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PROSPECTS OF IRANIAN INVESTMENTS IN RA

ПЕРСПЕКТИВЫ ИРАНСКИХ ИНВЕСТИЦИЙ В РА

Summary. The base for Armenian-Iran economic relations was laid from the very first days of independence of the Republic of Armenia. Nevertheless, at present the Iranian investments in Armenian economy are quite small due to the small consumer market of RA. In 2015, by becoming a member of EAEU, Armenia opens wide horizons for its investors considering the huge export market of the EAEU. The aim of this article is to identify the sectors of RA economy, which will allow the Iranian investors to make more profitable investments and to enter the EAEU market. For this research is applied the comparative analysis method.

Keywords: Foreign direct investments, investment climat, comparative analysis, revealed comparative advantage, EAEU market.

Аннотация. Основа армяно-иранских экономических отношений была заложена с первых дней независимости Республики Армения. Тем не менее, в настоящее время иранские инвестиции в армянскую экономику довольно малы из-за малого потребительского рынка РА. В 2015 году, став членом ЕАЭС, Армения открывает широкие горизонты для своих инвесторов в виде возможности выхода на огромный рынок ЕАЭС. Целью

данной статьи является выявить сектора экономики РА, которые позволят иранским инвесторам сделать более выгодные инвестиции и выйти на рынок ЕАЭС. Для этого исследования применяется метод сравнительного анализа.

Ключевые слова: прямые иностранные инвестиции, инвестиционный климат, сравнительный анализ, выявленные сравнительные преимущества, рынок ЕАЭС.

1. Statement of the problem

The Armenian-Iranian economic cooperation was originated from the very first days of Armenia's independence. The Islamic Republic of Iran (here in after referred to as the IRI) was among the first which on 25 December 1991 officially recognized the independence of the Republic of Armenia (here in after referred to as RA), thereby establishing the grounds for diplomatic and economic relations [15].

In 1990 the Republic of Armenia was in an unfavorable economic condition losing their foreign markets because of collapse of USSR. But this was not the only disaster for Armenia. RA suffered losses of human resources and of production capacities because of 1988-th earthquake and 1992-th Artsakh war. In these conditions the good relationships with neighboring Iran was very important for the further development of RA.

Statistical data, however, evidence that up to now the level of the Armenian-Iranian trade and investment cooperation is not satisfactory. As of the end of September 2016, the gross flow of FDI from the IRI to RA made 0.06% [10] of gross flow of total FDI in RA as of the same period, the same indicator did not exceed 0.1% in 1995-2015 [12]. This fact, however, has a number of objective reasons. The consumer market of RA is quite small, RA and the IRI are neighboring countries, therefore, when making investments in Armenia the Iranian businessmen do not resolve the problem of entering more

distant markets. Also we can state the fact, that in the small consumer market of RA there are already goods of different countries, both imported and locally produced, thus it is not so easy for the Iranian businessmen to resist the existing competition. This situation was during until 2015, when Armenia became a member of the Eurasian Economic Union (here in after referred to as the EAEU), thus opening the doors to the EAEU multimillion market for the investors in RA. This may serve as a new incentive to the Armenian-Iranian investment cooperation.

2. Analysis of recent researches and publications

The investment climate of RA and the factors impacting on it are analyzed by many economists. In his study Frunzik Voskanyan state that corruption hurts investment: he said that corruption not only affects the budget investments but also reduces the budget revenues by tax evasion and poor tax administration, which can be disastrous for further development of Armenia [11].

Many economists and international organizations have addressed the analysis of the Armenian-Iranian economic relations. European Center for Strategic Studies and Security has presented the possible areas of the Armenian-Iranian economic cooperation, including trade, energy sector, transportation system, etc.[3]. The economist L. Petrosyan has referred to the development of the Armenian-Iranian relations in 1991-2008 [26]. H. Markosyan and A. Minasyan have focused on the comparative analysis of individual sectors of economy of RA and the IRI, as a result of which have concluded that at present there exist a lot of preconditions for Armenian-Iranian economic cooperation[4].

T. Torosyan has addressed the Armenian-Iranian trade relations, indicating key reasons for decline and growth in the Armenian-Iranian commodity circulation[8]. H. Naveh touched upon the analysis of the Armenian-Iranian trade relations, presenting the Armenian-Iranian joint business prospects, as well as analyzing the Armenian-Iranian export and import dynamics in2000-2010 [6].

The analyses by T. Torosyan and M. Afra were directed to disclosing the competitiveness of the Iranian goods in the Armenian market, which revealed that in the Armenian market the Iranian goods were consumed mainly in 1992-2002, after which their competitiveness in the market was sharply declined, driven by the import of similar and more high-quality goods from European and other countries [7].

T. Torosyan and A. Yusefi have referred to the analysis of dynamics of the Armenian-Iranian investments, indicating that these investments are not of a satisfactory character and showing those main sectors of the economy in which investments have been made by the Iranian businessmen[9].

Various Armenian and other foreign authors have addressed the analysis of the Armenian-Iranian economic relations as well.

3. Formulation purposes of article

The problems of this research are presented below:

- to explain strengths and weaknesses of Armenian investment climate for Iranian investors,
- to reveal the sectors of the economy of RA, with more profitability for Iranian investors in the context of export to the EAEU market.

4. The main material

We have analyzed the factors supporting the investment climate of Armenia and Iran, distinguishing the similarities and differences, aiming to understand whether in new economic conditions there is a prospect for significant increase in the Iranian investments in RA and what reality should the Iranian investors face up when making investments in Armenia.

First, let us refer to the similarities between investment conditions of both countries.

- Both in RA and the IRI the protection of investments is established by the law – in RA by RA Law on Foreign Investments adopted in 1994[20] and in the

IRI by the Foreign Investment Promotion and Protection Act (FIPPA) adopted in 2002[18], according to which foreign investments made in the country are guaranteed, a non-discriminatory approach is ensured for domestic and foreign investors, etc.

- According to the same laws, both in RA and the IRI the enterprises with foreign capital are not subject to nationalization or confiscation, except for the extraordinary cases stipulated by the law. In such cases, the FDI must be totally reimbursed by current prices.
- RA and the IRI from 1995 and 2003 respectively are the members of the Multilateral Investment Guarantee Agency of World Bank Group [23], which means that foreign investments made in these two countries are insured by this agency against the risks arising for non-economic reasons.
- There operate free economic zones in RA and the IRI, where the investors are provided with tax and customs privileges.

However, RA investment climate has also a number of differences in comparison to the Iranian investment climate, which need to be taken into account by the Iranian businessmen when making investments in Armenia.

Natural and geographical differences

- The IRI is rich in natural resources, whereas RA is not.

The consumer market's differences

- The domestic consumer market of the IRI is quite large, whereas RA consumer market is small, however, when making investments in Armenia it is possible to export manufactured goods to the EAEU market under privileged conditions, and businessmen making investments in Iran lack such an opportunity.
- At the same time the life expectancy at birth in IRI is a little higher than in RA since 2010[21].

- Therefore the annual growth of GDP per capita in RA is much higher, than in IRI, however the GDP per capita in RA is less, than in IRI [21].

Differences related to production factors

- The FDI inflow in RA less than in IRI.
- The minimum salary in RA is AMD 55000, in the IRI it is equivalent to about AMD 78000 [19].
- The adults' literacy level, which is prioritized as a qualitative indicator of the workforce, is 100% in RA and 84% in the IRI [13].
- The interest rate of the credits provided to the private sector by commercial banks is 16.41% in average in RA, which is higher than the same indicator in the IRI. In IRI the this indicator is 14% in average [21].
- The index of innovations of 35.14 in RA is higher than that in the IRI of 30.52 [2].

Differences related to the activities of enterprises

- In terms of ease of doing business RA is ranked the 38th in the world and the IRI the 120th [10].
- In order to register a business in RA 4 days are required and in the IRI it takes 15.5 days, moreover the start-up procedurs to register a business in RA is less, than in IRI [5].
- Enterprises operating in Armenia pay 10 types of taxes, and 20 - in the IRI [21].
- In RA the profit tax rate is 20% [20], in the IRI it is 25% and the income tax in RA is 24.4-28%, but in IRI it is 30% [22].
- What about construction permit, in RA this process takes 84 days, in IRI this takes a little long time-99 days [6].
- When carrying activities in one of the free economic zones of Iran, legal entities are exempt from profit tax and individuals from income tax for 15 years[14]. When carrying activities in RA under the same conditions, legal

entities and individuals are exempt from profit tax and income tax respectively for an indefinite period of time [16].

- A foreign investor and foreign resident can take out up to USD 10000 in cash from RA [17], and up to USD 5000 from the IRI [24]. In case of exceeding this amount, the necessary amount should be withdrawn through the banking system.
- The index of protection of minority investors in RA is much higher (53), than in IRI (165). This means that minority investors were more protected in RA [10].
- Taking into account some freedom indexes we can state that in RA almost all of them are higher, than in IRI: this is true for labour freedom, trade freedom, business freedom, corruption freedom, investment freedom, economic freedom, financial freedom index etc [21].

Differences related to the foreign trade

- The annual growth of export in RA is more higher, than in IRI[13].
- What about the cost to export and cost to import, we must state that this indicator in RA is higher, so export and import are more expensive, than in IRI [21].
- At the same time the time for export and time for import in RA is less, than in IRI [10].

Among the above differences there are such that argument in favor of making investments in the IRI, whereas some other points evidence in favor of investing in RA. Therefore, the investors of both countries considering the above stated circumstances will be able to calculate gains and losses on the investments in each country, based on which the decision on making the investments shall be reached.

It is clear, however, that investments made in various sectors of RA economy will ensure different results for the Iranian businessmen. Thus, the

question arises as to which sector can be more promising for the Iranian businessmen to make investments.

Naturally, both in RA and the IRI there are sectors of economy where the operating entities are able to ensure competitiveness in foreign markets, considering the environmental, cultural, organizational, technical and technological and other factors.

From our side, as an indicator of having advantage in the EAEU market a revealed comparative advantage indicator offered by Bela Balassa is considered [1].

Thus, based on calculations let us identify the presence or absence of a revealed comparative advantage in each sector of economy of RA and the IRI. The sectors where both countries will have a revealed comparative advantage will be considered by us as an option for creation of an efficient investment cooperation through the establishment of joint ventures. The sectors where RA will and the IRI will not have a revealed comparative advantage will be regarded as promising sectors for investment in RA by the IRI. Calculations were made based on the information of the World Bank [25] for 2010-2015. As a result we can state that the most efficient sector of RA and the IRI economy for establishment of joint ventures is the mining sector where both countries have revealed comparative advantage in exports. Moreover, in this case it will not be effective to establish a joint venture in the near border free trade zone. This is one of unique areas where it would be desirable to make cluster-based investments in the same area where the relevant ore mines are located.

In addition, in RA the effective sectors for the Iranian investments can be food industry, production of stones, plaster and cement, precious stones and metals and also base metals and items of metal origin. At the same time, in some cases production of items of metal origin can be a logical continuation of activities of an entity established in the area of extraction of the given metal ore.

5. Insights from this study and perspectives for further research in this direction

The analysis conducted shows that RA investment climate has many advantages in comparison to the IRI investment climate from the point of view of public literacy, use of innovations, ease of doing business, business evaluation period, number of taxes paid by the entities and other factors. The sectorial analysis evidences that for the Iranian businessmen the best sector for establishment of joint ventures with Armenian partners is the mining sector, and in the food industry, production of stones and glass and items of metal origin the Iranian businessmen can make profitable investments both jointly with Armenian partners and alone. The investments made by this principle will enable the Iranian businessmen to enter the EAEU market on favorable terms by making investments in Armenia.

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