CONTEMPORARY ISSUES RELATED TO THE THEORY AND PRACTICE OF PUBLIC DEBT MANAGEMENT IN ARMENIA

Tatul Manaseryan
PhD, Doctor of Science in Economics, YSU Professor

Key words: public debt, foreign debt, public debt management, financial security, borrowings

Introduction

The basis for increasing the efficiency of public debt management in Armenia should be scientific arguments about the real reasons for the formation of public debt and its most preferable sources. Therefore, it is necessary to clarify the principles that will help to choose the sources of debt, which, in turn, will allow to make its management more flexible and optimal in the future. In the case of the Republic of Armenia, there is an obvious need to apply the principle of ensuring the diversity of sources of public debt.

Methodology

This study is based on principal approaches and methods developed by the government, local and international structures such as the IMF, the World Bank group, Basel Committee, etc. Economic and financial indicators, including public debt to GDP, as well as foreign depbt to GDP ratios for recent years are analyzed and assessed. This research considers the fact that the public external borrowings constitute the country's external public debt. In general, the public debt of the republic can exist in the following main forms:

• in favor of the specified creditors, credit agreements and contracts signed on behalf of the state with foreign states and international financial organizations,
• government securities issued on behalf of the Republic of Armenia,
• agreements on the provision of state guarantees to the country, guarantees of the state to ensure the fulfillment of obligations to third parties,
• restructuring of third-party debt at the expense based on the adoption of relevant laws,
• extension of the terms of debt agreements and contracts signed on behalf of the state in previous years, including international ones, and debt restructuring.

Literature review

While some experts focus on the impact of public debt profile on economic growth [Aiyedogbon et al., 2022, 19-22], others concentrate on macroeconomic implications and policy challenges, as well as on investment management and financial Innovations [Bogdan, 2021, 151-164]. At the same time, macroeconomic challenges include such issues as money supply, CPI and other related indicators. These issues are frequently discussed on various global platforms and academic circles [Chi, 2023, 94-104]. Also, boundedness and nonlinearities in state debt dynamics and management are essential [Gnegne & Jawadi, 2013] for careful TAR assessment in economic modelling. On the other hand, some experts pay keen attention on certain determinants of debt limits in local governments [Galiński, 2015, 376-382], based on international experience [Gentle, 2021], and post crisis developments [Kaya, 2023, 12-17] and previous trends [Klein, 1994, 245].

Analysis

As the government debt is formed from its obligations to both residents and non-residents, a clear distinction is made between domestic and external public debts. Armenia's external public liabilities consist of loans and borrowings from external sources, which form the country's financial obligations as a borrower of financial resources (or, like other countries, as a guarantor of loan repayment). The amount of debt should include only the amount of officially recognized direct financial liabilities of the state government sector, the servicing of which is carried out through the payment of interest or repayment of the principal amount. Guarantees for the repayment of other debts, as well as other contingent liabilities, are not taken into account until the state bodies begin payments on possible debt repayment. Contingent liabilities of state insurance programs or the Social Security Fund with a clear repayment term are also excluded from the total amount of officially recognized direct debt. Unpaid Current debt on liabilities is also excluded from the amount of debt until such time as these liabilities are recognized and take the form of debt obligations with clear deadlines. However, current debt should not be included in the total amount of debt, but should be shown as a separate line in the balance sheet. In particular, non-payment of salaries to civil servants, unlike buyers of government bonds (who have the right to choose), cannot be considered as voluntary lending by state bodies. The share of external net borrowed funds in the public debt of the Armenia is almost the half of the public debt.

The Armenian government plans to collect 2 trillion 873 billion drams in taxes, duties and other revenues in 2025, spend 3 trillion 482 billion drams, and since state budget expenditures exceed revenues, a deficit of 609 billion drams will arise in the budget[1]. And although there is a tendency to increase the share of domestic debt in the structure of public debt with the issuance of Eurobonds, nevertheless, according to our forecasts, no radical changes will be recorded in the structure of public debt in the coming years[2]. This principle, in turn, has led to a threat to financial security, dependence on external sources. In other words, it is necessary to maintain the principle of maximum reduction of dependence on external sources. Compared to the first years of independence, when the country's main lenders were the World Bank and the IMF, currently the EBRD, the ADB, other international and regional financial institutions and foreign governments are also among Armenia's lenders. This, in turn, reduces the dependence on external sources.

[1] The state budget of Armenia for 2025, https://168.am/2025/01/01/2146619.html
[2] The conversion of payments on the RA government's external debt was carried out based on the average exchange rates formed in the foreign exchange market. Source: Central Bank of the RA.

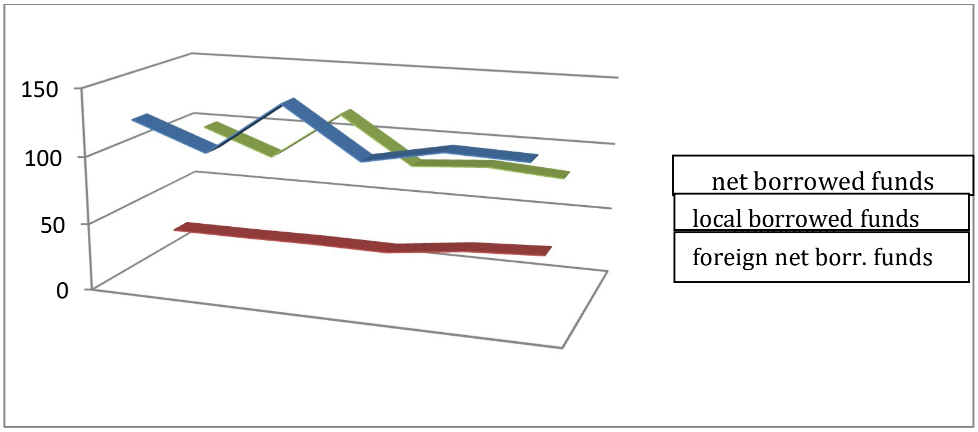

Figure 1. Financing the state budget deficit by borrowing in 2020-2025 (billion drams)

The next principle that should be observed when choosing any source is to ensure the lowest possible interest rates, a long period, in other words, the most favorable conditions. New approaches to debt portfolio management are somewhat identical to the well-known practice of managing a securities portfolio. However, if in the latter case the task is to increase their profitability, then in the case of debt portfolio management they strive to reduce costs. Moreover, to assess the effectiveness of debt management, a theoretically constructed basic model of the debt portfolio is used, subdivided by currency types, maturity dates, interest rate structure and a relatively even schedule of debt payments. Similar approaches to debt management are also used by Belgium, Portugal, and Argentina.

The selection of low-risk loans is of essential importance in the selection of debt acquisition. As a rule, floating interest rate loans are problematic and risky. Changes in the latter can lead not only to an increase in the actual volume of state debt, but also to inefficiency in their management. This means that preference should be given to fixed interest rate loans. In this regard, the risks associated with interest rates are becoming more important, especially since the share of floating interest rate loans from external sources has significantly increased in the structure of the RA government's debt. At the same time, it is important that the borrowed funds are expressed in a freely convertible currency, rather than a restricted one, which will not only facilitate their acquisition in international financial markets, but also make the debt management process expressed in them more predictable.

Table 1. Share of fixed and floating interest rate loans in the RA Government's debt structure in 2020-2025 (%)[3]

	2020	202 1	202 2	202 3	2024	2025 forecas
Government debt, including	100.0	100.	100.	100.	100.	100.0
Fixed interest rate	75.5	76.3	75.9	76.6	77.8	80.1
Floating interest rate	24.5	23.7	2	23.4	22.2	19.9
External debt of the Government, including	100.0	100. 0	100. 0	100. 0	100. 0	100.0
Fixed interest rate	71.8	72.3	7	72.0	73.1	75.6
Floating interest rate	28.2	27.7	28.4	28.0	26.9	24.4
Domestic debt of the Government, including	100.0	100. 0	100. 0	100. 0	100. 0	100.0
Fixed interest rate	96.0	97.1	98.1	98.9	99.5	100.0
Floating interest rate	4	2	1	1	0	-

Exchange rate risks are also present, since the majority of the state debt is in foreign currency, although according to the estimates obtained through stress tests, in the event of a 20% depreciation of the national currency, there will be no problems with debt servicing.

At the same time, this risk is mitigated to some extent due to the fact that the majority of the government's external debt is expressed in SDR, which represents a basket of four freely convertible currencies (USD: 41.9%, EUR: 37.4%, GBP: 11.3%, JPY: 9.4%), and is therefore less volatile.

Compared to the forecast exchange rates, a 1% deviation in the exchange rates of SDR, EUR, and JPY against the US dollar will change the external debt of the RA government by an average of USD 23.5 million. In terms of effective exchange rate risk management, it is not excluded that in the future debt managers will use different approaches common in the world. Currently, Armenia's 12 billion 842 million US dollars, of which the external public debt is 6 billion 454 million dollars.

In general, there is an interdependence between risk and profitability. The reforms currently being implemented in the financial system, in particular, the application of the principles of the Basel system, are impossible to imagine without the correct assessment of banking risks and their effective management. The important thing is not to exceed a certain level of risk, after which the dependence between risk and profitability is violated. At this time, the risk of incurring losses arises. The main problem of risk regulation is maintaining an acceptable ratio of profitability, security and solvency ratios. Risk level management solves a number of problems, starting from risk monitoring to its value assessment.

Conclusions

The above-mentioned principles are equally applicable to the formation of both external and internal public debt and its management processes. Moreover, in addition to state bonds of various maturities, separate programs of national importance can also be financed at the expense of targeted issuance and placement of state bonds.

Finally, one of the most important principles of the formation of public debt, the selection of its sources and its effective use is ensuring economic security.

The debt of government bodies is a component of the debts of the state sector of the economy The most important component of the structure and the driving force of changes in financial conditions. The state debt is the obligations of the republic in the form of state bonds, guarantees of third-party obligations, other obligations, as well as various debts assumed by various levels of the state. For Armenia, the state debt has not only economic, but also political significance.

References

1. Aiyedogbon, J. O., Zhuravka, F., Korneyev, M., Banchuk-Petrosova, O., & Kravchenko, O. (2022). Impact of public debt profile on economic growth: Evidence from Nigeria. Public and Municipal Finance, 11(1), 10-19. https://doi. org/10.21511/pmf.11(1).2022.02 Baniata,
2. Bogdan, T., & Lomakovych, V. (2021). Financialization of the global economy: Macroeconomic implications and policy challenges for Ukraine. Investment Man agement and Financial Innova tions, 18(1), 151-164. https://doi. org/10.21511/imfi.18(1).2021.13
3. Buriak, A., Lyeonov, S., & Vasylieva, T. (2015). Systemically important domestic banks: An indicator-based measurement approach. Prague Economic Papers, 24(6), 715-728. https://doi.org/10.18267/j. pep.531
4. Chi, N. T. D. (2023). Impact of money supply and macroeco nomic indicators on foreign portfolio investment: Evidence from Vietnam. Banks and Bank Systems, 18(4), 94-104. https://doi. org/10.21511/bbs.18(4).2023.09
5. Dudchenko, V. Yu. (2020). Interac tion of central bank independence and transparency: Bibliometric analysis. Business Ethics and Leadership, 4(2), 109-115. https:// doi.org/10.21272/bel.4(2).109 115.2020
6. Galiński, P. (2015). Determinants of debt limits in local govern ments: Case of Poland. Procedia – Social and Behavioral Sciences, 213, 376-382. https://doi.org/10.1016/j. sbspro.2015.11.554
7. Gentle, P. F. (2021). The USA federal debt-to-gdp ratio and the uni f ied budget act's lack of generally accepted accounting principles. SocioEconomic Challenges, 5(2), 49-57. https://doi.org/10.21272/ sec.5(2).49-57.2021
8. Gentsoudi, V. (2023). The impact of effective leadership on public sector's financial instru ments: Empirical evidence from Greece. Business Ethics and Leadership, 7(2), 47-54. https://doi. org/10.21272/bel.7(2).47-54.2023
9. Ghosh, A. R., Ostry, J. D., & Qureshi, M. S. (2015). Exchange rate management and crisis susceptibility: A reassessment. IMF Economic Review, 63, 238 276. https://doi.org/10.1057/im fer.2014.2

10. Gnegne, Y., & Jawadi, F. (2013). Boundedness and nonlinearities in state debt dynamics: A TAR as sessment. Economic Modelling, 34, 154-160. https://doi.org/10.1016/j. econmod.2013.04.006
11. Galiński, P. (2015). Determinants of debt limits in local govern ments: Case of Poland. Procedia – Social and Behavioral Sciences, 213, 376-382. https://doi.org/10.1016/j. sbspro.2015.11.554
12. Gentle, P. F. (2021). The USA fed eral debt-to-gdp ratio and the uni f ied budget act's lack of generally accepted accounting principles.
13. Kaya, H. D. (2023). The impact of the 2008–2009 global crisis on loan applications and access to finance. Financial Markets, Institu tions and Risks, 7(2), 12-17. https:// doi.org/10.21272/fmir.7(2).12 17.2023 27 Public and Municipal Finance, Vol. 13, Issue 1, 2024
14. Klein, T. M. (1994). External debt management: An introduc tion (Chinese) (World Bank Technical Paper No. 245). World Bank Washington DC. Re trieved from https://documents. worldbank.org/en/publication/ documents-reports/document detail/878191468181494972/ external-debt-management-an introduction

Tatul Manaseryan

Contemporary issues related to the theory and practice of public debt management in Armenia

Key words: public debt, foreign debt, public debt management, financial security, borrowings

It is obvious that at the current stage of socio-economic development, the state is faced with numerous problems, the solutions of which are conditioned by the availability of financial resources of the appropriate volume and quality. Therefore, it is important, first of all, to finance those programs that the country are of vital, strategic importance for the development of the economy. At the same time, it is necessary to substantiate the priorities that determine the development of the most competitive sectors of the economy with clearly developed criteria. In other words, an increase in public debt can also be justified in cases where borrowed funds are directed to the development of locomotive sectors of the economy (mainly industry), which are called upon to raise other industries and their infrastructures after them. This means that the involvement of public debt should be based on the program principle.