

Lessons to be learnt while addressing COVID-19 crisis



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We are shaping the future. While protecting ourselves from the economic shocks resulting from the spread of the coronavirus, or any other calamity, we are still shaping our future. Everything is in our hands. Armenia has been through the financial crisis of 2008-2009, another one in 2014-2015, and is currently facing a new blow, which we are yet to address. The financial-economic formula of addressing a crisis is the same: to solve a current problem at the expense of the future. The government has already announced about the social and economic support. However, there are looming questions: which is the source of this support and who will carry the burden in the future?

The economy has stopped, specifically the sectors that directly relate to human interaction and mobility, including service industry, transport and tourism. Such a crisis strikes in two directions and does so simultaneously. On one hand, the demand decreases: specific sectors stop their activities and there is no turnover. On the other hand, the investments cease. This chain reaction affects inter-related sectors: the businesses that have taken loans face the risk of inability to return those; jobs are reduced; and all these result in a further decrease of the demand. The overall demand and supply decrease. The already announced 'credit vacation' will curb the negative chain described above, to some extent, of course.

Lessons learnt from the 2008 crisis

The key lesson learnt from the 2008 crisis is one: we did not learn any lessons. Certainly, the current crisis differs from the previous one in regards to its content. The Armenian Dram is overvalued; reserves are large; there is financial stability; and there is no panic. All agree that it is crucial for the economy to be liquid: the money needs to 'work'. But how shall this be achieved?

The credit of USD500 million from Russia in 2008 was intended for injecting liquidity to the economy, mostly in the form of investments. However, the effectiveness of this measure is still unclear. The burden was shifted to the future. We solved the problem of a given moment at the expense of the future. Shall we repeat the same? What should be the sources of state support to the economy?

Here is a brief overview of the lessons not learnt:

- "Irrevocably loner" owners: Today many business people and owners look up to the state for support; they plead the banks for 'credit vacations', as they feel the impact of the crisis. However, when it comes to the principles of governance, transparency and legal activity, they rely only on themselves. They are reluctant to access stock exchange, to securitize and to follow the principles of corporate governance.

In 2008, the government provided numerous credits to large and medium businesses, in order for the latter to meet their credit responsibilities, to invest and to develop. During any crisis, when there is a capital market, and when businesses are capitalized, the market mechanisms provide a more effective inventory to the government and the central bank for effective intervention and support to the market. The Armenian market never capitalized.

- Recommendation: After the current crisis some large businesses will again apply for support. They will present business plans, and will start negotiating. Moreover, the strongest and simplest argument at their end will be: "We'll provide new jobs", or "We're all in the same boat". However, unlike in the previous times, the government should include a requirement for mandatory application of corporate governance in the future, and for capitalization of the business, in its support packages to the large



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businesses. Had it been required in the aftermath of previous crises, we would have been better off addressing the current crisis, as well as we would have had a larger inventory to do so.

- People outside the social support system: These are the people who work. They are the backbone of the economy. They are the meaning and goal of the economy. We have a group of working people who do not pay taxes. By not paying taxes they are able to resolve their social issues. They are able not to migrate. Conditionally, we can pardon their behavior, because thus they facilitate the state's burden. However, to provide social support to this group today is tricky: they cannot provide a statement from an employer about their income, and the potential losses and damages are not clear. For instance, reduced tourism will hit the taxi drivers quite hard, but they cannot provide a document proving the extent of their losses.

- Recommendation: Certainly people need social support, regardless of whether they are engaged in the formal or non-formal sector. Some countries have already had similar experiences by providing specific sums to their citizens. However, it is crucial to communicate to the people the importance of being a part of the social support system. If people feel neglected, they should remember that they were the ones who decided to hide.

You should be part of the social support system of the state, including healthcare, benefits and pensions, in order to be able to later claim such support. It should be unacceptable to continue to hide, when participation is due and to appear when support is provided.

In a crisis like this, support should be provided to all. However, it is important to communicate that the people, who prefer to hide, need to come out and be part of the system. The government in its turn should be able to design both the overall inventory of participation and of the social support. People need to understand what it means to be protected by the state.

- Financial source: The annual budget deficit for 2020 is AMD161 billion. The domestic debt will increase by AMD211 billion, and the external will decrease by AMD50 billion. The announced AMD150 billion for support is not a small burden for the budget of Armenia. External financing will increase the pressure on exchange rate. On one hand, it will solve the problem of the money source, and on the other, it will weaken economic competitiveness.

The theoretical solution is simple: 'consolidation' of internal savings. The financial system of Armenia has matured to the point where we have people with large savings, and the economy does not include only people with debts. Where will the people in the first group direct their savings? It is in this regard that the fiscal and monetary decision-makers design various financial interventions. Long-term debts are substituted by short-term debts; liquidity is enlarged; interest rates are reduced. The Central Bank has already reduced the interest rate. The first step is done, and the question is: "What's next?" This is a case when there is both deficit and surplus of money, and the real question is the distribution and preference. Economies withstand crises more easily when financial shocks do not change the currency preferences, something that we witnessed in crises of both 2009 and 2015. Today, on one hand, we should not allow such a scenario, and on the other, there are more opportunities for us to prevent such a scenario. The only question is: why should people trust that in case they direct their savings to the government's program to overcome the crisis through enlarging the deficit, these sums would be the best support to the Armenian economy (and will not transform into a source of inflation or new pressures of foreign currency instead)?

- Recommendation: Interventions to overcome the crisis should be clear, transparent and targeted; should meet the two principles mentioned above; should create important infrastructures and should not become an additional cheap speculative source of money for people. Today, one of the important questions has already been addressed: people are certain that corruption will not mar the use of these financial resources. The other significant detail is the targeted use, professionalism and real

positive impact. Indeed, during a crisis the nation becomes united, everybody wants to help everybody else. Moreover, consolidation based on patriotism can and does play a significant role. However, trust should be cemented with real actions, and people have to see results.

There may be various solutions. What is scarce is the time. It is of utmost importance that the solutions, aka short-term actions, be planned with strategic development goals in mind. Currently, an investment fund can be opened, and a requirement can be imposed on those getting investments that part of their shares should be passed on to the fund, which will be put for sale in the market after the crisis. If today is not the right time to transit to corporate governance, such a requirement can be ensured for the future, for instance, in the form of a prerequisite or a negotiated agreement. And yes, the 'notorious production site infected with coronavirus' should turn into a corporation if it expects any support. However, both in case of businesses and individuals, the mentioned solutions, increase of the demand to participate in the domestic debt market, and the unanimous efforts to overcome the crisis should be ensured through a mutual agreement. This is the moment when realization is more important than coercion. The mandatory requirement included in the support package should be simply a formal confirmation of a consciously made agreement to change behavior and attitude.

The fate of the investment fund can be unique. When the crisis is overcome, the market is stable and the fund will have got rid of the shares in a sale, it can turn into the initial provider of the capital necessary for the future health insurance system. Eventually, it is exactly at the time of this crisis that people realized the significance of health insurance. This can become the most important starting point for shaping a universal agreement.

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