



IMF Activities in Armenia

Nienke Oomes

IMF Resident Representative in Armenia

www.imf.org/yerevan

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Outline

1. IMF lending to Armenia
2. IMF technical assistance to Armenia
3. Recent exchange rate developments



1. IMF lending to Armenia

- Since 1994, the IMF has lent about \$600 mln to Armenia
- Another \$300 mln is expected to be disbursed in the next two years
- The latest IMF program was approved by the IMF Board on March 6, 2009

New IMF Program for Armenia

- Stand-By Arrangement (SBA)
- \$540 million for 28 months
- First \$240 mln was disbursed immediately
- Remaining US\$300 will be disbursed in 8 quarterly installments, subject to meeting IMF conditionality
- Interest rate: first \$270 mln at 1.56%, second \$135 mln at 2.56%, third \$135 mln at 3.56%
- Grace period: 3 years
- Maturity: 5 years

Main measures under the IMF Stand-By Arrangement

- **Return to a flexible exchange rate regime**
- **Strengthening the financial sector to maintain stability**
- **Target a fiscal deficit of around 3 percent, while protecting social spending and public investment**
 - The program allows for an increase in social spending by 0.3 percent of GDP to protect the poor
 - If additional external financing becomes available, the program allows for a \$200 mln increase in public investment and SME lending, bringing the deficit to around 5 percent
- **Continued reforms in tax administration:**
 - No more delays in VAT refunds during 2009
 - Interest payments on late VAT refunds from 2010
 - No more ad hoc requests for advance tax payments



2. IMF Technical Assistance to Armenia

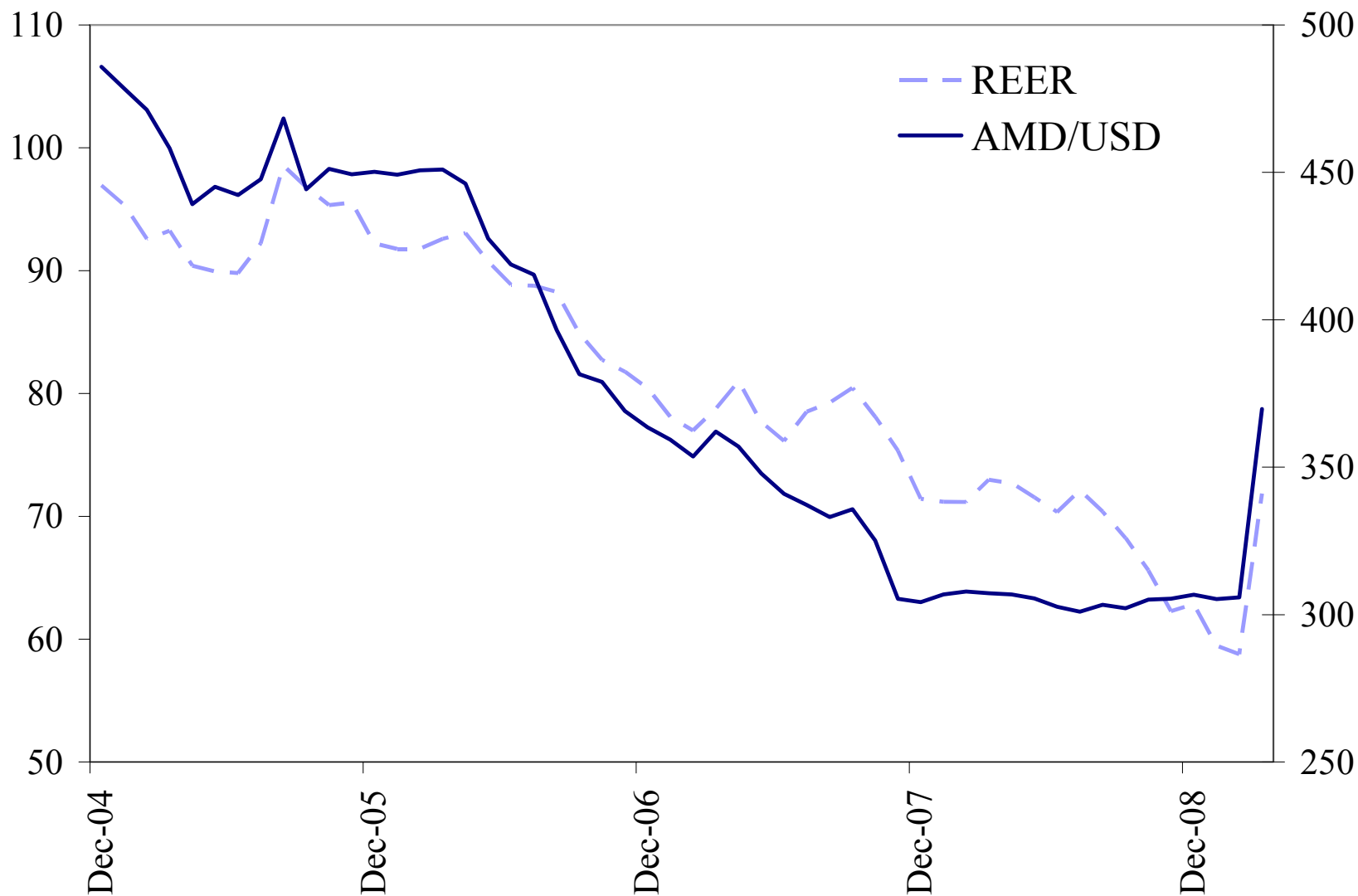
The IMF is providing technical assistance to Armenia in the following areas:

- Tax administration
- Unified tax code
- Monetary operations
- Exchange rate operations
- Inflation targeting
- Anti-money laundering
- Statistics

3. Recent exchange rate developments

- Armenia's real effective exchange rate had appreciated rapidly in recent years
- During 2005-2007, real appreciation was accompanied by nominal appreciation.
- This appreciation was mostly the result of large foreign exchange inflows (notably remittances and FDI) as well as high export prices (notably for copper and molybdenum).

Real and nominal exchange rate





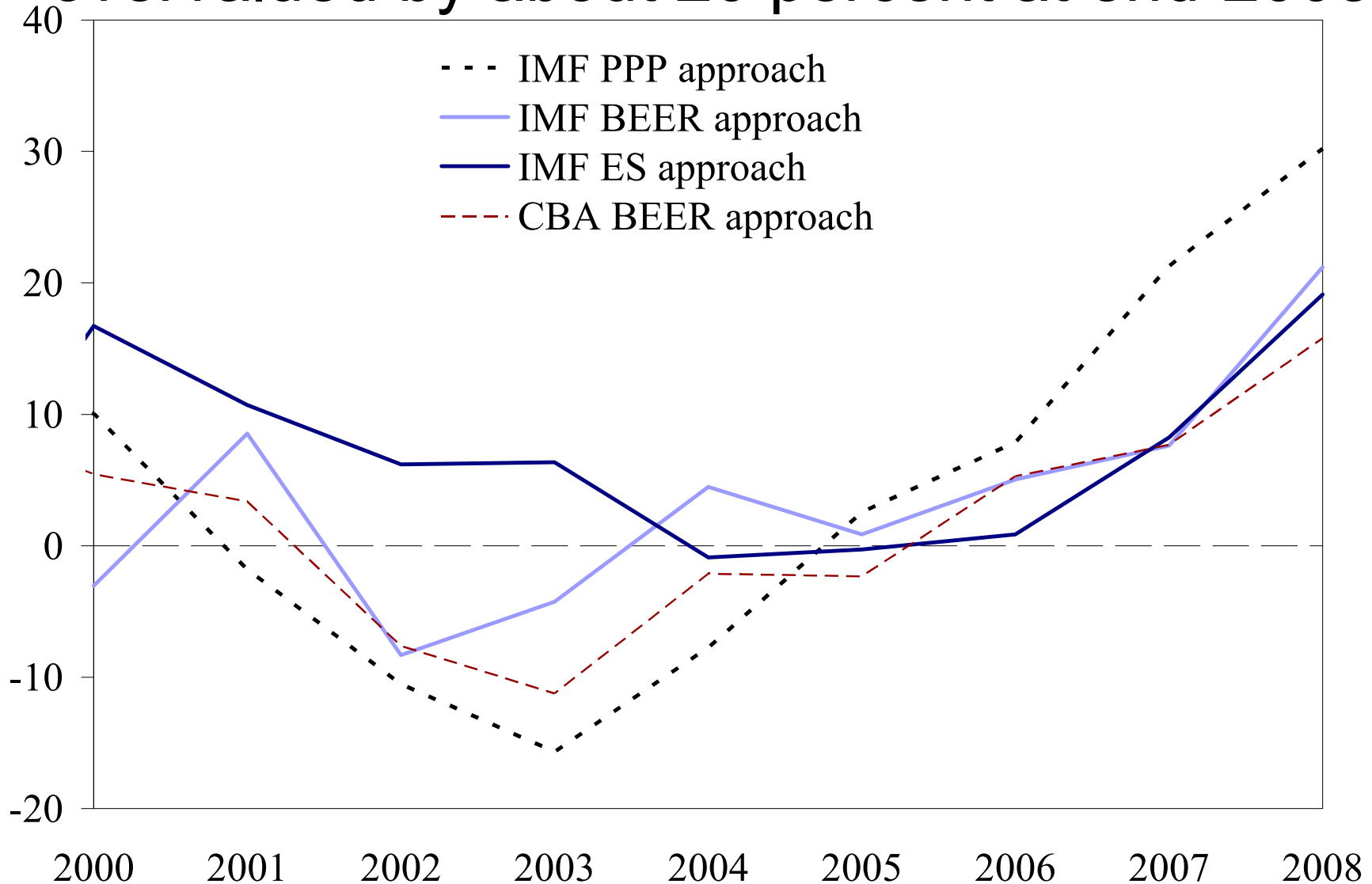
Recent exchange rate developments

- During 2008, the Central Bank of Armenia (CBA) kept the nominal AMD/USD rate within a very tight band.
- To do this, the CBA had to increasingly sell large amounts of dollars, especially in the last few months, which led to a significant loss in CBA reserves.
- This situation became unsustainable and the CBA announced on March 3, 2009 that it would return to a floating exchange rate regime
- As a result, the exchange rate immediately depreciated by about 20 percent

Why was dram depreciation necessary?

- Because of the global financial crisis, there has been a significant reduction of foreign currency inflows into Armenia.
 - Export prices have fallen significantly (copper and molybdenum prices lost about 2/3 of their value), leading to lower export revenues for exporters.
 - Global demand for Armenian exports has fallen, meaning a further reduction in export revenues.
 - The Russian economy is experiencing serious problems, meaning a reduction in remittances and foreign direct investment
- In addition:
 - The USD appreciated significantly against most other currencies
 - Many of Armenia's trade partners (e.g., Russia, Ukraine, Georgia) had already devalued against the dollar.

Our estimates confirm that the dram was overvalued by about 20 percent at end-2008.



But devaluation is not sufficient

- Now that the dram has depreciated by about 20 percent, the dram should be approximately in equilibrium
- However, having an equilibrium exchange rate alone is not sufficient.
- Competitiveness in Armenia should be improved further by implementing structural reforms aimed at
 - boosting productivity and innovation
 - increasing domestic competition
 - making tax and customs administration more transparent and fair
 - reducing corruption
 - improving the business environment more generally