

**CENTRAL BANK OF THE  
REPUBLIC OF ARMENIA**

*Approved under the Central Bank Board Resolution  
No 117A of 30.08.2019*

**Status Report on Implementation of the Monetary  
Policy Program  
(Q3, 2018 – Q2, 2019)**

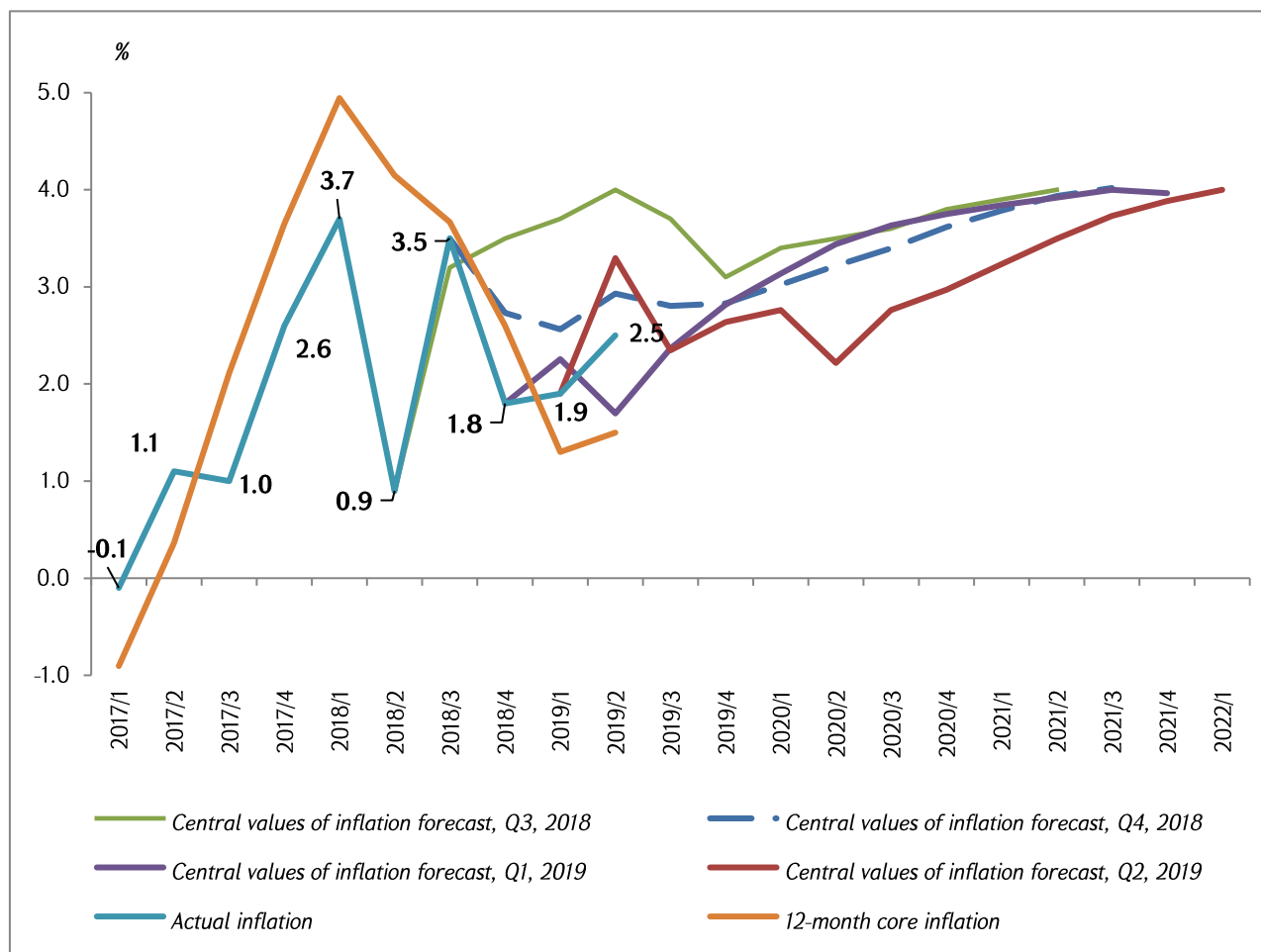
*The Central Bank of Armenia continued to pursue an expansionary monetary policy throughout the year starting from the third quarter of 2018 to the third quarter of 2019, which was mainly steered to neutralize the influence of the contractionary fiscal policy and a weak inflationary environment in the external sector on aggregate demand, hence domestic prices. However, either factor proved more contractionary than expected quarter-on-quarter, as a result of which both the 12-month headline and core inflation rates remained below the projected level, making up 2.5% and 1.5%, respectively, at the end of June 2019.*

## **1. MONETARY POLICY IN THE PERIOD UNDER REVIEW**

According to Q2, 2018 MP program, the low inflation environment would have to expand gradually over the upcoming year, which would mainly be driven by expected positive developments in the macroeconomic environment. These developments were supposed to be backed by a stimulative direction of the monetary policy and relatively high economic activity although there were already risks to declining domestic demand and inflationary environment in the external sector. According to the scenario, in view of the need to sustain the steady growth of domestic demand, the stance of the monetary policy had to be still expansionary and would only phase out gradually, in line with a recovery of inflation, while ensuring the objective of price stability.

Actual results in the period under review showed that the inflationary patterns have somewhat deviated from the projected scenario as the contractionary fiscal policy carried out that time has weakened the domestic demand; in the meantime, a slowing of global economic and demand growth rates was observable too. This has caused the 12-month core inflation to trend down to 1.5% in end-June 2019 from 4.1% in end-June 2018. On the other hand, earlier crop seasonality has brought in a severe volatility in prices of agricultural products, and the 12-month headline inflation fluctuated during that time in the range of 0.9-3.5%, as a result.

According to the Central Bank forecasts, the 12-month inflation will run below the target in the near future; it will then expand and stabilize around the target at the end of the forecast horizon



Over the past one-year period the Central Bank has pursued a stimulative monetary policy to bring the low inflation to the target level yet it has decided on a gradual recovery of inflation, since low inflation in a macroeconomic environment shaped at the time contributed to anchoring long-term inflation expectations and maintaining the purchasing power of income, according to the Central Bank estimation. Therefore, in the absence of considerable inflationary effects from external and domestic economies because of persistently weak global and domestic demand and that the monetary conditions were estimated rather expansionary, the Central Bank left the interest rate unchanged in the second half of 2018. Continued slowdown in global economic growth rates and expected weakening of the inflation environment in the world’s commodities market urged the Central Bank to somehow increase, in January 2019, the monetary stimulus and cut the refinancing rate by 0.25 pp to 5.75%; in the period February-June, it has left the interest rate unchanged, estimating the extent of stimulus sufficient on the brink of implementing an expansionary fiscal policy. At the same time, the Central Bank has signaled the financial market that in view of predictable macroeconomic developments, the monetary conditions have to be kept expansionary for as long as required, in fulfillment of the mid-term inflation target.

## 2. INFLATION IN THE PERIOD UNDER REVIEW

In a one-year horizon from Q3, 2018 to Q3, 2019, the 12-month inflation has persisted low, amounting to 2.5% y/y as of June 2019, mainly driven by a 16.9% y/y increase in prices of seasonal food products. In the meantime, the 12-month core inflation rate has reached 1.5%, whereas regulated service tariffs remained virtually unchanged over the past year.

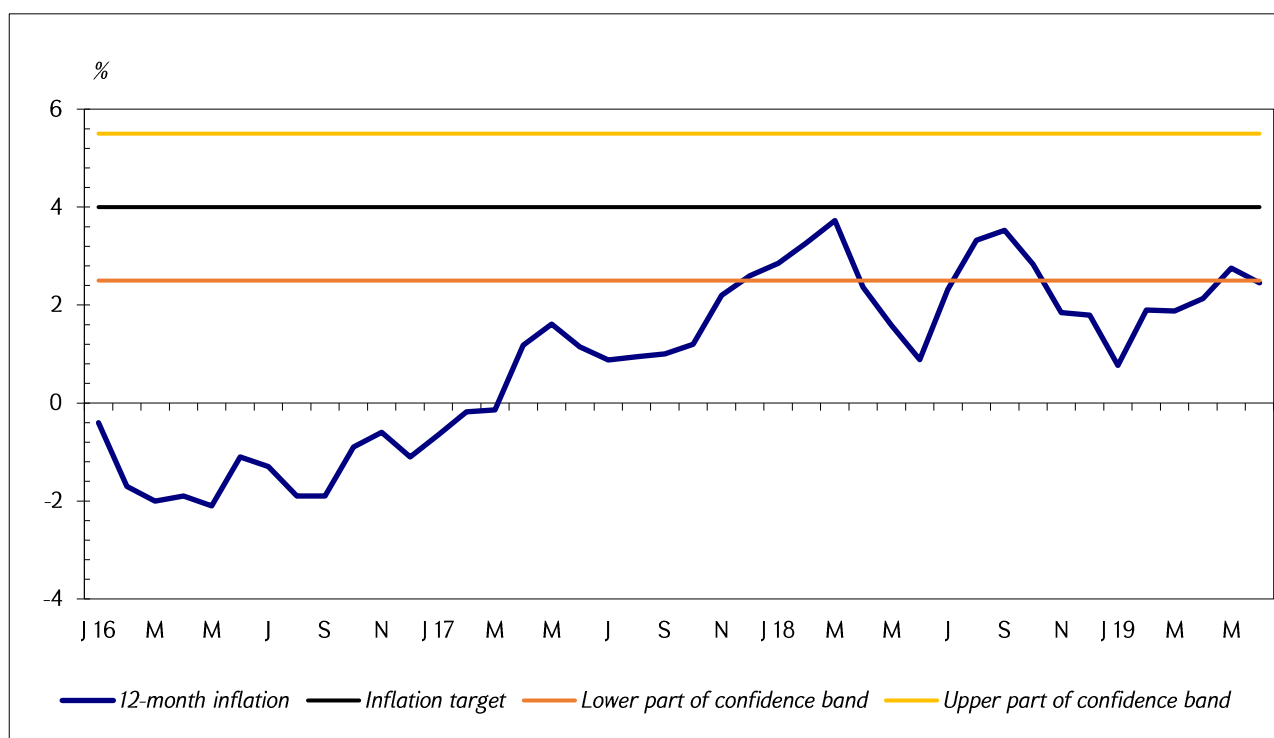
The y/y increase in seasonal food prices owed to a price rise in groups “Fruit”, “Vegetable and potatoe”, and “Egg” by 8.6%, 19.1% and 37.6%, respectively (combined contribution to the y/y inflation: about 1.8 pp).

The y/y increase of core inflation has been primarily driven by a price rise in groups “Bread products and grains”, “Meat”, “Tobacco products” as well as non-food groups “Clothes”, “Footwear”, and “Fuel” by 4.5%, 3.1%, 6.3%, 4.3%, 6.8% and 4.1%, respectively (combined contribution to the y/y core inflation: about 1.6 pp). At the same time, the falling of prices of dairy products, oils and fats, and sugar in the international markets have triggered a deflation of prices of the same products in the domestic market, by 2.1%, 3.1% and 8.4%, respectively.

In the last one-year period, inflation has been largely in line with demand developments, although somehow affected by the supply of individual commodity items. Particularly, caused by supply factors in the third quarter of 2018, the price of beef has grown (due to a reduced livestock) and the price of flour and bread began increasing starting from the fourth quarter (driven by international developments), with a combined inflationary effect estimated to have reached 0.4 pp). Note that the actual impact of change in customs duty on certain products made an estimated 0.3 pp contribution to inflation in the first quarter of 2019, mainly due to the increase in poultry prices.

**Chart 2**

***In the last one-year horizon the inflation environment has persisted low and the 12-month inflation rate fluctuated at the lower part of the confidence band***



*Growth of consumer prices by commodity group as key contributors<sup>1</sup>*

	Weights	June 2019 (y/y)		Q2, 2019 (q/q)	
		Growth	Contribution	Growth	Contribution
<b>Core inflation</b>	<b>72.7</b>	<b>1.5</b>	<b>1.1</b>	<b>0.2</b>	<b>0.16</b>
Bread products and grains	8.99	4.50	0.40	0.2	0.02
Meat	9.87	3.11	0.31	-1.5	-0.15
Dairy products	4.36	-2.12	-0.09	-1.2	-0.05
Oils and fats	2.77	-3.08	-0.09	-1.9	-0.05
Sugar	0.60	-8.43	-0.05	0.6	0.0
<b>Alcoholic beverage, tobacco products</b>	<b>4.54</b>	<b>4.0</b>	<b>0.18</b>	<b>2.2</b>	<b>0.10</b>
Tobacco products	1.8	6.33	0.11	2.9	0.05
Clothes	2.58	4.30	0.11	-1.4	-0.03
Footwear	1.52	6.85	0.10	4.8	0.07
Fuel	5.20	4.08	0.21	4.8	0.25
<b>Seasonal products</b>	<b>10.5</b>	<b>16.9</b>	<b>1.8</b>	<b>-20.1</b>	<b>-2.12</b>
Egg	1.44	37.51	0.54	-1.7	-0.02
Fruit	3.35	8.65	0.29	5.0	0.17
Vegetable	5.74	19.05	1.09	-35.0	-2.01
<b>Regulated services</b>	<b>16.7</b>	<b>-0.1</b>	<b>0.0</b>	<b>0</b>	<b>0</b>
Housing services, water, electricity, gas and other types of fuel	14.30	-0.10	-0.01	0	-0.01
Regulated transport services	2.22	0.24	0.01	0.1	0

<sup>1</sup> The Central Bank has calculated y/y data on structural elements of food products using information provided by Statistics Committee of the Republic of Armenia.