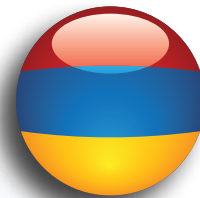


STRONGER ECONOMY

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EU4Business

Investing in SMEs in the Eastern Partnership

Armenia

COUNTRY REPORT
JUNE 2018



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Introduction

The EU4Business Secretariat is proud to present the third Country Report prepared under this initiative, following the first in late 2016, and the second publication in May 2017. Country Reports analyse the developments and achievements of the EU4Business initiative in each of the Eastern Partnership countries (EaP). They offer a review of the SME sector in the country, as well as of the economic and business environment in which enterprises operate. In addition, the 2018 Country Reports add two major new elements, namely the results of an SME survey and the outcome of round tables of EU4Business stakeholders carried out in each EaP country.

The national round tables were held between late February and early April 2018, and involved all the EU4Business stakeholders in each country, as you will see in Section 6 of the Report. The conclusions offer a unique perspective arrived at following a detailed joint consideration of all the EU4Business pillars and initiatives.

The results of the survey of SMEs benefiting from the EU4Business finance facility are presented in Section 5. They provide an overview of the impact of EU4Business, as perceived by the beneficiary enterprises themselves, at least a year after the lending operation has been completed.

We have also conducted a thorough analysis of some 150 documents and discussed these with a multitude of stakeholders to arrive at the impact assessment of the EU4Business portfolio, as presented in Section 3.

Finally, the two opening sections provide an economic overview by country and the state of affairs of the SME sector.

The EU4Business Secretariat has received tremendous research assistance from our country teams, based in the EY offices throughout the Eastern Partnership region, while the EU Delegations provided substantial support and data for the publication. DG NEAR was closely involved in report editing and verification. To all of them we extend our sincere thanks.

We anticipate that the materials presented here will support the reform discourse in each of the six countries, contributing to further enhancement of the SME climate and regulatory framework. The Secretariat looks forward to facilitating new national-level discussions on how further to improve effectiveness and delivery of EU support to the EaP's SME development and to work on new and innovative support instruments.

Boris Divjak, SME Expert
EU4Business Secretariat
www.eu4business.eu



SECTION 1:

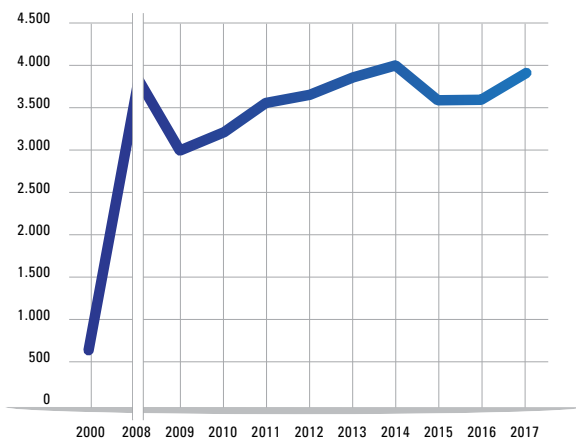
General economic overview of the country



1.1 Macroeconomic indicators

In 2017, GDP growth in Armenia outperformed expectations, recording the highest rate of growth in the past decade at 7.5% after a flat economic performance in 2016. Growth was driven mainly by a recovery in the external environment and supported by a strong rebound in domestic demand. Consumption benefited from higher incomes and recovery in remittances. On the production side, growth in 2017 was driven by a significant expansion in trade (16%), industry (10%), and services (9%). The high pace of growth continued in the first two months of 2018, and economic activity grew by about 9% year-on-year.

Figure 1.1: Republic of Armenia's GDP per capita (current US\$)



Source: Macroeconomic Indicators, World Bank

The period of deflation came to an end in 2017 and inflation began rising, reaching an annual rate of 2.6% by year-end, within the Central Bank of Armenia (CBA) inflation target of 4% (+/- 1.5 percentage points). Recovering domestic demand, gradually rising commodity prices, and excise tax hikes resulted in higher prices for food, beverages, cigarettes, and transport. Inflation continued to rise in 2018, reaching 3.3% in February.

Another factor contributing to inflation in January 2018 was the increase in customs duties for some 40 types of imported products as a result of Armenia's membership in the Eurasian Economic Union (EEU),

which sets higher uniform tax rates for a long list of imported items from countries outside the union¹.

The banking sector remains well capitalized and liquid. The economic recovery in 2017 is expected to have supported a further reduction in poverty rates, which have been on a declining trend since the global economic crisis. The economic outlook remains positive. The strong economic performance in 2017 suggests a window of opportunity to tackle and accelerate the challenging reforms to make the growth inclusive and sustainable in the medium term. On the back of sustained favourable external economic conditions and subject to robust structural reforms, medium-term growth is forecast to be around the potential growth rate (4%), based on private sector, export-led activity; the agribusiness, ICT, and tourism sectors in particular are expected to deliver solid growth as efforts to increase competitiveness and connectivity start to deliver results².

In comparison to the other Eastern Partnership (EaP) countries, Armenia recently rebounded to have higher than average growth rates, after years of trailing behind. The inflation rate has been well below the regional average, but as stated, this has also reversed out of deflation. Its export levels are the second lowest among the six in absolute terms but nearly doubling over the past decade. However, the fact that as percentage of GDP, Armenia has the lowest export volumes (33% compared to the EaP's average of 46%) indicates there is a lot of room for expansion. Crediting of the private sector has been on the rise and has overtaken the regional average with nearly 49% of GDP in 2016, according to the IMF, even though the lending interest rate is somewhat higher than the EaP's average, though dropping continuously – 14.4% in 2017, according to the WB. There has been no major exchange rate and local currency fluctuation in the past couple of years, so a Euro is worth 572 Armenian Dram (AMD) in mid-May 2018.

1 Extracted from the World Bank in Armenia, <http://www.worldbank.org/en/country/armenia/overview#3>

2 Extracted from the World Bank's Macro Poverty Outlook – Armenia, <http://pubdocs.worldbank.org/en/683891507031719168/Armenian-MPO-October-2017.pdf>

1.2 Trade volume with the EU – exports

This section focuses on Armenian exports to the EU on pre-selected trade categories which prove to have a high growth potential, with a high activity of SMEs and excluding large-scale activities. The selected trade flows will be analysed in terms of size, economic impact and employment impact³. On average, the impact on the economy of the EaP countries of these selected trade flows amounts to 1.5% of the GDP, and 1.3% of the total employment. The effect is in comparison smaller in Armenia in which the total impact of exports of the selected categories of the EU on the GDP and employment amounts to 0.1%. The reason for this is that many exporting categories are in fact large-scaled activities which were not included in the analysis.

During 2009 and 2016 on average the total Armenian exports of goods to the EU amounted to €378 million, of which only €9 million represent exports of relevant categories to the EU, after removal of large scale activities. The 72% of this, that is also considered to be stemming from potential growth categories, significant categories for Armenia, are:

- Preparations of vegetables, fruit, nuts or other parts of plants (categories in HS20)
- Articles of apparel and clothing accessories, not knitted or crocheted (categories in HS62).

Selected exports to the EU directly affect gross production in Armenia by €6 million. The value added associated with this is €5 million, and in total 500 jobs are associated with these exports.

As the production for exports involves additional supplies of intermediate goods and services, the total effect on the Armenian economy is larger than the direct effect. The total impact on value added is €7 million, or almost 0.1% of GDP. The total impact on employment is 1,000 jobs, i.e. 0.1% of total employment depends on exports of selected categories to the EU.

1.3 Business climate

Positioned 47th globally, the Republic of Armenia is an exact median of the six EaP countries in the Doing Business rankings of the WB by the ease and costs of business regulations. Georgia remains far ahead and somewhat better than Armenia are Moldova and Belarus, but they are all well ahead of Ukraine that trails the group.

However, the business climate has steadily been improving over the past five years, according to the indicator. Of the various topics that Doing Business covers, Armenia is most advanced with property registration and starting a business (13th and 15th position globally, respectively), while lagging behind with resolving insolvency, where it is ranked 97th of 190 countries ranked.

Corruption is a critical bottleneck for greater investment volume, as shown also by Transparency International's Corruption Perception Index, whose score for Armenia has been fluctuating over the past five years between 33 and 37 (100 being best and 1 worst), placing it in 2017 in 107th position globally among 180 countries, with a current score of 35⁴.

Armenia has a range of BSOs that actively engage in monitoring of the business environment, reporting on it and discussing progress with the public sector. Besides the official Chamber of Commerce, there are several other associations, including the foreign chambers and associations, such as American, British and European. Business Support Offices and Centres that grew out of the EBRD, EU, WB and Government projects are supporting SMEs through technical assistance, while also playing a role as a conduit for business environment improvement and proposing improvements to the authorities. Even though the chambers typically work with larger companies, all of the identified associations actively support SME development and promote policies aimed at their strengthening.

³ Panteia, (2018), Study: Key sectors and BSOs - Step 1 selection of the sectors). Data on trade flows sourced from the International Trade Centre (ITC).

⁴ According to the Corruption Perception Index of Transparency International: https://www.transparency.org/news/feature/corruption_perceptions_index_2017



EU4Business

ARMENIA: weaving tradition towards export success



“

Thanks to the contacts we established with the support of the EU, quality threads as well as international markets became part of our work.

”

Inga Manukyan is a co-founder, director and designer of LOOM LLC. Thanks to EU4Business support, LOOM weaving has expanded its knitwear business beyond the borders of Armenia, to the EU, U.S. and Russia. Two advisory support projects from the EBRD set the company going in the areas of branding, finances, sales and networking, while networking support from the EU-SMEDA project took the company to European trade fairs, a key step in expanding their suppliers and meeting new export clients.

Success stories:
Women in Business and
EU-SMEDA



SECTION 2:

Share of SMEs in the economy

According to the national statistics, for which the latest available are from 2016, the Republic of Armenia has a total of 78,246 SMEs. Most SMEs in Armenia's economy are micro enterprises, representing approximately 91% of all MSMEs present. Small enterprises represent almost 7% of SMEs. Both micro enterprises and small enterprises are mostly active in the established sectors of repair of motor vehicles and motorcycles, followed by manufacturing, and accommodation and public catering. Only 2% of SMEs are in fact medium-sized enterprises and share with the other two, a prevalence in the sectors of motor vehicle repair and manufacturing, with some relevant activity in the healthcare and social welfare services sector.

SMEs in Armenia contribute significantly to employment and job creation, with total SMEs in 2016 reporting 302,001 employees.

The three sectors which mostly employ personnel are reflected to the sectors in which the SMEs are in fact active: most employees work in the sector of motor vehicle repair, followed by manufacturing, and thirdly healthcare and social services, the latter mostly employed by medium-sized enterprises. SMEs represent the majority of businesses in Armenia and their contribution to the national GDP increases year by year. In 2015 it represented 30%, while in 2016 it was 36% of the total GDP.

The tables below provide a detailed account of SMEs' activity in Armenia on the basis of three indicators: number of SMEs, number of employees and SMEs' turnover, in all different trade categories⁵:

⁵ Ministry of Economic Development and Investments of the Republic of Armenia, SME Indicators 2016, <http://mineconomy.am/en/449>

Table 2.1: Number of SMEs as of 31 December 2016

2016	Extra small	Small	Medium	Total
Agriculture, forestry and fishing	383	65	19	467
Mining industry and open exploitation	278	47	9	334
Manufacturing, including:	6,012	683	210	6,905
<i>Non-food production industries</i>	3,670	398	128	4,196
<i>Food production industries</i>	2,342	285	82	2,709
Construction	892	448	130	1,470
Wholesale and retail trade, repair of Vehicles	44,760	1,651	399	46,810
Transportation and storage	881	282	66	1,229
Hospitality and catering	2,723	456	82	3,261
Telecommunication	1,394	269	61	1,724
Education	328	107	23	458
Healthcare and social welfare	782	192	160	1,134
Culture, Entertainment	480	38	15	533
Other	12,693	1,034	194	13,921
Total	71,606	5,272	1,368	78,246

Table 2.2: Number employees of SMEs as of 31 December 2016

2016	Extra small	Small	Medium	Total
Agriculture, forestry and fishing	832	1,221	1,289	3,342
Mining industry and open exploitation	1,127	805	815	2,747
Manufacturing, including:	14,481	13,683	18,102	46,266
<i>Non-food production industries</i>	8,261	8,116	10,891	27,268
<i>Food production industries</i>	6,220	5,567	7,211	18,998
Construction	3,827	8,983	10,899	23,709
Wholesale and retail trade, repair of Vehicles	36,471	22,465	22,139	81,075
Transportation and storage	3,229	5,526	4,441	13,196
Hospitality and catering	7,638	9,134	7,593	24,365
Telecommunication	4,170	5,082	5,585	14,837
Education	1,714	2,345	2,108	6,167
Healthcare and social welfare	4,705	3,652	17,585	25,942
Culture, Entertainment	1,200	797	1,277	3,274
Other	22,190	18,254	16,637	57,081
Total	101,584	91,947	108,470	302,001

Table 2.3: SMEs' turnover in AMD as of 31 December 2016

2016	Extra small	Small	Medium	Total
Agriculture, forestry and fishing	2,688,810,194	5,395,628,420	11,885,165,568	19,969,604,182
Mining industry and open exploitation	3,271,855,909	4,120,182,820	4,032,320,982	11,424,359,711
Manufacturing, including:	47,866,850,978	69,214,896,567	101,414,495,347	218,496,242,892
<i>Non-food production industries</i>	31,803,752,240	44,112,398,908	64,067,852,137	139,984,003,285
<i>Food production industries</i>	16,063,098,738	25,102,497,659	37,346,643,210	78,512,239,607
Construction	14,461,997,112	56,372,747,636	64,816,671,412	135,651,416,160
Wholesale and retail trade, repair of Vehicles	365,347,542,866	265,601,413,342	236,464,885,636	867,413,841,844
Transportation and storage	10,671,026,559	20,995,484,120	23,485,393,615	55,151,904,294
Hospitality and catering	17,727,082,423	28,315,660,087	29,299,712,983	75,342,455,493
Telecommunication	15,151,829,336	23,898,276,008	26,385,422,777	65,435,528,121
Education	1,725,350,805	3,108,569,046	4,356,931,564	9,190,851,415
Healthcare and social welfare	12,361,916,261	12,696,296,013	52,587,100,935	77,645,313,209
Culture, Entertainment	1,833,350,594	1,836,107,084	4,286,857,237	7,956,314,915
Other	85,028,138,573	101,886,162,188	86,676,004,631	273,590,305,392
Total	578,135,751,610	593,441,423,331	645,690,962,687	1,817,268,137,628

SECTION 3:

Overview of the EU4Business portfolio in Armenia

The EU4Business umbrella initiative has subsidised a total of 18 projects in Armenia since its inception. During the years 2009 to 2017, a total of 6 projects have been completed while 12 are still ongoing. These projects cover four key areas of support, and in Armenia most projects (8) have been set up to Improve knowledge base and business skills, 4 to Improve access to finance, 3 to Strengthen policy and the regulatory framework, and another 3 to Improve access to markets.

The table illustrates the distribution of projects in the different support areas, and which of those are ongoing and which are completed.

Table 3.1: EU4Business project portfolio

PROJECTS in ARMENIA				
Area of support	A: Improving Access to Finance	B: Strengthening policy and regulatory framework	C: Improving knowledge base and business skills	D: Improving access to markets
Ongoing projects	4	2	5	1
Closed projects	0	1	3	2
Total projects	4	3	8	3

Source: EU4Business database

The EU supported these ongoing projects through a contribution of approximately €31,850,000, which is mostly awarded to ongoing projects in the field of improvement of access to finance, followed by projects which address the need for improvement of the knowledge base and business skills.

Regarding completed projects, the EU contribution amounted to approximately €4,800,100. These contributions targeted projects for improvement of access to markets, an area in which two projects have been closed, and the area of improvement of knowledge base and business skills with three closed projects.

The EU4Business initiative and the projects implemented through it have a relevant impact on enterprises and on job creation.

The table below summarises these key impacts in terms of enterprises supported, the number of enterprises that received loans, the total value of the loans provided via the programmes, and the number of jobs created through the programme's support:

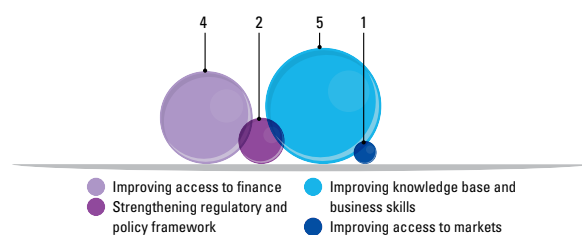
Table 3.2: EU4Business impact in Armenia

Impacts of EU4Business support	2009-2015	2016-2017	2009-2017
Number of enterprises supported with advisory services	348	258	606
Number of enterprises which received loans	10,090	2,550	12,640
Total value of loans disbursed (Euro)	323,100,000	94,019,383	417,119,383
Number of new jobs created	1,311	1,141	2,452
Number of jobs supported and sustained (advisory and financial projects)	18,741	4,290	23,031

Source: EU4Business database

Success stories from beneficiaries show the impact of different types of EU4Business support: in the case of knitwear manufacturer LOOM weaving⁶, advisory support under the Women in Business programme led to significant growth in turnover, customers and sales, while the testimony of fashion designer Alla Pavlova⁷ highlights the value of cluster creation for the fashion sector under EU-SMEDA.

Figure 3.1 Ongoing projects by objective



Source: EU4Business database

⁶ For the related success story, please refer to page 5.

⁷ For the related success story, please refer to page 15.



EU4Business

ARMENIA: helping a digital start-up reach out to Europe



“ Thanks to EU support we got lots of contacts, feedback on what we should improve, what to do to get in a specific market. ”

Mane Varosyan is one of the co-founders of TripleE, an augmented reality platform, receiving support from the EU-SMEDA project, including participation in start-up fairs and academies in Salamanca and Berlin, where the company gained experience and made vital contacts. Now, with ongoing support from EU-SMEDA, they are expanding their market into Europe.

Success stories:
Support to SME Development
in Armenia (SMEDA)

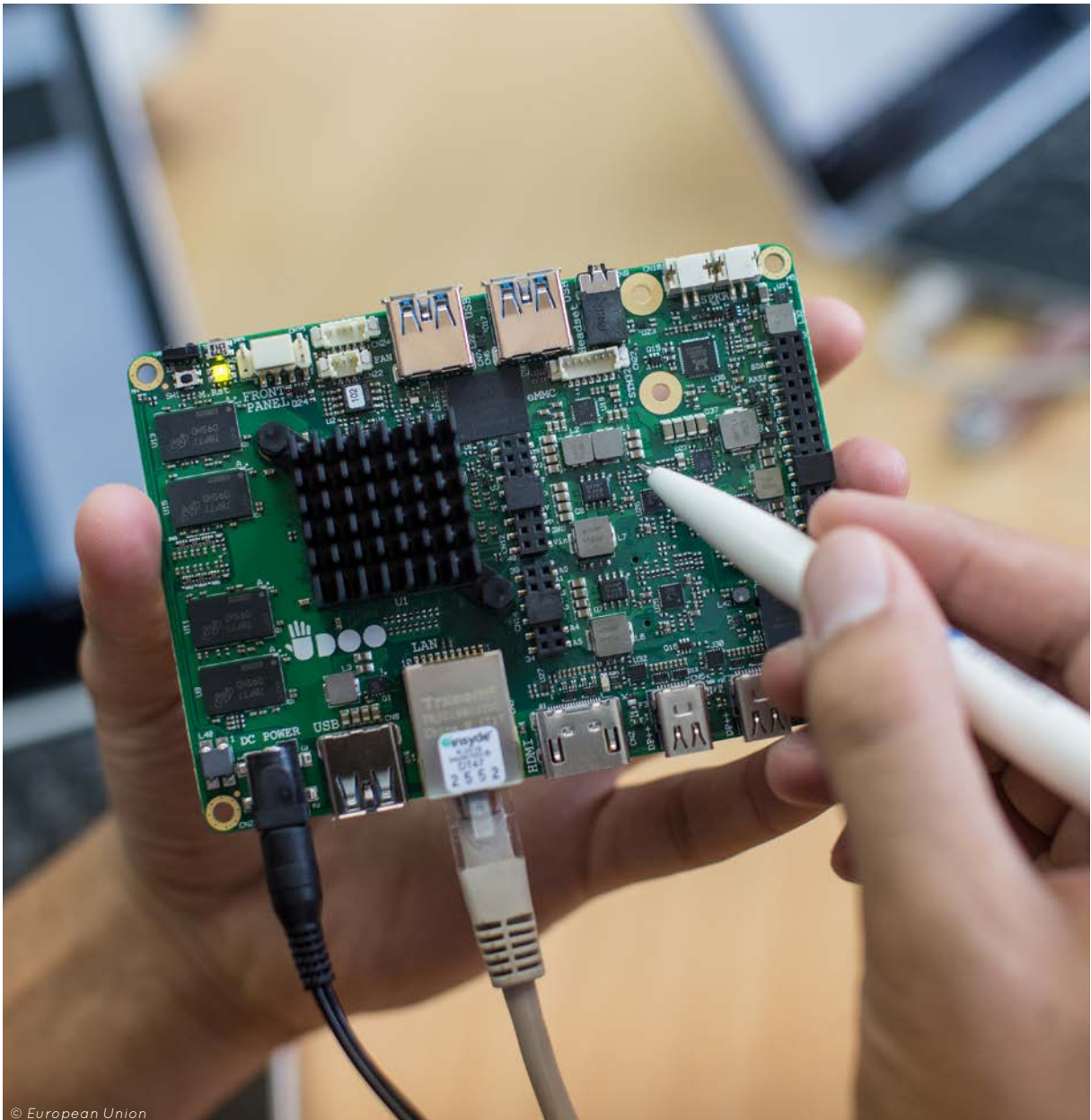
SECTION 4:

Donor support to the SME sector in the country - looking beyond EU4Business

Nearly 40 projects have been identified that focus on strengthening the role of SMEs in Armenia: 15 support SMEs with grants from a variety of bilateral and multilateral institutions, another 16 in the form of loans, often targeting SMEs directly or through the banking sector, like the access to finance pillar of EU4Business, and 5 projects are equity investments in SMEs. The Government of Armenia currently

supports six programmes, including a revolving guarantee fund and export financing insurance, which it runs exclusively with state funding.

Grant programmes largely look at increasing the value added to SMEs in strategic sectors, such as agribusiness, textile or tourism, but also targeting certain niches with high growth potential: export-



oriented industries, youth entrepreneurs, value chain development, etc. They are channelled through local, often rural communities, central public authorities, MSMEs directly, NGOs, BSOs (particularly sector representatives), consultancies (foreign and national) and the donors themselves. Grants rarely distort other market strengthening efforts, as they mostly aim at strengthening capacities, educating and training, enabling the target audience to add value or engage in a new niche or activity, or developing intermediaries and consultants who can then work with the ultimate beneficiaries.

The project sizes vary and they are mostly multi-million in scope, except for the largest programme, Competitiveness of Enterprises and Small and Medium-sized Enterprises (COSME) 2014 to 2020 Programme, which includes all the EaP countries and for the whole period amounts to €2.3 billion in total for all COSME members, including Armenia.

Loan programmes are less restrictive and target the most viable investments, as could be anticipated. Majority of ongoing SME finance programmes are concentrated on 'traditional' SMEs and donors have highlighted a few sectors as appropriate for investment: renewables and energy efficiency, rural entrepreneurship and infrastructure, agribusiness, etc. Many of these projects target specific instruments, such as enabling guarantee funds, portfolio diversification for banks, etc. and noteworthy are also the German-Armenian Fund (GAF) and the central authorities in case of the government guarantee fund. The funds are channelled through local banks, and all these projects amount to several hundreds of millions of Euros of investment, with the largest institutions involved being KfW and the Asian Development Bank.

Equity investment is led by the EBRD, typically through banks, except the Armenian SME Fund that is about to launch its own activities soon. Total equity investment in the country comes to about €100 million. In addition, Granatus Ventures is a venture capital firm established with a World Bank loan to the Government of Armenia, with co-investment from a private fund aimed at start-ups.

Finally, the Export Insurance Agency of Armenia seeks to provide export insurance to Armenian exporters against the financial losses incurred as a result of non-payment for supplied goods by their foreign buyers, or to provide pre-export financing insurance. Comparing these interventions to the suggested gap assessment as portrayed by the national round tables and other analyses deployed by the EU4Business Secretariat, most of the main needs are being met. A significant gap remains in access to finance in the following enterprise stages/sectors: (i) new businesses/early stage SMEs; (ii) innovative start-ups; and (iii) acceleration and internationalisation of SMEs.

The key issue is speed of implementation and disbursement of aid, which in turn depends on the speed of reforms and the local absorption capacity. This is undoubtedly a process that will take time, especially given the macroeconomic and systemic reforms that are almost a prerequisite. However, support programmes focused on grants (without a matching component) have often contributed towards skewed ineffective spending incentives rather than value creation and business development. The time has come for the investment mind-set in providing financial support to evolve. The next generation of financial instruments and support programmes should use blending to achieve the right incentives for SMEs and to drive business sophistication, corporate governance, internationalisation and value creation.

EU4Business could retain its focus on high-growth sectors such as the ICT industry, for which there is significant interest and a nascent local market. Its advantage is that it requires no fast and cheap land route for transport of goods/services, but also that various industrial parks and hubs can be developed throughout the country, therefore ensuring a balanced development of the capital vs. the regions of the country.

A range of instruments is needed for this development: from the actual funds to support business development to guarantee funds (particularly as many of the entrepreneurs have little starting capital), to tailored technical assistance and business coaching and mentoring in form of know-how and consultancy work. Enabling easier access to the EU market through business matching, participation in fairs and accessing specialised online facilities might be a relatively small investment yielding comparatively high growth. The potential impact of this kind of support is illustrated by the success of the TripleE tech start-up, which received support from the EU-SMEDA project⁸.

⁸ For the related success story, please refer to page 9.

SECTION 5:

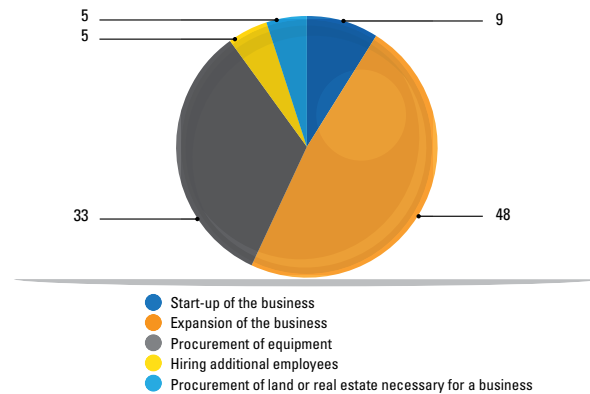
SME survey results

20 SMEs, all beneficiaries of the financial products of EU4Business, were surveyed in Armenia in the period March-April 2018⁹. All the respondents shortlisted were beneficiaries of the EFSE facility. 70% of those were limited liability companies and 30% were individual entrepreneurs. Half of them come from the retail sector and the rest from manufacturing and services almost equally. The vast majority had been in operation for more than 10 years prior to taking the loan, and the dominant employee size is up to 10 staff – 75% of them.

It is very interesting that the vast majority of respondents (75%) have no idea that the funds originate from the EU4Business programme or from the EU. They are simply aware of the bank from which they borrowed and for 100% of them it was the point of entry into the programme. Despite much praise in Armenia for the borrowing in local currency through EU4Business, 75% of respondents had borrowed in foreign currency, and they all obtained the full amount applied for. Exactly half of the respondents believe the terms were better than the otherwise market terms (45% see them as being no different and only one respondent as being worse).

In the case of Armenia, nearly half of respondents needed the funds for business expansion, but as the chart below illustrates, also for variety of other purposes, with none using the loan dominantly for working capital.

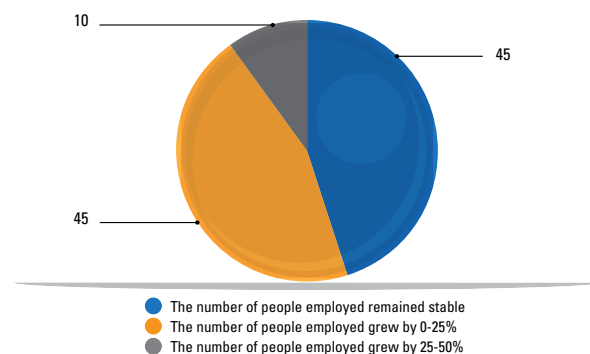
Figure 5.1: Loan purposes, in %



Source: EU4Business database

However, as a result of this expansion, the majority of the companies increased the size of their workforce. Interestingly, the majority of respondents acknowledged that women represented up to 50% of the new employees, whereas one company said that all new staff were women. The loan has played a very important or crucial role in increasing employment for 53% of those who hired, while for the others it was less critical or not at all important in generating jobs.

Figure 5.2: Impact of loan on employment, in %



Source: EU4Business database

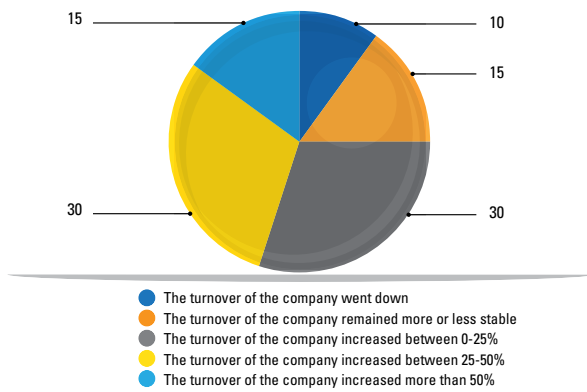
Only 20% of all SMEs in the survey export abroad, mostly to Russia (83%; others to the EU), but all of them export less than 25% of their total output. Also, most of them saw their export levels unchanged since they engaged with EU4Business, though one firm actually increased exports by up to a quarter as a direct result of the financial package from EU4Business.

⁹ A total of 130 SMEs were surveyed in five countries of EaP (Armenia, Belarus, Georgia, Moldova, Ukraine): 30 companies in the three countries with the DCFTA status and 20 in the other two. Initially, the key implementers provided twice as many SMEs, from which firms were contacted until the target number of interviews has been completed. The firms were chosen randomly, but a precondition was that they had taken an EU4Business financed loan at least one year before the beneficiaries' lists were prepared. In the countries where different projects were being run, the SMEs approached were from a proportional mix of such projects (provided via EBRD, EIB and KfW).

This is why the majority of the surveyed exporters indeed do see the loan as important for an increase in exports but interplaying with other market factors. When asked about the factors limiting their exports into the EU, they mostly cite unawareness and lack of knowledge of the procedures and standards, but also who their potential trading partners are, while a minority are bothered by the export/customs procedures.

The majority of the companies saw their turnover increase by up to 50% as a result of the loan, and 15% of them even more than that, although a quarter saw no change or even a reduction since the loan was taken. 47% of respondents said that the loan was crucial to increasing turnover, 42% important to a point, and only two companies found that the loan did not affect their turnover.

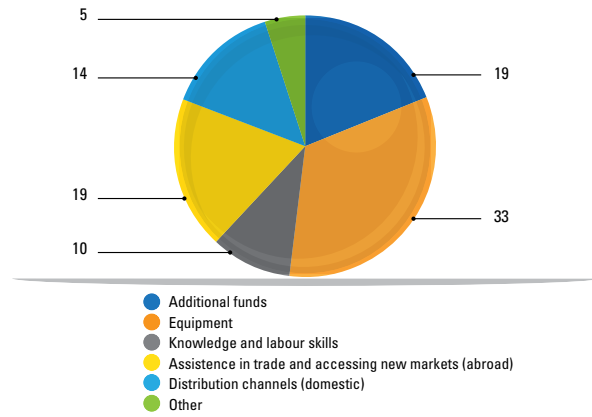
Figure 5.3: Impact of loan on turnover, in %



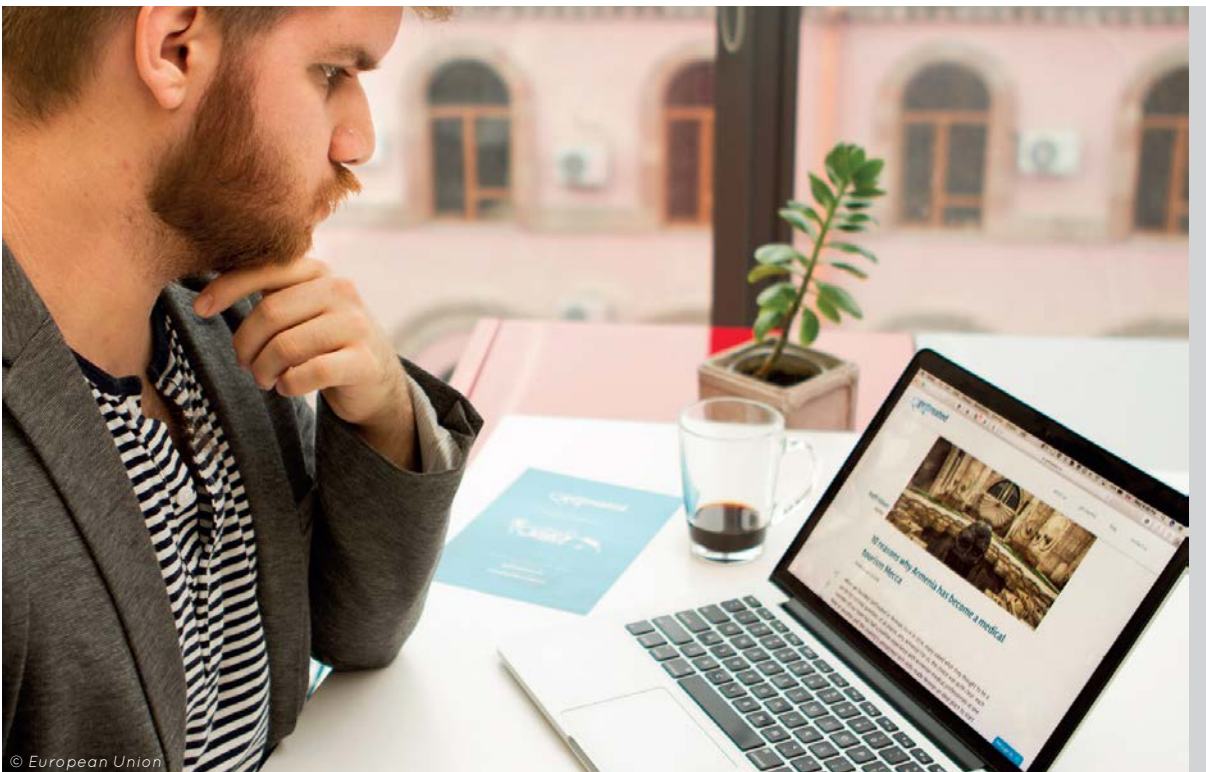
Source: EU4Business database

If they borrow again, it would mostly be aimed at more equipment but also investment in technologies and knowledge generally. For that they are looking to turn to the commercial banks or non-bank institutions where they are seeking loans under favourable conditions, primarily meaning lower interest rates than presently available.

Figure 5.4: Company's current needs, in %



Source: EU4Business database



Highlights of the round table discussion

The round table held in Yerevan on 30 March 2018 resulted in a dynamic discussion, during which 36 EU4Business stakeholders present in Armenia highlighted important achievements of the EU4Business initiative. The participants jointly concluded that the funding, support and training provided to SMEs in the framework of the EU4Business programmes, have had a significant impact on the further development and growth of the SMEs in Armenia. A number of key points have been identified for a possible follow-up as a way to further strengthen the impact of EU4Business. They follow the logic of the four pillars of EU4Business¹⁰.

6.1 Access to finance

- Main problems in access to finance are actually related to weak business management skills, lack of transparency or low corporate governance standards;
- Simply providing non-blended grants to SMEs, might create market distortions and is not desirable in the medium to long run, and may demotivate the creation of innovative solutions;
- Importance of equity investments as the next desired instrument was emphasized for SMEs, which often have a combined need for additional funding and management assistance. There is a need for more targeted and diversified financial instruments, e.g. equity-based financing and blending, 'business angels' investment, etc. Utilisation of blending and equity instruments aims to achieve positive incentives: reduce risk, induce transparency and good governance, add knowledge and motivate growing equity value;



- When a start-up has enough technological capabilities, but cannot receive investment because of gaps in product development, then an intervention by the financial schemes in the form of blended grants and/or subsidised support with mentorship may cover that gap. Indeed, gaps in access to finance in the following enterprise stages/sectors can be grouped as: (i) new businesses/early stage SMEs; (ii) innovative startups – need for pre-seed funding; (iii) internationalization of SMEs;
- New tools and instruments in financing, such as guarantees are required to address the needs of the market. Guarantees will help not only to provide financing, but also to cover credit risks, which will make it possible to provide loans for a longer period of time and manage or even reduce collateral requirements. These instruments can be blended;
- Engaging the diaspora network has some potential to match the available SME funds, but their trust in public sector run finance schemes has been lost. It is necessary to rebuild the trust, to engage the diaspora in the policy and legislation reform process;
- Way forward: utilisation of blending/equity instruments with the aim to achieve the right incentives (reduce risk, induce transparency and good governance, add knowledge and motivate growing equity value) would represent a shift to investment mind-set in providing financial support.

6.2 Access to knowledge and skills

- The importance of tailored technical assistance, including via coaching and mentorship, in particular for start-ups and innovative SMEs, has been highlighted in order to ensure appropriate absorption capacities and sustainable use of funding and other support. The value of ideas and incubation approach for the generation of a viable pipeline of ventures has been noted.



¹⁰ The national round tables were held in the capitals of all six EaP countries between late February and early April 2018, and engaged all the EU4Business stakeholders in each country: the EU Delegations, the IFIs involved, national counterparts – SME agencies and Ministries of Economy, commercial banks involved, business associations, key implementers and any other related party, totalling between 25 and 45 persons per round table. The discussions focused on the ongoing achievements across all four pillars of EU4Business, but the content was tailored to the priorities of each country. The discussants were specifically guided to address the forthcoming challenges anticipated and to propose solutions for the way forward.



EU4Business

ARMENIA: new horizons for fashion and design



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The sector-related education in Armenia does not provide the knowledge compatible with western standards, so there are lots of specific angles that designers still need to investigate.

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Alla Pavlova is one of several Armenian designers who joined together in a common fashion and design platform, made possible by financial support from the EU co-funded SMEDA project. Until now, young designers couldn't find professional help, guidance and education, but with EU support they have the opportunity to meet international experts and learn about the design process.

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Success stories:
Support to SME Development
in Armenia (SMEDA)

- Productivity has been highlighted as an issue for SMEs in Armenia. It was mentioned that 75,000 SMEs generate USD 1.5 billion in added value. Even though they create 30% of the jobs in Armenia, the quality of those jobs remains questionable. Ideally, SMEs should use new technologies and thus be more productive and competitive in external markets. Mechanisms and institutions should be created to train companies how to procure and use new technologies without incurring unnecessary costs. Productivity per employee should grow and the high-tech end of the market might even lower their current employment levels, outsourcing certain services to become more competitive;
 - Regional SMEs are more inclined to transfer their operation to larger cities, mainly the capital. Therefore, a balanced programmatic effort should be made to reach out, engage with and motivate SMEs in the regions to work and continue their growth at their present location, thus boosting the economy of their regions;
 - Many SMEs are insufficiently aware of all the challenges along the life cycle and need an individual support approach. This is particularly true with the start-ups that do not often know how to spend the borrowed funds in an economically sound way and get a better outcome from the assistance received, including entrepreneurial development. There is a clear need for more advisory projects, which include coaching and mentorship, on-the-job training and learning by doing, rather than collective mass education on general topics;
 - The importance of generating more synergies between EU4Business and the EU's COSME initiatives to make both more effective and to create new opportunities was highlighted;
 - Monitoring and measuring effectiveness of trainings for SMEs is critical to be able to assess the overall impact and outcome of the trainings, as well as their benefits for the SMEs in programming further support;
 - Communication and outreach for the various EU4Business programmes need to be improved, particularly in the regions. SMEs often do not know or do not understand the range of support available to them and their eligibility.
- Cluster strategies need a solid framework that includes definitions of clusters, target groups, leaders, management and support. Each group of SMEs faces different market development and challenges, and therefore needs a different type of support.

6.4 Regulatory reforms



- The government's commitment to continue improving conditions for SMEs and resolve issues that SMEs may be facing was highlighted. Solving the problem of the shadow economy and ending the patronage of selected businesses will lead to the improvement of the business and investment climate in Armenia.
- Advocating the best interest of SMEs excludes a top-down approach. The involvement of SME and Business Support Organisations (BSOs) should be encouraged and consultations regularly organised so as better to understand the requirements and priorities of SMEs in Armenia;
- One of the key challenges for the development of the equity market is the shadow economy, but also absence of corporate governance and a financial reporting system in Armenia (noted was the progress of the World Bank's STAREP project to adopt and promote such related regulation). To overcome these issues, it is important to develop capacities, upgrade management systems to make companies capable of absorbing new methods of company reporting and thus management, use new tools of financing, and upgrade their understanding of market behaviour.

Participants of the round table concluded that some continuation of this very first such gathering of all the stakeholders involved in the EU4Business is highly desirable.

6.3 Access to markets

- Support to exporting SMEs in the internationalisation stage is deemed largely insufficient;
- The quantity and quality of people in the innovation and tech sphere is far from sufficient to penetrate new markets. There are 10,000 marketable engineers in Armenia, while about 50,000 are needed to have a scalable ecosystem in Armenia. To become commercially visible, these skills and linkages should be developed;





THIS PROJECT IS FUNDED BY THE EUROPEAN UNION

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