IMPACT OF INTERNATIONAL FINANCIAL INSTITUTIONS ON THE ECONOMY OF ARMENIA

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Abstract- The ongoing globalization trends have flattened national economies, country boarders, and defined new perspectives and challenges for all countries, particularly those facing transition period. At this time, international financial institutions (IFI) have become the key drivers of capital and investment flows among countries. Moreover, the end of World War II tied economies with more regulated institutions and created new horizons for developing countries. Armenia, facing its transition period since independence from Soviet Union in 1991, has become a part of the global economy and has had to cope with globalization challenges. Therefore, the present paper is dedicated to the disclosure of impact of IFIs on Armenia economy, particularly whether the mentioned impact can be assess positively or negatively.

Keywords- International Financial Institution, Loan, Poverty, Economic Growth, Infrastructure, Technical Assistance

I. INTRODUCTION

International financial institutions are financial institutions which are established or founded by several countries and thus are subject to international law. Usually the governments of different countries represent the share participation into a given IFI and their representative officials are assigned for representing the country interests as a shareholder. Different IFIs have different shareholder participation requirements (GDP per capita, monetary policy, inflation, external debt, etc.), and those requirements are considered while examining separate cases of countries for participation. Any given IFI serves the role of developing economic regions, providing equal opportunities and sustainable growth. Armenia is also a part of global economy and thus, has participation in more than a dozen IFIs. Some of those institutions have had a great impact on the economy of Armenia, others have created challenges and thus increased the Armenia government burden as a stakeholder. Within present paper, the key players are examined as financial institutions with rather large impact on Armenia economic growth. Those institutions include European Bank for Reconstruction and Development (EBRD), International Financial Corporation (IFC), and Asian Development Bank (ADB).

II. DEFINING INTERNATIONAL FINANCIAL INSTITUTIONS GLOBALLY

In general terms, the objectives of IFIs have always been poverty alleviation, economic growth and protection of the environment. Traditionally, IFIs have promoted these objectives by working with governments and government agencies. This reflects the ideas and the capital structures which prevailed at the time of their creation. Broadly speaking, the IFIs have pursued these objectives with loans for public sector projects or programs, technical assistance, and policy-based lending. IFI loans have generally been made to, or guaranteed by, the borrowing states. Referring to the IFI definition provided above, the latter can be divided into several groups which are provided below:

- **Multilateral Development Banks**: A multilateral development bank (MDB) is an institution, created by a group of countries that provides financing and professional advising for the purpose of development. MDBs have large memberships including both developed donor countries and developing borrower countries. MDBs finance projects in the form of long-term loans at market rates, very-long-term loans below market rates, and through grants. The following are usually classified as the main MDBs: World Bank, International Fund for Agricultural Development, European Investment Bank, Islamic Development Bank, Asian Development Bank, European Bank for Reconstruction and Development, etc.

- **Bretton Woods Institutions**: These institutions were founded during the post war period in 1945s. They were aimed to assist in reconstruction of Europe and provide mechanisms for international cooperation in managing the global financial system. Bretton Woods Institutions include the World Bank, the IMF, and the IFC.

- **Regional Development Banks**: These banks consist of several regional institutions that have functions similar to the World Bank group's activities, but with particular focus on a specific region. Shareholders usually consist of the regional countries plus the major donor countries. The best-known regional banks cover regions that roughly correspond to United Nations regional groupings.

- **Other regional financial institutions**: These institutions include financial intermediaries of...
neighboring countries established themselves internationally to pursue and finance activities in areas of mutual interest; most of them are central banks, development and investment banks. Since its independence in 1991, Armenia has actively participated in international programs, grants, long term loans, issuance of securities in international markets and so on. Some of the key players in Armenian economy have been IBRD, IMF, IFC, EBRD, ADB, KFW, IFAD, etc. These institutions have provided technical and financial assistance, long and short term loans, debt and equity financing programs.

III. EBRD AND ITS PERSPECTIVE IN ARMENIA

EBRD was established to help build a new, post-Cold War era in Central and Eastern Europe. It has since played a historic role and gained unique expertise in fostering change in the region - and beyond. EBRD’s mission is to develop open and sustainable market economies in countries committed to applying, democratic principles. Their core values are leadership, teamwork, diversity, integrity, innovation, professionalism. Vision is stated as offering attractive conditions, the countries were successful in winning foreign direct investment, much of it long term, with associated benefits like know-how transfer and the introduction of international best practice in corporate governance. The EBRD has been part of this effort, and remains the region’s committed partner. Countries where EBRD invests have experienced varying degrees of economic controls in the past and are at different stages of completing the process to close the “transition gap”. It is commonly recognized that improvements in the living standards of people in the EBRD region depend on market economies that function well – where businesses are competitive, innovation is encouraged, household incomes reflect rising employment and productivity, and where environmental and social conditions reflect people’s needs.

The EBRD is owned by 64 countries, the European Union and the European Investment Bank. These shareholders have each made a capital contribution, which forms their core funding. Each shareholder is represented individually on the Board of Governors of the EBRD which has overall authority over the Bank.

Armenia joined EBRD in 1992, with capital subscription of €14,990,000. In Armenia EBRD focuses on developing the financial sector and improving access to finance. In near future, EBRD will focus on providing its traditional SME and micro-finance lines targeting areas outside Yerevan, the capital, and facilitating access to credit for SMEs in rural areas. It will launch agricultural credit lines in local currency and associated Technical Cooperation (TC), in particular as the sector becomes more commercialized. Moreover, cooperation with IMF and World Bank, it will engage in policy dialogue and provide TC to strengthen the Central Bank’s capacity to reduce inflation and dollarization and develop local money and capital markets. The Small Business Support team, established within EBRD office Armenia, helps small and medium business grow, succeed, then grow again, becoming genuine catalysts for their local economies, then their region. They connect their clients with local consultants and international advisers who can help transform a huge range of businesses. From the smallest looking to grow to those going global, their expert network of doers, thinkers and advisers help their clients to step up and start thinking big. EBRD supports businesses from many industries, such as food and beverages, wholesale and retail distribution, construction and engineering. In fact, 74% of its projects are outside Yerevan. Whether it’s a new website, a quality management system, a marketing strategy or even a completely new governance structure, they work with clients to define the best project to fit their needs. Moreover, EBRD will support clients through the whole process, using their years of experience to make sure the project achieves the best results. One year after every project, they return to measure the impact they made. And the results speak for themselves. Within a year of a project:

- 93% its clients in Armenia increase their turnover with a median increase of 47% and 89% improve their productivity, as they expand their business
- 59% see significant job creation
- 31% of its clients in Armenia secure external funding to finance their growth.

EBRD issued its first-ever bond in Armenian Dram (AMD), helping to drive forward the development of local capital market and providing funds for EBRD’s own lending to the Armenian economy in local currency. One-year bonds for a total of AMD 2 billion (approximately USD $5 million) were placed via an auction on the NASDAQ OMX Armenia exchange in Yerevan. This was the first publicly-auctioned issue by either a foreign borrower or an international financial institution on NASDAQ OMX and it was also the first floating rate note to be issued on the local market.

IV. IFC AND ITS PERSPECTIVE IN ARMENIA

IFC, one of the members of the World Bank Group, is the largest global development institution focused exclusively on the private sector in developing countries. Established in 1956, IFC is owned by 184 member countries, a group that collectively determines IFC’s policies. Their work in more than 100 developing countries allows companies and
financial institutions in emerging markets to create jobs, generate tax revenues, improve corporate governance and environmental performance, and contribute to their local communities. IFC’s main vision and goal is that people should have the opportunity to escape poverty and improve their lives. Unlike most other development institutions, IFC does not accept host government guarantees of its exposures. IFC raises virtually all of the funds for its lending activities through the issuance of debt obligations in the international capital markets, while maintaining a small borrowing window with IBRD. Equity investments are funded from capital (or net worth).

IFC’s main strategic areas are as follows: strengthen focus on frontier markets, address climate change and ensure environmental and social sustainability, address constraints to private sector growth in infrastructure, health, education, and the food-supply chain, develop local financial markets, build long-term client relationships in emerging markets.

As a one of the members of the World Bank Group, IFC has two overarching goals, i.e. end extreme poverty by 2030, boost shared prosperity in every developing country.

Armenia became a member and shareholder of IFC in 1995. IFC began providing advisory services in Armenia since 1999 and investing in economy since 2000. As of December 31, 2014, IFC’s long-term investment commitments in Armenia totaled $232 million, including $23 million mobilized from third parties, financing 41 projects across a range of sectors, including financial markets, manufacturing, agribusiness, services, and mining. In addition, IFC has supported trade transactions worth more than $110 million through its trade finance program. IFC also implements advisory projects in the areas of financial sector development, sustainable energy, regulatory simplification, and food safety.

One of the key objectives of the World Bank Group Country Partnership Strategy in Armenia is to support competitiveness and job creation. IFC contributes to this by:

- promoting greater access to finance for small and medium enterprises, and providing finance to competitive domestic companies to help them grow and create jobs,
- helping develop Armenia’s mining sector in a sustainable and socially inclusive manner,
- establishing a market for energy efficiency and renewable energy investments,
- improving the country’s investment climate and decreasing the costs of doing business, with a particular focus on the agribusiness sector.

V. ADB AND ITS PERSPECTIVE IN ARMENIA

While founding the institutions, ADB’s vision was to become a financial institution that would be Asian in character and foster economic growth and cooperation in the region - then one of the poorest in the world. The Philippines capital of Manila was chosen to host the new institution - the Asian Development Bank - which opened on 19 December 1966, with 31 members that came together to serve a predominantly agricultural region. Since its foundation ADB has been driven by an inspiration and dedication to improving people’s lives in Asia and the Pacific. ADB is committed to helping developing member countries evolve into thriving, modern economies that are well integrated with each other and the world. ADB is a multilateral development bank currently owned by 67 members, 48 from the region and 19 from other parts of the world. ADB’s main instruments for helping its developing member countries are policy dialogue, loans, equity investments, guarantees, grants, and technical assistance (TA). ADB’s focus on frontier markets, address climate change and sustainabl.

Since joining ADB in 2005, Armenia has received $847.3 million for advancing key projects in many areas such as transport infrastructure, finance, energy security, and water supply and urban services.

In Armenia, ADB, in collaboration with the European Bank for Reconstruction and Development, agreed to fund a project to rehabilitate the aging national power transmission system. This work will make power supplies across the country more reliable and efficient. In Armenia, ADB approved a loan of $49 million and a technical assistance grant of $900,000 to support the sustainability of the road and water sectors, and to help achieve the government’s development priorities for 2014–2025.
In transport, ADB is supporting the North–South Road Corridor Investment Program MFF. The $500-million MFF aims to develop an efficient, safe, and sustainable road network for Armenia, in pursuit of economic growth and regional cooperation. Another commitment in ADB’s transport program is a $400-million MFF, approved in 2011, for the country’s Sustainable Urban Development Investment Program. This program aims to help Armenia upgrade its urban transport services, improve living conditions, and bolster economic opportunities in selected towns. In water supply, ADB has provided $40 million as additional financing for the Water Supply and Sanitation Sector Project. The project will provide safe, reliable, and sustainable water services to a total of 18 towns and 92 villages in Armenia, all of which are now managed on commercial principles, and with environmentally sound practices. More than 600,000 Armenians have benefited from an ADB-supported project that upgraded water supply and sanitation systems in the central Asian country. In 2014, ADB approved the Infrastructure Sustainability Support Program, a $49-million loan that aims to strengthen management systems in the road transport and water supply sectors. Also in 2014, ADB extended its assistance to shore up Armenia’s energy security, approving the first sovereign loan in the country’s energy sector. The provision of $37 million will help to diversify energy sources, and to rehabilitate and upgrade electricity transmission and distribution networks. And there are also other projects in which ADB has its contribution. Total outstanding balances and commitments of ADB’s private sector transactions in the country as of 31 December 2014 was $102.1 million, representing 1.29% of ADB’s total non-sovereign portfolio. ADB’s Trade Finance Program (TFP) fills market gaps by providing guarantees and loans through partner banks in support of trade. The TFP has done over 10,300 transactions supporting over $20.5 billion in trade and over 6,000 small and medium-sized enterprises since 2004. In 2014, the TFP supported $3.8 billion in trade through over 1,900 transactions. In Armenia, the TFP works with four banks and has supported almost $38.2 million in trade between 38 transactions. In addition to filling market gaps, the TFP’s objective is to mobilize private sector capital/involvement in developing Asia. In Armenia, 70.7% of the $38 million in trade supported through the TFP was co-financed by the private sector.

While ADB will continue financing infrastructure, it will aim to gradually shift its focus to catalyzing support from the private sector, and providing knowledge products and services. Given ADB’s limited resources and assistance from other development partners, ADB won’t be significantly involved in the finance, health, and education sectors. In the transport sector, ADB will continue to support improving the north–south road corridor, and strengthening transport links between and within secondary towns, especially those with the highest poverty rates. To promote regional cooperation and integration, ADB will coordinate with Georgia to help improve roads linking Armenia and Georgia. It is too early in the implementation of operations to obtain a clear picture of ADB’s operational effectiveness, but there are positive signs of a strong, growing relationship. There is something that is clear: ADB provide money to RA which brings benefit to economies’ different spheres.

**RECOMMENDATIONS**

Summarizing the total impact of the above mentioned organizations on the economy of Armenia, the following points shall be emphasized:

- collaboration with IFIs create new investment opportunities in Armenia with lower interest rates,
- IFIs invest not only in finance, but also in management quality, technical assistance,
- IFIs integrate the Armenian economy into the foreign trade,
- participation of IFIs in local investment projects make them more attractive and secures for other external stakeholders,
- IFIs can lead to the development of stock exchange in Armenia,
- IFIs discover those weak points of the national economy, which can be rescued in case of sufficient investment and inject money there.

The above mentioned points are those benefits, which Armenia has taken ad continues to take from participation in IFIs. However, we shall also remember that IFIs set their own rules and Armenia shall comply those rules also. One of the main risks which IFIs have sufficient sensitivity, is the political risk, and any economic instability which is caused by political instability. From this point Armenia has to demonstrate enough integrity and democracy in order to continue to stay with IFIs and continue to attract new funds.

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