International Monetary Fund

Armenia and the IMF

Press Release:
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March 29, 2010

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Armenia: Letter of Intent and Technical Memorandum of Understanding

March 10, 2010

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ARMENIA: LETTER OF INTENT

March 10, 2010
Mr. Dominique Strauss-Kahn
Managing Director
International Monetary Fund
Washington, D.C. 20431

Dear Mr. Strauss-Kahn:

1. On the back of a strong policy response, Armenia is leaving behind a crisis of enormous proportions. Since the last review, our continued fiscal and monetary stimulus has stabilized the economy. Our exchange rate policy stabilized the dollarization process and has been instrumental in allaying concerns for financial stability. Structural reforms in the program are building the foundation for increased tax collection and improving safety nets to minimize the effects of the crisis on the poor.

2. Our performance under the program continues to be very strong. Almost all quantitative targets for end-December were met. The fiscal deficit, while providing key support to the economy, has been kept under control, allowing us to attain the end-December targets for the fiscal balance and net banking system credit to the government. We also met the end-September target for fiscal balance, for which, with provisional data, we had cautiously asked for a waiver of nonobservance at the time of the last review. The net international reserves target was comfortably met. However, despite our prudent monetary policy, the end-December performance criterion on net domestic assets of the Central Bank was narrowly missed due to strong temporary liquidity demands in the last few days of the year in advance of the unusually long holiday period. Also, the indicative target on the stock of tax credits for end-December was missed. As outlined below, structural benchmarks were implemented largely as planned.

3. This Letter of Intent builds on these achievements, laying out an agenda for 2010 that supports the exit path from the crisis. Our macroeconomic policies will need to strike a balance between the risk of choking off economic recovery and containing macroeconomic pressures that may emerge. We will also continue efforts on structural reforms to increase tax revenue, develop a sound financial system, and build the foundations for sustained diversified economic growth and poverty reduction. We remain committed to implementing the measures contained in previous letters of intent.

Recent Developments and Outlook for 2010

4. Economic activity has stabilized, while inflation has increased. Domestic demand, mainly for non-durable goods, has held steady thanks to our stimulus package. Recovery is evident in some sectors, including the mining and metallurgy industries. Inflation has increased on the basis of strengthening international commodity prices, some lagged pass-through effects from the exchange rate depreciation observed in the first part of

2009, and initial signs of pressure in selected services.

5. We expect a mild recovery in 2010. Prospects for the world economy and the Russian economy in particular have improved moderately, providing support for remittances and the tradable sector. Financial sector intermediation is picking up, and will support growth and domestic demand. Changes in private consumption and investment, which were contributing to the negative GDP growth in 2009, should make a positive contribution in 2010, whilst public consumption is expected to continue to show positive growth.

6. The external position remains vulnerable, but we aim to reduce the current account deficit over time. Despite the contraction in domestic demand and real depreciation, the 2009 current account deficit diminished only moderately in dollar terms and stands close to 14 percent of GDP, strongly influenced by the effect of regional trends in exports and remittances. External imbalances are expected to persist in 2010, reflecting the weak recovery of our main trading partners and continued strong public investment, while our gross financing needs broadly remain as envisaged in the beginning of the program.

Monetary, Exchange Rate and Financial Policies

7. We are adjusting our monetary stance in line with inflation developments. Inflation has now fallen out of our target band, so consistent with our price stability objective, we increased our policy rate by 100 basis points since the beginning of the year. We have also decreased the amount of outstanding repos significantly, while tight liquidity conditions have created a moderate wedge between our policy and market rates. We will further gradually adjust the policy rate to become positive in real terms. In this setting, inflation will come down from highs in the first quarter, and we will continue pursuing policies to bring it within the target band in the near future.

8. We will continue to strengthen our monetary framework. In light of increased dollarization, we will pay more attention to monetary aggregates, including base money, and consider the effectiveness of current rules of monetary policy implementation and communication in consultation with the Fund, including if necessary on-site discussions, assistance or studies by IMF experts. We aim to strengthen the transmission mechanism by implementing several dedollarization measures. And to enhance the effectiveness of our policy rate, we will use more frequently our available instruments to offset government's lumpy spending, therefore reducing the volatility of short-term market rates. To deepen the secondary market, we will also introduce an overnight interbank market trading platform in NASDAQ-OMX. Lastly, we will outline an effective communications strategy to explain to the public the temporary nature of price developments behind the headline index.

9. We remain committed to the floating exchange rate regime. We have intervened in the foreign exchange market to smooth excessive volatility and counter speculative pressures to prevent large depreciations from threatening monetary and financial stability.

We will continue to allow increased flexibility in exchange rate movements aiming at creating two-way risks in the market. In order to facilitate economic adjustments needed to maintain external stability, we will not intervene to resist fundamental trends in the exchange rate.

10. The health of the banking sector is improving, but we continue to closely monitor the situation. Banking sector balance sheets are improving steadily. Non-performing loans have been falling and profitability has turned positive since September. Lending activities have started recovering in recent months, fueled in part by our on-lending programs. We expect lending to continue to grow in 2010, although only at a moderate pace because of current and prospective prudential regulations. In the near term, dram lending is likely to be limited by high dollarization of deposits (as banks strive to balance their foreign currency position), but will still be supported by the continuation of the government's refinancing operations through the banking system. Capital and liquidity ratios remain strong and latest stress tests continue to show financial soundness.

11. We have taken concrete steps to limit vulnerabilities of the financial sector and we continue to improve our crisis preparedness and contingency planning. In April 2010, the limits on net open foreign exchange positions of +/- 7 percent of capital will come into full effect. We also plan to strengthen prudential regulations to address currency-induced credit risk to ensure that banks' capital buffer would be sufficient to deal with a deterioration in the FX loan portfolio. In particular, loan-loss provisioning requirements and risk weights in capital requirements for foreign currency loans will be increased (structural benchmark, June 2010). This year, we plan to formalize the Committee for Financial Stability (structural benchmark, September 2010), after we receive further assistance from Fund TA on contingency planning, specifically to set out modalities for policy makers to coordinate their policies and responses, including the division of responsibilities and information sharing among stakeholders (CBA, MOF, and DGF). We will also issue a prudential regulation requiring banks to prepare their contingency plans (structural benchmark, December 2010). Furthermore, we would welcome the opportunity to undergo a Stability FSAP Module to help diagnose and address remaining vulnerabilities.

12. Given these improvements, we plan to phase out the temporary crisis-related supporting measures this year. Specifically, the capital injection-matching subordinated debt facility and guarantee on interbank lending are no longer needed and will be discontinued to minimize risks to the CBA's balance sheet and potential conflict of interest.

Fiscal Policy

13. The fiscal deficit will be reduced in 2010, whilst social and capital spending will be maintained at an adequate level. We recognize that early withdrawal of fiscal stimulus could break the virtuous circle associated with an economic recovery. However, given positive signs in economic activity and debt sustainability concerns**,** we do not plan to increase the stimulus further. As such, the 2010 budget envisages broadly stable spending in nominal terms, while revenues will increase due to greater economic activity and

improved tax administration. This will still imply a lowering in the deficit to around 6 percent of GDP, down from 7.5 percent of GDP in 2009. We intend to save any revenue over-performance above budgeted amounts. In the unlikely event that revenues fall below expectations, we will implement contingency measures to ensure that the deficit target is respected. In absolute terms, the deficit will continue to be significant, but financing is already secured through external support from donors, and we intend to issue t-bills to cover the remaining financing needs.

14. We remain firmly committed to medium-term fiscal sustainability. To this end, our fiscal consolidation program envisages a gradual reduction in the deficit. We will meet the requirements of our law that the deficit must be brought below 3 percent of the average last three years' GDP when debt levels surpass 50 percent of GDP. The medium-term adjustment will rely on both revenue and expenditure measures, while ensuring sufficient social and capital spending. In order to strengthen our fiscal framework, we will submit to the government a medium term budget framework for 2011–13 laying out our revenue projections, assumptions, and risks, spending priorities, funding sources, debt dynamics, as well as specific measures to deal with transitory shocks and/or the materialization of contingent liabilities (structural benchmark, July 2010).

Fiscal Structural Reforms

15. The crisis did not hinder progress on our ambitious tax administration reforms. All VAT refund claims filed in 2009 have been processed within the statutory 90-day processing deadline, with the exception of a few cases in which delays were temporary due to taxpayers' failure to provide necessary documentation. We will continue to process them within that timeframe during 2010. We have also made progress in implementing reforms in other areas, including (i) the introduction of mandatory e-filing of tax returns in 2009 for large taxpayers, which will be expanded over the course of 2010 to all other taxpayers; (ii) the development of a concept note on risk-based selection of taxpayers subject to audit, which was approved by the cabinet; and (iii) the improvement of analytical capacity of the tax agents. In addition, in close cooperation with CBA, we aim to start efforts at the SRC to enforce currency regulations.

16. Going forward, we remain committed to our revenue administration reforms to enhance the business environment and ensure a sustainable revenue base. The overall stock of tax credits was marginally reduced in 2009, although the indicative target for end-December 2009 was missed. Nonetheless, we remain strongly committed to addressing the systemic problems underlying tax credits, and to implement measures to ensure that unwarranted advance tax payments do not arise. Moreover, we will continue to focus on further strengthening VAT refund processing, including by implementing a fully functional risk-management approaches in VAT refund processing for which we will (i) submit legislation to parliament to allow only high risk VAT refunds to be subject to review (structural benchmark, March 2010), and (ii) adopt a government decree establishing a mechanism for implementing such a system (structural benchmark, December 2010 with actual implementation taking place by June 2011). To further strengthen the penalty regime, we will submit legislation to parliament allowing consolidation of VAT returns and refund claims in a single application, which will also

contribute to streamlining the process. Fund TA is helping us in all these efforts, and we welcome the support provided by an IMF tax administration resident advisor who will commence his duties in March 2010.

17. Progress has been also made in tax policy to increase tax collection over the medium term. Specifically, and in line with our commitment to abolishing presumptive taxation for fuel and tobacco products, we have submitted legislation to parliament to bring these products within the regular VAT regime effective January 2011. Moreover, we will submit legislation to parliament to abolish the presumptive taxation regime for certain activities (structural benchmark, September 2010). Finally, we intend to review the selection criteria to optimize the amount of taxpayers in the large taxpayers unit.

18. We are committed to strengthening public financial management and our medium-term debt management capacity. We intend to move the accounts of the Project Implementation Units (PIUs) from commercial banks to treasury accounts. As such, we intend to strengthen our debt monitoring and planning capacity, in line with our objectives set at the time of the last review. Furthermore, we will adopt a time-bound action plan to develop and implement a comprehensive medium-term debt management strategy. Reflecting the adjustment of the current account and the projected rebound in growth, the external debt-to-GDP ratio is expected to remain sustainable despite the rapid rise in public debt in the last two years.

Other Reforms

19. We will continue our efforts to deepen structural reforms that will sustain economic recovery, enhance the productive capacity of the economy, and promote long-term economic growth. These reforms include substantial investments in transportation infrastructure and information technology. We continue to be 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 addressing conflict of interest issues involving public officials. Finally, we are considering measures to increase competition and level the playing field, with a view to eliminating market domination in key sectors. We expect that structural reforms will result in considerable competitiveness gains over the medium term.

20. We remain committed to reducing poverty and protecting the poorest members of our society. To that effect, and in collaboration with the World Bank, we have developed a strategy to further strengthen the targeting of social safety nets. Going forward, we intend to identify an indicator that reflects spending efforts in this area, which will enable us to assess the effectiveness of our social policies in tackling poverty.

Conclusion

21. We request the completion of the Third Review under the Stand-By Arrangement in light of the performance under the program and our continued commitment to strong

policies. Given the changed outlook, we also request modification of the end-March performance criteria for net international reserves, net domestic assets of the CBA, net banking system credit to the government, and the program fiscal balance. On the latter, we request a change in its definition to ease monitoring. In addition, we wish to reintroduce the indicative target on reserve money ceiling starting March 2010. Finally, we request the establishment of performance criteria for end-June 2010, and a waiver for the end-December 2009 performance criterion on net domestic assets of the CBA, given that the deviation was minor and temporary. We expect to complete the fourth review on or after May 14, 2010, and the fifth review on or after August 15. We will maintain the 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 Stand-By Agreement. 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 for 2010 and structural benchmarks are set out in Tables 1 and 2.

22. As we enter the post-crisis period, we are considering the merits of shifting to a Fund facility more tailored to our medium term challenges. In particular, weaknesses in our balance of payments and a large structural reform agenda will remain, and we will be in close contact with Fund staff on the facility most appropriate to address these challenges.

23. We authorize the IMF to publish the 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, 2008–10 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.
		Adj. Prog	Act.	Adj. Prog	Act.	Adj. Prog	Act.	EBS/09/155	Adj. Prog	Prel.	EBS/09/155	Prog.	Prog.	Prog.	Prog.
Performance Criteria															
Net official international reserves (floor, in millions of dollars)	1,056.6	455.9	654.1	990.7	1,089.7	828.7	1,097.4	976.8	989.8	1018.9	897.8	887.8	875.3	833.0	888.7
Net domestic assets of the CBA (ceiling)	75.3	143.6	32.3	-27.5	-115.9	-23.4	-87.4	-11.4	-12.1	**-11.7**	31.2	8.9	14.8	38.0	30.3
Net banking system credit to the government (ceiling)	-37.3	-23.6	**-10.6**	-120.9	-167.1	-113.5	-162.6	-50.6		-125.3	4.2	-91.6	-93.2	-76.8	-89.6
Program fiscal balance (floor) 3/	-68.2	-29.9	**-36.2**	-123.4	-91.2	-212.3	-205.9	-342.4	-385.8	-354.8	-89.0	-59.7	-92.5	-121.3	-148.6
External public debt arrears (continuous criterion)	0	0	0	0	0	0	0	0		0	0	0	0	0	0
Indicative Targets															
Reserve money (ceiling) 4/	449.7	381.3	**391.7**	…	…	…	…	…	…	…	…	496.7	512.6	534.3	562.7
Stock of tax credits (ceiling) 5/	154.4	154.4	147.0	147.0	134.9	145.0	143.3	134.9		152.8	…	148.0	…	…	…
Contracting or guaranteeing of new non-concessional debt (ceiling, in millions of dollars) 6/								0		0	195.0	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 September and December.
3/ Below-the-line overall balance excluding net lending until 2009. Below-the-line overall balance excluding net lending and project financing from 2010.
4/ Reintroduced starting March 2010.
5/ Indicative target up to end-March 2010.
6/ For 2009, cumulative beginning the second half and therefore excludes the Russian loan contracted in June 2009.

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

Item	Measure	Proposed Time Frame (End of Period)	Outcome
	<u>Tax administration</u>		
1	Meet the statutory 90-day processing deadline for all VAT refund claims filed in 2009.	Continuous in 2009	Met
2	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	
3	Adopt a government decree establishing a mechanism for implementing a fully functional risk management approaches in VAT refund processing.	December 2010	
	<u>Tax and social policy</u>		
4	In close collaboration with the World Bank, develop a strategy to further strengthen the targeting of social safety nets.	December 2009	Met
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	Met
6	Submit legislation to parliament amending the Law on Presumptive Taxes to allow transfer of certain types of activities identified in the Law on Presumptive Taxes to the general taxation system.	September 2010	
	<u>Fiscal sustainability</u>		
7	Submit a medium-term fiscal framework (2011–13) to the government.	July 2010	
	<u>Financial sector</u>		
8	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	
9	Formalize the Committee for Financial Stability in an MOU.	September 2010	
10	Issue prudential regulation requiring banks to prepare their contingency plans.	December 2010	

ARMENIA: 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 Stand-by Arrangement. This memorandum updates and replaces the TMU dated October 14, 2009. It 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 dated March 10, 2010, under which Armenia's performance under the program supported by the Stand-by Arrangement (SBA) will be assessed.

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 dram 385 per one U.S. dollar. The cross-rates for other foreign currencies are provided in Table 1.

3. For purpose of monitoring, the central government is defined as general government less local government and less off-budget funds.

I. Quantitative Targets

4. The program sets performance criteria and indicative targets for defined test dates (see Table 1 in the Letter of Intent dated March 10, 2010). 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 the net banking system credit to the general government;
- Ceiling on external public debt arrears (continuous);
- Floor on the program fiscal balance;

The program sets the following indicative targets:

- Ceiling on reserve money;
- Ceiling on tax credits stock;
- Ceiling on contracting or guaranteeing of new nonconcessional external debt by the public sector.

5. **The net official international reserves** (stock) will be calculated as the difference between total gross official international reserves (excluding reserve money denominated in foreign currencies) and gross official 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 excluding the balance on the government's Special Privatization Account (SPA) 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.

6. **The net domestic assets** are 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. 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. 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, the CBA's deposit facility, foreign currency swaps, and securities issued by the CBA are excluded from the reserve money definition.

7. **The banking system credit to the general government** is defined as the sum of net credit from the CBA and net credit from commercial banks to the general government.

- **The stock of net credit from the CBA to the general government** 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, 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 general government** includes: (1) gross commercial bank credit to the general government less general government deposits with commercial banks; 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).

8. **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.

9. **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 (excluding net project financing). 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 central government** equals the change during the period of net credit to the central government. Central government is defined as general government less local government and less off-budget funds.

- **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.

10. Those project implementation units, that carry out projects financed by the US-based Lincy Foundation, or other budget-related project implementation units maintain accounts at the CBA. The 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 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.

11. 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

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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.

[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.

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.

12. The program sets a ceiling on **reserve money**. Reserve money is defined as the sum of currency issued, required and excess reserves, and current and time deposit accounts of certain resident agents. The ceiling will be considered as met if the outcome is within AMD 5 billion of the indicative target set in Table 1 attached to the Letter of Intent dated March 10, 2010.

13. **The stock of tax credits (indicative target)** is 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.

14. **The program sets a ceiling on contracting or guaranteeing of new nonconcessional external debt by the public sector.** 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. For 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

15. 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 deposits 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.

- **External financing to the public sector**, defined as disbursements of loans from bilateral and multilateral donors for budget 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 budget support 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 budget support financing compared to programmed amounts (Table 3). The floor on the program fiscal balance will be adjusted downward by the amount of any shortfall in receipt of grants under the European Union budget support program.

- **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 [3]	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

[3] 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 . 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	Monthly	Within 45 days of the end of each

		wages, social contributions (including for pensions), family allowances, and amortization and domestic interest payments		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)
	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 Disbursments, 2009–10 1/
(In millions of U.S. dollars)

Mar-09		Jun-09		Sep-09		Dec-09		Mar-10	Jun-10	Sep-10	Dec-10
Prog.	Actual	Prog.	Actual	Prog.	Actual	Prog.	Actual	Prog.	Prog.	Prog.	Prog.
2.4	5.5	2.4	31.9	33.6	33.8	35.6	33.8	2.0	4.0	6.0	32.9

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)

	Mar-09		Jun-09		Sep-09		Dec-09		Mar-10	Jun-10	Sep-10	Dec-10
	Prog.	Actual	Prog.	Actual	Prog.	Actual	Prog.	Actual	Prog.	Prog.	Prog.	Prog.
Project financing	14.7	12.2	50.8	33.0	81.2	67.5	62.7	100.4	19.7	58.6	79.2	117.0
Budget financing	3.1	-	78.9	-	97.3	60.9	111.3	117.0	14.4	47.7	62.1	103.0
Russia	-	-	192.5	192.5	192.5	192.5	192.5	192.5	-	-	-	-
Total	17.8	12.2	322.3	225.5	371.1	320.8	366.5	409.9	34.1	106.3	141.2	220.1

1/ Cumulative from the end of the previous year, 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.

(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.