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Trade Policy Review Body

TRADE POLICY REVIEW

Report by the Secretariat

ARMENIA

Revision

This report, prepared for the first Trade Policy Review of Armenia, has been drawn up by the WTO Secretariat on its own responsibility. The Secretariat has, as required by the Agreement establishing the Trade Policy Review Mechanism (Annex 3 of the Marrakesh Agreement Establishing the World Trade Organization), sought clarification from Armenia on its trade policies and practices.

Any technical questions arising from this report may be addressed to Mr. John Finn (tel: 022 739 5081).

Document WT/TPR/G/228 contains the policy statement submitted by Armenia.

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SUMMARY

1. Armenia's accession to the WTO in 2003 consolidated a process of trade liberalization and institutional reforms that started soon after its independence from the Soviet Union in 1991. Since accession, reform has continued. Armenia has a liberal trade and investment regime. The average applied tariff, at 2.7%, is among the lowest of WTO Members. It grants MFN and national treatment to foreign investors, which are present in almost every economic sector. In many areas, particularly in services, Armenia's trade policies are more liberal than its WTO accession commitments.

2. Economic stability, along with foreign remittances and investment from the large Armenian diaspora, led to high levels of economic growth up until the global financial crises hit Armenia in 2009. Continued efforts to improve implementation of institutional and regulatory reforms and to develop a more diversified economy are key to Armenia's future economic growth.

(1) ECONOMIC ENVIRONMENT

3. Armenia is a land-locked country in the Southern Caucasus region which borders Azerbaijan, Georgia, Iran, and Turkey. The economic difficulties it faced with the collapse of the Soviet Union and the chaos that followed were exacerbated by the war in Nagorno Karabakh and the subsequent closure of its borders with Azerbaijan and Turkey.

4. Economic stabilization started with the introduction of the Armenian dram as the national currency late in 1993. At the same time Armenia began, with international support, to implement a wide range of economic reforms that included trade liberalization and its application to accede to the GATT and later the WTO.

5. Before and after acceding to the WTO in 2003, Armenia's economy grew very strongly, almost doubling in real terms between 2003 and 2008. The main driver of growth was domestic consumption fuelled by remittances from abroad and by improved productivity, which followed the rapid restructuring of the economy from the mid 1990s. GDP reached nearly US$12 billion and GDP per capita US$3,684 in 2008.[1]

6. Since 2003 the economy has changed a lot. Agriculture grew less rapidly than other sectors and its share of the economy fell to 18% in 2008, although it still employed almost half of the workforce. Manufacturing also declined in relative importance as services grew strongly to reach nearly three quarters of GDP in 2008. Within the services sector, construction grew most rapidly reaching 30% of GDP in 2008.

7. Unfortunately, the economy went into reverse in 2009. The global financial crisis and the down-turn of the world economy reduced remittances and foreign investment. The sudden drop in investment hit property prices and the construction industry. As construction activity had grown to be such a large part of the economy the decline in this sector hurt other areas. Overall economic growth went from 7% in 2008 to about -15% in 2009.

8. Throughout the review period of 2003 to 2009, inflation was kept in check (at around 4%) by the independent Central Bank. For most of this time the Armenian dram was allowed to float. The fiscal deficit was kept reasonably low and public debt decreased significantly as a percentage of GDP, although both indicators worsened considerably in 2009.

9. Overall, trade is about 43% of GDP and Armenia has a large deficit in trade in both goods and services (at 25% of GDP). During the review period, the trade deficit increased due to strong domestic demand and the loss of competitiveness of Armenian exports as large foreign exchange inflows caused the dram to appreciate. Furthermore, Armenia's closed

[1] The average exchange rate for the first half of 2009 was dram 1 = US$350.

borders, particularly with Turkey, led to transport costs higher than they might otherwise have been. The impact of high transport costs is particularly hard on heavy bulk commodities, like minerals, which make up a large proportion of Armenia's exports.

10. Foreign direct investment, mainly from Russia and the EU, increased considerably between 2003 and 2008, particularly in utilities, financial services, mining and food processing.

(2) INSTITUTIONAL FRAMEWORK

11. During the process of acceding to the WTO Armenia undertook considerable legal and institutional reform and made a comprehensive set of commitments. For example, it bound all tariff lines at rates between 0% and 15%, it replaced *ad valorem* customs fees with specific duties, and its services commitments covered almost all sectors.

12. Since it acceded, the process of legal and institutional reform has continued. Much of the reform is intended to improve the investment climate, governance, transparency and accountability: the Constitution was amended to improve the distribution of powers within the State; the Ministry of Economy became responsible for trade policy; and the State Revenue Committee took over responsibility for tax revenue and customs administration.

13. Armenia continues to face resource constraints to deal comprehensively with WTO issues. It has a Permanent Mission in Geneva, which currently has one diplomat who is responsible for WTO matters and other economic issues in other International Organizations.

14. In the negotiations under the Doha Development Agenda, Armenia is a member of the group of recently acceded Members (RAMs) and has participated in its proposals.

15. Armenia has nine trade agreements in force with other members of the Commonwealth of Independent States (CIS). Armenia is also working towards beginning negotiations on a deep and comprehensive trade agreement with the EU. Such agreement would go beyond tariffs and would require close alignment with the EU's laws in areas related to trade, including SPS and TBT measures, and intellectual property.

(3) MEASURES AFFECTING MARKET ACCESS FOR GOODS

16. The administration of customs procedures was significantly improved during the review period. The institutional structure was streamlined with the creation of the State Revenue Committee in 2008. At the same time, customs procedures were simplified and processing of imports made more efficient. The improvements included: the introduction of an on-line customs declaration system; the launch of a traffic light system for inspection of goods entering Armenia; and the reduction in the number of import documents required (from nine to three). However, customs clearance is still perceived by users as relatively slow and subject to a certain amount of corruption.

17. Despite improvements during the review period, there remain some concerns about the efficiency and transparency of the application of the legislation on customs valuation. The authorities stated that under-declaration of import values is a persistent problem that explains why transaction value is often not accepted for customs valuation. They also pointed out that importers have the right to appeal decisions of the customs authority and to use bank guarantees to cover duties in cases where documentation is incomplete.

18. Armenia's average applied MFN tariff is 2.7% with a simple tariff structure: no tariff quotas; 73% of tariff lines are duty free; and almost all the rest subject to a 10% tariff rate. There are 19 alcohol and tobacco items subject to non-*ad valorem* tariffs, for which

ad valorem equivalents (AVEs) were impossible to calculate. These specific duties are expected to be converted into *ad valorem* charges in January 2011.

19. Under Armenia's free-trade agreements with some CIS countries, all imports are duty free with no implementation period. Although 31% of Armenia's imports come from these countries, trade diversion is probably low given that duty-free rates also apply to most MFN trade.

20. Apart from import prohibitions applied to a number of products for health, security and environmental reasons, Armenia does not apply quantitative restrictions to imports. Anti-dumping and safeguard legislation has been in place since before accession to the WTO, but, so far, no investigations have been conducted and no contingency measures have been taken.

21. Certain imports are affected by a business licensing system applied to a list of economic activities, such as pharmacies and pharmaceuticals. Some of these licences are non-automatic and only granted with the approval of a licensing commission.

22. As in other areas, Armenia is working towards bringing its technical regulations and standards into conformity with the EU. Armenia did not adopt urgent measures during the review period and has notified to the WTO all the technical regulations that were considered to affect trade.

23. SPS policy, legislation, and implementation is also moving towards convergence with the EU. Nevertheless, lack of resources remains a significant problem, affecting the application of SPS rules not only for imported products but also for domestic production.

(4) MEASURES DIRECTLY AFFECTING EXPORTS

24. All exports of goods from Armenia are subject to a simple customs declaration system. During the review period, the documentation and the time required to export have been reduced. However, certification of origin is perceived by exporters as costly and complicated.

25. Armenia does not apply export taxes, although its legislation permits them. Export prohibitions apply only to a limited range of products such as weapons, ammunition, explosives, and narcotics. Armenia applies only those trade embargoes imposed by the UN Security Council Resolutions. Permission is required for exports of rare plants, animals, and objects considered of interest to the national heritage.

26. During the review period, there were no export processing zones in Armenia, no officially supported export credit schemes, and the government did not provide subsidies contingent on exports. The Armenia Development Agency, a public agency mainly financed by international organizations, is responsible for export promotion.

(5) OTHER MEASURES AFFECTING INVESTMENT AND TRADE

27. Armenia has continued to improve the legislative base for business, investment and trade. Although implementation continues to be a problem, this too is being improved. An enterprise (including an importer) must register as a legal entity in the State Registry, as well as in the regional offices of the tax authority and customs. A single rate of profit tax, at 20%, applies to all commercial organizations.

28. Foreign investment has been vital for economic growth in Armenia and is officially encouraged through the development of investment-friendly policies. The only restriction on foreign investment is the Constitutional ban on foreigners owning land in Armenia. Investors are also protected from adverse changes in legislation and from nationalization of property by the State. In addition, during the review period, the

Government offered a profit tax break and a tariff exemption for imports of certain capital inputs. However, there is no information available on their utilization.

29. Privatization continued during the 2003-09 period. As of end 2009 the process was essentially completed. Most of the enterprises still owned, wholly or partially, by the State are involved in health care, education, and military activities. The rest are non-operational.

30. Although Armenia's legislation on competition policy was enacted in 2000 and has since been brought into approximate conformity with that of the EU, concerns remain about the reach of the competition authority's powers and the lack of competition in several sectors.

31. In line with its WTO accession commitment, in October 2009 Armenia presented its initial offer and started negotiations with other WTO Members to accede to the Government Procurement Agreement. This follows the enactment in 2005 of the Law on Procurement, which applies to purchases of goods and services by public bodies. The preferred method of procurement is lowest price, and the Law contains no provisions promoting local content or domestic suppliers. Open tendering accounted for 78% of the total value of contracts awarded in 2008.

32. Since 2003, Armenia has continued to update its intellectual property legislation with new laws on copyrights and patents and amendments to its law on trade marks. In addition, draft laws sent to the National Assembly would extend the coverage of rights to geographical indications and appellations of origin. As in other areas, implementation of the law remains a challenge.

(6) TRADE POLICIES BY SECTOR

33. Agriculture development faces several major constraints such as: small and fragmented farms; mountainous terrain; an expensive and inefficient irrigation system; and lack of farm support services.

34. Despite these constraints, some subsectors, particularly alcoholic beverages, have scope for development. Improved irrigation and better financial services for farmers would also help agricultural development. However, significant foreign investment in agriculture is unlikely given the Constitutional prohibition on land ownership for non-Armenian citizens.

35. Armenia is a net food-importing country with most imports coming from Russia. Its main agriculture export is brandy, most of which goes to Russia.

36. Armenia has significant deposits of molybdenum, copper, and gold and smaller deposits of several other minerals. Thus, despite high transportation costs, mining accounts for over a quarter of Armenia's exports and has been a source of considerable foreign investment. The North-South Road Corridor, which would link the mining areas with Georgian ports on the Black Sea, would help to address transport costs.

37. The services sector grew strongly in both relative and absolute terms during the review period. In acceding to the WTO, Armenia undertook commitments in most service areas, the main exceptions being postal services, passenger transport, and air and rail freight transport.

38. With the exception of hydroelectricity, all primary energy supplies in Armenia are imported. The energy sector is dominated by Russian enterprises, which either own or operate the major power plants, the electricity distribution system, and the gas pipeline network. Although the infrastructure is being improved, much of it needs to be upgraded and some of it needs to be replaced.

39. Purchase and sale prices for electricity, gas, and thermal energy (in

addition to water and telecommunications) are set by the Public Services Regulatory Commission. The purchase prices for electricity set by the Commission encourage production from renewable sources. The Commission does not set prices for transport fuel, all of which is imported. The market for the import and distribution of fuel is concentrated with only two firms having 84% market share.

40. The financial services sub sector is relatively small and underdeveloped. Although it grew at an annual rate of 29% per year in 2003-08, this was from a very small base. Since 2003, Armenia has also taken steps to improve the stability of, and confidence in the banking sector with a deposit guarantee scheme and increased capital requirements introduced in 2004 and 2009 respectively. There are no restrictions on participation of foreign investors in the banking and insurance sectors. Furthermore, going beyond its accession commitments, Armenia permits branches of foreign banks to accept deposits from Armenian nationals. However, there are some restrictions on cross-border insurance services.

41. Telecommunications in Armenia are still at a developing stage, particularly internet access. The main cause of this lag in development is lack of investment during 1998-2004 when the market was controlled by a single company. During the review period, the Government renegotiated the sole service supplier's licence and gradually ended its exclusive rights. As a result, there are now no restrictions on the participation of foreign investors and, by end 2009, the applied legislation was more liberal than Armenia's GATS commitments.

42. The transport sector in Armenia is relatively well developed but in need of significant funds to maintain and upgrade existing routes and to build new ones. Armenia is participating in a number of regional initiatives, which are designed to improve transport in the region. Foreign investment is focused on road construction while public funds are mostly devoted to road maintenance. In 2008, a 30-year licence was granted for a Russian company to provide railway passenger and freight services, but the infrastructure remains state-owned.

43. Foreign professionals or enterprises are not restricted from setting up law or accountancy firms in Armenia. Both service sub sectors have undergone a lot of reform since 2003.

44. The Chamber of Advocates was established in 2005 and replaced the two bar unions. In August 2009, the Association of Accountants and Auditors of Armenia was recognized as the professional association representing accountants and auditors.

45. There are no restrictions on foreign investment in hotel services or on foreign nationals applying for tour-guide licences. Tourism is expanding in Armenia, with visitors coming mainly from countries with large diaspora communities. However, high flight costs and limited schedules, as well as high taxes on passengers and underdeveloped infrastructure appear to be hampering tourism growth.