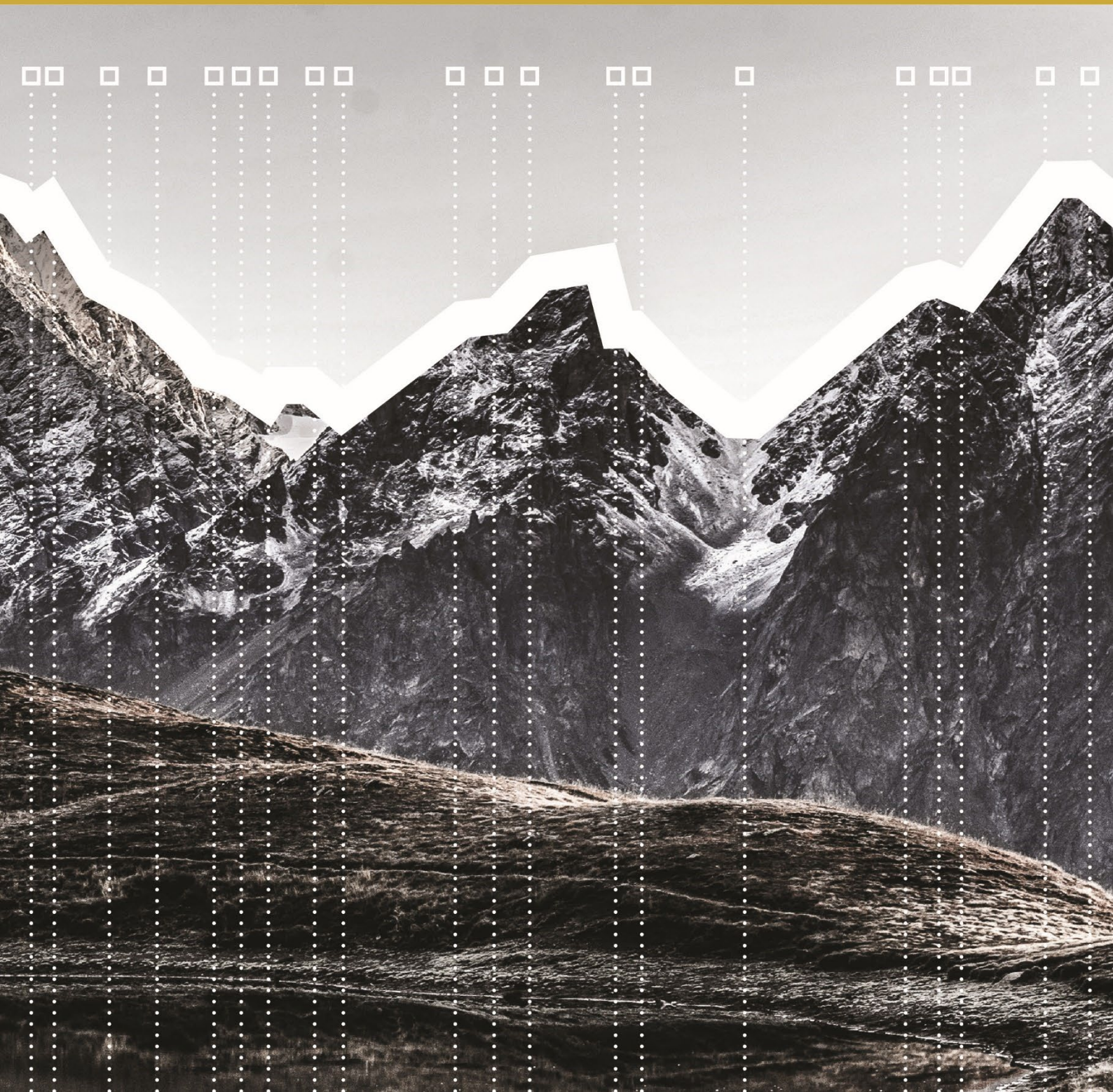




THE CENTRAL BANK OF
THE REPUBLIC OF ARMENIA

Inflation Report

2022 / 3



*Approved under the Central Bank Board
Resolution No 166A
dated 27.09.2022*

Inflation Report/3

Monetary Policy Program, Q3, 2022

✦
*Status Report on Implementation of the Monetary
Policy Program, Q2, 2022*

The inflation targeting strategy of the Central Bank of Armenia highlights the importance of communicating of the Bank to the general public by publishing, inter alia, quarterly inflation reports.

The first section of the inflation report includes the Monetary Policy Program that provides main directions of the monetary policy in the forecast horizon as well as forecasts of inflation and other macroeconomic indicators. These forecasts are based on the Bank's assessment of the current situation and future assumptions by the Bank, which also include the impact of the Bank operations.

The second section includes the Status Report on implementation of the monetary policy program of the previous year, which presents the results of monetary policy implementation and covers the actual developments in the domestic economy.

Publishing of inflation forecast and underlying assumptions in parallel to target inflation indicator makes monetary policy of the Bank more transparent, understandable and predictable, which considerably increases the public confidence in the Bank.

The Bank believes that a clear and trusted monetary policy positively affects the anchoring of inflation expectations and maintaining financial stability in terms of cost reduction.

According to the rule of monetary policy, the policy is aimed at minimizing the deviations between the 4% target and the inflation forecasts. The path to inflation rate shaped as a result of projected policy directions is published as a Projection Probability distribution chart for the 12-quarter time horizon.

Projections in this report are based on the actual information available by September 13, 2022, i.e., the day on which the refinancing rate was set, the results of survey conducted by the Bank and the judgment made pursuant to the information on future developments of the macroeconomic environment.

All inflation reports which have been published to date are available on the Bank's website (www.cba.am) which also contains all press-releases and other monetary policy-related publications.

Table of Contents

1. Executive Summary	5
2. Forecast, Forecast Changes and Risks	7
2.1. External Environment Developments	7
2.2. Forecasts	11
2.2.1. Inflation and Monetary Policy	11
2.2.2. Economic Activity	13
2.2.3. Comparison with Previous Projection	16
2.2.4. Key Assumptions and Risks	18
<i>Box 1. The results of survey on household and financial system expectations</i>	18
3. Actual Developments in 2022, Q2	24
3.1. Inflation	24
3.1.1. Fulfilment of the Inflation Target	24
3.1.2. Prices	26
<i>Box 2. Social Aspect of Inflation</i>	27
3.2. Economic Developments	29
3.2.1. Economy Position	29
3.2.2. The Expenditures Side of the Economy	29
3.2.3. The Production Side of the Economy	31
3.2.4. Labor Market	31
3.3. Financial Market Developments	32
4. Summing-up	35
Annex	
Minutes	36
The CBA Board Decision on Interest Rates	39
Press Release	40
Selected Macroeconomic Indicators	41
Charts	43
Tables	44

1. EXECUTIVE SUMMARY

In the third quarter of 2022, the slowdown in global trends of economic activity continued, particularly among the main partner countries of Armenia, mostly because of the Russian-Ukrainian conflict and the impact of various sanctions imposed on Russia. At the same time, as a result of the restraining monetary policy aimed at alleviating the high inflation environment in the partner countries, a gradual easing of the inflationary environment and a certain decrease of prices in international commodity markets is observed. Domestic economy still stays higher than expected, mainly due to demand factors. The latter are mostly expressed by a strong increase of external demand in the service sector, influenced by a significant inflow of international visitors, including tourists, and financial flows. While, in such circumstances, inflationary effects from the external sector are gradually weakening, domestic inflationary environment continues to expand, and inflationary expectations remain high, mainly due to the high demand.

The 12-month inflation remained high in the third quarter, totaling to 9.1% in August. According to the CBA's presented scenario, the actual high demand will significantly contribute to the high inflationary environment and inflationary expectations in the near future, therefore the Central Bank raised the policy interest rate at this stage again. At the same time, the Central Bank will consistently ensure stabilization of inflation through adequate actions and counteract every risk of deanchoring of inflation expectations.

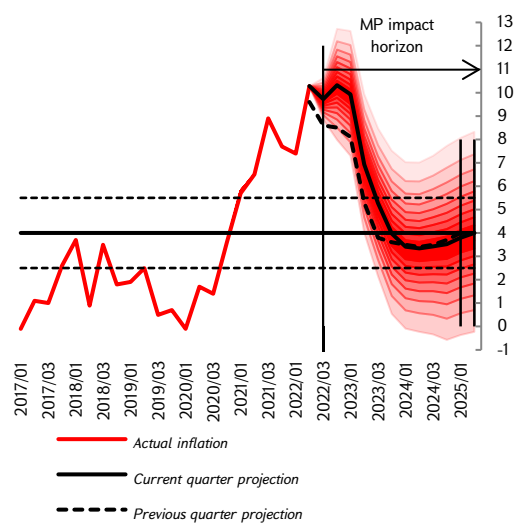
As a result of the implemented monetary policy and the expected macroeconomic developments, the 12-month inflation will gradually decrease and stabilize around the 4% target by close of 2023.

According to the CBA scenario, high economic activity will continue in the near future, as a result of which in 2022 economic growth will be significantly higher than the previous estimates. In the medium term, it will gradually decrease and stabilize around the long-term equilibrium level.

In 2022, the expected economic growth will mainly be due to the high demand in the service sector under the influence of international

Chart 1

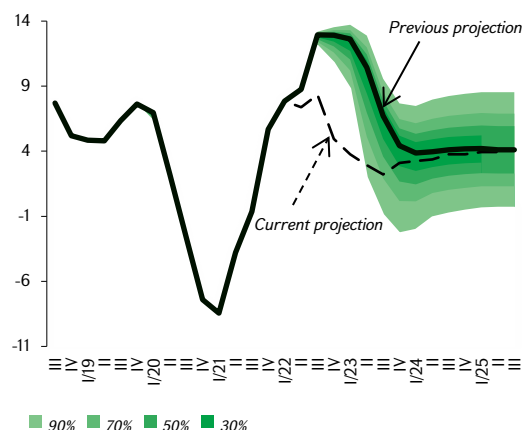
Inflation (12-month) projection probability distribution for 3-year horizon



Source: NSS, CBA projection

Chart 2

Real GDP growth (cumulative) forecast probability distribution for 3-year horizon



Source: NSS, CBA projection

¹ The growth rate of each quarter is calculated as the cumulative growth rate for the last four quarters.

visitors to Armenia, including tourists, and large-scale financial inflows. As a result of the gradual adjustment of the positive demand environment in the medium term, the economic growth will somewhat slow down, however, it will still remain high compared to the previous projections, due to the expected higher growth of state capital expenditures and productivity. It is expected that GDP growth will remain around its adjusted long-term sustainable level of 4.1% over the forecast horizon.

Risks of inflation deviating from the projected trajectory in the forecast horizon are balanced, whereas in terms of the short-term economic growth, downward risks prevail slightly (see the details in Subsection 2.2.4 “Key Assumptions and Risks”). In case of emergence of risks in any direction, the Central Bank stands ready to respond adequately, in order to ensure the price stability objective.

2. FORECAST, FORECAST CHANGES AND RISKS

2.1. External Environment Developments

Amid the high global inflation, and restrictive monetary policies conducted in developed and developing countries, a slowdown of the economic growth rate is globally observed. This process is still fueled by the disruptions in the supply of goods due to sanctions imposed as a result of the Russian-Ukrainian conflict, which, in turn, contribute to the reduction of the supply of intermediate and other types of goods, creating additional inflationary pressures. Subsequently, given the high inflation expectations, central banks of developed and a number of developing countries will continue to conduct contractionary monetary policy.

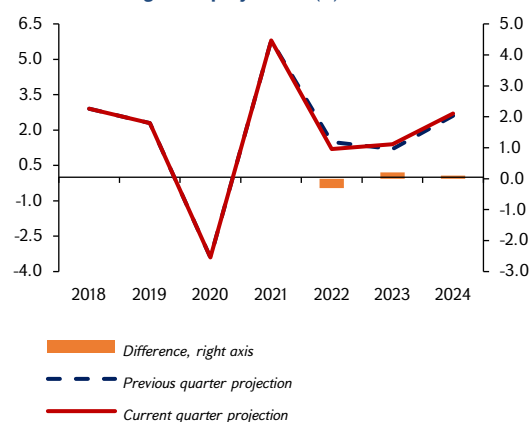
Amid the high global inflation, and restrictive monetary policies conducted in developed and developing countries, a slowdown of the economic growth rate is globally observed.

Economic Developments in the USA. Current developments in the US economy indicate a slower economic growth than previously expected. Thus, according to the Bureau of Economic Analysis of the US Department of Commerce, the growth of the US economy on a year-to-year basis in the second quarter of 2022 totaled 1.7%, which is in line with the CBA previous program projections. The growth of private consumption and investments contributed positively to the economic growth in the second quarter. It is expected that in the current and next years, particularly due to the sharp tightening of monetary policy, the economic growth in the USA will continue to slow down and will be somewhat lower than the long-term sustainable level.

According to the assessment of the Bureau of Economic Analysis of the Department of Commerce, in the USA² the second quarter inflation index of personal consumption expenses², in line with the expectations of the previous program, accelerated to 6.5%, and the annual index of consumer inflation reached 8.7%. Acceleration of personal consumption expenses and consumer inflation was mainly factored by the increase in the prices of energy carriers, as well as their secondary effect, as a result of the price growth of transportation services. It should be noted that the decline in the prices of energy carriers in July contributed to a slight slowdown in the inflation of personal consumption expenses in the USA, shaping it at the level of 6.3% y/y, and consumer inflation slowed down to 8.3% in August. Disruptions in supply chains, as well as high prices of used cars, continued to fuel

Chart 3

US economic growth projections (%)



Source: Bureau of Economic Analysis (BEA),
CBA projections

² The personal consumption expenditure price index target is 2%, which on average is commensurate with headline inflation of 2.3%.

high inflation. In the short term, despite a certain decrease in the prices of energy carriers, the high prices of the mentioned product groups, especially used cars and housing services, will continue to contribute to a high inflation environment.

Trends of overheating in the US labor market persist. Unemployment is already below the pre-crisis level, and vacancies still exceed the number of unemployed. In this context and given the high inflationary expectations, pressure is exerted on salaries, and subsequently on the acceleration of inflation.

Furthermore, amid the sustained positive demand and high inflation, prices of commodity groups with rigid prices, reflecting the long-term high inflation expectations, are still high. While they have somewhat decreased, they still remain above the target level. Accordingly, it is expected that the US Fed reserve will continue to tighten monetary conditions.

Hence, along with the tightening of monetary policy, the drop of prices in commodity markets, combined with the gradual recovery of global output and supply chains, inflation in the US will begin to gradually decrease in the medium term, approaching the target level at the end of the forecast horizon.

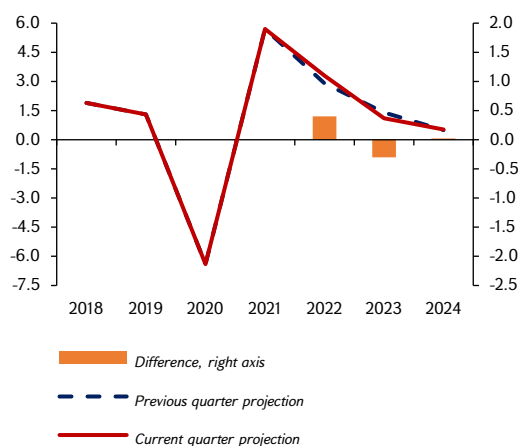
Economic developments in the Eurozone. In the second quarter of 2022, the economy of the Eurozone grew faster than expected in the previous program of the Central Bank of Armenia. According to the Eurostat estimates, economic growth in the Eurozone in the second quarter of 2022 totaled 4.1% y/y. The growth was mainly determined by the removal of restrictions related to pandemic, which had a one-time positive impact on the tourism industry. However, economic growth is expected to slow further due to less optimistic expectations regarding global demand. On the other hand, the Russian-Ukrainian conflict has a negative impact on the recovery of the Eurozone economy, as the gradual tightening of sanctions against Russia complicates trade relations between the countries, which, together with the continuous disruptions of the supply chains, will have a negative impact on the recovery of the economy both in the short and the medium term.

As a result, the economic growth of the Eurozone in the current year will be within in line with the previous estimate of the Central Bank, and the effects of the tightening economic policy and the weakening of external demand will be most evident in 2023.

Inflationary pressures in the Eurozone have grown. The ECB, as expected, tightened monetary policy by terminating the asset purchase programs and raised policy interest rate for the first time in the last decade. The growth of consumer prices was primarily determined by the growth in the prices of energy carriers (electricity and gas), which

Chart 4

EU economic growth projections (%)



Source: Eurostat, CBA projection

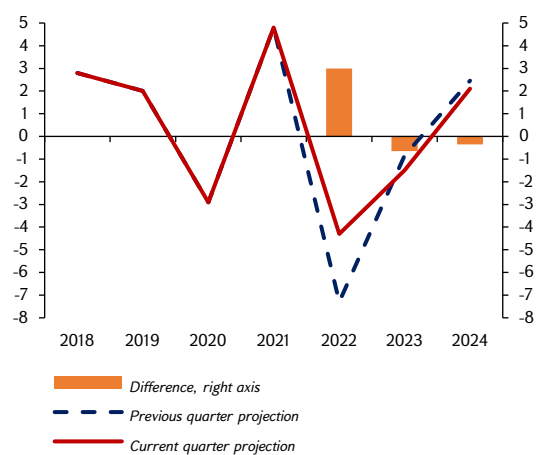
occurred due to the reduction of gas supply volumes by Russia as a result of the sanctions imposed amid the Russian-Ukrainian conflict, containing significant additional risks in terms of further acceleration of inflation.

In the second quarter of 2022, 8.0% y/y inflation was observed in the Eurozone, largely conditioned by the increase in the prices of energy carriers (oil and gas). Inflation in the Eurozone continued to accelerate in the third quarter of 2022, reaching 9.1% in August. It is expected that in the short term, the high prices of energy carriers (gas) will continue to fuel the high inflationary environment, at the same time, inflation will accelerate due to the significant recovery of domestic reserves as a result of lifting the restrictions related pandemic in the second quarter. Along with the gradual tightening of policy by the ECB, medium-term inflation will slow down and reapproach the target level in the final part of the horizon.

Economic developments in Russia. According to the State Statistical Service of Russia, despite the harsh economic sanctions imposed against the country because of the military-political conflict, decline in the Russian economy was substantially smaller than expected (4.0% y/y). The more positive exports performance in the second quarter, and stabilization of consumer activity and additional state spending contributed to the higher foreign and domestic demand. In general, the Russian economy has adapted to the current sanctions and their consequences faster than previously projected, as a result of which both domestic consumption and the country's trade turnover have recovered faster. The establishment of new trade relations was another important factor. Moreover, as a result of the policy conducted by the Bank of Russia, quick anchoring of inflationary expectations will also positively affect the decrease of the economy adjustment costs. Therefore, the current year's economic decline in the Russian Federation is estimated to be smaller than before, about 4.2%, and the estimates of economic activity in the following years will be close to the previous projections of the Central Bank.

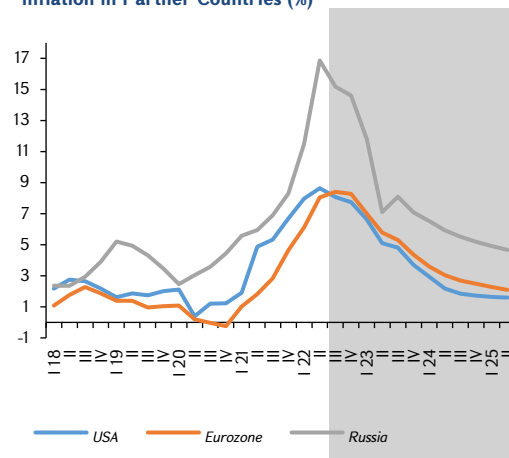
As a result of the effective monetary policy conducted by the Bank of Russia, i.e., prompt response to the sharp growth of inflationary expectations as a result of the military conflict and the imposed sanctions, and the consistent policy conducted thereafter, a significant decrease in inflation was observed. Thus, 12-month inflation in the second quarter of 2022 was 16.9% (significantly above the target level of 4%). However, in August, inflation dropped to 14.3%, due to the strong reaction to the effective monetary policy of the Bank of Russia and appreciation of the ruble. In the second quarter, the Bank of

Chart 5
Russia Economic Growth Projections (%)



Source: Rosstat, CBA projections

Chart 6
Inflation in Partner Countries (%)



Source: BLS, Eurostat, Rostat, CBA projections

Russia, despite declining, but still high inflation expectations, lowered the policy interest rate to a historically high level, from 20% to the pre-crisis level of 9.5%, then, in July and September, lowered it further correspondingly by 1.5 and 0.5 percentage points, to 7.5%, loosening somewhat the restrictions on capital flows.

According to the CBA current estimates, along with stabilization of inflation expectations and slowdown of inflation, the Bank of Russia will continue to gradually reduce policy interest rate and ease capital restrictions. As a result, inflation will reach the target level at the end of the forecast horizon without jeopardizing to a possible degree the process of long-term transformation of the economy.

Developments in commodity markets. Prices in almost all commodity markets have dropped due to the tightening of global financial conditions and positive factors of supply in various commodity markets.

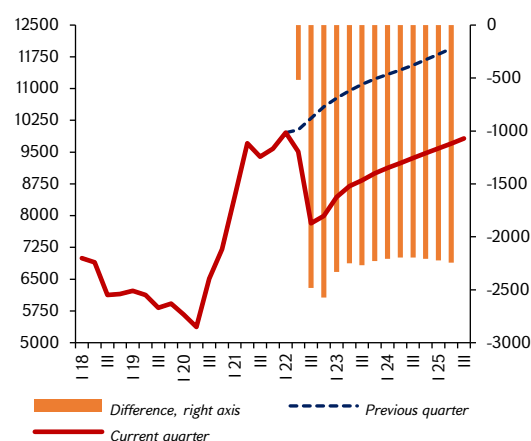
In the second quarter of 2022, prices in international copper market dropped due to the tightening of monetary conditions worldwide and the resulting decrease in the prices of financial assets and raw materials. Thus, in the second quarter of 2022, international copper prices decreased by 4.4% quarter-on-quarter, amounting to US\$ 9.6 thousand per ton, and the estimates of copper prices for the forecasted horizon were revised downwards compared to the previous program of the Central Bank. However, in the medium term, in case of gradual improvement of global demand and financial conditions, the international copper prices will grow to a certain extent, approaching the level of US\$ 9.5 thousand per ton at the end of the horizon.

Amid the military-political conflict and the application of sanctions against Russia, additional risks in terms of deepening the deficit were identified in the oil market, reflected by the increase in international oil prices and higher volatility in the second quarter. Accordingly, due to the risk of reduction in supply volumes and the recovery of demand in market, international oil prices grew in line with expectations in the second quarter, by 15.4% quarter-to-quarter. At the beginning of the third quarter, along with the certain alleviation of the risks on reduction of supply volumes by Russia, oil prices, like other raw materials, were affected by the more stringent global financial conditions, resulting in their certain decrease. Thus, oil prices in the forecast horizon will be affected by tighter monetary conditions in developed countries on one hand, and the uncertainties related to the supply on the other, including expectations of an increase in the supply in the event of easing sanctions against Iran. As a result, compared to the previous program, projections for the entire horizon have been

Prices in almost all commodity markets have dropped due to the tightening of global financial conditions and positive factors of supply in various commodity markets.

Chart 7

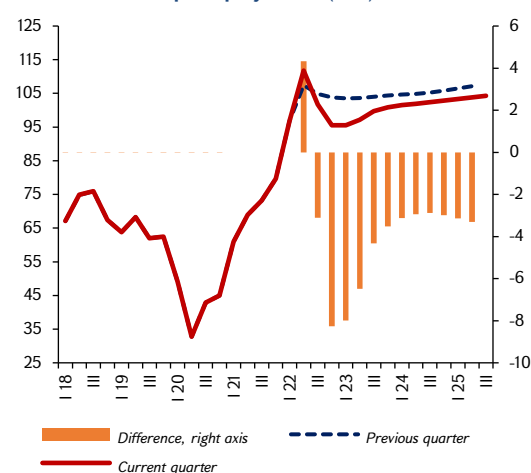
International Copper Price Projections (US\$)



Source: World Bank, CBA projections

Chart 8

International oil price projections (US\$)

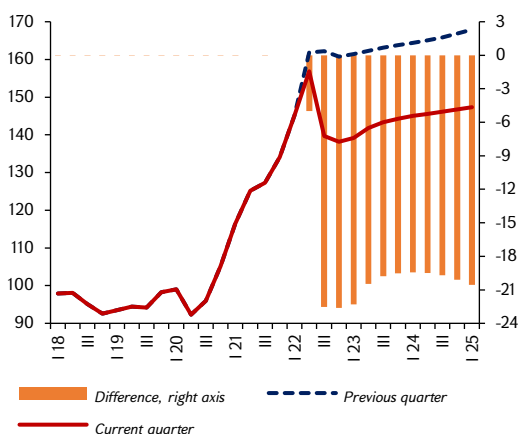


Source: World Bank, CBA projections

revised downwards. Due to the optimistic expectations regarding the volume of supply of certain commodities, and stricter global financial conditions, prices of food products decreased in the second quarter of 2022 for almost all commodity groups, staying below the previous CBA projections. At the beginning of the second quarter, the Russian-Ukrainian conflict had an additional inflationary effect on the prices of grain and vegetable oils, as both countries are their large producers and exporters. At the end of the quarter, the export disruptions in those groups were somewhat mitigated, as a result of which prices started to drop. Sugar prices fell at the end of the second quarter and the beginning of the third quarter amid expectations of good harvest in Brazil and India. It is expected that the above-mentioned factors of both financial conditions and supply will contribute to relatively low levels of prices in food markets throughout the forecast horizon.

Chart 9

International food price projections (index)



Source: FAO, CBA projections

2.2. Forecasts

2.2.1. Inflation and Monetary Policy

During the third quarter of 2022, the weak economic growth in the main partner countries of RA continues to be accompanied by a high inflationary environment. As a result of tightening of monetary conditions by developed countries, international commodity markets are witnessing the weakening of inflationary pressures. On the other hand, the high demand and economic activity Armenia continue to fuel inflation. In this situation, while the overall 12-month inflation has somewhat dropped compared to the previous month, totaling 9.1% in August, the 12-month core inflation has grown, making 10.2%. In the current situation, the Central Bank considers it necessary to raise policy interest rate by 0.5 percentage points.

Sluggish economic growth in partner countries persists. It is expected that under the consistent tightening policy conducted by the FRS in the USA, economic growth will continue to decrease gradually, in the so-called “soft landing” scenario, staying below the long-term sustainable level in the near future. Economic growth in the Eurozone in the second quarter exceeded the expectations under the previous program of the Central Bank, mainly due to a certain recovery of tourism and services sector as a result of the removal of the pandemic restrictions. However, it is expected that these positive developments will have a short-term nature and will cease in the near future under

the influence of a number of negative factors. In particular, the growth of geopolitical uncertainties, the prospects of global demand weakening, and the continuous disruption of supply chains as a result of the Russian-Ukrainian conflict will have a negative impact on the economic recovery of the Eurozone. Economic growth in the Russian Federation also exceeded the level expected under the previous program of the Central Bank of Armenia due to the positive contribution of additional state expenditures on the one hand and very positive export trends on the other, as well as stabilization of consumer activity.

Prices in international commodity markets have dropped significantly, which is due to the consistent tightening of global credit conditions, and favorable impact of supply factors of certain commodities. Subsequently, inflationary pressures on the domestic economy from the external sector will somewhat weaken in the near future.

In the third quarter, high economic activity continued, particularly in the services and construction sectors. On the other hand, the increase in demand for the Armenian tradable sector, including the significant inflow of international visitors, together with high remittances continue to positively contribute to a high level of total demand. As a result, the gap in demand is assessed as strongly positive, which continues to create inflationary pressures and contributes to the persistence of high inflationary expectations.

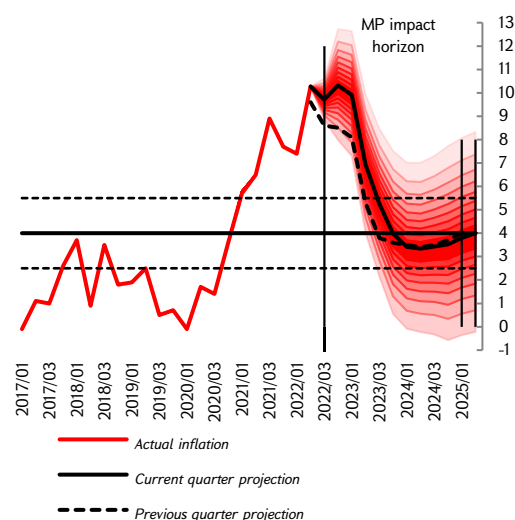
In the current situation, the CBA Board considered feasible to raise the policy interest rate by 0.5 percentage points. The Board will be consistent in ensuring stabilization of inflation and mitigation of inflationary expectations with necessary actions. In the medium-term, under the impacts of the implemented monetary policy and gradually weakening aggregate demand, inflation, while keeping above the target level in the short run, will gradually decrease, approaching and stabilizing around the target by close of 2023.

The CBA Board considers that the risks of inflation deviation from the projected trajectory are mostly balanced. In case of their emergence at any direction, the Board stands ready to respond adequately, in order to ensure the achievement of the price stability objective.

In the current situation, the CBA Board considered feasible to raise the policy interest rate by 0.5 percentage points.

Chart 1

Inflation (12-month) projection probability distribution for 3-year horizon



Source: NSS, CBA projection

Table 1

Period	Inflation Interval Projection Probability Distribution				
	<1.0%	1.0-2.5%	2.5-5.5%	5.5-7.0%	>7.0%
Q III 2022	0.0%	0.0%	0.0%	0.0%	100.0%
Q IV	0.0%	0.0%	0.0%	0.9%	99.1%

Q I 2023	0.0%	0.0%	0.3%	3.0%	96.7%
Q II	0.0%	0.6%	20.0%	30.1%	49.3%
Q III	1.2%	5.9%	47.0%	26.9%	19.0%
Q IV	7.6%	16.0%	52.1%	16.2%	8.1%
Q I 2024	12.7%	20.2%	49.8%	12.1%	5.2%
Q II	13.8%	20.6%	48.7%	11.8%	5.1%
Q III	14.2%	19.5%	47.0%	12.7%	6.6%
Q IV	15.3%	18.3%	44.2%	13.4%	8.8%
Q I 2025	13.2%	16.7%	44.1%	14.9%	11.0%
Q II	12.0%	15.6%	43.6%	15.9%	12.9%

Source: NSS, CBA projection

2.2.2. Economic Activity ³

Since the beginning of 2022, actual economic growth has been significantly higher than the previous CBA estimate. Annual economic growth is projected at 12.9% instead of the previous 4.9% driven by both domestic and foreign demand. The acceleration of demand is mostly driven by the inflow of international visitors from the Russian Federation, which in turn is reflected by the growth of exports in the services sector. The acceleration of private consumption will be driven by the decline in private savings, which is due to the resumption of international tourism in the world and the growth of remittances which is a result of certain appreciation of the Russian ruble and a smaller than expected decline in the Russian economy. While the uncertainties amid the Russian-Ukrainian conflict still persist, private investments are strongly accelerating, mainly due to the construction of residential buildings, which will continue to significantly contribute to economic growth during the year. Thus, the economic growth in 2022 will be higher at 12.9%.

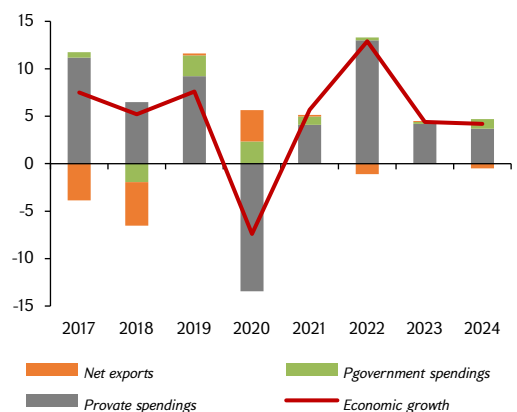
Compared to the previous program, the growth of economic activity in the medium-term horizon has been revised upward due to the reassessment of potential GDP growth as a result of the expected acceleration of capital expenditures.

External Demand. Amid the sanctions applied to the Russian economy, certain positive effects on the domestic economy from the external sector significantly exceeded the expectations outlined in the previous scenario. As a result, in terms of export of goods and

Since the beginning of 2022, actual economic growth has been significantly higher than the previous CBA estimate. Instead of the previous 4.9% annual growth projection, after the review of both domestic and foreign demand, a higher 12.9% economic growth is now projected.

Chart 11

Contribution of demand⁴ components to growth (percentage point)



Source: NSS, CBA estimates

³ For a detailed economic growth forecasts, see the "GDP Projection Probability Distribution", Chart 18, Table 2.

⁴ Change in the stock of tangible current assets is not accounted in demand, because it is calculated by the RA State Revenue Service as a balancing item and does not reflect the real level of investments, so the economic growth calculated by supply and demand may differ. See: https://www.armstat.am/file/article/sv_04_19a_112.pdf.

services, a higher growth is now projected. At the same time, as a result of strong domestic demand, compared to the previous scenario, a higher growth of import of goods and services is projected.

Against the background of ongoing restrictions on Russia, Armenia's export opportunities will expand given the upward reassessment of the export potential. At the same time, export of mineral products will slow down to a certain extent, but will be restored at the end of the year. As for the export of services, the large influx of international visitors will continue and, to this end, a significant increase in the average cost per tourist is expected⁵. As a result, in 2022, the growth of real exports of goods and services will be high, at 28.0%.

Given quicker recovery of domestic demand and the easing of pandemic restrictions by the European countries, a higher growth of real imports of goods and services is expected compared to the previous projection. A 24.0% growth of real imports of goods and services is estimated for 2022.

The assessment of remittances is based on the judgment about the more positive developments of the Russian economy compared to the assessment of the previous program. The net inflow of total remittances (including seasonal workers' incomes and private transfers) will decrease by around 7% in 2022, compared to the 13.0% decline indicated in the previous program.

The estimates above show that in 2022, the share of current account deficit in GDP will decrease in comparison to the previous estimate and will be in the range of 3.0-4.0%.

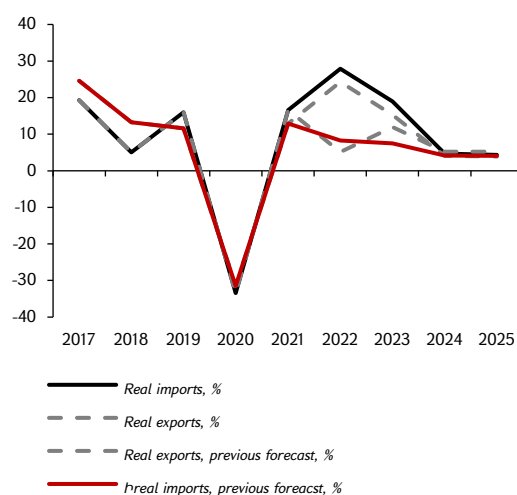
In the medium term, parallel to the easing of uncertainties, the gradual adjustment of the high external demand will be manifested by the increase and stabilization of current account deficit/GDP ratio at the estimated equilibrium level of 4.0-6.0%.

Fiscal Policy. The impact of the fiscal policy on the aggregate demand in 2022 was evaluated based on the adjusted estimates of the 2023-2025 Medium-Term Expenditure Framework Program⁶ (MTEFP), current developments and the CBA estimates made on those developments.

Given the actual developments in January-August 2022 and the recovery of economic activity, tax revenues of the state budget is expected to be higher for the first three quarters, which is a good

Chart 12

Flows of real exports and imports of goods and services in the medium term (%)



Source: NSS, CBA forecast

⁵ See "The RA Balance of Payments in January-March 2022" https://www.cba.am/Storage/AM/downloads/stat_data_arm/PRESS%20RELEASE-2022-Q1.pdf:

⁶ The adjusted program is the quarterly and annual program adjusted by the relevant Government decrees.

prerequisite for completing the annual tax revenue program of the state budget.

According to the CBA's estimate, in 2022 the share of taxes in GDP⁷ will decrease by 0.2 percentage points as a result of the higher growth of GDP over tax revenues.

Compared to the annual state budget program, the revenue surplus will total at about 70.0 billion dram, as a result of the higher-than-planned collection of taxes and other revenues, as well as certain shortfall of grants. In terms of public expenditures, the performance was at 94.9% or about 49.0 billion drams less than planned amid the expectations of shortfall of externally financed capital expenditures carried out with external support and the resulting co-financing savings for these expenditures.

According to the CBA estimates, in 2022, the share of expenditures in GDP will total 25.1%, dropping by 3.6 percentage points against the previous year. The share of deficit in GDP ratio will total 1.3 %, down by 3.3 percentage points over 2021.

As a result, after adjusting government budget expenditures and revenues from flows that do not have an impact on gross demand, in 2022, 1.2 percentage contractionary effect of fiscal policy is expected compared to 2021. The latter will be due to the expansionary revenue impulse and even more contractionary expenditure impulse.

Based on the 2023-2025 MTEFP, a weak leveraging effect of the fiscal policy is projected due to the large capital expenditures planned for that period and a certain slowdown of the GDP growth rate. Furthermore, along with the growth, the Government will proceed to smooth fiscal consolidation ensuring a gradual reduction of the budget deficit and debt burden due to the higher tax revenues and the improvement of the expenditure structure. At the same time, **as a result of the implementation of the capital expenditures specified in the 2023-2025 MTEFP, the share of expenditures in GDP will reach 6.3% from 4.3% in 2022, as a result the medium-term potential growth of GDP will reach around 0.4-0.5 percentage points.**

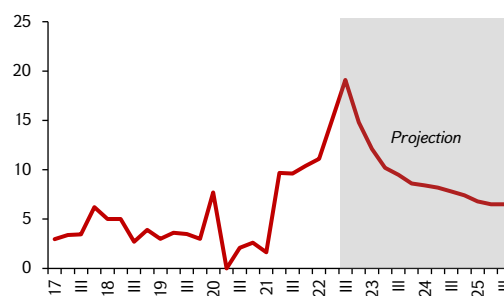
Labor Market. It is expected that in 2022, due to the positive economic developments and high demand, the unemployment rate will remain below its medium-term indicator at 14.1%, and will rise and stabilize around 15% in the medium term.

In 2022, as the positive GDP gap and high inflation persists, high growth in private wages is expected, around 15%. However, in the medium term, given the gradual adjustment of demand and

In 2022, 1.2 percentage contractionary effect of fiscal policy is expected compared to 2021.

Chart 13

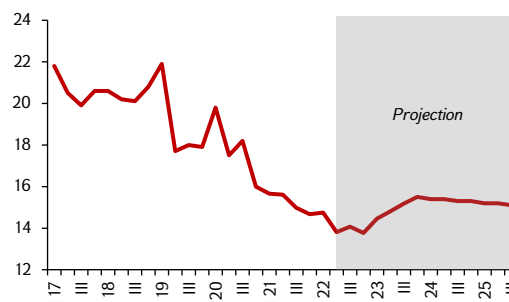
Nominal wage growth in private sector, y/y (%)



Source: NSS, CBA projection

Chart 14

Level of unemployment (%)



Source: NSS, CBA projection

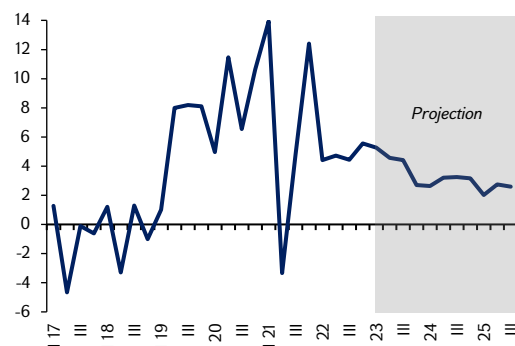
⁷ The GDP indicators used in the program are the CBA projections.

stabilization of inflation around its target, a certain slowdown in the growth of private wages is expected. Subsequently, at the end of the horizon, the increase in wages will stabilize around 7-8%.

Thus, due to the higher growth of private wages compared to productivity, in 2022 inflationary pressures from labor market will continue. Accordingly, the growth of unit labor costs during the year will be around 5.0%. In the medium term, inflationary pressures will weaken somewhat, and the growth of unit labor costs will stabilize in the range of 3-4%.

Chart 15

Unit labor costs growth, y/y (%)



Source: NSS, CBA projection

2.2.3. Comparison with the Previous Projection

Projections of economic growth in 2022 have been revised upwards.

Compared to the previous forecast, economic growth in 2022 was revised upwards and is projected at around 12.9% instead of 4.9%. The acceleration of economic growth is mainly due to the significant performance of the service sector, although in other sectors too more positive developments are expected as compared to the previous program.

High growth is expected in the services sector, which will be supported by the acceleration of both external and domestic demand, largely affected by more positive developments in the IT, financial, accommodation and catering services sectors as a result of the large inflow of international visitors. It is assumed that the growth of this sector will continue until the end of the year.

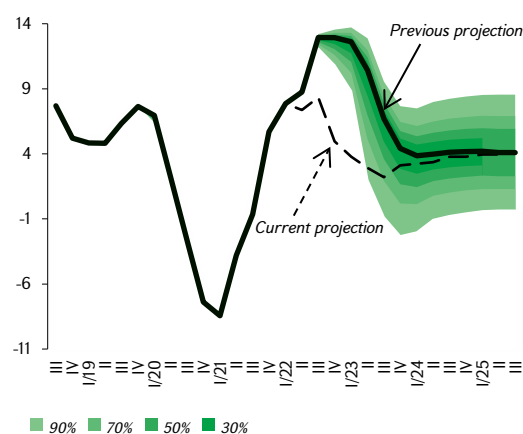
In the construction sector, a higher growth compared to the previous estimate of the Central Bank is expected, mainly due to the acceleration of the growth the construction carried out at the expense of the funds of organizations.

More positive developments are also expected in the agriculture sector, due to the higher growth of the crops sector compared to the CBA assessment. Some growth of the branch is expected in the second half of the year, again at the expense of the growth of the crops sector.

Industry sector growth has been revised upwards, mainly due to expected more positive developments in manufacturing. It is expected that the growth of external demand for food and beverages will continue, as a result of which the output and export of this sector will also accelerate to a certain extent.

Chart 16

Real GDP growth (cumulative) forecast probability distribution for 3-year horizon



Source: NSS, CBA projection

⁸ The growth rate of each quarter is calculated as the cumulative growth rate of the last 4 quarters.

As a result of the gradual adjustment of the current demand environment, economic growth will slow down in the forecast medium-term horizon. However, the medium-term economic growth estimate has been revised upwards due to higher expected growth in public capital expenditures and productivity, and GDP growth is expected to be close to its upwardly revised estimate (4.1%) at the end of the horizon (Chart 16).

Table 2

<i>Probability Distribution of Real GDP Growth (Cumulative) Projection</i>		
Period	30% Probability Interval	90% Probability Interval
2022 January-December / 2021 January-December	12.7 - 13.1	12.1 - 13.8
2023 January-December / 2022 January-December	3.5 - 5.3	0.5 - 8.3
2024 January-December / 2023 January-December	3.1 - 5.2	(-0.3) - 8.6
2025 January- June / 2024 January- June	3.1 - 5.1	(-0.3) - 8.5

Source: NSS, CBA projection

In 2022, the share of current account deficit in GDP will decrease compared to the previous projection, mainly because of the significant improvement in net export of services due to the high growth of external demand. At the same time, the decrease in remittances is estimated to be smaller due to more positive developments in the Russian economy than expected.

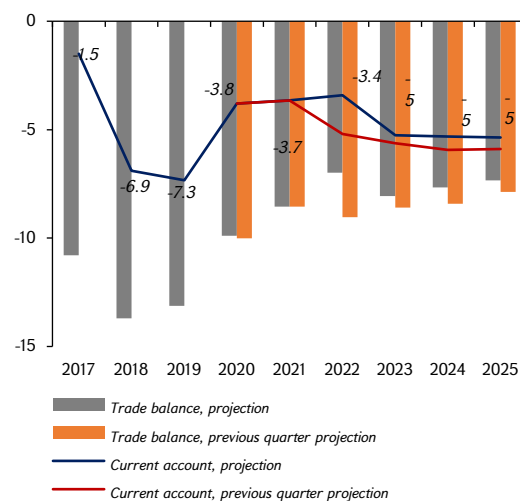
Compared to the previous projection, fiscal impulse will have a slightly more contractionary effect of about 1.2 percentage point: in case of full implementation of the adjusted tax program and 98.5% (CBA projection) execution of the adjusted expenditure program, revenue-neutral and cost-restraint effects are projected.

According to the current projection, general inflation in the short run will be higher compared to the previous program, mainly due to the higher level of core inflation and regulated services. The high level of core inflation will continue to be determined by the inflationary pressures transmitted as a result of the growth in domestic demand. Accordingly, compared to the previous plan, inflation in the near future will be at a higher level, and in the medium term it will decrease and from the end of 2023 stabilize around the target level (see Chart 1).

Short-term inflation expectations will be somewhat higher than the previous forecasts mostly due to the high actual demand in the domestic economy, although household surveys for the last two quarters indicate a decrease.

Chart 17

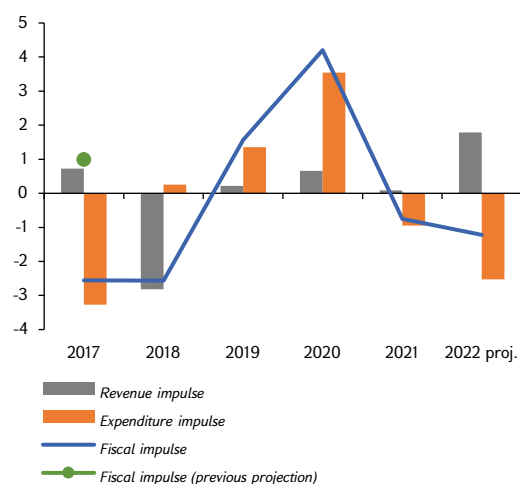
Current account/GDP medium-term projections (%)



Source: NSS, CBA projection

Chart 18

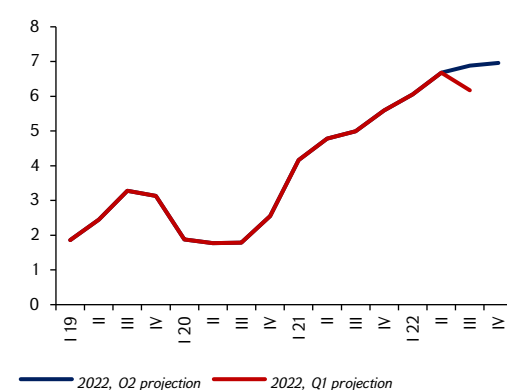
Fiscal impulse projection (percentage point)



Source: CBA estimate

Chart 19

Short-term inflation expectations (%)



Source: CBA estimate

2.2.4. Main Assumptions and Risks

This section presents the main assumptions underlying the Monetary Policy Program for the third quarter of 2022, and the risks to implementation of the program coming from external sector developments, fiscal policy, emerging trends and short-term projections.

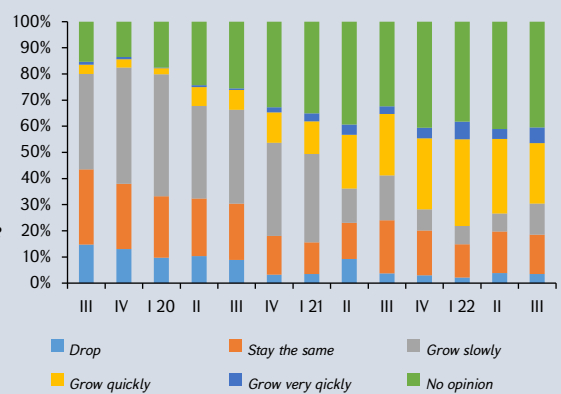
Box 1

The results of survey on expectations of households and the financial system

According to households' survey conducted by the Central Bank on expectations in terms of various macroeconomic indicators in Q2 2022, inflationary expectations have somewhat decreased, but still remain high. In particular, the share of households expecting high inflation for the one-year horizon in the structure of the surveyed households has somewhat decreased, while the share of those expecting low inflation has grown. The results of the survey show that in the second quarter, the uncertainty of the respondents regarding the expected inflation did not change significantly, and remains high.

Chart 20

Household inflation expectation surveys



Source: CBA

Projection Judgments

Table 3

Main Findings and Assumptions	Possible developments if these assumptions prove to be correct
Stringent sanctions imposed on Russia following the Russian-Ukrainian conflict will remain throughout the forecast horizon.	✓ Among the main trade partners of Armenia, economic growth in the USA and the Eurozone will be slower; the economic decline in Russia will be smaller due to lower contraction of demand and faster recovery.
At the same time, while supply chain disruptions have somewhat mitigated, in the short term they will still remain.	✓ As a result of the tightening of global financial conditions, prices in international commodity and food markets are expected at a low level.
Among the main partners of Armenia, the US FRS and the European Central Bank will continue to conduct a tighter monetary policy, ensuring relatively smooth adjustment of inflation and the economy.	✓ Inflation in partner countries will be affected by the decrease in commodity prices, but will remain high.

Given continuous tightening of monetary conditions by the US FRS, in the short-term Armenia's country risk-premium will remain at the current high level in line with the trends in the developing countries. At the same time, the tightening of global financial conditions will lead to a decrease in medium-term prices of financial assets, as a result of which the long-term stable levels of country risk-premium in the developing countries, including Armenia, will be somewhat adjusted upwards.	<ul style="list-style-type: none"> ✓ During the third quarter of the current year, the country's risk-premium increased to a certain extent because of the regional instability and the tightening of the FRS's monetary policy. According to current forecasts, it will still remain at the current high level in the short term, and then gradually approach a long-term stable level.
The impact of fiscal policy in 2022 is expected to be expansionary effects from revenue side and contractionary from expenditure side.	<ul style="list-style-type: none"> ✓ According to estimates, given implementation of the annual tax revenue program and 94.9% performance of the adjusted expenditure program, in 2022 fiscal policy will have a contractionary effect of about 1.2 percentage points. ✓ According to 2023-2025 MTEFP, in the mid-term a slight expansionary effect of the fiscal policy is expected due to the projected large volumes of capital expenditures and a certain slowdown in the GDP growth rate.
Amid the ongoing restrictions on the Russian Federation, Armenia's export opportunities will expand, also reflected by a certain growth of export potential. At the same time, the actual large flows of international visitors will be preserved in the short term.	<ul style="list-style-type: none"> ✓ In the short term, positive developments in the manufacturing sector will continue, including some expansion of the output capacities. ✓ As large flows of international visitors continue, positive external demand shocks will be preserved. ✓ Continuing high growth in information and communication sector until the end of the year, which will have approximately 1% impact on the GDP potential in 2022.
A certain negative contribution of the extractive industries to the growth of the GDP potential.	<ul style="list-style-type: none"> ✓ Monetary policy scenario does not incorporate operation of the Amulsar mine and the Alaverdi copper-molybdenum plant. Their potential impact is considered in forecast risks. ✓ Suspension of Teghut mine operations until the third quarter, inclusive, with subsequent restoration of the previous level of production and export. The closure of the Teghut mine will have around 1.1% negative contribution to industry in one quarter.
A certain expansion of the pent-up domestic demand during 2022, at the expense of savings accrued in previous years.	<ul style="list-style-type: none"> ✓ As a result of the global alleviation of restrictions related to the pandemic, recovery of tourism imports from RA is expected at the expense of private savings.
Changes in excise and customs rates by 2023 deriving from the requirement to apply common rates in the EEU.	<ul style="list-style-type: none"> ✓ The annual impact of the gradual excise tax change expected in 2021-2023 is estimated at about 0.4 percentage point, and the impact of the change in customs rates at 0.3 percentage point for each year.

Increase in GDP potential at the expense of public capital expenditures.	✓ As a result of implementation of the capital expenditures outlined in the 2023-2025 MTEFP, an increase in the medium-term potential growth of GDP is expected due to the increase in productivity and private investments arising from capital expenditures. The estimate of potential GDP growth was revised to 4.1% from the previous 3.6%.
--	---

Source: CBA

Forecast Risks

As a result of the Russian-Ukrainian conflict and the large-scale sanctions imposed on Russia, the high level of geopolitical uncertainties in the region persists. Periodic outbreaks and spreading waves of pandemics have a limited economic impact in the context of sufficient vaccination rates around the world. However, in some cases, such as in China, the waves of the pandemic are followed by a strong response, which has a significant negative impact on economic activity. In general, these factors continue to create risks and challenges in terms of stabilizing the global economy, ensuring regular operation and recovery of international commodity, food and financial, markets and the supply chains that have been disrupted before. As over a long time global inflation rates are significantly above the target levels, the risks of deanchoring of the long-term inflationary expectations persist. To this end, central banks of many countries are conducting or outlining a policy of quick tightening of monetary conditions. A significant portion of risks is linked with the uncertainties regarding the speed of tightening of the monetary policy by the FRS, leading to growth of volatility in global financial markets and a significant adjustment of asset prices.

These developments obviously create high uncertainty and significant risks for the RA economy as well. Further to the risks ensuing from the outside world, there are also risks related to the large-scale military aggression of Azerbaijan. These factors are still manifested through wider ranges of ambiguity around the forecasts of the central points of inflation and other key macro-indicators (See Charts 1 and 2): Accordingly, amid high uncertainties, only the most significant risks around the baseline scenario are presented below.

In terms of aggregate demand, the following risks stand out:

- The risks of a slowdown in external demand are mainly related to a possible sharp decline in the Chinese economy, which may have a deflationary effect on the international prices of food and inputs.

- The risks related to increased inflation and economic growth in the EU derive from developments in energy prices, under which the ECB will be consistent in mitigating the risks of deanchoring inflationary expectations.
- In the context of current regional geopolitical developments, there are mainly positive demand risks in terms of sustainability and volume of the expected inflow of international visitors and financial flows and their contribution to the national economy.
- Slowing down of seasonal migration from Armenia due to the unfavorable economic environment in the Russian Federation and restrictions on capital flows.
- In terms of the impact of fiscal policy on aggregate demand in 2022, there are risks to lower spending performance. As a result of the first 8 months of 2022, according to the CBA assessment, the budget surplus is mainly due to cost savings. Therefore, the bulk of the annual program of state budget expenditures will be implemented in the last quarter of the year. However, if savings of public expenditures and shortfall of external financing persist, the low performance of expenditures can continue, and they may have a greater restraining effect. It should be noted that in 2023 risks in the direction of increasing expenditures stand out, due to the reduction of the share of debt within GDP and loosening of the restrictions arising from the fiscal rule.
- In the environment of significant positive demand, difficulties arise in attracting additional labor and resources, causing risks of non-linear effects on inflation.

In terms of supply, the following inflationary risks stand out:

- Risks pertaining to commodity price projections related both to the scale of the global economic growth slowdown, and the possible disruptions in supply chains and regular supply volumes in international markets.
- Amid the persisting geopolitical tension, there are risks of deglobalization and inflationary risks arising from it.
- Commodity market imperfections and skewed inflation and exchange rate expectations bring about risks of inflationary nature relating to disproportionate passthrough of dram appreciation to prices of imported goods.
- The ongoing tension at the RA border and political uncertainties, result in inflationary risks related to excessive response of financial markets and the increase of Armenia's country risk-premium.

As a result, risks of inflation deviation from the forecast in the medium term are estimated to be balanced, and still high quantitatively (see Chart 1).

Further to the above-mentioned inflation risks, there are other potential medium-term risks in term of economic growth of bilateral nature, where upward risks somewhat prevail. In particular, risks are related to the following internal and external factors:

- Significant difficulties and disruptions in the activities of local companies with Russian capital, which will have a negative impact on the economic growth in Armenia.
- Negative risks associated with the spread of new waves of pandemic and its economic implications.
- Both positive and negative risks related to the nature, size, duration of capital-financial flows to the RA economy and the possible transformation of the economy.
- Risks related to the effectiveness of execution of capital expenditures outlined in the medium-term budget expenditure plan.
- Negative risks related to ongoing tension at the RA border and political uncertainties.
- Implementation of the € 2.6 billion EU Eastern Partnership assistance package implying an upward risk (annual GDP growth of 0.9-1.0%).
- Uncertainties related to the development of the Amulsar mine and Alaverdi copper smelter, which pose an upward risk.

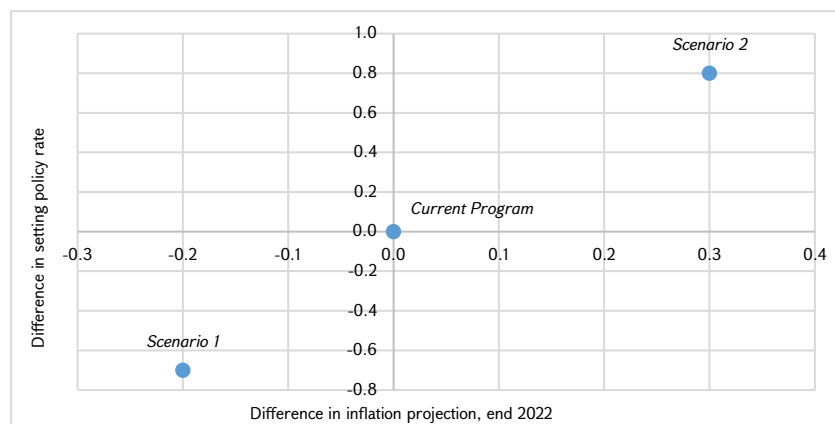
In general, as significant uncertainties remain related to geopolitical situation, coronavirus, deglobalization international supply chain rearrangements and possible financial and economic developments, the Central Bank seeks to reduce the potential risks arising from these uncertainties by modeling and evaluating different scenarios of further developments. In particular, given the peculiarities of the current stage and the possible emergence of various types of risks, two scenarios of economic developments have been considered in greater detail:

- Accumulated imbalances in real estate market will lead to a financial crisis and economic decline in China resulting in the slowdown of global demand and the decrease of prices in commodity markets, with subsequent external pressures on the RA economy that will be of more deflationary nature compared to the current program (Scenario 1).
- Highly inflationary environment creates grounds for the acceleration of inflation induced by wages. In the event high inflation environment persists and is combined with a strong positive demand and an increase in the bargaining power of employees, adjustment of wage growth to inflation can take place causing additional inflationary pressures compared to current program assumptions (Scenario 2).

Under these scenarios, the options of respective policy response were considered, with the view to taking adequate steps at the very first evidence of their emergence.

Chart 21

Economy response to external demand shock (under floating and regulated exchange rates)



Source: CVBA projection

3. ACTUAL DEVELOPMENTS IN Q1, 2022

3.1. Inflation

3.1.1. Fulfillment of the Inflation Target

According to the main assumptions of the scenario presented in the Q3 2021 program, due to the expected impacts of international commodity markets and the outpacing growth of domestic demand over the expansion of production capacities, in the first half of the reporting period from Q3 2021 to Q3 2022, a high inflation environment would continue. After that, gradually decreasing, in 2022, it would approach the 4% target, stabilizing around it in the medium term.

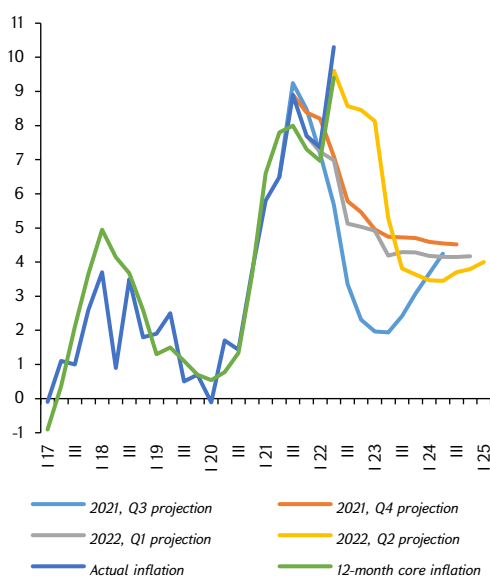
As expected, 12-month inflation in the reporting period gradually decreased till March 2022, and in February already totaled 6.5%, with a tendency to approach the target in the near future. However, as result of geopolitical developments, a significant expansion of inflationary environment strongly above the expected level was observed. Accordingly, the path to reach the target index in the second quarter has been adjusted for the short-term sector, and a higher level of inflation has been forecast.

Due to the large-scale vaccination against coronavirus from the beginning of the year and refraining from strict economic restriction, the recovery of global economic activity and foreign demand in the second half of 2021 continued at a faster pace. In Armenia, the inflationary factors mainly sustained due to the inflationary effects still transmitted from the external sector (high energy prices and supply chain disruptions) and shaping of a positive demand environment. The latter was greatly contributed by the high growth, especially in domestic services, which in turn, was affected by higher-than-expected growth of tourism. At the same time, despite a certain decrease in the 12-month inflation rates at the end of the year, public expectations of inflation remained high under the impact of persisting inflationary factors and the expected changes in the prices of regulated services. Given the above developments, the Central Bank continuously raised the refinancing rate in the second half of 2021, in total, by 1.25 percentage points.

In the first half of 2022, macroeconomic environment in Armenia, particularly inflationary developments were strongly affected by the Russian-Ukrainian conflict that escalated since the end of February,

Chart 22

During the period under review, dynamics of the 12-month inflation were generally in line with the outlined direction; only in the second quarter of 2022 the expected level was significantly exceeded, and subsequently, the short-term projections for the given quarter were revised upwards



Source: NSS, CBA projection

various sanctions applied to the Russian economy and the unprecedented uncertainties derived thereof. The latter were reflected in the significant slowdown of the growth rates in Armenia's main partner countries, and the extremely high inflation in international energy and commodity markets caused by the disruptions of supply chains. In the short term, these developments exerted negative impact on the domestic economy mainly by certain attenuation of economic activity, and on the commodity market in terms of high prices for some imported goods. Already in the second quarter of 2022, a significant acceleration of economic activity has been observed, mainly due to the high growth of the service sector, which, in turn, was contributed by the large-scale inflow of international visitors and finances to Armenia. This served as a significant factor in the expansion of the inflationary environment at the end of the reporting period, especially in the services sector. At the same time, the escalation of the Russian-Ukrainian conflict has strongly contributed to volatility of the RA financial market and the country risk premium in the short-term period, which also contributed to a certain rise of inflationary expectations and inflationary risks. In this situation, the Central Bank raised policy rate by 1.5 percentage points in the first half of 2022.

Furthermore, in response to the highly inflationary situation driven by geopolitical developments, the CBA tightened monetary conditions in March by a relatively large step of 1.25 percentage points. In the second quarter, the CBA refrained from changing interest rate, given that within inflation factors the effects of global inflationary phenomena and, especially, external demand prevailed, which, parallel to devaluation of the Armenian dram, would gradually decrease (see Box 2). In addition, a relatively large tightening of monetary conditions in the first quarter of 2022 was seen as a sufficient response to further mitigation of the highly inflationary environment.

Summing up, during the reporting period, refinancing rate was raised in general by 2.75 percentage points and in June 2022 was set at 9.25%.

Summing up, during the reporting period, refinancing rate was raised in general by 2.75 percentage points and in June 2022 was set at 9.25%.

Subsequently, as expected, the 12-month inflation grew in the first part of the reporting period, from 6.5% in June 2021 to 9.6% in November, after which, it decreased under transmitted effects of previous monetary policy actions to 6.5% in February 2022. Then, due to geopolitical developments, inflation grew significantly and reached 10.3% in June. It is estimated, that as a result of the implemented consistent monetary policy, inflation will gradually decrease and in the medium term, it will approach the 4% target.

3.1.2. Prices

A certain alleviation of the inflation environment observed from end 2021 was followed by its sharp acceleration from the second quarter of 2022.

A certain alleviation of the inflation environment observed from end 2021 was followed by its sharp acceleration from the second quarter of 2022.

At the beginning of the reporting period, the growth of prices of imported food and non-food products continued to contribute to the acceleration of core inflation. The latter was affected by both the prices of food products in international markets and the high aggregate demand. 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 (during that time prices of imported food products increased by about 15%). The growth of international energy prices affected domestic 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).

Due to the consistent monetary policy of the CBA, inflationary effects of the above-mentioned factors have weakened since the end of 2021 in line with the estimates. However, at the end of the first quarter of 2022, amid the escalation of the Russian-Ukrainian conflict, sanctions applied against Russia and the ensuing uncertainties, inflationary trends augmented. The aforementioned factors have had a significant inflationary impact, especially in terms of basic goods. At the same time, due to the factor of international visitors, acceleration of the domestic demand has put strong inflationary pressures in terms of locally produced goods and services as well, under which the prices of a number of services with relative price rigidities (apartment rent, restaurants and hotels, hairdressing, financial services) were adjusted.

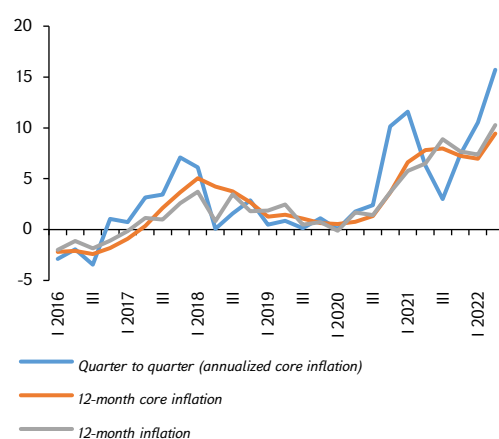
Growth of prices of “Tobacco” and “Alcoholic Beverages” product groups, in line with the estimates, continued to be affected by inflationary impact of the change of excise tax rates at the beginning of the year.

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 these factors in general persisted throughout the entire horizon of the reporting period.

Tariffs for regulated services in the first quarter of 2022 significantly expanded the inflationary environment due to the increase

Chart 23

Some mitigation of the inflationary environment in late 2021 was followed by its sharp increase in the second quarter of 2022



Source: NSS

in water supply tariffs since January, electricity tariffs since March, and natural gas tariffs since April. As of the end of June, their total contribution to 12-month inflation was about 1.0 percentage points.

Table 4

Consumer price inflation by commodity items as key contributors			
<i>Designation</i>	<i>Weight</i>	<i>12-month inflation as of March 2022</i>	<i>Contribution to inflation</i>
Core inflation	75.10	9.4	7.1
Bread and cereals	8.10	19.9	1.6
Meat	9.00	11.6	1.0
Oils and fats	2.60	5.1	0.1
Sugar	0.50	6.9	0.0
Dairy products	4.15	21.0	0.9
Alcoholic beverage	2.40	6.9	0.2
Tobacco	1.40	10.3	0.1
Clothing	1.30	10.5	0.1
Footwear	0.80	10.4	0.1
Household appliances	0.60	7.4	0.0
Fuel	6.80	9.5	0.6
Air passenger transportation services	0.60	17.6	0.1
Actual rent paid by the lessee for additional accommodation	1.00	32.9	0.3
Restaurants and hotels	1.00	6.8	0.1
Fees for services of banks, post offices	0.58	7.5	0.0
Imported food	14.8	14.4	2.1
Seasonal food	9.40	25.3	2.4
Eggs	1.30	-24.0	-0.3
Fruits	3.20	16.2	0.5
Vegetables	4.90	45.8	2.2
Regulated services	15.50	5.0	0.8

Source: NSS

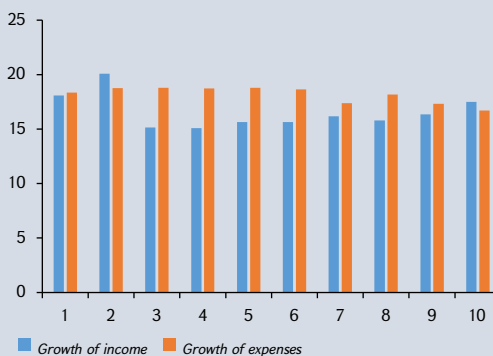
Social Aspect of Inflation

During the recent period, amid the high inflation both the worldwide and in Armenia, an intensive discussion of the social effects of inflation takes place, including in the context of possible effects of the exchange rate appreciation.

Box 2⁹

Chart 24

Compared to 2020, expenses growth has exceeded income growth in almost all decile groups (%)



⁹ Prepared by Diana Nazaryan from Monetary Policy Department.

Source: NSS, CBA estimates

In order to assess the differences in the impact of inflation within different social groups, an assessment of the change in income and expenses of different deciles of population was made (Q2, 2022 compared to 2020). In order to evaluate changes in income by decile groups, changes in the minimum wage threshold, as well as the average wage, pensions and transfers during the specified period were considered. At the same time, taking into account the consumer basket structure of each decile group, the change in expenses as a result of inflationary effects compared to 2020 was also calculated. As a result, in the considered period, in almost all decile groups, the growth of expenses exceeded the growth of income, reflecting general decline in the net income of households.

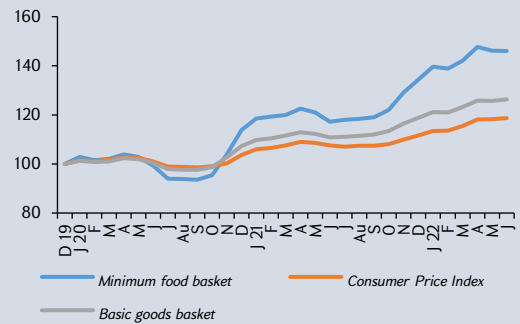
In terms of evaluating the social impact of changes in expenses, it is highly important to review the impact of changes in the prices of the minimum food basket and basic goods basket on vulnerable groups (first 4 decile groups) during the relevant period. First, since the beginning of 2020, the value of minimum food and basic goods baskets¹⁰ has grown by 46% and 26.3% respectively, while the value of the general consumer basket in the same period has grown by 18.7%.

Taking into account evaluations of the above-mentioned baskets¹¹ by the National Statistics Committee, it can be concluded that the growth of prices of the minimum food basket and the basic goods basket exceeds the growth of income several times, especially for social groups that are their main consumers.

It is noteworthy that recently, in the context of high external demand and large capital and financial inflows, appreciation of the AMD has had its positive effect not only in terms of general inflation, but also in terms of cost containment, especially in vulnerable segments. Thus, it is estimated that given unchanged exchange rate, the growth of the minimum food basket and basic goods basket would be about 4 percentage points higher. Subsequently, in order to curb high inflation, it would be necessary to implement extremely restraining policy by raising the refinancing rate.

Chart 25

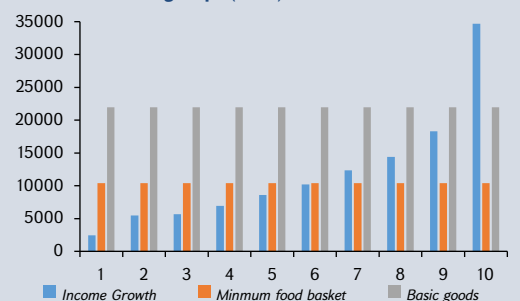
The growth of prices of the minimum food basket and essential goods basket outpaced that of the consumer basket (%)



Source: NSS, CBA estimates

Chart 26

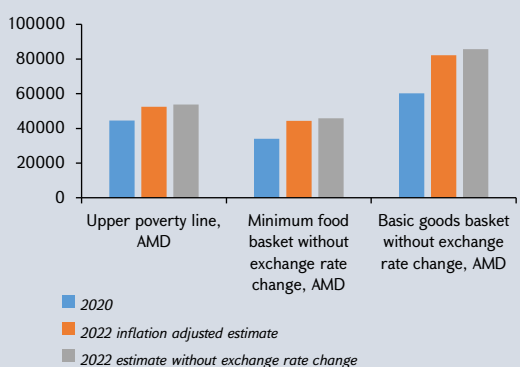
The growth of prices of the minimum food basket and basic goods basket was several times higher than the growth of income, particularly within the main consumer social groups (AMD)



Source: NSS, CBA estimates

Chart 27

If the exchange rate remained unchanged, the growth in prices of the minimum food basket and basic goods basket would be higher (AMD)



Source: NSS, CBA estimates

Import Prices. In the second quarter of 2022, a certain acceleration of food prices was observed worldwide, reflected in Armenia by the growth of import prices in USD terms. As a result of the growth of import prices of intermediate consumption goods,

¹⁰ In order to approximate the dynamics of the prices of products included in the baskets, products included in the minimum food basket calculated by the RA SC were used according to their weight in the consumer basket.

¹¹ Republic of Armenia economic performance in January-June 2022.

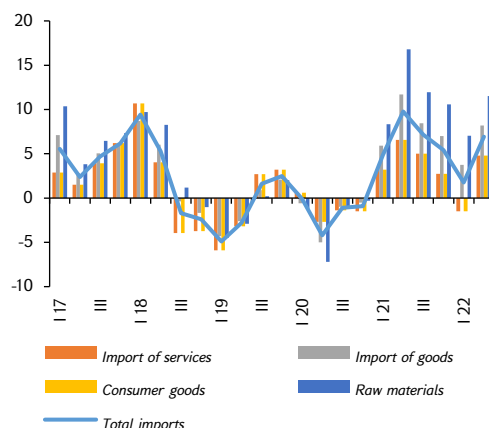
consumer goods and services grew as well. Thus, during the second quarter, import prices in USD terms grew by 5.7% compared to the previous quarter, with subsequent 6.9% y/y growth of prices compared to the same period of the previous year.

These growth of 6.9% was mainly contributed by the y/y growth in the prices of oil, wheat and sugar. Moreover, a y/y growth was observed in terms of almost all imported intermediate consumption goods. The growth of consumer goods prices in US\$ terms over the same quarter of the previous year was mainly conditioned by the sharp appreciation of the nominal exchange rate of Russian ruble against the US dollar.

The growth of import prices, parallel to the high domestic demand, was expressed by around 9.0% y/y growth of prices of imported goods in the consumer basket.

Chart 28

In 2022 Q2, the growth of dollar prices for imports of goods and services accelerated compared to the same quarter of the previous year, y/y, %



Source: CBA estimates

3.2. Economic Developments

3.2.1. Economy Position

During the reporting period, positive GDP gap expanded. In the second quarter of 2022, economic growth totaled 13% (see section 3.2.3), strongly above the Central Bank's previous projection. The main contributor of the high growth was the services sector affected by external demand, where the growth was much higher than expected. In addition, due to supply factors (capital and productivity growth in the industry and IT sector), the potential level of GDP has also expanded. As a result, the GDP gap has grown over the previous quarter, and it is estimated that it will remain in the positive range until the end of the year.

In the second quarter of 2022, economic growth totaled 13%.

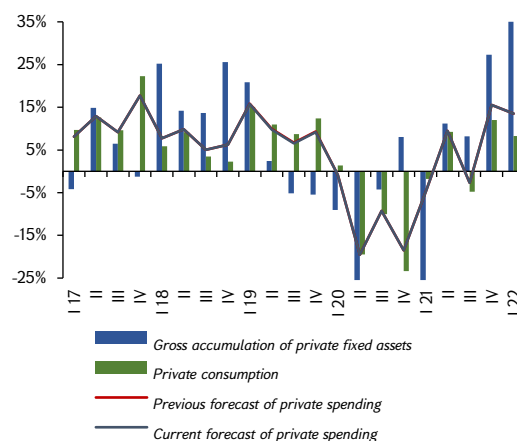
3.2.2. Expenditure Side of the Economy

In terms of domestic demand, the growth is strongly contributed by both domestic and foreign demand.

While during the first two quarters of 2022, the growth of private expenditures was in line with expectations, its structure has changed somewhat. Thus, due to the developments in the construction and manufacturing sectors, the growth of private fixed assets was higher than expected, totaling 35.5%, and the growth of private consumption

Chart 29

Private spending structure (y/y growth)



Source: NSS, CBA estimates

exceeded the estimated level, totaling 10.3%. According to the CBA estimates, the latter is also caused by the decrease in private savings due easing of restrictions related to international visits.

During the second quarter of 2022, amid the more positive than expected developments in the global and domestic economies, the real growth of exports and imports exceeded expectations. Under the restrictions on exports from other countries to the Russian Federation, a high growth of exports from Armenia to Russia was observed, amid certain weakening of the previous competitive environment in markets and the opening of new positions. With the unprecedented high growth in the number of international visitors, tourism developments have exceeded expectations. At the same time, driven by the domestic demand fast recovery, imports of goods and services exceeded expectations as well. Thus, in the second quarter of 2022, the growth of real exports of goods and services was 18.5% y/y, and the growth of the real import of goods and services was 18.4% y/y.

Summing up, the contribution of net real exports to GDP in the second quarter was less negative than projected.

According to estimates the decrease in the dollar value of net remittances (seasonal workers income and personal transfers) in the second quarter of 2022 will be smaller than estimated in the CBA program of the previous quarter, about 2.0% y/y. This is due to the less than expected decline of the Russian economy.

Fiscal Policy¹². Actual budget revenues in the second quarter of 2022¹³, shifted more in the direction of overperformance and expenditures - the shortfall. As a result, the impact of the fiscal policy on aggregate demand in the quarter was in line with the forecast and is estimated to expand by 0.6 percentage points.

Budget revenues in the second quarter of 2022 accounted for 105.1% of the CBA's projections mostly due to the surplus of tax revenues. Due to high economic growth and inflation, tax revenues exceeded the estimates of the Central Bank by 5.2%.

As a result of the increase of tax revenues, which was mainly in line with the nominal economic growth, revenue impulse was 0.2 percentage point expanding, which is in line with the previous estimate.

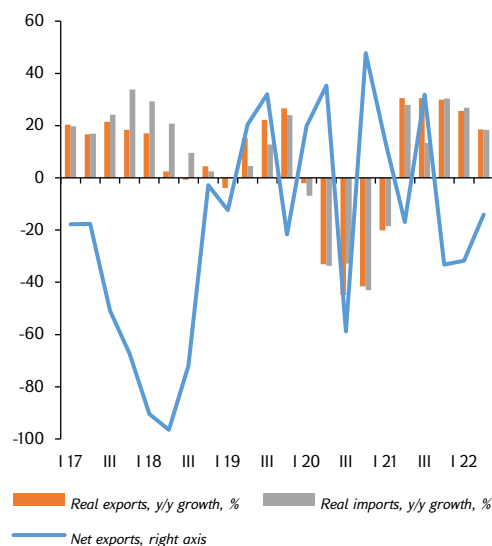
State budget expenditures in the second quarter totaled 99.1% of the Central Bank forecast, and net lending was within the projected

¹² The review of the fiscal sector was based on the actual consolidated budget indicators at the first quarter.

¹³ Revenue program is based on the current 2022 Government adjusted program. Expenditures are the CBA estimate.

Chart 30

In 2022 Q2, net exports position deteriorated (net real exports, y/y, %, positive sign - improvement)

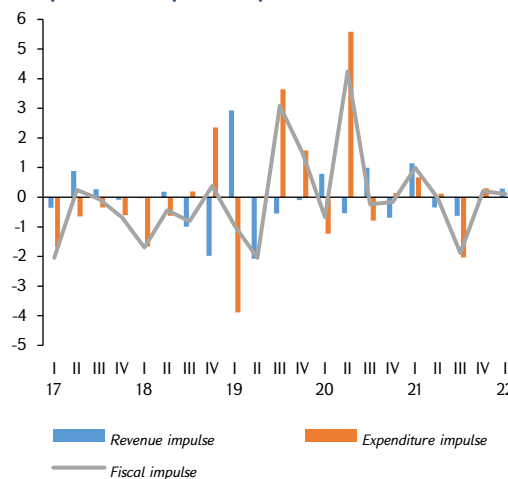


Source: NSS

The impact of the fiscal policy on aggregate demand in the second quarter was in line with the forecast and is estimated to expand by 0.6 percentage points.

Chart 31

Fiscal policy in the first quarter of 2022 had a neutral impact over the previous quarter



Source: CBA estimate

range. As a result, instead of the projected 1.2 percentage point, expenditure impulse was 0.7 percentage point expanding over the previous quarter. Within the state budget, expenditures on non-financial assets were fell short of the plan. Both internal and external capital expenditures underperformed, yet foreign financed expenditures' underperformance was deeper. As a result, of the above-mentioned developments, when revenues' performance exceeded that of expenditures, the state budget had a surplus of 11.2 billion drams in the second quarter. The surplus of the consolidated budget was about AMD 45.3 billion.

To summarize, in the second quarter of 2022, a mostly neutral impact of fiscal policy on demand and inflation was observed.

3.2.3. Output Side of the Economy

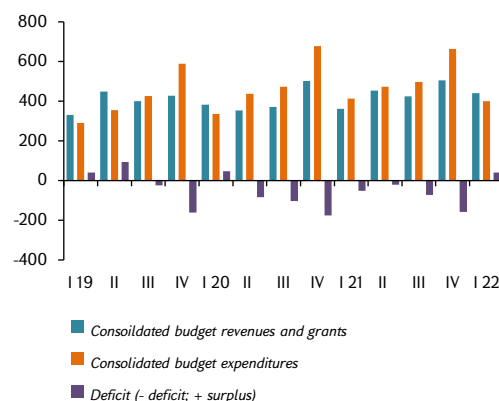
The high economic growth in the second quarter of 2022 compared to the previous estimate of the Central Bank, was mostly the result of relatively high growth in the services and construction sectors. A 20.1% growth in the services sector was greatly contributed by the high growth of the financial and insurance sector. In addition, against the background of the acceleration of both foreign and domestic demand, growth in other sectors of services continued. Furthermore, a 30.2% growth in the construction industry related to the large-scale construction in the real estate and transportation sectors. Due to the small growth in the crops sub-sector, decline in the agriculture sector was smaller than expected (1.5%). Developments of the industrial sector were close to the estimates of the Central Bank as 5.4% growth was observed. Negative contribution of the mining sector to the growth of the sector continued, but the problems in the sector have been somewhat smoothed. Positive developments continued in the processing industry, particularly in the spheres of food, beverages and basic metals production. The latter was expressed also in the high growth of export of this sector.

3.2.4. Labor Market

In the second quarter of 2022, the unemployment is estimated at around 13.8%, which is lower than the previous estimate of the Central Bank. The decrease in the level of unemployment is mainly due to the growth of demand and economic activity and, subsequently, employment. The high growth of private wages and the decrease of the

Chart 32

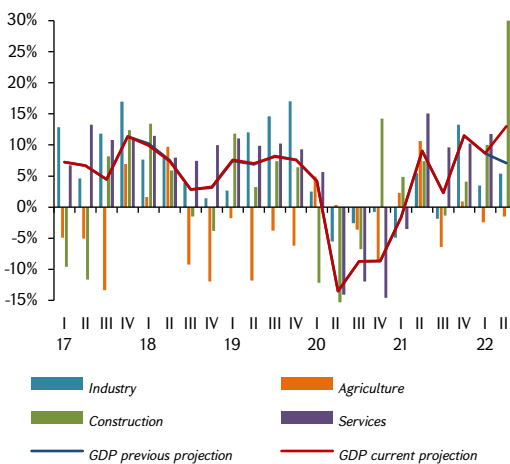
In 2022 Q1, state budget surplus was observed (AMD billion)



Source: NSS

Chart 33

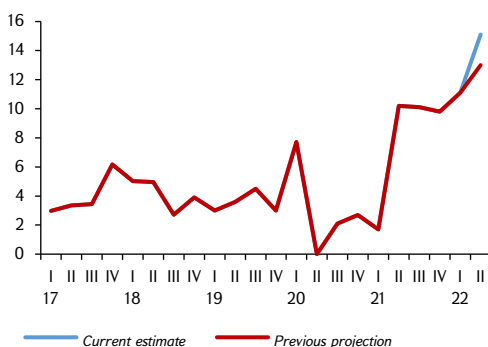
GDP Sectoral Structure (y/y growth, %)



Source: NSS, CBA estimates

Chart 34

In the first quarter of 2022, a surplus of the state budget was formed (AMD billion)



Source: NSS, CBA estimate

unemployment rate reflect the actual positive GDP gap and a high inflationary environment during the reporting period.

Compared to the Central Bank projection, the growth of private sector's nominal wages in the reporting quarter was quite high and amounted to 15.1% due to the higher-than-expected growth of economic activity. Private wages grew mainly in the service sector, reflecting the significant increase in demand and output volumes. In line with the inflation trends, the growth of real wages in the private sector in the second quarter was about 6%.

Reflecting the outpacing growth of private wages over the output per employee, unit labor costs of enterprises have somewhat increased. As a result, in the second quarter inflationary pressures from the labor market continued.

3.3. Financial Market Developments

In the second quarter of 2022, the Central Bank Board left the refinancing rate unchanged, at 9.25%.

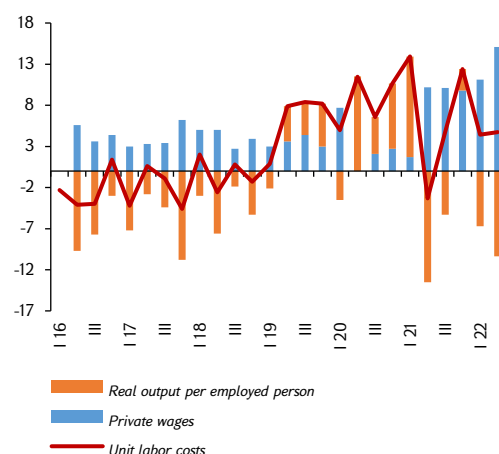
Given the persistence of inflationary environment effects transmitted from the external sector and a certain mitigation of that effect in terms of dram appreciation, and assessing satisfactory the effect of tightening by the large step of monetary conditions in the previous quarter in the current scenario, the Central Bank Board refrained from changing the interest rate in the second quarter. Given geopolitical developments, the Central Bank Board has further announced its readiness to take adequate actions in the event of high uncertainties related to the macroeconomic outlook, in order to stabilize inflation and neutralize the risks of deanchoring of inflation expectations.

Average quarterly interest rates in Armenia's financial market								
Indicators	04.08.21-14.09.21	15.09.21-02.11.21	03.11.21-14.12.21	15.12.21-01.02.22	02.02.22-15.03.22	16.03.22-03.05.22	04.05.22-14.06.22	15.06.22-02.08.22
Central Bank refinancing rate (end of quarter)	7.00	7.25	7.25	7.75	8.00	9.25	9.25	9.25
Central Bank repo rate	7.34	7.55	7.44	7.93	8.20	9.46	9.51	9.53
Interbank repo rate (up to 7-day)	7.14	7.84	7.05	7.68	8.14	9.39	9.65	9.55

¹⁴ Productivity In unit labor costs is represented by a negative contribution.

Chart 35

Unit labor costs growth, y/y (%)¹⁴

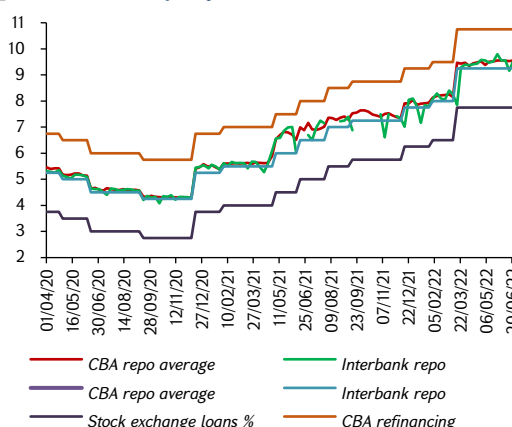


Source: NSS, CBA estimate

In the second quarter of 2022, the Central Bank Board left the refinancing rate unchanged, at 9.25%.

Chart 36

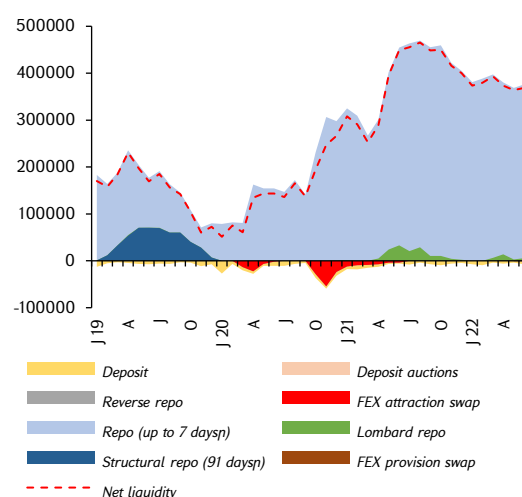
During the quarter, short-term interest rates stayed around the CBA policy rate



Source: CBA

Chart 37

Liquidity absorbed and injected through CBA transactions average monthly stock, AMD million



Source: CBA

Yield of government securities on a yield curve (as of end-quarter)								
Treasury bills (1 year)	8.18	8.58	8.84	9.02	9.08	10.13	10.25	10.41
Notes (5 year)	9.37	9.71	9.82	9.90	9.93	10.97	10.87	10.98
Bonds (30-year)	10.03	10.14	10.08	10.17	10.25	11.20	11.26	11.59

Source: CBA

During the second quarter of 2022, the financial system was characterized by a high level of liquidity and capital. The developments in financial market, including appreciation of the Armenian dram, were strongly affected by the large influx of international visitors and financial transfers. The Central Bank continued to provide commercial banks with the necessary amount of liquidity through the main instrument, while contributing to the formation of short-term market interest rates around policy rate.

Despite the unchanged level of policy rate during the quarter and the available liquidity in the financial system, the uncertainties in government bond market were expressed mainly in the short-term segment of the yield curve: relatively small demand for short-term bonds was accompanied by an increase in yields. Investors' expectations were anchored in the medium-term sector, and in the long-term sector, a small increase in yields was also observed. As a result, compared to the previous quarter, the upward movement of the yield curve at the end of June was on average 0.3 percentage points due to the increase in the yield of short-term and long-term bonds.

During the second quarter of 2022, parallel to expansion of funds attracted and provided by commercial banks expanded, decline in interest rates of foreign exchange funds was observed. This reflects the high level of foreign exchange liquidity in the banking system in the context of a large-scale foreign exchange inflow.

According to the lending conditions survey¹⁵, growth of price of the attracted resources and tightening of the regulatory field during the quarter had a restraining effect on lending conditions of banks and credit organizations. The observed slight positive effect was factored by general economic activity. At the same time, compared to the previous quarters, expectations regarding the levels of credit supply and demand have improved significantly. Total lending grew by 2.0% on a 12-month basis in June 2022, with mortgage lending growth continuing to be quite strong.

¹⁵ The survey of commercial banks and credit organizations on credit conditions is carried out quarterly. The survey for the second quarter of 2022 was conducted between July 8-18 this year.

Chart 38

In 2022 Q2, government bond yields grew both along all segments of the curve, more markedly in the short-term and long-term sectors

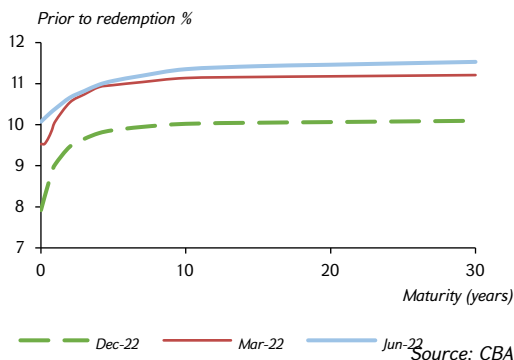


Chart 39

Dynamics of the CBA refinancing rate and government bonds yields

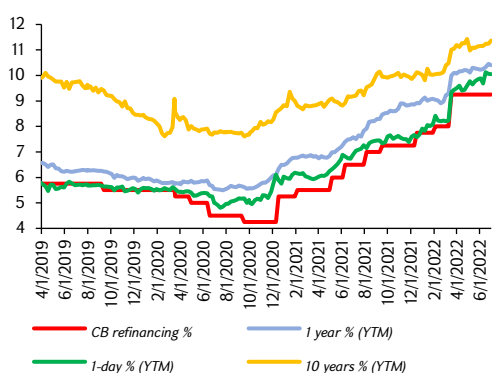
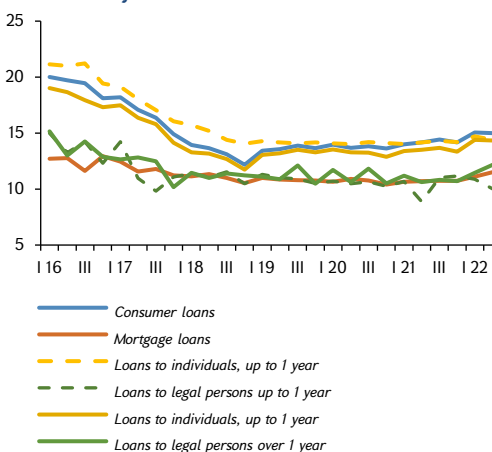


Chart 40

In the second quarter of 2022 lending rates grew only for mortgage and legal entity loans with a maturity of more than 1 year



The foreign exchange market was also active in connection with the events taking place in the financial market. Due to the large inflow of international visitors and financial flows to Armenia, appreciation of the Armenian dram that started in mid-March, continued during the second quarter of 2022. The average quarterly appreciation of the AMD/US dollar exchange rate was 8.1%, and the AMD/Russian ruble exchange rate depreciated by 16.6% due to the significant appreciation of the ruble against the US dollar in the Russian currency market. Given the large-scale of inflows as compared to the size of the Armenian currency market, the Central Bank had a situational intervention in the currency market, contributing to sustainable operation of financial markets and neutralization of short-term disruptions and emerging problems. As a result, during the second quarter, the volume of net purchases of US dollars by the Central Bank totaled US\$ 167.0 million.

Chart 41

12-month dynamics of banks' lending

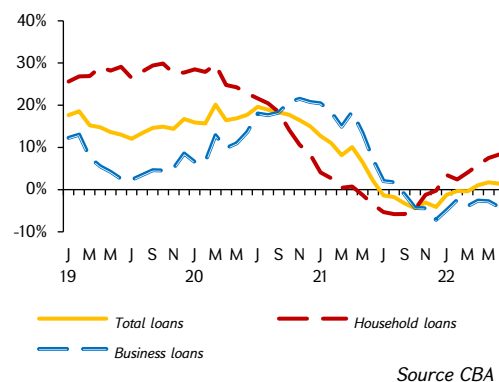
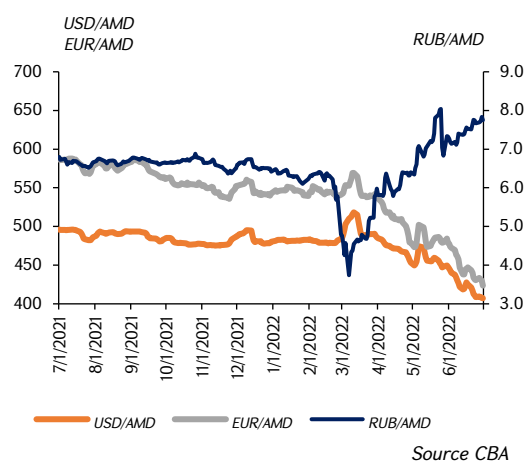


Chart 42

Exchange rates of different currencies against the AMD



4. SUMMING UP

According to the monetary policy program of the Central Bank of Armenia for the third quarter of 2022, the existing large demand will significantly contribute to persistence of high inflationary environment and inflationary expectations, hence, the 12-month inflation will stay above the target in the near future. In the short term, within inflation factors, impacts of demand, which are mainly manifested in the service sector, will prevail, with a significant increase in external demand due to the considerable inflow of international visitors and tourists and financial flows. In view of the above, the Central Bank raised policy rate at this stage. In the meantime, the Central Bank will consistent in taking adequate actions to stabilize inflation and to offset any risk of deanchoring of inflation expectations. In the medium term due to the implemented monetary policy the inflation will gradually decline and from the end of 2023 ***will stabilize around the 4% target.***

The risks of deviating from the projected inflation trajectory in the forecast horizon are balanced, and in case of their emergence the Central Bank stands ready to respond accordingly, in order to ensure the achievement of the medium-term price stability objective.

BOARD MEETING OF THE CBA

MINUTES (13.09.2022)

On the Refinancing Rate

The CBA Board Meeting of September 13, 2022 attended by CBA Governor M. Galstyan, Deputy Governors N. Yeritsyan and H. Khachatryan, and Board Members H. Ghahramanyan, D. Nahapetyan, A. Manukyan and L. Sahakyan

The Board meeting opened with presentation of the Situation Report as of September 13, 2022. It addressed the developments on inflation, external environment, and real, fiscal, financial and monetary sectors of the economy, at the same time taking into account the additional uncertainties as a result of the military operations on the Armenian-Azerbaijani border that started on the same day and their possible impacts.

As noted, in August 2022 0.2% inflation was recorded, against 0.4% inflation in the same month of the previous year. The month's inflation was mainly contributed by the growth of prices of non-food products and services by 0.4% and 0.6%, respectively, while food prices dropped by 0.2%. As a result of a significant growth of demand in the services sector, particularly large increase was recorded in the prices of products of “Recreation and Culture”, “Restaurants and Hotels”, “Housing services” and “Various Goods and Services” subgroups: 1.0%, 0.7%, 0.6% and 1.5% respectively (total contribution to inflation: 0.22 percentage points). The decrease in the prices of food products was mainly due to the decrease of the prices of “Fruit” and “Oils and Fats” sub-groups by 5.7% and 2.3%, respectively, which restrained the monthly inflation by 0.24 percentage points. At the same time, the prices of the subgroups “Dairy, Cheese and Eggs” and “Meat” grew by 1.2% and 0.8%, respectively (total contribution to inflation: 1.15 percentage points). ***As a result of these changes, the 12-month inflation slightly dropped to 9.1% at the end of the month. The 12-month core inflation continued to grow, totaling 10.2%.***

Current developments in the external sector were presented. As noted, in the third quarter, the trends of low economic activity and high inflation persisted in the global economy, and particularly the main partner countries of Armenia. The consistent monetary policy conducted by the central banks of partner countries of Armenia, in the contest of restraint economic activity and demand, contributes to

alleviation of the global inflationary environment, as well as to a certain drop of prices in international commodity market. At the same time, as a result of price shifts of energy carriers, risks of expanding inflation have emerged in Armenia's EU partner countries. It was noted that in the sustained high inflation environment, the central banks of developed countries will continue to conduct contractionary monetary policy, which will contribute to the alleviation of inflationary effects from the external sector.

The Board reviewed developments of the RA economy, it was noted that due to the high growth of the services and construction sectors, high economic activity continued in the third quarter of 2022. Positive developments also continue in the IT and manufacturing industry sectors, reflecting a certain growth in export and economic growth potential. In view of these developments, the Central Bank revised the economic growth forecast for 2022 and expects a significantly higher figure. However, it was noted that high economic growth was mainly contributed by demand factors, resulting from the large-scale inflow of international visitors and tourists, as well as financial flows. At the same time, it was stated that given the high aggregate demand, implementation of monetary and fiscal contractionary policies is crucial, the latter particularly in the context of tightening tax administration and adjusting the relevant tax policy.

The developments of the RA financial market were discussed and it was noted that in the third quarter, short-term market interest rates continued to shape around the policy rate. Due to the significant increase in the demand for domestic services by international visitors and the large financial inflow, in the second and third quarters an appreciation of the dram in RA foreign exchange market has been observed.

Concerning inflationary developments, the Board stated that while the external inflationary effects have somewhat weakened and inflationary expectations of households alleviated, the high demand existing in the domestic economy due to the sustained large influx of international visitors and tourists, significantly contributes to the expansion of the domestic inflationary environment and the persistence of high inflationary expectations.

It should be noted that the Board considered all the discussed issues in the context of the possible effects and risks of the military operations started on the Armenian-Azerbaijani border on the day of the session. In the context of uncertainty regarding the situation, the discussion mainly focused on the scenario of a certain weakening of economic activity and the emergence of

possible risks of inflationary factors. If as a result of the operational monitoring of the Central Bank, risks are identified in any direction, the policy will be adjusted accordingly.

After reviewing the Situational report and external and internal macroeconomic developments, the Board proceeded to the discussion of macroeconomic scenarios, monetary policy directions and the decision on policy rate. Forecasting team presented to the Board scenarios of future economic developments in the macroeconomic situation above described, including the relevant actions of monetary policy. According to some members of the Board, the existing positive high demand will significantly contribute to the expansion of inflationary environment in the near future, hence it is necessary to continue consistent tightening of monetary policy by raising policy rate. Other Board members considered that the weakening of inflationary effects from the external sector, the appreciation of the dram and the previous actions of the Central Bank policy have been already reflected in the dynamics of positive demand adjustment and plummeting of inflation and inflationary expectations, hence changing the monetary conditions at this stage was not feasible. ***Subsequently, the Central Bank Board decided by the majority of votes to raise refinancing rate by 0.5 percentage points.*** To this end, the Board emphasized its tenacity in ensuring stabilization of inflation with adequate actions and neutralizing any risk of deanchoring inflationary expectations. Under such policy measures, the 12-month inflation would be reduced and stabilize around the 4% target from the end of 2023.

The Board considers that the risks of inflation deviation from the projected trajectory are mainly balanced. In case of risks materialize in any direction, the Board stands ready to respond accordingly in fulfilment of the price stability objective.

The Board approved the decision on interest rates of monetary instruments of the Central Bank and the proposed press release, which are attached.

THE CENTRAL BANK OF THE REPUBLIC OF ARMENIA

BOARD DECISION

ON ESTABLISHMENT OF INTEREST RATES OF MONETARY POLICY INSTRUMENTS OF THE CENTRAL BANK OF ARMENIA AND PRESS RELEASE ON REFINANCING RATE

By virtue of Article 2(3), Article (20) “c” and “e” of the law “On the Central Bank of the Republic of Armenia”, and provisions of the Republic of Armenia law “On Normative Legal Acts”, the Board of the Central Bank of the Republic of Armenia enacts:

1. Set the refinancing rate of the Central Bank of the Republic of Armenia at 10.0%.
2. Set the Lombard repo facility rate offered by the Central Bank of the Republic of Armenia at 11.5%:
3. Set the deposit facility rate offered by the Central Bank of the Republic of Armenia at 8.5%.
4. Approve the press release on the refinancing rate of the Central Bank of the Republic of Armenia (attached).
5. This decision shall enter into force on the day following the day of its publication on the website of the Central Bank of the Republic of Armenia.

Martin Galstyan,
Governor of the Central Bank September 13, 2022

PRESS RELEASE
13.09.2022

At September 13, 2022 meeting, the CBA Board decided to raise the policy rate by 0.5 percentage points setting it at 10%.

In August 2022, 12-month inflation decreased to 9.1% at the end of the month. 12-month core inflation continued to grow reaching 10.2%.

In the third quarter of 2022, low economic growth and high inflation continued to sustain in the main partner countries of Armenia. The central banks of advanced countries will continue to conduct contractionary monetary policy. This will be reflected in the tightening of global financial conditions and in slowing of economic activity. Subsequently, a certain drop of prices will be observed in the international commodity markets, contributing to the gradual easing of the global inflationary environment. Hence, it is expected that inflationary effects from the external sector will subdue.

During the third quarter of 2022, high economic activity continued to be observed in Armenia. It mostly is witnessed in services and construction sectors. Positive developments continue in the export sector as well. High economic growth is predominantly driven by the demand factors. Again, its main contributors are the significant influx of international visitors and remittances. High demand contributes to the expansion of the inflationary environment and persisting high inflationary expectations.

In the current situation, the Board finds it appropriate to raise the policy rate. Relatively contractionary monetary policy and dram appreciation will gradually contribute to curbing demand and reducing inflationary expectations. The CBA Board is consistent in taking adequate actions to stabilize inflation and to offset any risk of deanchoring of inflation expectations. In line with the outlined monetary policy scenario, the 12-month inflation will gradually decline and from the end of 2023, will stabilize around the 4% target.

The CBA Board considers that the risks of inflation deviation from the projected trajectory are mainly balanced. Should the risks materialize in any direction, the Board stands ready to respond accordingly in fulfilment of the price stability objective.

CBA Public Relations Service

ARMENIA: SELECTED MACROECONOMIC INDICATORS

Indicators	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025
	actual	actual	actual	actual	actual	actual	actual	program	program	program	program
External sector											
USA economic growth (% <i>real growth</i>)	2.7	1.7	2.3	2.9	2.3	-3.4	5.8	1.6	1.4	2.7	2.9
Eurozone economic growth (% <i>real growth</i>)	1.9	1.8	2.7	1.9	1.3	-6.5	5.4	3.3	1.1	0.5	1.1
Russia economic growth (% <i>real growth</i>)	-1.9	0.2	1.8	2.8	2.0	-2.9	4.7	-4.2	-2.3	2.1	1.5
USA inflation (<i>average</i> , %)	0.1	1.3	2.1	2.4	1.8	1.2	4.7	8.1	5.1	2.2	1.6
Eurozone inflation (<i>average</i> , %)	0.0	0.2	1.5	1.7	1.2	0.3	2.6	7.8	5.6	2.9	2.0
Russia inflation (<i>average</i> , %)	14.4	6.8	3.6	2.8	4.4	3.3	6.7	14.0	8.5	5.8	4.6
Oil price (US\$/barrel)	53.5	45.0	54.6	71.4	64.1	42.5	71.0	101.5	98.3	102.2	104.1
Copper price (US\$/barrel)	5497.4	4867.6	6201.5	6544.7	6024.1	6191.2	9314.7	8820.9	8740.6	9301.1	9766.2
FAO index	93.0	91.9	98.0	95.9	95.0	98.0	125.7	144.9	142.1	145.8	148.4
Domestic economy											
Prices											
Inflation (y/y, <i>end of period</i> , %)	-0.1	-1.1	2.6	1.8	0.7	3.7	7.7	10.3	4.0	3.4	4.0
Consumer price index (y/y, <i>average</i> , %)	3.7	-1.4	1.0	2.5	1.5	1.2	7.2	8.6	7.0	3.5	4.0
Core inflation (y/y, <i>average</i> , %)	5.1	-2.0	0.8	4.0	1.2	1.3	7.2	8.7	6.7	4.5	4.0
Gross product											
GDP (<i>billion Armenian dram</i>)	5043.6	5067.3	5568.9	6017.0	6543.3	6181.7	6983.0	8430.3	9156.8	9922.6	10746.6
GDP (% <i>real growth</i>)	3.2	0.2	7.5	5.2	7.6	-7.4	5.7	12.9	4.4	4.2	4.1
Supply											
Industry (% <i>real growth</i>)	6.2	7.7	11.7	4.9	12.0	-1.7	3.5	3.2	5.3	4.9	5.0
Agriculture (% <i>real growth</i>)	13.2	-5.0	-5.1	-6.9	-5.8	-4.1	-0.6	3.2	2.8	3.2	2.8
Construction (% <i>real growth</i>)	-3.1	-14.1	2.8	0.6	6.5	-6.7	3.1	14.1	7.8	5.5	5.3
Services (% <i>real growth</i>)	1.6	3.2	10.6	9.1	10.0	-9.7	7.9	19.4	4.0	3.9	3.9
Taxes, net (% <i>real growth</i>)	-5.1	-3.7	9.7	8.0	7.1	-10.0	7.4	10.1	4.7	4.5	4.2
Demand											
Consumption (% <i>real growth</i>)	-6.0	-2.1	11.6	3.8	11.7	-10.9	4.2	11.0	2.3	4.1	4.0
Public consumption (% <i>real growth</i>)	4.7	-2.4	-2.1	-3.0	12.9	9.2	8.4	-1.8	-6.9	5.8	3.7
Private consumption (% <i>real growth</i>)	-7.5	-2.1	14.0	4.8	11.5	-14.0	3.4	13.8	4.3	3.8	4.0
Gross accumulation of fixed assets* (% <i>real growth</i>)	2.5	-11.4	9.7	4.8	4.4	-1.5	6.3	19.6	10.6	5.6	5.2
Public investment** (% <i>real growth</i>)	13.6	5.0	31.7	-37.4	31.1	16.2	-9.9	17.4	26.5	4.2	3.5
Gross accumulation of private fixed assets (% <i>real growth</i>)	1.2	-13.9	6.2	19.6	-0.5	-5.7	11.2	20.2	7.2	5.9	5.7
Export of goods and services (% <i>real growth</i>)	4.9	21.3	19.3	5.0	16.0	-33.4	17.1	27.9	19.0	4.7	4.3
Import of goods and services (% <i>real growth</i>)	-15.3	6.3	24.6	13.3	11.6	-31.4	12.5	24.3	15.3	4.1	4.0
Current account											
Balance of trade (<i>million US dollar</i>)	-1186.4	-976.9	-1400.9	-1724.4	-1727.9	-1382.2	-1594.3	-2046.0	-2159.4	-2176.1	-2186.0
Balance of services (<i>million US dollar</i>)	-96.4	70.4	159.4	24.7	-66.9	118.0	398.0	702.8	538.8	510.4	462.8
Remittances (<i>million US dollar</i>)	1098.3	1009.4	1179.3	1136.2	1143.8	1046.2	1295.2	1208.5	1086.9	1032.9	987.5
Current account (<i>million US dollar</i>)	-284.7	-107.9	-173.9	-875.9	-1002.3	-477.8	-551.5	-658.0	-1057.0	-1156.1	-1259.0
Balance of trade (<i>share in GDP</i> , %)	-12.2	-8.6	-10.8	-13.7	-13.1	-10.0	-8.6	-7.0	-8.1	-7.7	-7.3
Balance of services (<i>share in GDP</i> , %)	-0.9	0.7	1.4	0.2	-0.5	0.9	2.8	3.7	2.7	2.3	2.0
Remittances (<i>share in GDP</i> , %)	10.4	9.5	10.2	9.1	8.4	8.3	9.3	6.3	5.4	4.8	4.2
Current account (<i>share in GDP</i> , %)	-2.7	-1.0	-1.5	-7.0	-7.3	-3.8	-3.9	-3.4	-5.3	-5.3	-5.4

Items	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025
	actual	actual	actual	actual	actual	actual	actual	program	program	program	program
Public sector***											
Revenues and grants (billion Armenian dram)	1167.7	1171.1	1237.8	1341.7	1559.1	1560.4	1683.8	2000.9	2253.8	2537.6	2856.5
Tax revenues (billion Armenian dram)	1067.9	1079.7	1158.0	1258.1	1464.3	1385.2	1586.9	1900.0	2176.4	2467.0	2790.3
Expenditures (billion Armenian dram)	1409.0	1449.1	1504.8	1447.1	1623.0	1894.3	2004.3	2112.1	2546.0	2810.9	3138.9
Deficit (billion Armenian dram)	-241.3	-278.0	-267.0	-105.4	-63.9	-333.9	-320.5	-111.2	-292.2	-273.3	-282.4
Revenues and grants (share in GDP, %)	23.2	23.1	22.2	22.3	23.8	25.2	24.1	23.7	24.6	25.6	26.6
Tax revenues (share in GDP, %)	21.2	21.3	20.8	20.9	22.4	22.4	22.7	22.5	23.8	24.9	26.0
Expenditures (share in GDP, %)	28.0	28.6	27.0	24.1	24.8	30.6	28.7	25.1	27.8	28.3	29.2
Deficit (share in GDP, %)	-4.8	-5.5	-4.8	-1.8	-1.0	-5.4	-4.6	-1.3	-3.2	-2.8	-2.6
Monetary sector											
Broad money (y/y, end of period, %)	10.8	17.5	18.5	7.5	11.2	9.0	13.1	-	-	-	-
Dram broad money (y/y, end of period, %)	5.2	24.8	28.9	13.2	21.5	14.8	12.8	-	-	-	-
Loans to economy (y/y, end of period, %)	-3.3	6.0	16.5	17.2	18.5	14.3	-3.9	-	-	-	-
USD/AMD (Armenian dram for one US dollar)	477.9	480.5	482.7	483.0	480.4	489.0	503.8	-	-	-	-
<p>* Hereinafter, the Central Bank will only present the indicator of the aggregate fixed asset accumulation instead of the aggregate accumulation, since the change in tangible working capital inventories is considered by Armenia's Statistics Committee as a balancing item and it does not show the true level of the aggregate accumulation. See https://www.armstat.am/file/article/sv_04_19a_112.pdf.</p> <p>** Actual indicators of public investment are capital expenditures of the consolidated budget, and the forecasts are based on the currently revised macro framework for 2022-2024.</p> <p>*** Indicators of the 2022 state budget are the CBA estimates. The source of 2023-2024 indicators is the Government MTEFP.</p>											

CHARTS

Chart 1	Inflation (12-month) projection probability distribution for 3-year horizon	5
Chart 2	Real GDP growth (cumulative) forecast probability distribution for 3-year horizon	5
Chart 3	US economic growth projections	7
Chart 4	EU economic growth projections	8
Chart 5	Russia economic growth projections	9
Chart 6	Inflation in partner countries	9
Chart 7	International copper price projections	10
Chart 8	International oil price projections	10
Chart 9	International food price projections	11
Chart 10	Inflation (12-month) forecast probability distribution for 3-year horizon	12
Chart 11	Contribution of demand components to growth	13
Chart 12	Flows of real exports and imports of goods and services in the medium term	14
Chart 13	Nominal wage growth in private sector, y/y	15
Chart 14	Level of unemployment	15
Chart 15	Unit labor costs growth, y/y	16
Chart 16	Real GDP growth (cumulative forecast probability distribution for 3-year horizon)	16
Chart 17	Current account/GDP medium-term projections	17
Chart 18	Fiscal impulse projection (percentage point)	17
Chart 19	Short-term inflation expectations	17
Chart 20	Household inflation expectation surveys	18
Chart 21	Scenarios of economy response to external demand shock	23
Chart 22	During the period under review, dynamics of the 12-month inflation were generally in line with the outlined direction; only in the second quarter of 2022 the expected level was significantly exceeded, and subsequently, the short-term projections for the given quarter were revised upwards	24
Chart 23	Some mitigation of the inflationary environment in late 2021 was followed by its sharp increase in the second quarter of 2022	26
Chart 24	Compared to 2020, expenses growth has exceeded income growth in almost all decile groups	27
Chart 25	The growth of prices of the minimum food basket and basic goods basket outpaced that of the consumer basket	28
Chart 26	The growth of prices of the minimum food basket and basic goods basket was several times higher than the growth of income, particularly within the main consumer social groups	28
Chart 27	If the exchange rate remained unchanged, the growth in prices of the minimum food basket and basic goods basket would be higher	28
Chart 28	In 2022 Q2, the growth of dollar prices for imports of goods and services accelerated compared to the same quarter of the previous year	29
Chart 29	Private spending structure	29
Chart 30	In 2022 Q2, net exports position deteriorated	30
Chart 31	Fiscal policy in the first quarter of 2022 had a neutral impact over the previous quarter	30
Chart 32	In the first quarter of 2022, a surplus of the state budget was formed	31
Chart 33	GDP Sectoral Structure	31
Chart 34	Private nominal wages	31

Chart 35	Unit labor costs	32
Chart 36	During the quarter, short-term interest rates stayed around the CBA policy rate	32
Chart 37	Liquidity absorbed and injected through the CBA transactions	32
Chart 38	In 2022 Q2, government bond yields grew both along all segments of the curve, more markedly in the short-term and long-term sectors	33
Chart 39	Dynamics of the CBA refinancing rate and government bonds yields	33
Chart 40	In the second quarter of 2022 lending rates grew only for mortgage and legal entity loans with a maturity of more than 1 year	33
Chart 41	12-month dynamics of banks' lending	34
Chart 42	Exchange rates of different currencies against the AMD	34

TABLES

Table 1	Inflation Interval Projection Probability Distribution	12
Table 2	Probability Distribution of Real GDP Growth (Cumulative) Projection	17
Table 3	Projection assumptions	18
Table 4	Consumer price inflation by commodity items as key contributors	27
Table 5	Average interest rates in Armenia's financial market	32