Armenia: Country Profile

30 Oct 2009

The economy will experienced a sharp contraction in 2009 but a modest recovery is forecast in 2010. The fall in commodity prices has drastically reduced revenues from mining exports, a major source of income for the country. Russian firms control virtually all the country's energy sector and are establishing themselves in other areas. Approximately 70% of large enterprises and 80% of small enterprises have been privatised. The country's economic base is extremely narrow, limiting growth prospects.

ECONOMIC PERFORMANCE AND POLITICAL FRAMEWORK

Area

29,800 square kilometres

Currency

Dram (AMD = 100 luma)

Location

Geographically, the Republic of Armenia occupies the south-western sector of the land mass known as Transcaucasia and borders Turkey and Iran in the south. Politically it spans the gulf between the former Soviet Union and the Islamic states of the Middle East. Armenia was formed as a protective haven for members of the Armenian Church from all parts of the region. The capital is Yerevan.

Head of State

Serge Sargsyan (2008)

Head of Government

Tigran Sargsyan (2008)

Ruling Party

The government is formed by a three-party coalition.

Political Structure

Armenia declared its unilateral independence from the Soviet Union in 1991, a decision confirmed by a national referendum later that year when 94% voted in favour. Armenia's executive president is elected by popular vote and serves a four-year term. The National Assembly has 131 members, elected for a five-year term, with 41 members in single-seat constituencies and 90 chosen by proportional representation. The seats determined by proportional representation are distributed among those party lists which have received at least 5% of the total of the number of votes.

Last Elections

Presidential elections were held in February 2008. Sargsyan, the sitting prime minister, defeated Levon Ter-Petrosian, the country's first president. Sargsyan received almost 57% of the vote. The losers claimed voter fraud and western observers voiced concern about the process of vote counting. Elections to the National Assembly were held in May 2007. The Republican Party of Armenia took 64 seats, the Prosperous Armenia Party received 18 seats, the Armenian Revolutionary Federation won 16 seats and the centrist Rule of Law Party took 9 seats. The remaining seats went to smaller parties and non-partisans.

International Issues

Armenia's relations with Turkey are improving. In 2009, the two countries signed an agreement to open their borders and normalise relations. Armenia's dispute with neighbouring Azerbaijan over the sovereignty of Nagorno-Karabakh still lingers despite US efforts to ease tensions.

Economic Structure and Major Industries

Agriculture accounts for about one third of GDP. Cattle, sheep and pigs are the main forms of livestock. Traditionally, most operations in this sector have been under the control of the state but the number of privately-owned farms now exceeds that of state-run farms. Output rose by just 1.3% in 2008 owing to a poor harvest of wheat and other non-irrigated crops. Economists predict faster growth for 2009.

Industry accounts for a third of GDP. Approximately 70% of large enterprises and 80% of small enterprises have been privatised. Manufacturing growth slowed to just 2.4% in 2008, hampered by slumping foreign demand and weaker prices. Output of processing industries has also stagnated. The narrow manufacturing base is a serious barrier to growth. Several mines ceased operations in 2009 owing to the sharp drop in mineral prices on the world market.

Both services and construction have enjoyed strong rates of expansion, helping to drive the economy. Output of services rose by 9.0% in 2008 while construction grew by 7.3%. Growth in both industries is lower than in recent years, however. Financial reforms have strengthened the banking sector but the rapid growth of credit exposes banks to a number of risks.

Business Environment

Approximately 70% of large enterprises and 80% of small enterprises have been privatised. Armenia became a member of the WTO in 2003 and legislation to adhere to WTO rules was passed in 2004. The government is committed to additional reforms intended to reduce the costs of doing business and encourage more competition. Reforms in the tax regime and customs procedures are planned.

The energy sector is undergoing significant reforms, including the privatisation of two power plants. Collection rates in the energy sector have reached 100% and the sector is no longer receiving subsidies. The management of irrigation will be transferred to user associations over the medium term. Such a decentralised approach is expected to increase efficiency. The mining and metallurgy sectors are also undergoing restructuring.

The government has announced plans to provide liquidity support to troubled banks, encourage the restructuring of some and to strengthen bank supervision. Tax evasion is widespread. There is also a heavy reliance on indirect taxes. Foreign and joint-venture companies are the predominant tax payers while most large domestic companies manage to avoid taxes. Simplifications in the VAT regime will be introduced in 2009.

Table 1 Indicators of Business Environment: 2009

Indicator	2009
Business start-up	
Cost (% of GNI per capita)	4
Duration (days)	18
Dealing with construction permits	
Time (days)	116
Cost (% of GNI per capita)	28
Employing workers	
Rigidity of employment (index)	31
Ratio of minimum wage to average value added per worker	0.2
Redundancy costs (weeks of salary)	13
Tax rate	
Total tax rate (% profit)	36.2
Corporate tax rate ((% profit)	12.1
Labour tax and contributions (% of commercial profits)	23
Exporting	
Documents for export (no.)	5
Time to export (days)	17
Cost to export (US$ per container)	1,731
Importing	
Documents for import (no.)	7
Time for import (days)	20
Cost to import (US$ per container)	2,096
Protecting investors	
Investor protection index	5
Closing a Business	
Time (years)	1.9

Cost (% of estate)	4

Source: Euromonitor International based on the World Bank

Note: Figures for dealing with construction permits refer to the time and cost of building a warehouse, including licenses and permits. Rigidity of employment takes into account the difficulty of hiring, the rigidity of hours worked (scheduling of non-standard work hours and annual paid leave) and the difficulty of firing. The index ranges from 0 to 100 with higher values indicating a greater measure of rigidity. The redundancy cost indicator measures the cost of advance notice requirements, severance payments and penalties due when terminating a redundant worker, expressed in weeks of salary. If the redundancy cost adds up to 8 or fewer weeks of salary and the worker can benefit from unemployment protection, a score of 0 is assigned for the purposes of calculating the aggregate ease of doing business ranking. The cost of exporting and importing is recorded as the fees levied on a 20-foot container in United States dollars. All the fees associated with completing the procedures to export or import the goods are included. The total tax rate measures the amount of taxes payable by the business in the second year of operation, expressed as a share of commercial profits. The taxes included are profit or corporate income tax, social security contributions and other labour taxes paid by the employer, property taxes, turnover taxes and other small taxes (such as municipal fees and vehicle and fuel taxes). Data referring to labour taxes and contributions assumes the employee earns a salary plus benefits that are equal to the economy's average wage. The investor protection index takes into account the extent of disclosure, extent of director liability and the ability of shareholders to sue directors for misconduct. The index ranges from 0 to 10 with higher values indicating greater investor protection. The cost of the proceedings for closing up a business is recorded as a percentage of the estate's value. The cost is calculated on the basis of survey responses by insolvency practitioners and includes court fees as well as fees of insolvency practitioners, independent assessors, lawyers and accountants.

Energy Markets

Armenia has no proven oil reserves and is completely dependent on imports of refined products. Oil consumption fell by 90% in the first five years after independence and has remained stagnant since then. The Russian state-owned natural gas monopoly, Gazprom, has a long-term supply agreement with Armenia. Some analysts are concerned that the move leaves Armenia at a disadvantage in dealing with the Russian oil monopoly.

At present, natural gas accounts for at least half of domestic energy consumption. In order to diversify its natural gas supplies, Armenia is very interested in purchasing natural gas from Iran. In 2005, construction began on the Iranian portion of an Iranian-Armenian pipeline. Initially, Armenia will receive 38 billion cubic feet per year with plans to double the volume of imports by 2019. This is a significant pipeline because it allows Armenia to access Iran and Turkmenistan's gas exports without having to use Caspian Sea export routes. Nuclear power still accounts for 30% of total electricity generation and is produced at a potentially dangerous Soviet-era facility.

Overview of the Economy

Armenia's economy has performed very strongly since the turn of the century. Real GDP grew by more than 13% per year in 2003-2007 and per capita income in US dollars has tripled since 2000. Official figures indicate that unemployment fell to single digits during this period but survey results suggest the actual figure is much higher.

Growth has been driven by a combination of private consumption, inflows of FDI and remittances. All these sources are falling in 2009, however, as the global recession takes a toll. Improvements in the country's relations with its neighbours and greater stability at home promise more lasting benefits.

Most foreign investment has been channelled into construction and mining with public investment focused on improvements in infrastructure. Overall economic performance, however, is heavily dependent on conditions in Russia which is experiencing a sharp deceleration in growth.

ECONOMIC OUTLOOK

Key Points

- After recording one of the fastest rates of growth of all countries in the Commonwealth of Independent States during recent years, international economists a contraction of as much as 15.6% in 2009. A modest recovery is forecast in 2010.
- Investment inflows have dropped owing mainly to weaknesses in the Russian economy. In 2009, the IMF approved a loan of US$540 million to help the struggling economy.
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- Remittances are a major driver of private consumption. Russia is the source of more than three-quarters of all remittances and these are plummeting as the Russian economy weakens.
- Official figures indicate that unemployment is falling. However, survey results suggest the actual figure is 20-30%. Many of the country's younger and better educated workers have emigrated.

Economic Prospects

Since the global downturn began, the Armenian economy has worsened rapidly. The fall in commodity prices has drastically reduced revenues from mining exports, a major source of income for the country. International economists expect a contraction of as much as 15.6% in 2009. A modest recovery is expected in 2010 as export performance improves.

Investment inflows have dropped owing mainly to weaknesses in the Russian economy. Russia is also the source of more than three-quarters of Armenia's remittances and these are plummeting as the Russian economy has weakened. External debt rose by more than 14% in 2008, though the government's share in this total fell. In 2009, the IMF approved a loan of US$540 million to help the struggling economy.

The trade deficit will continue to be substantial because the economy depends so heavily on imports. The current account deficit is expected to rise to reach 13.7% of GDP in 2009, leaving Armenia especially vulnerable to external shocks. Donor assistance is expected to bridge this gap.

Political Stability and Risks

Although the economy has been strong, Armenia has not benefited from commensurate job creation or poverty reduction. The poverty rate has fallen below 27% and income inequality has been reduced.

The country's tax system is being improved but remains rudimentary and contributes to the low standard of living. The financial and judicial systems are even more underdeveloped and hinder progress. Human capital has deteriorated, in part through migration.

Moscow's influence in the economy is substantial. Russian firms control virtually all the country's energy sector and are establishing themselves in other areas.

Evaluation of Market Potential

The country's economic base is extremely narrow, hindering the realisation of sustainable rates of growth. A more diversified structure is also needed to alleviate Armenia's extensive dependence on imports. The government's plans to promote more development of the private sector are a partial response.

Prospects would be significantly better if an agreement to resolve the conflict with Azerbaijan over Nagorno-Karabakh was concluded. This would allow Armenia's closed borders with Azerbaijan and Turkey to reopen, a move that should significantly boost trade. The outlook is also contingent on the economic situation in Russia. Finally, the tax-to-GDP ratio at just 14.4% of GDP is lower than in most other CIS countries and falls short of the levels in higher-income transition economies.

Statistical Summary

	2004	2005	2006	2007	2008	2009
Inflation (% change)	7.0	0.6	2.9	4.4	8.9	3.4
Exchange rate (per US$)	533.45	457.69	416.04	342.08	305.97	363.27
Lending rate	18.6	18.0	16.5	17.5	17.0	18.8
GDP (% real growth)	10.5	13.9	13.2	13.7	6.8	-14.4
GDP (national currency millions)	1,907,945.0	2,242,880.0	2,656,190.0	3,149,280.0	3,646,110.0	3,165,537.1
GDP (US$ millions)	3,576.6	4,900.5	6,384.5	9,206.3	11,916.6	8,714.0
Population, mid-year ('000)	3,063.4	3,066.7	3,070.5	3,074.8	3,080.0	3,086.7
Birth rate (per '000)	14.4	14.7	14.9	15.1	15.3	15.4
Death rate (per '000)	8.4	8.5	8.6	8.6	8.7	8.8
No. of households ('000)	1,007.7	1,019.5	1,028.4	1,037.5	1,046.9	1,055.8
Total exports (US$ millions)	715.0	950.4	1,004.0	1,219.1	1,057.2	697.7
Total imports (US$ millions)	1,351.0	1,767.9	2,194.4	3,281.9	4,427.4	3,303.2
Tourism receipts (US$ millions)	171.0	220.0	271.0	305.0	382.0	400.2
Tourism spending (US$ millions)	179.0	236.0	286.0	294.0	333.8	380.3
Urban population ('000)	1,966.4	1,963.6	1,961.9	1,961.4	1,962.2	1,964.7
Urban population (%)	64.2	64.1	63.9	63.8	63.8	63.7
Population aged 0-14 (%)	22.6	21.9	21.4	20.9	20.5	20.3
Population aged 15-64 (%)	65.6	66.1	66.6	67.3	67.9	68.4
Population aged 65+ (%)	11.8	12.0	12.0	11.8	11.6	11.3
Male population (%)	46.8	46.7	46.7	46.6	46.6	46.6
Female population (%)	53.2	53.3	53.3	53.4	53.4	53.4
Life expectancy male (years)	68.1	68.2	68.3	68.4	68.5	68.6
Life expectancy female (years)	74.8	74.9	75.0	75.1	75.2	75.3

Infant mortality (deaths per '000 live births)	26.0	23.0	21.0	18.9	17.7	16.8
Adult literacy (%)	99.5	99.4	99.5	99.5	99.5	99.5

Imports and Exports

Major export destinations	2008 Share (%)	Major import sources	2008 Share (%)
Europe	65.9	Europe	46.2
Other countries	20.4	Other countries	21.4
North America	6.5	Asia Pacific	17.6
Africa and the Middle East	3.9	Africa and the Middle East	6.9
Asia-Pacific	2.1	North America	5.7
Latin America	1.1	Latin America	1.9

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