

**CENTRAL BANK OF  
THE REPUBLIC OF ARMENIA**

*Approved under the Central Bank Board  
Resolution No 85A, dated  
May 31, 2022*

**STATUS REPORT ON IMPLEMENTATION OF THE  
MONETARY POLICY PROGRAM  
(Q 2, 2021 – Q 1, 2022)**

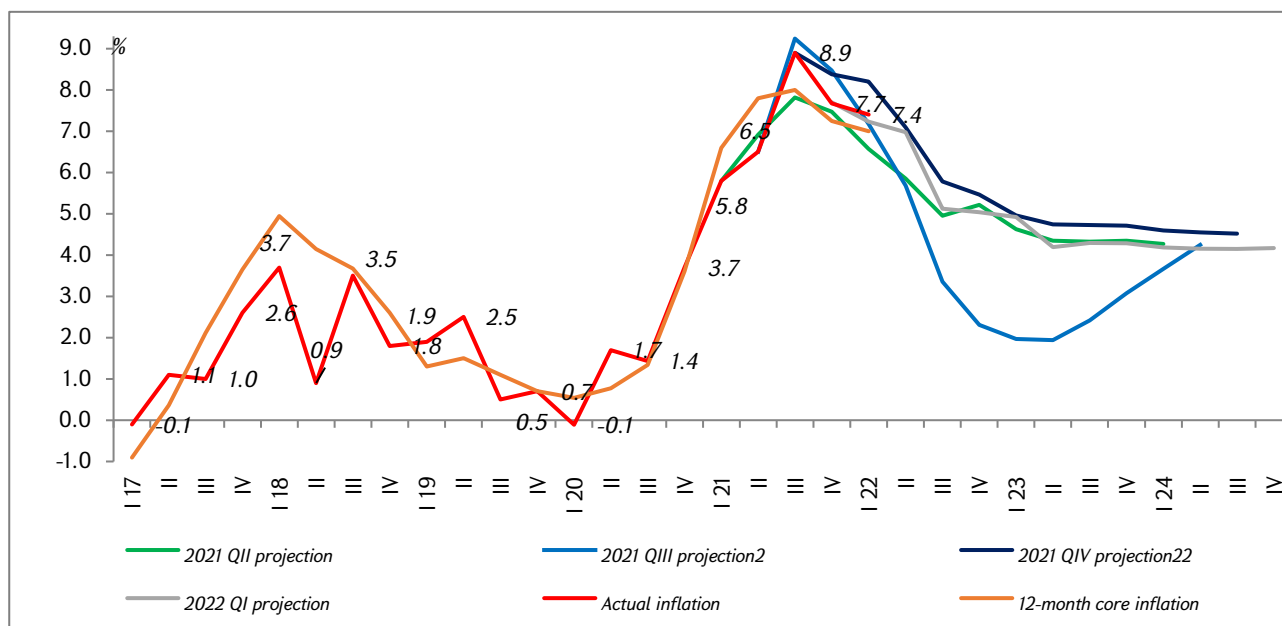
*In the period from the 2nd quarter of 2021 to the 1st quarter of 2022, a high inflationary environment persisted in Armenia. With the widespread use of coronavirus vaccines world-wide, the impact of the pandemic on the global economy has been significantly mitigated. As a result, economic activity and aggregate demand recovered faster than expected during the reporting period. At the same time, with the growth of demand, external inflationary environment has significantly expanded because of the disruption of value chains. Another negative factor that emerged in the first quarter of 2022, was the escalation of the Russian-Ukrainian conflict and the imposition of severe sanctions on Russia since the end of February, leading to unprecedented uncertainties in international commodity markets. Amid this situation, a significant impact of inflation has been transferred to the prices of the RA commodity market through a number of imported goods, which in turn was reflected in the surge of inflation expectations and risks. Given the existing situation and pursuant to the goal of ensuring price stability, during the reporting period the Central Bank continued to pursue a policy of neutralizing monetary expansionary stance, gradually raising policy interest rate. Thus, during the reporting year, policy interest rate was raised by a total of 3.75 percentage points and set at 9.25% in March 2022. Subsequently, in the context of external inflation, expansion of the domestic inflationary environment has slowed down. 12-month inflation in March 2022 was 7.4% against 5.8% inflation at the beginning of the reporting period in March 2021. The Central Bank expects that in the medium-term 3-year horizon inflation rate will gradually subdue and stabilize around the target of 4%.*

## 1. MONETARY POLICY IN THE PERIOD UNDER REVIEW

The program for the beginning of the period, i.e. the second quarter of 2021, outlined the main assumptions of monetary policy scenario according to which, the trends of economic activity observed at the beginning of the year and faster recovery of aggregates demand would continue in the coming quarters.

During the reporting period, macroeconomic developments both in global and the Armenian economy terms, surpassed the expectations. In parallel, due to the rapid growth of demand and a number of supply factors, inflationary environment expanded as well. Hence, inflation in each subsequent quarter exceeded the expected level, in view of which, the projected short-term inflation trajectory to reach the target in each subsequent quarter of the reporting year was adjusted upwards.

**12-month short-term inflation forecasts for the period of 2021 QII - 2022 QI, were periodically revised upwards**



Thus, in the second quarter of 2021, amid the widespread coronavirus vaccination, a faster recovery of global economic activity and external demand was observed. Against the background of positive developments in demand, under the influence of a number of supply factors (forecasts of low supply of new crops, increase in freight costs, value chain disruptions) significant inflationary developments were observed in the international commodity markets. This, in turn, was reflected in a high inflationary environment in the main partner countries of the Republic of Armenia, as a result of which inflationary pressures were transmitted to the economy of the Republic of Armenia through a number of imported food products. At the same time, beginning from the second quarter, inflation was further driven by domestic demand factors conditioned by the outpacing growth of private consumption over the output capacity expansion opportunities. The latter was

mainly due to the sharp increase in household consumption expenditures at the expense of the accumulated savings, as well as the large inflow of remittances from abroad.

Amid the inflationary developments described above, in the first half of the year, the Central Bank continued to pursue a policy of tightening monetary conditions, gradually reducing and neutralizing the expansionary monetary stance. Thus, in 2021 QII, the Central Bank raised its policy rate by 1.0 percentage points.

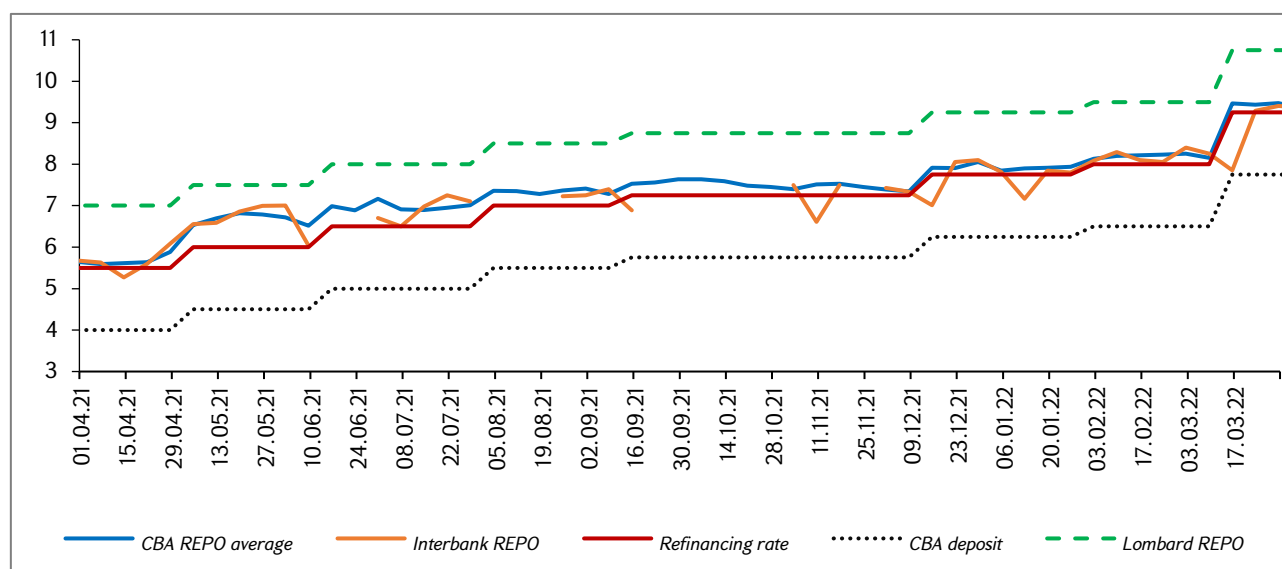
Changes in domestic prices in the second half of 2021 were mainly affected by external demand factors in the domestic services sector, due to higher-than-expected tourism growth. At the same time, uncertainties over the economic and geopolitical outlook in QIII have been reflected by rising inflation expectations. In such circumstances, the Central Bank raised the refinancing rate by a large step of 0.75 percentage points in the third quarter as well.

Despite the slight decline of 12-month inflation rates in the fourth quarter, inflation factors persisted under inflationary spill-over effects from the external sector (persisting high energy prices and disruptions in value chains) and persisting positive demand environment. At the same time, the impact of current inflation factors and expected changes in the prices of regulated services in the fourth quarter was reflected in the public inflation expectations. In view of these developments, the Central Bank raised the refinancing rate additionally by 0.5 percentage points in the fourth quarter.

In the first quarter of 2022, macroeconomic environment and especially inflationary developments in Armenia were greatly affected by the Russian-Ukrainian conflict escalating since the end of February, numerous sanctions imposed on the Russian economy and the resulting unprecedented uncertainties. The latter were reflected in a significant slowdown of the economic growth rates in the main partner countries of Armenia, as well as outstandingly high inflation in international energy and food markets as a result of value chain disruptions. In the short run, these developments transferred the negative impact on the Armenian economy mainly in terms of certain weakening of economic activity, and on the domestic commodity market by formation of high prices on some imported goods. Furthermore, inflationary environment was to some extent fueled by the acceleration of internal demand due to the factor of international visitors to Armenia. As a result of the escalation of the Russian-Ukrainian conflict, at the end of the first quarter, a significant increase in the volatility of the Armenian financial market and the country's risk-premium was observed, which further contributed to the growth of inflation expectations. In view of these developments, the Central Bank raised policy rate by 1.5 percentage points in the first quarter.

In the reporting period, short-term interest rates in Armenian financial market mostly shaped around the CBA policy interest rate. It should be noted that geopolitical developments in early 2022 lead to the growing uncertainty in Armenian currency market in March, which was reflected in the AMD volatility.

### Dynamics of CBA instruments and short-term market interest rates



To sum up, policy rate in the reporting period grew by 3.75 percentage points and was set at 9.25% in March 2022.

As a result, as expected, 12-month inflation grew in the first half of the reporting period, from 5.8% in March 2021 to 9.6% in November 2021, after which it decreased under spill-over effects of previous monetary policy actions. In February 2022 it dropped to 6.5%, rising again in March to 7.4%. It is estimated, that as a result of consistent monetary policy, inflation will gradually decrease approaching the target of 4% in the medium term.

## 2. INFLATION IN THE PERIOD UNDER REVIEW

The acceleration of inflation, observed since the beginning of 2021, continued and, in line with the projections, inflation environment remained high throughout the reporting period.

The growth of inflation at the beginning of the period was generally the result of acceleration of core inflation, to which inflation of imported food and non-food products contributed strongly. The latter was affected both by prices of food products in international markets and the short-term the exchange rate depreciation in that sector. Thus, spill-over effects from international markets resulted in a sharp growth in the prices of “Bakery and Cereals”, “Meat Products”, “Oils and Fats” and “Sugar” commodity groups in the domestic economy, and the growth of international energy prices affected internal fuel prices. The sharp growth of international freight prices is also notable as it had a direct impact on inflation of imported goods (in particular, electrical appliances, clothing and footwear, as well as personal care items).

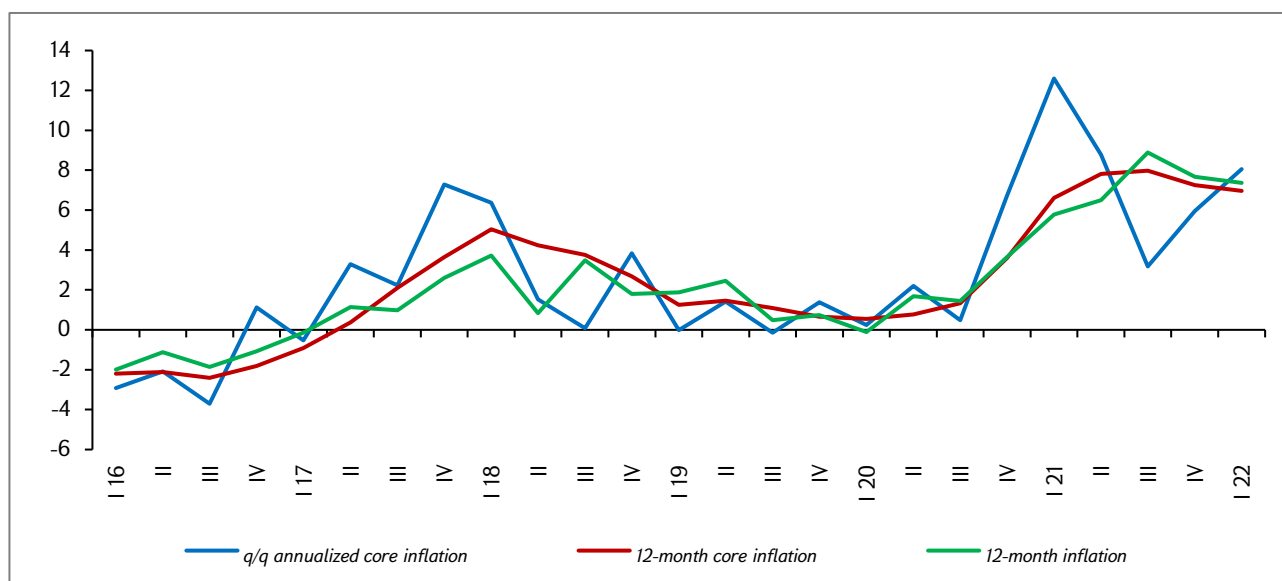
In line with the projections, by the end of 2021, price-impact effects of the above-mentioned factors have weakened. However, at the end of the first quarter of 2022, inflation accelerated sharply because of the escalation of the Russian-Ukrainian conflict, imposition of sanctions on Russia, and the resulting uncertainty. These factors caused significant inflationary pressure, particularly in terms of basic goods. At the same time, due to the factor of international visitors to Armenia, the acceleration of domestic demand has increased inflationary pressures on locally produced goods and services, under which the prices of a number of services with relative price rigidity (apartment rent, restaurants and hotels, hairdressing, financial services) have been adjusted.

Growth of prices of “Tobacco” and “Alcoholic Beverages” product groups, in line with the estimates, continued to be affected by inflationary impact of the change of excise tax rates at the beginning of the year.

In addition to the above-mentioned factors, low deflation of seasonal food products, not typical for the season, has in turn significantly contributed to the acceleration of inflation in the second and third quarters of 2021. In particular, the low deflation of vegetable prices was mainly caused by bad weather conditions, reduction of sown areas of certain products and the growth of exports. The impact of those factors persisted throughout the reporting period.

The rise of tariffs on regulated services (water supply in January and electricity in March) further contributed to the growth of inflation expectations.

***Inflationary environment persisted throughout the reporting period***



Designation	Weight	12-month inflation in March 2022	Contribution to y/y inflation
<b>Core inflation</b>	<b>75.1</b>	<b>7.0</b>	<b>5.2</b>
Bread and cereals	8.1	13.3	1.1
Meat	9.0	9.7	0.9
Oils and fats	2.6	7.8	0.2
Sugar	0.5	24.7	0.1
Alcoholic beverage	2.4	6.4	0.2
Tobacco	1.4	8.8	0.1
Clothing	1.3	6.9	0.1
Footwear	0.8	7.8	0.1
Household appliances	0.6	7.7	0.0
Medicines and health products	3.6	-0.8	0.0
Fuel	6.8	5.9	0.4
Air passenger transportation services	0.6	-11.2	-0.1
Outpatient care services	2.7	0.9	0.0
Actual rent paid by the apartment renter for additional accommodation	1.0	17.8	0.2
Restaurants and hotels	1.0	5.5	0.1
<b>Seasonal food products</b>	<b>9.4</b>	<b>16.8</b>	<b>1.6</b>
Eggs	1.3	-12.5	-0.2
Fruits	3.2	-3.8	-0.1
Vegetables	4.9	40.8	2.0
<b>Regulated services</b>	<b>15.5</b>	<b>3.6</b>	<b>0.6</b>