

Financial Stability Report (2014 annual report)

2015-05-05

This Financial Stability Report presents an assessment of potential risks that could threaten the stability of financial system of the Republic of Armenia as well as the capacity of the financial system to absorb such risks. More detailed information on Armenia's macroeconomic environment and financial system analyses is available in the Central Bank's periodicals, such as Annual Report of the Central Bank, Status Report on Monetary Policy Implementation and Armenian Financial System: Development, Regulation, Supervision.

PREFACE

The main risks affecting financial stability of Armenia persisted during 2014, meanwhile the impact of a set of risks to financial stability of Armenia expanded. The unsteady pace of economic growth recovery of developed countries and continuous slowdown of developing countries' economic growth of the first half of the year were maintained further. Decreased prices of base metals in international markets, the reduced demand for main products exported from Armenia and absence of growth of the Armenian industry contributed to lower domestic economic growth. Geopolitical developments created additional obstacles to Russia's economic growth, which in turn affected negatively the inflow of private transfers to Armenia and export volumes to Russia, highlighted in November-December 2014.

The global economic recovery was slower during the second half of the year, which resulted in a 0.3 percentage point lower global economic growth assessment as compared to the beginning of the year. Although the USA recorded high economic growth, the Euro area countries experienced lower-than-expected economic growth, mainly due to geopolitical developments. In developing countries the trend of economic growth slowing was maintained, which in turn has contributed to world trade cut and dropped prices of some exchange-traded commodities. Monetary authorities of developing and developed countries continued pursuing an expansionary monetary policy to support economic growth. These accommodative monetary policies become more difficult in developing countries parallel with countervailing measures to domestic currency depreciations. During the year, interest rates of monetary instruments remained at low levels, while the termination of quantitative easing program by the U.S. Federal Reserve has created

expectations of an increase in interest rates not sooner than in the third quarter of 2015.

Economic developments in Armenia's main trade partners some countries of the European Union and Russia (for details, please see box "Economic developments in Russian Federation") – have been unexpectedly unfavorable, and their impact on the domestic economy manifested in the second half of the year (for details, please see section "Developments in the global economy"). In 2014, economic growth in Armenia was 3.4% (3.5% in 2013). The slower growth rate was mainly due to growth absence in industry, a decline in construction indicators and decreased growth rates reported in other sectors of the economy (for details, please see section "Macroeconomic environment Developments in Armenia"). The growth rate of lending by banking sector reduced as compared to the previous years due to low economic growth and fall in private remittances. Parallel a slowdown of decreasing trend of capital adequacy was recorded. Armenian banking system had capital adequacy and liquidity ratios above the regulatory requirements, and manageable market risks.

Though in some cases on an upside track, risks in the financial system remain manageable in terms of financial stability (for details please see sections "Stability of financial institutions of Armenia" and "Financial market infrastructures stability").

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