



# Country Operations Business Plan

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November 2007

Armenia  
2008–2010

Asian Development Bank

## CURRENCY EQUIVALENTS

(as of 16 November 2007)

Currency Unit	–	dram (AMD)
AMD1.00	=	\$0.0031
\$1.00	=	AMD319.37

## ABBREVIATIONS

ADB	–	Asian Development Bank
ADF	–	Asian Development Fund
ADTA	–	advisory technical assistance
COBP	–	country operations business plan
ERIOS	–	Economic Report and Interim Operational Strategy
EU	–	European Union
GDP	–	gross domestic product
IDA	–	International Development Association
IOS	–	interim operational strategy
JFPR	–	Japan Fund for Poverty Reduction
PPTA	–	project preparatory technical assistance
PRSP	–	Poverty Reduction Strategy Paper

## NOTES

- (i) The fiscal year (FY) of the Government and its agencies ends on 31 December.
- (ii) In this report, “\$” refers to US dollars.

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## CONTENTS

	<b>Page</b>
I. INTRODUCTION	1
II. CONSISTENCY OF THE PROPOSED BUSINESS PLAN WITH THE ECONOMIC REPORT AND INTERIM OPERATIONAL STRATEGY	1
III. INDICATIVE LENDING AND NONLENDING PROGRAMS	2
IV. RESULTS-BASED MONITORING	3
<b>TABLES</b>	
1 Indicative Assistance Pipeline for Lending Products	4
2 Indicative Assistance Pipeline for Nonlending Products and Services	5
3 Summary Information on Proposed Indicative Lending for 2009–2010	6
4 Summary Information on Proposed Indicative Nonlending Products and Services for 2008–2009	7
5 Sector Results Framework	8

## I. INTRODUCTION

1. The *Economic Report and Interim Operational Strategy* (ERIOS) for 2006–2009 for Armenia was endorsed by the Asian Development Bank (ADB) Board of Directors on 1 August 2006.<sup>1</sup> To commence operations in the country, the strategic priorities were identified as acceleration of rural development, promotion of the private sector and enhancement of regional cooperation. Continued progress in macroeconomic, fiscal and debt management reaffirms the Government's commitment to reform and growth. Following strong growth of 13.3% in 2006, 12% year-on-year growth in gross domestic product (GDP) was recorded in the first 7 months of 2007, supported by the construction sector, retail trade and other services. Poverty declined sharply from 34.6% in 2004 to 29.8% in 2005, accompanied by a reduction in extreme poverty from 6.4% to 4.6%. Prudent debt management policies effectively halved the debt-GDP ratio, from 33% in 2004 to about 17% in mid-2007. Parliament has approved the 5-year action plan for 2008–2012 of the newly appointed Government of Armenia (the Government). The Government's "second-generation reforms" are designed to strengthen democracy and rule of law, combat corruption, ensure continued economic growth, establish social justice and further reduce poverty. During the 5-year period, the Government projects an annual growth rate of 8%, reduction in poverty incidence to 11.2%, and elimination of extreme poverty.

2. The Armenian economy's capacity to borrow nonconcessional resources and repay its loans has strengthened with economic growth, a favorable macroeconomic outlook, improved creditworthiness and emerging investment opportunities. The level of concessionality of new external borrowing is expected to decline in the future, as Armenia's income rises. Based on the 2006 review of its creditworthiness by the International Monetary Fund, the country may become eligible for nonconcessional borrowing from 2008. International Development Association (IDA) repayment terms are envisaged to harden as per capita income is expected to exceed the IDA eligibility threshold for 2 consecutive years.

3. Armenia and the European Union (EU) have reached agreement over the country's action plan under the EU's European neighborhood policy. The action plan will last for 5 years and involves areas of economic development and cooperation. Observers from the Council of Europe's Parliamentary Assembly reaffirmed their largely positive assessment of the 12 May 2007 parliamentary elections. A new coalition government was formed with a majority of key ministers retaining their previous positions.

## II. CONSISTENCY OF THE BUSINESS PLAN WITH THE ECONOMIC REPORT AND INTERIM OPERATIONAL STRATEGY

4. As envisaged in the ERIOS, the country operations business plan (COBP) described below is designed to be consistent with the interim operational strategy (IOS) and coordinated with major development partners. This will help advance ADB's harmonization and alignment agenda. The annual country programming missions will determine the specific lending and technical assistance (TA) operations, based on (i) the Government's evolving development priorities, (ii) the continued relevance of ADB's IOS in addressing these priorities, and (iii) progress in implementing the portfolio of projects. A gradual commencement of operations and a learning process approach will promote strong cooperation and understanding between the Government and ADB. This approach will also allow ADB to be responsive and address project implementation issues from the outset. Monitoring of program implementation would be based on the results framework developed in the ERIOS.

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<sup>1</sup> ADB. 2006. *Economic Report and Interim Operational Strategy (2006–2009): Armenia*. Manila.

5. Taking into account lessons derived from implementation of the IOS, it is proposed to commence a Country Partnership Strategy in 2008 for delivery in 2009. In parallel, ADB will be working with the Government in preparing governance and anticorruption risk assessments and formulating mitigating measures. This will focus on the adequacy of public financial management and procurement systems, and of the governance and institutional arrangements in the operational sectors.

### III. INDICATIVE LENDING AND NONLENDING PROGRAMS

6. Armenia is classified as a Group B1 developing member country of ADB, eligible for resources from the concessional Asian Development Fund (ADF) as well as ADB's ordinary capital resources (OCR). On the basis of the results of the 2006 country performance assessment (CPA) exercise under ADB's performance-based allocation policy,<sup>2</sup> Armenia has been allocated \$66.66 million in ADF resources for 2007–2008. The allocations are based on the ADF resource envelope as estimated by ADB, which may be affected by movements in the exchange rates, the actual timing of ADF contributions from donors and changes in ADB membership. The 2007 CPA exercise is currently being undertaken to determine ADF allocations for 2009–2010. The allocations would also depend on ADF X discussions currently underway, and the pledges made by ADF donor countries. For planning purposes, indicative lending from ADF is assumed to be \$88.0 million for the 2009–2010 period. In addition to the country-level ADF allocation, funding of regional projects from the regional pool of ADF resources will also be explored. As the Government's priorities under its Poverty Reduction Strategy Paper<sup>3</sup> (PRSP) are expected to be fulfilled before the target of 2015, OCR lending is envisaged for sovereign interventions by 2010. The nonlending program has been designed to support preparation of projects, develop capacity and provide advisory services to the Government.

7. In view of the Board's recommendation to design a focused and short-term assistance program to enable learning from experience, and to address the Government's request for speedy assistance, the entire ADF allocation for 2007–2008 will be utilized in 2007. The lending portfolio in 2007 comprises two projects funded from ADF resources: Water Supply and Sanitation Sector Project for \$36 million and Rural Roads Sector Project for \$30.6 million. The focus in 2008 will be on efficient and effective implementation of these projects, supplemented with technical assistance. The program for 2008–2010 includes projects proposed to be funded from both country-level and regional ADF resources and OCR. The nonlending program will support the Government's need to address pro-poor initiatives through advisory TA (ADTA) focused on capacity building, training and studies, and through project preparatory TA (PPTA) to prepare for forthcoming lending operations. TA of \$3.2 million is planned over 2008–2009, supplemented by a \$2.0 million Japan Fund for Poverty Reduction (JFPR) grant in 2008. Additional cofinancing through bilateral trust funds will be explored. Tables 1 and 2 present the lending and nonlending pipeline. A summary description of the proposed interventions is given in Tables 3 and 4. The Government is also participating in a number of regional TA projects. The scope of the assistance program is commensurate with the Government's absorptive capacity and ability to provide counterpart funds.

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<sup>2</sup> ADB. 2001. *Policy on Performance-Based Allocation for Asian Development Fund Resources*. Manila.

<sup>3</sup> Republic of Armenia. 2003. *Poverty Reduction Strategy Paper*. Yerevan.

#### **IV. RESULTS-BASED MONITORING**

8. As outlined in the ERIOS, the sectors covered in the country assistance program are consistent with ADB's Medium-Term Strategy II. The proposed projects are linked to the ERIOS results framework through the sector results framework presented in Table 5. It reflects the indicators and activities appropriate for the COBP. The sector interventions are selected to address the identified development challenges and issues so as to achieve the relevant ERIOS outcomes through appropriately defined tracking and outcome indicators and milestones. ADB will promote partnerships in development partner-supported areas that are expected to influence the outcomes in the sector results framework.

Table 1: Indicative Assistance Pipeline for Lending Products

Sector Project/Program Name	Targeting Classifi- cation	Thematic Priority	Dept/ Division	Year of Project Preparatory Assistance	Total	Cost (\$ million)					
						OCR	ADB		Total	Govt	Co- financi ng
							Loans	Grants			
<b>2009</b>											
<b>Transport and Communications</b>											
1. Rural Roads Sector Project II	GI	ECG	CWRD/ CWID	2008	50.0		50.0		50.0	TBD	TBD
2. Regional Transport Infrastructure <sup>a</sup>	GI	ECG/REG	CWRD/ CWID	2008	50.0		50.0 <sup>a</sup>		50.0	TBD	TBD
<b>Subtotal</b>					<b>100.0</b>		<b>100.0</b>		<b>100.0</b>		<b>TBD</b>
<b>2010</b>											
<b>Finance/ Law, Economic Management and Public Policy</b>											
1. GFR Program	GI	GOV	CWRD/ CWGF		38.0		38.0		38.0	TBD	TBD
<b>Industry and Trade</b>											
1. Economic Development and Trade	GI	ECG	CWRD/ CWGF	2009	50.0	50.0			50.0	TBD	TBD
<b>Subtotal</b>					<b>88.0</b>	<b>50.0</b>	<b>38.0</b>		<b>88.0</b>		<b>TBD</b>
<b>Water Supply, Sanitation, and Water Management</b>											
1. Urban Services to Improve Environment (Standby project)	GI	ENV	CWSS	2010	38.0					TBD	TBD
<b>Total (Firm projects)</b>					<b>188.0</b>	<b>50.0</b>	<b>138.0</b>		<b>188.0</b>		<b>TBD</b>

ADB = Asian Development Bank; ADF = Asian Development Fund; CWGF = Governance, Finance, and Trade Division; CWID = Infrastructure Division; CWRD = Central and West Asia Department; CWSS = Social Sectors Division; ECG = sustainable economic growth; ENV = environment sustainability, GFR = Governance and Finance Reform; GI = general intervention; GOV = governance; Govt = Government; OCR = ordinary capital resources, REG = regional cooperation; TBD = to be determined.

<sup>a</sup> Proposed to be funded from the regional pool of ADF resources, subject to availability.

Source: Memorandum of Understanding signed on 17 October 2007 between the Government of Armenia and ADB Country Programming Mission.

**Table 2: Indicative Assistance Pipeline for Nonlending Products and Services**

Sector Assistance Name	Responsible Division	Assistance Type	Sources of Funding		Total (\$'000)		
			ADB			Others	
			Source	Amount (\$'000)		Source	Amount (\$'000)
<b>2008</b>							
<b>Finance/Law, Economic Management and Public Policy</b>							
1. GFR Cluster Technical Assistance I	CWGF	ADTA	TASF	700	700		
<b>Transport and Communications</b>							
1. Rural Road Sector Project II	CWID	PPTA	TASF	600	600		
1. Regional Transport Infrastructure	CWID	PPTA	TASF	600	600		
<b>Water Supply, Sanitation, and Waste Management</b>							
1. Community Water Supply Interventions	CWSS	Grant	JFPR	2,000	2,000		
<b>Subtotal</b>				<b>3,900</b>	<b>3,900</b>		
<b>2009</b>							
<b>Finance/Law, Economic Management and Public Policy</b>							
1. GFR Cluster Technical Assistance II	CWGF	ADTA	TASF	700	700		
<b>Industry and Trade</b>							
1. Economic Development and Trade	CWOC	PPTA	TASF	600	600		
<b>Subtotal</b>				<b>1,300</b>	<b>1,300</b>		
<b>Water Supply, Sanitation, and Waste Management</b>							
1. Urban Services to Improve Environment (Standby project)	CWSS	PPTA	TASF	600	600		
<b>Total (Firm projects)</b>				<b>5,200</b>	<b>5,200</b>		

ADB = Asian Development Bank; ADTA = advisory technical assistance; CWGF = Governance, Finance, and Trade Division; CWID = Infrastructure Division; CWOC = Country Coordination and Regional Cooperation Division; CWSS = Social Sectors Divisions; GFR = Governance and Finance Reform, JFPR = Japan Fund for Poverty Reduction, PPTA = project preparatory technical assistance; TASF = Technical Assistance Special Fund.  
Source: Memorandum of Understanding signed on 17 October 2007 between the Government of Armenia and ADB Country Programming Mission.

**Table 3: Summary Information on Proposed Indicative Lending for 2009–2010**

<b>Project Name</b>	<b>Description</b>
2009: Rural Roads Sector Project II	<p>The main objective of the proposed project is to contribute to poverty reduction and inclusive growth by providing the rural population with enhanced access to employment opportunities, markets, social services, regional centers and the capital city.</p> <p>The project will upgrade feeder roads identified for improvement (in parallel with MCC's roads program), develop a new transport sector strategy and enhance the institutional capacity of the Government in the field of transport sector management.</p>
2009: Regional Transport Infrastructure	<p>By modernizing international transport corridors, the project will enhance Armenia's economic competitiveness, trade and business opportunities, thereby contributing to its economic development.</p> <p>Support to international transport infrastructure will reduce transport costs and increase interregional transit traffic.</p>
2010: Governance and Finance Reform Program	<p>The support through this project will promote an enabling environment for private sector development and enhance government effectiveness.</p> <p>ADB's assistance in this area will help the Government implement its innovative governance reforms program.</p>
2010: Economic Development and Trade	<p>Expansion of trade and economic cooperation will help Armenia integrate into the global economy and enhance its economic development through potential benefits from trade, investment and growth and associated increases in living standards.</p> <p>This project will facilitate trade and development cooperation with Armenia's neighbors.</p>

ADB = Asian Development Bank, MCC = Millennium Challenge Corporation.

Source: Memorandum of Understanding signed on 17 October 2007 between the Government of Armenia and ADB Country Programming Mission.

**Table 4: Summary Information on Proposed Indicative Nonlending Products and Services for 2008–2009**

<b>Project Name</b>	<b>Description</b>
2008: GFR Cluster Technical Assistance I	The assistance under this ADTA will help the Government implement financial sector reforms in the possible areas of public finance (e.g. procurement; public financial management; auditing standards; external debt management) and the financial sector (e.g., non-bank financial institutions).
2008: Rural Roads Sector Project II	PPTA
2008: Regional Transport Infrastructure	PPTA
2008: Community Water Supply Interventions	JFPR
2009: GFR Cluster Technical Assistance II	The second phase of this ADTA would continue the process initiated under the first phase.
2009: Economic Development and Trade	PPTA

ADB = Asian Development Bank, ADTA = advisory technical assistance, GFR = Governance and Finance Reform, JFPR = Japan Fund for Poverty Reduction, PPTA = project preparatory technical assistance.  
Source: Memorandum of Understanding signed on 17 October 2007 between the Government of Armenia and ADB Country Programming Mission.

**Table 5: Sector Results Framework**

Relevant ERIOS Outcomes	Key Opportunities and Constraints	Sector-Level Outcomes		Areas of Interventions	Partnership
		Sector Outcomes to be influenced by ADB Operations and Outcome Indicators	Sector Milestone (Tracking) Indicators		
<b>Sector: Water Supply, Sanitation, and Waste Management</b>					
Higher rural living standards from better water supply system and municipal services (PRSP, para. 115, 360, 376).	Poor rural water supply and waste management systems keep standard of living low.	Improved access, availability, and quality of rural drinking water (PRSP, para. 374).  Improved waste collection and processing technologies (PRSP, para. 366).	Investment in drinking water to GDP ratio increases from 0.4% in 2004 to 0.7% in 2009 (PRSP, Table 7.13).  Reduced health and economic consequences of hazardous waste and improved environmental standards contribute to improved living standards.	Water supply and sanitation projects	The projects will be coordinated with partners active in the sector.
<b>Sector: Transportation and Communications</b>					
Good road connectivity of village communities to town centers and markets (PRSP, para. 115, 389, 391)	Limited access to markets and social services constrains growth of economic activities and keeps living standards low in rural areas	Significant increase in traffic on rural roads in 2010, compared to 2007.  Due to improved rural roads, access to markets will create additional employment generation and development of agribusiness and other rural enterprises.	1,200 km rural roads improved by 2010; increase in road capital repair to GDP ratio from 0.6% in 2007 to 1.0% in 2010.	Rural road sector projects	Activities will be coordinated with the World Bank, MCC and Lincy Foundation to enhance the impact of rural roads rehabilitation.

Relevant ERIOS Outcomes	Key Opportunities and Constraints	Sector-Level Outcomes			
		Sector Outcome(s) to be influenced by ADB Operations and Outcome Indicators	Sector Milestone (Tracking) Indicators	Areas of Interventions	Partnership
Economic distance to external markets and cost of transport abroad reduced (PRSP, paras. 143/157)	Bottlenecks along the regional transport corridors.	Reduction in travel time for regional traffic and increase in cross-border traffic.	Better transport connectivity and significant potential increase in 2010 compared to 2007 in investment and growth, resulting from higher trade. Exports grow at 9.2% annually from 29.6% of GDP in 2002 to 31.9% in 2009 (PRSP, Table 6.1)	Regional transport infrastructure	The activities will be coordinated with major development partners in the area.
<b>Sector: Finance/ Law, Economic Management and Public Policy</b>					
Improved business and investment environment for job creation and attracting investments (PRSP, para. 207)	Business environment lagging behind EU membership candidate countries in transition. Limited access of private sector to medium and long-term financing.	Institutional and financial management reforms (PRSP, para. 168)  Well-developed long-term financing mechanisms (PRSP, para. 227)	Index of confidence in economic policies and the administrative conduct of the state (min: 1, max: 6) rises from 3.33 in 2001 to 5.0 in 2015 (PRSP, Table 6.8)	Governance and finance reforms  Possible private sector equity investments, loans, credit lines, partial credit or political risk guarantees; mobilization of private capital for private and mixed enterprise infrastructure	The activities will be coordinated with major development partners in the area.
Poverty reduction through availability of long-term financial resources (PRSP, para. 227).		Significantly wider access of private companies to financial resources (PRSP, paras. 214, 216)	Target indicator for financial market and nonbank financial institutions rises from 2 in 2001 to 3 in 2009 (PRSP, Table 6.8) <sup>a</sup>		
Improved access of private enterprises to bank financing (PRSP, para. 219, 220).			The population has significantly wider access to financial resources (PRSP, para. 214)		

ADB = Asian Development Bank, ERIOS = Economic Report and Interim Operational Strategy, GDP = gross domestic product, EU = European Union, MCC = Millennium Challenge Corporation, PRSP = Poverty Reduction Strategy Paper.

<sup>a</sup> Rating of 1 indicates insignificant changes compared to a central planning system; 4+ indicates standards comparable to developed countries.

Source: Memorandum of Understanding signed on 17 October 2007 between the Government of Armenia and ADB Country Programming Mission.