



ARMENIA	2016
Population, million	3.0
GDP, current US\$ billion	10.5
GDP per capita, current US\$	3,525
Poverty rate (\$5/day 2005PPP terms)	71.7
Life Expectancy at birth, years (2015)	74.5

At a Glance

- Twenty-five years after independence, Armenia is in the final stages of a political transition to a parliamentary republic.
- A combination of low commodity prices, declining remittances, and increased political uncertainty undermined Armenia's growth and fiscal position in 2016 and reversed the trend in poverty reduction. Although the economy is expected to recover modestly over the medium term, elections in May 2017–18 will likely delay progress on the structural reform agenda and undermine prospects for further poverty reduction.
- The key economic challenge for Armenia is to reinforce macroeconomic stability and uncover new sources of steady and shared growth, anchored in a well-integrated and competitive economy.
- The World Bank Group is in the final year of implementing a Country Partnership Strategy that supports key investments focused on strengthening competitiveness and job creation and improving efficiency and equity in social services.

Country Context

Armenia's transition from a semi-presidential system to a parliamentary republic is close to complete. Parliamentary elections in April 2017 were conducted according to the amended Constitution and new electoral law, and the president will be elected by parliament rather than popular vote in spring 2018.

Armenia's national and regional contexts show that the country is at an inflection point. Since 2000, growth has slowed, and with it, the rate of poverty reduction. Some deceleration is due to the weaker performance of the country's main trading partners and a slowdown in remittance-providing countries.

However, the incipient recovery of global commodity prices buoyed the extractive industries, and rising private consumption might facilitate renewed growth in the services and retail trade sectors.

All of these require action to both raise the pace at which Armenia grows and ensure that the new pattern of growth is shared and alleviates poverty. Growing without trade will have its limits, particularly if transfers from abroad fall; growing with more trade requires structural changes.

Although poverty reduction has been impressive, a large proportion of people in Armenia are still vulnerable. Persistent geographic disparities indicate that a deeper understanding of the causes and possible solutions is needed, bearing in mind that the economy is still heavily dependent on mineral resources and agriculture.

The World Bank and Armenia

For 25 years, the World Bank has been a key partner for Armenia, with a sustained history of successful sectoral investments and an equally deep history of policy reform dialogue.

The current Country Partnership Strategy for 2014–17 supports improved outcomes in competitiveness and job creation and efficiency and equity in social services, with a cross-cutting focus on improving governance.

Both the World Bank and International Finance Corporation (IFC) portfolios are at a historic high in Armenia, with finance mobilized from a range of concessional sources using diverse instruments. The World Bank Group is increasingly focused on sharing country knowledge and operational experience to leverage other development partners' resources for effective public investment.

Key Engagement

Events such as the 1988 Spitak earthquake illustrate the devastation, economic damage, and loss of human life that can result from disasters. This earthquake resulted in over 24,000 deaths and a direct economic impact estimated at US\$15 billion. Due to Armenia's aging infrastructure, the country remains highly vulnerable, as a large-scale disaster is likely to result in a high number of casualties and significant damage to public and private assets.

One of the most vulnerable sectors is education, as 90% of schools were built prior to the first Seismic Code that was adopted in 1994. To address this issue, Armenia has made the seismic safety of schools a national priority.

Using data and analysis provided by the World Bank and the United Nations Children's Fund and the seismic retrofitting experience of high schools financed by the Bank's Education Improvement Project, the Government launched the Safe School Improvement Program (SSIP) in 2015. This is Armenia's first effort to address the seismic vulnerability of school buildings at scale.

WORLD BANK PORTFOLIO

No. of Projects: 16

Lending: \$621.4 Million

IBRD: 13 Loans (\$529.0 Million)

IDA: 5 Credits (\$108.9 Million)

SREP: 1 Grant (\$8.55 Million)

SSIP's current target is to improve the safety of 426 schools—31% of all schools in the country, with funding of US\$88.5 million provided by the Asian Development Bank.

As part of the Armenia National Disaster Risk Management (DRM) Program, the World Bank is helping the Government develop technical guidelines for retrofitting and reconstruction and also providing training to government officials, engineers, and private contractors. As part of an agreement with donor partners, the Government has committed to using the new guidelines to update Armenia's normative documents.

With these efforts under way, Armenia is better positioned to ensure that investments in strengthening infrastructure will help protect students and reduce potential damages and loss in school facilities located in high and medium seismic hazard zones. The country has also reduced potential education disruptions that would result from having to repair schools in the event of an earthquake.

The Program is helping to advance resilience across other sectors by improving disaster risk information, strengthening institutions, and increasing the understanding of fiscal risks. In 2017, the World Bank is helping the Government better understand the fiscal impacts of disasters and providing policy options for disaster risk financing and insurance. These efforts will increase DRM capacity and preparedness while protecting fiscal balances to help reduce the fiscal burden of disasters on the government, businesses, and households.

Recent Economic Developments

Growth slowed considerably to 0.2% in 2016 from 3% in 2015, due to the protracted slump in global metal prices, falling remittances, and an unexpected cabinet reshuffle, all of which affected market sentiment. A 20% expansion in the non-resource tradable sectors failed to offset a double-digit contraction in construction and a substantial decline in agricultural output. Domestic demand weakened significantly. However, in January 2017, the economy was showing some signs of renewed dynamism, as the activity index grew by 6.5% year-on-year.

The fiscal deficit widened to 5.4% of GDP in 2016 from 4.8% in 2015, driven by expenditure overruns and weak revenue collection. The higher deficit brought public debt to 55.4% of GDP at end-2016, triggering the fiscal rule and consolidation at the beginning of 2017. Tax reforms have strengthened revenue performance; changes to the excise tax regime in January 2017 have more than doubled excise revenues, although the new Tax Code (approved in 2016) will fully take effect only in 2018.

In view of the weak economic activity, the central bank cut the policy rate gradually from over 10% in January 2016 to 6% in February 2017. However, the high levels of dollarization (63% of total loans and 66% of deposits) limit the effectiveness of the monetary stimulus. Weak domestic demand, a reduction in utility tariffs, a continued decline in import prices, and the appreciation of the dram caused a cumulative deflation of 1.4% between December 2015 and December 2016.

The financial sector remained stable throughout 2016. Enhanced bank capitalization standards (in line with Basel III) have been met by 17 banks (93% of total banking assets). Total credit to the private sector grew by 15% by December 2016 (y-o-y), while lending in domestic currency rose by 24%. However, the ratio of nonperforming loans (NPLs) rose to 10%. The current account deficit remained narrow at an estimated 2.4% of GDP in 2016, supported by a 20% increase in

exports coupled with anemic import demand. Remittances, after falling by 35% in 2015, dropped a further 10% in 2016. Declining wage and remittance income increased the poverty rate from 22.6% in 2015 to 23.9% in 2016.

Economic Outlook

Growth is projected to accelerate to 2.7% in 2017, reflecting the sustained expansion of the tradable sectors and a modest recovery in domestic consumption. Medium-term growth is projected to average 3% a year, given uncertainties in the external environment. The Government's planned expenditure restraint and full implementation of the Tax Code are expected to keep the fiscal deficit below 3% of GDP over the medium term.

Policy changes envisaged in the Tax Code would boost revenues by 2 percentage points of GDP by 2021. Future poverty reduction will hinge on the recovery of the domestic economy, labor market dynamics, and remittance inflows. Low growth rates, unfavorable external conditions, and limited fiscal space could slow the pace of poverty reduction; as a result, the poverty rate is projected to fall from 23.8% in 2017 to 22.2% in 2019.

Armenia's medium-term outlook remains sensitive to internal and external factors, which entail both upside and downside risks. Growth prospects depend on the Government's ability to speed up structural reform, challenged by parliamentary and presidential elections in April 2017 and May 2018. Domestic political pressures could compound the negative impact of external shocks.

Upside risks include a new Framework Agreement with the European Union (EU) and an increase in trade with Iran. The recent mandatory increase in capital-adequacy ratios is strengthening the financial sector, but the rise of NPLs poses new challenges. Specifically, poverty is projected to decline to 23.8% in 2018 from 25.2% in 2016.

Project Spotlight



Armenia is one of the most efficient agricultural producers in the Europe and Central Asia region.

During 2004–15, real agriculture labor productivity in Armenia increased by 120%, driven by higher agriculture productivity and a shift to higher value agriculture products. Agriculture also has a “level playing field,” as women currently account for 55% of all agricultural employment in Armenia.

Armenia benefited from early and bold reforms

related to land and water, as seen in the *Enabling the Business of Agriculture 2017* scores on land, where Armenia is ranked 7th out of 38 countries, and water, where it is 5th out of 62.

An important component of the good policy choices that drive the sector has been supported by the completed **Community Agriculture Resource Management and Competitiveness (CARMAC)** project and its successor **CARMAC 2**:

- 142,000 people, 13% of Armenia’s rural population residing in 81 pastoral communities, benefited from services provided by CARMAC’s pasture users cooperatives. Over 100 additional pastoral communities with 285,000 people (26% of the rural population) are being supported by CARMAC 2.
- Over the past five years, cash incomes of project beneficiaries increased 126% due to a 37% increase in cattle milk productivity and weight gains of 27%. Five veterinary service centers (VSCs) were built and the necessary equipment and training provided to private veterinarians. Four additional VSCs will be established by CARMAC 2.
- Over 15 years, new agriculture technologies and knowledge have been promoted through the establishment of and continuous assistance to 10 marz Agriculture Support Centers and the National Agriculture Support Center.
- A “one-stop-shop” Service Center on Food Safety provides support to a nucleus of small and medium-sized food processors and exporters to upgrade their food safety standards, with 29 enterprises already assisted.

Going forward, new and expanded areas of engagement in the sector will include support to further land reform, agriculture export promotion, and evidence-based agriculture policy making.



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