

The Monetary Policy Programm of the Republic of Armenia 2008

2008-03-28

Principles of monetary policy

In 2008, the Central Bank of Armenia (the CBA) will continue the transition to a fully-fledged inflation targeting strategy. According to the Republic of Armenia Law on the Central Bank, the primary objective of the CBA is to ensure price stability: this is how the CBA contributes to an economic policy of attaining strong and sustainable growth in the long run. Given the current inflationary macro-environment in the Armenian economy and the expectations that inflationary risks will persist in the external world, a target band of 4% + 1.5% inflation has been set for 2008.

The CBA's implementation of the inflation targeting strategy in 2008 will be guided by the following considerations:

The CBA's main and primary objective is to ensure price stability (the annual inflation target for 2008-2010 has been set at 4% (+1.5%));

Headline inflation, i.e. the growth of the consumer price index, which represents the growth of prices of 470 consumer goods and of services tariffs, is set as the inflation indicator.

The inflation forecast is set as the nominal anchor.

Short-term interest rate is accepted as the operational target.

A repo (refinancing) operation, for which a rate is set on the second business day of each month for that month, is used as the main instrument of monetary policy. Monetary policy will transmit impulses to the economy not only through a change in interest rates, but also by leaving them unchanged over a certain time period.

At the beginning of each quarter, the CBA Board decides on the directions of monetary policy for the quarter ahead, relying on inflation forecasts, external world and economic development scenarios, and inflationary risks.

A 12-month period is set as the time horizon for meeting the inflation target, which means that, each quarter, the upcoming 12-month inflation is forecast, with the implementation of monetary policy aiming to eliminate the deviation between the target and forecast.

To ensure the accountability and transparency of monetary policy, the CBA publishes quarterly Inflation Reports, which provide the inflation analysis for the preceding period, the factors driving inflation, and the inflation forecasts for the following period. According to Article 6(4) of the Republic of Armenia Law on the Central Bank, the CBA shall, within the two months following each of the first and third quarters of the year, submit to the National Assembly the approved Monetary Policy Programs and Inflation Reports for the relevant quarters. Quarterly Minutes on Interest Rate are released, which are effectively quarterly programs of monetary policy that include one-year forecasts of macroeconomic and monetary indicators, as well as the CBA Board's deliberations and decisions on the directions of monetary policy. Every month, immediately after the CBA Board has set the interest rate, the CBA issues a press release, and during the next 10 days the Minutes on Interest Rate for the relevant month is published. Minutes on Interest Rate also appear in the CBA's monthly Bulletins in the form of Monetary Overviews and Quarterly Inflation Reports (Quarterly Reviews), as comments on the inflation management policy and a reflection of potential developments of inflation expectations.

More comprehensive analyses and comments will be devoted to the following exceptions that are considered as non-monetary factors affecting inflation in international practice:

A considerable changes in global prices;

Considerable exchange rate fluctuations of national currency driven by external shocks;

Notable changes in agriculture, which are reflected in commodity prices;

Significant changes in regulated prices;

Natural disasters and other force-majeure situations that may trigger supply or demand-driven price shocks.

The latter can generate mostly supply shocks, which are non-recurrent and transient, and

neutralizing their impact by means of monetary policy would hamper the growth of economic activity. In countries with a short history of low inflation, such shocks usually shape inflationary expectations. Therefore, the CBA considers necessary to issue detailed comments on the inflationary impact of such factors and the CBA's stance thereon.

The CBA will continue to monitor the developments of demand for the dram and dramization, in particular, and will meet such demand with a view to the priority of its main objective. The conditional inflation forecast will be published in 2008, as well, involving a presentation of qualitative characteristics of monetary policy implementation. The CBA will continue to forecast macroeconomic indicators using the Quarterly Projection Model (QPM), which combines interest rates, inflation, and business cycles in order to opt the main directions of monetary policy necessary for achieving the inflation target. In both the inflation model and publications, the CBA will continue to present forward-looking perspectives.