**International Monetary Fund**

Republic of Armenia and the IMF

**Press Release**:
IMF Completes Second Review Under Stand-By Arrangement with Armenia, Approves Request for Waiver of Nonobservance of Performance Criterion, Modification of Performance Criteria, and Rephasing of Purchases
November 2, 2009

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# **Republic of Armenia:** Letter of Intent and Technical Memorandum of Understanding

October 14, 2009

**ARMENIA: LETTER OF INTENT**

October 14, 2009

Mr. Dominique Strauss-Kahn
Managing Director
International Monetary Fund
Washington, D.C. 20431

Dear Mr. Strauss-Kahn:

1. 2009 has been an extremely challenging year for Armenia. The sharp deterioration in the external outlook beginning in late 2008 led to a substantial weakening of the balance of payments, with pressures on the exchange rate and growing concerns about the financial system. While the return to the floating exchange rate in March 2009 has served the economy well by restoring confidence and reducing concerns about financial stability, the economic decline has deepened. Both the balance of payments and the public finances have likewise weakened further.

2. We have responded forcefully to the crisis, implementing macroeconomic policies and structural reforms aimed at mitigating its impact and setting the stage for a rebound. Timely support from the IMF has been an important element of our strategy, first with the approval of the Stand-By Arrangement in March of this year, followed by an augmentation of resources at the time of the First Review.

3. Program performance has been very strong (Tables 1 and 2). All quantitative performance criteria for end June were met, and all performance criteria for end-September for which data are available have also been met. Given that the final data are not yet available for the program fiscal balance at end-September, we are requesting a waiver of nonobservance for this performance criterion, which we expect to have missed by a small margin. In addition, all structural benchmarks for end-June and end-September were implemented.

4. This letter of intent outlines the policies we intend to pursue in the remainder of 2009 and in 2010 to achieve our program objectives, namely to help adjust to the worsened outlook, maintain confidence, and protect the poor. These policies supplement those outlined in the memoranda of economic and financial policies dated March 2, 2009 and June 5, 2009.

5. We welcome the Executive Board's decision to back the US$250 billion general SDR allocation. We intend to use our share of the allocation to bolster the CBA's international reserves.

## I. Recent Developments and Outlook for 2009-10

6. The contraction in economic activity in Armenia has deepened. Growth has fallen by more than 18 percent in the first seven months of 2009 driven by the collapse in the construction sector as remittances from abroad, notably Russia, slowed down. We anticipate some improvement in the economy by the end of 2009 with a pick up of activity in industry, as the mining sector benefits from the weaker exchange rate and rising metal prices, and the construction sector stabilizes. Nonetheless, real GDP is now projected to fall by around 15 percent in 2009. Inflation remains contained on the background of weak domestic demand, but could increase moderately in the coming months as international commodity prices strengthen. Falling exports on account of feeble external demand and significantly lower remittances have widened the current account deficit, despite the significant decline in imports.

7. We expect the economy to gradually recover during the next year, supported by a rebound in services, agriculture, and industry, particularly mining. However, prospects for recovery in Armenia will depend crucially on improvements in external conditions, and in particular on a turnaround in the Russian economy.

## II. Monetary, Exchange Rate, and Financial Policies

8. Our monetary policy continues to be underpinned by an inflation targeting framework. However, in the context of falling output and weak price pressures, the CBA's stance has so far continued to focus on easing credit conditions. Credit to the private sector has been declining since end-March, as borrowers wait for the economic uncertainty to clear and banks continue to keep tight lending criteria in light of the heightened credit risk. With price pressures still contained, the CBA can focus on overcoming the credit crunch consistent with the inflation target. In light of this, it has gradually lowered its policy rate to 5 percent in September, down from its peak of 7.75 percent in the aftermath of the return to the floating exchange rate regime. We expect credit to start rising again toward the end of the year as a result of the loose monetary conditions and of our various programs to support bank lending to the private sector. These include the CBA's foreign-financed on-lending window to finance SMEs through commercial banks and the mortgage refinancing facility offered by the newly-created mortgage operator.

9. We stand ready to adjust the monetary stance in line with inflation developments in the coming months. Besides the possible increase in international commodity prices, the abundant dram liquidity resulting from our expansionary policies could weaken the exchange rate and further add to price pressures. To preempt excessive liquidity buildup, the CBA has suspended the outright purchases of government securities, and is relying more on the available monetary operations instruments, including foreign exchange swaps. Without

undermining its overarching objective to stimulate economic activity, and market conditions permitting, the Ministry of Finance will increase its net T-bill issuance in coordination with the CBA. This will help absorb some of the excess liquidity, while allowing the government to refinance its debt at attractive interest rates. Proceeds from the issuance would be placed at the central bank at market interest rates.

10. We remain committed to the floating exchange rate regime and strive to promote increased exchange rate flexibility. In this context, the CBA will adhere to its internal guideline on foreign exchange intervention strategy introduced in June 2009. The strategy is designed to allow the exchange rate to move freely, with interventions limited to smoothing excessive exchange rate volatility and rebuilding reserves. The CBA will take particular care to avoid giving the market any perception, verbally or otherwise, of targeting a particular exchange rate level or band. In addition, to enhance transparency, the CBA will refrain from conducting foreign exchange intervention with counterparties other than foreign exchange market operators and government entities.

11. We continue to closely monitor the health of the financial sector and are ready to promptly take necessary actions to preserve financial stability. The latest stress tests show that the banking system remains sound with high capital and liquidity ratios, and is now less exposed to exchange rate risk. While non-performing loans have increased due to the economic crisis, banks are taking appropriate action by provisioning fully and by working with borrowers to restructure troubled but viable loans.

12. We will reduce banking sector vulnerabilities by imposing additional prudential measures, as appropriate. We intend to restrict banks' reliance on a single source of funding, and reinstate limits on net open foreign exchange positions to ensure proper exchange rate risk management. We are in close consultation with market participants to ensure proper design of these measures and maximize their effectiveness.

13. We have made good progress on strengthening financial safety net and crisis preparedness. The government has approved the changes proposed by the Deposit Guarantee Fund (DGF) to enhance its effectiveness (structural benchmark, end-June 2009) and submitted the relevant law amendments to parliament in September. The changes include doubling the coverage on both domestic and foreign currency deposits, reviewing the appropriate level of coverage every 5 years, and increasing the financial resources of the DGF with government back-up funding. The proposed doubling of coverage would bring the coverage level to approximately 2.5 times per capita GDP. To further enhance our crisis management capability, we will participate in a regional crisis simulation exercise as part of the crisis preparedness programs organized by the Toronto Centre, which will provide an opportunity to test the effectiveness of our existing policy tools and coordination and decision-making mechanism framework. We also expect to receive Fund technical assistance in this area starting in October.

14. The draft legislation on the recapitalization of the CBA with marketable interest-bearing securities was submitted to parliament (structural benchmark for end-September

2009). The MOF will gradually issue government bonds to recapitalize the CBA, and bond issuance would follow a clear schedule to enhance the credibility of this operation and support the financial strength and independence of the central bank. The issuance of these securities would also help the development of the local debt market.

## III. Fiscal Policy

15. A counter-cyclical fiscal policy remains appropriate for Armenia to minimize the impact of the global downturn on our economy. The government is implementing an expansionary strategy based on an increase in nominal spending compared to last year, despite the collapse in tax revenues under the impact of the crisis. This fiscal impulse goes beyond the effect of automatic stabilizers, as we are increasing capital expenditures and lending to SMEs and key enterprises compared to last year, while ringfencing social expenditures. In line with this stance, we will allow the fiscal deficit to rise up to 7.5 percent of GDP. Financing relies heavily on generous external financing from bilateral and multilateral partners, including the Fund.

16. However, we remain committed to a sustainable medium-term fiscal position. Because of the large external borrowing secured in 2009, the public-debt-to-GDP ratio is projected to more than double this year and to continue to rise in the coming years. While the public debt remains manageable, its rapid accumulation calls for undertaking strong fiscal consolidation as soon as possible. In addition, we intend to work with our development partners to obtain more favorable terms for new borrowing.

17. We will accordingly tighten fiscal policy starting next year. The 2010 budget that we will submit to parliament envisages a fiscal tightening of about 1½ percent of GDP as the economy is expected to rebound under the effect of this year's expansionary policies. The fiscal adjustment will hinge on increasing tax collection in line with the economic recovery and on containing expenditures, mainly capital spending, compared to this year's levels. We plan to finance the fiscal deficit from external sources—albeit to a lesser degree than in 2009—and a moderate increase in domestic debt. Should the economic crisis persist longer than anticipated, we stand ready to loosen our fiscal stance, provided that adequate domestic or external financing is available.

## IV. Fiscal Structural Reforms

18. We remain committed to our tax administration reform program based on a self-assessment model to enhance the business environment and ensure a sustainable revenue base. To this end, we have submitted to parliament draft legislation to strengthen penalties for false VAT refund claims and to pay interest on all late legitimate VAT refund claims (structural benchmark for end September 2009), and we have further decreased the stock of tax credits (indicative target). We have made progress in implementing reforms in other areas, including the introduction of e-filing of tax returns by December 2009 for large taxpayers, and over 2010-2011 for all other taxpayers; the improvement of analytical capacity of the tax services; and development of a plan for further strengthening the large

taxpayer inspectorate. In the remainder of 2009 and in 2010, we will continue to focus on addressing the systemic problems underlying tax credits, and ensuring the functionality of the risk-based audit system. We will also proceed with implementing a fully functional risk-based approach to VAT refund processing, a necessary condition for which is a change in legislation so to allow only high-risk VAT refunds to be subject to review (structural benchmark for end-March 2010). Finally, we will consider strengthening penalty regimes for all taxes by introducing graduated penalty rates, based upon the severity of the offence. Fund TA is helping us in all these efforts.

19. In the tax policy area, we are committed to abolishing presumptive taxation for fuel and tobacco products. To this effect, legislation will be submitted to parliament to bring all tobacco and petroleum products within the regular tax regimes (excise tax, customs duties, profit tax, and VAT), effective January 2011 (structural benchmark for end December 2009). To improve the effectiveness of social spending, the government is working with the World Bank to further strengthen the targeting of social safety nets (structural benchmark for end December 2009).

20. We also intend to strengthen our debt monitoring and planning capacity, notably regarding data on receipts and projections of foreign grants and loans. To this end, we will approve by end-March 2010 a time-bound action plan to strengthen our public debt management with the aim of developing a comprehensive medium-term debt strategy, preconditions for which are (a) the implementation of a public debt management information system; (b) the restructuring of the Public Debt Management Department (PDMD) of the Ministry of Finance along functional lines; and (c) the consolidation of public debt management within the PDMD. Timely delivery of technical assistance will be crucial to the successful implementation of this reform.

## V. Other Structural Reforms

21. We believe that deepening structural reforms will boost the productive capacity of the economy, help support the economic recovery, and promote long-term economic growth. These reforms include substantial investments in transportation infrastructure, information technology, and telecommunications, and a continued push to strengthen education services. Likewise, we are committed to maintaining an open trade regime. We are carrying out a number of initiatives to improve Armenia’s business environment, with a focus on improving the capacity of regulatory bodies and the ease of doing business. We also intend to continue our anti-corruption efforts, notably by enforcing the constitutional provisions restricting public officials from engaging in commercial activities.

## VI. Conclusion

22. We request the completion of the Second Review under the Stand-By Arrangement in light of the strong performance under the program and our continued commitment to strong policies. In addition, we request a waiver of nonobservance for the end-September performance criterion on the program fiscal balance, a target which we expect to have missed

by a small margin. Since this review combines what were the second and third reviews under the original schedule, we request that the amounts previously scheduled to be available following the second and third reviews become available upon completion of this review, and we intend to purchase the SDR37.72 million that will be available to us upon completion of this review. We will maintain the usual close policy dialogue with the Fund and stand ready to take additional measures, as appropriate, to ensure the achievement of the government's social and economic objectives under the Stand-By Arrangement. We will continue to consult with the Fund on the adoption of measures, and in advance of revisions to the policies contained in the LOI, in accordance with the Fund's policies on such consultation. We will also provide the Fund with the information it requests for monitoring progress during program implementation.

23. The program will continue to be monitored via quarterly performance criteria, indicative targets, and structural benchmarks. We request the modification of the performance criteria for end December 2009, the establishment of performance criteria for end March 2010, and indicative targets for the remainder of 2010 as specified in the attached Table 1. Given the expected deterioration in our debt outlook, we also request that the program include an indicative target on contracting or guaranteeing new nonconcessional debt by the public sector, which would help inform our policy decisions. We expect to complete the third review of the program on or after February 15, 2010, and the fourth review on or after May 14, 2010. The attached Technical Memorandum of Understanding updates definitions for the adjusters related to external financing to the public sector Structural benchmarks under the program are described in Table 2.

24. We authorize the IMF to publish this Letter of Intent and its attachments as well as the accompanying staff report.

Very truly yours,

/s/
Tigran Sargsyan
Prime Minister
Republic of Armenia

/s/
Tigran Davtyan
Minister of Finance
Republic of Armenia

/s/
Artur Javadyan
Chairman of the Central Bank
Republic of Armenia

Table 1. Armenia: Quantitative Targets, 2009-10 1/
(in billions of drams, at program exchange rates, unless otherwise specified)

| | 2008 | 2009 | | | | | | | | | | | 2010 2/ | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | Dec. | Mar. | | | Jun. | | | Sep. | | | Dec. | | Mar. | Jun. | Sep. | Dec. |
| | | Country Report No. 09/140 | Adj. Prog. | Prel. | Country Report No. 09/214 | Adj. Prog. | Prel. | Country Report No. 09/214 | Adj. Prog. | Prel. | Country Report No. 09/214 | Prog. | Prog. | Prog. | Prog. | Prog. |
| **Performance Criteria** | | | | | | | | | | | | | | | | |
| Net official international reserves (floor, in millions of dollars) | 1,056.6 | 455.9 | | 654.1 | 1,008.3 | 990.7 | 1,089.7 | 923.3 | 899.8 | 1,150.7 | 839.8 | 976.8 | 897.8 | 802.3 | 792.5 | 834.1 |
| Net domestic assets of the CBA (ceiling) | 75.3 | 148.9 | 143.6 | 32.3 | -117.8 | -27.5 | -115.9 | -60.0 | -50.7 | -97.3 | 24.5 | -11.4 | 31.2 | 73.0 | 79.1 | 84.4 |
| Net banking system credit to the government (ceiling) | -37.3 | -23.6 | | **-10.6** | -217.6 | -120.9 | -167.1 | -163.7 | -124.7 | -147.5 | -118.6 | -50.6 | 4.2 | 53.0 | 53.6 | 56.5 |
| Program fiscal balance (floor) 3/ | -73.0 | -31.9 | -29.9 | **-36.4** | -123.4 | | -87.4 | -212.3 | | -210.1 | -287.8 | -342.4 | -89.0 | -152.7 | -197.4 | -239.7 |
| External arrears (continuous criterion) | 0 | 0 | | 0 | 0 | | 0 | 0 | | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| **Indicative Targets** | | | | | | | | | | | | | | | | |
| Stock of tax credits (ceiling) 4/ | 154.4 | 154.4 | | 147.0 | 147.0 | | 134.9 | 145.0 | | 134.9 | 145.0 | 134.9 | … | … | … | … |
| Contracting or guaranteeing of new non-concessional debt (ceiling, in millions of dollars) 5/ | | | | | | | | | | | | 0 | 195.0 | 225.0 | 300.0 | 325.0 |

1/ All items as defined in the TMU. The figures in bold indicate when a target has not been met.
2/ Indicative targets for June, September, and December.
3/ Below-the-line overall balance excluding net lending.
4/ Indicative target up to end-December 2009.
5/ For 2009, cumulative beginning the second half and therefore excludes the Russian loan contracted in June 2009.

Table 2. Armenia: Proposed Structural Benchmarks for the Second, Third, and Fourth Reviews

| Item | Measure | Proposed Time Frame (End of Period) | Outcome |
| --- | --- | --- | --- |
| | Tax administration | | |
| 1 | Meet the statutory 90-day processing deadline for all VAT refund claims filed in 2009. | Continuous in 2009 | Met |
| 2 | Submit legislation to parliament to (a) strengthen penalties for overstated VAT refund claims effective January 2010, and (b) pay interest on all legitimate VAT refund claims filed after December 2009 and not refunded within 90 days, with interest to be paid out of VAT revenues. | September 2009 | Met |
| 3 | As a necessary condition for implementing a fully functional risk-based approach to VAT refund processing, submit legislation to parliament that allows only high-risk VAT refunds to be subject to review. | March 2010 | |
| | Tax and social policy | | |
| 4 | In close collaboration with the World Bank, develop a strategy to further strengthen the targeting of social safety nets. | December 2009 | |
| 5 | Submit legislation to parliament to bring petroleum and tobacco products within the regular tax regimes (excise tax, customs duties, profit tax, and VAT), effective January 2011. | December 2009 | |
| | Financial sector | | |
| 6 | Approve a plan to increase the resources of the Deposit Guarantee Fund. | June 2009 | Met |
| 7 | CBA to adopt a formal foreign exchange market intervention strategy consistent with IMF technical assistance. | June 2009 | Met |
| 8 | Start offering repo operations with a maturity of at least three months. | June 2009 | Met |
| 9 | Submit to parliament an amendment to Article 11 of the “Law on the Central Bank of the Republic of Armenia” to allow a gradual recapitalization of the CBA with marketable interest bearing securities. | September 2009 | Met |

## Armenia: Technical Memorandum of Understanding

This memorandum sets out the definitions for quantitative performance criteria, indicative targets, benchmarks, adjusters, as well as the reporting modalities referred to in the Letter of Intent, under which Armenia's performance under the program supported by the Stand-by Arrangement (SBA) will be assessed.

### I. Quantitative Targets

1. **The program targets a minimum level of net official international reserves (NIR) of the Central Bank of Armenia (CBA; performance criterion)**. The stock of such reserves will be calculated as the difference between total official gross international reserves (excluding reserve money denominated in foreign currencies) and official gross reserve liabilities. Total gross official international reserves are defined as the CBA's holdings of monetary gold (excluding amounts pledged as collateral or in swaps), holdings of Special Drawing Rights (SDRs), including the August 28, 2009 General allocation and the September 9, 2009 Special allocation, any reserve position in the IMF, and holdings of convertible currencies in cash or in nonresident financial institutions (deposits, securities, or other financial instruments). Gross reserves held in the form of securities and other financial instruments are marked to market. Gross reserves are reported separate from the balance on the government's Special Privatization Account (SPA) and the Millennium Challenge Account (MCA) and exclude capital subscriptions in foreign financial institutions and illiquid foreign assets. Official reserve liabilities shall be defined as the total outstanding liabilities of the government and the CBA to the IMF and convertible currency liabilities of the CBA to nonresidents with an original maturity of up to and including one year. NIR is monitored in U.S. dollars, and, for program monitoring purposes, assets and liabilities in currencies other than the U.S. dollar shall be converted into dollar-equivalent values using the exchange rates as specified in Table 1.

2. **The program targets a maximum level of net domestic assets (NDA) of the CBA (performance criterion).** For program purposes, NDA is defined as reserve money minus NIR, minus reserve money denominated in foreign currencies, plus medium- and long-term liabilities (i.e. liabilities with a maturity of one year or more) of the CBA, plus the balance of outstanding Fund purchases credited to the government account at the CBA. To evaluate program targets, the dram-equivalent values of NIR, medium- and long-term liabilities, and reserve money in U.S. dollar are calculated at the program exchange rate of dram 385 per U.S. dollar. The dram-equivalent value of reserve money in euro is calculated at the program exchange rate specified in Table 1. NDA is composed of net CBA credit to the general government; outstanding credit to domestic banks by the CBA (including overdrafts) minus liabilities not included in reserve money (exclusive of accrued interest), and other items net.

Reserve money is defined as the sum of currency issued, required and excess reserves, and current and time deposit accounts of certain resident agents.[1]

3. **The program targets a maximum level of net banking system credit to the government (performance criterion), defined as** the sum of net credit from the CBA and net credit from commercial banks to the central government.

- **The stock of net credit from the CBA to the government,** which includes the CBA's holdings of treasury bills and treasury bonds less all types of government deposits with the CBA (including the deposits in the Treasury Single Account, deposits of donor-financed project implementation units, the Lincy foundation, and balances of proceeds from the sale of humanitarian assistance). Treasury bonds are valued at the purchase price and excluding accrued interest, and treasury bills are valued at the purchase price plus the implicit accrued interest.

- **Net credit from commercial banks to the government** includes: (1) gross commercial bank credit to the central government less government deposits with commercial banks (including the counterpart funds of certain government on lending to the economy financed by the Lincy Foundation and the World Bank); and (2) bank holdings of treasury bonds (valued at the purchase price and excluding accrued interest) and treasury bills (valued at the purchase price plus the implicit accrued interest).

4. **The program imposes a zero ceiling on external payment arrears (continuous performance criterion)** defined as all unpaid debt-service obligations (i.e., payments of principal and interest) arising in respect of public sector loans contracted or guaranteed including unpaid penalties or interest charges associated with these obligations that are overdue beyond 30 days after the due date.[2]

5. **The program targets a minimum level of the program fiscal balance (performance criterion).** The fiscal balance is measured as the negative of the sum of net domestic banking system credit to the government, domestic nonbank net financing, and external net financing to the government. Should a general subsidy be introduced off-budget, the overall balance will be measured including the subsidy as part of government spending.

- **Net banking system credit to the government** equals the change during the period of net credit to the government.

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[1] Liquidity absorbing transactions under reverse repurchase agreements, the CBA's deposit facility, foreign currency swaps, and securities issued by the CBA are excluded from the reserve money definition.

[2] The public sector is defined following the *Government Financial Statistics Manual* (GFS 2001) and *System of National Accounts* (1993 SNA). It includes the general government and nonfinancial public enterprises.

- **Nonbank net financing** equals the sum of: (1) the change during the period of outstanding treasury bills and bonds to nonbanks (including accrued interest for treasury bills and excluding accrued interest for treasury bonds);[3] (2) any other disbursement or transaction that increases nonbanks' claims on the central government plus withdrawals from the special privatization account or the treasury sub-account containing privatization proceeds in dram, less amortizations made by the central government to private resident nonbank agents.

- **External net financing** equals total debt-increasing disbursements from non-residents to the central government (including Fund net purchases credited directly to the government accounts at the CBA) less total amortizations from the central government to non-residents. All foreign-currency denominated transactions are recorded in drams using the prevailing exchange rate at the time of the transaction.

6. The project implementation units, which carry out projects financed by the US-based Lincy Foundation, maintain accounts at the CBA. These grants are recorded in the fiscal accounts as external grants on the revenue side and as foreign-financed capital expenditure on the expenditure side. In addition, any loans extended by the U.S.-based Lincy foundation to finance investments and that are intermediated through the banking system are recorded in the financial accounts as a financing item below the line and are thus excluded from net lending.

7. Foreign currency proceeds from selling enterprises are deposited into the Special Privatization Account (SPA). The account is held at the CBA and the proceeds are invested abroad together with the CBA's international reserves. These proceeds are included in the definition of the monetary accounts of the CBA as part of net foreign assets with a counter entry in other items net. Any budgeted withdrawal from the SPA will be accounted for as privatization proceeds used to finance the budget and will be recorded below the line. Any unanticipated withdrawal from the SPA will be recorded below the line as privatization receipts; these withdrawals, however, will be replenished during the same fiscal year. Domestic currency proceeds from selling enterprises to residents are deposited in a sub-account of the treasury single account.

8. **The program targets a maximum level of stock of tax credits (indicative target)** defined as the sum of outstanding accumulated credit by the State Revenue Committee (SRC) of all types of tax revenues (VAT, profit tax, excises, income tax, presumptive payments, and others) resulting from advanced tax payments to be offset against future tax liabilities.

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[3] Domestic nonbank holdings of treasury bills and treasury bonds are defined as total outstanding treasury bills and bonds less holdings by the banking system and the State Fund for Social Insurance.

9. **The program sets a maximum on contracting or guaranteeing of new nonconcessional external debt by the public sector (indicative target).** The definition of debt, for the purposes of the program, is set out in Executive Board Decision No. 12274, Point 9, as revised on August 24, 2000. For program purposes, nonconcessional external loans are defined as loans from lenders other than the IMF with a grant element of less than 35 percent of the value of the loan. The grant element is to be calculated as follows: the grant element of a debt is the difference between the net present value (NPV) of debt and its nominal value, expressed as a percentage of the nominal value of the debt. The NPV of debt at the time of its contracting is calculated by discounting the future stream of payments of debt service due on this debt. The discount rates used for this purpose are the currency specific commercial interest reference rates (CIRRs), published by the Organization for Economic Cooperation Development (OECD). For debt with a maturity of at least 15 years, the ten-year-average CIRR will be used to calculate the NPV of debt and, hence, its grant element. For debt with a maturity of less than 15 years, the six month average CIRR will be used. To both the ten-year and six-month averages, the same margins for differing repayment periods as those used by the OECD would continue to be added (0.75 percent for repayment periods of less than 15 years, 1 percent for 15 to 19 years, 1.15 percent for 20 to 29 years, and 1.25 percent for 30 years or more). Loans provided by a private entity will not be considered concessional unless accompanied by a grant or grant element provided by a foreign official entity, such as both components constitute an integrated financing package with a combined grant element equal to at least 35 percent. Previously contracted nonconcessional external debt that has been rescheduled will be excluded from the definition of "new debt" for the purposes of this performance criterion.

## II. Adjusters

10. The quantitative performance criteria and indicative targets under the program are subject to the following adjusters, calculated, where relevant, using program exchange rates:

- **Changes in reserve requirements**: The ceiling on the NDA of the CBA will be adjusted downward (upward) by the amount of banks' reserves freed (seized) by any reduction (increase) of the reserve requirement ratio on both domestic currency and foreign currency deposits relative to the baseline assumption as per the following formula: $\Delta NDA = \Delta rB$, where B denotes the level of the reservable deposits in the initial definition and $\Delta r$ is the change in the reserve requirement ratio.

- **KfW and World Bank loan disbursements**: the ceiling on the NDA of the CBA will be adjusted upward (downward) by the full amount of any excess (shortfall) of disbursements from the KfW and World Bank loans directed at SME financing compared to programmed amounts (Table 2). The floor on NIR will be adjusted upward (downward) by the cumulative amount of any excess (shortfall) of these disbursements compared to program amounts.

- **External financing to the public sector**, defined as disbursements of loans from bilateral and multilateral agencies for budget, project support, and the $500 million Russian loan disbursed in 2009 (including Fund purchases credited directly to the government accounts at the CBA), with the exception of the KfW and World Bank disbursements mentioned above:

    - The floor on NIR will be adjusted upward (downward) by the cumulative amount of any excess (shortfall) of external financing in the form of budget support (excluding Fund disbursements to the government) compared to program amounts (Table 3).

    - The ceiling on NDA will be adjusted upward by the amount of any shortfall of external financing in the form of budget support compared to program amounts.

    - The ceiling on net banking sector credit to government will be adjusted upward by the cumulative amount of any shortfall of total external financing compared to programmed amounts (Table 3).

    - The floor on the program fiscal balance on a cash basis will be adjusted downward by the cumulative amount of any excess of total external financing compared to programmed amounts (Table 3).

- **Recapitalization of the CBA**: the ceiling on net credit of the banking system to the government will be adjusted upward by the full amount of the recapitalization of the CBA.

## III. Data Reporting

The government will provide the IMF the information specified in the following table.

| Reporting Agency | Type of Data | Description of Data | Frequency | Timing |
|---|---|---|---|---|
| CBA[4] | CBA balance sheet | Summary | Daily | The following working day |
| | CBA balance sheet | Summary at program exchange rates; and by chart of accounts at actual official exchange rates | Monthly | Within seven days of the end of each month |
| | Monetary survey | Summary banking system balance sheet for the central bank at both program exchange rates and by chart of accounts at actual official exchange rates; the consolidated balance sheet of commercial banks by chart of accounts at actual official exchange rates | Monthly | Within 25 days of the end of each month |
| | International reserves | By chart of accounts; at (i) program exchange rates; and (ii) at actual official exchange rates | Daily | The following working day |
| | Foreign exchange market | Official exchange rates (buying and selling); daily trade volume, and weighted average exchange rate of the interbank, intrabank and Nasdaq-OMX | Daily | Within 1 day |
| | Foreign exchange market | CBA foreign exchange operations, (exchange rate, volume, counterpart) | Daily | Within 1 day |
| | Foreign exchange market | Exchange rate (buying and selling) | Daily | Within 1 day |
| | Interest rates | Refinance rate | At least monthly | Within 1 days of the CBA Board decision |
| | Interbank money market | Daily interbank repo volume and interest rate and number of trades | Daily | Within 1 day |
| | CBA operations | Repo (reverse repo) operations, open market operations, Lombard credits, deposit facility, and foreign exchange swaps (volumes, maturity, yields, exchange rates) | Daily | Within 1 day |
| | Bank liquidity | Reserves and excess reserves, by currency | Monthly | Within 15 days of the end of each reference period |

[4] As defined in CBA resolution No. 201 (December 6, 1999).

| | | | | |
|---|---|---|---|---|
| | Interest rates and flows of the funds attracted and allocated by commercial banks | By currency and maturity | Weekly | Last working day of the week |
| | T-bill and coupon bond financing, CBA securities | Auction data: date, original and remaining maturities, issuance volume, allocation, average yield and coupon yield (if available) | Weekly | Last working day of the week |
| | Banking data | Sectoral distribution of loans and deposits; dollarization of loans and deposits; loan maturities; interbank rate, by volume and maturity; T-bill rate, bond yield; deposit and lending rates, by maturity; monthly weighted average interest rate on government bonds | Monthly | Within 25 days of the end of each month |
| | Banking indicators | Capital adequacy; asset composition and quality; profitability; liquidity; open FX positions; and compliance with prudential norms | Monthly | Within 30 days of the end of each month |
| | Banking sector stress tests | Results of stress tests on exchange rate, liquidity, and credit risk | Monthly | Within 30 days of the end of each month |
| | CPI | Index of core inflation | Monthly | Within 21 days of the end of each month |
| | Transfers | Non-commercial transfers of individuals | Monthly | Within 30 of the end of each month |
| | Other monetary data | IFS format | Monthly | Within 45 days of the end of each month |
| Ministry of Finance (MOF) | T-bill and coupon bond financing | By holders, i.e., CBA, resident banks, resident nonbanks, and nonresidents | Monthly | Within 7 days of each month |
| | External debt | Disbursements and stock of outstanding short-term and contracting or guaranteeing and outstanding stock of medium-and long-term external debt of the government, the CBA, and state-owned companies (by company); any stock of arrears on external debt service and outstanding stock of government guarantees and external arrears | Monthly | Within 21 days of the end of each month (preliminary data ) and within 45 days of the end of each month (final data) |
| | Revenue collection | Total revenue collected separately by the tax administration and customs administration, including revenue by individual tax, and social contributions | Monthly | Within 7 days of the end of each month |
| | Expenditure arrears | Government | Monthly | Within 45 days of the end of each month for government arrears |

| | | | | |
|---|---|---|---|---|
| | Privatization receipts | Balance on the SPA; gross inflows into and outflows from the SPA during the month, specifying the nature of each transaction | Monthly | Within 7 days of the end of each month |
| | Treasury single account (TSA) | Detailed breakdown of central treasury account, including deposits at the central treasury, community budgets, off budget account, monetization account, state budget account and the Republic correspondent account—flows during the month and end of month stocks. | Monthly | Within 7 days of the end of each month |
| | Consolidated central government | State budget | Monthly | Within 30 days of the end of each month |
| | Consolidated general government | Central and local governments, and Non-Commercial Enterprises that belong within the general government (NCEs) | Quarterly | Within 60 days of the end of each quarter |
| | Consolidated general government | Central and local governments, and NCEs that belong within the general government | Annual | Within 180 days of the end of each year |
| | Budget execution | All cash receipts, cash expenditures, including domestic and external debt-service payments, external and domestic borrowing operations, and inflow of grants to the central government; expenditure data will be provided according to both economic and functional classifications, consistent with the GFSM2001 methodology | Monthly | Within one month following the end of each quarter. |
| NSS | Balance of payments | Detailed export and import data | Monthly | Within 28 days of the end of each month |
| | | Detailed export and import data | Quarterly | Within 45 days of the end of each quarter |
| | | Detailed balance of payments data | quarterly | Within 60 days of the end of each quarter |
| | CPI | By category | Monthly | Within 5 days of the end of each month |
| State Revenue Committee | Tax arrears | By type of tax | Monthly | Within 30 days of the end of each quarter (monthly data provided on a quarterly basis) |

| | | | | |
|---|---|---|---|---|
| | | For or the 30 largest debtors and for all major companies in the energy, water, and irrigation sectors | Quarterly | Within 30 days of the end of each quarter |
| | Tax credits | Detailed data, by type of tax, of outstanding tax credits for all types of tax revenues | Monthly | Within 45 days of the end of each month (monthly data provided on a quarterly basis) |
| | VAT refund claims in arrears | Detailed data on VAT refunds in arrears which include all outstanding VAT refunds that have not been accepted (and refunded), or offset (in full or in part), or rejected (in full or in part) after the 90 day statutory processing period. Number of refund applications processed per month. | Monthly | Within 45 days of the end of each month (monthly data provided on a quarterly basis) |
| | Import data | 1. Total value of recorded imports, breaking out raw diamond imports;<br>2. Total value of non-duty free recorded imports;<br>3. Number of total transactions involving recorded imports;<br>4. Number of total transactions involving non-duty free recorded imports<br>5. Value of recorded imports where customs value was assessed using transaction prices, breaking out raw diamond imports;<br>6. Value of non-duty free recorded imports where customs value was assessed using transaction prices;<br>7. Number of transactions involving recorded imports where customs value was assessed using transaction prices;<br>8. Number of transactions involving non duty free recorded imports where customs value was assessed using transaction prices | Quarterly | Within 30 days of the end of each quarter |

Table 1. Armenia: (Program) Exchange Rates of the CBA
(As of December 31, 2008 for dollars per currency rates)

| Country | Drams Per Currency | Dollars Per Currency |
|---|---|---|
| Australian dollar | 266.57 | 0.6924 |
| Canadian dollar | 313.39 | 0.8140 |
| Swiss franc | 365.58 | 0.9496 |
| Danish krone | 73.26 | 0.1903 |
| Euro | 546.00 | 1.4182 |
| Pound sterling | 558.68 | 1.4511 |
| Japanese yen | 4.27 | 0.0111 |
| Norwegian krone | 55.20 | 0.1434 |
| Russian ruble | 13.13 | 0.0341 |
| Swedish krone | 18.21 | 0.0473 |
| U.S. dollar | [...] | 1.0000 |
| SDR | 593.00 | 1.5403 |

Table 2. Armenia: KfW and IBRD SME Loan Disbursements, 2009–10 1/
(in millions of USD)

| March-09 | | June-09 | | September-09 | December-09 | March-10 |
|---|---|---|---|---|---|---|
| Prog | Actual | Prog | Actual | Prog | Prog | Prog |
| 2.39 | 5.48 | 2.39 | 31.90 | 33.63 | 35.63 | 2.00 |

1/ Cumulative from the end of the previous year.

Table 3. Armenia: External Financing to the Public Sector,
2009-10 (program) 1/
(in billions of drams)

| | March-09 | | June-09 | | September-09 | December-09 | Mar-10 |
|---|---|---|---|---|---|---|---|
| | Prog | Actual | Prog | Actual | Prog | Prog | Prog |
| Project financing | 14.72 | 12.20 | 50.82 | 33.01 | 81.21 | 62.69 | 18.18 |
| Budget Financing | 3.09 | - | 78.93 | - | 97.34 | 111.28 | 17.63 |
| Russia | - | - | 192.50 | 185.09 | 192.50 | 192.50 | - |
| **Total** | **17.81** | **12.20** | **322.25** | **218.09** | **371.05** | **366.47** | **35.81** |

1/ Cumulative from the end of the previous year, at program exchange rates, excluding grants.

## IV. Guidelines on the Indicative benchmark with Respect to Foreign Debt

Excerpt from Executive Board Decision No. 12274, as revised on August 24, 2000.

9. (a) For the purpose of this guideline, the term “debt” will be understood to mean a current, i.e., not contingent, liability, created under a contractual arrangement through the provision of value in the form of assets (including currency) or services, and which requires the obligor to make one or more payments in the form of assets (including currency) or services, at some future point(s) in time; these payments will discharge the principal and/or interest liabilities incurred under the contract. Debts can take a number of forms, the primary ones being as follows:

    (i) loans, that is, advances of money to obligor by the lender made on the basis of an undertaking that the obligor will repay the funds in the future (including deposits, bonds, debentures, commercial loans, and buyers’ credits) and temporary exchanges of assets that are equivalent to fully collateralized loans under which the obligor is required to repay the funds, and usually pay interest, by repurchasing the collateral from the buyer in the future (such as repurchase agreements and official swap arrangements);

    (ii) suppliers’ credits, that is, contracts where the supplier permits the obligor to defer payments until some time after the date on which the goods are delivered or services are provided; and

    (iii) leases, that is, arrangements under which property is provided which the lessee has the right to use for one or more specified period(s) of time that are usually shorter than the total expected service life of the property, while the lessor retains the title to the property. For the purpose of the guideline, the debt is the present value (at the inception of the lease) of all lease payments expected to be made during the period of the agreement excluding those payments that cover the operation, repair or maintenance of the property.

   (b) Under the definition of debt set out in point 9 (a) above, arrears, penalties, and judicially awarded damages arising from the failure to make payment under a contractual obligation that constitutes debt are debt. Failure to make payment on an obligation that is not considered debt under this definition (for example, payment on delivery) will not give rise to debt.