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

May 30, 2011

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REPUBLIC OF ARMENIA: LETTER OF INTENT

The Acting Managing Director   Yerevan, May 30, 2011
International Monetary Fund
Washington, D.C. 20431

Dear Acting Managing Director:

1. **Armenia continues its path of recovery and stabilization in spite of the emergence of fresh challenges.** Most sectors of the economy grew in 2010, with public finances improving considerably. The financial sector is expanding rapidly and continues to be well capitalized. However, agriculture sector developments locally and internationally have hampered economic growth and fueled inflation. In this context, our longer-term challenges regarding structural rigidities and social protection and development have become all the more critical.

2. **Performance under our program supported by arrangements under the Extended Fund and Extended Credit facilities (EFF/ECF) has been very strong**. The program is on track with all continuous and periodic quantitative performance criteria and indicative targets for end-December 2010 as well as all indicative targets for end-March 2011 observed. The structural benchmarks were also met.

3. **This Letter of Intent (LOI) describes policies we intend to implement for the remainder of 2011.** Our near-term macroeconomic policies will continue to be geared towards containing macroeconomic pressures while avoiding major disruptions to the still fragile recovery. We remain committed to our reform program aimed at economic growth and poverty reduction, fiscal and debt sustainability, and developing a sound financial system.

I. RECENT DEVELOPMENTS AND OUTLOOK

4. **The economic recovery has been relatively weak and uneven across sectors, with headline inflation reaching exceptional levels.** In 2010, mining, industry, trade, and transportation grew strongly, supported by a recovery of external and domestic demand and increased financial intermediation. In contrast, agricultural production dropped sharply due to unfavorable weather conditions and underlying structural weaknesses in the sector. This resulted in weaker-than-expected overall GDP growth. Consumer prices increased to 11.5 percent in March, mainly driven by a surge in food prices, attributable both to domestic supply constraints and high global food prices, with some initial signs of second-round effects also observed. The fiscal deficit has narrowed considerably, due to expenditure restraint in spite of higher prices. Both trade and remittance inflows have rebounded, but the current account deficit remains high. Banks

remain well capitalized and liquid, and credit to the economy is booming, notably in foreign currency.

5. **The economy is set to recover at a faster pace in 2011, with the pickup driven mostly by a recovery in agricultural production.** High oil prices will likely increase remittances from Russia. We expect agricultural production to recover strongly at around 9–10 percent, on the back of improved weather conditions and measures taken by the government to support the agricultural sector. However, growth in other sectors is expected to remain moderate, particularly in construction, a key pre-crisis growth driver, with overall GDP projected to grow by around 4.6 percent.

6. **The medium-term outlook will continue to be challenging, as external demand and remittances are likely to recover only gradually, while FDI and private investment remain weak**. GDP growth is expected to be around 4−4½ percent over 2012−13. Barring further shocks, inflation is expected to revert to the CBA's target band of 4 ± 1½ percent during the first half of 2012. Public debt is also expected to fall to around 41 percent of GDP by 2013 under the medium-term expenditure framework. On the basis of structural reforms, fiscal consolidation, and inflation reduction, the current account deficit is expected to be reduced considerably.

II. The Program for 2011

A. Fiscal Policy and Debt Sustainability

7. **We continue to focus on reducing the deficit to help ease inflationary pressures, address external imbalances, and ensure fiscal and debt sustainability.** In 2010, we were able to reduce our deficit by nearly 3 percentage points of GDP to just under 5 percent. Building on this success, we will further reduce the deficit to 3.9 percent of GDP in 2011, and we expect a deficit of 3.2 percent of GDP in 2012. We will continue down this consolidation path and project to reach a deficit target of 2.4 percent of GDP by the end of our program. Our goal of improving the revenue-to-GDP ratio by 0.4 percentage points per annum remains, as does our commitment to save at least half of tax revenue overperformance relative to EFF/ECF projections. As in the past, we will continue to prioritize fiscal consolidation, adjusting spending as needed, informed by the ongoing Public Expenditure Review.

8. **We will implement a further set of measures to increase our low tax-to-GDP ratio.** The centerpiece is to phase in an increase in excise taxes over four years from 2012. Since 2002, excise tax yields have been substantially eroded—by 2 percentage points of GDP—by the effects of inflation on unadjusted tax rates. At the same time, we will introduce legislative changes to automatically update specific tax rates in response to annual inflation beginning in 2012 (Structural benchmark, August 2011). Further, to strengthen collections from property taxes, we will work to align cadastre values with recent property sales. This will involve, among other actions, providing cadastral

passports for older buildings and ensuring consistent recording of all property sales with the State Committee of the Real Property Cadastre. We will adjust the specific tax on cars annually for inflation, and further revise upwards the rates on luxury and sport utility vehicles for 2012 (Structural benchmark, December 2011). More broadly, we are at the beginning stages of developing a detailed strategy paper on a broader tax reform plan (Structural benchmark, December 2011). The strategy will build on recent technical assistance received from the Fund.

B. Monetary and Exchange Rate Policy

9. **We will continue to take decisive action to contain inflation**. In light of the food price shocks and some signs of second-round effects, we have responded vigorously by raising our policy rate by 125 bps, increasing reserve requirements on foreign liabilities, and stepping up communication to explain the exogenous and expected temporary nature of the shock. With agriculture set to rebound, international food price inflation decelerating, and inflation expectations broadly anchored, we believe that inflation will start to decline, gradually returning to within the target band in the next 7−10 months. However, if inflationary pressures persist, we stand ready to increase the policy rate further with supporting steps to tighten liquidity conditions.

10. **We remain committed to a floating exchange rate.** Our interventions in the foreign exchange market will continue to aim at smoothing large exchange rate movements, while not resisting fundamental trends. We also aim to continue guarding international reserves as a buffer against exogenous shocks. We intend to lock in strong performance on international reserves by increasing our program targets for the remainder of 2011, in comparison with targets set at the time of the First Review. We will communicate clearly and act accordingly to ensure that market participants recognize the two-way risks in the foreign exchange market.

11. **We will continue to strengthen the status of the CBA policy rate as the market reference rate.** Recognizing that persistent excess liquidity weakens the impact of policy rate changes on the economy, we will step up liquidity management in dram markets so that market rates will move in line with the policy rate. To this end, we have conducted reverse repo operations and if conditions warrant, will restart the issuance of central bank bills. In addition, we will develop a deposit auction to enable the CBA to absorb liquidity with greater flexibility (Structural benchmark, September 2011). We will also improve our communications on liquidity management by publishing liquidity forecasts with the indication and T-bill issuance for liquidity management (Structural benchmark, December 2011). To enhance further the interest rate channel, we are also pursuing initiatives to develop the market for dram instruments such as supporting the efforts by NASDAQ OMX Armenia to develop term interbank markets.

12. **We remain determined to reduce dollarization, given that it weakens the monetary transmission mechanism.** We have continued to raise the proportion of dram

denominated reserve requirements for foreign liabilities to increase the spread between dram and foreign currency deposits. The increase in reserve requirements on foreign liabilities is intended to make dram deposits more attractive. While this has reduced deposit dollarization, foreign currency loans continue to grow rapidly in the context of abundant foreign currency liquidity. We acknowledge that successful dedollarization will ultimately hinge on our commitment to a flexible exchange rate policy and economic and price stability. We will remain vigilant to ensure that near-term dedollarization measures do not disrupt financial intermediation

C. Financial Sector Stability and Development

13. **We are committed to preserving the stability of the banking system and deepening financial intermediation.** Despite rapid credit growth, mostly in foreign currency, we remain confident of the soundness of the Armenian banking system, as banks remain liquid and well-capitalized. Nonetheless, recognizing that the high level of dollarization poses significant risks to financial stability, we raised capital and provisioning requirements on foreign currency loans in September 2010 and January 2011, respectively. We will continue monitoring FX-induced credit risk and foreign currency liquidity risk of banks and take further steps to limit vulnerability as needed.

14. **We continue efforts to enhance the resilience of the banking system.** In line with the Fund's technical assistance recommendations, we will enhance our supervisory framework with a more forward-looking assessment of potential risks. To this end we are improving our stress testing methodology, with a view to capturing linkages between the real and financial sectors. We have established a permanent internal financial stability committee which meets quarterly to assess developments and the outlook for the financial sector. The forthcoming FSAP Update will help shape financial stability policy to increase the resilience of the banking sector.

15. **We will strengthen our crisis preparedness and contingency planning.** We have issued a regulation requiring banks to set up contingency plans for liquidity and solvency support. The banks have already submitted plans, and the supervision arm of the CBA will review their coverage and adequacy. We are also drafting a crisis management framework that will identify the roles and responsibilities of each party in the CBA and the steps that will be taken in the event of a crisis. The framework is expected to be completed by September and approved by management by the end of the year. We have also developed scenarios for a crisis simulation exercise and will carry out drills before the end of the year.

III. Structural Reforms

A. Fiscal Reforms

16. **We have reduced the costs of tax compliance.** We have made tax reporting and payment less frequent, and reduced the number of forms needed. We have extended the e-filing system to over 4,000 taxpayers, and are expecting to operate electronic processing of tax returns and automated invoice processing by end-2011. We have improved the quality of taxpayer services, and are studying the introduction of a tax mediator/reconciler to improve the fairness of the tax system.

17. **We have made progress in the area of tax administration.** We finalized manuals in tourism, real estate, and transport using cash register machines for tax audits for usage starting January 2011. We increased the number of large taxpayers (LTPs) covered by the large taxpayer office by about 100 through December 2010 with a view to ensuring that LTPs' contribution in terms of total domestic revenues is continuously increasing compared to the previous year and in line with international best practices. We adopted a government decree establishing a mechanism for implementing a fully functional risk management approach in VAT refund processing. This will be fully operational by June 2011 (Structural benchmark, June 2011).

18. **Notwithstanding this progress, we will enhance our tax administration reforms efforts.** We will develop a Three-Year Strategic Plan for Tax Administration (2012−15) to map out our transition towards a more efficient and fairer tax system. As a first step towards achieving this broader reform effort, we will establish a taxpayer registry. The registry should help us to begin to make progress with the large stock of outstanding VAT credits. Establishing the registry is expected to take a number of steps, including: compiling existing taxpayer information; cross-checking this with supplementary data source and eliminating duplicates; identifying non-filers; and making contact with taxpayers. Completion of these steps would constitute establishment of the registry (Structural benchmark, December 2011). We are working to enhance information sharing between the Ministry of Finance and the State Revenue Committee to strengthen our assessment of revenue developments and our capacity for tax policy and revenue administration. Work in this area will commence with formation of a joint revenue analysis and forecasting committee to undertake an inventory of tax data now available and production of a new tax database for analysis of trends and policy initiatives.

B. Other Structural Reforms

19. **We have stepped up our efforts to improve the business environment.** We established a "one-stop shop" and an electronic business registration system, which have significantly reduced the cost and time for business registration. From January, we have also reduced substantially the number of licenses required for various business activities. Notably, the time and cost for obtaining construction permits have decreased

significantly. Furthermore, measures such as easing the requirement of certificates of origin for exports and reducing the time required for custom formulation for imports have reduced the cost of trading across borders. In addition, we are working with the European Union to undertake customs reform aimed at improving compliance and governance, while speeding clearance. We passed amendments to the Law on Competition to enhance the power of the Competition Commission, through strengthened inspections, improved methodologies, and increased penalties for monopolistic behaviors. In the area of anti-money laundering and combating the financing of terrorism (AML/CFT), we will submit to parliament later this year a package of bills to amend relevant laws and address shortcomings.

20. **We are developing an export promotion strategy.** We are in the process of creating an export-oriented free-economic zone for the agricultural sector and high-tech industry. We will take steps to strictly limit leakage and loss of fiscal revenues from any free zones. We will also take measures to address the obstacles identified by the European Commission in February 2009 to prepare for a Deep and Comprehensive Free Trade Area with the EU (e.g., product and sanitary standards, non EU-aligned trade and investment regulations, and competition rules). A negotiation team has been established with the Ministry of Economy as coordinator, aiming to start negotiations with the EU as soon as possible.

21. **We continue to work to shield the most vulnerable from the effects of the crisis and food price shock.** Notwithstanding the difficult fiscal situation, we met our social expenditure targets, and we will further increase the social spending on the Family Benefit Program and lump-sum financial aid by 16 percent in 2011 (indicative target). In addition, we introduced a targeted gas price subsidy for the poor covered by savings in other areas and an interest rate subsidy for the agricultural sector paid for by a contingency item in the budget.[1] Moreover, in order to further improve the registration process, coverage, and provisioning of social assistance, we adopted in January a decree on introducing an integrated system for the provision of social protection services, followed by a time-bound action plan in March. We will submit the amendments to Parliament in October (structural benchmark, December 2011).

22. **We are finalizing an Annual Progress Report on our Sustainable Development Plan,** and work has started on an updated strategy paper which will set out our vision for our nation's economic growth and social development over the long term.

[1] During April 1, 2011—March 31, 2012, the natural gas tariff for targeted vulnerable people is reduced to AMD100/cubic meter, from AMD132/cubic meter, up to a usage of 300 cubic meters in total during this period (the regular tariff of AMD132/cubic meter is charged to the use of natural gas exceeding 300 cubic meters).

IV. Conclusion

23. **Given our strong program implementation, we request the completion of the second review of the EFF/ECF program and the associated disbursement of SDR 36.2 million.** We also request modification of the end-June performance criteria for net international reserves and net domestic assets, as well as for the program fiscal balance in accordance with a revised definition. In addition, we request the establishment of performance criteria for end-December 2011. We will maintain a close policy dialogue with the Fund and stand ready to take additional measures, as appropriate, to ensure the achievement of the government social and economic objectives under the EFF/ECF program. We will continue to consult with the Fund on the adoption of measures, and in advance of revisions of the policies contained in the LOI, in accordance with the Fund's policies on such consultation. We will also provide the Fund with information it requests for monitoring progress during program implementation. The program's quantitative performance criteria and indicative targets, as per attached Technical Memorandum of Understanding and structural benchmarks are set out in Tables 1 and 2. The third review is expected to be completed on or after September 30, 2011. The fourth review is expected to be completed on or after March 30, 2012.

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/
Vache Gabrielyan
Minister of Finance
Republic of Armenia

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

Table 1. Armenia: Quantitative Targets for 2010-11 1/

(In billions of drams, at program exchange rates, unless otherwise specified)

	2010						2011								
	Mar. 2/	Jun.	Sep.	Dec.			Mar. 3/			Jun.		Sep. 3/		Dec.	
	Act.	Act.	Act.	Country Report No. 10/350	Adj. Prog.	Prel.	Country Report No. 10/350	Adj. Prog.	Prel.	Country Report No. 10/350	Prog.	Country Report No. 10/350	Prog.	Country Report No. 10/350	Prog.
Performance Criteria															
Net official international reserves (floor, in millions of U.S. dollars)	895	912	933	808	763	885	831	748	833	780	795	801	769	747	819
Net domestic assets of the CBA (ceiling)	-28	-16	-10	125	116	56	99	98	85	121	109	138	143	190	155
Program fiscal balance (floor) 4/	3	-22	-40	-140	-140	-124	-34	-34	-4	-58	-50	-90	-99	-112	-187
External public debt arrears (continuous criterion)	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
Indicative Targets															
Reserve money (ceiling)	465	435	438	540	545	508	515	520	506	530	522	555	538	596	563
Average concessionality of newly disbursed debt (floor, in percent) 5/				30	30	32								30	30
Social spending of the government (floor) 6/	7	15	23	31	31	31	9	9	9	18	18	27	27	36	36

Sources: Armenian authorities; and Fund staff estimates.

1/ All items as defined in the TMU.
2/ The net official international reserves balance excludes the total IMF disbursement received by Armenia on March 31.
3/ Indicative target.
4/ Below-the-line overall balance excluding net lending and project financing until March 2011. Below-the-line overall balance excluding net lending from June 2011.
5/ Assessed on a calendar year basis.
6/ Defined as 100 percent of the budgeted amount of the family benefit program and lump-sum financial aid.

Table 2. Armenia: Structural Benchmarks Under the EFF/ECF Arrangement

Item	Measure	Proposed Time Frame (End of Period)	Outcome
Tax administration			
1	Issue a government decree stipulating that clarifications and interpretations of laws, regulations, and procedures on taxes, duties, and mandatory fees should be approved by the Ministry of Finance. These clarifications and interpretations will become normative acts to be published and applied consistently across all taxpayers effective September 1, 2010.	July 2010	Met
2	Set up a Tax Appeals Council under the Government to deal with legal and procedural disputes of taxpayers.	September 2010	Met with delay
3	Develop manuals in tourism, real estate, transport, and sectors using cash register machines for tax audits for usage starting January 2011.	December 2010	Met
4	Simplify the reporting system by reducing the frequency of reporting to tax authorities and considerably streamline tax forms for VAT, profits tax, and personal income tax.	December 2010	Met
5	Adopt a government decree establishing a mechanism for implementing a fully functional risk management approach in VAT refund processing.	December 2010	Met
6	Implement a fully functional risk-based management approach in VAT refund processing.	June 2011	
7	Set up a taxpayer registry.	December 2011	
Tax policy			
8	Increase the tax rate structure for up-market luxury vehicles and SUVs for 2012 and adjust the specific tax on cars annually for inflation.	December 2011	
9	Introduce legislative changes that provide for annual automatic indexation of excises for inflation.	August 2011	
10	Approve a Tax Strategy paper.	December 2011	
Social policy			
11	Submit amendments to existing laws to parliament to enable the full functioning of an integrated system for the provision of social protection services.	December 2011	
Fiscal and debt sustainability			
12	Approve a medium-term expenditure framework (2011–13), including a medium-term debt management strategy.	August 2010	Met
Monetary sector			
13	Approve terms and conditions for deposit auction to enable the CBA to absorb liquidity with greater flexibility.	September 2011	
14	Publish the CBA's liquidity forecast that provides projected amount of dram liquidity before CBA's actions with indication of separate components such as currency outside the CBA, net foreign assets, government transactions excluding treasury bill issuances, and treasury bill issuances for liquidity management purposes.	December 2011	
Financial sector			
15	Issue prudential regulations to specifically address currency-induced credit risk, including increased loan-loss provisioning requirements and higher risk weights in capital requirements for foreign currency loans.	June 2010	Met
16	Formalize the Committee for Financial Stability in an MOU to set the modalities for main policy makers to coordinate their policies and responses in case of an imminent critical situation in the banking sector.	September 2010	Met
17	Issue prudential regulation requiring banks to prepare their contingency plans for liquidity and solvency support.	December 2010	Met

REPUBLIC OF ARMENIA: UPDATED TECHNICAL MEMORANDUM OF UNDERSTANDING

1. This memorandum sets out the understandings between the Armenian authorities and the IMF staff regarding the definition of performance criteria and indicative targets, their adjusters, and data reporting requirements for the three-year EFF/ECF Arrangement as per the Letter of Intent dated May 20, 2011 (LOI).

2. For program monitoring purposes, all foreign currency-related assets, liabilities, and flows in the monetary accounts will be evaluated at program exchange rates. The program exchange rate of the Armenian dram to the U.S. dollar is set at 385 dram per one U.S. dollar. The cross-rates for other foreign currencies are provided in Table 1.

I. Quantitative Targets

3. The program sets performance criteria and indicative targets for defined test dates (see Table 1 in the May 20, 2011 LOI). The program sets the following performance criteria:

- Floor on the net official international reserves (NIR) of the Central Bank of Armenia (CBA);
- Ceiling on the net domestic assets (NDA) of the CBA;
- Ceiling on external public debt arrears (continuous); and
- Floor on the program fiscal balance;

The program sets the following indicative targets:

- Ceiling on reserve money;
- Floor on average concessionality of new debt; and
- Floor on social spending of the government.

4. **The net official international reserves** (stock) of the Central Bank of Armenia (CBA) will be calculated as the difference between total gross official international reserves (excluding commercial bank required and excess reserves at CBA in FX) and gross official reserve liabilities.

- Gross official international reserves are defined as the CBA's holdings of monetary gold (excluding amounts pledged as collateral), holdings of Special Drawing Rights (SDRs), including the August 28, 2009 General Allocation and the September 9, 2009 Special Allocation, the country's reserve position at 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. Excluded from gross reserves are the balance on the government's Special Privatization Account (SPA), capital subscriptions in foreign financial institutions and illiquid foreign assets, any assets that are pledged, collateralized, or otherwise encumbered, claims on residents, claims in foreign exchange arising from derivatives in foreign currencies vis-à-vis domestic currency (such as futures, forwards, swaps, and options), precious metals other than gold, assets in nonconvertible currencies, and illiquid 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, as well as commitments to sell foreign exchange arising from derivatives (such as futures, forwards, swaps, and options).

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.

5. **Reserve money** is defined as the sum of currency issued, required and excess reserves, and current and time deposit accounts of certain resident agents. Liquidity absorbing transactions under reverse repurchase agreements, foreign currency swaps, and securities issued by the CBA are excluded from the reserve money definition. The ceiling will be considered as met if the outcome is within AMD 5 billion of the indicative target sets in Table 1 attached to the Letter of Intent dated May XX, 2011.

6. **Net domestic assets** are defined as reserve money minus NIR, minus commercial bank required and excess reserves at CBA in FX, plus medium and long-term foreign liabilities (i.e. liabilities with a maturity of one year or more) of the CBA, minus the balance of outstanding Fund purchases credited to the government account at the CBA. 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 and other items net.

7. **External public debt arrears** are 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.[1] The ceiling on external payment arrears is set at zero.

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[1] 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 (as defined in paragraph 12).

8. **The program fiscal balance** is cumulative from the beginning of the fiscal year and is measured from the financing side as the negative of the sum of net domestic banking system credit to the central government, net domestic nonbank financing, and net external financing to the central government. Should a general subsidy or any other fiscal transaction be introduced off-budget, the overall balance will be measured including the subsidy and other fiscal transactions as part of government spending

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

- **Net nonbank 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);[2] (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 drams, less amortization paid by the central government to private resident nonbank agents.

- **Net external 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 amortization 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.

9. External and domestic net lending, which are recorded as financing items, are *excluded* from the calculation of the program fiscal balance. This effectively treats net lending as an expenditure item when loans are made and as a revenue item when the loans are repaid.

10. Some project implementation units maintain accounts at the CBA. Grants received by these units 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 to finance investments 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. Under previous Technical Memoranda of Understanding, these activities were excluded from the calculation of the program fiscal balance. This treatment reflected lags in receiving information from project implementation units and on project loans intermediated through the banking system. With the shift to semi-annual program reviews with the EFF/ECF arrangement and consolidation of the accounts of these units in the Treasury, there is no

[2] 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.

longer a need for such exclusion, and these activities are now fully accounted for in the program fiscal balance.

11. Foreign currency proceeds from selling enterprises are deposited into the Special Privatization Account (SPA). The SPA 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 and are also treated as a financing item and recorded below the line.

12. The program sets an annual indicative floor of 30 percent on average concessionality of new debt on a disbursement basis on debt with nonresidents with original maturities of one year or more contracted and guaranteed by the public sector.

- The monitoring of the average concessionality target is done on a disbursement-by-disbursement basis and consistent with the methodology used in the DSA to calculate the original average concessionality target. In particular, the discount rate and the exchange rates used in the DSA should be used for the monitoring. The concessionality of floating interest rates will be assessed based on the interest rates as of June 1 of the preceding year.

- The public sector comprises the general government, the central bank, and nonfinancial public enterprises (enterprises and agencies in which the government holds a controlling stake—typically owns more than 50 percent of the shares, but which are not consolidated in the budget).

- For program purposes, the guarantee of a debt arises from any explicit legal obligation of the public sector to service a debt in the event of nonpayment by the debtor (involving payments in cash or in kind), or from any implicit legal or contractual obligation of the public sector to finance partially or in full any shortfall incurred by the debtor.

13. The program sets a floor on **social spending of the government**. For the purposes of the program, social spending of the government is defined as 100 percent of the budgeted amount of the family benefit program and lump-sum financial aid.

II. Adjustors

14. 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 and the ceiling on reserve money 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 liabilities relative to the baseline assumption as per the following formula: $\Delta NDA = \Delta rB$, where B denotes the level of liabilities subject to reserve requirements in the initial definition and Δr 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.

- **Budget support grants to the public sector** are defined as grants received by the general government for direct budget support from external donors and not related to project financing.

- **Budget support loans to the public sector** are defined as disbursements of loans from bilateral and multilateral donors for budget support and Fund purchases credited directly to the government accounts at the CBA.

- **Project financing to the public sector** is defined as disbursements of loans from bilateral and multilateral donors for public sector projects.

- **The floor on NIR** will be adjusted upward (downward) by the cumulative amount of any excess (shortfall) of budget support loans or budget support grants (excluding Fund disbursements to the government) compared to program amounts (Table 3). The floor on NIR will be adjusted downward for any external public debt amortization amounts in excess of program amounts.

- **The ceiling on NDA** will be adjusted downward by the amount of any excess of budget support loans or budget support grants compared to program amounts (Table 3).

- **The floor on the program fiscal balance on a cash basis** will be adjusted upward (downward) by the cumulative total amount of the budget support grants received in excess (to account for a shortfall) of the program amounts (Table 3), subject to a cap of \$25 million in either direction. The floor on the program fiscal balance on a cash basis will also be adjusted downward (upward) by the cumulative total amount of the project financing received in excess (to account for a shortfall) of the program amounts (Table 3), subject to a cap of \$50 million in either direction.

III. Data Reporting

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

Reporting Agency	Type of Data	Description of Data	Frequency	Timing
CBA	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
	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 . For project implementation units, 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
	Domestic expenditure arrears	All unpaid claims outstanding at the end of the month which includes wages, social contributions (including for pensions), family allowances, and amortization and domestic interest payments	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,	Quarterly	Within 30 days of the end of each

		and irrigation sectors		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)
	Large taxpayers	Data on the number of taxpayers and amount of taxes managed by the large tax inspectorate	Monthly	Within 45days after the end of each month
	Import data	1. Total value of recorded imports, breaking out raw diamond imports; 2. Total value of non-duty free recorded imports; 3. Number of total transactions involving recorded imports; 4. Number of total transactions involving non-duty free recorded imports 5. Value of recorded imports where customs value was assessed using transaction prices, breaking out raw diamond imports; 6. Value of non-duty free recorded imports where customs value was assessed using transaction prices; 7. Number of transactions involving recorded imports where customs value was assessed using transaction prices; 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 in U.S. 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
SDR	593.00	1.5403

Table 2. Armenia: KFW and IBRD SME Loan Disbursements, 2010-11 1/
(In millions of U.S. dollars)

Mar-10	Jun-10	Sep-10	Dec-10		Mar-11		Jun-11		Sep-11		Dec-11	
Actual	Actual	Actual	Country Report No. 10/350	Prel.	Country Report No. 10/350	Prel.	Country Report No. 10/350	Prog.	Country Report No. 10/350	Prog.	Country Report No. 10/350	Prog.
0.0	0.0	5.0	29.9	5.0	2.0	0.0	4.0	2.0	6.0	4.0	8.0	25.8

1/ Cumulative from the end of the previous year.

Table 3. Armenia: External Disbursements to the Public Sector in 2010-11 1/
(In millions of U.S. dollars)

	Mar-10	Jun-10	Sep-10	Dec-10		Mar-11		Jun-11		Sep-11		Dec-11	
	Actual	Actual	Actual	Country Report No. 10/350	Prel.	Country Report No. 10/350	Prel.	Country Report No. 10/350	Prog.	Country Report No. 10/350	Prog.	Country Report No. 10/350	Prog.
Project financing	63	107	145	187	193	14	30	61	62	95	109	159	158
Budget support loan	0	38	67	116	96	56	0	85	66	131	91	160	175
Budget support grant	…	…	…	…	…	…	8	…	41	…	41	…	82
of which: EU program	…	…	0	0	0	25	0	25	20	50	20	50	50
Total	63	145	212	303	289	95	30	171	168	275	240	368	414

1/ Cumulative from the end of the previous year.

IV. Guidelines on the Indicative Benchmark with Respect to the Definition of External Debt

For program purposes, the definition of debt is set out in Executive Board Decision No. 12274, Point 9, as revised on August 31, 2009 (Decision No. 14416-(09/91)).

(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.