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THE WORLD BANK AND ITS ROLE IN THE ECONOMIC DEVELOPMENT OF ARMENIA

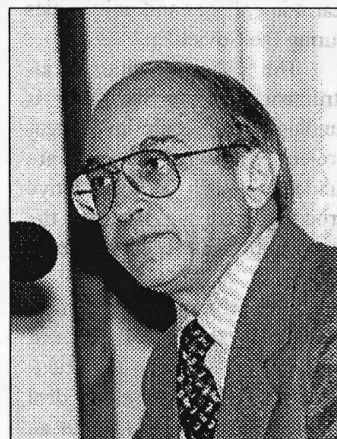
Vahram Nercissiantz

Chief of the World Bank Resident Mission in Armenia

Today I will be speaking about four topics concerning the World Bank. First, I will give a brief description of the background of the World Bank and Armenia's membership in the World Bank. Then I will be talking about the instruments of the World Bank assistance, its strategy, and those projects which have been implemented in Armenia so far, as well as about our future plans.

The World Bank is an international financial organization which was created in 1945, right after the Second World War. The purpose of the World Bank is to enhance peace through economic instruments. Just as the United Nations assists and enhances peace with political processes, the World Bank and the International Monetary Fund try to enhance peace with economic instruments.

Armenia's membership in the World Bank began in September of 1992. Informal contacts between Armenia and the World Bank started in the summer of 1990 and continued through the time when it became a member. Therefore, Armenia's association with the World Bank began



much earlier than that of other CIS countries. With the membership of Armenia in the World Bank several other CIS countries joined the World Bank, and today the membership of the World Bank is 180 countries. In other words, Armenia is a small shareholder of the World Bank.

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The instruments of the World Bank assistance have evolved during the 50 years. Initially it was just financial assistance which was given for only specific projects. Over the years, we have developed other techniques, other instruments. Those include initially providing analytical support to define those sectors in a country where investments can be successfully made. This helps our member countries to develop the analytical foundation on which government decisions are made. Government decisions are always important. They can succeed or fail. However, the probability of success is always higher when there is an intellectual or analytical foundation for that decision.

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During and after the revolution, Armenia has required a great deal of technical assistance in terms of analytical work. Often this kind of analytical work helps the member countries, particularly those in the CIS, to learn about the international experience rather than what they may have read or learnt in colleges and universities during the Soviet Era.

The other traditional instrument that we are using is funding of a specific investment project. Of course, projects are funded through a competitive process where we prioritize the projects by least cost and most effect.

Over the years, we have developed another instrument which is assistance to a particular sector. In this case, we deal not with specific projects but an investment program in a particular sector. We do not know what we will be financing in the beginning. We agree with the

authorities to implement investment programs, small and large, which will meet certain selection criteria and methodology. Funding is provided to all those projects which enter into that investment program and satisfy the investment selection criteria.

In more recent years, we have developed what we call policy of lending. This does not consider any specific project or specific investment program. This is basically to encourage policy reforms, to help the structural reform process. Especially in circumstances when the country in transition tries to overcome the budget deficit cutting expenditures and controlling the expenses to enhance stabilization. The World Bank has provided two such lendings to Armenia.

Another instrument of assistance that exists which we have not yet provided to Arme-

nia but we hope to soon, is guarantees. This is one of the most recent instruments and this is for countries like Armenia where privatization is underway. When we try to attract foreign capital to a country, the investors would like to find out whether there is any kind of guarantee. Here, we are speaking not about commercial guarantees, but political ones. The

“There is much analytical work to be done, there is much to learn.”

investors try to get some kind of guarantee from us which would assure them that there will not be political revolution, nationalization, and other such elements which would negatively impact investments. The World Bank does not provide that kind of guarantee in every country. We provide that guarantee for those countries where we are confident about the country's future, its stabilization, where there is

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Vahram Nercissiantz came to the United States in his teens after graduating from the Armenian Community School in Tehran. He received his Bachelors and Masters degrees from the University of Oregon in finance and economics. After completing fellowship assignments at the headquarters of the Chase Manhattan Bank and Union Carbide Corporation in New York, Mr. Nercissiantz joined the World Bank in 1969 where he has made a career in designing economic policy reforms and investment projects for various developing countries around the world.

In 1970s Mr. Nercissiantz was working mostly for the Africa region assisting the newly independent countries in strengthening their institutional and policy frameworks in country economic management and development.

In 1980s Mr. Nercissiantz was totally engaged in Latin America assisting several countries such as Mexico, Brazil, Peru and Venezuela.

In 1990s Mr. Nercissiantz has been working on the states of the former Soviet Union. Since the summer of 1990 his work has heavily focused on the economic transformation of the newly independent Armenia. Mr. Nercissiantz has advised the Armenian Government on design of the land reform, trade liberalization, privatization, social safety net, and country economic stabilization and management. Since 1992, Mr. Nercissiantz has also focused on mobilization of large amounts of external financial assistance to Armenia for enhancing the structural reforms and generating economic growth.

In June 1992 Mr. Nercissiantz helped establish the World Bank Resident Mission in Armenia, and he is currently the Chief of the Resident Mission.

In October 1995 Mr. Nercissiantz was awarded an honorary doctorate from the Yerevan Institute of National Economy for "his outstanding achievements in research and great contribution to Republic's economic development."

a very good policy dialog and reforms are progressing well.

In addition to that, there are some grants that we give from time to time. These are grants for institutional development. For example, we provided such a grant for lake Sevan to protect the environment. We plan to give a grant to the telecommunications sector which will address the privatization process of that sector. We are trying to see if we can have that type of grant to enhance the institutional framework for the cultural organizations. It is obvious that those organizations are dependent on the Government budget and often have problems being financed from that source. Currently, we are trying to mobilize external and internal resources as well returns from investments, and other sources within the business community. I think it is high time to mobilize resources for cultural development as well. It may seem that the World Bank is providing loans which reminds of the grants or credits given for 35 years and without interest. However, there is a small charge, less than 1% which is to service the loan.

Let us talk about the strategy assistance of the World Bank. When we began to study the situation in Armenia, it was at the time when the Soviet Union was collapsing and many of the subsidies from the center to the republics was decreasing, and the country clearly had to go through structural reforms. Armenia's case was different from the other CIS countries as here there was the additional burden of the earthquake disaster zone. So, one of our early interventions was to try to decrease the weight from the government's shoulders so that it

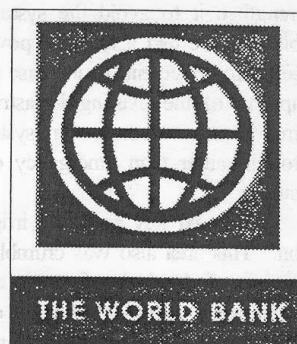
could concentrate on the economic re-structuring, to do the necessary analytical work and try to design policy reforms, and to have time, daily, to deal with the country's economic management. One of the first loans that the World Bank provided was for the earthquake zone: 28 mln. US dollars. That gave an opportunity to the authorities to concentrate on the economic reforms. As I have already mentioned, there is much analytical work to be done, there is much to learn. The officials need to learn from the experience of other countries. After all, we do not want to repeat others' mistakes.

We have the experience of Eastern Europe and Latin America

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where we have gone through these reforms over the years. You might argue that those were not countries which used to be within a centralized economic system. Nevertheless, they had many of the characteristics of CIS countries: the protectionism policies, major distortions flowing from that protectionism, etc. Thus, there is quite a bit of experience that could be shared by the Armenian authorities through analytical work.

We packaged an institutional building loan which helped first to provide some key analytical skills in the areas of trade, liberalization, privatization, social sector development. After that we provided a



training program. I should mention that during these two years we have developed a well-prepared staff which in many areas compares very favorably to some of those in neighboring countries. That partly explains why Armenia has been able to achieve many reforms: it has had such a competent economic team from the very beginning. They are respected in the world. And I am talking about the leaders since 1992, the time period during which the association with the World Bank became more efficient.

The next phase was to focus on the strategy for saving the infrastructure. For some time no repair, no maintenance of the infrastructure had taken place, thus it had begun to crumble. And it came to a point where any further erosion would have required much more investment in the future. I refer to the key areas of infrastructure and particularly to the power sector. Let us remember the conditions in 1992-93 when the electricity supply was irregular, the lines were overloaded, the transformers were not working, etc. There was a danger of having the total system collapse; then, the reconstruction of the system would have required many years. So, there was an emergency need to try to improve the infrastructure, and (continuation on p.4)

strengthen it to avoid the system's collapse. We had a loan for power sector improvement: to increase the capacity of the existing infrastructure; in other words, for system growth rather than emergency operations.

The next key area was irrigation. This area also was crumbling because of the lack of repair and maintenance. And this was in circumstances when agrarian reforms were underway and land was privatized, and farmers were expecting an irrigation war, because the irrigation water supply was declining due to the erosion of the infrastructure. So, the next intervention was the 42 mln. US dollar loan.

Another problem was the roads. Armenia is a landlocked country which needs to export goods, but is under blockade. Still, its internal market is too small to be able to affect the economy. Roads are a basic infrastructure and our next assistance was in that area.

But first were the policy loans which we made in terms of enhancing the structural reforms which flow directly to the budget. However, that was after we had agreed with the authorities on some of the structural and infrastructure reforms.

Another way of intervention was the Social Investment Fund which was a specific investment. We tried the Social Investment Fund in Latin America and succeeded in a number of countries including Nicaragua, Albania, and other Central European countries. And currently we are trying it in Armenia. The idea of it basically is that a micro-project is being implemented within the community, where the community organizes itself and is directly involved in the

project implementation. At the same time, by providing funding for such specific, defined projects, you increase employment. This is a solution to some of the social concerns.

The next phase of our social intervention is into the health and education sectors. It is obvious, that the latter can not sustain itself and has to be part of a reform program. Currently, the World Bank is considering a project which will help fund investments in that sector and especially in the basic health or family health care system.

In education, again, the situation is not satisfactory and a way is to be found to come out of this predicament. There is need for a sup-

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port provision for textbooks, for teachers training for an improved education delivery system.

There are expectations for investments in the industrial sector. I hope that in the near future there will also be long-term investments in agriculture, as well as in housing sector.

The World Bank does not consider giving loans to state-owned enterprises. Why would we provide loans to enterprises which have already proven that they cannot produce competitively? They have to be privatized and that process is currently underway.

The first loan for enterprise development will be 16.75 mln dol-

lars and will be approved on December 19. The idea here will be that the World Bank will bring wholesale resources and distribute them to private enterprises whether they are privatized or emerging. That will be implemented on the basis of three selection criteria. The investment will be provided through banks.

I hope before too long there will be a loan for agriculture which I am calling loans for agricultural support services. Generally, land reform in Armenia was implemented in the right way, however, this does not mean everything went smoothly. Our intervention in this sector will address those shortcomings. One of the most essential goals is the privatization of the agro-processing enterprises, the formulation of the cadaster system, and improvement of farmers professional skills.

I would like to once again emphasize that the World Bank appreciates the economic performance of the Republic of Armenia. There are three years with registers growth, it is about two years that the Dram is stable which, factually, is the most stable currency in the region. Of course, during the transition period there are a lot of things to be done. Results of the reforms do not become evident immediately. Fruits of the reforms do not come immediately after the decisions are made. However, I should say that in countries where the World Bank has tried, the production response has been expressed in living standards and quality of life in a short time.

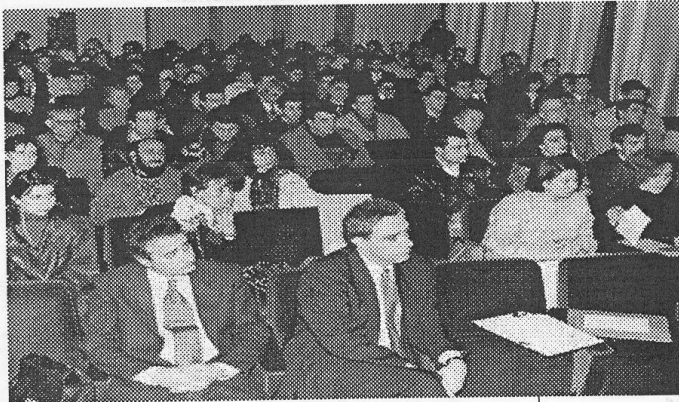
Those of the young generation who are involved in today's processes will see the fruits of the reforms. I hope that these speedy reforms will bring significant improvement in living standards.

QUESTIONS AND ANSWERS

Q. - The World Bank has given loans for roads. How is control being implemented? You, probably, know that the quality of the road built to Sevan is much lower than the quality of the road that it used to be.

A. - Our bank has certain mechanisms of control--and experts as well. Over the years, we have come up with the idea that the procurement is gone through a competitive process. We have supervisory missions which regularly arrive in Armenia and know how to check. We had a case, for example, and that was the only case in Armenia, where there seemed to be a lack of adequate procedural supervision in the implementing agency. We have seen this in a number of projects around the world.

Every project has to be audited independently by independent auditors. The independent auditors have different ways of checking and letting us know. I also have my ear to the ground. I am usually trying to understand the situation, make



sure that we do not abuse public funds. And I must say, no funds so far have been abused.

There is another thing I would like to mention. We also examine the project in terms of its impact. We have a group that we call operation and evaluation which directly reports to the President of the World Bank. They evaluate after the projects are done to see whether the objectives of the projects are met. From such analysis, we acquire lessons of experience. The purpose is not to

say what we did well and what we did not do well. The idea is to gather lessons and experience to better design future projects.

Q. - As someone well familiar with the so-called kitchen (or inside workings) how would you evaluate the perspectives of the economic development of Armenia?

A. - Structural reforms are in place. Some additional structural reforms will have to take place. I think, the next phase is going to be more development and production, not so much stabilization. We have had 5% growth so far. With the privatization of enterprises, I expect higher level of growth. So, I think, by the end of this decade the economic benefits and fruits of the reforms will be visible much more than they are now.

Q. - A considerable sum of money has been given to Armenia so far. Don't you think that because of this, Armenia may become a puppet of the World Bank?

A. - Funds, as I said earlier, are for 35 years and with hardly any interest. I am sure a country like Armenia is going to become quite developed. And the loans that we are giving now, in comparison to both the size of what the economy will be when the loans come due, and even in terms of the dollars inflation, will be very insignificant. If we take into account the concept of the time value of money I do not see reasons to worry.

Q. - To what extent does the problem of Nagorno Karabakh affect the policy of the World Bank towards Armenia?

A. - Armenia is an independent state. Nagorno Karabakh is a different entity. Surely, the conflict there has something to do with the apprehension of private investors. After all, a lot of investors hear only about Karabakh, Chechnia, Abkhazia and they say this is a bad address in which to invest. However, in terms of the World Bank I should say that we are not a political

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organization and we do not follow a political agenda. We have our own criteria and we have basically said that the conflict does not affect the republic's resources, our projects. Thus, it does not make sense for us to withdraw from assisting a country which is very progressive in policy reforms and is committed to the development of the country.

Q. -What are the relationships between the World Bank and the present Government of Armenia?

A. - Obviously, to assist a country, the World Bank has to have an entry point. The entry point in all cases is development. We have very close working relations with the Government. I also have very close relations

with other sectors, as well as with the Parliament. I have close contacts in the judicial sector, both in the Constitutional Court and the Supreme Court. At present, we are trying to see if we can assist in judicial sector reforms. And the reason being that a lot of reforms that we have done so far cannot be sustained unless there is a judicial sector which would provide a process for the continuation of reforms. I visit the rural areas of the country quite often, I meet farmers and industrialists. I keep in touch with the media. Contacts is one of the points on my agenda.

THURSDAY, DECEMBER 19



MR. GAGIK HAROUTUNYAN

President of the Constitutional Court
of the Republic of Armenia

presents a lecture on

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