

Inflation report 2023/1 (Monetary Policy Program Q1, 2023, Status report on implementation of the Monetary Policy Program, Q4, 2022)

2023-03-27

Executive summary

In the first quarter of 2023, the economic activity remains sluggish in the world economy and, particularly, the main partner countries to Armenia. In these countries, the 12-month inflation is gradually slowing down, largely owing to the continued decrease in the food and energy prices. However, the impact of high demand and inflation expectations on the inflation still prevailing; specifically, the growth of service prices in a number of advanced economies continues to stay significantly above the target value. Under these circumstances, the central banks of developed countries will carry on tightening the monetary conditions. This will lead to a further gradual weakening of demand and continue to reflect the decline in prices in commodity markets in the short-term perspective.

High rates of growth of economic activity are persisting in Armenia in the beginning of the year, which is considerably backed by strong external demand in the service sector, as well as high growth registered in the construction branch. The elevated activity is accompanied by increased export and GDP potential observable in the industry and services sectors. This is also demonstrated by the appreciation of real and nominal exchange rate of the Armenian dram. The overall inflation environment in Armenia continues to mitigate as a result of the implemented contractionary monetary policy, the dram appreciation and weakened inflationary influence from the external sector. However, strong demand and the declining but still high inflation expectations contribute to the growing of wages and prices of individual goods and services.

In general, with uncertainties carrying on, the Central Bank of Armenia attempts to reduce the possible risks arising therefrom by building and discussing different scenarios for the situation development, the most likely of which is outlined in detail in this monetary policy program.

In the first quarter of 2023, the 12-month inflation reduced to a certain extent but still remains high, making up 8.1% in February. According to the scenario presented by the

Central Bank of Armenia, the headline inflation will, mainly owing to the above-mentioned supply factors, decrease rapidly in the near future, yet the prices of some goods and services (especially unregulated services) will continue to increase, incurring the effects of the established high demand and inflation expectations. Based on what was mentioned above, the Central Bank of Armenia found it reasonable to stick to relatively tight monetary conditions at this stage, taking into consideration that the inflation was still high in commodity groups which stand out primarily with rigid prices.

In view of the monetary policy implementation and expected macroeconomic developments, the 12-month inflation will decrease in the course of the year and stabilize at a later point in time around the 4% target.

According to the scenario presented by the Central Bank of Armenia, high economic activity will be sustained in the near future, whereas the growth in 2023 is expected to be higher relative to the one outlined in the scenario of the previous program. In the latter part of the mid-term horizon, the growth will gradually slow down and stabilize around the long-term equilibrium.

The economic growth expected in 2023 will mostly be driven by rather high growth in services and construction. In turn, the growth of construction will notably be determined by construction activities related to the operation of the Amulsar gold mine. The operation of the Amulsar gold mine will positively contribute to the growth of the GDP potential in 2024 and, to a certain extent, in 2025, thus helping to maintain a high level of economic growth. Nevertheless, in the medium term, the economic growth will slow down as the positive GDP gap will gradually close along with the adjustment of high demand. At the end of the horizon, the economic growth will shape near its long-term sustainable level of 4.0%.

In the 3-year policy horizon, the risks of inflation and economic growth deviating from the projection paths are mostly balanced (see subsection 2.2.4). In the case of risks emerging in any direction, the Board of the Central Bank of Armenia will adequately respond and ensure the fulfilment of the price stability objective.

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[Graphs and tables Q1, 2023](#)