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# Roaring Ahead : How Has Armenia Managed To Slash Its Poverty Rate And Become A Model For Other Developing Nations?

By S. Adam Cardais  
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To appreciate just how far Armenia has come in the last 15 years, it helps to imagine yourself living through an Armenian winter in the early 1990s.

It's the middle of January, it's five degrees below zero, and you and your family have only two hours of electricity a day - such was the abysmal state of the energy sector in a country crippled by the dissolution of the Soviet Union, a traumatic earthquake in 1988, and war with neighboring Azerbaijan.

But Armenia has been "radically transformed," in the words of one World Bank official, since its independence from the former Soviet Union. Today, the average Armenian has electricity around the clock.

An influx of cash and a series of reforms have taken Armenia from economic basket case, with GDP plummeting 50 percent between 1990 and 1993, to "Caucasian tiger," to quote a World Bank report issued earlier this year. It has become a model transition economy that should continue prospering with a second wave of reforms.

GDP has increased more than 10 percent a year for a decade largely thanks to robust investment in a booming construction industry by the Armenian diaspora in Europe and the United States. Sharp growth in the services sector, including the financial sphere, and retail trade are also contributors, according to the European Bank for Reconstruction and Development.

"Given the fact that it doesn't have natural resources, its growth is quite impressive," says Heike Harmgart, country economist for Armenia at the EBRD.

And the most laudable aspect of that growth, World Bank economist Aristomene Varoudakis says, is "that macroeconomic stability has been preserved. Inflation has remained low," between 3 percent and 4 percent. Last year was an exception to this trend, with inflation climbing to 5.6 percent, but the International Monetary Fund forecasts a fall to 4 percent in 2007.

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This fiscal discipline is an indication the government has backed up the bountiful diaspora remittances, which are more good fortune than anything else, with sound policy. Indeed, remittances alone don't make Armenia a model transition economy. A series of early, sustained governmental reforms enabled the country to capitalize on the cash inflow.

For instance, the government eliminated wage controls and privatized the majority of land and small businesses in the mid 1990s to encourage investment in construction and other sectors. The central bank has also been a key reformer, streamlining its operations and improving supervision over the banking industry to spur a dynamic financial services sector in a short period.

More recently, a new credit bureau to bolster small business lending and a modernized bankruptcy law have further improved the investment climate, two

reasons Armenia ranks 39th out of 178 economies in the World Bank's "Doing Business 2008" report.

On all of these reforms, Armenia has been wise to cooperate closely with international institutions such as The World Bank and the IMF.

"The Armenian government has been listening to institutions very well, which is positive," Harmgart says. "The government has always been open minded."

It would be hard to overstate the benefit this economic revolution has brought the population. According to the World Bank report, the poverty rate has fallen from more than 55 percent in the early 1990s to 30 percent. Extreme poverty had dropped to 5 percent two years ago.

#### GENTRIFYING NEIGHBORHOOD

The good news for the region is that Armenia's prosperity isn't unique. Georgia's economy is growing at just under 10 percent and is one of the leading reformers in the world, at No. 18 on the "Doing Business 2008" report. Azerbaijan posted a whopping 34.5 percent GDP growth in 2006 thanks to its thriving oil industry.

As in these countries, though, there's still a lot of progress to be made in Armenia. Tax evasion remains rampant. It's extremely costly for an individual or business to file taxes, and tax revenues are only 15 percent of GDP, one of the lowest rates in the region, resulting in less money for strengthening the economy or fighting poverty through spending on education or health care.

The government is trying to increase tax compliance by introducing a system that allows payers to submit their returns by post or electronically, publishing a list of the country's largest contributors in a sort of ego-driven motivator, and opening specialized collections units, but more progress is needed.

Corruption, though becoming less pronounced, is also a major concern, as is Armenia's over-reliance on the construction industry. Though analysts predict Armenia will sustain double-digit growth in the short and medium term, it has to begin diversifying its economy by making trade more dynamic and attracting new knowledge-based investments, such as IT companies.

Reforms in corporate transparency, competition, and education will be central to realizing this goal, but "these are more complex reforms than the first round," Varoudakis points out.

Armenia has without a doubt taken great strides, but nothing highlights progress like starting from nothing. If the country wants to remain a "Caucasian tiger," it had better prioritize these difficult reforms now.

These will take a lot longer than turning on the power.

S. Adam Cardais, a former business editor at The Prague Post, is a freelance journalist based in Berlin.

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