

Conclusion of the Central Bank of the Republic of Armenia issued with regard to the
“Annual Report on Execution of State Budget 2024
of the Republic of Armenia¹”

Macroeconomic environment²

In the course of 2024, the risks to economic growth slowdown persisted in the global landscape and the main trade partner countries to Armenia amid ongoing geopolitical tensions and uncertainties. This was accompanied by a continued decrease in inflation, although in trade partner countries the prices of goods and services (those known to have sticky prices) remained relatively high. In such a situation, central banks maintained relatively tight monetary conditions.

The high economic growth recorded in the Republic of Armenia at the beginning of 2024 gradually slowed down, reaching 5.9% for the year. Even though 1 percentage point lower than the Republic of Armenia Government’s target value, the growth indicator came to shaping around a long-term sustainable potential growth level. The sectors of the economy such as construction, trade and services continued to contribute significantly to economic growth. The 2024 economic growth was further influenced by the concentration of growth in specific sectors on the one hand and by individual short-term factors, on the other. This has brought in considerable uncertainties over the sustainability of economic growth, the long-term outlook, as well as future trends in domestic demand.

The economic growth in 2024 was concurrent with a gradual slowdown in high external demand shaped in recent years, which was reflected in a continuous decrease in non-commercial remittances and tourism flows. In the meanwhile, domestic demand has been regaining momentum, as both private consumption and investment, including public investment are growing high. At the same time, based on the year’s results a double-digit growth in foreign trade was posted owing mainly to high volumes of re-exports. Moreover, the export growth outpaced the import growth, as a result of which the net export position improved and positively contributed to the economic growth. In parallel, a modest rebound in domestic demand contributed to a continued widening of the current account deficit, which moved 1.6 percentage points closer to its estimated sustainable level relative to GDP.

It is also noteworthy that with economic activity slowing down and economic growth approaching its potential level, the fiscal policy had a close to neutral, slightly expansionary impact on aggregate demand, mainly due to the reported growth in public consumption and capital investment compared to the previous year.

Thus, in 2024, Armenia’s economic growth has moderated toward more sustainable long-term levels; however, certain structural characteristics of the economy continue to present **uncertainties and risks in terms of achieving relatively inclusive, sustainable, and long-term high growth**.

¹ In the context of preparing its conclusion on the state budget execution report, the Central Bank of the Republic of Armenia bases its assessment of budget execution on a set of principles, including ensuring medium-term debt sustainability, the cyclical direction and stance of the fiscal policy, the promotion of long-term economic growth, and other relevant considerations.

² The numerical data and estimates in this document are taken from the report on the execution of the State Budget 2024 of the Republic of Armenia, relative to the adjusted budget plan.

Inflation and monetary policy

In 2024, the inflationary environment in the economy remained sluggish, largely due to the still deflationary spillover effects from the external sector, as well as the weakening of external demand for some domestic services. It should also be noted that the overall demand environment and labor market conditions softened and stabilized to a certain extent, contributing to a decline in wages, a moderation in the inflation of services with typically sticky prices, and a reduction in inflation expectations. In this situation, the 12-month inflation remained below the target throughout the year, amounting to 1.5% in December of 2024. Moreover, the 12-month core inflation also remained low during the year, making up 0.9% at the end of the year.

Given the 12-month inflation slowing considerably, the trends of gradual adjustment in demand and inflation expectations, as well as the relatively stable level of inflation in wages and non-tradable goods known to have typically sticky prices, in 2024 the **Central Bank of the Republic of Armenia continuously reduced the policy rate by a total of 2.25 percentage points** (setting it at 7.0% at the end of the year).

Fiscal policy

The fiscal policy for 2024, in line with the Government's medium-term program, followed the principle of increasing investment levels to enhance economic potential while maintaining debt sustainability. However, in the context of the economic growth slowdown and structural peculiarities, on the one hand, and the implementation of fiscal support programs aimed at addressing urgent needs in individual sectors, on the other, **the fiscal policy has somewhat deviated from the target benchmarks**. As a result, with a lower-than-expected economic growth and gradually weakening aggregate demand, **the fiscal policy had a close-to-neutral, minor expansionary impact on aggregate demand in 2024** (the fiscal impulse reaching 0.5).

The slowdown in economic growth in 2024 affected tax collection, recording lower-than-planned tax growth rates. Thus, tax revenues increased by 5.1% compared to 2023, and the tax-to-GDP ratio decreased by 0.5 percentage point to 23.6%³. It is worth noting that tax-to-GDP ratio was 1.3 percentage points below the projection for the year, also falling behind the target benchmark set for the medium term. This is primarily determined by structural changes in tax bases, taxable consumption, and, specifically, imports aimed for domestic consumption, amid slowing economic growth. **As a result, the revenue impulse had a minor expansionary, near-to-neutral, effect on aggregate demand**. It should be noted that the significantly lower-than-planned tax revenues during the year have created risks in terms of the current year's fiscal deficit and public debt increase, and the overall impact of fiscal policy on demand.

Thus, in 2024, **the prevalence of short-term factors in the structure of economic growth once again underscores the importance of implementing tax policy adjustments that are aligned with the economy's structure and of ensuring greater efficiency in budgetary redistribution to meet targeted tax revenue objectives**.

³ The revenue and expenditure indicators for the period 2020–2023 included income tax refunds on mortgage loan interest under revenues, whereas in 2024, these were recorded under expenditures. As a result of this change in the accounting methodology for tax revenues – specifically the treatment of interest refunds on mortgage loans – the growth in tax revenues and state duties is estimated at 4.5%. It should be noted that in 2024, the refunded amount totaled approximately AMD 68.6 billion.

Following the principle of enhancing economic potential and achieving the targeted economic growth rate, the 2024 state budget expenditure policy continued to prioritize increasing capital expenditures and implementing fiscal support programs addressing urgent social needs⁴. As a result, the 2024 state budget expenditures increased for both current and capital programs; however, actual spending fell short of planned levels, indicating under-execution across expenditure items. Thus, the 2024 state budget expenditures of the Republic of Armenia have grown by 16.0% relative to the previous year due to a 16.3% increase in current expenditures and a 12.8% increase in expenditures on non-financial assets⁵. This has been concomitant with a smaller increase – 1.7 percentage points – in the ratio of public spending to GDP, compared to the planned 3.0 percentage points. The deviation was primarily due to lower-than-projected capital investment, which fell short by approximately 1.3 percentage points. As a result, the share of state budget expenditures in GDP for 2024 has grown to 29.2%, with the share of current expenditures-to-GDP ratio increased by 1.3 percentage points compared to the previous year, and expenditures on non-financial assets increased by 0.3 percentage point. It is noteworthy that despite the growth in capital investments, it stood behind the target set for the year and the Government's program and amounted to 5.5% of GDP.

In view of the above-mentioned developments in the field of public spending, the budget expenditures had a close-to-neutral, slightly expansionary impact on aggregate demand.

It is worth noting that the execution of capital expenditures, which in recent years has been accompanied by a continuous increase in projected volumes, has deteriorated to some extent in 2024. Thus, the execution rate of capital expenditures stood at 84.7% of the revised plan, compared to 95.8% in the previous year, and 78.5% relative to the original state budget. In such a case, **there is need to emphasize that the issue of increasing the efficiency of capital program management and implementation remains relevant. Moreover, any under-execution of capital expenditures creates a risk to ensuring the target indicators of potential economic growth in the medium term.**

As a result of the relatively low execution of both state budget revenues and expenditures, **the budget deficit in 2024 – though below the level projected for the budget – was more than twice the size of the previous year's deficit.**

Thus, in 2024, the state budget deficit of the Republic of Armenia increased by AMD 187.2 billion compared to the previous year and amounted to AMD 376 billion, standing 17.6% below the indicator projected under the program. The deficit as a share of GDP also came in below the projection, amounting to 3.7%, compared to the projected 4.6% figure and against that of 2.0% in 2023. At the same time, the budget execution was carried out in compliance with fiscal and budgetary rules, and throughout the year, the state budget deficit of the Republic of Armenia remained consistently below the level of capital expenditures. In 2024, as in the previous year, a substantial part – as much as 95.5% – of the deficit was covered by domestic funding sources, while the deviation from the projected external financing remained lower than expected. It is noteworthy that the budget deficit financing costs have decreased somewhat in the course of 2024 on the back of falling interest rates on government bonds thanks to the gradual easing of monetary policy.

⁴ Specifically, urgent social needs included the allocation of financial resources to support the people forcibly displaced from Nagorno-Karabakh and the areas affected by floods.

⁵ The increase in expenditures compared to the previous year's figure (excluding refunds for interest payments on mortgage loans) amounts to 13.3%. Relative to the previous year, the state budget expenditures-to-GDP ratio has increased as well, from 27% to 28.5% (excluding refunds for interest payments on mortgage loans).

As a result, although the fiscal policy in 2024 was largely neutral, the **fiscal challenges stemming from the structural characteristics of economic growth, along with the continued under-execution of capital expenditure programs, brought about certain uncertainties and risks in terms of maintaining an appropriate stance of the fiscal policy within the economy.**

The Republic of Armenia Government debt burden in 2024 remained below the 50% threshold set by Armenia's fiscal rules, reflecting fiscal and debt sustainability, as well as a continued positive macroeconomic environment. Thus, in 2024, amid low growth in government debt relative to nominal GDP, the debt-to-GDP ratio decreased by 0.1 percentage point compared to the previous year and amounted to 48.3%. It should also be noted that the Government's debt burden was also lower than the indicator set by the 2022-2026 debt burden reduction program.

Subsequently, alongside the implementation of state investment programs aimed at enhancing the economy's potential in 2024, we may record that ensuring public debt sustainability and applying an adequate and effective debt management strategy in the context of budget deficit financing are key prerequisites for **maintaining fiscal policy flexibility, sustaining programs that target medium-term economic growth, and establishing the necessary safeguards for improved debt servicing prospects.** In summary, let us assert that despite persisting challenges and uncertainties, as well as the slowdown in economic growth and structural peculiarities, the effective combination of fiscal and monetary policies **made it possible to ensure macroeconomic stability in the Republic of Armenia** in 2024. However, amid emerging macroeconomic uncertainties, the outcomes of the fiscal policy implemented in 2024 diverged from the medium- and long-term objectives. In this context, **the Central Bank of the Republic of Armenia highlights the importance of measures aimed at achieving the necessary sectoral redistribution stemming from the structural characteristics of economic growth, as well as the need to ensure the projected levels of state capital expenditures.** At the same time, in the context of effectively balancing fiscal sustainability with economic stimulus over the medium term, the Central Bank of the Republic of Armenia emphasizes that taking up consistent and effective measures to achieve the targets set by the Armenian Government is important.