

## **Appendix**

*Approved By  
Board of the Central Bank of Armenia  
Decision No. 206 A dated 28.11.2023*

# **STATUS REPORT ON IMPLEMENTATION OF THE MONETARY POLICY PROGRAM (Quarter 4, 2022 – Quarter 3, 2023)**

*The inflationary environment in the Republic of Armenia has eased significantly in the time period from the fourth quarter of 2022 to the third quarter of 2023. This was primarily facilitated by the weakening of external inflationary effects, as well as the monetary policy implemented by the Central Bank of Armenia. In particular, there was a significant decrease in food and energy prices in international commodity markets from the end of 2022, mainly due to the contractionary monetary policy implemented by the central banks of leading countries.*

*Based on still high inflation expectations and the need to manage existing inflationary risks, the Central Bank of Armenia continued to pursue a policy of tightening monetary conditions in the fourth quarter of 2022, increasing the policy rate by a total of 0.75 percentage points. In the first half of 2023, taking into account significantly slowing 12-month inflation on the one hand and continuing high demand and inflation expectations on the other, the Central Bank left the policy rate unchanged until June. In the June-September period, given a rapid decline in inflation amid the transmission of deflationary effects from the external sector and some neutralization of inflationary factors in the domestic economy, the Central Bank eased monetary conditions, lowering the policy rate by a total of 1.0 percentage points.*

*As a result, due to the deflationary effects from the external sector and the contractionary monetary policy implemented by the Central Bank, both headline and core inflation decreased rapidly during the reporting period. As such, the 12-month inflation decreased by about 10 percentage points during the reporting period and reached 0.1% at the end of September 2023. Nevertheless, in the observed period, given continued high demand and inflationary expectations in the Republic of Armenia, inflation of services and some goods adjusted at a relatively slow pace.*

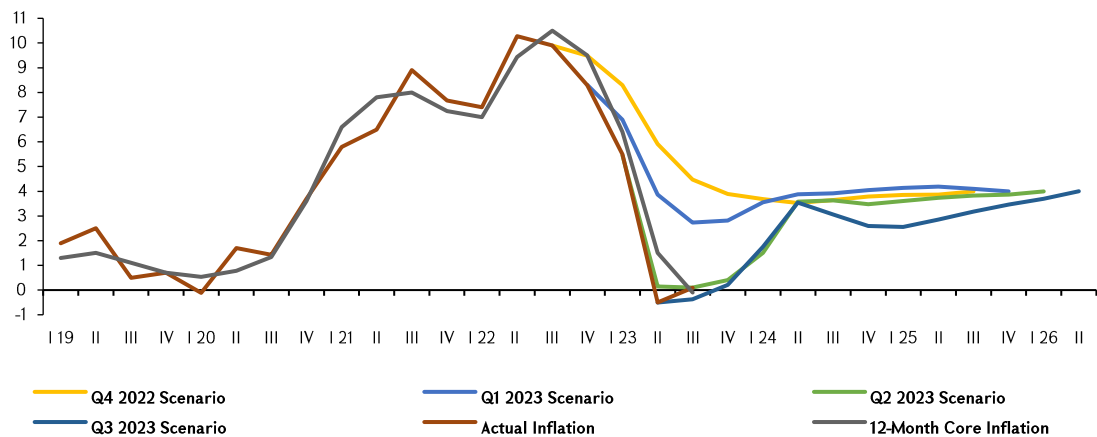
## 1. MONETARY POLICY IN THE REPORTING PERIOD

According to the main judgements of the scenario presented in the program for the fourth quarter of 2022, the high inflation environment and inflation expectations would have persisted in the near short term due to the inflationary impact from foreign markets and the high demand formed in the Armenian economy in the context of the expected large inflow of international visitors and financial resources. At the same time, it was estimated that, in the medium term, the effects of global inflationary phenomena and external demand would weaken with the continuous appreciation of the Armenian dram and, together with the impact of the contractionary monetary policy implemented by the Central Bank of Armenia, would contribute to the reduction of inflation, stabilizing it around the target 4% indicator from the second half of 2023.

In the reporting period, 12-month inflation decreased at a faster rate than expected, mainly due to the rapid and significant weakening of external inflationary effects, as well as the impact of the continued appreciation of the dram. In that situation, the projected inflation trajectory for the short-term sector was significantly adjusted downwards in the estimates for each successive quarter.

*Chart 1*

**The 12-month inflation showed a sharp decline during the period under review, based on which, the short-term estimate for each subsequent quarter was significantly revised downward.**



According to the actual macroeconomic developments of the reporting period, the pace of economic activity has continued to slow down in the global economy and in Armenia's main partner countries, mainly due to the impact of the ongoing Russia-Ukraine conflict and various sanctions imposed on Russia. At the same time, as a result of the implementation of the contractionary monetary policy aimed at overcoming high inflation from partner countries, there was a slowdown in demand and some softening of the inflationary environment, as well as a significant decrease in energy and food prices in international commodity markets. Under these conditions, the external inflationary impact

on the Armenian economy has significantly weakened. During the observed period, higher than expected activity was recorded in the Armenian economy, due mainly to demand factors. These manifested primarily in the form of a significant increase in external demand in the services sector, influenced by significant inflows of international visitors, including tourists, and financial resources. There were positive developments also in the IT and manufacturing sectors, reflected in increasing production capacity and exports in these sectors. At the same time, high demand from international visitors and a significant inflow of financial transfers from abroad resulted in a significant appreciation of the dram in the Armenian currency market. The last part of the reporting period also saw a slight recovery in domestic demand, due to increased domestic consumption in the context of rising incomes.

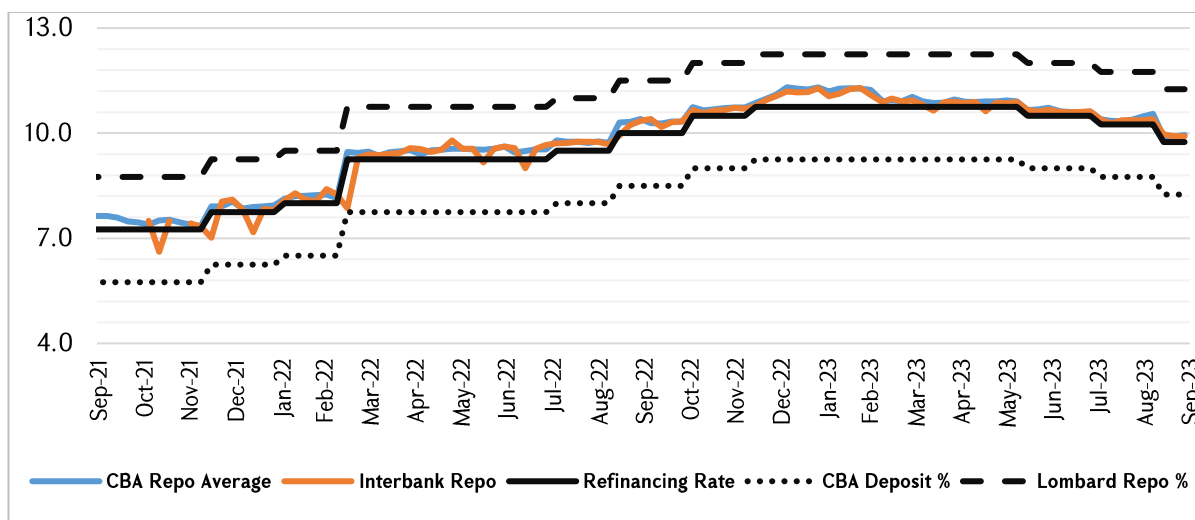
With the prospect of such developments, in the fourth quarter of 2022, despite a slight weakening of the inflationary effects on the Armenian economy from the external sector, the Central Bank continued to pursue a contractionary monetary policy, increasing the policy rate by a total of 0.75 percentage points. The contributions of continuing high demand and inflation expectations in the short term to maintaining high inflation of wages and a number of goods and services were taken into account in this consideration (see Chart 3).

In the first half of 2023, inflationary effects from the external sector weakened significantly due to the deflationary phenomena observed in terms of imported food products. At the same time, prices of goods and services with “sticky” prices have adjusted at a slow pace amid continuing high demand and inflationary impact from the labor market. Given this situation, the Central Bank left the policy rate unchanged until June, maintaining relatively tight monetary conditions.

In the June-September period, with the prospect of continued deflationary trends in both external and domestic commodity markets and a significant neutralization of inflationary factors, the Central Bank lowered the policy rate by a total of 1.0 percentage points, setting it at 9.75%.

During the reporting period, due to the continuation of the Russia-Ukraine conflict, as well as the escalation of events around Artsakh, in the conditions of increased volatility of the Armenian financial market, the Central Bank has been consistent in achieving the goal of adequate regulation of liquidity in the financial market, as a result of which market interest rates have mainly been shaped around the operational target, the policy rate. These developments were reflected in the currency market. The Central Bank responded to this through situational intervention in the market to aid the normal functioning of the financial market.

**Behavior of Central Bank Instruments and Short-Term Market Interest Rates**



In summary, it should be noted that during the year under review, as a result of contractionary monetary policy implementation, the appreciation of the dram, and the significant weakening of the inflationary impact from the external sector, 12-month inflation decreased by 9.8 percentage points, reaching 0.1% at the end of September 2023. The 12-month core inflation also decreased at a rapid pace and was in the negative range at the end of September, reaching -0.1%. It is estimated that 12-month headline inflation will remain below the target level in the near future, then gradually increase and stabilize around the target level of 4% in the medium term.

## 2. INFLATION COMPONENTS IN THE REPORTING PERIOD

In the fourth quarter of 2022, the inflationary effects from the external sector continued to weaken. At the same time, the growth of demand in the domestic economy resulted in the inflationary environment being reflected in the maintenance of high price levels for some goods and services (see Chart 3).

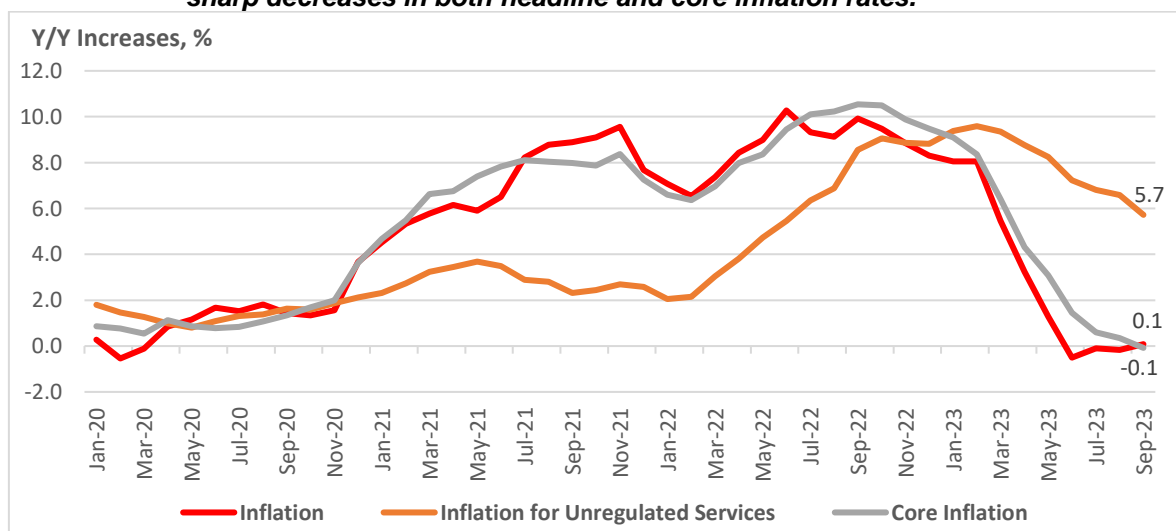
As such, inflation in global food markets, triggered by the Russia-Ukraine conflict in early 2022, particularly impacting bread products, cereals, meat products, dairy products, and oils and fats, began to ease off by the end of 2022. This was caused by the decrease in the prices of some products (sunflower oil, grains, sugar) in the international commodity markets in the context of expected weak demand in the global economy and the tightening of financial conditions. Simultaneously, the drop in energy prices toward the year's end notably influenced prices within the Armenian fuel products market. However, this impact was largely canceled out by the end of the reporting period.

It should also be noted that the strengthening of the Armenian dram, coupled with the growth of external demand, also had a significant impact on the prices of imported goods. Thus, during the reporting period, in the context of a 5.4% appreciation of the Armenian dram, the price increase for imported non-food products was restrained by 0.7 percentage points.

On the other hand, the high demand generated in the Armenian economy from the large flow of international visitors increased inflationary pressure on locally produced goods and especially on services, as a result of which tariffs for a number of services with relative price rigidity (apartment rentals, restaurants and hotels, hairdressers, medical, financial, and postal services) have been adjusted. The tariffs remained high during the reporting period and only showed a slight downward trend at the end.

Chart 3

**External inflationary effects were significantly mitigated during the reporting period, resulting in sharp decreases in both headline and core inflation rates.**



Among the components of core inflation, the increase in the prices of the Tobacco Products and Alcoholic Beverages product groups, as expected, had an inflationary effect on changes in excise tax rates at the beginning of the year, especially with regard to tobacco products. As a result of the relative decline in export volumes, milder inflation of local alcoholic beverages has somewhat restrained the inflationary manifestations in the general product group.

Apart from the mentioned factors, the inflation slowdown at the start of the reporting period was mostly due to a milder-than-expected rise in seasonal food prices. This was driven by the gradual improvement of harsh weather conditions in early 2022 and notably warmer weather in the second quarter of 2023.

The secondary inflationary effects triggered by raised tariffs on regulated services in early 2022 intensified in the latter part of the year but nearly disappeared by the end of the reporting period.

Table 1

Product Group	Weight	12-Month Inflation in September 2023	Contribution to Y/Y Inflation
<b>Core Inflation</b>	<b>73.9</b>	<b>-0.1</b>	<b>-0.1</b>
Bread Products and Cereals	8.5	-8.3	-0.7
Meat	10.6	-0.5	-0.1
Oils and Fats	2.9	-21.0	-0.6
Sugar	0.5	-8.1	0.0
Dairy Products	4.4	-0.2	0.0
Alcoholic Beverages	2.5	5.6	0.1
Tobacco Products	2	11.4	0.2
Clothing	2.2	3.0	0.1
Shoes	1.2	7.0	0.1
Household Appliances	0.6	3.7	0.0
Fuel	5.4	-2.4	-0.1
Passenger Air Travel	1.1	18.9	0.2
Outpatient Services	2.6	6.1	0.2
Actual Rent Paid by Tenant for Additional Accommodation	1.1	9.2	0.1
Restaurants and Hotels	1.9	5.3	0.1
Banking and Post Office Service Fees	0.8	13.1	0.1
<b>Imported Food Products</b>	<b>15.3</b>	<b>-7.7</b>	<b>-1.2</b>
<b>Seasonal Food Products</b>	<b>11</b>	<b>5.0</b>	<b>0.5</b>
Eggs	1.6	15.1	0.2
Fruits	4.1	-0.4	0.0
Vegetables	5.3	6.6	0.3
<b>Regulated Services</b>	<b>15.1</b>	<b>0.3</b>	<b>0.0</b>