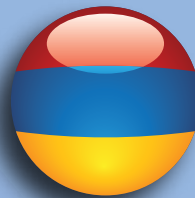


STRONGER ECONOMY

#eu4business



EU4Business

Investing in SMEs in the Eastern Partnership

Armenia

COUNTRY REPORT
JUNE 2019



10 YEARS 
EaP | Eastern
Partnership

1. Recent economic developments in the country

Armenia's real GDP expanded by an estimated 8.5 per cent in the first half of 2018 before slowing down to an estimated 3.0 per cent in the second half of the year, giving an overall growth rate for the year of 5.2 per cent. A contraction in production in the agriculture and mining and quarrying sectors weighed on the growth of exports and economic output in the second half of the year. At 28.5 per cent, capital investments were the largest contributor to growth.

However, this impressive growth is largely explained by one-off methodological changes; the increase in gross fixed capital formation was 5 per cent. Household consumption and exports both grew, albeit at lower rates than a year earlier. A strong expansion in consumer loans and a steady inflow of money transfers from abroad supported private consumption growth. The current account deficit widened significantly from 2.4 per cent of GDP in 2017 to 9.1 per cent in 2018, in part financed by foreign investments and increased bank deposits in foreign currency.

The dram remained relatively stable against the US dollar. According to preliminary estimates, economic output grew by 6.5 per cent year-on-year in the first two months of 2019. This positive growth trend is expected to continue with real GDP growth of 4.5 per cent in both 2019 and 2020.

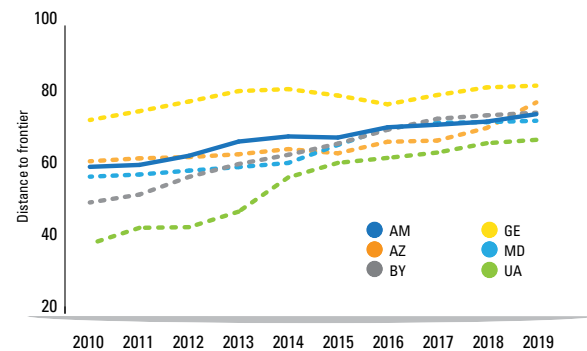
In February 2019, the authorities reached a staff-level agreement with the IMF on a three-year Precautionary Stand-By Arrangement (SBA). Subject to approval by the IMF Executive Board, the SBA aims to support the new government programme, which is focused on achieving stronger and more inclusive growth, while at the same time preserving macroeconomic and financial stability.

(<https://www.ebrd.com/where-we-are/armenia/overview.html>)

2. Business environment: Armenia and the EaP

The six Eastern Partner countries have been making steady progress in improving the business climate for SMEs. This overview of the Doing Business indicator of the World Bank shows how Armenia has improved over the years, gradually closing the gap with the best performing countries of the world ('distance to frontier'). Armenia started off at 60% of that distance to frontier, but now stands at 75%.

Doing Business - Distance to frontier, EaP

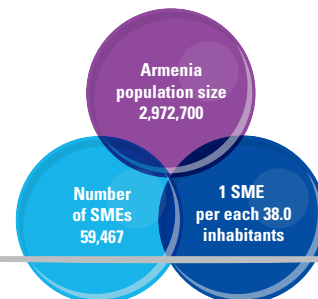


Source: Doing Business, World Bank, www.doingbusiness.org¹

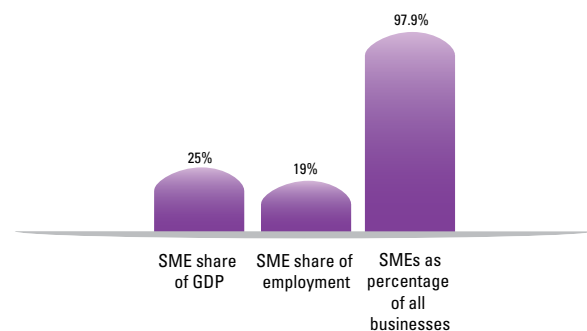
3. National SME performance

a. Share of SMEs in the economy

Armenia has an average number of SMEs per capita in relation to the other Eastern Partner countries, but one of the highest shares of employment generated by the SME sector. Likewise, the share of SMEs in GDP comes to a significant fraction of the national economic output, the highest of the six Eastern Partner countries.



State of affairs of SMEs in 2017



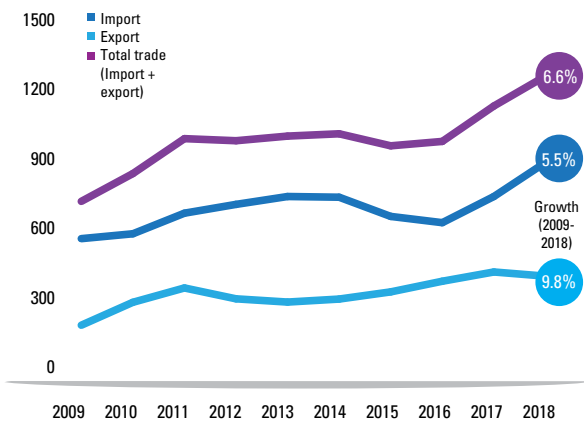
Source: OECD Compendium of Enterprise Statistics in Armenia 2018 and Official Yearbook of the Statistical Committee of the Republic of Armenia 2018

¹ An economy's ease of doing business score is reflected on a scale from 0 to 100, where 0 represents the lowest and 100 represents the best performance. For example, an ease of doing business score of 75 in Doing Business 2018 means an economy was 25 percentage points away from the best regulatory performance constructed across all economies and across time.

b. Trade with the EU

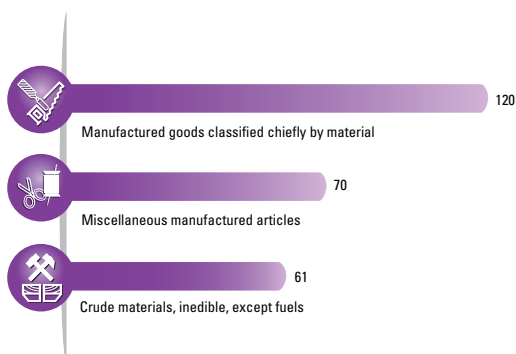
There has been a faster growth in exports to the EU than imports from it, although trade in both directions has been on the rise. Armenia currently imports EUR 863 million and exports 373 million worth of goods and services from and to the EU respectively.

Trade figures (EUR million)

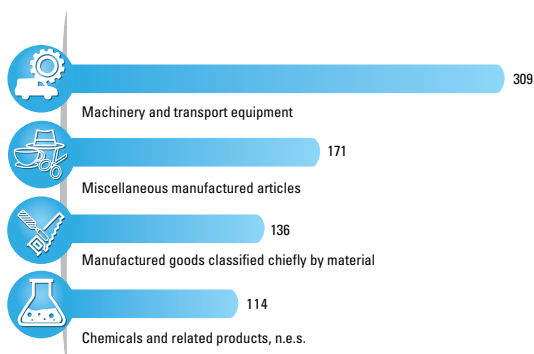


Below are the top products exported from Armenia to the EU and those imported the other way.

Top exported products in 2018 (EUR million)



Top imported products in 2018 (EUR million)



All trade data from DG trade

(https://webgate.ec.europa.eu/isdb_results/factsheets/country/).

4. SME legislation and institutional framework

Building on the findings and recommendations of the SME Policy Index 2016, the Government of Armenia has shown its willingness and taken steps to improve the policy environment for small and medium-sized enterprises. An initial effort in this direction has led to the adoption of an SME strategy covering the period 2016-2018. Following the implementation period of the Strategy, an external evaluation was conducted pointing to the main developments and challenges of the SME policy. The Government of Armenia is now in the process of drafting of a new medium-term SME strategy for the coming years, with the active engagement of all stakeholders, including the private sector.

Key SME legislation in the country

Law on State Support for Small and Medium Entrepreneurship, adopted in December 2017

Name and date of establishment of the SME agency

Small and Medium Entrepreneurship Development National Centre (SME DNC), March 2002

Achievements in improving the SME climate

- Regulatory policy, where a guillotine process launched in 2012 has resulted in the review and simplification of 75% of existing laws and regulations; the recent establishment of the commercial and insolvency court in January 2019; and the introduction of a one-stop-shop for full company registration, which now takes only 4.5 days.
- Public procurement, as the new law adopted in 2016 aligns with EU directives, including regarding SMEs. To complement this, a revision of the e-procurement system took place in 2018.
- Improved SME innovation and R&D support. The Government adopted the Strategic Programme for Science Sector Development (2017-2020) and expanded its technology support and infrastructures services (extension of public-private partnerships through establishment of the Convergence Centre for Engineering and Applied Science in 2019).
- Provision of extensive SME support by SME DNC through trainings and awareness-raising activities, providing loans, improving SME exporting potential. Lately, the Government has expanded the range of services provided (8,010 information and consulting services to 4,000 SMEs, and 314 training sessions held in 2018).

EU4Business: From Policies to Action progress (OECD)

The OECD actively co-operates with the Government of Armenia, working primarily with the Ministry of Economic Development and Investments on the following reforms:

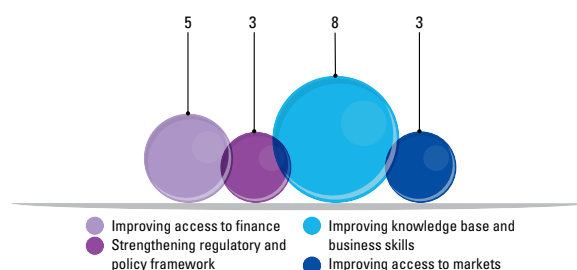
- At the **country level**, the OECD worked closely with Statistical Committee of the Republic of Armenia (Armstat) to improve its capacity to collect, analyse, disseminate and harmonise official business statistics. This work resulted in the publication of a Compendium of Enterprise Statistics in Armenia 2018, produced by the OECD in co-operation with Armstat. The Compendium presents comprehensive and detailed information about the role played by the SME sector in Armenia's economy. Another important outcome of the project was the production by Armstat of the first Statistical Bulletin on Small and Medium Entrepreneurship in the Republic of Armenia, 2018.
- The OECD also provides assistance to the Government of Armenia to develop its SME strategy, in particular with regards to supporting public-private consultations and adopting elements of an effective monitoring system. The OECD will further support the Ministry of Economy in the finalisation of the strategic document through review of draft strategy and provision of recommendations for its improvement.
- In addition to this, Armenia is joining the OECD FDI Regulatory Restrictiveness Index. Armenia is now undergoing the review of its regulatory measures, with results expected by the end of 2019.
- At the **regional level**, Armenia participates in the third round of the SBA Assessment, which will result in a regional benchmark to be published by March 2020. The new exercise is more ambitious than the previous editions, and relies on a new methodology that goes beyond the scope of SME policy to incorporate overall business environment conditions, including the topics of competition, business integrity and contract enforcement. An important milestone in this process took place in Yerevan on 23 May 2019, consisting of a public-private reconciliation meeting to discuss preliminary findings, progress in SME policy since the 2016 assessment and to clarify outstanding issues/gaps in the assessment findings. For this activity, the OECD is working closely with the Ministry of Economy to provide support in strengthening existing public-private dialogue activities.

5. EU4Business portfolio for the country

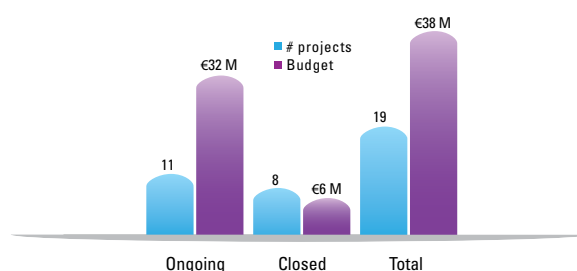
The total number of projects in Armenia is 19, of which the largest group focuses on improving knowledge base and business skills. Out of the 19, eight have been closed and the others are ongoing, with a total value of almost EUR 38.3 million.

a. Impact to date

Ongoing projects by priority area - Armenia



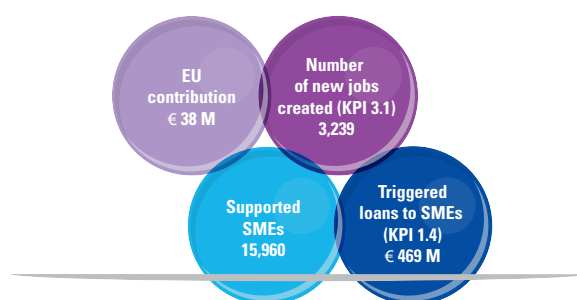
Armenia country portfolio



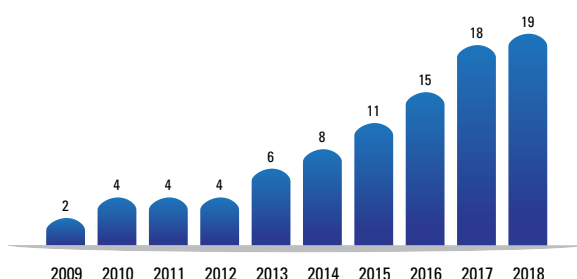
b. Implementation progress - 10 years of EU4Business in the country

The funds invested by the European Union triggered additional loans and financial assistance in the country, effectively increasing the assistance 12-fold. This benefitted 15,960 SMEs and created an estimated 3,239 jobs, beyond the sustained ones. The number of projects in the country, and with it the EU's assistance, has been on the steady rise over the ten years of EU4Business's operation.

Implementation progress



Number of projects in Armenia



Source: EU4Business Secretariat project database

6. Stakeholder assessment

a. Findings from the SMEs - Focus group assessment, Yerevan, 29 April 2019

i. Key issues

Discussion among SMEs focused mostly on the shortage of qualified workforce. SMEs find it very difficult to find skilled labour of almost any type. By skills, SMEs do not only refer to specialised skills, but say that even very general, basic skills are often hard to locate. This is particularly the case outside the capital Yerevan. Moreover, as soon as people receive some training, they tend to move to the capital.

Other than the need for entrepreneurial and specialised skills, SMEs are short of opportunities to professionally network, twin, cooperate with other SMEs nationally and internationally. There is a clear preference to hear and learn from more experienced peers, those who have been successful in business. SMEs particularly need technical expertise on industrial or sector development, new innovative production processes or products, and certification (particularly in food processing).

Beyond standards and certification, Armenian SMEs say they would also strengthen their export potential through better development of infrastructure (transport routes). This would also support a more even development of the regions, as opposed to the current emphasis on the capital, but also easier access to the workforce. For services that can be sold online transport is irrelevant, but delivery time is high because of the issues with Armenian access to certain commercial online payment systems (it appears that the critical PayPal issue has recently been solved).

ii. SMEs' own needs assessment/priorities

SMEs are critically interested in creating sector-related networks to increase mutual learning and exchange of experience, as well as increasing business opportunities. They want to have access to those peers and industry experts who can deepen their knowledge of the targeted technical issues.

Top needs to access foreign (EU) markets include: tailored industry and market advisory services, marketing and advertising support, financial management and accounting; financial planning for business expansion; support for woman entrepreneurs and support for social entrepreneurship.

While financial products have been in high demand, financial needs remain strong, with focus on investment capital to keep up with growing demand. Soon the time will come when the Armenian financial market would be ready for further diversification of investment and lending instruments.

Finally, SMEs encourage strongly the continuation and strengthening of the government's efforts to ease the regulatory burden for entrepreneurs and further level the playing field. One specific issue that requires urgent attention is that of work permits/residence cards.

b. Views of the implementers - Armenia EU4Business Roundtable, Yerevan, 30 April 2019

i. Key issues

The Roundtable discussion started with presentations by the largest implementers. The EBRD, in working with SMEs, cooperates with 150 pre-qualified consultants who provide consulting services to businesses. These consultants frequently help businesses to improve financial management before the EBRD can commit funds (they further cooperate with 12 partner banks for the provision of loans). Some views were expressed, particularly in the IT sector, that there is no lack of demand but a lack of selling skills, which is why knowledge is critical. Building the capacities and skills of the labour force and then retaining them is a challenge. Similar to the IT sector is tourism, which also lacks both hard and soft skills, with both sectors particularly attractive for youth employment and creativity generation. Generally, many participants agreed that creativity and innovation are serious laggards in Armenia's entrepreneurial society, going beyond the issue of trainable business management skills, and requiring long-term development capacities.

The Roundtable was of the view that entrepreneurs are often not even aware of their actual needs for technical assistance and even when they do acknowledge it, they are not prepared to pay for these. On the other hand, when workshops addressing these shortcomings are provided free of charge, company owners fail to attend them.

The government is undergoing profound changes and is very slow in adopting reforms. It would also be helpful to receive further support for the inclusion of disadvantaged groups, such as people with disabilities in the regions. A case study of an inclusive bakery in Gyumri was presented, an establishment that employs people with disabilities. Yet marketing and visibility were highlighted as key challenges for the project.

ii. Suggestions of the Roundtable going forward

For some businesses, particularly in the high-tech sector, growth does not necessarily mean job creation, in fact it may mean a reduction of existing labour, and this needs to be reflected appropriately in the impact assessment. Technological development for such firms means elimination of positions or radical shifts of the skillsets required for the jobs. Companies fail to recruit sufficiently qualified professionals, particularly in the regions, due to the outdated and inappropriately managed educational institutions.

The participants agree with the view of the SMEs that networking among entrepreneurs needs to intensify so they can make better use of peer-to-peer learning. The issue of effective networking between SMEs was also discussed. The creation of a platform bringing SMEs, implementing partners and public organisations together might be an effective low-cost option. The SME Agency (DNC) should step up their efforts to transform the Centre into a hub of collaboration between SMEs, the government and various programmes (pilot was presented). Start-ups could get business orientation and the Agency could evaluate SMEs and selectively finance viable ideas, etc. Yet coordination between various programmes must improve, which will translate in better access to successful businesspeople, who could lead by example.

c. Summary of recommendations for next planning cycle

Both SMEs and implementers agree that support is needed in the following areas:

- Provision of tailored, specialised technical assistance, chiefly focused on accessing new markets (industry advice, marketing, certification, online sales skills, etc.).
- Continue some of the general business courses (online and in person): marketing and advertising services, financial management.
- Support to vulnerable groups (woman entrepreneurs, youth, regions) and social entrepreneurship.
- Create a networking platform linking start-ups to successful businesses for learning and training purposes.
- Reporting of project implementation should be in Armenian rather than English.
- Longer term government commitment to developing educational institutions serving real market needs; levelling the playing field for SMEs.





Armenia:
Weaving tradition towards export success



“Thanks to the contacts we established with the support of the EU, quality threads as well as international markets became part of our work.”

Inga Manukyan
Co-founder, director and designer of LOOM LLC

Women in Business programme and EU-SMEDA

Thanks to EU4Business support, LOOM Weaving has expanded its knitwear business beyond the borders of Armenia: advisory support from the EBRD set the company going in branding, finances and sales, while networking support from the EU-SMEDA project supported participation in European trade fairs.



Armenia:
Training young people for a digital future in the regions



“For us, the project was the most successful model compared to other training courses, because it exactly targeted the needs of the business.”

Gayane Araqelyan
Co-founder and Executive Director of the Digital Pomegranate company

Boosting Technological Development in Shirak Marz

The Digital Pomegranate, a software development platform, has got new employees trained thanks to the project, co-funded by the European Union, and implemented by the Microsoft Innovation Center Armenia (MICA). The received support was not limited to the trainings and mentorship: assistance was also provided for setting up the workplace for new employees who had graduated from the trainings.

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