

Financial Stability Report (2011 1st half)

2011-09-27

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.

ABSTRACT

During the first half of 2011 there was no reported growth of risks undermining Armenia's financial stability, while all changes along the way further solidified the stability of the system. Increased prices of raw materials as well as recovering inflow of transfers and domestic demand contributed to the growth of GDP. The rise in prices of basic commodities, food products in particular, in world markets noticed since the second half of the previous year as well as reported slump in supply of domestic agriculture in the first half of the year further fuelled high inflationary environment, added to inflationary expectations and negatively affected real household incomes. No worsening of risk levels was observed in the financial sector while expectations of further positive development solidified instead. The banking system brought growth of lending back on track yet it broadly remained conservative in terms of assessing borrowers.

The global economic growth continued albeit downside risks to the economic growth increased. In advanced economies the sovereign and private debt burden persisted at high levels which limit the state's ability to intervene and hinder the growth of demand and prevent the economy from reviving further. In a complicated situation like this, implementing exceptionally coordinated policies and taking unified approaches to regulation and supervision reforms in the financial system is equally important to all countries. In the face of continued rise in manufacture and food prices, curbing inflation has become a priority for developed countries, too, bringing forward risks to restricting further economic growth. The recovery is slower-than-forecast in Armenia's main partner countries in Russia, some Euroarea countries in which may create negative impact on the Armenian economy already (see details in Developments in world economy section).

According to the Armenian National Statistics Service data, Armenian economy expanded at an annualized rate of 2.7 percent in the first half of 2011. Growth was reported in all sectors of the economy, except for construction where volumes of privately funded construction are still small. In the first quarter of 2011, amid high inflationary environment, the Central Bank gradually tightened the monetary policy conditions by raising the refinancing rate a total of 1.25 pp since the start of the year. In the months ahead, the Central Bank was predominantly neutral with its policy as it left the refinancing rate unchanged and preferred to not tighten monetary policy conditions further. Based on June data, the 12-month inflation was 8.5 percent, remaining far above the confidence band (see details in "Financial stability in macroeconomic environment in Armenia" section).

In the first half of 2011 Armenian commercial banks posted growth indicators while maintaining their capital adequacy and liquidity ratios above normative requirements and handling market risks within a comfortable territory of manageability. During the first half of the year profitability of the banking sector has grown, with return on assets reaching 2.2 percent and return on equity, 11.7 percent. Banks and credit organizations further eased lending conditions and the growth rate in lending persisted, amounting to 18 percent (see details in "Stability of financial institutions in Armenia" section).

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