



**EUROPEAN NEIGHBOURHOOD AND PARTNERSHIP  
INSTRUMENT**

**ARMENIA**

**COUNTRY STRATEGY PAPER  
2007-2013**

## **Table of contents**

|  |    |
|--|----|
| 1. EXECUTIVE SUMMARY .....   | 4  |
| 2. THE OBJECTIVES OF EU/EC CO-OPERATION WITH ARMENIA .....   | 4  |
| 2.1. Overall external policy goals of the EU .....   | 4  |
| 2.2. Strategic objectives of EU/EC cooperation with Armenia.....                                     | 5  |
| 3. AN OUTLINE OF THE ARMENIAN POLICY AGENDA .....  | 6  |
| 3.1. General aspects.....  | 6  |
| 3.2. Internal Policy .....   | 6  |
| 3.3. The Conflict over Nagorno Karabagh.....   | 7  |
| 3.4. External Policy .....   | 7  |
| 4. THE POLITICAL, ECONOMIC, SOCIAL AND ENVIRONMENTAL<br>SITUATION.....                               | 8  |
| 4.1. General Aspects: .....  | 8  |
| 4.2. The political situation.....  | 8  |
| 4.3. The economic situation and trade structure .....  | 10 |
| 4.4. Analysis of social developments .....   | 11 |
| 4.5. Analysis of the environmental situation.....  | 12 |
| 4.6. Perspectives .....  | 12 |
| 5. OVERVIEW OF PAST AND ONGOING EC ASSISTANCE .....  | 13 |
| 5.1. EC assistance to Armenia 1991-2006 .....  | 13 |
| 5.2. Key lessons learnt for the new programming cycle .....  | 14 |
| 5.3. Coordination and complementarity with other donors.....   | 15 |
| 5.4. Consistency of EC cooperation policy with other core policies of the EU<br>(“policy mix”) ..... | 16 |
| 6. THE EC RESPONSE STRATEGY .....  | 16 |
| 6.1. Principal objective.....  | 16 |
| 6.2. EC assistance priorities .....  | 17 |
| 6.3. Instruments and means .....   | 20 |
| ANNEX 1 .....  | 24 |
| LIST OF ABBREVIATIONS AND ACRONYMS.....  | 24 |
| ANNEX 2.....   | 25 |
| ARMENIA AT A GLANCE.....   | 25 |
| ANNEX 3.....   | 28 |
| DRAFT COUNTRY ENVIRONMENT PROFILE.....   | 28 |

ANNEX 4..... 31

ACTIVITIES OF OTHER DONORS, INCLUDING MEMBER STATES..... 31

ANNEX 5..... 33

“POLICY MIX” CONSIDERATIONS IN THE CONTEXT OF THE ARMENIA CSP 33

## **1. EXECUTIVE SUMMARY**

This Country Strategy Paper (CSP) for Armenia covers the period 2007-2013. Assistance to Armenia over that period will principally be provided under the new European Neighbourhood and Partnership Instrument (ENPI) which is being established to provide assistance for the development of an area of prosperity and good neighbourliness involving the European Union and the partner countries covered by the European Neighbourhood Policy (ENP)<sup>1</sup>.

Funding levels for Armenia under the national ENPI allocation are currently estimated at € 98,4 million for the period 2007-2013. In addition, Armenia will benefit from allocations under the ENPI regional programme and from allocations under CBC (Black Sea Programme), thematic and nuclear programmes.

The principal objective of EU-Armenia cooperation at this stage is to develop an increasingly close relationship between the EU and Armenia, going beyond past levels of cooperation to a deepening of political cooperation and accompanied by continued economic growth and continued results in poverty reduction.

EC assistance over the period covered by this strategy will help to achieve the above policy objectives. Under the National Indicative Programme (NIP) 2007-2013 this translates into priority support for three strategic categories:

- i) Strengthening of democratic structures and good governance;
- ii) Further support to regulatory reform and administrative capacity building;
- iii) Support for poverty reduction efforts

The new Strategy Paper for Armenia has been developed in close consultation with the Armenian authorities and fully reflects national priorities. Member States, other donors and civil society organisations have been consulted during the drafting process.

## **2. THE OBJECTIVES OF EU/EC COOPERATION WITH ARMENIA**

### **2.1. Overall external policy goals of the EU**

As a global player, the EU promotes its standards, values and interests through the use of various instruments, ranging from the Common Foreign and Security Policy (CFSP), assistance and trade to the external dimension of the EU's internal policies.

In particular, the EU strives to promote prosperity, solidarity, security and sustainable development worldwide.

Of utmost importance for the EU is the determination of the right "policy mix". This means that in the light of the EU's strategic external relations objectives policy coherence needs to be ensured between all available instruments in dealing with Armenia.

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<sup>1</sup> **Regulation 1638/2006.** Armenia may also benefit from assistance under the Stability Instrument.

## **2.2. Strategic objectives of EU/EC cooperation with Armenia**

A combination of country-specific, regional and global strategic objectives shape the EU/EC's approach to cooperation with Armenia:

### ***A mutually beneficial partnership promoting Armenia's reform agenda***

The EU and Armenia commit themselves in the Partnership and Cooperation Agreement (PCA), which came into force on 1 July 1999, to a partnership which provides for close political and mutually beneficial trade and investment relations as well as economic, social, financial and cultural cooperation. The partnership is intended in particular to promote Armenia's transition to a fully fledged democracy and market economy.

### ***Implementing the European Neighbourhood Policy (ENP) and the EU-Armenia ENP Action Plan***

The objective of the ENP is to share the EU's stability, security and prosperity with neighbouring countries, including Armenia, in a way that is distinct from EU membership. The ENP is designed to prevent the emergence of new dividing lines in Europe by offering neighbouring countries closer political, security, economic and cultural cooperation. It also addresses one of the European Union's strategic objectives set out in the European Security Strategy of December 2003, namely bolstering security in the EU neighbourhood. ENP partners are expected to benefit from closer cooperation with the EU, the chance to participate in EU programmes and a stake in the EU's internal market, which will strongly support their own political and economic reforms.

The EU and Armenia have therefore agreed to specific objectives in an ENP Action Plan endorsed by the EU-Armenia Cooperation Council on 14 November, 2006..

### ***Security Challenges***

In the European Security Strategy of 12 December 2003 the EU acknowledged that as a Union of 25 States with over 450 million people producing a quarter of the world's Gross Domestic Product (GDP), it is inevitably a global player.

One of the key policy implications of the European Security Strategy is the need for the EU to "promote a ring of well-governed countries to the East of the European Union and on the borders of the Mediterranean with whom we can enjoy close and cooperative relations". In addition to this, the Strategy clearly acknowledges the importance of promoting an international order based on effective multilateralism.

In this context the EU aims to stabilise the whole Southern Caucasus region and attaches great importance to the peaceful resolution of the conflict over Nagorno Karabagh. It is actively involved in ongoing efforts to achieve a settlement, amongst other things through the good offices of the EU's Special Representative for the Southern Caucasus.

### ***Development policy objectives***

The EU's development policy as expressed in the European Consensus for Development is driven by the primary objective of poverty reduction, with the complementary aims of promoting good governance and greater respect for human rights in a bid to ensure the

stability and security of the countries concerned in the regional context.. At the same time, it emphasises the need for a differentiated approach depending on the context and the particular needs of individual states. These objectives also apply to Armenia, in order to promote achievement of the Millennium Development Goals.

With a GNI of USD 1.326 per capita (2005/ source: IMF) Armenia is classified as a lower middle income country in the OECD's Development Assistance Committee (DAC) list of aid recipients. Account must therefore be taken of development policy objectives and in particular of the Millennium Development Goals (MDGs) in defining cooperation objectives with Armenia. In this context it is important to note that an Economic Growth and Poverty Reduction Strategy Paper for the period 2004-2006 was adopted by the government in August 2003 and approved in November 2003. A PRSP update should be ready by the end of 2006.. A "First National Report on MDGs in the Republic of Armenia" was adopted and published by the GoA in 2001.

### 3. AN OUTLINE OF THE ARMENIAN POLICY AGENDA

#### 3.1. General aspects

Since Armenia's **geopolitical situation** is highly complex (land-locked country, closed borders to the West with Turkey and to the East with Azerbaijan), its foreign policy is based on the pursuit of "multidirectional complementarity" whereby the country seeks to maintain strong relations with other relevant partners like the EU, Russia and the US. However, Armenia has especially welcomed the EU's enlargement in May 2004 and its inclusion in the European Neighbourhood Policy in June 2004. More recently a clear preference for Europe and a tendency towards better EU integration and acceptance of EU common values and standards has become very obvious.

On this basis, Armenia's policy objectives could be summarised as follows:

#### 3.2. Internal Policy

***Consolidating democracy, the protection of human rights and fundamental freedoms:*** Armenia is clearly committed to improving the stability and effectiveness of institutions guaranteeing democracy, the protection of human rights and fundamental freedoms.

***Consolidating the rule of law:*** Especially after the Constitutional Reform (final referendum on 27 November, 2005) the Government of Armenia (GoA) is committed to promoting judicial reform in order to ensure an independent judiciary, to strengthen its administrative capacity and to ensure impartial and effective prosecution. Important steps have already been taken in this regard, in particular towards a more independent, a better trained and better organised judiciary (judges and prosecutors) and through legislative and organisational reforms.

***Effective fight against corruption:*** Armenia acceded to the Council of Europe's Group of States against Corruption (GRECO) in 2003. In June 2004 a Council to fight corruption was established with the task of supervising the implementation of a three-

year anti-corruption strategy designed with major donors and approved in November 2003.

***Public sector reform:*** The government has also embarked on an ambitious programme of comprehensive public sector reform, including the administrative and regulatory reforms necessary to improve public governance and local self-government.

***Improving the investment climate:*** Actively addressing the broad range of issues affecting the investment climate with a view to strengthening investors' confidence is a key component of the government's approach to further economic growth. In this respect the creation of an environment of free economic competition and continued reforms of the financial sector, tax and custom systems as well as further development of the agricultural sector are on the GoA's agenda.

***Improving welfare, reducing poverty and enhancing the provision of social services:*** Within the PRSP the government has committed itself to implementing anti-poverty measures as well as improving social services, education and access to health protection in particular at regional and local level.

***Security of energy supply:*** This is an issue of major concern to the Armenian authorities and they are looking into ways of guaranteeing the security of energy supplies by developing alternative energy sources (thermo / hydro / wind), through the continued use of nuclear power and diversifying gas supply by setting up a gas pipeline connection with Iran. Despite this policy of diversification, it appears that the energy sector in Armenia is increasingly coming under Russian influence, if not control.

### **3.3. The conflict over Nagorno-Karabakh**

Finding a peaceful solution to the conflict over Nagorno-Karabakh is always described a key priority of the Armenian government despite present difficulties in reaching agreement with Azerbaijan on a framework for peace settlement.

### **3.4. External policy**

***Orientation towards the European Union and greater integration into co-operation arrangements in Eastern Europe:*** Armenia has put orientation towards the European Union firmly at the centre of its political agenda and is systematically pursuing a policy of EU integration.

***Other regional initiatives:*** Due to its land-locked situation Armenia is also committed to greater involvement in other regional cooperation initiatives within the Black Sea region and in the so-called Baku initiatives to promote regional cooperation on transport and energy. Armenia participates also actively in the TRACECA Secretariat and in TRACECA meetings.

***Promoting trade:*** Armenia became a member of the WTO on 5 February 2003. Trade policy issues are therefore at the heart of the government's economic strategy. Achieving full compliance with WTO requirements and further regulatory approximation with the EU acquis on several trade-related issues envisaged in the PCA and the ENP Action Plan should help Armenia to increase and diversify exports.

For the time being, the country benefits from the EU Generalised System of Preferences (GSP), but intends to qualify for the “GSP + “.

#### 4. THE POLITICAL, ECONOMIC, SOCIAL AND ENVIRONMENTAL SITUATION

##### 4.1. General Aspects:

|  |   |                             |
|--|---|-----------------------------|
| Area 29.700 km <sup>2</sup>            | Population: 3.0m in 2005                        | GNP/Capita EUR 1339         |
| Real GDP growth rate<br>>10% 2001-2005 | Real level of 2005 GDP as<br>% of 1989 GDP: 98% | Inflation rate 0.6% in 2005 |

Armenia’s political, economic and security situation is heavily influenced by its geographic position as a landlocked country with closed borders to the West (Turkey) and the East (Azerbaijan) with no energy resources at all and a persisting conflict over Nagorno-Karabakh with Azerbaijan.

Much of Armenia’s future progress will depend on improved relations with neighbours, re-opening of closed borders and successful and peaceful conflict settlement. These issues have so far limited Armenia’s internal development especially in the social, institutional and economic sectors and in building up a stable and secure energy supply. The difficult political situation has also impeded the country’s involvement in regional cooperation activities.

##### 4.2 Political situation

As regards its **internal political situation** Armenia is a Presidential Republic based on the principle of the separation of powers. Its Constitution was adopted in 1995, but underwent considerable reform by the end of 2005. The Constitutional Reform 2005 was one of the core commitments undertaken by Armenia upon accession to the Council of Europe (CoE). The amendments envisage a more balanced distribution of power within the central government structure as well as increased independence of the judiciary, the media and local self government bodies from the executive branch. The reform was positively assessed by the OSCE and the Venice Commission of the CoE but considerable follow-up reform efforts are needed to make it a full success.

The latest presidential and parliamentary elections were held in Armenia in 2003. OSCE/ODIHR stated that the parliamentary elections marked an improvement over the 2003 presidential election in both campaign and media coverage but fell short of international standards for democratic elections in a number of key respects, in particular the counting and tabulation of votes. The reports on both elections set out detailed recommendations including changes to the legislative framework, notably the electoral code and improvements in electoral administration. The opposition organized demonstrations because of these irregularities and a large number of administrative arrests was made, the offices of several political parties were raided and attacks against journalists took place. As a result of these events, Armenia’s parliamentary opposition

has been observing a partial boycott of parliament which still hampered the work on the revision of the Constitution and electoral code in 2005 and continues until today.

Irregularities were again reported during the Constitutional Referendum in November 2005 and led to urgent requests from the EU and Member States that improvements should be made ahead of parliamentary and presidential elections in 2007 and 2008.

Otherwise, the internal political situation in Armenia has remained relatively stable in recent years with a three party coalition running the country. Only recently one party left the governing coalition. However, the latter still has a majority.

For several years now the governing coalition has been committed to continued structural reforms that are necessary to build a democratic state and a competitive market economy. However, despite progress in the economic and social spheres over the last few years, structural change and consolidation of what has been achieved so far is still necessary. Further democratic and economic reforms, poverty eradication, promotion of the rule of law and human rights, the fight against corruption and conflict resolution are substantial challenges for the years to come and for the European Neighbourhood Policy in Armenia.

Whereas the reform process in the economic sphere has progressed very well in recent years, the reform process in the political and institutional sphere has been proceeding on a different path; democratic structures and the rule of law should therefore be an important area on which cooperation between government and donors could focus.

Concerning **Armenia's external situation** the conflict over Nagorno-Karabakh and closed borders with Turkey as well as Azerbaijan hinder Armenia's development considerably. Much of the country's future overall progress will therefore depend on successful conflict settlement and on the normalisation of relations with neighbours.

The Armenian foreign policy agenda is clearly dominated by the **NK conflict** and efforts towards peaceful conflict settlement continue with the support of the OSCE Minsk Group as a mediator. A breakthrough for a peace agreement was expected at the last meetings between President Kocharian and his Azerbaijani colleague Aliyev in Rambouillet (February 2006) and in Bucharest (June 2006). However, no deal was struck on those occasions. This triggered some disappointment in the international community, which felt that both countries should have better exploited an election-free year. After an interruption for several months FMs of both countries started to meet again in early October 2006.

Relations with **Turkey** continue to be "non-existent". Apart from differences over each country's interpretation of the tragic events of 1915, which Armenia wants Turkey to recognise as genocide, borders remain closed from the Turkish side and there are no diplomatic relations. After the start of EU-Turkey accession talks, Armenian President Kocharian wrote to President Barroso and several Commissioners in order to request that the opening of Turkey's border with Armenia and the normalization of relations between Turkey and Armenia (= "good neighbourly relations") should be at the top of the agenda for accession negotiations. However, apart from an exchange of letters between Turkish President Erdogan and Armenian President Kocharian in 2005, no further bilateral contacts have been reported.

**Russian-Armenian relations:** From the three SC countries Armenia has closest relations with Russia. Especially in the energy sector Russian influence seems to be growing despite the GoA's efforts to diversify and secure energy supply through diversification of energy sources and to create storage facilities. Russia holds financial control until 2008 over the ageing Medzamor Nuclear Power Plant (MNPP) which still covers around 40% of Armenia's energy needs and continues to represent a considerable risk for the whole of Europe due to its age and its location in a highly seismic zone.

The EC and other donors continue to provide nuclear safety assistance to the plant and continue to urge the GoA to prepare a strategy for early decommissioning and to develop alternatives to nuclear energy supply. The ENP Action Plan confirms Armenian intentions to shut down the plant before 2016, once sufficient alternatives are in place. However, whereas consensus on a definite final closing date and on decommissioning have not been reached for the time being, Armenia is serious about building a new nuclear option. Chances are high that cooperation with Russia on this will continue.

In a very recent move Russia also invested €250 million during 2006 in the Hradzan V Thermo Power Plant Project. However instead of paying money, Russia will keep gas tariffs at €55 instead of €110 as with other Russian trading partners.

### 4.3 The economic situation and trade structure

Armenia has enjoyed a very strong **economic** performance with double-digit growth rates for several years. Real GDP increased on average 12.3% annually during 2001-2005. Growth has been driven in particular by investment and consumer spending, supported by remittances and increases in private disposable income. The high growth is particularly visible in the booming construction sector. Growth in the industrial sector and agriculture has been more moderate, while services have performed well. Investment and productivity increases have been supported by continued progress with structural reforms although bureaucracy, corruption and limited access to finance still contribute to a weak business climate. Macroeconomic stability is supported by prudent monetary and fiscal policies. A significant appreciation of the Dram is however weakening external competitiveness and harming beneficiaries of dollar-denominated remittances.

Remittances from the Armenian Diaspora have contributed significantly to the economy. Transfers officially amount to about 8% of GDP, but unofficial estimates are much higher. Remittances appear to have been mostly invested in housing, land, education and small businesses.

FDI net inflows increased slightly to about USD 250 million (5% of GDP) in 2005, while portfolio investment and other investment flows remain almost negligible. The GoA is determined to further improve the investment atmosphere in order to attract new investment.

The social situation in Armenia remains marked by sharp inequalities and strong social polarization. Despite the good macroeconomic performance and commendable achievements to fight poverty within the framework of the Government's Poverty Reduction Strategy Paper (PRSP), adopted in August 2003 (Armenia is ahead of schedule in reaching the benchmarks set by the PRSP), 32% of the population are reportedly still living below the poverty line<sup>2</sup>. Reported unemployment is around 8%, though unofficial estimates suggest figures closer to 20-25%. Dependency on self-

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<sup>2</sup> 2003 figure. Defined as household expenditure of less than US\$ 24 per month. Source: IMF.

employment activities and/or informal activities in the shadow economy is high. An update of the PRSP is expected in late 2006.

Tax revenues increased significantly in 2005-2006, although from a very low level, making it easier for the GoA to spend on social security, health and education in accordance with the PRSP. The 2006 budget continues to focus on social spending, mainly healthcare and education. According to GoA's planning public sector salaries will be raised and more resources will be spent especially on improvement of infrastructure.

Decommissioning of the Medzamor nuclear power plant will have significant fiscal implications. Despite longstanding international requests to close down Medzamor, the power plant continues to cover 40 % of Armenia's electricity consumption. The international community remains worried because this type of nuclear power plants cannot be upgraded to current safety levels and because Medzamor is located in a highly seismic zone. The GoA has now decided to build an even bigger new nuclear power plant in the same area when Medzamor is decommissioned. In the EU's view it remains doubtful whether such action is needed in order to generate sufficient replacement capacity. The country has developed enough alternative energy sources to replace the 400 Megawatt currently stemming from Medzamor. Current Armenian ideas go however towards export of energy.

Armenia's external trade remains very low and little diversified (main exports are base metals and precious stones) in spite of Armenia being a WTO member since 2003 and benefiting from the EU's GSP. Improvements in this regard should be pursued as a matter of priority. The current account deficit decreased slightly to about 4% of GDP in 2005. The current account and debt position is sustainable.

The EU is Armenia's main trade partner, accounting for 46.5% of Armenia's exports and 28.2% of its imports. EU-Armenia trade has been growing over the last five years, but similarly to Armenia's trade with the world in general, it is still very low and non-diversified. Exports to and imports from the EU increased to about €416 million and €528 million, respectively, in 2005.

#### **4.4. Analysis of social developments**

As indicated above, economic growth has started to have an impact on poverty; however, regional disparities have widened as the rise in living standards is concentrated in the capital Yerevan whereas other regions have been largely left behind. About 5% of the population still live in temporary shelter (refugees and those in the 1988 earthquake zone).

The World Bank estimates that Armenia is likely to meet the Millennium Development Goals for gender and education, may meet the goals for poverty reduction, infectious diseases and environmental sustainability, but is unlikely to meet those on child mortality and maternal health.

Emigration has radically changed Armenia's demographics during recent years and the labour force has declined since the beginning of the 1990s. Around one million persons, or about 25% of the population, have left the country. While contributing to private consumption in Armenia through remittances, emigration has resulted in an aging

population, a gender imbalance and a loss of skilled labour. There has been a sharp fall in the birth rate from 21.6/1000 (1989) to 12.1/1000 currently; life expectancy is around 73.4 (National Statistics 2005). The death rate increased from 6.3 per 1000 in 1999 to 8.1 per 1000 in 2003 (National Statistics, 2005). Nearly two thirds of the population live in urban areas, the capital Yerevan alone absorbing about one third of the total population.

Although the PRSP envisages a 14% per annum increase over the period 2004-2015, sufficient government expenditure on social issues as a percentage of GDP has not materialised in the past. Social transfers were equivalent to only about 4.5% of GDP. For the future, the GoA has announced a considerable increase in social spending. This is indeed also visible in the Government's Medium Term Economic Framework. Compared to 2005, a raise in health expenditure is scheduled to rise in 2006 by 16,1 %, in 2007 by 29,6 % and in 2008 by 16,6 %. According to the Armenian MTEF, increased public financing of social insurance and social security, as well as enhanced efficiency of such expenditure will be considered a top priority over the whole MTEF period and the development of a social security system is one of the basic tasks. The MTEF also states that increasing public expenditure on education and improving the overall situation in that sector will be prioritised over the whole MTEF 2006-2008 period. Compared to the respective previous year, expenditure will rise in 2006 by 14,4 %, in 2007 by 14,1% and in 2008 by 20,1 %.

Concerning pensions, there are also considerable changes underway. The current level of pensions is below the minimum subsistence level; the Central Bank of Armenia has however now put forward proposals for the development of a pension system following the so-called "three-pillar model".

#### **4.5. Analysis of the environmental situation<sup>3</sup>**

Armenia faces significant challenges in order to promote environmental protection. Key areas include air quality, water quality and supply, waste management, nature protection, land use, industrial pollution, trans-boundary environment issues and climate change including multilateral environmental agreements. Institutional and administrative capacities exist but could be further strengthened, in particular as regards implementation and enforcement of legal provisions. Civil society also needs strengthening in order to be a valuable partner for the government in the development of environmental protection.

#### **4.6. Perspectives**

The agreement on the joint EU- Armenia Action Plan concluded in the context of the European Neighbourhood Policy creates a unique opportunity for Armenia to transform itself into a more modern and democratic country; it will also allow to make further progress with economic reform and to further promote economic growth. The Action Plan provides a concrete tool for further promoting the country's European aspirations. As Armenia makes genuine progress in carrying out internal reforms and in coming closer to European standards, relations between the EU and Armenia will become deeper and stronger.

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<sup>3</sup> A more detailed description of the environmental situation in Armenia can be found in the Country Environment Profile annexed to this CSP (Annex 2).

If settlement of the conflict over Nagorno Karabagh still would take place soon, this would give further development an additional boost.

## **5. OVERVIEW OF PAST AND ONGOING EC ASSISTANCE**

### **5.1. EC assistance to Armenia 1991-2006**

European assistance to Armenia since 1991 amounts to more than 380 million EUR. Humanitarian assistance (notably ECHO and Food Aid Operations) has accounted for nearly 120 million EUR alone and has contributed to alleviating the very severe humanitarian situation in the mid-1990s. TACIS national allocations over the years and the Food Security Programme (FSP) represent around 100 million EUR each. Since Armenian independence, the TACIS programme has efficiently contributed to the transition towards market economy, notably by assistance in the fields of legal and regulatory reform, approximation of Armenian legislation to that of the EU and support for Armenia's WTO accession. TACIS has also contributed to Armenia's economic recovery through support to the private sector and small and medium sized enterprises.

The EC has additionally spent around €29 million of TACIS funds on improving safety of the Medzamor Nuclear Power Plant (MNPP) despite wider plans to urge GoA to decommission the Nuclear Power Plant as soon as possible.

After approval of the Country Strategy Paper in December 2001, TACIS assistance to Armenia in the period 2002-2006 focused on continued support for institutional, legal and administrative reform as well as on support in addressing the social consequences of transition. TACIS has also provided essential assistance to the implementation of Armenia's Poverty Reduction Strategy approved in 2003. Both, the 2002-2003 and 2004-2005 Action Programme (10 million EUR each) are currently being implemented. The TACIS Action Programme 2006 (17 Mio EUR) has been approved on 31 July 2006. It has been designed in coherence with mutually agreed priorities in the PCA and the ENP Action Plan. It is to be seen as a transition link towards new instruments under the ENP.

Armenia has also participated in TACIS Regional Programmes with projects such as TRACECA, INOGATE and the Caucasus Regional Environmental Centre (REC).

Under the Food Security Programme (FSP) the EC has provided significant budgetary support to key agricultural and social sectors in Armenia and has thus played an important role in tackling poverty in country. The combination of budget support and technical assistance through FSP (with complementary TACIS technical assistance in the agriculture and child care fields) has also enabled notable progress in the field of land reform and public finance management. Implementation of FSP has been very successful and continued support is therefore envisaged also for 2005-2006 (21 million EUR) notably to assist Armenia in continuing to implement its Poverty Reduction Strategy.

The EC European Initiative for Democracy and Human Rights (EIDHR) Programme launched its activities in support of NGOs in Armenia in 2003 with the objective of promoting and protecting human rights and democratization as well as conflict prevention and resolution. The 11 projects of the 2003 programme have been completed. Though these were small projects, the impact has been impressive. Final presentations

were well received and a new call for proposals under EIDHR micro projects 2005-2006 is under way.

The Tempus Programme has provided considerable support to the modernisation and the reform of the higher education system in Armenia. Since 1996, Tempus has funded 13 cooperation projects with EU higher education institutions in the areas of curriculum development, university management and structural reform.

As for the 6<sup>th</sup> Framework Programme for Research and Development, the Armenian National Research and Education Network (ARENA) participates in a project for the provision of services for Internet offerings to Research and Education Networks in the Caucasus and Central Asia (OCCASION, budget 1,3 M € 2005-2007).

Finally, Armenia has also benefited from EC Macro-Financial Assistance (MFA, consisting of a grant of 30 Million € and a loan of 28 Million €). It ended in 2005 after Armenia repaid its last debt to the EC.

## 5.2. Key lessons learnt for the new programming cycle

The Commission has launched an evaluation of the TACIS Programme for Armenia and of the TACIS Programme as a whole at the end of 2004. Findings from both reports are relevant and must be taken into account for this new programming cycle.

### **Evaluation of the TACIS Programme as a whole:**

The draft Tacis evaluation suggests that, overall Tacis interventions were highly relevant and responded to the needs identified. However, particularly in the early years, the programme was mainly governed by a “top-down” approach. This was partly a consequence of the need for institution-building in the transition countries and partly due to an insufficient sense of ownership on the part of the national authorities. National Indicative Programmes (NIPs) also tended to be too detailed which restricted adaptability at project identification level to respond flexibly to evolving needs.

In new programming exercises, the EC will focus on defining strategic priorities and objectives rather than specific activities or delivery mechanisms. National authorities are being involved in this process from the very beginning and have shown a greater level of commitment and ownership as a result of the clearer political framework provided by ENP and the ENP Action Plans.

According to the programme evaluation the Tacis programme is characterised by a large number of “**stand alone**” **technical assistance projects**, particularly in the area of institutional and administrative reform. These actions often achieve good results at project level but have **less impact at sector and national policy level** partly due to a lack of continuity and coherent long-term sector planning. On the contrary, the Food Security Programme (FSP), which provides budgetary support upon achievement of pre-defined benchmarks, is said by most stakeholders to have had significant impact at policy and sectoral level due to higher national ownership leading to stronger commitment to implement reform proposals and policies.

### **Country specific evaluation:**

The evaluation concluded that through interventions supporting the reform of the institutional and legal framework governing economic activity, through provision of advice and training etc. the EC has made an effective contribution to the transition of Armenia to a market economy. It had also provided an important contribution to securing and diversifying Armenian energy supply sources, thus relaxing a major constraint to economic growth. Technical assistance provided in the framework of the food security programme had efficiently assisted the government in improving the management of public resources.

The EC had also effectively supported this development through a technical assistance to the GoA in the negotiations which led to Armenia's accession to WTO in 2003, and helped the government implement post-accession commitments. Poverty had been directly addressed through interventions in social sectors and the Food Security Programme in particular had given significant support in alleviation.

The evaluation mentioned however that issues related to the transition of Armenia to a democratic society have only gradually gained importance in the EC's cooperation. It concludes the Commission had hardly made use of its political leverage to induce GoA to strengthen democracy and the rule of law.

As lessons learned the country specific evaluation points out the EC should make democratic progress, respect of human rights and enforcement of the rule of law a priority for future cooperation. Besides this, all financing instruments should be integrated in the Country Strategy, in the National Indicative Programme and Action Programmes and interventions should in general be limited to a number of concentration areas (e.g. approximation of the Armenian legislation relative to economic activity and trade to that of the EC and further poverty alleviation through continued support to agricultural and rural development policy, social policy and education.

The support to democratic progress should finally be seen as a transverse issue to be addressed through all EC interventions.

Concerning energy, the dialogue on the Medzamor issue and support of GoA's endeavours to diversify energy supply sources, promote energy efficiency, energy savings and the use of renewable energies, as well as to reduce the country's dependency on imported energy should be further continued.

Concerning modalities of assistance it was highly recommended to strengthen the link between policy dialogue and cooperation and to strengthen donor coordination.

### **5.3. Coordination and complementarity with other donors**

The principal donors in Armenia, in addition to the EC, are the World Bank, UNDP, USAID, EBRD and, of the EU countries, especially France, Germany, Greece and Italy. Donor's coordination can be assessed as quite good and well working; it could however be still improved at general and sectoral level and the Government of Armenia should take the lead on this. Until now, general donor coordination meetings are held each month where main activities and achievements are presented and discussed. Examples of successful co-ordination can be found in almost all areas of intervention, amongst the most successful ones are energy, regional development, IT development and Education. Also, when it comes to PCA implementation, donors' community as a whole is involved at various levels.

Most donor activities focus on social and economic development, on good governance issues, in particular on public administration reform and public finance management (see Annex on Donor Activities ).

The EC is currently active in all the above mentioned areas with specific emphasis on institutional and economic reform, including on regulatory issues. Under the new strategy, EC assistance will additionally and in particular focus on governance issues. The EC will also substantially increase its assistance to target more directly poverty reduction and economic growth in particular at regional and local community level, including social services and education.

In this context government-led donor coordination including effective inter-ministerial information sharing mechanisms need to be further strengthened in order to ensure extensive coherence between the EU- Armenia Action Plan and other government programmes at all times.

When preparing this strategy the EC consulted other donors at an early stage to ensure cohesion and complementarity. Future donor coordination on programme identification and implementation, especially when it relates to the implementation of the National Programme for PCA implementation, will be key in order to support Armenian reform plans in the most efficient and cost-saving way. Such coordination will be particularly important as the EC will increasingly be providing assistance on the basis of sector programmes, including pool-funding and budgetary support as appropriate.

#### **5.4. Consistency of EC cooperation policy with other core policies of the EU (“policy mix”)**

Relations with Armenia are affected by a number of other Community policies. Therefore choosing the right “policy mix” is very important. This concerns in particular the areas of Common Foreign and Security Policy (CFSP), energy, development policy and Justice, Liberty and Security (JLS), including migration, border management and the fight against organised crime like the trafficking in human beings and drugs (see Annex 5).

### **6. THE EC RESPONSE STRATEGY**

#### **6.1. Principal objective**

The principal objective of EU-Armenia cooperation at this stage is to develop an increasingly close relationship between the EU and Armenia, going beyond past levels of cooperation, to deeper political cooperation and gradual economic integration.

EC assistance over the period covered by this strategy will therefore aim to support these policy objectives which find their joint and detailed expression in the Partnership and Cooperation Agreement (PCA) which came into force on July 1, 1999 and the EU-Armenia Action Plan which was adopted on November 14, 2006. The strategy is also fully aligned with the Economic Growth and Poverty Reduction Strategy Paper of the GoA which was adopted by the government in November 2003.

## 6.2. EC assistance priorities

EC assistance priorities are presented in the strategy paper under the seven general headings in the EU- Armenia Action Plan.<sup>4</sup> For the short term they focus however as well and in particular on the eight Priority Areas defined in the ENP Action Plan. These commonly agreed Priority Areas are:

- Strengthening of democratic structures, of the rule of law
- Strengthening of respect for human rights and fundamental freedoms
- Encourage further economic development, enhance poverty reduction efforts and social cohesion
- Further improvement of investment climate and strengthening of private sector led growth
- Further convergence of economic legislation and administrative practices
- Development of an energy strategy, including an early decommissioning of the Medzamor Nuclear Power Plant
- Contribute to a peaceful solution of the Nagorno Karabagh conflict
- Enhanced efforts in the field of regional cooperation

These assistance priorities apply in principle to all assistance instruments and programmes which will or might be available for Armenia. Under the National Indicative Programme 2007-2010 (1) support strengthening democratic structures and good governance (2) support for regulatory reform and administrative capacity building and (3) support for poverty reduction efforts have been defined as especially important areas for EC assistance.

### *Political dialogue and reform*

EC assistance in this area will focus on strengthening democracy and good governance, the rule of law, human rights and fundamental freedoms. Very important in the first place is to foster different reforms (e.g. judiciary) in this field, but also to improve the development of civil society, including in the social and economical sectors, and to support independent media.

In the field of enhanced cooperation on foreign and security policy, particular attention will be given to issues related to weapons of mass destruction, conflict prevention and crisis management with a view in particular to contributing to peacefully solving the conflict over Nagorno Karabagh, as well as in dealing with the consequences of the illicit manufacture, transfer and circulation of small arms, light weapons, ammunition and their excessive accumulation and uncontrolled spread.

### *Cooperation for the settlement of the conflict over Nagorno Karabagh*

The EC will continue its engagement in support of a peaceful settlement of the conflict over Nagorno Karabagh .

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<sup>4</sup> The ENP Action Plan is the most recent document containing a specific set of EU- Armenia policy objectives. Although it comes to an end early in 2011 the priority areas for action defined therein will determine the assistance priorities even beyond that date.

This involves in the first place supporting efforts of the EUSR and the OSCE Minsk Group, but also to encourage people to people contacts, to actively involve civil society in peaceful conflict solution efforts and to support humanitarian and de-mining initiatives.

Depending on developments regarding the peaceful settlement of the conflict over Nagorno Karabagh, the EC will provide specific assistance related to all aspects of peaceful conflict settlement and settlement consolidation.

Under the appropriate financial instrument, the EC could also provide support for confidence-building initiatives in the South Caucasus region.

### ***Economic and social reform, poverty reduction and sustainable development***

EC assistance will also address the key issues of poverty reduction, economic growth and the reduction of social inequality as a main priority area, thereby concentrating especially on comprehensive actions at regional and local level (e.g. enhanced access to and quality of social services, in particular education). Issues linked to local and rural economic development and improving the capacity of local public authorities should also be of importance in this context.

Besides the above mentioned focal areas assistance to establish a fully functioning market economy and to further strengthen public finance management should help to foster economic growth, thereby contributing to reduce poverty and regional imbalances. This entails improving the investment climate by ensuring transparency, predictability and the simplification of procedures, and promoting further development of the private sector. The promotion of sustainable development in all relevant sector policies, including agriculture, is a further important issue to be addressed.

### ***Trade-related issues, market and regulatory reform***

Further EC assistance will be offered to support the process of market and regulatory reform so as to enable Armenia to comply with its obligations under the Partnership and Co-operation Agreement (PCA), under WTO rules and to support implementation of the ENP Action Plan. In particular it would mean EC assistance for implementation of the National Programme for PCA implementation adopted by the GoA in early spring 2006, if a good and clearer indication where to prioritize can be agreed with the government.

The assistance could cover support for the approximation of legislation with international and EU standards in a broad range of areas, notably

- trade facilitation issues, in particular customs legislation and procedures (including meeting World Customs Organisation's standards on security of the international trade supply chain),
- technical regulations, standards and conformity assessment, sanitary and phytosanitary issues (SPS),
- establishment and company law, financial services and markets,
- strengthening of the overall administrative capacity of the tax administration and reform of the tax system in compliance with general EU and international principles in order to improve revenue collection,
- competition,
- consumer protection policy,
- development of an efficient legislative and administrative framework for SMEs,

- protection of intellectual and industrial property rights,
- public procurement procedures,
- statistics.

However, providing support and technical assistance for administrative capacity building in all the above-mentioned areas and to all involved government institutions will be of equally high importance.

### ***Co-operation in the Field of Justice, Freedom and Security***

In line with the ENP Action Plan EC assistance in this area should focus on migration issues including readmission and asylum, fighting terrorism and organised crime, including trafficking in human beings and drugs, the illicit spread of small arms and light weapons and money laundering. Effective border management including document security / biometrics, support for fighting organised crime and effective management of migratory flows are other issues for support under this headline.

EC assistance in these fields should promote institutional reform as well as capacity building .

### ***Cooperation in specific sectors, including transport, energy, environment and information society.***

Reinforcing administrative capacity to elaborate and implement sectoral strategies and policies which are closer to relevant EU policies and legislation is a general priority in the above areas.

In the energy sector, reinforced support will be continued in the area of improving energy efficiency, energy savings and promoting new or renewable energies and for the decommissioning of Armenia's outdated nuclear power plant. If necessary, support could also be provided for the implementation at national level of the recommendations of the working groups established during the Baku Energy Ministerial Conferences.

In the field of transport, support could be envisaged for road rehabilitation at local and regional level and for priority measures in line with the recommendations of the High Level Group on the extension of the major trans-European transport axes towards neighbouring countries and regions as well as in line with the priorities identified, within the framework of the Baku Working Groups and adopted during the Baku Ministerial Transport Conference of May 2006 in Sofia. In road transport, taking into account that the country is a Contracting Party to AETR, support should be given for the implementation of the digital tachograph.

With regard to the environment, particular attention will be given to support for the implementation of multilateral environmental agreements, in particular the UN Framework Convention on Climate Change and its Kyoto Protocol, and the UN-ECE conventions. Activities linked to water quality improvement, for example through the relevant component of the EU Water Initiative, could also be envisaged. Further priority areas are waste management and nature protection as well as promoting civil society development and better awareness raising on environmental issues.

As far as information society is concerned, support could be envisaged for putting in place a comprehensive regulatory framework including licensing and the progressive approximation with the EU acquis and for promoting the use of online services by

businesses, administration and citizens, in areas such as e-Government, e-Health or e-Education.

An adequate participation in the 7<sup>th</sup> Framework Programme could be ensured by linking of the Armenian National Research and Education Network (ARENA) to the European Network GEANT 2.

Upon special Armenian request giving support for scientific and technological cooperation could be an important contribution to the sustainable and equitable economic development of Armenia. Actions in this field should include Armenia's increasing participation in research-related activities, joint research projects, the Marie-Curie international mobility scheme and practical training for scientists.

### ***People-to-people contacts***

In this field, assistance for reforming and upgrading the education system with a view to convergence with EU standards and practices will be essential as well as support for youth exchanges and cooperation. It will also help to strengthen democratic development, social stability and economic competitiveness.

Possible actions include reinforced participation in programmes such as Tempus and Youth in Action, greater opportunities for Armenian nationals to participate in exchange programmes such as Erasmus Mundus and investigating the scope for cooperation in the framework of EU programmes in the field of culture. It should also mean to further support the full implementation of the Bologna process for the higher education sector in Armenia, further support for reforms in the field of education, including for VET.

Gender as a cross-cutting issue should be integrated to the fullest possible extent into programmes for all the key issues outlined above.

## **6.3. Instruments and means**

From 2007 on, EC assistance will be provided through a set of new instruments. While the European Neighbourhood and Partnership Instrument (ENPI), including not only its national but also its trans-national/regional, cross-border and thematic components, will be the principal new tool for providing assistance to Armenia, certain measures, in particular in the area of conflict prevention and crisis management and resolution, may also be supported under the future Stability Instrument.

The introduction of these new external assistance instruments will substantially increase flexibility of EC assistance, since technical assistance will no longer be the predominant channel for external assistance programmes.

As indicated in the ENP Action Plan, new cooperation tools like Twinning or TAIEX will play an essential role in achieving the Action Plan's objectives. These instruments, together with other types of assistance (infrastructure and equipment funding, pool funding and budgetary support - in particular in the context of sector-wide approaches (SWAPs)) will be available and used whenever appropriate.

Twinning and TAIEX could be phased in already under current annual TACIS Action programmes in order to allow smooth habituation.

As appropriate, Armenia will also receive support for participation in Community programmes, agencies and networks, insofar as these will be open to the country. The

more detailed framework provided by the ENP Action Plan will help to identify possible support in this field and to ensure the consistency of EU assistance within specific sectors.

In general, with ENPI being a policy driven instrument, it is necessary to ensure that co-operation with Armenia provides appropriate support to fulfil commitments under the ENP Action Plan.

Interest rate subsidies and other ways of blending grants and loans can leverage investments by international financial institutions in the fields of environment, energy and transport. Whenever interest rate subsidies are considered, their relevance shall be assessed on a case-by-case basis and care should be taken to avoid significant market distortions. As regards environment, relevant sectors include water management, waste management and industrial pollution. For energy, possible areas include renewable energy resources and energy efficiency. Energy infrastructure/network investments should in principle be commercial operations given their financial return. In exceptional circumstances, though, where specific EU interests are involved (notably, energy security of supply) and it appears difficult to get a project started, targeted interest rate subsidies or other ways of combining grants and loans might also be considered for particular investment projects. Regarding transport, interest rate subsidies or other blending schemes would focus on catalysing funds for critical infrastructures of strategic importance, such as cross-border measures on the priority axes or the missing links necessary for their completion.

### ***ENPI national allocation for Armenia***

Assistance provided under the national ENPI envelope for Armenia will focus on the initially mentioned **three priority areas** which have been selected on the basis of joint EU- Armenia policy objectives. In case that a still stronger prioritization will be requested the first sub-priorities under each headline will get most attention, and support will be based on lessons learnt from the previous assistance programmes and on complementarity with other donors<sup>5</sup>. Depending on developments regarding the settlement of the conflict over Nagorno-Karabakh, the EC would provide specific assistance related to all aspects of peaceful conflict settlement and settlement consolidation.

#### *Priority Area 1: Support for Democratic Structures and Good Governance*

Sub-priority 1: Rule of law and reform of the judiciary

Sub-priority 2: Public administration reform, including local self government / public finance management / public internal financial control and external audit / combat of corruption

Sub-priority 3: Human rights, fundamental freedoms, civil society, people to people contacts

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<sup>5</sup> For the first four years covered by this strategy further details will be elaborated in the National Indicative Programme 2007-2010.

## *Priority Area 2: Support for Regulatory Reform and Administrative Capacity Building*

Sub-priority1: Approximation of legislation, norms and standards (mainly based on National Programme for PCA implementation) and administrative capacity building

Sub-priority 2: Sector-specific regulatory aspects (including environmental aspects) and administrative capacity building

## *Priority Area 3: Support for Poverty Reduction Efforts*

Sub-priority 1: Education

Sub-priority 2: Regional development and social Services

## ***ENPI trans-national / regional programme<sup>6</sup>***

The regional ENPI component will help to meet the objectives outlined in this strategy and the conclusions and recommendations of the working groups established in the framework of regional cooperation by addressing a limited number of priorities which are relevant to Armenia, but have a genuine regional dimension both in terms of joint implementation and regional impact.

At sectoral level, this relates in particular to **transport** (the development of major trans-national transport axes in line with the recommendations of the High Level Group, the recommendations of the Baku working groups adopted during the last Baku Transport Ministerial Conference as well as the TRACECA Strategy adopted during the TRACECA Ministerial Conference in May 2006 in Sofia), **energy** (covering, in the context of the follow-up to the Energy Ministerial Conference in Baku of 13<sup>th</sup> November 2004, all regional elements in this domaine, in particular in relation to harmonising energy markets, safety and security of energy production, transportation and supplies, energy efficiency, energy savings and renewables and facilitating investments in energy projects of common interest), and **environment** (targeting *inter alia* the regional dimension of the EU Water Initiative, cooperation on regional seas and rivers including on biodiversity, regional aspects of sustainable management of forests and compliance with multi-lateral agreements, climate change and industrial pollution, information, monitoring and assessment and civil society cooperation in the environment field) as well as **information society** (South Caucasus Programme for linking with the pan – European Grid infrastructure).

Beyond that, **the fight against trans-national organised crime, and customs** can be addressed more effectively at a regional level. This may include action in connection with customs and border management, fighting international crime, and migration and asylum management. Finally, there will also be scope for regional **SME cooperation and civil society cooperation**.

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<sup>6</sup> Details will be elaborated in a separate Regional Strategy Paper/Regional Indicative Programme.

### ***ENPI-Inter Regional Programme<sup>7</sup>***

The ENPI-wide programme will include activities which for reasons of coherence, visibility and administrative efficiency are best implemented in the same way for all the neighbouring countries. Examples are TAIEX, TEMPUS and the new Scholarship Programme.

### ***ENPI Cross-Border Cooperation (CBC) / Neighbourhood and Partnership Programmes (NPP)***

NPPs will be based on two types of programs: bilateral programs (typically involving two countries sharing a border) and multilateral programs (e.g. for the Black Sea). Since Armenia does not have any physical borders with the EU in the near future, it could only be involved in multilateral cooperation (Black Sea Programme) under the NPP.

### ***ENPI Thematic programmes<sup>8</sup>***

A set of five thematic programmes will be available under the new set of instruments: Food Security (in form of a phasing out programme in 2007), Migration and Asylum, Investing in People, Local Actors in Development, Environment and Sustainable Management of Natural Resources including Energy. Out of these especially the programme on “Migration and Asylum” (ex-Aeneas) could be relevant for Armenia. Other thematic programmes of potential relevance to Armenia are the ones on “Investing in People”, “Food Security” and on “Environment and Sustainable Management of Natural Resources including Energy” as well as the new Instrument for Democracy and Human Rights. Since the above areas are however also addressed under the national, regional or CBC ENPI envelopes, additional thematic activities will be launched only if they provide clearly an added value.

It is also likely that the thematic programme for “Food Security” will continue for a short-term transition phase in Armenia.

### ***Stability Instrument***

The main goal of the Stability Instrument is to provide an effective, timely, flexible and integrated response to crises, emerging crises or continued political instability.

In the case of Armenia this is particularly relevant with regard to the conflict over Nagorno Karabagh. New efforts are currently being made to peacefully settle this conflict, but there is little hope that this might actually happen in the near future. In case of a peaceful conflict settlement, support, especially for the needed rehabilitation and reconstruction, could be provided under this instrument.

Finally, future EC contributions to the International Science and Technology Centre (ISTC) in Moscow, which is dedicated to the non-proliferation of technologies and expertise related to weapons of mass destruction and which also covers Armenia, are expected to be provided under the framework of the Stability Instrument.

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<sup>7</sup> Details will be elaborated in a separate strategy paper for the ENPI-Inter-Regional Programme.

<sup>8</sup> Financial resources allocated to each thematic programme will be programmed on the basis of a single strategy document. CSPs/RSPs, in establishing the policy mix should identify opportunities for adding value to the NIPs/RIPs by using thematic programmes.

## **ANNEX 1**

### **LIST OF ABBREVIATIONS AND ACRONYMS**

|         |   |
|---------|---|
| AP      | Action Plan (also: ENP Action plan or EU-Moldova ENP Action Plan) |
| BSEC    | Black Sea Economic Cooperation Pact                               |
| CBC     | Cross-border Cooperation  |
| CEP     | Country Environment Profile                                       |
| CFSP    | Common Foreign and Security Policy                                |
| CIS     | Commonwealth of Independent States                                |
| CoE     | Council of Europe   |
| DAC     | Development Assistance Committee                                  |
| EIB     | European Investment Bank  |
| EBRD    | European Bank for Reconstruction and Development                  |
| ECHO    | European Commission Humanitarian Aid Office                       |
| EG-PRSP | Economic Growth and Poverty Reduction Strategy Paper              |
| EIDHR   | European Initiative for Democracy and Human Rights                |
| ENP     | European Neighbourhood Policy                                     |
| ENPI    | European Neighbourhood and Partnership Instrument                 |
| FDI     | Foreign Direct Investment   |
| FSP     | Food Security Programme   |
| FTA     | Free Trade Agreement  |
| GDP     | Gross Domestic Product  |
| GNI     | Gross National Income   |
| HDI     | Human Development Index   |
| IFIs    | International Financial Institutions                              |
| IMF     | International Monetary Fund                                       |
| ISTC    | International Science and Technology Centre                       |
| JHA     | Justice and Home Affairs  |
| JLS     | Justice, Liberty and Security                                     |
| MDG     | Millennium Development Goals                                      |
| MoU     | Memorandum of Understanding                                       |
| NGO     | non-governmental organisation                                     |
| NPP     | Neighbourhood and Partnership Programme                           |
| ODA     | Official Development Assistance                                   |
| OECD    | Organisation for Economic Cooperation and Development             |
| OSCE    | Organisation for Security and Co-operation in Europe              |
| PCA     | Partnership and Cooperation Agreement                             |
| PPP     | Purchasing power parity   |
| RIP     | Regional Indicative Programme                                     |
| RSP     | Regional Strategy Paper   |
| SME     | Small and medium enterprises                                      |
| SP      | Stability Pact for South-Eastern Europe                           |
| SPS     | Sanitary and phytosanitary issues                                 |
| SWAP    | Sector-wide Approach  |
| TAIEX   | Technical Assistance Information Exchange Unit                    |
| UNDP    | United Nations Development Programme                              |
| WMD     | Weapons of Mass Destruction                                       |
| WTO     | World Trade Organisation  |

## ANNEX 2

### ARMENIA AT A GLANCE



### Selected economic and social indicators

#### General Data

|                          |                   |
|--------------------------|-------------------|
| Area                     | 29,700 sq km      |
| Population               | 3.2 m (2005)      |
| Urban population         | 64.1% (2005)      |
| Life Expectancy          | 73.4 (2005)       |
| Population growth rate   | -0.2% (2003-2015) |
| Fertility Rate per woman | 1.3 (2000-2005)   |
| Human Development Index  | 83                |

## **Economy**

|  |                                     |
|--|-------------------------------------|
| Nominal GDP 2005 (USD)                             | 4.9 bn                              |
| GNP per capita 2005 (USD)                          | 1523.8                              |
| GDP by sector (2005)                               |                                     |
| Agriculture  | 18.7 %                              |
| Industry   | 18.8 %                              |
| Trade  | 10.5 %                              |
| Construction                                       | 21.7 %                              |
| Transport and Communications                       | 05.6 %                              |
| Others   | 16.2 %                              |
|  |                                     |
| Real GDP growth rate (2005)                        | 13.9%                               |
| Estimated real level of 2005 GDP as % of 1989 GDP: | 98%                                 |
| Inflation:   |                                     |
| 2002   | 1.2%                                |
| 2003   | 4.7%                                |
| 2004   | 7.0%                                |
| 2005   | 0.6%                                |
|  |                                     |
| External debt (2005 USD)                           | 1,117 m                             |
| Debt service (2005 USD)                            | 29 m                                |
|  |                                     |
| <b>Trade (2005)</b>                                |                                     |
| Exports of goods & services:<br>USD 950,4 m        | Exports to EC: USD 442,8 m (46,6 %) |
| Imports of goods & services:<br>USD 1767,9 m       | Import from EC: 590,4.0 m (33,4%)   |
| Current account balance:USD -817,6 m               | Trade balance with EC: USD -147.6 m |
| FDI: USD 1154.41 m                                 | FDI of European origin: USD 554.97m |

## **Social Development**

|  |       |
|--|-------|
| Adult literacy rate:                           | 98,3% |
| Enrolment for primary schools (2005)           | 90,2% |
| Infant mortality per 1000 live births (2005)   | 11,4  |
| Under 5 mortality per 1000 births (2005)       | 13,6  |
| Contraceptive prevalence rate (2004)           | 54 %  |
| Access to essential drugs (2000))              | 40 %  |
| Access to safe water                           | 92%   |
| Access to sanitation                           | 84%   |
| Population undernourished 2000-2002            | 34%   |
| Number of Doctors / 100,000 people (1990-2004) | 353   |

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### *Sources:*

*UNDP Human Development Report 2005*  
*Armenian European Legal and Policy Advice Centre AEPLAC*  
*Economist Intelligence Unit EIU Country Analysis 2006*  
*Economic Development and Research Centre NGO Armenia 2005*

## ANNEX 3

### COUNTRY ENVIRONMENT PROFILE

#### 1 State of the environment

The key environment issues in Armenia relate to air quality, water quality, waste management, nature protection and land use.

While emissions from stationary and mobile sources decreased in the 1990s, **air pollution** is becoming an important issue in urban areas.

As regards **water quality**, drinking water quality is being affected by deteriorating infrastructure. Waste water treatment infrastructure needs upgrading. Lake Sevan, the primary water resource of the country, has been subject to overexploitation resulting in a significant lowering of the water level.

**Waste management** is a serious challenge, including with regard to prevention, collection, treatment, recovery and final disposal. There is no disposal facility for hazardous waste. Stocks of obsolete pesticides constitute an important environment problem.

As regards **nature protection**, Armenia's rich biodiversity is under threat including from industrial pollution and increased pressures on forests and wetlands. Deforestation is an important challenge.

With regard to **land use**, soil erosion, mainly caused by poor agricultural practices and over-grazing, constitutes a challenge. A large part of the country is subject to desertification.

As regards **industrial pollution**, the main industrial activities relate to chemicals, electronic products, machinery and textiles and mining, entailing severe pollution.

Current **trans-boundary environment issues** include the use and protection of shared waters – in particular the Kura-Araks river basin, which is an essential source of fresh water for the Southern Caucasus region. Existing problems in the Kura river basin are related to both quantity and quality of water. Water quality is affected by discharges of municipal and industrial waste-waters and return flow from agriculture.

As regards **global environment issues and climate change in particular**, Armenia acceded to the Kyoto Protocol in April 2003 and therefore needs to implement the relevant provisions and, where appropriate, implement concrete policies and measures to reduce greenhouse gas emissions, in particular in the energy and heavy industry sectors.

#### 2 Environment policy

Armenia developed a National Environmental Action Plan in 1998 (revised in 2004) setting as priorities: air, land and water pollution; over-exploitation of natural resources and threatened ecosystems; and environmental health problems and hazards. A National Environmental Health Action Plan was approved in 2002. The 2003 Poverty Reduction Strategy Paper also identifies environment as a priority area.

Sector-specific action plans and strategies have been elaborated on desertification, biodiversity and specially protected areas, ozone-depleting substances, integrated water resource management and persistent organic pollutants. An action plan on Lake Sevan was adopted in 1998.

### **3 Environment legislation and implementation**

The Constitution requires the State to protect the environment as well as to ensure rational use of natural resources. No framework legislation on environment has been adopted, and therefore the sector is regulated by the Civil, Administrative, and Criminal Codes, the Law on Inspections and the Law on Licensing. A Law on Environmental Impact Assessment was adopted in 1995 which, together with the 1991 Principles of Legislation on Nature Protection, grant citizens the right to request environmental information and be involved in the decision making process. In 2002 an information centre on environment was established.

The Ministry of Nature Protection has been preparing laws to introduce new environment quality standards aiming to reflect international practice and EU legislation. A new Land Code was adopted 2001 and a Water Code as well as mineral resources code in 2002. Laws are under preparation on permits, public participation, seismic safety, mineral research, environmental fees as well as environmental education.

Overall, environment legislation is in place in several areas, but still needs to be further developed, in particular with regard to proper implementation. Armenia also faces difficulties with enforcement of legal provisions due to limited administrative capacities and financial resources, especially at regional and local levels.

### **4 Administrative capacity**

The Ministry of Nature Protection was established in 1991. A number of other Ministries are also involved in environmental matters, such as the Ministries of Finance and Economy, Health, Agriculture, Internal Affairs, and Justice. The State Environmental Inspectorate is responsible for emission control, which is performed also by regional inspectorates. Water-supply issues are dealt with under the State Committee on Water Management. The Environmental Monitoring Centre, Hydro-meteorological Department and Geological Department carry out environmental monitoring activities.

In order to enhance strategic planning, implementation and enforcement of environment legislation, the strengthening of administrative capacities at national, regional and local levels constitutes an important challenge for Armenia, including with regard to coordination between relevant authorities.

### **5 Participation in regional and international processes**

Armenia has ratified the relevant **international and regional conventions** to which it is signatory, with the exception of the Strategic Environmental Assessment Protocol of the UN-ECE Convention on Environmental Impact Assessment in a Transboundary Context. Armenia has also not signed the UN-ECE Convention on the Protection and Use of Transboundary Watercourses and International Lakes.

Armenia participates in the **“Environment for Europe” process**, which is a multilateral framework created in 1989 to steer the process of invigorating environmental awareness in the countries of Central and Eastern Europe, emerging from the old regimes and moving closer to the EU. The core activities of this process are undertaken by a Task Force co-chaired by the Commission and an NIS Environment Ministers.

Armenia is participating in the Eastern European, Caucasus and Central Asia component of the EU Water Initiative, a regional component of the **EU Water Initiative** as announced at the 2002 World Summit on Sustainable Development. The initiative aims to promote better water governance and coordination between stakeholders.

Armenia also participates in the **Europe and North Asia Forest Law Enforcement Governance (FLEG) process** concerning forest governance and the protection and sustainable management of forests in the region.

Armenia is a co-founder (together with Georgia, Azerbaijan and the European Commission) of the Caucasus Regional Environmental Centre (REC). The REC Caucasus, with headquarters in Georgia, aims to address regional environment issues in the Southern Caucasus through the promotion of regional co-operation between various stakeholders at all levels, involving actors of civil society, governmental bodies, local communities and the business sector. The REC Caucasus also aims to promote public participation in environmental decision making.

## **6 Key environment areas where action is required**

Armenia faces significant challenges to promote environment protection. Key areas include air quality, water quality, waste management, nature protection and land use. As regards climate change, Armenia needs to implement the relevant provisions under the Kyoto Protocol to the UN Framework Convention on Climate Change. Armenia has significant possibilities to use flexible mechanisms under the Protocol.

The country’s institutional and administrative capacity requires further strengthening, in particular as regards strategic planning, implementation and enforcement of legislation. A fully operational Caucasus Regional Environment Centre could well assist in promoting environmental awareness and protection by providing a forum for cooperation between all stakeholders.

Key environment areas where action is required are identified in the environment section of the EU - Armenia Action Plan. It defines a set of priorities for actions with regard to environmental governance, issue-specific activities as well as international and regional cooperation on environment issues. Progress towards implementing the Action Plan will also contribute to fulfilling the objectives of the Partnership and Cooperation Agreement.

## ANNEX 4

### ACTIVITIES OF OTHER DONORS, INCLUDING MEMBER STATES

#### *Member states*

From the **EU-25**, F, D, DK, H, I, SWE, NL and UK provide assistance to Armenia.

**F** focuses on support to university education, culture and health care.

**D** promotes local self –governance, judicial reform and rule of law, vocational training, infrastructure development such as rehabilitation of water systems and electricity transmission.

**DK** promotes stabilization of the Caucasus region, including Armenia, by improving the conditions for the refugees, internally displaced persons (IDPs) and minorities in society. The regional programme will achieve these objectives by strengthening the authorities and the actors within the civil society to integrate refugees, IDPs and minorities into society. 3,200,000 euros have been committed to activities in the Caucasus region from 2005-2007.

**SW** promotes local self-governance, judicial reform and rule of law, vocational training, SME development, and promotion of mortgage lending. It gives as well support to a project on rural development.

**EL** supports projects in health care and education, telecom and business training. It also participates in the World Bank structural adjustment credit.

**I** supports the health care sector by upgrading hospital technical infrastructure. It also fights trafficking in people and contributes to reconstruction of a child care centres.

**NL**'s key areas of cooperation are macro support, human rights and good governance.

**UK** promotes regional development and public sector reform. It also assists with improving public expenditure planning mechanisms.

#### *Other donors including IFIs*

**OSCE** is active in fighting corruption, in anti-trafficking, democratization, electoral reform, environment, human rights, media, human rights and rule of law.

**EBRD** is intensifying efforts to improve the country's investment climate. Together with the IMF and World Bank, the EBRD is active in restructuring the energy sector, further strengthening the financial sector and providing support for SMEs. Armenia is part of EBRD's 'Early Transition Countries' initiative. Launched in April 2004, the initiative aims to increase investments in the Bank's seven poorest countries. Through 2005, the EBRD completed 8 investments in Armenia, totalling EUR 116m.

The **World Bank (WB)** runs many programmes in Armenia, including structural adjustment credits (a 5th SAC started in 2003, focusing on social reforms and business climate) and sectoral credits (energy, transport, water, education...) which are also linked to the PCA. In 2006 fiscal year World Bank commitments to the country had reached US \$ 398,6 m (118, 6

m for 2006, plus 280 m ongoing projects). The World Bank's last Country Assistance Strategy (CAS) approved by the Bank in June 2004 focused on making growth more pro-poor and reducing poverty resulting from lack of income. The real focus is on reduction of inequalities. World Bank Poverty Reduction Support Credits (PRSCs) are intended to support policy and institutional reforms in the furtherance of the official Poverty Reduction Strategy Paper (PRSP). The PRSCs focus on four critical reform themes: (i) consolidating macroeconomic discipline and strengthening of governance; (ii) sharpening competition and entrenching property rights; (iii) mitigating social and environmental risks, and (iv) modernising the rural economy. The first PRSC is proposed to be extended on the basis of policy and institutional reform actions taken as agreed with the International Development Agency. Subsequent PRSCs shall be made available as the agreed triggers of policy. The credit shall help to sustain economic growth and poverty reduction by advancing high priority reforms identified in the PRSP and by providing resources for the budget, if institutional reforms are satisfied. The strategy envisages a lending programme of between US\$ 150 million and US\$ 164 million.

Both the IMF and the World Bank have provided continuous support to Armenia with concessional funds and large-scale technical assistance.

**IMF** just completed the second review under the Poverty Reduction and Growth Facility (PRGF) arrangement for Armenia and released a further SDR 3.28 million (about 4.9 mln US\$) under the arrangement. This brings the total amount drawn under the arrangement to SDR 9.84 million (about 14.7 m US\$).

**UNDP** provides assistance in many sectors related to economic development, information technologies and decentralisation. It particularly assists the ministry of Trade and Economic Development in elaborating a 20-year Economic Development Plan.

**USAID** provides technical and financial assistance to some key sectors (customs reforms). It is involved in a Commercial Law and Economic Regulation Program, has a WTO programme addressing subcomponents such as technical regulations (for WTO compliance), trade policy training, standards (to replace GOST standards), trade related intellectual property measures (TRIPs). USAID is also supporting a long term project to assist the State Commission on Protection of Economic Competition.

In 2005 Armenia has received USAID funding of 65 Mio \$.

**MCC:** Armenia has reached an agreement in 2006 for support under the "Millennium Challenge Account. The funding foresees 238 m \$ over 5 years, for irrigation and rural roads. The first year will start with a planned allocation of 12, 6 m \$.

## ANNEX 5

### “POLICY MIX” CONSIDERATIONS IN THE CONTEXT OF THE ARMENIA CSP

**CFSP:** Efforts towards peaceful settlement of the conflict over Nagorno Karabagh play an important role in the context of the **Common Foreign and Security Policy (CFSP)**. The settlement process has recently entered a new phase with greater EU involvement through the services of the EUSR for the Southern Caucasus.

The since 1994 persisting conflict over Nagorno Karabagh **has also taken a toll in economic terms since it hinders considerably economic development in the region**. The disruption of trade links had a negative effect on both sides, in Armenia and Azerbaijan.

Depending on developments regarding a peace deal, the EC could provide **further specific assistance** related to aspects of peaceful conflict settlement and settlement consolidation.

**Mines:** Because of the conflict over Nagorno Karabagh Armenia is also affected by antipersonnel landmines (APL).

**Cooperation on energy:** Armenia is still to a high degree dependent on imports, in particular from Russia. Recent events related to gas tariff disputes, notably on gas pricing, between Russia and several former Soviet Republics showed the high vulnerability of Armenia in this regard. Armenia continues however with efforts to diversify sources of energy supply and requests EU assistance on this matter. The energy sector also suffers from inefficiency, insufficient bill collection, payment arrears and a need to invest in outdated infrastructure. Against this background, support for energy-related issues will be one element of the EC's future assistance strategy.

Until successful decommissioning of the country's outdated nuclear power plant (Medzamor) it will be most important to invest in nuclear safety as well.

**JLS cooperation:** In terms of the **migratory situation**, Armenia is an important source country for illegal migrants to the EU (partly due to the widespread Armenian diaspora also in EU Member States). Due to the difficult economic situation the incentive to seek employment abroad remains strong, with a considerable number of Armenian citizens falling victim to various forms of trafficking. Cooperation on JLS matters is therefore an area which forms an important part of the ENP Action Plan.

**Development Cooperation:** Armenia belongs to the WB category of lower middle income countries. General principles and EC policies regarding **development cooperation** therefore still apply. The Armenian government adopted an Economic Growth and Poverty Reduction Strategy Paper (PRSP) in August 2003 and approved a First National Report on the Millennium Development Goals (MDGs) in 2001. Country-specific MDGs have been developed as well. Both lines for orientation have influenced the new external assistance strategy for Armenia considerably. It has therefore a strong focus on poverty reduction, in particular at regional and local community level and on education.

**Trade:** In the area of **trade policy** the EU is a key import and export market for Armenia which is currently benefiting from the General System of Preferences (GSP). Improving the system of certification and the control of rules of origin are important prerequisites in this regard. The Armenian government is actively working on these issues.

**Transport:** In the field of **transport** Armenia played an active part in the EU-Black Sea-Caspian Basin Ministerial Conference in November 2004 in Baku and continues to play an active role in their follow-up Working Groups. Armenia also participates actively in the TRACECA Secretariat and TRACECA meetings and adopted the TRACECA strategy and the conclusions of Baku transport working groups during the Baku and TRACECA Ministerial conferences which took place back to back in May 2006 in Sofia. The EC has a strategic interest in providing support for areas identified as important in this context and for priority measures in line with the recommendations of the High Level Group on the extension of the major trans-European transport axes towards neighbouring countries and regions. The Commission also adopted in March 2005 a Communication proposing the creation of a wider European Common Aviation Area including the neighbouring countries of the EU by 2010. It also includes the objective of Armenia joining this initiative in the medium term.

**Environment:** As regards environment protection, **global and transboundary environment threats** like climate change affect Armenia as well as the EU. Both parties are therefore committed to implementing the Kyoto Protocol and the UN Framework Convention on Climate Change. Trans-boundary environmental threats include the use and protection of shared waters, in particular the Black Sea. Current EC support in this area is mostly provided on a regional basis. Follow-up measures could run under future assistance programmes.

**Information Society:** A comprehensive and transparent regulatory framework for the Armenian electronic communication sector is essential in order to promote investment. Approximation with the EU acquis will also facilitate trade in communication services. Regarding information technology, linking the Armenian National Research and Education Network (ARENA) to the European GEANT 2 and to the pan- European Grid infrastructure could give the Armenian research and education sector access to e-science resources in Europe.