CENTRAL BANK
OF ARMENIA

ANNUAL REPORT

2017



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2017



YEREVAN 2018

Content

01

THE CENTRAL BANK OF ARMENIA 16

About the Central Bank 17

Review of Strategic Directions 20

02

MAINTAINING PRICE STABILITY 24

Monetary Policy 25

03

MAINTAINING FINANCIAL STABILITY 30

Financial System Stability, Regulation and Supervision 31

Payment and Settlement System 36

Securities market 39

04

OTHER OBJECTIVES OF THE BANK

40

Currency issuance and currency circulation in Armenia 41

Organizing and regulating the framework to combat money laundering and terrorism financing 44

Protection of consumer rights and interests in the financial system 48

International reserves management 51

05

INSTITUTIONAL DEVELOPMENT

52

Institutional development of the Bank 53

Dilijan Training and Research Center 66

06

ANNUAL FINANCIAL ACCOUNTS OF THE CENTRAL BANK

72



Arthur JAVADYAN

Chairman of the Central Bank
of Armenia

Chairman address

Dear reader,

This annual report of the Central Bank of the Republic of Armenia provides an overview of the main developments of the Bank's activity for 2017, namely the results of the policy carried out to maintain price and financial stability.

In a low inflation environment in 2017, the Bank continued implementing a contractionary monetary policy. The refinancing rate fell to 6.0 percent and remained at that level until the end of the year. A low policy rate of the Bank continued to be reflected in interest rates of government bonds, dram deposits and loans, bolstering the growth of domestic demand. As a result, domestic demand expanded and inflation amounted to 2.6 percent at the end of the year, staying within the confidence band.

Rebounding economic activity, steadier expectations of income from the external sector and expansionary monetary policy have all contributed to the strengthening of the financial system, including the extent and scope of financial intermediation. The banking system has secured a significant increase in all key indicators. Credit organizations, insurance companies and other financial system participants too have ended the year with the growth of main financial ratios. Accelerated growth of assets in mandatory funded pension schemes during the year is worth mentioning.

In view of highlighting the importance of financial stability, the Bank continued efforts in improving its regulatory and supervisory functions. Changes in the regulatory framework were mainly aimed at bringing it into line with the new Constitution of the Republic of Armenia, as well as internalizing best international standards.

In the context of financial stability, activities in the regulation and

supervision framework contributed to the enhancement of the financial system's stability as the macroeconomic situation improved. The banking system continued to offer sufficient capital adequacy and high liquidity standards. Improved quality of loan portfolio has positively affected the total capital adequacy of banks.

The "Financial Education in Schools" program, which has been developed in cooperation with the Armenian Ministry of Education and Science and is now in a testing phase, is aimed at ensuring necessary conditions for the protection of consumers' rights and legitimate interests in the financial system.

Improving the professional qualities and competences of the employees remains a priority for the Bank in achieving its objectives. To make sure the staff benefits lifelong education, the Bank has been expanding cooperation with international organizations as well as with central banks and prestigious training centers in different countries.

STAGES
OF THE BANK'S DEVELOPMENT

1993	Introduction of the national currency
1994	Formulation of the monetary policy
1996	Adoption of core legislation on the Central Bank and banking
1996-2001	Creation and implementation of the national payment and settlement system
2002-2004	Development of a regulatory framework for financial market participants and setting-up of infrastructures
2005	The Central Bank as a megaregulator and responsible for financial stability
2006	Inflation targeting
2007	Protection of consumer rights and awareness of financial services
2007- to date	Development of a non-bank sector
2012- to date	Institutional reforms and infrastructure developments

THE BOARD
OF THE CENTRAL BANK OF ARMENIA



Arthur JAVADYAN
Chairman
of the Central Bank



Nerses YERITSYAN
Deputy Chairman



Vakhtang ABRAHAMYAN
Deputy Chairman





Oleg AGHASYAN



Ashot MKRTCHYAN



Armenak DARBINYAN



Arthur STEPANYAN

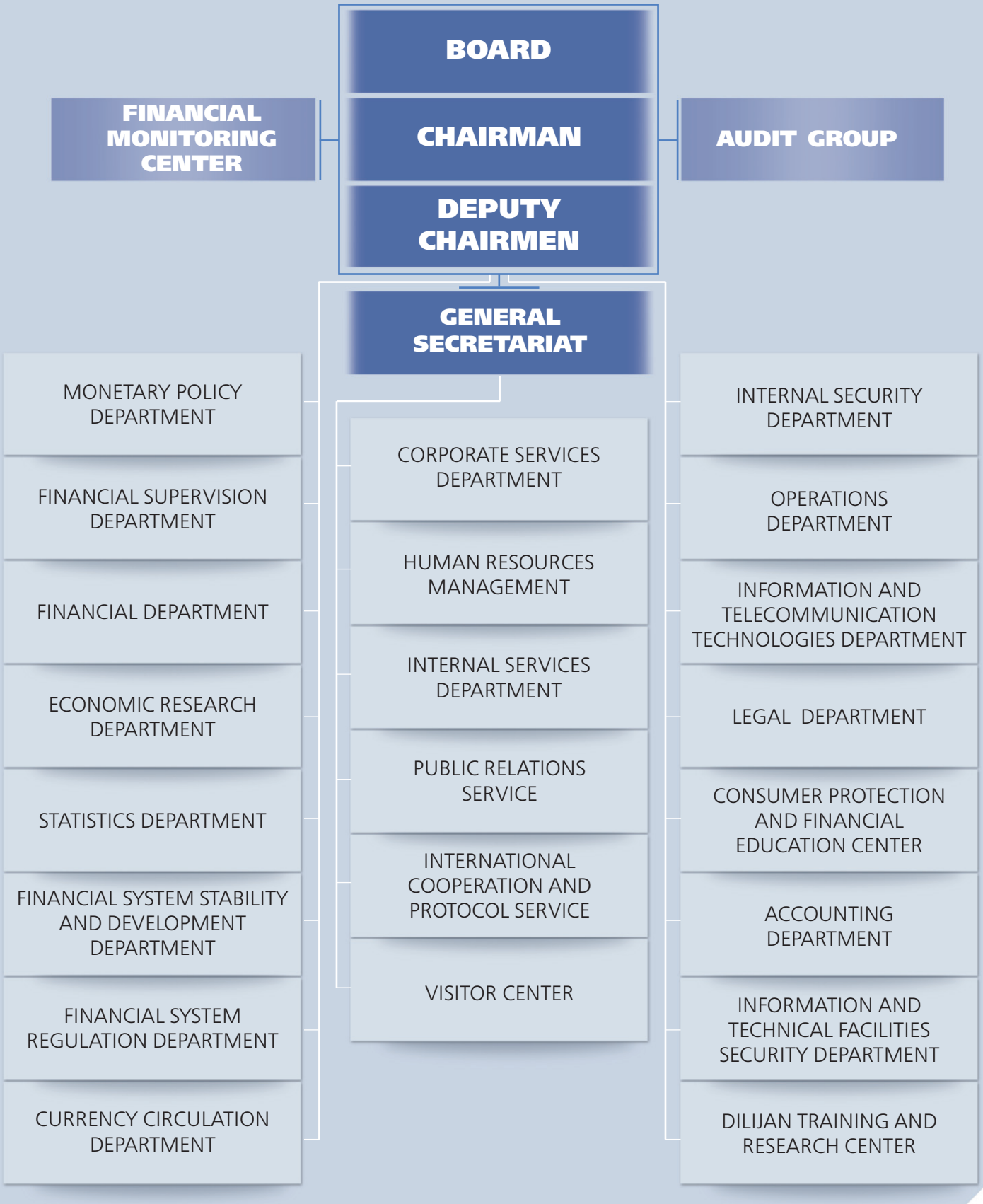


Arkadi KHACHATRYAN

THE MANAGEMENT
OF THE CENTRAL BANK OF ARMENIA

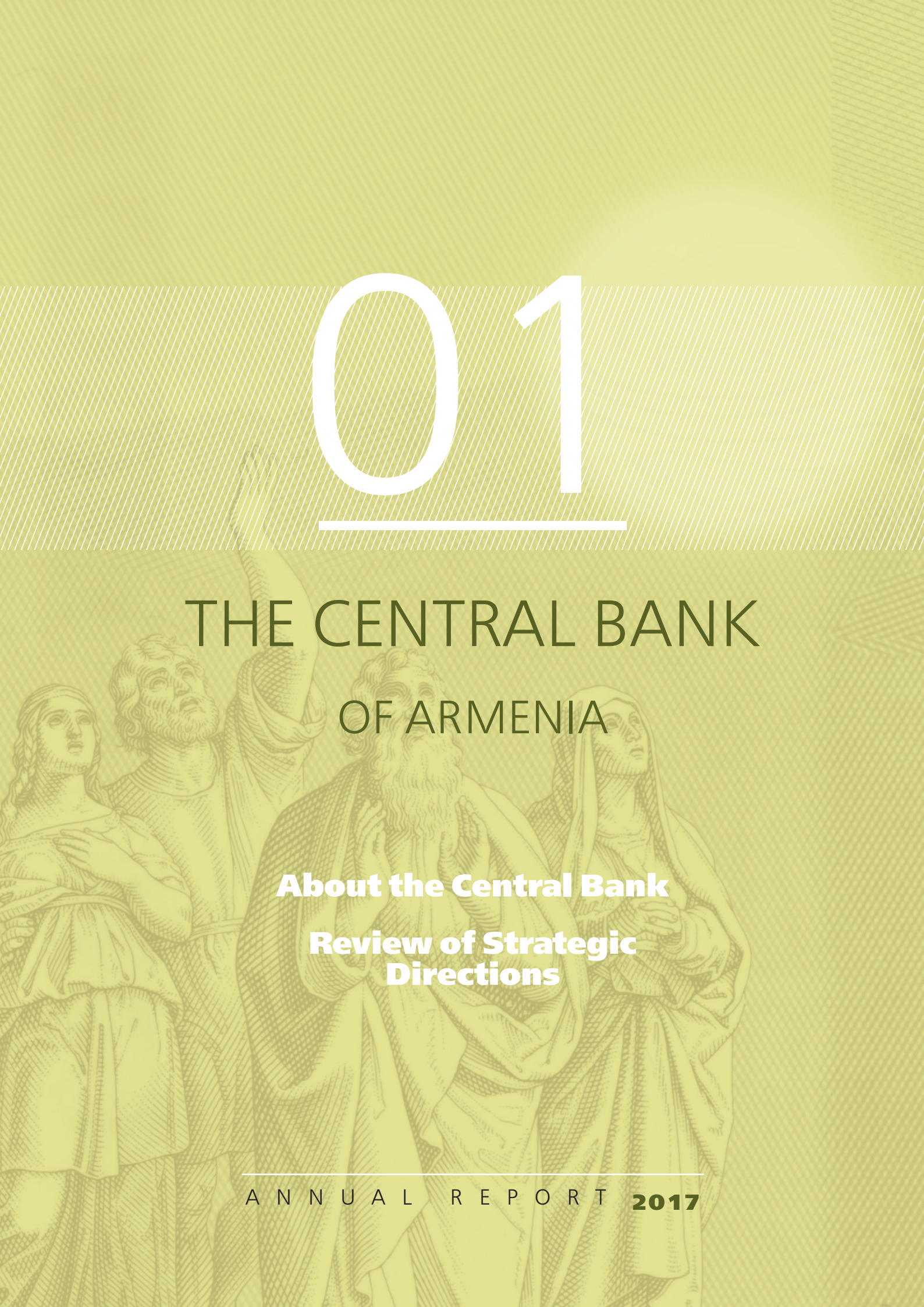


STRUCTURE
OF THE CENTRAL BANK OF ARMENIA



01

THE CENTRAL BANK OF ARMENIA



About the Central Bank

Review of Strategic Directions

ABOUT THE CENTRAL BANK

The primary goal of the Central Bank of the Republic of Armenia is to maintain price stability in the Republic of Armenia, according to the Republic of Armenia Law on the Central Bank. To achieve this goal, the Bank has a function of taking measures to attain price stability while formulating, approving and implementing monetary policy programs.

Mission of the Bank:

- be an internationally recognized institution that is independent, dynamic, prestigious, transparent and knowledge-based, and be an effective onlooker of development trends in global financial system,

- maintain institutional capacity to timely respond to the change in economic environment and effectively influence the economic processes,

- support sustainable macroeconomic development of the country, while being an important partner to the Government of Armenia in facing economic challenges.

REVIEW OF STRATEGIC DIRECTIONS

The 2015-2017 strategy of the Bank establishes that as an independent institution as well as guarantor of price and financial stability in the medium and long run, the Bank remains committed to fulfilling its primary objective by looking to maintain sustainable economic development, integrate to international markets and play an important role in providing financial services at the regional level.

For effective handling of the tasks, more efforts were spent by the Bank in 2017 to introduce and apply best international practice to the financial sector while pursuing diversity and sustainable development in the sector.

In 2017, the Bank prioritized the following objectives:

Maintaining price stability

The monetary policy carried out by the Bank in 2017 under the inflation targeting strategy was further steered to maintaining price stability and anchoring public expectations around the inflation target. Under the expansionary monetary policy implemented since the second half of 2015, trends of growing domestic demand and inflation began to be observable early in 2017. In such a situation, the Bank looked to maintain the expansionary aspect of the **monetary policy** during 2017 too, supporting the growth of aggregate demand and fulfilment of the inflation target. As a result, growing gradually, the 12-month inflation rate has entered a positive territory since April and was at the end of the year in the confidence band: it amounted to 2.6% at the end of December.

Maintaining financial stability

The Bank continued its efforts to strengthen financial stability and further raised the effectiveness of the regulatory and supervisory framework in 2017.

In view of economic activity set to recovery and stabilizing flow of incomes from the external sector in 2017, the financial sector participants expanded the scope of financial intermediation. As of the end of the year, the financial system assets-to-GDP ratio and the economy lending-to-GDP ratio have amounted to 91.4% and 49.8%, respectively.

The banking sector remains the largest pillar of the financial system, as it accounts for 85.5% of the system's assets. The banking sector has reported a significant growth of all balance sheet indicators. Other participants of the financial system have also reported growth in key indicators.

Other objectives of the Bank

Issuing currency of the Republic of Armenia, and organizing the currency cycling: In the reporting period the Bank issued the "Noah's Ark" collector banknote, the first Armenian banknote printed on a composite material.

To organize the fight against money counterfeiting, the Bank's expert laboratory has been furnished with new equipment for the banknote expertise.

To publicize national, historical, cultural, spiritual values of Armenia and to satisfy the numismatic demand of collectors, in 2017 the Bank issued commemorative coins of precious metals, which are dedicated to the anniversaries of renowned Armenians and landmark events.

Organizing and regulating a framework to combat money laundering and terrorism financing (AML/CFT): In the reporting period the AML/CFT risks were assessed within the framework of the Interagency Committee. In particular, steps were taken to assess the criminal cases and judgments on previous crimes on money laundering, the AML/CFT risks, and to evaluate the risk of AML/CFT abuse by commercial and non-commercial organizations.

Protection of consumer rights and lawful interests in the financial system: The Bank continued efforts to protect the rights and lawful interests of consumers in the financial system by making sure financial service providers practice a fair business conduct, an appropriate institutional environment and a financial education framework are in place.

As part of measures aimed at increasing public awareness of financial education in Armenia, year 2017 marked the pilot launching of the component of financial education to 4 school curricula for children in grades 2-12. A total of 13 schools were included in the program.

Management of international reserves: The Bank continued its strategy of managing international reserves of Armenia by taking a least-risk-involvement approach, which is aimed at increasing the safety, liquidity and effectiveness of management of the reserves.

In 2017, the level of international reserves of Armenia further complied with all international criteria to foreign currency reserves, particularly in terms of the economy's ability to absorb possible shocks. In 2017, the international reserves of Armenia secured about five months' coverage for imports and nearly eight years' coverage for servicing short-term (up to 1 year) liabilities.

Institutional development

As the information security management system further develops and improves, in 2017 the Bank emphasized the need to develop the domestic financial and banking system's cybersecurity.

The Bank enhanced its bilateral and multilateral cooperation with partner institutions, as well as international financial organizations.

In 2017, the Dilijan Training and Research Center posted significant achievements and success in three main areas – **research, international cooperation and social responsibility.**

As of the end of the year, about 26% of the Bank's staff (193 employees) worked at the Center.

02

MAINTAINING PRICE STABILITY

Monetary Policy

MONETARY POLICY

Primary goal of the Bank

According to Article 4 of the Republic of Armenia Law on the Central Bank, **the primary goal of the Bank is maintaining price stability**, whereby the Bank contributes to the policy of achieving a long-term sustainable and high economic growth. For ensuring price stability, the Bank sets a medium-term inflation target and decides on such a target in order to anchor public expectations and secure a path to streamlined macroeconomic stability. In Armenia, the inflation target is outlined in the monetary policy programs of the Bank, medium-term expenditures frameworks of the Armenian Government, the Republic of Armenia laws on state budget as well as in sustainable development projects. The Bank enjoys operational independence; it is free in deciding on a strategy for conducting monetary policy, setting intermediate and operational targets and using monetary instruments.

In the context of **inflation targeting strategy of the Bank**, a projected path to bringing inflation to the target serves an intermediate target and short-term interest rate serves an operational target for the Bank. The 7-day repo agreement is the main instrument of the Bank's monetary policy, the interest rate (refinancing rate) of which is set by the Board of the Bank according to a pre-announced timetable. Interest rates of the monetary policy instruments take effect on the day following the setting.

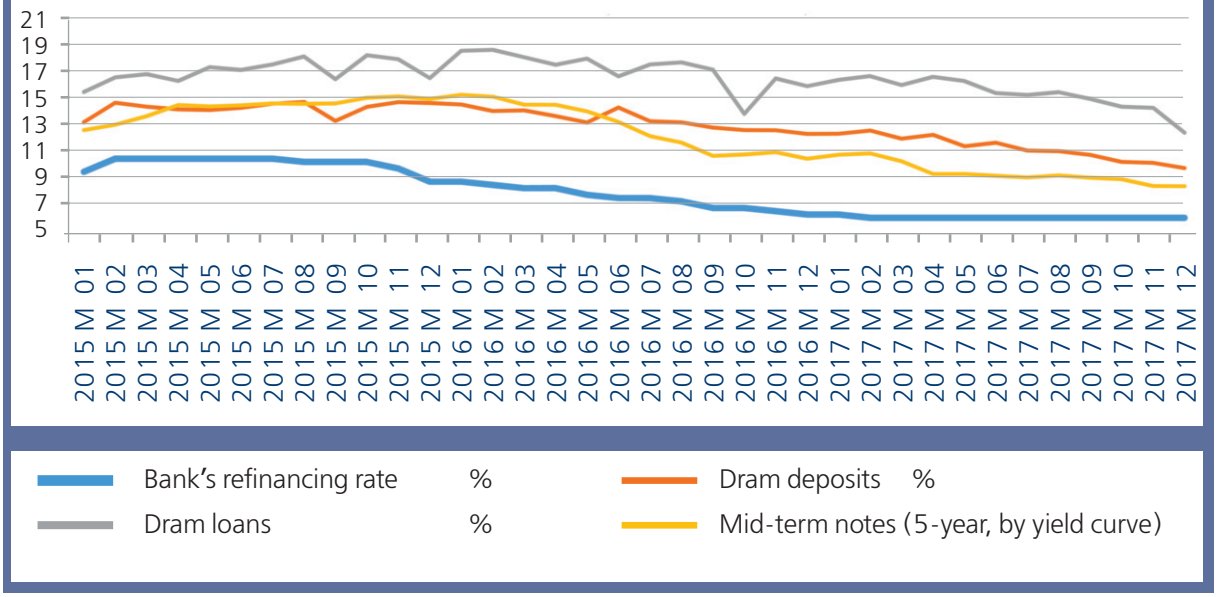
One of the main ways the Bank communicates to the public is through publication of inflation reports on a quarterly basis[1]. The first part of the inflation report contains the current quarter's monetary policy program and the second part presents the status implementation of the previous quarter's monetary policy program steered to attain the inflation target.

1 1 Please see the periodicals "Inflation Report" of the Central Bank: (www.cba.am).

Implementation of monetary policy

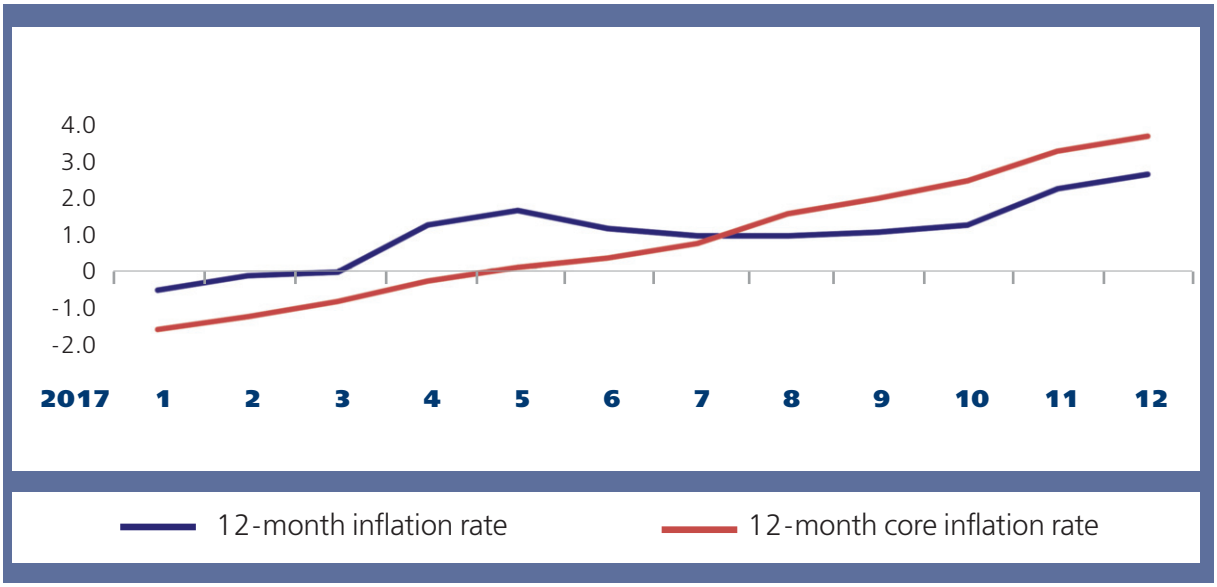
In view of the macroeconomic situation and inflation, developments and taking into account the moderate inflationary effects expected from both external and domestic sectors, **in 2017 the Bank remained committed to carrying out a monetary policy which had been expansionary since the second half of 2015.** In February too, the Bank lowered the refinancing rate by 0.25 pp, keeping it at a low level up until the end of the year. Such a monetary policy, reckoned the Bank, was expansionary enough to facilitate the growth of domestic demand and help the inflation stabilize around the target in the forecast horizon. In the meantime, trends of falling interest rates in the market persisted throughout the year as monetary conditions remained expansionary.

Figure 1: Interest rates of the Armenian financial market



Actual inflation developments suggest that both headline and core inflation rates gradually increased in 2017. In the direct monetary policy influence point of view, the increase of the **12-month core inflation rate from** -1.8% at the end of the previous year to 3.6% in end-December is remarkable. This has been greatly fostered by expansionary monetary policy implemented by the Bank in the course of the last two years and relatively high economic activity observed in the world and in Armenia since the start of 2017. The slowdown in growth of prices of seasonal agricultural products has somewhat absorbed the impact of the above mentioned factors however, in which case the **12-month inflation rate amounted to 2.6% at the end of 2017, staying within the confidence band**.

Figure 2: In end-2017, the 12-month inflation rate remained in the confidence band



Note that the inflation rate increased rapidly in the fourth quarter when a sharp rise in prices for some products (butter and meat) in the international food markets affected the domestic prices of these products. At the same time, the rise in prices for these products as well as expectations of possible effects from the change in tax and customs rates planned in early 2018 added to inflation expectations during the quarter.

Monetary policy implementation: improvement and advancement

The **Forecast and Policy Analysis System (FPAS) of the Bank** can advance only if its quantitative and qualitative components are further improved and refined. This helps the Board of the Bank to have a clear understanding of the macroeconomic situation and make more informed decisions about the directions of the monetary policy.

Improving the FPAS in a longer-term perspective has two continuous aspects:

- Inclusion of specificities of the Armenian economy into the current system and advancing it technically,
- Improvement of the current system through transition to the Dynamic Stochastic General Equilibrium (DSGE) model framework.

The following work was done in the framework of the first aspect in 2017:

1. Analysis of inflation expectations and of confidence in the policy, and incorporating the outcome into the FPAS. The short-term and long-term inflation expectations, which are also viewed as determinants of confidence in the monetary policy, were separated.
2. Improving the model of forecasting the macroeconomic indicators of the external world by advancing the analysis of the economic policy of the external world.
3. Technical update of the main model of inflation through transition to a new software framework, which allows to increase the quality of internal data and reporting and will provide room for improving the technical basis of satellite models later on.

The second aspect involved the following activities:

1. Study of asymmetric responses of the monetary policy specific to the Armenian economy through the DSGE model. The research was done under the joint program by the Bank and Davis Center of Harvard University.
2. Final-stage work for building DSGE 2 models that consider the behavior of the real sector: the first is for optimal monetary policy choice where heterogeneous firms are concerned, and the second is for studying the problems of investment and capital accumulation and identifying the level of a balanced economic growth.

Statistics

The Bank collects, compiles and publishes the monetary and financial sector statistics and external accounts statistics, pursuant to the goals set forth in the Republic of Armenia Law on the Central Bank. The Bank uses the statistics internally in implementation of its mandate for formulating a monetary policy, maintaining price stability, developing payment and settlement system, financial supervision and such other functions. In addition to the compilation of statistics, the Bank regularly conducts sample research and statistical surveys in different sectors of the economy to fill out the gap of information which is almost impossible to obtain from official statistical sources, but which is needed for effective implementation of its operations. The statistics compiled and published by the Bank is for access to government departments, financial market

participants, international institutions, mass media and general public.

In 2017, the Bank continued delivering timely and accurate statistical data to the public. Further work was done to broaden the scope of and accessibility to statistical data, improve the methodology for data collection and alignment with international criteria[2].

New data collecting and calculation

In 2017, to improve the statistics of external accounts, the Bank elaborated, in cooperation with the National Statistics Service of Armenia, a template to reporting form for non-financial organizations' external debt. Starting from 2018, this instrument will allow the NSSA to collect, and provide the Bank with, information on current and future flows relating to the servicing of these organizations' external debt.

A survey has been launched as part of collecting and processing the so-called Big Data, which is aimed at tackling the Bank problems, increasing the effectiveness and efficiency of forecasting macroeconomic indicators. Titled as "The Use of Big Data in the Central Bank of Armenia", the survey was approved by Irving Fisher Committee and appeared in the relevant paper[3].

2 The Bank publishes the statistical data in section "Statistics" of its homepage (www.cba.am).

3 "The Use of Big Data in the Central Bank of Armenia", https://www.bis.org/ifc/publ/ifcb44.pdf.



03

MAINTAINING FINANCIAL STABILITY

Financial System Stability, Regulation and Supervision

Payment and Settlement System

Securities market

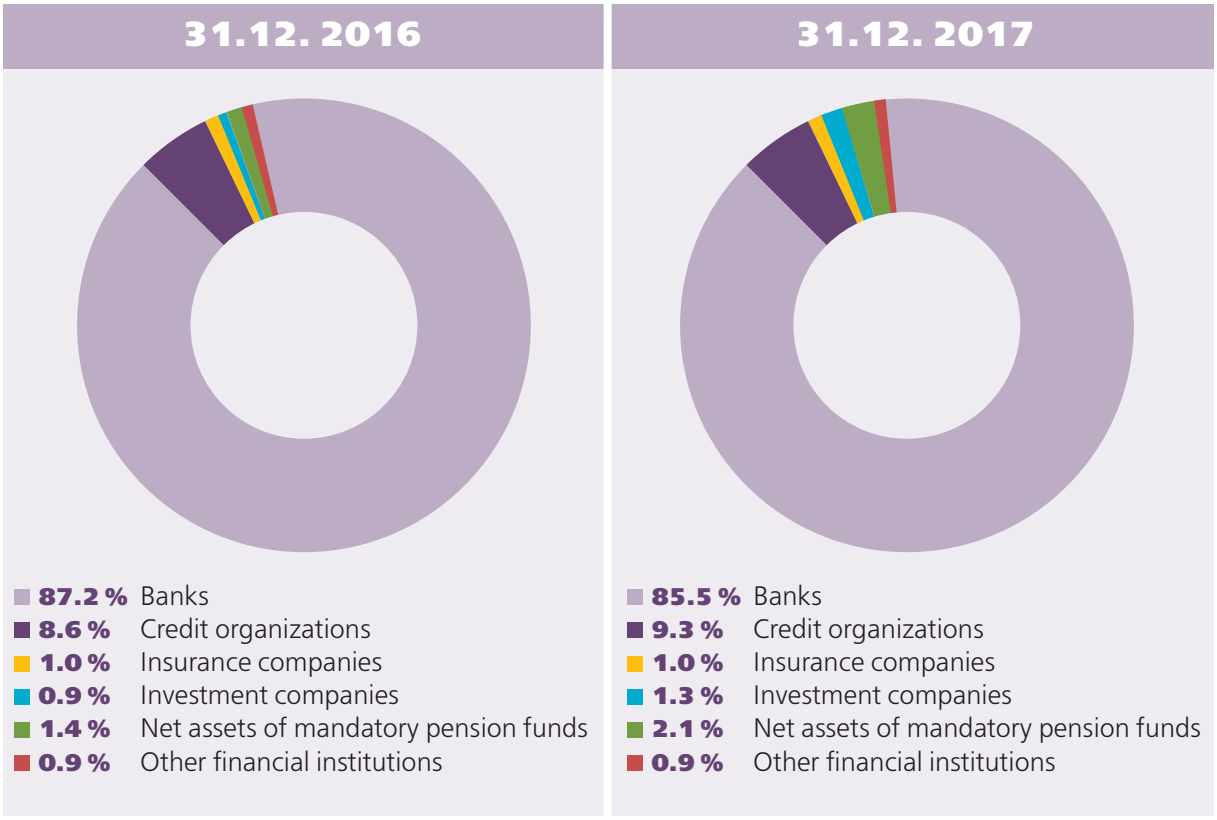
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FINANCIAL SYSTEM STABILITY, REGULATION AND SUPERVISION

In view of economic activity set to recovery and stabilizing flow of incomes from the external sector in 2017, the financial sector participants expanded the scope of financial intermediation. As of the end of the year, the financial system assets-to-GDP ratio and the economy lending-to-GDP ratio have amounted to 91.4% and 49.8%, respectively.

The banking sector remains the largest pillar of the financial system; it accounts for 85.5% of the system's assets (see Figure 3).

Figure 3: Assets of the financial system



In 2017, assets of the banking system grew by 9.2%, total capital by 4.9% and total liabilities by 10.1%. The amount of loans to the economy increased by 8.5%. The banking system reported net profit of AMD 39.7 billion (as of 31.12.2016: AMD 31.7 billion), with return on assets (RoA) and return on equity (RoE) ratios amounting to 1.0% and 6.0% (as of 31.12.2016: 0.9% and 5.8%), respectively. The increased profitability owed mostly to net reduction of provisioning against assets loss.

The expansionary monetary policy conducted by the Bank, competition between financial organizations and current liquidity in the banking system continued facilitating the reduction in interest rates of financial instruments offered by commercial banks. Note that most remarkable was the falling of interest rates of dram loans.

Figure 4: Interest rate of loans to legal persons

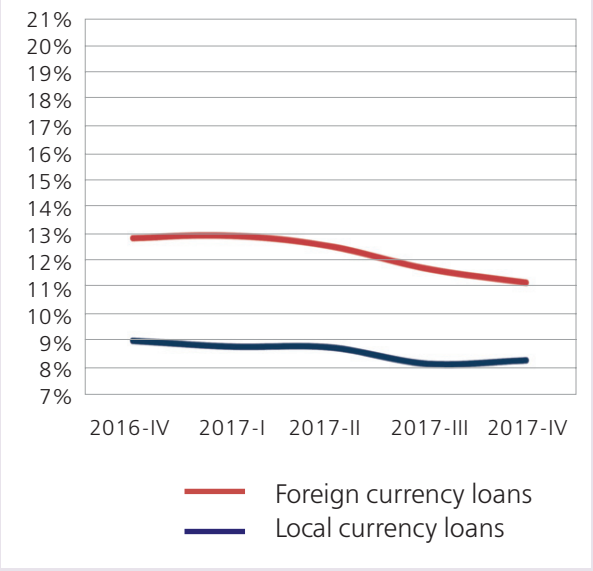
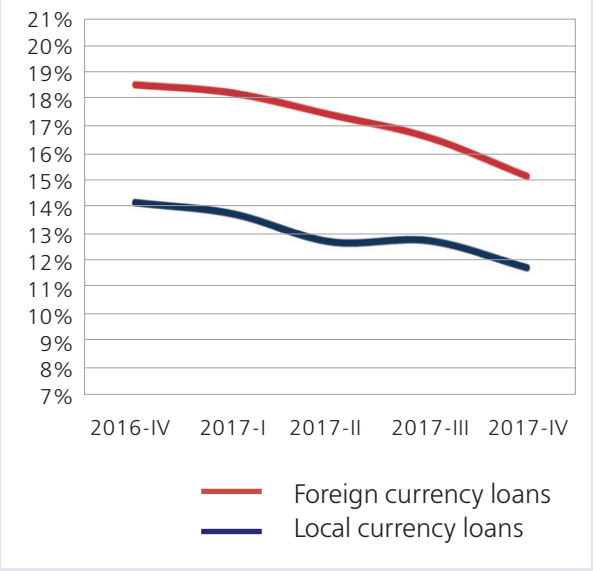


Figure 5: Interest rate of loans to individuals



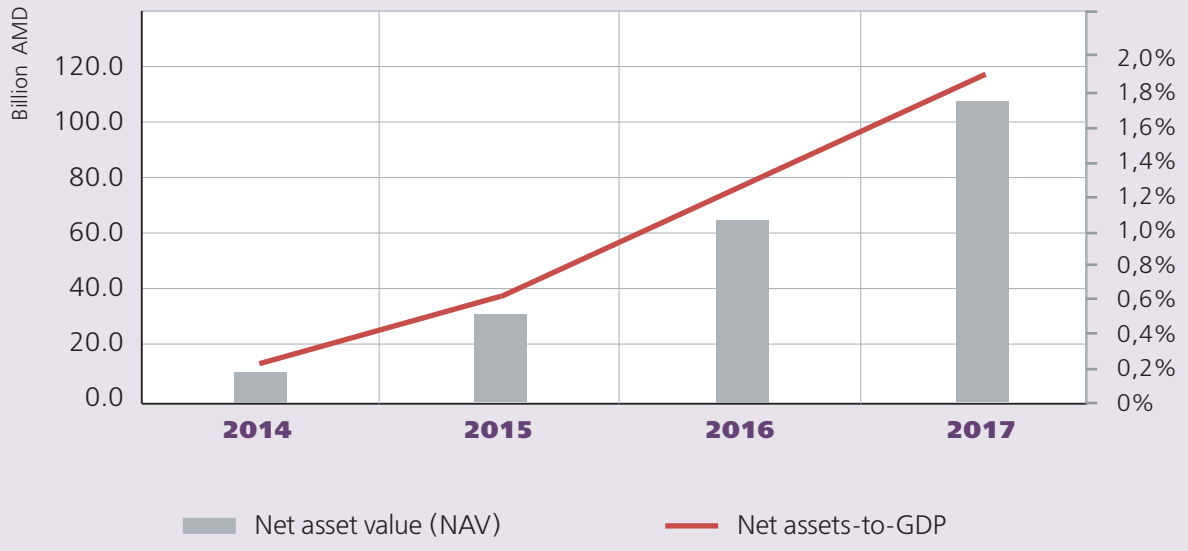
The capital adequacy and liquidity ratios, which determine the banking system stability, continue running above their minimum requirements. Thus, in the reporting period the total capital adequacy ratio amounted to 18.6% (minimum threshold: 12.0%). The banking system liquidity persists at a high level as well – this ratio is well above the minimum requirement across all banks, pointing to the high liquidity in the system. As of the end of 2017, commercial banks' total and current liquidity ratios have amounted to 32.1% and 141.7% (minimum thresholds: 15.0% and 60.0%), respectively.

The year saw improvement in recoverability of loan portfolio of the banks. The share of non-performing loans ("watched", "non-standard" and "doubtful" risk categories) has decreased by 1.2 pp to 5.5% in total loans.

Other participants of the financial market have also reported growth of the key balance sheet indicators . The total capital of **credit organizations** has increased by 41.4%, liabilities by 3.5%, assets by 21.1%. The total capital of **insurance companies** has decreased by 1.1% but liabilities have grown by 11.2% and assets by 6.1%. The total capital of investment companies has grown by 51.9%, liabilities by 55.3% and assets by 54.8%. The net assets of mandatory pension funds managed by asset managers have grown by 67.0% to AMD 105.6 billion.

At the end of the year, the net assets-to-GDP ratio of pension funds reached 1.9%.

Figure 6: Value of net assets of pension funds



In 2017 the Bank continued supervision through off–site and on–site inspection over the activities of financial institutions with the aim to maintain financial system stability, evaluate financial market participants' exposure to risks, legal and normative framework compliance and to make sure an effective framework to combat money laundering and terrorism financing is in place and interests of consumers in the financial market are duly protected.

The main task of off-site supervision is to monitor day-to-day activities and performance of financial institutions on the basis of reports, information, claims and other deliverables from them, make analysis of their financial condition, figure out unacceptable risks, check compliance of their activity with the legal framework and promptly react, if necessary.

In 2017 the Bank further spent efforts to identifying financial institutions' exposure to risks, evaluating business conduct and accuracy of reportable information and engaging in other supervisory activities of relevance. During the year the Bank completed 186 on-site inspections.

Infringements revealed through supervision were remedied and measures were taken to prevent the ones in the future.

Activities as part of improvement of the financial system oversight during 2017 included:

- Transition from a rules-based supervision model to a risk-based and forward-looking supervision, driven by the developments in financial markets of the world. In the reporting period, the risk-based supervision approach was further developed and implemented at the Bank. The reforms are aimed at streamlining supervisory capacities in order to achieve increased effectiveness in carrying out supervision.
- In the context of financial stability and development, in 2017 the Bank designed and conducted another financial crisis management simulation exercise. The exercise participants were the Bank management, employees from different departments and the staff of the Deposit Guarantee Fund. The exercise was simulated around an alleged bankruptcy of the bank and subsequent remuneration of guaranteed deposits resulting therefrom, with a view to revealing possible problems with deposit remuneration, how to solve them, and identifying barriers to cooperation and communication between different institutions. Such exercises help participants get more prepared for emergency situations.

In 2017 there were certain changes in the field of financial regulation, as follows:

Changes and supplements were introduced to the "Law on the Central Bank of Armenia", the "Law on Regulations", the "Law on Budgetary System", the "Law on Housing Mortgage Crediting", the "Law on Consumer Crediting", the "Law on Banks and Banking", the "Law on Insurance and Insurance Activity", the "Law on Bank, Credit Organization, Investment Firm, Investment Fund Manager and Insurance Company Bankruptcy", the "Law on Public Auctions", and to the Republic of Armenia Civil Procedure Code.

The amendment to these laws pursued to:

- bring the current regulatory framework into line with the new Constitution,
- simplify the procedure of exchange of information between the supervisory authorities;
- make the protection of consumer rights and legitimate interests an all-encompassing process in mortgage lending and improve the mortgage lending and subsequent servicing procedures,
- introduce the banking regulation requirements set out in Basel 3 Accord,
- make the insurance regulation and supervision framework utmost compliant with international standards (in particular, compliance with the IMF and WB FSAP mission recommendations).

PAYMENT AND SETTLEMENT SYSTEM

In 2017, the Bank continued activities in maintaining vibrant, more reliable and secure payment and settlement systems, expanding the value of non-cash payments, improving the regulatory framework for these systems and streamlining the procedures for primary placement of government securities.

Securities accounting systems

In 2017, to secure a full procedure of primary placement of government securities through NASDAQ OMX Armenia, the Bank developed, in elaboration with the Armenian Ministry of Finance, statutory documents that govern the circulation of government securities; as well as relevant electronic message formats and final settlement rules for primary placement of government securities were designed and introduced. More refined mechanisms using the Treasury Direct were in place for settlement of primary placement of government securities through the Central Depository of Armenia, and now the investors will be allowed to purchase government bonds on a non-cash basis.

Payment instruments and infrastructure

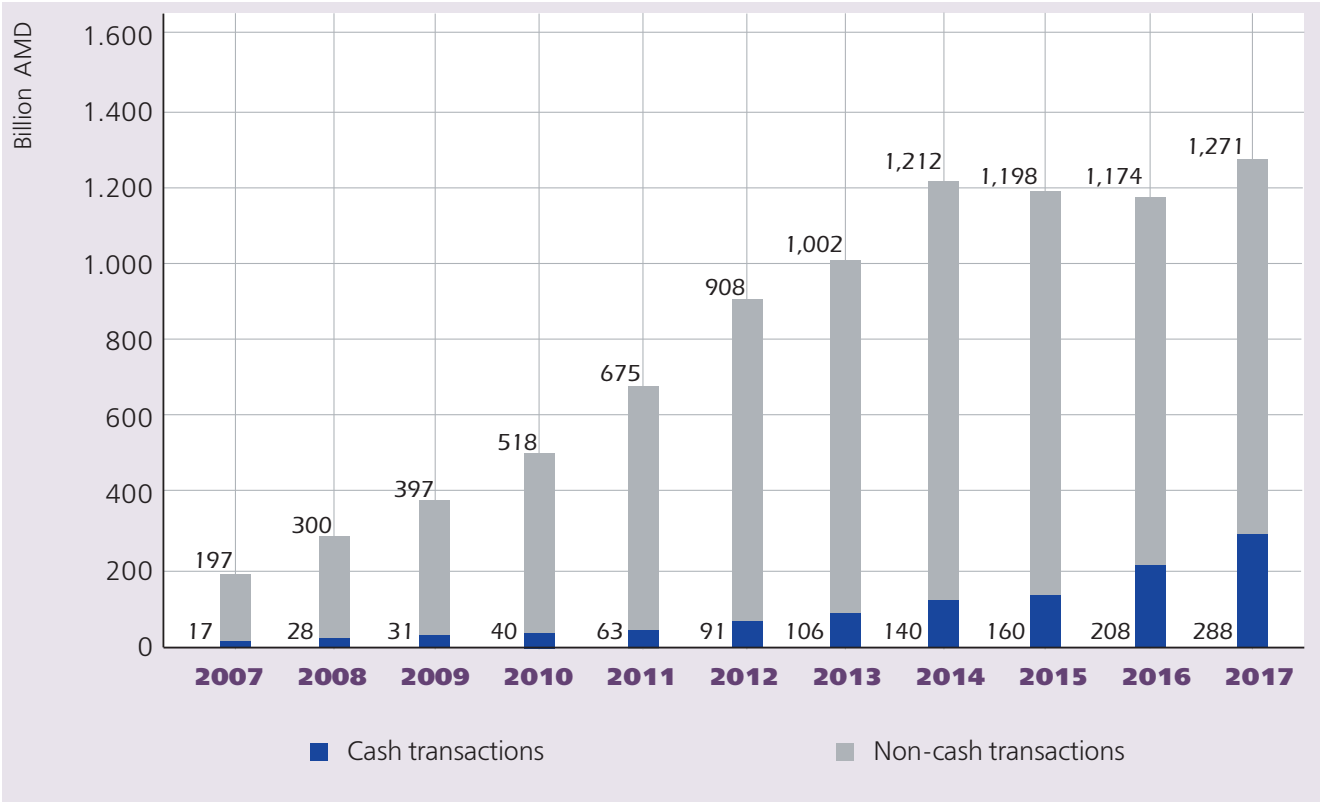
The servicing of chip cards of the Armenian "ArCa" payment system in Russia and the servicing of payment cards of the Russian "Mir" payment system in Armenia has been in place starting from 2017.

In the reporting period, further work was done to improve the regulatory framework for the infrastructure that secures the servicing of payment instruments. Specifically, the changes made it possible to provide a broad range of banking services through the automated equipment in a round-the-clock mode. At the same time, stricter requirements to the ATM security have reduced the probability of theft of banknotes packed in the ATMs. Additionally, for improved quality of

services rendered by banks, cardholders have been allowed to get their one-time activation code through a short message or e-mail, instead of issuing a PIN in a closed envelope. As of the end of 2017, a total of 15 commercial banks in Armenia had issued payment cards and offered their clients card-related servicing. All these banks are members to ArCa, a unified cards payment platform. There are 1.7 million cards in circulation in total.

In the reporting period, operations with payments cards in the Republic of Armenia totaled an estimated AMD 1 trillion 558.9 billion. The value of non-cash payments by cards has increased by 38.5% to AMD 298.3 billion, of which the value of Internet transactions amounted to AMD 145.6 billion. As a result, the share of non-cash payments by cards in total card operations has grown by 4.1 pp compared to the previous year, reaching 19.1% (see Figure 7).

Figure 7: Operations executed with payment cards in Armenia



International cooperation

In 2017, the Bank continued its cooperation with national (central) banks of the Eurasian Economic Union member states in the field of payments and settlements. Particularly, the National Payment Systems Development Working Group carried on its activities to coordinate the implementation of national payment card systems and the ISO 20022 Standard, and the transmitting of financial messaging and developing financial technologies.

SECURITIES MARKET

The Bank continued its capital market development efforts in 2017. The package of legislative reforms in developing the field of securitization of assets and mortgage-back securities market was finalized and presented to the Armenian National Assembly.

In 2017, in view of offering new instruments to the money market, the Bank embarked on introducing a trilateral repo instrument, in cooperation with the Asian Development Bank and the Central Depository of Armenia. Unlike the bilateral repo instrument in current use, this new instrument will provide for the servicing of transaction settlements and management of risks by a third-party agent. This will help cushion the counterparty risk and exempt the parties from a number of transaction-related functions (appraisal by the agent of market value of underlying securities as a pledge, making sure the underlying securities are equivalent to the amount of repo, and etc.).

Measures to improve the treasury bills placement and repurchase auctions were in place. In particular, NASDAQ OMX Armenia has been arranging such auctions since April 25, 2017 through Genium INET, an electronic trading system that uses state-of-the-art technology solutions. The system has made the entering of bids a simpler process while letting the trades be executed in microseconds. The system provides for the T + 1 settlement, which gives the participants to trading an additional advantage in terms of liquidity management.

04

OTHER OBJECTIVES OF THE CENTRAL BANK

Currency issuance and currency circulation in Armenia

Organizing and regulating the framework to combat money laundering and terrorism financing

Protection of consumer rights and lawful interests in the financial system

International reserves management

CURRENCY ISSUANCE AND CURRENCY CIRCULATION IN ARMENIA

The Bank is mandated to organize and regulate the currency circulation while adhering to the principles of reliability, convenience, efficiency and continuity.

The Bank provides cash services to its customers in regions of Armenia and the Republic of Artsakh through Yerevan-based general cash center and regional cash centers (RCC). The allocation of RCCs has improved to ensure better cash circulation and further continuity in cash servicing offered to the banks. In the reporting period, the Goris RCC terminated its activities and a new cash center, equipped with modern banknote recounting and sorting facilities, started in town Sisian to serve the customers in the southern part of Armenia.

In 2017, relative to the previous year, the value of cash circulation of the Bank has grown by 12.8%. Regional cash centers provided as much as 18.6% of total cash circulation of the Bank. Like in previous years, RCCs carried out transactions for cash withdrawal, constituting 81.1% of their total turnover.

Figure 8: Cash circulation of the Bank in 2017

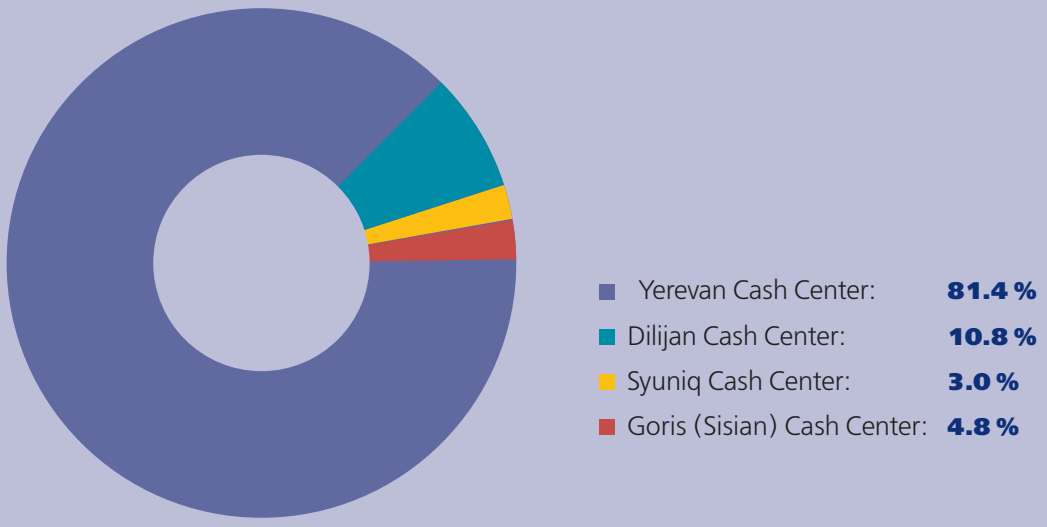
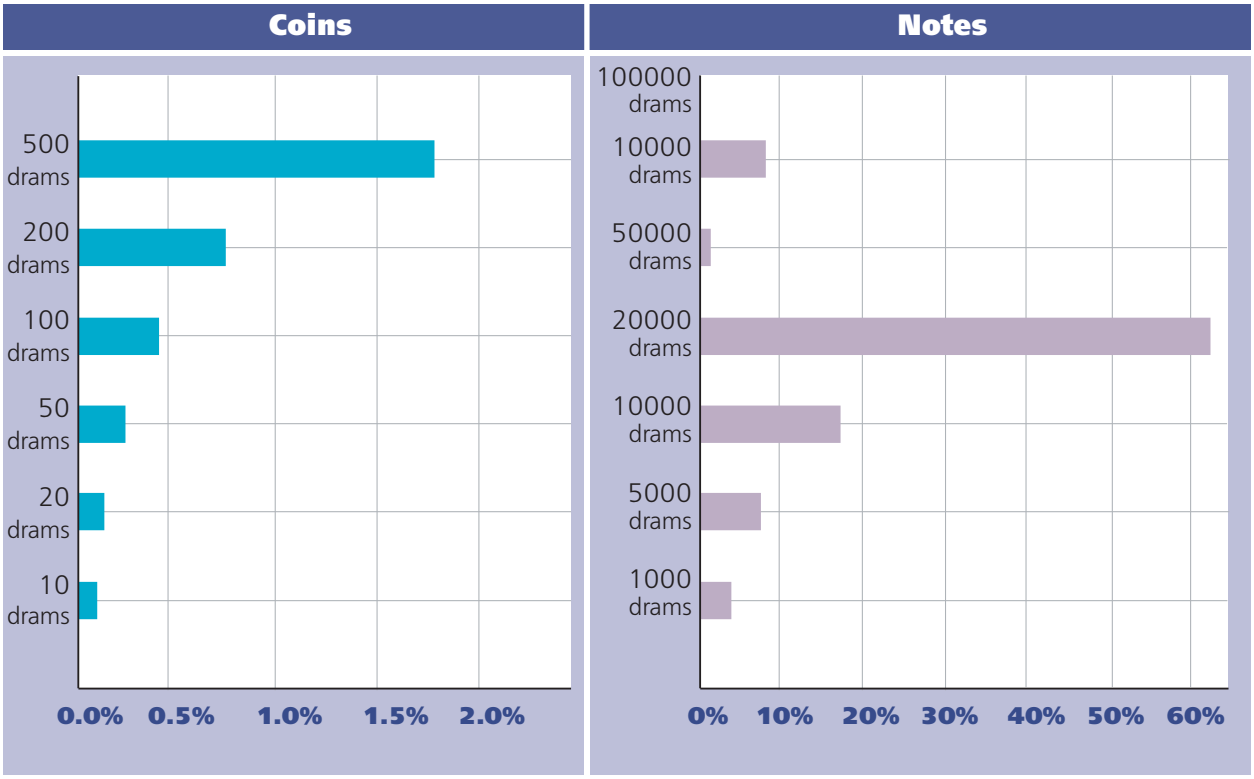


Figure 9: Type structure of currency outside the Bank as of 31.12.2017



On November 22, 2017, the “Noah’s Ark” collector banknote with nominal value Dram 500 was put into circulation. As well as the first collector banknote issued by the Bank, it was the first banknote printed using a composite material. It represents a cotton paper with a layer of polyester coated on both sides. More endurance and longer circulation life gives this banknote an undisputed edge. In view of the advantages this composite material has, there is intention to use it in printing the next series of Armenian banknotes.



To better organize the fight against money counterfeiting, the Bank boasts a special laboratory that is furnished with new equipment for banknote expertise. As cooperation with the Armenian law enforcement authorities continued, more analytical work was done to assess the methods and approaches to making and grouping of the counterfeit banknotes detected by the Bank.

In 2017, as in previous years, the Bank issued commemorative coins made of precious metals. This is done to proliferate national, historical, cultural and spiritual values, on the one hand, and to satisfy growing demand of collectors for numismatic values, on the other. As usual, the commemorative coins are dedicated to renowned Armenians and landmark events. The commemorative coins put in circulation included “Alexander Mantashyan-175”, “Hamo Beknazaryan-125”, “The 25th anniversary of formation of the Armenian Army”, “The 25th anniversary of liberation of Shushi”, “The anniversary of Armenia’s membership to IMF/WB ”, “The Collective Security Treaty-25 and the Collective Security Treaty Organization-15”, “Hovhannes Aivazovsky-200”, “Noah’s Ark”, “The 300th anniversary of establishment of the Mekhitarist Congregation of Venice”. In 2017, the Bank participated in International Numismatics Program “World Labyrinths”, under which two new silver coins were issued.

ORGANIZING AND REGULATING THE FRAMEWORK TO COMBAT MONEY LAUNDERING AND TERRORISM FINANCING

In 2017, further works for combatting money laundering and terrorism financing included conducting strategic and operational analyses, taking preventive measures to deal with potential suspicious transaction indicators, implementing a regulatory framework and strengthening national and international cooperation in compliance with best international practice.

Strategic and operational analyses

The purpose of conducting strategic analyses by the Financial Monitoring Center is to identify ML/TF risks and take measures towards the identified risks.

In the reporting period, in the framework of the Interagency Committee works have resumed for the national assessment of ML/TF risks. Particularly, actions were taken to analyze the criminal cases and convictions with ML predicate offences, latent criminality and corruption, in order to assess the associated ML/TF risks, as well as to evaluate the risk of profit and non-profit organizations being misused for ML/TF purposes.

Driven by the importance of mitigating ML risks in the real estate sector and to tackle other issues of relevance, the FMC drafted relevant regulatory amendments back in 2016, which was aimed at limiting cash transactions in buying and selling real estate. In 2017, several meetings and discussions were organized with legal scholars on the subject of the draft amendments. Following the required amendments, the draft r amendments were approved by the Government and presented to the National Assembly of Armenia. The approval of the draft amendments is expected in the first quarter of 2018.

In addition to strategic analyses, operational analyses are conducted as well to detect potential ML/TF cases. In the reporting period, a total of 280 suspicious transaction reports were analyzed. The suspicious transaction reportswere related to suspicions of money laundering and predicate offenses. The most common schemes in the analyses are as follows:

- Various fraud schemes, including:
  - Obtaining bank card information by way of mistreating cardholders, illegitimate transactions via virtual POS terminals by using stolen bank card information,
  - Attempts to legalize proceeds of crimes committed through the use of various mass marketing schemes.
- Transit flow of funds through the Armenian banking system, where the funds originateoutside of Armenia, in other countries with unknown (potentially criminal) sources,
- Financial transactions potentially aimed at tax evasion, illegal entrepreneurship and unreported economic activity,
- Other cases with similarities to the schemes described in the typologies published by the Bank.

Based on the results of analyses disseminations with ML hypothesis were made to law enforcement authorities and foreign financial intelligence units. The table below presents statistical data for 2016-2017 on disseminations made to law enforcement authorities resulting from analyses with ML hypotheses, as well as on requests made by the FMC to law enforcement authorities and vice-versa, instigated criminal cases and conviction.

	2016	2017
FMC referrals to law enforcement authorities	34	37
Information FMC requested from law enforcement authorities	11	5
Information law enforcement authorities requested from FMC	36	58
Criminal cases instigated	5	2
Convictions	0	4

Convictions had the following predicate offenses: theft, fraud, production and alienation of counterfeit payment instruments, and tax evasion. It should be noted that one of the four convictions was for a standalone ML offence.

Preventive measures

Preventive measures taken in the area of AML/CFT are of a key importance in terms of identifying, assessing and mitigating ML/TF risks. These are the instructions (notification) provided by the FMC to the reporting entities for suppressing the ML/TF risks identified as a result of strategic and operational analyses.

In the reporting period, 30 instructions (notifications) were cascaded to reporting entities. These measures were directed towards raising awareness on ML/TF risks and implementing preventive measures related to the following cases, including:

- Cases with elements of fraud schemes,
- Inflows and outflows from geographies associated with high risk,
- Cash transactions and business relationships,
- Risks inherent to mediated/transit flows of funds.

In addition to the above, the reporting entities were provided with feedback with the aim of informing them on the progress and results of the analyses.

In order to mitigate TF risks arising from the increasing international threat of terrorism, continued efforts were invested into collection of information in the context of international cooperation on financial transactions to and from geographies associated with high TF risk, directed towards the identification of potential sources of funding, patterns, schemes and persons involved in TF. The collected information

is systematically analyzed both by reporting entities and the FMC. The FMC analysis demonstrates that TF risks continue to be very low in Armenia. At the same time, instructions were cascaded to reporting entities in order to implement additional measures in relation to transfers to and from geographies associated with high TF risk and to collect maximum detailed information (where impossible, transactions are subject to refusal).

In order to effectively mitigate TF risks, continuous efforts were invested in the reporting period to implement the restrictive measures imposed by international organizations. In particular, the following information was published on the FMC website and notified to reporting entities:

- Updates in the lists published by or in accordance with the UN Security Council resolutions that stipulate for the freezing of assets of persons under, inter alia, UNSCR 1267/1989/2253 designations on ISIL (DA'ESH) and Al-Qaeda, UNSCR 1988 designations on the Taliban, and UNSCR 1718 designations on North Korea;
- The FATF statements on countries with strategic deficiencies in their AML/CFT systems, as well as on countries with such strategic deficiencies monitored by the FATF under its on-going global AML/CFT compliance process.

It is worth mentioning that Republic of Armenia continues to have a very low level of TF risk.

PROTECTION OF CONSUMER RIGHTS AND LAWFUL INTERESTS IN THE FINANCIAL SYSTEM

Protection of consumer rights in the financial market

The protection of consumer rights and lawful interests in the financial market by the Bank has been achieved through fair conduct of organizations providing financial services, provision of appropriate institutional environment and financial education.

Regulatory framework development

To encourage closer communication with guarantors, a number of requirements were defined for financial institutions in 2017. From now on, the guarantors will be notified of their rights and obligations, will receive their copy of the contract and will be informed of the change in the essential terms and conditions of the contract before signing the contract.

For stronger protection of the rights of users of insurance services, a number of requirements to information disclosure, transparency and communication were proposed to apply to insurance companies and insurance brokers. The draft developed requirements to easier access to information about the services provided through automated machines (ATMs, payment terminals, etc.) for executing financial transactions.

Minimum requirements were also proposed to the content of information and how such information should be published by financial institutions via the social media networks.

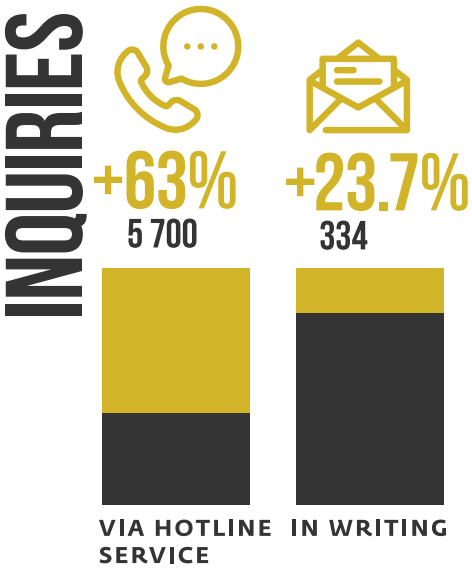
Oversight of business conduct

In 2017 the Consumer Protection and Financial Education Center continued on-site and off-site surveillance of financial organizations.

The on-site surveillance of many financial organizations has provided for studies which measured the adequacy of delivery of services, complaint and dispute resolutions, information disclosure policies and how they were applied, consumer exposures to risk and legal compliance.

As part of off-site examinations, the CPFEC monitored, on a monthly basis, radio advertising by financial organizations in addition to their TV commercials. The information of services provided by financial organizations published on the websites and the system Financial Assistant has been monitored on a quarterly basis.

In 2017, the CPFEC continued responding to consumer complaints received in writing and via a hotline service. During the year over 5700 calls were received via a hotline service. This means more than 3500 calls or a 63% increase of calls compared to the previous year. In 2017, the CPFEC received 334 complaints, which represents a 23.7% increase (67 more complaints) relative to the previous year.



Increasing the level of financial literacy of consumers in Armenia

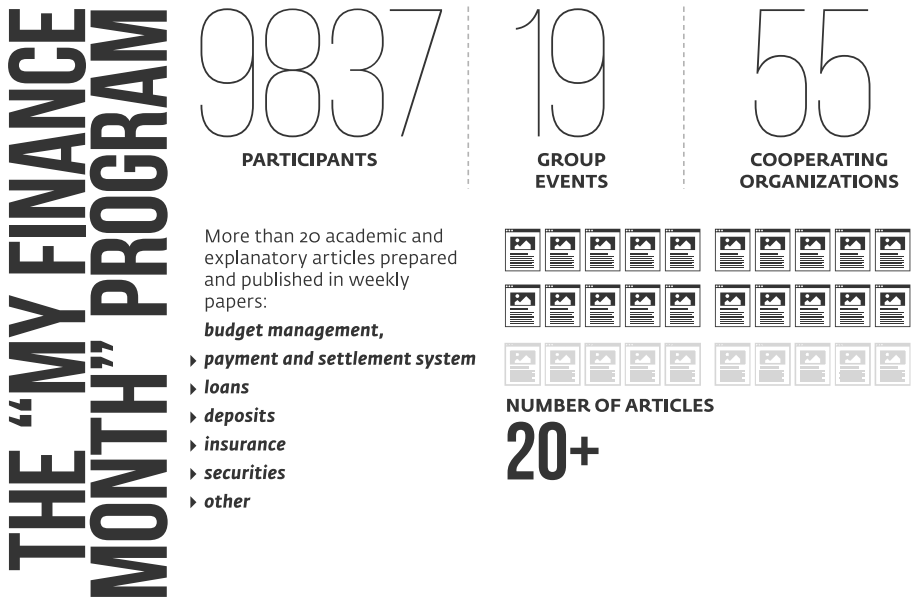
In September of 2017, there was a pilot launching of the component of financial education to 4 school curricula for children in grades 2-12. The project embraced 46 teachers having passed a relevant training and 1725 schoolchildren from a total of 13 schools.

In the reporting year, the "Financial Education in Rural Communities" program was underway and the assessment of its impact continued. In addition, in collaboration with the Consultative Group to Assist the Poor, 21 different financial education events were developed based on the behavioral research with a view to strengthening financial knowledge of people in rural communities.

Year 2017 saw the fourth "My finance month" program. With participation of 9837 people, a total of 55 organizations cooperated and 19 events were held in the framework of this financial education initiative. The CPFEC prepared and published more than 20 academic and explanatory articles on budget management, payment and settlement

system, loans, deposits, insurance, securities and so on. The program is aimed at helping the public get a clear understanding of finance and, particularly, the financial services. Other educational measures taken in 2017 included:

- The "History of Money Circulation in Armenia: Finance for All" exhibition,
- The "Seminars for the Military Personnel" project,
- The "Citizen" project,
- The "Good Camp" educational project, and
- The "Smartest" project.



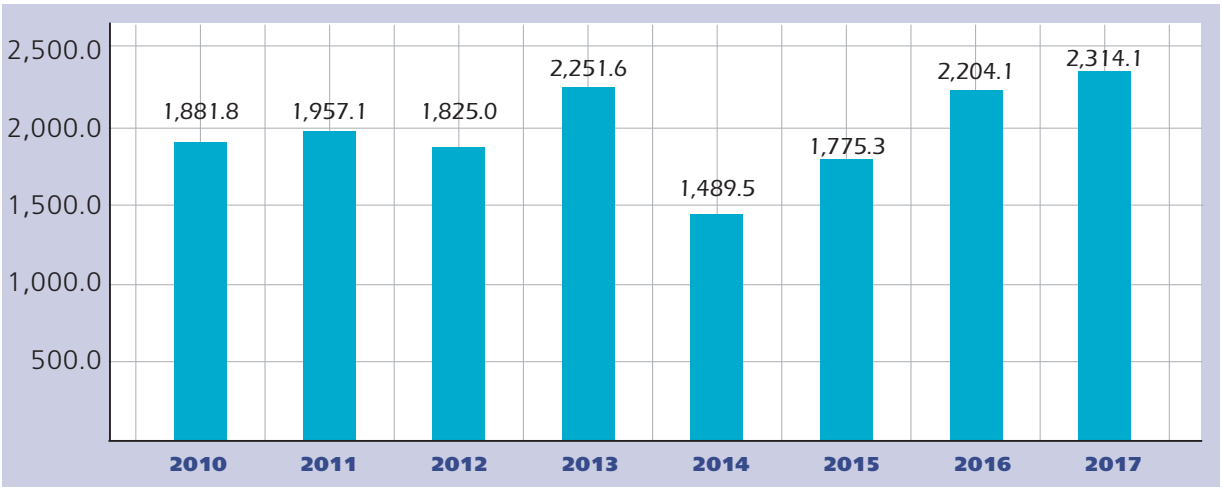
Work was done to provide further coverage of the funded pension scheme in Armenia.

As social media remains an important platform for stressing the importance of and increasing the interest in financial education, a variety of websites, including abcfinance.am (via same-name pages of Facebook, YouTube, Twitter) were further used to that effect. **The CPFEC enhanced its cooperation with international institutions supporting consumer protection and financial education, such as the Organization for Economic Cooperation and Development (OECD), the International Financial Education Network (INFE), the Alliance for Financial Inclusion (AFI), the Eurasian Economic Partnership, and the Child & Youth Finance International.**

INTERNATIONAL RESERVES MANAGEMENT

In 2017, gross international reserves of Armenia grew by about USD 110 million to nearly USD 2,314 million at the end of the year (see Figure 10).

Figure 10: International reserves of Armenia (million US dollar)



The growth of reserves during the year owed to around USD 426 million-worth inflow of funds and income from management of reserves, roughly USD 163 million-worth reduction of the balance on correspondent accounts of commercial banks and about USD 101 million-worth purchase of foreign currency at the domestic market. At the same time, repayment of the sovereign debt principals and interests amounted to around USD 286 million.

In 2017, Armenia's international reserves continued to be compliant with all adequacy requirements, particularly, in terms of Armenian economy's ability to absorb possible external shocks. In 2017, international reserves of Armenia averaged to about five months' of imports and nearly eight years' short-term (up to 1 year) liabilities.

05

INSTITUTIONAL DEVELOPMENT

Institutional development of the Central Bank

Dilijan Training and Research Center

INSTITUTIONAL DEVELOPMENT OF THE CENTRAL BANK

Governance of the Bank

The Board represents top management of the Central Bank, according to the Republic of Armenia Law on the Central Bank[4]. The Board consists of Chairman, two Deputy Chairmen of the Central Bank, and five Members. Chairman and Deputy Chairmen are included in the Board *ex officio*.

Chairman of the Central Bank is the highest official of the Bank. Chairman of the Central Bank is appointed by the Armenian National Assembly upon recommendation of President of the Republic of Armenia, for a 6-year term. Chairman is responsible for fulfilment of the Central Bank objectives[5]. Chairman coordinates the activities of the Central Bank; represents the Central Bank in the Republic of Armenia, other states and international organizations; exercises authority not reserved to the competence of the Board. Where Chairman is absent or otherwise unable to act, such powers are to be vested with one of the Deputies, and where Deputies are absent or otherwise unable to act, such powers are to be vested with the eldest Board Member of the Central Bank. Deputy Chairmen of the Central Bank are appointed by President of the Republic of Armenia, for a 6-year term. Chairman and Deputy Chairmen as well as Board Members cannot serve as a member of managing body of any party, be involved in activities other than scientific research, pedagogical and creative activities.

Board Members of the Central Bank are appointed by President of the Republic of Armenia for a 5-year term. Board Members cannot hold any other position in the Bank.

4 See details in the Republic of Armenia Law on the Central Bank.

5 The 2015 constitutional amendments have taken effect since April 9, 2018, whereby chairman of the Central Bank should be elected for a six-year term by the Armenian National Assembly upon suggestion by a relevant standing commission of the National Assembly, at the voting of at least three-fifths of the total number of deputies.

Accountability of the Bank

In fulfilling its objectives, the Bank is independent from state authorities of the Republic of Armenia. The Bank maintains its accountability pursuant to the terms and procedure determined by the Republic of Armenia Law, the Central Bank strategy and internal rules and policies.

The Bank presents the Monetary *Policy Program* and S*tatus Report on Implementation of Monetary Policy (Inflation Report)* as well as *Expenditures Estimate and Capital Investment Program*, with performance sheet papers, to the National Assembly of the Republic of Armenia. Furthermore, the Bank provides its "Annual Report of the Central Bank" for public disclosure. The annual report incorporates the Bank's annual financial accounts the compliance of which to international standards is verified every year by internationally recognized audit firms.

In addition to the aforementioned papers, the Bank publishes the following periodicals: *Financial System of the Republic of Armenia: Development, Regulation and Supervision, Financial Stability Report, Central Bank Bulletin, Central Bank Statistical Bulletin, Commemorative Coins of the Republic of Armenia.*

The Bank maintains accountability also through its official website (www.cba.am) which contains the Central Bank Development Strategy, regular issues of periodicals, the Board minutes and press releases on the refinancing rate, and other information on the Bank's operations and activity and the financial system as a whole.

Information security management

Seeking more technologically advanced information security management system, the Bank emphasized the need to develop the domestic financial and banking system's cybersecurity in 2017.

In March of 2017, the Board of the Bank decided to allow an obligatory evaluation of IT infrastructure vulnerabilities and regular testing of penetration by reputed firms specialized in the field.

With a view to early detection of cybersecurity threats and rapid response to incidents, the Bank initiated as establishment of a specialized platform for security officers of the Bank and commercial banks.

Many meetings and seminars on cybersecurity were aimed at raising the awareness and sharing of experience.

As a result, there has been a sharp decrease in the number of incidents threatening the information security with applied IT, more input by the financial and banking system participants in the field of security was observable, while qualification of security specialists has improved.

Cooperation with international organizations

In 2017, the Bank sustained its multilateral and bilateral cooperation with international financial institutions.

The visits of the IMF Armenia mission and management of the Dutch and Belgium subgroup during the year contributed to closer ties. Issues discussed during the meetings covered, among others, bilateral cooperation, current economic situation in Armenia, the fiscal and monetary policy, the strengthening of international reserves, reduction of public debt, maintaining of stability of the banking system. As the Bank continued coordinating the process of Armenia's sovereign rating in collaboration with international rating agencies, the representatives of "Moody's" and "Fitch", international rating agencies, paid visits.

There was further collaboration in developing international standards in the field of AML/CFT with international organizations and partner countries involved in introducing and implementing those standards, including cooperation with the Council of Europe's MONEYVAL Committee, the Egmont Group, the Parties to the Warsaw Convention, the Eurasian Group, the Board of Directors of CIS Financial Intelligence Units, as well as financial intelligence units of other partner countries.

As part of cooperation with foreign financial intelligence units, the Bank received 27 requests from those FIUs and made 12 thereto during 2017. The last two years' data suggest that most requests have been sent to the FIUs of the United States, Latvia and Russia, and, accordingly most requests have been received from those of Russia, Lithuania, Ukraine, USA and Moldova.

In order to expand business ties, learn the macroeconomic situation in the country and negotiate a variety of issues related to the banking business, financial institutions and representatives which visited the Bank in 2017 included the delegation of the National Bank of the Kyrgyz Republic led by Chairman Tolkunbek Abdygulov, the delegation of the Central Bank of the Islamic Republic of Iran led by President Abdolnaser Hemmati, the Eurasian Development Bank delegation led by Chairman Dmitry Pankin, the Black Sea Trade and Development Bank delegation led by Secretary General Serafeim Tsokas, the Bank of America Merrill Lynch representatives, the Russian VTB delegation led by President of the Bank Andrey Kostin, and etc.

During the year, the Bank has organized dozens of business meetings, conferences, workshops, round tables and forums.

Of these events, the following are worth mentioning:

- The annual meeting of the IMF and WB (Belgium/Netherlands) Constituency, with participation of over 100 delegates from 14 countries, headed by central and national banks' chairmen and finance ministers.



- The regular meeting of the Board of Heads of Central/National Banks of Eurasian Economic Union.
- The roundtable on the development of new technologies for non-cash payments in payment systems, organized in collaboration with MasterCard, with participation of commercial banks of Armenia.
- The 12th meeting of the Interstate Coordinating Board of Heads of Insurance Supervisors of the CIS Member States.
- The regular meeting of the Supervisory Board of the KfW Development Bank, Germany.
- The annual meeting of the Federation of Euro-Asian Stock Exchange, organized with the support of the Bank.
- The National Payment and Settlement System Development Consultation, with the participation of Eurasian Economic Union central/national banks' chairmen.

In 2017, the Bank concluded agreements, contracts and memoranda of understanding with central banks of other countries as part of both bilateral cooperation and in the framework of intergovernmental committees, as follows:

- The Memorandum of Understanding and Cooperation between the Central Bank of the Republic of Armenia and the National Bank of the Kyrgyz Republic signed on January 25, 2017.
- The Memorandum of Understanding on Cooperation in the field of Insurance between the Central Bank of the Republic of Armenia and the Insurance Bureau of the Central Bank of the Islamic Republic of Iran signed on February 9, 2017.
- The Loan Agreement on SME Funding for Energy Efficiency (Phase 2) signed on December 18, 2017 between the Central Bank of the Republic of Armenia and the KfW Development Bank of Germany, within the framework of the German-Armenian Fund's program, for an amount of EUR 15 million.

During the year, employees of the Bank attended a variety of events, including annual meetings, forums, international conferences on banking and finance, symposiums, roundtable meetings, consultations, exhibitions and workshops, in the framework of both technical assistance and bilateral and multilateral cooperation. Nearly 210 employees of the Bank appeared with reports and speeches on topics covering various aspects of the Bank's activities.

As part of bilateral cooperation in 2017, the Bank continued enhanced cooperation with international partner financial institutions as well as respected scientific and educational establishments.

Employees of the Bank actively participated in many training programs organized in Armenia and abroad, attended workshops and consultations, and paid visits for exchange of experience.

Human Resources management

At the end of December 2017 the Bank had 736 employees, working on open-ended and fixed-term contracts, of which 436 were women and 300 men. The average age of employees is 40. A total of 89 employees left the Bank during the year in comparison with the previous year's figure of 32.

The year was remarkable in terms of structural changes. With the view to increase labor productivity and redistribute functions, the Bank carried out reorganization of a number of its structural units, which has reduced 34 job positions.

As much as 17 vacancies in the Bank were filled based on the winning results of the relevant competition. During the year, 60 employees earned promotion (four of who for a managerial position) for taking up a function of increased complexity.

The Bank further maintained a policy that encouraged recruiting young specialists (with no professional experience) while providing them with an opportunity to grow professionally and fill up vacancies in the future. Eight young specialists signed fixed-term employment contracts with the Bank after having completed the regular two-month program "The Central Bank: an introductory course" in 2017.

In 2017, a total of 105 students from tertiary enrollment in Armenia took their research internship at the Bank.

During the year, 25 applicants participated in the Isahak Isahakyan Stipend Eligibility Contest announced by the Bank. The best of them – 1 from Yerevan State University (Ijevan branch), 1 from Armenian State University of Economics and 1 from Artsakh State University were awarded the Isahak Isahakyan Stipend. Introduced in 2003, the Isahak Isahakyan Stipend has been granted so far to 90 best students with economic background.

During the year, 50 employees of the Bank lectured at a number of universities and other educational establishments, delivering their knowledge and experience to young professionals.

Staff training and professional qualification

As part of staff training and development policy which contributes to career growth of employees of the Bank, further measures were taken to enhance professional integrity of the staff in 2017.

In 2017, employees of the Bank passed training at banks, other financial institutions and training centers abroad and educational centers, including Dilijan Training and Research Center, in Armenia, and benefited from attending courses led by lecturers of well-known international universities.

During the year, 187 employees of the Bank participated in trainings organized by the above-mentioned institutions to enhance professional knowledge and improve skills in the field of strategic development of the Bank.

With further commitment to sharing of knowledge and expertise accumulated over the years, the Bank has organized, by the use of internal resources, 10 seminars for as much as 428 employees to communicate its current issues and functions and to help them develop important skills for professional activities.

In the reporting period, 17 employees took online training courses on financial supervision offered by the Financial Stability Institute.

Job rotation, another tool for professional development, was offered to 8 employees of the Bank in 2017 to make sure a reserve of managerial staff is in place and both experienced professionals and young specialists are given a chance to broaden their knowledge.

During the year, employees of the Bank passed international certification and qualification exams in the field of finance, accounting, audit, insurance, information technologies. As of 2017, 63 employees had international certificates of qualification and 53 were taking exams. **Six employees of the Bank are full members of CFA and ten are full members of ACCA.**

Public relations

In 2017, further work was done by the Bank to communicate its activity in exercising financial regulation, coordinating the financial sector as well as events in the financial market to the general public.

The Bank regularly announced its actions, projects, undertakings about monetary policy, financial supervision and financial stability to financial market participants and general public, and arranged meetings to discuss matters of interest.

During the year, 8 Board decisions on repo operations (refinancing rate) were published. Brief statement on the Board decisions came immediately after the decision by the Board while the Board Minutes

were published within 10 days. A total of 4 Board Minutes were published in the periodical “Inflation Report”.

A number of meetings with the participation of mass media managers and representatives of the Bank management were organized during the year. Social networks remain an important platform for the Bank to publish news, messages and other materials featuring its activities.

During the year, the Bank organized 5 events with the participation of mass media and 41 interviews. In 2017, the Bank received 19 queries in writing to which responses were given through an established procedure under law. The Bank answered promptly to numerous oral queries. Full answers were provided to 178 online inquiries from individuals and organizations. There were 32 releases on the Board meetings and 12 releases on repo interest rate of the Bank published during the year.

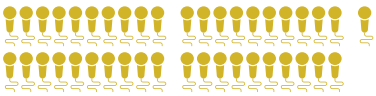
PUBLIC RELATIONS

EVENTS ORGANIZED BY PRESS SERVICE OF THE BANK

5

INTERVIEWS

41



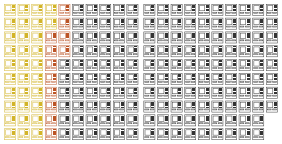
19
QUERIES IN WRITING

178
ANSWERS TO ONLINE INQUIRIES

THE NUMBER OF PRESS RELEASES

198

32 ON THE BOARD MEETINGS OF THE BANK



12 ON INTEREST RATE OF REPO OPERATIONS

Visitor Center [6]

In 2017, the Visitor Center of the Bank was a winner in the "Financial PR of the Year" nomination offered by the Armenian PR Association, an education and information body, for promulgating the history of money circulation and the monetary policy.

In 2017, the Center hosted 9 815 visitors in c. Yerevan and 11 515 visitors in the regions of Armenia. This attendance rate is 9.5% higher from the relevant figure (10 513 visitors) reported in the previous year.

The Center continued its educational project "One Day at the Central Bank" for the servicemen and alumni of educational institutions of the Armenian Ministry of Defense. During the year, the Center received a total of 218 servicemen/alumni and teaching staff.

In May 2017, the Visitor Center participated in the international program "Museums Night", and hosted 1306 visitors in the framework of that event.

In 2017, the Center arranged an exhibition of numismatic – historical and cultural – values of State Treasury of Armenian Ministry of Finance.

In September 12-19, 2017, a regular traveling exhibition titled "History of Money Cycle in Armenia: finances for all" was organized in Kapan, the regional center of Syuniq. The event consisted of two parts – a film that featured the history of circulation of the Dram and a series of seminars on personal finances. Such exhibitions help people and especially schoolchildren and students learn more of the history of the national currency, the security features of the Dram, the main functions of the financial system, the rights of users of financial services. The exhibition in Kapan gathered 1 700 visitors (schoolchildren, students, teachers, lecturers and general public).

In 2017, the Visitor Center cooperated with the Children of Armenia Fund, the Jinishian Memorial Foundation, the Junior Achievements of Armenia, the AGBU Vache and Tamar Manoukian High School (California), the Armenian PR Association, the "Armenia Education" foundation, the "Retail Group Armenia", the IAB International Business Academy, the "Khnko-Aper" National Children's Library, the "Youth Development and Empowerment Institute", the AMI Club, the "Smash Studio", the "Astgh 8", the Montessori City Armenia, the "Happy Day" children summer schools, as well as with the Office of Financial System Mediator, as it hosted schoolchildren from all regions of Armenia.

During the year, educational and informational trainings were also organized for the teachers of Yerevan High School No. 115 and of a number of schools in Gyumri and rural communities of Shirak region.

6 See details on www.visitorcentre.cba.am, www.museum.cba.am, www.cba.am.

Internal audit

The function of internal audit of the Bank is entitled to the Audit Group which is set up by the Board of the Bank according to the Republic of Armenia Law on the Central Bank. The Group performs its functions in compliance with Armenian law, International Professional Practices Framework of the Institute of Internal Auditors as well as statutes developed by COSO Internal Control - Integrated Framework and CobIT information technologies documentation.

The Bank's internal audit function is performed in line with the definition of internal auditing and standards as well as the ethical rules, according to external evaluation report of experts of the Bank of Netherlands. To this end, most recent evaluation was carried out in 2017, and the Bank's Audit Group has again given the highest "Compliant" ranking.

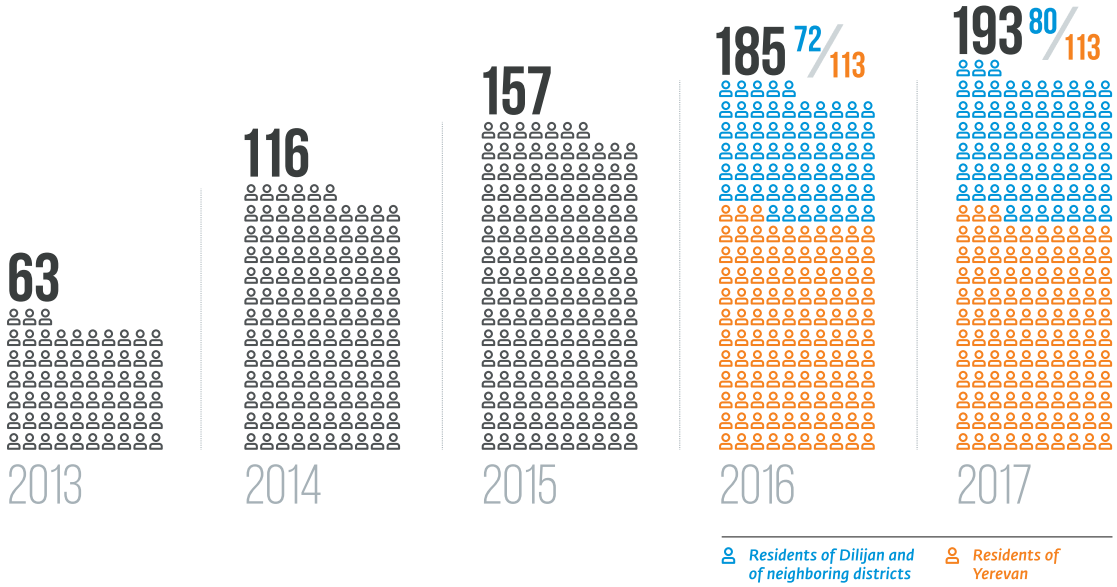
The employees of the Audit Group are members to the Institute of Internal Auditors, Information System Audit and Control Association, Association of Chartered Certified Accountants, and hold international qualification (CIA, CRMA, CISA, CRISC, ACCA) as established by these institutions.

DILIJAN TRAINING AND RESEARCH CENTER

The Dilijan Training and Research Center of the Bank continues its path to becoming a leading research, scientific and educational institution at the regional level. In 2017, the Dilijan TRC reported significant achievements and success in the field of research, international cooperation and social responsibility. **The Bank's mission is to make the Dilijan TRC an academic environment that will facilitate research activities through a study of current problems of the economics and international experience of how these can be handled in practice. Seeking to foster an environment where the decision-making is research-based, the Dilijan TRC will provide high-quality research on emerging economies and support the effective fulfilment of the objectives of the Bank.** The Dilijan TRC in

DILIJAN TRAINING AND RESEARCH CENTER

STAFF



increasingly recognized as a place where representatives of central banks, other financial institutions, international organizations and private sector businesses of Armenia, countries of the region, Eastern European countries can meet and research can be done. **In 2017, more employees of the Bank were relocated to the Dilijan TRC, and now it has 193 employees.**

In 2017, employees of the Dilijan TRC continued research activities which started in 2015. During the year, the Dilijan TRC arranged advanced courses on economics which were conducted by reputable experts invited from the world's best universities and international organizations.

In 2017, Junior Maih, a consultant/senior economist at the National Bank of Norway and Business School Prof. of Economics, Xavier Raurich, a lecturer of Barcelona University, Christiano Lawrence Joseph, Prof. of Economics at Northwestern University, USA, Tigran Poghosyan, an IMF economist and others visited the Dilijan TRC to deliver consulting and lectures and for joint research activities.

The Dilijan TRC's activities in the reporting period included a tax policy survey in collaboration with the Armenian Ministry of Finance, the central banks' transparency assessment under general programs implemented in cooperation with the IMF, a number of analyses on economic growth potential of developed economies in the aftermath of the financial crisis, a financial inclusion and financial literacy survey in conjunction with the Asian Development Bank Institute. Most of the surveys will be published in 2018 as working papers for international institutions and the Bank.

The cooperation with the World Bank continued in 2017 in the framework of the program on developing effective ways in increasing financial literacy. The program constituted behavioral studies through interviews which the relevant staff of the World Bank and the Bank conducted in a handful of rural communities – about 15 villages of Tavush, Lori and Gegharqunik regions of Armenia. The studies have revealed behavioral assumptions which would underlie the formulation of a more effective financial literacy policy.

As part of cooperation with the American University of Armenia, specialists of the Dilijan TRC had an opportunity to teach at the University's Master of Economics program, which is being carried out at the TRC. In 2017, 41 students studied here in two stages.

In 2017, eight students from Harvard, Stanford, Bocconi, New York, and London universities passed their summer pre-diploma internship at the Dilijan TRC.

In 2017, the Dilijan TRC organized dozens of regional and international symposiums, conferences, workshops, training courses, a technical ideas hackathon, forums and such other events.

In May 2017, the first phase of the "Central Bank and Commercial Bank Employee Certification" program took place in the International Financial Cooperation Center of the Bank in Vienna, Austria. It was organized by the joint efforts of the Central Bank of Armenia, the Government of Netherlands and the Development Financial Institution. The second phase of the certification took place at the Dilijan TRC in September. The lecturers of the program included Prof. Dr. James Stock of Harvard University, Prof. Jaume Ventura of Barcelona University, Prof. Dr. Florencio Lopez de Silanes (SKEMA B.Sch and U.S.NBER) Business School and National Bureau of Economic Research, and Prof. Dr. Joseph A. McCahery (Tilburg University).

The Bank has implemented the "Advanced Macroeconomic Policy Modeling" at the Dilijan TRC, in collaboration with the IMF Research Department. This is intensive training project which brings together researchers and academics from macroeconomic policymaking institutions across the world. The work drafts prepared on the basis of the research under the project have been submitted to the IMF.

The cooperation with partner organizations involved:

- An international training course on "Issuance of New Series of Banknotes" organized with the participation of experts from Giesecke և Devrient.
- A regional conference on "Climate Change, Credit Analysis and Asset Allocation in Low-Income Environment" held jointly with "Amundi".
- An international training course on "Protection of Interests of Policyholders and Ensuring Financial Stability through Risk-Based Supervision and Proportionality" with the participation of Financial Stability Institute of the Bank for International Settlements.
- An international training course on "Consolidated Supervision" organized jointly with the Toronto Center.
- The "Dilijan International Summit" held at the Dilijan TRC, aimed at bringing together young people who want to create their own start-ups in Armenia.
- The Consultative Discussion on "Armenia's Administrative and Territorial Development Reform and Investment Environment" held at the Dilijan TRC.

The Dilijan TRC has arranged 6 educational programs for the Economic Research Department employees of the Bank with the participation of lecturers from leading educational establishments around the world. The aforementioned programs and other events organized at the Dilijan TRC provide the participants, including the Bank staff, with an opportunity to study the industry's international experience, which allows making further analyses and research and raises the effectiveness in performing the tasks.

As part of cooperation with central and national banks of member states of the Eurasian Economic Union, the Dilijan TRC has arranged a number of seminars involving 144 representatives of banks from both EEU and other countries. The Bank has arranged tailor-made courses for sharing experience and presenting best practices of the Bank.

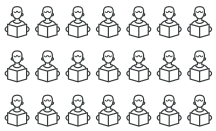
DILIJAN TRAINING AND RESEARCH CENTER

EDUCATIONAL AND TRAINING PROGRAMS

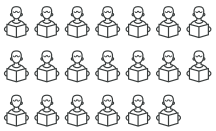
60+ EVENTS

1000+ PARTICIPANTS

AMERICAN UNIVERSITY OF ARMENIA



GROUP 1 **21**



GROUP 2 **20**

WORK INTERNSHIP



2014 **3**

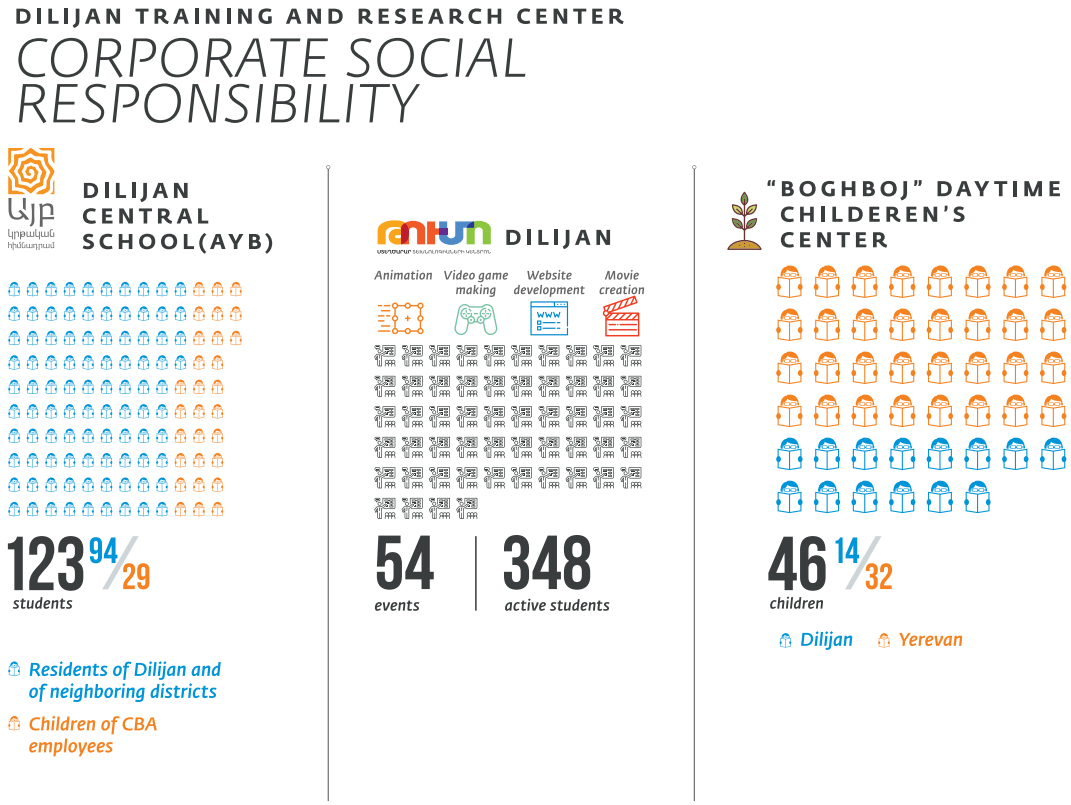
2015 **9**

2016 **6**

2017 **8**

Social aspect

Contributing to the development of the town Dilijan remains the Bank's mission as a key corporate social responsibility component.



The normal functioning of the Dilijan Central School, the Tumo Center for Creative Technologies, the Knowledge for Development Center's Library and other important infrastructures continued by the support of the Bank. Further educational programs are aimed at facilitating comprehensive development of children.

- The Knowledge for Development Center encourages the town children and children from rural communities in the vicinity to use the library's rich literature, share a common platform for interaction and debate, take part in open classes and go to events organized by the Center. In 2017, the Knowledge for Development Center served more readers, totaling 1649. Compared with the previous year, the library provided 287 more books, amounting to 5328. The Center was proactive in organizing a great variety of events (as much as 128, with involvement of more than 2000 participants) to let them develop creativity in themselves. The Knowledge for Development Center's Museum opened at the Dilijan TRC in February 2017 and has since received 2005 visitors and arranged more than 50 intellectual events. The Center has launched a new "Citizen On-the-Go" initiative – a platform where people, successful

in any particular field, will share their experience and knowledge with children, revealing the pros and cons of that field, which will help children with professional orientation. More than 500 children have participated in this initiative.

- The Dilijan Central School, which is managed by AYB educational foundation, currently has 123 schoolchildren nearly 80% of who are Dilijan residents, while part of the teaching staff having passed training by the AYB educational foundation curriculum, live in the neighborhoods.
- In 2017, the number of young people having attended TUMO, a center for creative technologies, was 348. This project proved increasingly attractive to teenagers aged 12-18. Over time, the spectrum of projects for creative technologies offered by TUMO has expanded to include 54 general courses and 4 specific courses.

DILIJAN TRAINING AND RESEARCH CENTER

CORPORATE SOCIAL RESPONSIBILITY

KNOWLEDGE FOR DEVELOPMENT CENTER

LIBRARY

120+
EVENTS

1649
SUBSCRIBERS

2 000+
PARTICIPANTS

10 000+
BOOKS

MUSEUM

50+
EXCURSIONS

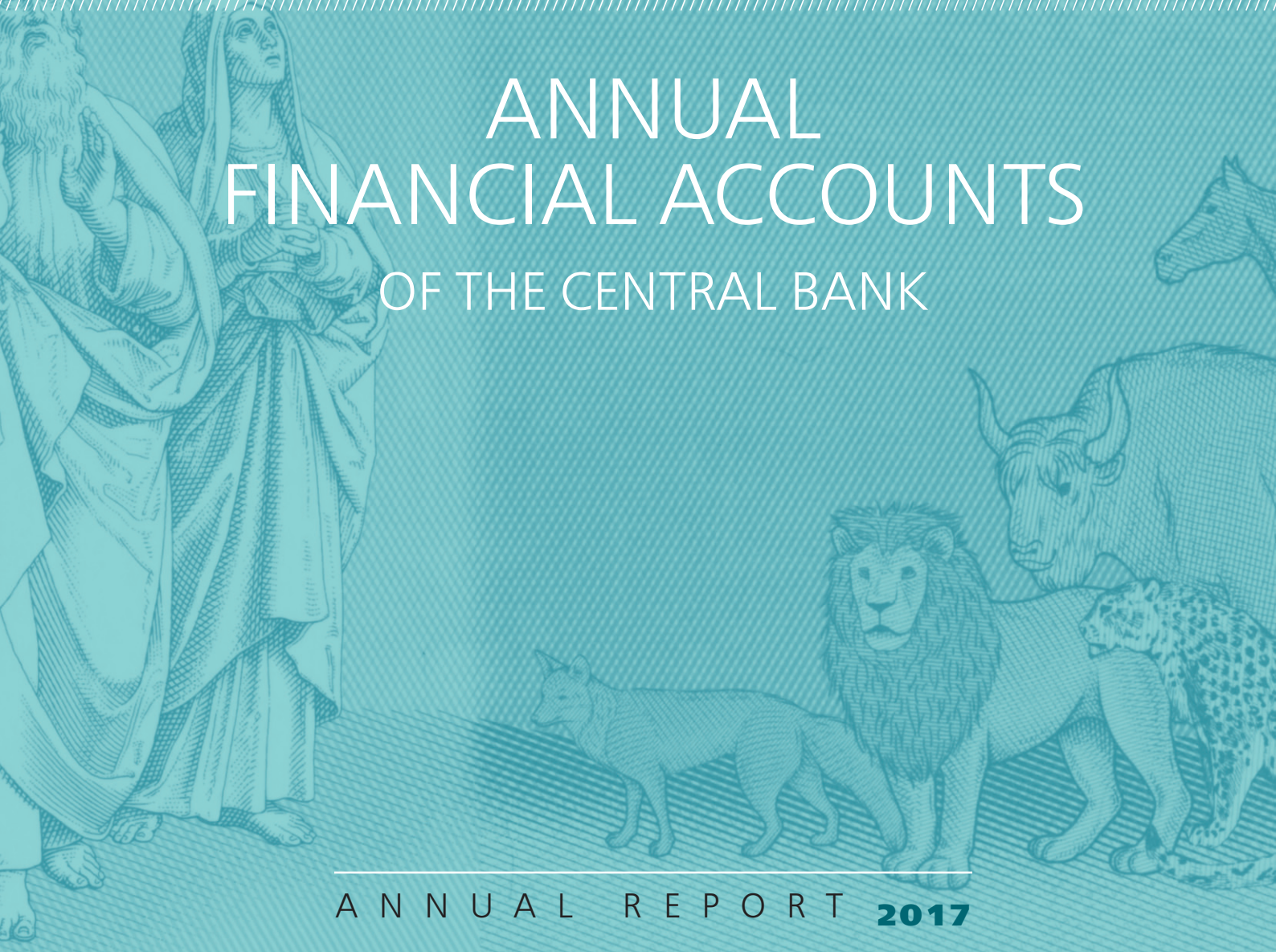
2 000+
VISITORS

50+
AWARENESS COURSES

06

ANNUAL FINANCIAL ACCOUNTS

OF THE CENTRAL BANK





CENTRAL BANK
OF ARMENIA