

Chapter 7. Armenia: Small Business Act country profile

In 2018, Armenia underwent significant political changes leading to the election of a new parliament and the formation of a new government. The new government has embarked on an ambitious reform agenda that includes SME development as a priority. Due to the political changes and persistent economic challenges, Armenia has achieved only limited progress since the 2016 SBA assessment. Nevertheless, despite the lack of a comprehensive medium-term SME strategy, the institutional and regulatory framework for SME policy has further improved as the SME DNC (the SME agency) has extended the scope of services provided to SMEs, and a revised e-procurement system was introduced in 2018. There has been also a growing focus at the policy level on the importance of entrepreneurial human capital for national competitiveness, and the government's efforts in this area should be recognised and further supported.

Going forward, Armenia should finalise and adopt its SME Development Strategy 2020-2024 and establish an efficient monitoring and evaluation system. Priority actions should focus on enhancing e-government services, improving bankruptcy procedures, offering better services to exporters, and creating a competition-friendly business environment.

Key findings

Figure 7.1. SME Policy Index scores for Armenia

Country scores by dimension, 2020 vs. 2016

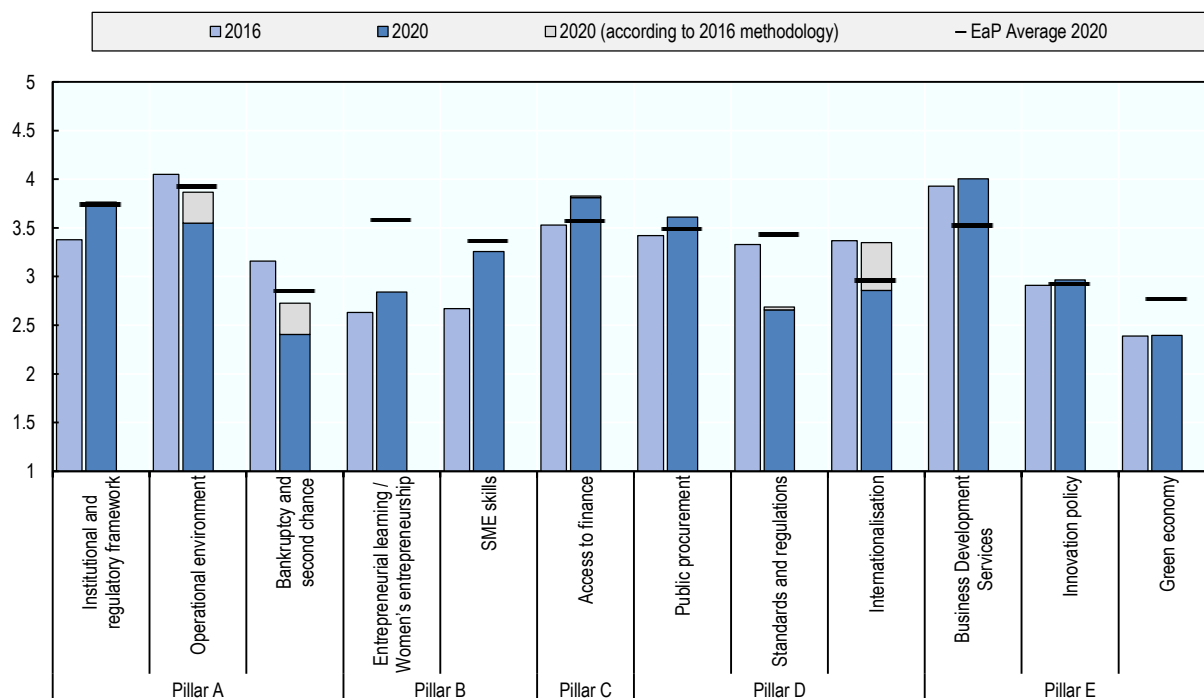
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Table 7.1. SME Policy Index scores for Armenia, 2020 vs. 2016

Pillar	Dimension	ARM 2020	ARM 2016	EaP average 2020	ARM 2020 (2016 methodology)
A	Institutional and regulatory framework	3.76	3.38	3.74	3.76
	Operational environment	3.55	4.05	3.92	3.87
	Bankruptcy and second chance	2.40	3.16	2.85	2.73
B	Entrepreneurial learning / Women's entrepreneurship	2.84	2.63	3.58	n.a.
	SME skills	3.26	2.67	3.36	n.a.
C	Access to finance	3.81	3.53	3.57	3.83
D	Public procurement	3.61	3.42	3.49	3.61
	Standards and regulations	2.66	3.33	3.43	2.69
	Internationalisation	2.86	3.37	2.96	3.35
E	Business development services	4.00	3.93	3.53	4.00
	Innovation policy	2.96	2.91	2.92	2.90
	Green economy	2.40	2.39	2.77	2.40

Table 7.2. Implementation progress on SME Policy Index 2016 priority reforms – Armenia

Priority reforms outlined in SME Policy Index 2016	Key reforms implemented so far
<u>Pillar A – Responsive government</u>	
<p>Adopt a comprehensive, longer-term SME strategy.</p> <p>Improve statistics collection (availability, methodologies, alignment with new definition).</p>	<p>A mid-term SME strategy for 2016-2018 was adopted; a new longer-term strategy covering 2020-2024 is under development;</p> <p>National Statistical Office started producing regular SME statistics with the first Statistical Bulletin on SME in line with Eurostat-OECD methodology published in 2018;</p> <p>Regulatory guillotine process covered 75% of existing laws and regulations;</p> <p>Special tax simplification system for microenterprises and family businesses introduced.</p>
<u>Pillar B – Entrepreneurial human capital</u>	
<p>Integrate the entrepreneurship key competence into curricula and teacher training across all levels of education.</p> <p>Embed lifelong entrepreneurial learning into government documents; introduce a graduate tracking system in vocational education and training (VET).</p> <p>Improve systematic data collection.</p> <p>Systematically promote and support the exchange of good practice.</p>	<p>Introduced an entrepreneurship module ensuring gradual competence development from primary to upper secondary schools including VET by 2020;</p> <p>Initial teacher training in entrepreneurial learning at primary level in place, planned for secondary level;</p> <p>Good practice in entrepreneurial learning and women's entrepreneurship promoted and shared;</p>
<u>Pillar C – Access to finance</u>	
<p>Strengthen creditor rights – including through a reform of the insolvency legislation.</p> <p>Establish an online registry for security interests over movable assets (following 2014 law).</p>	<p>Breadth of credit information coverage has increased making it easier for individuals and businesses to build a credit history;</p> <p>The registry for security interests over movable assets established and its accessibility improved through online registration and searchability;</p> <p>Financial education in secondary schools is being piloted with a view of full-scale roll-out by 2021.</p>
<u>Pillar D – Access to markets</u>	
<p>Develop and implement targeted support measures for exporting SMEs, including an enabling environment for trade finance.</p> <p>Increase compliance of national technical regulations and standards with international and EU standards.</p> <p>Strengthen public procurement legislation and promote SME participation.</p>	<p>Co-financing mechanism for participation in international trade fairs introduced;</p> <p>New public procurement law adopted in line with the EU Directives; introduction of the revised e-procurement system in 2018;</p> <p>Export Insurance Agency of Armenia provides financial services for exporters.</p>
<u>Pillar E – Innovation and Business Support</u>	
<p>Introduce specific measures to promote the private business development service (BDS) market.</p>	<p>A co-financing mechanism involving private sector service providers was implemented by Business Armenia for export activities;</p> <p>Expansion of innovation infrastructure with focus remaining on IT sector;</p> <p>SME strategy contains provisions for development of SME greening.</p>

Context

Economic snapshot and reform priorities

Following near stagnation in 2016, mainly due to the slowdown of economic activity in major trading partners, Armenia has experienced a strong recovery. A supportive external environment and improved domestic economic fundamentals have boosted private

consumption, investment and exports. Real GDP growth reached 7.5% and 5.2% in 2017 and 2018, respectively. The positive economic outlook continues despite a slightly lower GDP growth rate of 5.2% in 2018 due to a fiscal tightening and slower inflows of remittances and FDI (Table 7.3). Nevertheless, Armenia still faces major socio-economic challenges with substantial unemployment (17.7% in 2018) (Asian Development Bank, 2019^[1]) and one-fourth of the population still living below the national poverty line, contributing to sizable emigration (Economist Intelligence Unit, 2019^[2]).

The economy is driven mainly by industry and agriculture, which in 2017 accounted for 25.3% and 14.9% of GDP, respectively (World Bank, 2019^[3]). Exports are concentrated in terms of both products (ores and metal accounted for nearly 40% of exports in 2017) and destination markets (nearly one-fourth of exports went to Russia in 2017) (Statistical Committee of the Republic of Armenia (Armstat), 2019^[4]). The country is also highly reliant on remittances, which amounted to 13% of GDP in 2017, with nearly 64% coming from Russia (World Bank, 2019^[3]; World Bank, 2019^[5]). This dependence exposes Armenia to external shocks, such as volatility in commodity prices and economic downturns in Russia. Furthermore, the economy is highly dollarised: rising international rates and dollar appreciation create a risk of capital outflows.

Since 2014, exports of goods and services have grown steadily, reaching 37.3% of GDP in 2017 (as compared to 28.6% in 2014) with some trends in the diversification of the export basket, i.e. textile exports increased from 3% in 2014 to 6% as a share of total exports in 2017 (WITS, 2019^[6]; UN Comtrade, 2019^[7]). Despite a decreasing trend observed since 2009, Armenia still runs a negative current account. After a sharp fall driven by the 2009 world economic crisis, net FDI inflows are still declining, limiting further opportunities for economic growth. Net FDI inflows stood at USD 2% of GDP in 2018, well below the 8.1% recorded in 2009 (Table 7.3).

Table 7.3. Armenia: Main macroeconomic indicators, 2013-18

Indicator	Unit of measurement	2013	2014	2015	2016	2017	2018
GDP growth*	Percentage, y-o-y	3.3	3.6	3.2	0.2	7.5	5.2
Inflation**	Percentage, average	5.8	3.0	3.7	-1.4	1.0	2.5
Government balance ¹ **	Percentage of GDP	-1.6	-1.9	-4.8	-5.6	-4.8	-1.8
Current account balance*	Percentage of GDP	-7.3	-7.8	-2.7	-2.1	-3.0	-9.4
Exports of goods and services*	Percentage of GDP	28.4	28.6	29.7	33.1	37.3	37.5
Imports of goods and services*	Percentage of GDP	48.2	47.0	41.9	42.8	49.5	52.9
FDI net inflows*	Percentage of GDP	3.1	3.5	1.7	3.2	2.2	2.0
General government gross debt**	Percentage of GDP	36.3	39.4	44.1	51.9	53.7	51.3
Domestic credit to private sector*	Percentage of GDP	42.4	48.9	45.6	48.9	51.5	55.6
Unemployment ² *	Percentage of total active population	16.2	17.5	18.3	17.6	17.8	17.7
Nominal GDP*	USD billion	11.1	11.6	10.6	10.5	11.5	12.4

¹ General government net lending/borrowing.

² Modeled ILO estimates.

Source: *World Bank (2019^[3]), *World Development indicators*; **IMF (2019^[8]), *World Economic Outlook*, both accessed in December 2019.

Following the 2014 economic slowdown, the government took significant steps to pursue fiscal consolidation, closely monitoring its monetary policy and implementing structural reforms. In 2018, a new tax regime and renewed efforts to improve tax administration helped narrow the fiscal deficit to 1.6%. The Central Bank of Armenia has gradually lowered its refinancing rate, which has supported domestic credit to the private sector (Table 7.1). In February 2019, the Parliament adopted a five-year programme on economic development that gives priority to fighting corruption and improving the business environment, notably through FDI attraction and export promotion. Given the strong support provided by international organisations, the authorities reached a staff-level agreement with the IMF on a USD 250 million three-year precautionary Stand-By-Arrangement (SBA) to support the implementation of the governments' reform plans (EBRD, 2019^[9]).

Business environment trends

Since 2016, Armenia has fallen back in the World Bank's *Doing Business* ranking, slipping from 35th place to 47th (World Bank, 2019^[10]). Though this outcome largely reflects reform activism elsewhere rather than a deterioration of conditions inside Armenia, the Bank's indicators show no progress on getting credit, and only incremental changes have been implemented on paying taxes and resolving insolvency. However, the country still ranks high on starting a business (10th) and registering property (13th).

Building on the findings and recommendations of the SME Policy Index 2016, the government has taken steps to improve the policy environment for SMEs. An initial effort in this direction led to the adoption of an SME strategy covering the period 2016-18. A subsequent external evaluation of the strategy highlighted the main achievements and challenges of SME policy. The government is now drafting a new medium-term SME strategy for 2020-25, engaging with all stakeholders including the private sector.

In 2018, Armenia experienced significant political changes that led to the election of a new parliament and the formation of the new government. The new government put forward an ambitious reform agenda that aims, among other things, to combat corruption, improve the efficiency and independence of judiciary, and enhance the overall business climate to attract investment and boost entrepreneurship. The turbulent political transition and the ongoing process of restructuring ministries and state agencies have had a negative impact on Armenia's performance in this round of the SBA assessment, but if the government successfully follows through on its reform commitments, the coming years will see considerable progress. Even in the difficult context of the recent past, Armenia has managed to broaden the scope of the support services it provides to SMEs by establishing a dedicated SME agency (the SME DNC¹), advanced in the development of the new SME strategy, and revised its e-procurement system to enable greater SME participation.

SME sector

The SME definition in place in Armenia since 2011 is in line with the EU definition, as it is based on three criteria covering employment, turnover and balance sheet (Table 7.4).

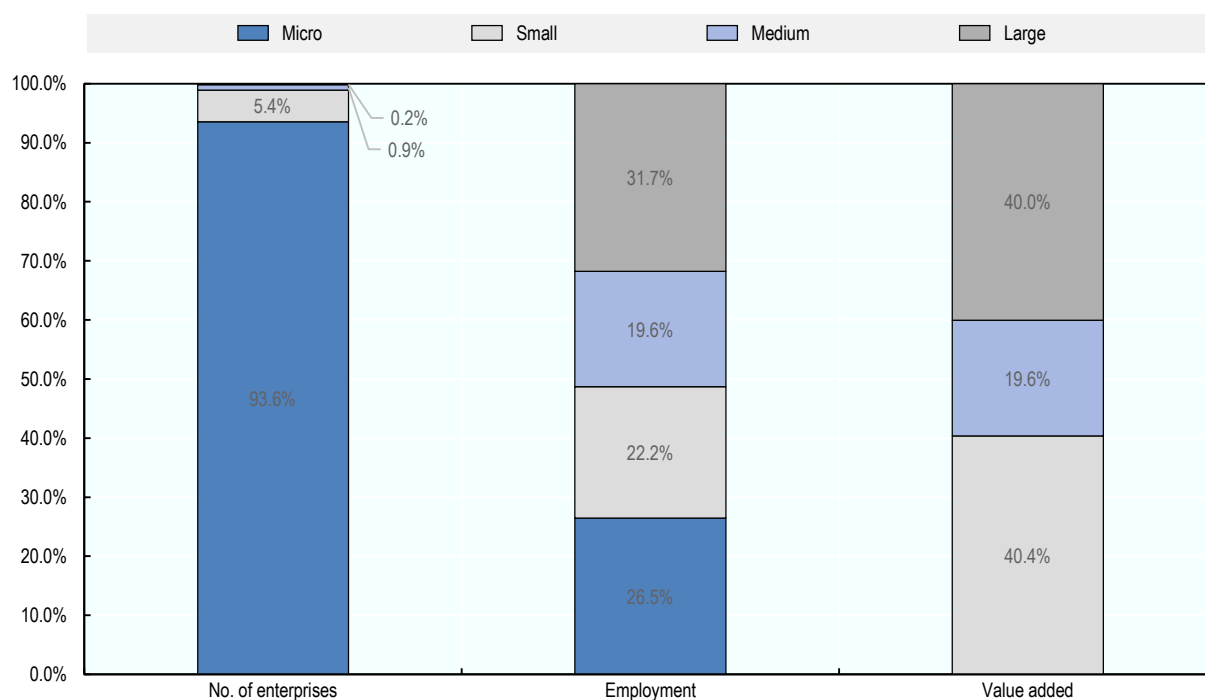
Table 7.4. Definition of micro, small and medium enterprises in Armenia

	Micro	Small	Medium
Employment	< 10 employees	< 50 employees	< 250 employees
Annual turnover	≤ AMD 100 million (EUR 185 580)	≤ AMD 500 million (EUR 927 900)	≤ AMD 1 500 million (EUR 2 783 700)
Balance sheet	≤ AMD 100 million (EUR 185 580)	≤ AMD 500 million (EUR 927 900)	≤ AMD 1 000 million (EUR 2 041 380)

Note: Exchange rate as of October 2019, <https://www1.oanda.com/lang/it/currency/converter/>

Source: Amendments to the Law on State Support of Small and Medium Entrepreneurship (2011)

According to the 2018 data, SMEs comprise more than 99.8% of all enterprises in the business economy,² with microenterprises constituting 93.6% of them. SMEs account for 68% of total business employment and generate up to 60% of value added in the business sector, which is broadly comparable with the SME performance in the EU.

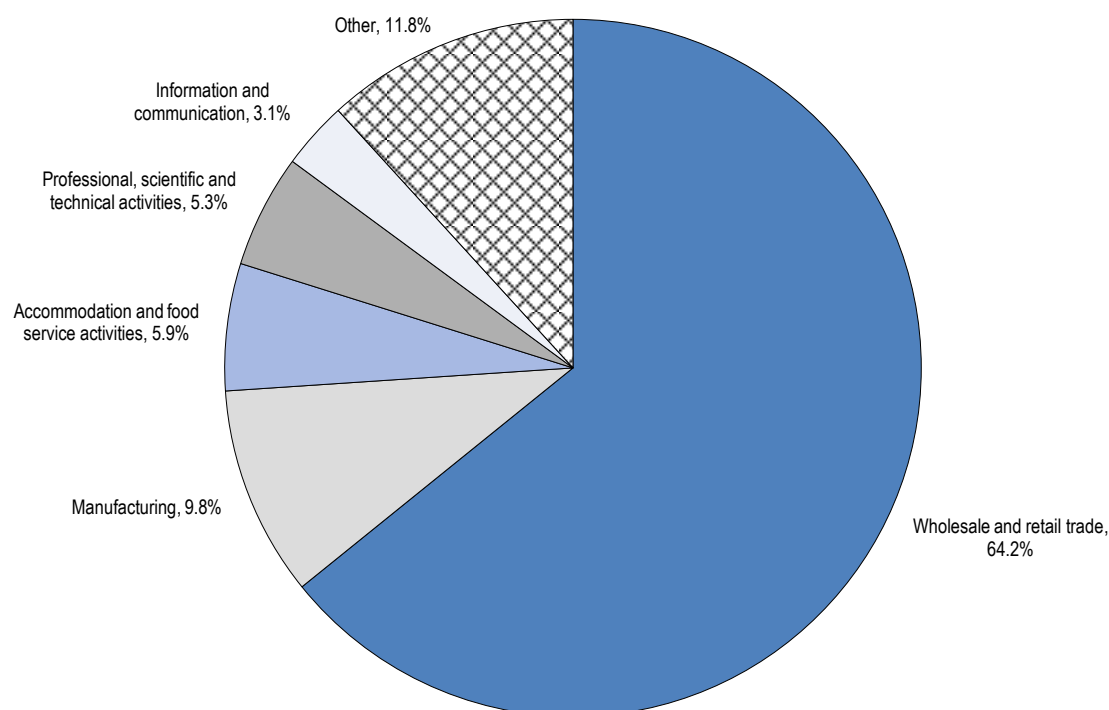
Figure 7.2. Business demography indicators in Armenia, by company size, 2018

Note: Micro-enterprises are included in small enterprises category for value added.

Source: Armstat, (2019^[11]), *Small and Medium Entrepreneurship in the Republic of Armenia, 2019*.

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Most SMEs in Armenia are concentrated in relatively low value added activities, such as wholesale and retail trade (64%) and manufacturing (10%).

Figure 7.3. Sectoral distribution of SMEs in Armenia, 2018

Note: Sectors include section B to N, the sector S95, excluding sector K (financial intermediation services) of ISIC rev.4. "Other" includes Administrative and support service activities, Real estate activities, Transport and storage, Construction, Repair of computers, Mining, Energy, and Water supply.

Source: Armstat, (2019^[11]), *Small and Medium Entrepreneurship in the Republic of Armenia, 2019*.

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SBA assessment by pillar

Level playing field pillar

Competition

Armenia's legal framework for competition incorporates most of the basic building blocks necessary for an effective competition law regime. The enforcement body, the State Commission for the Protection of Economic Competition (SCPEC), is an independent institution, and has most of the required powers and instruments at its disposal, but some important enforcement tools are missing. SCPEC actively reviews laws and regulations and, within its mandate, advocates the lowering of barriers to entry and competition. All of SCPEC's recent recommendations have led to the necessary changes in draft laws and regulations. In addition to competition rules, SCPEC enforces rules against unfair competition and on consumer protection.

SCPEC's actual competition enforcement activity is limited to merger control and abuse-of-dominance investigations. It investigated 65 mergers in 2017-18 and imposed fines on a few companies for an abuse of dominance. Although anticompetitive agreements are prohibited, there was no enforcement against cartels in 2014-18. This is certainly related to

the lack of effective “dawn raid” powers.³ SCPEC is required by law to notify undertakings three days in advance of a planned inspection. This requirement severely hampers investigations into illegal cartels, as it ensures that incriminating direct evidence can be destroyed or hidden by the time the inspection actually takes place. The competition authority has not yet developed any guidelines for businesses on the interpretation and implementation of the competition law, with the exception of those on prevention and detection of anticompetitive agreements in public procurement processes.

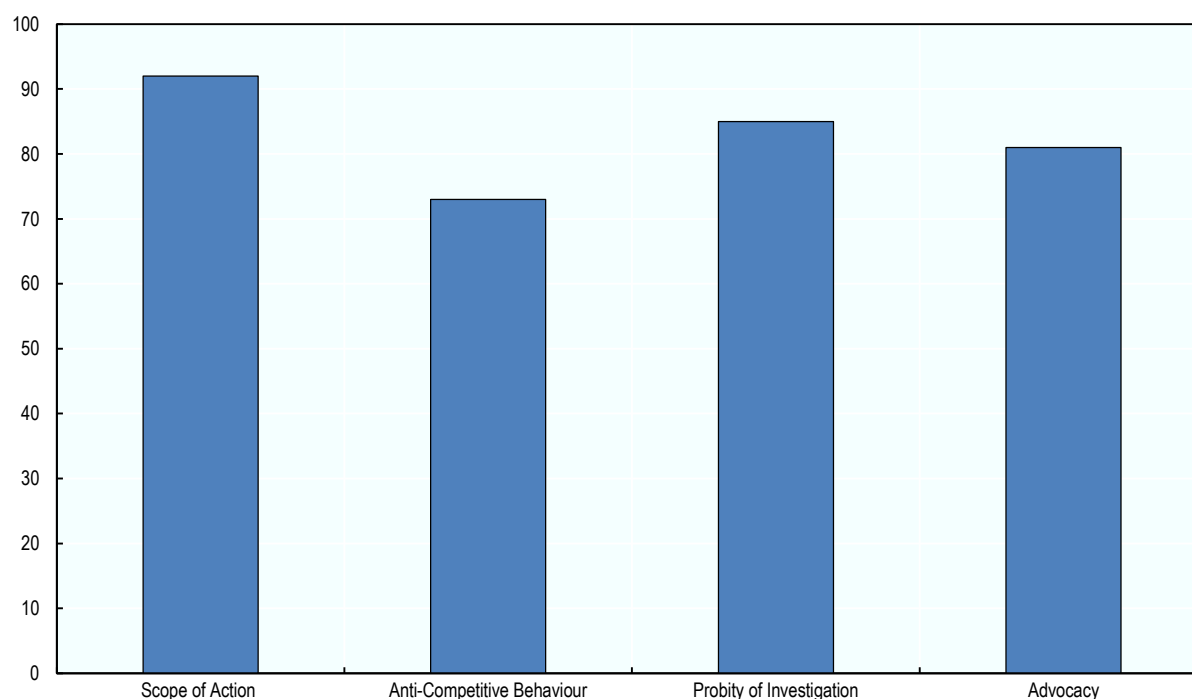
Changes to competition law in 2018 introduced a margin of discretion for imposing fines and personal liability of state officials and managers for competition violations, as well as clarification of the definition of an abuse of dominance.

However, important challenges remain:

- Compared to enforcement against unfair business practices and in consumer protection matters, competition enforcement is seriously underdeveloped. The emphasis, however, needs to be reversed. Competition enforcement is designed to tackle long-term obstacles to competition and the root causes of market distortions. Unfair business practices and unfair terms vis-à-vis consumers are often symptoms of underlying competition problems that are not addressed by current enforcement practices.
- Effective enforcement requires functioning tools and procedures. In terms of tools, “dawn raid” powers are recognised as an indispensable tool for uncovering illegal cartels. Cartel agreements cannot be established based on parallel conduct of observations or other indirect evidence alone. They require direct proof of communication or agreement. Moreover, cartels are a pervasive problem in small economies, like Armenia’s, where a small number of players dominate many sectors. As a result, taxpayers or consumers pay from 10–20% higher prices for goods and services, including when it comes to public procurement. All enforcement instruments would benefit from legal deadlines that are more flexible and, when necessary, longer. Currently, an investigation cannot last longer than 90 days, which is relatively short by international standards. When necessary, longer timelines would enable better enforcement cases based on international best practice.
- Highly qualified enforcers are needed to act in an institutional environment that guarantees independence from political or private stakeholder interventions. SCPEC needs to establish a reputation for impartial and neutral enforcement against public and private restrictions to competition. In order to attract and retain highly qualified lawyers and economists, the salaries would need to increase significantly, and with it the overall budget of SCPEC, including for office equipment.
- In order to promote an overall positive attitude to competition, SCPEC needs to increase its efforts to explain its benefits to the general public, policy makers, government officials, the media, private practitioners and the business community.

Figure 7.4. Competition Policy in Armenia

Percentage of formally adopted competition policy criteria, as of June 2019



Note: The chart above refers to the percentage of competition policy criteria formally adopted in the legal framework. It gives equal weight to all criteria. This does not illustrate actual enforcement activity in terms of relevance or quantity or indicate the relevance or suitability of the criteria.

Source: SBA questionnaire, interviews with Competition Authority of Armenia and business associations.

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Contract enforcement and alternative dispute resolution

In Armenia, commercial disputes are heard by civil courts of first instance, and a simplified procedure for small claims allows for faster and less-costly dispute resolution. Only a few court procedures are automated, including random case assignment to judges,⁴ e-payment of court fees, and publication of court judgements on a dedicated website (www.datalex.am). A platform for e-filing of court claims is being tested and e-service of process is not yet available, but the establishment of a full-fledged e-justice system is foreseen in the 2018-2023 Strategy for Judicial and Legal Reforms. In recent years, Armenia has not made progress in the *Doing Business* ranking when it comes to enforcing contracts, as it move from a score of 70.46 (28th) in 2016 to 69.7 (30th) in 2019. The authorities still need to do more to increase the overall efficiency and quality of the judicial process when enforcing contracts (e.g. ensuring implementation of the e-justice reform).

The protection of property rights in Armenia has strengthened, and the country now ranks 46th in the World Economic Forum's Global Competitiveness Index (GCI) (World Economic Forum, 2019^[12]). Armenian legislation provides for administrative and criminal liability for violation of intellectual property rights (IPR), and IPR-related disputes are normally resolved by specialised judges within courts of first instance. The government can do more to ensure proper enforcement of the IPR protection system, including by providing judges treating IP cases with sufficient training and knowledge. Although the

mechanism for appealing administrative decisions is in place, the government should also ensure efficient private-to-public litigation (in cases where the decisions of public authorities affect the property rights of SMEs) by establishing an institution in charge of protecting business rights against administrative decisions.

Alternative dispute resolution (ADR) mechanisms are embedded in the law, but their usage by businesses remains limited. While arbitration is a well-known practice, mediation, which is less costly for SMEs, was legally introduced only in 2015. The government has taken several initiatives to increase adoption of ADR, such as the creation of a list of licensed mediators, training for judges, and public awareness campaigns. Still, the government could step up its efforts to promote ADR by raising awareness among businesses, especially SMEs, on the benefits of ADR and building up the trust of the private sector in ADR, including by creating incentives for their usage by businesses (e.g. requirement for pre-filing mediation in certain type of litigation).

Business integrity

Armenia put in place an Anti-Corruption Strategy for 2015-18 to tackle corruption in both public and private sectors. Despite its importance, the strategy did not directly address business integrity issues and no study of corruption risks in the private sector was carried out by the government to identify the main risks for businesses and to design relevant measures to address them through tailored compliance mechanisms (ACN, OECD, 2018^[13]). The only study of corruption risks in the business sector in Armenia was carried out by the Armenian Lawyers' Association with the support of EU and OSCE (Armenian Lawyers' Association, 2017^[14]). At the same time, the 2018 changes in the government were driven by, among other things, a strong anti-corruption agenda, and the new government plans to address business integrity through a new strategy for 2019-2021 that is pending for approval by the Parliament. Going forward, Armenia could conduct a study of corruption risks in the private sector (in close co-operation with companies and business associations) to underpin the design of integrity measures under the upcoming Action Plan.

Armenia has recently stepped up its efforts to prevent corruption in the private sector. In March 2019, Amendments to the Law on State Registration of Legal Entities providing for disclosure of beneficiary owners of companies were adopted.⁵ The Law on Whistle-blowing,⁶ which provides for protection of whistle-blowers' rights, entered into force in January 2018. The anonymous unified electronic platform for reporting corruption (www.azdararir.am) that was envisaged by the law became operational in May 2019. In addition, businesses can report corruption through the Bizprotect⁷ whistle-blowing platform that was launched with support from the EU's Support for SME Development in Armenia (SMEDA) programme in January 2019 (80 reports recorded so far). In 2017, the parliament's Standing Committee on Financial and Economic Affairs discussed the new draft Criminal Code providing for criminal liability of legal persons for corruption-related offences, but the draft is still pending approval. In this regard, the government should continue working towards criminalisation of corruption for legal entities to ensure more-transparent operations in the business sector.

Although the government has co-operated with business associations in the area of corruption prevention (anti-corruption measures in tax and customs were developed by the State Revenue Committee in co-operation with NGOs), the scope of this co-operation remains limited and could be further enhanced. The government could envisage introducing financial and other incentives for companies to adopt business integrity measures (i.e. tax reductions, benefits when participating in public procurement/getting loans, whitelists,

integrity awards, etc.) and support business associations that promote compliance principles among their members and adopt codes of conduct (i.e. support in organisation of meetings, training events, awareness-raising campaigns).

Pillar A – Responsive government

Institutional and regulatory framework for SME policy

Armenia has conducted a proactive SME policy since the early 2000s and over the years it has established a relatively advanced institutional policy framework, in spite of the lack of a clearly defined SME development strategy. The mandate to design and co-ordinate SME policy has been assigned to the Ministry of Economy. The SME Development National Centre (SME DNC), established in 2002, is in charge of policy implementation, offering a wide range of support programmes through its headquarters in Yerevan and its network of ten regional offices.

Budget support has been secured through the government's Medium-Term Expenditure Programme and donor funding. SME support activities are organised on the basis of the Annual State Programme for SMEs and Entrepreneurship Support. State financial allocations to the SME sector have been limited and donor support remains crucial. For several years, Armenia lacked a comprehensive SME strategy. A first mid-term (2016-2018) SME Development Strategy was elaborated and approved only in 2015. However, the strategy failed to introduce clear policy guidelines and define mid-term objectives, while it remained disconnected from the design and implementation of the annual support plans. The way forward thus contemplates the introduction of clearly defined objectives, reasonable quantitative targets, key performance indicators and priority actions.

Armenia's new government has expressed its determination to strengthen the institutional framework and fill the mid-term strategic gaps. The SME policy mandate is assigned to the Ministry of Economy with an expanded portfolio covering economic development, investment, agriculture and tourism, while the SME DNC is expected to take over some of the functions previously performed by Business Armenia, the country's investment and export promotion agency, which was reorganised in 2018.

A new SME development strategy covering 2020-24 was being prepared at the time of writing (mid-2019) and it has been structured in line with the objectives of the country's medium-term development plan. The new strategy will focus on improving the regulatory framework and the business environment, raising SME productivity, increasing SME export orientation and technological upgrading, and supporting entrepreneurship in the least-developed regions.

The Statistical Committee of the Republic of Armenia (ArmStat) has made efforts to improve the quality and the availability of SME statistics. In 2018 the Committee produced, in co-operation with the OECD, a Compendium of Enterprise Statistics (2019^[15]) that provides for structural and business demography indicators on SMEs (Box 7.1).

Box 7.1. SME statistics production and dissemination in Armenia

The need to enhance the quality of SME statistics in Armenia was highlighted by the 2016 SBA assessment in EaP countries as a main priority to improve monitoring and evaluation of SME policies in the country. Throughout 2017-18, the State Statistical Committee of Armenia (Armstat) worked with international partners, including OECD, to improve its capacity to collect, analyse, disseminate and harmonise official business statistics. As a result, Armstat implemented a methodology to harmonise the development and collection of entrepreneurship indicators in line with the international standards, i.e. the [OECD-Eurostat Entrepreneurship Indicators Programme](#) and, in particular, the *Eurostat-OECD Manual on Business Demography Statistics*.

In 2018, Armstat produced the first [Statistical Bulletin on Small and Medium Entrepreneurship in the Republic of Armenia, 2018](#), which presents comprehensive and detailed information about the role played by the SME sector in Armenia's economy. The publication has adopted the suggested OECD template for the dissemination of statistics, which includes the use of various figures and tables and covers such indicators as number of enterprises (by size class and economic activity), turnover, persons employed, average salaries, gross value-added of SMEs, and information on the birth and death of enterprises (by age, economic activity and geographical region).

Source: Armstat (2018^[16])

The level of labour and enterprise informality in Armenia stood at 35.96% of GDP in 2018 (Medina and Schneider, 2018^[17]) and has been declining over the last ten years, while the number of enterprises reporting having to deal with unfair competition from informal enterprises is relatively contained (12.8% according to the 2013 World Bank/EBRD Enterprise Survey⁸). Although a comprehensive strategy for reducing informality is not in place, actions have been taken to reduce the regulatory burden on small enterprises, reduce tax rate and simplify tax administration procedures.

Regulatory reform has been a long-term government priority. A multi-year “guillotine programme” started in 2012 has substantially reduced the number of redundant laws and regulations governing business activities. As a result, Armenia ranks high in a number of World Bank 2020 *Doing Business* indicators, such as starting a business (10/190) and registering a property (13/190) (World Bank, 2019^[10]). However, the overall country performance shows a great variability over the indicator range, implying that the regulatory reform process is still not completed. Armenia has also taken steps to introduce regulatory impact analysis (RIA) as part of the legislative and regulatory process. The Normative Legal Order defines the criteria for RIA application, and RIA is expected to be applied systematically by the end of 2019.

Armenia has a long practice of conducting frequent public-private consultations, and a Business Support Office established by the EBRD and chaired by the Prime Minister has been in operation since 2007. The Ministry of Economy has also conducted frequent consultations involving the main SME and sectorial organisations, although the consultative process has not been formalised and there are no obligations to publish the minutes of the consultation sessions. Private sector representatives also sit on the governing board of the SME DNC. Although the political changes that took place in 2018 partially disrupted the consultative process, the government is committed to conducting a series of consultations as part of the final process of approval of the new SME strategy.

Operational environment for SMEs

Compared with the 2016 assessment, Armenia's overall score in this dimension has moderately decreased. While incremental progress has been observed in a number of areas (especially in company registration), government action has recently lost momentum in the area of e-government services and no progress has been made with respect to open data. The introduction of two new sub-dimensions, tax administration and business licencing, is also capturing policy aspects of relative under-performance.

Armenia adopted a Strategic Programme for Digital Governance in 2014 and since then has been expanding the range of e-government services and their accessibility. The range of services currently available for all enterprises registered in Armenia is quite comprehensive and includes online filing of tax returns and social security contributions, an e-pension platform, e-cadastre services, e-procurement services, and e-company registration. Access is granted through a bi-lingual portal (www.egov.am) that re-directs users to the relevant website. The "Armenia Digital Agenda – 2030", an updated e-government strategy covering all areas of public administration, was drafted in 2017, but its adoption and implementation is currently on hold, pending a review by the new government established after the 2018 general elections, while the Armenia Digital Foundation, previously in charge of the strategy co-ordination, has been dissolved.

More tangible progress has been made in the area of business licencing and in particular on company registration. As a result of the regulatory guillotine, the number of required business licences and permits, including building permits, has been considerably reduced. A full set of information, including licence applications, is available online (www.e-gov.am/licenses), while the Ministry of Finance and the National Chamber of Auditors regularly review and monitor the licencing procedures.

Company registration procedures have become simpler since the launch in 2011 of a Business Entry One-stop Shop operating as a single-window facility, with 33 locations across the country. A parallel online registration facility is also available. According to the 2020 *Doing Business* report, the entire procedure for registering a limited liability company currently takes 4 days, requires three procedures, and costs an amount equal to 0.8% of the per capita income. In 2020, Armenia ranked 10th in the *Doing Business* indicator for starting a business, while its distance from the frontier was set at 96.1/100, the third highest performance in the EaP region after Georgia and Azerbaijan (World Bank, 2019_[10]).

Armenia has introduced a special tax regime for microenterprises and family businesses. Currently small enterprises with a turnover up to ADM 9 million (~ EUR 16 702⁹), family business with a turnover up to AMD 18 million (~ EUR 33 404¹⁰) and individual entrepreneurs are exempted from the payment of all state taxes. The threshold for VAT registration is set at AMD 115 million (~ EUR 213 417¹¹). Tax administration is relatively simplified and tax declarations can be filed online. However, according to the 2020 *Doing Business* report, the number of tax payments per year (15) and the time required to fulfil tax obligations (264 hours per year) are relatively high. The post-filing index, which measures the efficiency of VAT reimbursement and the complexity of tax auditing, used to be relatively low in past assessments. It has recently increased, reaching a score of 74.9/100. The combination of a generous tax regime for microenterprises and family businesses, combined with simplified tax administration and the application of a threshold for VAT, may have helped to contain enterprise informality, but at the same time may have also introduced perverse incentives against the scaling-up of enterprise turnover. To this extent, the next necessary step consists in the assessment of the impact of the special tax

regime and other tax incentives applied to microenterprises and family businesses in order to reveal possible impediments to enterprise growth.

Bankruptcy and second chance

Since 2015, Armenia's position in resolving insolvency in *Doing Business* has slipped (95th in 2020, compared to 69th in 2015), due to the lack of recent improvements in its insolvency framework and progress achieved by other economies (World Bank, 2019^[10]).

The Law on Bankruptcy (2006, revised in 2007), continues to define the insolvency framework. The legislation formally provides with restructuring procedures, protection of creditors' rights and discharge procedure. Specialised commercial and insolvency courts were also introduced in January 2019.

However, the legislation could be further improved to reach international standards, while remaining implementation issues hamper its efficiency. The management of debtor's assets is a strong weakness of the framework. Even though restructuring proceedings are available, the large majority of cases are liquidations, denoting a credit-driven preference for resolving financial distress. In addition, the avoidance of pre-insolvency transactions is poorly framed and lacks guidance for courts and practitioners. The low participation of the creditors in the decision-making process is another issue, despite the fact that the creditors are paid first out of the proceeds of liquidation.

Moreover, prevention measures have yet to be introduced and implemented in Armenia to support financially distressed entrepreneurs. Pre-insolvency tools and training, early-warning systems and insolvency-related proceedings at the early stage of financial distress are key practices that Armenia could introduce into its insolvency framework. The introduction of a new sub-dimension on bankruptcy prevention measures associated with the poor performance of Armenia in this area, caused a drop in the overall score for the bankruptcy and second chance dimension. In addition, although there are no discriminatory provisions limiting access to public support and public tenders by entrepreneurs seeking a fresh start, Armenia should consider implementing a dedicated policy strategy or information campaign to promote second chance.

Pillar B – Entrepreneurial human capital

This section focuses on the human capital dimensions of the Small Business Act for Europe. First, it examines how entrepreneurial learning is addressed in the education system and particularly focuses on entrepreneurship as a key competence – a factor in Armenia's wider drive for competitiveness, growth and employment. Second, the discussion focuses on developments in women's entrepreneurship. Finally, both policies and support for SME training are addressed.

Human capital development is recognized as leverage for sustainable economic growth and job creation in any country. Armenia's progress in this regard since 2016 is particularly noticeable in entrepreneurial learning, as it was integrated into curricula of primary up to higher education levels and vocational education and training (VET). Teaching, practical entrepreneurial experience and career guidance take place. However, among the key areas recommended for improvement are policy coordination and strategy. As for support for SMEs, it is provided in the areas of youth, women, start-ups, family businesses, SME internationalization, SME growth, and participation in the digital economy. Monitoring and evaluation of training on SME performance are well developed, but a systematic approach

to the collection and analysis of SME skills intelligence, including training needs analysis, is still lacking.

Entrepreneurial learning

In Armenia, the education level of the active adult population is high, while high level of qualification mismatch and youth unemployment (38.4% in 2017) (Statistical Committee of the Republic of Armenia (Armstat), 2018_[18]) are complemented by educated youth being predominantly over-qualified (Palmer, 2017_[19]). Therefore, entrepreneurial learning is an important measure with regard to increasing youth employability. Since 2016, Armenia has established elements of a structured national partnership on entrepreneurial learning that has extended beyond VET (although the most developed partnership structures continue to exist in the area of VET).

In 2017, the Ministry of Education and Science signed a Memorandum of Understanding with Junior Achievement Armenia to implement a mandatory entrepreneurship module for grades 2-11 until 2020 to ensure gradual competence development between education levels. In primary schools, entrepreneurial learning has been integrated as a component of the “Technology” subject. For VET, a specific entrepreneurship module for business planning skills was introduced. Knowledge, skills and attitudes that VET learners acquire are now regarded as learning outcomes within the education standards and curricula for 56 VET specializations.

As recommended in 2016, initial teacher training on entrepreneurial learning for primary schools is now provided, with government plans to extend it to secondary schools in the near future. In addition, teaching and learning materials have been developed. Thus, teacher manuals for the new entrepreneurship module cover, at grade 2, an overview of entrepreneurship, idea generation and activity planning; at grade 3, information on innovation, creativity, business ideas, product presentation and advertising; and at grade 4, market research and business planning. Under the EU budget-support program Better Qualification for Better Jobs (2017-2020), entrepreneurship was also integrated as a career option in VET career guidance.

Going forward, the government should move beyond its financial and economic literacy focus towards developing an entrepreneurial mindset. To do this, it would be essential to complement the separate subject approach with developing attitudes and transversal competences in all subjects, introducing active teaching and learning methods, pre- and in-service teacher and school/university manager training. Aligning pedagogical institutes and universities to the reform agenda by adapting teacher qualification standards would be of high importance as well. Further, a strategy and action plan for key competence development for formal and higher education, VET and non-formal learning is required. An existing body, e.g. SME DNC, could systematically monitor progress on implementation. The government could further ensure a comprehensive approach to SME support and national policy partnerships through, inter alia, widening the SME Development Council’s scope, introducing a working group on education and involving national education stakeholders.

In addition, working to improve co-operation between education institutions and businesses through private sector involvement in skills-intelligence collection and analysis, and by offering mandatory practical experience to all learners, could be an important step forward. Further, using practical experience as a systematic approach to competence development, for instance, as part of the new entrepreneurship module in secondary schools or as part of

the work-based learning opportunities in VET, would help reduce unemployment rates in the long term and ensure a skilled labour force for the internal market and beyond.

Women's entrepreneurship

According to the State Statistical Committee of Armenia, women are more likely than men to pursue university studies (32.0%, versus 27.6% of men, aged 15-75 in 2017) and firms with female top managers are more likely to introduce new products or services on the market. Still, men are slightly more likely to be self-employed and only 20.3% of employers were women in 2017 (Statistical Committee of the Republic of Armenia (Armstat), 2018^[18]). Women's entrepreneurship support therefore has great potential. In Armenia, the law on "State Support for Small and Medium Enterprises" identifies main directions of state support for SMEs that include support for women's entrepreneurship. The dedicated Women's Entrepreneurship Strategy developed in 2014 aims to increase women's participation in economic development and women's entrepreneurship and the latter was also set as a strategic goal by the SME Development Strategy 2016-2018. At implementation level, SME state support annual programs include a dedicated section on women's entrepreneurship.

Throughout 2016-2018, government carried out training and provided consulting services for enterprises with little or no experience, conducted capacity-building activities, and organised the Prime Minister's "Best Women Entrepreneur" Award. Funds for these activities were ensured with donor support, e.g. a SME DNC and Asian Development Bank program provided one-off financial support, training and consulting for start-ups.

An action and an indicator on awareness creation and role models were included in the women's entrepreneurship strategy, and the SME Development Strategy 2016-2018 includes "supporting women's entrepreneurship" as a priority. However, support at national level is very limited and takes place mostly in the capital. NGOs are often the main promoters of women's entrepreneurship. Overall, since the last SBA assessment, support for women's entrepreneurship has remained stable but there is significant room for improvement.

Going forward, Armenia should enhance its stakeholder coordination on women's entrepreneurship through a structured national partnership, e.g. through the SME Development Council. This partnership should involve all key stakeholders and lead policy design in this area. Thus, the action plan could include promotion activities, such as dissemination of success stories of female entrepreneurs, as well as envisage capacity-building activities – for instance, training to increase women's leadership and management competences. Furthermore, attributing the functions of progress and results monitoring and impact evaluation to an institution, e.g. to the SME DNC, would be an important step toward ensuring the efficiency of measures provided by the strategy and needed flexibility for strategic adjustments. Another key area for improvement would be ensuring the systematic collection of business statistics, including sex-disaggregated data.

Enterprise skills

Although SMEs account for the vast majority of active businesses in Armenia (99.8% in 2017), Armenia's education system remains unable to meet the needs of SMEs, thus creating constraints in terms of SMEs' ability to innovate and increase their competitiveness (Armenia Business Coalition, 2018^[20]). Knowledge of the current and future skills needs of SMEs and financial support for SME training are hence essential to efforts to tap into SME potential.

The SME State Support Annual Program offers assistance in the areas of youth entrepreneurship development, women's entrepreneurship and SME internationalization. SME DNC's membership in the Enterprise Europe Network provides opportunities for enterprise growth and development. In order to strengthen state support for SME participation in the digital economy, the Enterprise Incubator Foundation (EIF) was established (www.eif.am).¹² It is responsible for implementing the State Program on Development of Information Technologies by carrying out a range of activities, from ICT training for SMEs, schools and adults to the organization of coding sessions, competitions and tech talks. In the scope of the "Support for the raising of IT sector competitiveness in Armenia" and "Support for the activities of technological centres" programs, training was offered in digital skills and in operating in the EU Digital Single Market. SME DNC is the body charged with monitoring the effectiveness of state SME support programmes.

Continuous co-ordination at the national level of the collection and analysis of SME skills intelligence is needed to bring together the various information sources from a wide variety of stakeholders. The established Armenian Business Coalition, which has been tasked with providing research that will feed into the development of the new SME strategy, is already a good start in this direction. It is recommended to maintain such efforts, but at the same time to build on the SME Development Council's potential to co-ordinate the wide variety of organizations involving state and non-state stakeholders by economic sector.

Armenia could also ensure the quality of, and expand, its e-training offer through 1) e-training courses that allow for flexible participation (e.g. on-demand online courses) and 2) offline virtual training for rural areas where internet access is limited. Further focus on knowledge acquisition in all fields, from management to entering online markets, is needed to address SME knowledge gaps and boost their competitiveness.

Publishing all available training events for SMEs on the SME DNC website would facilitate access to knowledge, while establishing the SME training quality assurance framework would ensure high quality capacity-building services. Moreover, putting in place regular implementation and impact monitoring of government programmes to improve SME skills would contribute to better resource allocation.

Going forward, three issues appear to be a priority for Armenia. First, integrating the entrepreneurship key competence into the curriculum would help Armenia to consolidate and focus all entrepreneurial learning policies, as well as ensure support at the system level. Second, updating the women's entrepreneurship support strategy and setting up a structured policy partnership would move women's entrepreneurship support to the next level. Finally, in order to support the relevance and quality of training provision, the government could consider establishing a system for collecting and analysing SME skills intelligence.

Pillar C – Access to finance

SMEs' external finance in Armenia is dominated by bank lending, while non-bank alternatives are experiencing a relatively low uptake and could benefit from a strengthening of the legal framework underpinning them. Steps are being taken to support SME financing through a range of government programmes, but monitoring and evaluation of such programmes is not prevalent. Positive steps have been taken to improve financial literacy, and increased efforts to target entrepreneurs specifically could help address some of the access-to-finance issues SMEs face.

Legal and regulatory framework

As is the case in most economies, a pledge over immovable property is the most frequent form of security for banks. The use of pledges of movable assets as a security interest is also common, partly supported by the updated legal framework for collateralised lending put in place shortly after the publication of the last report and the ensuing improvements in the registry for security interests over movable assets. A new online database now allows for the registration and search of pledges, a clear improvement over the assessment in 2016. However, a score of 6 out of 12 possible points in the “Strengths of Legal Rights” index in the World Bank’s *Doing Business 2020* report suggests further room for improvement when it comes to Armenia’s secured transactions framework (World Bank, 2019_[10]). Creditors lack rights to direct the insolvency process, e.g. when it comes to the appointment of an insolvency practitioner and their right to information as well as their approval in the case of a sale of substantial assets of the debtor. In addition, issues have been identified by the EBRD with regard to the regulatory framework for insolvency practitioners, due to lack of proper regulatory oversight by the existing self-regulatory organisation (SRO) of insolvency practitioners and sanctioning of professional misconduct. The existing automated appointment system is proposed to be improved by transferring management of the system from the SRO to the Ministry of Justice. At the same time a greater focus should be placed on improving practitioner skills in the area of recovery and reorganisation rather than liquidation. A draft law to address these issues is awaiting parliamentary approval.

Credit information coverage has further improved from 65.8% during the last assessment to 82.5% through a private credit bureau (World Bank, 2019_[10]). This is partly due to a wider range of information sources. For instance, Armenia is one of the only countries in the region to collect data from utilities. Individuals are entitled to one free copy of their credit report per year. Banking supervision has been strengthened with the adoption of a risk-based supervision framework in 2017, and higher capital requirements have led to recapitalisation and consolidation in the sector. The implementation of Basel III requirements is under way. In addition, foreign currency lending to unhedged borrowers is discouraged by applying higher risk ratings and provisioning requirements on foreign exchange lending compared to loans in local currency.

Sources of external finance for SMEs (bank financing, non-bank financing, venture capital)

Bank intermediation has increased since the last assessment, with bank credit to GDP standing at around 52% as of December 2018, compared to 42% in December 2015.¹³ Looking at both banks and credit organisations, year-on-year credit growth has been in double digits since late 2016. However, more disaggregated data suggests that apart from some stronger growth in business loans throughout 2018, the increase has been largely driven by lending to households. As such, the share of business loans in total lending has declined to 43% as of June 2019 compared to the time of the last assessment, when it stood at around 50%.¹⁴ Furthermore, a high number of banks and credit organisations exist and while some consolidation has taken place in recent years, further consolidation could help more effective and efficient credit allocation in the economy. In this environment, access to finance for SMEs remains an issue even though the extent is difficult to pinpoint due to a lack of SME specific data. Given the substandard quality of financial reporting by many corporates, banks rely heavily on collateral, which exacerbates the access-to-credit problem for SMEs.

There are public programmes in place to facilitate SME access to bank financing, and others are currently in the planning and design stage. Existing programmes focus on sub-sets of SMEs such as, for example, young firms and agricultural producers. Loan guarantees for up to 70% of the principal loan amount are available to eligible SMEs through the Small and Medium Entrepreneurship Development National Centre Fund (SME DNC). Financial support is also available through several programmes managed by the German-Armenian Fund (GAF). Different IFI-funded programmes aimed at improving access to finance for SMEs exist, including for female-owned or -managed enterprises as well as firms active in agriculture and tourism. Finally, the Ministry of Agriculture (now a part of Ministry of Economy) has several programmes in place to support agricultural producers, many of which are SMEs. This includes interest rate subsidies and other support measures. Plans are in place to expand interest rate subsidy programmes, targeting SME finance and the provision of micro-credit. Monitoring and evaluation of the various government programmes is rarely carried out and results are not publicly available.

Access to non-bank financing instruments more generally is underdeveloped. Microfinance is mainly provided through credit organisations. Activities are regulated by the Law on Credit Organizations, but a specific definition of microfinance is missing, which presents operational challenges in the sector. There are plans for reform by drafting a law on microfinance, but this process is at an early stage. Leasing and factoring activities are regulated by provisions in the Civil Code, rather than through a specific law. A law on leasing activities was drafted in recent years to establish a clear legal framework, but it has not been adopted yet. To support the development of the sector, the establishment of a specific support scheme is being discussed, but its details are still to be confirmed. Uptake is low for both instruments at 1% or less of GDP (World Bank, 2019^[3]).

Private equity more generally is not very well developed as a market, and scarce investment opportunities as well as limited exit opportunities have constrained investor appetite. The full implementation of the pension reform could allow a local institutional investor base to contribute to the development of the market. In 2013, Armenia's first venture fund, Granatus Ventures, was launched to invest in start-ups with an IT focus. With a current portfolio of 14 companies and one successful exit, more time will be needed to evaluate the success of the fund. In 2019, the EU and EBRD have provided EUR 16 million to support the launch of the Amber Capital EU-Armenia SME Fund that seeks to raise EUR 70 million for equity investments in Armenian SMEs. Recently, the Business Angel Network of Armenia (BANA, www.bana.am) has been established to bring together investors from Armenia and the Armenian diaspora abroad to support start-ups in the country. This can be an important conduit for providing potential investors with a platform. Beyond that, the government launched a programme in 2018, Neruzh (www.neruzh.am), to support Armenians living abroad who want to return to establish a business in Armenia in their endeavour. Finally, Armenia is enacting legal reforms to allow investment-based crowdfunding platforms to operate in the country. The Central Bank of Armenia, together with the EBRD, is developing secondary legislation to that effect. This could develop into another alternative financing source for small businesses and start-ups.

Financial literacy

Since 2014, no new assessment of the population's financial literacy has taken place. However, the Central Bank of Armenia is planning to conduct a "Financial Capability Barometer" in 2019. A National Strategy on Financial Education is in place and the Central Bank of Armenia carries out training events and workshops; so far these have been targeted at the general population, however. The Central Bank has also put in place a website called

“finInfo” (www.fininfo.am), which provides information on different financial products. These products are mainly targeted at consumers, but agricultural loans are also included. The SME DNC offers financial literacy training targeted at small and microenterprises, with around 400 participants annually.

The introduction of financial education into the secondary school curriculum is underway, with a pilot launched in the 2017-18 academic year. The plan is to roll out mandatory financial education in secondary schools by 2021, including training courses for teachers.

Pillar D – Access to markets

Public procurement

Public procurement is currently regulated by the Public Procurement Law (PPL) of 16 December 2016, Government Decree No. 526-N of 4 May 2017, and several other pieces of secondary legislation. Although a number of the PPL’s provisions reflect obligations under the Treaty on the Eurasian Economic Union, it broadly corresponds to international practice, with the organisation of the review system being one important exception. However, there is no overall strategy for developing the public procurement system, nor for supporting SME participation in it.

A department of the Ministry of Finance has been designated as the authorised body in charge of the regulation and co-ordination of public procurement. Its functions also cover training for contracting authorities and enterprises, as well as administrative support for the two persons reviewing complaints. Complaints can be lodged for a small fee, but the set-up is not considered to fully meet the Government Procurement Agreement (GPA) standards.

Apart from the possibility of dividing tenders into lots, there are no specific provisions in the PPL to facilitate participation by SMEs. Nevertheless, they benefit from a general requirement for proportionality and from the possibility, at the time of tendering, to simply state their compliance with qualification and exclusion criteria, with supporting documentation to be provided only later, if required at all. On the other hand, the obligation to provide a tender security – and the requirement for suppliers to provide evidence of having properly performed at least one similar contract within the year of submission of the bid and three years prior to it – have the effect of restricting participation by many SMEs.

A new electronic procurement system that became operational in 2018 has the potential to facilitate SME participation, but it is limited by its exclusive reliance on price as the only award criterion and by its application exclusively to a specific list of items adopted by the government. In addition, the Ministry of Finance website contains a wide variety of public procurement notices and information; however, many contracts are still concluded without publication of a notice, meaning that the share of non-competitive procedures is fairly high. Website access is open, but several types of notices do not contain full information and refer to .pdf files, meaning that access to more granular data is limited. The annual reports do not detail SME participation.

- With respect to SME participation in public procurement, there has been little progress since 2016, except for the increased potential of the revised e-procurement system – the use of which should however be better promoted; the share of competitive procedures is also improving, but from a very low level. The legal and institutional framework for public procurement and current practices thus still have

room for improvement in several important respects: The requirements for past experience should be simplified, harmonised and made more proportionate.

- The reliance on price as the only award criterion should be decreased.
- Efforts should be made to raise the share of competitive procedures.
- Access to data should be improved in order to better analyse barriers faced by SMEs in public procurement, so that they can be addressed by e.g. preparing more comprehensive guidelines and offering adequate training for both contracting authorities and prospective tenderers.

Standards and technical regulations

Armenia pursues a dual approximation strategy in terms of its quality infrastructure policy. On the one hand, Armenia joined the Eurasian Economic Union (EAEU) in 2014, which entailed both 1) adopting the EAEU's system of standards, conformity assessment and technical regulation and 2) ending previously held negotiations with the EU on a possible Association Agreement (AA). On the other hand, the country had already re-designed its institutional and legislative framework, which remains in place, during the EU AA negotiations.¹⁵ Moreover, Armenia signed a Comprehensive and Enhanced Partnership Agreement (CEPA) with the EU in 2018, which also foresees approximation with EU technical regulations and standards.¹⁶ including considering negotiating an Agreement on Conformity Assessment and Acceptance of Industrial Products (ACAA). In this context, Armenia is aiming at effectively combine the benefits of its participation in EAEU and EU trading blocks.

In recent years, the development of Armenia's national quality infrastructure has somewhat lost momentum. For example, the country has lost ground to other EaP members in terms of the international recognition of the accreditation system, e.g. through lack of a membership in the International Laboratory Accreditation Cooperation (ILAC) or the International Accreditation Forum (IAF) or a Bilateral Agreement (BLA) with the European co-operation for Accreditation (EA). In terms of metrology, the institution and legislative framework are in place, yet the current national strategy developed in 2010 lacks an update and investment into metrology laboratories would help develop industrial services. The faltering dynamic seems to be connected to the political uncertainty and the halt of the approximation process with the EU, which meant putting on hold regular evaluations and capacity building programs that resumed only recently.

This policy approach translates into the following situation in practice for SMEs. Access to markets in other EAEU member states is generally not a problem thanks to common standards, technical regulation and mutual recognition of conformity assessments. Trade with the rest of the world, in particular the EU and the US, requires information about other countries' systems of standards and technical regulation, as well as internationally recognized conformity assessment from accredited laboratories. While different sources of information exist (SME DNC, Enterprise Europe Network, Chambers of Commerce etc.), incomplete international recognition of the country's accreditation system and insufficient domestic supply of conformity assessment services (e.g. de facto monopolies for organic certification, much lower number of conformity assessment bodies than e.g. in Georgia or Moldova) make domestic conformity assessment for international markets expensive, time-consuming and complex.

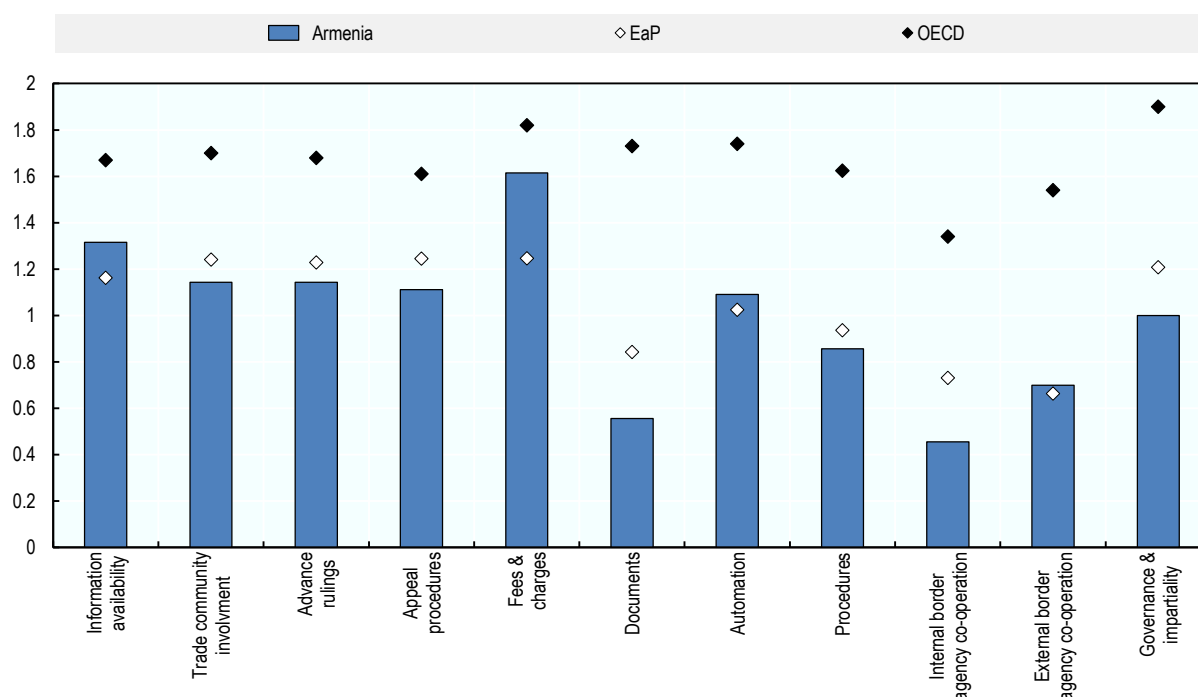
The Ministry of Economy is currently working on a new Quality Infrastructure Strategy for 2020-2025, which should tackle key issues such as creating more competition and offering

conformity assessment services. It also envisages deepening the existing co-operation between the National Institute for Standardisation and the SME DNC for a better and more effective integration of information and consultancy services on quality infrastructure into the SME DNC business services.

SME internationalisation

Although Armenia's total exports increased by 50% from 2014 to 2017 (in real terms), this export growth benefited mostly large companies, with the value of SME exports representing only 13% of total exports in 2017, well below the EU average of 50%. According to the 2020 World Bank *Doing Business* report, Armenia ranks 43rd on trading across borders (up from 110th in 2015), with border compliance still taking 27 hours, more than two times longer than the OECD average (12.8 hours) (World Bank, 2019^[10]). According to the 2017 OECD Trade Facilitation Indicators, Armenia performs slightly below the EaP regional average; moving forward it could, for example, improve both the provision of adequate and timely information on regulatory changes and the capacity of IT systems to exchange documents electronically (OECD, 2017^[21]). Armenia's modest performance in the TFIs, newly added in the scoring of the *SME internationalisation* dimension, contributes to the drop of the score respect to the previous assessment.

Figure 7.5. OECD Trade Facilitation Indicators for Armenia, 2017



Note: TFIs take values from 0 to 2, where 2 designates the best performance that can be achieved.

Source: OECD, Trade Facilitation Indicators Database, <https://oe.cd/tfi>.

StatLink  <http://dx.doi.org/10.1787/888934087287>

The Export-led Industrial Development Strategy adopted in 2011 continues to be the main strategic document guiding policy developments in the area of SME internationalisation. However, its implementation has been limited, with many foreseen programmes still not

operational. Prior to its reorganisation in 2019, Business Armenia was responsible for export promotion activities, such as facilitation of trade missions, SME participation in trade fairs, and informational support and consultancy services. It is not clear which institution will take over the export support and promotion services that were previously provided by Business Armenia. Ensuring that the institutional knowledge of Business Armenia is preserved and effectively transferred to its successor should be a short-term priority for the government.

The SME DNC, with the support of the Enterprise Europe Network, provides mostly information services to SMEs that are interested in export or co-operation with international suppliers. In the area of SME–FDI linkages, Armenia does not provide any support to encourage and facilitate the creation of supply chain linkages between local SMEs and large investors. There is also limited support to enhance the usage of e-commerce as a sales channel for SMEs. Moving forward, Armenia could start providing training and consultation services to improve the export readiness of SMEs and facilitate their integration into global value chains.

The Export Insurance Agency of Armenia (EIA), which has been operational since 2015, is a state-owned institution that provides exporters with export insurance services. In 2018, the total portfolio value of the EIA was USD 16.5 million, with 50 companies benefiting from its services (up from 15 companies in 2015). Moving forward, Armenia could raise awareness among SMEs of the services provided by the EIA and ensure transparency and monitoring of its activities.

Pillar E – Innovation and Business Support

Business Development Services

SME DNC acts as the main public organisation for providing business development services (BDS), including financial support services, to SMEs in Armenia. It operates based on annual action plans containing a list of planned initiatives and corresponding budgets and timeframes.

The government-provided BDS feature a donor-funded, full-cycle support programme for start-ups, including training in marketing, organisation and financial planning, followed by the provision of loans to the best-rated business plans through SME DNC's partner banks and an accompaniment of the start-ups during the following six months. Other services include promotion and branding for goods and services, export assistance and support in the introduction of new technologies, as well as provision of general business information through SME DNC's website (www.smednc.am), which could benefit from regular updates.

In 2018, SME DNC provided 8010 information and consulting services to 4000 start-ups and SMEs and held 314 training sessions, with 96% of beneficiaries operating outside the capital. It had wide geographical coverage through its 10 regional offices; however, at this stage it is unclear if those offices will remain open. As a member of the Enterprise Europe Network (EEN) and in co-operation with EEN partner organisations, SME DNC also offers free consultations and training courses (229 internationalisation training events were held in 2018) as well as providing information on market conditions, European legislation and policies. Start-up support is complemented by Armenia's Enterprise Incubator Foundation, which provides a range of advisory and business services along with incubation facilities, targeting particularly the ICT sector. In addition, the innovation hub Hero House (www.herohouse.am), co-funded by the EU and GIZ, hosts the Armenian StartUp

Academy (www.startupacademy.am) that provides a 12-weeks flagship pre-acceleration program. In general, efforts could be undertaken to offer more targeted support to businesses, based on skills-needs assessments and an analysis of demand and supply of BDS in the country, which have not been carried out in recent years.

Private sector involvement in BDS provision has been ensured through a co-financing mechanism implemented by Business Armenia in the framework of the Export-led Industrial Development Policy. Business Armenia's website lists private sector BDS providers that offer their services at a discounted rate for beneficiaries of the agency (up to 30% of co-financing by Business Armenia), including, among other things, services for certification of products, market information, workforce development and introduction of innovations. However, given the recent reorganisation of Business Armenia it is currently unclear how its functions will be redistributed to ensure the continuity of the services it provides.

While there is no independent impact evaluation of government-provided BDS, there are annual progress reports on the SME strategy published by the Ministry of Economy as well as implementation results presented in SME DNC's annual activity reports. Monitoring could be further improved by complementing programme implementation indicators (number of training events conducted, budget spent, materials distributed) with key performance indicators to better capture programme impact on SME performance.

Innovation policy

The policy framework for innovation in Armenia has not evolved substantially since the 2016 SBA assessment. The "Concept Jump-start Strategy for Designing Innovation Economy", which dates back to 2011, remains the main document outlining the government's vision for increasing the competitiveness of the national economy. Elements of innovation policy and guidelines for supporting SMEs in this direction can be found scattered among other programmatic documents, including the 2015 "Export-led Industrial Strategy". Against this background, a new innovation strategy is expected to be adopted and it should systematise policies and clarify the institutional actors responsible for promoting innovation in Armenia.

The above has not prevented Armenia from continuing and expanding its initiatives to support innovation, which nevertheless remain mostly limited to the IT sector. The Enterprise Incubator Foundation (EIF) is the main actor behind most of Armenia's innovation infrastructure: it has established techno parks in the country's three largest cities (with the support of the World Bank), provides business incubation services and training, and supports SMEs in developing and marketing technical innovations. More recently, two initiatives expected to increase activity in high-value manufacturing and applied sciences have been announced: 1) the "Engineering City", a USD 20 million investment to build a physical environment with research and prototyping laboratories for companies in the automotive, semiconductor, electronics and material science sectors; and 2) the "EU-TUMO Convergence Centre for Engineering and Applied Science",¹⁷ a EUR 25 million EU-sponsored project providing industry-led project-based STEM education along with research facilities for applied sciences and services for start-ups and small technology companies.

Direct financial instruments for innovative SMEs are also available, though they are predominantly donor-driven and somewhat limited in scale. In particular, the EU-funded "Innovation Matching Grant" and the "Science and Technology Entrepreneurship Program" provide SMEs with grants of up to EUR 50 000 with the objective of stimulating

the rate of technology absorption, the commercialisation of research ideas, and collaboration between science and the private sector.

Overall, Armenia's support for innovation for SMEs is available through isolated initiatives, implemented by seemingly unco-ordinated actors, and directed mostly at companies in the IT sector. With the upcoming innovation strategy, the government should build on some of its successful IT-oriented projects to 1) broaden the palette of its policy tools to encompass other sectors of the economy, 2) further develop linkages between research institutions and the business sector, and 3) increase policy co-ordination among the different actors in the innovation ecosystem. Close monitoring to assess the impact of the strategy and of specific policy tools, which is still very limited, should also become a regular exercise performed by the different institutions in charge of innovation policy.

SMEs in green economy

Armenia continues to move forward on improving its approach to greening SMEs, albeit inconsistently across the board. The SME State Support Annual Program 2018 includes “enhancing energy efficiency activities and supply of products and services by SMEs aimed at developing green economy” as a pillar. However, this is not supported by an action plan for implementation, measurable targets, or an expected impact. This limits the government's ability to implement effective policies related to SME greening.

In terms of its environmental regulatory approach for SMEs, Armenia is shifting to a risk-based approach for environmental impact assessments (draft law “On environmental impact assessment and expertise”) as well as for compliance monitoring (2011 amendments to the Law on “Organising and carrying out inspections in the Republic of Armenia”). However, these have yet to be implemented in full.

While the Ministry of Environment and the Ministry of Territorial Administration and Infrastructure are both available to provide guidance to SMEs on an ad-hoc basis, more clearly tasking an agency with outreach to SMEs on greening would be more effective. The SME DNC, for example, may make a better “one-window” approach for SMEs to get information on available green initiatives. It would also increase the potential for outreach to SMEs about the business case for enhanced efficiency, as currently there does not appear to be a high level of awareness among SMEs. Armenia would also benefit from green SME policies that target specific sectors; these are currently limited to supporting small hydroelectric power producers.

Sectoral analysis: SME perspectives on the agribusiness sector in Armenia

Agribusiness is a fast-growing industry in Armenia. The agricultural sector remains essential for the economy of the country as it is the main source of economic activity in rural areas and a significant contributor to GDP. It produces 14.9 % of GDP (as of 2017) and employs about 36.6 % (2017) of the working population (FAO, 2019^[22]). The sector accounts for 14.7% of total exports, with potential for growth (Growth Lab, Harvard University, 2019^[23]). Production is diversified – including fruits and vegetables, dairy, tobacco, and beverages – but the capacities are not sufficient to process the potential production of the agricultural sector.

Evidence collected during the private sector focus group meetings provided important insights on the main barriers faced by SMEs operating in the agribusiness sector in Armenia:

- Despite subsidised interest rates for bank loans for specific projects (e.g. leasing of agriculture machinery, investments in drip irrigation or anti-hail protection systems), SMEs report difficulties in accessing finance due to stringent collateral requirements. In addition, entrepreneurs often have to provide banks with personal properties as additional guarantees.
- The poor conditions of the irrigation infrastructure in rural areas – water loss reaches 80% in some areas – as well as low availability of fertilisers and pesticides significantly affect the productivity of food producers.
- Limited logistics and transport infrastructure are a major problem faced by food producers willing to reach international markets. For some destinations (e.g. UAE), there is no alternative to shipment by air, which limits capacity, volume and weight.
- The costs of certification are high due to an oligopoly of conformity assessment bodies (e.g. for organic certification). In addition, SMEs often have to contract with foreign-based certification bodies to export to the US or the EU, with extra costs attached.
- Although labelling and marketing regulation is in place, in practice it is rarely applied. This hampers innovative SMEs' access to the domestic market – especially organic food producers facing unfair competition with fake products labelled as organic. Retailers reinforce the competition by paying little attention to the origin or the specificities of products.

Given the aforementioned challenges, the government could consider the following next steps:

- Developing agribusiness is a precondition for an export-based agriculture sector in Armenia. The government could enhance the provision of targeted support programmes or expand the existing ones. For instance, promoting alternative sources of financing for small food processors would allow them to modernise their equipment and pay for certification.
- Promoting the creation of supply chain linkages between food retailers and small food producers would also allow the latter to upgrade their packaging and marketing practices and better promote their products – and would encourage them to engage in larger markets despite the tax threshold.

The way forward

Armenia has experienced modest progress since 2016, and the government has embarked on an ambitious reform journey that includes SME development among its priorities. The following measures could be considered by the government to further strengthen the system:

- Armenia could step up its efforts to create a level playing field for all firms through actions in the area of competition, contract enforcement and business integrity. To stimulate competition, Armenia could prioritise effective enforcement against illegal cartels; this will require functioning tools and procedures, including highly qualified staff in the competition authority and the extension of legal deadlines for cartel investigations. In addition, in order to attract and retain highly qualified lawyers and economists, SCPEC's budget should be increased to allow for higher staff salaries and office equipment. To provide for efficient enforcement of

contracts, Armenia should continue its court automation efforts and reforms in the justice sector. In addition, promoting ADR use by SMEs through awareness-raising activities and the introduction of specific incentives could help build ADR culture within the Armenian business community. Furthermore, when elaborating anti-corruption policy, conducting a study of corruption risks in the private sector with a focus on SMEs (in close co-operation with companies and business associations) would be an important step towards an evidence-based business integrity policy. In order to effectively prevent and prosecute corruption, Armenia might also consider establishing a mechanism for criminal liability of legal persons for corruption.

- The Armenian government has conducted a proactive SME policy since the early 2000s. To further develop the institutional and regulatory framework, Armenia should finalise and adopt its draft SME Development Strategy 2020-2024. Its effectiveness as a policy tool would depend on the introduction of clearly defined objectives, reasonable quantitative targets, results-based key performance indicators and a detailed action plan containing priority actions and a full costing of measures. Moreover, the SME operational environment would benefit from an assessment of the impact of the current simplified tax regimes and incentives that apply to microenterprises and family business, to ensure that they are not hindering enterprises' growth through possible hidden incentives. Finally, Armenia should strengthen its bankruptcy prevention measures by introducing into its insolvency framework pre-insolvency tools and training, early-warning systems and insolvency-related proceedings at the early stage of financial distress.
- As regards the way forward for the area of entrepreneurial human capital, in *entrepreneurial learning*, Armenia should move beyond a financial and economic literacy focus towards the development of entrepreneurship key competence. This includes integration of entrepreneurial learning outcomes in education curricula across various subjects, introduction of active teaching and learning methods, offering practical entrepreneurship experience to all learners and support to pre- and in-service training for teachers and school/university managers – to prepare them for competence-based approach in education. It is also important to improve cooperation between education institutions and businesses in the area of entrepreneurial learning and ensure the development of entrepreneurship key competence when designing work-based learning in VET and higher education. Such reform steps should be reflected in the government strategies and action plans and supported by the national policy partnership.

For *women's entrepreneurship* support, Armenia should enhance stakeholder coordination through a structured national partnership, and agree on a new action plan including: promotion activities (such as dissemination of success stories of female entrepreneurs), as well as capacity building actions (for instance, training to increase women's leadership and management competences).

On *SME skills* support, Armenia needs to focus on the collection and analysis of skills intelligence, as well as on progress monitoring and impact evaluation of the skills support measures. Extending the SME Development Council's scope and introducing working groups on entrepreneurial learning and women's entrepreneurship could be considered. It is important to build the Council's potential to co-ordinate a wide variety of stakeholders across all policy areas of human capital development. SME DNC's role in the evaluation of effectiveness and

efficiency of support measures is critical, and its capacity for systematic collection of business statistics, including sex-disaggregated data, should be supported.

- Further steps should be taken to improve SME access to finance, in particular by strengthening the legal framework for secured creditors and improving creditor involvement in insolvency proceedings. This would bring regulation more in line with international best practice and could help stimulate SME lending by reducing associated risks. A range of financing support programmes is in place and new ones are being developed; however, monitoring and evaluation is not regularly part of programme design and, even when it is carried out, the results are not available to the public. Putting in place a process to evaluate public programmes is an important step in determining effectiveness and drawing lessons for the design of future programmes. Adopting specific legal frameworks, for microfinance and leasing in particular, could help provide certainty for those sectors and transactions. This could support the supply of related services and open up the possibility of developing more-sophisticated products. It would be an important step in diversifying sources of funding for SMEs and allowing for the tailoring of financial products to different needs. Finally, expanding information sources and financial education awareness-raising campaigns to target entrepreneurs specifically would help provide SME owners and managers with the skills necessary to improve their accounting and business planning and enable them to take advantage of different financing products. For example, an online platform with explanations of different business relevant financial products and information about their availability can help close information gaps. Having a credible and reliable platform can go a long way in supporting the diversification of funding sources, by raising the awareness of small business owners who tend to have fewer resources to shop around. This could be done through a new portal or added to existing resources, such as the information website FinInfo.am.
- In order to further facilitate SME access to markets, the government should consider additional actions in the area of public procurement, standards and technical regulations, as well as export promotion. With regard to public procurement, the use of e-procurement could be better promoted; the requirements for past experience should be simplified, harmonised and made more proportional; and additional award criteria (other than price) could be considered for awarding contracts. Moreover, the share of competitive procedures could be raised, and the generation and accessibility of data on SME participation enhanced. Finally, the capacity of contracting authorities and prospective tenderers could be strengthened through adequate training. Even though access to markets in other EAEU member states is generally not a problem, Armenia could seek international recognition of the country's accreditation system – for example, by joining the International Laboratory Accreditation Cooperation (ILAC) or the International Accreditation Forum (IAF) or by concluding a Bilateral Agreement (BLA) with the European co-operation for Accreditation (EA). In terms of metrology, Armenia could invest more in metrology laboratories, which need to be modernised to better help develop industrial services. SME internationalisation can be further improved through the provision of adequate and timely information on regulatory changes as well as through the possibility of IT systems for exchanging documents electronically. The government should also ensure that the institutional knowledge of Business Armenia is preserved and effectively transferred to its successor. Once established, the new agency could consider providing training and consultation on the export

readiness of SMEs, raising awareness for the services provided by the EIA, and ensuring transparency and monitoring of its activities.

- To further improve the performance in Innovation and Business Support, actions could be taken to offer more targeted support to businesses, based on skills needs assessments and an analysis of demand and supply of BDS in the country. Better monitoring and evaluation systems could help assess the impact of support programmes on SME performance. To support innovation, Armenia could expand its initiatives to promote innovative companies beyond the IT sector, further develop linkages between research institutions and the business sector, and increase policy co-ordination among the different actors in the innovation ecosystem. Finally, in order to move forward on improving its approach to greening SMEs, Armenia should develop a clear implementation plan on support for SME greening, including measurable targets and expected impact, so as to allow for the enforcement of effective policies. In addition, the government should provide a single point of access for SMEs to obtain information on green practices (i.e. through SME DNC).

Conclusion

Table 7.5. Roadmap for policy reforms – Armenia

Promoting a level playing field for all enterprises
<ul style="list-style-type: none"> • Enable and prioritise enforcement against hard-core cartels by giving SCPEC effective investigation tools. • Increase budget of SCPEC to allow for recruitment of highly qualified staff and to ward off corruption risks. • Conduct a study of corruption risks in the private sector in close co-operation with companies and business associations to underpin the design of integrity measures under the new Anti-Corruption Strategy. • Introduce criminal liability of legal persons for corruption, including providing for an efficient enforcement mechanism. • Promote business integrity measures adoption by SMEs through awareness-raising activities. • Continue implementing the e-justice system to ensure effective automation of planned court procedures. • Ensure that judges treating IPR-related cases have sufficient knowledge in IP law and experience for quality dispute resolution. • Promote ADR use by SMEs for commercial dispute resolution through awareness-raising campaigns and leveraging legal incentives for ADR use by businesses.
Strengthening the institutional and regulatory framework and operational environment for SMEs
<ul style="list-style-type: none"> • Ensure participatory process in the finalisation and adoption of the new SME development strategy, setting clearly defined objectives, reasonable quantitative targets, key performance indicators and priority actions. • Assess the impact of the special tax regime and other tax incentives applied to microenterprises and family business to determine possible hidden incentives discouraging enterprise growth. • Upgrade the e-government strategy, elaborate an implementation action plan and mobilise the necessary resources. • Take action to adopt an open-data approach in the framework of e-governance. • Streamline the insolvency legislation, in particular on creditors' participation in the decision-making process, avoidance of pre-insolvency transactions or access to restructuring procedures for SMEs. • Introduce insolvency prevention measures (information tools and early-warning system). • Implement a comprehensive and proactive second-chance strategy.
Promoting skills and entrepreneurship development
<ul style="list-style-type: none"> • Consolidate and focus all entrepreneurial learning policies and support at the system level by integrating the entrepreneurship key competence into the curriculum. • Move women's entrepreneurship support to the next level by agreeing on the update of the women's entrepreneurship support strategy and setting up a structured policy partnership. • Establish a system for collection and analysis of SME skills intelligence as a way to support relevance and quality of training provision.
Facilitating SME access to finance
<ul style="list-style-type: none"> • Complete reforms to the insolvency and restructuring legal framework to strengthen creditor rights, improve the insolvency framework and promote corporate recovery. • To improve awareness, establish an information platform containing details about financial products relevant to business owners.

Supporting SME access to markets

- Ensure transfer of institutional knowledge and capacity to Business Armenia's successor.
- Increase awareness and enhance the provision of export support and promotion services, including training and consultancy services to SMEs.
- Promote expansion of conformity assessment services and ensure competition between domestic conformity assessment (CA) bodies.
- Work towards full international recognition for the national accreditation body.
- Increase the use of e-procurement, while promoting the use of award criteria other than price only.
- Build the capacity of the contracting authorities to ensure wider competition, with greater transparency.
- Improve access to data, analyse issues SMEs face in public procurement and address them through more-comprehensive guidelines and adequate training for both contracting authorities and prospective tenderers.

Enhancing SME competitiveness

- Broaden the palette of policy tools available to support innovative companies beyond IT sector.
- Further develop linkages between research institutions and the business sector.
- Increase policy co-ordination among the different actors in the innovation ecosystem with an Innovation Strategy and action plans.
- Improve monitoring and evaluation of current support programmes, measuring the impact of support programmes (particularly BDS) on SME performance.
- Provide a single point of access for SMEs to get information on green practices (i.e. through SME DNC).
- Develop a clear implementation plan on support for SME greening, including measurable targets and expected impact.

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Notes

¹ The SME Development National Centre of Armenia, <http://www.smednc.am>.

² Sectors include section B to N, the sector S95, excluding the sector K - financial intermediation services of ISIC rev. 4.

³ So-called “dawn raids” are surprise onsite inspections conducted by competition authorities. They can be a critically important tool for anti-cartel enforcement, in particular.

⁴ As foreseen by Judicial Code of Armenia, Art 42, para 4,5, cases requiring a certain type of expertise are assigned to the judge specialized in the matter within the general competence court.

⁵ Applicability of sanctions in case of failure to disclose the final owners of the company to be seen following February 20, 2020, as indicated by the Law.

⁶ Law No. HO-97-N of June 9, 2017.

⁷ <https://bizprotect.am/en/>

⁸ <https://www.enterprisesurveys.org/data/exploreeconomies/2013/armenia>

⁹ As of October 2019, <https://www1.oanda.com/lang/it/currency/converter/>

¹⁰ Idem.

¹¹ Idem.

¹² Other programmes providing training in ICT sector are Microsoft Innovation Centre Armenia (jointly established by USAID, Microsoft Corporation and EIF in 2011) and ISTC Foundation (jointly founded by IBM, USAID, Armenian Government and Enterprise Incubator Foundation in 2015).

¹³ Loans provided by banks only; excludes other financial service providers such as credit organisations.

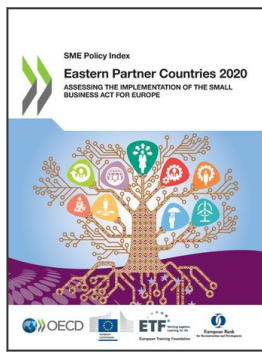
¹⁴ Own calculations based on data by Central Bank of Armenia (Monetary and Financial / Real Sector statistics).

¹⁵ Quality Infrastructure Policy 2010-2020 (2010), e.g. Law on Technical Regulations (2012), Law on Standardization (2012).

¹⁶ see CEPA, Art. 130:

<https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A52017JC0037>.

¹⁷ <https://www.convergence.center/>



From:

SME Policy Index: Eastern Partner Countries 2020

Assessing the Implementation of the Small Business Act for Europe

Access the complete publication at:

<https://doi.org/10.1787/8b45614b-en>

Please cite this chapter as:

OECD, *et al.* (2020), “Armenia: Small Business Act country profile”, in *SME Policy Index: Eastern Partner Countries 2020: Assessing the Implementation of the Small Business Act for Europe*, OECD Publishing, Paris/European Union, Brussels.

DOI: <https://doi.org/10.1787/95f303db-en>

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