



## **MIDDLE EAST AND CENTRAL ASIA DEPARTMENT**



# **Caucasus and Central Asia: Outlook and Policy Challenges**

## **Navigating the Evolving Goeconomic Landscape**

**NOVEMBER 2024**

Umang Rawat  
Resident Representative for Armenia

# IMF at a glance

- **Key Mandate:** Promoting global economic and financial stability
- Role of the IMF

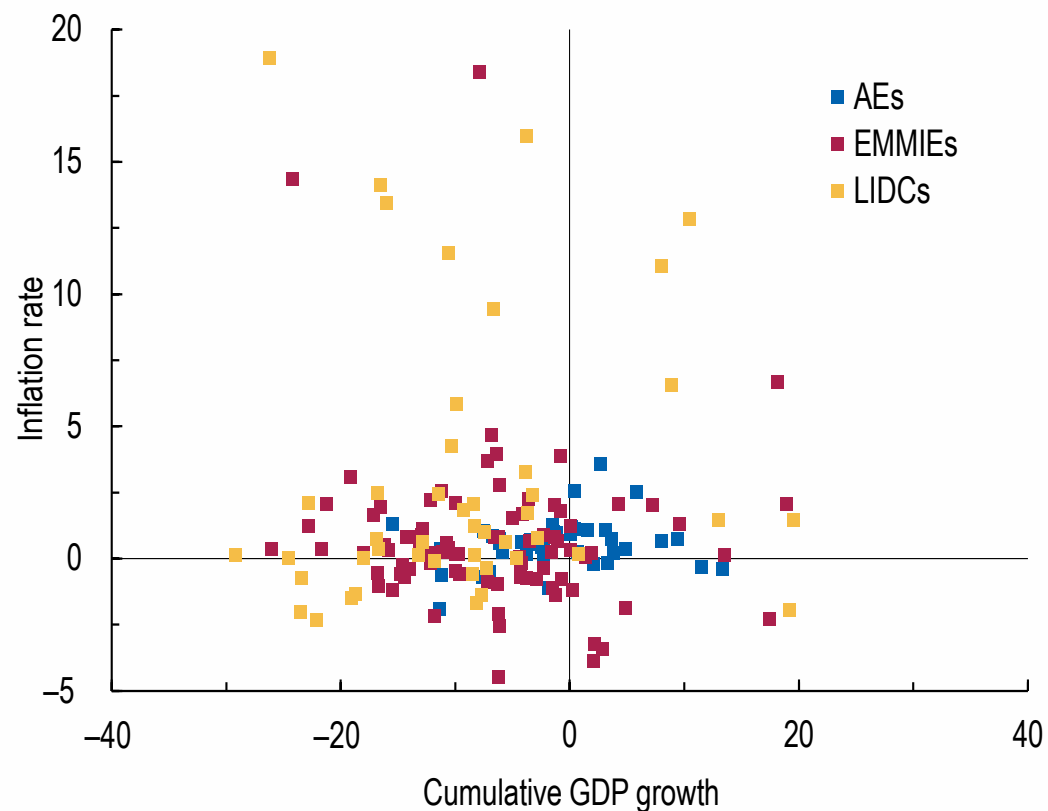
Policy Assessment and Advice	Lending	Capacity Development
Bilateral; Regional; and Global/multilateral surveillance	Non-concessional lending → crisis management and prevention	Bilateral support
Evenhanded approach	Concessional lending → zero interest rate	Technical Assistance
Systemic countries/spillover or cross-country effects	Conditionality → Flexible, focused, macro-critical	Training/Workshops

# Recent Developments

# Past four years - uneven performance across countries

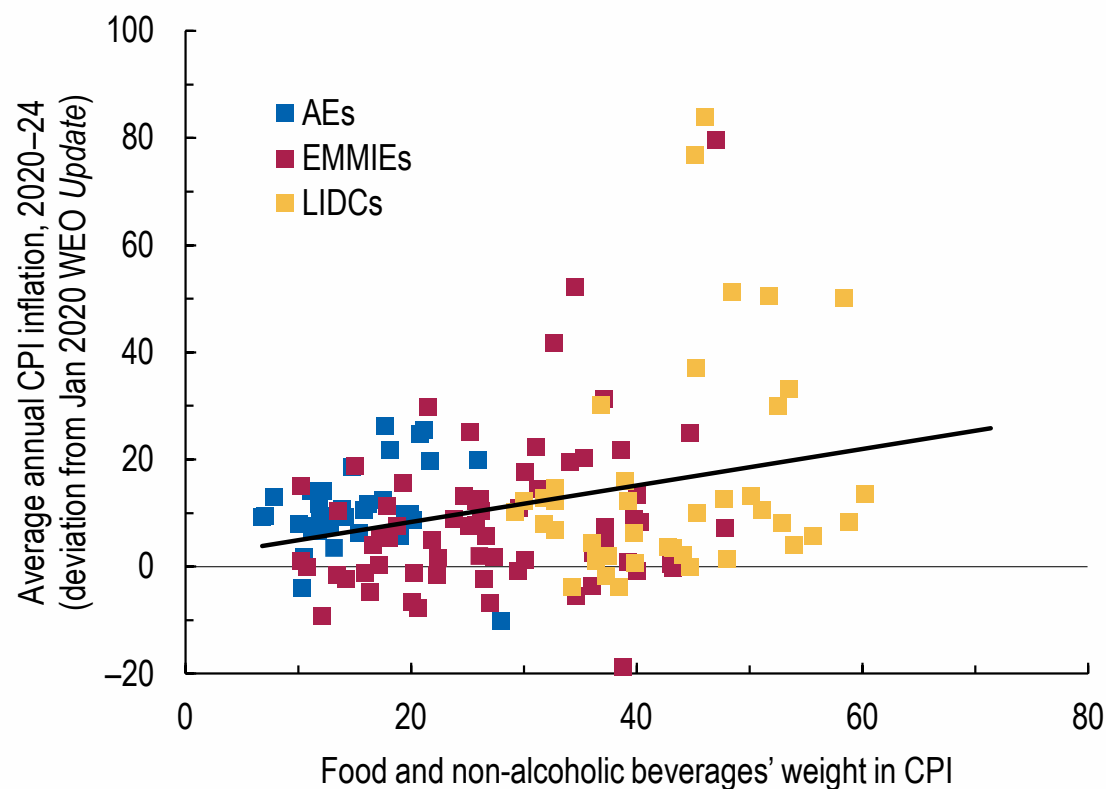
## Growth and Inflation Revisions

(Percentage points; relative to January 2020 WEO Update)



## Inflation Surprises and Importance of Food in CPI

(Percent)

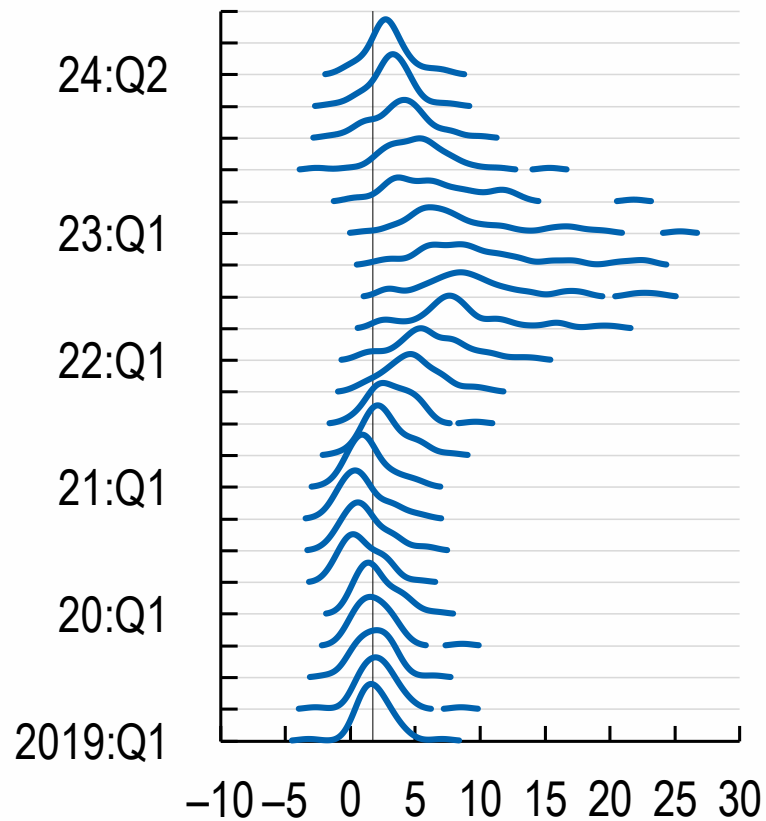


Source: IMF staff calculations.

# Inflation declining and converging across countries supported by tight monetary policy...

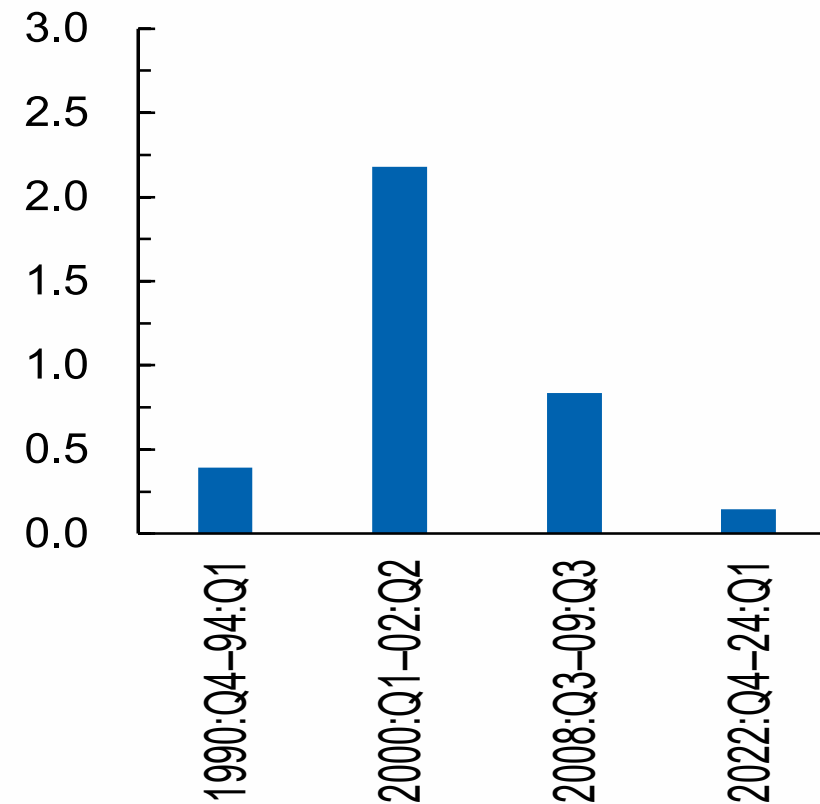
## Headline Inflation Distribution

(Percent, year over year)



## Output-Inflation Sacrifice Ratio

(Change in output gap for a change in inflation)



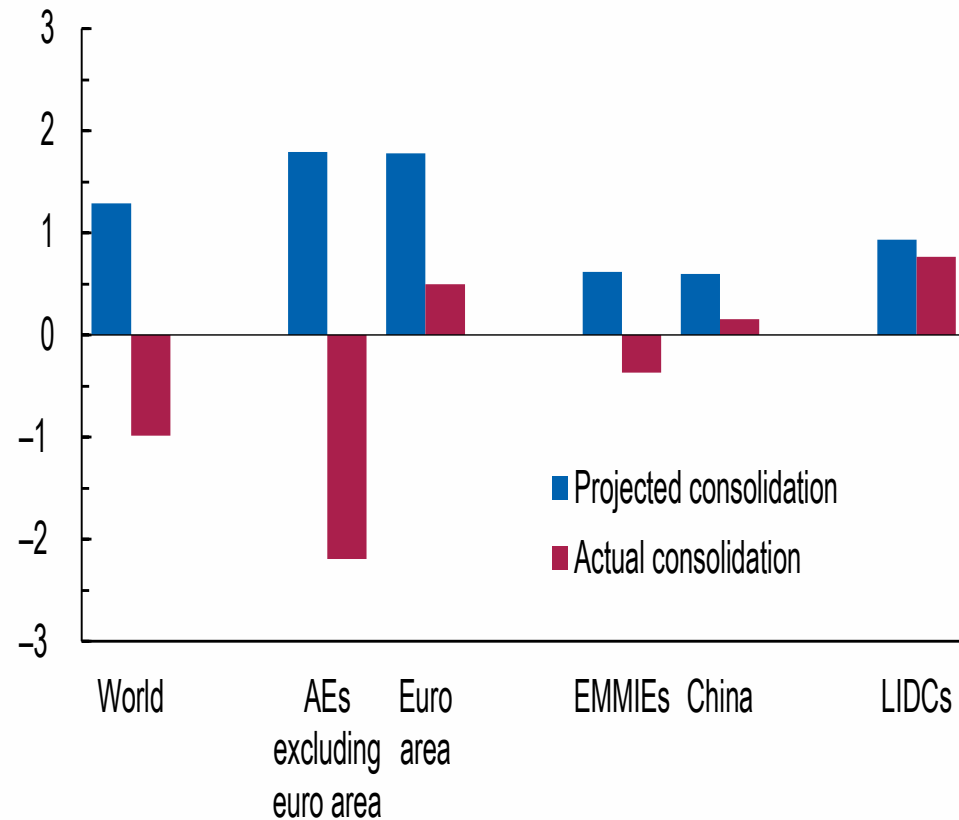
Sources: OECD and IMF staff calculations.

Note: The sample for the headline inflation distribution includes 32 advanced economies and 13 emerging market and developing economies. The sample for estimating the sacrifice ratio includes 37 advanced economies.

# ... combined with loose fiscal policy

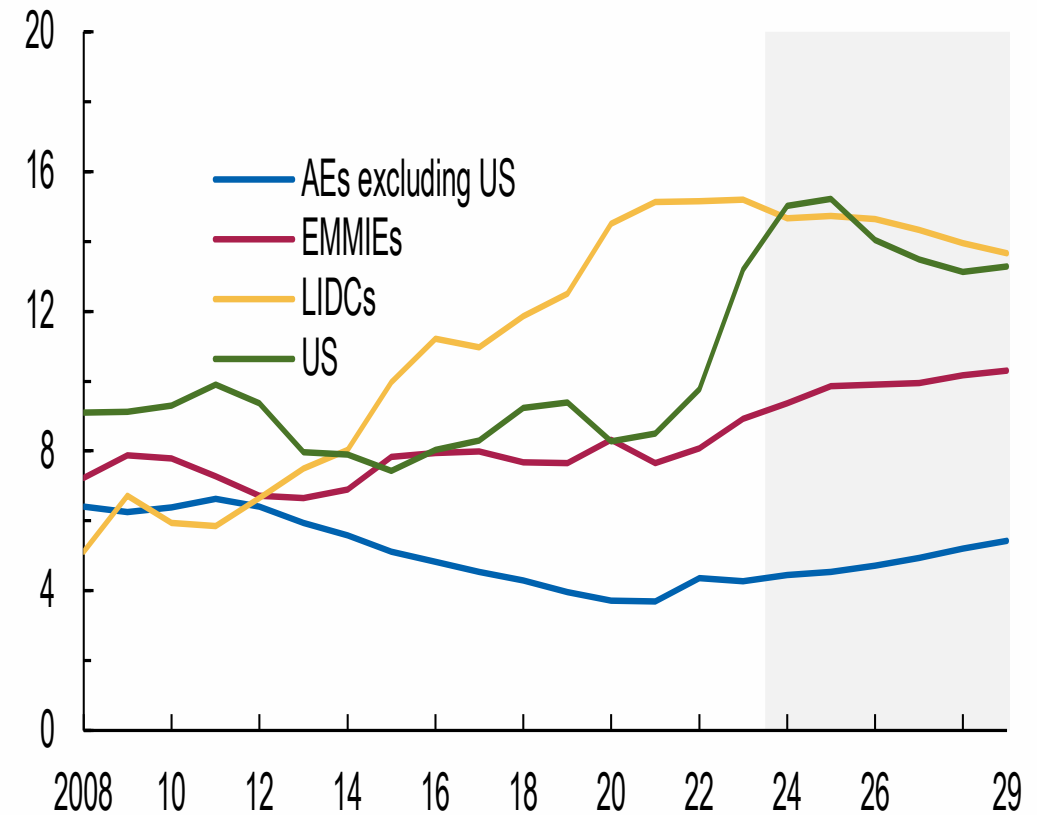
## Fiscal Slippage

(Percentage points; 2024 minus 2022 primary balance)



## General Government Interest Payments

(Percent of general government revenues)



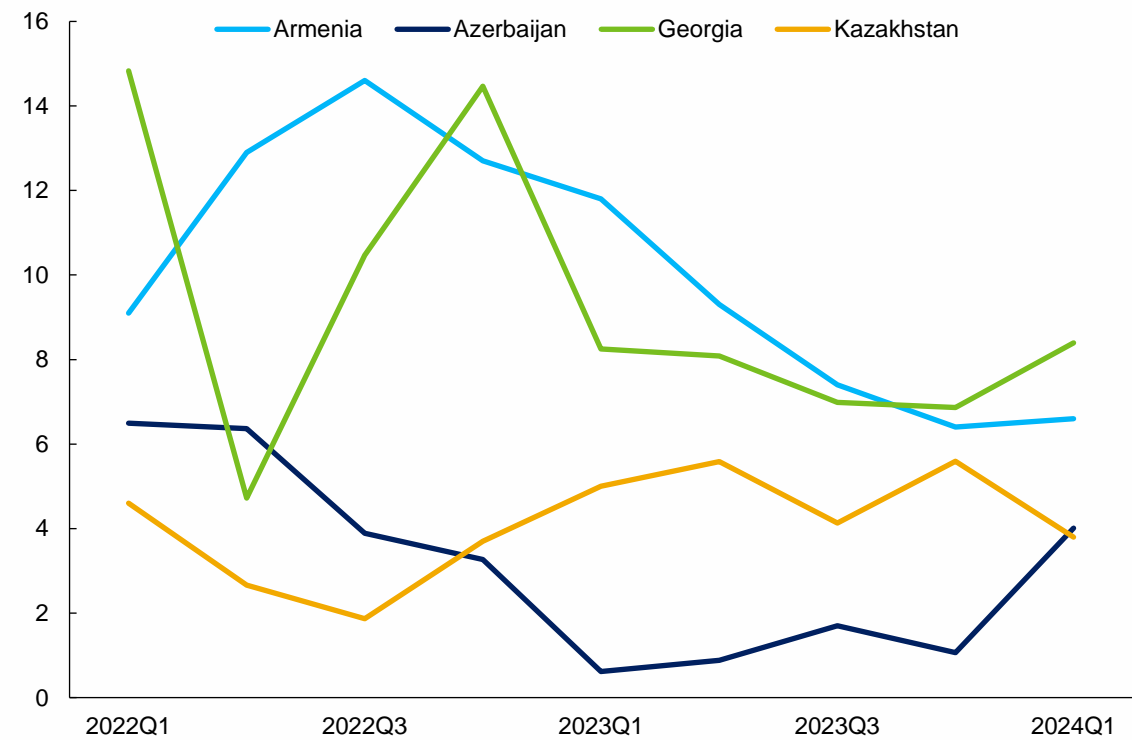
Sources: IMF staff calculations.

# Growth in the CCA remains robust and inflation has decelerated

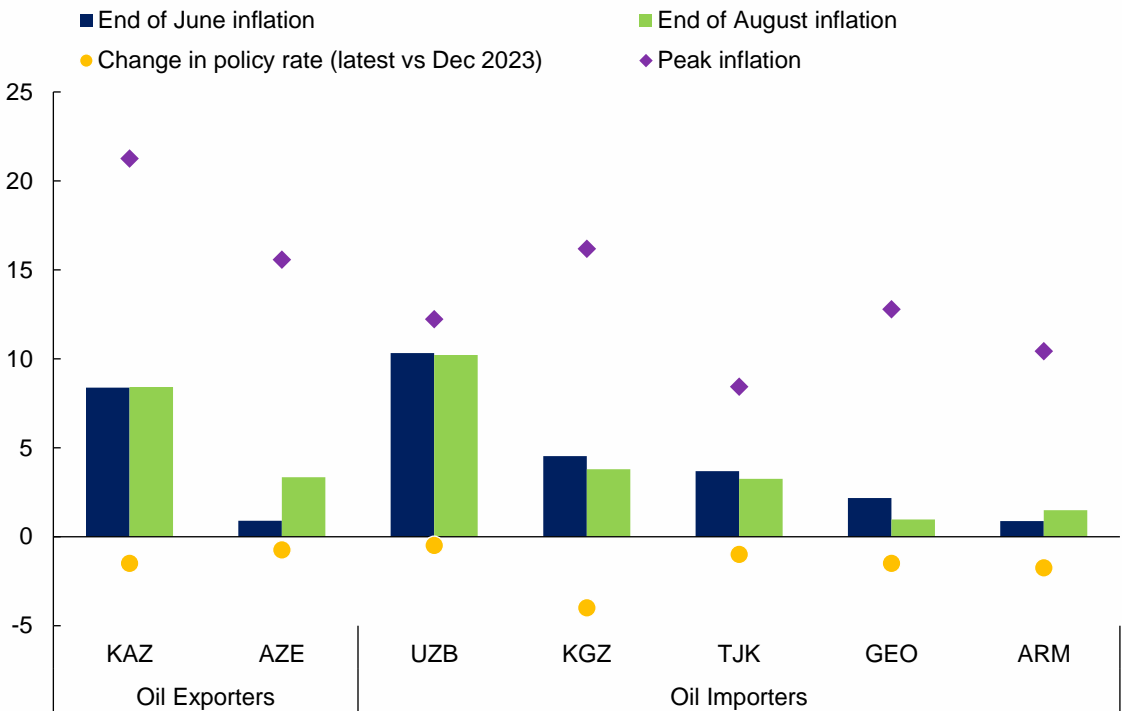
Across CCA economies, growth has remained robust

Inflation has come down and a loosening cycle has also begun

CCA: Real GDP Growth  
(Year-over-year percent change)



CCA: Headline CPI and Change in Policy Rate  
(Year-over-year percent change)



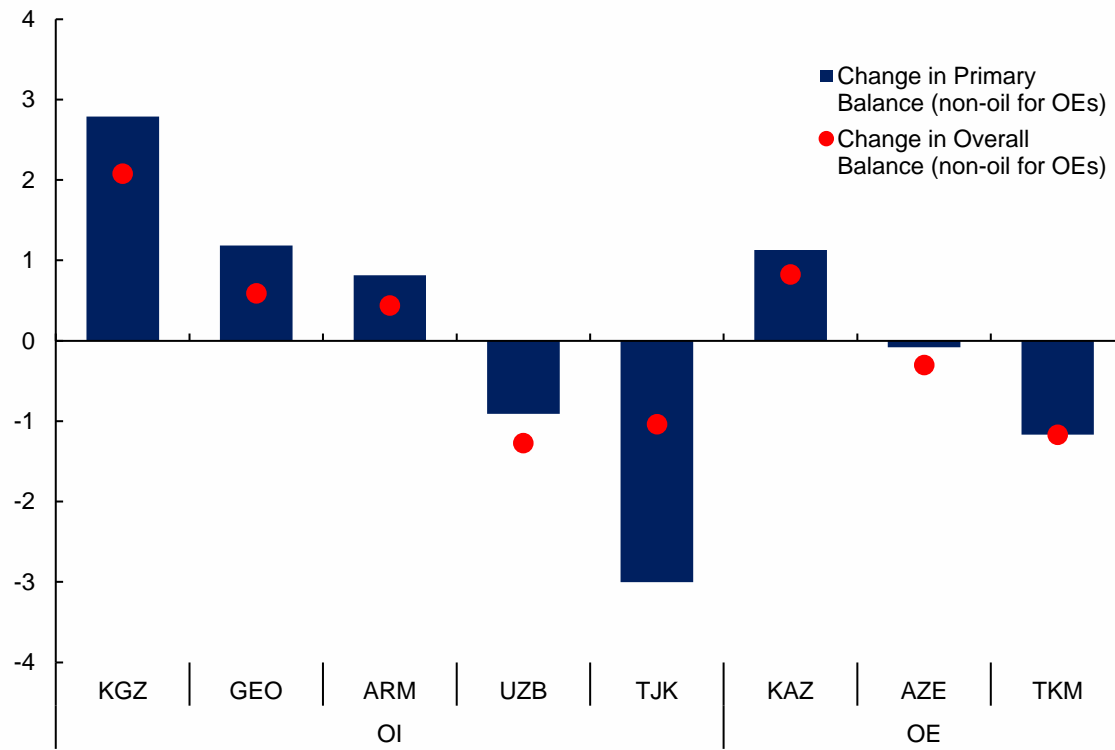
Sources: Haver Analytics; and IMF staff calculations.

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# Some improvement in fiscal balances but weaker external positions

Primary balances strengthened in a few economies

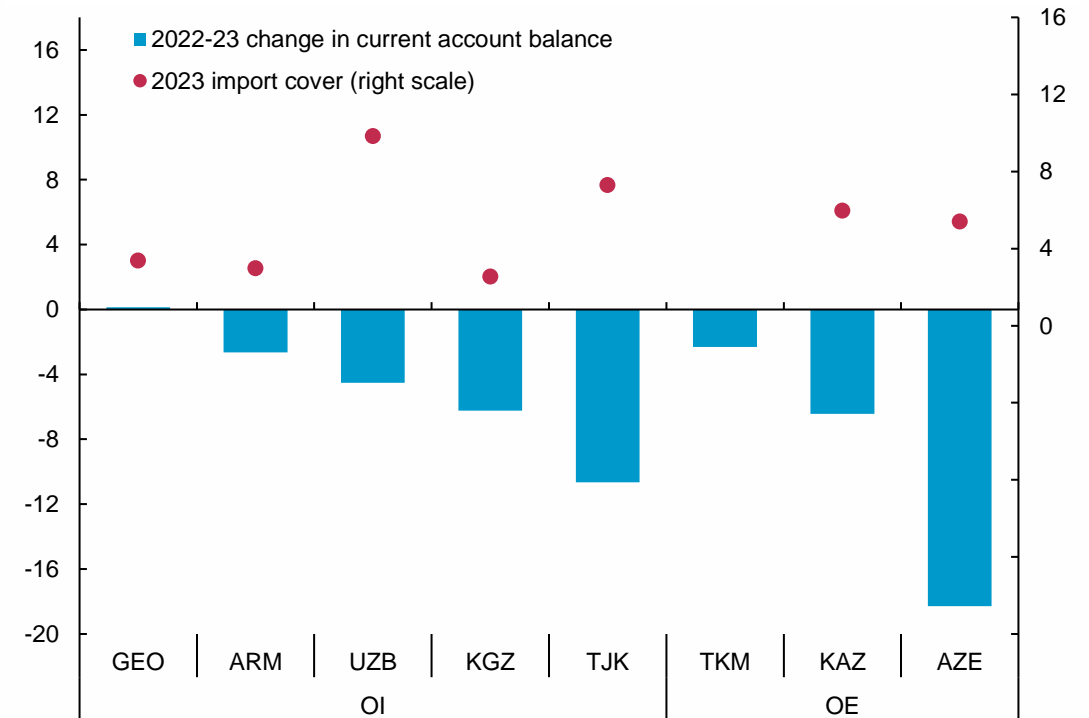
**Change in Primary Balances (excluding grants), 2022-23**  
(Percent of GDP; percent of non-oil GDP for oil exporters, average)



Sources: IMF, World Economic Outlook database; and IMF staff calculations.  
Note: Country abbreviations are International Organization for Standardization country codes. OI = oil importers; OE = oil exporters.

While current account balances deteriorated, reserve positions remained mostly adequate

**Change in Current Account Balance and Import Cover, 2023**  
(Current account balance in percent of GDP, import cover in months of imports covered by reserves)







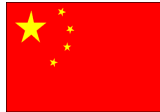



Sources: IMF, World Economic Outlook database; and IMF staff calculations.  
Note: Country abbreviations are International Organization for Standardization country codes. OI = oil importers; OE = oil exporters.



# The Outlook

# Growth Projections

*(percent change from a year earlier)*

								
	World	Advanced Economies	U.S.	Euro Area	China	Russia	Armenia	Emerging Market and Developing Economies
2023	3.3	1.7	2.9	0.4	5.2	3.6	8.3	4.4
Revision from Jul. 2024	0.0	0.1	0.4	-0.1	0.0	0.0	-0.4	0.0
2024	3.2	1.8	2.8	0.8	4.8	3.6	6.0	4.2
Revision from Jul. 2024	0.0	0.1	0.2	-0.1	-0.2	0.4	0.0	0.0
2025	3.2	1.8	2.2	1.2	4.5	1.3	4.9	4.2
Revision from Jul. 2024	-0.1	0.0	0.3	-0.3	0.0	-0.2	-0.4	-0.1

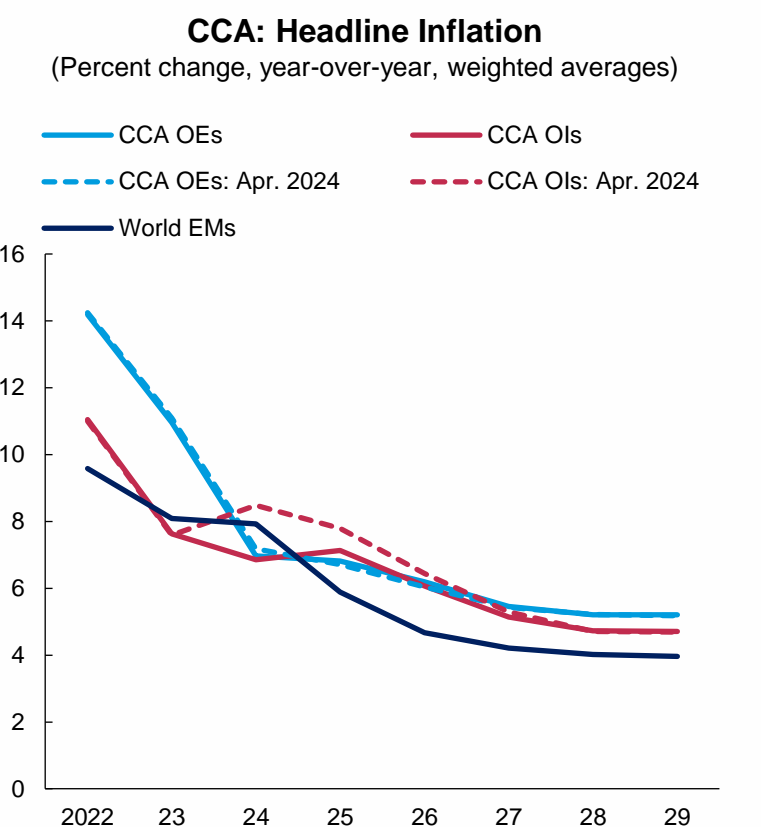
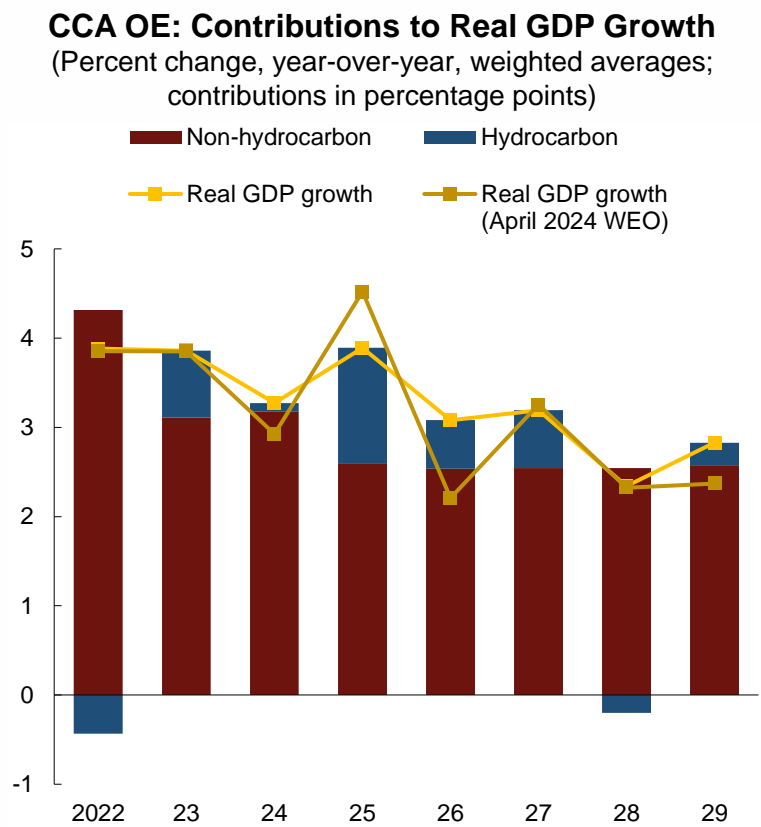
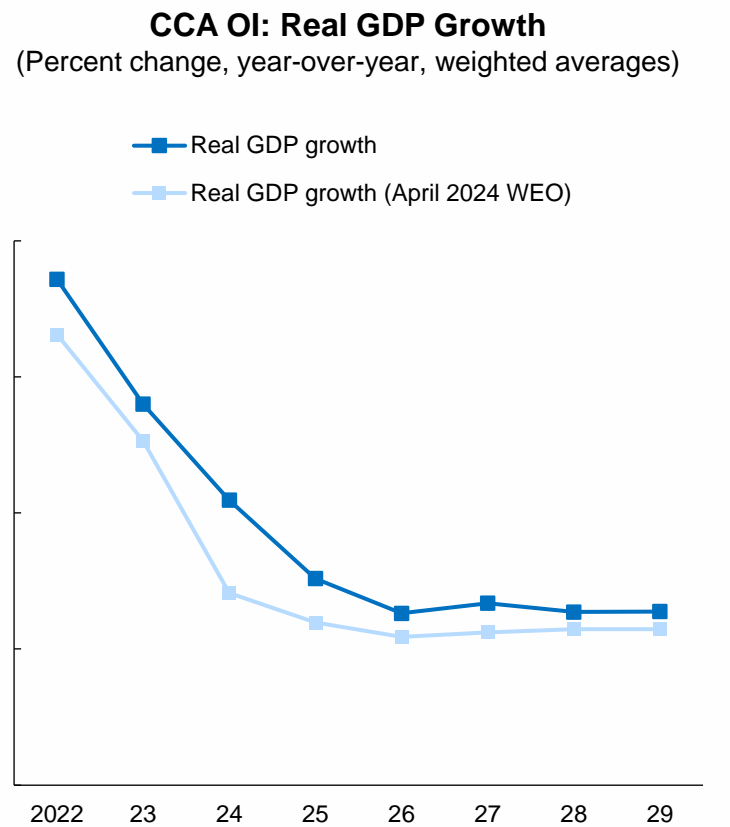
Source: IMF, October 2024 *World Economic Outlook*.

# CCA: Growth is projected to remain robust but moderate over the medium term; Inflation to continue declining

Growth projected to moderate over the medium-term, though reform implementation provides support

Subdued hydrocarbon production is expected to weigh on growth in the medium term for hydrocarbon exporters

Inflation is projected to continue declining



Sources: IMF, *World Economic Outlook* database; and IMF staff calculations.

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# Growth in the CCA is driven less by capital deepening than elsewhere, while labor has been more important

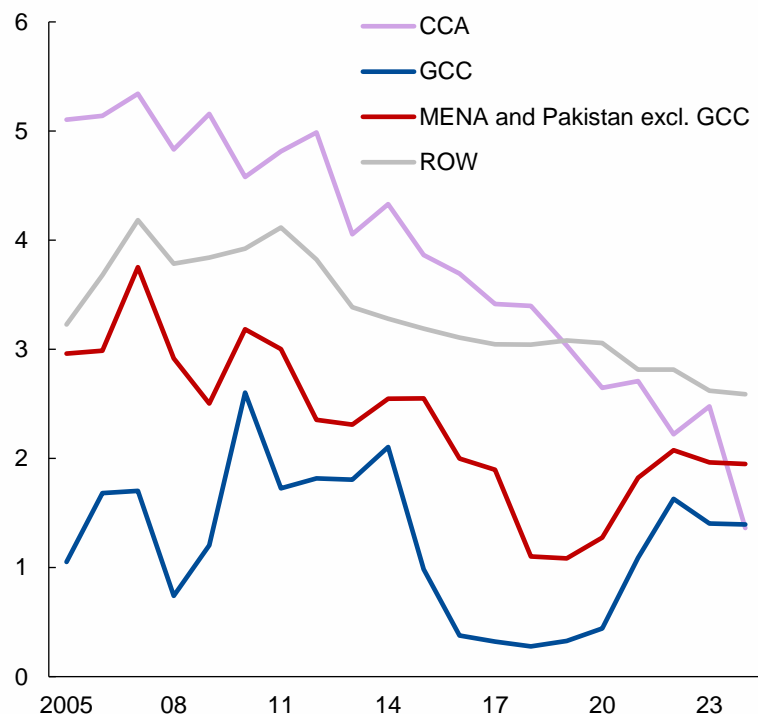
Medium-term growth prospects in the CCA have been deteriorating over the past 15 years

TFP and labor have been key contributors to growth across CCA economies ...

... however, TFP's contribution to growth have declined since the boost following independence in the 1990s

## Five-Year-Ahead Real GDP per Capita Projections

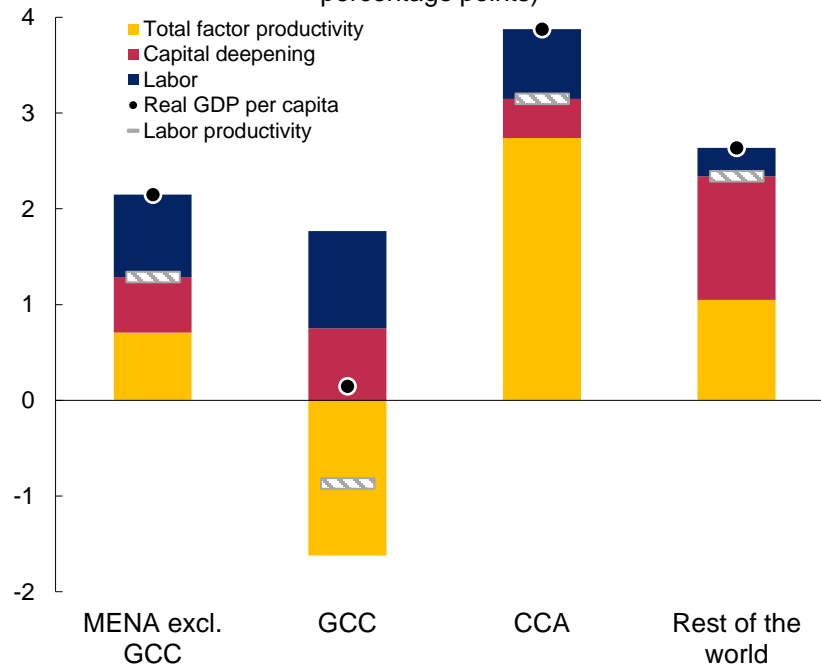
(Year-over-year percent change)



Sources: IMF, World Economic Outlook database; and IMF staff calculations.  
Note: Countries weighted using purchasing power in international dollar weights.  
CCA = Caucasus and Central Asia; GCC = Gulf Cooperation Council; MENA = Middle East and North Africa; ROW = rest of the world.

## Contributions to Real GDP per Capita Growth, 1995-2023

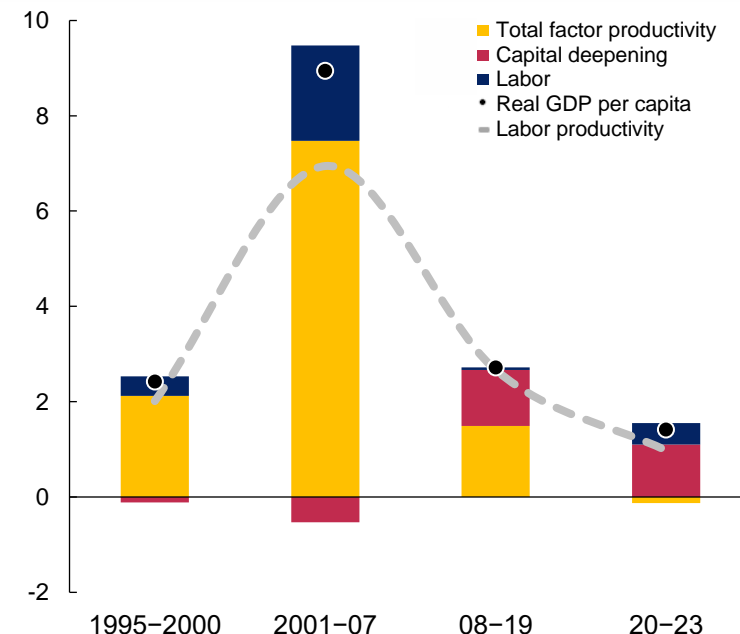
(Average year-over-year percent change; contributions in percentage points)



Sources: International Labour Organization; Penn World Table version 10.01; United Nations, World Population Prospects; and IMF staff calculations.  
Note: Countries within group weighted using purchasing power in international dollar weights. Contributions of capital deepening and employment per capita reflect the shares of the respective factor inputs in output and their growth rates. Labor productivity is real GDP per employed worker.

## CCA: Contributions to Real GDP per Capita Growth

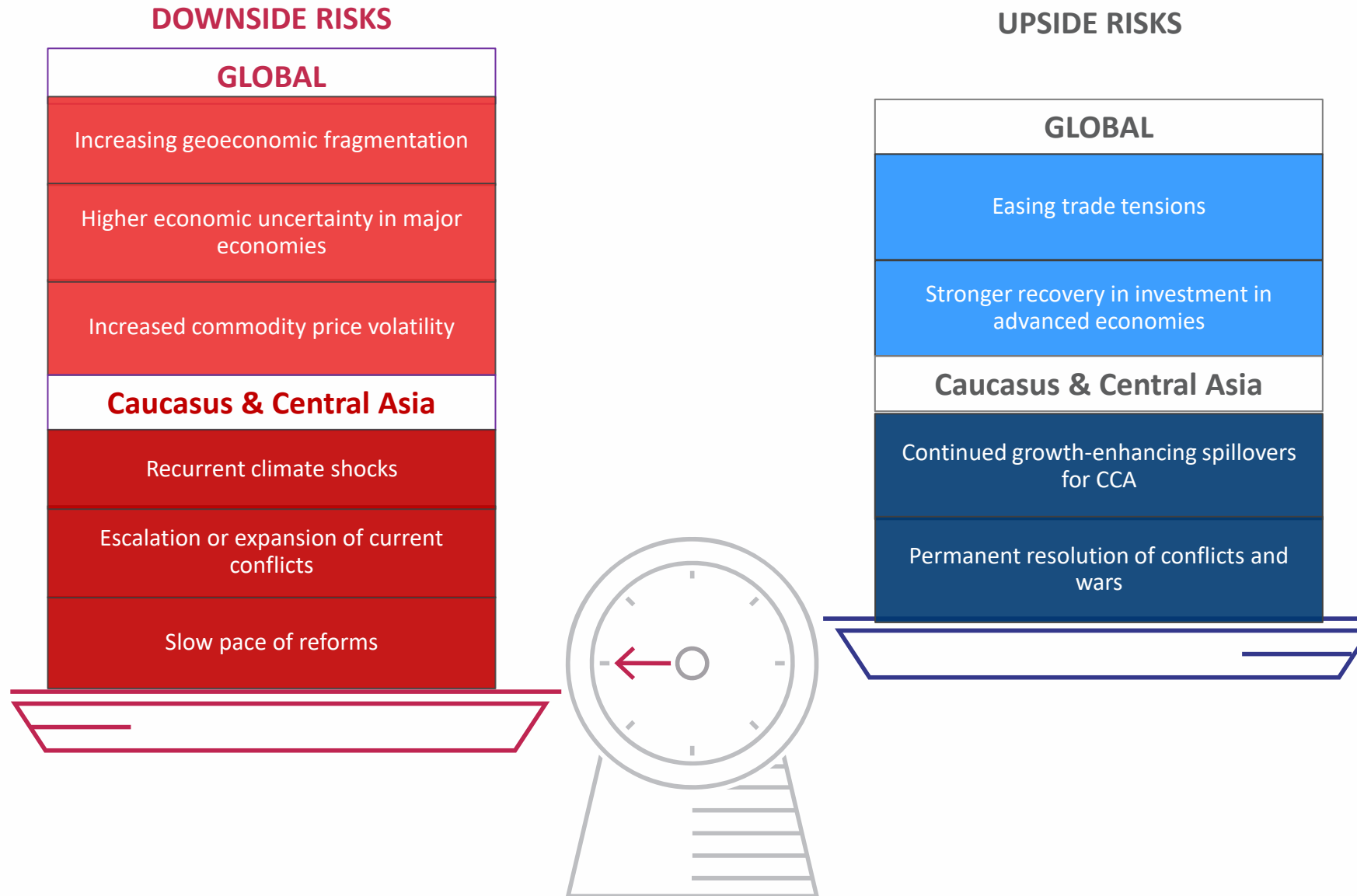
(Average year-over-year percent change; contributions in percentage points)



Sources: International Labour Organization; Penn World Table version 10.01; United Nations, World Population Prospects; and IMF staff calculations.  
Note: CCA sample comprises Armenia, Kazakhstan, and the Kyrgyz Republic.

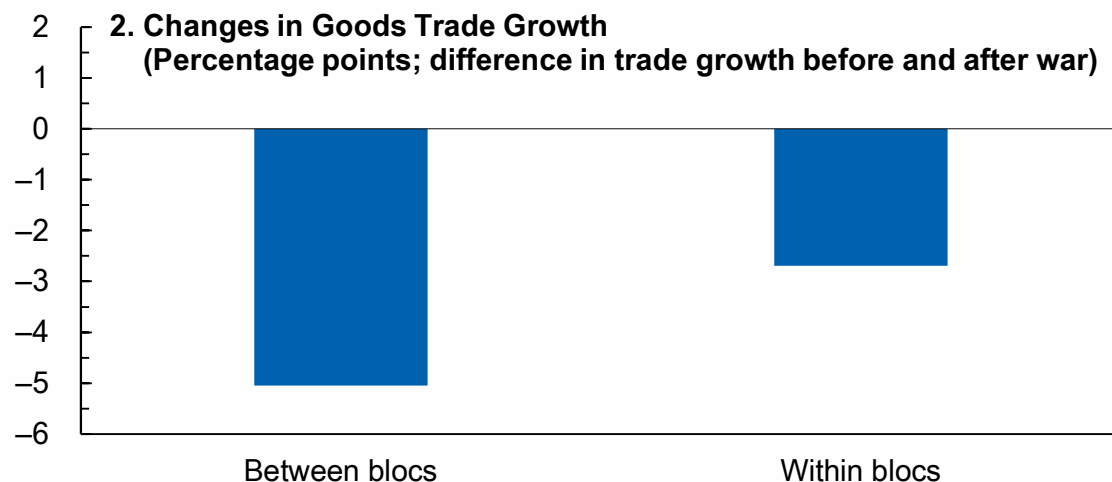
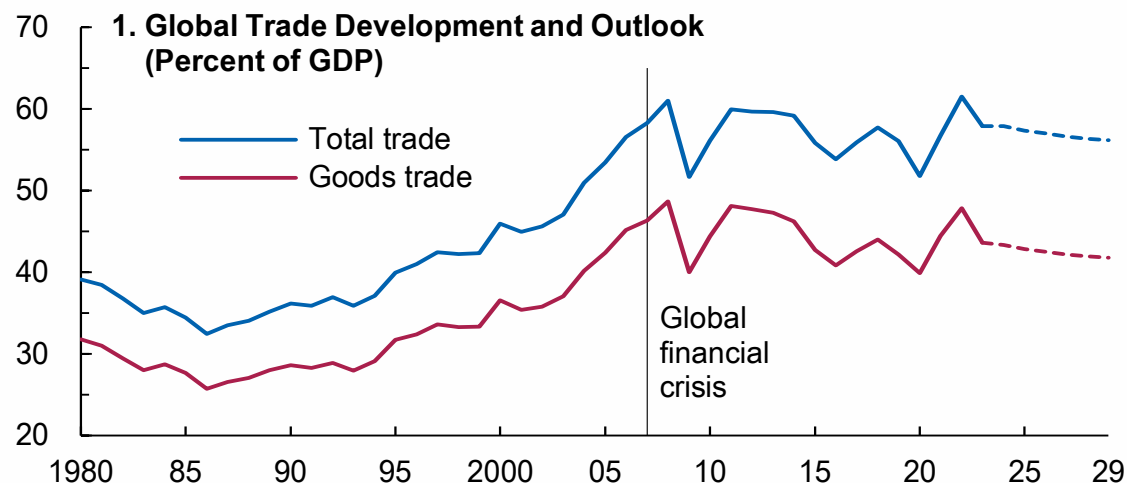
# Risks

# Uncertainty surrounding the outlook is high and risks are tilted to the downside

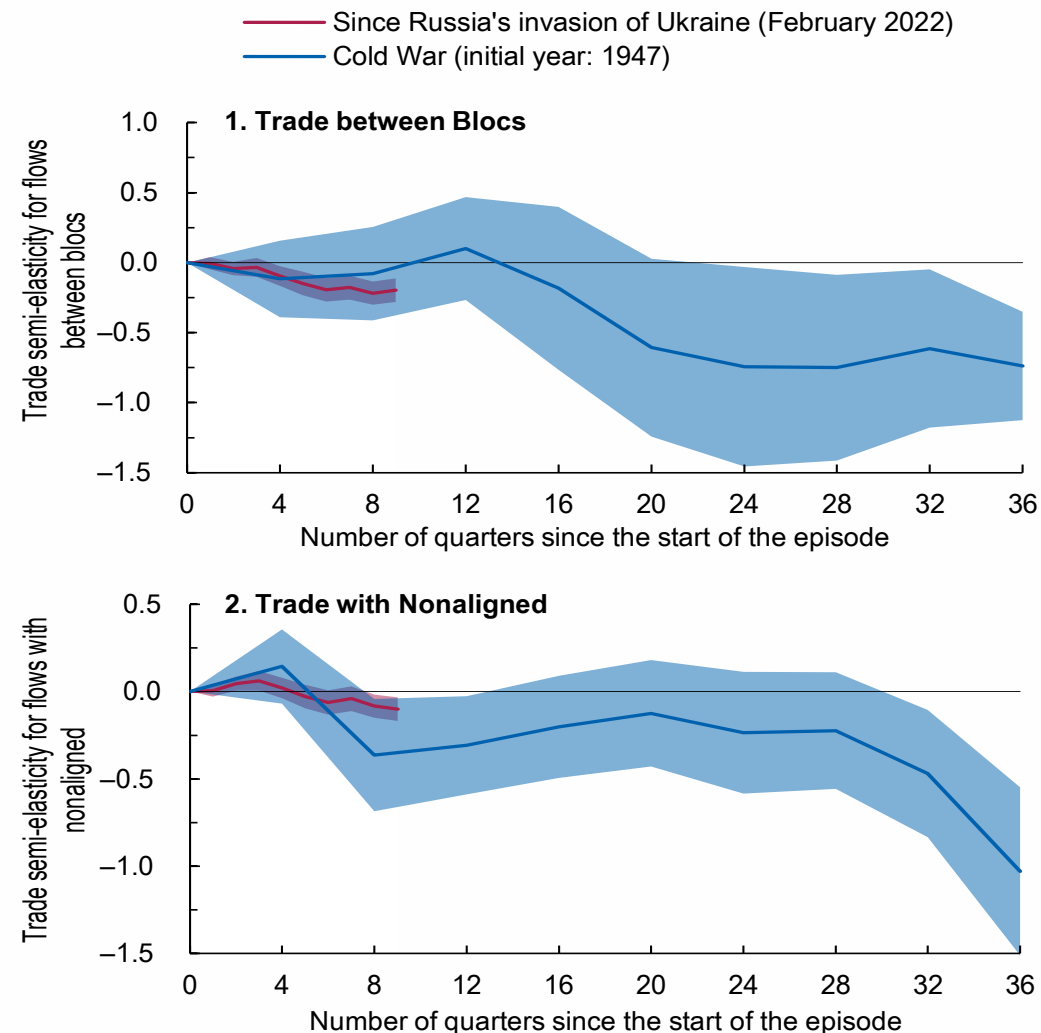


# Global trade stable, fragmentation starting to emerge

## Globalization and Trade Fragmentation



## Trade Fragmentation: Cold War and Now



Sources: Gopinath, Gourinchas, Presbitero, and Topalova (2024); and IMF staff calculations.

Note: The right figure plots the change in global trade between blocs (panel 1) and with nonaligned countries (panel 2) during the Cold War (blue line, with  $t_0 = 1947$ ) and since Russia's invasion of Ukraine (red line, with  $t_0 = 2021:Q4$ ).



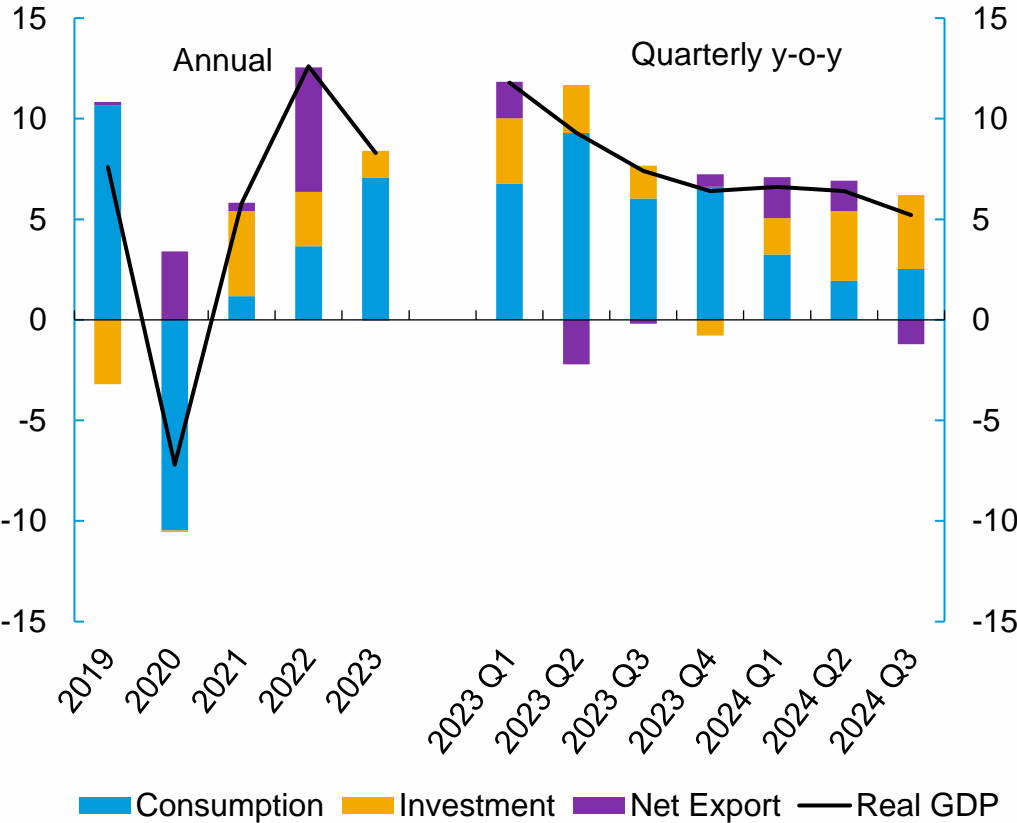




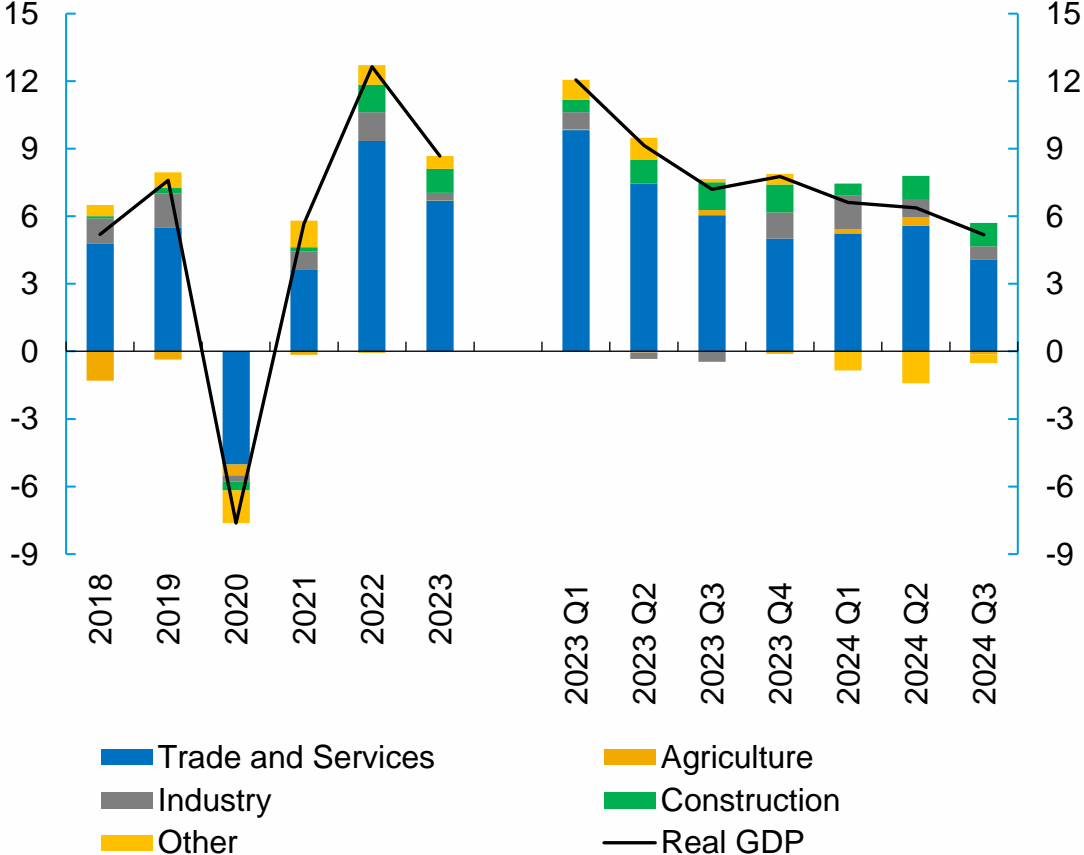
# Armenia: Recent Economic Developments

# Armenia: Growth remains strong but is gradually normalizing

Contributions to Real GDP Growth  
by Expenditure Components  
(Percent and percentage points)



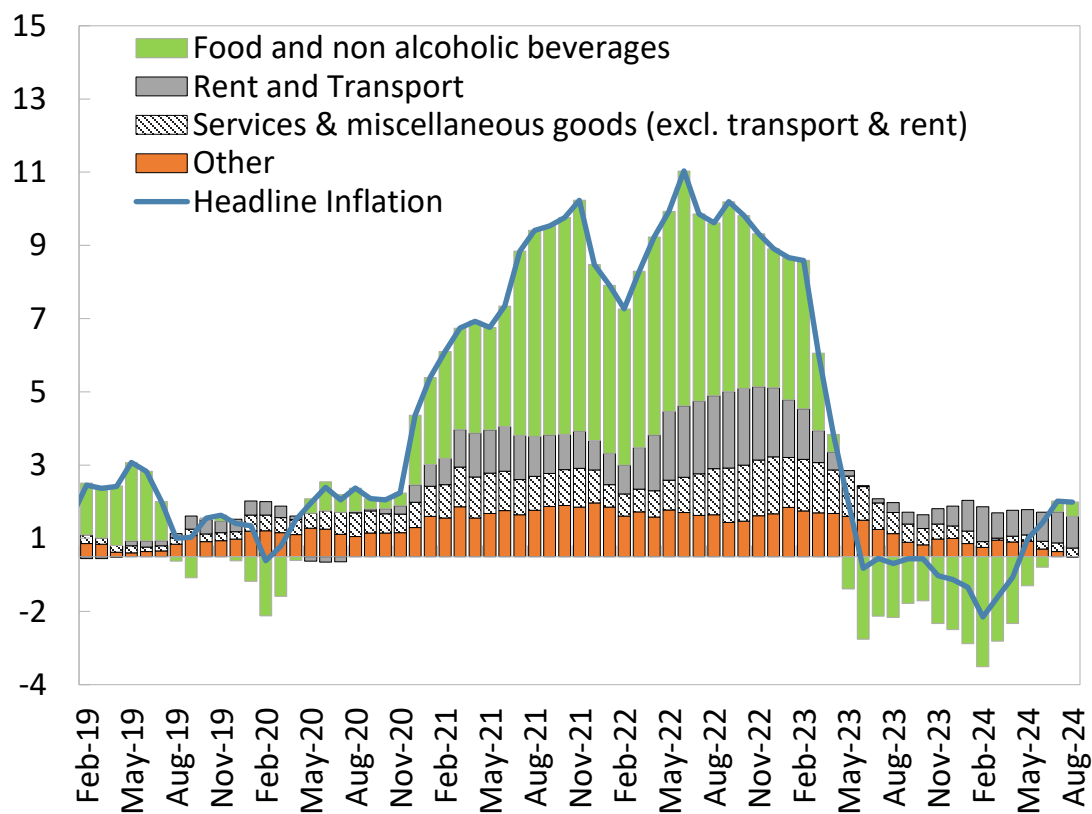
Contributions to Real GDP Growth by  
Sector  
(Percent and percentage points)



Source: RA NSC and IMF

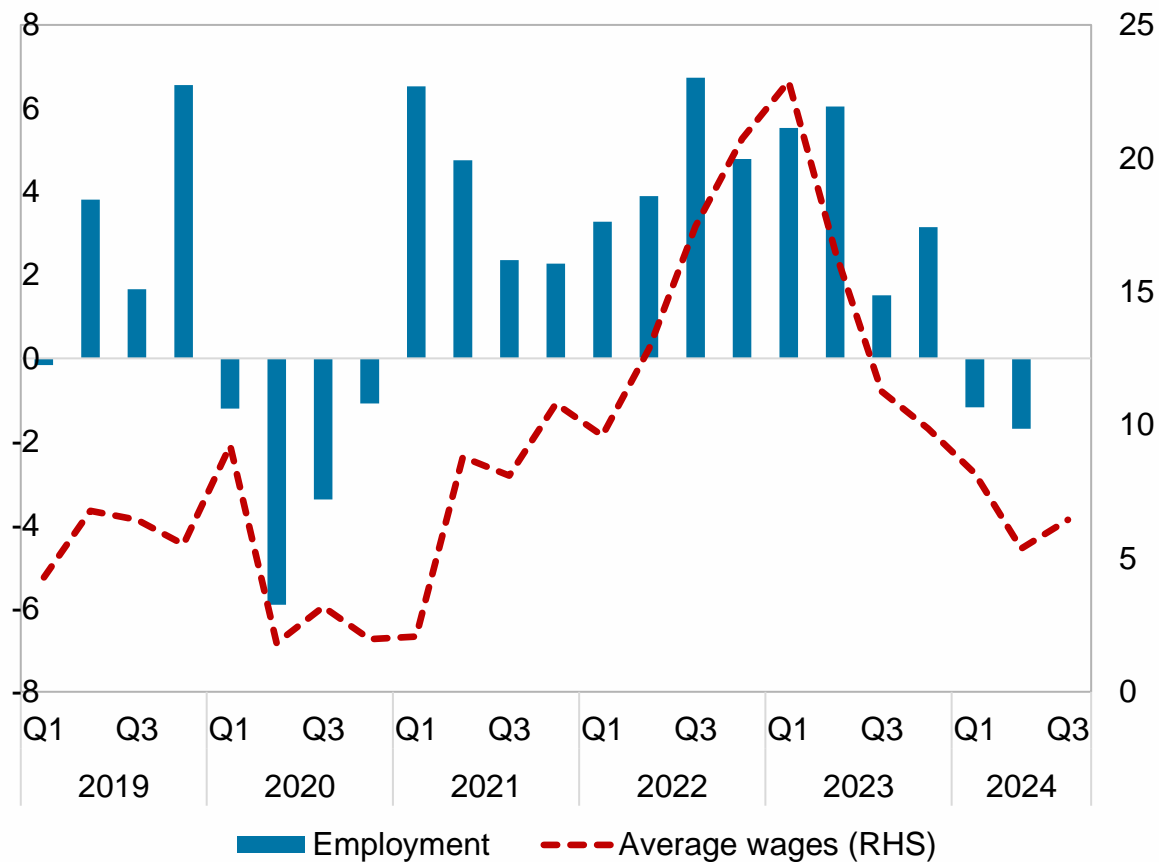
# Inflation remains subdued amid contained wage pressures

Armenia: Contributions to Inflation  
(Percent, y-o-y)



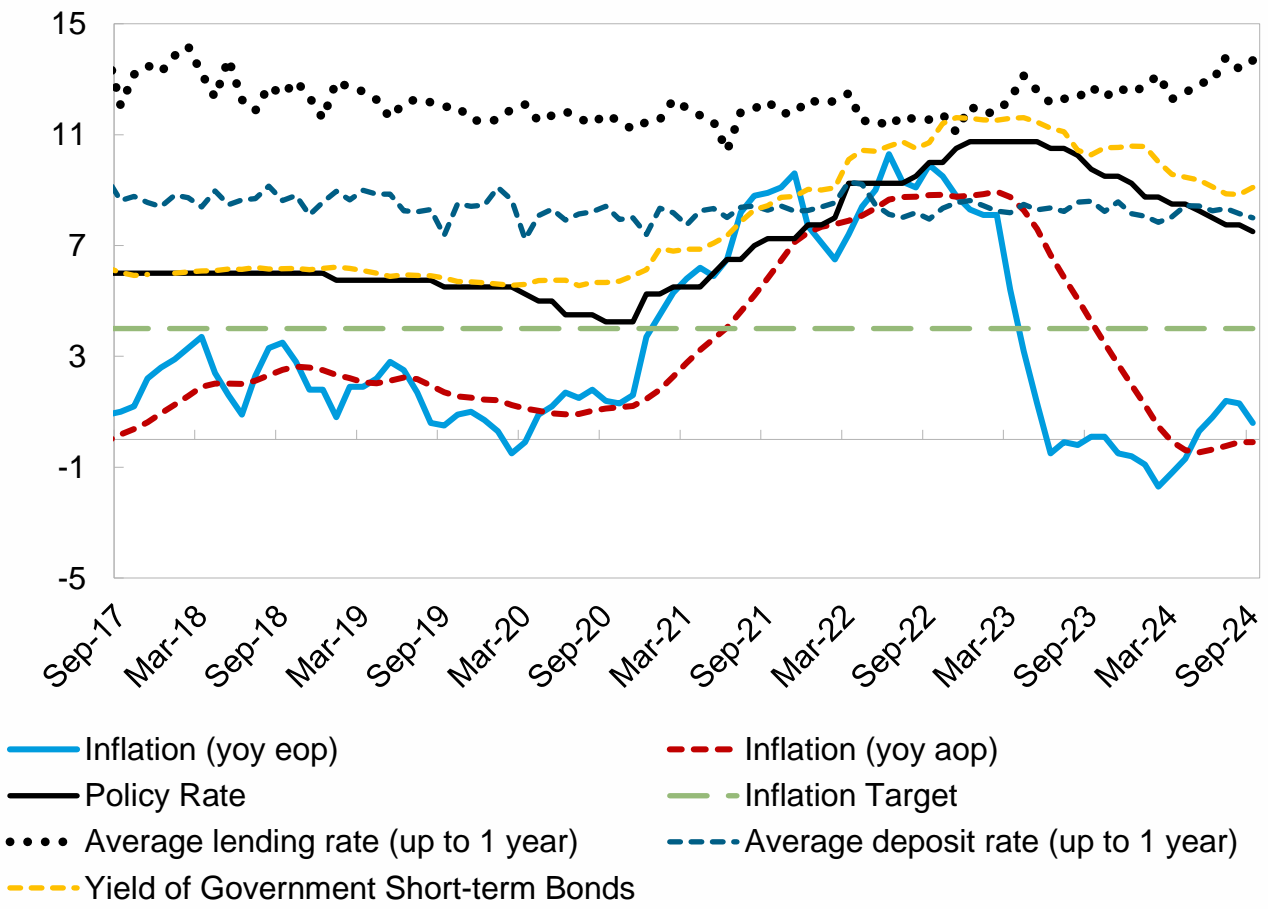
Source: Haver.

Nominal Wage and Employment Growth  
(Percent, y-o-y)

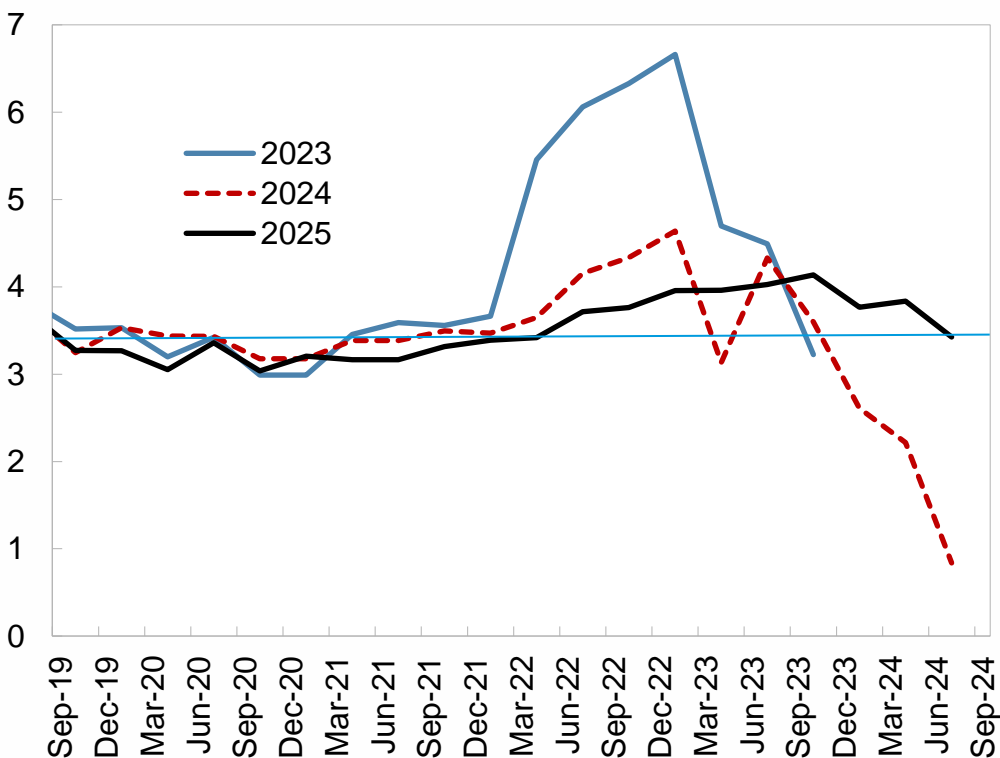


# Gradual monetary policy normalization has been appropriate and data-driven

Inflation and Policy/Interest Rates  
(Percent)

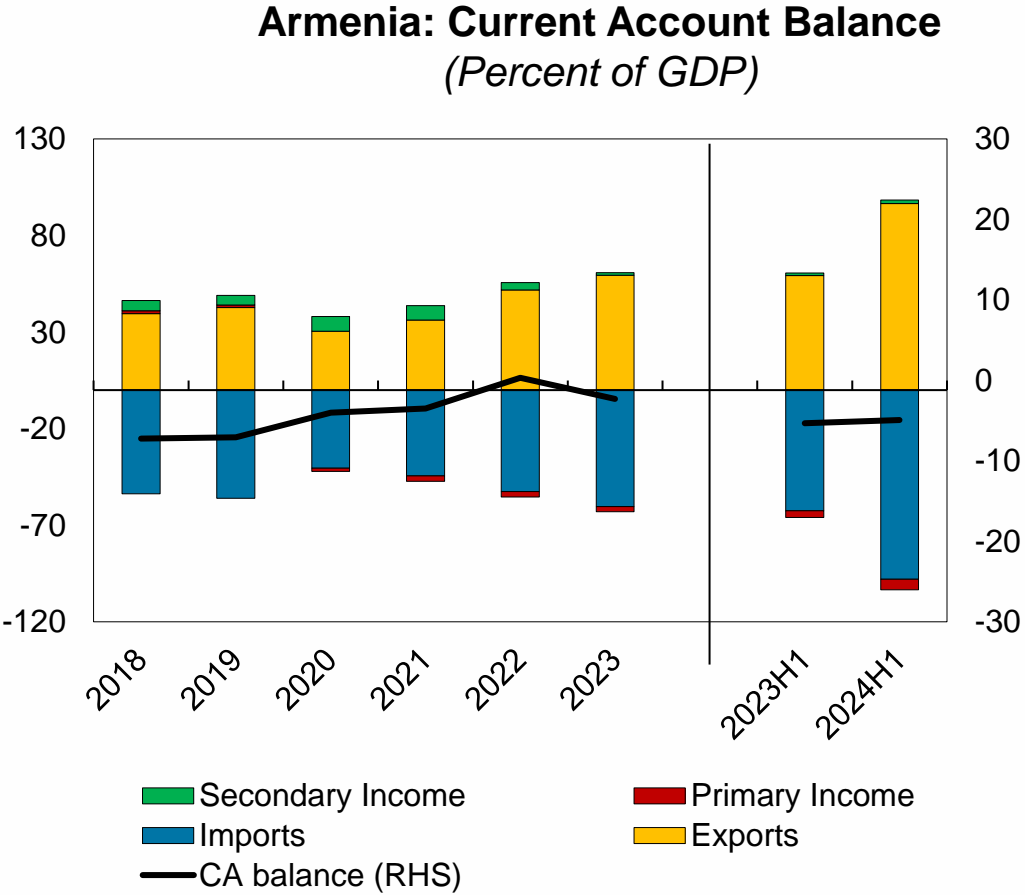


Inflation Expectations  
(Percent, eop)

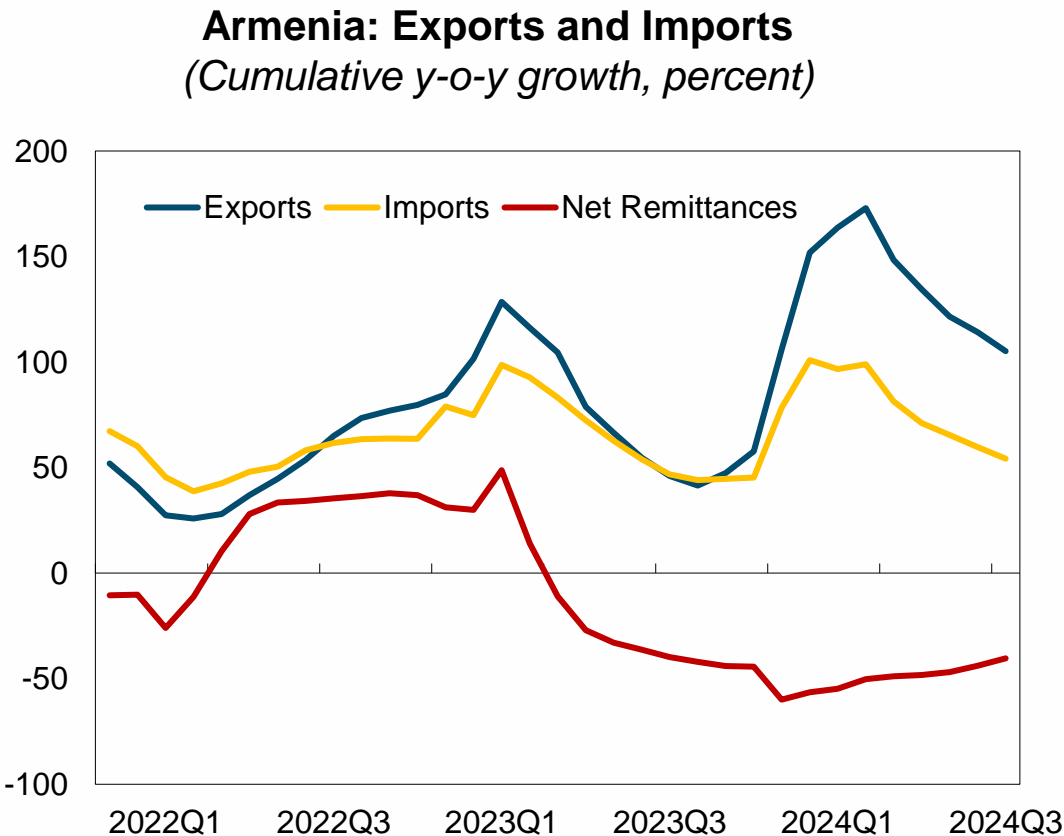


Source: Consensus Economics Forecasts.

# The current account has turned into a moderate deficit as transitory factors dissipate



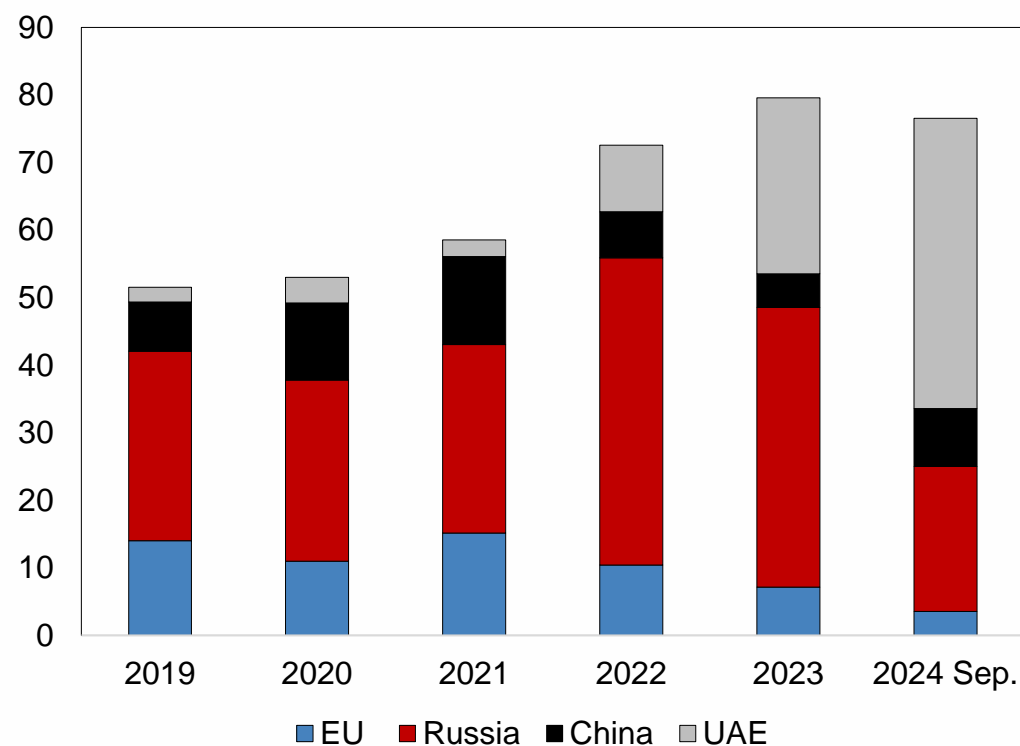
Source: Armstat and IMF staff calculations.



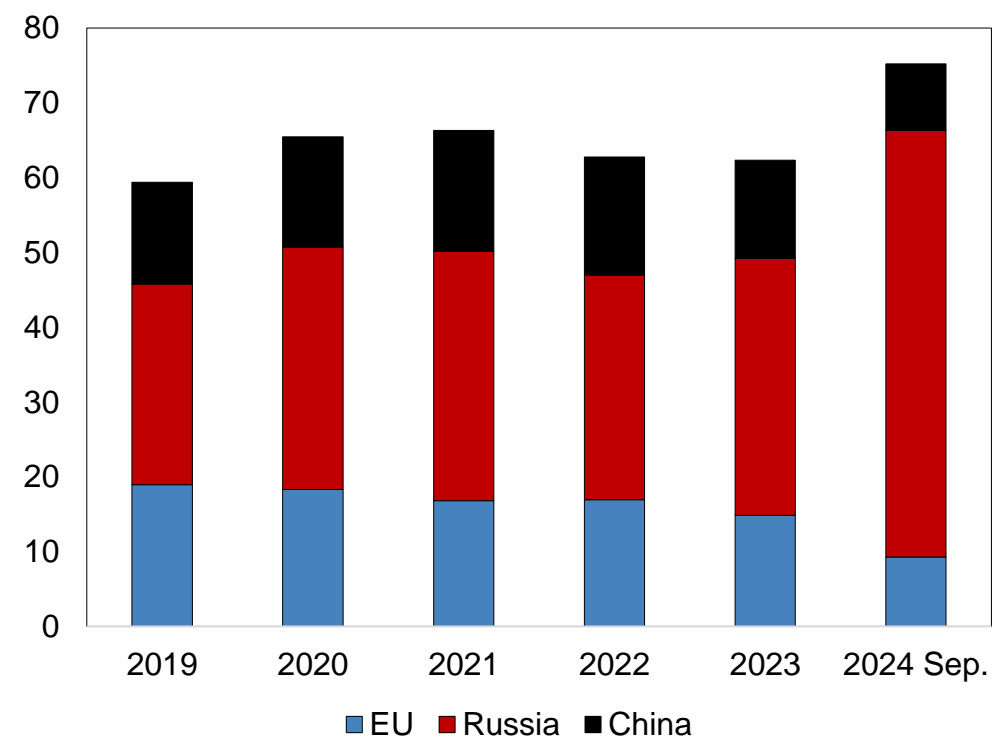
Source: Armstat and IMF staff calculations.

# Recent increase in trade is driven by gold transit trade between Russia and UAE

Armenia: Main export destinations  
(percent in total)



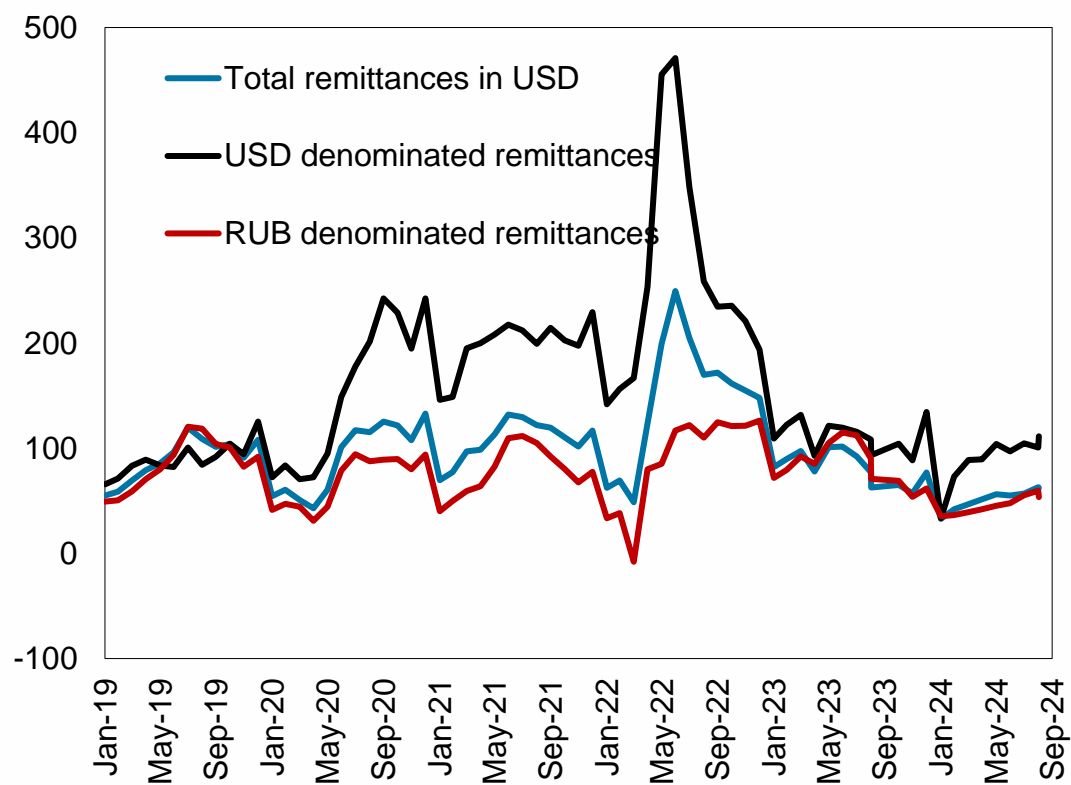
Armenia: Main import destinations  
(percent in total)



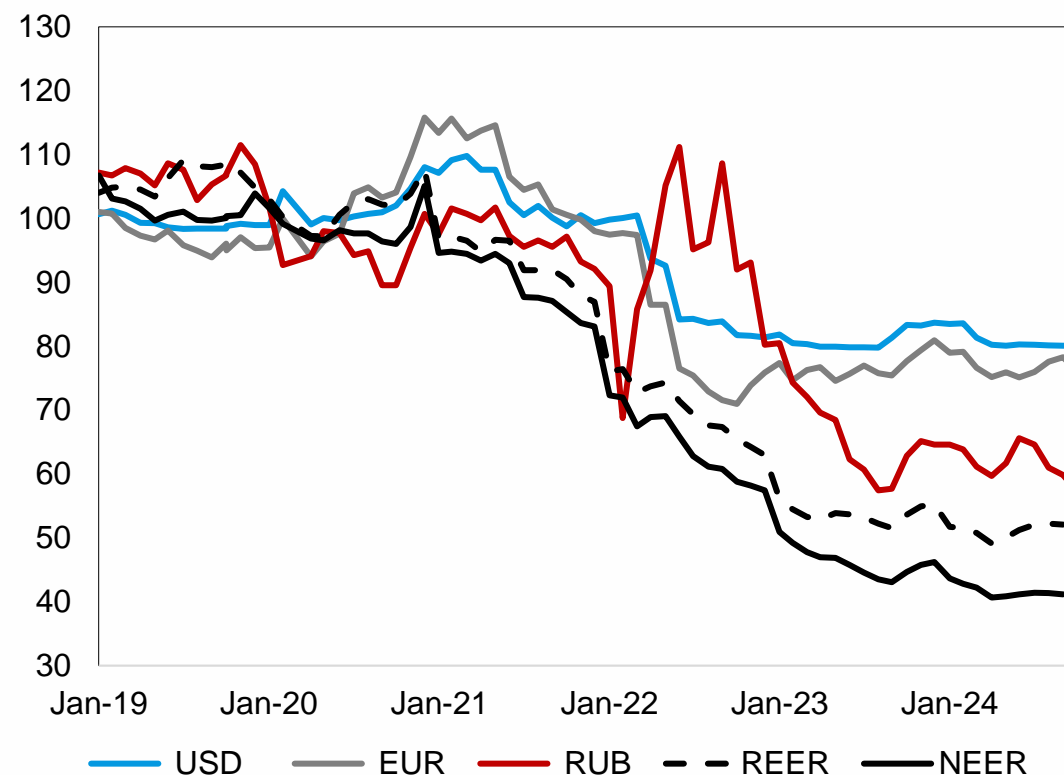
Source: Armstat and IMF staff calculations.

# Remittances and exchange rates

**Armenia: Remittances**  
(index, 2018 Dec=100)



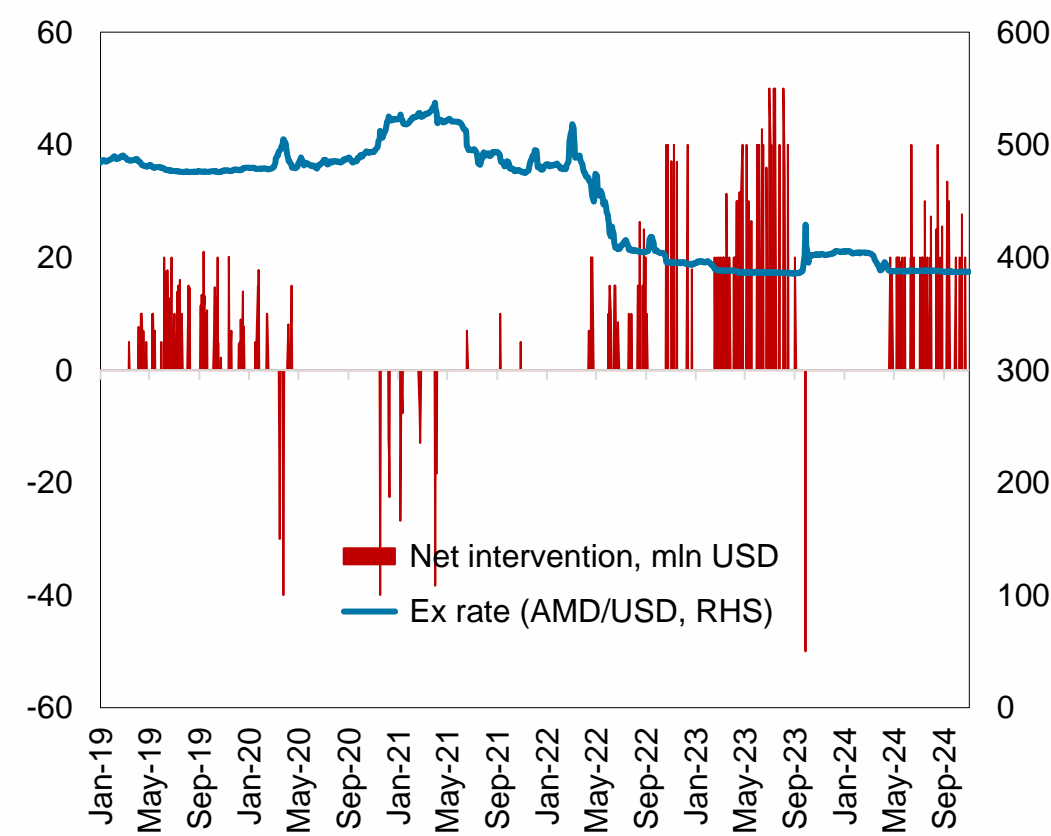
**Armenia: Exchange Rates**  
(index, 2018 Dec=100)



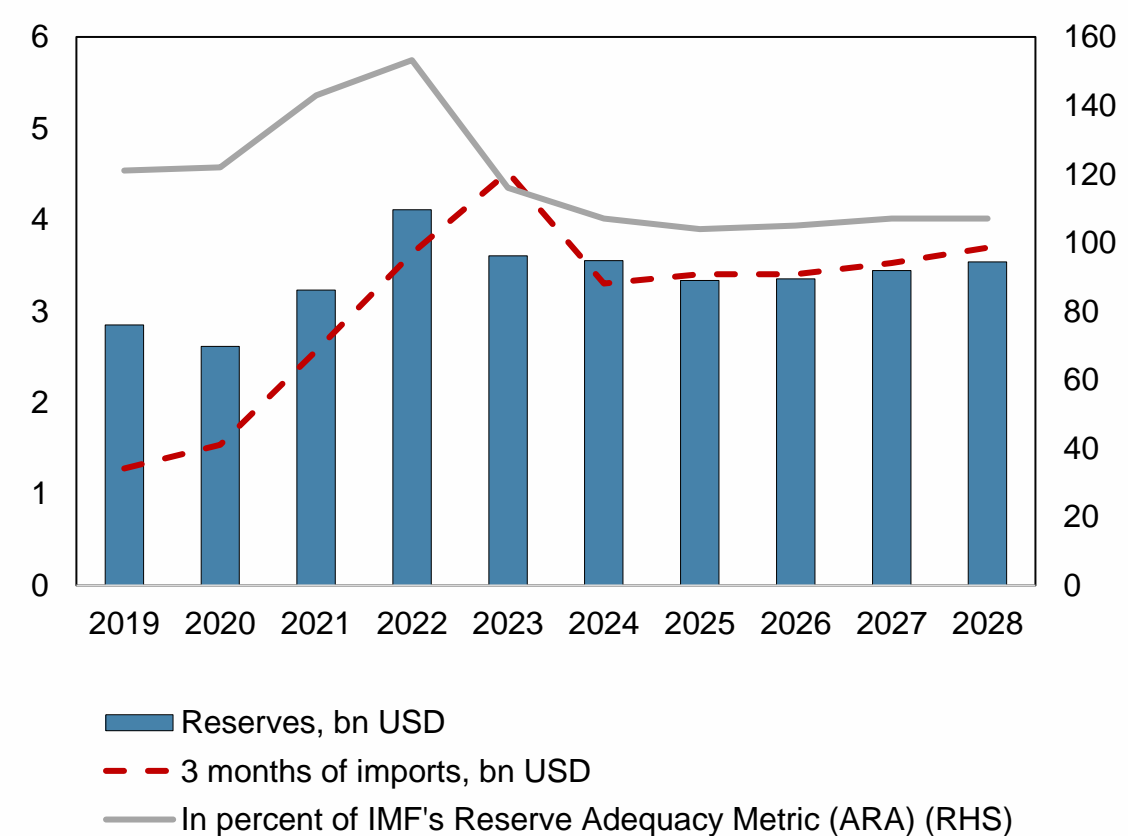
Source: CBA and IMF staff calculations.

# Reserve coverage remains adequate

FX Intervention and Exchange Rate



Reserve Adequacy Metrics

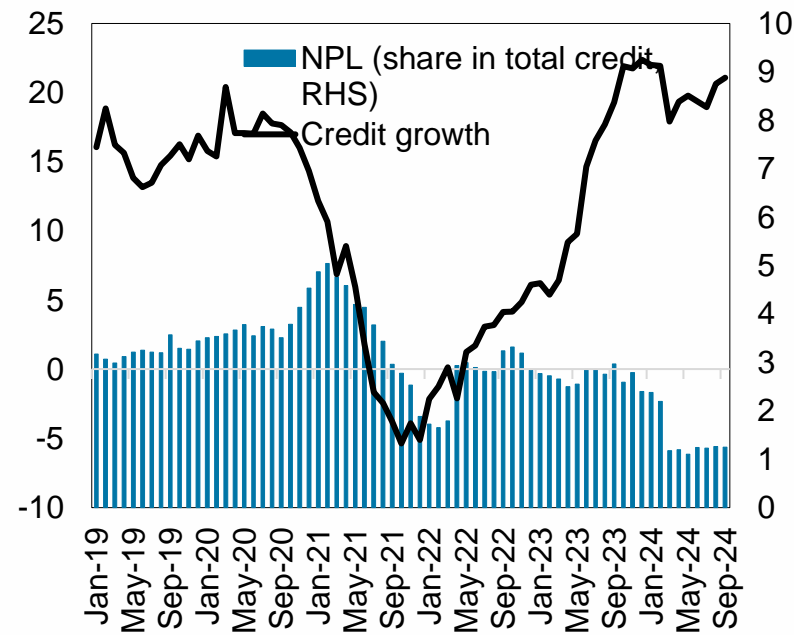


Source: CBA and IMF staff calculations.

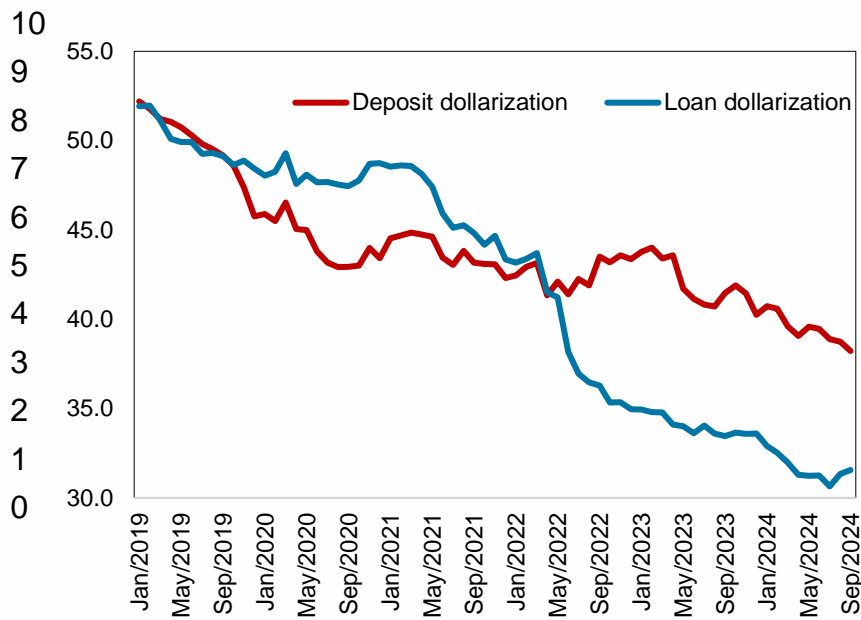


# Financial soundness indicators are solid, but a pickup in credit growth warrants monitoring

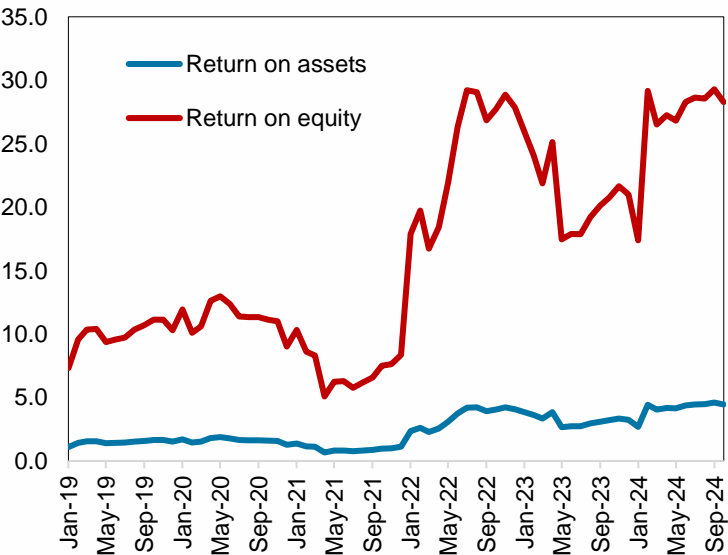
Credit growth and NPL  
(Percent)



Dollarization  
(Percent)



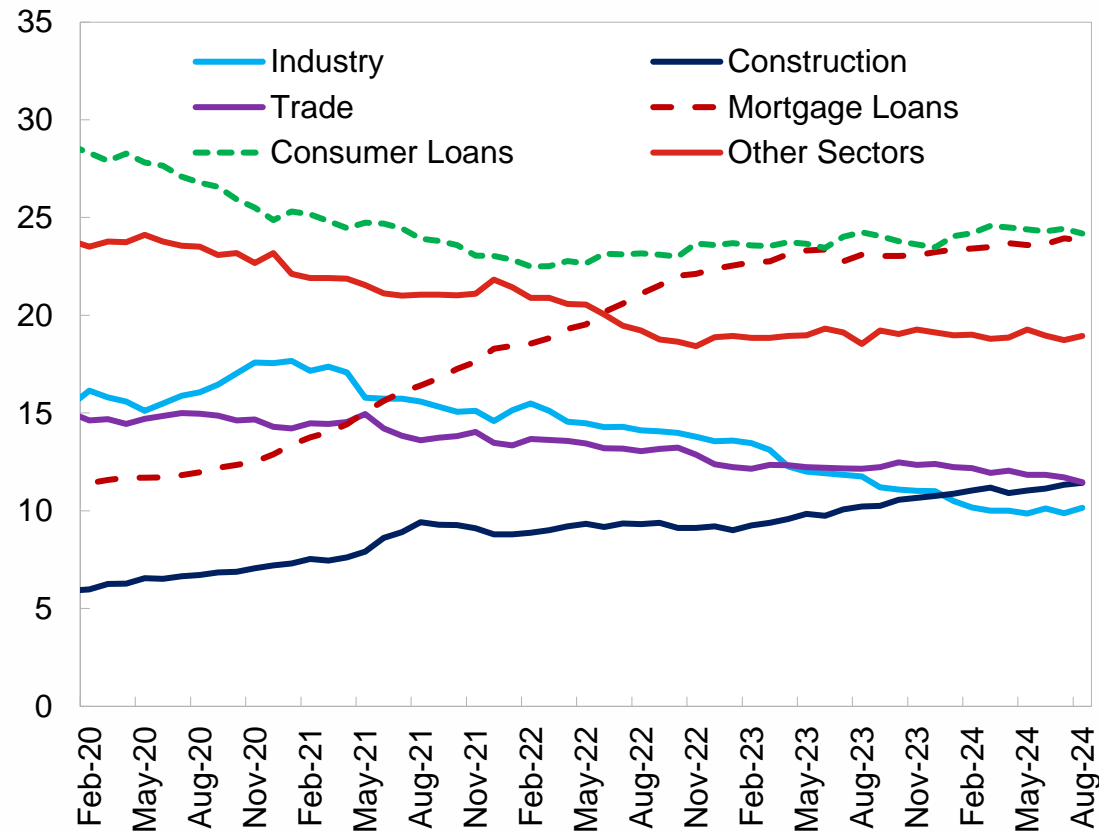
Banking Sector Profitability  
(Percent)



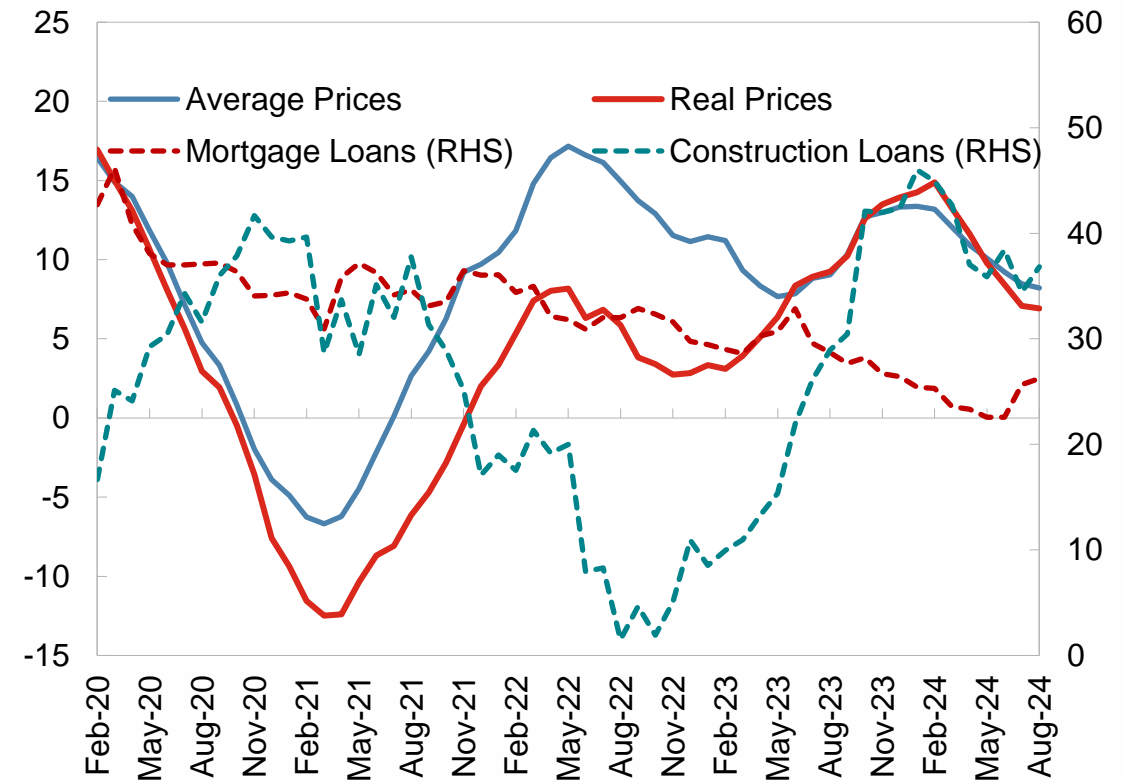
Source: CBA and IMF staff calculations  
Note: Dollarization is calculated for residents

# Credit growth concentrated in the real estate sector with prolonged overvalued house prices in Yerevan

**Sectoral Distribution of Loans**  
(In percent of total)



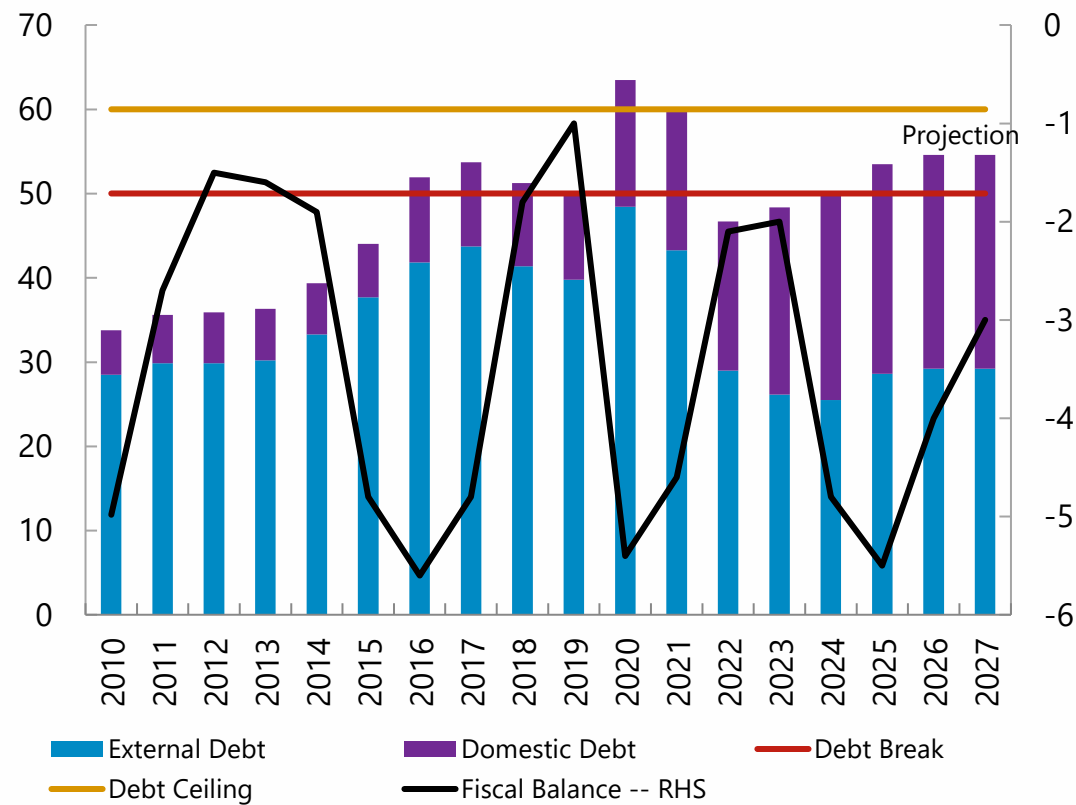
**Average Apartment Price in Yerevan**  
(Percent, Y-o-Y change)



Sources: CBA, ARMSTAT and IMF staff calculations.

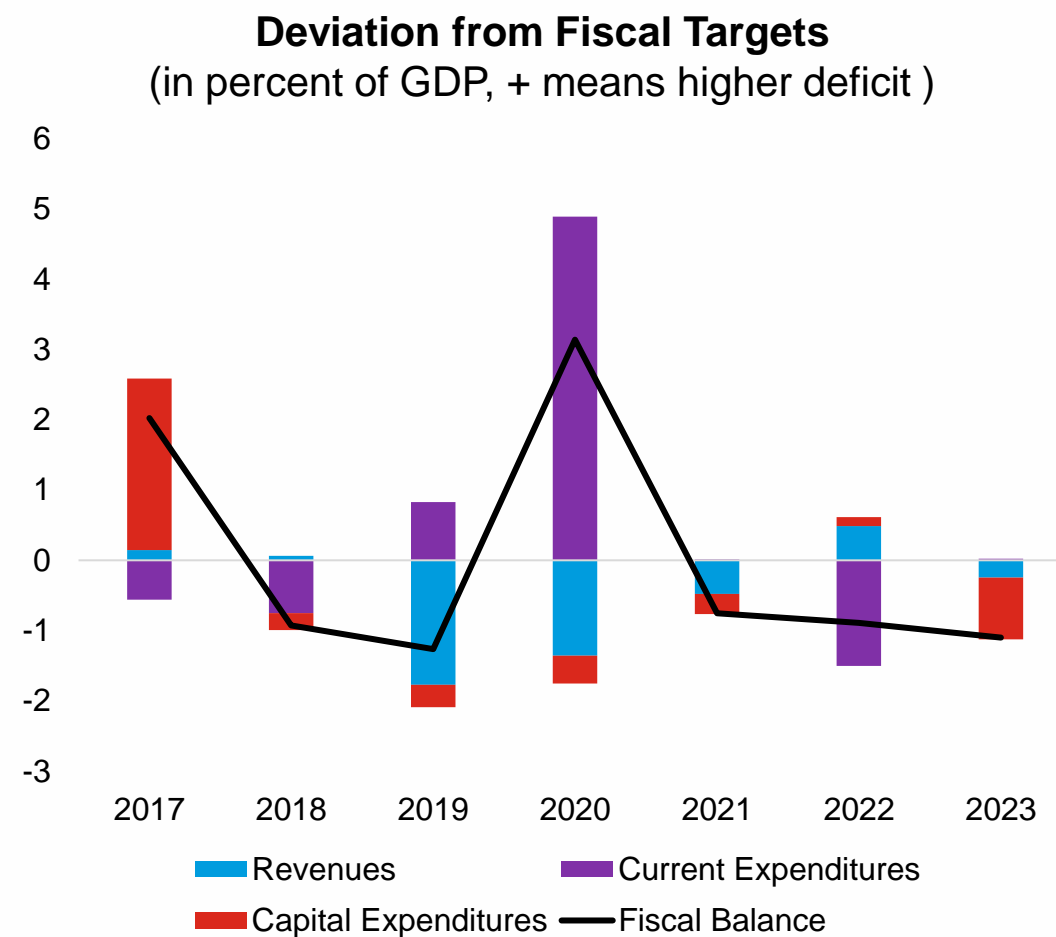
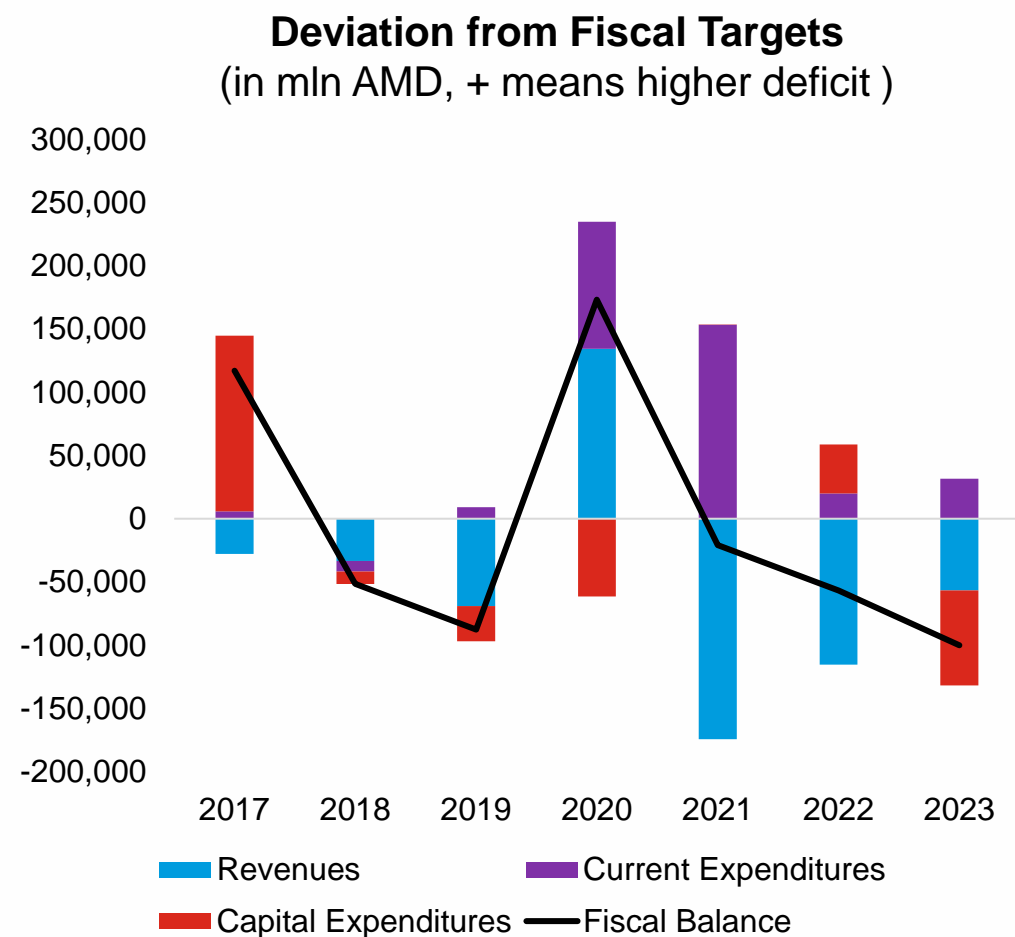
# Fiscal policy consolidation is needed to keep debt moderate in the medium term

Central Government Debt and Fiscal Balance  
(Percent of GDP)



Source: RA Ministry of Finance and IMF staff calculations.

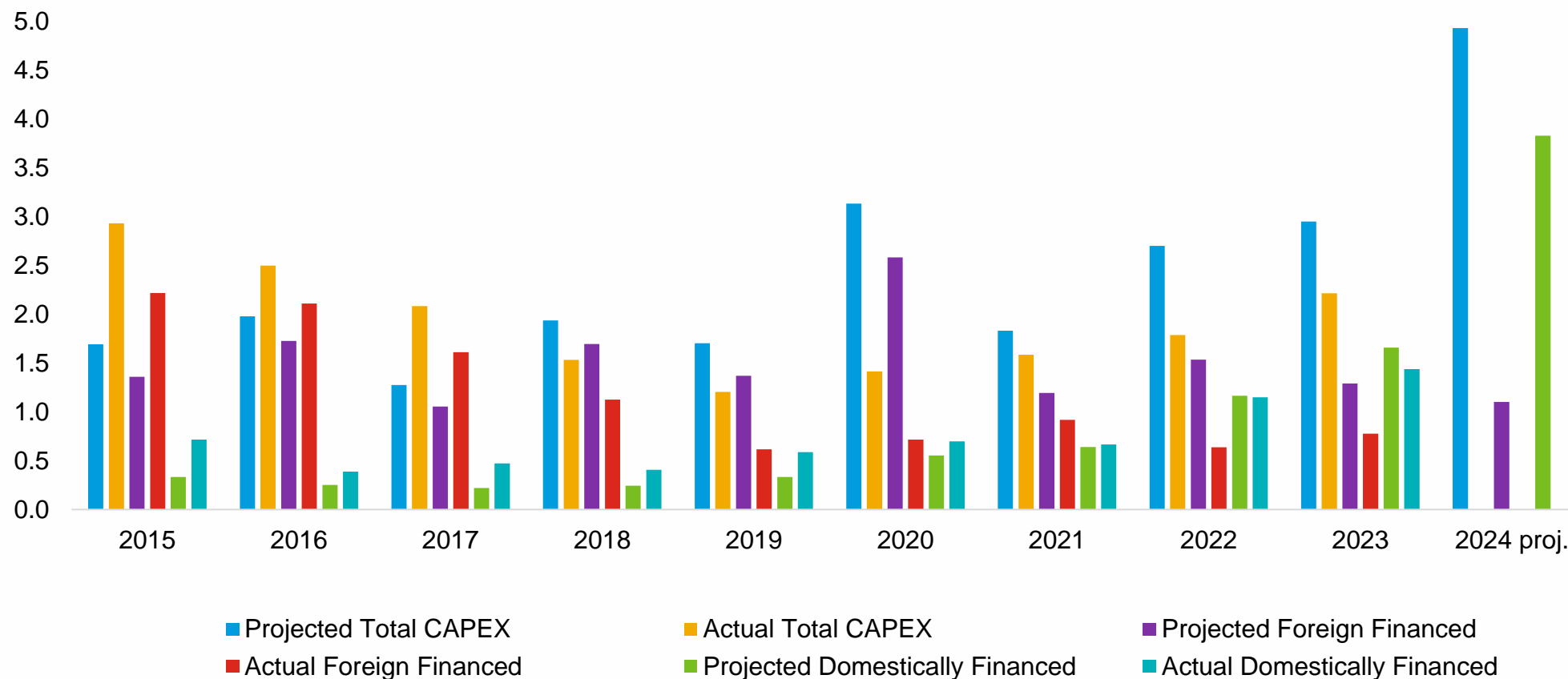
# Fiscal policy has been countercyclical



Source: RA Ministry of Finance and IMF staff calculations.

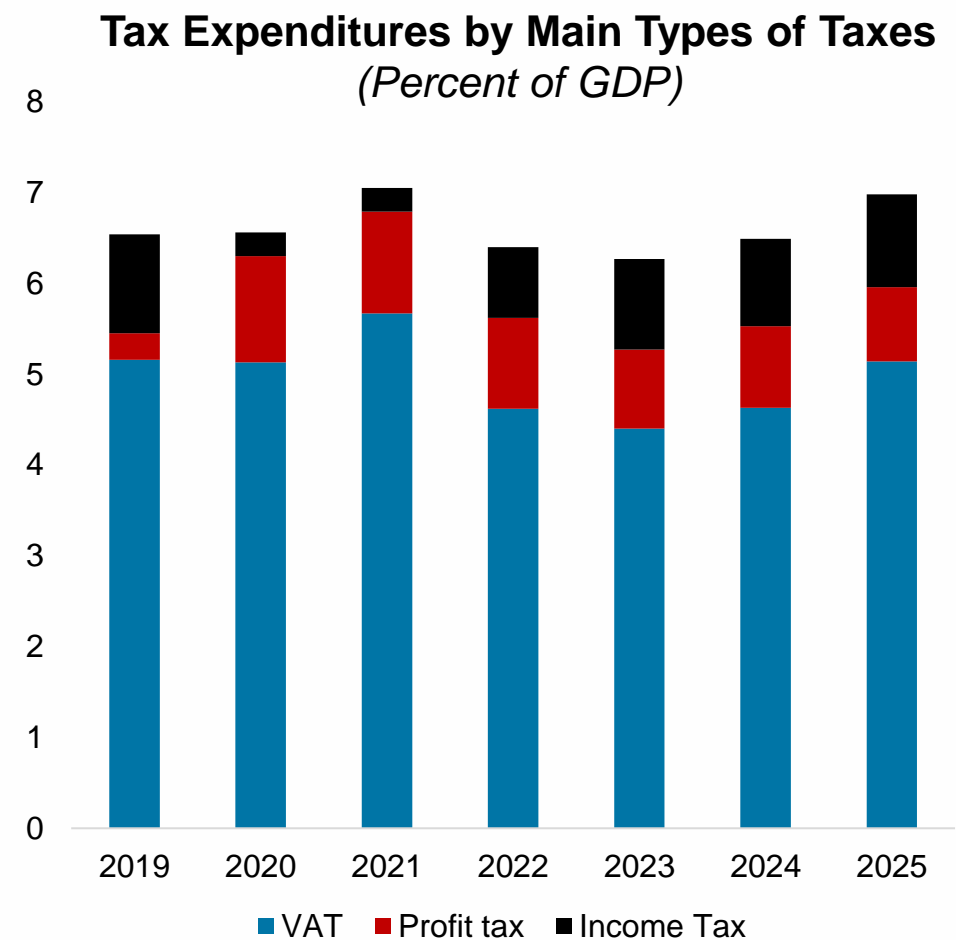
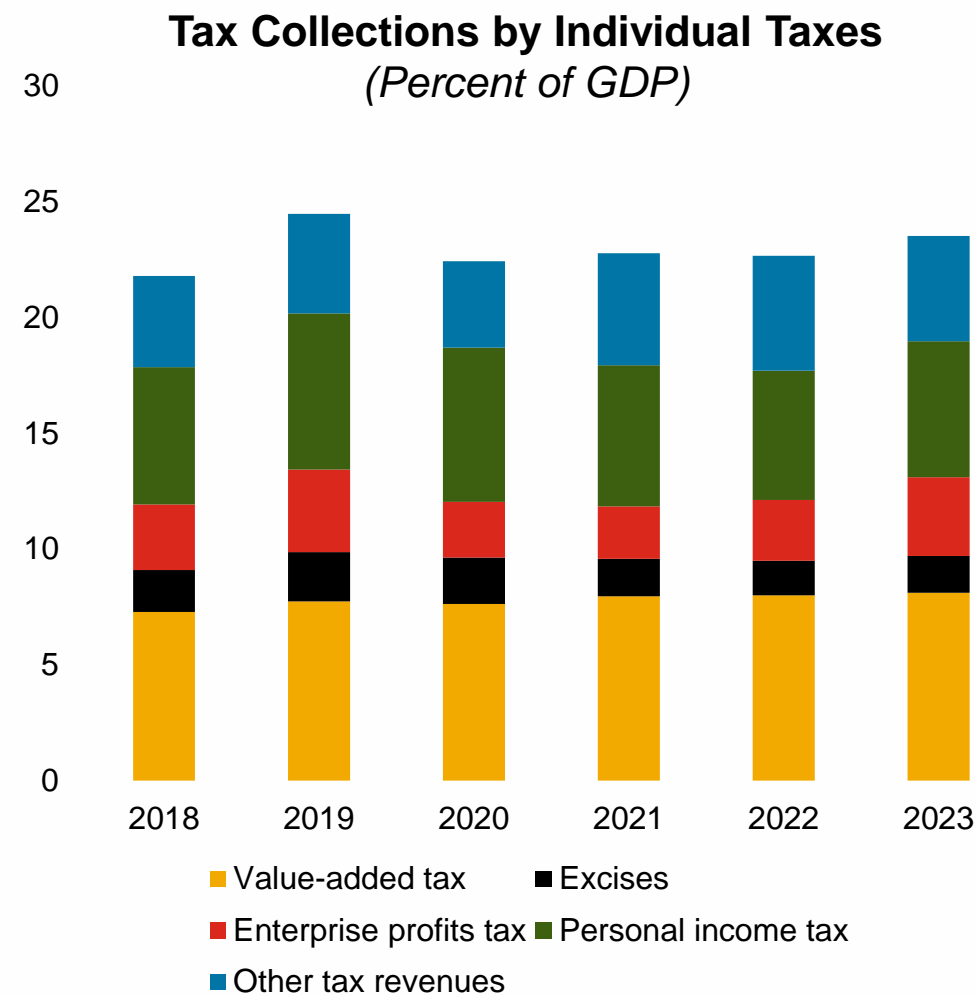
# Under-execution of capital expenditure persists driven mainly by foreign financed projects

Capital Expenditures by Sources of Financing  
(in percent of GDP)



Source: RA Ministry of Finance and IMF staff calculations. Defense capital expenditures are not included.

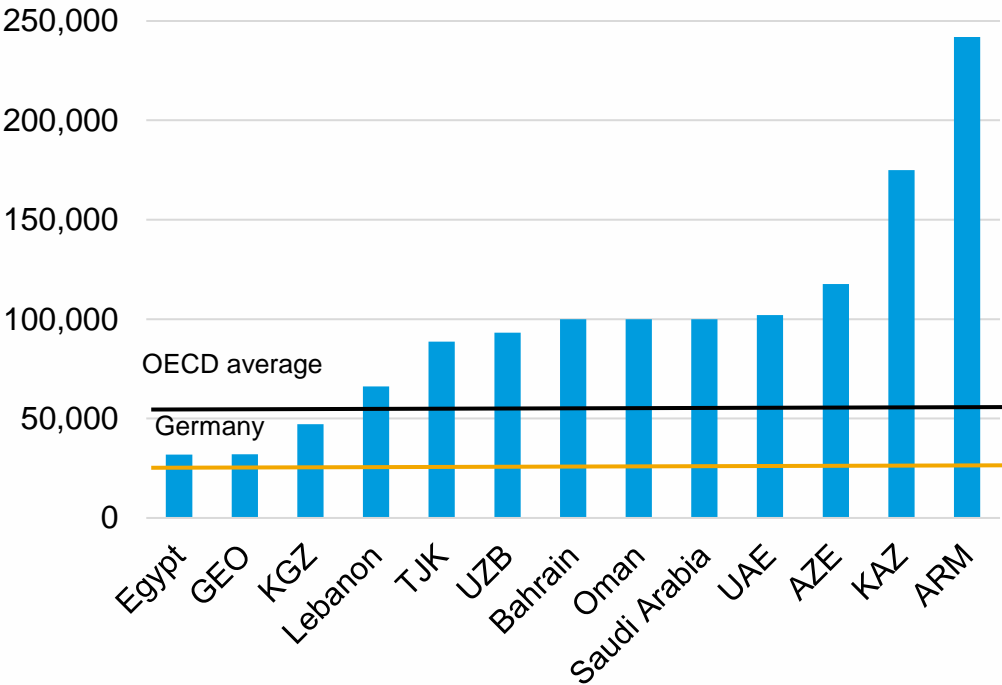
# Tax collections are robust, but room for growth friendly tax policy changes exists



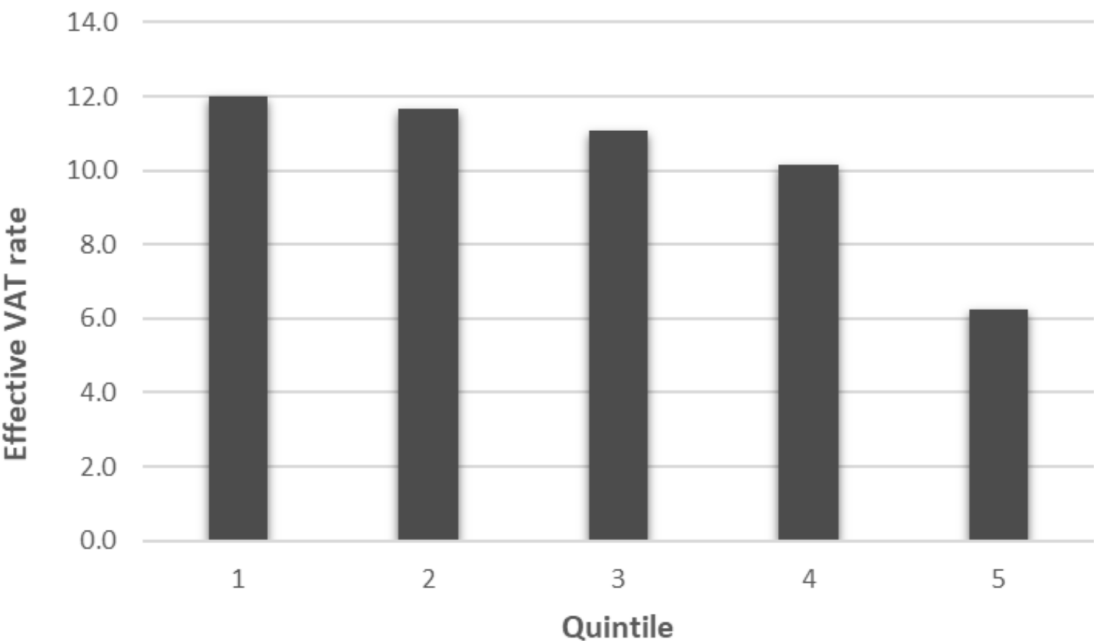
Source: RA Ministry of Finance and IMF staff calculations.

# VAT expenditures should be lowered, including via lowering the VAT registration threshold

VAT Registration Threshold  
(2021, USD)

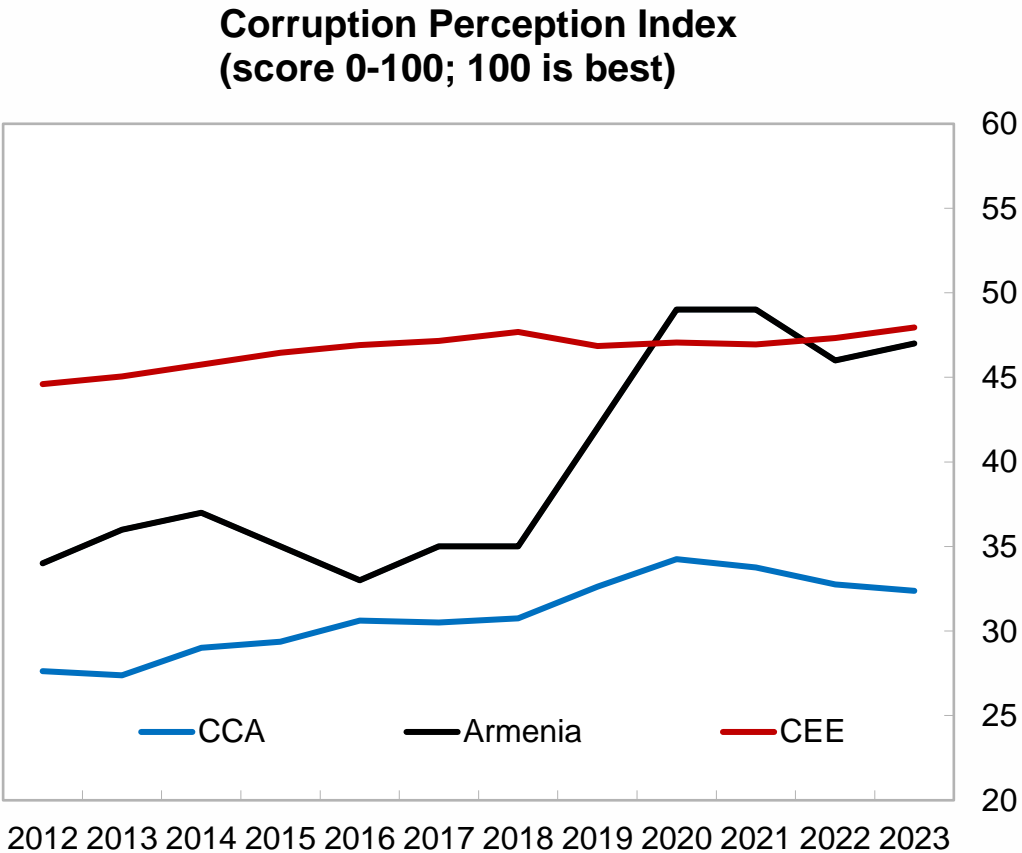
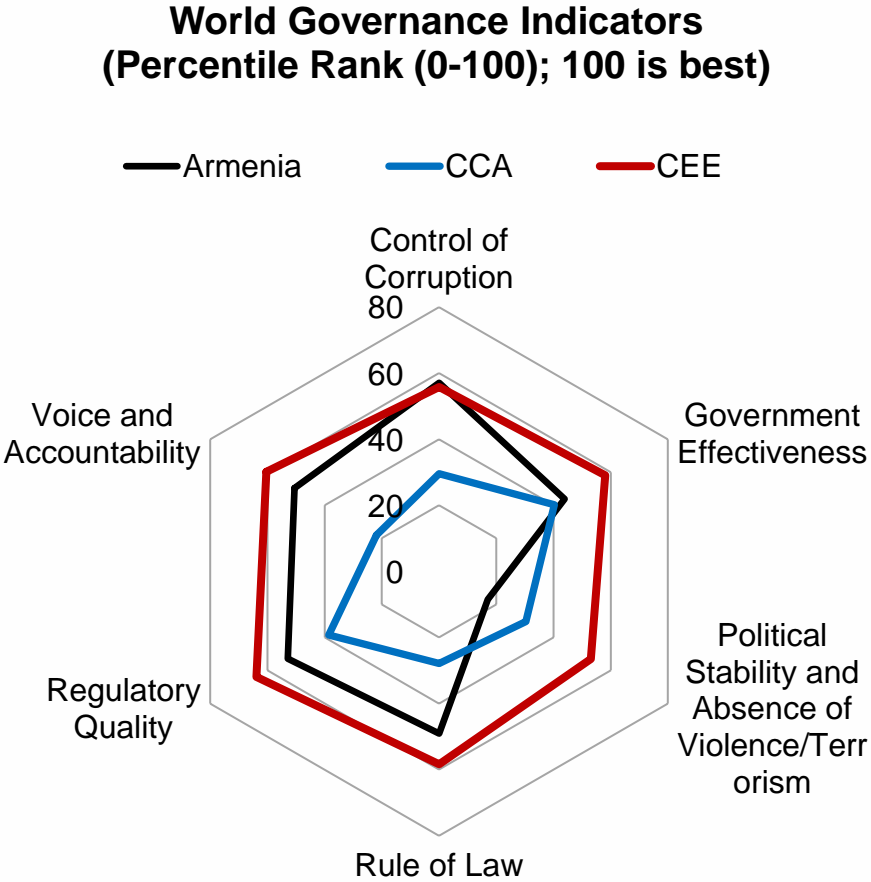


VAT Distribution



Sources: IMF Departmental Paper (2022); IMF Staff calculations

# While corruption perception has improved, there is room for further governance enhancements

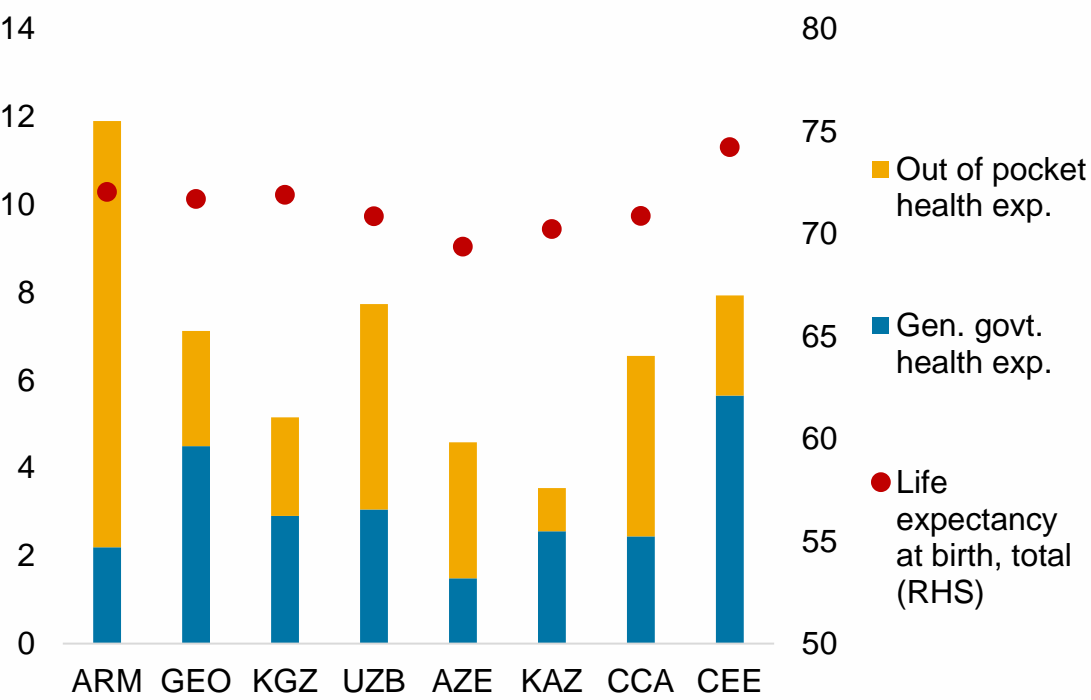


Sources: World Bank WGI; Transparency international; CCA – Caucasus and Central Asia; CEE – Central and Eastern Europe

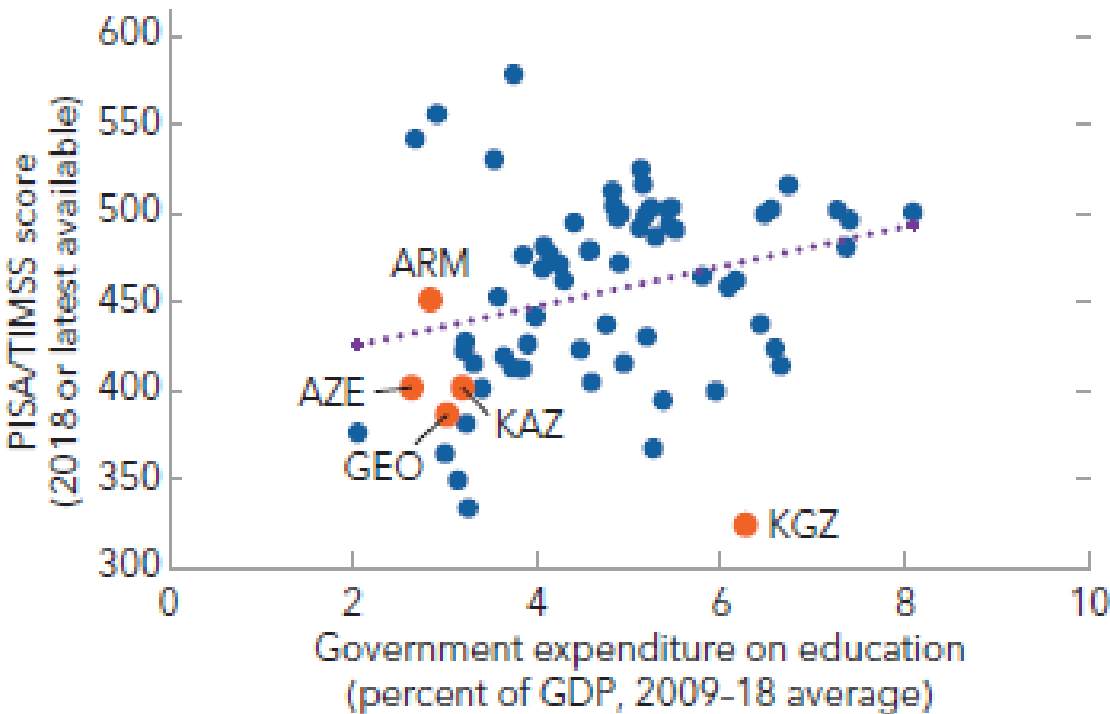


# Higher public spending in health and education is needed to boost human capital

Health Spending and Life Expectancy (2021)  
(Percent of GDP and years, respectively)



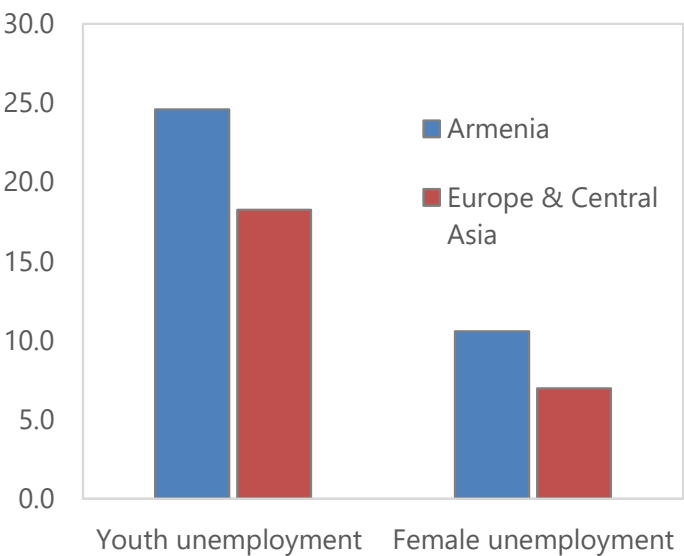
Education Expense and PISA/TIMSS Scores



Source: WHO, Global health expenditure database, World Bank, WDI, and IMF staff calculations

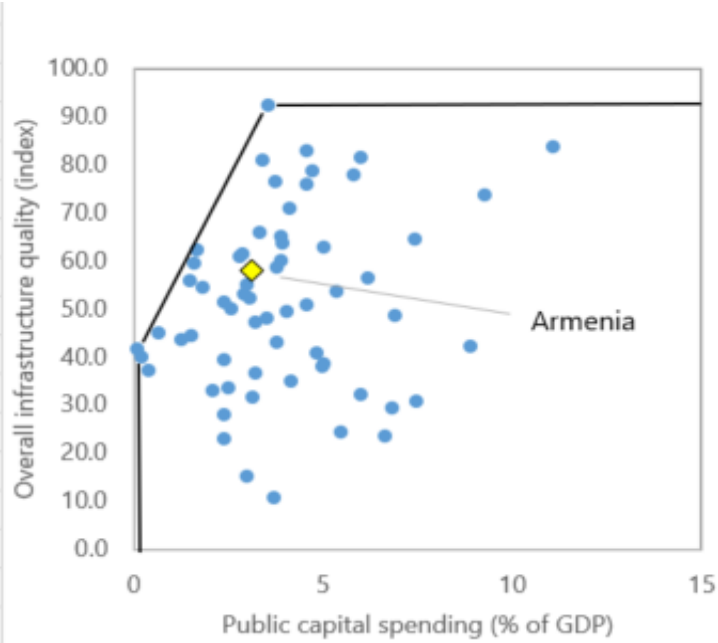
# Other constraints to growth including structural unemployment, investment inefficiency and access to finance

Youth and female unemployment  
(Percent)



Source: IMF (2023)

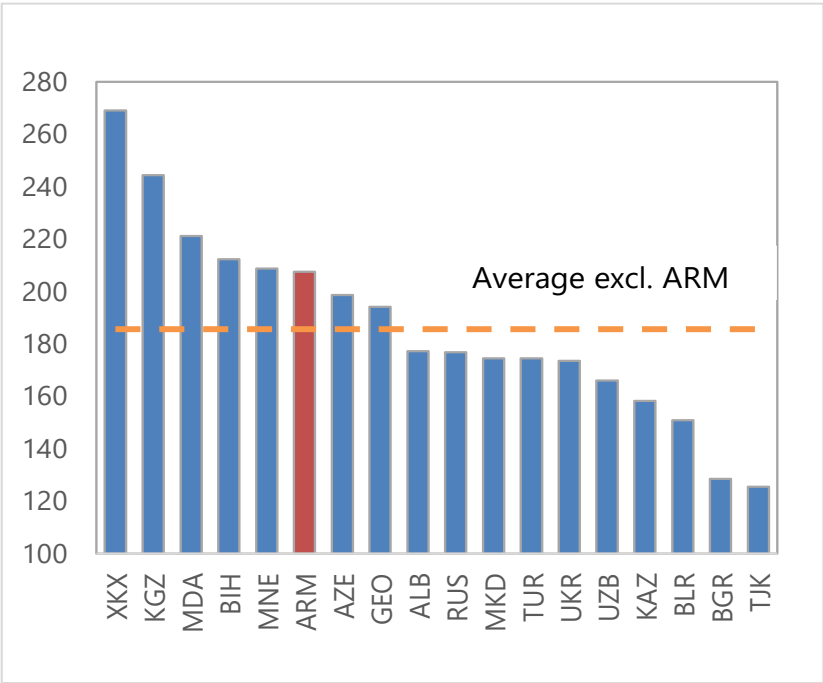
Public investment efficiency frontier  
(Perceived quality)



Source: IMF Staff estimates.

Note: Results should be interpreted with caveats as they are derived from perceptions-based data.

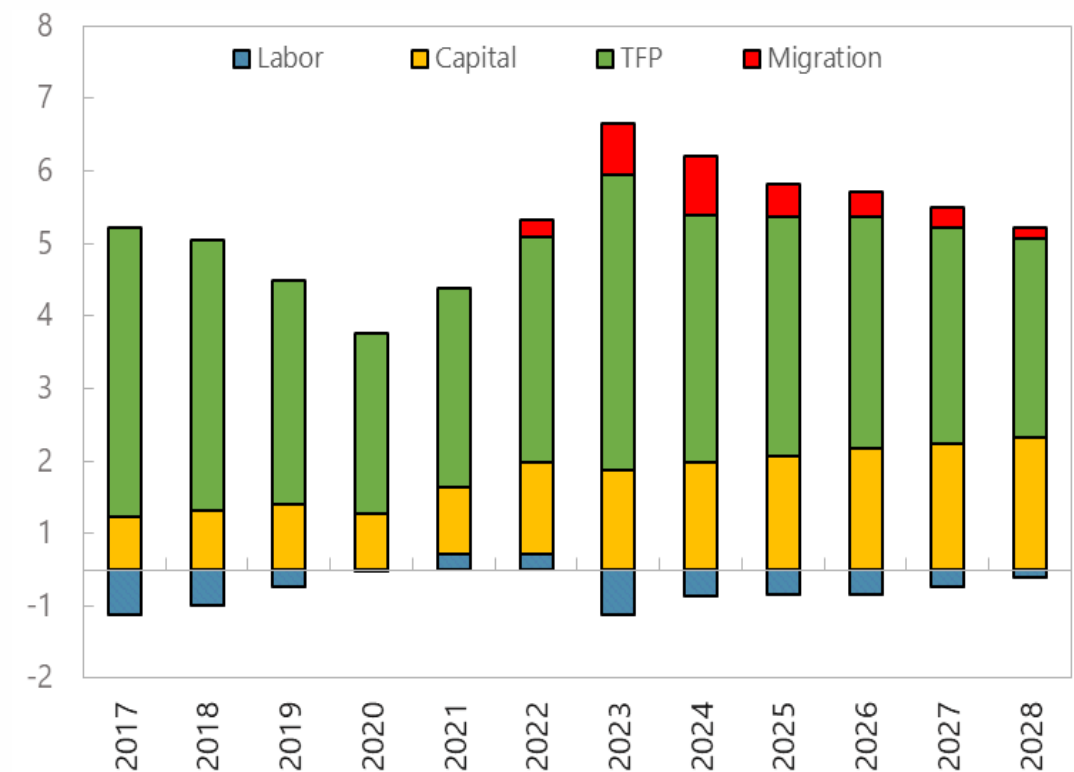
Collateral requirements  
(Percent of total loan amount)



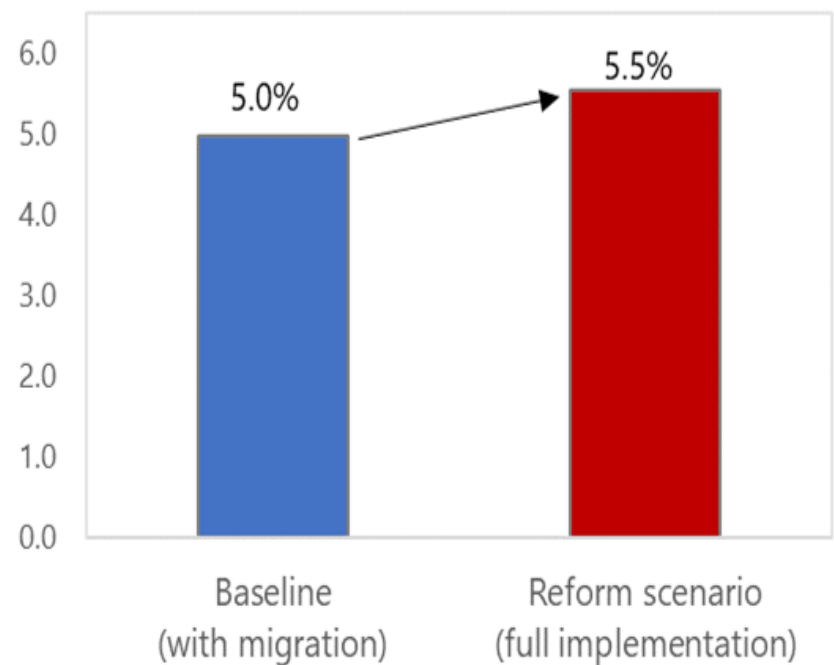
Sources: Global Financial Development database (November 2021 edition) and staff calculations.

# Stronger reform implementation is needed to boost long-term growth

Potential Growth Decomposition, Including Migration  
(Percentage points)



Impact of Reforms on Potential Growth  
(Percentage points, 2023-28 average)



Source: IMF (2023)

# Stand-By Arrangement: Program Implementation

36-month; Precautionary; semi-annual reviews; quantitative performance criteria and structural benchmarks; SDR 180 million (about US\$250 million or 140 percent of Armenia's quota in the IMF).

- Three reviews completed; fourth review ongoing
- All end-June quantitative performance criteria were met (NIR, fiscal target, budget domestic lending, external public debt arrears)
- Progress on structural benchmarks has been ongoing
- A few structural benchmarks were reset

# IMF staff current projections

## Armenia: Selected Economic and Financial Indicators, 2021–29

	2023	2024	2025	2026	2027	2028	2029
	Act.	Proj.					
National income and prices:							
Real GDP (percent change)	8.3	6.0	4.9	4.5	4.5	4.5	4.5
CPI (period average; percent change)	2.0	0.2	3.1	4.0	4.0	4.0	4.0
Fiscal balance (percent of GDP)	-2.0	-4.8	-5.5	-4.7	-4.3	-3.6	-3.0
Public debt (in percent of GDP)	50.7	52.4	55.6	56.6	57.4	57.2	55.5
Central Government's debt (in percent of GDP)	48.4	49.7	53.3	54.8	55.9	55.6	54.1
Current account balance (in percent of GDP)	-2.3	-4.2	-4.8	-5.0	-5.0	-5.0	-5.0

Sources: Armenian authorities; and Fund staff estimates and projections.

1/ Gross international reserves in months of next year's imports of goods and services, including the SDR holdings.

# Ongoing structural benchmarks to be implemented

Deadline	Status	Macro Criticality	Measure
June 2024	Implemented with delay	Improve tax compliance	Submit to parliament an amendment to the Tax Code to empower the SRC with authority to audit natural persons and include broader indirect audit methods.
September 2024	Implemented with delay	Improve public financial management	Submit to parliament an amendment to the Budget System Law and revise the PIM decree to clarify the definition of public investment projects in both legal frameworks.
June 2024	Expected to be implemented by mid-December	Enhance labor force participation and boost employment.	Approve a costed employment strategy that details plans to bolster active labor market policies and modernize labor market statistics to inform the implementation of employment policies.
June 2024	Proposed to be rescheduled to March 2025	Strengthen the regulatory and supervisory framework	Prepare and submit to parliament a draft law for an enhanced bank resolution framework that is in line with the Financial Stability Board's Key Attributes for Effective Resolution Regimes for Financial Institutions.
September 2024	Proposed to be rescheduled to March 2025	Support export-oriented growth	Complete and approve an export strategy that identifies and streamlines bottlenecks to export expansion.

# **Thank you**

**[www.imf.org/yerevan](http://www.imf.org/yerevan)**