



## **PRESS STATEMENT**

IMF Resident Representative Office

Yerevan, Armenia

September 13, 2006

An IMF mission visited Yerevan from August 31 through September 13. The goals of the mission were to conduct the third review of Armenia's economic performance under its current Poverty Reduction and Growth Facility (PRGF) arrangement with the IMF, and to hold the Article IV consultation discussions.

### **Recent Economic Developments**

The IMF mission found that the Armenian economy has continued to perform very well. Real GDP grew by 11.6 percent in the first seven months of 2006, driven by strong growth in construction and services, which was financed in part by remittances and other foreign exchange inflows. These large inflows have given rise to both nominal exchange rate appreciation (of around 15 percent against the U.S. dollar since the beginning of the year) and inflation. In addition, inflation increased because of higher prices for energy, raw materials, and agricultural products (including higher world prices for sugar), and strong wage growth. The end-year inflation rate is now likely to be around 5 percent.

The IMF team was pleased to find that fiscal policy has remained sound thus far in 2006. The overall fiscal deficit for the first half of 2006 was smaller than initially foreseen, largely because of stronger revenue performance. Tax revenue grew by almost 20 percent during the first 8 months of 2006, relative to the same period in 2005. The IMF estimates that the government is on track to meet the overall fiscal deficit target of 2.3 percent of GDP for 2006.

### **Program Summary**

The IMF mission concluded that Armenia's PRGF-supported program continues to be on track. The government and the central bank implemented many significant measures under their program.

The IMF mission and the authorities agreed in principle on new economic program targets for 2007 and for the medium term. The targets for 2007 are 9 percent real GDP growth, 4 percent inflation, and an overall fiscal deficit of 2.4 percent of GDP.

Given Armenia's need to reduce poverty by means of social and physical infrastructure projects, the IMF mission agreed with the government that the fiscal deficit targets should be achieved mostly by raising tax revenues, rather than by cutting expenditures. The mission thus supports the government's plans to increase tax revenues by improving tax administration. Over the medium term the objectives are to continue with tax policy reforms that will reduce privileges and loopholes. In addition, the IMF mission agreed with the government that tax administration should continue to focus on improving tax audits, tax arrears collection, and the VAT refund system. These steps could improve the business climate, which is necessary to spur investment, and reduce the size of the shadow economy.

The mission believes that financial sector development is essential for sustaining strong economic growth. The economic program calls, therefore, for better enforcement of existing banking laws, and for measures to promote the development of the insurance and capital markets. Financial sector development, however, hinges on integrating the shadow economy into the official one.

Finally, the mission recognizes that real exchange rate appreciation, if it continues, may hurt the competitiveness of the economy. In order to reduce this risk, the IMF team recommends a more effective coordination between the monetary and fiscal authorities, as well as measures to increase competition and raise productivity in the Armenian economy.

## **BACKGROUND INFORMATION**

### **PRGF program**

The Poverty Reduction and Growth Facility (PRGF) is the IMF's concessional facility for low-income countries. PRGF-supported programs are based on country-owned poverty reduction strategies adopted in a participatory process involving civil society and development partners and articulated in the country's Poverty Reduction Strategy Paper. This is intended to ensure that PRGF-supported programs are consistent with a comprehensive framework for macroeconomic, structural, and social policies to foster growth and reduce poverty. PRGF loans carry an annual interest rate of 0.5 percent and are repayable over 10 years with a 5½ -year grace period on principal payments.

Armenia's economic program, which is supported by an IMF arrangement under the Poverty Reduction and Growth Facility, aims to achieve more broad-based growth and generate employment-creating economic activities in order to further reduce poverty. A main pillar of the reform program is to generate additional domestic resources, which would finance poverty-reducing and growth-enhancing expenditures as official assistance is likely to decline over time. Prudent monetary and fiscal policies aim at maintaining macroeconomic stability, while financial sector development and the improved governance envisaged by the program would support dynamic economic growth.

Armenia's request for a three-year PRGF arrangement of SDR 23 million (about US\$34 million) was approved by the IMF's Executive Board on May 25, 2005. Thus far, two of the six semi-annual reviews were completed. The equivalent of SDR 3.28 million (about US\$4.9 million) will be made available upon the completion of the third review.

### **New website**

The IMF has launched a new website for the IMF Resident Representative Office in Armenia, with the goal of making more information about IMF activities in Armenia available to the press and the public. The address of the website is [www.imf.org/yerevan](http://www.imf.org/yerevan).

### **New Resident Representative**

Since August 21, 2006, Ms. Nienke Oomes has replaced Mr. James McHugh as Resident Representative for the International Monetary Fund in Armenia.