AREMENIA

FINANCIAL SECTOR ASSESSMENT

June 9, 2009

TABLE OF CONTENTS

I. INTRODUCTION AND EXECUTIVE SUMMARY

USAID/Armenia is currently assisting Armenia's financial sector with technical assistance provided through a contract administered by Emerging Markets Group. This project, entitled Financial Sector Deepening Program (FINREP), which started in October 2006, will end September 2009.[1] The Mission's financial sector counterparts including the Central Bank, the Ministry of Finance, the Union of Armenian Banks, requested that the Mission consider providing further assistance through a new activity that would continue the principal tasks of FINREP. The Mission decided that to properly design a new financial sector activity it would conduct an assessment with the help of USAID's financial sector experts in Washington. It decided to have a broad assessment to ensure in order to gain a fresh look at the sector and to adjust the financial sector program to the constraints of decreases in the overall budget levels of the Mission. More specifically, the Mission set forth the following questions for the Assessment Team to answer:

- What elements are missing in Armenia's financial market infrastructure that limits fulfillment of its role in supporting growth of the real economy?
- Is the absorptive capacity of the financial sector an issue?
- Given USAID budget realities, what are the key areas of the financial sector that USAID needs to focus on to fulfill its goal of 'Increased Access to Finance'?
- What are the most promising areas for USAID interventions?
- What mechanisms should USAID consider employing?
- Is there a credible strategy that will allow USAID to phase out and exit from assistance to the financial sector in Armenia? Are there meaningful opportunities for public private partnerships?
- Has the current worldwide financial sector crisis affected the financial sector of Armenia? If yes, then what would be possible intervention that UAID could initiate to cushion the effect of the crisis?

The Mission underscored the importance of the question regarding 'access to finance' especially regarding SMEs. The Mission noted that SME expansion and hence the economic growth is usually constrained by limited access of businesses to financial services. Without access to finance SMEs, in particular, will not succeed in their drive to build productive capacity, acquire or absorb new technologies, nor can they expand to compete in global markets or even strike business linkages with larger firms. Access to finance allows smaller firms to benefit both in terms of entry and realizing growth possibilities. Inclusive financial systems also improve the composition and competition in the private sector. Finally, the poor may benefit from having jobs and higher wages, as better developed financial systems improve overall efficiency and promote growth and employment. In sum, the improved access to finance enhances the economic development, creates more employment opportunities and enhances the economic development.

[1] For detailed information on the Financial Sector Deepening Project refer to www.fsdp.am.

This report will proceed in the following fashion:

1. The **Introduction and Executive Summary** will include a description of the assessment methodology, general findings, and recommendations.

2. The **Financial Sector Development Assessment** will review Armenia's financial sector before and currently in economic crisis.

3. The section on **Mechanisms** will review the several mechanisms that the Mission should consider in proceeding with a new financial sector program.

4. The Team lays out the **Priorities** that emerge from its assessment.

5. The Team responds to the Mission's **Questions and Answers** set forth for the Team's guidance.

6. The Team lays out the Options that the Mission should consider given the **Priorities,** the available **Mechanisms**, and a straight-line budget and an increased budget.

7. The Teams makes its **Recommendations** in light of its findings.

The Mission assembled the Assessment Team of Haikanush Bagratunyan, Hugh Haworth, Roberto Toso, and Karen Dallakyan.[2] The Team conducted this review based on the Financial Sector Assessment Framework presented in **Appendix A**. The review combines an examination of financial sector development indicators as advanced by EE.EG.MT and a specific examination of the impact of the global financial crisis advanced by Chemonics International (**Appendix C**), along with an extensive set of interviews. The Team conducted the field work for the Assessment, April 6-23, 2009.

From the assessment it is readily apparent that two overriding financial sector issues face Armenia at this time, both stemming from the impact of the global financial crisis.

The first issue is the lack of decisive 'technical' leadership in a few key areas needed to restore confidence in the financial and economic system of Armenia.

> There is no question that there are highly talented officials in the government and in the Central Bank of Armenia (CBA) who are doing well in responding to the economic crisis. Yet their response appears to be a set of stop-gap measures that will only provide short-term fixes and not address the more troubling underlying problems of the financial system and the economy at large. For example, lending in the local currency will not occur soon unless the CBA offers a hedge to banks in order to overcome their aversion to lending in Armenian dram (AMD). The CBA is willing to entertain this idea, but does not have the confidence, and outside counsel, to start the effort. Another example is the

[2] Ms. Haikanush Bagratunyan, Financial Sector Specialist; Hugh Haworth, Senior Financial Market Advisor; Roberto Toso, Director, Chemonics Internaional; and, Karen Dallakyan, banking expert on loan from HSBC Bank, Armenia.

popular cynicism that the response of the government to the crisis will favor large, well-connected business interests and will have little impact on improving the status and condition of those who are not equally favored by the current system.

The second issue is the lack of credit lines during the crisis and beyond.

During the next year and possibly beyond, considerable attention is needed to increase credit from the current depressed levels in order to forestall a further worsening of the economic situation. The problem of limited access to credit did not begin with the crisis, but existed well before it. This problem reflects numerous challenges in the financial sector such as inadequate size, efficiency, and reach of the financial sector as well as the preparation of enterprises, especially SMEs, to obtain credit when they have not developed adequate business and financial plans.

The third issue is the financial system's market foundation problems

Access to credit has been a problem even before the crisis and this reflects numerous challenges in the financial infrastructure related to corporate governance, accounting, financial disclosure, creditors' rights, foreclosure procedures, and movable property registries. To address these challenges requires that banks, non-bank institutions and the financial authorities establish an agenda of specific reforms that can be resolved by collaboration and commitment among the public and private sectors, coupled with appropriate outside expertise.

The fourth issue is the need to develop long-term financing, institutional investors, and support of pension reform

Pension reform cannot proceed except on paper without the availability of domestic capital. Therefore, all bond markets need to be resuscitated: government, sub-sovereign, and corporate. Also, contractual savings through insurance programs are essential. Asset managers and institutional investors are required to intermediate between pension funds and capital sources. All these reforms are needed and, when implemented, will serve to provide long-term financing sorely needed by enterprises both large and small in Armenia.

The fifth issue is the development of professional skills across the financial sector

Financial sector professional development programs have been developed for actuaries and risk managers, but they are in very early stages. Furthermore, financial analysts, internal auditors, and internationally certified accountants are needed. The CBA has singled out this need as a clear requirement for progress in the development of the financial sector and specifically asked for assistance in developing sustainable programs for training these professionals.

The Assessment Team recommends that USAID address these five challenges through a new financial sector program that includes the establishment of three public-private partnerships.

The Mission should consider a three-part financial sector program for the coming four years. It would consist of the Mission buying into EGAT's FS Share Program to gain a macroeconomic-stress expert for nine months, who will provide the quick response to the crisis that is required to restore the near-term confidence in Armenia's financial system. The second part is contracting a follow-on activity to the soon-to-be-completed Financial Sector Deepening Program. The new contracted program will be able to address all five financial sector priorities outlined in the Assessment. Part Three is the establishment of three pubic-private partnerships: the World Bank's Modernization Program, the Center for Entrepreneurship and Executive Development, Small Enterprise Assistance Fund. These PPPs will be able to provide a sustainable response to critical challenges to Armenia's financial sector including the lack of efficiency and responsiveness of the financial system. It will be better if the Mission made the proposed contractor as the umbrella for the three public-partnerships to help in the establishment of the PPPs and monitoring their performance.

II. ARMENIA'S FINANCIAL SECTOR DEVELOPMENT

II.a. FINANCIAL SECTOR DEVELOPMENT OVERALL (PRE-CRISIS)

In 2008, Armenia ranked 19 of 28 transition economies, according to the Financial Sector Development Indicators (see Appendix B).

The ranking is a composite of the indicators for the macroeconomy (4 indicators), the market foundation for the financial sector (8 indicators), banking reforms and progress (5 indicators), bank size and efficiency (5 indicators), NBFI reforms and progress (5 indicators).

Up to the crisis, the macroeconomy had been strong in most respects with the clear exception of the current account deficit and structural reforms.

Two macroeconomic indicators were exceptionally strong: the five-year average growth rate in the GDP was 11.6% at the end of 2008 and average inflation over the same period was 3.8%.

One area of concern within the macro-economy prior to the crisis was the current account deficit, which, at 12.6% relative to GDP, indicates that the country is vulnerable to economic downturns if the terms of trade were to move against it.

Bankers, businessmen, and civil society counterparts interviewed as part of the assessment commented on the fact that the government has not adequately pursued structural reforms (e.g., competition policy, tax and customs, trade barriers). The government indirectly agreed with some of these observations. In the government's request for a stand-by agreement with the IMF, the authorities stated they "will continue its wide-ranging structural reform agenda.…. a key area will be continued effort to strengthen the business environment, with a focus on tax administration reforms and the fight against corruption."[3] Outside observers note that the slowness of progress on the

[3] Republic of Armenia's Request for Stand-By Arrangement to the IMF, March 3, 2009, Page 14.

structural reforms undermine the attraction of Armenia for foreign direct investment (FDI). They contend that Armenia will not be internationally 'competitive' in attracting the necessary investment to not only weather the current economic stress but also to regain the growth necessary for long-term progress. These observers called for a greater public-private dialogue on macroeconomic policy and the structural reform agenda.

The EBRD pointed out in its 2008 Transition Report that the "procedures for registering property and licensing are more straightforward than in most transition economies. Nevertheless, the tax and customs administration is still a weak point and corruption remains a serious problem." [4]

In the same report the EBRD also highlighted the improved competition regulatory framework that came into force in April 2007 that granted the Competition Commission additional rights of inspection and imposed stricter sanctions for infringements of the Commission's rules. However, "the Commission continues to maintain a low profile, and there has, so far, been very little actual enforcement. In particular, in the import sector existing monopolies remain unregulated, thus limiting competition."[5]

A refection of the lack of progress on the structural reforms is the informal economy. Armenia is suspected to have one of the largest portions of its economic activity in the informal sector – about 46%. By this figure, it is ranked 16th out of 104 countries in terms of countries with the largest informal sectors. [6]

In terms of the foundation for financial system growth, Armenia ranks less favorably vis-à-vis its peers.

Armenia's score across the market foundation indicators averages 1.6 (out of 5), which compares with the average of 2.3 for Southeast Europe, and 3.6 for the Northern Tier. Of special note among this set of indicators is accounting and auditing (score 1.2), which is weak. Also two other indicators display areas of concern: strength of investor protection (score of 2.0) and the protection of minority shareholder's interests (score 1.7).

Ethical behavior of firms and investor protection indicators are below average. The legal rights index, which represents progress on bankruptcy and collateral procedures, appears to be moderately satisfactory but still remains of concern. And according to the EBRD, the secured transaction law is malfunctioning.

Throughout the financial sector, observers who were interviewed underscored the need for improved accounting, financial disclosure, and corporate governance. Additionally, observers called for improvements in the financial infrastructure in areas such as

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[4] See the EBRD 2008 Transition Report at Page 96.
[5] Ibid, Page 96.
[6] The definition and measurement of the informal economy is subject to considerable debate. One source for the 'latest' (2005) compilations provided here is NationalMasters.com-
http://www.nationmaster.com/graph/eco_inf_eco-economy-informal&int=-1,

collateral and movable property registries, foreclosure procedures, and the underpinnings to secured lending.

Investment into and by the financial sector is influenced in good part by the quality of accounting, auditing and reporting transparency and the ability of clients to gain redress through the legal system on commercial and financial matters.

In terms of banking reforms, Armenia is approximately average relative to its E&E peers.

The EBRD 2008 Transition Report scores on banking reforms in the E&E region show Armenia with a score of 2.7 (out of 5), which is the average for Eurasia but below the average for Southeast Europe and the Northern Tier (3.1 and 3.8 respectively). While the soundness of banking indicator, as perceived by independent observers, is average relative to peers,[7] the capital adequacy ratio was very high at the end of 2008 at 28%. This compares favorably with most countries, which averaged at or below 12% prior to the global financial crisis.

The Central Bank of Armenia became the unified regulator in October 2006 and has imposed regulatory reforms to strengthen and promote the financial system. It has implemented the first pillar of Basel II Accord provisions. The CBA has introduced risk-based supervision. In 2007, the government, with Central Bank leadership, adopted legislation on asset securitization and mortgage-backed securities to promote the development of the mortgage market, on anti-money laundering, on the disclosure of financial terms of consumer loans and bank deposits, and on the establishment of financial ombudsperson services.

In 2008, the CBA increased the reserve requirements on foreign currency deposits from 8 to 12% and guided the passage of a new law on cash transactions limits that will support the de-dollarization in the banking system.

By comparison, indicators for the size and efficiency of the banking sector are less favorable.

Currently the banking system comprises 22 relatively well capitalized banks. At the end of 2009 the total capitalization of the bank system was about 27% and the share of total assets and total loans was 29.1% and 16.9% of GDP, respectively. However, total banking sector assets to GDP is substantially below the transition economies' average of over 50%.

The amount of domestic credit generated by the banking system is one of the lowest among its peers with a figure of 8.7% relative to GDP. The average for all countries in the region is 35.3%. Even before the global financial crisis, the level of financial intermediation in Armenia's banking system was low.

[7] World Economic Forum Global Competitiveness Report, 2008-09, Page 298.

Deposits in the system amounted to about 15% relative to GDP through 2008. This compares to the CBA's estimate of dollar cash-in-circulation of about 35 % relative to GDP. Banks were not able to mobilize the domestic deposit base during the recent years of strong economic growth. A good part of this problem relates to the historical experience in the initial chaotic years after independence.

In 2007, Era Dabla-Norris and Holger Floerkemeier for the IMF conducted an empirical study of Armenia's bank efficiency and market structure.[8] They concluded the Armenia's banking sector's productivity is low by international comparison, which indicates that there is still room for consolidation, cost rationalization and technological progress. In this respect, a competition policy that fosters bank growth and cost rationalization, for example through mergers and acquisition and/or the entry of first-tier international banks, can help to reduce lending rates and spreads. Consolidation of the banking sector should, however, proceed through a market-driven process rather that through regulatory measures such as further increase in minimum capital requirement, that are already comparatively high in relation to the current size of the banking system. A successful competition policy should aim to reduce market segmentation, increase market transparency, and create a level playing field for all market participants.

Of special note is the low score of ease of access to loans. Armenia scores near the bottom, although it should be noted that the data for three of the five indicators in this category date back to 2005 and should be treated with caution.

The non-bank financial institution indicators for Armenia demonstrate an early stage development of the sector.

The EBRD indicator for non-banking sector reforms was 2.3 (out of 5) in 2008, which is nearly equal with Eurasia overall and the average for Southeast Europe. Yet, all other indicators are low. The indicator for the market value of listed securities is in the lowest quintile of the transition economies.

OMX/NASDAQ, at the end of 2007, acquired the Armenia Stock Exchange. The acquisition will provide for support for the development of the capital markets going forward. It should open up funding opportunities for larger enterprises. The government has supported stock-market capitalization through a recent legislative package on capital market development that includes tax breaks for companies that list on the stock exchange.

Various observers interviewed stated that the non-bank financial institution sector is providing neither competition to the banking sector nor a capital cushion to the banking sector. Further, they noted that there is a dearth of financial products, especially those that have tenors beyond a year. They underscored the weakness of the insurance sector and the securities market. They lamented the fact that these sectors were not sufficiently developed to act as a cushion for the banking system when it is most needed, during a financial crisis as the country is currently experiencing. Further, they pointed out the

[8] Era Dabla-Norris and Holger Floerkemeier, "Bank Efficiency and Market Structure: What Determines Banking Spreads in Armenia?", IMF Working Paper, WP/07/134, June 2007

criticality of having developed insurance and securities markets for the success of the upcoming pension reform program.

IIb. FINANCIAL SECTOR ASSESSMENT IN LIGHT OF THE CRISIS

One of the Assessment Team, Roberto Toso, and his Chemonics International colleagues, conducted a specific, detailed financial crisis assessment, which has been incorporated here as part of the overall Financial Sector Assessment. Please turn to Appendix C for their "Rapid Financial Crisis Assessment Final Report: Armenia."

It is clear that the Armenian economy was and will continue to be deeply affected by the global financial crisis.

Up until late 2008 the Armenian leadership declared confidently that the country would remain relatively isolated from the turmoil of the global financial crisis. This seemed somewhat improbable to many, but the dimensions of the impact were unclear. Remittances had already started to decline towards the end of 2008. On March 3, 2009, the AMD lost 30% of its value in a single day. The Central Bank stopped supporting the currency. The government and the IMF began discussions on a stand-by loan on the order of $540 million. The IMF projects that the GDP for 2009 will drop by 1.5%. Others place the figure closer to a 5% decline.[9] Remittances, which make up 20% of Armenia's GDP, were down 40% in February 2009 from a year earlier. Export revenue in March 2009 was down 51% from a year earlier. First quarter figures for construction show a 21% decline from a year earlier. International prices of Armenia's major exports such as copper and molybdenum in the first quarter of 2009 are about one half of the levels of a year earlier.

The short-term macro-economic outlook is very challenging.

The significant slowdown experience by Russia and other countries will cause remittances to be well below the levels of recent years, with a negative impact on domestic demand. Activity in the construction sector is expected to decelerate dramatically, and difficulties in mining are bound to persist. According to the IMF, "a gradual recovery may be possible starting in 2010, depending on global developments, but downside risks are prevalent."[10]

Currently, the financial sector is under stress.

Despite high capital adequacy ratios of 27.9%, which are over twice the minimum requirement of 12%, and low levels of non-performing loans, banks appear to be

[9] IMF, May 10, 2009 press release
[10] IMF Staff Report – republic of Armenia's request for Stand –By arrangement, IMF Country Report No. 09/140, May 8, 2009, Page 11.

vulnerable to liquidity problems. This reflects the fragile confidence of the public in the banking system due to previous episodes of devaluations and bank runs in Armenia.

There is a dram shortage in the banking system.

Banks have reduced their lending activities in AMD, particularly by not rolling over such loans as they fall due, and are attempting to pass the exchange rate risk to borrowers by switching to dollar loans. Currently, AMD lending is now largely funded by a number of IFI initiatives to promote local currency lending to the SME sector.

In the Assessment Team's interviews, counterparts stressed the nearly catastrophic problems created by the rapid devaluation of the AMD in March 2009.

For months proceeding the sharp fall in the AMD there was a growing apprehension of the pending devaluation. Bank clients were able to transfer the vast majority of their deposits from AMD accounts to hard currency accounts or FX, chiefly USD dollar, accounts. Bank balance sheets suffered. Their deposit base shifted from roughly 75%-25% in AMD-FX to the reverse of nearly 25%-75% in AMD-FX. Meanwhile, banks' outstanding loans remained principally AMD denominated. Due to this low AMD deposit base and great uncertainty about the strength of the AMD, banks have almost completely stopped further lending in dram, thus causing their principal source of profits to plummet. As most businesses and consumers cannot borrow in FX, the lack of credit available through AMD loans will affect their ability to stay afloat. A vicious downward spiral has begun.

Bankers and the IFIs noted that the new special donor SME lending facilities will help considerably if they are fully utilized.

They noted however that many, if not the vast majority, of SMEs seeking these special loans will not qualify without assistance, due to poor financial reports and weak credit applications. This will become a growing problem in the efforts of the government and IFIs to restore credit, especially to this highly vulnerable group. Further, observers in the government and the IFIs noted that the ability of the government and the bankers to create and maintain credit guarantees and subsidy programs necessary to weather the crisis will become a large issue.

Trade finance has been handled by very few financial institutions in Armenia.

Up to the global financial crisis trade finance was conducted, in largest part, by foreign banks, in some cases, through Armenian subsidiaries or correspondent banks. Now, with the crisis, the foreign banks have cut back their involvement with Armenian banks, traders, importers, and exporters. There may be potential for generating more trade finance within Armenia given proper skill development, which will prove to be invaluable if there will be further global financial stress.

II.c. FINANCIAL SECTOR RATINGS

Table A below summarizes the data available to the Assessment Team from the statistical sources and the interviews.

> One can see that all but the third component, Bank Supervision, represent challenges that need to be addressed in order to advance Armenia's financial system to the level needed by the economy. The first component, macroeconomic, is of special note because it is here where much of public cynicism arises. USAID cannot easily assist Armenia with challenges such as the structural issues (e.g., competition policy). However, there are opportunities to assist on very specific, short-term matters such as developing and implementing a hedging mechanism to engender greater lending in the near term. This will be received with considerable enthusiasm.

The sixth component, the corporate sector's access to credit, is of great significance in the current environment.

> The issue here is the lack of preparation or 'bankability' of so many of the SMEs, which is both a short-term and a long-term challenge. In the short-term SMEs are not able to qualify for the new on-lending facilities funded by the World Bank and other donors. It is also a long-term challenge in that there needs to be a systemic response to reach the many SMEs that are not receiving proper training (e.g. business and financial planning, marketing).

TABLE A: FINANCIAL SECTOR ASSESSMENT RATINGS

Development Areas ** denotes crisis-sensitive topic*	**Rating** **1 = worst** **5 = best**	**Comments**
1. Macroeconomic ***(Public Sector Financial Soundness)***		
• Fiscal and current account balances, exports, taxes, external debt*	**2.0**	• Rapidly declining remittances, exports, and rising current account deficit has weakened what had been a relatively strong macroeconomic picture.
• Monetary policy, currency, international reserves, hedging, strategy*	**3.0**	• Now the IMF and CBA have good policies in place; nevertheless, currency volatility has to be addressed by hedging mechanisms for increased lending.
• Structural reforms, e.g. competition policy, tax and customs	**2.0**	• Lack of meaningful competition and open trade is a burden to the economy and affects the financial sector.
2. Financial Sector Foundations and Infrastructure *(Market Foundation)*		
• Legal rights for sector: bankruptcy, foreclosures, collateral, secured lending, creditors rights, dispute resolution	**2.0**	• Legal rights are lacking in some instances; where they are adequate they are poorly and unevenly implemented.
• Corporate governance, financial disclosure, minority shareholder rights, accounting, actuary, secured lending, collateral and bankruptcy	**2.0**	• Corporate governance has not become a common practice, except for a small number of banks and companies.

• Professional and professional association development: accounting, actuary, banking, insurance, asset and risk management • Credit information systems, payment systems • Public awareness & financial literacy*	**2.5** **3.5** **1.5**	• Professional development of sector experts is constrained by support from the industry. • The credit bureau is working well. • Financial literacy is low.
3. Bank Supervision and Reform *(Regulatory Institutional Strength)* • Legal and regulatory, supervision, enforcement, inspections, risk and crisis management, deposit insurance* • Banking sector soundness* • Bank rehabilitation*	**3.5** **3.5** **3.0**	• The unified financial sector regulatory, the CBA, has been progressive and capable. • Banks are very well capitalized. • The CBA has managed bank rehabilitation well, chiefly through mergers and acquisitions.
4. Bank Size, Efficiency, Soundness, and Competition • Size, efficiency, competition of banking • Soundness • Access to finance: supply-side development of credit, credit guarantees, subsidies, asset-based finance (warehouse receipts, purchase order, factoring), outreach, scoring, technology enhancements*	**1.5** **2.5** **2.0**	• The banking system is passive, not competitive or efficient. • Banks had high capital levels, good asset quality, earnings, and liquidity. Now there is serious stress and concern with capital levels looking only adequate for the time being with no further deterioration. • Many instruments that should be available to finance business are weakly developed.
5. Non-Bank Financial Institutions *(NBFIs)* • Legal, regulatory, supervision, enforcement, inspections, risk and crisis management • MSME finance (supply-side development) • Bond markets (government, sub-sovereign, corporate) and equity markets* • Pension reform, institutional investing, asset management • Insurance (e.g., motor vehicle, employers, health)	**3.0** **2.0** **1.5** **2.0** **1.5**	• The regulation of the NBFI sector is adequate. • Only a few institutions are capable of offering meaningful financial services to SMEs. • Bond and equity markets barely started to form before a dormant period with the crisis. • Pension reform is underway but still in its earliest stages. • Insurance is nascent.
6. Corporate Sector Financial Condition and Access to Finance • Corporate structure • Corporate earnings, profits, and	**2.0** **2.0**	• Large enterprises are generally monopolistic • Companies are severely impacted by the

leverage • SME access to finance: development of enterprises, bankability, business and financial plans*	**2.0**	crisis with declining sales and earnings • Armenian enterprises have not borrowed internationally, shielding them from current global financial turmoil. For SMEs access to finance has been poor, even domestically; most are ill-equipped to attract and gain commercial financial services.

III. NEAR- AND LONG-TERM PRIORITIES

Table B summarizes the development priorities facing Armenia's financial sector. Development and crisis priorities are determined on the basis of three criteria:

1. What are the critical gaps in Armenia's financial markets that are not being adequately addressed and in which USAID can make a difference?
2. Can these gaps be addressed given the Mission's human resource and budgetary limitations?
3. Do the counterparts have the capacity and commitment to succeed in addressing the subject challenges?

TABLE B: FINANCIAL SECTOR DEVELOPMENT PRIORITIES, NEAR- AND LONG-TERM

Development Areas	Near-Term Priority	Long-Term Priority
1. Macroeconomic *(Public Sector Financial Soundness)*	**High priority**. The government needs to restore confidence and point the way to economic and financial recovery. Key to success here will be the development of a hedging mechanism to 'restart' lending in dram and optimizing the various special credit facilities sponsored by the government and the IFIs.	**Low priority** for financial sector activity. Macroeconomic structural reforms (e.g. competition and trade policies, tax administration) are clearly needed. But, a separate program outside the financial sector sphere will be the better way to proceed.
2. Financial Sector Foundations and Infrastructure *(Market Foundation)*	**High priority**. Improving the financial market foundation through better foreclosure procedures and better creditors' rights are essential. But, the solution is a long-term public-private partnership established to properly address the complex issues attendant here.	**High priority**. Support professional development of risk managers, actuaries, and asset managers, and financial analysts as requested by the CBA.

3. Bank Supervision and Reform *(Regulatory Institutional Strength)*	**Not a near-term priority.** The CBA has been cautious and firm in administering prudential regulation and capital requirements.	**Medium-level priority.** Over the coming years, risk-based supervision will need to be enhanced and less reliance given to high-level capital requirements.
4. Bank Size, Efficiency, Competition, and Modernization	**This is a long-term phenomenon.**	**High priority.** The small size of the banking system and the limited access to credit reflects low competition and efficiencies in the sector.
5. Non Bank Financial Institutions	**Low priority**. The CBA regulates this sector well. Development of the market is a long-term priority.	**High priority**. The capital markets give neither capital cushion nor competition to the banking sector. Pension reform will not proceed without the expansion of the insurance industry, securities markets, the development of venture capital and institutional investors.
6. Corporate Sector Financial Condition and Access to Finance	**High priority.** SMEs will need assistance to gain credit by preparing better business and financial plans.	**High priority.** Continued attention to improving SMEs' 'bankability'

Five major priorities emerge from the ratings and the interviews.

Priority #1: Restoration of confidence in the economy and in the financial sector

The first is the restoration of confidence in the economy and in the financial sector during the crisis and beyond. All observers are fully aware that the global economic contagion cut external demand for Armenian goods and services, which is the principal reason for the financial stress in the country now. Furthermore, they realize that the banking system is relatively strong and will weather the crisis without significant support from the government. At the same time, the banking system is passive, not competitive, and will not provide meaningful, critically needed long-term financing. In the end, observers contend that without significant structural reforms to provide the basis for a stronger, more robust recovery and for a diversified, more competitive economy, the financial sector will remain passive. What is needed is 'technical' leadership. GOAM and the CBA have talented leaders, but lack the innovation necessary to restructure the economy, especially the financial sector. A key example of what is needed is the implementation of a hedging mechanism to unleash dram-denominated lending while the currency is viewed as too risky to use. Another example is the establishment of long-term funding sources to do project financing for trade, industry, infrastructure, and agriculture. Proper direction of the ongoing pension reform will support the demand side of the long-term financing challenge. Furthermore, the government needs to support the demand side of the equation by promoting more open capital participation in the banking system and public infrastructure projects. Also, better conditions for insurance programs, e.g. employers, health and life insurance, are needed, which are a solid source of the needed capital.

Leadership is required to articulate this as a package of inter-connected reforms and to carry the reforms through to fruition.

Priority #2: Restoration of credit and access to credit by supporting the newly created special facilities

The second priority is the restoration of credit lines during the crisis and access to credit generally. For a period extending through 2010 and possibly beyond, considerable attention should be devoted to this matter. In the near term, the government will need to ensure that its own special credit facilities and the donor-sponsored ones are being utilized to the fullest extent possible. Some observers have contended that these facilities are too complex and difficult to use, an issue that needs to be addressed. Equally important is the fact that most potential borrowers, especially the SMEs, are ill-prepared to garner loans. They have inadequate business and financial plans, and thus are mostly 'un-bankable.' Special effort will be required to facilitate better loan applications in the near term.

Priority #3: Address the financial system's inefficiency and market foundation problems

Access to credit has been a problem even before the crisis. This reflects numerous challenges in the financial sector, such as the lack of adequate size, efficiency, and reach of the financial sector as well as deep-seated problems in the financial infrastructure related to creditors' rights, foreclosure procedures, and movable property registries. Thus, the third priority is to address the system's inefficiency and market foundation problems. This requires that banks, non-bank institutions and the financial authorities establish an agenda of specific reforms that can be resolved by collaboration and commitment, coupled with appropriate outside expertise. Often, authorities do not realize how costly the lack of certain protections for creditors can be and how those additional costs can reduce the credit flowing to business.

Priority #4: Combine pension reform with the development of long-term finance

The fourth priority is bringing the pension reform and the development of long-term finance together, noted above under macroeconomic leadership. Pension reform cannot proceed except on paper without the availability of domestic capital. Therefore, all bond markets need to be resuscitated: government, sub-sovereign, and corporate. Also, contractual savings through insurance programs are essential. Asset managers and institutional investors are needed to intermediate between pension funds and capital sources. If they are not developed, pension contributions will go only into a 'government savings account' or a non-tradable government bond equivalent, or they will be invested overseas. Clearly, the preferred route is to have the financial markets of Armenia invest in private enterprise and public projects funded through transparent capital market operations.

Priority #5: Develop financial sector professional skills

The fifth priority is the development of the professional skills in the financial sector. Programs have been started recently for actuaries and risk managers, but they are in very early stages. Furthermore, financial analysts, internal auditors, and internationally certified accountants are needed. The CBA has singled out this need as a clear requirement for progress in the development of the financial sector and specifically asked for assistance in developing sustainable programs for training these professionals.

IV. DEVELOPMENT MECHANISMS

Over the past six years USAID/Armenia has devoted significant resources to developing the required infrastructure for a modern financial system, and these efforts have helped put in place the building blocks for a potentially effective, dynamic system.

The Mission launched the Financial Sector Deepening Project (FSDP) in October 2006, which has succeeded in many respects. FSDP is scheduled to complete its mandate in September 2009. It is a broad, comprehensive project designed to contribute to improving the efficiency and viability of financial markets, introducing a wider array of products in banking, mortgage insurance, and private pensions. It also assists the Central Bank in its efforts improve the soundness, safety, stability and integrity of the financial sector. FSDP has also supported advances in accounting and auditing sectors. The CBA, market participants that have been supported by FSDP, and donors have all praised the Project. The quality of technical expertise provided to counterparts has been key to the advances in many vital programs such as risk-based supervision, development of the actuarial profession, the preparation and qualification of commercial banks for the World Bank SME on-lending facility. The CBA specifically praised the legal and regulatory drafting FSDP has conducted in the areas of risk-based supervision, accounting and pension reform. There is little question that a follow-on contract to continue the unfinished agenda makes sense in several scenarios that will be discussed below.

Looking forward, USAID/Armenia should consider contracting for a follow-on activity for the Financial Sector Deepening Project.

This way the Mission can address all the financial sector development and crisis priorities that it chooses to address with maximum control and responsiveness. A follow-on contract can also serve as the umbrella program for launching all public-private partnerships that the Mission will undertake in the financial sector.

The Mission should consider utilizing the EGAT Financial Sector Share Program.

EGAT created FS Share as a mechanism for disseminating knowledge about financial sector development and lessons learned by USAID in conducting financial sector development programs. FS Share has a mission buy in feature for obtaining rapid response expertise on any financial sector issue; such buy ins, though, are of a shorter duration of up to six to nine months in duration. USAID/Armenia has already employed FS Share as a mechanism to conduct the Rapid Response Financial Sector Assessment, which was provided in May 2009 and is attached here as Appendix C.

The Mission should also consider supporting the World Bank Modernization Program (WBMP), a public-private partnership that will address a range of issues but will focus principally on increasing the efficiency and efficacy of financial sector institutions.

> This platform provides project development skills to the public and to the private side of the financial sector to address key challenges such as increasing finance to SMEs, adopting industry-wide credit-scoring techniques, and reducing foreclosure delays through commercial services. See the WBMP website: http://www.spi-romania.eu/convergence-program.

The Mission should also consider lending support in the establishment of a Center for Entrepreneurship and Executive Development (CEED).

> This public-private partnership is a platform that stresses directed, targeted training to successful SME executives who reached a critical juncture in their development. Through demand-driven, short-term, focused training and extensive mentoring, executives in CEED centers in Southeast Europe have demonstrated the value of the program through accelerated growth of their members and a self-sustainable institution within three years. Access to credit is one of CEED's three major objectives. Through seminars, consultancies, and venture forums, CEED provides a roadmap for gaining finance, and connecting with potential investors. See CEED's website: http://www.ceed-global.org/web/default.aspx.

Another public-private partnership that the Mission should consider supporting is the Small Enterprise Assistance Fund (SEAF).

> SEAF funds have been established in many countries of Eastern Europe and Eurasia but not in the Caucasus. SEAF are venture capital funds that invest in SMEs with mezzanine financing and equity, serve on the boards of the companies, and mentor their growth until SEAF can sell their stake profitably. SEAF is currently preparing to establish a single fund for all three countries of the Caucuses. See the SEAF website: http://www.seaf.org.

The Mission should consider further use of the Development Credit Authority (DCA).

> The Mission has provided credit guarantees to Armenian banks so they will on-lend with greater confidence to SMEs. These have been moderately successful to date. The Mission is considering additional credit guarantee options to provide targeted funding to enterprises in three or more targeted sectors that the government has identified as having the greatest potential for raising Armenia's competitiveness (e.g., information technology, tourism, pharmaceuticals). The World Bank, the government, and the Central Bank, launched at the start of 2009 a $50 million special facility for enhanced lending to SMEs. With this special, rather large program, there is less need for USAID to consider a DCA credit guarantee program for SMEs until initial results are available from the World Bank facility.

The last PPP that the Mission should consider is the E&E Bureau's regional program -- Partners for Financial Stability (PFS).

> PFS has provided work shops and study tours for Armenian financial-sector professions over recent years. E&E is currently recasting PFS to be more responsive to the needs of missions in light of the global financial crisis. It will also provide rapid response facilities for missions who will buy in to the program on an-as-needed basis. See the PFS website: http://www.pfsprogram.org

V. OPTIONS FOR APPLYING MECHANISMS AGAINST PRIORITIES

The Assessment Team has crafted three options for addressing the financial sector priorities in Armenia.

> The Mission faces trade offs when attempting to address all the priorities for financial sector assistance that are evident, while crafting solutions to the sector challenges that are sustainable, and, all the while, facing restrained budgets. The Mission can contract a follow on activity that can address all the challenges set forth in the assessment. Contracts provide flexibility and precision in developing the responses the Mission will want to undertake. Contracts, on the other hand, do not provide the sustainability that public-private partnerships (PPPs) do. Public-private partnerships, conversely, are targeted responses with limited focus. Furthermore, PPPs are not well suited to 'mentor' government institutions. Thus, a combination of a contract and the generation of public private partnerships will be the optimal solution.

OPTION ONE: CONTRACT FOR A FOLLOW-ON TO THE FINANCIAL SECTOR DEEPENGING PROJECT

Develop a follow-on project to the Financial Sector Deepening Project (FSDP) to address all five priorities set forth in the Assessment.

> As noted above contracts can be crafted to handle any or all of the development priorities the Mission wants to undertake. Thus, the Mission should consider contracting a follow-on activity to FSDP for that purpose. Given the global financial crisis has added a sense of urgency to restoring confidence in the financial system, the Mission may want to use in the nearest term EGAT's FS Share Program to obtain the services of the macroeconomy-stress expert to address pressing matters including the development of hedging mechanisms to restore lending in dram.

OPTION TWO: ESTABLISH THREE PUBLIC-PRIVATE PARTNERSHIPS

The mission should consider establishing the following four PPPs:

- **World Bank's Modernization Program.** WBMP will be able to address two sets of challenges that are central to increasing access to credit: 1) market infrastructure challenges; and, 2) the efficiency and responsiveness of financial intermediaries.
- **Center for Entrepreneurship and Executive Development.** CEED will be able to provide targeted training to successful SME executives who have reached a critical juncture in their development, especially their ability to access financial services.
- **Small Enterprise Assistance Fund.** A SEAF will serve as the venture capital that is keenly sought in Armenia. SEAF will be able to invest in SMEs with mezzanine financing and equity, serve on the boards of the companies, and mentor their growth until SEAF can sell their stake profitably.

OPTION THREE: COMBINE OPTIONS ONE AND TWO

The Mission should consider combining Options One and Two by buying in to FS Share to gain the quick response to the crisis that is recommended here. At the same time, the Mission should contract a follow-on activity to FSDP that can address all five financial sector priorities outlined in the Assessment. The contractor will be able to serve as the umbrella for all public-partnerships by assisting the Mission in establishing the PPPs and monitoring their performance.

VI. ANSWERS TO MISSION'S QUESTIONS, AND RECOMMENDATIONS

- **What elements are missing in Armenia's financial market infrastructure that limits fulfillment of its role in supporting growth of the real economy?**

  Apart from the credit bureau and payment systems, all other elements of the market infrastructure are weak or relatively weak. This includes accounting, corporate governance, creditors' rights, and foreclosure procedures. These infrastructure challenges represent serious obstacles to the development of Armenia's financial sector.

- **Is the absorptive capacity of the financial sector an issue?**

  There may be a question of absorptive capacity with certain counterparts apart from the Central Bank. However, it appears that commitment and policy environment may be playing a larger role in restraining development in many areas of the financial sector.

- **Given USAID budget realities, what are the key areas of the financial sector that USAID needs to focus on to fulfill its goal of 'Increased Access to Finance'?**

  With limited resources, the key areas of focus for the Mission should be the following: creation of hedging mechanisms to increase lending in dram; addressing infrastructure challenges, especially creditors' rights, foreclosures (lower risks), credit scoring; increasing bankability of SMEs; and, enhancing the use of the special SME finance facilities already provided by the donors. With greater resources, the Mission should also address support for institutional investing and the development of long-term financing instruments, followed by added assistance to professional development of key sector experts such accountants, actuaries, and risk managers.

- **What are the most promising areas for USAID interventions?**

  The Central Bank of Armenia has stated its priorities for assistance from USAID: accounting, actuarial training, and pension reform. Given the prominence of the CBA in the development of the financial sector, the greatest likelihood of success lies in the areas where the Central Bank is the champion. On the other hand, the CBA may be open to addressing the other priorities that are spelled out here in the Assessment. If the CBA is willing to work with USAID on all five priorities the goal of "Increased Access to Finance" will be achievable.

- **What mechanisms should USAID consider employing?**

  The Assessment Team described above numerous mechanisms and combinations of mechanisms that could be employed. The Mission should consider using at the minimum a contract for a follow-on activity and the establishment of three PPPs detailed in the Options Section.

- **Is there a credible strategy that will allow USAID to phase out and exit from assistance to the financial sector in Armenia? Are there meaningful opportunities for public private partnerships?**

  Yes, as noted above, there are several meaningful opportunities for establishing PPPs that will pave the way for the Mission to exit from assistance to the financial sector. What the PPPs cannot do is assist the government address the macroeconomic issues that are undermining confidence in the financial sector during the crisis. That will require a contract.

- **Has the current worldwide financial sector crisis affected the financial sector of Armenia? If yes, then what would be possible intervention that UAID could initiate to cushion the effect of the crisis?**

  Yes, the crisis has frozen credit. The Mission should respond to Development Priority #1, restoration of confidence in the financial sector by addressing the macro-economic challenges; and, Priority #2, increasing access to credit by supporting the newly created special facilities that will increase lending to SMEs. These are the most immediate responses that will help cushion the effect of the crisis.

VII. RECOMMENDATION

The Assessment Team recommends that USAID address these five challenges through a new financial sector program that includes the establishment of three public-private partnerships.

The Mission should consider a three-part financial sector program for the coming four years. It would consist of the Mission buying into EGAT's FS Share Program to gain a macroeconomic-stress expert for nine months, who will provide the quick response to the crisis that is required to restore the near-term confidence in Armenia's financial system. The second part is contracting a follow-on activity to the soon-to-be-completed Financial Sector Deepening Program. The new contracted program will be able to address all five financial sector priorities outlined in the Assessment. Part Three is the establishment of three pubic-private partnerships: the World Bank's Modernization Program, the Center for Entrepreneurship and Executive Development, Small Enterprise Assistance Fund. These PPPs will be able to provide a sustainable response to critical challenges to Armenia's financial sector including the lack of efficiency and responsiveness of the financial system. It will be better if the Mission made the proposed contractor as the umbrella for the three public-partnerships to help in the establishment of the PPPs and monitoring their performance.

VII. Acronyms

AMD	Armenian dram
CBA	Central Bank of Armenia
CEED	Center for Entrepreneurship and Executive Development
EBRD	The European Bank for Reconstruction and Development
E&E	USAID European and Eurasia Bureau
EGAT	USAID Economic Growth, Agriculture, and Trade Bureau
FDI	Foreign Direct Investment
FSDP	USAID/Armenia Financial Sector Deepening Project
FS Share	USAID EGAT Bureau's Financial Sector Share Program
GOAM	Government of Armenia
IMF	International Monetary Fund
IFI	International Finance Institutions
NBFI	Non-Bank Financial Institutions
PFS	USAID E&E Bureau's Partners for Financial Stability
PPP	Public-Private Partnerships
RFCA	Rapid Financial Crisis Assessment
SEAF	Small Enterprise Assistance Fund
SME	Small & Medium Enterprises
WB	World Bank
WBMP	World Bank Modernization Program

VIII. List of Interviews

ACBA-Credit Agricole. Stepan Gishyan, General Manager.

ACP-Armenian Copper Programme. Tigran Khachatryan, Chief Financial Officer.

Ameria Bank. Artak Hanesyan, General Director and Chairman of the Management Board. Levon Arevshatyan, Director Corporate Banking. Andrei Shikevich, CFA, Director of Investment Banking and Management Board Member.

American Chamber of Commerce in Armenia. David Atanessian, President.

Anelik Bank CJSC. Bagrat A. Tshzmachyan, Deputy Chairman of the Board.

Aregak Universal Credit Organization. Armine Aghajanyan, Finance Director.

Capital Asset Management. Tigran Karapetyan, General Director and Partner.

Cascade Investments. Haik Papyan, CFS, Executive Director.

Central Bank of Armenia. Dr.Vache Gabrielyan, Deputy Chairman.

Converse Bank. Ararat Ghukasyan, Chairman of the Management Board and Executive Director.

ERDC Research Center. Gagik Torosyan, Director.

Financial Sector Deepening Project. USAID. Martin Dinning, Chief of Party; Richard Webb, Resident Insurance Advisor; John Fitzgerald, Resident Banking Adviser; Edgar Karapetyan, Acting Team Leader.

First Mortgage. David Atanessian, Managing Partner & CEO.

HSBC. Tim Slater, Chief Executive Officer.

Inecobank. Avetis Baloyan, Chief Executive Officer. Anatoli Tirosyan, Department Head, Branch Network Coordination.

Insurance Association of Armenia. Paylak Ghukasyan, President.

International Finance Corporation. Nerses Karamanukyan, Head Office Yerevan.

International Monetary Fund. Nienke Oomes, Resident Representative in Armenia. Ara Stepanyan, Economist.

KfW. Dr. Karapet A. Gevorgyan, Representative in Armenia.

London-Yerevan Co Insurance Company. Aram Piruzyan, Managing Director.

Ministry of Economy and Development. Nerses Yeritsyan, Minister.

Ministry of Finance. Vardan Aramyan, Deputy Minister of Finance.

NASDAQ OMX. Armen Melikyan, CEO. Rouzanna Sarkissian, Head of Marketing and Communications.

Pro Credit Bank. Ashot Abrahamyan, Deputy Executive Director.

SME Association of Armenia. Syran Avagyan, President, Special Advisor to the President of Armenia on SMEs.

SME Development National Center of Armenia. Ishkhan Karapetyan, Executive Director.

SPI Albania. Ramona Vali Bratu, Albania General Manager.

The World Bank. Aristomene Varoudakis, Country Manager Armenia Office.

Unifish-Noy Fish LTD. Armen Mkrtchyan, Founder and President.

Union of Banks of Armenia. Emil Soghomonyan, Chairman; Seyran Sagsyan, Executive Director.

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X. Appendix A

Financial Sector Assessment Framework and Methodology

The Financial Sector Assessment (FSA) Framework examines six components that impact financial sector development: 1) macroeconomics; 2) market foundation; 3) bank supervision and regulatory strength; 4) bank size, efficiency, soundness, and modernization; 5) non-bank financial institutions; and, 6) the corporate sector financial condition.

The major sources of the information underpinning these ratings are: the World Bank's Financial Sector Development Indicator Program[11]; the World Economic Forum Financial Development Reports[12]; the European Bank for Reconstruction and Development Transition Reports[13]; Chemonics International Rapid Financial Crisis Assessment Program (Appendix C); and, most importantly, field interviews with key counterparts in the public and private sphere who responded to questions on the developmental and financial crisis challenges facing Armenia.

Financial Sector Assessment Framework

Development Areas ** denotes crisis sensitive topic*
1. Macroeconomic (Public Sector Financial Soundness) • Fiscal and current account balances, exports, taxes, external debt * • Monetary policy, currency, international reserves, hedging, strategy * • Structural reforms: competition policy, tax and customs, trade barriers
2. Financial Sector Foundations and Infrastructure (Market Foundation) • Legal rights for sector: bankruptcy, foreclosures, collateral, secured lending, creditors rights, dispute resolution • Corporate governance, financial disclosure, minority shareholders rights, accounting, actuary, secured lending, collateral and bankruptcy • Professional and professional association development: accounting, actuary, banking, insurance, asset and risk management • Credit information systems, payment systems • Public awareness & financial literacy *
3. Bank Supervision and Reform (Regulatory Institutional Strength) • legal and regulatory, supervision, enforcement, inspections, risk and crisis management, deposit insurance * • Banking sector soundness * • Bank rehabilitation *

[11] The World Bank's financial Sector Development Indicator website: http://www.fsdi.org/
[12] The World Economic Forum Financial Development Reports website: http://www.weforum.org/en/initiatives/gcp/FinancialDevelopmentReport/index.htm
[13] The European Bank for Reconstruction and Development Transition Reports website: http://www.ebrd.com/pubs/econo/tr08.htm

4. Bank Size, Efficiency, Soundness, and Modernization • Size, efficiency, competition of banking • Bank soundness • Access to finance: supply-side development of credit, credit guarantees, subsidies, asset-based finance (warehouse receipts, purchase order, factoring), outreach, scoring, technology enhancements *
5. Non Bank Financial Institutions • legal, regulatory, supervision, enforcement, inspections, risk and crisis management • MSME finance (supply-side development) • bond markets (government, sub-sovereign, corporate) and equity markets * • pension reform, institutional investing, asset management • insurance (e.g., motor vehicle, employers, health)
6. Corporate Sector Financial Condition and Access to Finance • Corporate earnings, profits, and leverage • Access to finance: demand-side development of enterprises, bankable SMEs, business and financial plans *

Appendix A (continued)

Financial Sector Assessment Interviews

Development Areas	Questions are open ended to garner unsolicited insights on the quality of the institutions involved in the specific component or sub-component indicated. Often they are based on quantitative and qualitative information provided in IFI reports on the financial sector. The insights gained from the interviews elaborate the ratings that are derived from quantitative sources.[14]
1. Macroeconomic *(Public Sector Financial Soundness)*	Questions are directed to how the macro economy is performing, how it is affecting the individual and institution, as well as eliciting suggestions on possible interventions by donors in assistance to the institutions that manage the macro economy.
2. Financial Sector Foundations and Infrastructure *(Market Foundation)*	Questions would be directed to the areas of specific interest to the interviewed party. For instance, accounting firms would be more appropriate to query about financial disclosure and corporate governance; while, financial institutions are more appropriate to query about the legal rights affecting their business transactions such as foreclosures, secured lending and creditors' rights.

14

- The World Bank's financial Sector Development Indicator website: http://www.fsdi.org/
- The World Economic Forum Financial Development Reports website: http://www.weforum.org/en/initiatives/gcp/FinancialDevelopmentReport/index.htm
- The European Bank for Reconstruction and Development Transition Reports website: http://www.ebrd.com/pubs/econo/tr08.htm

3. Bank Supervision and Reform ***(Regulatory Institutional Strength)***	Questions are based on the bank examination program called CAMEL (capital, assets, management, equity, and liabilities). Questions are also based on the ratings and reports on bank regulation and supervision provided by the IFIs.
4. Bank Size, Efficiency, Soundness, and Modernization	Questions are generally based on the quantitative indicators of the size, efficiency, soundness, and outreach of the banking system as reported in the statistical sources used in the Assessment Framework.
5. Non Bank Financial Institutions	Questions would be directed to the areas of specific interest to the interviewed party. For instance, the NBFI regulators would be queried about their policies, inspection programs, and the status of their risk management program. Asset managers and institutional investors would be queried on the status of their firms and the challenges they face.
6. Corporate Sector Financial Condition and Access to Finance	Questions to enterprises cover the financial condition of the firms and their access to financial services.

XI. Appendix B

ARMENIA FACT SHEET: Financial Sector Development

As of May 13, 2009

This fact sheet provides an overview of financial sector development in Eastern Europe and Eurasia (E&E) countries, highlighting Armenia. Five indices (composed of 28 sub-indices) pinpoint progress that has been made, as well as highlight the remaining challenges that might hinder overall economic growth. Tables A and A.1-A.5 detail the indices, sub-indices and data for each country. The five indices are:

1. Macroeconomic Foundation
2. Foundation for Reform in the Financial Sector
3. Reforms and Progress in the Banking Sector
4. Size and Efficiency of the Banking Sector
5. Reforms and Progress in the Non-Bank Financial Institutions Sector.

Map: Financial Sector Development in E & E (1= least developed, 5 = most developed)

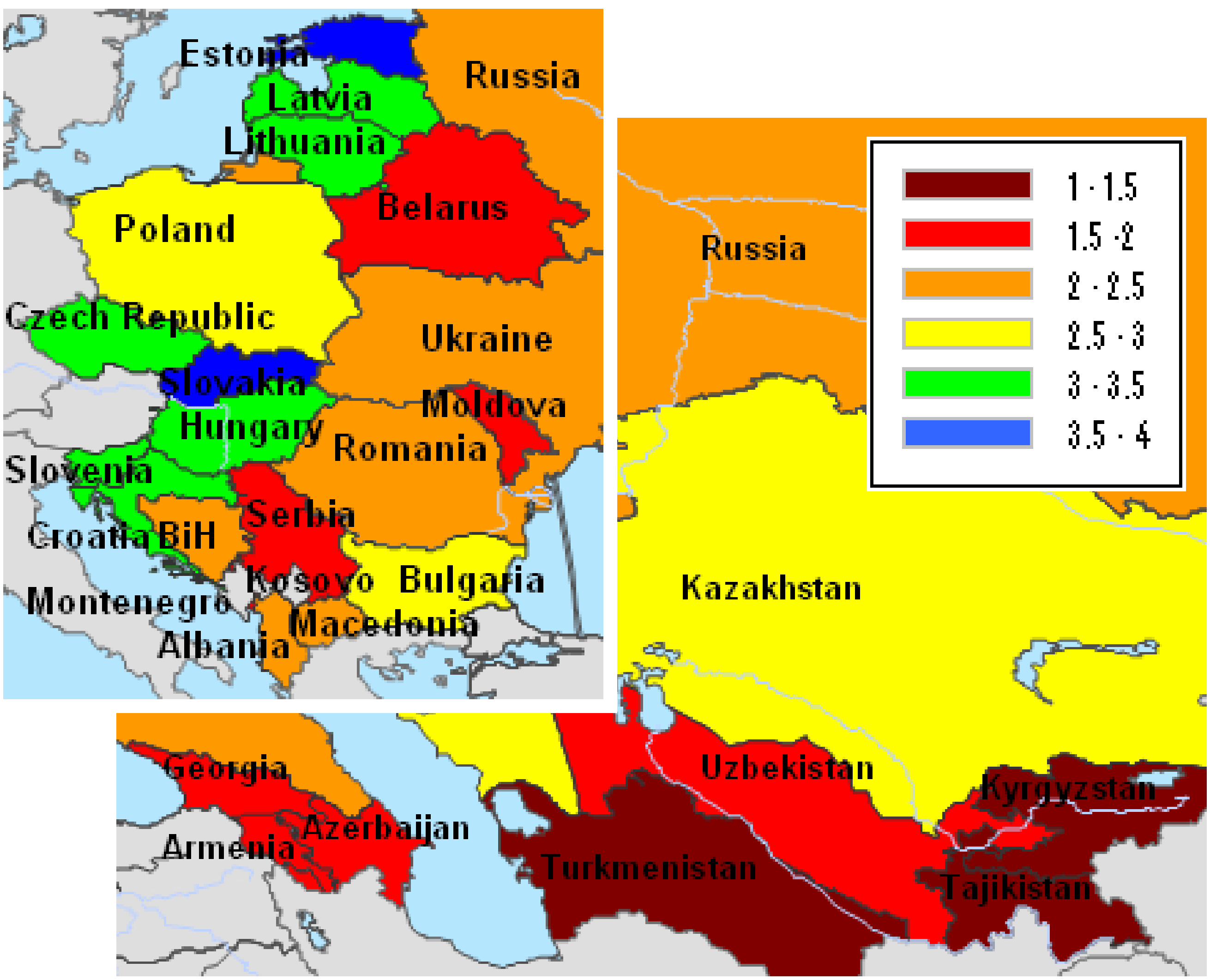

Table A
Overall Financial Sector Indices for the E&E Region (0=worst, 5=best)

Country	1. Macro-economic Foundation (2007-08) Index*	2. Foundation for Reform in Financial Sector (2008) Index	3. Reforms and Progress in the Banking Sector (2008) Index	4. Size and Efficiency of the Banking Sector (2005-08) Index	5. Reforms and Progress in the NBFI Sector (2007-08) Index	Overall Average (2005-2008) Index
Estonia	2.6	4.3	4.6	4.1	4.2	4.0
Czech Rep.	3.4	3.3	3.4	3.9	4.2	3.6
Slovak Rep.	3.6	3.6	4.1	3.8	1.5	3.3
Montenegro	1.8	2.9	4.0	4.7	3.1	3.3
Poland	3.1	3.7	2.2	3.3	4.1	3.3
Slovenia.	3.1	3.7	2.8	3.6	3.0	3.2
Lithuania	2.5	3.2	4.3	2.8	3.3	3.2
Hungary	2.2	3.0	3.1	3.7	3.9	3.2
Croatia	2.3	3.0	3.7	3.8	3.1	3.2
Bulgaria	1.6	2.1	3.4	4.1	2.9	2.8
Latvia	2.2	3.4	3.5	2.6	2.1	2.8
Romania	2.1	2.7	2.8	2.6	2.8	2.6
Kazakhstan	2.8	1.9	2.4	2.5	2.7	2.5
Russia	3.2	1.1	1.9	2.5	3.3	2.4
Georgia	2.8	2.3	3.2	1.6	1.2	2.2
Macedonia	2.0	1.7	2.7	1.6	3.0	2.2
Albania	2.51	2.0	3.3	2.3	0.6	2.1
Bosnia	1.6	1.2	2.8	2.6	2.0	2.0
Armenia	***3.1***	***1.6***	***2.5***	***1.8***	***1.0***	***2.0***
Azerbaijan	3.8	2.7	0.9	1.2	1.1	1.9
Ukraine	2.0	0.8	2.1	2.3	1.3	1.7
Serbia	1.1	1.7	2.0	1.0	2.3	1.6
Belarus	2.9	0.7	1.1	1.3	2.0	1.6
Kyrgyz Rep.	1.4	1.4	1.4	1.4	2.1	1.5
Uzbekistan	3.3	1.4	0.6	0.6	1.8	1.5
Moldova	1.0	1.3	2.0	1.0	1.2	1.3
Tajikistan	2.0	0.6	1.1	0.3	0.6	0.9
Turkmenistan	4.0		0.3	0.2		
Kosovo	n/a	n/a	n/a	n/a	n/a	n/a
All of E&E	2.7	2.3	2.6	2.4	2.2	2.4
BRC - 2006	2.2	2.7	3.4	3.3	2.6	2.8
NT - 2006	3.0	3.6	3.6	3.5	3.3	3.4
SEE	2.1	2.3	3.0	2.5	2.3	2.5
Caucasus	3.2	1.9	2.0	1.5	1.2	2.0
Eurasia	2.6	1.1	1.7	1.7	2.1	1.8

See Attachment A for notes on and sources of data for this table.

Table A.1
Macroeconomic Foundation for Financial Sector Development

Country	Average growth in GDP per capita over last 5 years (IMF-WEO, 2008)		Gross domestic savings as % GDP (WDI, 2007)		Average inflation rate over last 5 years (IMF-WEO, 2008)		Current account balance as % GDP (IMF-WEO, 2008)	
	%	Index	%	Index	%	Index	%	Index
Albania	6.0	1.5	0.2	0.9	2.4	5.0	-13.5	1.1
Armenia	***11.6***	***4.6***	***18.7***	***2.4***	***3.8***	***3.7***	***-12.6***	***1.7***
Azerbaijan	20.0	5.0	54.9	5.0	12.5	0.2	35.5	5.0
Belarus	9.9	4.4	18.9	2.8	10.9	1.3	-8.4	3.0
Bosnia	5.9	1.3	-15.4	0.4	3.6	3.9	-15.0	0.9
Bulgaria	6.3	2.0	12.9	1.9	7.3	2.4	-24.4	0.2
Croatia	4.2	0.2	25.1	3.3	4.0	3.5	-9.4	2.2
Czech Rep.	5.4	1.1	30.2	4.1	3.1	4.4	-3.1	4.1
Estonia	6.0	1.5	29.3	3.7	6.1	2.8	-9.2	2.4
Georgia	7.9	3.7	2.8	1.3	7.8	2.2	-3.1	4.1
Hungary	2.9	0.0	24.6	3.1	5.2	3.2	-9.2	2.4
Kazakhstan	8.4	4.3	40.4	4.8	10.2	1.7	-22.6	0.4
Kosovo	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
Kyrgyz Republic	5.2	0.7	-19.8	0.2	10.6	1.5	-6.5	3.3
Latvia	7.4	3.3	17.2	2.0	9.1	2.0	-13.2	1.3
Lithuania	7.0	2.8	17.5	2.2	5.4	3.0	-11.6	2.0
Macedonia	4.6	0.4	4.0	1.5	2.7	4.8	-13.1	1.5
Moldova	6.2	1.9	-14.9	0.6	11.4	1.1	-19.4	0.6
Montenegro	7.1	3.1	-0.4	0.7	4.3	3.3	-31.4	0.0
Poland	5.3	0.9	20.5	3.0	2.8	4.6	-5.5	3.9
Romania	6.8	2.6	9.6	1.7	7.1	2.6	-12.6	1.7
Russia	7.0	2.8	33.0	4.4	11.4	1.1	6.1	4.4
Serbia	6.3	2.0	2.6	1.1	11.5	0.6	-17.3	0.7
Slovak Rep.	7.4	3.3	26.7	3.5	3.4	4.1	-6.3	3.5
Slovenia.	5.0	0.6	29.4	3.9	3.2	4.3	-5.9	3.7
Tajikistan	8.0	3.9	-22.7	0.0	11.4	1.1	-8.8	2.8
Turkmenistan	12.1	4.8	40.2	4.6	9.4	1.9	19.6	4.8
Ukraine	6.4	2.4	18.8	2.6	14.6	0.0	-7.2	3.1
Uzbekistan	8.1	4.1	30.2	4.1	11.8	0.4	13.6	4.6
All E&E Countries	7.6	3.6	16.7	2.4	6.5	2.1	-5.9	2.6
BRC-2006	5.8	3.1	3.4	2.3	5.8	2.2	-14.2	1.3
NT - 2006	6.5	3.6	3.6	3.3	3.9	2.9	-9.7	2.4
SEE	5.4	2.9	3.8	1.2	5.1	2.7	-11.8	1.8
Caucasus	14.4	4.8	30.0	3.1	7.2	1.7	3.9	3.0
Eurasia	7.4	4.0	14.6	2.7	11.4	0.6	-3.4	3.2
Ave. of Big 3	2.5	0.8	17.4	2.3	2.9	3.5	-3.2	3.3

See Attachment A for notes on and sources of data for this table.

Table A.2
Foundation for Reform in Financial Sector, Part 1

Country	Financial market sophistication (WEF-GCR, 2008)		Credit information coverage (bureaus and registries) (WB-DB, 2008)		Strength of auditing and reporting standards (WEF-GCR, 2008)		Restrictions on capital flows (WEF-GCR, 2008)		Part 1 average (2008)
	Score	**Index**	**%**	**Index**	**Score**	**Index**	**Score**	**Index**	**Index**
Albania	2.3	0	0	0	3.8	0.8	3.9	1.2	0.5
Armenia	3.0	***1.0***	***24***	***3.0***	***4.0***	***1.2***	***5.0***	***3.3***	***2.1***
Azerbaijan	4.1	3.2	1	0.6	4.4	3.0	3.9	1.2	2.0
Belarus	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
Bosnia	2.7	0.4	69	4.6	3.6	0.2	4.3	2.5	1.9
Bulgaria	3.3	1.4	31	3.8	4.3	2.4	4.2	2.1	2.4
Croatia	4.3	3.6	72	4.8	4.7	3.6	4.5	2.7	3.7
Czech Rep.	4.7	4.6	65	4.4	5.1	4.2	5.4	3.8	4.3
Estonia	5.8	5.0	21	2.8	5.5	5.0	6.1	5.0	4.5
Georgia	3.5	1.8	5	1.8	4.3	2.4	5.6	4.2	2.6
Hungary	4.4	4.0	10	2.4	5.1	4.2	5.5	4.0	3.7
Kazakhstan	3.7	2.2	26	3.4	4.1	1.4	3.5	0.4	1.8
Kosovo	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
Kyrgyz Republic	2.8	0.8	4	1.4	3.6	0.2	4.2	2.1	1.1
Latvia	4.5	4.2	4	1.4	5.1	4.2	5.7	4.6	3.6
Lithuania	4.3	3.6	9	2.2	5.0	4.0	5.0	3.3	3.3
Macedonia	3.3	1.4	7	2.0	4.1	1.4	4.1	1.7	1.6
Moldova	3.2	1.2	0	0.0	4.3	2.4	3.7	0.6	1.0
Montenegro	3.8	2.8	26	3.4	4.1	1.4	5.6	4.2	3.0
Poland	4.2	3.4	52	4.0	4.6	3.4	4.9	3.1	3.5
Romania	3.7	2.2	25	3.2	4.5	3.2	4.6	2.9	2.9
Russia	3.7	2.2	10	2.4	3.8	0.8	3.2	0.2	1.4
Serbia	2.6	0.2	92	5.0	4.1	1.4	3.7	0.6	1.8
Slovak Rep.	5.0	4.8	56	4.2	4.9	3.8	5.7	4.6	4.4
Slovenia.	4.6	4.4	3	1.0	5.2	4.8	5.1	3.7	3.5
Tajikistan	2.7	0.4	0	0	3.3	0	4.1	1.7	0.5
Turkmenistan	n/a	n/a	n/a	n/a	n/a	n/a	4.0	1.5	1.5
Ukraine	3.6	2.0	3	1,0	3.7	0.6	3.7	0.6	1.0
Uzbekistan	4.0	3.0	2	0.8	4.2	2.2	3.1	0	1.5
All E&E Countries	3.6	2.5	16.4	2.4	4.3	2.4	4.7	2.5	2.3
BRC - 2007	3.5	2.3	3.4	4.1	4.5	3.1	4.5	2.4	3.0
NT - 2007	4.5	3.6	3.6	3.2	5.0	4.2	5.6	4.1	4.0
SEE	3.2	1.6	28.5	3.0	4.2	2.1	4.4	2.0	2.1
Caucuses	3.2	1.6	5.0	2.1	4.0	1.6	4.8	2.9	1.7
Eurasia	3.1	1.6	1.1	0.7	3.8	0.7	3.7	0.6	0.7
Average Big 3	5.5	4.8	84.3	4.8	5.8	4.8	5.7	3.9	4.6

See Attachment A for notes on and sources of data for this table.

Table A.2 (continued)
Foundation for Reform in Financial Sector, Part 2

Country	Strength of investor protection (WEF-GCR, 2007)		Ethical behavior of firms (WEF-GCR, 2007)		Protection of minority shareholders' interests (WEF-GCR, 2007)		Legal rights index (WB-DB, 2007)		Part 2 average (2007)	Overall indicator (Parts 1&2) (2007)
	Score	Index	Score	Index	Score	Index	Score	Index	Index	Index
Albania	7	0.2	3.9	2.7	4.0	2.5	9	4.2	3.3	2.0
Armenia	***5.0***	***2.0***	***3.4***	***0.8***	***3.5***	***1.7***	***7***	***2.3***	***2.2***	***1.6***
Azerbaijan	7	1.0	4.3	4.2	3.6	1.3	8	3.3	3.3	2.7
Belarus	5	n/a	n/a	n/a	n/a	n/a	n/a	n/a	0.5	0.7
Bosnia	5	2.0	3.0	0.2	3.3	1.3	5	0.8	1.7	1.2
Bulgaria	6	4.0	3.7	3.1	3.3	1.3	8	3.3	3.0	2.1
Croatia	4	0.4	4.0	3.4	4.1	3.8	6	1.3	2.3	3.0
Czech Rep.	5	2.0	3.8	3.4	4.2	4.1	6	1.3	2.7	3.3
Estonia	6	4.0	4.8	4.8	4.9	5.0	6	1.3	3.4	4.3
Georgia	6	0.8	3.8	1.6	3.5	0.9	6	1.3	2.6	2.3
Hungary	4	1.0	3.8	3.1	4.6	4.8	7	2.3	2.7	3.0
Kazakhstan	6	3.4	3.6	1.9	3.8	2.5	5.0	1.3	2.3	1.9
Kosovo	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
Kyrgyz Republic	8	4.0	3.1	0.0	3.2	0.5	7	2.3	2.9	1.4
Latvia	6	3.4	4.0	3.4	4.1	4.1	9	4.4	3.7	3.4
Lithuania	5	2.8	4.4	4.7	4.3	4.1	5	0.8	2.3	3.2
Macedonia	5.	2.0	3.6	1.4	3.9	2.8	7	2.3	2.2	1.7
Moldova	5	1.8	3.4	0.8	3.9	0.08	8	3.3	2.3	1.3
Montenegro	6	5.0	4.0	1.6	3.8	2.8	9	4.2	3.5	2.9
Poland	6.	4.0	4.5	4.2	4.3	4.5	8	3.3	3.5	3.7
Romania	6.0	4.0	3.6	1.9	4.1	2.8	8	3.3	3.3	2.7
Russia	5	2.8	3.5	0.6	3.3	0.5	3	0.4	1.5	1.1
Serbia	5	2.8	4.0	3.4	3.2		7	2.3	2.1	1.7
Slovak Rep.	5	1.0	3.9	4.1	4.2	3.8	9	4.2	3.4	3.6
Slovenia.	7	3.4	4.6	5.0	4.0	3.6	6	1.3	3.3	3.7
Tajikistan	3	0.0	3.5	0.8	3.8	2.8	2	0.3	1.1	0.7
Turkmenistan	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
Ukraine	4	0.6	3.3	0.2	3.3	0.5	9	4.2	2.2	0.8
Uzbekistan	4	1.0	3.8	2.7	3.8	2.8	3	0.4	1.5	1.4
All E&E Countries	4.9	2.3	3.8	2.5	3.7	2.5	5.7	2.2	2.4	2.3
BRC - 2006	5.0	2.8	3.9	2.8	3.7	2.6	5.0	1.4	2.4	2.7
NT - 2006	5.3	2.7	4.2	4.1	4.3	4.2	5.9	2.3	3.3	3.6
SEE	4.9	2.6	3.7	2.2	3.6	2.1	6.3	2.7	2.4	2.3
Caucuses	4.4	1.3	3.7	2.2	3.3	1.3	6.0	2.7	1.9	1.9
Eurasia	4.6	1.7	3.3	0.5	3.1	0.3	5.7	2.3	1.2	1.1
Average Big 3	7.8	4.8	5.4	4.8	5.5	4.8	7.7	3.7	4.5	4.6

See Attachment A for notes on and sources of data for this table.

Table A.3
Reforms and Progress in the Banking Sector

Country	Banking reform & interest liberalization (EBRD-TR, 2008)	Assets of the banking system held by the state (percent of total) (EBRD-TR, 2008)		Assets of system held by foreign owned banks (percent of total) (EBRD-TR, 2008)		Domestic credit to the private sector relative to GDP (EBRD-TR & WDI, 2008)		Soundness of banks (WEF-GCR, 2008)		Overall indicator
	Score, Index	%	Index	%	Index	%	Index	Score	Index	Index
Albania	3.0	0.0	5.0	94.2	4.6	36.4	2.0	5.0	1.6	3.3
Armenia	***2.7***	***0.0***	***5.0***	***49.0***	***1.9***	***8.7***	***0.2***	***5.2***	***2.6***	***2.5***
Azerbaijan	2.3	42.4	0.6	7.5	0.6	15.2	0.4	4.7	0.8	0.9
Belarus	2.0	76.5	0.2	19.7	0.9	25.0	1.1	n/a	n/a	1.1
Bosnia	3.0	1.9	3.3	93.8	4.4	25.4	1.3	5.1	2.0	2.8
Bulgaria	3.7	2.1	3.1	82.3	3.1	78.4	4.3	5.4	2.8	3.4
Croatia	4.0	4.7	2.3	90.4	3.9	76.6	4.1	5.8	4.0	3.7
Czech Rep.	4.0	2.4	2.9	84.8	3.3	39.9	3.0	5.8	4.0	3.4
Estonia	4.0	0.0	5.0	98.7	4.8	89.3	4.6	6.4	4.8	4.6
Georgia	2.7	0.0	5.0	90.6	4.1	30.5	1.5	5.4	2.8	3.2
Hungary	4.0	3.7	2.7	64.2	2.4	59.2	3.7	5.4	2.8	3.1
Kazakhstan	3.0	0.2	3.9	38.5	1.5	45.9	3.3	4.5	0.4	2.4
Kosovo	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
Kyrgyz Republic	2.3	8.7	1.5	58.7	2.0	18.7	0.9	4.1	0.0	1.4
Latvia	4.0	4.2	2.5	63.8	2.2	93.9	4.8	5.7	3.8	3.5
Lithuania	3.7	0.0	5.0	91.7	4.3	61.2	3.9	6.1	4.6	4.3
Macedonia	3.0	1.4	3.5	85.9	3.5	36.4	2.0	5.0	1.6	2.7
Moldova	3.0	9.5	1.4	24.8	1.1	39.5	2.8	5.1	2.0	2.0
Montenegro	3.0	0.0	5.0	78.7	3.0	127.6	5.0	5.8	4.0	4.0
Poland	3.7	19.5	0.8	75.5	2.6	33.4	1.9	5.1	2.0	2.2
Romania	3.3	5.7	2.1	87.3	3.7	32.9	1.7	5.5	3.4	2.8
Russia	2.7	n/a	n/a	17.2	0.7	38.5	2.6	4.9	1.4	1.9
Serbia	3.0	15.8	1.0	75.5	2.6	37.5	2.4	4.8	1.2	2.0
Slovak Rep.	3.7	1.0	3.7	99.0	5.0	42.3	3.1	6.4	4.8	4.1
Slovenia	3.3	14.4	1.2	28.8	1.3	79.0	4.4	5.6	3.6	2.8
Tajikistan	2.3	7.2	1.9	6.6	0.4	16.0	0.7	4.5	0.4	1.1
Turkmenistan	1.0	93.7	0.0	1.1	0.0	1.4	0.0	n/a	n/a	0.3
Ukraine	3.0	8.0	1.7	39.4	1.7	58.8	3.5	4.7	0.8	2.1
Uzbekistan	1.7	67.6	0.4	4.4	0.2	15.9	0.6	4.3	0.2	0.6
All E&E Countries	3.0	15.3	1.0	57.4	2.5	35.3	2.5	5.2	2.5	2.6
BRC 2007	3.7	4.0	2.6	86.3	3.8	47.6	3.4	5.4	3.4	3.5
NT 2007	3.8	6.1	2.1	77.8	3.4	54.8	3.9	5.7	3.9	3.6
SEE	3.1	4.0	2.6	83.4	3.7	35.4	2.5	5.2	2.6	3.1
Caucasus	2.6	17.0	3.5	46.3	2.0	13.6	0.5	4.9	1.5	2.0
Eurasia	2.7	34.4	1.2	21.2	1.1	31.0	2.2	4.8	1.5	1.7
Average Big 3	n/a	n/a	n/a	n/a	n/a	184.7	4.8	6.1	3.9	4.4

See Attachment A for notes on and sources of data for this table.

Table A.4
Size and Efficiency of the Banking Sector

Country	Financial depth (M2/GDP) (WDI, 2007)		Bank size indicator (WB-FG, 2005)		Bank efficiency indicator (WB-FG, 2005)		Ease of access to loans (WB-GCR, 2008)		Access to banking (WB-FG,2005)		Overall indicator only #1 & #3 (2007-08)
	%	Index	Rank	Index	Rank	Index	Score	Index	Rank	Index	Index
Albania	51.0	3.7	95	1.0	81	1.6	3.3	2.2	45	2.9	3.0
Armenia	***21.4***	***1.1***	***71***	***2.0***	***18***	***4.3***	***2.3***	***0.0***	***78***	***1.6***	***0.6***
Azerbaijan	14.5	0.0	52	2.8	86	1.3	2.6	0.4	81	1.3	0.2
Belarus	21.2	0.9	72	2.0	92	1.1	n/a	n/a	82	1.1	0.9
Bosnia	56.6	4.3	30	3.8	68	2.1	2.7	1.0	61	1.8	2.6
Bulgaria	74.4	4.8	40	3.3	7	4.7	4.0	4.2	43	3.4	4.5
Croatia	72.9	4.6	34	3.6	24	4.0	3.3	2.2	22	4.7	3.4
Czech Rep.	71.4	4.4	41	3.3	27	3.9	3.7	4.0	35	3.7	4.2
Estonia	50.3	3.1	63	2.3	2	5.0	4.6	5.0	21	5.0	4.1
Georgia	19.8	0.7	73	1.9	33	3.6	3.0	1.6	86	0.3	1.2
Hungary	50.9	3.5	39	3.4	8	4.7	3.3	2.2	23	4.5	2.9
Kazakhstan	36.4	1.9	54	2.7	19	4.2	3.5	3.4	84	0.5	2.6
Kosovo	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
Kyrgyz Republic	31.2	1.5	83	1.5	83	1.5	3.0	1.6	83	0.8	1.5
Latvia	44.7	2.4	n/a	n/a	n/a	n/a	3.4	2.8	n/a	n/a	2.6
Lithuania	44.9	2.6	59	2.5	48	3.0	3.6	3.6	56	2.1	3.1
Macedonia	48.3	3.0	n/a	n/a	n/a	n/a	2.4	0.2	n/a	n/a	1.6
Moldova	34.5	1.7	n/a	n/a	n/a	n/a	2.6	0.4	n/a	n/a	1.0
Montenegro	102.6	5.0	n/a	n/a	n/a	n/a	4.2	4.4	n/a	n/a	4.7
Poland	47.2	2.8	46	3.1	28	3.8	3.4	2.8	31	4.2	2.8
Romania	36.6	2.0	81	1.6	46	3.1	3.6	3.6	47	2.6	2.8
Russia	40.2	2.2	61	2.4	29	3.8	3.0	1.6	55	2.4	1.9
Serbia	16.3	0.6	n/a	n/a	n/a	n/a	2.9	1.4	n/a	n/a	1.0
Slovak Rep.	54.8	3.9	44	3.2	30	3.8	4.5	4.8	44	3.2	4.3
Slovenia.	50.6	3.3	38	3.4	51	2.9	4.2	4.4	33	4.0	3.9
Tajikistan	21.4	1.1	n/a	n/a	n/a	n/a	2.6	0.4	n/a	n/a	0.8
Turkmenistan	15.0	0.2	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	0.2
Ukraine	54.9	4.1	69	2.1	59	2.5	3.4	2.8	92	0.0	3.4
Uzbekistan	15.0	0.2	n/a	n/a	n/a	n/a	2.7	1.0	n/a	n/a	0.6
All E&E	38.1	2.6	57.3	2.6	42.0	3.2	3.2	2.4	55.1	2.5	2.4
BRC - 2005-6	53.5	3.7	51.7	2.8	25.7	3.9	3.5	3.3	37.3	3.6	3.5
NT - 2005-6	49.1	3.7	47.1	3.0	27.7	3.9	3.9	4.1	34.7	3.8	3.7
SEE	48.6	3.4	56.0	2.7	45.2	3.1	3.1	2.4	43.6	3.1	2.7
Caucasus	15.9	0.7	65.3	2.2	45.7	3.1	2.5	0.7	81.7	1.1	1.6
Eurasia	33.4	2.2	67.3	2.2	60.0	2.5	2.9	1.4	76.3	1.1	1.8
Average Big 3	94.0	4.9	7	4.5	12	4.6	4.3	4.5	13.0	5.0	5.0

See Attachment A for notes on and sources of data for this table.

Table A.5
Reforms and Progress in the NBFI Section

Country	Non banking sector reforms (EBRD-TR, 2008)	Regulation of the securities exchanges (WEF-GCR, 2008)		Financing through the local equity market (WEF-GCR, 2008)		Market value of listed securities (% GDP) (WDI & WBFG, 2007)		Value of Turnover of Securities (% Market Capitalization) (WDI & WBFG, 2007)		Overall indicator
	Index	Score	Index	Score	Index	%	Index	%	Index	Index
Albania	1.7	2.4	0.0	2.2	0.2	n/a	n/a	n/a	n/a	0.6
Armenia	***2.3***	***3.1***	***0.4***	***3.0***	***0.6***	***0.1***	***0.0***	***6.1***	***1.7***	***1.0***
Azerbaijan	1.7	3.4	1.2	2.9	0.4	n/a	n/a	n/a	n/a	1.1
Belarus	2.0	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
Bosnia	1.7	3.9	2.6	3.5	1.7	n/a	n/a	n/a	n/a	2.0
Bulgaria	3.0	3.7	1.8	3.7	2.1	13.9	4.0	34.2	3.6	2.9
Croatia	3.0	4.4	3.2	4.5	4.2	8.0	3.1	8.6	1.9	3.1
Czech Rep.	3.7	4.9	4.2	4.4	4.0	24.9	4.5	68.7	4.5	4.2
Estonia	3.7	5.6	5.0	4.8	4.8	9.9	3.6	34.9	3.8	4.2
Georgia	1.7	3.7	1.8	3.2	1.2	0.5	0.7	4.4	0.7	1.2
Hungary	4.0	4.9	4.2	3.6	1.9	34.4	4.8	106.0	4.8	3.9
Kazakhstan	2.7	3.4	1.2	3.9	3.3	8.6	3.3	20.9	3.1	2.7
Kosovo	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
Kyrgyz Republic	2.0	2.9	0.2	3.2	1.2	4.0	1.9	131.2	5.0	2.1
Latvia	3.0	4.8	3.8	3.7	2.1	0.5	0.7	4.8	1.0	2.1
Lithuania	3.3	5.2	4.8	4.6	4.4	2.7	1.7	10.1	2.1	3.3
Macedonia	2.3	4.2	3.0	3.9	3.3	6.7	2.9	26.5	3.3	3.0
Moldova	2.0	3.1	0.4	3.1	0.8	2.3	1.4	5.9	1.2	1.2
Montenegro	1.7	5.1	4.6	5.0	5.0	10.6	3.8	3.9	0.5	3.1
Poland	3.7	4.8	3.8	4.6	4.4	20.1	4.3	47.5	4.0	4.1
Romania	3.0	4.1	2.8	3.9	3.3	4.9	2.1	20.8	2.9	2.8
Russia	3.0	3.6	1.6	3.8	2.7	58.4	5.0	58.9	4.3	3.3
Serbia	2.0	3.7	1.8	3.8	2.7	6.1	2.6	14.6	2.6	2.3
Slovak Rep.	3.0	4.4	3.2	3.4	1.5	0.1	0.0	0.5	0.0	1.5
Slovenia.	3.0	4.6	3.6	4.3	3.8	6.0	2.4	12.3	2.4	3.0
Tajikistan	1.0	3.2	1.0	3.1	0.8	n/a	n/a	n/a	n/a	0.6
Turkmenistan	1.0	n/a	n/a	1.6	0.0	n/a	n/a	n/a	n/a	0.5
Ukraine	2.7	3.1	0.4	3.7	2.7	1.4	1.2	2.6	0.2	1.3
Uzbekistan	2.0	3.8	2.4	3.8	2.7	0.4	0.5	5.9	1.2	1.8
All E&E Countries	2.5	4.0	2.4	3.8	2.3	33.5	2.5	24.8	2.4	2.3
BRC - 2006	2.8	4.1	2.5	4.0	2.6	42.5	2.8	20.2	2.5	2.6
NT - 2006	3.4	5.0	4.2	4.5	3.7	31.2	2.9	34.8	2.7	3.4
SEE	2.2	3.9	2.3	3.8	2.5	41.6	2.9	20.1	2.7	2.3
Caucasus	1.8	3.5	1.2	3.1	0.7	4.8	0.4	14.4	2.0	1.2
Eurasia	2.4	3.3	1.0	3.7	1.9	56.5	3.3	24.2	1.9	2.1
Average Big 3	n/a	5.4	5.0	5.3	5.0	278.5	5.0	209.4	5.0	5.0

See Attachment A for notes on and sources of data for this table.

Appendix B (continued): Notes and Data Sources

Notes:

- BRC 2006 = Bulgaria-Romania-Croatia in their graduation year of 2006.
- NT-2006 = the status in 2006 of the Northern Tier of the eight transition economies that acceded into the EU in 2004. The eight NT countries are the Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Slovakia, and Slovenia.
- SEE = Southeast Europe, which includes Albania, Bosnia and Herzegovina, Bulgaria, Croatia, Kosovo, Macedonia, Montenegro, Romania, and Serbia. There is scant data available on the financial sector for either Kosovo or Montenegro.
- CAR = the five countries of Central Asia: Kazakhstan, the Kyrgyz Republic, Tajikistan, Turkmenistan, and Uzbekistan.
- Big Three = U.S., U.K., and Japan.

Key to Sources:

- EBRD-TR: European Bank for Reconstruction and Development Transition Reports
- IMF-WEF: International Monetary Fund's World Economic Outlook
- WB-FfA: World Bank's 2008 publication "Finance for All?"
- WB-FSDI: World Bank's Financial Sector Development Indicators
- WEF-GCR: World Economic Forum's Global Competitiveness Report
- WB-DB: World Bank's Doing Business Report
- WB-WDI: World Bank's World Development Indicators

Table A.1: Macroeconomic Foundation for Financial Sector Development

- Growth in GDP per capita, IMF-WEO
- Gross domestic savings % GDP, WB-WDI
- Inflation, IMF- WEO
- Current account balance %GDP, IMF- WEO

Table A.2: Foundation for Reform in the Financial Sector:

- Financial market sophistication, WEF-GCR, 8.01
- Credit information coverage WB-DB
- Strength of auditing and reporting standards, WEF-GCR, 1.16
- Restriction on capital flows, WEF-GCR, 8.05
- Legal rights index (hard data), WEF-GCR, 8.09
- Strength of investor protection (hard data) WEF-GCR, 8.06
- Ethical Behavior of Firms, WEF GCR, 1.15
- Efficacy of corporate boards, WEF-GCR, 1.17
- Protection of minority shareholders' interests, WEF-GCR, 1.18

Table A.3: Reforms and Progress in the Banking Sector:

- Bank reform and interest rate liberalization – EBRD-TR
- Assets of banking system % of total held by state, EBRD-TR

- Assets of banking system % of total held by foreign institutions, EBRD-TR
- Domestic credit to the private sector – WB-WDI
- Domestic credit by banks – WB-WDI
- Soundness of banks, WEF-GCR, 8.07

Table A.4: Size and Efficiency in the Banking Sector:

- M2/GDP – WB-WDI
- Bank size indicator, WB-FSDI
- Bank efficiency indicator, WB-FSDI
- Interest rate spread, WB-WDI
- Ease of access to loans, WEF-GCR, 8.03
- Access to Banking and Financial Services, WB-FfA

Table A.5: Reforms and Progress in the Non Bank Financial Sector

- NBFI reform EBRD-TR
- Regulation of securities exchanges, WEF-GCR, 8.08
- Financing through local equity market, WEF-GCR, 8.02
- Security market capitalization/GDP, WB-WDI
- Security market turnover/GDP, WB-WDI