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# IMF Lends Armenia \$540 Million to Counter Crisis Impact

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Armenia hit by several large external shocks

Real growth to contract in 2009

Authorities to adopt measures to offset crisis impact, boost confidence, and help poor

The IMF has approved a \$540 million loan to Armenia to help the country in the southern Caucasus cope with the impact of the global economic and financial crisis.

Additional financing will be provided by Armenia's donors and international partners, including the World Bank.

The loan comes days after the Central Bank of Armenia announced it would return to a floating exchange rate regime, a move designed to improve the competitiveness of Armenian exports and help country better adjust to the worsening global environment. The Fund's approval of the 28-month Stand-By Arrangement enables Armenia to draw about \$240 million immediately.

'The Armenian authorities have put together a strong and credible economic program to address the deterioration in Armenia's external outlook, restore confidence in the currency and financial system, and protect the poor,' IMF Managing Director Dominique Strauss-Kahn said in a statement.

The IMF has lent more than \$50 billion so far to help countries cope with the fallout from the global crisis.

Rapid deterioration of outlook

Armenia, a country of about 3 million people that borders Iran and Turkey, had enjoyed several years of double-digit growth until as recently as 2007. Since the onset of the global crisis, however, the country has experienced a series of adverse shocks. Falling international commodity prices have adversely affected mining, a key export sector, leading to lower revenues for exporters and substantial job losses. With neighboring Russia experiencing serious economic difficulties, both remittances and foreign direct investment have also fallen.

In addition, market confidence in Armenia's currency and financial system had been weakening in recent months, with the result that capital outflows picked up. And economic activity has now slowed to the point that the country's real GDP growth is likely to be negative in 2009.

Restoring confidence

To put the economy back on track, the Armenian authorities have developed a policy package that aims to restore confidence in the currency and financial system. The program's key features include:

¢ Return to a flexible exchange rate regime. The Central Bank of Armenia announced on March 3 that it would no longer intervene in the market, except to smooth extreme volatility, and raised its policy interest rate by 100 basis points. Following the announcement, the dram (Armenia's currency)

depreciated about 20 percent, and since then, has broadly remained in that range. The flexible exchange rate will improve the competitiveness of Armenia's exports and help those who receive remittances from abroad.

¢ An increase in the refinancing rate. The move to increase the refinancing rate by 1 percentage point to 7.75 percent is designed to increase confidence, help reduce the inflationary pressures likely to result from the depreciation of the dram, and reduce incentives for banks to engage in speculative behavior.

¢ Supportive financial sector policies. The central bank has pledged to provide liquidity support to banks, address bank restructuring issues, if needed, and strengthen banking supervision.

¢ Prudent fiscal policy. The authorities plan to limit the deficit in 2009 to about 3 percent of GDP, although their program allows them to spend 'as external financing becomes available' up to an additional \$200 million, or 2 percent of GDP, on public investment and increased spending on small and medium-sized enterprises.

¢ Continued reforms in tax administration. The authorities plan to continue structural reforms to strengthen public finance management, in particular tax administration, and the financial sector.

¢ Targeted support for poor. The program foresees an increase in social spending of 0.3 percent of GDP relative to the budget, to protect the country's poor through well-targeted social safety nets.

#### Pressure on regional currencies

Armenia's decision to allow its currency to depreciate (a consequence of letting the market determine the dram's exchange rate) is not unique in the region. The Russian economy has been seriously affected by the sharp drop in oil prices, as a result of which the ruble has gradually lost 35 percent of its value. The large depreciation of the Russian ruble has put pressure on other regional currencies: Belarus and Kazakhstan have both devalued their currencies by 20 percent in recent weeks, and Georgia has devalued by 11 percent.

Armenia's loan provides exceptional access to IMF financing (amounting to 400 percent of the country's quota), in view of the large shocks the economy is experiencing. The authorities' strong policy measures 'justify the exceptional level of access to Fund resources and deserve the support of the international community,' Strauss-Kahn said.

<http://www.imf.org/external/pubs/ft/survey/so/2009/CAR030909B.htm>

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