

REGIONAL ECONOMIES

**THE SOCIOECONOMIC SITUATION
IN ARMENIA**

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(Erevan, Armenia)***A. General Assessment**

On the whole the processes unfolding in Armenia can be seen elsewhere, in all countries with transitional economies. Still, there are certain purely Armenian specifics caused by the country's economic, political, and cultural specifics and national psychology. It is these specifics and this psychology that force each and every country to choose the path of economic reforms.

Alexander Neklessa has offered a highly original description of the current changes: "Today the neoliberal program, which can be called a 'secular religion of the current century' together with communism and chauvinism, is realized fast in dramatic circumstances."¹ In other words, there are no standard principles or models to be realized with equal success in all countries.

One should accept as the most general observation that worldwide rivalry is based on high technologies and a flexible nation-state system. It is not accidental that the societies based on the nation-state principles (Japan, China, "the four Asian tigers," Israel, etc.) can promptly respond to global developments and create flexible economic systems. In fact, everything that is going on today has displayed two trends: first, an opposition to the architects of the new world order and the efforts to create a relatively independent system that would include certain elements, high-tech production being one of them. No scientific and technological potential is possible without developed production. A nation that loses the prospects for its scientific and technological development is left without one of the key reasons for its continued existence. The second trend of contemporary development calls for an adjustment to the challenges created by the architects of the new world order and survival within their program as a servicing country.

An analysis of what is going on in Armenia says that the country is heading toward the second trend. It seems that it is developing into a servicing country in all spheres, especially where the brain drain is

¹ A. Neklessa, "Konets tsivilizatsii ili konflikt istorii," *ME i MO*, No. 3, 1999, p. 32.

concerned. As soon as the status of a servicing country takes its final shape, Armenia will be robbed of its future: this status creates different survival criteria.²

B. Development Trends

To assess the economic situation let us discuss certain figures.

Table 1

Annual per Capita Incomes
in the South Caucasian Countries (\$)

Countries	1994	1995	1997	1998	1999	2000	2002
Armenia	6.0	14.6	27.7	35.7	37.7	42.1	43.1
Azerbaijan	13.3	14.1	35.8	43.5	44.8	49.5	55.8
Georgia	5.7	10.6	33.4	39.8	33.5	36.6	—

Source: *Statistical Yearbook of South Caucasus. Armenia, Azerbaijan, Georgia, 2000*, p. 80; *Statistical Yearbook of South Caucasus. Armenia, Azerbaijan, Georgia, 2002*, p. 57.

The table says nothing about the sources of income growth. In Armenia people's incomes are growing to a great extent thanks to the money their relatives send them from abroad (about \$400 million every year). In fact, the registered economic growth could not push the incomes that high; besides, the incomes are unevenly distributed. The republic's GDP depends, to a great extent, on money from abroad that ensures a definite consumption level, which is part of the GDP structure. Financial aid coming from the All-Armenian Foundation and Linsi Foundation is of great importance, yet the money is never used for the much-needed investments.

To assess how incomes are distributed among social groups the author, together with a group of Armenian economists (A. Markarian, A. Vardanian, S. Avetisian), carried out a research project in which the population was divided into the following groups:

- I. People living on money they earn themselves or on wages.
- II. People with considerable additional incomes: aid coming from other countries; hard currency coming from relatives living abroad; aid from rich relatives living in Armenia; foodstuffs supplied by relatives from the countryside (in Armenia this is fairly important).
- III. Pensioners. They can be divided into those who can still work and earn money; those who are looked after by children or other relatives; inmates of old people's homes; beggars.
- IV. People living on unearned incomes such as bribe-taking civil servants. There are bureaucrats from ministries among them, people working in the city and district executive structures; in law enforcement and military structures; monopoly spheres of economic and other services; a numerous group of those who appropriate incomes produced in the industrial sphere; those who have grown rich as a result of privatization, and bribe-taking people working in the sphere of education, health protection, etc.
- V. Unemployed living on incidental earnings.

² See: S. Davoian, A. Markosian, G. Sargsian, *Reformy v stranakh s perekhodnoy ekonomikoy*, Tigran Mets Publishers, Erevan, 2003, p. 171.

Taking into account the fact that the Gini coefficient has increased, the income distribution among different social groups did not change much: the social polarization level remains practically the same (the lower steps of the ladder are occupied by families with many children, pensioners, and unemployed—about 1 million in all).

Table 2

Families Grouped by Daily Incomes (\$)

Category	Volume of daily income of one family	Number of families	Volume of daily income by families	Share of families as a whole (%)	Share of family incomes as a whole (%)
I	200 and more	3,000	600,000	0.38	8.32
II	150-170	3,000	525,000	0.38	7.28
III	50-100	14,000	1,050,000	1.77	14.56
IV	20-50	89,000	3,115,000	11.28	43.21
V	10-20	50,000	750,000	6.34	10.4
VI	5-10	20,000	150,000	2.53	2.08
VII	2-5	200,000	700,000	25.34	9.71
VIII	1,5-2	180,000	262,500	19.01	3.64
IX	0.25-0.30	100,000	27,500	12.67	0.38
X	Below 0.25	160,000	28,000	20.2	0.38
	Total	789,000	7,208,000	100.0	100.0

Source: Droshak, No. 17-19, 1995-1996, p. 98.

The above shows that 0.76 % of the families enjoy 15.5% of the total income; 11.28%, 43.21% of the total income; 77.3%, 14.11% of the total income. I have already written that even though the per capita income has recently increased, its distribution among the social groups remained practically the same. According to official information, even if the gap did not grow wider, social stratification remained the same and too close to the critical level: nearly 80% of the families are struggling below the poverty level. An average share of the poor (living on less than \$1 a day) is 5.1% in Eastern Europe and Central Asia; 15.3% in Eastern Asia and the APR; 40.1% in South Asia, and 46.4% in the sub-Saharan countries.³

According to official data, the minimum per capita consumption basket in Armenia is 28,000 drams (about \$48), which means that with an average wage of \$43 (that few people earn) the level of poverty in the country is very high.

One should say that the level of emigration is equally high: people are driven away by the economic situation as well as by the political and sociopsychological conditions. They are trying to escape the unfavorable moral and psychological climate (injustices, corruption, and frequent violations of laws). This atmosphere robs the country of its future. There are no official figures on emigration and the demographic situation in general. "Distorted official information about the population size, its age-and-gender structure and the reproduction processes has created a wide gap between real and official assessments of the social situation in the coun-

³ See: S. Davoian, A. Markosian, G. Sargsian, op. cit., p. 57.

try.⁴ This can be said about all other spheres, which makes it hard to use official statistics for any assessments. For example, according to official figures, there are 3,210,000 people living in Armenia while alternative estimates quote the figures of 2.2 to 2.5 million which look much more real. According to official statistics, “in December 2002 the unemployment level was 9.1%,”⁵ the alternative figure being about 40%.

In the last ten years the birth rate dropped by more than 50% as a result of emigration (9.0% in 2000 compared with 21.6% in 1991). In 1998, the main natural growth index (the difference between the number of births and deaths) was 16,156 people; in 1999, 12,415; in 2000, 10,321; in 2001, 8,100.⁶

Certain figures can be used to judge the perspectives of any given country; I have in mind the share of the GDP spent on education. In Germany the figure is 4.9%; in France, 6%; in Italy, 4.9%; in the U.K., 5.3%; in the U.S., 5.4% while in Armenia it is as low as 2.4%.⁷ This means that Armenia lacks a development strategy of its human capital that is mainly responsible for economic growth. In Armenia with its traditional bias for learning and science human capital is especially important. Today, the share of culture, sport and religion in the state budget is meager 2.2%; it cannot create a basis, either in education or in culture, needed to ensure future progress.

A system of indices of economic security based on a certain threshold index formulated by Sergei Glaz'ev, a Russian academic and politician, can be used to assess the present situation in Armenia.

Table 3

Economic Security Indices

Indices	Threshold Index (%)	Real Situation in RA (%)
1. Per capita GDP as compared with the G7 countries	50	2.6
2. Correlation between investments and GDP	25	—
3. Correlation between scientific research and GDP	2	0.2
4. Share of population living below the poverty level	7	70
5. Income gap between 10% of the richest and 10% of the poorest	8 times	100 times
6. Unemployment level	7	40 (unofficial figure) 9.1 (official figure)
7. Annual inflation	20	3
8. Budget deficit	5	4.1
9. Level of dollarization	25	41
10. Correlation between foreign debts and GDP	25	47.3

Sources: Armenia. *Issledovania gosudarstvennykh dokhodov*, 28 April, 2003, p. 4; “Godovoy otchet Tsentral'nogo Banka RA, 2002,” *Voprosy ekonomiki*, No. 10, 1998, p. 36.

⁴ Ibid., p. 218.

⁵ “Sotsial'no-ekonomicheskaia situatsia v RA v ianvare-dekambre 2002 goda,” in: *Natsional'naia statisticheskaia sluzhba RA*, Yerevan, 2003, p. 147.

⁶ See: S. Davoian, A. Markosian, G. Sargsian, op. cit., pp. 218-219.

⁷ See: Ibid., pp. 188-189.

From this it follows that according to several indices the country is below the minimally acceptable level. One should say that the system of Glaz'ev is not an integral one: there are other criteria beyond it. I have in mind the country's dependence on foreign financial sources; monopolization of the national market by transnational corporations; the scope of capital outflow; threats to economic and currency independence, etc. which are hard to be expressed in figures. If adjusted to the development specifics of a state (region) the system offered by Glaz'ev makes it possible to assess the economic situation in the country. No adjustments, however, can change the logic of such assessments.

The economic processes underway in Armenia lead to the following conclusions: economic growth depends on the money coming from abroad; institutional changes are slow and ineffective; the republic cannot compete with its neighbors while privatization as an economic instrument cannot distribute the funds efficiently.

C. Main Causes

The economic situation in Armenia is far from satisfactory for the following reasons:

- a) *Disintegration of the Soviet system and disruption of the traditional economic ties.* Until 1998, 90% of the industrial raw materials and 65% of consumer goods were imported. On the other hand, the share of end products among the republic's products was merely 20 to 25%.
- b) *Tension created by the Karabakh conflict and blockade of Armenia.*
- c) *Transfer from one economic system to another takes time and is crisis ridden.*
- d) *Ineffective realization of the public choice principles.* This problem common to nearly all countries during periods of transition is, in fact, an intertwining of economic, sociopsychological and geopolitical factors, which is very hard to address successfully. Social development is a totality of complex and contradictory processes in which public choice plays the key role. Its principles directly affect the economic system for an obvious reason that any economic policy is determined by the nature of political system, which is, in turn, the result of public choice.

At the civilizational level Armenian society theoretically accepted a state political system that suited its axiological system while in practice many factors turned out to be negative ones: to specify the ideological foundations the nation has to identify its specific nature. In other words, what was needed was a scientifically substantiated approach that is missing for objective reasons.

The Third Republic inherited numerous negative Soviet phenomena while public choice was obviously affected by the absence of adequate traditions and institutions. It means that the present situation is deeply rooted in the past and is burdened with numerous historical, civilizational, geopolitical, psychological, and other factors. Since many propositions of the national program based on certain values and ideas remain unspecified, the principles of public choice cannot be realized with any degree of efficiency.

- e) *The absence of counterweights between the economic and political systems.* While the regularities of public choice remain untapped to the full extent and because of operation of numerous levers the political system dominates over the economic one. This is mainly a shortcoming of any transitional economy. Political systems in newly independent states are not easy to create: public organizations with no social bases of their own are trying to play the role of such political systems by using political levers. On the whole, the following factors are indispensable for a successful emergence of a political system: mutually balanced legislative, executive and judicial powers; political parties and democratic institutions; a lower level of dependence on all sorts of international organizations and other countries. All post-Soviet states have to grapple with these problems because in the Soviet past the balance between the legislative, executive and judicial powers was a purely formal one and there was only one party.

Dependence on other countries is caused by objective reasons: the economically weak states cannot oppose global challenges on their own. This explains why in Armenia the principle of balance of power does not work properly and why there are no counterweights between the economic and political systems. The present constitution has given wide powers to the president, which the National Assembly is unable to balance. This is why the constitution should be amended: the presidential powers should be trimmed in favor of the National Assembly.

Any political system should be based on genuine democratic principles, which requires a real, not formal, balance between the legislative, executive, and judicial powers and the rule of law. Normally, the countries in transition respond with stronger central power to numerous problems, which is frequently interpreted as an onslaught of dictatorship. This is not a dictatorship since it is not aimed against the people; more likely than not it is manifested in authoritarian regimes that are either part and parcel of national mentality or are an inevitable feature of the transition period. To be successful such regimes should follow state-by-stage programs and act within the laws (China, Vietnam, Cambodia, etc. are the best examples).

The economic system in Armenia is a very weak counterbalance to the political system; in a way it is its appendage, which explains, among other things, the high level of shadow economy in the country (50 to 60 percent).

- f) *An imperfect institutional system.* The economic thought of the 20th century overcame the postulates of the classical and neoliberal economic theories and pointed out that the self-regulation levers should be supplemented with corresponding institutions. While the economic levers betray the nature of inner impulses, an institution presents a sum-total of principles on which the economic, legal, cultural, sociopsychological relationships rest. Together, the levers and the institutions act efficiently. Even the developed countries have to improve their institutions all the time to overcome internal contradictions and paradoxes of axiological criteria present in all relationships. In all social orders and irrespective of their nature certain institutions add efficiency to economic levers (or deprive them of it). Naturally enough, in transitional societies the problem acquires vital importance, therefore efficiency and rational behavior cannot be achieved through economic liberalization alone.
- g) *Inefficient tax-and-budget and monetary policies.* The state uses these instruments to achieve macroeconomic stability and encourage growth. In Armenia the situation is a contradictory one: the country has so far failed to realize a flexible tax policy. According to the chambers of commerce of the U.S. and the EU, “among the former Soviet countries Armenia comes the last but one before Georgia with 14.5% where the share of tax revenues in the GDP is concerned and is below the average CIS figure of 24.8%.”⁸ This means that the state cannot pursue a socially oriented budget policy and cannot address economic problems related to specific economic priorities. Analysts believe that low tax revenues are caused, among other things, by a high share of shadow economy in the country: “In Armenia there is no balance between the tax base and tax collection; the aims of the taxation system and the methods of tax collection should be revised. Lack of balance is pernicious for Armenia.”⁹

The above-mentioned joint report of the chambers of commerce points to the high taxes, unpredictability of the system of tax collection and the difficulty in observing laws in Armenia as the country’s main problems.¹⁰ Frequent changes of laws cause disorder in the tax system since laws are frequently borrowed from other countries and alien legal systems. As a result they cannot be applied in Armenia, which leads to corruption in the system of tax collection.¹¹

⁸ *Reformy nalogovoy sistemy Armenii, perspektivy inostrannykh investitsiy. Doklady torgovnykh palat SShA i Evropeyskogo soiuza v Armenii*, Erevan, August 2003, p. 1.

⁹ *Ibid.*, p. 2.

¹⁰ See: *Ibid.*, p. 3.

¹¹ See: *Ibid.*, p. 4.

The monetary policy can be described as excessively strict. The unfavorable macroeconomic situation prompted reduction in money supply to curb inflation carried out in disregard of the socioeconomic situation. Even if increased money supply does increase inflation to a certain extent, monetarization of budget deficit is the correct answer to the problem.

Reduced money supply leads to higher interest rate that affects investments, which means that the Ms-r-I-Y principle and the money levers are used with little effect. Long-term investments, one of the sources of the real sector developments, are not stimulated.

The insignificant share of the commercial banks' gross capital in the GDP is due to not only the low level of savings and investments but also to lack of confidence in these banks. The laws and the Central Bank's policy also contribute to this state of affairs. The Central Bank is exploiting the vagueness of laws to bankrupt some of the commercial banks. Normally (that is, in the market system) banks merge for economic considerations in an effort to boost their efficiency. This may improve the entire system. The Central Bank's spokesmen offer this as an explanation, yet reality is different. It was discovered that the Central Bank had been involved in bankruptcies of certain commercial banks, which did nothing to improve the system and slowed down the flow of investments to the domestic market. The Central Bank should act within the laws to promote economic revival—in actual life it, while formally accepting the European standards and the holes found in laws, makes impossibly high demands on commercial banks (even though it is aware of their inapplicability in the current situation) and sometimes even arbitrarily interprets their actions. This affects the distribution of the investment functions and of public capital in general.

- h) *Discrepancy between the scientific and educational system and modern requirements.* The tendencies described above affected the educational system, one of the strategic spheres of any state, in which the following trends can be observed:
1. At all times the superpowers pursue their very special policies. Today, they are aiming at creating marginalized and economically dependent units expected to supply raw materials and brains to the developed countries. The long-term strategic programs of all strong states mention brain drain as one of the major factors. In this way the national gene pool of the exporting countries changes its quality. While in the Ottoman and Soviet (especially in the 1930s) empires the intellectual potential was physically exterminated, today the process has assumed latent forms. The creative potential of the Armenians that should serve its countries is exploited elsewhere.
 2. The educational programs are changed and the system is crumbling. This is caused by the state's weakened control over the educational system and its transfer to the "base" sphere of the market relationships; in particular, schools are supplied with textbooks very much below the educational standards. The content has been changed in such a way that the spiritual and intellectual potential of the new generation will be affected while its mentality will differ from what we have now. The credit programs offered by the international financial organizations have contributed to the process. So far, the republic has no money to pour into the educational system while the international credit programs do practically nothing to encourage publication of textbooks suitable for our national mentality and realization of certain indispensable measures. The Soviet school, on the whole, ignored the ethnic problems and was ideologically dominated, yet it gave profound knowledge of scientific disciplines. Today, the programs have not only failed to change the Soviet educational system in an effort to adjust it to the ethnic way of life and the centuries-old traditions of thinking but also nearly ruined the system of secondary education. Any school reform needs adequate funding—a lack of a national program and an absence of interest in this problem among the national elite deprived the school reform in Armenia of financial support.

- i) *The moral and psychological atmosphere.* Any economic analysis usually ignores the moral and psychological aspects, yet all internal impulses of the social system's self-regulation are based on the moral and psychological values manifested in principles, traditions and concepts (justice, truth, etc.). A U-turn in any sphere of public life will be possible only if these values are revived; this is not a self-propelling process—it requires adequate measures on the part of the state, as the supreme manifestation of the common will. To accomplish this we should first complete the process of state formation.

It follows from the above that in view of our country's specific development we should set up a model that would regulate its political and economic system in order to ensure the optimal development of all spheres of public life.