

Armenia: Time to Change the Pace

Armenia has made great progress since independence—thanks to the efforts of successive governments. Long gone are the days of severe energy shortages, high inflation and persistent economic contraction. Gone are the days when Armenians could not find what they needed in shops, or lost their savings in banks. Gone, too, are the recent days when some believed the global crisis would cripple Armenia's economy for years. Now, a new government is inheriting a growing economy that provides better-paying jobs, better infrastructure, and stable prices, a country with a wide variety of products and services, and a sound financial system for saving and borrowing.

Nevertheless, the new government will also face significant challenges, as unemployment, poverty, and emigration are still too high. Armenians are renowned as well-educated and entrepreneurial, and have done very well in other countries where they have emigrated. This success abroad raises a key question: what could be done better at home, so that more Armenians can do very well inside Armenia?

Armenia's isolated geographical situation represents a critical handicap, especially given the small domestic market. Overcoming this must be a priority. Geography can't be changed, but its effects can be mitigated: history has shown repeatedly that geography and geopolitics do not condemn countries to economic mediocrity. Armenia's isolation demands better policies: free trade agreements, infrastructure upgrades, an improved aviation framework, and further diplomatic efforts to establish ties with neighbors are all part of the needed mix.

Armenia has come a long way in carrying out reforms that other successful transition countries have undertaken. Inefficient state firms have long been privatized, guaranteeing better services and more reasonable prices. Costly and inefficient subsidies have been eliminated, and targeted protections for the most vulnerable put in place. Foreign trade has been liberalized: consumers have access to inexpensive and varied goods and services, and producers have access to materials for further processing and production in Armenia. Well-managed monetary policy has helped to keep inflation low. Fiscal policy has helped stabilize the economy when Armenia has confronted shocks, and public debt is sustainable. Pension reforms will support the dignity of old age in Armenia while reducing fiscal risks associated with pension spending. New legislation has helped to grow a functioning market economy.

However, the agenda is not yet finished. Further, ambitious measures are needed to support private investment as the primary engine of economic growth. In particular, more needs to be done to protect investors' rights to have a fair chance to earn

profits. It is still common for well-connected parties to have privileged market position, or for profits to be wrongfully lost. Until a more decisive approach and proper incentives for risk-taking are well established, there will not be enough investment, jobs, or hope in Armenia's future.

Also, the state needs to be more effective. It lacks sufficient resources to materially improve services like health, education, roads and energy generation. The government needs to do more to collect taxes: some, such as excises, are low by international comparison, and tax collections from some firms and sectors are also too low. The government also needs to do more to ensure that its spending is efficient, transparent, and gets to the right places. It also needs to continue to ensure that public resources are not used to rescue private firms that have been poorly managed.

A new government, with fresh political capital and a horizon free of elections, needs to take action to advance this agenda. We think the gradualist approach has run its course. Unless changes are deep and swift, the positive results that Armenians desire will also be gradual in coming, if they come at all. Decisive changes, made quickly and comprehensively, should persuade Armenians and others abroad that society rewards those who work hard, think big and take chances, not those whose best asset is a privileged connection. Armenian workers, managers, students and pensioners—all Armenians—should perceive that the game is fair, open and reaching for best solutions for ordinary Armenians; they should be able to trust that the state is a partner and not an adversary or a protector of vested interests.

Such dramatic changes don't come about as a result of passionate rhetoric, or of slow and incremental policy change; they require a transformational strategy with clear, irrevocable signs that some behaviors will not be welcome anymore in Armenian society. And they can unleash the Armenian people's full potential.

Armenia can shift gears and speed up the pace to a better future. The people are ready to fasten their seat belts. Now it's time for the government to act.

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