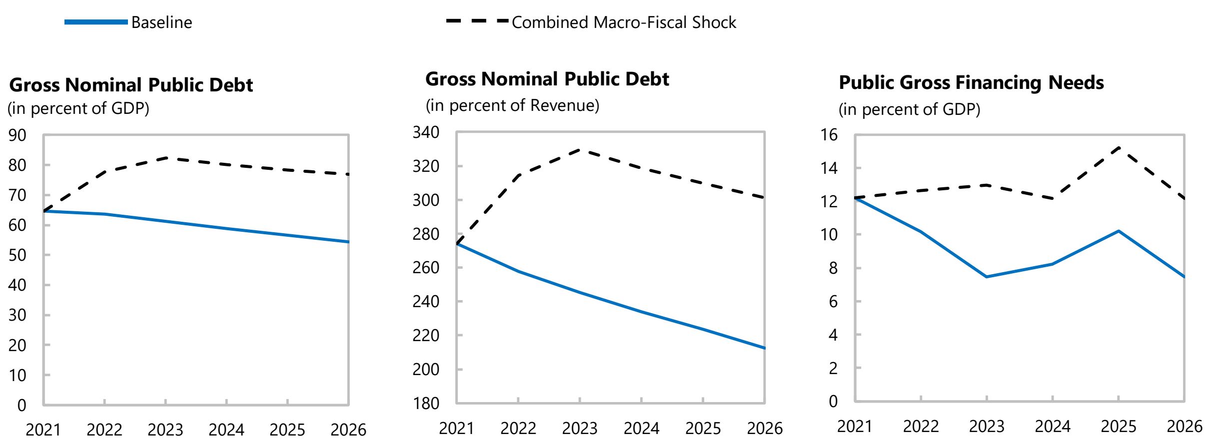
4/ Data cover annual obervations from 1990 to 2011 for advanced and emerging economies with debt greater than 60 percent of GDP. Percent of sample on vertical axis.

Figure A4. Armenia Public DSA - Stress Tests

Macro-Fiscal Stress Tests



Additional Stress Tests



Underlying Assumptions
(in percent)

Primary Balance Shock	2021	2022	2023	2024	2025	2026
Real GDP growth	5.5	5.3	5.0	4.8	4.7	4.8
Inflation	7.8	6.3	4.5	4.1	3.8	3.6
Primary balance	-4.3	-3.4	-0.8	0.2	0.3	0.3
Effective interest rate	4.7	4.9	4.8	4.8	4.8	4.6
Real Interest Rate Shock						
Real GDP growth	5.5	5.3	5.0	4.8	4.7	4.8
Inflation	7.8	6.3	4.5	4.1	3.8	3.6
Primary balance	-4.3	-2.4	0.7	0.2	0.3	0.3
Effective interest rate	4.7	4.9	5.4	5.7	6.1	6.5
Combined Shock						
Real GDP growth	5.5	0.8	0.5	4.8	4.7	4.8
Inflation	7.8	5.2	3.4	4.1	3.8	3.6
Primary balance	-4.3	-3.9	-2.0	0.2	0.3	0.3
Effective interest rate	4.7	5.2	5.3	5.8	6.2	6.6

Real GDP Growth Shock	2021	2022	2023	2024	2025	2026
Real GDP growth	5.5	0.8	0.5	4.8	4.7	4.8
Inflation	7.8	5.2	3.4	4.1	3.8	3.6
Primary balance	-4.3	-3.9	-2.0	0.2	0.3	0.3
Effective interest rate	4.7	4.9	4.8	4.9	4.9	4.7
Real Exchange Rate Shock						
Real GDP growth	5.5	5.3	5.0	4.8	4.7	4.8
Inflation	7.8	10.5	4.5	4.1	3.8	3.6
Primary balance	-4.3	-2.4	0.7	0.2	0.3	0.3
Effective interest rate	4.7	5.2	4.6	4.5	4.5	4.4

Source: IMF staff.

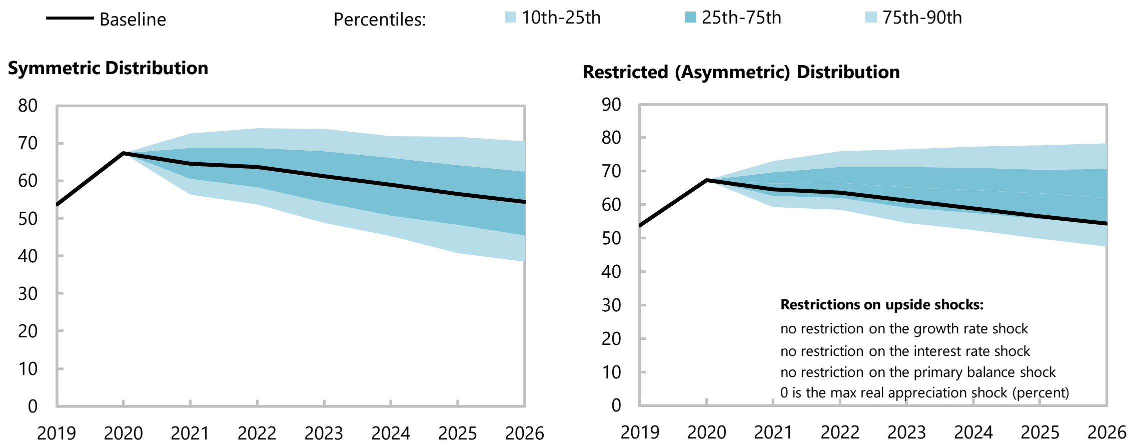
Figure A5. Armenia Public DSA Risk Assessment

Heat Map

Debt level 1/	Real GDP Growth Shock	Primary Balance Shock	Real Interest Rate Shock	Exchange Rate Shock	Contingent Liability shock
Gross financing needs 2/	Real GDP Growth Shock	Primary Balance Shock	Real Interest Rate Shock	Exchange Rate Shock	Contingent Liability Shock
Debt profile 3/	Market Perception	External Financing Requirements	Change in the Share of Short-Term Debt	Public Debt Held by Non-Residents	Foreign Currency Debt

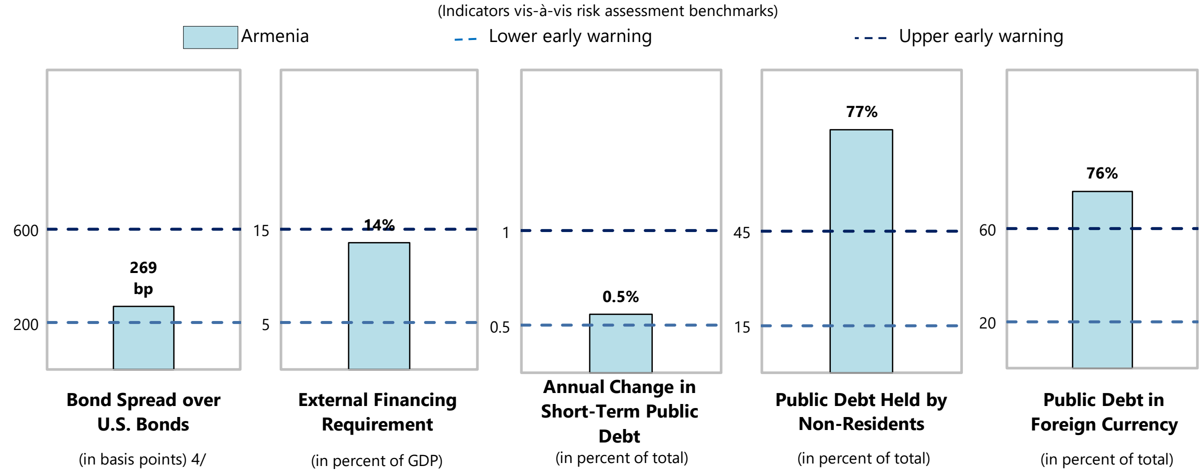
Evolution of Predictive Densities of Gross Nominal Public Debt

(in percent of GDP)



Debt Profile Vulnerabilities

(Indicators vis-à-vis risk assessment benchmarks)



Source: IMF staff.

1/ The cell is highlighted in green if debt burden benchmark of 70% is not exceeded under the specific shock or baseline, yellow if exceeded under specific shock but not baseline, red if benchmark is exceeded under baseline, white if stress test is not relevant.

2/ The cell is highlighted in green if gross financing needs benchmark of 15% is not exceeded under the specific shock or baseline, yellow if exceeded under specific shock but not baseline, red if benchmark is exceeded under baseline, white if stress test is not relevant.

3/ The cell is highlighted in green if country value is less than the lower risk-assessment benchmark, red if country value exceeds the upper risk-assessment benchmark, yellow if country value is between the lower and upper risk-assessment benchmarks. If data are unavailable or indicator is not relevant, cell is white.
Lower and upper risk-assessment benchmarks are:

200 and 600 basis points for bond spreads; 5 and 15 percent of GDP for external financing requirement; 0.5 and 1 percent for change in the share of short-term debt; 15 and 45 percent for the public debt held by non-residents; and 20 and 60 percent for the share of foreign-currency denominated debt.

4/ An average over the last 3 months, 09-Aug-21 through 07-Nov-21.

Armenia. Decomposition of Public Debt and Debt Service by Creditor, 2020-2022[1]

	Debt Stock (end of period)			Debt Stock (end of period)			Debt Service (is represented on an instrument principle, data by residency principle is not available)					
	2020			2020			2020	2021	2022	2020	2021	2022
	(In US$)	*(Percent total debt)*	*(Percent GDP)*	*(In US$)*	*(Percent total debt)*	*(Percent GDP)*	*(In US$)*			*(Percent GDP)*		
Total	7945.2	100.0	62.9	7945.2	100.0	62.9						
External	6036.2	76.0	47.8	6110.5	76.9	48.3	566.9	472.7	460.5	4.5	3.4	2.9
Multilateral creditors[2,3]	3914.5	49.3	31.0	3914.5	49.3	31.0	295.7	308.4	289.1	2.3	2.2	1.8
IMF	516.0	6.5	4.1	516.0	6.5	4.1						
World Bank	1827.7	23.0	14.5	1827.7	23.0	14.5						
ADB/AfDB/IADB	788.3	9.9	6.2	788.3	9.9	6.2						
Other Multilaterals	782.4	9.8	6.2	782.4	9.8	6.2						
o/w: list largest two creditors		0.0	0.0									
EDB	317.0	4.0	2.5	317.0	4.0	2.5						
EIB	247.5	3.1	2.0	247.5	3.1	2.0						
list of additional large creditors		0.0	0.0									
Bilateral Creditors[2]	1175.4	14.8	9.3	1175.4	14.8	9.3	110.3	106.2	113.3	0.9	0.8	0.7
Paris Club	1148.4	14.5	9.1	1148.4	14.5	9.1	103.4	103.4	103.4	0.8	0.7	0.7
o/w: list largest two creditors	756.5	9.5	6.0	756.5	9.5	6.0						
Germany/KFW	397.1	5.0	3.1	397.1	5.0	3.1						
RF	359.4	4.5	2.8	359.4	4.5	2.8						
list of additional large creditors		0.0	0.0									
Non-Paris Club	27.0	0.3	0.2	27.0	0.3	0.2	2.8	2.8	2.8	0.0	0.0	0.0
o/w: list largest two creditors	27.0	0.3	0.2	27.0	0.3	0.2						
Export-Import Bank of China	23.0	0.3	0.2	23.0	0.3	0.2						
Abu-Dhabi Fund for Development	4.0	0.1	0.0	4.0	0.1	0.0						
list of additional large creditors	-											
Bonds (in column C bonds (Eurobonds) are presented on a residency principle, in column G they are represented on an instrument principle)	**925.7**	11.7	7.3	**1000.0**	12.6	7.9	159.0	55.5	55.5	1.3	0.4	0.4
Commercial creditors	20.6	0.3	0.2	20.6	0.3	0.2	1.9	2.6	2.6	0.0	0.0	0.0
o/w: list largest two creditors												
Erste Bank/Austria	9.8	0.1	0.1	9.8	0.1	0.1						
Raiffeisen Bank/Austria	7.7	0.1	0.1	7.7	0.1	0.1						
list of additional large creditors												
Other international creditors	-			-			-	-	-			
o/w: list largest two creditors												
list of additional large creditors												
Domestic (in column C dom. debt is presented on a residency principle, in column G it is represented on an instrument principle)	1909.0	24.0	15.1	1834.8	23.1	14.5	378.3	211.3	148.7	3.0	1.5	0.9
Held by residents, total	1909.0	24.0	15.1	1828.5	23.0	14.5	N/A	N/A	N/A	N/A	N/A	N/A
Held by non-residents, total				6.3	0.1	0.0	N/A	N/A	N/A	N/A	N/A	N/A
T-Bills	90.9	1.1	0.7	90.9	1.1	0.7	64.8	90.9	0.0	0.5	0.7	0.0
Bonds	1743.9	21.9	13.8	1743.9	21.9	13.8	313.5	120.4	148.7	2.5	0.9	0.9
Loans	0.0			0.0	0.0	0.0	-					
Memo items:												
Collateralized debt[4]												
o/w: Related												
o/w: Unrelated												
Contingent liabilities												
o/w: Public guarantees	8.6	0.1	0.1	8.6	0.1	0.1						
o/w: Other explicit contingent liabilities[5]												
Nominal GDP	12641			12641			12641	13888	15729			

1/As reported by Country authorities according to their classification of creditors, including by official and commercial. Debt coverage is the same as the DSA, however CBA debt conversions to USD are based on end of the year exchange rates, while the Government debt conversions are based on average annual exchange rates. As a result this leads to different valuation in the stock of debt relative to the DSA.

2/Some public debt is not shown in the table due to [confidentiality clauses/capacity constraints].(Include for all creditor groups where applicable)

3/Multilateral creditors" are simply institutions with more than one official shareholder and may not necessarily align with creditor classification under other IMF policies (e.g. Lending Into Arrears)

4/Debt is collateralized when the creditor has rights over an asset or revenue stream that would allow it, if the borrower defaults on its payment obligations, to rely on the asset or revenue stream to secure repayment of the debt. Collateralization entails a borrower granting liens over specific existing assets or future receivables to a lender as security against repayment of the loan. Collateral is "unrelated" when it has no relationship to a project financed by the loan. An example would be borrowing to finance the budget deficit, collateralized by oil revenue receipts. See the joint IMF-World Bank note for the G20 "Collateralized Transactions: Key Considerations for Public Lenders and Borrowers" for a discussion of issues raised by collateral.

5/Includes other-one off guarantees not included in publicly guaranteed debt (e.g. credit lines) and other explicit contingent liabilities not elsewhere classified (e.g. potential legal claims, payments resulting from PPP arrangements).

Annex II. Risk Assessment Matrix[1]

Risk Assessment Matrix				
Risk	**Description**	**Likelihood**	**Possible Impact**	**Policy Advice**
External Risks and Spillovers				
Global resurgence of the COVID-19 pandemic	Local outbreaks lead to a global resurgence of the pandemic (possibly due to vaccine-resistant variants), which requires costly containment efforts and prompts persistent behavioral changes rendering many activities unviable.	**Medium**	New more dangerous virus strains could delay the phase-out of lockdown measures and resumption of economic activity. Continued containment necessitates higher budget spending and lower revenues, weakening fiscal balance. Slower global growth would reduce oil and natural gas exports.	Additional fiscal measures to ensure adequate, temporary, and targeted support to the population most adversely affected and vulnerable to the pandemic.
Uncontrolled COVID-19 local outbreaks and subpar /volatile growth in affected countries	Outbreaks in slow-to-vaccinate countries force new lockdowns. For many Emerging Markets and Low-Income Countries, policy response to cushion the economic impact is constrained by lack of policy space, with some market access countries facing additional financial tightening as a reassessment of growth prospects.	**High**	The new lockdown might trigger capital outflows, depreciations, and debt defaults.	Additional fiscal measures to ensure fast vaccine rollout for the population, and targeted support to the population most adversely affected and vulnerable to the pandemic.
Disorderly transformations	COVID-19 triggers structural transformations, but the reallocation of resources is impeded by labor market rigidities, debt overhangs, and inadequate bankruptcy resolution frameworks.	**Medium**	This, coupled with a withdrawal of COVID-19-related policy support, undermines growth prospects and increases unemployment with adverse social/political consequences. Adjustments in global value chains and reshoring (partly driven by geostrategic and national security concerns) shift production activities across countries.	Fiscal measures to improve spending efficiency can create the fiscal space for implementing structural reforms to diversify the economy. This can ensure adequate and targeted support to the population.

[1] Risk assessment matrix shows events that could materially alter the baseline path.

Risk Assessment Matrix				
Risk	**Description**	**Likelihood**	**Possible Impact**	**Policy Advice**
Intensified geopolitical tensions and security risks	Geopolitical tensions in selected countries/regions cause economic/political disruption, disorderly migration, higher volatility in commodity prices (if supply is disrupted), and lower confidence, with spillovers to other countries.	**High**	Geopolitical uncertainties in the Middle East and Central Asia region, specifically through trade and investment.	Structural reforms to diversify the economy would mitigate risks stemming from geopolitical tensions and security. Strengthen social safety nets to cushion impact of shocks on vulnerable sectors.
Rising commodity prices amid bouts of volatility	Commodity prices increase by more than expected against a weaker U.S. dollar, post-pandemic pent-up demand and supply disruptions, and for some materials, accelerated plans for renewable energy adoption. Uncertainty surrounding each of these factors leads to bouts of volatility, especially in oil prices.	**Medium**	Uncertainty surrounding each of these factors leads to bouts of volatility, especially in oil prices.	Continue the dedollarization efforts. Maintain exchange rate flexibility. Strengthen banking supervision and provision in the event of higher NPLs in dollar.
De-anchoring of inflation expectations in the U.S. leads to rising core yields and risk premia.	A fast recovery in demand (supported by excess private savings and stimulus policies), combined with Covid-19-related supply constraints, leads to sustained above-target inflation readings and a de-anchoring of expectations. The Fed reacts by signaling a need to tighten earlier than expected. The resulting repositioning by market participants leads to a front-loaded tightening of financial conditions and higher risk premia, including for credit, equities, and emerging and frontier market currencies.	**Medium**	DSA suggests that Armenia's external debt is not sensitive to interest shocks given that most of debt is concessional. Nonetheless, higher international interest rates would impose higher costs on the rollover of $750 million Eurobonds in 2021.	Continue the dedollarization efforts. Maintain exchange rate flexibility. Strengthen banking supervision and provision in the event of higher NPLs in dollar.

Risk Assessment Matrix				
Risk	**Description**	**Likelihood**	**Possible Impact**	**Policy Advice**
Cyberattacks	Cyberattacks on critical infrastructure, institutions, and financial systems trigger systemic financial instability or widespread disruptions in socio-economic activities and remote work arrangements.	**Medium**	The lack of information about Internet connectivity and cyber-defenses of key institutions and the fast-evolving nature of the cyberattack vulnerabilities make any assessment of systemic risks and their potential economic costs highly uncertain.	Strengthening international and regional cooperation and developing government and business contingency and continuation plans. Creating a national cybersecurity agency
Higher frequency and severity of natural disasters related to climate change	This can cause severe economic damage to smaller economies susceptible to disruptions and accelerate emigration from these economies. A sequence of severe events in large economies reduces global GDP and prompts a recalculation of risk and growth prospects. Disasters hitting key infrastructure or disrupting trade raise commodity price levels and volatility.	**Medium**	Higher frequency and severity of natural disasters would cause severe economic damages and disrupt economic activities.	National adaptation and mitigation policies to strengthen the resilience against climate change risks.
Domestic Risks				
Financial sector risks	Risks could increase after the pandemic. Stress could arise from the rising exposure to the real estate sector and to small and medium size enterprises, where the long-term impact of the pandemic is likely to be more severe.	**Medium**	A rise in NPLs could increase contingent government liabilities and could also undermine the stability of the financial system.	Enforce prudential and provisioning rules that are consistent with international standards and strengthen further the regulatory and supervisory framework. Implement macroprudential measures
Regional conflict	Risks from sharp, renewed Nagorno-Karabakh-related tensions.	**Medium**	Conflict would have severe impacts, including possible regional military action.	Continue with dialogue. Prepare and implement contingency plans.

Risk Assessment Matrix				
Risk	**Description**	**Likelihood**	**Possible Impact**	**Policy Advice**
High inflation	Pent-up in consumption, supply constraints, global and domestic food inflation could lead to prolonged periods of high inflation.	**High**	High inflation could un-anchor inflation expectations; leading to a higher dollarization an extended period of monetary policy tightening that will subside economic activity.	Analyze drivers of inflation, improve the methodology behind inflation expectations, anchor inflation expectations, deliver clear communication on monetary policy priorities.

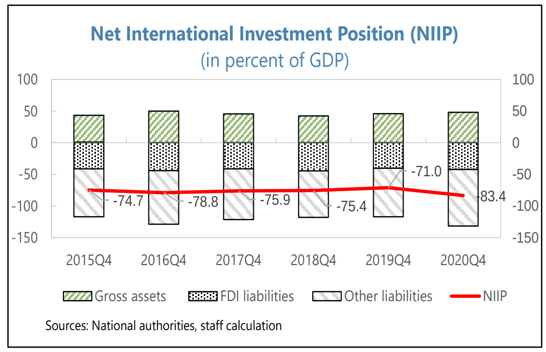
Annex III. External Sector Assessment

Overall Assessment: *The external position of Armenia in 2020 is assessed as broadly consistent with the level implied by fundamentals and desirable policies.*

Policy Responses: *Continued prudent fiscal policy, exchange rate flexibility, and structural reforms to boost competitiveness would bolster buffers and support the economy's resilience against potential exogenous shocks. With continued policy efforts, the current account is expected to converge to the norm over the medium term.*

Foreign Assets and Liabilities: Position and Trajectory

1. Background. The net international investment position (NIIP) has ranged between -70 and -80 percent of GDP in recent years. The NIIP worsened to -83.4 percent of GDP in Q4 2020, reflecting the decline in nominal GDP in US$ terms (mostly due to negative real growth in Armenian Dram terms) and increases in public debt to respond to the COVID-19 pandemic. In recent years, the share of FDI liabilities, about 40 percent of which have originated from Russia, in total liabilities has declined as other (non-FDI) liabilities have increased.



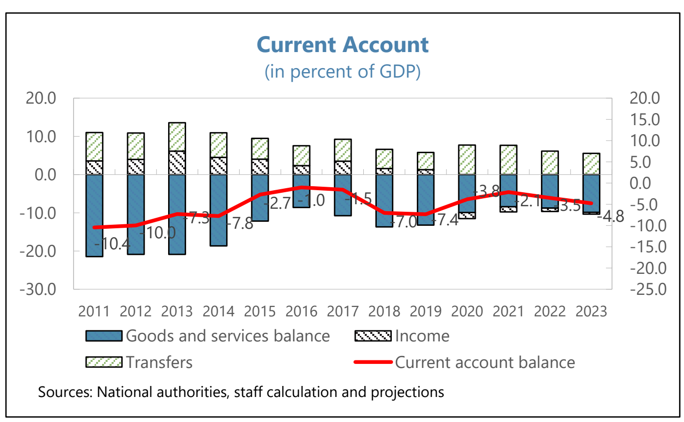
Sources: National authorities, staff calculation

2. Assessment. The NIIP does not present an immediate risk to external sustainability. The NIIP (in percent of GDP) would stabilize even if the current account balance stayed around the norm (-5.8 percent of GDP). However, vulnerability of the NIIP position may have increased somewhat, as the share of debt liabilities in gross liabilities increased from 72 percent at end-2015 to 80 percent at end-2020.

2020 (percent GDP) (at end-Q4 2020)	NIIP: -83.4	Gross Assets: 48.0	Debt Assets: 22.4	Gross Liab.: 131.5	Debt Liab.: 104.5

Current Account

3. Background. The current account balance is estimated to have improved to -3.8 percent of GDP in 2020 from -7.4 percent of GDP in 2019, reflecting import compression following the COVID-19 pandemic and military conflict. The current account balance improved to 2.2 percent of GDP during the first half of 2021 and is



Sources: National authorities, staff calculation and projections

projected to improve further during the rest of 2021, supported by robust exports and remittances. Over the medium term, the current account balance is expected to converge toward the norm of around -5.8 percent of GDP (see below) amid solid export growth and moderate import growth on the back of prudent macroeconomic policies.

4. Assessment. *The Current Account (CA) model* implies a current account gap of 0.8 percent of GDP. Temporary factors associated with the military conflict in late 2020 on the actual CA is estimated at 1.2 percent of GDP, yielding an adjusted CA of -5.0 percent of GDP (see the text table). While the CA norm from the model is -4.8 percent of GDP, there are Armenia-specific factors (1 percentage point), including a persistent need for investment-related imports.[1] This adjustment is consistent with the government commitment to an investment-led growth model. Consequently, the adjusted CA norm is -5.8 percent of GDP, which gives a CA gap of 0.8 percent of GDP. *The real effective exchange rate (REER) model* provides an implied current account gap of 3.3 percent of GDP. The policy gap is estimated to be positive (1.7 percent of GDP), reflecting the need to expand public health expenditure. Finally, *the External Sustainability (ES) model* suggests a gap of 0.8 percent of GDP. Given the estimates provided by the CA and ES models, the external position in 2020 is assessed to be broadly in line with the level implied by fundamentals and desirable policies.[2] The projected improvement in the current account balance in 2021 suggests a move of the assessment in the direction of the external position being moderately stronger than fundamentals, though the comprehensive assessment would need to wait for full-year 2021 data.

Armenia: Model Estimates for 2020 (in percent of GDP)

	CA model	REER model	ES model
CA-Actual	**-3.8**		
Cyclical contributions (from model) (-)	-0.2		
COVID-19 adjustor (+) 1/	-0.3		
Additional temporary/statistical factors (+) 2/	-1.2		
Adjusted CA	**-5.0**		
CA Norm (from model) 3/	**-4.8**		
Adjustments to the norm (+)	-1.0		
Adjusted CA Norm	**-5.8**		**-5.8**
CA Gap	**0.8**	**3.3**	**0.8**
o/w Relative policy gap	1.7		
Elasticity	-0.30		
REER Gap (in percent)	**-2.6**	**-11.1**	**-2.7**

1/ Additional cyclical adjustment to account for the temporary impact of the pandemic on oil trade balances (-0.3 percent of GDP).
2/ Temporary factors associated with the military conflict in late 2020: import compression (0.4 points); and voluntary private transfers from overseas to the *All Armenian Fund* (0.8 points)
3/ Cyclically adjusted, including multilateral consistency adjustments.

[1] Staff has maintained the assumption in previous external sector assessments (e.g., in IMF Country Report No. 20/176).

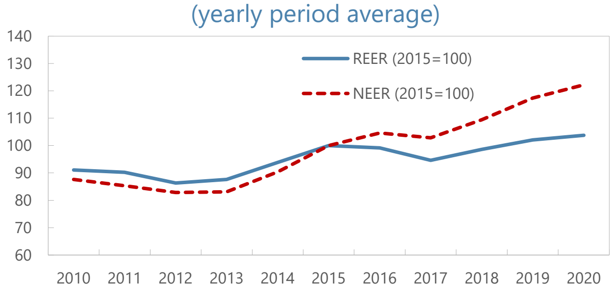
[2] The staff's overall assessment relies on the CA and ES models, because the estimate by the REER model, which is at odds with the former two models, is driven by a few relatively volatile variables (e.g., remittances).

Real Exchange Rate

5. Background. The CPI-based REER appreciated slightly by 1.6 percent in 2020, reflecting appreciation against non-US trading partners. The Armenian Dram depreciated by about 8 percent against the US dollar during 2020, much of which (7 percentage points) occurred after the conflict started in late September 2020 (a ceasefire was reached on November 10). In 2021, although the Dram depreciated initially, on net it appreciated by 9 percent against the US dollar between the beginning of the year and end-October. The REER was relatively stable between 2015 and 2019 (left chart of the text figure). Armenia's governance indicators (World Governance Indicators) rose substantially relative to its regional peers between 2015 and 2019, suggesting that non-price competitiveness may have improved during this period (right chart of the text figure).

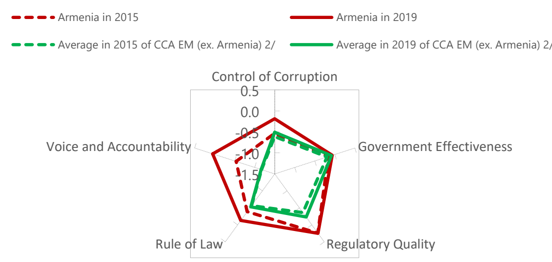
6. Assessment. By relying on the CA model (as in "Current Account" section above), the REER gap is estimated at -2.6 percent in 2020.

Exchange Rate
(yearly period average)



Sources: National authorities, staff calculation

Changes in Worldwide Governance Indicators 1/ between 2015 and 2019

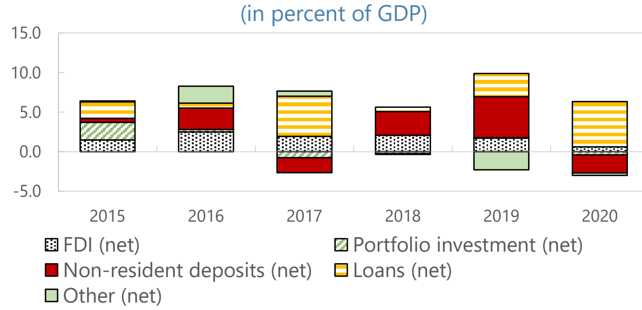


1/ These indicators should be interpreted carefully, as they are derived from perceptions-based data.
2/ Caucasus and Central Asia emerging economise: Azerbaijan, Georgia, Kazakhstan, and Turkmenistan.
Source: Worldwide Governance Indicators, D. Kaufmann (Natural Resource Governance Institute and Brookings Institution) and A.Kraay (World Bank). The indicators are produced following the methodology in Kaufmann, Kraay and Mastruzzi (2010).

Capital and Financial Accounts: Flows and Policy Measures

7. Background. In 2020, non-resident deposits experienced sharp net outflows (2.3 percent of GDP) after strong net inflows in 2019 (5.2 percent of GDP), but the outflows of non-resident deposits were offset by net loan inflows (5.7 percent of GDP, including Fund financing). In recent years, non-resident deposits have been driving capital flows. Contributions of FDI to capital flows have been relatively stable (1–2 percent of GDP), while those of the capital account and portfolio investment remain relatively limited. The authorities have not introduced any capital flow management measures.

Capital Flows
(in percent of GDP)

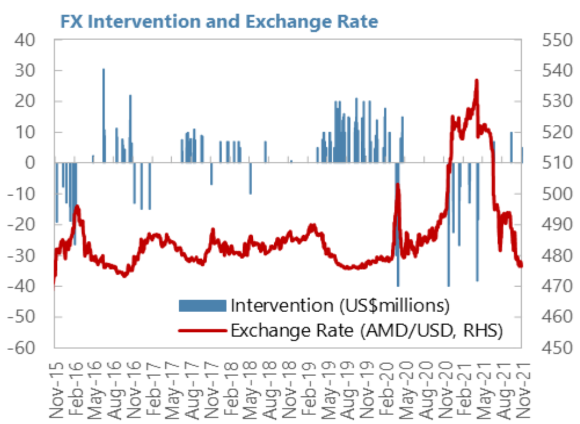


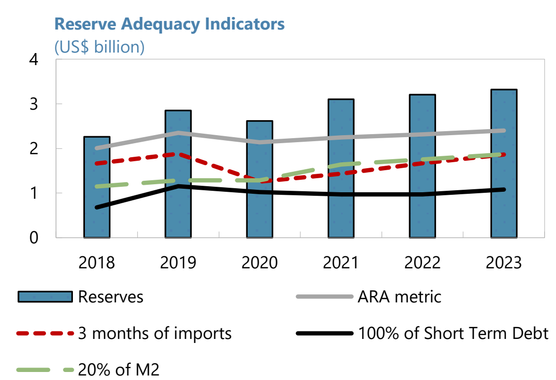
Sources: National authorities, staff calculation

8. Assessment. Vulnerabilities related to capital flows include the high dollarization and presence of sizable non-resident foreign currency deposits in the banking system. In the case of adverse external shocks, these vulnerabilities could amplify capital outflow pressure.

FX Intervention and Reserves Level

9. Background and assessment. Gross reserves declined to US$2,616 million (about 21 percent of GDP) at end-2020 from US$2,850 million at end-2019. Private capital flows (e.g., non-resident deposits) and public debt service contributed to the decline, although they were partially offset by Fund financing (about US$300 million). During 2020, the authorities' intervention on the sell side amounted to US$238 million. They intervened on the buy side to the value of US$91 million in April when market pressure subsided and in January–February before the COVID-19 pandemic started, leaving net intervention during 2020 at US$147 million. In 2021 the authorities intervened on the sell side by US$156 million during between January and April to mitigate disorderly market conditions, and since then they have purchased back US$22 million. During 2017–2019, the authorities intervened mostly on the buy side. Under the IMF's reserve adequacy metric (ARA) for floating exchange rate regimes, the gross reserves are estimated to be adequate at about 120 percent at end-2020 and to stay above this level over the medium term.





Sources: National authorities, Central Bank of Armenia, and staff calculations

External Debt Sustainability

10. Hit by the twin shocks of the COVID-19 pandemic and military conflict, Armenia's external debt-to-GDP ratio is expected to rise during 2021 but gradually decline over the medium term. In the baseline scenario, the debt-to-GDP ratio reached 100 percent of GDP at end-2020, and is projected to decline to around 96 percent of GDP at end-2021. The results of standardized shocks highlight vulnerabilities. Shocks to growth, the non-interest current account, and the combined shock scenario all result in a significant increase in external debt to around 85–90 percent of GDP by 2026. A one-time 30 percent real exchange rate depreciation would have an even larger impact on external debt, increasing debt to around 120 percent of GDP. However, external debt remains more resilient to interest rate shocks because of the relatively large share of concessional financing in external public debt.

Table 1. Armenia: External Debt Sustainability Framework, 2017–26

(In percent of GDP, unless otherwise indicated)

		2017	2018	2019	2020			Projections 2021	2022	2023	2024	2025	2026	Debt-stabilizing non-interest current account 6/
1	**Baseline: External debt**	88.7	85.9	89.0	100.1			**96.4**	**88.0**	**85.6**	**82.9**	**79.8**	**77.1**	**-5.3**
2	Change in external debt	-3.5	-2.9	3.1	11.1			-3.6	-8.4	-2.4	-2.7	-3.1	-2.7	
3	Identified external debt-creating flows (4+8+9)	-7.5	-1.4	-1.7	10.5			-8.5	-9.4	-2.2	-2.5	-2.8	-2.5	
4	Current account deficit, excluding interest payments	-2.3	3.4	3.7	-0.6			-1.9	0.0	1.4	2.2	2.6	2.9	
5	Deficit in balance of goods and services	10.8	13.6	13.2	9.9			8.4	8.8	9.9	10.2	10.0	9.8	
6	Exports	38.3	39.7	42.0	29.8			32.8	33.7	34.9	35.8	35.4	35.0	
7	Imports	49.0	53.3	55.2	39.7			41.3	42.4	44.7	46.0	45.5	44.9	
8	Net non-debt creating capital inflows (negative)	-1.2	-1.8	-1.8	-0.2			-1.6	-1.6	-2.0	-2.4	-2.4	-2.3	
9	Automatic debt dynamics 1/	-4.0	-3.0	-3.6	11.2			-5.0	-7.8	-1.6	-2.3	-3.0	-3.0	
10	Contribution from nominal interest rate	3.8	3.6	3.7	4.4			4.0	3.5	3.4	3.3	3.0	2.8	
11	Contribution from real GDP growth	-6.3	-4.3	-6.0	7.1			-5.0	-4.5	-4.2	-3.8	-3.7	-3.5	
12	Contribution from price and exchange rate changes 2/	-1.5	-2.3	-1.3	-0.2			-4.0	-6.8	-0.8	-1.7	-2.4	-2.3	
13	Residual, incl. change in gross foreign assets (2-3) 3/	4.0	-1.5	4.9	0.6			4.9	1.0	-0.2	-0.2	-0.2	-0.3	
	External debt-to-exports ratio (in percent)	232.0	216.5	212.0	336.3			293.8	261.6	245.4	231.6	225.3	220.1	
	Gross external financing need (in billions of US dollars) 4/	1.9	2.5	2.8	2.6			2.1	2.7	3.3	3.6	4.3	4.0	
	in percent of GDP	16.8	19.8	20.7	20.3	10-Year	10-Year	15.5	16.9	19.7	20.4	22.2	19.2	
	Scenario with key variables at their historical averages 5/							**105.4**	**106.9**	**106.8**	**106.8**	**106.7**	**106.6**	**-2.4**
						Historical	Standard							
	Key Macroeconomic Assumptions Underlying Baseline					Average	Deviation							
	Real GDP growth (in percent)	7.5	5.2	7.6	-7.4	3.5	4.5	5.5	5.3	5.0	4.8	4.7	4.8	
	GDP deflator in US dollars (change in percent)	1.7	2.7	1.6	0.2	-0.2	4.5	4.1	7.6	0.9	2.1	2.9	3.0	
	Nominal external interest rate (in percent)	4.5	4.4	4.7	4.6	4.2	0.6	4.4	4.1	4.1	4.1	3.9	3.8	
	Growth of exports (US dollar terms, in percent)	23.7	12.1	15.7	-34.2	6.9	16.9	21.2	16.1	9.8	9.7	6.7	6.7	
	Growth of imports (US dollar terms, in percent)	26.4	17.5	13.1	-33.2	4.2	18.8	14.2	16.4	11.8	9.9	6.6	6.5	
	Current account balance, excluding interest payments	2.3	-3.4	-3.7	0.6	-2.6	4.0	1.9	0.0	-1.4	-2.2	-2.6	-2.9	
	Net non-debt creating capital inflows	1.2	1.8	1.8	0.2	3.2	2.5	1.6	1.6	2.0	2.4	2.4	2.3	

1/ Derived as [r - g - r(1+g) + ea(1+r)]/(1+g+r+gr) times previous period debt stock, with r = nominal effective interest rate on external debt; r = change in domestic GDP deflator in US dollar terms, g = real GDP growth rate, e = nominal appreciation (increase in dollar value of domestic currency), and a = share of domestic-currency denominated debt in total external debt.

2/ The contribution from price and exchange rate changes is defined as [-r(1+g) + ea(1+r)]/(1+g+r+gr) times previous period debt stock. r increases with an appreciating domestic currency (e > 0) and rising inflation (based on GDP deflator).

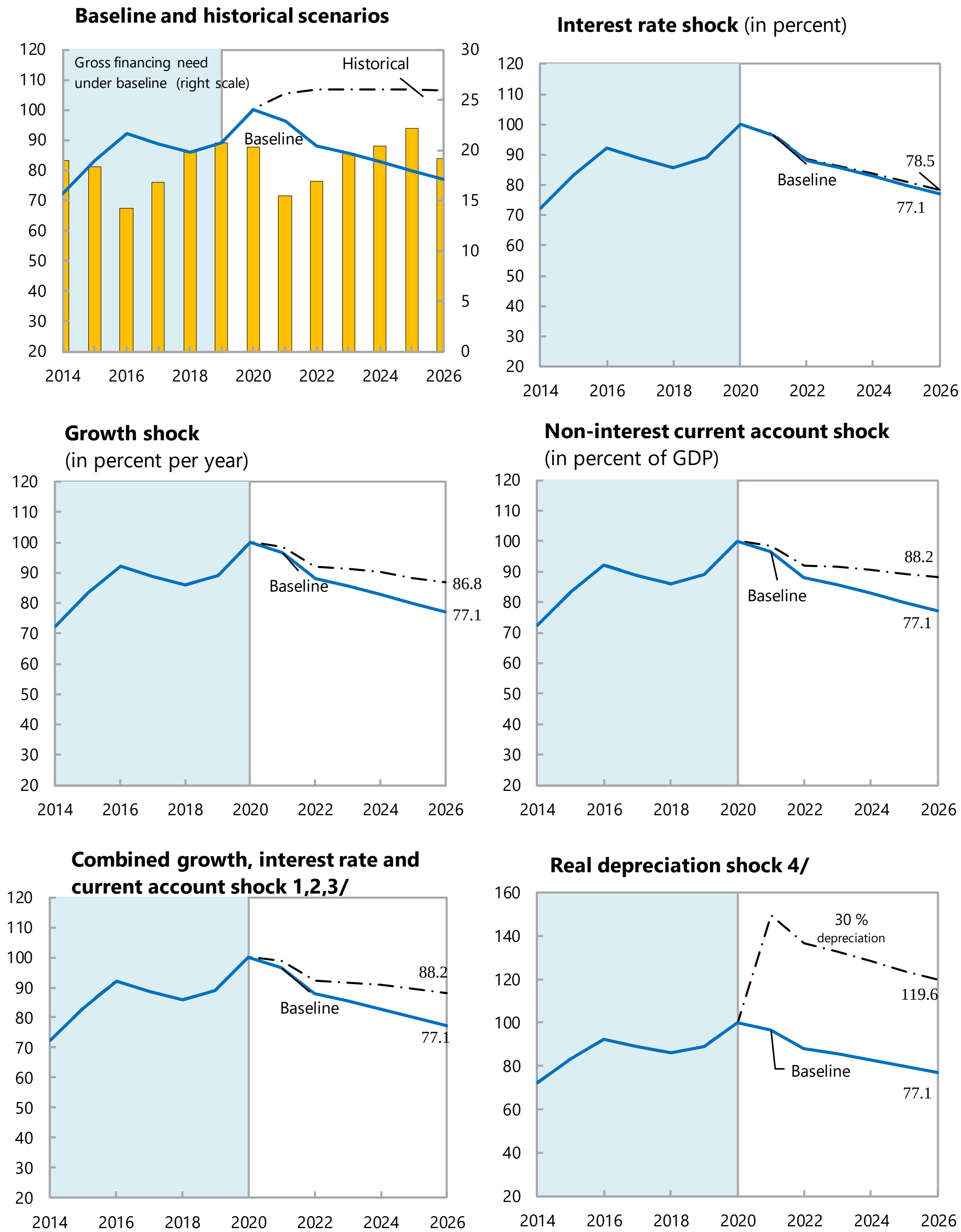
3/ For projection, line includes the impact of price and exchange rate changes.

4/ Defined as current account deficit, plus amortization on medium- and long-term debt, plus short-term debt at end of previous period.

5/ The key variables include real GDP growth; nominal interest rate; dollar deflator growth; and both non-interest current account and non-debt inflows in percent of GDP.

6/ Long-run, constant balance that stabilizes the debt ratio assuming that key variables (real GDP growth, nominal interest rate, dollar deflator growth, and non-debt inflows in percent of GDP) remain at their levels of the last projection year.

Armenia: External Debt Sustainability: Bound Tests 1/ 2/



Sources: International Monetary Fund, Country desk data, and staff estimates.
1/ Shaded areas represent actual data. Individual shocks are permanent one-half standard deviation shocks. Figures in the boxes represent average projections for the respective variables in the baseline and scenario being presented. Ten-year historical average for the variable is also shown.
2/ For historical scenarios, the historical averages are calculated over the ten-year period, and the information is used to project debt dynamics five years ahead.
3/ Permanent 1/4 standard deviation shocks applied to real interest rate, growth rate, and current account balance.
4/ One-time real depreciation of 30 percent occurs in 2021

Annex IV. Implementation of the 2019 Article IV Recommendations

1. **The 2019 Article IV Consultation with Armenia focused on four pillars:** (i) anchoring fiscal policy on the fiscal rule to maintain debt sustainability, and creating space for priority (social and capital) spending; (ii) further strengthening of the monetary policy framework and maintaining a flexible exchange rate system; (iii) safeguarding the financial system and improving access to finance; and (iv) implementing a strong package of structural reforms, with renewed emphasis on inclusiveness and governance.

2. **The 2019 Article IV occurred together with a request for a 36-month Stand-By Arrangement (SBA) amounting to US$248.2 million.** At the time, the authorities indicated that they were planning to treat the program as precautionary. The SBA aimed at supporting the authorities' efforts in strengthening the economic fundamentals and policy frameworks, with a rich structural reform agenda, particularly in the area of governance and business climate.

Fiscal Policy

3. **The 2019 Article IV Consultation recommended promoting growth-friendly fiscal consolidation.** The key medium-term challenge was identified as preserving debt sustainability, while maintaining space for investment and social spending. In line with the upgraded fiscal rule, the authorities prepared a corrective action plan to bring central government debt to below 50 percent of GDP by 2023.

4. **These recommendations only begun to be implemented and had to be revised following the two large shocks to the Armenian economy in 2020.** During 2019–21 revenue increased by 1ppt of GDP on average compared with 2016–18, allowing for a consequent increase in social spending even while debt fell to 50 percent of GDP in 2019. However, capital expenditure remained unchanged (as percent of GDP), generally suffering from execution problems, while other current spending rose (especially in 2020). As a result, fiscal deficits and debt increased, leaving public debt at 63 percent of GDP at end-2020. While the 2019 budget was in line with the fiscal rule, the escape clause was used in 2020 and 2021 to allow for the financing of support measures. Targeted and temporary fiscal flexibility was necessary in 2020 to respond to the consequences of the COVID pandemic and the military conflict with Azerbaijan in 2020. With the recovery underway in 2021, the authorities have reiterated their commitment to reducing government debt in line with the fiscal rule for 2022 and beyond.

Monetary Policy and Financial Sector

5. **The 2019 Article IV Consultation recommended continued strengthening of the inflation targeting (IT) framework, exchange rate flexibility, and development of capital markets, the supervisory framework, and macroprudential tools.** The effectiveness of the IT framework should be further strengthened by developing a well-functioning interbank market

and enhancing the CBA's communication capabilities. The CBA committed to drawing on the FSAP 2018 recommendations, including strengthening the regulatory and supervisory framework for banks, fostering financial inclusion, and preparing a plan to develop capital markets.

6. These recommendations have largely been implemented. Monetary policy has been guided by the IT regime, while anchoring inflationary expectations. The CBA has started to hold press conferences after board meetings as well as after publishing financial stability reports to improve communication. Exchange rate flexibility was preserved, proving particularly important during 2020. The CBA has largely intervened only to counter disorderly market conditions. In line with the FSAP recommendations, the CBA aligned its NPL definition with international standards and is scheduled to introduce Loan-to-Value (LTV) limits on new mortgages in April 2022. The regulatory and supervisory framework for banks has also been enhanced. To operationalize aspects of the authorities' 2020 Capital Market Development Program, the CBA has prepared a 2021 action plan that suggests deepening FX, money and sovereign markets, strengthening the primary dealer network, and developing an electronic platform for FX trading platform.

Structural Reforms

7. The structural reforms agenda for the 2019 Article IV Consultation focused on reforms toward developing a dynamic market-based economy, strengthening governance and fair competition, promoting inclusive growth over the longer term.

8. Progress has been made, with the government's new 2021–26 program expected to build on this progress. The authorities adopted a law on a single autonomous anti-corruption entity (Law on Anticorruption Committee), prepared an annual action plan to improve the business environment, and developed a comprehensive education reform strategy and employment strategy. The new 2021–26 government program is building on some of these priorities, including improving the business environment, strengthening corporate transparency and governance, operationalizing the new Anti-Corruption entity, and improving the efficiency of SME support.

Annex V. The 2021–26 Government Program

The government's 5-year program comprises six priority areas:

1. Security and foreign policy: Key priorities include modernizing the army, strengthening the strategic Russian-Armenian partnership, and working toward the re-opening of regional infrastructure.

2. Economy: The government intends to pursue a knowledge-based, export-oriented, investment-driven growth strategy, aimed at reducing poverty. Key objectives for the next 5 years are outlined in Box 1.

3. Infrastructure Development: The focus will be on transportation, road construction, water, and energy sectors.

- **Transportation:**
  - **Road transportation:** A unified route network will be introduced—providing quality transport services to all communities in the Republic at affordable costs and improved information systems. This will require the use of latest technologies to i) carry out electronic monitoring and control; ii) introduce unified ticketing, interactive maps, and effective rapid response systems in road tolls.
  - **Air transportation:** Aviation safety will be improved by upgrading standards through i) regulating the operation of unmanned aerial vehicles; ii) signing and introducing an Agreement on the Common Aviation Area of the Republic of Armenia and European Union and EU Member States; iii) negotiating with major foreign airlines to develop joint local air carriers; iv) working with the airport concessionaire to improve the quality of services and lower tariffs; v) improving access to airport by construction of new roads; and vi) establishing new organizations specialized in the aviation sector.
  - **Rail transportation:** Safety and service quality will be improved through acquisition and modernization of passenger-freight rolling stock; amendments to the Concession Agreement; investment of about AMD 39 billion over the next 3 years for renovations within the agreements reached with the Concessionaire (and AMD 95 billion over the period 2025–38).
  - **Water transportation:** The government plans to develop and adopt a law on commercial navigation and increase cargo turnover under the Armenian flag.
- **Road construction:** The Government plans to develop a safe, cost-effective, and environmentally safe road network that is well connected internationally, including to facilitate exports. Reforms include rehabilitation and construction of interstate and national-local roads (about 500 km annually), tunnels, and bridges; modernization of traffic accident data collection

and analysis systems; implementation of the North-South Road Corridor project; and reconstruction of Vanadzor-Alaverdi-Bagratashen interstate road (M-6, 52 km). Also, the impact assessment of climate change on road infrastructure is envisaged. The government considers launch of a public-private partnership mechanism in the field.

- **Water management:** The goal is to improve water supply (including for drinking and irrigation) and drainage management through reforms which include i) reconstruction of the emergency sections of "Arpa-San" tunnel; ii) building reservoirs; iii) promoting the use of water-saving irrigation systems (e.g., a complete reconstruction of inter-economic-in-house irrigation networks by 2023 will generate 7.3 million kwh of electricity savings annually and increase irrigated lands by 1373 hectares); iv) implementation of 10 priority anti-flood programs; and v) carrying out the restoration of water supply and drainage systems in 11 cities and 41 rural settlements, and rehabilitation of distribution networks.

- **Energy independence and security.** The overall goal is to ensure a reliable and high-quality supply of electricity and gas to consumers (including from renewables). Policy measures include a gradual liberalization of the electricity market; modernization of the second power unit of the Armenian NPP by 2026 (and for another 10 years through additional investment) and construction of a new nuclear power unit; increasing the share of solar energy production to 15 percent by 2030; finalization of the Armenia-Iran-Georgia-Russia quadrilateral North-South Electricity Corridor initiative; becoming an electricity hub in the region through the operation of the Armenia-Iran and Armenia-Georgia 400 kV overhead power transmission lines; promotion of energy efficiency measures under the requirements of the Armenia-EU Comprehensive Extended Partnership Agreement; and implementation of knowledge-based and smart energy sector programs.

4. Human capital development: Target areas include demography, migration, education, science, health, labor and social protection, youth, culture, sport, and environmental protection.

- **Education:** Steps will be taken to create an inclusive education environment; modernize content, curricula, information technologies, and infrastructure; strengthen "education-science-labor market" link through separate quantitative targets in general, pre-school, vocational training, and higher education.

  - **General education** will be enhanced through the introduction of new standards in all grades by 2026; renovation and construction of at least 300 schools; creating modern natural science and engineering laboratories; adopting new textbooks and educational materials; introducing a differentiated professional development policy for teachers enabling them to have at least a 30–50 percent salary increase; improve management and financing systems by digitizing processes; and developing e-learning tools to ensure access to education at all levels.

  - **Pre-school education.** The focus will be on renovation and construction of at least 500 kindergartens and preschools by 2026; increasing the number of 3–5-year-old children

enrolled in pre-school institutions to at least 85 percent by 2026; introducing effective mechanism of remuneration for teacher-educators by the example of general education.

- **Vocational training** will be enhanced through modernization of educational programs; introduction and expansion of work-based dual training in at least 2 educational institutions per year; assessing new management models; introduction of attestation systems and linking them with remunerations; improving the building conditions, providing laboratories (at least 2 institutions per year).

- **Higher education.** Attention will be paid to reviewing the content of curricula and outcome-based structures by 2025; internationalization of higher education; gradual increase of funding for higher education; providing an attractive physical, virtual, and socially attractive environment (e.g., establishing an Academic City); creating effective collaboration between schools, universities, and the private sector to raise awareness of the demand for future professions.

- **Health:** The government strives to enhance access to high-quality healthcare. This will require a comprehensive health insurance system; prevention and early detection of infectious and non-communicable diseases; providing free drugs for the list of severe and long-lasting diseases; focusing on mother- and child-health care; expansion of the e-health system; providing smooth operation of the health care system in emergencies and martial law situations; improve the system of epidemiological surveillance of infectious diseases, in particular, learning lessons from the Covid-19 pandemic; modernization of regional medical organizations (50 health facilities); providing medical institutions with qualified specialists in the field of healthcare continuously increasing the salaries of medical workers, according to the results and introducing a system for licensing of medical workers by 2025.

- **Employment and social protection** policies will be guided by a strategic document that comprehensively responds to the existing problems of the sector. Following steps will be taken by 2026:

  - ✓ Equalize the amounts of minimum pensions and average pensions with the values of food and consumer baskets, respectively.
  - ✓ Set the minimum salary at AMD 85,000.
  - ✓ Eliminate extreme poverty.

  Social assistance will strike a balance between covering basic needs and disincentives to work. It is planned to i) increase the coverage of social assistance; ii) improve their targeting through means testing; iii) provide disability benefits or jobs to those with disabilities incurred during military service; iv) improve gender equality; v) assess the social needs of about 1000 elderly people cared for in social protection institutions outside. By 2023, day care centers will be established in all regions with at least 50 visitors each, 3 crisis centers for 60+ elderly will be established, home care will be introduced in all regions.

- **Environmental protection** will focus on increasing the country's resilience to climate change through adaptation and mitigation policies. Priorities include efficient use of water resources (e.g., Lake Sevan); improving waste management; sustainable forest management; ensuring a gradual reduction and limitation of the use of disposable polyethylene products; review the threshold for taxation of metallic minerals; harmonization of environmental legislation with the instructions of the Armenia-EU Comprehensive Extended Partnership Agreement and ongoing cooperation with international organizations operating in this field.

5. Law and justice: Measures to create and develop an anti-corruption system include

- ✓ Assist the CPC in developing legislation and capacities,
- ✓ Launch the full operation of Anti-Corruption Committee and Anti-Corruption Court.
- ✓ Develop structures for confiscation of Illicit Property and operationalize it,
- ✓ Implement comprehensive assessment of corruption risks at the state and local level, development of action plans based on it.
- ✓ Develop mechanisms for monitoring anti-corruption programs.
- ✓ Digitalize public services by providing them through a single electronic platform.
- ✓ Establish joint public service offices in the regions.
- ✓ Include subject programs on anti-corruption education in all levels of education.

6. Institutional development. The government plans to improve public service delivery (driven by public administration reforms), align programs with strategies, and pursue prudent public finance policies.

- **Public service delivery and human resources** will be reviewed and modernized by establishing a unified horizontal system in which

  - ✓ Positions and functions are complementary.
  - ✓ Hiring, firing, performance appraisal, training, and work organizations are modernized.
  - ✓ A senior executive corps is formed as a group of professionals holding managerial positions.
  - ✓ The remuneration system is made attractive, merit based (depending on the scope of responsibility and competencies), and rewards are separated from pay. Such reforms should be budget-neutral, at least in the first phase.
  - ✓ The current system of education, training and retraining of civil servants is reviewed.
  - ✓ Digitalization is pursued.

- **Public finances.** Growth-friendly tax policies and expenditure savings should result in low budget deficits. Alongside 7–9 percent growth, such deficits should guarantee debt sustainability.

  - ✓ **Spending.** Efforts will be made to speed up the implementation of capital projects; create a Public Investment Programs (PIP) database; tap the into private-sector’s resources through PPPs; increase the share of spending on human capital and infrastructure;

introduce a new e-procurement system in line with modern functional requirements; and institute the logical chain of "function-body-responsibility-result-evaluation" in the public administration system.

- ✓ **Revenues.** Steps will be taken to rationalize inefficient and untargeted tax expenditures; establish a fair and equitable tax burden; study the taxation of dividends and interest incomes and propose changes if necessary; gradually reduce mortgage interest deductions in Yerevan and target this incentive toward urban development; reform taxation of the agricultural sector; expand the geography of double taxation agreements; and introduce an effective system of individual income declarations alongside improved incentives via "social credits", where individuals can reduce their tax liabilities for justified (documented) expenses on social, education, health, housing purposes. The government would also analyze the possibility of abolishing import taxation at the importation phase (that is taxing all imports not at the border, but in Armenia). These policies will ensure that the tax-to-GDP ratio improves by 2.6 pp by 2026. bringing the ratio to at least 25 percent of GDP.

- ✓ **Debt management.** Increase the share of AMD-denominated debt to reduce exposure to exchange rate risks. Return to full compliance with Fiscal Rules.

Annex VI. Methodology: Inflation Drivers in Armenia

The annex provides some background information on the methodology used to analyze the drivers of inflation in Armenia presented in Box 2. It describes the reduced-form Phillips curve and the structural vector autoregression (VAR) approaches.

1. A reduced-form Phillips curve is estimated for Armenia, taking the following functional form[1]:

$$\pi_t = \beta_1 \pi_{t-1} + \beta_2 \pi_t^e + \beta_3 y_t + \sum_{i=0}^{1} \beta_{i+4} \Delta P_{t-i} + FE + \varepsilon_t \quad (1)$$

where t indexes the quarterly time period, starting in Q1 2011. π_t is CBA's seasonally adjusted measure of core inflation, which excludes seasonally volatile goods (fruits, vegetables, eggs) and publicly regulated services. π_t^e is a survey-based measure of inflation expectations constructed by staff, which is calculated as the difference in the share of respondents who expect high or very high inflation and those that expect low or decreasing inflation over the next 12 months, with 1 unit representing 10 percentage points in the regression. y_t is the CBA's output gap estimate, and ΔP_{t-i} is the change in Armenia's seasonally adjusted import price index. Time fixed effects (FE) are added to capture any trend in inflation over time.

2. A structural VAR model for a small open economy like Armenia takes the following form:

$$\Delta y_t^* = \sum_{j=1}^{k} a_{11j}\, \Delta y_{t-j}^* + e_{1t} \quad (2)$$

$$\Delta \pi_t^* = \sum_{j=1}^{k} a_{21j}\, \Delta y_{t-j}^* + \sum_{j=1}^{k} a_{22j}\, \Delta \pi_{t-j}^* + e_{2t} \quad (3)$$

$$\Delta y_t = \sum_{j=1}^{k} a_{31j}\, \Delta y_{t-j}^* + \sum_{j=1}^{k} a_{32j}\, \Delta \pi_{t-j}^* + \sum_{j=1}^{k} a_{33j}\, \Delta y_{t-j} + \sum_{j=1}^{k} a_{34j}\, \Delta s_{t-j} + \sum_{j=1}^{k} a_{35j}\, \Delta \pi_{t-j} + e_{3t} \quad (4)$$

$$\Delta s_t = \sum_{j=1}^{k} a_{41j}\, \Delta y_{t-j}^* + \sum_{j=1}^{k} a_{42j}\, \Delta \pi_{t-j}^* + \sum_{j=1}^{k} a_{43j}\, \Delta y_{t-j} + \sum_{j=1}^{k} a_{44j}\, \Delta s_{t-j} + \sum_{j=1}^{k} a_{45j}\, \Delta \pi_{t-j} + e_{4t} \quad (5)$$

$$\Delta \pi_t = \sum_{j=1}^{k} a_{51j}\, \Delta y_{t-j}^* + \sum_{j=1}^{k} a_{52j}\, \Delta \pi_{t-j}^* + \sum_{j=1}^{k} a_{53j}\, \Delta y_{t-j} + \sum_{j=1}^{k} a_{54j}\, \Delta s_{t-j} + \sum_{j=1}^{k} a_{55j}\, \Delta \pi_{t-j} + e_{5t} \quad (6)$$

where t indexes the quarterly time period, starting in 2007Q3. y_t^* is the log of the weighted average of normalized seasonally adjusted real GDP of Armenia's main trading partners (China, Russia, and Germany), π_t^* is seasonally adjusted import price index, π_t is the CBA's seasonally adjusted measure of core inflation, y_t is log of seasonally adjusted real domestic GDP, and s_t is seasonally adjusted nominal effective exchange rate. The structure of the system is such that y_t^* and π_t^* evolve independently of domestic variables for Armenia (π_t, y_t, and s_t), while the latter consistent with assumptions for a small open economy could depend on their own current and lagged values as well as on current and lagged values of y_t^* and π_t^*.

[1] The approach follows Chapter 2 from the October 2021 WEO, adapted for Armenia.

The orthogonal innovations from this recursive structure define five different shocks, which are interpreted as foreign demand (coming from y_t^*), foreign supply (coming from π_t^*), domestic demand (coming from y_t), NEER (s_t), and domestic cost (π_t). The VAR was estimated based on quarterly data and using one lag.

Appendix I. Letter of Intent

Ms. Kristalina Georgieva
Managing Director
International Monetary Fund
Washington, DC 20431

Yerevan, November 19, 2021

Dear Ms. Georgieva:

1. In the attached update to the Memorandum of Economic and Financial Policies (MEFP) from May 2, 2019, we reconfirm our strong commitment to sound policies and the objectives of the economic program supported by our IMF Stand-by Arrangement (SBA), notwithstanding the economic impact that the twin shocks of 2020 had on Armenia.

2. After a severe recession in 2020, our economy is rebounding strongly in 2021, although inflation has also picked up considerably. Spurred by recovering external and domestic demand, the economy posted almost 5 percent growth in first half of 2021. Assuming that the impact of Covid-19 remains muted, the economy is projected to recover further in the remainder of 2021 and through 2022. Annual CPI inflation accelerated to 8.9 percent in September driven by pent-up consumption, supply constraints, global and domestic food inflation, and pass-through from dram depreciation in early 2021. The fiscal deficit narrowed in the first half of 2021 owing to strong revenue collection, and a gradual scaling down of the emergency spending necessitated by the twin shocks of 2020. Capital and liquidity buffers have remained strong. The external position has also strengthened, with the currency appreciating in the past few months.

3. We continue to focus on advancing our reform agenda, which has been recently elaborated through the Government's 2021-26 Program and approved by the National Assembly in August. Our key goal is to ensure resilient, export-led, and inclusive growth, which is critical for the future prosperity of the Armenian people. To achieve our goals, we will need to maintain fiscal sustainability, develop human capital, enhance social safety nets, bolster financial sector resilience and domestic capital markets, and improve the business climate and governance through ambitious structural reforms. To ensure continued progress toward fiscal sustainability, we plan to adopt the 2022 budget by end-December consistent with program targets and aim to improve the efficiency and equity of our tax system by broadening the tax base and strengthening revenue administration while also creating space for higher capital and social spending.

4. Notwithstanding a challenging environment, we have managed to keep program implementation broadly on track. We met all quantitative performance criteria (QPCs) and indicative targets (ITs) for end-December 2020 and end-March except for the March NIR IT. Aside from the QPC on NIR and MPCC inflation target band, we also met all end-June quantitative conditionality. The pre-election period has delayed the completion of some SBs, although we remain committed to the implementation of the underlying actions. We also propose some new benchmarks (outlined in the attached memorandum), which we expect to complete between now and the end of our current

IMF-supported program, which expires on May 16, 2022. The NIR fell below the June (adjusted) target by US$144 million, reflecting larger-than-projected government foreign exchange conversions ($60 million) and sell-side intervention in Jan-Apr 2021 (US$ 156 million) to counter disorderly market conditions following the ceasefire agreement over Nagorno-Karabakh. We are, therefore, requesting a waiver for the nonobservance of June-2021 QPC on NIRs based on several corrective actions: (i) the establishment of a committee, comprising the CBA and MoF, to improve projections for government conversions, and the ongoing efforts to strengthen the MoF's capacity to collect data on their demand for such FX conversions; (ii) implementation of measures to develop the functioning and depth of the foreign exchange market, as specified in the MEFP; and (iii) the saving of the SDR allocation. Moreover, end-June inflation (6.5 percent) breached the upper-bound of the MPCC, triggering a Board consultation, which we will undertake as part of this review cycle.

5. Based on the steps that we have already taken and our commitments under the program, we request completion of the fourth and fifth reviews and plan to purchase drawing rights under the SBA for budget support purposes upon completion of the reviews. While we believe that the policies set forth in the attached MEFP are adequate to achieve the macroeconomic and financial objectives of the program, we will take any additional measures that may be needed. We will consult with the IMF on the adoption of these measures, and in advance of revisions to the policies contained in the MEFP, in accordance with the IMF's policies on such consultation. We will also provide IMF staff with the data and information requested for the purpose of monitoring program implementation. Reaffirming our commitment to transparency, we consent to the IMF's publication of this letter along with the attached MEFP and the Technical Memorandum of Understanding (TMU), as well as the IMF staff report for the 2021 Article IV consultation and the combined fourth and fifth reviews under the SBA, subject to Executive Board approval.

Yours sincerely,

/s/
Nikol Pashinyan
Prime Minister

/s/	/s/
Tigran Khachatryan	Martin Galstyan
Minister of Finance	Governor, Central Bank of Armenia

Attachment I. Memorandum of Economic and Financial Policies (MEFP)

1. This memorandum supplements our memoranda of May 2 and December 3, 2019 as well as April 30 and November 24, 2020—providing information on recent developments and highlighting our key policies for the remainder of 2021 and 2022.

RECENT ECONOMIC DEVELOPMENTS AND OUTLOOK

2. Economic performance in 2021 has been strong with inflation picking up. Spurred by recovering external and domestic demand, the economy posted 5 percent growth in 2021H1. Annual CPI inflation accelerated to 9.1 percent in October driven by pent-up consumption, supply constraints, global and domestic food inflation, and pass-through from dram depreciation in early 2021. The fiscal deficit narrowed in 2021H1 owing to strong revenue collection, and a gradual scaling down of emergency spending to the twin shocks of 2020 (as outlined in our memorandum of November 24, 2020). Capital and liquidity buffers have remained strong, helped by the measures that we introduced to cushion the banking system from the impact of the pandemic, including the restriction on dividend distributions, and tightening of underwriting standards by banks in response to the economic uncertainty. The external position has also strengthened, with the currency appreciating over the past few months.

3. While we expect our policy actions and ongoing reforms to deliver visible near-term benefits, we are cognizant of downside risks including from the fourth wave of COVID-19 infections. We project the Armenian economy to remain on a recovery path in the remainder of 2021 and through 2022, benefiting from the lifting of the political uncertainty following the June elections as well as our planned reform agenda (as outlined in our 5-year Government program and the 2022 draft budget). To limit the risks from elevated COVID-19 infections, we plan to continue accelerating our vaccination efforts and have procured sufficient vaccines to inoculate 63 percent of the Armenian population (or 75 percent of the population aged 12 and above). We expect inflation to begin moderating by mid-2022, as the effect of supply-side and external shocks dissipate, and the impact of recent monetary policy actions become fully felt. As elaborated below, our draft 2022 budget is in line with the objectives of the Government 2021-26 program and balances near-term support with the medium-term needs for higher capital spending and, in line with Armenia's fiscal rules, the rebuilding of fiscal buffers. We expect financial conditions to remain favorable in the near term. Robust exports and remittances are expected to narrow the current account deficit in 2021.

4. To ensure the smooth and credible implementation of the government's 5-year program, we are working with line ministries and agencies to develop concrete action plans with associated key performance indicators and costings. The Government program should facilitate Armenia's transition to a knowledge-based, private- and export-led economy, where growth is both more inclusive and sustainable (¶17). The program's priorities include

security and the reopening of regional infrastructures; human capital and infrastructure development; improved public service delivery; good governance; law and justice; and other institutional reforms. We plan to release detailed action plans by December 1, 2021 and align the programs of line ministries and agencies with government's strategic objectives. We also intend to embed the cost of various programs in budgets and medium-term expenditure frameworks (MTEF).

FISCAL POLICY

5. **In 2021, higher-than-budgeted revenues are expected to narrow the fiscal deficit despite unexpected outlays.** Tax revenues were buoyed by the economic recovery, a temporary surcharge on mining exports and increases in labor duties.[1] However, the tax-to-GDP ratio is set to remain at 22.5 percent, slightly higher than collected pre-pandemic. Additional spending to cover post-conflict needs (2.3 percent of GDP including a 1.3 percent of GDP loan to Nagorno-Karabakh), as well as pandemic-related health and economic support measures (0.5 percent of GDP including 0.1 percent of GDP in loans). However, the rest of public expenditure, including capital spending, has been contained and is on track to be broadly consistent with budgeted levels despite higher than anticipated inflation. As a result, the 2021 fiscal deficit is expected to reach 4.7 percent of GDP, which is 0.7 percentage points lower than the 2020 deficit and the budgeted target at the time of the third review.

6. **Our 2022 draft budget strives to support the recovery and growth potential through increased public capital spending while safeguarding fiscal sustainability.** We intend to limit the 2022 budget deficit to AMD 243 billion or 3.1 percent of GDP. Further, we plan to increase current spending to AMD 1,843 billion (23.4 percent of GDP, 1½ percentage points lower than 2021), including about AMD 70 billion in reserve funds that we intend to use if actual revenues in 2022 evolve in line with our nominal budgeted revenues These reserve funds will be made available for additional spending in the areas declared by the Government or to address any risks which may occur through the course of the year to the extent that the cumulative quarterly tax revenues align with budgeted plans. Excluding reserve funds, nominal current spending will remain below its estimated 2021 level. We have allocated AMD 347 billion (4.4 percent of GDP) to public capital spending to address infrastructure gaps, support the recovery, and boost medium-term growth potential. We expect to raise total revenues of around 24.7 percent of GDP helped by the economic rebound as well as our efforts to eliminate unproductive and distortive tax loopholes and to improve tax compliance.

7. **We plan to cover our gross financing needs from domestic and external sources, including our development partners.** We expect around $400 million in external official budget support and project loans, and intend to request support from our development partners. Specifically, we will be working with the EU to agree on the modalities of cooperation (including the sectors for support, and the composition of their planned support package, as well as its

[1] Mandatory withholdings from wages to finance compensation payments for killed and wounded soldiers and their families.

timing). We plan to finance the 2022 state budget deficit by borrowing 250 billion drams on a net basis from domestic markets. In meeting our financing needs, we will ensure that the government's cash deposits maintain a sufficient cushion for cash-flow management purposes as well as contingent needs, while also not creating undue pressure on the external sector.

8. We reiterate our commitment to medium-term fiscal sustainability and will work to ensure sufficient space for public investment and social spending. We plan to steadily reduce the fiscal deficit-to-GDP ratio in the medium-term which will place the government debt-to-GDP ratio on a declining path in line with our fiscal framework. Specifically, if Government's expectations realize, central government debt to GDP will fall below 60 percent by end-2023, and with continuous fiscal efforts, move towards 50 percent, in line with our fiscal rule. To this end, we aim to increase the tax-to-GDP ratio by 0.5 percentage points of GDP each year to reach 25 percent in 5 years (from 22.4 percent in 2020) through growth-friendly measures, including by widening the VAT net to cover electronic services, by scaling down mortgage interest tax deductions, by reforming the turnover and microenterprise tax regimes to remove tax arbitrage opportunities (see below), and by introducing individual personal income tax declarations over time as well as other measures to boost revenues including through improved compliance. Finally, we will strive to ensure that current expenditure growth is in-line with Armenia's fiscal rules. By raising domestic revenue and reprioritizing current spending, we will be able to allocate additional resources to the social safety nets and public investment which are critical to delivering the government's growth and inclusion goals while meeting our debt objective.

9. We will strive to mitigate the macro-fiscal impact of any major new downside shock. Our primary concern will be to ensure national security, support for the vulnerable and necessary health spending. To limit the impact of any new shock on the budget, we will, as in 2020, reallocate and reprioritize spending within the current spending envelope, as well as reallocate underutilized/delayed capital spending, and consider other potential options.

STRUCTURAL FISCAL POLICIES

10. We continue to modernize our tax policy and administration systems. We are bringing forward reforms that improve efficiency and fairness of the tax system, remove distortions, support inclusive growth, foster compliance, and boost revenue collection.

- We intend to consolidate and update various existing tax policy strategies into a single overarching document featuring detailed actions plan and implementation timeline by end-April 2022.

- We are working to strengthen the mining sector taxation following a thorough review of existing legislations and sufficient public consultation. Our aim will be to ensure that the government captures a fair share of extra-profits generated by high international commodity prices without impeding future development of the sector. We commit to carefully review existing legislations, with the assistance of the IMF before preparing future

legislative reforms (new February 2022 SB). We aim to introduce the new permanent taxation regime applicable to the mining sector.

- We plan to submit legislative packages to the National Assembly by June 2022 to (i) eliminate CIT deductions for larger firms based on invoices from micro enterprises, (ii) move the taxation of micro enterprises away from a lump-sum PIT towards the general PIT regime, and (iii) adjust the turnover tax rate to at least equalize the tax burden across the turnover and general taxation regimes as well as consider whether a reduction in the VAT registration threshold could be appropriate, with the intention of changes coming into effect by January 1, 2023.

- We plan to make several other revenue-raising reforms to the tax system while making it equitable. To this end, we will (i) bring B2C electronic services under the VAT net by end-2021; (ii) phase out mortgage interest PIT deductions for new apartments and private houses in the territory of Yerevan by January 1, 2025 and redirect the program toward regions; (iii) assess other VAT exemptions with the support of development partners and eliminate those that are ineffective and expensive; and (iv) revise the capital income taxation and terminate exemptions or differential tax treatments that create arbitrage opportunities.

- Guided by a comprehensive review of securities' taxation supported by IMF TAs, we aim to remove impediments to capital market development in Armenia, including by improving tax transparency and certainty of securities taxation.

- We will finalize Armenia's tax gap analysis with a view to reducing policy and compliance gaps. Particularly, we will finalize the currently conducted VAT gap estimations and commence compliance gap estimations for CIT and PIT with IMF assistance. Guided by the IMF's RA-GAP methodology, we will institute regular compliance gap estimations to identify areas of improvement and guide reform progresses, as well as assist in effective compliance risk management.

- We will strengthen the legislative and regulatory framework to improve tax compliance management. Specifically, we will legislate changes to end the publication of audit targets in advance of tax audits by May 2022 and assess the adequacy of fees and penalties for non-compliant behavior and raise them when warranted. We will also update the legal framework and practices related to indirect tax audits, including by expanding the types of methods used, by revising and clarifying when and which indirect audit methods can be applied, by shifting the burden of proof more towards taxpayers when indirect audits are used, and by allowing for greater access to key data sources.

- We plan to introduce an individual income tax declaration system over time. We consider such declarations to be an important tool for reducing informality and narrowing the tax gap. To ensure progress in this area, we will work towards legislative changes that allows the SRC greater access to relevant data as needed to verify declared income and tax

liability, in line with international best practices. Moreover, we view individual income tax declarations as an important tool for identifying the vulnerable and improving the design and targeting of our social assistance programs.

11. In line with our public financial management strategy, we are working on strengthening fiscal governance, transparency, and long-term sustainability.

- ***Budget process.*** We are committed to improve our program-based budgeting process and to strengthen linkages between strategic planning and budget preparation (including by accurately estimating the cost of programs and by setting measurable key performance indicators). With assistance from the IMF, we plan to reformulate the structure and functions of our Budget Department to further enhance its institutional, personnel, and analytical capacities. We aim to strengthen the methodology used to distinguish mandatory expenditure from discretionary spending, and to better integrate the PIM system within the budget process and medium-term expenditure framework.

- ***Public expenditure review.*** We will work to improve the analytical capacity of the Ministry of Finance to increase the efficiency and effectiveness of current spending. To this end we will pilot an expenditure review of the wages in the central Government with IMF technichal assistance with active involvement of the MoF staff (April 2022 SB). The level of on-lending for Nagorno-Karabakh in 2021 reflects the need to ensure the well-being and address the humanitarian needs of the local population. Along with the Nagorno-Karabakh authorities, we intend to undertake an evaluation of this support during 2022 with the intention of ensuring the efficiency and effectiveness of this support, aiming to graduate such support, which of course highly depends on the speed of conflict resolution and overall geopolitical situation in the region in large.

- ***Public investment management (PIM).*** We are committed to operationalizing (rolling-out) of the PIM decree approved in May 2021 in full. The Ministry of Economy will engage in outreach activities with line ministries to showcase the system and ensure that all new investment projects follow the approved appraisal and selection processes. The Investment Committee will be inaugurated in January 2022. We will develop and publish a project database that will provide comprehensive information on all newly proposed projects regardless of financing source (external or internal), including PPPs. It will cover 5 project concept notes by May 2022 and the number will increase to 10 by October 2022. We will aim at providing information about the lifetime fiscal implications of projects (beyond the MTEF horizon when necessary) in the database.

  For transparency purposes, we will publish the assessment of cost overruns and the remaining cost obligations for ongoing large, funded projects in budget documents. We will also start compiling a database of comprehensive information (including lifetime costs) on past major public investment projects completed within the last 1-2 years.

- ***Public-private partnerships (PPPs).*** We are fully committed to complete the PPP Operational Framework, and report PPP-related fiscal risks and costs.

- As part of July 2021 amendments to the PPP law, we aim to approve a decree by March 2022 (proposed new SB) to set a cap on direct liabilities, thereby limiting annual payment commitments for any future year that could crowd out other priority spending.

- We have incorporated PPPs in the enhanced PIM framework where all public investment projects are developed, assessed, selected, procured in a transparent and competitive way, and implemented according to unified procedures, rules, priorities, and constraints. We will write secondary legislation to determine a PPP-specific legal framework for procurement that is aligned with best international practice. We will ensure that the process for unsolicited proposals, allowed by the newly amended PPP law, will follow these principles. Chapter 4 of the UNCITRAL model legislative provisions on PPPs will guide the rationale for any exceptions to general competitive procurement principles.

- We will also ensure timely and transparent communication of PPP related costs and risks in line with international best practice (Fiscal Transparency Handbook 2018).

- Cognizant of significant fiscal risks that PPPs may carry, we will refrain from contracting any new PPPs at any government level until both the MoE and MoF are prepared to fully evaluate and manage such risks, i.e., until the enhanced public investment management process (covered in this and the preceding bullets) is fully rolled out and applied to PPPs.

- We will ensure that all PPPs that have been legislated by a government decree before the effective date of the amended PPP law will have undergone a thorough and comprehensive assessment of fiscal risks. As we are aware of the reputational and fiscal risks associated with operating outside of the new PPP legislative framework, we commit to publish such evaluation in the budgetary documents as well as all past and future contractual documents related to such PPPs in the budgetary documents.

- ***Fiscal risks management***. The newly reorganized and enhanced fiscal risk function in the MoF will be adequately resourced to enable a comprehensive monitoring, assessment, and management of fiscal risks. We will also foster better coordination on fiscal risks across different public entities, including between the MoF, MoE, and the CBA. We will continue to strengthen the comprehensive and consolidated fiscal risk summary in budget documentations.

- ***Fiscal transparency.*** We are committed to improve fiscal transparency and governance practices. We will convene relevant stakeholders to assess how to improve the usefulness of budget documentation and reporting. We will also deliver on the improvement plan for government finance statistics (GFS) approved in 2020. Specifically,

- By the first quarter of 2022, we will finalize the Public Sector Institutional Table compiling a comprehensive sectorized list of all public sector entities to allow for the extension of GFS coverage and improvement of fiscal risk monitoring.

- We will ensure that all State-owned enterprises and their subsidiaries publish financial statements and report adequately on the use of funds they hold We will review, and if necessary, improve the governance and reporting standards and ensure that those standards are followed strictly.

- We will publish the details of the release of the second tranche of funding for Armenian National Interests Fund, including the specifics of how the first AMD 5 billion was used (in light with the spirit of the Government Decree N 771-L), as well as the intended purpose and use of the recently released funds.

- We will strengthen and formalize cooperation between compilation institutions (MoF, Armstat and CBA).

- We will improve the compilation and reporting of expenditure budget plans and their execution. We will update the charts of accounts and use the detailed Treasury data to ensure records are in line with GFSM 2014 and can facilitate their meaningful interpretation. We will publish breakdowns of programs and activities to detailed economic and functional classifications on a quarterly basis and include such breakdowns at the aggregate level in the State Budget Law.

- ***Exchange rate arrangement.*** The MoF will continue to use market-determined exchange rates for all budget transactions and for transactions by project implementation units. The CBA and MoF have agreed on a new draft amendment to the 2007 contract to be implemented from January 1, 2022. Under the amendment, if during the day the prevailing market exchange rate deviates by more than two percent from the buy and sell exchange rates set by CBA for this day at the time of the transaction with the MoF, then the Central Bank shall set new buy and sell exchange rates to ensure that the difference from the prevailing market exchange rate is not greater than two percent. The CBA will not execute transactions in respect of payment orders received from the MoF at exchange rates differing from the newly-set sell exchange rates.

MONETARY AND FINANCIAL SECTOR POLICIES

12. To ensure price and financial stability, the CBA has gradually tightened monetary policy and further strengthened its regulatory and supervisory framework. All banks have adequate capital and liquidity largely owing to buffers that were in place prior to the pandemic and regulatory measures that were introduced to preserve the stability of the financial system. NPLs have also been on a downward trend since February 2021. To facilitate timely identification of risks to financial stability, we will continue to undertake comprehensive top-down solvency

and liquidity stress testing. We also plan to improve our bottom-up stress testing capabilities and the use of cybersecurity simulation exercises to inform our cyber threat response.

- ***Policy rate.*** To limit inflationary risks and anchor inflation expectations, we have raised rates since December last year (cumulatively by 300 bps), bringing the policy rate to 7.25 percent in September. While we see these as effective steps to manage inflation dynamics, we stand ready to adjust monetary policy accordingly in response to changes in the economic outlook and inflation expectations. The end-June inflation (6.5 percent) breached the upper-bound of the program monetary policy consultation clause (MPCC), triggering a Board consultation, which will be undertaken as part of this combined fourth and fifth reviews under the SBA, and Article IV Consultation (see attached letter, Attachment III).

- ***Net international reserves.*** We remain committed to exchange rate flexibility, with intervention limited to mitigating disorderly market conditions. Government foreign exchange conversion needs have been volatile, and this volatility partly contributed to the nonobservance of the June-2021 performance criterion on net international reserves. To improve the quality of projections on planned conversions, and their timely incorporation in CBA FX liquidity projections, the CBA and the MoF established a committee in September 2021 to improve projections of such conversions. Relatedly, the MoF is strengthening its capacity to collect data from line ministries on demand for FX conversions. More generally, we are taking measures to strengthen FX market functioning and depth (¶14), which should also limit the risk around predicting the movement in NIR. We remain committed to strengthening reserve buffers opportunistically when market conditions are favorable. Finally, we plan to save additional SDR allocation to boost reserves and have purchased $22 million since June 2021.

- ***Liquidity provision.*** Domestic markets have generally functioned smoothly since the onset of the COVID-19 pandemic, as the CBA has conducted repos and FX swap operations to provide the market with liquidity in line with the demand. As a result, the short-term interbank interest rate has remained close to the target policy rate. We will continue to ensure adequate liquidity in domestic markets.

- ***Regulatory and supervisory responses.***

- We have introduced new asset classification and provisioning rules which align the NPL definition with international standards. We will enhance the supervision of banks' loan loss provisioning processes including those used to estimate Expected Credit Losses (ECL) under IFRS 9.

- We will also be reviewing our regulatory and supervisory framework to address the risks from digitization and new products. Further, we recently established a Working Group on Environmental, Social and Governance (ESG) risks as part of efforts to build our capacity to assess and mitigate these risks within the Armenian banking system.

- We will introduce a supervisory platform to support the collection, validation, analysis, storage and reporting of information from banks to help inform supervisory activities and risk mitigation measures. In line with the World Bank (WB) Technical Assistance (TA), we will also develop our internal processes for the assessment of banks' Internal Capital Adequacy Assessment Process (ICAAP) with a view to introducing Pillar 2 buffers within 2 – 3 years.

- In line with the WB TA, we plan to improve our resolution framework by developing our capacity and processes to effectively resolve banks if the need were to arise. We also plan to enhance our capacity to evaluate the viability and sustainability of banks' business models including the assessment of drivers of profitability, strategic plans, and banks' implementation capacity.

- ***COVID-related macroprudential measures***. In response to COVID-19, we encouraged banks to use the combined capital buffers to absorb losses and maintain lending to the economy. Consistent with the assessment of the cyclical risks and the continuing uncertainty about future developments, the CBA maintained the countercyclical capital buffer rate at zero percent of risk weighted assets and these measures are aligned with Basel III recommendations. Given the reduction in uncertainty over the impact of the pandemic, and to improve the resilience of the banking system to further shocks, we will require banks to maintain a capital conservation buffer of 1.5 percent, and systemically important banks to hold additional capital requirement of 1.0 percent above the minimum capital requirements from January 2022. The plan is to subsequently increase these buffers to 2.5 percent (by January 2024) and 1.5 percent (by January 2023), respectively. We have also required all banks to seek CBA authorization before they can distribute dividends or pay bonuses to management.

13. The CBA has strengthened its communication strategy as a part of a broader effort to enhance monetary transmission and in response to the COVID-19 situation.

- The CBA Governor holds regular press conferences on monetary policy and financial stability issues.

- The CBA regularly holds meetings with financial institutions to discuss CBA forecasts and assist with any other issues which financial organizations are facing.

- The CBA hotline service has been working in emergency mode to promptly address the public's questions, concerns, and queries over CBA policy.

- The CBA includes the results of stress tests in financial stability reports and plans to review its monetary policy report and construct a new CBA website.

14. We continue working on promoting capital market development and digitalization of the financial sector. We approved a comprehensive capital market development strategy in

2020 and are developing an action plan with specific milestones and timelines covering reforms to the money market, FX market, sovereign market as well as derivative markets, building on the IMF TA. This action plan will be jointly implemented by the CBA and the Ministry of Finance. Specifically, we are committed to creating centralized platforms for overnight repo market and for the FX market by March 2022 (proposed new SB), as well as a methodology to create money market reference rates, based on developed and liquid overnight repo market. We have finalized the framework and rules for a centralized foreign exchange trading platform that should result in a more liquid market. In the meantime, negotiations are underway to sell equity shares of the Armenia Securities Exchange to Warsaw Stock Exchange. We have also adopted an ambitious plan on the digital transformation of financial services, including the payment services, which we expect will create a secure ecosystem for digitalized financial services leveraging on digital identity and interoperability.

15. We continue to strengthen our macroprudential toolkit and have adopted stressed Loan-to-Value (LTV) limits, which will take effect for new mortgages from April 2022. The limits will be 90 percent for local currency and 70 percent for FX loans (March 2021 SB). We will also continue to explore the use of other macroprudential measures to complement the LTV limits including higher sectoral risk weights and plans to establish a debt service to income (DSTI) limit. We will implement any necessary monitoring and enforcement procedures to ensure full compliance with and effective implementation of these measures once they are introduced.

16. We have finalized a strategy for a phased exit from non-core CBA operations. This strategy includes: (i) transferring full control of the activities to independent and professional Boards of Directors; (ii) clearly defining any public objectives that should continue to be pursued by these entities after the exit of the CBA, including safeguards for users and consumers; (iii) setting up a comprehensive strategy for the pursuit of these objectives after the exit of the CBA, defining any roles played by regulation, public supervisory bodies, public agencies and government entities, subsidies, or strategic minority public participation in the company's capital; (iv) undertaking feasibility analysis of market conditions and defining CBA's exit options, principles and models; (v) in line with the strategies thus defined, attracting institutional private sector investors or, in case of critical infrastructure, transforming into an independent, transparent and sustainable institutions. In the selection of institutional investors, which could include multinational or reputable international companies and organizations providing extensive transfer of knowledge and know-how, we will follow best international practices to ensure transparency and accountability in the process. With respect to our participation in Stak Money Transfer/Processing, Armenian Card, and ACRA, we will continue our involvement in digitalization and financial inclusion investments to support the financial sector digital transformation over the medium term. Some activities providing infrastructural services could also be merged and rendered more efficient through innovation, including by adopting and expanding Digital and Fintech solution for high quality, competitive and affordable services.

STRUCTURAL REFORMS

17. The Government's Program for 2021-26 emphasizes our commitment to structural reforms to attract investment and enhance inclusive growth. We intend to pursue a knowledge-based, export-oriented, investment-driven growth model, aimed at reducing poverty and enhancing social protection. Achieving these objectives requires the following steps:

- Boosting the manufacturing, tourism, and agriculture sectors through land, water management, labor, and transportation reforms as well as digitalization.
- Building stronger trade links, with a more diversified export basket and markets.
- Infrastructure development aimed at improving connectivity (including road construction), urban development, and green energy generation.
- Expanding economic opportunities through SME support, capital market development and improved access to finance, education and healthcare reforms, and increased female labor force participation (helped by childcare support).
- Human capital development and increased and better targeted social assistance.
- Improved corporate governance as well as judicial and anti-corruption reforms.
- Public administration reforms to improving service delivery.

18. To support this structural reform agenda, we will aim to create space through growth-friendly revenue-enhancing tax policies, spending prioritization, and higher quality investment. We strive to achieve these objectives by designing detailed sectoral action plans (including by line ministries), by aligning the ongoing and prospective programs with the Government program’s strategic objectives, while at the same time maintaining medium-term sustainability and full compliance with fiscal rules. In undertaking this development program, we will be technically and financially supported by several of our development partners, including ADB, the European Union, EBRD, EIB, and the World Bank.

PROGRAM MONITORING AND SAFEGUARDS

19. The program will continue being monitored through quantitative performance criteria, indicative targets (Table 1), a monetary policy consultation clause, and structural benchmarks (Table 2). The sixth and final review, to be completed on or after April 15, 2022, will be based on end-December 2021 targets and other relevant performance criteria.

Table 1. Armenia: Quantitative Performance Criteria, Indicative Targets and Consultation Clause 1/

(In billions of drams, at program exchange rates, unless otherwise specified)

	2020					2021									2022
	Sep. [3/]	Dec. [2/]				Mar. [3/]			Jun. [2/]				Sep. [3/]	Dec.	Mar. [3/]
	Act.	EBS 20/178	Adjusted Target	Act.	Status	EBS 20/178	Adjusted Target	Act.	EBS 20/178	Adjusted Target	Act.	Status	EBS 20/178	Prog. [2/]	Proj.
Performance Criteria															
Net official international reserves (stock, floor, in millions of U.S. dollars)	1,332	1,348	1,099	1,131	Met	1,474	1,735	1,695	1,464	1,610	1,475	Not met	1,471	1,331	1,282
Program fiscal balance (flow, floor) [4/]	-240	-517	-433	-421	Met	-181		-72	-253		-127	Met	-356	-492	-160
Budget domestic lending (cumulative flow, ceiling)	40	115		41	Met	45		0	45		31	Met	45	50	45
External public debt arrears (stock, ceiling, continuous criterion)	0	0		0	Met	0		0	0		0	Met	0	0	0
MPCC 5/															
Inflation (upper-outer band, inflation consultation, percent)	4	4.5		4.5		5.0			5.1				5.2	11.0	10.0
Inflation (upper-inner band, percent)	3.3	3.5		3.5		4.0			4.1				4.2	9.0	8.0
Inflation (mid-point, percent)	1.4	1.5		3.8	Met	2.0		5.8	2.1		6.5	Not met	2.2	8.5	7.5
inflation (lower-inner band, percent)	0.0	0.0		0.0		0.0			0.1				0.2	3.5	3.5
Inflation (lower-outer band, inflation consultation, percent)	0.0	0.0		0.0		0.0			0.0				0.0	2.5	2.5
Indicative Targets															
Net domestic assets of the CBA (stock, ceiling)	390	622		599	Met	605		348	589		464	Met	572	755	757
Avg. concessionality of newly contracted ext. debt (flow, floor, in percent) [6/]	...	30		43	Met	...		...	...		...	...	...	30	...
New government guaranteed external debt (stock, ceiling, in millions of USD) [7/]	0	100		0	Met	100		0	100		0	Met	100	100	100
Social spending of the government (flow, floor) [8/]	44	58		62	Met	16		17	32		33	Met	48	65	17

Sources: Armenian authorities; and Fund staff estimates.

1/ All items as defined in the TMU, based on program exchange rates in the TMU.

2/ Quantitative performance criteria at test dates.

3/ Indicative target.

4/ Below-the-line overall balance excluding net lending.

5/ If the end of period year-on-year headline inflation is outside the upper/lower bound, a formal consultation with the Executive Board as part of program reviews would be triggered.

6/ Assessed on a calendar year basis, excluding the Eurobond and any similar refinancing instruments.

7/ Includes both concessional and non-concessional debt, excluding the Eurobond and any simliar refinancing instruments.

8/ Defined as spending on the family benefit program and lump-sum financial aid, one-time childbirth benefits, and childcare benefits for children less than two years of age.

Table 2. Armenia: Structural Benchmarks				
Measures	**Responsible Agency**	**Time Frame**	**Status**	**Macro Criticality/Status**
Fiscal				
Create an action plan to implement key recommendations from IMF TA on tax administration on developing a compliance strategy and strengthening core functions and processes	State Revenue Committee (SRC)	June 2019	Met	Improve tax administration and compliances
Submit a draft law "On Establishing Market Evaluation Procedure for Real Estate Taxation" to the National Assembly to implement a value-based recurrent property tax with appraised property values closely aligned to market prices	Deputy Prime Minister's Office	June 2019	Met	Enhance revenue mobilization and fairness
Submit a public-private partnership (PPP) law to the National Assembly, establishing reporting and monitoring as well as requiring a ceiling on government exposure from such partnerships	Ministry of Economic Development and Investments (MoE)	June 2019	Met	Incentivize FDI and investment in infrastructure projects
Design an action plan to improve tax compliance and raise tax-to GDP ratio in the medium term, based on a study identifying tax potential and factors preventing tax collection reaching this potential	Deputy Prime Minister's Office	December 2019	Not met. Split into new SBs with new dates.	Improve tax administration and compliances
Design a Compliance Risk Management strategy to improve tax administration and compliance, based on IMF TA recommendations.	State Revenue Committee	September 2020	Met	Improve tax administration and compliance
Conduct a study identifying tax potential and factors preventing tax collection reaching its potential.	Deputy Prime Minister's Office	October 2020	Not met, implemented with delay	Create fiscal space
Design an action plan to reduce the tax policy gap identified in the study.	MoF	December 2020	Not met, implemented with delay	Create fiscal space
Develop and approve by ministerial order a plan for how GFS in Armenia will be extended and improved over the next two to three years.	MoF, in collaboration with the CBA and Armstat	September 2020	Met	Improve government statistics

Table 2. Armenia: Structural Benchmarks (continued)

Compile a comprehensive sectorized list of all public sector entities, with IMF TA support.	MoF and Armstat	March 2021	Met	Improve government statistics
Compile and estimate all the existing and future contingent liabilities associated with implemented and approved PPPs	MoF	January 2021	Met	Improve fiscal risk management
Approve and publish a decree setting a cap to the total contingent liabilities contracted from PPPs.	MoF	February 2021	Not met, implemented with delay	Improve fiscal risk management
Build a database of projects covering both externally and domestically funded projects that provides information on projects throughout their lifecycle.	MoE and MoF	December 2020	Not met MEFP commitment (¶11), May 2022	Enhance project selection and monitoring.
Revise the turnover tax legislation by reducing the VAT registration threshold to AMD 60.00 million and adjusting tax rates to equalize the tax-burden across the turnover and general taxation regimes, effective from January 1, 2022.	MoF	May 2021	Not met. MEFP commitment (¶10), to revise the turnover tax legislation to take effect from January 1, 2023	Enhance revenue mobilization and fairness
Undertake a public expenditure review, with a view to identifying options for efficiency gains and improving the social protection system.	MoF	May 2021	Not met MEFP commitment (¶11), with a new SB for April 2022.	Create fiscal space
Conduct the review of securities' taxation to ensure appropriate taxation in this area and identify possible distortions and impediments to capital market development.	MoF	June 2021	Met	Promote capital market development and ensure fair taxation

Table 2. Armenia: Structural Benchmarks (continued)

Include in the 2022 budget documentation a comprehensive list with all ongoing public investment projects and new public investment projects starting in the budget year, including PPPs, providing comprehensive information on lifetime fiscal implications, including project by project information for all externally financed projects and large domestically financed projects (at least 50 percent of investment volume from domestic financing).	MoF	October 2021	Not met. MEFP commitment (¶11) to improve transparency around the PIM process	Enhance project selection and monitoring
Undertake a careful review of the taxation and fee regime applicable to the mining sector with a view to its reform so that (i) the government captures its fair share of returns from national resources; and (ii) the future development of the sector is not jeopardized	MoF	February 2022		Enhance revenue mobilization
Approve a decree to set a cap on direct PPP-related liabilities, thereby limiting annual payment commitments for any future year that could crowd out other priority spending	MoF	March 2022		Improve fiscal risk management
Undertake a public expenditure review of civil service compensation.	MoF	April 2022		Improve the analytical capacity of the Ministry of Finance to increase the efficiency and effectiveness of current spending
Monetary and Financial				
Prepare a time-bound action plan and communication strategy to boost foreign currency liquidity buffers as described in the 2018 FSAP recommendations (paras 19, 21 and 32) through a combination of liquidity tools	Central Bank of Armenia (CBA)	September 2019	Met	Enhancing macro prudential measures
Develop a capital market development program	MoE, CBA, MoF	May 2020	Not met. Implemented with delay	Create access to long-term, local-currency finance and improve monetary policy transmission

Table 2. Armenia: Structural Benchmarks (continued)

Develop a framework for strengthening financial reporting and auditing to establish the public oversight body and the Chamber of Accountants and Auditor, focusing on improving corporate financial information and reducing SME financial reporting requirements with assistance by the World Bank	MoF	March 2020	Met	Strengthen transparency and improve SME's access to finance
Prepare a medium-term exit strategy to phase out the CBA involvement in non-core central bank activities (i.e., development lending and subsidiaries)	CBA	April 2021	Not met. Implementation pending	Curtail engagement in quasi-fiscal activities that do not relate to core central bank's mandate; eliminate potential financial and reputational risks.
Introduce limits to stressed Loan-to-Value (LTV) ratio	CBA	March 2021	Not met. Implemented with delay	Mitigate credit risks from unhedged borrower and vulnerabilities from rapid credit growth and dollarization This measure has been approved, and given a required notification period, is expected to start in April 2022.
Create and operationalize an over-the-counter commercial trading platform for the overnight repo market and for the FX market transactions	CBA	March 2022		Support capital market development and access to finance.
Structural				
Submit to the National Assembly a draft law on a single autonomous anti-corruption entity in line with international standards, which combines all detection and investigative functions	Ministry of Justice (MoJ)	September 2020	Not met, implemented with delay	Combat against corruption
Adopt a legislation to require the establishment of a registry of beneficial ownership information, which is adequately resourced and staffed, and can conduct verification, first beginning with companies in the extractive industry, as identified in the EITI 2016 Standard	MoJ	June 2019	Met	Combat against corruption
Prepare an annual action plan to improve the business environment to address core issues identified by the 2019 Doing Business	MoE	February 2020	Met	Improve business climate

Table 2. Armenia: Structural Benchmarks (concluded)

Conduct an efficiency review of the existing government SME support programs and consolidate support mechanisms, tools and programs	MoE with support from the CBA	September 2020	Not met	Improve effectiveness of the SME state support activities and enhance access to finance
Develop Armenia’s employment strategy for 2019–23	MoL	December 2019	Met	Reduce unemployment and enhance inclusiveness of vulnerable groups in the labor market
Submit to the National Assembly a draft law on Higher Education and Science which sets the legal ground for (i) reforming the tertiary education management system; (ii) upgrading licensing and accreditation requirements, state financing principles, supervision mechanisms for quality of education services.	Ministry of Education and Science	June 2020	Not met, implemented with delay	Improve growth inclusiveness
Develop a comprehensive education reform strategy	Ministry of Education and Science	June 2020	Met	Enhance equitable access to education and improve physical conditions.

Attachment II. Technical Memorandum of Understanding (TMU)

1. This memorandum sets out understandings between the Armenian authorities and the IMF staff regarding the definition of performance criteria (PCs) and indicative targets (ITs), adjusters, and data reporting requirements for the Standby Arrangement as per the Letter of Intent and Memorandum of Economic and Financial Policies (LOI/MEFP) dated April 26, 2019.

2. For program monitoring purposes, all foreign currency-related assets, liabilities, and flows in the monetary accounts will be evaluated at program exchange rates. The program exchange rate of the Armenian dram to the U.S. dollar is set at 483.75 dram per one U.S. dollar. The cross-rates for other foreign currencies are provided in Table 1.

QUANTITATIVE TARGETS

3. The program sets PCs, ITs, and the Monetary Policy Consultation Clause (MPCC) for defined test dates (see Table 1 in the MEFP).

The program sets the following PCs:

- Floor on the net official international reserves (NIR) of the Central Bank of Armenia (CBA);
- Floor on the program fiscal balance;
- Ceiling on domestic budgetary lending; and,
- Ceiling on the stock of external public debt arrears (continuous).

The program sets the following ITs:

- Ceiling on the net domestic assets (NDA) of the CBA;
- Floor on average concessionality of newly contracted external debt;
- Ceiling on new government guaranteed external debt; and,
- Floor on social spending of the government.

The program sets the following MPCC:

- Headline inflation.

4. **The net official international reserves** (NIR) (stock) of the Central Bank of Armenia (CBA) will be calculated as the difference between total gross official international reserves (excluding commercial bank required and excess reserves at CBA in FX) and gross official reserve liabilities.

- **Gross official international reserves** are defined as the CBA's holdings of monetary gold (excluding amounts pledged as collateral), holdings of Special Drawing Rights (SDRs), including SDR allocations, the country's reserve position at the IMF, and holdings of convertible currencies in cash or in nonresident financial institutions (deposits, securities, or other financial instruments). Gross reserves held in the form of securities and other financial instruments are marked to market. Excluded from gross reserves are the balance on the government's Special Privatization Account (SPA), capital subscriptions in foreign financial institutions and illiquid foreign assets, any assets that are pledged, collateralized, or otherwise encumbered, claims on residents, claims in foreign exchange arising from derivatives in foreign currencies vis-à-vis domestic currency (such as futures, forwards, swaps, and options), precious metals other than gold, assets in nonconvertible currencies, and illiquid assets.

- **Official reserve liabilities** shall be defined as the total outstanding liabilities of the government and the CBA to the IMF (excluding SDR allocations) and convertible currency liabilities of the CBA to nonresidents with an original maturity of up to and including one year, as well as commitments to sell foreign exchange arising from derivatives (such as futures, forwards, swaps, and options).

NIR is monitored in U.S. dollars, and, for program monitoring purposes, assets and liabilities in convertible currencies other than the U.S. dollar shall be converted into dollar-equivalent values using the convertible exchange rates as specified in Table 1.

5. **MPCC headline inflation** is defined as the year-on-year rate of change of the Consumer Price Index as measured by Armenia's National Statistics Service. The MPCC will be considered met if headline inflation falls within the upper and lower (outer bands) around the mid-point target specified in Table 1 in the LOI/MEFP. Consultation with IMF Board would be triggered for end December 2021 test date if inflation falls outside the outer bands. The consultation with the Board will be on the reasons for the deviation and the proposed policy response before further purchases could be requested under the SBA. Specifically, the consultation will explain (i) the stance of monetary policy and whether the Fund-supported program remains on track; (ii) the reasons for deviations from the specified band, taking into account compensating factors; and (iii) on proposed remedial actions, as deemed necessary. In addition, a staff consultation clause whereby the CBA will consult with IMF staff on the outlook for inflation and the proposed policy response will be triggered if inflation falls outside the inner bands and within the outer bands (Table 1 in the LOI/MEFP) for the December 2021 test date.

Inflation Consultation Bands

	Dec-21	March-22
Upper outer band	11.0	10.0
Upper inner band	9.0	8.0
Center point	8.5	7.5
Lower Inner band	3.5	3.5
Lower outer band	2.5	2.5

Source: IMF Staff.

6. **Net domestic assets** are defined as reserve money minus NIR, minus other assets not included in gross official international reserves, minus commercial bank required and excess reserves at CBA in FX, plus medium and long-term foreign liabilities (i.e., liabilities with a maturity of one year

or more) of the CBA, plus other foreign liabilities not included in official reserve liabilities, minus the balance of outstanding Fund purchases credited to the government account at the CBA. NDA is composed of net CBA credit to the general government plus outstanding credit to domestic banks by the CBA (including overdrafts) minus liabilities not included in reserve money and other items net.

7. **External public debt arrears** are defined as external debt obligations of the government that have not been paid when due in accordance with the relevant contractual terms (taking into account any contractual grace periods).[1] This PC excludes arrears on external financial obligations of the government subject to rescheduling.[2] This PC is to be monitored continuously by the authorities and any occurrence of new external arrears should be immediately reported to the Fund. The ceiling on external payment arrears is set at zero.

8. **The program fiscal balance** is cumulative from the beginning of the fiscal year and is measured from the financing side as the negative of the sum of net domestic banking system credit to the central government, net domestic nonbank financing, and net external financing to the central government. Should a general subsidy or any other fiscal transaction be introduced off-budget, the overall balance will be measured including the subsidy and other fiscal transactions as part of government spending.

- **Net banking system credit to the central government** equals the change during the period of net credit to the central government.

- **Net nonbank financing** equals the sum of: (1) the change during the period of outstanding treasury bills and bonds to nonbanks (including accrued interest for treasury bills and excluding accrued interest for treasury bonds);[3] (2) any other disbursement or transaction that increases nonbanks' claims on the central government plus withdrawals from the Special Privatization Account (SPA) or the treasury sub-account containing privatization proceeds in drams, less amortization paid by the central government to private resident nonbank agents.

- **Net external financing** equals total debt-increasing disbursements from non-residents to the central government (including Fund net purchases credited directly to the government accounts at the CBA) less total amortization from the central government to non-residents. Net external financing also includes any privatization proceeds received from non-residents in foreign currency and not held in the SPA.

9. **Budgetary ER.** Foreign currency-denominated transactions take place at the prevailing ER at the time of the transaction. The framework arrangement will not be modified (in substance) but

[1] The term debt will be understood as defined in Guidelines on Public Debt Conditionality in Fund Arrangements, Decision No. 16919-(20/103).

[2] The public sector is here defined following the Government Financial Statistics Manual (GFS 2001) and System of National Accounts (1993 SNA). It includes the general government and nonfinancial public enterprises (as defined in paragraph 14).

[3] Domestic nonbank holdings of treasury bills and treasury bonds are defined as total outstanding treasury bills and bonds less holdings by the banking system and the State Fund for Social Insurance.

may be clarified to the extent necessary to avoid noncompliance with the program continuous PC on non-introduction of new exchange restrictions and multiple-currency practices, or intensification of existing ones. External and domestic net lending, which are recorded as financing items, are excluded from the calculation of the program fiscal balance, which is calculated from the financing side (see ¶8). This effectively treats net lending as an expenditure item when loans are made and as a revenue item when the loans are repaid.

10. Transactions related to the extension of the operating life of the Metsamor nuclear power station—which will take place via lending from the Russian Federation to the Ministry of Finance of Armenia and from the MoF of Armenia to the Armenian Nuclear Power Plant JSC—will be excluded from the measure of the program fiscal deficit.

11. Some project implementation units maintain accounts at the CBA. Grants received by these units are recorded in the fiscal accounts as external grants on the revenue side and as foreign-financed expenditure on the expenditure side. In addition, any loans to finance investments that are intermediated through the banking system are recorded in the financial accounts as a financing item below the line and are thus excluded from net lending.

12. Foreign currency proceeds from selling enterprises are credited to the SPA and their use is reflected in the state budget. In addition, the Government will ensure full transparency of revenues and spending from the sales of major assets (beyond regular day-to-day operations) of enterprises with state ownership. The SPA is held at the CBA and the proceeds are invested abroad together with the CBA's international reserves. These proceeds are included in the definition of the monetary accounts of the CBA as part of net foreign assets with a counter entry in other items net. Any withdrawal from the SPA will be accounted for as privatization proceeds used to finance the budget and will be recorded below the line. Domestic currency proceeds from selling enterprises to residents are deposited in a sub-account of the treasury single account and are also treated as a financing item and recorded below the line. Finally, as noted in ¶8, privatization proceeds received from non-residents in foreign currency and not held in the SPA are also treated as a financing item (sale of financial assets) and recorded below the line.

13. **Domestic budgetary lending** is defined as the gross amount of new loans made to resident individuals, enterprises, or entities financed from the state budget or other general government resources. This includes, but is not limited to, loans financed from the Economic Stabilization Fund and lending under existing or prospective government programs, such as agricultural sector support and real estate development programs, among others. Lending operations related to targeted projects financed with external loans and grants will be excluded from the calculation of the ceiling on budget domestic lending.

14. **Floor on average concessionality of newly contracted external debt.** The program sets an annual indicative floor of 30 percent on the average concessionality of new debt on a contraction basis with nonresidents with original maturities of one year or more as contracted and guaranteed by the public sector, but excludes purchases from the IMF, the Eurobond issuance, and any similar refinancing instruments. The concessionality floor is calculated on a calendar-year basis.

- The grant element is the difference between the present value (PV) of debt and its nominal value, expressed as a percentage of the nominal value of the debt. The PV of debt at the time of its contracting is calculated by discounting the future stream of payments of debt service due on this debt. The discount rate used for this purpose is a unified discount rate set at 5 percent.

- The public sector here comprises the general government (central plus local governments and covering the state budget and state debt), the central bank, and nonfinancial public enterprises (enterprises and agencies in which the government holds a controlling stake—typically owns more than 50 percent of the shares, but which are not consolidated in the budget).

- For program purposes, the guarantee of a debt arises from any explicit legal obligation of the public sector to service a debt in the event of nonpayment by the debtor (involving payments in cash or in kind), or from any implicit legal or contractual obligation of the public sector to finance partially or in full any shortfall incurred by the debtor.

15. **Ceiling on government guaranteed external debt.** In addition to the indicative floor on average concessionality, a separate, cumulative ceiling (IT) of $100 million for the program period applies to new government guarantees of the total of concessional and non-concessional external financing, excluding the Eurobond and any similar refinancing instruments. The issuance of debt guarantees will be measured at the exchange rates listed in Table 1. The above limit covers debt guarantees issued by the general government to entities outside the general government (excluding the CBA). Guarantee issuance will be monitored on a monthly basis and the Ministry of Finance will provide data within 21 days from the end of the month.

16. The program sets a floor on **social spending of the government**. For the purposes of the program, social spending of the government comprises the family benefit program and maternity benefits, one-time childbirth benefits, childcare benefits for children less than two years of age, and additional emergency or temporary spending for social protection related purposes appropriated through the budget (or supplementary budget).

17. The quantitative performance criteria and indicative targets under the program are subject to the following **adjusters**, calculated, where relevant, using program exchange rates:

- **Changes in reserve requirements**: The ceiling on the NDA of the CBA will be adjusted downward (upward) by the amount of banks' reserves freed (seized) by any reduction (increase) of the reserve requirement ratio on both domestic currency and foreign currency liabilities relative to the baseline assumption as per the following formula: $\Delta NDA = \Delta rB$, where B denotes the level of liabilities subject to reserve requirements in the initial definition and Δr is the change in the reserve requirement ratio.

- **Budget support grants to the public sector** are defined as grants received by the general government for direct budget support from external donors and not related to project financing.

- **Project support grants** are defined as grants received by the general government for public sector projects.

- **Budget support loans to the public sector** are defined as disbursements of commercial loans (e.g., Eurobonds), loans from bilateral and multilateral donors for budget support, and Fund purchases credited directly to the government accounts at the CBA.

- **Project financing to the public sector** is defined as disbursements of loans from bilateral and multilateral donors for public sector projects.

- **The floor on NIR** will be adjusted upward (downward) by the cumulative amount of any excess (shortfall) of budget support loans, and project financing loans and grants disbursed through the CBA, compared to program amounts (excluding Fund purchases by the government) as indicated in the first line of Table 2. The downward adjustment will not exceed the amount as indicated in the second line of Table 2. The floor on NIR will be adjusted downward for any external public debt amortization amounts in excess of program amounts. The floor on NIR will be adjusted upwards by the amount of any funds received for privatization proceeds received from non-residents in foreign currency and not held in the SPA.

- **The ceiling on NDA** will be adjusted downward (upward) by the cumulative amount of any excess (shortfall) of budget support loans, and project financing loans and grants disbursed through the CBA compared to program amounts (first line of Table 2). The upward adjustment will not exceed the amount as indicated in the second line of Table 2.

- **The floor on the program fiscal balance on a cash basis** will be adjusted upward (downward) by the cumulative total amount of the budget support grants received in excess (to account for a shortfall) of the program amounts (Table 3), subject to a cap of $100 million per year in either direction. The floor on the program fiscal balance on a cash basis will also be adjusted downward (upward) by the cumulative total amount of the project financing loans received in excess (to account for a shortfall) of the program amounts (Table 3), subject to a cap of $100 million in either direction.

- **The ceiling on domestic budgetary lending** will be adjusted upward by the amount of undisbursed funds under domestic budgetary lending programs approved in the previous year.

DATA REPORTING

18. The government and the CBA will provide the IMF the information specified in the following table:

Reporting Agency	Type of Data	Description of Data	Frequency	Timing
CBA	CBA balance sheet	Summary	Daily	The following working day
	CBA balance sheet	Summary at program exchange rates; and by chart of accounts at actual official exchange rates	Monthly	Within 25 days of the end of each month
	Monetary survey	Summary banking system balance sheet for the central bank at both program exchange rates and by chart of accounts at actual official exchange rates; the consolidated balance sheet of commercial banks by chart of accounts at actual official exchange rates	Monthly	Within 25 days of the end of each month
	International reserves	By chart of accounts; at (i) program exchange rates; and (ii) at actual official exchange rates	Daily	The following working day
	Foreign exchange market	Official exchange rates (buying and selling); daily trade volume, and weighted average exchange rate of the interbank, intrabank and Nasdaq-OMX	Daily	Within 1 day
	Foreign exchange market	CBA foreign exchange operations, (exchange rate, volume)	Daily	Within 1 day
	Foreign exchange market	Exchange rate (buying and selling)	Daily	Within 1 day
	Interest rates	Refinance rate	At least monthly	Within 1 days of the CBA Board decision
	Interbank money market	Daily interbank repo volume and interest rate and number of trades	Daily	Within 1 day
	CBA operations	Repo (reverse repo) operations, open market operations, Lombard credits, deposit facility, and foreign exchange swaps (volumes, maturity, yields, exchange rates)	Daily	Within 1 day
	Bank liquidity	Reserves and excess reserves, by currency	Monthly	Within 15 days of the end of each reference period
	Interest rates and	By currency and maturity	Weekly	First working day

Reporting Agency	Type of Data	Description of Data	Frequency	Timing
	flows of the funds attracted and allocated by commercial banks			of the next week
	T-bill and coupon bond financing, CBA securities	Auction data: date, original and remaining maturities, issuance volume, allocation, average yield and coupon yield (if available)	Weekly	First working day of the next week
	Banking data	Sectoral distribution of loans and deposits; dollarization of loans and deposits; loan maturities; interbank rate, by volume and maturity; T-bill rate, bond yield; deposit and lending rates, by maturity; monthly weighted average interest rate on government bonds	Monthly	Within 25 days of the end of each month
	Banking indicators	Capital adequacy; asset composition and quality; profitability; liquidity; open FX positions; and compliance with prudential norms	Monthly	Within 30 days of the end of each month
	Banking sector stress tests	Results of stress tests on exchange rate, liquidity, and credit risk	Monthly	Within 30 days of the end of each month
	On-lending via commercial banks	On lending via the CBA and government (from, KfW, WB, ADB, etc.) by type of on-lending projects (including loan disbursements and repayments)	Monthly	Within 10 days of the end of each month.
	CPI	Index of core inflation	Monthly	Within 21 days of the end of each month
	Transfers	Non-commercial transfers of individuals	Monthly	Within 35 of the end of each month
	Other monetary data	IFS format	Monthly	Within 45 days of the end of each month
	Balance of payments	Detailed balance of payments	Quarterly	Within 95 days

Reporting Agency	Type of Data	Description of Data	Frequency	Timing
		data		of the end of each quarter
	T-bill and coupon bond financing	By holders, i.e., CBA, resident banks, resident nonbanks, and nonresidents	Monthly	Within 7 days of each month
	External debt	Disbursements and stock of outstanding short-term and contracting or guaranteeing and outstanding stock of medium-and long-term external debt of the government, the CBA, and state-owned companies (by company); any stock of arrears on external debt service and outstanding stock of government guarantees and external arrears	Monthly	Within 21 days of the end of each month. For project implementation units, within 21 days of the end of each month (preliminary data) and within 45 days of the end of each month (final data)
Ministry of Finance	Revenue collection	Total revenue collected separately by the tax administration and customs administration, including revenue by individual tax, and social contributions	Monthly	Within 7 days of the end of each month
	Domestic expenditure arrears	All unpaid claims outstanding at the end of the month which includes wages, social contributions (including for pensions), family allowances, and amortization and domestic interest payments	Monthly	Within 45 days of the end of each month for government arrears
	Privatization receipts	Balance on the SPA; gross inflows into and outflows from the SPA during the month, specifying the nature of each transaction	Monthly	Within 7 days of the end of each month
	Treasury single account (TSA)	Detailed breakdown of central treasury account, including deposits at the central treasury, community budgets, off budget account, monetization account,	Monthly	Within 7 days of the end of each month

Reporting Agency	Type of Data	Description of Data	Frequency	Timing
		state budget account and the Republic correspondent account—flows during the month and end of month stocks.		
	Consolidated central government	State budget	Monthly	Within 30 days of the end of each month
	Consolidated general government	Central and local governments, and Non-Commercial Enterprises that belong within the general government (NCEs)	Quarterly	Within 60 days of the end of each quarter
	Consolidated general government	Central and local governments, and NCEs that belong within the general government	Annual	Within 180 days of the end of each year
	Budget execution	All cash receipts, cash expenditures, including domestic and external debt-service payments, external and domestic borrowing and lending operations, and inflow of grants to the central government; expenditure data will be provided according to both economic and functional classifications, consistent with the GFSM2001 methodology	Monthly	Within one month following the end of each quarter.
National Statistical Service	Balance of payments	Detailed export and import data (issues that have arisen in 2015 with EEU trade data need to be overcome as soon as possible)	Monthly	Within 28 days of the end of each month
		Detailed export and import data	Quarterly	Within 45 days of the end of each quarter
	CPI	By category	Monthly	Within 5 days of the end of each month

Reporting Agency	Type of Data	Description of Data	Frequency	Timing
State Revenue Committee	Tax arrears	By type of tax	Monthly	Within 30 days of the end of each quarter (monthly data provided on a quarterly basis)
		For or the 30 largest debtors and for all major companies in the energy, water, and irrigation sectors	Quarterly	Within 30 days of the end of each quarter
	Tax credits	Detailed data, by type of tax, of outstanding tax credits for all types of tax revenues, in both net and gross terms	Monthly	Within 45 days of the end of each (monthly data provided on a quarterly basis)
	Tax Revenues	Tax Revenue by type of tax	Monthly	Within 45 days of the end of each quarter (monthly data provided on a quarterly basis)
	VAT and turnover tax	Number of registered taxpayers	Monthly	Within 45 days of the end of each month (monthly data provided on a quarterly basis)
	VAT refund claims in arrears	Detailed data on VAT refunds in arrears which include all outstanding VAT refunds that have not been accepted (and refunded), or offset (in full or in part), or rejected (in full or in part) after the 90-day statutory processing period. Number of refund applications processed per month.	Monthly	Within 45 days of the end of each month (monthly data provided on a quarterly basis)

Reporting Agency	Type of Data	Description of Data	Frequency	Timing
	Large taxpayers	Data on the number of taxpayers and amount of taxes managed by the large tax inspectorate	Monthly	Within 45days after the end of each month
	Import data	1. Total value of recorded imports, breaking out raw diamond imports; 2. Total value of non-duty-free recorded imports; 3. Number of total transactions involving recorded imports; 4. Number of total transactions involving non-duty-free recorded imports 5. Value of recorded imports where customs value was assessed using transaction prices, breaking out raw diamond imports; 6. Value of non-duty-free recorded imports where customs value was assessed using transaction prices; 7. Number of transactions involving recorded imports where customs value was assessed using transaction prices; 8. Number of transactions involving non duty-free recorded imports where customs value was assessed using transaction prices	Quarterly	Within 30 days of the end of each quarter
	Automated VAT refunds	Number of refunds that were processed automatically (share of total refunds); total value of automated and automatic refunds and offsets; average waiting time (days) to receive refund	Monthly	Within 45 days of the end of each month (monthly data provided on a quarterly basis)
	Risk-based selection	Percentage of selected companies	Monthly	Within 45 days

Reporting Agency	Type of Data	Description of Data	Frequency	Timing
	approach	chosen on the basis of risk-based approach, identified revenue from risk-based audits		of the end of each month (monthly data provided on a quarterly basis)
	Pension system	Number of participants in the pension second pillar, social payments and funded contributions	Monthly	Within two months of the end of each quarter (monthly data provided on a quarterly basis)

Table 1. Armenia: (Program) Exchange Rates of the CBA
(As of December 28, 2018, in U.S. dollars per currency rates)

		USD	AMD
AMD	Armenian Dram	0.002	1.00
XDR	SDR	1.387	670.79
USD	U.S. Dollar	1.000	483.75
CHF	Swiss Franc	1.015	491.12
GBP	Pound Sterling	1.264	611.61
JPY	Japanese Yen	0.009	4.38
EUR	EURO	1.144	553.65
CNY	Chinese Yuan	0.146	70.48
AUD	Australian Dollar	0.704	340.75
CAD	Canadian Dollar	0.735	355.46
XAU	Gold (1 gram)	40.76	19,721.11

Source: National Authorities and IMF Staff Calculations

Table 2. Armenia: External Disbursements through the CBA in 2021–22 1/
(In millions of U.S. dollars)

	Mar-21 Prog.	Jun-21 Prog. 2/	Sep-21 Prog. 2/	Dec-21 Proj. 2/	Mar-22 Proj.
Loans and grants disbursed through the CBA	515	630	743	772	11
Maximum adjustment allowed	515	130	143	72	11

1/ Cumulative during the year
2/ The maximum cumulative adjustment is lower than in March to allow for possible temporary delays in the mobilization of external financing.

Table 3 Armenia: External Disbursements to the Government in 2021–22 1/
(In millions of U.S. dollars)

	Mar-21 Prog.	Jun-21 Prog.	Sep-21 Prog.	Dec-21 Proj.	Mar-22 Proj.
Budget support grants	0	0	0	11	0
Project financing loans	30	80	86	162	24

1/ Cumulative during the year

Attachment III. Consultation with the IMF Executive Board on the Missed Inflation Target Under the MPCC

Consultation on Breach of MPCC Target in June 2021.

Central Bank of Armenia

November 30, 2021

In June 2021, CPI inflation increased to 6.5 percent, 1.4 percent above the upper bound of the inflation consultation band of 5.1 percent, agreed under the SBA. This letter explains: (1) the reasons why inflation has breached the upper limit of the inflation consultation band; and discusses: (2) the policy response and (3) the outlook of inflation.

1. Inflation deviation from the consultation band

Over the first half of 2021 inflation has been accelerating driven by a few significant external and domestic factors, which we briefly discuss below:

Global economy and international prices

Unprecedented expansionary monetary and fiscal policies all over the world, sharp opening up of economies, and the rapid vaccination rollout during 2021 have resulted in a quick recovery of global demand. The recovery in demand, accompanied by disruptions in global supply chains and commodity markets led to significant inflationary pressures in international markets. As a result, inflation has increased markedly in major trading partners of Armenia. The 12-month inflation in Armenia increased from 3.6% in December of 2020 to 6.5% in June of 2021 primarily due to imported products prices, and secondary effects on other CPI basket components.

Uncertainty and depreciation of exchange rate

Since the last months of 2020, uncertainty has increased drastically in Armenia amid the ending of the military conflict in the Nagorno-Karabakh Conflict Zone and the subsequent political processes. The higher uncertainty has led to volatility in financial markets and depreciation pressures on domestic currency. The resulting notable depreciation of Armenian dram, about 10% since the end of 2020, affected the prices of imports contributing to higher inflation. At the same time, given the uncertainty around the future economic outlook, the share of firms changing their prices increased sharply, accelerating the usual price adjustment process. This further fueled the ongoing inflationary processes in Armenia during the first months of the year.

Domestic demand recovery

At the beginning of 2021, domestic demand was projected to remain subdued during the year given the high level of uncertainty, which would prompt an accumulation of precautionary savings. Domestic demand, however, has demonstrated signs of rapid recovery, which was pronounced by

pent-up private consumption, as households started to spend previously accumulated precautionary savings. Private investment remained subdued holding back the recovery of productive capacities necessary to keep up with the surging demand. The outpacing growth of consumption over the supply potential and the tightening labor market have also contributed to the expansion of the inflationary environment.

To summarize, higher-than-projected global inflation, disproportionate reaction of price-setting firms to the economic uncertainty and faster-than-expected recovery of pent-up consumption have all contributed to the acceleration of headline inflation away from the projected path and above the upper bound of the consultation band.

2. Policy response

In December 2020, when inflation was still below the target, the CBA reacted to *expected* inflation and increased the policy rate by 100bps, well ahead of other countries in the world The CBA's forward-looking policy balanced the risks of deanchoring inflation expectations and derailing the recovery of demand. In the course of 2021, when demand started to outpace productive capacities, monetary policy continued to increase its policy rate to curb the emerging demand cycle and control inflation expectations. In total, since December last year, the CBA has increased the policy rate by 300bps to 7.25% in September 2021. As a result, the CBA reduced the expansionary conditions, and brought them close to neutral stance. The forward-looking and consistent monetary policy tightening since the end of last year, is estimated to be sufficiently effective in containing the inflation and guiding it towards the 4% target in the medium-term horizon.

3. Inflation outlook

In September of 2021, the 12-month inflation in Armenia amounted to 8.9%. During the second half of the year, prices of seasonal goods (especially vegetables) have significantly contributed to rising inflation because of poor harvest and booming export. According to the current baseline, international commodity prices will remain high through the medium-term horizon, while the disruptive supply conditions will gradually subside over the course of 2022. At the same time, the consolidating fiscal policy in Armenia will have mainly contractionary impact on domestic demand over the medium run, while the private demand conditions will normalize. Finally, the tightening of monetary policy since the end of last year is will have sufficient impact to contain inflationary pressures. Under these conditions, the 12-month inflation is projected at 8.5% at the end of the year, then approaching the 4% target at the end of 2022 and stabilizing around it in the medium term.

In the view of remaining uncertainties around the pandemic, economic outlook and future inflationary developments, the CBA closely monitors the economic situation both in the world and domestically, and stands ready to respond accordingly in fulfilment of the price stability objective.

/s/

Martin Galstyan, Governor