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REPUBLIC OF ARMENIA: LETTER OF INTENT

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

Yerevan, November 11, 2010

Dear Mr. Strauss-Kahn:

1. **Armenia has exited the crisis, but the economic recovery is fragile and a swift return to the high pre-crisis economic growth is unlikely.** Thus far in 2010, growth has been positive, and public finances have improved considerably. The financial sector continues to be well capitalized and stable. Nonetheless, the economy faces considerable headwinds, including weak external demand, important structural rigidities, and social challenges. Sustained fiscal adjustment is needed, and in the financial sector, continued steps are warranted to deepen intermediation, lower dollarization, and reduce vulnerabilities. At the same time, we will aim at reducing external imbalances and enhancing competitiveness.

2. **Performance under our Extended Fund Facility and Extended Credit Facility (EFF/ECF) programs has been very strong.** The program is on track with all quantitative performance criteria and indicative targets for end-June 2010 as well as all indicative targets for which data are available for end-September 2010 observed. The structural benchmarks were also met, except for the benchmark on the establishment of the tax appeals board which was met with a delay.

3. **This Letter of Intent (LOI) builds on the LOI and MEFP agreed between the Armenian authorities and the Fund under the EFF/ECF arrangement approved on June 28, 2010.** Our near-term macroeconomic policies will continue to aim at balancing the need to support the ongoing economic recovery and contain eventual macroeconomic pressures. We remain committed to our reform program aimed at economic growth and poverty reduction, fiscal and debt sustainability, reducing external imbalances, and developing a sound financial system.

I. Recent Developments and Outlook

4. **The pace of economic recovery thus far in 2010 has been somewhat lower than projected at the time of the program approval, while inflation is higher.** GDP growth was 3.1 percent in January–August 2010, driven by a recovery in services, industry, and construction, offset in part by an unprecedented decline in agricultural output due to bad weather conditions. Both trade and remittances have rebounded after a sharp decline last year, but the current account deficit, while declining, remains high. Fiscal performance has

been strong in the first eight months of 2010 due to higher tax collections, including VAT and social contributions, and restrained spending. After falling to 5.7 percent in June (year-on-year), consumer prices increased to 9.6 percent in August mainly driven by a surge in food prices, notably for bread and fruit and vegetables. Banks remain well capitalized and liquid, and credit to the economy is picking up, notably in foreign currency.

5. **In the short term, the economic outlook remains subdued.** Growth in Russia and Europe—Armenia’s largest trade partners—is likely to be sluggish in the near term. Due to the poor agricultural output and base effects from the resumption of growth in the last quarter of 2009, GDP growth could be slower in 2010 than projected earlier. On this basis, and mindful of downward risks, GDP is projected to grow at about 4 percent in 2010.

6. **The medium-term outlook will continue to be challenging, and thus the pace of growth is uncertain and the economy is unlikely to return to pre-crisis growth rates.** We expect GDP growth to rise to 4.6 percent in 2011, supported by strengthening domestic demand and a recovery of the agriculture sector. However, with external demand and remittances recovering only gradually, and FDI and private investment likely to remain weak, growth is expected to stay at about 4–4½ percent over 2012–13. Inflation is expected to revert to the CBA’s target band during the second half of 2011. Public debt is also expected to drop to about 43½ percent of GDP by 2013 under the newly approved debt management strategy and the medium-term expenditure framework. The current account deficit is expected to be reduced considerably.

II. The Program for 2010 and 2011

A. Fiscal Policy and Debt Sustainability

7. **As the economy recovers, we are gradually unwinding the fiscal stimulus to ensure fiscal and debt sustainability.** We remain committed to reducing our deficit to 4.8 percent of GDP in 2010 followed by a further reduction in 2011 to 3.9 percent of GDP. This reduction in the deficit is predicated on improvements in tax administration and limited increases in spending. With the improving economic activity and renewed efforts to strengthen tax administration, we expect the tax-to-GDP ratio to increase by about 0.5 percent per annum. During 2010–11, we will implement contingency measures if revenues underperform relative to projections under the program, including by adjusting spending as needed to achieve the deficit target. We will continue to adhere to our commitment to save at least half of any tax revenue over-performance above the current projections reflected in the EFF/ECF program. Over the medium term, given the need to free up some fiscal space because of a sharp increase in public debt during the recent crisis, our fiscal policy will aim at further reducing the deficit to about 2 percent of GDP by 2013.

8. **In order to improve the transparency and planning of government operations, we re-introduced our medium-term expenditure framework (MTEF), suspended temporarily during the crisis.** The MTEF, approved in August of this year, is geared at

promoting growth, while placing public debt on a downward path and shifting spending toward social programs and investment in key sectors. With the economic crisis over, we intend to wind down our net lending program financed by the Russian loan, ensuring that such programs support small and medium-sized enterprises and exports. In addition, we have been consulting with our international partners on enhancing budgetary expenditure framework and the efficiency of spending.

9. **Our efforts to strengthen debt management have materialized in the adoption of a new medium-term debt management strategy in July 2010.** Under our program, we intend to keep the public and publicly guaranteed debt stock at about 50 percent of GDP in 2010–11, and gradually reduce it over the medium term. We will also adhere to the average concessionality target as agreed under the program by strictly limiting nonconcessional borrowing to financially viable projects. We intend to strengthen our debt monitoring and planning capacity. We have recently adopted a time-bound action plan to implement the debt management strategy.

B. Monetary and Exchange Rate Policy

10. **Monetary policy will continue to focus on price stability under our inflation targeting framework.** We have kept our policy rate constant since May, communicating clearly to the market that the recent shock to prices is temporary and exogenous and that demand pressures remain subdued. We believe that second-round effects will not be large and inflation will gradually decline to within the target band by mid-2011. Nonetheless, we will continue monitoring price and output developments and adjust our monetary stance as needed.

11. **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 proven buffer from exogenous shocks. To avoid creating market perceptions of a return to maintaining an exchange rate target level or range, we will communicate clearly and act accordingly to ensure that market participants recognize the two-way risks in the foreign exchange market.

12. **We will continue to strengthen the monetary transmission mechanism.** We are striving to enhance the link between our policy rate and retail rates. To this end, we will manage liquidity actively to keep market interest rates close to the policy rate and, thus, advance the status of the policy rate as the market reference rate. To enhance further the interest rate channel, we are also considering initiatives to develop the market for dram instruments. We will standardize the pricing and settlement of treasury bills in line with international practice and facilitate transactions in the securities market. The law on mandatory third-party liability insurance passed in June 2010 and the law on private investment funds—currently with parliament—are expected to promote market development.

13. **We remain determined to reduce dollarization, given that it weakens the monetary transmission mechanism.** An earlier regulation requiring a quarter of banks' reserves on foreign currency deposits to be maintained in drams has widened interest rate spreads between dram and foreign currency deposits. We have raised this proportion to one half in September aiming to trigger a further shift in the composition of deposits. In addition, the CBA and SRC are working on a plan to strengthen enforcement of foreign exchange regulations which require the use of drams in certain transactions and for listing the prices of goods and services. The draft law on restricting large cash transactions in the real sector is currently being reviewed by the parliament. We acknowledge that successful dedollarization will ultimately hinge on maintaining a track record of macroeconomic stability.

C. Financial Sector Stability and Development

14. **We are committed to preserving the stability of the Armenian banking system and are promoting reforms to enhance its resilience and increase the efficiency of financial intermediation.** Despite considerable improvement in recent years, private sector credit reached only 20 percent of GDP and residents are hoarding cash, including in foreign exchange. There is great scope for increasing financial access and deepening financial intermediation which would help improve the traction of monetary policy. We intend to undertake a full FSAP update in mid-2011, which would focus not only on financial stability issues, but also analyze the impediments to credit growth and financial intermediation.

15. **We continue our work on enhancing risk management and the supervisory framework to limit vulnerabilities in the financial sector.** Recent prudential regulations have focused on ensuring proper management of foreign currency (FX) risk and FX-induced credit risk. In August 2010, the limits on net open foreign exchange positions were made symmetric at ± 7 percent of bank capital. Prudential regulations on higher capital and provisioning requirements on foreign currency loans were issued to become effective in September 2010 and January 2011, respectively. In addition, we intend to require banks to pay extra attention to FX-induced credit risk assessment. Furthermore, in line with the Fund's technical assistance recommendations, we envisage to enhance our supervisory framework with a more forward-looking assessment of potential risks.

16. **We continue strengthening our crisis preparedness and contingency planning.** We have formalized the Committee for Financial Stability through a memorandum of understanding identifying actions and responsibilities of relevant institutions in various crisis events (Structural benchmark, September 2010). We are drafting a regulation requiring banks to set up their contingency plans for liquidity and solvency support (Structural benchmark, December 2010). We envisage a comprehensive contingency plan that would include stress tests designed by the banks themselves with an action plan on how to deal with these stress scenarios.

III. Structural Reforms

D. Fiscal Reforms

17. **Fiscal reforms, notably enhancing revenue management, continue to be a centerpiece of our program commitments.** Our efforts are primarily focused on ensuring lasting improvements in tax administration, enhancing the integrity of the system, and achieving efficiency gains, while providing incentives for taxpayers to comply. We set up a tax appeals board under the government to deal with legal and procedural disputes of tax payers (Structural benchmark, September 2010). In case of a difference of opinion between the SRC and the appeals board, the decision of the Prime Minister will be binding and final for the SRC. Moreover, a government decree was issued stipulating that clarifications and interpretations of laws and legislative provisions on taxes, duties, and mandatory fees should be agreed in advance with the Ministry of Finance. We are finalizing the development of manuals in tourism, real estate, transport, and sectors using cash register machines for tax audits for usage starting January 2011 (Structural benchmark, December 2010). However, manuals for mining will be developed in 2011, as we continue to work with the World Bank on revising the mining code. Furthermore, continued progress has been achieved in (i) extending the e-filing system of tax returns to about 3,000 taxpayers, with all large taxpayers currently reporting electronically, and (ii) improving the quality of taxpayer services, including through the creation of a full scale taxpayer service center.

18. **Looking ahead, further measures are envisaged to modernize tax administration to enhance revenue collection and secure a sustainable revenue base.** Consistent with the earlier commitments for the near term we will:

- Overhaul the VAT refund processing system. We will adopt a government decree establishing a mechanism for implementing a fully functional risk management approach in VAT refund processing (Structural benchmark, December 2010), and ensure this approach is fully operational by June 2011 (Structural benchmark, June 2011).
- Increase the number of large taxpayers (LTPs) by about 100 by December 2010 with a view to ensuring that LTPs' contribution in terms of total domestic revenues is continuously increasing compared to the previous year.
- Simplify the reporting system by reducing the frequency of reporting to tax authorities and considerably streamlining tax forms for VAT, profit tax, and personal income tax (Structural benchmark, December 2010).
- Continue analyzing the systemic problems underlying the difficult issue of tax credits and implement measures to reduce the stock of tax credits by December 2010.

19. **Going forward, we will embark on a number of important reforms**, including (i) structural and staffing reforms in tax inspectorates; (ii) strengthening the analytical and research capacity at the SRC and the Ministry of Finance; and (iii) launching a risk-based system for selection of taxpayers for audit, and implementing a comprehensive planning system for audits. We will develop a Three-Year Strategic Plan for Tax Administration (2012–15), outlining further reforms.

20. **We are stepping up our efforts in the tax policy area.** In particular, the presumptive taxation regime for petroleum products will be abolished and these products will be moved to the regular taxation regime starting January 2011. Moreover, we will gradually increase the presumptive payment for tobacco products with a view to harmonize the excise rates for imported and domestic tobacco over the course of 2011–13. Furthermore, we are committed to moving tobacco products from the presumptive to the regular taxation regime by 2014, and have passed the law pertaining to these changes in October 2010. Finally, we have submitted legislation to parliament to allow transfer of certain activities identified in the Law on Presumptive Taxes to the general taxation system in September 2010.

21. **We plan to introduce a funded pension pillar in 2014.** The related legislative package has passed the first reading at the parliament. We will ensure that realistic estimates for the full costing of the reform plan are taken into account, including those associated with the planned increase in basic pensions.

IV. Other Structural Reforms

22. **We intend to update our Sustainable Development Program (SDP) by the time of the second review of the EFF/ECF program.** The updated SDP will serve as the basis for our macroeconomic policy by providing an analytical background and ensuring a high participatory process of the civil society in economic management.

23. **Corruption remains a serious impediment to development and growth and a major challenge for policy makers.** In this area, we are committed to reversing the recent deterioration noted by several international indicators. Notably, a draft law has been submitted to parliament, which intends to address conflict of interest issues restricting public officials from engaging in commercial activities. We aim to strengthen the capacity of the competition commission in order to diminish monopolistic behavior in key sectors. We intend to take measures to strengthen competition and further reduce barriers to entry for new businesses, including a recent cabinet decree to create a one-stop shop for business registration.

24. **A number of reforms are planned under the umbrella of the recently-launched negotiations for an EU Association Agreement with Armenia.** We will revisit our regulations and practices regarding standardization, certification, intellectual property rights, competition rules, and public procurement procedures. The aim is to cut red tape and

promote private investment and exports by bringing the above procedures and regulations in line with best international practice.

25. **In the social policy area, we aim to reverse the recent increase in poverty and improve access to social services.** Our reform efforts to improve the quality of education and health spending are expected to bear fruit through greater efficiency of spending. Also, we aim to gradually increase allocations for health spending which remain in particular low for Armenia's income level. In addition, we will continue our efforts to better target our anti-poverty programs, as well as increasing their coverage. In collaboration with the World Bank, we will submit amendments to existing laws to enable the full functioning of an integrated system for the provision of social protection services (Structural benchmark, December 2011). We have also continued our progress toward achieving the Millennium Development Goals, as indicated by lower maternal mortality rates as well as an increase in life expectancy.

V. Conclusion

26. **Given our strong program implementation, we request the completion of the first review of the EFF/ECF program and the associated disbursement of SDR 36.2 million.** We also request modification of the end-December performance criteria for net international reserves, net domestic assets, and the program fiscal balance. In addition, we request the establishment of performance criteria for end-June 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. We have cooperated with the IMF to update the safeguards assessment. The second review is expected to be completed on or after March 31, 2011 and will assess performance as of end-December 2010. The third review is expected to be completed on or after September 30, 2011.

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

Very truly yours,

/s/
Tigran Sargsyan
Prime Minister
Republic of Armenia

/s/
Tigran Davtyan
Minister of Finance
Republic of Armenia

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

Table 1. Armenia: Quantitative Targets for 2010-11 1/
(In billions of drams, at program exchange rates, unless otherwise specified)

	2009		2010							2011						
	Dec.	Mar. 2/	Jun.		Sep. 3/			Dec.		Mar. 3/		Jun.		Sep. 3/		Dec. 3/
	Act.	Act.	EBS/10/119	Adj. Prog.	Act.	EBS/10/119	Adj. Prog.	Prel.	EBS/10/119	First Review	EBS/10/119	First Review	EBS/10/119	First Review	First Review	First Review
Performance Criteria																
Net official international reserves (floor, in millions of U.S. dollars)	1,019	895	824	824	912	855	787	929	829	808	856	831	793	780	801	747
Net domestic assets of the CBA (ceiling)	-12	-28	38	38	-16	46	74	-9	85	125	51	99	95	121	138	190
Program fiscal balance (floor) 4/	-355	3	-75	-75	-24	-92	-92	-76	-133	-140	-36	-34	-88	-58	-90	-112
External public debt arrears (continuous criterion)	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
Indicative Targets																
Reserve money (ceiling)	...	465	503	508	435	534	539	438	575	540	541	515	570	530	555	596
Average concessionality of newly disbursed debt (floor, in percent)			30	30	31	30	30	30	30	30	30	30	30	30	30	30
Social spending of the government (floor) 5/	...	7	15	15	15	23	23	23	31	31	9	9	18	18	27	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 until 2009. Below-the-line overall balance excluding net lending and project financing from 2010.

5/ 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
<u>Tax administration</u>			
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 board 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	
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	
5	Adopt a government decree establishing a mechanism for implementing a fully functional risk management approach in VAT refund processing.	December 2010	
6	Implement a fully functional risk-based management approach in VAT refund processing.	June 2011	
<u>Social policy</u>			
7	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	
<u>Fiscal and debt sustainability</u>			
8	Approve a medium-term expenditure framework (2011–13), including a medium-term debt management strategy.	August 2010	Met
<u>Financial sector</u>			
9	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
10	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
11	Issue prudential regulation requiring banks to prepare their contingency plans for liquidity and solvency support.	December 2010	

REPUBLIC OF 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 three-year EFF/ECF Arrangement as per the Letter of Intent dated November 11, 2010 (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 dram 385 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 November 2010 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 (quarterly on a disbursement basis); 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 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, the CBA's deposit facility, 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 set in Table 1 attached to the Letter of Intent dated November 11, 2010.

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. **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.

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 11).

7. **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.
- **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.

8. Those project implementation units, which carry out projects financed by the U.S.-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.

9. Foreign currency proceeds from selling enterprises are deposited into the Special Privatization Account (SPA). The account is held at the CBA and the proceeds are invested abroad together with the CBA's international reserves. These proceeds are included in the definition of the monetary accounts of the CBA as part of net foreign assets with a counter entry in other items net. Any budgeted withdrawal from the SPA will be accounted for as privatization proceeds used to finance the budget and will be recorded below the line. Any unanticipated withdrawal from the SPA will be recorded below the line as privatization

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.

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.

10. The program sets a 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 during the period 2010.

- 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 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.

11. 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

12. 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 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.

- **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.
- **External financing to the public sector** is 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, 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 or EU grants in the form of budget support (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 external financing or EU grants in the form of budget support compared to program amounts.
- **The floor on the program fiscal balance on a cash basis** will be adjusted upward (downward) by the cumulative total amount of the EU budget grants received in excess (to account for a shortfall) of the program amounts (Table 3).

III. Data Reporting

13. 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	All unpaid claims outstanding at the	Monthly	Within 45 days of

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

State Revenue Committee	Tax arrears	By type of tax	Monthly	Within 30 days of the end of each quarter (monthly data provided on a quarterly basis)
		For or the 30 largest debtors and for all major companies in the energy, water, and irrigation sectors	Quarterly	Within 30 days of the end of each quarter
	Tax credits	Detailed data, by type of tax, of outstanding tax credits for all types of tax revenues	Monthly	Within 45 days of the end of each month (monthly data provided on a quarterly basis)
	VAT refund claims in arrears	Detailed data on VAT refunds in arrears which include all outstanding VAT refunds that have not been accepted (and refunded), or offset (in full or in part), or rejected (in full or in part) after the 90 day statutory processing period. Number of refund applications processed per month.	Monthly	Within 45 days of the end of each month (monthly data provided on a quarterly basis)
	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	<ol style="list-style-type: none"> 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)

Dec-09	Mar-10	Jun-10		Sep-10		Dec-10		Mar-11		Jun-11		Sep-11	Dec-11
Actual	Actual	EBS/10/119	Actual	EBS/10/119	Actual	EBS/10/119	Prog.	EBS/10/119	Prog.	EBS/10/119	Prog.	Prog.	Prog.
33.8	0.0	0.0	0.0	2.0	5.0	27.8	29.9	2.0	2.0	4.0	4.0	6.0	8.0

1/ Cumulative from the end of the previous year.

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

	Dec-09	Mar-10	Jun-10		Sep-10		Dec-10		Mar-11		Jun-11		Sep-11	Dec-11
	Actual 2/	Actual	Prog.	Actual	EBS/10/119	Prel.	EBS/10/119	Prog.	EBS/10/119	Prog.	EBS/10/119	Prog.	Prog.	Prog.
Project financing	261	62	95	106	143	148	188	187	4	14	43	61	95	159
Budget financing	304	0	38	38	114	67	163	116	57	56	86	85	131	160
EU grant	...	...	...	...	23	0	23	0	23	25	23	25	50	50
Total	565	62	133	144	281	216	374	303	84	95	152	171	275	368

1/ Cumulative from the end of the previous year, excluding non-EU grants.

2/ Excluding Russia loan in the amount of 500 million U.S. dollars.

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.