



IPR

INVESTMENT POLICY REVIEW



ARMENIA



UNITED NATIONS



IPR

INVESTMENT **POLICY** REVIEW



ARMENIA



UNITED NATIONS
Geneva, 2019

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NOTE

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The following symbols have been used in the tables:

- **Two dots (..)** indicate that data are not available or not separately reported. Rows in tables have been omitted in those cases where no data are available for any of the elements in the row.
- **A hyphen (-)** indicates that the item is equal to zero or its value is negligible.
- **A blank in a table** indicates that the item is not applicable.
- **A slash (/) between dates** representing years – for example 2009/10 indicates a financial year.
- **Use of an en dash (–) between dates** representing years – for example 2008–2010 signifies the full period involved, including the beginning and end years.
- **Reference to “dollars” (\$)** means United States dollars, unless otherwise indicated.
- **Annual rates of growth or change**, unless otherwise stated, refer to annual compound rates.
- **Details and percentages** in tables do not necessarily add to totals because of rounding.



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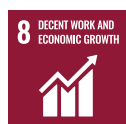


PREFACE

UNCTAD Investment Policy Reviews (IPR) are intended to help countries improve their investment policies with the objective of meeting the Sustainable Development Goals (SDG) and to familiarize governments and the international private sector with an individual country's investment environment. The reviews are considered by the UNCTAD Commission on Investment, Enterprise and Development. The analysis is based on the Investment Policy Framework for Sustainable Development (IPFSD) and its core principles and guidelines (UNCTAD, 2015). The recommendations of the IPR are then implemented with the technical assistance of development partners, including UNCTAD. The support to beneficiary countries is delivered through a series of activities that can span several years. Consistent with the SDGs, IPRs encourage official development assistance and investment in countries where needs are greatest. The IPR recommendations are in line with countries' national development plans and focus on key development sectors, including agriculture, mining, manufacturing, tourism and infrastructure. By helping countries in this manner, the IPR programme notably contributes to:



SDG 1 target b: “to create sound policy frameworks at the national, regional and international levels, based on pro-poor and gender-sensitive development strategies, to support accelerated investment in poverty eradication actions”.



SDG 8 target 2: “achieve higher levels of economic productivity through diversification, technological upgrading and innovation, including through a focus on high-value added and labour-intensive sectors”.



SDG 10 target b: “to encourage official development assistance and financial flows, including foreign direct investment, to States where the need is greatest, in particular least developed countries, African countries, small island developing States and landlocked developing countries, in accordance with their national plans and programmes”.



SDG 17 target 3: “to mobilize additional financial resources for developing countries from multiple sources”.

The IPR of Armenia was initiated at the request of H.E. Mr. Armen Sarkissian, President of the Republic of Armenia. It analyses the legal and regulatory framework for investment, and contains a strategic analysis on how to attract export and efficiency-seeking investment to Armenia. The IPR is based on a fact-finding mission undertaken in March/April 2019, as well as additional information made available to UNCTAD until 15 October 2019. The mission received the full cooperation of the relevant ministries, departments and agencies, in particular the Ministry of Economy, and the Trade Representative of Armenia to Switzerland, Mr. Hayk Hovhannissyan. The mission also benefited from the views of the private sector, both foreign and domestic, as well as bilateral partners and development agencies. The Government also provided logistical support to the IPR process and several agencies of the United Nations in Armenia, including the United Nations Development Programme (UNDP) and the United Nations Industrial Development Organization (UNIDO), provided substantive contributions. A preliminary version of this report was discussed at national validation workshops in Yerevan on 4 October 2019. This final version contains all the comments and suggestions gathered from stakeholders.

Geneva, November 2019



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ABBREVIATIONS

| | |
|---------------|--|
| ACIF | Armenian contractual investment fund |
| ADB | Asian Development Bank |
| ADR | alternative dispute resolution |
| AI | artificial intelligence |
| AMD | Armenian Dram |
| ARMNAB | National Accreditation Body of Armenia |
| ATOM | advanced tomorrow |
| BIT | bilateral investment treaty |
| CFC | controlled foreign company |
| CIS | Commonwealth of Independent States |
| CIT | corporate income tax |
| CEPA | Comprehensive and Enhanced Partnership Agreement |
| CMO | contract manufacturing organization |
| CMT | cut-make-trim |
| CSR | corporate social responsibility |
| CRO | contract research organization |
| DDI | direct domestic investment |
| DFDI | diaspora foreign direct investment |
| DIAE | Division on Investment and Enterprise |
| DWCP | Decent Work Country Programme |
| EA | European Cooperation for Accreditation |
| EAEU | Eurasian Economic Union |
| EBRD | European Bank for Reconstruction and Development |
| ECU | Eurasian Customs Union |
| EIA | environmental impact assessment |
| EIF | Enterprise Incubator Foundation |
| EIS | environmental impact studies |
| EPZ | export processing zones |
| ESG | environmental, social and governance |
| EU | European Union |
| FAST | Foundation for Armenian Science and Technology |
| FDI | foreign direct investment |
| FET | fair and equitable treatment |
| FEZ | free economic zone |
| FTA | free trade agreement |
| GDP | gross domestic product |
| GNI | gross national income |
| GSP | Generalized System of Preferences |
| ha | hectare |
| IBFD | International Bureau of Fiscal Documentation |
| ICC | International Chamber of Commerce |
| ICSID | International Centre for the Settlement of Investment Disputes |
| ICT | information and communication technology |
| IFI | international financial institution |



| | |
|-----------------|---|
| IIA | international investment agreement |
| ILO | International Labour Organization |
| IMF | International Monetary Fund |
| IP | intellectual property |
| IPA | investment promotion agency |
| IPFSD | Investment Policy Framework for Sustainable Development |
| IPR | investment policy review |
| ISDS | investor–State dispute settlement |
| ISO | International Organization for Standardization |
| IT | information technology |
| MFN | most-favoured nation |
| MNE | multinational enterprise |
| MSMEs | micro, small and medium-sized enterprises |
| MRO | maintenance, repair and overhaul |
| NT | national treatment |
| NPUA | National Polytechnic University of Armenia |
| OBOR | One-Belt-One-Road |
| ODA | official development assistance |
| OECD | Organization for Economic Cooperation and Development |
| PCT | Patent Cooperation Treaty |
| PE | permanent establishment |
| PPP | public–private partnership |
| R&D | research and development |
| SARM | National Institute of Standards of Armenia |
| SAFE | simple agreements for future equity |
| SDGs | sustainable development goals |
| SEA | strategic environmental assessments |
| SEZ | special economic zones |
| SME | small and medium-sized enterprises |
| SOE | State-owned enterprise |
| SRC | State Revenue Committee |
| STEM | science, technology, engineering, and mathematics |
| TIFA | trade and investment framework agreement |
| TIP | treaty with investment provisions |
| TRIPS | trade-related aspects of intellectual property rights |
| TVET | technical and vocational education and training |
| UAE | United Arab Emirates |
| UNCITRAL | United Nations Commission on International Trade Law |
| UNCAC | UN Convention on Anti-Corruption |
| UNCTAD | United Nations Conference on Trade and Development |
| UNDP | United Nations Development Programme |
| UNIDO | United Nations Industrial Development Organization |
| VAT | value added tax |
| YSU | Yerevan State University |
| WHT | withholding tax |
| WIPO | World Intellectual Property Organization |
| WTO | World Trade Organization |
| WTTC | World Travel and Tourism Council |



KEY MESSAGES

- Almost 30 years after independence, Armenia has reached a turning point. Calls for improved governance and increased representation, together with mounting discontent about the conflict of interest generated by the proximity between the political and economic spheres, have fuelled a peaceful revolution in 2018. A new Government is in place, setting the path towards sustained democracy and good governance. The authorities have promised to deliver an *economic revolution* to fight poverty and unemployment through a structural transformation led by high-tech activities and supported by the modernization of traditional ones. Plans to improve the business environment, increase investment, including foreign direct investment (FDI), and fight corruption have been announced. The Government has called on UNCTAD to provide support in identifying key obstacles to efficiency-seeking investment and assist Armenia become an export hub for both goods and services.
- Armenia's efficiency profile is characterized by a well-educated workforce, strong skills heritage and competitive salary levels. In addition, planned infrastructure projects could facilitate access to key markets, and add to existing trade preferences, including with the Eurasian Economic Union (EAEU) and the European Union (EU).
- The Investment Policy Review (IPR) has identified several export and efficiency-seeking industries that can aim for billion- and half-billion-dollar export sales in goods and services over the next 10 to 20 years:
 - *Billion-dollar club* – industries already near \$1 billion in value of annual exports or which can achieve the target within 10 years, i.e. high technology, with a special focus on artificial intelligence, data science and deep technology, tourism and textile and garments.
 - *Emerging billion-dollar club* – industries which could achieve \$1/2 billion in value of annual exports in 10 years and strive for \$1 billion in 20 years. Targets are wine, agri-business and pharmaceuticals.
 - *Nascent candidates* – industries with potential but for which it is too early to set export targets. These are business process outsourcing, regional logistics and food safety, aircraft repair and maintenance, regional financial services and higher education.
- FDI inflows have been on a declining trend since 2008 and, currently, a “wait-and-see” attitude, associated with the recent political transition, prevails among investors. Promising sectors cannot be sustainably developed solely based on the existing efficiency profile – modernizing investment is required and policy actions needed to reassure investors.
- Investment in the target industries can come from a mix of sources, and local investors, supported by the diaspora, will continue to play a key role. For each target industry, a tailored investment promotion strategy needs to complete sector-specific policy packages, including but not limited to tax policy measures, as well as concrete actions to improve the overall investment climate. Chief among those are measures aimed at strengthening governance, ensuring a level playing field among economic actors and promoting the Government's role of guarantor thereof.
- Beyond measures to tap the export potential through investment, the IPR is guided by the broader policy objective of promoting inclusive growth and sustainable development – in particular spreading benefits to the regions, employment creation and linkages with local suppliers. It recommends increasing domestic value-added by moving to full package manufacture in the textiles and garments industry, and extending benefits to areas outside Yerevan in tourism. It also considers ways to deepen the high-technology sector and make Armenia a leading hub for innovation, data science and artificial intelligence (AI), as well as how to extend R&D capability in the pharmaceutical industry and transform a small generics industry into larger-scale manufacturing.



CONTEXT

Armenia faces unique geopolitical challenges and opportunities. The country is landlocked and faces important trade limitations. These are associated with border restrictions to the East (Azerbaijan) and West (Turkey), resulting from tensions and the unresolved dispute over the Nagorno-Karabakh region, and from international sanctions on its neighbour to the South (the Islamic Republic of Iran) as well as on its main trading partner (the Russian Federation). In addition, one of the main export routes, the Verkhniy Lars border crossing between Georgia and the Russian Federation, becomes often impracticable due to the weather conditions (when snow or rain impede transit), while exports through the Georgian ports on the Black Sea are affected by unreliable ferry schedules. Armenia, however, is also the cradle of a trading civilization at the crossroads between the Eurasian Economic Union (EAEU), the European Union (EU) and the Persian Gulf countries, which it is uniquely positioned to service, thanks to its proximity and preferential trade regimes.

Sustained growth in the early 2000s has spurred remarkable economic progress, but poverty and unemployment remain high. During 2001–2007, the economy was growing at an average rate of 12.5 per cent per year. It was fuelled by high inflows of remittances and foreign direct investment (FDI), which stimulated domestic demand and the development of sectors including financial services, information and communication technology (ICT) and extractive industries. A number of external shocks depressed growth over the last decade, when Armenia was hit by the global economic and financial crisis, the reduction in copper prices since 2011 and the economic slowdown in the Russian Federation. As these factors subsided, the Armenian economy returned to higher growth rates, with gross domestic product (GDP) expanding by 7.5 per cent in 2017 and 5.2 per cent in 2018.¹ Economic growth has had a positive impact on poverty reduction and inequality has declined (IMF, 2017). However, unemployment remains high (at 16.9 per cent in the 4th quarter of 2018) and 25.7 per cent of the population still lived under the national poverty line in 2017, according to the Statistical Committee of the Republic of Armenia. Also, geographical disparities remain strong, with the uplands areas often poorer (ADB, 2018).

A range of ambitious policy reforms has supported Armenia's performance. A wave of privatizations and the adoption of a liberal foreign investment law in the 1990s have spearheaded the transition to a market economy. Although more than 140 State-owned enterprises (SOEs) remain in operation, the private sector now accounts for about three quarters of economic activity. In addition, since the mid–2000s, a series of reforms have streamlined regulations and brought several laws and policies in line with international practice. A new Comprehensive and Enhanced Partnership Agreement (CEPA) with the EU, signed in November 2017, is expected to further support the reform process.² A constitutional referendum in December 2015 has also changed the structure of Government and introduced a parliamentary democracy. These and other reforms have resulted in Armenia's climbing in international business rankings (World Bank, 2018a; World Economic Forum, 2019).

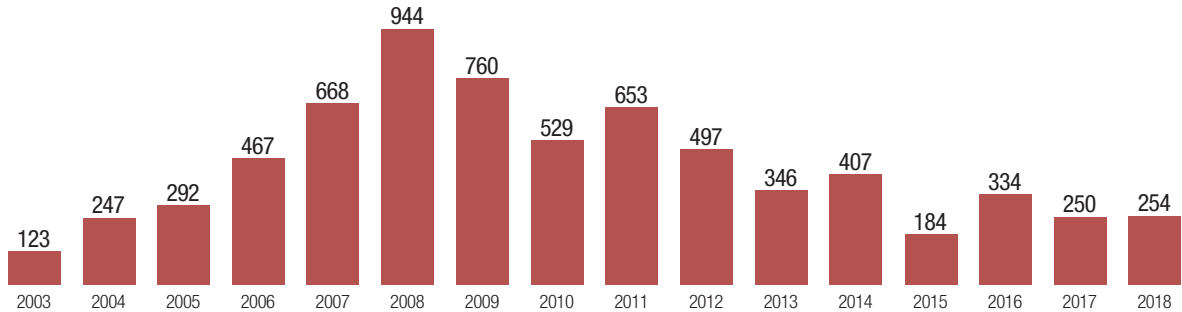
The economy is open to trade, and exports are on the rise and increasingly diversified. Member of the World Trade Organization (WTO) since 2003, Armenia is also signatory to bilateral trade agreements with several countries of the Commonwealth of Independent States (CIS). In 2015, Armenia acceded the EAEU, a customs and economic union with Belarus, Kazakhstan, Kyrgyzstan and the Russian Federation. Generalized system of preferences (GSP) arrangements are in force with several trading partners, including Canada, Switzerland and the United States, and Armenia has GSP+ status with the EU. Beyond the recent



CEPA, the Government signed an open skies agreement with the EU to facilitate and upgrade transport connectivity. Trade in goods and services is equivalent to 87 per cent of GDP, and the export of goods more than doubled between 2010 and 2017 (WTO, 2018), resulting in sustained improvements in the current account. Although exports remain resource-dependent, with mining products (mainly copper and ores) constituting the main export, some diversification is taking place into non-traditional markets (e.g. China and the countries of the Persian Gulf) as well as products (e.g. tobacco, wine, fresh fruits and vegetables, clothing or information and technology (IT) products).

FDI flows have mirrored economic performance, but struggle to recover... In the first decade of the 2000s, Armenia attracted increasing inflows of FDI in energy, mining, ICT, banking and real estate, among others. This was the outcome of privatization initiatives as well as investment by resourceful diaspora individuals who channelled investments to high growth market segments.³ The economic and financial crisis halted the growth trajectory of FDI inflows to Armenia, and they have been trending downwards since their peak of \$944 million in 2008 (figure 1). The reduced scope for privatization-related inflows as well as divestment in the banking sector associated with more stringent deposit requirements contributed to the downfall. More recently, disputes affecting headline projects with foreign investment, such as the gold development project by Lydian International (Amulsar Gold Project),⁴ purported instances of restrictive business practices and uncertainties associated with the recent political transition have contributed to a “wait-and-see” attitude among investors. As a result, average FDI inflows between 2014 and 2018 have almost halved compared to their 2009–2013 levels (table 1).

Figure 1. Armenia, FDI Inflows, 2003–2018 (Millions of dollars)



Source: Central Bank of the Republic of Armenia and UNCTADStat.

...and Armenia is not performing as well as competitor economies in FDI attraction. Armenia was not alone in following such an FDI trajectory. Average annual inflows of FDI fell by a quarter across transition economies in the aftermath of the global economic and financial crisis. However, some of Armenia’s key competitors in FDI attraction managed to reverse the decline faster, including its immediate neighbours (Azerbaijan and Georgia). Armenia is also among the countries that experienced the most significant losses in terms of FDI per capita and relative to GDP in the comparators’ sample between 2009–2013 and 2014–2018. Furthermore, its FDI stock is the second lowest in the region in absolute terms, and among the lowest in relative terms (table 1). While the statistics fail to capture foreign investment that is channelled to Armenia through remittances, they also point to the need to identify and address remaining weaknesses in the investment climate as well as the economic structure of the country, that are together failing to stimulate broad-based foreign investor interest.

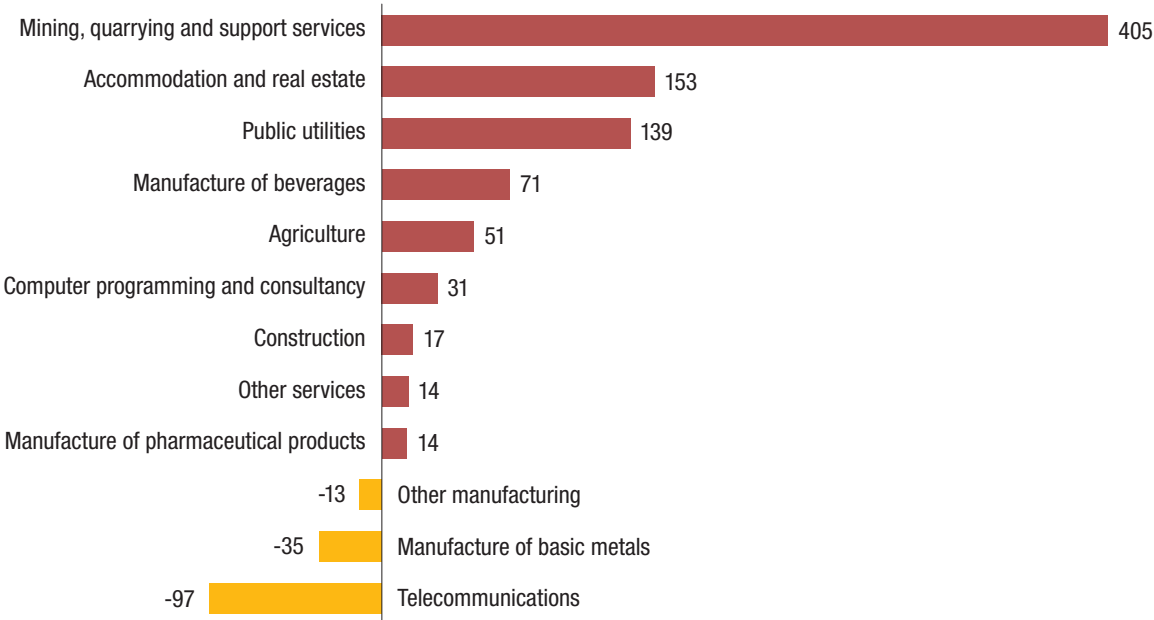
Table 1. FDI attraction performance of Armenia and selected regional comparator economies

| Economies | Average inflows of foreign direct investment | | | | | | Foreign direct investment stock | | | | |
|------------------------------------|--|-----------|----------------------|-----------|-------------------------------------|-----------|--|-----------|-----------------------------|----------------------|--------------------------------------|
| | Millions of dollars | | Per capita (dollars) | | Per \$ 1 000 gross domestic product | | As percentage of gross fixed capital formation | | Total (millions of dollars) | Per capita (dollars) | Percentage of gross domestic product |
| | 2009–2013 | 2014–2018 | 2009–2013 | 2014–2018 | 2009–2013 | 2014–2018 | 2009–2013 | 2014–2018 | 2018 | | |
| Armenia | 557 | 285 | 193 | 98 | 55 | 25 | 19 | 14 | 5 511 | 1 878 | 44 |
| Azerbaijan | 1 428 | 3 450 | 154 | 357 | 22 | 71 | 10 | 32 | 31 060 | 3 130 | 68 |
| Belarus | 2 186 | 1 496 | 231 | 158 | 35 | 25 | 10 | 9 | 20 761 | 2 196 | 35 |
| Bulgaria | 2 104 | 1 780 | 285 | 250 | 39 | 32 | 17 | 16 | 49 276 | 7 003 | 76 |
| Estonia | 1 337 | 967 | 1 006 | 738 | 63 | 37 | 26 | 15 | 24 342 | 18 628 | 82 |
| Georgia | 937 | 1 633 | 225 | 414 | 68 | 107 | 33 | 41 | 17 626 | 4 511 | 107 |
| Lebanon | 3 399 | 2 599 | 745 | 439 | 85 | 50 | 32 | 24 | 66 187 | 10 862 | 117 |
| Republic of Moldova | 275 | 209 | 67 | 52 | 42 | 27 | 18 | 12 | 4 047 | 1 002 | 42 |
| Romania | 3 365 | 4 668 | 165 | 236 | 19 | 23 | 7 | 10 | 94 021 | 4 802 | 39 |
| Serbia | 2 991 | 3 003 | 332 | 341 | 60 | 61 | 30 | 30 | 44 109 | 5 034 | 79 |
| Ukraine | 6 284 | 2 322 | 138 | 52 | 41 | 23 | 23 | 16 | 43 757 | 994 | 35 |
| Transition economies | 70 763 | 47 913 | 235 | 157 | 29 | 22 | 12 | 11 | 803 594 | 2 609 | 35 |
| Commonwealth of Independent States | 58 122 | 38 547 | 249 | 161 | 26 | 20 | 11 | 10 | 670 350 | 2 768 | 33 |

Source: UNCTADStat.

The recent trends in FDI by sector indicate interest in new sectors but also divestment in traditional ones. Due to changes in the methodology for FDI data collection, it is not possible to compare the sectoral distribution of FDI before and after 2014. However, the data for 2014–2017 points to the following: 1) the mining sector has been the largest recipient of FDI to Armenia in recent years, overtaking the energy sector which had for long attracted the largest share of investment (figure 2). Within mining, most FDI has concentrated in prospecting and development activities (Lydian gold mine), while more traditional metal ores mining has experienced divestment; 2) FDI is supporting the expansion of the high-growth sectors of the economy, including traditional ones, such as tourism (now the second largest recipient of inflows together with real estate) and alcoholic beverages (4th largest recipient), but also, though in smaller volume, emerging export sectors, such as agriculture, information technology and pharmaceuticals; and 3) recent years have seen divestment in a number of sectors, including telecommunications (Orange left Armenia in 2014), but also manufacture of basic metals as well as other manufacturing.

Figure 2. **Cumulative FDI inflows to Armenia by type of activity, 2014–2017** (Millions of dollars)



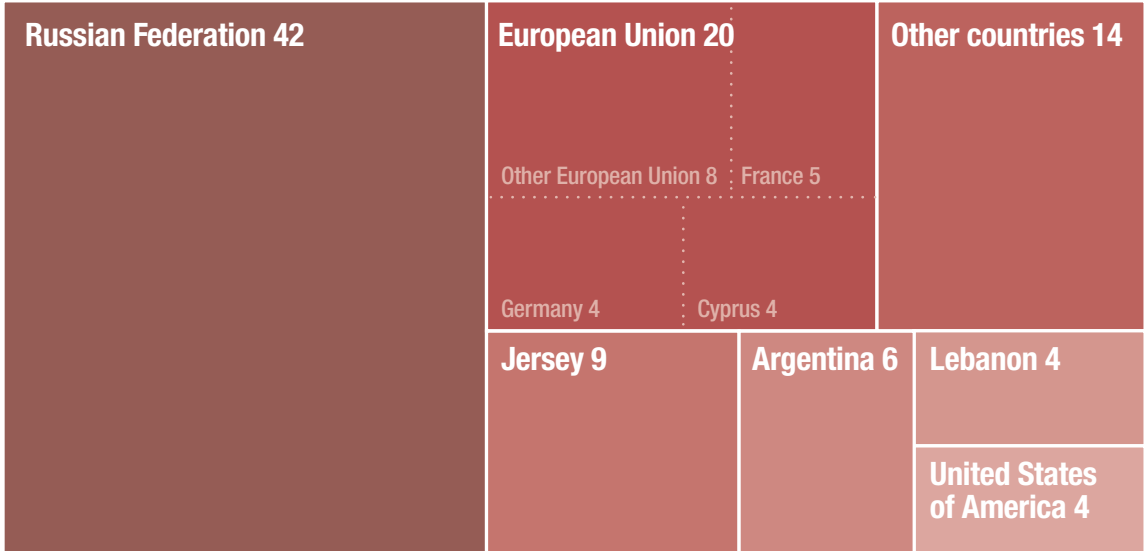
Source: UNCTAD calculations based on the Statistical Committee of the Republic of Armenia
 Notes: Financial sector data is collected separately by the Central Bank of Armenia and does not appear in the chart. Public utilities include electricity, gas, steam and conditioning supply; water collection, treatment and supply.

FDI inflows have become more diversified but continue relying on the diaspora. As shown in figure 3, the Russian Federation remains the largest source of FDI to Armenia, accounting for over 40 per cent of the total FDI stock in 2017. Russian FDI has been traditionally concentrated in energy, mining, transport, banking, trade and telecommunications. However, the country’s share has declined from almost 60 per cent in 2008, after a significant withdrawal of capital from sectors such as real estate and mining of metal ores. Recent Russian FDI has targeted primarily gas and telecommunications. EU countries together account for 20 per cent of total FDI, stable since 2008. The largest share of EU investment comes from France (beverages, water supply and sewerage management) and Germany (mining and basic metals manufacture). Jersey, origin of FDI by Lydian International, accounts for 9 per cent of the total FDI stock. Other notable investor countries include Argentina (airports and wine), the United States (IT and electricity) and Lebanon (telecommunications, food, garbage collection and disposal). With the exception of Jersey,

these are also among the main population centres of the Armenian diaspora – a community of over seven million people (more than double the population of the country). Strategically, this group of investors represents an opportunity for further investor targeting. However, the predominance of diaspora investors could also signal the need to broaden outreach beyond investors already familiar with the country (see chapter II).

The private sector identifies governance issues as key constraints on investment and business in Armenia but views on the future are optimistic. Despite the recognized improvements in the business climate, surveys of the private sector and UNCTAD’s interviews with business associations, investors and representatives of trading partners identify corruption and entrenched business interests among the main obstacles to investment and business operations in Armenia (WEF, 2019; EBRD, 2018). Examples put forward include political or business motivated use of customs and tax inspections, rent-seeking and inefficiencies in the judiciary and unpunished anti-competitive business practices. Importantly, however, all interviewees also point out to significant improvements in those areas since the Government has taken action and adopted steps to tackle monopolies and corruption, and to deal with tax and customs evasion (see chapter I of this report). It is unclear, therefore, the extent to which these issues still affect the business climate or represent the long tail of legacy perceptions still permeating the economic environment.

Figure 3. Armenia’s FDI stock by country of origin, 2017 (Percentage)



Source: UNCTAD calculations based on the Statistical Committee of the Republic of Armenia.
 Notes: Financial sector data is collected separately by the Central Bank of Armenia and does not appear in the chart.

The Government has recently announced an economic revolution to fight poverty and unemployment. In February 2019, the Prime Minister presented a five-year plan to the Parliament and announced the beginning of a nationwide economic revolution, aimed at significantly decreasing poverty and unemployment by 2023. The plan sets ambitious objectives for the growth of GDP and exports. It also emphasizes the need to improve the investment environment, continue tackling the governance issues and increase domestic investment and FDI inflows in Armenia. The aim is to achieve “a structural transformation of the economy in which the high-tech industry becomes the locomotive...and exports of goods and services become the basic engine”. The plans also define the Government’s vision for the development of key sectors, including tourism, agriculture and processing industries, high technologies and mining.

The authorities have requested this Investment Policy Review (IPR) to focus on assisting Armenia become a hub for the attraction of export and efficiency-seeking investment. The IPR of Armenia aims to provide concrete recommendations on improving the investment environment to support the sustainable development objectives set by the Government as part of its reform agenda. Towards this end, chapter I of this Review provides policy recommendations on how to strengthen the legal, regulatory and institutional framework for investment and increase the overall competitiveness of Armenia's business environment. Chapter II presents a strategy to attract and benefit from FDI in selected sectors and segments, including tourism, high technology (comprising not only software and engineering, but also artificial intelligence (AI), data science and other frontier activities), wine and agribusiness, as well as textiles, and pharmaceuticals, and grow several of them into achieving an export value of one billion dollars in 10 years. Selected regional services with potential but for which it is too early to set export targets are also considered, including business process outsourcing, regional logistics and food safety, aircraft repair and maintenance, regional financial services and education services.





Chapter

1

The
investment
framework





Since independence, Armenia has deployed consistent efforts to improve the legal and regulatory framework for business, and although several laws require updating and finetuning in line with good practice, no major legislative gaps exist. Indeed, in some areas, such as business registration or access to land, Armenia has become a model for other countries. Notwithstanding remaining complexities, Armenia has also moved to simplify its tax regime and streamline incentives, modernize its competition policy framework and improve governance. It is also in the process of upgrading the legislation in other areas, including foreign investment, corporate governance, intellectual property, environmental protection, as well as labour and foreign hire. Clear challenges, however, persist in several of these areas, and the analysis contained in this chapter aims to support the reform efforts by identifying remaining bottlenecks and providing inputs and recommendations to further strengthen the legal and institutional framework and its impact on sustainable development. The analysis as well as the recommendations are based on the Investment Policy Framework for Sustainable Development – IPFSD (UNCTAD, 2015).

A. FDI-SPECIFIC POLICY FRAMEWORK

Armenia’s FDI regime comprises several laws and policy documents. These include the Constitution, the Law on Foreign Investment of 1994 and the Law on Free Economic Zones of 2011. The Law on Foreign Investments of 1994 spells out the main principles of the country’s regulation of FDI and provides general provisions governing it, including entry rules and establishment procedures, guarantees on investment treatment and protection as well as access to incentives. In 2015, the Government also adopted an *Investment Policy Concept*, which expresses general principles guiding investment policy in Armenia, and includes a timetable of activities to address investment climate challenges and meet certain goals to further improve it. The Ministry of Economy is the main government body with a remit for investment policy in Armenia.

The Law on Foreign Investments is outdated, and a new law is being considered. The need for reform stems from the fact that the Law on Foreign Investments of 1994 was issued soon after the independence of Armenia, and before much of the new legal and institutional framework for private sector development was introduced (e.g. the laws and institutions regulating company establishment, licensing, competition, intellectual property, fiscal regime, among others). Whereas many of the provisions of the law contained general principles, some of them were too generic, never operationalised, or have in other cases become outdated. For instance, rather than stipulating the rights and obligations of foreign investors, the law refers to the relevant legislation in several areas, including economic activities open or restricted to investors, registration and termination of activities, access to land, taxation and others. The law contains no reference to the mandate and role of investment promotion authorities regarding business facilitation and on their role in determining access to incentives. Indeed, since the law was passed, no by-laws were adopted and Armenia has had several institutional set-ups for investment promotion (see chapter II). Accession to the EAEU has also had implications for the trade and investment regimes.

1. *Entry and establishment*

Foreign investment is defined broadly. The definition included in the Law on Foreign Investments of 1994 states that foreign investment is “any type of property, including financial resources and intellectual values, which is being directly invested by a foreign investor in commercial and other activities implemented in the territory of Armenia to gain profit (revenue) or to achieve any other beneficial result”. This is completed by a definition of an “enterprise with foreign investment”, which refers to “an enterprise of any organizational-legal type created in compliance with the legislation of Armenia; the founder or a participant in which is a foreign investor”. Thus, the law covers a broad variety of investments beyond direct investments (e.g. intellectual property, debt securities, concessions), and the co-existence of the asset-based definition with the enterprise-based one is unusual. Moreover, there is no definition of what threshold of foreign ownership is required for foreign investments to qualify as FDI in terms of percentage of shareholding, location of headquarters or substantive business activities.

Armenia’s legal regime for investment is generally open... The Constitution of Armenia protects all forms of property and states that everyone shall have the right to own, use and dispose, at its discretion, legally acquired property. The Law on Foreign Investments defines the conditions under which foreign



investment is permitted. According to its provisions, enterprises with foreign investment may conduct any economic activity which complies with the goals and objectives stated in the law, is not limited or prohibited by the legislation of Armenia or due to national security requirements (art. 6). None of the restricted activities, however, are spelled out in the law. Armenia's Law on Privatization adds that foreign companies have the same right to participate in privatization processes as Armenian firms. Importantly, the Government does not impose any type of screening on foreign investment in any sector of the national economy. The Law on Foreign Investments states that certain economic activities may be conducted by enterprises with foreign investment only after obtaining a licence (art. 14). However, no such requirement was identified in the sectoral legislation and in the new draft Law on Foreign Investments this provision was removed.

...with some entry restrictions contained in the sectoral legislation. In media, foreign ownership shall not exceed 49 per cent of the shares required for decision-making in the production of film, video, television programmes, musical and other audio recording as well as organizing and broadcasting television and radio programmes, unless international agreements provide otherwise (Law 97 of 2000 on Television and Radio). In addition, a law approved in 2010 on television and radio broadcasting prohibits ownership of more than one channel in the same area of broadcasting and limits the broadcast of programmes produced in foreign countries to up to 45 per cent of overall monthly airtime. In air transport, the granting of aircraft operator certificates requires that at least 51 per cent of shares belong to citizens of Armenia and (or) legal entities created in Armenia (Law on Aviation).⁵ These restrictions are common to many countries. Some professional activities are also reserved for Armenian nationals, which could act as an indirect entry constraint for firms providing such services. These include notaries, crew members of aircrafts registered in Armenia, professionals undertaking cartography, geodesy, measurement and land management (Law 81 of 2007 on Aviation; Decree 1441 of 2011; Law 274 of 2001 on Notary).

The high degree of concentration in several markets limits additional investment. Since independence, many assets have remained in the hands of the State, and in some cases, privatization has resulted in high market concentration. Such is the case in the forestry sector, electricity generation (wind), electric power transmission and distribution, oil and gas distribution and freight rail transport, which have typically monopolistic market structures that *de facto* limit new investment, both local or foreign (see section F of this chapter).⁶

2. Treatment and protection

The legislation grants high standards of protection and guarantees to investors. The Law on Foreign Investments grants national treatment of foreign investors by stipulating that “the legal regime related to foreign investments and the methods of their implementation cannot be less favourable than the regime governing the property, property rights and investment activities of citizens, legal entities and unincorporated enterprises of Armenia” (art. 6).⁷ There are no discriminatory performance requirements in place regarding the use of local employment or domestic content in the production of goods and services. A stability clause in the law mandates that in the event of amendments to the “legislation regulating foreign investment”, the legislation effective at the time investments were made shall continue to apply for a period of five years (upon the request of the investor, art. 7). The formulation of this clause is not sufficiently clear, and the stability guarantee could be interpreted to apply to any regulations affecting foreign investment, rather than being limited to the Law on Foreign Investments itself.



Expropriation of foreign investments is prohibited, except under exceptional circumstances. Foreign investments are protected from nationalization and Government bodies cannot arbitrarily expropriate foreign investments. According to the Law on Foreign Investments, “expropriation may be allowed only as an extreme means in case of emergency, applied only upon the judgement of a court of law and against full compensation” (art. 8). Prompt compensation should be paid for any material and moral damages, including lost profits, at current market prices or prices determined by independent auditors. The law mandates that compensation shall be paid either in the currency invested, or in any other currency mutually agreed upon by the parties, including any interest due calculated at current rates for deposit accounts established on the loan market of Armenia. Contrary to modern practice, the Law does not contain a non-discrimination guarantee in case of expropriation. The law also does not contain a reference to appeal procedures, but these were specified in the Law on Alienation of Property for the Needs of Society and the State of 2006.⁸ Investors interviewed by UNCTAD during the preparation of this Review did not report expropriation as a concern.

There are no exchange rate or other restrictions on the transfer of capital. The Law on Foreign Investments has stipulations concerning the disposal of a foreign investor’s profits and other capital linked to investments. Accordingly, investors have the right to freely dispose of investments after paying taxes and other fees. Foreign investors shall also be entitled to open bank accounts in Armenia and to use their legally obtained revenues to acquire foreign currency or commodities on the domestic market. The same guarantees apply to investors with regards to repatriation of capital and “other funds legally obtained as a result of investments”, though these latter are not further defined.

Foreign investors can enjoy specific privileges, but the procedures to access incentives are not clearly detailed. The Law on Foreign Investments stipulates that the authorized capital of a foreign investment enterprise, as well as the goods used in its production process (e.g. raw materials, semi-finished production, supplementary items, spare parts, etc.) are exempt from customs duties (see also section C of this chapter). Furthermore, foreign investors undertaking projects that may merit non-financial support (e.g. access to State or community land) can negotiate directly with the authorities and obtain approvals through a Government Decree, which may be issued in an *ad hoc* manner by the State or municipalities. The Law on Foreign Investments also says that those “privileges shall apply to those enterprises with foreign investment where such investment is no less than 30 per cent at the moment of their foundation” (art. 19). Investors located in free economic zones (FEZs) can enjoy additional benefits, for instance, regarding business facilitation, tax and customs (see section C). Government stakeholders have acknowledged in interviews during the UNCTAD fact-finding mission that the lack of by-laws clarifying procedures to apply for general and zone-specific incentives have made the Law on Foreign Investments and on FEZs less effective in promoting FDI.

The Law on Foreign Investments does not contain specific provisions on access to domestic courts. Investors consider access to justice between private parties in Armenia slow, inefficient and often unfair. The Government is developing a Commercial Code. In the meantime, the laws regarding commercial and contractual matters are set forth in the Civil Code. Because the country lacks Commercial Courts and the use of alternative dispute resolution (ADR) mechanisms is limited, most disputes involving contracts, ownership of property or commercial matters are resolved by litigants in the courts of general jurisdiction, which are overwhelmed by the volume of cases. Moreover, courts suffer from low levels of efficiency, independence and professionalism. As a result, commercial disputes take months or years to adjudicate (see section H).

With regards to investor-State dispute settlement (ISDS), national and international arbitration is available to investors. The Law on Foreign Investments provides investors with access to ISDS through the filing of claims at domestic courts. International arbitration is also possible in cases where investments are protected by international investment agreements (IIA, see below). Armenia is a party to the International Centre for Settlement of Investment Disputes (ICSID) Convention and has ratified the United Nations Commission on International Trade Law (UNCITRAL) Convention on the Recognition and Enforcement of Foreign Arbitral Awards (1958 New York Convention).

The draft Law on Foreign Investments under discussion seeks to address some of the issues raised above...The changes contemplate clarifications on all aspects of the investment process. Proposed amendments include:

- Re-wording the provisions on investor protection to refer to expropriation, forced alienation and indirect expropriation of investments (instead of the narrower terms nationalisation and confiscation).
- More precise provisions concerning the transfer of FDI-related funds, including the right to transfer profits, dividends, capital gains, and proceeds from the sale of all or any part of the foreign investment, interests, royalty payments and other fees, among others.
- The specification that foreign currency transfers would be calculated at the market rate of exchange prevailing as of the date of transfer, as it is common international practice.⁹
- More specific procedures on available benefits for specific economic activities and in specific geographical areas, including free of charge provision of land, subsidies to cover loan interests, guaranteed offtake of production and the provision of state guarantees and simplification of administrative procedures.
- Provisions to ensure that disputes arising in respect of foreign investments be resolved between parties through negotiations, consultations or mediation, where appropriate. Moreover, in case of ISDS, the amendment also includes a provision that grants advance consent to international arbitration by either the International Chamber of Commerce (ICC), the International Court of Arbitration or an *ad hoc* arbitration court according with proceedings either under international or domestic arbitration rules.
- The alignment of any provisions regarding access to customs benefits with the regulations of tariff privileges established by the Commission of the EAEU.

...but the proposed changes fail to address some shortcomings and introduce unwarranted excessive guarantees. The draft Law on Foreign Investments fails to address some of the issues of the existing Law, but it would also offer new guarantees to foreign investors which appear excessive. In particular, it:

- retains a broad asset-based definition of foreign investment, which raises the concerns discussed above.
- offers pre-establishment national treatment to foreign investors, effectively limiting the capacity of the State to impose FDI entry limitations.
- clarifies that the stability guarantee offered to investors only refers to the provisions of the law itself, but it broadens the guarantee to “the entire period of his investment” (art. 9), which appears to impose excessive limitations on the State’s right to regulate.

- offers foreign investors standards of treatment which are typical of IIAs but which are out of place in a national law on investment. These include fair and equitable treatment, full protection and security, minimum standards and most-favoured nation (MFN).
- retains the entitlement for investors to “judicial compensation for material and moral damages, including loss of profits, caused to them by the improper performance of the administrative bodies of the Republic of Armenia and their officials of their obligations established by the law toward foreign investors or enterprises with foreign investment” (art. 9 of current law and art. 11 of new law). What would constitute “improper performance” is, however, not clarified, and the provision therefore risks exposing the State to excessive liabilities.

3. International investment agreements

Armenia has concluded 43 bilateral investment treaties (BITs), 38 of which are in force.¹⁰ An equal share of the treaties was signed with European countries and Asian countries (44 per cent), followed by countries from the Americas (10 per cent) and Africa (2 per cent). Around half of Armenia’s BITs were concluded with developed countries (49 per cent) and the other half was split between developing countries (32 per cent) and countries with economies in transition (19 per cent). In addition, Armenia is a party to seven treaties with investment provisions (TIPs)¹¹ and two regional TIPs – the Treaty on Eurasian Economic Union and the Commonwealth of Independent States Convention on Protection of Investor Rights (see annex I for the list of Armenia’s IIAs). While the former contains substantive investor protections and ISDS, the latter includes investment protections tied to domestic law and non-binding commitments to arbitration. Armenia is also a party to the Energy Charter Treaty, which provides detailed investor protection and access to ISDS.

The main features of Armenia’s IIAs include:

- A broad asset-based definition of investment, except for the Armenia–Canada BIT, which excludes specific assets such as real estate or property that was not acquired for the purpose of economic benefit.
- Post-establishment national treatment (NT) and MFN clauses, except for BITs concluded with Canada, Finland, Japan and the United States, which cover pre-establishment as well. Some of the BITs have exceptions (e.g. to non-discrimination rules for economic integration agreements and taxation).
- A fair and equitable treatment (FET) provision, unqualified in most treaties, except for the Japan BIT, where the FET is qualified with reference to the international minimum standard, and the BITs with Canada and France, where the FET is qualified with reference to principles of international law.
- Unqualified clauses on direct and indirect expropriation. Exceptions or limitations are rare but do occur. For example, carve-outs for compulsory licences in conformity with WTO obligations are included in the BITs with Canada and Japan.
- “Umbrella” clauses in more than half of the BITs. So-called umbrella clauses bring contractual and other obligations under the umbrella of the investment treaty by requiring a host State to respect any obligation assumed by it with regards to a specific investment (for example, in a concession contract), making them potentially enforceable through ISDS.



- Free transfer of any investment-related funds with no exception, except for the BITs concluded with Romania and Japan, which include balance of payment exceptions. Several other BITs e.g. those with Lithuania and Latvia, contain specific exceptions, such as for the protection of rights of creditors and to ensure compliance with other laws and regulations.

Several BITs include national security or public policy exceptions. For example, the BITs with Kazakhstan, Finland and India contain national security exceptions, whilst the ones with Canada and Japan contain public health and environment exceptions. The BITs with Latvia and the United States as well as the Eurasian Economic Union – Viet Nam FTA include both national security exceptions and public health and environmental exceptions. The BITs with Finland and Latvia include exceptions for measures taken to maintain public order, provided they are not arbitrary, unjustifiable or disguised restrictions on investment. The BITs with Canada and Japan also include a carve-out for prudential measures.

Several BITs include investment facilitation provisions. Notably, they provide that, once established, investment shall be granted all necessary approvals, including for the hiring of key foreign personnel. The BITs with Argentina and India are examples of this approach. Moreover, the BITs with Argentina and Romania include investment promotion provisions encouraging the exchange of information on investment opportunities.

Access to ISDS is granted in all BITs. Arbitration is available to investors generally through the UNCITRAL Rules, the ICSID Convention, ICSID Additional Facility Rules or the Rules of the Arbitration Institute of the Stockholm Chamber of Commerce. Domestic courts of the host State are also an option. In some BITs, such as the one with Lithuania, investors are required to exhaust all local remedies before approaching international arbitration bodies. In others, investors have the choice of approaching domestic courts first. While some ISDS clauses are broad (i.e. covering any dispute related to investments), the scope of ISDS is limited to “treaty claims only” in the BITs with Argentina, Austria, Canada, Japan, Spain and the United States as well as the Eurasian Economic Union – Viet Nam FTA.¹² The BIT with Canada provides specific procedures for ISDS cases regarding taxation and prudential measures.

Armenia has been a respondent to few international arbitration cases in recent years. As of April 2019, at least four investor–State dispute settlement cases have been brought by foreign investors before international arbitration tribunals. Each of these disputes, concerning investments in manufacturing, real estate, mining and public infrastructure, involved alleged breaches of clauses of the BIT between Armenia and the United States. Amongst these, one of the disputes was settled, another was decided in favour of the State, and two are pending.¹³ Armenian investors have not initiated any treaty-based ISDS case against other States.

Assessment and recommendations

National policies

Over the last decades, the Government of Armenia has made great efforts to build an open regime for FDI through various legislative reforms. Soon after independence, a Law on Foreign Investments was enacted, which includes basic guarantees. The passing of the Laws on Privatization of 1997 and on SEZs in 2011 were also important landmarks towards promoting investments in priority sectors. Some concerns remain, however, regarding the clarity of key provisions and the alignment of the Law on Foreign Investments with



modern practice. For instance, key concepts of investment legislation require some refining and additional clarity, including the definitions of investment and investor, the conditions for transfer of funds and currency convertibility, the stability guarantee, the access to incentives and to ISDS procedures. Whereas some amendments that are currently being considered are likely address these challenges, others may also result in unnecessary costs and/or liabilities to the State. Given the goal of using FDI policy to achieving sustainable development, it is recommended that the Government of Armenia adopts the new draft Law on Foreign Investments with the following revisions:

1. **Clarify key FDI-related provisions**, in such areas as entry restrictions, standards of treatment, expropriation, transfer of funds, dispute settlement and access to incentives.
2. **Reflect the mandate of investment promotion authorities**. The key mandates and roles of investment promotion institutions should be included in the revised Law.
3. **Revise and harmonize the definition of investment and investors**. All laws and regulations on investment should contain coherent definitions on what constitutes “foreign investor” and “foreign investment”.
4. **Limit potentially excessive investor guarantees**. This includes removing the reference to FET, MFN, full protection and security and minimum standards, but also reconsidering the need for an open-ended stability clause, as well as the entitlement to compensation in case of improper performance by the public administration.
5. **Include refinements to the guarantees in case of indirect expropriation**. By clarifying what indirect expropriation entails, increased predictability could be achieved without unduly compromising the ability of the State to regulate.
6. **Introduce a provision indicating that foreign investors shall not be accorded privileges beyond those afforded to Armenian investors in similar circumstances**. There is no reason why foreign investors in Armenia should be offered tax and other privileges not available to Armenian investors. This would only encourage local investors to register companies abroad and invest in Armenia as foreign investors (so called “round-tripping investment”).
7. **Reduce the country’s exposure to ISDS**. In light of the recent surge of ICSID arbitration cases, Armenia should consider strengthening dispute prevention policies, including by promoting consultation, investor–State dialogue and prioritising ADR and domestic solutions.

International investment agreements

The review of Armenia’s treaty network shows that it mainly consists of first-generation IIAs that were signed in the 1990s. Recent treaties often differ from the old-generation treaties by including provisions to preserve regulatory space and/or minimize exposure to investment arbitration. These elements comprise clauses that: a) limit the treaty scope (e.g. by excluding certain types of assets from the definition of investment); b) clarify obligations (e.g. more detailed clauses on FET and indirect expropriation); and c) contain exceptions to transfer-of-funds obligations and/or carve-outs for prudential measures (UNCTAD, 2018a). Armenia may want to modernize its treaty network and bring it in line with today’s sustainable development imperatives and international best practices.

In order to modernise the investment treaty network, Armenia could refer to UNCTAD's Reform Package for the International Investment Regime (UNCTAD, 2018b). The package covers three phases of sustainable development-oriented IIA reform: 1) providing different options to design modern IIA clauses; 2) offering 10 options to modernize the existing stock of old-generation treaties; and 3) stating an approach to strengthen investment policy coherence (e.g. maximize synergies between the national and international level framework for investment, meet the challenges arising from the fragmentation of the IIA regime). The Government of Armenia can determine which of the proposed options are best suited to support the country's national development objectives and UNCTAD stands ready to assist in this endeavour. In line with these objectives, this IPR recommends to:

8. **Set up a sequence of reform actions for updating the IIA network.** Such initiative could contemplate the following steps: a) assessing the existing investment treaty network and identify key provisions for improvements; b) developing a model treaty to guide in future negotiations and in amending existing outdated treaties; and c) modernizing the treaty network based on a careful and fact-based cost-benefit analysis.
9. **Clarify key provisions of IIAs and incorporate a sustainable development dimension by adding or amending clauses of treaties with the goal to:**
 - *Refine key concepts*, with a view to avoiding unanticipated and broad interpretations by tribunals (clearer definitions of investment, indirect expropriation, FET).
 - *Safeguard the State's right to regulate for public policy objectives, while maintaining effective investment protection.* This would imply better focusing treaty scope by using carve-outs, exceptions and exclusions, while carefully considering the type of obligations to be included in the treaty.
 - *Strengthen investment promotion and facilitation provisions*, including by adding joint regional investment promotion provisions and including an ombudsperson for investment facilitation.
 - *Ensure responsible investment*, notably by adding "not lowering of standards" clauses and establishing provisions on investor responsibilities, such as clauses on compliance with domestic laws and on corporate social responsibility.
10. **Improve the investment dispute settlement mechanisms in IIAs**, including by prioritising domestic solutions using filters and by adding new elements (e.g. building in effective alternative dispute resolution or introducing an appeals facility).¹⁴
11. **Enhance systemic consistency**, by improving the coherence of the IIA network at the bilateral and regional levels, managing the interaction between IIAs, and linking IIA reform to the domestic policy agenda.

B. COMPANY OPERATIONS

1. Registration, licensing and liquidation

The standard range of company structures is available to investors. The Civil Code defines various forms of company structure, including the standard joint-stock and limited liability types that are common in other jurisdictions. In addition, it is possible to create firms in the form of partnerships (general and limited), supplementary liability, as well as register as individual entrepreneurs (arts. 26, 51 and 72). With regards to FDI, subsidiaries, branches and representative offices of foreign companies are also regulated in the Code (art. 61 and art. 75).

The procedure for company registration is straightforward. According to the Civil Code (art. 56), all legal persons are subject to registration. In March 2011, a Business Entry One-Stop Shop was launched in the Ministry of Justice. At present, starting a company takes the following steps: 1) registering at the State Register Agency of Legal Entities (online, at the one-stop shops in the Ministry or at different offices of the Service Centres of the State Register Agency of Legal Entities);¹⁵ 2) opening a bank account (in Armenian drams (AMD) or other currencies); 3) registering in the tax report system (online or at the State Revenue Committee); and 4) registering employees (online). According to the Ministry of Justice, all the procedures that are person-based are deemed efficient by users, and they have been facilitated thanks to agreements with banks and the postal company (*Haypost*) that set up offices in these institutions to provide registration and other services on behalf of the Ministry.¹⁶ These reforms have helped Armenia rank high (8th worldwide) on the “starting a business” indicator of the Doing Business, behind Georgia (2nd), but above all other CIS economies (World Bank, 2018a).

Much progress is also registered in the area of licensing. The list of activities for which licensing is mandatory is described in art. 43 of the Law on Licensing of 2001, and was last revised in 2017. Although the list includes activities subject to licensing in most countries, a periodic revision of the activities subject to licensing remains opportune.¹⁷ Armenia has also carried out significant reforms to simplify licensing. Licences can now be obtained online through a new electronic system (e-gov.am/licenses). The law requires that licences be issued within 23 days upon submission of complete application documents.

eGovernment initiatives will further improve business facilitation. With the help of UNCTAD's eRegulations programme – launched in June 2018 with the assistance of UNDP and funding from the Government of Austria – 10 key business procedures have been fully mapped and listed online, including all requirements for starting a business, obtaining residency, registering intellectual property and other property rights. The next steps include mapping the procedures to become a resident of free economic zone, obtaining a country of origin certificate, getting a construction permit, and signing subscription contracts with utility providers.¹⁸ The procedures were selected based on investor priorities according to survey information. Once the mapping is finished, UNCTAD will propose simplification measures for the procedures deemed most burdensome through the mapping exercise, which will be completed before the end of 2019. The Government and UNDP have signaled their intention to continue collaborating with UNCTAD on Business Facilitation issues and the automation of selected services is planned for 2020.



Corporate governance has also been the subject of reform, but is still to be addressed comprehensively... With the help of international partners (e.g. the World Bank, the European Bank of Reconstruction and Development and the Department for International Development of the United Kingdom), Armenia has been updating legislation on corporate governance and bankruptcy (e.g. Laws on Joint Stock Companies, the Law on Banks and Banking Activity, the Law on Securities Market, the Law on Bankruptcy). It also developed a Code of Corporate Governance for companies listed in the Stock Exchange, which was adopted in 2010. At present, the country ranks 51st worldwide on the protection of minority shareholders and the disclosure of information to the public in the Doing Business, which is relatively high, but below the regional average for Europe and Central Asia. Several investors interviewed by UNCTAD as well as recent reports assert a lack of adequate corporate governance in the operation of businesses in Armenia. Among the issues highlighted are the need to improve the internal and external auditing of firms, enhance the powers of independent Directors in Boards, and improve the position of shareholders with regards to pre-emptive rights on capital increases and protection against insider trading.¹⁹ A draft reform of the corporate governance legislation is reportedly being considered by the National Assembly to address some of those issues. Armenia is also developing a framework to establish a public oversight body and the Chamber of Accountants and Auditors – a crucial step toward improving financial transparency (IMF, 2019).

...and resolving insolvency remains costly. The policy framework of bankruptcy procedures also needs improvement. Armenia scores low on the “resolving insolvency” indicator (ranked 95th) of the Doing Business 2019 (World Bank, 2018a), due primarily to its high costs and the low recovery rate (38 cents on the dollar). Indeed, not only are insolvency cases in Armenia expensive, but they almost always result in liquidation.²⁰ This precludes the economy from accessing the benefits of orderly company reorganization (e.g. retained jobs and higher economic activity). The lack of dedicated commercial courts and alternative dispute resolution in addressing debt issues in commercial disputes exacerbates these challenges (see section H). Improving the governance of bankruptcy procedures remains one of the priorities of the Government. In June 2019, a draft law on Making Amendments and Supplements to the Law on Bankruptcy was submitted to the National Assembly. The draft envisages reducing the remuneration of bankruptcy managers, to reduce the cost of bankruptcy proceedings. In addition, premiums have been set for the bankruptcy manager for submitting a financial recovery plan, as well as for recovery of a bankrupt person, with the aim of promoting the increase of financial recovery cases.

2. Access to land

Land is largely in private hands and foreign investors can access it through the private market or through Government concessions. Privatization of land in Armenia was initiated in the 1990s and 73 per cent of land is now in private hands. As mentioned in section A, foreign born individuals cannot directly own land in Armenia. However, a foreign-owned company registered in Armenia can own land. According to the Land Code, whereas no time limitations are set on the lease of private land, accessing public land is more restrictive (art. 48). State and community owned land can be rented for up to 99 years, except for the agricultural land, which cannot be rented for more than 25 years at a time. The State land tenancy rights are provided by tenders and by public auctions, except in special cases defined by the Government (art. 205). Foreigners can also be 100 per cent owners of real estate in Armenia (except land): they can acquire, hold, lease, sell, bequest and otherwise dispose of their property on equal basis with locals.



Titles are secure and registration and transfer procedures efficient. Armenia has established one of the most efficient land management regimes among CIS countries. With the help of international development partners, including the World Bank and the Swedish International Development Cooperation Agency, Armenia successfully mapped and registered 97 per cent of land parcels, and land tenure is deemed secured (UNECE, 2017a). Registering property rights requires few steps, several of which can be completed online and within 4–5 days, as recorded in UNCTAD’s eRegulations Armenia. In addition, in 2017, Armenia improved the land dispute resolution mechanisms to align them with good international practice. Despite these achievements, land availability and consolidation issues persist, which affect in particular the agricultural sector, as discussed below.

Land consolidation issues persist. It is estimated that more than half of the total agricultural land is pasture lands, located in mountainous areas that are mainly community (i.e. municipal) and state-owned. As it is the case in many other countries with economies in transition, when privatization of collective lands occurred in Armenia, the rural landscape that resulted was often very fragmented and economically inefficient. The farms that could be set up faced high production costs (i.e. irrigation, agricultural machinery, feed and fuel costs), which ultimately led to land abandonment in many areas. Various land consolidation exercises were undertaken to encourage farmers to sell or merge their properties, including with the help of international partners, but the process to increase the average size of farms and agricultural efficiency has been slow (Sahakyan, 2007; UNDP, 2004; Grigoryan, T, Hakhnazaryan, et al. 2008). Statistics shared by the Ministry of Territorial Administration show that out of a total 372,343 ha of State land available for concession in 2018, 87.6 per cent were being leased as of 1 January 2019. There is some variation across regions, but in the most fertile provinces, the bulk of State land was being effectively leased.²¹ The lack of working irrigation infrastructure affects the leasing of remaining public lands.

Notwithstanding the limited availability of State-owned land, the potential for increased use of private land is significant. A large percentage of arable land in private hands (33.32 per cent) is estimated to be unused or abandoned (World Bank, 2018b). However, the land sales market is underdeveloped due to limited finance and no transfer tax exemptions. Private lease is often not an option in Armenia because it is short term and deemed insecure by investors, as key issues like tenancy duration, renewals, dispute resolution mechanisms are not properly regulated in the Land Code. In such a context, building on the successful experience of land administration (see chapter I, section B) should be a key priority for the Government to continue land reforms. The Government has recently engaged in negotiations with landowners to facilitate transactions with foreign investors, and there are some successful experiences in wine production, as discussed above. And although no land bank or other database of available lands exists, investors were able, through the assistance of Business Armenia, to identify plots available for lease or purchase from private owners. Such cooperation and facilitation may be affected by ongoing Government reforms, which include the merger of land administration with infrastructure functions under one single ministry as well as the ongoing restructuring of investment promotion institutions (see chapter II, section II.C).

Assessment and recommendations

During recent years, the Government has made significant efforts to improve business facilitation, as a result of which Armenia adopted modern cadastre, land and business registration systems. However, in some areas, reforms are incomplete, and in other cases, their potential effects may have been undermined



by governance challenges. Interviews with stakeholders during the fact-finding mission for this Review confirmed the view that the country's attractiveness to investments could be enhanced if corporate governance were improved. In these areas, it is recommended that the Government:

1. **Moves forward with the introduction of eGovernment tools for business facilitation.** The Government should continue the mapping of registration and licensing procedures with the goal to improve business facilitation. UNCTAD stands ready to provide technical support for the completion of these tasks as well as for the simplification and automation of selected procedures in line with the Government priorities.
2. **Bolsters the legal framework on corporate governance and bankruptcy.** Considering that the basic legislation is already in place, the focus should be on making it more comprehensive and upgrading its quality. Key priorities include:
 - a. Moving forward with the reform of the Corporate Governance legislation with the goal of improving internal and external auditing of firms, and shareholder protection. Introducing mandatory external auditing of financial statements in line with good international practice could also be considered.
 - b. Amending legislation to improve the position of shareholders with regards to their voting rights and access to information.
 - c. Reforming the bankruptcy regime by encouraging company restructuring and ADR mechanisms.

Recommendations on access to land are detailed in chapter II, section B.2 on agribusiness.

C. TAXATION

Over the last two decades, the Government made important progress in reforming the tax regime and mobilizing tax revenues, but significant challenges remain. Tax revenues have increased gradually from 14.6 per cent of GDP in 2002 to 21 per cent of GDP in 2018,²² a change that resulted from the implementation of comprehensive tax policy and administration reforms. A new Tax Code, in force since January 2018, aimed at further increasing the tax base, improving equity and addressing the problem of informality, including by shifting the balance from direct to indirect taxation. Other challenges, however, still need to be addressed, and while corporate taxes are generally competitive,²³ administration costs are high and overly favourable regimes for small businesses risk discouraging upscaling. Finally, the free zone regime has defeated its original purpose and its design counters good practice internationally.²⁴

1. General regime

A single corporate income tax (CIT) applies to most economic activities, with a limited number of exceptions. The rate is set at 20 per cent and applies to all firms that are resident in Armenia as well as non-resident entities doing business through a permanent establishment (PE). The rate will be lowered to 18 per cent, starting in 2020.²⁵ This is part of a comprehensive reform aimed at ensuring that the sum of the CIT rate and the dividend withholding rate would equal the personal income tax rate, so as to reduce opportunities for arbitrage between the two. The CIT is levied annually on a company's worldwide profits.²⁶ Taxable income includes proceeds from the sale of goods and services, capital gains, dividends, royalties and interest and rents and other similar payments.²⁷ Losses may be carried forward for up to five years, except for losses derived from mergers, acquisitions or other changes in legal entities, which may not be carried forward. Income from some activities (e.g. the sale of agricultural products and equipment for agricultural production)²⁸ or locations (e.g. the FEZs) are exempt from corporate income tax or benefit from a preferential rate (table I.2). There is no tax on capital gains separate from CIT. The general regime is competitive and the total tax rate amounts to 18 per cent of business profits,²⁹ compared to an average of 32.3 per cent for the group of countries in Europe and Central Asia (World Bank, 2018a).

Conventional allowances for deductible expenses are in place and depreciation follows the straight-line method since 2018. In principle, all expenses linked to business operations are deductible. Deductions are allowed in the tax year during which the corresponding income is generated, but expenses incurred in the previous tax year may also be deductible if linked to the current year.³⁰ Expenses on scientific research and/or experimental design works and services (R&D) are fully deductible. Depreciation is compulsory, also in years of losses and, for certain categories of assets, accelerated depreciation is also allowed. Table I.1 shows minimum depreciation terms as they apply for the separate groups of fixed assets (art. 121).³¹ Assets whose value does not exceed AMD50,000 (~ \$100) may be depreciated in the first year of acquisition.

Withholding rates apply to payments to non-resident firms. Unless a tax treaty provides otherwise, dividends, interests, royalties, income from the lease of property, and capital gains are subject to withholding tax at a rate of 10 per cent. The dividends withholding rate will be reduced to 5 per cent in 2020, as part of the comprehensive reform of personal and corporate income tax mentioned above.³² Payments for insurance, reinsurance, and transportation are taxed at a rate of 5 per cent. Other income (from services) received from Armenian sources is subject to withholding taxation at the rate of 20 per cent (art. 125).



Table I.1. **Amortization terms**

| Type of asset | Minimum amortization term (years) |
|--|-----------------------------------|
| Buildings and construction | 20 |
| Hotels | 10 |
| Assembly lines and automated equipment | 5 |
| Manufacturing equipment | 3 |
| Computers, other calculating devices and communication equipment | 1 |
| Other fixed assets | 8 |

Source: Ministry of Finance of the Republic of Armenia.

Armenia does not allow group taxation, and it only recently introduced transfer pricing regulations.

Transfer pricing rules were adopted for the first time in the Tax Code of 2018. They cover certain taxpayers whose sum of relevant transactions exceed AMD200 million (~ \$414,000) in any reporting year.³³ The rules apply the arm’s length principle. They also describe available calculation methods and specify sources of information for analysing transfer pricing and documentation requirements, amongst other provisions. However, due to lack of capacity, the Government has decided to postpone their implementation until 2020. It is expected that the implementation of transfer pricing rules will have a significant impact on revenue collection. The Tax Code includes no special group taxation nor controlled foreign companies (CFC) provisions.

2. Customs, value added tax (VAT) and other taxes

Since accession to the EAEU in 2015, customs policy follows the EAEU foreign trade policy. Import of goods from the EAEU member States is exempt from customs duties if goods maintain the status of EAEU goods. Customs duty rates for goods imported from non-EAEU countries are stated in the Decision of the Council of the Eurasian Economic Union N 54, 16.07.2012, except for about 800 tariff lines for which other tariff rates are applied for a transitional period ending in 2025. Essential goods, such as raw materials, are exempt from customs duty. As for the exports, there is zero customs duty rate for export. Customs payments are charged by persons whose goods cross the customs border of Armenia from non-EAEU member countries. As for imports from EAEU countries, there are no customs payments unless the goods are recognized as foreign according to the legislation. Transportation of goods from EAEU countries to Armenia is done by transit customs procedure except for the cases of transportation by air, electric shaft and pipelines. The customs authorities charge customs payments and other payments. Customs payments consist of customs duties, taxes and customs fees. Other payments include anti-dumping, special compensation duties, as well as ecological road taxes. Customs duties have three types of rates: *ad valorem*, fixed and mixed. In case of *ad valorem* rate, customs duties are calculated on the customs value of the imported goods and border authorities must consider specific EAEU rules to determine the customs value on which customs duty and import taxes will be applied.

Armenia’s VAT is output based, applying to the supply of goods, the performance of work or the provision of services in the national territory. The standard VAT rate on goods and services and the importation of goods is 20 per cent. Since 1 July 2019, all legal entities and individual entrepreneurs are



considered taxable and must be registered for VAT purposes if their annual taxable turnover for the previous year exceeds AMD115 million (~ \$243,000), in which case VAT will be applicable to the exceeding amount. This threshold is unusually high, above that of any EU country, where VAT payment thresholds range from a minimum of €10,000 to a maximum of €95,000, or that of neighbouring Georgia (~ \$36,000).³⁴ Taxpayers who are not eligible or do not register for the simplified turnover regime (see below) should also account for VAT. Firms registered for VAT may deduct it on their inputs from the amount charged on their sales and report the difference to the tax authorities.³⁵

A large number of transactions and operations are VAT exempt. Several transactions (over 50), including those related to agriculture and food industry, as well as most media, financial, scientific and research activities, creative industries and education services, are VAT-exempt (art. 64 of Tax Code). Certain imported goods are also exempt, including capital, equipment and other goods. Exports of goods and related services are zero-rated. In addition, advertising, consulting, marketing, design, engineering, legal, accounting, audit, data processing, and other related services provided to non-residents are also zero-rated if the non-resident's place of business is outside Armenia. The taxpayer may receive the VAT refunds on a quarterly basis. The Tax Code sets a maximum period of 55 working days for VAT refund. However, stakeholders in the private sector have claimed that delays may occur, particularly for VAT refunds of zero-rated exports.³⁶

Other levies include excise duties, land and property taxes. The production or import of certain goods (i.e. some alcoholic beverages, tobacco and petroleum related products) is subject to excise duties, which have fixed amounts or variable percentage rates (or both) applying to the volume of goods (litre or kilogramme amount).³⁷ As of 1 January 2020, only the fixed amount will apply. Land taxes are paid biannually by landowners as well as leaseholders of State-owned land (rates vary between 15 per cent for net income agricultural land and between 0.5 and 1 per cent for non-agricultural land). Property taxes rates for buildings deemed to be public and industrial structures are 0.3 per cent. Both land and property taxes are paid at the municipal level on the cadastral value of plots. For motor and water vehicles, there are different rates applying to vehicles based on their capacity (horsepower) and number of seats. If a unit is older than three years, the amount of property tax is reduced by an initial 10 per cent, and a further 10 per cent decrease each additional year (up to 50 per cent). The introduction of a unified real estate tax replacing the property tax and land tax is planned for 2021. Finally, mining activities are subject to additional taxation, including royalties, nature utilisation payments and environmental pollution taxes, which are regulated by the Tax Code and Subsoil Code.

3. Simplified tax regimes

A mandatory *patent fee* regime applies to companies engaged in certain activities. This regime replaces the CIT and VAT. It consists of a lump-sum payment (the *patent fee*), which is due on a quarterly basis and varies depending on the type of activity. The following business activities must register for the *patent fee* regime: taxi services, bus and minibus transportation services, hairdresser services, vehicle maintenance services, vehicle parking services, table tennis and billiard games, gaming and vending machines, dentistry and dental mechanics, betting and Internet betting, and jewellery sales (precious stones, precious metals and jewelry of precious metals) on jewellery markets and malls. This regime will be repealed as of 1 January 2020.

An optional turnover tax regime is available for small businesses and individual entrepreneurs.

It applies to businesses with annual turnover not exceeding AMD115 million (~ \$243,000), and replaces the VAT and/or CIT for SMEs, except for individual entrepreneurs for whom it replaces only VAT. For firms enrolled under this regime, the taxable base is derived from the business turnover and is due on a quarterly basis. The rates depend on the type of business activity, and are payable selectively at the following rates: trade (5 per cent), recyclable materials sales (1.5 per cent), newspapers sales by publishers (1.5 per cent), manufacturing (3.5 per cent), rent, interest, royalties, alienation of assets (10 per cent), notary services (10 per cent), lottery revenues (25 per cent), catering and restaurant services (6 per cent), other activities (5 per cent).³⁸ Taxpayers engaged in the following types of business are not eligible for the turnover tax regime: producers or importers of excisable goods (they will become eligible as of 1 January 2020), companies under the *patent fee* regime, banking, loan, insurance and investment companies, security market participants, pawnshops, currency exchange offices, casinos and gambling offices as well as auditing companies.

Small family business undertaking certain activities are eligible for a simplified flat-rate regime.

Firms owned, managed and employing solely members of the same family (mothers, fathers, brothers, sisters, spouses and children), and whose annual turnover in the preceding year does not exceed AMD24 million (~ \$ 50,000), can opt to register for the *Family company* regime (art. 267). A fixed monthly tax payment of AMD5,000 (~ \$10.5) for each employee is due. Taxpayers engaged in the following types of business are not eligible for this tax regime: trade companies, companies under the *patent fee* regime for the activities conducted under that regime, producers or importers of excisable goods (they will become eligible as of 1 January 2020), banking, loan, insurance, and investment companies, currency exchange offices, lotteries and gambling office (casinos) and auditing companies, among others.

Changes to the simplified regimes are forthcoming, with the goal to further streamline taxation for MSMEs.

As of 1 January 2020, the patent fee regime will be abolished. A single micro-entrepreneurship taxation regime will replace the self-employed and family business taxation systems. Under the single regime, companies with annual turnover up to AMD24 million (~ \$50,000) will benefit from income exemptions for all basic taxes. Micro-entrepreneurs will have the opportunity to engage individual workers (whether or not they are family members and without limits on the number), subject to a fixed monthly tax payment of AMD5,000 (~ \$10.5) per employee. The new regime will co-exist with the turnover tax regime and the general regime.

4. Incentives

Recent reforms have streamlined the number of incentive schemes, though several are still in place.

Income tax holidays, tax deferral or exemptions from customs duties aim at promoting a range of activities including agriculture, investment funds, information technology, carpets, and renewable energy production (table I.2). After accession to the EAEU in 2015, the Government exempted investment-related import of equipment and raw materials from non-EAEU countries from customs duties and enacted exemptions to the imports of capital investment-related goods from VAT payments at the border. Until 2018, customised incentives were also granted to export-oriented companies as well as companies conducting Government approved projects outside Armenia (mostly in the construction sector), but these schemes have now been cancelled and it is reported that very few companies benefited from them.³⁹ Although some of the schemes (e.g. the IT regime) have been altered several times, a cost-benefit analysis still needs to be undertaken to assess their impact in terms of job creation, skills development, technology transfer and revenue losses.⁴⁰



Table I.2. **Summary of incentives schemes available to investors**

| Regime | Eligibility requirements | Benefits |
|--|--|---|
| Agriculture and hand-made carpets | <ul style="list-style-type: none"> • Agricultural production and equipment for agricultural production (subject to certain limitations) and hand-made carpets | <ul style="list-style-type: none"> • Exempt from CIT and VAT. |
| Investment funds | <ul style="list-style-type: none"> • The Investment Funds Law of 2010 regulates investment funds, including hedge funds | <ul style="list-style-type: none"> • CIT taxed at 0.01 per cent of the tax base, corresponding to the total amount of net assets established in Armenia. • Custody services and the allocation and/or buyback of securities issued by the funds are not subject to VAT. • Investment from a natural person and profit from the sale of fund securities are not subject to CIT. • For the purpose of determining the profit tax base, expenses for the acquisition and alienation of securities proving the participation in the investment funds, as well as other expenses for the participation in those funds shall not be deemed expenses for profit tax. |
| R&D | <ul style="list-style-type: none"> • Companies undertaking basic or applied research | <ul style="list-style-type: none"> • For the purpose of determining the tax base for resident profit taxpayers and non-resident profit taxpayers carrying out activities in Armenia through a permanent establishment, the gross income shall be deducted in the amount of the expenses made on scientific research and/or experimental design works and services carried out immediately by the profit taxpayer or upon the order thereof, in the full amount thereof during the tax year when those expenses were made. • VAT exemption for transactions on R&D aimed at knowledge generation, including fundamental and applied research; as well as works performed within the framework of general education programmes. |
| Importation of capital goods | <ul style="list-style-type: none"> • Companies importing capital equipment | <ul style="list-style-type: none"> • VAT exemptions for imports described in Chapters 84 and 85 of the Harmonized Commodity Description and Coding Systems, comprising most capital equipment. |
| Disabled employees | <ul style="list-style-type: none"> • Companies employing disabled persons | <ul style="list-style-type: none"> • 150 per cent deduction of wages and other payments made to disabled employees. |
| Free economic zones | <ul style="list-style-type: none"> • Resident companies and FEZ managers | <ul style="list-style-type: none"> • CIT exemption throughout the life of the project. • VAT exemption on import for the supply of services of operators throughout the life of the project. • Import of goods from outside the EAEU is exempt from VAT if exported within 180 days from their importation (including to EAEU member States). • Tax exemption on property tax, real estate tax, customs duties and others tax privileges. |
| Information technology | <ul style="list-style-type: none"> • Companies undertaking IT activities, including techno-parks, incubators and accelerators involved in IT projects • Company can only perform IT activities (defined by a threshold of 70 per cent of turnover) • Must have at most 30 employees • Eligible companies require certification | <ul style="list-style-type: none"> • CIT exemption for income from revenues from IT activities. • New start-up companies in the IT sector are exempt from corporate income tax for a period of 5 years, until 31 December 2022. A flat personal income tax for employees of these companies is set at 23 per cent, as of 1 January 2020. |
| Renewable energy production | <ul style="list-style-type: none"> • Licensed resident companies involved in the production of electric energy from renewable sources | <ul style="list-style-type: none"> • CIT exemption for income from revenues from electric energy sales. The exemption applies to sales to licensed energy distribution companies. |

Source: Tax Code (2018), Law On Amendments and Addenda to the Law on State Support of Information Technologies (2019), Law On Making Amendments to the Tax Code (2019), PWC (2018) and IBFD (2019).



In addition, a number of FEZs have been established with the goal to promote export-led growth...

According to the Law on FEZs of 2011 (last amended in 2018), investors established in FEZs benefit from generous tax and customs incentives, including lifetime CIT and VAT exemptions. Goods processed in the zones are also deemed to be outside the customs territory of EAEU. Non-tariff benefits apply, in the form of access to land, infrastructure, logistics and other services provided by the zone managers. These are selected through concession contracts. The Government also retains the ultimate authority to grant resident status to companies that sign lease agreements with the organizers. Four FEZs have been set up to date: 1) the Alliance FEZ, which opened in August 2013, focusses on high-tech industries such as information and communication technologies (ICTs), electronics, pharmaceuticals and biotechnology, architecture and engineering, industrial design and alternative energy; 2) the Meridian FEZ, which opened in Yerevan in 2015, with firms carrying out jewellery production, watch-making and diamond-cutting; 3) the Meghri FEZ, which opened in 2017 at the border with the Islamic Republic of Iran; and 4) The Ecos FEZ in Hrazdan, with a focus on attracting companies undertaking high-tech innovations.

...but a series of challenges have reduced their impact. A Decree of 2011, amended in June 2019, defines common criteria for the selection and operation of the zone managers. However, the application procedures for resident companies and the eligibility requirements depend on regulatory decrees specific to each individual FEZs, and these have been altered over time, often with no relation to the zones' original purpose. For instance, a Decree of 15 December 2014 allowed firms to apply for residence status in the Alliance FEZ upon condition that no similar production occurred in Armenia, but regardless of any export orientation.⁴¹ Second, at least in the case of one zone visited by UNCTAD, the state of the facilities and infrastructure has fallen below standards in the region and beyond. Third, Armenia's accession to the EAEU has reduced the comparative advantage of some incentives and raised costs (e.g. higher import tariffs for inputs used in goods that are sold within EAEU and lower VAT benefits). Furthermore, the incentives in place have not encouraged spillover and linkages effects, nor regional development within the country. Finally, as discussed further in chapter II, it is also not straightforward that the mandated sectors should receive fiscal support, which increases the case for proper cost-benefit assessment.

5. Paying taxes

The Government is making efforts to streamline tax payments and modernize auditing. According to the Doing Business 2019, a medium-sized manufacturing company in Armenia spends on average 262 hours paying taxes each year (i.e. corporate income, VAT and social contributions), which requires 14 payments, compared to 214 hours on average in the Europe and Central Asia region. The country is ranked 82nd in the global index, which is slightly behind the regional average, and significantly behind its neighbour Georgia, which is ranked 16th (World Bank, 2018a). The ongoing efforts to move towards 100 per cent electronic declaration and processes by 2020 will be crucial to improve performance, but it will be important to retain the possibility to file paper declarations as an alternative, which is particularly relevant for rural areas.

But other issues remain, which affect tax collection. Despite continued and significant progress, tax revenues remain low (20.6 per cent of GDP in 2018), which represents a challenge in the path to sustainable development (IMF, 2019). Challenges include the complexity and scope of the tax treatment of MSMEs and of the incentive regimes. The capacity of the State Revenue Committee (SRC), in charge of tax and customs administration to monitor and enforce compliance is also limited. Governance has been an issue, and several

stakeholders interviewed by UNCTAD reported that tax and customs inspections and fines were often used in the past as tools for providing a competitive edge to selected companies. A hotline has been active since 2010 at the SRC, receiving large numbers of inquiries and/or complaints, upon which investigations on misconduct can actually be started.⁴² However, the system still depends on the regular court system for appeals, which may compromise its effectiveness (see section H). All interviewees expressed confidence in the new Government administration's willingness to fight these practices but pointed to the need for improved auditing of tax payments, particularly with regards to companies which enjoy incentives. The introduction of electronic certificates of origin systems could help minimize misreporting at the borders.

Assessment and recommendations

The general CIT regime is competitive. Recent reforms have made the general regime simpler and streamlined the number of incentive schemes, thus expanding the tax base and reducing the costs of tax compliance (e.g. by speeding up the payment of VAT refunds and clarifying the rules for tax audits). Improvements to transparency and fairness are also being implemented through online tools, some of which are aligned to requirements to integration into the EAEU (e.g. on customs procedures). The Government has also announced that the existing tax rates, simplified regimes and incentives schemes will be further reduced and/or harmonised to make their administration smoother and remove the scope for arbitrage between corporate and personal income taxation.

These efforts, however, are undermined by the persistence of several problematic issues. In particular, the differential treatment resulting from the array of MSME schemes, together with continued changes to the Tax Code, have created undue complexity and uncertainty. The simplified tax regimes, which can be powerful tools to promote formalization and enterprise development, have been overused. While some consolidation of the various schemes is planned, the eligibility for the turnover tax regime, already wide, is set to widen further, which risks discouraging company growth and fostering the atomization of large companies. The FEZ regime is also unusually generous from the tax standpoint and its design and implementation, which was not part of a long-term strategy to promote local value addition, counters good practice. Looking forward, it is recommended that the Government:

1. **Reduces the threshold of application of the turnover tax regime.** Efforts to streamline the simplified tax regimes should be accompanied by a reduction in the scope of application of the turnover tax regime, which should be narrowed down to adequately target small companies. An alternative approach is to replace all simplified regimes in favour of a tax allowance which gives a non-filing threshold.
2. **Introduces group tax relief to promote cross-sectoral investment.** At present, individuals consolidate income from all sources but related companies cannot. Armenia should adopt the policy of many other countries, including the United Kingdom and the United States of allowing tax consolidation amongst related companies, subject to qualifying rules and restrictions as appropriate. Note that this results in a deferral and not loss of government tax revenue. Tax losses surrendered by one company in a group to another are no longer available to the surrendering company to carry forward (see chapter II for a practical application of this measure to key industries).
3. **Adopts comprehensive cost-benefit analysis of incentives schemes.** Many incentives are subject to adoption or revision without adequate impact assessment. Several of them counter good practice, by offering tax privileges which are not time-bound or by providing tax holidays rather than

encouraging capital investment and re-investment. The free zone regime is a case in point. Another is the tax exemption limited to for farm income, which risks encouraging artificial separations between agriculture and agribusiness operations (see chapter II, section B.2).

4. **Reforms the FEZ regime to encourage value-addition, regional development, and linkages.** Performing FEZs can contribute not only to exports, but also to value addition and sustainable development, including through regional development, transfer of technology, skills development and other spillovers to the domestic economy. In line with the analysis of on special economic zones (UNCTAD, 2019a), the Government could consider amending the FEZ legislation and policy with the goal to:
 - a. Reassess mandated activities for existing and future FEZs while also narrowing down the amount and focus of incentives. A regional development dimension for FEZs should also be incorporated.
 - b. Extend selectively the eligibility criteria for incentives to domestic suppliers of resident companies, so that they could indirectly become exporters.
 - c. Consider the development of an *SDG-model zone*. Such zone would be built around four key elements: 1) a strategic focus on attracting investment in *SDG-relevant* activities; 2) highest level of environmental, social and governance (ESG) standards and compliance; 3) promotion of inclusive growth through linkages and spillovers; and 4) provision of high-quality infrastructure and facilitation services.
 - d. Set up a linkages development initiative, such as UNCTAD's business linkages programme, to increase the competitiveness of local suppliers for activities where they do not meet required standards.
5. **Works to enhance the capacities of the tax and customs revenue authority to monitor tax compliance by:**
 - a. Furthering efforts to introduce electronic technologies for tax and customs payments. E-tools can help reduce administration costs, encourage formalization and reduce the risks of tax evasion through misreporting and corruption at the borders.
 - b. Implementing the transfer pricing legislation. The Government counts with a solid legislation, but it needs to be made operational. Initial phases for collecting documentation for transfer pricing could be started immediately with the help of local accountancy firms. More complex steps, including auditing, could be undertaken at a later stage.
 - c. Increasing capacity for monitoring and auditing of taxpayers by public authorities. The effectiveness of e-tools and transfer pricing methods could be enhanced by providing adequate training to staff of the Ministry of Finance and the State Revenue Committee.

Specific tax policy recommendations related to key priority sectors, including tourism, high-tech, textiles and garments, wine and agribusiness are discussed in chapter II of this report.

D. LABOUR AND FOREIGN HIRE

1. General labour regulations

Labour market regulations in Armenia balance employee protection and business needs, though parts of the regime need updating. The Constitution mandates the State to contribute to employment and the improvement of working conditions for the population. It also guarantees basic labour rights and entitlements, including work freedom, right to strike as well as requirements on safety and hygiene. Other protected rights include social security during old age, for disability and unemployment. The Labour Code of 2004 regulates most aspects of collective and individual labour relations. Other legal acts supplement the Code by addressing specific aspects of employment, minimum wage, the organization of trade unions, civil service and public associations, amongst others. As discussed in the following sections, the resulting regime generally provides fair balance between employers and workers rights, but several regulations require updating in line with current international labour standards.

Armenia is a party to 29 ILO Conventions, including the eight fundamental ones, all of which have been ratified. No major infringements of the ILO fundamental conventions are reported, but some shortcomings exist in translating commitments into norms. As signalled by development partners, better alignment between definitions in national legislation and ILO requirements on topics such as freedom of association and collective bargaining, forced labour, discrimination against women and exploitation of children (particularly in the informal sector) is needed.⁴³

The legislation allows for standard work hours and premium pays, but some gaps exist on other employment-related policies. The standard workday has maximum eight hours with a maximum number of working days of six per week. Normal working time may not exceed 40 hours per week and premium pays per hourly work are available for night shifts (30 per cent), work on holidays (100 per cent) and overtime work (50 per cent). In no case the working overall time should be longer than 12 hours per day and 48 hours per week. Paid annual leave is also available, the minimum period is 20 working days in the case of a five-day working week and 24 working days in the case of a six-day working week. Paid maternity and paternity leave is also regulated by law. However, no fixed number of fully paid days of sick leave is granted in the legislation.

The Labour Code allows for flexibility in the duration of labour contracts. Whereas some restrictions are in place, (e.g. written contracts are mandated with some standard provisions; fixed-term contracts are prohibited for permanent tasks), the Code is flexible for hiring provisions. For instance, it does not impose a maximum length for single fixed-term contract, including renewals. With regards to probationary periods, they are possible with a maximum length of three months, but in certain unspecified cases, they may be extended up to six months. The Code allows to conclude labour contracts for an indefinite period or for a specific one (e.g. home, seasonal and temporary work). A contract of employment may not contain provisions less favourable to workers than those stipulated by labour law.

Termination procedures and redundancy costs are not overly onerous. According to the Labour Code, the termination of a contract of employment may intervene for several reasons. These include rescission at the initiative of the worker or of the employer. A seven-day notice period applies when termination is



mutually agreed by the parties.⁴⁴ The power of the employer is limited in a number of circumstances, including during a temporary absence of the worker such as for sick or annual leave. Some protection in case of dismissal is also guaranteed to the workers with family responsibilities, and in case of collective dismissals, for which the employer is required to notify the Government and the workers' representative two months in advance. Dismissals are deemed collective if they involve, within two consecutive months, the termination of employment of more than 10 per cent of the total number of employees and of at least 10 people. For dismissal of less than 10 employees, third-party notification is not needed. Workers are eligible for dismissal benefits ranging from 10 to 44 days of average daily salary depending on the grounds for dismissal, the length of tenure and other circumstances. This can be increased by collective agreements. Retraining and reassignment is required before redundancy dismissals, but neither priority rules for redundancies nor for reemployment are set (World Bank, 2018a).

The Labour Code describes basic principles for social partnership between employer associations and labour unions, including the right to collective bargaining. The legislation guarantees freedom of association for social partners. Collective agreements are possible at four levels: State, branch, regional and enterprise levels. The length of these agreements is decided by the partners, but it cannot be longer than three years (renewal is possible for another three years). Agreements at the enterprise level may not contradict the Labour Code and any existing higher-level collective agreements. Agreements at other levels may also not contradict the Labour Code.

The minimum wage is set through tripartite consultations. The Ministry of Labour and Social Affairs is the executive body that develops and implements policies in the field of employment and social protection.⁴⁵ Since 2005, Armenia has worked to establish a framework for effective consultations with representative employers' and workers' organizations at all stages of the minimum wage fixing and adjustment process, after ratifying the ILO Convention 131 of 1970. However, the wage settlement mechanism is still weak, amongst other reasons due to limited unionization (Gabrielyan and Mnatsakanyan, 2014). As discussed in chapter II, Armenia has wage cost advantages, particularly for skilled labour. At present, the monthly minimum wage is AMD55,000 (~ \$115), unchanged since 2015, and well below the average net salary of AMD130,000 in 2018. The Government recently approved a proposal to raise it to AMD68,000. The proposal was submitted to the National Assembly.

Armenia does not have a specialized labour court system and disputes are dealt with in the ordinary civil judiciary system. Conflicts over contracts of employment by individuals are dealt with by the ordinary courts, with rules according to the Civil Procedure Code. These require that they be solved in the first instance court within three months. Given the inefficiencies of the courts' system described in section H of this chapter, solving labour disputes can become a lengthy process. Collective disputes require additional steps, including mandatory conciliation by a commission composed of equal representation of the parties to the dispute. In case of failure of conciliation, the parties may invite a mediator and only if the mediator fails to reach consensus can the parties go to court.

The right to strike is inscribed in the Constitution, but Armenia's legislation is still to conform with international commitments. Although no official statistics are available, strikes are not a significant issue, and a low percentage of population is unionised. The Labour Code authorizes strikes in case of non-settlement of a collective labour dispute related to collective agreements. Trade unions may declare strikes if such a decision is supported by two-thirds of the enterprise workers by secret ballot. A reform to reduce the threshold is being considered by the Government with the goal to align it to ILO requirements.

In a context of high unemployment rate, enhancing the rights of women and youth remains a priority. According to official statistics, Armenia has one of the highest unemployment rate in Europe and Central Asia region (see context). Whereas the variation by gender for the overall rate is small, in the case of youth unemployment, gender variation is significant (it affects about 45 per cent of young women and 24 per cent of young men aged 15 to 29). The share of informally employed persons is also high (48 per cent of the working age labour force).⁴⁶ Moreover, although the principle of equal treatment is laid down in the Constitution, there is no implementing secondary legislation, and while the Labour Code grants equal pay for equal work for men and women, it does not rightly incorporate the principle of equal pay for work of equal value. Neither does it promote gender neutral hiring nor guarantees paid paternity leave (European Commission, 2018).

There is also a need to boost the capacities of labour inspectorates. The current capacities of labour inspectorates allow neither for adequate monitoring on matters linked to general working conditions and employment relations (i.e. wages, employment contracts, welfare provisions), nor for an effective supervision of occupational health and safety standards.⁴⁷ The situation has led to remarks by the ILO supervisory bodies on the application of the Labour Inspection Convention 81 of 1947. At the time of the fact-finding mission for this Review, the Government was working on mapping the agencies involved on protection of employee rights as defined in the Convention with the goal to identify gaps and solutions for responsible agencies (e.g. tax, labour or other inspectorates).

The Government has recently signed a Decent Work Country Programme (DWCP) for 2019-2023 with the ILO, which will address some of the most urgent challenges. The programme priorities and key country outcomes were developed in close consultations with tripartite constituents and other national stakeholders. The programme builds upon the results of the previous DWCP 2007–2011 and the implementation of the agreed Decent Work Agenda for 2012–2016. As part of its objectives, the ILO will support the Government to apply the Conventions and Recommendations of the ILO within the context of a comprehensive reform of the Labour Code. The goal will be to put the national legal framework in line with current international labour standards, protect labour rights and ensure decent working conditions for all categories of workers, amongst others.⁴⁸

2. Foreign hire

Armenia faces skills shortages and mismatches, which may increase the demand for foreign hire. Armenia has historically benefitted from strong science education, and some universities have attracted international attention.⁴⁹ However, concerns about the continued availability and quality of skills in these and other sectors have emerged, which vary by field of specialisation (see chapter II, section B). In this context, Armenia's flexible approach to foreign hire serves the country well.

The Law on Foreigners of 2006 was only recently operationalised. Most foreign workers in the country are diaspora Armenians, often not required to apply for work permits. After the enactment of Decree 493 of 2016, which defined procedures for processing permits, the Government set up an administration and monitoring system. Accordingly, foreign hire requires approval by the Government on a case-by-case basis. The regime makes no distinction between intra-company transfers and local hire of foreign workers. The employer submits documentation on the candidates' professional education and qualifications (approved by consular certification or apostille) to the Ministry of Labour and Social Affairs, together with payment of

AMD25,000 (~ \$52). The Ministry conducts a market test, as part of which it may offer the employer an Armenian citizen candidate that meets the requirements. The permit is granted if no candidate is available or after the employer refuses any suggested candidate. The Ministry must approve or reject the application within five working days and send a written notice within three days after a decision is made.⁵⁰ The legislation does not specify the duration of the permit or its renewal, but the Ministry generally grants a one-year permit and renews it upon specific requests.⁵¹ The work permit is complementary to the residence visa, which is requested separately.

Investors, key personnel and certain categories of skills are exempt from work permitting. Highly skilled foreign specialists, business owners, executives and certain other categories of workers are exempt from work permit requirements. However, they still need to obtain temporary (for one year or longer) or permanent residence visas, which are issued by the Police. Directors as well as specialists required to train employees may not need to apply for work permits if in Armenia for periods shorter than six months (Law on Foreigners, art. 23).⁵² Furthermore, there is a list of specific technical and high-skilled categories that are exempt of permitting. These include some professions of vocational education in natural sciences (i.e. sub-categories of technicians for operation and technical maintenance of computing tools and computer networks, web design, and computer design) and agriculture (i.e. sub-categories of the agronomist profession, including organization of the farmer economy and greenhouse economies) (Annex 2 of Decree 73 of 2006). In addition, professionals with higher education qualifications in the following fields are also exempt: ICT, management and administration, food technologies and finance (Annex of Decree 1191 of 2014).

The Government has indicated that it built the priority lists based on surveying and informal consultations with the private sector. At the time of the fact-finding mission for this IPR, employers did not raise major concerns about hindrances in obtaining permits for workers and key personnel, even if no institutionalised system of consultation to determine missing skills is in place. Indeed, Armenia ranks 7th in the world on ease of hiring foreign labour according to the global competitiveness rankings of the World Economic Forum (WEF, 2019). According to information received from the authorities, in July 2019, a new Government decree introduced additional improvements to the regime. The key changes include: the list of professions that allow highly qualified foreign specialists to work in Armenia without a work permit has been clarified and new professions have been added; foreigners with scientific degrees can now work in Armenia without a work permit; and the work permits' application and registration process has been upgraded with the introduction of modern tools, such as an electronic registry, the possibility to use the scanned copy of the applicant's passport, and by enabling employers to submit job vacancy information electronically if an e-signature is available.

Assessment and recommendations

There is a need to update some of the provisions of the labour regime in line with international requirements and to address some pending social and gender concerns. Armenia also faces the double challenge of retaining the skilled labour it needs for its economic transformation and, at the same time, meeting the contemporary skills needs of the private sector. The recently implemented foreign-work permit system should help reduce the impact of missing skills, but it should be completed by improving communication between private sector and education institutions in the longer term. In order to address pending challenges, it is recommended that the Government:



1. **Moves forward with reforms to align the Labour Code and related legislation with current international labour standards.** In line with international commitments, priority should be given to addressing gender discrimination at the workplace, combating child labour and reducing barriers to unionisation and the right to strike.
2. **Works with international partners to strengthen the labour inspectorates.** Emphasis should be on ensuring that the human and financial resources match the mandates and can help foster compliance with the law at the workplace.
3. **Continues to hold consultations on the minimum wage,** with the goal to increase it in line with productivity improvements, as budget constraints relax.
4. **Adopts an institutionalised mechanism to determine the scarce skills list for work permit exemption.** Setting up of an institutionalised mechanism to determine missing skills (a “scarce list system”) in consultation with unions, employer associations, the Chamber of Commerce and Industry of the Republic of Armenia and education institutions should be considered. Such a system could help regularly update the list of exempted professions and skills so that they result of multi-stakeholder consultations and better reflect market needs.

E. ENVIRONMENT

Environmental challenges abound and the environmental protection regime is recent and requires proper implementation and monitoring. Armenia faces several environmental challenges. Some of them have to do with the country's location in arid and mountainous lands, which make it vulnerable to desertification, landslides, land degradation and desalination in the Ararat Valley. These geographical constraints are compounded by the consequences of man-made actions linked to illegal felling and logging, use of solid fuel and unsustainable practices in agriculture that contribute to climate change and land degradation.⁵³ During the Soviet period, the country also became highly polluted due to heavy industrial development, and tended to overlook related environmental harms in the form of air and water pollution at least until the 1980s, when some chemical producing factories were closed. After independence, environmental protection laws were enacted, but implementation has lagged in some areas, including monitoring.

The country's mining activity calls for additional attention. Mineral extraction projects differ in the types of extracted metals and materials. Overall, 670 mines with solid minerals are registered in the Government's state reserve of mineral resources, and potential exists for further exploitation of copper, gold, silver, lead, zinc and molybdenum deposits.⁵⁴ Mining could bring significant development benefits through exports, employment and linkages. However, the environmental governance of the sector has been called into question. The uncertainty around the *Amulsar Gold Project* described in the context, and the protests and blockades by environmental activists and villagers have brought international attention to the concerns regarding environmental permitting, monitoring and compliance in the country.⁵⁵

A Law on Environmental Impact Assessment and Expertise was adopted in 2014 to align Armenia's norms with EU regulations and directives, but gaps remain. It sets modern environmental protection principles and tools, and regulates both environmental impact assessments (EIAs) by private experts and strategic environmental assessments (SEA) by the authorities in areas such as energy, transport or mining projects.⁵⁶ In line with good practice, it distinguishes between categories of projects depending on the severity of environmental risks. Accordingly, whereas for two categories technical requirements are stringent and imply the undertaking of EIAs, for the third category there is no assessment involved, but only a preliminary screening before licensing and issuing an expert report. It should be highlighted, however, that some of the categories are too broadly defined, which may lead to ambiguous interpretation by investors and/or authorities. Furthermore, for some activities, including in the mining industry, there is a clear need for sector-specific by-laws clarifying the steps and responsibilities of all stakeholders involved. In addition, EIAs undertaken for major projects often have deficits of information needed for compliance with applicable law. For instance, they tend not to be comprehensive enough and often disregard the indirect impact of projects (Policy Forum Armenia, 2010).

The law also sets specific time limits for the undertaking of expert examinations of EIAs. Following the Law, the Ministry of Nature Protection has a remit for implementing environmental licensing. Investors must approach the Ministry to obtain technical guidelines for undertaking EIAs, which, in the absence of the relevant by-laws and guidelines, may require up to 30 days. After investors fulfill the requirements for impact studies, they need to present the EIA to the Ministry for expert examination. According to the legislation, the expert assessment by the Government may take up to 60 working days for the high-risk



category of projects, and up to 40 days for the less risky ones. These periods can be extended by 10 to 30 days depending on the risk category of the project and the type of inaccuracies to address. The Ministry reported that delays are unusual, and in any case, the whole process never takes more than 90 days – after which investors are eligible to seek compensation through the court system. Between 2014 and 2018, the Ministry reviewed a total of 552 EIAs, with limited variation per year (between 100-125 projects). It also reported no significant backlog of projects waiting for assessment.

Although there are legal requirements for disclosure and public participation in EIAs, public engagement remains limited. Legislation mandates public notice and public hearings according to secondary legislation to be established by the authorities. The law states that “while carrying out the assessment, comments and recommendations of participants of the process shall be taken into account, and in case of their rejection, the respective explanations shall be provided” (see art. 17.3), and that “in the framework of the process of environmental impact assessment, the initiator may seek advice from the heads of the affected communities and civil society stakeholders” (art. 17.6). However, these principles require further regulation to be operationalised,⁵⁷ which is compounded by the limited availability of education and awareness for environmental issues in Armenia. As a consequence, until recently, levels of public participation have been weak.

A number of issues reduce the effectiveness of environmental monitoring. A separate, independent State body, the Inspectorate for Nature Protection and Mineral Resources, handles ecological inspections during project implementation. The Inspectorate’s capacities are limited, and even though in recent years, the authorities have worked to improve them, results are still to be felt on the ground. Furthermore, laws may not be strictly interpreted due not only to legal ambiguity, but also to weak governance linked to conflict of interests or corruption (see section H). There are also concerns that the fines and consequences for lack of compliance are too low and do not constitute an adequate deterrent. Finally, awareness on environmental regulations is also limited, particularly amongst small investors (World Bank, 2017).

Since 2016, with assistance of the United Nations Economic Commission for Europe (UNECE), the Government has worked to improve the environmental protection regime. In 2017, a draft regulation was prepared to introduce amendments in the Law of 2014, but the Government change in 2018 delayed its approval. The new authorities are again reviewing the legislation, with the goal to incorporate guidance for the undertaking of strategic ecological impact assessment, in line with the UNECE Espoo Convention, and to align public consultations provisions with the UNECE’s Aarhus Convention.⁵⁸ The changes being considered also include reducing the number of project categories to two: one for projects with significant impact, which will undergo EIAs within a period of 60 days, and one for low impact projects, which will qualify for operations without an impact assessment. The reform will also broaden the remit of the Ministry for monitoring filling and reclamation after mining activities are completed. In addition, the Government is working on secondary legislation to define sector-specific procedures and provide improved guidance to investors in several areas, including geological research, explorations, reclamation of sites after mine closures (including principles on restoration of affected land and water resources, atmospheric air, flora and fauna). By-laws on the undertaking of systemic ecosystem impact assessment in the mining sector as well as the assessment of environmental and social impact and compliance of mining projects are also being considered.

Assessment and recommendations

The proper licensing, monitoring and evaluation of projects in environmentally-sensitive areas should continue to be a priority for Armenia, which will likely have an impact on the outcomes of its investment attraction strategies. Whereas the legal and institutional framework has been improved in recent years, further work is needed to clarify procedures, responsibilities and liabilities. Looking forward, it is recommended that the Government:

1. **Moves forward with planned reforms to improve the strategic assessment of environmentally sensitive projects.** Whereas the risk-based criteria for the SEA process is in line with international practice and does not seem to generate delays, there is a need to improve clarity of procedures in secondary legislation, especially for mining-related activities. Key priorities include the need to integrate a social impact assessment and public consultations in the overall process strategic assessment. The by-laws being considered contain detailed information on the depth of the impact studies and consultations required and should be enacted as legislation.
2. **Improves the governance of environmental compliance monitoring.** The availability of human resources of inspectorates should be adequate and rent-seeking opportunities should be minimized through proper training and the establishment of internal oversight and control mechanisms.
3. **Increases awareness on the environmental permitting process among the general population.** It is essential that the population concerned by environmentally-sensitive projects be fully informed and consulted as to the potential impact of new projects. Awareness should also be built around the key aspects of the environmental permitting and protection process, the avenues for public consultations and participation, the Government's monitoring and enforcement activities as well as the mitigation measures adopted. Channels could include public campaigns through education and media institutions to promote participation of civil society in discussions about environmentally sensitive projects.

F. COMPETITION REGIME

Armenia has kept updating its competition legislation to align it with international practice. During recent years, the authorities have implemented various reforms to Armenia's competition policy, including through UNCTAD's assistance.⁵⁹ The Law on Protection of Economic Competition (2000) and its subsequent amendments (2011, 2013, 2017, 2018 and 2019) provide the main framework for competition policy in Armenia. The legislation has been aligned with international standards and commitments, including provisions of the EAEU and the EU CEPA Agreement.

The legislation contains standard provisions to promote a competitive economic environment. According to the Law of 2000, agreements (horizontal or vertical) preventing, restricting or distorting competition are prohibited.⁶⁰ The law also bans abuses of dominant position and regulates market concentration that may result in the absence or restriction of competition. Dominant position is presumed for market shares of at least one third for a single undertaking, 50 per cent for two undertakings, or two thirds for three undertakings in case their market shares do not exceed 1/10th of the given market, or if an economic entity has market power in a given commodity market.⁶¹ Concentrations – including mergers, acquisitions of shares or assets, amalgamations and incorporations – are subject to *ex ante* control by the competition authority when the asset-based notification thresholds are met (art. 9.1). If the competition authority estimates that concentration can lead to the creation or strengthening of a dominant position, it can prohibit such practice or impose remedies, including fines. The latter are determined by the authority and may reach up to 10 per cent of the proceeds of the year preceding the infringement.⁶²

The competition authority has a broad range of functions. The State Commission for the Protection of Economic Competition (the Commission) was established in 2001. The Commission has had the status of “autonomous body” since 2015, with members appointed by a majority vote of the National Assembly for periods of five years with the possibility of renewal for the second term. Its main functions include: 1) detection and disclosure of abuses of monopolistic or dominant positions, of anti-competitive agreements and of unfair competition practices; 2) control of mergers and acquisitions; and 3) monitoring and control of State aid. The most recent amendments to the competition legislation have further enhanced the powers of the Commission, by improving definitions and clarifying criteria for the detection of prohibited activities and by adding administrative liability for anti-competitive agreements between officials of state bodies and economic entities (WTO, 2018). The authority is now also empowered to start investigations on its own initiative, in line with UNCTAD's recommendations in this area (UNCTAD, 2010).

Evidence points to increasing success in enforcing competition rules in recent years... Statistics show that the enhanced powers of the Commission have led to more active enforcement. For the period 2010–2017, the Commission reports that 425 market studies were undertaken and 1253 proceedings initiated, the bulk of which dealt with mergers and unfair competition. Hundred decisions were appealed in courts, 83 of which were left unchanged. The monitoring of market concentration for certain commodities that are socially sensitive remains amongst the Commission's key priorities (i.e. sugar, petroleum, diesel fuel, butter, wheat, flour, dairy product, chicken egg, chicken meat, and sunflower oil). Whereas many of these products are imported, statistics shared by the Commission show that the number of importers has significantly increased in recent years (for instance, over the period 2014–2018, the market players in sugar increased from 36 to 75, in flour from 20 to 171 and in wheat from 30 to 84). The progress has also

been reflected in international rankings such as the WEF's Global Competitiveness Report, where Armenia moved from 133th to 24th place over the period 2010–2019 in the market dominance indicator (WEF, 2010 and 2019).

...but important concerns remain. Whereas privatization reforms have significantly reduced State presence in the economy, several sectors are still considered cartelized or suffer weak competition (see section A). Similarly, fluctuations in the price of imported goods do not follow international trends, which can be attributed to the presence of monopolies and the creation of commodity-based cartels that are stronger in the retail sector (Bertelsmann Stiftung, 2018). Finally, in key public services, such as energy, water supply and telecommunications, the price-setting process may not be sufficiently transparent to reflect public interests (Bertelsmann Stiftung, 2018; WTO, 2018).⁶³ UNCTAD's Interviews with private sector stakeholders confirmed the view that competition can be impeded by “unwritten” rules that create an uneven playing field. The negative business perceptions were often related to unfair treatment in policy areas the monitoring of which is not under the remit of the competition authorities, such as the granting of import licensing, access to real estate, trade at the borders or the uneven application of tax rules. This is the reason why improving competition requires a holistic approach that also considers other governance challenges (see section H).

Assessment and recommendations

Although competition policy has been the object of significant reforms that aligned Armenia's framework with international good practice, significant anticompetitive practices persist, which point to the need of addressing market dominance and restrictive business practices from a holistic perspective. In the future, it is recommended that the Government:

1. **Increases the investigative powers of the Commission.** The authority has been empowered to conduct *ex-officio* investigations. UNCTAD's “Voluntary peer review of competition policy” in 2010 also called for granting the Commission the power to conduct unannounced “dawn raids” of business enterprises to obtain corporate records in paper or electronic form, subject to judicial oversight (UNCTAD, 2010).
2. **Improves coordination between the competition authority, sectoral regulators and ministries** and ensure that price determination in public services is based on transparent information and consultations with all stakeholders, including consumers.
3. **Continues building the capacities of the Commission's staff.** UNCTAD has extensive experience in providing technical assistance and capacity building on competition policy and has engaged with the Armenian authorities in the past. It stands ready to further support according to the Government's priorities.

G. INTELLECTUAL PROPERTY AND QUALITY INFRASTRUCTURE

Intellectual property plays a crucial role in Armenia's future development. Armenia's objective to promote efficiency seeking and export-oriented investments relies heavily on technologically intensive sectors like IT, engineering and pharmaceuticals, which often involve the transfer of knowledge as well as the assignment and licensing of intellectual property (IP)⁶⁴ (see chapter II). Overall, the existing framework provides protection of IP rights for the creative industries as well as scientific work, including IT and computer programming. It allows for the registration of patents, industrial design and trademarks.⁶⁵ Inventions can also be protected as utility models or trade secrets, and signs can be protected as geographical indications or designations of origin. The basic national legislations include the Law on Copyright and Related Rights of 2006, the Law on Inventions, Utility Models and Industrial Designs of 2008, the Law on Trademarks of 2010, the Law on Geographical Indications of 2010 and the Law on Legal Protection of Topographies of Integrated Circuits of 1998. The Law on the Protection of Economic Competition, the Civil Code and the Criminal Code also contain provisions that are relevant for IP. With regards to international commitments, Armenia has ratified most of the relevant World Intellectual Property Organization (WIPO) treaties, and national legislation has been reviewed in the WTO's Council for TRIPS. Accession to the EAEU has further highlighted the importance of IP protection from a regional standpoint, although the parties to the treaty will not lose regulatory powers on this field.⁶⁶

The Intellectual Property Agency in the Ministry of Economy has a remit for registering and enforcing IP rights in Armenia. The agency is responsible for registering and overseeing the overall governance of IP-related matters, including legislation and compliance as well as cooperation with international organizations like WIPO, the WTO, the Eurasian Patent Office and the World Customs Organization. In 2005, Armenia created an IP Rights Enforcement Unit in the Organized Crime Department of the Armenian Police, which acts based on complaints from right holders (UNECE, 2014).

Despite a comprehensive legal framework on IP, Armenia's industry-science linkages are under-developed and innovation performance is deemed weak, although notable exceptions exist. Good practice indicates that for technologically intensive-activities, investment regimes should promote private sector cooperation, reward linkages with domestic universities and facilitate joint ventures and all technological transactions (UNCTAD, 2011). In Armenia, a recent assessment has pointed to the lack of commercialization of science, and weak cooperation between academia and business as a symptom of limited communications between innovation stakeholders (FAST, 2018). One of the reasons is a legal loophole regarding the attribution of intellectual property rights in employment contracts in higher education institutions, which reduces opportunities for the commercialization of IP rights through the creation of spin-off companies from universities or research institutes. In particular, the Law on State Non-Commercial Organizations constrains engagement in entrepreneurial activities by projects managed by State research institutes, requiring prior Government approval.⁶⁷ Some stakeholders have nonetheless managed to overcome these hurdles, and positive examples of linkages between education and industry are emerging in the high-tech arena (see chapter II).

Armenia also lacks a modern research exception in its domestic patent law. Art 17(2) of the Law on Inventions (2008) exempts "scientific research or scientific experiment" from patent protection. This is



arguably too narrow. Germany and the United Kingdom, for instance, allow researchers to engage in any research on a patented substance, even with a commercial objective. The restriction on scientific research may be an obstacle to effective university-industry collaboration on R&D. The law should not refer to “scientific” research, but to “experimental use”.

Limited support for patenting abroad could also deter investment in high-value added activities.

Patent registration abroad is expensive, but it is a must for high-tech industries that wish to export to advanced industrialized countries in Europe, the United States or Japan. In the absence of foreign patent registration, Armenian patentees face the risk that their codified knowledge may be imitated abroad. However, a recent study concluded that when applicants wish to file a patent application abroad, the Government is unable to provide much assistance. Its role is generally limited to the provision of basic information on patent fees and patent attorneys (UNECE, 2014).

Low awareness and poor monitoring of violations to intellectual property harm the business climate.

Due to the slowness of the judiciary, the bulk of cases involving copyright or patent infringements are settled through out-of-court proceedings (see section H). While the Government has made efforts to strengthen protection, enforcement mechanisms could be improved. Compliance has lagged particularly at the borders. The Government has recently created units in customs and police to improve the seizing of counterfeited goods, but results are still to be seen in statistics. In the context of investment promotion strategies for nascent industries that significantly rely on branding (e.g. agriculture, wine) (see chapter II), mislabeling of imported inputs can be an existential threat. Thus, adequate monitoring of certificates of origins and standard compliance is crucial. At the time of the fact-finding mission for this Review, the Government was developing an IP education programme to sensitize students in university to improve their knowledge about IP rights, but awareness remains quite limited amongst the general public.

Standardization and certification register good progress, but gaps persist.

Both national legislation and the EAEU contain provisions on standards, technical regulations and conformity assessment. Each of these issues are under the remit of different Government units that form part of the national quality infrastructure. The National Institute of Standards (SARM) acts as the national standardization body, coordinating the activities of various technical committees. The National Institute of Metrology and the National Accreditation Body (ARMNAB) are also significant stakeholders. SARM keeps an index of standards, which covers international (ISO), CIS (GOST), EU (EN), Armenian (AST) and other standards. In recent years, there has been a convergence toward the use of international standards and certification procedures (e.g. in energy and construction). Certificates of conformity recognized by SARM are required for the commercialization of most food products, alcoholic drinks, and electro-technical and petroleum products (WTO, 2018). However, conformity assessment results are not recognized internationally and ARMNAB – though an associate member of the European Cooperation for Accreditation (EA) – is yet to join the EA Multilateral Recognition Arrangement.⁶⁸ In addition, despite improvements, some old GOST standards are still in use (United States Department of Commerce, 2019).

Increasing capacities for compliance with IP rights and enhancing certification bodies should be a priority.

A recent World Bank report that elaborates on findings of its Enterprise Survey noted that even though the diffusion of internationally-recognized quality standards in Armenia is above that of comparators like Serbia and Slovenia, the export participation of the country is much lower, signaling unexploited export potential.⁶⁹ Whereas the survey did not focus on specific industries, evidence from UNCTAD’s fact-finding mission, based on interviews with private stakeholders in the IT and pharmaceuticals sectors, shows



that indeed, many businesses in these industries seek neither IP protection nor certification for Armenian products abroad. At the same time, IP protection and certification for high-value products to meet the standards of target markets in the Russian Federation, Europe or the United States, is considered to be very expensive.

The Government is working on updating the IP legislation... The goal is to broaden the scope of protected rights and align them with requirements of the EAEU. In particular, the revised Law on Copyright will include provisions from international agreements (i.e. the Marrakesh and Beijing Treaties). New regulations on patents and industrial design and amendments to the Law on trademarks are also being considered. The Intellectual Property Agency and the Ministry of Justice have proposed changes to the Civil Code and the Criminal Code aimed at providing more details on the information that courts should take into consideration when determining IP-related damages and compensation.⁷⁰ The approval of these legal reforms was delayed due to the change in Government but the bills will be re-submitted to the National Assembly for consideration before the end of 2019.

...and offering IP rights-related services. Armenia is a participant in the WIPO Technology and Innovation Support Centre (TISC) programme. It provides innovators in developing countries with access to locally based, high quality technology information and related services, helping them to exploit their innovative potential and to create, protect, and manage their IP rights. The Foundation for Armenian Science and Technology (FAST) along with the Intellectual Property Rights Centre of Armenia have engaged in agreement and established the first TISC centres in Armenia.⁷¹

Assessment and recommendations

During recent years, the Government has worked to align domestic intellectual property legislation and quality certification to both international requirements and modern standards, even if monitoring and compliance has lagged and public awareness is weak. Looking forward, the Government should consider to:

1. **Work to improve the fluidity of industry-science linkages.** Measures include removing legal loopholes that prevent the commercialization of inventions in higher education and research institutions, promoting industrial clusters and leveraging on the Armenian diaspora of scientists. Armenia's booming industry in ICT and engineering shows that successful interactions are possible and could be replicated (see chapter II). In addition, the establishment of Technology Transfer Offices (TTO) at the universities and scientific centres could be considered. Given the existing capacities of research and the size of the country, it is suggested to establish a TTO at a national level, which would coordinate and support commercialization efforts on a centralized basis. Upon success and growth of the scale and volume of commercializable research, decentralization of TTOs could take place.
2. **Enhance the capacities of the Intellectual Property Agency.** This should aim at ensuring that it can better assist firms on strategic decisions about IP protection. In particular, the following is recommended:
 - a. Intensify cooperation between the IP Agency and WIPO to assist in seeking patent protection for Armenian inventions abroad, i.e. under the WIPO-administered Patent Cooperation Treaty (PCT), which facilitates the administrative burden for patentees (filing one international application under the PCT rather than individual national applications).



- b. The IP Agency should not only register IP rights but take a pro-active role in facilitating university-industry linkages, e.g. through 1) workshops on patent policies for universities; 2) legislation that facilitates university patenting but in return obliges universities to market their inventions through licensing agreements with the private sector.
3. **Enhance quality certification with the goal to obtain market access for selected products.** In the context of EAEU integration, this will already occur for certain target activities (e.g. pharmaceutical generics). For other products, targeting investments from multinational enterprises (MNEs) could help reduce non-tariff barriers in certain markets – for instance, agricultural fresh products – (see chapter II). In the longer term, the Government could also consider signing mutual recognition agreements with third-country authorities regarding the conformity assessment of regulated products.
4. **Improve awareness, monitoring and compliance of IP rights.** Ongoing education campaigns should be continued and extended to the general population, and the capacity of the police to detect violations should be increased. Given Armenia's efficiency-seeking investment strategy, compliance requires a holistic approach that also contemplates effective monitoring at the borders and anti-corruption measures (see section H).

H. GOVERNANCE

1. Judiciary

Stakeholders in both the private and public sectors consider the Armenian courts system inefficient and prone to corruption. Interviews by UNCTAD consistently highlighted the inefficiency and lack of predictability involved in commercial dispute resolution as one of the key issues affecting the Armenian investment climate. In the absence of specialized tribunals, commercial and contractual matters are governed by civil courts, which suffer from huge backlogs. Solving a commercial dispute can reportedly take several years.⁷² The Ministry of Justice recognizes the severity of the issue and attributes it, among others, to the low number of professional judges (8 per 100'000 citizens compared to an average of 22 per 100'000 in other countries of the Council of Europe (Council of Europe, 2018)), which has remained practically unchanged, despite the increasing number of court cases over recent years.⁷³ Additional factors are the relatively low salaries and budget allocations to the judiciary, which contribute to rent-seeking behavior (see below).

Alternative dispute resolution (ADR) mechanisms, including mediation and arbitration, are available but their use is limited. Armenia adopted a Law on Commercial Arbitration based on the UNCITRAL Model Law in 2006 and an Arbitration Court was established at the Chamber of Commerce and Industry of the Republic of Armenia in 2007. However, neither mediation nor arbitration are widely used, and they have had no real impact on reducing the pressure on the judiciary system. Representatives of the Chamber interviewed during the fact-finding mission estimated that less than 20 cases are submitted yearly to ADR. The lack of awareness of ADR mechanisms is certainly an issue. But specific formulations in the Law also limit resort to arbitration. These include provisions which make it difficult to determine the exact court that would have jurisdiction to perform supporting functions to the arbitration tribunal; provisions which makes the granting of interim measures before the appointment of arbitrators practically impossible; or the absence of legal guidelines for the national courts that need to appoint the arbitrators if the parties have not reached an agreement.⁷⁴

The Government has embarked on an extensive judiciary reform project, with the help of development partners. The Council of Europe has been providing support to the implementation of the judicial reform in Armenia, and assisted the Government implement the 2012–2017 Strategic Programme for Legal and Judicial Reforms. The Council provided legal drafting support, as well as institutional and capacity-building support to the Ministry of Justice, judicial institutions, judges, advocates, mediators and arbitrators. This assistance was instrumental in the adoption of a new Judicial Code and a new Civil Procedure Code, along with revisions of the draft Code of Administrative Offences and a number of other legal acts (Council of Europe, 2019). Long-term institutional reforms in the field of justice are an urgent priority for the current administration. The Ministry of Justice has elaborated the draft 2019–2024 Judicial and Legal Strategy and the related action plan. A working group including representatives of civil society has been established that will look at efficiency and transparency concerns. Reforms being considered include undertaking “integrity checks” for judges, increasing the number of judges and improving court and penitentiary infrastructure.⁷⁵ The creation of commercial courts is not being prioritized due to budget concerns. As part of its support programme, the Council of Europe will continue assisting to improve ADR policy, train students, mediators and arbitrators, and enhance awareness about ADR mechanisms (Council of Europe, 2019).

2. Public governance and corruption

The Armenian society has called on the authorities to improve public governance, fight corruption and address entrenched conflict of interest. Given the context of a small, landlocked economy with high concentration in several markets, conflict of interest and the political use of regulatory and monitoring agencies have, for long, restricted the integrity of markets and hampered fair business competition, as reflected in several international rankings and reports.⁷⁶ Most stakeholders agree that these issues have played a deterrent role on investment, including FDI. A lack of progress in this area was a significant reason behind the mass protests in 2018 that led to the most recent government change.

Poor enforcement has limited the effectiveness of an otherwise comprehensive anti-corruption framework. Until recently, the fight against corruption had primarily concerned the legislative side, i.e. the passing of basic regulations on ethics and conflict of interests, whistleblower protection, the criminalization of trading in influence and illicit enrichment. Impact, however, was limited, largely due to poor enforcement. Anti-corruption competences are spread across several agencies and investigative skills are weak. The Commission for the Prevention of Corruption, supposed to take over the asset declaration system from the Ethics Commission, has not been established and courts struggle to manage workloads (IMF, 2019). The most recent monitoring under the Istanbul Anti-corruption Action Plan recommended Armenia to better ensure judicial and prosecutorial independence and integrity, and expand efforts to detect, investigate and prosecute high-profile and complex corruption cases.⁷⁷ It also recommended transparent and objective selection of members of the Commission for the Prevention of Corruption; implementation of the newly adopted legislation on whistleblower protection, improved scrutiny of asset declarations, increased transparency in the election of prosecutors and the introduction of corporate liability for corruption offences (OECD, 2018).

The new administration has generated hope for a new era, and some results are already showing. The commitment and political willingness to combat corruption is at the core of the new Government's agenda. The business sector recognizes that the positive effects of such political will are trickling down the public administration. Many reported, for instance, that rent-seeking and harassment by customs or tax officers, often motivated by the need to protect specific business interests, has gone down significantly. Statistics also show an increase in corruption-related prosecution cases between 2017 and 2018 (from 500 to 1988), of which 1469 resulted in criminal charges (compared to only 403 in 2017).

The Government has recently adopted a draft Anti-Corruption Strategy, and several initiatives to improve governance are ongoing. One key objective of the Strategy is to establish a unified specialized anti-corruption law enforcement body, which will combine all operative and investigative powers, with a remit to implement the Anti-Corruption Strategy (Council of Europe, 2019).⁷⁸ The Strategy also envisages the establishment of anti-corruption courts and specialized department within Prosecutor General's office. A special subchapter of the Strategy is dedicated to the further developing the asset declaration system, which is also the object of a draft law amending the Public Service Law. In addition, in May 2019, an electronic platform for anonymous reporting was launched to ensure the implementation of the whistleblower protection legislation. Finally, a draft revision of the Criminal Code, which is to be submitted to the Parliament, contains regulations on the introduction of corporate liability for corruption offences.

But several issues persist. Transparency International has expressed concerns that the document lacks performance indicators and explicit monitoring procedures. The fact-finding mission for this report has also



found that parallel anti-corruption strategies or action plans are being developed by a number of agencies, including the Ministry of Justice and the Customs and Tax administration, without adequate coordination. This is one aspect which the Strategy aims to address by assigning a coordinating role to the Ministry of Justice. The Strategy states that risk assessments shall be conducted in all state bodies and several municipalities. Based on the risk assessment sectoral anti-corruption action plans will be developed and adopted.

Assessment and recommendations

The findings of this IPR share the general concerns of several stakeholders that a dysfunctional judiciary and poor governance could undermine the best of efforts regarding other business climate reforms. There is a clear need to restore citizens' confidence in their institutions and build a sound basis for economic growth. As it was mentioned in other sections of this IPR, in addition to improving the independence and probity of the judiciary, the findings from interviews with private stakeholders have pointed to the need to adopt a holistic approach to the fight against corruption that delivers progress in the following areas: a) transparency and equal treatment at the borders with regards to trading internationally, particularly for the application of customs duties and VAT; b) internal oversight and control of inspectorates, particularly in sensitive areas like taxation, labour and environment; c) transparency on import licensing and access to land; and d) the effectiveness of competition policy. To ensure success, it will be key that the Government does not lose the momentum it gained after the last election. In particular, it is recommended that the Government:

1. **Moves forward with planned reforms to speed up judiciary procedures.** Efforts should focus on reducing the caseload per judge as well as on addressing budgetary constraints, including the salary of judges.
2. **Improves and promotes ADR.** Key actions include raising awareness amongst private stakeholders and general public as well as increasing skills of mediators and arbitrators through training, including by development partners. Changes in legislation may be needed to speed up the recognition of awards by arbitration tribunals in courts.
3. **Implements the Anti-Corruption Strategy and proceeds with the establishment of a unified anti-corruption body and specialized anti-corruption courts.** This should be accompanied by the adoption of criminal sanctions to prevent undue influence on the operations of the body by political, business and other interests.



Armenia is a small landlocked country with exceptional geopolitical and logistical obstacles to trade. Upon independence in 1991, there was a painful collapse of some prominent industries, as their assured markets were lost, but a traditional strength in science and technology survived. Now, nearly 30 years later, there is a sense that Armenia is truly an “economy in transition” with growth in areas of traditional strength and an emerging revival in dormant sectors of the economy. Non-traditional exports are growing, though from a small base, and high-tech activities are booming, fuelled by local skills and the diaspora. Looking to the future, this report is tasked to assess the prospects for export and efficiency-seeking investment, with particular reference to the role that FDI could play in developing traditional sectors (e.g. textiles, agribusiness, wine or tourism) as well as new sectors (such as artificial intelligence and deep technology, pharmaceuticals and several regional services) and contributing to sustainable development and inclusive growth. The chapter begins with the strategic context: what are Armenia’s export markets, does it offer the efficiencies that investors seek and how much of a resource is the diaspora? This part is not prescriptive. The current market arrangements and the efficiency profile are taken as given to identify the investment prospects for export and efficiency-seeking investors. The second part selects the most likely winners and assesses their prospects for FDI attraction. Where needed, new policy measures are proposed to complete the reforms recommended in chapter I. A review of key outcomes needed in the current re-engineering of investment promotion closes the chapter.



Chapter

2

Strategy

I. STRATEGIC CONTEXT

A. THE MARKET POTENTIAL

1. Overall trade landscape

Despite constraints due to Armenia's landlocked position and political barriers to trade with neighbours, exports are expanding quickly. For political reasons, Armenia is unable to export to or through neighbouring Turkey and Azerbaijan. All merchandise exports are shipped overland and, apart from minor current flows to the Islamic Republic of Iran, must be transported north through Georgia. Yet, as mentioned in the context, the ratio of exports plus imports to GDP is 80 per cent. And, despite the constraints, some investors interviewed for this report prefer to see Armenia as a hub with under-exploited regional potential. Mining has been the mainstay of exports since independence but other products exports are expanding quickly from a small base. Armenia's main exports are shown in table II.1.

Table II.1. **Armenia's merchandise exports by main product group, 2010–2017**
(Thousands of dollars and percentages)

| Products | Cumulative exports | Compound annual growth rate |
|---|--------------------|-----------------------------|
| Manufacture of metals and non-metal minerals | 3 335 699 | -3 |
| Metal ores and metal scrap | 2 866 539 | 20 |
| Beverages and tobacco | 2 147 952 | 21 |
| Food and live animals | 831 778 | 15 |
| Apparel and clothing | 523 684 | 33 |
| Machinery and transport equipment | 453 300 | 4 |
| Mineral fuels, lubricants and related materials | 409 831 | 3 |
| Chemicals and related products | 222 095 | 15 |
| Total exports | 12 153 366 | 11 |

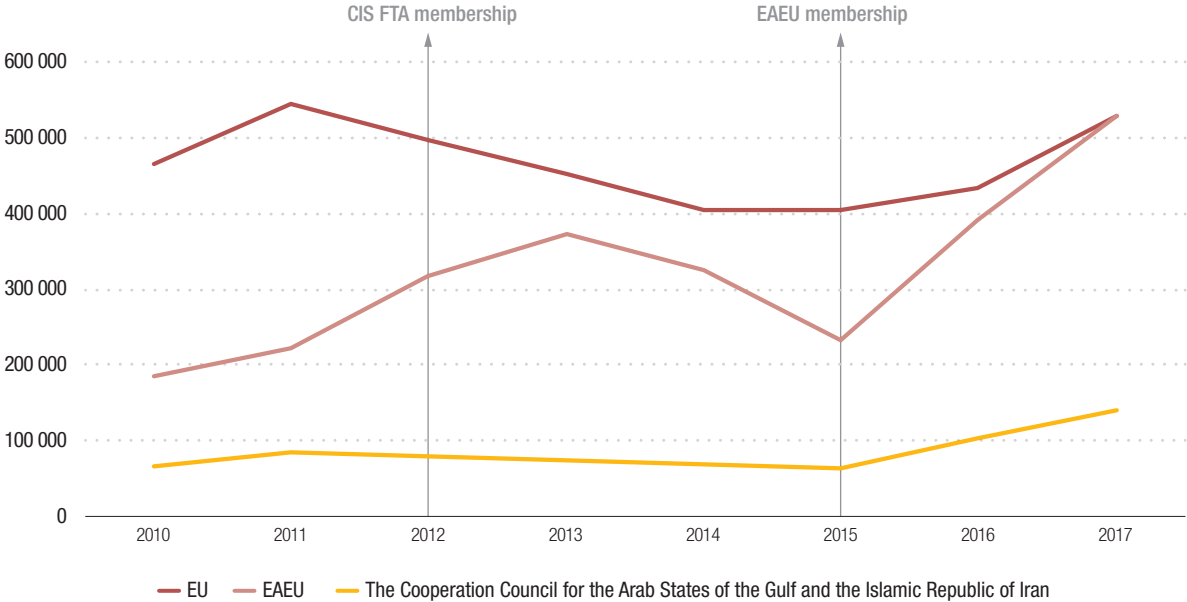
Source: UNCTADStat.

Armenia has preferential trade arrangements with its principal trading partners: The Russian Federation and the European Union. As mentioned in the context, since 2015, Armenia has been a member of the Eurasian Economic Union (EAEU), which is a customs union with a common external tariff. The customs union effectively sets Armenia's trade policy in negotiating free trade agreements (FTAs) with third countries. The first EAEU FTA entered into force in October 2016 with Viet Nam. The EAEU has signed a framework economic cooperation agreement with China and concluded a temporary FTA with the Islamic Republic of Iran in May 2018 (WTO, 2018). It is negotiating additional FTAs with Egypt, India, Serbia and



Singapore. Armenia also benefits from unilateral preferences granted by the European Union (and Norway) under the GSP+ system. It has further GSP arrangements with Canada, Japan, Norway, Switzerland and the United States. Figure II.1 shows the trends in overall merchandise exports of Armenia to three key markets – the EAEU, the European Union and to the Islamic Republic of Iran and the Gulf States. More detail on the size and accessibility of these markets to Armenian products is given in the sections below.

Figure II.1. Armenia’s merchandise exports to key trading partners, 2010–2017 (Thousands of dollars)



Source: UNCTAD Intrastat.

2. The Eurasian Economic Union

Armenia, member of the EAEU since 2015, has preferential access to its largest market, the Russian Federation, and to Belarus, Kazakhstan and Kyrgyzstan. It had already enjoyed duty free entry to these markets at least since a free trade agreement in 2012, the CIS FTA. The customs union gives Armenia preferential access to a market with a GDP of \$1.6 trillion, compared with Armenia’s GDP of around \$12 billion. Table II.2 indicates the size of tariff protection afforded to union members by the common external tariff and the union’s imports from all sources. Simple and weighted average tariffs on EU and Turkey imports into the EAEU on product categories of interest to Armenia are chosen to illustrate the protective effect.⁷⁹ Overall, the protective effect is moderate but the single market is very large relative to Armenia’s size.

Since 2010, Armenia’s total exports of goods have more than doubled to stand at \$2.24 billion in 2017. The Russian Federation is by far the largest Armenian market in the Union. Exports to the country tripled in that period to \$516 million. They account for around 27 per cent of Armenia’s sales of goods abroad. Brandy and wine (about 90 per cent and 10 per cent of beverages values respectively) account for the bulk of these exports. But garments, foods and jewellery have shown strong growth from humble beginnings (table II.3).

Table II.2. **Tariffs of the EAEU on selected products imported from the EU and Turkey, 2017**

| HS Code | Product | EU tariff (Per cent) | Turkey tariff (Per cent) | Total EAEU Imports* (Billions of dollars) |
|---------|---|-------------------------|-----------------------------|--|
| 01-05 | Animal products | 7.07/1.06 | 6.05/6.46 | 8.4 |
| 06-14 | Vegetable products | 7.06/4.58 | 5.26/3.41 | 14 |
| 16-24 | Prepared foods and beverages, tobacco products | 8.32/7.25 | 6.89/6.69 | 13.3 |
| 30 | Pharmaceuticals | 3.95/3.73 | 4.2/3.68 | 12.8 |
| 50-63 | Textiles | 6.61/4.87 | 6.10/4.01 | 13 |
| 71 | Jewellery items | 9/13/10.22 | 8.85/11.67 | 0.6 |
| 72-83 | Base metals | 6.32/6.63 | 6.12/7.30 | 22.8 |

Source: UN Comtrade.

Note: Presentation format is simple average/weighted average. * Imports from all sources excluding Armenia.

Table II.3. **Armenia's merchandise exports to the Russian Federation by main product, 2010–2017** (Millions of dollars)

| | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 |
|---|-------|-------|-------|-------|-------|-------|-------|-------|
| Beverages | 88.9 | 108.5 | 166.2 | 179.9 | 150.5 | 86.0 | 138.4 | 201.5 |
| Textiles and garments | 1.5 | 1.2 | 1.1 | 1.6 | 1.3 | 22.7 | 43.4 | 58.3 |
| Fruits and vegetables | 12.7 | 23.1 | 39.1 | 48.0 | 40.4 | 32.4 | 62.6 | 47.5 |
| Non metallic mineral manufactures | 16.7 | 21.6 | 33.9 | 45.9 | 43.6 | 8.8 | 36.7 | 45.9 |
| Fish and fish preparations | 4.6 | 12.0 | 21.0 | 32.8 | 30.6 | 13.3 | 11.3 | 20.2 |
| Machinery and transport equipment | 13.7 | 26.4 | 18.4 | 11.7 | 11.1 | 7.1 | 22.1 | 17.6 |
| Medicinal and pharmaceutical products | 0.9 | 1.0 | 1.1 | 1.4 | 1.8 | 2.8 | 6.1 | 11.2 |
| Others | 35.5 | 17.6 | 26.6 | 33.7 | 29.2 | 47.3 | 53.7 | 113.9 |
| Total exports to the Russian Federation | 174 | 211 | 307 | 355 | 308 | 221 | 374 | 516 |
| Total exports to all countries | 1 011 | 1 334 | 1 380 | 1 480 | 1 519 | 1 485 | 1 792 | 2 245 |

Source: UNCTADStat.

3. The European Union

The European Union has reached out to Armenia in granting favourable trade access, but overall trade has not expanded and remains dominated by mineral exports. In 2009, Armenia was granted GSP+ status, which allows duty free terms on an expanded range of imports. In July 2018, the Comprehensive and Enhanced Partnership Agreement came into force, which reinforces the willingness of the EU to be a beneficial partner. The value of all goods' exports to the EU, however, has stayed constant at



around \$500 million since 2010 with copper, iron and steel continuing to account for around 80 per cent of exports. As a consequence of this trend, the EU's share of total Armenian goods' exports has fallen from 50 per cent of exports in 2010 to 28 per cent in 2017. The EU reports a rise in imports from Armenia under GSP+ from €42 million in 2014 to €108 million in 2016.⁸⁰ However, most of those imports were aluminium, iron and steel in both years. The only bright spot is in garments whose value has risen from a very modest \$14 million in 2010 to \$54 million in 2017.

A more detailed look at the effective benefits of GSP+ is required, in product areas of interest to Armenia. An analysis was made by UNCTAD of applied EU tariffs facing a selection of major or competing exporting countries for products of interest. These were fruit and vegetables (fresh and processed), flowers, garments, wine and pharmaceuticals. Applied rates took into account, for selected leading or competing exporters, the existence of preferential trade regimes with the EU. There are several of these:

- The Everything-but-Arms (EBA) scheme offers zero tariffs to least developed countries. Bangladesh exports \$17 billion worth of garments and accessories per year to the EU under this scheme.
- The wide availability of the GSP scheme and, to some extent, the GSP+ scheme. For example, GSP+ applies to Sri Lanka's \$1.7 billion of garments' exports to the EU annually.
- The extension of trade preferences to Cotonou countries under Economic Partnerships Agreements.
- The many free trade agreements completed by the EU, which are especially useful to Asian and South American countries.

Also the recent accession to the EU of lower income Eastern European countries (Bulgaria and Romania in 2007, Croatia in 2013) gave them access to the EU single market.

The GSP+ scheme does not confer advantaged access to the EU versus competing suppliers, but removes the disadvantage of MFN tariffs. The analysis confirmed that the GSP+ is a "good fit", i.e. it offers duty free access to key Armenian products.⁸¹ It does not confer superior market access on Armenia but, importantly, levels the playing field. Armenia's eligibility will be reviewed when it reaches a certain national income threshold. It is certainly worth retaining as the EU is a huge nearby market (table II.4 gives examples). However, the conclusion is that the GSP+ scheme is not a source of unrivalled competitive advantage, and Armenia will have to rely on its commercial prowess to carve out its place in the EU market. At present, it has less than 1/10th of 1 per cent of European imports in products of interest.

Table II.4. EU total Imports of selected products of interest to Armenia 2017

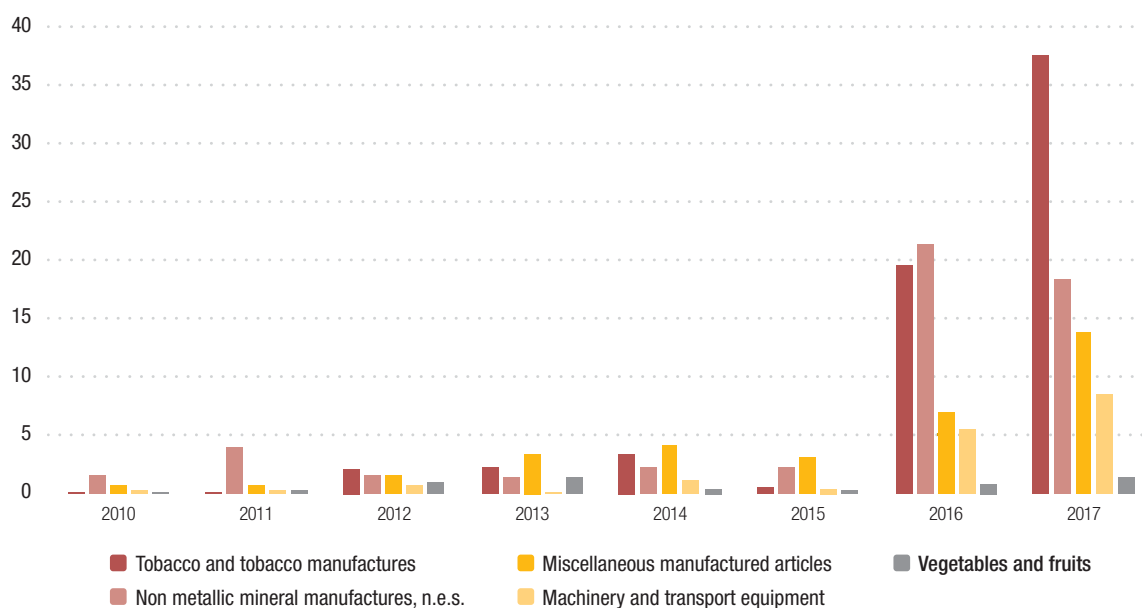
| HS Code | Product category | Imports (Billions of dollars) |
|----------|-------------------------|-------------------------------|
| 07,08,20 | Fruit and vegetables | 35.1 |
| 60-63 | Textiles and garments | 59.9 |
| 30 | Pharmaceutical products | 74.7 |

Source: UN Comtrade.

4. The Islamic Republic of Iran and the Gulf States

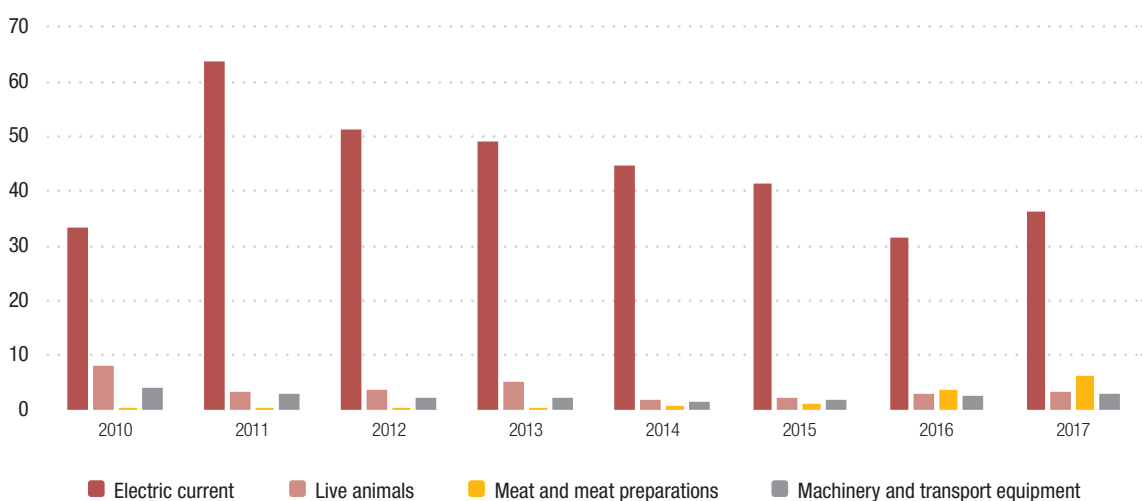
At first sight, the region appears a highly prospective target but trade is narrowly focussed. Figures II.2 and II.3 show the regional trend by main export products for the period 2010–2017. Data for country

Figure II.2. **Main exports from Armenia to GCC countries, 2010–2017** (Millions of dollars)



Source: UNCTADStat.

Figure II.3. **Main exports from Armenia to the Islamic Republic of Iran, 2010–2017** (Millions of dollars)



Source: UNCTADStat.

of destination show that Iraq, the Islamic Republic of Iran and the United Arab Emirates are Armenia's 4th, 8th and 9th biggest export markets and account for around one-quarter of all exports. However, the trade is heavily concentrated by both product and individual country import. Iraq's imports (\$150 million in 2018) were almost entirely one commodity – tobacco products (mainly cigarettes). In 2018, of \$94 million of total exports to the Islamic Republic of Iran, \$76 million was electricity generated in Armenia from Iranian gas. Exports to the United Arab Emirates in 2018 totalled \$73 million, of which \$34 million was tobacco products and \$31 million was jewellery products. There are negligible exports to the Gulf States' biggest economy, Saudi Arabia.

There could be selective opportunities for other Armenian products. The Islamic Republic of Iran is a billion-dollar import market for fruits and vegetables (although mostly tropical products) and Iraq imports over \$300 million worth every year. Saudi Arabia imports over \$3 billion fruit and vegetables and more in textiles and garments. Pharmaceuticals is also a consistently large market, with many of these countries importing more than \$1 billion worth annually.

5. Services

Services can access world markets with few barriers. Armenia can access a global market for its leading services, in particular high-tech services such ICT, systems engineering and contracted R&D (see section II of this chapter). These can be largely performed without the need to create a permanent establishment abroad. Financial and professional services will typically be regulated in host countries but in the single EAEU market there is likely to be either a common or shared regulatory approach to licensing. For the purposes of this report (apart from a discussion in Part III of regional financial services), it can be taken that the export services market is open and large.



B. THE EFFICIENCY PROFILE

Comparative rankings broadly confirm the advantages (labour) and disadvantages (infrastructure) in Armenia’s profile for efficiency-seeking FDI. Table II.5 presents a snapshot based on the Global Competitiveness Rankings for 2019 prepared by the WEF. Each pillar in the table is a composite of several performance indicators, with ranking out of 140 countries. The table compares Armenia with fellow EAEU members⁸² and with other neighbours in the region – Azerbaijan, the Islamic Republic of Iran, Georgia and Turkey. Labour is likely to be a key advantage in terms of costs and well-functioning labour market. Conversely, infrastructure is always going to have a low ranking in a landlocked country with no overland transit rights in two neighbouring countries. However, the picture is more nuanced as will be seen in this discussion below of the individual items.

Table II.5. **Armenia in the global competitiveness rankings 2019**

| Pillar | Armenia | Best in EAEU* | Best in region* |
|----------------|---------|-----------------------|-----------------------|
| Infrastructure | 60 | Russian Federation 50 | Azerbaijan 38 |
| ICT adoption | 59 | Russian Federation 22 | Russian Federation 22 |
| Skills | 61 | Russian Federation 54 | Georgia 46 |
| Labour market | 32 | Kazakhstan 25 | Azerbaijan 21 |

Source: WEF, 2019.

Note: *Excluding Armenia. Belarus is not covered in the rankings.

1. Labour costs, skills and availability

Armenia has wage cost advantages, particularly for skilled staff. Average salaries are similar to those paid elsewhere in the region, apart from much higher remuneration in the Russian Federation (table II.6). Data for 2016 show an industry dispersion – the lowest in agriculture and processing (\$206–295 per month) and the highest in finance and insurance (\$819 per month). A marked wage cost advantage against competing suppliers of particular Armenian exports is shown in table II.7, including for the IT sector, although with significant variance (table II.8). Comparable data for skilled and executive staff in other industries are not available but they are also likely to be competitive with international norms (Ministry of Economic Development and Investments, 2017).

However, Armenia ranks less well when pay and productivity are combined. Its is 54th on the “Pay and Productivity” sub-indicator of the global competitiveness rankings, suggesting an issue with labour productivity. By comparison, the Russian Federation’s ranking on this sub-indicator (37th) is much better than its overall labour ranking (62th) (WEF, 2019). Interviews for this report, and detailed analyses at industry level, consistently point to lack of investment in modern equipment and technology and poor management and operational practices in industry and agriculture.⁸³ There are also issues with skills.

A widely varying skills profile has not fully broadened since independence. The areas of excellence assigned to Armenia within the Soviet Union were science and microelectronics. The first Soviet computer was built in Armenia and, during that era, 40 per cent of mainframes for the entire Union were manufactured in Armenia. These areas of excellence are reflected today in a flourishing high-tech sector.

Table II.6. **Gross average monthly wages** (Dollars at current exchange rates)

| Pillar | 2015 | 2016 | 2017 |
|---------------------------------|------|------|---------|
| EAEU | | | |
| Armenia | 359 | 363 | 404 |
| Belarus | 422 | .. | .. |
| Kazakhstan | 568 | 418 | 463 |
| Kyrgyzstan | 209 | 212 | 223 |
| Russian Federation | 558 | 547 | 671 |
| Other regional countries | | | |
| Azerbaijan | 455 | 313 | 307 |
| Georgia | 396 | 397 | 398 |
| Bulgaria | .. | .. | 537 |
| Romania | .. | .. | 819 |
| Western Europe | .. | .. | 3–4000* |

Source: United Nations Economic Commission for Europe.

Note: *Excluding Portugal.

Table II.7. **Hourly compensation in Armenia and major exporting countries** (Dollars per hour)

| Product | Armenia | Comparators | | |
|--------------------|---------|-------------|-----------------------|----------------------|
| Food and beverages | 2 | Brazil (8) | Spain (23.4) | Holland (34.6) |
| Textiles | 1.2 | China (4.5) | Turkey (4.1) | Italy (27.1) |
| Pharmaceuticals | 2.65 | India (2.4) | United Kingdom (36.6) | Switzerland (101.2) |
| IT | 4.5 | India (5.4) | China (5.4) | United States (53.5) |

Source: Business Armenia.

Table II.8. **Monthly salaries in the Armenian IT sector 2017** (Dollars per month)

| Profile | Salary |
|------------------------------|---------|
| Junior technical specialist | 300–400 |
| Software developer | 630 |
| Senior specialist | 3500 |
| Average monthly salary in IT | 1025 |

Source: Enterprise Incubator Foundation 2018.

In other areas, skills are less well-developed. Empirical studies have shown that there is a skills mismatch between market needs and the curricula and quality of training of technical and vocational education and training (TVET) institutions, particularly in sectors that are a priority for Armenia's development, such as tourism and agriculture (World Vision Armenia, 2018). For instance, basic training on foreign languages and more specialised knowledge on viticulture and green housing are deemed below standard or missing.



Entrepreneurship skills and general hard skills, such as basic accounting or finance, are also in need of improvement. The situation is more serious in rural areas, where youth unemployment is higher. There is also a gender dimension, with around 80 per cent of TVET education favouring young women, many of whom, in spite of possessing education and skills, remain outside the labour force due to family responsibilities or childcare (EU, Save the Children and MediaMode, 2018).

Education participation rates are only moderate and in-company training is not widespread. In 2017, Armenia's tertiary enrolment rate was 52 per cent, higher than in Azerbaijan (27 per cent) and close to Georgia's (58 per cent), but significantly lower than in the Russian Federation and Ukraine, where the enrolment threshold is above 80 per cent. The linkages between education and industry are also deemed weak, and although notable exceptions exist (box II.1), in-company training is not common.⁸⁴ Whereas employers point to deficiencies in the educational system for not providing adequate specialists that match labour market needs, the management of educational institutions point to a lack of involvement of private sector stakeholders on such issues as syllabus preparation for the provision of practical skills to the students (EU, Save the Children and MediaMode, 2018). This lack of communication likely exacerbates a tendency of young Armenians to emigrate, possibly in response to a lack of job opportunities in a context of high unemployment rates. The emigration of skilled labour increases the inflow of remittances, but it may also lead to an overall reduction in the country's prosperity (IMF, 2017).

A sobering assessment is made in recent reports. Recent research raises concerns about the direction of education, and some investors and commentators have also raised concerns as to the maintenance of standards and the suitability of the education system to the needs of the modern workforce. A report found that skill shortages negatively affected more than 70 per cent of businesses surveyed, and 64 per cent of those companies did not have a training budget (ILO, 2016). These results should be treated with caution – over 2/3rds of surveyed companies had less than five employees, and over a third were in agriculture, hunting and forestry. Whilst the results are skewed to SMEs, and primary industry in particular, they do suggest skills gaps exist despite the performance of the high-tech industries. A comprehensive report sponsored by the EU also notes that: "As in other CIS countries, the population of Armenia is well-educated. . . but despite the large-scale reforms supported by the international donor community in Armenia, numerous studies point to a backsliding in the quality, access and integrity in education." Moreover, the budget for education has declined to 2.2 per cent of GDP in 2018, according to the report, which compares with 7-10 per cent spent on education in EU countries (EU, Save the Children and MediaMode, 2018).

There is full awareness of the need to match qualifications to labour force needs. The Ministry of Education is determined to align outputs more closely with the needs of the private sector. There are many initiatives, often with donor support and usually in collaboration with the private sector. Examples include:

- The introduction of entrepreneurship courses at primary school.
- The "Make it Match" and the "Work Armenia" programmes aimed at strengthening education and labour market linkages, capacity building for structural changes in the economy and formation of knowledge-based economy.
- The participation in the Torino process to boost work-based learning.
- The development of a national qualifications system that parallels the European Qualifications Network.
- The introduction of business management degrees, including executive MBA programmes.



Engineering/IT is the top area of job demand according to experts and the human development pipeline seems strong. The growth in demand for IT skills has been enormous. There were around 800 actively operating IT companies by 2017 including start-ups and nearly 90 per cent were started after 2000. They employed over 15,000. Universities appear to have responded – during the school year 2017/18, 3,000 students were enrolled in university IT courses and 10,070 students in all IT and high-tech areas (12.8 per cent of the university population) (ETF, 2018). And although gaps persist, as highlighted above, skills have been strengthened by collaboration with industry as noted in box II.1. Moving into data science and artificial intelligence (AI), the next frontiers for Armenia (see section B.1.), will require increased collaboration with industry and the development of schools and special education programmes to nurture AI specialists.

Box II.1. **University-industry collaboration in ICT and engineering education**

Eight universities offer ICT and related engineering studies programmes, the largest of which are the National Polytechnic University of Armenia (NPUA) and the Yerevan State University (YSU). NPUA hosts the Armenian National Engineering Laboratories (ANEL). The main goal of the Project is to meet the demand of the engineering industry in quality specialists and graduates educated on up-to-date technological base to confront the employee shortage and to increase value-added and innovativeness of Armenian high-tech businesses, thus increasing their international competitiveness. The objectives of the project are to strengthen the educational capabilities and enhance the research potential of the Armenian engineering sector by upgrading and expanding the NPUA educational and research facilities to the world standard through the establishment of ANEL. Several of these universities have collaborative programmes with leading international companies. Examples include:

- PUA hosts the Microsoft Innovation Centre of Armenia to prepare students and industry with the specialist IT skills, particularly in programming, to work in the industry or begin start-ups.
- YSU hosts the Innovative Solutions and Technologies Centre, which includes IBM as a sponsor, for training in cloud computing, cyber security, cognitive computing, data analytics and artificial intelligence. A new master's degree programme in big data began in 2017. This is a joint project by the Government of Armenia, Enterprise Incubator Foundation, IBM, the United States Agency for International Development (USAID) and the Yerevan State University.
- Synopsis runs undergraduate and graduate programmes at several universities including micro-electronics at NPUA and integrated circuits design at YSU.
- Samsung partners YSU in the Samsung Learning Centre.
- The Armenian-Indian Centre for Excellence in Information and Communication Technologies is a joint project of the Governments of Armenia and India, which is implemented by Enterprise Incubator Foundation (from the Armenian side) and C-DAC centre (from the Indian side). The Centre is located at Yerevan State University and delivers both short-term and long-term courses designed to fit a wide variety of audiences;
- The Gyumri Information Technologies Centre (GITC) is a technological educational center which provides post-graduate ICT workforce training. GITC was created to support potential IT development in the regions. It trains highly-qualified individuals for world-class projects, helping to develop the information technology sector in Gyumri, introducing advanced learning methodologies, and creating jobs.
- The Vanadzor Technology Centre (VTC) was established by the Enterprise Incubator Foundation with the support of Government of Armenia and the World Bank. The goals of the Centre include development of technical and business skills, promotion of technological entrepreneurship, commercialization of innovative research undertakings, creation of new technology companies, attracting of foreign investment and others.

Source: Enterprise Incubator Foundation



Low labour productivity is not necessarily a disadvantage for efficiency-seeking investment, provided that good general education standards are maintained. FDI can supply the equipment, technology and management techniques to overcome productivity problems arising within the firm. There are opportunities for brownfield investment and, potentially, for high incremental rates of return to investment in modernisation. Examples include: vineyard yields per hectare have risen 80 per cent since 2003; UNIDO estimates that output per garment worker can increase 20 per cent by improved organization and training alone, i.e. quite apart from equipment modernisation.

Armenia is not yet endowed with a strong pool of professionally trained managers, but the diaspora is a resource to fill advanced skills gaps. Some universities are offering undergraduate business administration degrees, and the American University of Armenia offers an executive MBA programme. Many of today’s CEOs spent their formative years under a centrally-planned system, and the local business community freely acknowledges that many businesses are not managed to modern standards.⁸⁵ However, the level of university enrolment in the population at large, and the possibility to tap into the diaspora resource pool suggest that Armenia is unlikely to have any competitive disadvantage in this regard. There is no aggregate data on the number of returnees from the diaspora, but the in-country mission for this report encountered many examples of skilled diaspora recruited to work with foreign investors. In addition, Armenia’s regulation on foreign hire are flexible (see chapter I, section D).

2. Infrastructure and utilities

Energy and telecommunications are reliable, accessible and reasonably priced – but neither a competitive advantage nor disadvantage. *Electricity generation* is partially liberalised. Distribution is privately operated and new generation capacity is concessioned to private investment under government offtake agreements. There is competent execution of plans to meet future demand and it is likely that the distributor will in future be allowed to commission some of its own generation capacity. Electricity tariffs for industrial users are in the range of 5-8 cents/kWh, which is an acceptable range for investors and similar to costs elsewhere in the EAEU, except in Kyrgyzstan. *Telecommunications*, including broadband and internet services, are privately operated. International internet bandwidth per internet user is the best in the EAEU, apart from Belarus. Fixed broadband is adequate although noticeably lags service in the Russian Federation (table II.9). It is understood that there have been recent improvements in broadband provision which should improve competition. For example, VEON Armenia has begun to roll out a 100Mbps fixed-broadband service. Mobile broadband has expanded strongly with large investments in modernisation in the roll out of 4G. The Government is also planning the introduction of 5G. In 2017, investment in telecommunications services represented 3.4 per cent of gross fixed capital formation, much higher than in the Russian Federation (1.7 per cent).

Table II.9. Regional broadband service

| Fixed broadband | Armenia | Belarus | Kazakhstan | Kyrgyzstan | Russian Federation |
|------------------------|----------------|----------------|-------------------|-------------------|---------------------------|
| Monthly charge (\$) | 5.83 | 4.5 | 5.9 | 8.4 | 3.4 |
| Speed (Mbit/s) | 4 | 3 | 1 | 0.5 | 30 |

Source: International Telecommunications Union, 2017 and Government of Armenia
Notes: Measures of internet speed by Ookla, a company that specializes in internet speed testing worldwide indicate the following broadband speeds in Mbit/s for 2019: Armenia (24.05), Belarus (47.9), Kazakhstan (36.31), Kyrgyzstan (25.49) and Russian Federation (53.73). Available at: <http://worldpopulationreview.com/countries/internet-speeds-by-country/>, accessed on 9 October 2019.

Transport infrastructure and related services are a drag on Armenia's efficiency profile but they are not barriers to investment in several promising sectors. Due to its landlocked location and geopolitical obstacles, it is unsurprising that Armenia ranks 112th globally in road connectivity (but better on road density and condition). The low ranking perhaps understates its connectivity to its main market, the Russian Federation, and prospectively large trading partner, the Islamic Republic of Iran. Also, it is closer to the European market than many competing host countries for investment in certain sectors. These include agribusiness and textiles and garments. Armenian garment producers are only seven days away door-to-door from European customers compared with Asian competitors. From Bangladesh (a major garment exporter), it requires 27 days to ship a twenty-foot container to Rotterdam (UNCTAD, 2013). The services industries such as IT, contract R&D providers and tourism businesses are largely, but not entirely, immune from transport inefficiencies (see below). However, these are barriers to heavy industry, which depends on efficient turn-around of imported raw materials and components. For this reason too, Armenia will not find manufacturing niches in global value chains, especially those that function with just-in-time methods.

Air connections are inadequate for services businesses and tourism but are improvable. Direct air services from Russian Federation are adequate, but not so from Europe.⁸⁶ Continued economic growth and rising demand should eventually solve this. Meanwhile, it is reported that talks are underway to introduce one of the largest European low-cost carriers to Armenia. On the plus side, the Yerevan International Airport is modern, and passenger handling by airport staff and border officials are very efficient.

3. Support services and facilities

Professional services are well catered for. The big four accounting firms are represented in Armenia. Local firms also have staff with professional body qualifications gained overseas and are a competitive alternative to the big four firms in the SME and larger company markets. None of the major international law firms are present. However, many of the local practices have staff admitted to the bar in western jurisdictions. And, naturally as an international IT hub, local firms are well able to provide high-quality IT services to resident companies.

Quality facilities at competitive cost are available. Quality office space is readily available, especially in Yerevan. Rental costs are lower than for equivalent space in the Russian Federation and in Georgia. Factory and warehousing space is also readily available at costs which are lower than in neighbouring countries.⁸⁷

C. THE DIASPORA

The diaspora is Armenia's key competitive edge. There are an estimated 7.2 million Armenians living in 137 countries. The largest population is in the Russian Federation (2.6 million), followed by the United States (1.6 million) and France (700,000). The Middle East is well represented with sizable populations in the Islamic Republic of Iran (120,000) and Lebanon (140,000). So is Latin America, especially Argentina (128,000) and Brazil (100,000).⁸⁸ This diaspora is, in many ways, Armenia's key competitive edge, as discussed in the sections below.

Diaspora foreign direct investment – DFDI – is a major resource for Armenia. An analysis reported by the World Bank for 1994 to 2004 found that 69 per cent of foreign investors were diaspora related and 68 per cent of companies with FDI had diaspora ties.⁸⁹ It also showed that the Russian Federation (29 per cent), the United States (17 per cent) and the Islamic Republic of Iran (14 per cent) were the leading home countries of diaspora investors. Another analysis published in 2013 found only a limited relationship between the diaspora in source countries and their share in FDI in Armenia. It seems likely that the EU and the United States were under-represented, although the latter was especially important in connections between Silicon Valley and the rise of Armenia's ICT industry.

The importance of the diaspora has almost certainly broadened over time. More recent research on the role of DFDI is not available, but the sectoral distribution of FDI discussed in the context of this report points to its increased relevance. Argentina is notable, for example, in investment in the Yerevan airport and the *Tierras de Armenia* wine development. However, the Russian Federation probably still stands out for the size of its DFDI and the diaspora philanthropic contributions to business foundations, such as TUMO and FAST. Seven Russian-Armenians are in the Forbes Russia list for 2019 of the 200 wealthiest Russians, which is telling of the potential for further DFDI expansion (see sections below). It is fair to note that the strong presence of DFDI is not a result of pro-active targeting of potential investors among the diaspora. Also, some very notable contributions by the diaspora have been philanthropic rather than direct investment.

Armenia has almost unmatched ability to access talent and business connections in every field. A current list identifies 108 business leaders across 20 countries as belonging to the diaspora.⁹⁰ Probably only Israel matches Armenia in the ability of a small country to find such talent, wealth and business connections among its diaspora.

II. INVESTMENT TARGETS AND MEASURES

A. INTRODUCTION

The Government's mandate for this report is to advise on the prospects for export-creating and efficiency-seeking FDI, a key national goal. In 2011, the Government adopted an export-led industrial development strategy and later added innovation to this strategy. As discussed in the Context, this approach is also promoted in the current Government's programme, within an overall objective of achieving sustainable development and inclusive growth.

The approach of this report is to identify likely billion-dollar export industries and emerging billion-dollar candidates and to advise on achieving these targets. It includes services as well as industry. In each case, the report assesses business prospects and challenges, and investigates potential investment sources, including FDI.⁹¹ Finally, the report recommends policy measures to help achieve the targets. The targets are specified as:

- *Billion-dollar club* – industries already near \$1 billion in value of annual exports or which can achieve the target within 10 years, i.e. high technology, with special focus on artificial intelligence, data science and deep tech, tourism and textile and garments.
- *Emerging billion-dollar club* – industries which could achieve \$1/2 billion in value of annual exports in 10 years and strive for \$1 billion in 20 years. Targets are wine, agribusiness and pharmaceuticals.
- *Nascent candidates* – industries with potential but for which it is too early to set export targets. These are business process outsourcing, regional logistics and food safety, aircraft repair and maintenance, regional financial services and higher education.

Investment and exports are not an end in themselves. Export values have been chosen as readily identifiable “headline” targets but of course do not capture the economic and social contributions of investment. This report is also governed by the broader issues of promoting inclusive growth and sustainable development – in particular spreading benefits to the marzes (regions), employment creation and linkages with suppliers – as well to increasing domestic value added. Nevertheless, a small country that can achieve at least five billion-dollar export industries will, with supportive policies, be in the position to provide good living standards to its citizens.

FDI will have a useful but far from singular role. FDI is valuable when it can bring markets, capital, technology and modern management to local industry. FDI can help in the development of several of Armenia's small but emerging export industries. They are now growing but present a clear need for modernisation – in equipment, operating practices, management and export marketing. However, the core of business development remains the entrepreneurship and risk-taking of local business, whether large industrial groups or SMEs. This is especially true in that the Armenian export industry does not, with the exception of high-tech, have the scale, maturity or brand recognition to attract large foreign investors.



FDI should be sought in multiple streams. First, is the diaspora which is important enough to be considered a strategic resource and have its own nomenclature – DFDI. The second is the private equity stream – investments targeted on modernising existing businesses. The sources are private equity funds and the international financial institutions – the Asian Development Bank (ADB), the European Bank for Reconstruction and Development (EBRD) and the World Bank Group. Amber Capital is an example (box II.2). The third is international venture capital focussed on funding start-up businesses, especially in high-tech. Lastly, there is the traditional FDI – multinational enterprises that will expand their business operations across borders in search of efficiencies or markets. DFDI and private equity can fill a wide gap in Armenia between traditional FDI and local investment.

Box II.2. Private equity fills a gap

The UK-based global asset management firm Amber Capital is planning to launch Armenia's first SME-focused private equity fund with a target size of around \$50 million. The fund's anchor investors are the EU, the EBRD and the fund's managers.

The fund will seek investment opportunities of up to \$10 million in various strategic sectors for the country, including agriculture, energy, manufacturing and IT. The investment strategy will consist of accelerating the growth of the target companies to turn them from domestic to regional leaders while applying the highest standards of corporate governance, transparency and financial management.

The fund says it will be able to offer exposure to the fast-evolving Armenian economy to a wide range of institutional investors and capitalize on the long-term growth trend of regional integration.

The fund is expected to start operating in the second half of 2019.

Source: UNCTAD's interview with the company.



B. TARGETS

1. The billion-dollar club

Tourism

Tourism may be close to achieving \$1 billion in receipts despite Armenia’s low profile and poor air links with Europe. Armenia had 1.65 million international tourist visitor arrivals in 2018,⁹² up sharply from 558,000 a decade earlier. A 2016 survey found that about half of all arrivals (2.5 million) were visitors to friends and family, whilst 14.4 per cent were visitors for holiday and leisure.⁹³ This leads to an estimate of about 360,000 discretionary tourist arrivals. One source estimates that *travel and tourism* expenditure has reached over \$1.1 billion but this may relate to all visitor arrivals. Taking a broader view of “leisure spend” of all international visitors, this source estimates that receipts were \$962 million in 2017.⁹⁴ The EU and the Russian Federation each supplied one-quarter of the overall visitors, the Islamic Republic of Iran 17 per cent and the United States 10 per cent. However, the Islamic Republic of Iran appears to be the top source of discretionary tourists (14 per cent of arrivals), followed by the United States (7 per cent).⁹⁵ Only a third of overall visitors arrived by air – confirmation perhaps of poor air links with Western Europe.

A mix of DFDI and local investment has greatly improved hotels and restaurants in Yerevan. Yerevan boasts at least eight 4-star and higher category of hotels. Major chains, such as Accor and Intercontinental are represented, although not in their luxury segments. Other chains include Marriott & Alexander, Hilton, Radisson, Best Western and Wyndham. One estimate puts the stock of FDI in the sector at \$500 million, although this may be the built value of internationally-branded hotels, which typically operate franchise systems for local owners/developers.

Mass tourism organized by large tour operators is not an option as the next leg of development. Armenia will not be a destination for large tour operators/investors, as it does not offer beaches and year-round warm climate. Moreover, the built hotel offer is 4 to 4+ stars, which prices Armenia out of much of the mass market. The tourism offer will be more selective for individual and small group visits in areas of cultural and religious interest (including splendid ancient churches), mountain scenery, hiking, wine trails and skiing. Nevertheless, tourist arrivals are expected to grow strongly for these niche markets.

Spreading tourism benefits to the regions will be the key next stage of development. More investment will be needed in lodging and attractions outside Yerevan. There appears to be substantial capacity in the Yerevan hotel and restaurant industry to accommodate more arrivals, most of whom will base their stay in Yerevan and undertake side trips to attractions. For example, a survey by the UNDP has identified cluster potentials in three marzes – an eco-corridor, a tourism hotspot and agro-market and a wine/gastro destination (UNDP, 2019). However more regionally-located hotels and guesthouses of acceptable standard are needed to anchor visits to the regions. To supplement private investment in regional hotels, there are plans to encourage communities to renovate abandoned buildings to guest house standards and lease them to private operators on a profit share basis.

New policy measures can help to grow and spread the benefits of tourism. Policy measures are needed to support growth and regional development. In particular:



- a. Armenia should follow the lead of many other countries and levy a tourism tax to fund priority needs of the sector. These taxes are usually levied as a set amount per room night (e.g. €2.5 per night in Barcelona, €3.13 per night in larger cities and resort towns in Slovenia, and €1.57 in hostels or camps) or as a percentage of the hotel bill (e.g. 4 per cent in Budapest, Bulgaria, 5 per cent in some cities in Germany, 1 per cent in Romania). The tax rate can vary by standard of establishment and by city or region. In Armenia's case, a modest tax (e.g. \$2) could be levied on hotels in Yerevan only and used to fund two outcomes – regional attractions with municipality involvement and tourism promotion on a co-funding basis with the industry.
- b. Armenia is not well-promoted and its attractions are significantly under-appreciated by the market. Most promotion seems to be left to the industry, which finds it expensive to exhibit at marketing fairs. A double-tax deduction for marketing expenses could also be considered.
- c. Improved air links are essential for growth. It is reported that the Government talks with Europe's largest budget operator to begin flights. It is understood that the Government is unwilling to accede to the airline's request to waive the \$20 departure tax. This may be a false economy compared with the benefits for tourism (and business) of more flights and calls for cost-benefit analysis.
- d. Since Armenia's offer is not low-end tourism, it must keep facilities in excellent condition. Most 4+ star hotels are in good condition because they were recently constructed. The industry should be encouraged to not let standards drop. Tax policy can also assist achieve this objective. Currently, hotels are allowed a 10-years depreciation term, which is double the standard rate for buildings and construction; 8-year terms are set for "other assets" which presumably includes fittings. The latter rates should be increased for hotels, given their high wear and tear so as to encourage regular upgrades. Mauritius, which has a high-end tourist industry, allows 25 per cent depreciation (four years) as it is the policy of many hotels to completely refurbish rooms every four years to keep them to a high standard. A depreciation policy to encourage refurbishment every five or six years should be considered for Armenia.

Most investment is likely to come from DFDI and local business groups, although similar opportunities do attract niche foreign investors and regional chains. Current tax measures appear not to be a disincentive to hotel investment. The proposal elsewhere in this report to permit grouping for tax purposes would lend further support to investment in this industry. There are opportunities for more aggressive incentives for hotel development, which other countries more dependent on tourism have adopted. But it would be more in keeping with Government objectives to target a next round of incentives and investor targeting to tourism investment outside Yerevan. This approach would complete the proposed room levy, which could be devoted partially to regional tourist improvements. In this regard, it is also recommended that:

- e. The Government should draw up a list of anchor regional tourism investments – hotels, lodges, restaurants and major visitor attractions, such as ski fields. Investment in anchor projects should attract full 100 per cent depreciation in the first year. This will help investor cash flow and debt service, and provide attractive group relief whilst deferring rather than removing tax revenues to Government.

High technology – from ICT and engineering to AI, data science and deep tech

The high-tech sector is booming. A comprehensive report by the Enterprise Incubator Foundation (EIF) found about 800 ICT companies in active operation (including internet service providers), generating a



turnover of \$922 million, up 20.5 per cent from 2017. Most of these companies (95 per cent) were started since 2000, of which 150 were started in the 2018 alone.⁹⁶ Software and services companies accounted for \$730 million of industry turnover in 2018, of which about \$393 million was exports. Industry employment is around 16,000. The industry is growing at 20 per cent a year, and should comfortably reach the billion-dollar export mark (EIF, 2018). Currently, the main business areas in Armenia in this sector are customised software, web design and development, IT services and consulting, mobile app development and system design and atomisation. Other business lines are chip design and testing, computer graphics and multimedia and games. Looking to the future, Armenia aims to deepen the sector and become a leading hub for innovation, data science and artificial intelligence (AI).

There is a notable foreign investor presence. About 30 per cent of Armenia's ICT companies are foreign-owned. Half of these are United States-owned and there is significant presence from European (23 per cent) and Russian investors (17 per cent). The EIF notes that foreign investment typically began as small development outposts. It grew as confidence in Armenia's capability increased to encompass R&D, design, coding and testing and in some cases also marketing and customer support. FDI includes global leaders in the field (box II.3).

Box II.3. **Leading global ICT/engineering companies in Armenia**

Synopsis, a private company from the United States, is a global leader in electronic design automation. The Yerevan office, its largest outside the United States, employs 450 engineers. The Armenian company grew from an acquisition in 2004. Among other things, the Yerevan office is involved in the design and testing of computer chips.

National Instruments, another company from the United States, has designated its Yerevan operation as the regional office for Europe, the Middle East and Africa. It deals with systems engineering covering the automotive, telecommunications and semi-conductor fields amongst other industries. It has grown from a three-person operation in 2005 to now employing 70 staff.

ISB, a Canadian manufacturer of electronic safety and automation products, has announced plans to open its first overseas R&D centre in Armenia.

Mentor Graphics, a subsidiary of the German company Siemens since 2017, works in integrated circuits and embedded software. It entered Armenia in 2018 through a group acquisition of a company with an office in Yerevan.

VMWare of the United States provides high-tech operations management tools. It established in Armenia in 2010 through a group acquisition. In 2018, it is reported to have added 40 engineers and researchers to its local staff.

Cisco, the United States chip and circuit maker, opened an office in Armenia in 2014.

Oracle, the United States software company, acquired LiveLook a cloud computing specialist and decided to maintain the Yerevan office for R&D. It has announced plans to expand into a 200-300 staff R&D centre.

Source: EIF and investor interviews.

Local start-ups have flourished, supported by Government initiatives and international venture capital, and *deep tech* is expected to complete Armenia's growing position in contract R&D. Some are purely local start-ups, including spin-offs from the foreign-owned R&D centres, others are founded by returning diaspora with Silicon Valley exposure, and some have both elements. Box II.4 gives a sample of some of the better-known ventures and illustrates the variety of technologies being developed. The sector



receives Government support and a Law on State Support to the Information Technologies Sector was adopted in May 2019, including tax privileges for newly established and start-up entities (see chapter I, section C). A leading industry insider believes that the brightest future for Armenia's young industry will be in games and data analytics.⁹⁷ A taste of potential is given by the work of the futuristic FAST, which aims at producing an ecosystem for science and technology advancement in data science, artificial intelligence, robotics, advanced materials and biotechnology, all exponents of “deep tech”, i.e. technology based on tangible engineering innovation or scientific advances and discoveries.⁹⁸ FAST aims to bring Armenia into the top 10 most innovative countries in the world, and top five in data science and artificial intelligence (AI), by 2041 (FAST, 2019a). It proposes a boost in national R&D spending (currently lagging at only 0.2 per cent of GDP) and a number of initiatives. These include a training programme on science, technology, engineering and mathematics (STEM), research grants and incubators to begin the commercialisation process. One aspect will be the creation of AI and data analytics centres in foreign companies based in Armenia (with three targeted for 2020). Fast is also working on the establishment of an Innovation District in Yerevan, which will be anchored by an Adaptive Innovation Campus (box II.5). A presidential initiative in this area was also recently launched. Called “Advanced Tomorrow” (ATOM), it will consist of several components, including a city of science and technologies, hosting major international organizations, research centres and universities as well as the “Museum of Tomorrow”.

Box II.4. Armenia ICT start-ups

Pride of place belongs to PicsArt a photo editing and sharing app which was started in 2012 in the United States by the ex-CEO of a German company. It has based most of its operations in Armenia. Development was supported by major United States venture capital firms Sequoia and Insight Venture Partners. It has just passed 500 million downloads, and is on course to be Armenia's first unicorn when it goes to IPO.

The digital publishing platform Joomag is Armenia based. It enables self-publishers to publish and sell their work. It is also a re-seller in digital form of mainstream print publications.

An online tool for learning programming code learning, SoloLearn, recently received a \$5.6 million development injection from Naspers Ventures. It won Facebook's start up App of the year in 2017.

Triada Studio in Yerevan developed the award winning Shadowmatic puzzle app.

2Hz has attracted funding from the United States for noise reduction technology in online communication using neural network technology.

Lionsharp is start up creator of Voiceboard for gesture and voice-controlled presentations.

Triple-E is an augmented reality start-up which has received Dutch venture capital support.

A start-up developing an online HR tool Teamable has received \$5 million in United States venture capital backing.

Source: EIF interview and thenextweb.com/asia/2017/03/17/armenias-rising-tech-scene-ne (accessed on 01 August 2019).

R&D up to prototype stage and “sandbox” interventions are Armenia's niche in industrial global value chains. A recent analysis concludes that Armenia's participation in global value chains is limited (World Bank, 2017). This is true if the focus is on the processing part of value chains. Armenia's logistics issues mean that it is unlikely to be able to import heavy raw materials and components for competitive processing and re-export. But this is looking in the wrong place. A significant part of manufacturing value added is in



services, and Armenia is well positioned in this respect. It offers skilled professionals at competitive cost with multilingual ability (supplemented, if necessary, by returning diaspora). It is able to expand its contract R&D up to the point of producing prototypes (which do not present logistics problems). It can also offer “sandbox” solutions which involve testing software and prototypes in isolated conditions before integration. An engineering cluster is emerging, capped by the construction of the high-tech Engineering City on the outskirts of Yerevan, which will augment this capability. The Engineering City is an innovative ecosystem where the engineering and high-tech companies develop and implement innovative ideas based on modern infrastructures. The Project envisages the establishment of several units, including a business acceleration working area, an engineering centre, laboratories, workshop studios and small-scale sample production workshop factories. Technological companies will also be allocated land in the City. In this environment, the UNCTAD mission saw a team developing prototype optical systems for autonomous driving vehicles. With supporting policies, Armenia can credibly aim at becoming a world leader in AI and data sciences.

Box II.5. Armenia's Innovation District and Adaptive Innovation Campus

A flagship initiative by FAST and the Government of Armenia is the establishment of an Innovation District. The District aims to offer globally competitive education, research and innovation infrastructure to induce knowledge generation and commercialization in STEM. It is planned as a 60-hectare area in Yerevan where the boundaries of innovation are tested through experimentation labs, acceleration and incubation spaces, a data centre, business centres, advanced prototyping centres, smart solutions, a living lab environment and more. Much of the innovation created, explored and tested within the district is powered by a regulatory sandbox that serves as a test ground for government regulations and policies on disruptive technologies, which can later be scaled through the country and the world.

The first phase of the project is Adaptive Innovation Campus, Business Park, and Data Centre. The Campus is a 20,000 square metre facility, aiming to catalyze and boost regional innovation. Its main objective is to cultivate a science- and tech-driven innovation ecosystem that hosts and fosters the full life-cycle of innovation from revolutionary science discoveries to global commercial successes. The Campus aims to be a collaboration hub where inventors, scientists, students, entrepreneurs, business professionals and investors come together to generate new ideas for disruptive innovation, test them in advanced lab infrastructure, and create commercializable products and solutions.

The Adaptive Innovation Campus will consist of five main structural areas: experimentation, incubation, acceleration, customer experience, and recreational areas. Its objectives include:

- Enhancing the education system by partnering with university programmes and building new components within curriculum to fill in current gaps;
- Facilitating applied research in four fields of science through competency centres and experimentation labs;
- Fostering the commercialization of science by turning innovative ideas into science- and tech-driven companies;
- Catalyzing the development of science-focused ventures; and
- Showcasing the latest developments in science, technology and innovation through a unique smart environment.

Source: FAST.

A comprehensive strategy for positioning Armenia as a leading world centre in AI, data science and deep tech is needed. A global race to become the world leader in artificial intelligence has started. Since 2017, close to 30 developed as well as developing countries, and also regional groupings, such as the European Union and the Nordic-Baltic Region, have developed AI strategies. Their focus vary, and strategies deal with different aspects of AI policy: scientific research, talent development, skills and



education, public and private sector adoption, ethics and inclusion, standards and regulations as well as data and digital infrastructure (Dutton, 2018). They all aim, however, to promote the use and development of AI. While several initiatives are in place in Armenia as well, as discussed above, no comprehensive AI development strategy has yet been formulated by the authorities. Based on the review of recent strategies and initiatives across the globe and building on the policy work already undertaken in the context of FAST, it is recommended that the Armenia adopts an AI development strategy based on the three pillars: the enabling framework, the clustering dimension and the promotion dimension.

Enabling framework

Regulations are key to support and promote the development of science, technology and innovation, including frontier technologies such as AI, data science and other deep tech. They are also key to ensure that the use and development of such technologies is transparent, explainable and non-discriminatory. In this regard, it is recommended that the authorities:

- a. **Carefully evolve corporate and securities law to address practices in the high-tech sector.** The sector has raised concerns that:
 1. The Law on Joint Stock companies does not permit common stock to be issued in more than one class with varying voting, dividend and other rights. In particular, this prevents founders from retaining enhanced voting rights after public capital raisings – a practice in this sector abroad. Certainly Armenian law should enable different classes of shares to be issued. But care should be taken with this liberalization, as the general framework and practices of good governance in Armenia still need strengthening e.g. in relation to protection of minority shareholder rights (see chapter I, section B).
 2. Securities regulation does not properly address funding instruments popular in high-tech, such as convertible notes and simple agreements for future equity (SAFE). Armenian practice should evolve to cover these forms of financing but, again, with care. Armenia does not have a sophisticated investor population and maintaining investor protections and the reputation of the financial system are paramount.
- b. **Develop a “regulatory sandbox” regime for non-financial services.** Often new technologies, including prototypes, have to move out of the laboratory and be tested in real life conditions. The sandbox approach enables this testing in conditions which control the risks to health and safety and the environment.⁹⁹ Obvious examples are driverless cars and drones, and several countries have created regulatory sandboxes. FAST is leading discussion of this issue (FAST, 2019b). No overarching legislation is needed in Armenia. Rather the Ministry of Economy should be appointed as the regulatory sandbox gatekeeper, and applications to apply for sandbox approval should go to the Ministry. Its role would be to identify and bring together the affected regulatory ministries and agencies. Together they would design the rules and monitor the testing, and recommend changes to the relevant legislation or regulation if required. For example, the ministry in charge of transport would develop the regulatory sandbox for driverless vehicles. Further to extensive research carried out by the Central Bank of Armenia, the application of the sandbox regime to financial services would appear premature for the country at this stage.
- c. **Address the modernization of the IP regime.** As discussed in chapter I (section G), removing legal restriction to scientific research and facilitating university patenting are among the key reforms that

would promote more effective university-industry collaboration on R&D. This would be crucial for deepening the high-tech sector into AI, data science and other frontier activities. In particular, the patent protection exemption contained in Law on Inventions of 2018 should be broadened to include “experimental use”. In addition, the Law on State Non-Commercial Organizations should be revised to promote the commercialization of IP rights through the creation of spin-off companies from universities or research institutes. Finally, the Government should consider supporting foreign patent registration by Armenian companies, which is a must for high-tech industries that wish to export to advanced industrialized countries in Europe, Japan or the United States.

- d. **Retain fiscal competitiveness in the area.** No additional tax incentives are necessary to spur investment, but existing ones should be retained and better communicated. The sector already benefits from tax incentives at corporate and personal level (see chapter I). These include a little known tax incentive on R&D expenditure, which few in the industry appear aware of. It has been proposed that tax on employees working outside Yerevan be further reduced to a regional spread of investment. The objective is worthy, but it would be unfair for high-paid ICT workers to be paying even less tax than lower-paid workers in other occupations in the regions.
- e. **Adopt data protection and AI ethics frameworks.** Finding the right balance between policy support and regulation will be paramount to the development and impact of high-tech sectors. AI and data science are data-centric businesses, in which personal data is a core resource. This raises a number of regulatory concerns, in particular data privacy and protection issues. Also, the business models of digital platforms tend to accentuate market concentration, and to raise the barriers to entry for new competitors. Furthermore, with digital firms, for which intangible (and therefore highly movable) assets play a key role, finding adequate taxation formula is key. Each of these issues poses significant regulatory challenges, and balancing support to the development of these frontier sectors with the imperative to address the related policy challenges will determine Armenia’s success in making the sector a contributor to its sustainable development. The EU’s work in these areas is advanced and can provide useful policy guidance for Armenia.¹⁰⁰ The Digital Economy Report also includes a detailed analysis and policy recommendations in each of these areas (UNCTAD, 2019b).

Clustering dimension

The development of advanced digital technologies, such as AI and big data, relies heavily on the establishment of innovation clusters. Securing the right skills, actors, policies, infrastructure and services is crucial, but it will not suffice unless the Armenian science and technology ecosystem also fosters the continuous interaction among these elements. The authorities have already adopted or planned several initiatives to promote domestic clustering, including the “Engineering City”, the “ATOM” initiative and the “Innovation District” presented above. The Armenian AI development strategy should complete these initiatives with measures aimed at further supporting clustering, with the diaspora and within the global innovation value chain. In this regard, it is recommended that the authorities:

- a. **Update educational programmes and strengthen university-industry collaboration.** Recent estimates show that there are only around 22,000 experts in the world who can create machine learning systems. This shows that the talent shortage in this area is real (Gagne, 2018). STEM education requires significant investment. This is not limited to higher levels of education, where data science and AI solutions should integrate the curricula at undergraduate and master’s levels. It extends to primary and middle schools, where students should be introduced to coding and statistics.



In addition, a partnership approach between the public and private sector in the design and delivery of work-based learning and training systems should be adopted. As mentioned above, university-industry collaboration should also be strengthened (see recommendation I.G.1).

- b. **Increase R&D funding and government support.** The Government can also play a more direct role in the sector's development by increasing R&D spending. Several options exist. Beyond the establishment of AI hubs and incubators, which is common to most countries which have adopted an AI strategy and is well underway in Armenia as well, the authorities could follow international policy experience. This includes direct funding of AI research and training initiatives (e.g. China or India), the active recruitment of global AI talents (e.g. China, Germany, Sweden or Taiwan), the adoption of large-scale projects in national defence, medicine or public safety (e.g. the Republic of Korea, Singapore) or the integration of AI into government services (e.g. Germany or Italy).
- c. **Establish an Armenian “Diaspora innovation network”.** The diaspora can become a formidable asset not only in financing science and technology-intensive startup projects at the seed stage through an “Angel network”, but also in complementing the domestic skills' base via the attraction of international talent. Indeed, FAST estimates that the Armenian scientists in the diaspora are roughly equal in number (based on the estimate of 3,000 to 3,700) to Armenian science community within the country. In 2018, the Ministry of Diaspora of the Republic of Armenia, in cooperation with FAST, initiated and organized a Diaspora youth startup programme called “Neruzh” for young entrepreneurs of Armenian descent who wish to bring their startup ideas and projects to Armenia. In 2019 the Ministry of Diaspora of the Republic of Armenia transferred the programme's responsibility to the Ministry of High-Tech Industry. Pro-active engagement of the diaspora should continue, and should be supported by the establishment of a customer relationship management system, as discussed in section C. The provision of research funding and state-of-the-art infrastructure facilities should also be employed as part of the diaspora skills' attraction package.
- d. **Set up a Strategic Council for AI Technology.** The Ministry of High-Tech Industry has initiated many collaborative programmes to establish and promote AI and Cybersecurity ecosystems in Armenia. Following the example of Japan, Armenia could also set up an advisory council under which representatives from academia, industry and government could come together and pursue cooperation in research and development. The Council would assist in the development and finalization of the AI strategy, and also in the development of sector-specific guidelines on privacy, security and ethics, as discussed above. The Strategic Council could be assisted by an international advisory board, including international experts.

Promotion dimension

Establishing Armenia as a worldwide hub for AI and related activities will also require professional branding and promotion. In this area, Armenia has employed tangible efforts. One of the key outcomes is the hosting of the World Congress on Information Technology in Yerevan in October 2019. It attracted the world's leading academics, technologists and entrepreneurs, and included sessions on topics ranging from artificial intelligence, virtual reality and smart cities to cybersecurity, climate change, and more.¹⁰¹ Another initiative of the Ministry of High-Tech Industry is the “Virtual Bridge”, which aims to make Armenia a “regional Silicon Valley” by connecting virtually the Armenian ICT/engineering companies to the international market and the world's leading companies. FAST organizes an annual event called “The Global Innovation Forum”. In 2019, the event is focussed on “Transforming Intelligence”, and is set to explore the impact of AI on science and



society from the scientific, technological, and industrial perspectives. As discussed in details in section C, below, beyond punctual initiatives however, Armenia is currently under-promoted, and its future investment promotion setting is still taking shape. In this respect, as for each target industry, it is recommended that a Principal be appointed for AI and related sectors as the authorised government official within the new investment promotion setup to lead and coordinate investment promotion. The details of this proposal are discussed in section C.

Textiles and garments – a revival

After independence, Armenia’s huge textile and garment industry nearly collapsed. Armenia was a major supplier within the Soviet Union and employed 150,000 workers in the industry (perhaps as much as 20–25 per cent of national employment). The industry suffered a steep collapse, and regions were especially hard hit as the assured market disappeared. By 2012, only around 2,500 were employed in the industry. Some operations survived as privatised firms, but many factories were abandoned.

The industry is undergoing a revival from a low point. Industry employment has risen to nearly 4,700 – the single major source of which is the Darbbag’s sewing factory (widely known as Gloria) in the northern municipality of Vanadzor, which employs 2,500 in a cut-make-trim (CMT) operation. The value of exports has risen very quickly in recent years with the Russian Federation as the major destination (table II.10). Exports to Europe include coats, raincoats and jackets to well-known brands such as Moncler, Armani and Valentino.

Table II.10. **Armenian textiles and garments exports** (Millions of dollars)

| | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 |
|--------------------|------|------|------|------|------|-------|-------|
| Total | 18.4 | 38.1 | 49.8 | 68.1 | 91.4 | 123.4 | 211.2 |
| Russian Federation | 0.8 | 1.3 | 0.9 | 27.5 | 43.2 | 70.9 | 132.5 |

Source: UN Comtrade.

The export revival is healthy, but is based on piecemeal investment and achieves low value added. About one-half of the industry is CMT, based on fabrics and accessories supplied by customers. Most of the other half is “own production”, relying on fabrics and accessories imported by the producer. The remainder is production of towels, bathrobes, socks and gloves. The domestic value-added in CMT operations is low – around 20 per cent of the export value. Moreover, for FDI, CMT is possibly the most efficiency-seeking investment of all – it is exceptionally footloose in response to changes in labour cost and/or trade preferences, as seen in the relentless migration of CMT across Asian countries.

Development of exports by the Armenian textiles and garment industry has to fit into the international structure of the industry. Clothing is sold in brands – whether fashion labels, sports brands or store ranges. The manufacture of the vast majority of branded clothing is outsourced internationally. Outsourcing is dominated by large Chinese and South Korean companies, which locate parts of the value chain in the lowest cost countries, often on a sub-contract basis. They can shift CMT production swiftly and also respond to trade preferences in major markets.¹⁰² There are exceptions to outsourcing, mainly in high fashion and fast fashion. High fashion labels need to show manufacture in country of origin (e.g. Gucci – “Made in Italy”). Fast fashion is manufactured close to market to achieve rapid turnover of products.

The best example is the ultra-fast Zara label, which is made mostly at home by its Spanish owner Inditex or otherwise very close to market. However, even in outsourced products, lead time to market is important to many fashion brands. Thus, along with cost of production, lead time is an important determinant of where investment will be made.

Armenia has several competitive advantages. First, it is closer than Asian suppliers to European and Russian markets. For example, the Gloria factory can truck finished garments door-to-door to Western Europe in seven days. Secondly, it has lower wage rates than in China and Eastern Europe, much lower than in Turkey (a major producer) and among the lowest in the EAEU, as reported in a comprehensive recent report on the sector (ADB and UNIDO, 2018). Thirdly, it has a reputation for ethical treatment of the workforce, which is an increasingly important factor in Western consumer choice.¹⁰³ Finally, it offers competitive energy costs.

There are competitive disadvantages too, but these are operational, reflecting the current state of the industry...The ADB and UNIDO above compared Armenia with potential competitors from Bulgaria, China, Romania, Serbia, Turkey and Uzbekistan in 2017. It found that, when productivity is considered, Armenia's labour cost advantage narrows to only Turkey and Romania for simple CMT, and disappears entirely in more complex CMT operations. Low labour productivity is attributed to lack of training and aging machinery (averaging over 10 years), among other issues. A further disadvantage for "own production" operations is cost against lead time in sourcing fabric. Make up and transport of fabric from Turkey takes 35 days; fabric from China is cheaper but the total lead time is 75 days. This is a serious disadvantage in large swathes of the industry, which require fast turn-around.

...and can be addressed with modern investment and good management. There is an immediate opportunity for investment in CMT operations to turn Armenia's wage rate advantage into a decisive regional labour cost advantage. Modern equipment, better training and conditions and more advanced operating practices could all be brought alongside better market research and marketing skills. This investment is unlikely to come from the major Asian contractors or their subcontractors. They would have probably found their way to Armenia already if an overwhelming combination of preferences and low labour cost were available. It is more likely to come from private equity sources of FDI. Current CMT offers turnaround opportunities on which private equity thrives.

Long-term sustainability requires investment in full-package manufacturing. A general conclusion of this report is that Armenian manufacturing will not be competitive if it needs to import significant raw materials and/or components for re-processing. Logistics time and costs preclude Armenia from the manufacturing side of global value chains. In the apparel industry, Armenia's future in sustainable outsourcing is "full-package" manufacturing. This means having an industry able to manufacture and dye fabric from stocks of yarn, produce accessories such as zips and buttons and thence make the finished garment. The best producers can go from design sketches and fabric approval to finished garment delivered to the customer in six weeks. Armenia has cost and location advantages for the European brands and should be able to attract FDI to provide capital, technology and the essential customer relationships. There is evidence that this is happening in partnership with the local industry. Alex Textile (box II.6) is an example and other industrial groups could follow suit. The long term is therefore to move from contract production to the creation of Armenia's own brands. This would give full control within Armenia to investment decisions and increase value added. A programme is underway with UNIDO assistance and Russian aid. Working with the Burgo fashion school of Milan, it has created and exhibited six collections of women's wear under



the “5900BC” tag. A first step is to assist Russian chains to fill out their own-label fashion lines by using samples from Armenia. These chains have a large share of the market. It would be a logical next step to establish Armenian brands in these outlets. Participation in fashion brand creation could be potentially attractive for DFDI.

Box II.6. Alex Textile

Alex Textile is owned by a local businessperson. It was established in 2014 and currently has 1,000 employees in a cut-make-trim operation producing baby clothes and underwear. It also produces FALKE-like quality upmarket socks in a well-equipped operation with 100 employees. A further 100 employees produce high-class sweaters in a joint venture with French FDI.

The company is investing in a fabric-to-finished garment (“full-package”) factory for leading European brands, such as Zara and Jennifer. It expects to employ 3,000 people. This venture will be a joint venture with ASA Garments of China. For the Chinese investor, this will dramatically reduce lead times in supplying European customers.

Alex Textile also formed a joint venture with a Lebanese investor to produce home and bathroom textiles with production to start in 2019. An acrylic yarn facility with Lebanese and Syrian investors is expected to begin production in 2020.

The total planned investment is around \$100 million, and the company expects that 90 per cent of all output will be exported.

Source: UNCTAD interviews with the company.

The outcome should be a more sustainable industry, and one that is generating greater domestic value added. Partnerships with local producers are the most likely debut point for independent foreign investors. Achieving this will require a number of policy actions:

- a. Adopt concerted and targeted investment promotion to introduce new full-package foreign investors (see section II.C).
- b. Consider supporting the acquisition of key assets. There is no strong case for broad-based incentives to accelerate investment given Armenia’s moderate rates of corporate taxation. Group taxation relief, as recommended in chapter I, would be a key factor in attracting investment from established local industrial groups. Any additional incentives for this industry should be precisely targeted. For example, it might be appropriate to allow faster depreciation on the acquisition of key assets needed to deepen and sustain the industry – in particular on fabric and accessories manufacturing machinery.
- c. Provide more direct support for the design segment to create Armenian design expertise and brands. Measures taken by governments elsewhere include creation of a school of design, prizes awarded at exhibitions (in the form of cash and paid mentoring) to help commercialisation as well as access to general SME support programmes.
- d. Support sponsored visits by diaspora with industry experience to provide guidance on branding, promotion and other aspects of commercialisation.

Such measures would build on UNIDO project, which has made a good start in this area. The Government should draw up a fashion design plan encapsulating such initiatives.



2. The emerging billion-dollar club

Wine – the renaissance of ‘old world’ wines

DFDI has led a renaissance of the industry. Armenia lays claim to be the world's oldest wine producer – from 6100 BC. But unfortunately, it left the Soviet Union with outdated techniques and poor-quality grape production. The subsequent land privatisations created a plethora of small vineyards of one to two hectares, without the capital or technology to improve quality and productivity. The area of working vineyards plunged after independence from 21,000 hectares in 1991 to 13,000 hectares in 2003. In 2006 a newcomer, *Tierras de Armenia*, began a \$30 million development of 400 hectares to produce higher quality wines under the *Karas* label. *Tierras de Armenia* is an investment by an Armenian-Argentinian and a classic example of committed diaspora investment. It deployed modern viticulture techniques and an experienced winemaker. Output from its existing plantings will double over the next three years. The company owns a further 1,900 hectares, and is currently pausing further development to assess the take-up of its current production on the market.

A mix of further DFDI and domestic investment has created new wineries, quality brands and rising productivity in the vineyards. Armenia has currently 52 wineries, up from 27 in 2013; 10 are modern units established in the last decade, and three or four of these wineries are regarded as producing wines of exceptional quality. Quality has risen and also productivity, with national average yields per hectare rising by about one-third over the last decade. By 2017, the area planted had almost recovered to 18,000 hectares. Importantly, modern techniques have increased yields, and total output is estimated to have risen from four million litres in 2003 to 10 million litres in 2017, of which an estimated 50 per cent is exported (compared with 25 per cent a decade ago).¹⁰⁴ Total wine exports, in 2018, were \$9.4 million, still small, but up from \$4.2 million in 2015.¹⁰⁵

A major opportunity is to promote *Areni Noir* red wines as the flagship of the industry. The rise to international recognition of the Malbec variety in Argentina and Sauvignon Blanc variety from the Marlborough region of New Zealand show what can be achieved even with “new world” wines from regions remote from the major consumer markets.¹⁰⁶ The *Areni Noir* grape is native to the Vayots Dzor region to the south of Yerevan, where approximately 1,500 hectares are planted/available. A further 3,500 hectares in other regions could be suitable for the *Areni* variety. White wines are also showing promise.

The industry has competitive advantages. The ability to promote exciting indigenous varieties – especially *Areni Noir* as highlighted – is the key competitive advantage. The other competitive advantages are moderate land and labour costs, excellent terroir with good limestone and volcanic soils in the growing areas and favourable climate. Land is available even in the prime Vayots Dzor region for \$10,000 per hectare and for as little as \$2-4,000 per hectare in other regions. Labour costs for development and cultivation are comparable to Georgia and the Republic of Moldova – major competitor suppliers to the Russian Federation – and significantly lower than in new world producers such as Chile, Argentina and South Africa. However, supplies are mostly imported – bottles, corks, fertilizer and pesticides – which partly offsets the land and labour cost advantages. Overall, a good margin can be earned.

The industry should target \$500 million of wine exports in 10–15 years and a billion dollars in 20–30 years. New investment in grape production of \$750 million and great attention to marketing are required to achieve the billion-dollar target.¹⁰⁷ Importantly, 30,000 hectares of low yielding land would be



converted to more productive use. Policy reforms and new measures in collaboration with the industry will be essential to achieve these targets.

Policy measures to incentivise *aficionado* investors will be needed together with support to increase yields and quality of small growers. It is highly unlikely that the global drinks companies will be early stage FDI. They barely featured in the emergence of new world wines and were only late stage acquirers of established brands.¹⁰⁸ Pernod Ricard, the owner of Armenia's Ararat brandy, has no plans to branch out into winemaking.¹⁰⁹ Judging by the new world wines' experience investors are more likely to be conversions to wine by farm owners and wealthy wine *aficionados*. Among the latter, there are especially likely to be resident high-income earners and the diaspora who have ready capital to deploy. In many cases, individual investors will need to be networked in order to create efficient scale properties. Limited Partnership structures will be required (and are permitted in Armenian law). Tax measures which cater to these investor profiles are needed to greatly accelerate investment.¹¹⁰

The current tax system is not well suited to modern agribusiness, including wine production, either to maximising investment or smallholder yields in the industry. Currently, Government expenditure of agricultural extension services is very low – less than \$1 million per annum or about \$3 per holding for all small farmers of grapes and other products. At present, farm production is exempt from personal and corporate tax. However, agricultural processing is taxable, and any integrated operation of production and processing is fully taxable. The farming exemption possibly reflects the historic situation of low farm incomes from the hundreds of thousands of very small holdings created by privatisation. Yet, modern large holdings are also exempt, and when they have processing operations there is an artificial incentive to split the operations for tax purposes. Worse, it does not recognise good practice for processors, such as winemakers, to control a significant part of produce supply in order to guarantee quality and availability. The move off an *ad valorem* excise tax is a good start in encouraging higher value wine production (see chapter I, section C).¹¹¹ Tax measures should also recognise the help which processors can give small producers to improve quality and yields. The following tax reforms for wine and agribusiness generally are recommended, in addition to the changes in general tax policy proposed in chapter I:

- a. Subject to cost-benefit analysis, the tax exemption for farm income should be abolished and no distinction made between farming and processing as income sources.¹¹² A small tax allowance can be introduced to protect farmers on very small holdings.
- b. To replace this reform and more directly incentivise investment, 150 per cent depreciation of capital investment should be introduced, and immediate expensing allowed in the year of investment.
- c. Given the length of time that grape and stone fruit plantings take to bear, a longer or indefinite loss-carry forward period should be allowed.
- d. A double deduction should be allowed for marketing expenses.
- e. Support given by packers and processors to small farmers should be expensed as a double deduction. Support could range from supply of improved planting materials to arranging export certification for fruit and vegetables (which can cost \$10,000 per grower according to interviews with investors).

Group tax relief is especially important in the wine industry. It can be a powerful incentive to be able to deduct the inevitable losses in the early investment from other income. This was an important accelerator of the New Zealand wine boom. Yet this option is denied to companies and an important incentive is lost. Group relief for all companies was recommended in chapter I.



A comprehensive promotion and quality assurance regime must also be put in place. There are promotional challenges if a huge expansion of wine production is to be absorbed at remunerative prices. Recommendations in this area include to:

- a. Introduce in law a small levy on wine exports to fund export market promotion by a recognised industry body.
- b. Establish quality and brand recognition in the Russian Federation above Moldovan and Georgian wines (whereas they are currently in a similar price bracket).¹¹³ The Russian Federation still takes 80 per cent of Armenia's exports.
- c. Lift sharply the profile of Armenian wine in other markets especially for *Areni Noir* and the other premiums.
- d. Provide quality assurance to protect the good name of the industry. One scandal can decimate the export market in the food industry. A joint public-private body should be established to certify the authenticity of all wine (and brandy) exports on a fee-for-service basis as a mandatory export requirement.¹¹⁴ The Australia's Wine Research Institute is a good example.

Agribusiness – target FDI in fruits and vegetables

Agribusiness exports fruit, vegetables and flowers in fresh and processed form. Exported vegetables include tomatoes, cucumber, bell peppers and mushrooms, and Armenia is a traditional exporter of stone fruits, such as apricots from extensive orchards. More recent and larger-scale investment has been on intensive cultivation of fruit and construction of modern greenhouses.¹¹⁵ There are said to be about around 340,000 very small farm holdings (between 1.2 and 1.4 hectares) created in the privatisations after the Soviet era (World Bank, 2018b). Reports have noted poor agricultural practices in small holdings, including inappropriate storage, application of fertilisers and pesticides, poor choices of planting materials among other things. The Government's goal of fostering inclusive growth requires continued attention to this sector because it is an income source for so many people. In the long run, there will inevitably be consolidation of small holdings and population decline in rural areas. But for now, raising productivity and market access of small farmers must go hand-in-hand with plans for investment in large and modern units.

Investment in modern production has grown rapidly and yielded marked productivity gains. The most recent study found that the area under greenhouses had expanded rapidly – from 510 hectares in 2011 to 1,220 hectares in 2016. Still, only 10 per cent of the area under greenhouses was covered by modern glass structures, and in general there is a gulf between practices in small and medium-sized greenhouses and those of large scale. There are remarkable productivity gains from high-tech greenhouses. One source estimates a three- to five-fold gain in output per hectare in vegetables and more than double in flowers (World Bank, 2016). It reports high rates of return on large high-tech greenhouse investment despite its cost. Modern greenhouses under glass with drip irrigation and gas-fired heating costs around \$1 million per hectare. The Government has supported the industry by deferring VAT on capital equipment and planting materials.

Most exports are to the Russian Federation and diversification is challenging. Nearly 90 per cent of \$80.4 million of exports in 2018 went to the Russian Federation. This level of dependence suggests a strong need to diversify. Some change is happening. For example, the fast growing Spayka transport group has branched out into agribusiness and a recent venture with ADB support includes exports of tomatoes



and bell peppers to the United Arab Emirates. Diversification will be challenging. Israel and Turkey are major exporters to Europe, and have respectively 8,000 and 35,000 hectares already under glass. Food safety and phytosanitary regulations are strict, and certification is beyond the means of small producers. Nevertheless, the regional market is substantial, and the European import market of \$35 billion is huge.

The potential for more productive use of private land is significant. Nearly a third of arable land in private hands is estimated to be unused or abandoned (World Bank, 2018b). The land sales market is underdeveloped, and foreign-owned companies can own land. In the past, they have been assisted by Business Armenia to identify plots. The Government is also considering a more joined-up approach by merging land administration and infrastructure functions (see chapter I, section B).

The potential benefits of introducing well-established foreign investors into the value chain as packers or processors is clear. Local investment will be insufficient for the opportunities and challenges. FDI is needed for the whole package of capital, expertise, established distribution channels and extension support to contract growers.

For fresh fruit and vegetable expansion, Israeli FDI could be an ideal fit. Apart from technology and market access, they have experience in managing contract growers (cooperatives in some cases). They could invest in central farm and processing facilities to full EU certification standards, and assist contracted growers to improve productivity and operate to export standards. This would help to address underfunded Government extension services.¹¹⁶ Several Israeli companies have extensive customer networks and distribution facilities in Europe, and are growers and/or have grower networks.¹¹⁷ Agrexco, which markets under the Carmel brand, is a buyer and distributor with an extensive international network. It works closely with growers to achieve quality and meet sanitary and food safety standards. The Mehadrin Group has 5,000 hectares under cultivation and exports throughout Europe. AdaFresh is an exporter with a logistics centre in the Netherlands. It is not averse to investing overseas as it announced plans in 2017 to acquire 94 hectares in Kenya to produce basil for the European market. Arava Export Growers is a cooperative which has formed a company to export and now includes 50 per cent private investment. It has distribution subsidiaries in the United States and in the Netherlands and a sales office in the United Kingdom.

The prospects for FDI in processed fruits and vegetables are much less apparent. Processed foods – sold in cans, bottles, jars, bags – are either branded or private label (sold as own brands by supermarkets). The branded space is dominated by the major food companies such as Unilever, Nestle and Kraft-Heinz, which invest in established brands with large markets or sometimes fast-growing cult brands. Armenia does not offer the brands or scale to attract these companies, given both the small domestic market and its hitherto limited penetration of the Russian market. At a secondary scale, there is a raft of branded producers. But very often, especially in Europe, their brands (e.g. tomato paste) have been carefully nurtured over decades, and are rooted in individual products in specific regions of their home countries. The production for these brands would not travel outside these countries or regions. Armenia would need to find foreign investors who produce branded products that are not region-specific alongside private label production for supermarkets. One such is Bonduelle but it is a rarity. The most likely development path is further growth in locally-owned businesses, such as Eurotherm, which exports canned and bottled products under its Noyen brand and also supplies private label buyers in the Russian Federation. It has produced under contract to Bonduelle and supplies ingredients to Kraft-Heinz in the Russian Federation. The most likely investment source for processing companies is private equity and the international financial institutions (IFIs).



Growth in the industry cannot just rely on investment in advanced technology. The capital requirements are too large, and FDI on the required scale will not be forthcoming. Simply to double the current area with modern greenhouses would require at least \$120 million. Armenia's thousands of smallholders are a latent resource if they can be assisted with low-cost productivity and quality improvements. This is where packers and processors working with outgrowers can make a crucial difference. The FDI promotion effort should focus on attracting these investors as the nucleus of the industry, as discussed in section II.C.

The policy measures proposed for the wine industry are apposite to this industry, but more aggressive incentives would be appropriate. Unlike the wine industry, fruit and vegetables will not attract aficionado investors to be central growers and processors. Recommendations in this area include:

- a. There is a case for stronger incentives to attract investors with appropriate commitment to working with smallholders to reduce rural poverty. These could range from tax exemption and tax allowances to grants of improved or unimproved land.
- b. In addition to ongoing land consolidation initiatives, the Government could consider:
 1. Amending legislation on land lease to allow for longer contract periods.
 2. Creating a land bank that facilitates matchmaking and expedites transactions between rural owners and foreign investors. Such types of institutions may take multiple set-ups. The recent experience of Business Armenia in identifying plots could help inform the one that is best suitable for Armenia.
 3. Introducing a concession scheme in which the Government offers long-term leases of serviced land at low cost to qualified investors. The concession scheme would set out the terms of the support and protections to be given to participating smallholders. A pilot project would be a good start.
- c. Regulatory restraints should be addressed. A recent report refers to “complex import procedures for agriculture sector inputs, [and] cadastral classification of greenhouse structures” as impediments to industry investment (World Bank, 2018b). These matters are not insuperable and should be remedied quickly.¹¹⁸

Pharmaceuticals – from CROs to CMOs

Armenia is currently on the bottom rungs of the global pharmaceutical industry. Unlike the capital-light IT industry, the Armenian pharmaceutical industry does not have access to the deep pools of risk capital needed to innovate in this sector (where a single new drug can take 10 years and a billion dollars to reach market). The industry produces a small range of generic drugs, mostly for the domestic market. Exports of pharmaceuticals were \$21.3 million in 2018, mostly to the Russian Federation and other EAEU countries. One producer, Liqvor, exports most of its products and accounts for 40 per cent of all pharmaceuticals exports. Apart from products, Armenia also has contract research organizations (CROs). One example is Azad Pharmaceuticals, which performs R&D on new formulations of drug compounds. Started in 2004, it has four synthesis laboratories and one analytics laboratory with 60 employees, of whom 40 are chemists. Another CRO is FMD K&L, a United States company that provides data management services to the industry. There is no discernible investment in Armenia by production outsourcing specialists – the so-called contract manufacturing organizations (CMOs).



Could FDI help Armenia reach a goal of \$500 million of pharmaceutical exports of goods and services in 10 years? One industry source believes \$300–400 million is achievable, with a half billion a very top estimate.¹¹⁹ Underpinning this optimistic view is the traditional Armenian strength in science. A sector profile draws attention to the “rich human capital of professionals in Biochemistry, Molecular Genetics and Microbiology” supported by a strong academic and research institutions.¹²⁰ The answer lies in examining prospects in three areas: exports of generics, growth in contract R&D and securing investment by CMOs.

Production of generics has grown from small beginnings in a highly competitive international industry dominated by China and India. The EAEU is the primary market and one where Chinese and Indian generics are in less demand. One investor says the industry’s growth will depend on “novation” rather than innovation – repackaging and relabelling products, but also on some original R&D to create more advanced versions of generics (biosimilars). The Armenian industry offers skilled staff at much lower cost than in developed countries but not as low as in India. It will find niches in its primary markets and steady growth in exports but is unlikely to attract a paradigm shift in efficiency-seeking FDI.

Investment by CROs offers the most immediate growth potential. Armenia offers a compelling combination of highly skilled professionals at competitive cost to a large global industry. The scale of professional labour might be an ultimate constraint, probably requiring up to 2,000 professionals per \$100 million of exports.¹²¹ It is unlikely that corporate tax incentives would be required since tax exposure can easily be optimised in work performed between related companies. There seem good opportunities for attracting investment in this sector in collaboration with universities and research institutes. The first step is to understand whether qualified staff will be available to support expansion of CRO. Thus, it is recommended that:

- a. A survey be carried out to determine the future availability of research professionals in the pharmaceutical industry and set out follow-up actions. The survey should also take account of requirements for generics manufacturers and the possible development of contract manufacture (below).

Contract pharmaceutical manufacture has market potential, and logistics difficulties are surmountable, but does Armenia have any decisive competitive advantage? The EAEU market is large. The Russian Federation alone imports over \$10 billion of medicines a year (UNCTADStat).¹²² Armenia has access to that in the single market which should include (i) mutual recognition or common regulation of medicine approvals; and (ii) ability to tender for public procurement of medicines.¹²³ Ingredients and finished products have high value to weight and would seem not to present the logistics issues of conventional manufacturing. However, manufacture is much more capital intensive than R&D. Hence, the lower cost of skilled personnel is a less important advantage and may not be sufficient to entice investment from CMOs. Tax incentives might also not be enough to attract CMOs versus other regional locations, especially the Russian Federation itself. But other types of policy support may be explored. In particular:

- b. The Government might need to provide seed funding in the form of first-class facilities. A comprehensive upgrade of one of the free zones could be a place to start.¹²⁴
- c. Contract manufacturing is a well-developed sector in the global pharmaceutical industry. Thus, given the market potential and accessibility of this market, the Government should undertake a full study of investment prospects in CMO and the measures that would be needed to attract foreign CMOs to locate in Armenia to produce for the EAEU market.

3. Nascent candidates – regional services

In several interviews during the UNCTAD fact-finding mission, it was suggested that Armenia has the infrastructure, flexibility and openness to service as a hub for the export of services to the region. Several possibilities are considered below – business process outsourcing, financial services, aircraft repair and maintenance, and education. Health services is not considered here, although it was the stated purpose of visit by a surprisingly large number in the visitor arrivals statistics.¹²⁵

Business process outsourcing (BPO)

BPO is a prime example of efficiency-seeking FDI. Specific corporate processes are outsourced and offshored to take advantage of lower costs – typically labour costs –but these must be completed by multilingual ability, quality telecommunications and inexpensive office space. BPO functions can range widely. One common activity is call centres (offering “help desk” customer support in order fulfilment, service and maintenance, billing enquires and post-purchase technical support). Another is telesales. Other services can include web design and maintenance, social media support services. They can extend to support to recruitment, legal services, accounting, software solutions and data management. Companies can off course offshore these functions under their direct control. But very often – especially in the less technical areas – it will be contracted out to a specialised BPO operator who will own and operate the facility.

Call centres would be an excellent fit for Armenia and could attract FDI. Armenia offers well-educated multilingual staff – Russian, English and Armenian – and good telecommunications. Moreover, call centres can be situated outside Yerevan to provide much needed employment opportunities in the regions where they also offer the possibility of revitalising neglected property. They are not necessarily high paying jobs but would help to address currently high youth and female unemployment outside Yerevan.

The call centre and other BPO opportunities should be promoted to specialist foreign investors. They have the market contacts to bring scale to the operations, to properly equip the centres and give the necessary training and support to the staff. There are many foreign investors in this line of business. An example is Teleperformance, a well-established French investor with many overseas operations. Vigorous FDI promotion and facilitation can bring good results. An example is the Dominican Republic which offers bilingual services to Central America and the United States. CEI-RD, its investment promotion agency, has prioritised services’ outsourcing. It is remarkably pro-active in facilitating new investors and in aftercare to encourage re-investment.¹²⁶ The country now has 100 suppliers employing 45,000 people, many outside the capital city.¹²⁷

Regional financial services

There are three possible scenarios for Armenia to develop regional financial services. The first is to create a regional capital markets hub. The second, of which there are two variants, is to become the preferred intermediary country for investment in the region, especially in the Russian Federation. The third is to develop an offshore financial services industry. These scenarios are propositions only and need to be carefully evaluated. The options are not mutually exclusive, but it is helpful to review them separately.

Financial services talent is not a constraint. They require a variety of advanced skills in corporate banking, investment banking, brokerage, trading, research and fund management. Undoubtedly within



the diaspora, there is abundant talent and enterprise in all the financial skills (and associated legal and accounting professions) needed to realise any of above scenarios where there are gaps in local expertise. In that respect, Armenia is much better resourced at the outset than countries such as Mauritius and Singapore, which are examples of small countries which embarked on developing regional financial hubs. In principle, talent is not a constraint in Armenia and a decided resource, although there might need to be incentives (such as periods of deemed non-residence for tax purposes, taxation of foreign income on a remittance basis) to encourage returnees if a decision were made to accelerate any regional financial services proposition.

A regional capital market hub, the first scenario, is not a prospect in the short to medium term. A regional capital market would seek to be a major issuer and trader for the region in equities and bonds, a regional stock exchange, a centre for fund management and a base for venture capital and private equity activities. The legal and institutional infrastructure is already in place, including a well-regulated stock exchange and depositary and arrangements for collective investment schemes. But as a small, low-middle income country, Armenia does not yet have the domestic savings base to kickstart this market and indeed the domestic capital market is only in an embryonic stage of development. Obviously, Armenia would need to tap into regional capital sources, but the issue is how best to do this in Armenia's overall interests. This is the subject of the other two scenarios but the evolution of scenario one – a regional capital market – will be returned to later.

A second scenario is to develop as an intermediary for outside investments into the region. There are two variants which, for convenience, can be labelled the Cyprus model and the Irish model. The Cyprus model is a pass-through approach. Inward investment to the ultimate host country is channelled through an intermediary country to benefit from a favourable double tax treaty. In Armenia's case, it would require a very favourable double tax treaty with regional countries, particularly the Russian Federation (zero withholding taxes) and tax free pass-through of dividend and other remittances via Armenia back to investors' home countries. Cyprus already provides such a facility for foreign investors in the Russian Federation. Armenia could not offer better terms – even assuming that the Russian Federation would be willing to provide such a regime. In the Irish model, there is generally applicable zero or very low corporate tax which encourages investors to set up regional headquarters and service facilities with international invoicing operations designed to minimise group taxation. Both models require the establishment of resident companies in the jurisdiction. In the Cyprus model, they employ the services of local lawyers and accountants, and generate services' exports directly or in the form of professional fees. The Irish model indirectly generates export revenue through retention in-country of earnings by employees and professional service providers. Neither model expands the capital base to provide value-added financial services in the region. Nor would either benefit Armenia's image as they bespeak of financial engineering and tax avoidance rather than the substantive industries that Armenia can offer. Finally, the Irish model depends on instituting generally applicable rates of zero or very low tax. The Government should judge whether either form of regional financial service is feasible or desirable.

A third scenario is a fully-fledged offshore financial services sector. In this scheme local and international banks¹²⁸ are incentivised to set up offshore subsidiaries, which can conduct business effectively as non-resident entities. They can accept deposits from and make loans to parties in other countries without incurring any taxes, except perhaps on employee income, in the host country. Again, these schemes provide employment to professionals and support staff – which can be very important in small countries with few natural advantages – but little other economic benefit. In recent years, many of



these jurisdictions have received a bad press as tax havens and, worse, as poorly regulated hotspots for money laundering. They can lead to reputational damage. In addition, Armenia would need to be acutely aware of political risks arising if such arrangements facilitated capital outflow from the Russian Federation, which became unacceptable to the Russian authorities. On balance, it seems unlikely that Armenia needs to take the risks involved in view of the limited benefits, given that it has much to offer in more substantive sectors.

A natural evolution as a capital hub is likely to be the best approach for Armenia. By providing a safe harbour environment, Armenia can aim to evolve in the long term as a regional capital hub. The right environment will entail:

- A safe, stable business environment with competitive tax rates.
- A well-functioning stock exchange and depository system.
- A first-rate commercial justice system.
- Low corruption and a safe and pleasant living environment (e.g. Singapore).
- Maintaining bank integrity. Arguably, and despite recent consolidation, there are many banks in Armenia which increases the risk of bank failures or might encourage some to cut corners in areas such as money laundering. The recent bank scandal in Estonia is a salutary reminder.

Among specific measures to help this evolution, Armenia offers a special vehicle: the Armenian Contractual Investment Fund (ACIF). The ACIF enables non-residents to hold most types of global assets in a regulated but very low tax Armenian entity. Importantly, residents of the EAEU member States are not subject to controlled foreign corporation rules. This enhances the regional appeal. Resulting financial flows would presumably be allowable by member States as falling within the concept of a single capital market. The ACIF scheme would be of most benefit if some of the ACIF funds were held in Armenian assets. For example, there could be stipulation to achieve a long-term holding of say 5 per cent in Armenian assets. This could be built up from remitted dividends and interest. It would need to be investigated whether this is feasible within EAEU rules.

Other specific measures to accelerate capital market development should be investigated. A cost-benefit analysis should be undertaken of proposed tax incentives to encourage local issuance and portfolio inflows. These include corporate tax exemption for companies listing on the exchange and relief on withholding taxes on non-resident acquirers of listed shares and debt instruments. UNCTAD's experience is that corporate tax relief offered to encourage public listing is not very cost-effective. There might be more scope for some withholding tax relief to encourage foreign portfolio investment. Any regulatory improvements to promote a local brokerage and fund management industry should also be looked into.

Logistics and food safety

International transport initiatives... Large international transport projects, such as the Baku-Tbilisi-Kars railway and the construction of a new Baku International Sea Trade Port (Alat) – which aims to become the biggest multi-purpose port in the Caspian Sea – have increased possibilities for the South Caucasus to become a hub on the China-Europe trade route.¹²⁹ Armenia is also exploring the potential for increased international transport connectivity, and it is supporting the introduction of a Persian Gulf – Black Sea multimodal transport corridor, connecting the Islamic Republic of Iran with Europe via Armenia and Georgia,

in the One-Belt-One-Road initiative (OBOR). Not only would the project help overcome the constraints posed by the country's landlocked geographic position, but it would also place Armenia on a new China–Europe transport route.

...open new opportunities for Armenia in the area of logistics and food safety. Given Armenia's well-developed services sector and IT infrastructure, and the market opportunities opened by these projects, in particular the vast needs of managing the logistics created in the framework of OBOR, the country could aspire to serve as a logistics hub. It could provide efficient online management of goods in transit through the multimodal transportation systems in parts of the Middle East or CIS region, with the involvement of both domestic and international investors. In particular, Armenia could become a hub for food safety,¹³⁰ through a stronger national quality infrastructure and the enhancement of standards and quality controls. As mentioned in chapter I (section G), this would also entail targeting investments from MNEs to assist reduce non-tariff barriers in certain markets – for instance, agricultural fresh products. Additional initiatives could include introducing food law in law schools. In the longer term, the Government could also consider the signing of mutual recognition agreements with third-country authorities regarding the conformity assessment of regulated products. The high-tech profile of the country could also support this objective. Armenia is well positioned to develop and apply IT solutions for food safety and traceability, e.g. by using blockchain technology to facilitate the process of recording transactions and tracking assets across the regional network.

Aircraft repair and maintenance

The aircraft repair market in the region is worth investigating. The commercial aviation maintenance, repair and overhaul (MRO) market is worth about \$88 billion worldwide. Many smaller airlines outsource their maintenance, which suggests opportunity for a regional operation. Estonia and Lithuania are examples. They have MRO operations for the Baltics region and are expanding. Magnetic MRO, the Estonian company, grew out of the aircraft repair needs of Estonian Air and its part owner SAS, which serviced aircraft in Estonia. It grew with help from venture capital. In 2017, with revenues of €70 million and 400 employees, it was named Estonia's company of the year.¹³¹ In 2018, it was acquired by a Chinese company Guangzhou Hangxin Aviation Technology.¹³² FL Technics, the Lithuanian MRO company, is expanding with strong support of the Government, which sees it as the core of an aviation technology cluster.¹³³ The company reports that 30 per cent of its net profit is earned from servicing clients in the Russian Federation and the CIS. FL Technics is owned by Avia Solutions Group, headquartered in Cyprus.

Armenia might have the profile to attract efficiency-seeking FDI in the MRO industry. It has ample capacity at the Yerevan airport and the profile of competitive skilled labour costs that are important investment factors in this industry. It might need to invest heavily in specialist training, as there could well be skills gaps due to lack of a national air carrier (which ceased operations in 2003). On the other hand, the industry offers interesting opportunities for Armenia's high-tech sector in areas such as automated scanning.

Education services

The cross-border flow of students is usually from lower income to higher income countries. And some developed countries such as Australia and the United Kingdom have significant export earnings from overseas students. This is supported by pro-active policies to attract foreign students. At present,



Armenia has 7,000 foreign students at its universities, with most of them being exchange students.¹³⁴ By comparison (in population size) in 2017, Ireland attracted around 23,000 foreign university students and New Zealand around 28,000. In the latter case, the economic value is estimated at NZ\$1.1 billion (~ \$715 million) (NRB, 2016).

Currently, Armenia is likely to be a net importer of education services. Some foreign institutions have set up programmes in Armenia to fill perceived gaps in national education. There include universities with State support from France and the Russian Federation. Other examples are collaborations between overseas and Armenian universities, such as the Anglia Ruskin University partnership with the Armenian State University of Economics to offer an MBA programme leading to the award of a British degree. A business degree is also offered by the British School of Business Armenia, and the UWC Dilijan College, officially opened in October 2014, had been a pioneer in actively targeting international students.

Armenia is not currently ranked highly enough to be an exporter of education services within the region. A very important driver is the ability to offer a degree from a highly ranked name university or at least a degree from a well-regarded university plus English language proficiency. Armenia does not offer a recognised name university. None is in QS World University Rankings of the top 10 in the “Emerging Europe and Central Asia” group. Yerevan State University is the top ranked Armenian university in the Webometrics Ranking of World Universities run by the Spanish Research Council at a low 2,632 (the National Polytechnic University is ranked 15,377 on the same system). No Armenian university is ranked in the Times Higher Education World University Rankings 2019 of 1,250 universities (perhaps because no data were submitted). These rankings may or may not reflect the quality of Armenia’s best universities, but they are the current international perception available to prospective students. Armenia seems to have done little to date to change that perception or promote the excellence of its best institutions.

Could Armenia attract an offshoot of a leading university to become a name for a regional hub? It is very expensive for universities to establish stand-alone facilities in another country and burdensome to relocate a high-quality faculty. Very few leading universities have done so and prefer collaborations with local institutions to spare investment and secondment of staff. The best example of a stand-alone investment is the Institut Européen d’Administration des Affaires – INSEAD, investing in a Singapore campus as a regional hub for an assured large Asian market. The Russian Federation and the Islamic Republic of Iran would be essential markets for Armenia for the investment of an international leader to be viable. Armenia would need to ask in what disciplines and tuition language it could hope to attract the volumes of students needed to support the entry of a leading university.

The best approach could be to build university-industry collaborations in IT. The most promising route for Armenia could be to expand on the successful examples of university-industry collaborations – such as the Microsoft Centre and the Synopsys collaboration with the National Polytechnic University (box II.1). These leading companies provide high-name recognition and quality assurance. If this is feasible, supporting policies would be needed. Among these would be reasonable rights to work whilst studying and, upon graduation, rights to work in the Armenian IT industry. These work rights are integral parts of leading countries promotion programmes. They are also seen as providing longer-term benefits to the country if the best and brightest take up residence rights or return home and forge trade and investment links with their *alma mater* country.



C. INVESTMENT PROMOTION AMAZING ARMENIA

Armenia is clearly under-promoted, yet the investment promotion agency has been abolished. *Business Armenia*, the investment promotion agency (IPA), was recently dissolved. This action does not necessarily reflect on its performance since it seems to have been well-regarded by investors.¹³⁵ The change is part of a Government-wide streamlining programme promised in the most recent national elections. *Business Armenia*'s functions are to be absorbed by the Ministry of Economy. This is not the first reorganization. *Business Armenia* itself was formed by the merger, in 2014, of the Industrial Development Fund, the National Competitiveness Framework and the National Tourism Agency under the original name of the Development Foundation of Armenia.

Whatever the institutional shape of investment promotion, the functionality should meet certain tests. The institutional arrangements for investment promotion had not been settled at the time of preparing this report. Recommendations therefore focus on key functions and these are set out in the form of tests that any new arrangements should meet. These are:

- Visibility and accessibility;
- Adequate provision for four key roles – promotion, facilitation, aftercare and advocacy;
- Control of national branding;
- Coordination within ministries and with industry initiatives;
- No regulatory or incentive powers;
- Separation of investment and export promotion.

In addition, there are two practical features of Armenia's investment promotion scene to be considered – the diaspora and the free economic zones.

It should go without saying that the investment promotion operation should be visible and accessible. Surprisingly, this is not always so with IPAs. In this case, care must be taken not to bury the operation within the Ministry. The physical location should be ground floor and not gated through the security apparatus. It should have major signage on the street and in the front of the building. There should also be clear social media separation from the Ministry website.

The operation should cater for promotion, facilitation, aftercare and advocacy. These are the classic roles of IPAs. These should all be part of the operation but exercised in conjunction with other ministries and agencies, the Chamber of Commerce and Industry and other industry associations (see more below). In the case of advocacy, if the operation remains within the Ministry of Economy, the new operation would not have an advocacy function. This would be performed by the Investment Department of the Ministry. But the operation should be able and encouraged to relay investor concerns to policy personnel in the Ministry.

The investment promotion nucleus should control national branding... One, universal, country brand should be created and owned by the operation to maximise impact. The brand should extend to export promotion and tourism promotion (e.g. Invest in Amazing Armenia, Visit Amazing Armenia).



...but, apart from branding, investment promotion is a shared responsibility to be coordinated within Government and with industry. An agency should not claim exclusive rights to investment promotion. It should supplement and complement the efforts and expertise of other ministries and industry associations.¹³⁶ For example, mining and energy specialists are usually well equipped to structure and present investment opportunities, and will always be the first port of call for investors. On the other hand, some ministries, such as education and health, usually have little investment promotion expertise. They should welcome professional assistance. Armenia's Ministry of Foreign Affairs has a well-meaning attempt to promote education through a website page "Study in Armenia" but it clearly lacks the impact that professional help from a specialist operation would provide.

Investment promotion and export promotion should usually be separated, and SMEs not neglected, if they form part of the IPA mandate. UNCTAD's recommendation is that these functions should be separated. They are ostensibly similar but require different skills. Experience is that export promotion – being the more straightforward activity with more immediate results – tends to dominate resource allocation. FDI promotion suffers and local SMEs get scant attention. It is true that many countries, especially smaller ones with limited funds, combine the two functions and this was the case with Business Armenia. The new arrangements give the opportunity to separate these activities at headquarter level. This would give a sharper focus to promoting foreign investment and, importantly, to assisting local investors. However, if the new arrangements permit, there is a case for combining investment and export promotion in respect of two target industries – tourism and wine. In these industries, there will often be a mix of investors, distributors and consumers at trade fairs and exhibitions and in on-line engagement. There are likely to be synergies and economies in combining both functions. Abroad, small countries with limited diplomatic missions will necessarily require their commercial attaches and trade representatives to cover both fields.¹³⁷

A clear case for, and full participation from, key regulatory arms of government is needed if facilitation is organized as a "one-stop shop". The one-stop shop (or "window") arose as a means of helping investors to navigate red tape in difficult countries. Best practice is to have no need for a one-stop shop because regulations are clear, and permits are issued promptly and fairly. On this basis, Armenia does not appear to need a one-stop solution. However, if judged necessary in the new arrangements, the one-stop shop must have the full cooperation of all regulatory agencies. In practice, this means physical location of officers representing all the agencies in one central facility. These are the operations that work best. The officers represent their agencies not just to advise on regulatory requirements. They should be empowered where possible to issue permits or otherwise act as liaison points for the more complex areas (such as environmental licences).

The investment promotion unit should not have regulatory or incentive powers. Regarding *incentives*: for two reasons it is not usually good policy to enable promotion agencies to decide whether tax incentives apply in individual cases. First, it becomes difficult to judge the *bona fides* of an agency's promotional and aftercare outreach if investors must necessarily approach it to claim incentives. This is even more acute if the general tax regime is uncompetitive, fortunately not the case in Armenia. The second, and related reason, is that incentives discriminate between investors. Agencies with incentive-granting powers tend to ignore the interests of those who do not qualify. This may especially be the case where incentives have size thresholds (investment size, job creation, exports for example) and SMEs get little attention. The best approach is to design incentives that can be claimed as part of the normal process of tax filing. Currently, Armenia follows good practice in this respect. Regarding *regulatory powers*: deciding on whether to approve a proposed foreign investment in a restricted activity is a policy not an operational issue. It is best left to the relevant ministries.



The substantial diaspora presents special issues and opportunities for investment promotion. The size and spread of Armenia's diaspora population and its investment impact were noted in section I.C above. The question is whether this natural resource leads to a certain lethargy in investment promotion to the diaspora as well as a lack of attention to non-diaspora sources. There is evidence both ways. The presence of Azad Pharmaceuticals is a result of classic investor targeting of a Swiss diaspora investor, but the very low international profile of Armenia is suggestive the other way. The new arrangements will need to provide for three things:

- Better mapping of the diaspora and its potential, including through a Customer Relationship Management system;
- Pro-active targeted promotion to the diaspora with key performance indicators to measure value-added by the promotion effort.¹³⁸ Direct contact with industry insiders could be especially helpful in fashion, wine, food processing, education and pharmaceuticals, in addition to the obvious area of high-tech and innovation, as discussed in section B.1. The Armenian diaspora like to be associated with quality products according to an insider;
- Prescriptive attention to major capital exporting countries which have no Armenia diaspora. This means the Asian leaders in particular.¹³⁹

Appoint a Principal to lead investment promotion in each priority industry target. Targeted investment promotion requires prioritization of resources and efforts. It is recommended that within the new promotion arrangements, a Principal be appointed as the lead for each of the target industries in the billion-dollar club and emerging billion-dollar club. Over time, two special projects principals could also be employed to cover the varied opportunities in nascent candidate activities. The Principal would be the authorised government official within the new investment promotion setup to lead and coordinate investment promotion. Since each target industry has a different set of promotional needs, the Principal, in each case, should be required to develop a business plan for meeting the targets and challenges. The business plan for each target industry should include:

- The appropriate approach to branding, targeting, facilitation and aftercare;
- The requirement for industry studies;
- Coordination arrangements with other government departments and agencies concerned with the industry;
- Mechanisms for engagement with local business;
- A plan for outreach to the diaspora;
- Networking with international financial institutions, development partners, non-governmental organizations and private equity groups;
- Input to support programmes to develop local industry, including SME programmes and linkages to foreign investors.

The free economic zones should be revamped. Free economic zones are meant to facilitate export processing in an extra-territorial customs jurisdiction of minimal taxes and red tape. The Alliance zone has kept its tax-free status but now permits pioneer manufacturing aimed 100 per cent at the domestic market. Normally, private owners of zones are a self-motivating arm of investment promotion – they are landlords seeking tenants to avail of attractive facilities. This seems to have broken down in the Alliance zone.



Although privately-owned, the facilities are dilapidated and present an unattractive prospect. Other zones were not visited by the UNCTAD fact-finding mission, but it is understood that the zone near the Iranian border is under-used. As discussed in the World Investment Report 2019, most zones failures worldwide can be traced back to problems such as poor site locations or poor zone design with inadequate facilities (UNCTAD, 2019a). In this regard, the role of the free economic zones should be re-examined. In at least one case, they have moved far from their original purpose (see chapter I, section C). The most obvious outcome would be to turn them into industrial estates in which tax privileges, if any, are based on the activity not on the location. Pharmaceutical CMOs and full-package textile manufacturers would be ideal candidates. In addition to a solid regulatory framework, strong institutions and good governance, active support to promote clusters and linkages is key to maximizing the success and sustainable development impact of zones (UNCTAD, 2019a).

III. ASSESSMENT AND KEY MEASURES

Armenia has sufficiently large and accessible markets to aim for several billion- and half-billion-dollar export sales over the next 10–20 years in both goods and services. With the EAEU, Armenia has moderate – single digit – tariff preferences in merchandise trade and there is a noticeable uptick in its exports to this market since joining in 2015. The EAEU market is likely to be especially important in underpinning investment in one of the billion-dollar candidates – textiles and garments – and two of the emerging billion-dollar candidates – wine and pharmaceuticals.¹⁴⁰ The EU imports many billions of dollars of products of interest to Armenia. The EU's GSP+ scheme does not confer lower tariffs on Armenia's exports compared with many competitor exporters but at least levels the playing field. So far, the take up of this opportunity in the target areas has been limited. This cannot be excused by Armenia's logistics difficulties. Indeed, Armenia is virtually on Europe's doorstep compared with the lengthy supply chains of many successful exporters to Europe. In product markets, the EU is a particular opportunity for investment in agribusiness and textiles and garments, and is the obvious growth market for tourism.

Armenia has a particular efficiency profile of a well-educated workforce at attractive pay levels with a strong skills/cost profile in high-tech areas. The latter is most prominent in ICT and engineering but is also expressed as R&D competence in industry and pharmaceuticals. R&D to prototype stage is Armenia's niche in the global value chains of heavy manufacturing. For light industry, an educated work force on low pay is not a sufficient or sustainable efficiency offer. Low productivity – due to shortcomings in training, equipment, and work practices – negates low wage cost as a source of competitive advantages (as demonstrated in the textiles and garment industry). Modernising investment can address productivity issues and build out industry into a more sustainable offer. Productivity issues also arise in agribusiness and wine production, but already the gains from investment in better equipment and technology are evident. Low wage cost has to be converted into low labour cost. The message could be put more starkly – unless modernising investment is attracted to agribusiness and light industry, they are not sustainable simply based on an educated work force on low wages.

Regional services markets present unrealised opportunities for Armenia's efficiency profile. Investment prospects in business process outsourcing, aircraft repair and maintenance and, possibly, in IT-related higher education are suggested.

Increasing domestic value-added and boosting incomes in the marzes are key outcomes for investment strategy and must be reflected in policy measures. This report sets export outcomes as headline investment targets, but these are not the ultimate economic or social benefits. For example, increasing domestic value-added by moving to full-package manufacture is essential to employment and sustainability in the textiles and garments industry; extending tourism benefits to areas outside Yerevan is a vital outcome in this industry. The pharmaceutical industry needs to consider how best it can extend R&D capability and a small generics industry into larger scale manufacturing.

Investment in the target industries will be from a mix of sources. Local investors, supported by the diaspora will play the key role. This will be supplemented by selective FDI, interventions by private equity and international financial institutions. Outside the high-tech sector, Armenian industry does not yet have the scale or maturity to attract leading foreign investors. On the other hand, there is much good will from foreign aid donors in support studies and programmes which help industries to attract and benefit from private investment. For each target industry, table II.11 summarizes the key segments, investment and skills needs, sources of potential investment as well as supporting policy measures.

Each target industry needs a tailored investment promotion strategy. The target industries vary in their stage of development and potential investors and need unique strategies. Thus, it is recommended that a Principal person be appointed for each target to lead the investment promotion effort on the basis on an agreed business plan.

Armenia under-promotes investment and exports. The Government is reforming investment promotion and the new arrangements are not part of this report. Some functional tests for the new promotional regime are nevertheless suggested as guidance for the reform. Certainly, a case could be made for more Government expenditure on promotion. In two specific target industries – tourism and wine – where investment and export promotion are closely related, levies are proposed. These would support the export promotion which underpins investment. In these cases, it would be sensible for the Principal to lead both investment and export promotion.

Apart from boosting promotion, relatively straightforward and non-controversial policy measures are needed in the target sectors....They need to build on the existing high-quality overall investment climate. Most measures are tax related and are of a type which are relatively common elsewhere. Non-tax policy measures include: i) improving European access – air links, visas and extension of the GSP+ scheme; and ii) influencing EAEU policy developments affecting the regional capital market, public procurement, cross-border recognition of professional qualifications and free trade negotiations. In selected cases, direct support measures should be considered – such as in agribusiness through concessioning serviced land to processors willing to support out-growers or providing first class facilities at low cost to start-up contract pharmaceutical manufacturers.

...together with concrete policy actions to improve the overall investment climate. As discussed in the context, foreign investors are still in a wait-and-see posture. Established investors told UNCTAD that there is a noticeable improvement in areas of good governance affecting business since the change of Government. They are not yet certain that the changes for better will be sustained. A similar wait-and-see attitude is likely to affect potential foreign investors. Settlement of the Lydian gold mine dispute will be an important step. Beyond that, several measures are recommended in chapter I. Among them, two stand out: one is to strengthen anti-corruption by establishing a unified anti-corruption body with full investigative powers, backed by a strong penalties regime. The second one is to strengthen the commercial branch of the judiciary to rule on inter-business disputes and injustices perceived by business in their dealings with Government by providing increased staff, commercial training and salaries.

Table II.11. Target industries and key related actions

| Targets | Segments | Investment and skills needs | Sources | Key actions |
|-------------------------------------|---|---|--|---|
| Billion-dollar club | | | | |
| Tourism | <ul style="list-style-type: none"> • Culture and religion • Exploration and adventure • Wine and gastro | <ul style="list-style-type: none"> • Lodgings, attractions and restaurants outside Yerevan | <ul style="list-style-type: none"> • DFDI • DDI • niche FDI • regional chains | <ul style="list-style-type: none"> • Introduce a tourism levy and fund • Provide marketing support • Promote improved air links • Foster standards • Introduce group tax relief and accelerated depreciation • Prepare a list of anchor projects |
| High-tech | <ul style="list-style-type: none"> • Artificial intelligence • Data science • System and chip design and testing • Software and application development • Multimedia and games | <ul style="list-style-type: none"> • Contract R&D • Prototype production • AI and data analytics | <ul style="list-style-type: none"> • FDI • DFDI • DDI | <ul style="list-style-type: none"> • Adopt a comprehensive AI strategy • Evolve corporate and securities law • Introduce a regulatory sandbox for non-financial services • Upgrade IP for university-industry collaboration • Retain fiscal competitiveness • Establish data protection and AI ethics frameworks • Increase R&D funding and direct government support • Upgrade STEM education • Set up an Armenian “Diaspora innovation network” • Establish a Strategic Council for AI Technology |
| Textiles and garments | <ul style="list-style-type: none"> • Full-package manufacturing • Armenia’s own brands | <ul style="list-style-type: none"> • Upgrading of CMT operations • Market research and marketing skills • Design expertise | <ul style="list-style-type: none"> • Partnerships • FDI-DDI • Private equity • FDI • DFDI | <ul style="list-style-type: none"> • Introduce group tax relief • Allow faster depreciation on manufacturing machinery • Create a design school • Establish SME support programmes • Set up diaspora support initiatives |
| Emerging billion-dollar club | | | | |
| Wine | <ul style="list-style-type: none"> • High-end • Indigenous varieties | <ul style="list-style-type: none"> • 30,000 hectares of high-yield land • (\$750 million) | <ul style="list-style-type: none"> • DFDI and DDI • “Afcionados” | <ul style="list-style-type: none"> • Consider faster depreciation and immediate expensing • Provide indefinite loss-carry forward • Allow double-deduction for marketing expenses • Provide small farmers support • Introduce group tax relief • Adopt a promotion and quality assurance regime |

.../



| Targets | Segments | Investment and skills needs | Sources | Key actions |
|--|--|---|---|---|
| Emerging billion-dollar club | | | | |
| Agribusiness | <ul style="list-style-type: none"> Fresh fruit and vegetables Canned and bottled products | <ul style="list-style-type: none"> High-tech greenhouses (min. \$120 million) Intensive fruit Private label production Packers and processors | <ul style="list-style-type: none"> FDI (Israel) DDI Private equity IFIs | <ul style="list-style-type: none"> Support contract-farming and outgrowers Introduce group tax relief Provide tax allowances for sourcing from smallholders Establish land banks and longer lease-periods Land concession scheme for processor/outgrowers Remove regulatory constraints |
| Pharmaceuticals | <ul style="list-style-type: none"> Contract R&D Generics expansion Contract manufacturing | <ul style="list-style-type: none"> 2,000 professionals per \$100 million of R&D revenue | <ul style="list-style-type: none"> FDI DDI (generics) | <ul style="list-style-type: none"> For contract R&D expansion: skills survey For contract manufacturing: <ul style="list-style-type: none"> market study first-class facilities and free zones upgrading |
| Nascent candidates | | | | |
| Business process outsourcing | <ul style="list-style-type: none"> Call centres Software solutions and data management Web design and maintenance | <ul style="list-style-type: none"> Language and other skills available Infrastructure and office facilities available | <ul style="list-style-type: none"> FDI | <ul style="list-style-type: none"> Focus on specialized operators and call centres Promote locations outside Yerevan |
| Regional financial services | <ul style="list-style-type: none"> Regional capital hub | <ul style="list-style-type: none"> Skills' gaps could be filled by diaspora if necessary | <ul style="list-style-type: none"> FDI DFDI | <ul style="list-style-type: none"> Significantly increase fight against corruption Improve commercial justice system Encourage diaspora returnees Continue promoting bank consolidation and integrity Promote localization of ACIF funds |
| Logistics and food safety | <ul style="list-style-type: none"> Trading hub Food safety hub | <ul style="list-style-type: none"> IT infrastructure and skills available Need transport infrastructure investment | <ul style="list-style-type: none"> FDI DFDI DDI | <ul style="list-style-type: none"> Promote increased international transport connectivity Enhance quality certification and controls Sign mutual recognition agreements on conformity assessment of regulated products |
| Aircraft repair and maintenance | <ul style="list-style-type: none"> Maintenance, repair and overhaul (MRO) | <ul style="list-style-type: none"> Infrastructure available Need significant skills' investment | <ul style="list-style-type: none"> FDI | <ul style="list-style-type: none"> Provide specialist training Linkages support initiatives with high-tech sector |
| Education services | <ul style="list-style-type: none"> Specialized IT education centres | <ul style="list-style-type: none"> University-industry cooperation | <ul style="list-style-type: none"> FDI-DDI partnerships | <ul style="list-style-type: none"> Foreign students' working rights Access to Armenian IT industry after graduation |

Notes: FDI – foreign direct investment; DFDI – diaspora foreign direct investment; DDI – direct domestic investment.



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ANNEX I. INTERNATIONAL INVESTMENT AGREEMENTS AND TREATIES WITH INVESTMENT PROVISIONS

| Parties | Date | Status | |
|---|---|--------|--------------------|
| <i>Bilateral investment treaties between Armenia and...</i> | | | |
| 1 | Argentina | 1993 | In force |
| 2 | Austria | 2001 | In force |
| 3 | Belarus | 2001 | In force |
| 4 | Belgium-Luxembourg Economic Union | 2001 | In force |
| 5 | Bulgaria | 1995 | In force |
| 6 | Canada | 1997 | In force |
| 7 | China | 1992 | In force |
| 8 | Cyprus | 1995 | In force |
| 9 | Egypt | 1996 | In force |
| 10 | Finland | 2004 | In force |
| 11 | France | 1995 | In force |
| 12 | Georgia | 1996 | In force |
| 13 | Germany | 1995 | In force |
| 14 | Greece | 1993 | In force |
| 15 | India | 2003 | Terminated |
| 16 | Iran, Islamic Republic of | 1995 | In force |
| 17 | Iraq | 2012 | In force |
| 18 | Israel | 2000 | In force |
| 19 | Italy | 1998 | Expired/Terminated |
| 20 | Japan | 2018 | In force |
| 21 | Jordan | 2014 | In force |
| 22 | Kazakhstan | 2006 | In force |
| 23 | Kyrgyzstan | 1994 | In force |
| 24 | Korea (Republic of) | 2018 | In force |
| 25 | Kuwait | 2010 | In force |
| 26 | Latvia | 2005 | In force |
| 27 | Lebanon | 1995 | In force |
| 28 | Lithuania | 2006 | In force |
| 29 | Netherlands | 2005 | In force |
| 30 | Qatar | 2002 | In force |
| 31 | Romania | 1994 | In force |
| 32 | Russian Federation | 2001 | In force |
| 33 | Sweden | 2006 | In force |
| 34 | Switzerland | 1998 | In force |
| 35 | Syrian Arab Republic | 2009 | In force |
| 36 | Tajikistan | 2002 | Not in force |
| 37 | Turkmenistan | 1996 | Not in force |
| 38 | Ukraine | 1994 | In force |
| 39 | United Arab Emirates | 2016 | In force |
| 40 | United Kingdom | 1993 | In force |
| 41 | United States | 1992 | In force |
| 42 | Uruguay | 2002 | In force |
| 43 | Viet Nam | 1993 | Not in force |
| <i>Treaties with investment provisions</i> | | | |
| 1 | Armenia – Singapore Agreement on Trade in Services and Investment | 2019 | Not in force |
| 2 | Armenia – EU CEPA | 2017 | In force |
| 3 | Armenia – United States TIFA | 2015 | Not in force |
| 4 | CIS Investor Rights Convention | 1997 | In force |
| 5 | EAEU Treaty | 2014 | In force |
| 6 | EAEU – Viet Nam FTA | 2015 | In force |
| 7 | The Energy Charter Treaty | 1994 | In force |

Source: UNCTAD's International Investment Agreements Navigator, available at: investmentpolicy.unctad.org/international-investment-agreements.



ANNEX II. SUMMARY OF RECOMMENDATIONS

| What to do? | Why? | How? |
|---|--|---|
| <p>1. Improve the FDI-specific regime</p> | <p>The Government of Armenia has made great efforts to build an open regime for FDI through various legislative reforms. The enactment of the privatization and SEZ laws were important landmarks towards promoting investment in priority sectors. However, some concerns remain regarding the clarity of key provisions and the alignment of the Law on Foreign Investments of 1994 with modern practice. Also, Armenia's investment treaty network consists mainly of first-generation IIAs, which should be modernized to better integrate the national development objectives and sustainable development elements.</p> | <p>Measures affecting the national legal framework for FDI</p> <p>I.A.1 Clarify key FDI-related provisions in such areas as entry restrictions, standards of treatment, expropriation, transfer of funds, currency convertibility, dispute settlement and access to incentives</p> <p>I.A.2 Reflect the mandate of investment promotion authorities in the revised law</p> <p>I.A.3 Revise and harmonize the definition of investment and investors across all laws</p> <p>I.A.4 Limit potentially excessive investor guarantees, such as FET, MFN, full protection and security and minimum standards, and reconsider the need for an open-ended stability clause, as well as the entitlement to compensation in case of improper performance by the public administration</p> <p>I.A.5 Include refinements to the guarantees in case of indirect expropriation to increase predictability</p> <p>I.A.6 Introduce a provision indicating that foreign investors shall not be accorded privileges beyond those afforded to Armenian investors in similar circumstances</p> <p>I.A.7 Reduce the country's exposure to ISDS by strengthening dispute prevention policies, promoting consultation, investor-State dialogue and prioritising ADR and domestic solutions</p> <p>Measures affecting the international legal framework for FDI</p> <p>I.A.8 Set up a sequence of reform actions for updating the IIA network</p> <p>I.A.9 Clarify key IIA provisions (e.g. FET or indirect expropriation) and incorporate a sustainable development dimension</p> <p>I.A.10 Improve the investment dispute settlement mechanisms in IIAs, including by prioritising domestic solutions using filters and by adding new elements such as an appeal facility</p> <p>I.A.11 Enhance systemic consistency, by improving the coherence of the IIA network at the bilateral and regional levels, managing the interaction between IIAs, and linking IIA reform to the domestic policy agenda</p> |

What to do?

2. Strengthen corporate governance and operations

Significant reforms to improve business operations and facilitate access to land were recently implemented. Further efforts, notably regarding the corporate governance and bankruptcy regime are required.

Why?

- I.B.1 Move forward with the introduction of eGovernment tools for business facilitation, including the mapping, simplification and automation of key procedures
- I.B.2 Bolster the legal framework on corporate governance and bankruptcy, including by:
- a. Moving forward with the reform of the corporate governance legislation to improve internal and external auditing of firms and shareholder protection. Introducing mandatory external auditing of financial statements in line with good international practice could also be considered
 - b. Amending legislation to improve the position of shareholders with regards to their voting rights and access to information
 - c. Reforming the bankruptcy regime by encouraging company restructuring and alternative dispute resolution mechanisms

How?

3. Address pending issues in the tax regime

The general tax regime has been streamlined, which has improved transparency and tax compliance, and further reforms are planned. However, the simplified tax regimes, which can be powerful tools to promote formalization and enterprise development, have been overused. These, together with continued changes to the Tax Code, have created undue complexity and uncertainty. While some consolidation of the various schemes is ongoing, the eligibility for the turnover tax regime, which was already wide, had widened further with the recent reform of the Tax Code and risks discouraging company growth. The FEZ regime is also unusually generous from the tax standpoint, and its design and implementation counter good practice.

- I.C.1 Reduce the threshold of application of the turnover tax regime
- I.C.2 Introduce group tax relief to promote cross-sectoral investment
- I.C.3 Adopt comprehensive cost-benefit analysis of incentives schemes
- I.C.4 Reform the FEZ regime to encourage value-addition, regional development and linkages by:
- a. Reassessing mandated activities for existing and future FEZs while narrowing down the amount and focus of incentives
 - b. Extending selectively the eligibility criteria for incentives to domestic suppliers of resident companies
 - c. Considering the development of an “SDG-model zone”
 - d. Setting up a linkages development initiative
- I.C.5 Enhance the powers of the tax and customs revenue authority to monitor tax compliance by:
- a. Furthering efforts to introduce electronic technologies for tax and customs payments
 - b. Implementing the transfer pricing legislation
 - c. Increasing capacity building for monitoring and auditing of taxpayers by public authorities



| What to do? | Why? | How? |
|--|--|--|
| 4. Enhance labour policy and facilitate access to skills | The labour regime balance employers and workers rights. Nevertheless, several regulations require updating in line with international labour standards. Armenia also faces the double challenge of retaining skilled labour and meeting the contemporary skills needs of the private sector. | <p>I.D.1 Move forward with the reforms to align the Labour Code and related legislation with current international labour standards</p> <p>I.D.2 Work with international partners to strengthen the labour inspectorates</p> <p>I.D.3 Continue to hold consultations on the minimum wage, with the goal to increase it in line with productivity improvements, as budget constraints decrease</p> <p>I.D.4 a. Adopt an institutionalised mechanism to determine the scarce skills list for work permit exemption</p> |
| 5. Strengthen the environmental protection regime | Whereas the legal and institutional framework for environmental protection has been improved in recent years, further work is needed to clarify procedures, responsibilities and liabilities. | <p>I.E.1 Move forward with planned reforms to improve the strategic assessment of environmentally sensitive projects</p> <p>I.E.2 Improve the governance of environmental compliance monitoring</p> <p>I.E.3 Increase awareness on environmental affairs amongst the general population, encouraging educational and media campaigns, CSR programmes and public consultations</p> |
| 6. Foster fair and effective competition | Significant reforms have aligned Armenia's competition framework with international good practice, but several anti-competitive practices persist. A holistic approach to promoting a competitive business environment is needed. | <p>I.F.1 Increase the investigative powers of the Commission</p> <p>I.F.2 Improve coordination between the competition authority, sectoral regulators and ministries and ensure that price determination in public services be based on transparent information and consultations with all stakeholders, including consumers</p> <p>I.F.3 Continue building the capacities of the Commission staff</p> |
| 7. Strengthen intellectual property rights | Important efforts have been deployed to align the domestic intellectual property legislation and quality certification to international requirements and modern standards. Nevertheless, monitoring and compliance lag and public awareness remains weak. | <p>I.G.1 Improve the fluidity of industry-science linkages by removing legal loopholes that prevent the commercialization of inventions in higher education and research institutions, promoting industrial clusters and leveraging on the Armenian diaspora of scientists</p> <p>I.G.2 Enhance the capacities of the Intellectual Property Agency to assist firms on strategic decisions about IP protection by: <ul style="list-style-type: none"> a. Intensifying cooperation between the IP Agency and WIPO to assist in seeking patent protection for Armenian inventions abroad b. Facilitating university-industry linkages through: 1) workshops on patent policies for universities; 2) legislation that facilitates university patenting in return for universities marketing their inventions through licensing agreements with the private sector </p> <p>I.G.3 Enhance quality certification to obtain market access for selected products</p> <p>I.G.4 Improve awareness, monitoring and compliance on IP rights</p> |



| What to do? | Why? | How? |
|--|--|---|
| 8. Improve governance and commercial justice | A dysfunctional judiciary system and poor governance could undermine the impact of business climate reforms. There is a need to restore citizens' confidence in institutions and build a sound basis for economic growth. In addition to improving the independence and probity of the judiciary system, the Government needs to adopt a holistic approach to the fight against corruption. | <p>I.H.1 Move forward with planned reforms to speed up judiciary procedures</p> <p>I.H.2 Improve and promote ADR by raising awareness, increasing skills of mediators and arbitrators and revising the legislation to speed-up the recognition of awards by arbitration tribunals in courts.</p> <p>I.H.3 Implement the Anti-Corruption Strategy and proceed with the establishment of a unified anti-corruption body and of specialized anti-corruption courts.</p> |
| 9. Promote export and efficiency-seeking investment for the <i>Billion-dollar club</i> | Armenia has access to sufficiently large and accessible markets. It also has an efficiency profile characterized by a well-educated workforce, strong skills heritage and competitive salary levels. The country is well positioned to aim for several billion- and half-billion-dollar export sales over the next 10–20 years. The Billion-dollar club includes industries already near \$1 billion in value of annual exports or which can achieve the target within 10 years, i.e. tourism, high-tech, and textile and garments. Several policy measures are needed to support growth and regional development towards the objective. | <p>Tourism</p> <p>II.B.1 Levy a tourism tax to fund priority needs of the sector. A modest tax (e.g. \$2) could be levied on hotels in Yerevan only and used to fund two outcomes – regional attractions with municipality involvement and tourism promotion on a co-funding basis with the industry</p> <p>II.B.2 Introduce a double tax deduction for marketing expenses to foster promotion of Armenia's attractions</p> <p>II.B.3 Improve air links and consider waiving the \$20 departure tax on flights from Armenia</p> <p>II.B.4 Encourage high standards at the tourism industry to promote Armenia as a high-end destination. Incentives could include a depreciation policy to encourage refurbishment every five or six years</p> <p>II.B.5 Draw up a list of anchor regional tourism investments outside Yerevan – hotels, lodges, restaurants and major visitor attractions such as ski fields – to attract investors</p> <p>High-tech – ICT, engineering and deep tech</p> <p>II.B.6 Carefully evolve corporate and securities law to address practices in the high tech sector</p> <p>II.B.7 Develop a regulatory sandbox regime for non-financial activities to enable testing new technologies in controlled conditions and appoint the Ministry of Economy as the regulatory sandbox gatekeeper</p> <p>II.B.8 Address the modernization of the IPR regime (see I.G.1 to I.G.4)</p> <p>II.B.9 Retain fiscal competitiveness in the area and better communicate existing incentives, including on R&D</p> <p>II.B.10 Adopt data protection and AI ethics frameworks</p> |



| What to do? | Why? | How? |
|---|---|---|
| | | <p>II.B.11 Update STEM education curricula, including by introducing data science at undergraduate and master's levels and coding and statistics in primary and middle schools and strengthen university-industry collaboration</p> |
| | | <p>II.B.12 Increase R&D funding and government support based on international policy practice</p> |
| | | <p>II.B.13 Establish an Armenian "Diaspora innovation network" supported by a CRM system and state-of-the-art research infrastructure</p> |
| | | <p>II.B.14 Set up a Strategic Council for AI Technology with representatives of academia, industry and government</p> |
| <p>Textiles and garments</p> | | |
| | | <p>II.B.15 Adopt concerted and targeted investment promotion to introduce new full-package foreign investors</p> |
| | | <p>II.B.16 Allow faster depreciation on the acquisition of key assets needed to deepen and sustain the industry – in particular for fabric and accessories manufacturing machinery</p> |
| | | <p>II.B.17 Provide more direct support for the design segment to create Armenian design expertise and brands (e.g. a school of design, prizes and exhibitions as well as access to general SME support programmes)</p> |
| | | <p>II.B.18 Involve the diaspora with industry experience to provide guidance on branding, promotion and other aspects of commercialisation</p> |
| <p>Wine</p> | | |
| <p>10. Promote export and efficiency-seeking investment for the <i>Emerging billion-dollar club</i></p> | <p>The emerging <i>billion-dollar club</i> includes industries which should achieve \$1/2 billion in value of annual exports in 10 years and strive for \$1 billion in 20 years. Targets are wine, agri-business and pharmaceuticals.</p> | <p>II.B.19 Subject to cost-benefit analysis, abolish the tax exemption for farm income and remove the distinction between farming and processing as income sources. A small tax allowance can be introduced to protect farmers on very small holdings</p> |
| | | <p>II.B.20 Introduce 150 per cent depreciation of capital investment and allow immediate expensing in the year of investment</p> |
| | | <p>II.B.21 Allow longer or indefinite loss carry forward period to the industry, in view of the length of time that grape and stone fruit plantings take to bear</p> |
| | | <p>II.B.22 Allow double deduction of marketing expenses to support branding and promotional activities</p> |
| | | <p>II.B.23 Allow support given by packers and processors to small farmers to be expensed as a double deduction</p> |

| What to do? | Why? | How? |
|-------------|------|---|
| II.B.24 | | Establish a comprehensive promotion and quality assurance regime, by: <ol style="list-style-type: none"> Introducing a levy on wine exports to fund export market promotion by a recognised industry body Promoting quality and brand recognition in the Russian Federation above Moldovan and Georgian wines Lifting the profile of Armenian wine in other markets especially for Areni Noir and the other premiums Establishing a joint public-private body to certify the authenticity of all wine (and brandy) exports on a fee-for-service basis as a mandatory export requirement |
| | | Agribusiness |
| II.B.25 | | Introduce stronger incentives to attract investors ready to work with smallholders to reduce rural poverty. These could range from tax exemption and tax allowances to grants of improved or unimproved land |
| II.B.26 | | Amend legislation on land-lease to allow for longer contract periods |
| II.B.27 | | Create a land bank that facilitates matchmaking and expedites transactions between rural owners and foreign investors |
| II.B.28 | | Introduce a concession scheme in which the Government offers long-term leases of serviced land at low cost to qualified investors, while supporting and protecting participating smallholders |
| II.B.29 | | Address regulatory restraints to industry investment, including complex import procedures and cadastral classification of greenhouse structures |
| | | Pharmaceuticals |
| II.B.30 | | Carry out a manpower survey to determine the future availability of research professionals in the pharmaceutical industry and set out follow-up actions |
| II.B.31 | | Provide seed funding in the form of first-class facilities and consider the comprehensive upgrading of a free zone |
| II.B.32 | | Undertake a full study of investment prospects in CMO and measures needed to attract foreign CMOs to produce for the EAEU market |

What to do?

11. Promote export and efficiency-seeking investment for the Nascent candidates

Nascent candidates are activities which have potential but for which it is too early to set export targets. These include business process outsourcing, financial services, logistics and food safety, aircraft repair and maintenance and higher education, all of which could make of Armenia a regional services hub.

Why?

Regional services hub: BPO, financial services, logistics and food safety, aircraft repair and maintenance and education

II.B.33 Facilitate the establishment of call centres/business process outsourcing opportunities outside Yerevan to create employment opportunities in other regions

II.B.34 Provide a safe harbour environment to the development of a regional capital market hub. This would entail competitive tax rates, reliable justice system, a well-functioning stock exchange and repository system, low corruption and health banking system

II.B.35 Increase the impact of the ACIF scheme by promoting holding of ACIF funds in Armenian assets and investigate measures to accelerate capital market development, including encouraging local issuance and portfolio inflows

II.B.36 Establish Armenia as a logistics and food safety hub through online management of goods in transit, a stronger national quality infrastructure, and the negotiation and implementation of mutual recognition agreements on conformity assessment of regulated products

II.B.37 Invest in specialist training required for commercial aviation maintenance, repair and overhaul (MRO) services

II.B.38 Support the export of education services by building on university-industry collaborations in high-tech, promoting cross border recognition of diplomas, and adequate work and residence rights for foreign students

II.C.1 Ensure visibility and accessibility of the investment promotion operation, both in physical and social media terms

II.C.2 Provide adequate provision and mandate for investment promotion, facilitation, aftercare and advocacy, and refrain from assigning regulatory functions or incentive powers

II.C.3 Assign the investment promotion nucleus control of national branding. The brand should extend to export promotion and tourism promotion

II.C.4 Mandate it to coordinate investment promotion initiatives with other ministries and industry associations, such as those in charge of agriculture, education and health

II.C.5 Separate investment and export promotion at headquarter level to give a sharper focus to promoting foreign investment and, importantly, to assisting local investors (except in respect of tourism and wine where combining investment and export promotion may be beneficial)

12. Strengthening investment promotion

the country's investment promotion framework is undergoing a major revision. The IPR proposes recommendations to improve investment promotion whatever the future institutional shape adopted.



| What to do? | Why? | How? |
|-------------|------|--|
| II.C.6 | | <p>Better utilize the Diaspora as a partner in FDI promotion through:</p> <ol style="list-style-type: none"> Mapping of the diaspora and its potential through a Customer Relationship Management system Targeted diaspora promotion with key performance indicators on value-added by the promotion effort Targeting focus on major capital exporting countries which have no Armenia diaspora, the Asian leaders in particular |
| II.C.7 | | <p>Appoint a Principal to lead investment promotion for each of the target industries in the billion-dollar club and emerging billion-dollar club. The Principal should develop a business plan for each target industry, including:</p> <ul style="list-style-type: none"> the appropriate approach to branding, targeting, facilitation and aftercare the requirement for industry studies coordination arrangements with other government departments and agencies concerned with the industry mechanisms for engagement with local business a plan for outreach to the diaspora networking with international financial institutions, aid donors, NGOs, and private equity groups input to support programmes to develop local industry, including SME programmes and linkages to foreign investors |



NOTES

- ¹ World Bank national accounts data (accessed 15 October 2019), available at: data.worldbank.org/indicator/NY.GDP.MKTP.KD.ZG?locations=AM&view=chart
- ² The signing of the CEPA with the EU is expected to bring Armenia's laws and regulations more closely in line with the EU's in the areas of business environment, agriculture, transport, environment, consumer protection and the energy sector.
- ³ It is estimated that 69 per cent of FDI originate from the diaspora over the period 1998–2004 (EV Consulting, 2011). Several stakeholders interviewed by UNCTAD in preparation for this report indicated that many Armenian residents also channelled investment back to Armenia as FDI during the early 2000s for tax-related purposes (so-called “round-tripping” FDI).
- ⁴ Amulsar gold mine, discovered in 2006 in the South of Armenia, is owned and operated by Lydian International. The mine, which is nearing completion, has recently been the object of protests and blockades by local residents and environmental activists. They have effectively halted the company's operations. At the time of UNCTAD's fact-finding mission, the Government of Armenia had commissioned an independent environmental expertise to determine the way forward.
- ⁵ The authorized body for technical regulation can apply exceptions if there are special reasons and the operator will be based in Armenia (Law 81 of 2007 on Aviation, art. 43).
- ⁶ World Bank, Investing Across Borders iab.worldbank.org/data/exploreconomies/armenia - investing-across-sectors.
- ⁷ As discussed in section B, foreign individuals cannot own agricultural land, but foreign companies registered in Armenia can. In addition, in the context of integration to the EAEU, the Government reserves the right to accord differential treatment to investors from EAEU countries in the following sectors and activities: airport and airport operation services, postal services, investment in freshwater fisheries, energy industry, arms and explosive manufacturing industries, public law enforcement and correctional services, social services – except for welfare – primary and secondary education, public training, health and childcare and financial services (see the bilateral investment treaty with Japan).
- ⁸ The Law on alienation also stipulates that expropriations shall be carried out in exceptional cases and in the manner prescribed by law and that Initial and adequate compensation shall be granted against alienated property (art. 3).
- ⁹ Amendments would also include the possibility of capital movement controls for purposes of maintaining financial system stability, combating circulation of illicitly obtained funds and terror financing, preventing business risks or for statistical purposes. Significantly, the new law will also authorize to impose limitations on the transfer of funds as a result of non-discriminatory and good faith application of laws regulating the following matters: (a) bankruptcy, insolvency, and the protection of the rights of creditors, (b) issuing, trading and dealing in financial instruments, including securities and bonds, (c) criminal or penal offences, (d) filing of reports with financial regulatory authorities and record keeping, and (e) ensuring execution of orders, judgments and other public legal acts in judicial or administrative proceedings.
- ¹⁰ The following analysis is based on IIAs for which the text was available in one of the six official languages of the United Nations. Two BITs have been effectively terminated – Armenia–India in March 2017 and Armenia–Italy in January 2018.
- ¹¹ The Armenia – EC Cooperation Agreement was replaced by the Armenia – EU CEPA, when it came into force on 1 June 2018. The scope and depth of the investment provisions in Armenian TIPs range from binding substantive investment protection (e.g. the Eurasian Economic Union – Viet Nam FTA) to provisions on investment cooperation (e.g. the Trade and Investment Framework Agreement (TIFA) with the United States).
- ¹² The Eurasian Economic Union – Viet Nam FTA is included in the analysis relating to BITs because it includes BIT-like substantive investment protection provisions (Section V).
- ¹³ One case has been decided on the merits in favour of Armenia (*TS Investment v Armenia*). Two cases are currently pending, *Borkowski and Rasia FZE v Armenia* (ICSID Case No. ARB/18/28) (filed in 2018) and *Arin Capital and Khudyan v Armenia* (ICSID Case No. ARB/17/36) (filed in 2017). The fourth case, *Global Gold Mining v Armenia* (ICSID Case No. ARB/07/7) (filed in 2007), was settled by the parties (see *Rasia FZE, Joseph K. Borkowski v. Armenia, 2018*; *Arin Capital and Khudyan v. Armenia, 2017*; *Global Gold Mining v. Armenia, 2007*; and *TS Investment v. Armenia, 2007*, icsid.worldbank.org/en/Pages/cases/casedetail.aspx?CaseNo=ARB/18/28;investmentpolicyhub.unctad.org/ISDS/CountryCases/9?partyRole=2(accessed 10 January 2019).



- ¹⁴ Several recent IIAs have omitted the ISDS clause altogether relying instead on a State-State dispute settlement mechanism. See the recent Cooperation and Facilitation agreements concluded by Brazil for example.
- ¹⁵ Electronic registration is available at e-register.am/am/ but it is not commonly used, mainly due to the requirement to obtain e-signature, which implies additional cost and time. When registration is done online, founder(s) still need to visit the registry in order to obtain a hard copy of the incorporation documents (World Bank, 2018a).
- ¹⁶ Some users prefer face-to-face interaction mainly because of the requirement to obtain e-signature, which implies additional cost and time. When registration is done online, owners still need to visit the registry in order to obtain hard copy of the incorporation documents (World Bank, 2018a).
- ¹⁷ The activities subject to licensing include: banking and financial-banking organizations; trading in weapons; healthcare services; education services; postal communication industry; transport services, as well as service providers requiring professional capability, such as physicians, bankers, financial brokers and auditors, among others.
- ¹⁸ See armenia.eregulations.org/ (accessed 1 June 2019).
- ¹⁹ See, for instance, EBRD (2017), Corporate Governance in Transition Economies Armenia Country Report, May.
- ²⁰ Because in insolvency proceedings in Armenia the automatic stay of enforcement proceedings does not apply with regards to secured creditors, a Bank has an incentive to initiate foreclosure and directly enforce its collateral (World Bank, 2018a).
- ²¹ For instance, 93.6 per cent in Gegharkunik, 68.9 per cent in Lori and 76.6 per cent in Kotayk.
- ²² According to the official statistics of Ministry of Finance of the Republic of Armenia.
- ²³ The general corporate income tax rate in Armenia will be 18 per cent, starting in 2020. In other EAEU countries it is as follows: Belarus: 18 per cent; Kazakhstan: 10 per cent, Russian Federation: 20 per cent. The average corporate income tax rate in the European Union is 19.37 per cent, and 23.38 per cent across OECD countries. See: KPMG International, at: <https://home.kpmg/xx/en/home/services/tax/tax-tools-and-resources/tax-rates-online/corporate-tax-rates-table.html> accessed 23 September 2019.
- ²⁴ This section is based on the Tax Code of Armenia, the tax documentation of the International Bureau of Fiscal Documentation and PricewaterhouseCoopers (IBFD, 2019; PWC, 2018). Unless otherwise noted, quotes refer to the Tax Code of Armenia. Estimations on the dollar value of Armenian drams are based on the IMF average exchange rate for year 2018 (i.e. one dollar equals AMD483).
- ²⁵ The Draft Law “On Making Amendments and Addenda to the Tax Code of the Republic of Armenia”.
- ²⁶ Whereas the Government taxes resident-entities on their worldwide income, non-residents are subject to CIT only on their Armenian-sourced income.
- ²⁷ For investment funds, taxable income is the value of the net assets. The corporate income tax computation is based on the profit and loss account, as adjusted in accordance with tax law provisions (arts. 106 and 107). The CIT rate for investment funds (excluding pension funds and warranty funds) registered in the Republic of Armenia, as well as for securitisation foundations, is 0.01 per cent of the tax base.
- ²⁸ Agriculture production is considered separate from food production, which is taxed according to the general regime
- ²⁹ The total tax rate measures the amount of taxes and mandatory contributions payable by the business in the second year of operation, expressed as a share of commercial profits.
- ³⁰ The following expenses are partially deductible (arts. 120 and 123): donations, up to 0.25 per cent of gross income; expenses for foreign trips, up to 5 per cent of gross income (for local trips, up to AMD12,000 (~ \$25) per day of per diem expenses); interest paid for bank loans, up to the amount resulting from applying twice the official bank rate of the Central Bank of Armenia; interest paid for other loans (with certain limitations); and representative expenses, up to 0.5 per cent of gross income, but not more than AMD5 million (~ \$10,350).
- ³¹ Before 1 January 2018, a “group method” was applied to fixed assets built on or after 1 January. Non-depreciable assets include land, museum collections, architectural monuments, works of art, constructions in progress, public roads, assets used for investment projects, items related to film archives, inventory and property that is fully deducted in the current year and publicly used property.
- ³² Dividends paid by the Panarmenian Bank are exempt from withholding tax.



- ³³ For application of the transfer pricing rules, the revenue authorities will focus on completeness of calculation and payment of the following taxes: CIT, VAT and mineral royalty tax (for the use of metal mineral resources).
- ³⁴ See: avalara.com/vatlive/en/eu-vat-rules/eu-vat-number-registration/vat-registration-threshold.html (accessed on 4 July 2019.)
- ³⁵ VAT payers should file unified return of VAT and excise tax on a monthly basis.
- ³⁶ The processing of refund differs between local producers and exporters of zero-rated products. For local producers, the refund period takes six months. For the refund of VAT of zero-rated products for export, the refund is upon application, but the precondition is that the export actually takes place, and it is done in proportion to the volume of exports (i.e. the VAT refund cannot be more than the exports value).
- ³⁷ In the case of brandy, for instance, the excise tax rate depends on the ageing period, and ranges from AMD3,000 per litre for beverages with ageing period of one to three years, to AMD22,000 per litre for ageing of 20 years or more. For wine, the excise tax is 10 per cent, but not less than AMD100 per litre. Both brandy and wine excise tax rates are set to increase yearly between 2020 and 2023, with the adoption of the Draft Law “On Making Amendments and Addenda to the Tax Code of the Republic of Armenia”. The draft would also remove the percentage of wine excise tax rate.
- ³⁸ Firms engaged in trading activities are eligible for a tax credit of 4 per cent of the purchasing costs of the imported goods destined for trading activities. The amount of tax payable on income received from trading activities is subject to a minimum of 1.5 per cent of the total trade turnover. The unused portion of the tax credit can be used in future tax periods. Turnover taxpayers engaged in catering and restaurant activities are eligible for a tax credit of 3 per cent of the purchasing costs of the imported goods destined for catering and restaurant activities. The amount of tax payable on income received from catering and restaurant activities is subject to a minimum of 4 per cent of the total trade turnover.
- ³⁹ The benefits granted (i.e. reduced CIT and personal income tax rates for employees) will expire by 2021. However, decrees can still be used for the granting of non-fiscal incentives, mostly with regards to access to State-owned land, which may be provided free of charge at the State or municipality level.
- ⁴⁰ Stakeholders in the IT sector interviewed during the fact-finding mission have mentioned that the eligibility requirements for accessing incentives were not properly advertised amongst potential beneficiaries, and many were not aware of their existence.
- ⁴¹ See fez.am/eng/index.php?o=28#metka (accessed 14 May 2019).
- ⁴² Information shared by the State Revenue Committee showed that as of 2019, 63,082 inquiries were received by the call centre, including 50,308 on tax matters and 12,576 on customs.
- ⁴³ Pending issues concern high minimum membership requirements for the formation of trade unions and employers' organizations, ambiguous provisions on workers' representation in the absence of trade unions as well as limitations to the right to strike (European Commission, 2018).
- ⁴⁴ In the case of a fixed-term contract of employment is terminated on its expiration (Article 111 Labour Code). Before the date of expiration, both parties should comply with the requirement of ten-day written notice.
- ⁴⁵ Pay issues are regulated by the Employment Wages Act of 2001, the Act on Remuneration of Civil Servants of 2002, and the Minimum Wage Act of 2004.
- ⁴⁶ See lo.org/moscow/news/WCMS_701758/lang--en/index.htm for further details (accessed 2 June 2019).
- ⁴⁷ According to the Ministry of Labour and Social Affairs, workers' grievances that may remain unattended due to poor inspections include reimbursements for overtime work, dismissals, as well as rendering of rest and vacation times.
- ⁴⁸ See ilo.org/moscow/news/WCMS_701758/lang--en/index.htm (accessed 2 June 2019).
- ⁴⁹ Whereas most foreign students are members of the diaspora, some schools (e.g. medicine economics) have introduced degrees in English and French language to broaden their visibility.
- ⁵⁰ As part of the process, the Ministry may offer the employer an Armenian citizen candidate that meets the requirements of the employer. It would only grant the permit if the employer refuses the suggested candidate.
- ⁵¹ If the employer does not conclude an employment contract within one month after obtaining the work permit, the permit may be revoked by the authorities. The law also mandates employers to reimburse the foreign employee's expenses if the employer does not conclude the employment contract within one month after obtaining a work permit.

- 52 Other exempt categories include individuals holding permanent and special residency status in Armenia, refugees, invited lecturers of foreign education institutions, accredited representatives of foreign media; students working as part of exchange programmes during holidays, and specialists eligible to work as part of international treaties signed by Armenia.
- 53 See UNECE, 2017a and 2017b and UN Armenia, 2016.
- 54 These include seven copper molybdenum, four copper, 14 gold and gold polymetallic, two polymetallic, two iron and one aluminum mines. Besides basic metals there exist also rare and scattered elements – rhenium, selenium, tellurium, cadmium, indium, helium, thallium, bismuth (UNECE, 2017b).
- 55 The conflict has so far involved litigation in national courts, but the company has also called for formal negotiations with the Government, see lydianinternational.co.uk (accessed 2 June 2019).
- 56 Strategic environmental assessment means the evaluation of the likely environmental, including health, effects, which comprises the determination of the scope of an environmental report and its preparation, the carrying-out of public participation and consultations, and the taking into account of the environmental report and the results of the public participation and consultations in a plan or programme. (art. 2, para. 6 of the SEA Protocol to Espoo Convention).
- 57 These would include a clear definition of stakeholders to be consulted and the specification of guidelines and manuals which could challenge expert assessments (see Geghamyan and Pavlickova, 2019)
- 58 According to UNECE, the EIA and SEA systems established by the law are not completely in line with the provisions of the UNECE Espoo Convention and its Protocol on SEA (UNECE, 2017b).
- 59 The country undertook a Voluntary Peer Review of its Competition Policy in 2010 (UNCTAD, 2010).
- 60 Some exceptions apply as follows: an anticompetitive agreement shall not be deemed to be (1) vertical agreements of economic entities if the share of each of the participants in that agreement does not exceed 20 per cent in the relevant commodity market; 2) agreements concluded between economic entities included in the group of entities, if one of those undertakings has established direct or indirect control over another economic entity as well as if these economic entities are under the direct or indirect control of one person which carries out activities simultaneously on the side of several economic entities included in the group of persons (Law on Protection of Economic Competition, art. 5.1, 7).
- 61 An economic entity or entities cannot be considered as dominant if, as a seller or purchaser, they capture no more than 10 per cent of the given market in terms of sale or acquisition volumes.
- 62 Furthermore, the failure to declare a concentration may result in a fine of up to AMD5 million.
- 63 The sectoral regulator, the Public Services Regulatory Commission, counts with significant responsibilities, including setting tariffs, issuing licences and setting standards.
- 64 In the pharmaceutical sector, for instance, engaging foreign firms also involves contract research organizations, engineering, training, laboratory and other consultancy services (UNCTAD, 2011).
- 65 Copyright does not require registration. Designs are protected for five years from the application and can be renewed for five years at a time, but for no more than 25 years in total. Trademarks protection is 10 years from filing and can be renewed indefinitely.
- 66 EAEU legal provisions include all categories under the TRIPS Agreement, and are contained in the Treaty's Section XXIII on "Intellectual Property" (articles 89-91) and the "Protocol on Protection and Enforcement of Intellectual Property Rights" (Annex 26) (WTO, 2018).
- 67 According to existing legislation, State universities and research institutes are autonomous legal entities, that are not under the remit of the Ministry of Education and Science. However, many state universities fail to exercise their autonomy and have adopted charters abiding to Ministerial supervision and to the Law on SNCS. There are, however, a few exceptions (e.g. the Yerevan State Medical University, and the Agrarian University), which have adopted more flexible charters (UNECE, 2014).
- 68 It is also still to join the International Accreditation Forum and International Laboratory Accreditation Cooperation mutual recognition agreement (UNECE 2019).
- 69 Only 15 per cent of Armenian firms export (directly or indirectly). This is well below the average of comparator countries (24 per cent) and despite the large share of firms having internationally recognized quality certification (45 per cent) (World Bank, 2017).
- 70 Amongst other changes, the new legislation will regulate the rights of disabled artists and orphan, works and it will further specify the existing provisions copyright contract rights and phonogramme producers' rights, which will be harmonized with copyright holders' rights (WTO, 2018).

- 71 For reference see: https://www.wipo.int/tisc/en/search/search_result.jsp?country_id=6
- 72 This contrasts with Armenia's position on the Doing Business 2019 rankings, in which the country is ranked 24th worldwide on enforcing contracts. It should be highlighted that World Bank methodology is based on a case study of Yerevan, where courts may show higher than average performance compared to the rest of the country (World Bank, 2018a).
- 73 The Ministry of Justice reports that in 2013, 48 540 civil cases were received in the courts of general jurisdiction, rising to 137 003 in 2017 and 129 941 in 2018. 3376 bankruptcy cases were received in 2013, 9218 in 2017 and 9326 in 2018.
- 74 For a comprehensive treatment of those issues, see Khachatryan, 2018.
- 75 The Ministry of Justice also plans to introduce the following reforms to strengthen the judiciary: 1) a complete declaration of property, income, interests and expenses of judges; 2) the harmonization of grounds for imposing disciplinary liability upon judges and 3) the improvement of the procedure for imposing disciplinary liability upon judges.
- 76 Armenia ranked 105 out of 180 in the 2018 Corruption Perceptions ranking of Transparency international, a poor record compared to its peers, including the best in the region (Georgia ranked 41).
- 77 The Istanbul Anti-Corruption Action Plan is a sub-regional peer review programme launched by the OECD Anti-Corruption Network for Eastern Europe and Central Asia.
- 78 The Draft Strategy was posted on the internet as of 19 December 2018 and is available at: e-draft.am which is a unified website of the Ministry of Justice for publication of draft legal acts.
- 79 Weighted average takes into account the size of imports on individual tariff lines in each category.
- 80 \$57.4 million (2014) and \$143.1 million (2016) at mid-year exchange rates.
- 81 Brandy was not included in the analysis.
- 82 Excluding Belarus which is not included in the rankings.
- 83 See for example the review in part III of labour costs in the textiles and garments industry.
- 84 Other examples include cooperation between the French University in Armenia and Pernod Ricard Company (Ararat Brandy Factory), or between commercial banks and the Armenian State University of Economics, where successful students are able to do internships and have "learn by doing" experiences, which could lead to employment contracts after completion of their studies.
- 85 Meeting with business leaders at the Union of Manufacturers and Businessmen of Armenia.
- 86 Several investors highlighted this issue to the UNCTAD interview team.
- 87 Industry sources.
- 88 Estimates are for 2016 as compiled by the Ministry of Diaspora.
- 89 Cited in World Bank, 2017.
- 90 Estimates of the Ministry of Diaspora.
- 91 International agencies and bilateral partners – in particular the ADB, the World Bank Group, UNIDO, UNDP and the Deutsche Gesellschaft für Internationale Zusammenarbeit – have commissioned important relevant studies and programmes which have benefited this report.
- 92 Statistical Committee of the Republic of Armenia based on "WTO methodology" and sample surveys of total visitor arrivals of around 2.5 million.
- 93 Published by the State Committee on Tourism "Tourist Sector Armenia" 2016.
- 94 To some extent the figures are conjectures as Armenia does not report in the UN standard format Tourism Satellite Account.
- 95 World Travel and Tourism Council.
- 96 This industry background draws on the EIF review.
- 97 Investor interview.



- ⁹⁸ The definition if from TechWorks at: techworks.org.uk/about/what-is-deep-tech (accessed 5 July 2019).
- ⁹⁹ A regulatory sandbox is a regulatory approach, typically summarized in writing and published, that allows live, time-bound testing of innovations under a regulator's oversight. Novel financial products, technologies and business models can be tested under a set of rules, supervision requirements, and appropriate safeguards (UNSGSA, 2018).
- ¹⁰⁰ See, for instance, the "Ethics Guidelines for Trustworthy Artificial Intelligence" prepared in 2018 by the High-Level Expert Group on Artificial Intelligence set up by the European Commission as part of the EU's AI strategy. Available at: ec.europa.eu/futurium/en/ai-alliance-consultation/guidelines#Top (accessed 22 July 2019).
- ¹⁰¹ See wcit2019.org (accessed on 22 July 2019).
- ¹⁰² For example, the African Growth and Opportunity Act and the Dominican Republic-Central America FTA schemes, which give preferential access to the United States market for certain Africa and the Caribbean countries respectively.
- ¹⁰³ And where bad practices can go viral in seconds on social media.
- ¹⁰⁴ Estimates supplied by Winemakers Association.
- ¹⁰⁵ UN Comtrade and Statistical Committee of the Republic of Armenia.
- ¹⁰⁶ New Zealand wine exports rose from \$41 million in 1996 to \$1.2 billion in 2016.
- ¹⁰⁷ Based on estimates provided by Armenian consultancy Wineworks. Excludes wineries.
- ¹⁰⁸ For example, the largest New Zealand brand, Montana Wines was acquired as a mature company and was eventually bought by Pernod Ricard and re-branded as Brancott Estates.
- ¹⁰⁹ Investor interview.
- ¹¹⁰ Presently it is believed that only 170 hectares will be planted in 2019.
- ¹¹¹ AMD150 (~ \$0.31) from January 2019.
- ¹¹² As a transitional arrangement, depreciation accumulated over the previous 10 years development should be allowed to be brought forward as a tax expense, to honour the tax-free conditions under which existing investments were made. If so, the proposed group relief should not be available for these costs.
- ¹¹³ For some time there will still be a major Russian market for non-premium wines.
- ¹¹⁴ In coordination with procedures for specific importing countries, e.g. the EU's wine export certificate.
- ¹¹⁵ No statistics were found on the proportion of exports emanating from high tech green houses and intensive orchards. But they are likely to account for the bulk of the recent rapid growth of agri-business exports.
- ¹¹⁶ The World Bank 2016 report estimates that less than \$1 million is spent annually on extension services, ~ \$3 on average per farm for the estimated 330,000 smallholders.
- ¹¹⁷ In 2017, Israel exported \$503 million worth of fruits (fresh and dried), nuts and fresh vegetables to the EU which is testimony to its ability to access that market. Armenia exported only \$85,000 worth to the EU in that year.
- ¹¹⁸ The report also identifies access to land, irrigation and energy efficiency issues as impediments. However, investors seem able to cope with these according to comments made to the UNCTAD mission.
- ¹¹⁹ Investor interview.
- ¹²⁰ Select Armenia. Pharmaceutical Industry Overview.
- ¹²¹ Based on \$50,000 revenue per researcher.
- ¹²² Pharmaceuticals is one of the largest import markets in the EAEU countries and the wider region as noted above in section I.A market profile.
- ¹²³ Producers of finished products and active pharmaceutical ingredients within the EAEU have a 20 per cent preference in public procurement.
- ¹²⁴ The privately-operated Alliance Free Economic Zone is in very unattractive condition.



- ¹²⁵ Health tourism is mentioned in the section dealing with tourism. The UNCTAD fact-finding mission did not establish whether health reasons are an adjunct to visits to family or friends or a genuine stand-alone reason for visiting Armenia.
- ¹²⁶ UNCTAD visited a Teleperformance operation in the Dominican Republic in 2015. CEI-RD had assisted its establishment by finding premises, helping to obtain permits and holding job fairs to facilitate recruitment of staff.
- ¹²⁷ CEI-RD website, accessible at: ceird.gob.do/wp/ (accessed on 26 June 2019).
- ¹²⁸ They can also be used for insurance, consulting, aircraft and ship broking and leasing.
- ¹²⁹ See recent analysis on this subject at: thediplomat.com/2019/06/can-china-broker-the-resolution-of-the-armenia-azerbaijan-conflict/, emerging-europe.com/voices/chinas-obor-initiative-opportunities-for-the-south-caucasus/ and jamestown.org/program/south-caucasus-eyes-becoming-a-hub-along-eu-china-transportation-route/ (accessed 1 July 2019).
- ¹³⁰ See the interview with H.E. Mr. Armen Sarkissian, at: armenpress.am/eng/news/980055/ (accessed on 2 July 2019).
- ¹³¹ See investinestonia.com (accessed on 26 June 2019).
- ¹³² Recently, it has announced that it is considering a relocation from Estonia due to dissatisfaction with entry procedures for foreign specialists and tax policies.
- ¹³³ See investlithuania.com (accessed on 26 June 2019).
- ¹³⁴ Interview with Ministry of Education. Exchange students are officially termed “credit-mobile” students and are not counted in international statistics on foreign students.
- ¹³⁵ Comments made in investor interviews.
- ¹³⁶ In some countries, UNCTAD has advised IPA's to enter into written protocols with other government agencies so that lines of cooperation are clear and beneficial to a whole-of-government promotional effort.
- ¹³⁷ UNCTAD provides training programmes and materials in investment promotion for diplomatic staff.
- ¹³⁸ For example, the Irish Government is reputed to have contacted the CEO's with Irish names of every significant United States company to begin a dialogue about Irish investment opportunities. Armenia's Ministry of Diaspora is compiling a comparable list which currently numbers 108 business leaders in 20 countries.
- ¹³⁹ The diaspora populations are small in China (1,000), Japan (75), South Korea (20) and Singapore (110).
- ¹⁴⁰ Access to Russian Government procurement in pharmaceuticals could be especially important for manufacturing (as distinct from R&D) options in this industry.



The Investment Policy Review of Armenia is the latest in a series of investment policy reviews undertaken by UNCTAD at the request of countries interested in improving their investment framework and climate. The economies included in this series are:

| | | |
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