



**Central Bank**  
of Armenia

**2025 Q3**

# **Monetary Policy Report**

Monetary Policy Program

Published September 16, 2025

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In addition to the Monetary Policy Report, the CBA concurrently publishes additional materials on its website, which the reader is encouraged to reference. These include the [MPR Chart Pack](#) (containing statistical charts and tables for global and domestic economic developments as well as the illustrative scenario projections) and the [Transparency Report](#) (providing transparency into how the Board of the CBA arrived at its decision).

**DISCLAIMER** The data presented in this report is current as of September 12, 2025.

# 01 |

## Executive Summary

# A. Executive Monetary Policy Statement

At its meeting today, the Board of the Central Bank of Armenia decided to keep the key policy rate (refinancing rate) unchanged at 6.75%.

Annual CPI inflation increased slightly in Q3 2025, standing at 3.6% in August. Meanwhile, core inflation edged up, standing at 3.7% Y-o-Y in August.

In Q3 2025, risks of a further slowdown in demand conditions globally and in Armenia's key partner economies persist, while inflationary pressures in the US have intensified. Uncertainty surrounding US trade policy and its macroeconomic implications remains elevated. Uncertainty has also increased regarding the medium-term implications of US fiscal policy, including the extent of aggregate demand support, the resulting rise in public debt, and its potential impact on long-term interest rates. At the same time, persistent geopolitical uncertainty and tensions in international trade relations continue to pose risks of supply chain disruptions and renewed global inflationary pressures. Further, global food prices have ticked up since the beginning of the year, primarily driven by supply factors. A persistence of these trends could be a primary source of further increases in global inflationary pressures. In this context, considering weakening demand conditions on the one hand and persistent inflationary risks on the other, central banks in major economies would be expected to either maintain or gradually ease their tight monetary stance.

In the third quarter of 2025, economic activity in Armenia continued to accelerate. Growth in demand-driven sectors continues to offset the gradual dissipation of certain short-term, non-structural growth drivers. Sustained, robust growth in the construction and services sectors has remained the key driver of overall economic activity. Following sustained declines in 2024 and Q1 2025, external demand for services has increased in Q2 and Q3. At the same time, uncertainty remains elevated regarding the sustainability of this growth, its long-term trajectory, and the future outlook for domestic demand. In this context, demand continues to have a neutral impact on inflation, while recent increases in headline and core inflation have been driven by supply-side factors. Wage growth, non-traded sticky price inflation, and inflation expectations continue to stabilize. At the same time, risks for medium-term demand pressures from fiscal policy persist.

In the context of current macroeconomic developments, financial markets in Armenia generally expect the Central Bank of Armenia to gradually lower the refinancing rate over the next twelve months to approximately 6.25%.

In order to manage possible risks stemming from conditions of high uncertainty, the Board considers multiple scenarios during its deliberations. On the one hand, the Board discussed Case A-type scenarios where possible underlying developments would require a higher path for the policy rate relative to current market expectations. This includes scenarios related to risks of a rising neutral rate globally and in Armenia in the context of fiscal policies, as well as risks of expanding demand conditions. On the other hand, the Board also discussed Case B-type scenarios where potential economic developments imply a more rapid and aggressive downward path for the policy rate than what is currently priced in markets. These scenarios include concerns regarding a weak demand environment forming and deepening in the economy due to a potential gradual adjustment of real estate prices, as well as overall concerns about the outlook for the global economy.

Seeking to manage the macroeconomic implications that could stem from Case A-type scenarios materializing, the Board finds it appropriate to keep the policy rate unchanged in the current round.

The Board resolutely affirms its commitment to adopting the appropriate policy actions and strategy to ensure the price stability objective of 3% inflation in the medium term.

Approved by the Board of the Central Bank of Armenia  
September 16, 2025

**Governor**  
Martin Galstyan

**Deputy Governors**  
Armen Nurbekyan  
Hovhannes Khachatryan

**Board Members**  
Davit Nahapetyan  
Artak Manukyan  
Levon Sahakyan  
Narek Ghazaryan

## B. Summary of Economic Conditions

### Global Economy

In Q3 2025, the global growth outlook has continued to deteriorate. In the United States, recent volatility in GDP growth due to swings in imports and inventories adds uncertainty about the health of the underlying economy and aggregate demand conditions. Consumption, the major driver of US growth in the post-Covid era, has shown signs of cooling while still remaining broadly elevated. Further, sharp downward revisions to Q2 labor data suggest meaningful weakening in labor market conditions. At the same time, significant tightening of migration policy could create labor supply issues and bring about excessively tight labor market conditions, fueling risks of further inflationary pressures.

Amid these conditions, uncertainty surrounding the outlook for US economic policies—particularly trade and fiscal policy outlook—remains elevated. Given the significant expected expansion of the fiscal deficit and national debt, risks of a potential rise in long-term interest rates have deepened. Such developments could impact not only the future course of the Federal Reserve's monetary policy but also impact the neutral interest rate in, and capital flows to, emerging markets.

While US inflation continued to gradually recede toward the target in recent quarters, trade policy continues to pose meaningful upside risks. A significant increase in imports and inventories in Q1 helped shield consumers from increased prices, but recent three months have shown signs of growing inflationary pressures emerging for consumer goods most sensitive to tariffs. An acceleration of these trends could bring about a significantly more inflationary environment, but the extent and nature of any inflationary acceleration would depend on the trajectory of domestic demand conditions. These issues significantly complicate the Federal Reserve's trade-off between maintaining price stability and achieving full employment, a challenge that is further compounded by potential risks of deteriorating central bank independence.

Following a strong uptick in growth in the Eurozone in Q1 2025 due to short-term factors, growth in Q2 slowed meaningfully to 0.1% Q-o-Q, reflecting sustained structural challenges and economic uncertainty stemming from global trade policy. The inflationary environment continued to remain stable, with headline inflation converging around the target for several consecutive months. Meanwhile, indicators of underlying inflation, while still above the target, are gradually moderating, while tight labor market conditions also exhibit modest, though mixed, signals of softening. However, the medium and long-term growth outlook remains uncertain and problematic. On the one hand, structural challenges within the Eurozone and an imbalanced trade deal with the US continue to weigh on sentiment and growth potential. On the other hand, sweeping fiscal stimulus measures aimed at addressing structural challenges could have positive impacts on certain productive sectors, but the emphasis on increasing defense output could have uneven and inflationary implications.

Oil prices continued to adjust downward, and while markets continue to price sustained declines in prices through 2026, significant uncertainty around the trajectory of oil prices persists. On the one hand, slowing global demand, coupled with actual and expected increases in supply by OPEC+ countries, could each support a downward trend for oil. On the

other hand, the potential for an escalation in geopolitical tensions, as well as risks of secondary sanctions against Russia, pose risks of supply chain disruptions and upward price pressures.

In Q2 2025, Russia's economic growth weakened significantly to 1.1% Y-o-Y. At the same time, headline and core inflation, despite moderating somewhat in recent months, still remain well above target. Meanwhile, slowing credit activity, along with persistent deceleration in trade and services, pose further downside risks to domestic demand. On the other hand, labor market conditions remain exceedingly tight, exerting sustained inflationary pressures on the economy. Further, oil price uncertainty could pose risks to fiscal policy, while a weakening growth outlook could negatively impact non-oil and gas revenues and pose additional downside risks to the economy. The combination of weakening demand conditions, persistently tight labor market conditions, and high inflation expectations pose serious challenges to the Central Bank of Russia in managing the inflation-output tradeoff, even as the CBR continues to ease the policy stance.

### Domestic Demand Conditions

In Q2 2025, economic growth in Armenia accelerated somewhat, standing at 5.9% Y-o-Y, at the upper end of most estimates of its long-run sustainable level. Growth in the second quarter was concentrated in demand-driven sectors including construction and services, which could pose risks to the future sustainability of growth and the long-term outlook. Construction continues to grow at a rapid pace, but persistent risks of a gradual adjustment in real estate prices could threaten growth in adjacent sectors, contribute to weakening demand conditions, and pose deflationary pressures. At the same time, while growth in services remains driven by IT and Financial Services (together contributing 2.0 p.p. to overall growth), signs of acceleration in other services subsectors could point to a potential expansion in aggregate demand conditions. Trade and industry continued to slow amid a gradual fading of certain short-term, non-structural factors. However, select sub-sectors of manufacturing and mining continued to show positive signs, with strong growth in output, exports, lending activity, and production capacity. In this context, various signals point to a possible emergence of a positive output gap in Q2 2025.

Following record inflows in 2023, tourist flows to Armenia in 2024 and through 2025 Q1 had substantially moderated. However, beginning in May, tourist flows to Armenia have increased significantly to historically high levels, driven by a recovery in tourism from Russia as well as significant growth from other, non-traditional markets. The persistence of these trends could increase external demand pressures and exert inflationary impacts, especially on services exposed to external demand. Given the above, significant uncertainty regarding the outlook for external demand persists in both directions, driven by questions an uncertain Russian outlook, as well as stagflationary risks in the global economy amid overall economic policy uncertainty.

Uncertainties persist about seasonal migration to Russia and the channels through which remittances are transferred. On the one hand, a strengthening ruble could increase incentives

for labor migration to Russia. On the other hand, uncertainties surrounding the Russian economic outlook and tightening migration policies may act as limiting factors. The latter scenario could support an increase in labor supply within Armenia and contribute to easing inflationary pressures.

Uncertainty continues to surround domestic demand conditions. Strong growth in lending activity, domestic tourism, and high accumulated savings that could be oriented toward consumption could point to robust domestic demand. However, the structural characteristics of economic growth could suggest risks of a weak demand environment emerging.

There is considerable uncertainty regarding the impact of fiscal policy on aggregate demand. While tax collection in 2025 YTD has been strong, risks of future revenue underperformance persist. This, coupled with potential increases in current expenditures given the need for social assistance programs, could have short- to medium-term implications on deficit and debt levels. At the same time, potential growth in certain capital expenditures (especially road construction projects) could pose risks of expansionary demand pressures. On the other hand, risks of capital expenditure underperformance, as well as the structural characteristics of these expenditures, could mitigate fiscal policy's impact on aggregate demand.

## Labor Market & Inflation

Underlying labor market conditions remain a key source of uncertainty. While unemployment increased in Q1 in line with seasonal trends, its current level of 13.9% remains near long-term sustainable levels. The labor market survey suggests Y-o-Y declines in the number of unemployed and strong increases in the number of employed persons, a trend that is corroborated by the increase in the number of registered employees (per SRC data). While the latter data could merely reflect a gradual, structural decline in the shadow labor market in favor of formal employment, taken together, these signals from the labor market could point to still-strong demand conditions in the economy. On the other hand, wage growth continues to stabilize in the range of 5-6%, and is somewhat more evenly distributed across sectors of economy than in recent quarters. This could suggest more balanced labor market conditions and fewer structural imbalances in the economy. In the medium and long term, a potential expansion in labor supply could ease labor market conditions further and reduce market-driven pressures. The primary uncertainties in this context relate to the Russian economic outlook, flow of Armenian labor migrants to Russia, domestic labor market participation, and integration of economically inactive populations into the workforce.

Over 2025, inflation has shown some signs of accelerating, with CPI standing at 3.6% Y-o-Y in August. Since the beginning of the year, acceleration in annual inflation has been primarily driven by above-average increases in seasonal food prices, though its impact has been largely neutralized in June-August. At the same time, inflationary pressures from the global economy, particularly for imported food, have increased, reflecting increases in global food prices. Additionally, the deflationary pressures from non-food products observed earlier in the year have gradually subsided, and in August, year-on-year inflation stood at 1.1%. A persistence of global supply-side factors affecting imported goods prices could be a primary source of further increases in domestic inflationary pressures. Services inflation has increased somewhat in 2025, mainly due to high inflation for air transport services;

excluding this subgroup, services inflation has remained stable and below target. At the same time, inflation for services highly exposed to external and domestic demand (e.g. hotels, restaurants, etc.) increased since May, consistent with increases in tourist inflows observed during this period. The persistence of these trends amid growing external demand could serve as a source of upward pressure moving forward. However, Non-Traded Sticky Price Inflation (NTSPI), which captures domestically-driven demand dynamics, has continued to remain stable, in the range of 2.0- 2.5% Y-o-Y. Conversely, core inflation has accelerated somewhat since the beginning of the year (3.7% Y-o-Y in August), primarily reflecting the above-described increases in imported non-seasonal food and certain exportable services. In this context, inflation expectations have continued to steadily decline, approaching the target level, supported by a prolonged low-inflation environment.

## Financial Markets & Monetary Policy

Market expectations of the CBA policy rate path have remained largely unchanged since the latest decisions, and continue to reflect an expected gradual reduction in the policy rate to 6.25% over the next eight decisions. Given the above, the yield curve has remained largely unchanged, although very modest upward shifts in the long-term portion of the curve could suggest expectations of slightly higher long-term rates, in the context of neutral rate and risk premium uncertainty.

In recent months, Armenia's country risk premium has remained below the long-term stable level determined by the country's fundamentals. In particular, recent declines could reflect a favorable reassessment of risks, supported not only by the easing of overall sentiment toward emerging markets but also by expectations of a cooling in immediate geopolitical risks in the South Caucasus. These factors, together with Armenia's macroeconomic stability and growth in productive capacities, provide certain positive factors for a possible reassessment of the country's risk premium and reduction in the neutral rate, which, *ceteris paribus*, could exert deflationary pressures through a relatively tighter monetary policy stance. In this context, several rating agencies note that the ultimate, fundamental adjustments in the country risk premium in response to the above developments would come only after the expected economic implications materialize. On the other hand, any potential upward adjustment of the country risk premium would instead pose risks for a revision of the neutral rate to the upside, which, all else being equal, could create inflationary pressures due to a more accommodative monetary policy stance.

Considering the persistence of numerous types of uncertainty, the CBA builds and evaluates several different scenarios for future economic developments in order to manage possible risks stemming from these key areas of uncertainty. The illustrative Case A scenario presented in the MPR (policy rate path above market expectations), derives from risks of an increase in external demand, driven by strong tourism growth, sustained and growing demand for Armenian goods and especially services, as well as increases in remittances. Under this scenario, while the exchange rate would be expected to act as the primary shock absorber, a higher path for the policy rate would be necessary to prevent localized inflation pressures (for services highly exposed to external demand) translating into higher generalized inflation expectations.

The illustrative Case B scenario outlined in the MPR (lower policy interest rate path versus market expectations) is

grounded in the assumption that Armenia's productive capacities, particularly in high value-add exportable sectors including IT, financial services, and manufacturing, have increased considerably in recent years. This increase in productivity may have positively impacted the productive potential of the economy, which, in tandem with an improved investment climate and persistent capital flows, may have resulted in an historical and expected appreciation of the real exchange rate trend. This, in turn, implies a lower level of the real and nominal neutral rate, requiring an appropriate adjustment in the policy rate path below what markets currently expect to prevent the formation of persistent deflationary pressures

*As part of its prudent risk management framework for monetary policy, the CBA builds and discusses various scenarios, summarized in the Taxonomy of Scenarios. These scenarios reflect key sources of risk and uncertainty that could lead to unwelcome policy errors (that might drive the economy into "dark corners"), which policymakers hope to minimize through a least-regrets decision-making model. For communications purposes, the MPR includes a deeper dive into two illustrative scenarios almost randomly selected from the Taxonomy, which reflect illustrative future paths of the economy that would require either a higher path for the policy rate (Case A) or a lower path of the policy rate (Case B) relative to current market expectations. These illustrative scenarios do not represent a most-likely future, assign weight or probability to outcomes, or reflect the Board's most-favored scenarios.*

# 02 |

## Monetary Policy Objectives & Framework

# Statement of Long-Run Monetary Policy Objectives

Adopted effective March 12, 2024; renewed effective March 18, 2025

As enshrined in “The Law of the Republic of Armenia on the Central Bank of Armenia,” the primary objectives of the Central Bank of Armenia are to ensure price stability and financial stability. The Board of the CBA is committed to using its full suite of monetary policy instruments to achieve its price stability mandate and provide a nominal anchor for the economy.

We emphasize that the primary objectives of price stability and financial stability are a means to an end. The ultimate purpose of the CBA as an accountable public-sector institution is improving the welfare of our nation. A commitment to achieving low and stable inflation provides a credible nominal anchor for the economy and thereby anchors inflation expectations, helps to avoid inefficient boom-bust cycles, stimulates investment, supports the economic development of the country, and improves living standards over time.

The CBA develops and implements monetary policy to achieve its price stability objective. The fundamental role of monetary policy is to provide an anchor for inflation and inflation expectations. The Board believes that a three percent inflation target is consistent with its price stability mandate. The inflation target is expressed in terms of the Consumer Price Index (CPI), since it is the best measure of the cost of living and final consumption expenditures, and is the primary reference point for market participants when making planning decisions and setting contracts. Nevertheless, the overall CPI basket of goods and services includes several items that are subject to seasonal fluctuations and global economic developments, which are not directly influenced by monetary policy. We therefore consider alternative measures of inflation, such as core and non-traded sticky prices, which can provide useful information on the underlying inflationary environment.

The CBA’s primary means of adjusting the stance and path of monetary policy is through changes in the expected path of short-term interest rates. If interest rates were to be constrained by the effective lower bound, the Bank would be prepared to use its full range of policy tools.

While emphasizing the primacy of achieving the price stability and financial stability mandates over the medium term, the CBA recognizes that it is also responsible for managing the short-run tradeoff between inflation and output. In an open market economy, periodic economic and financial shocks cause economic activity and inflation to fluctuate over time. In this context, the CBA does not target CPI inflation on a period-by-period basis and does not attempt to bring CPI inflation back to the target in the short term if it would result in undue economic and financial instability. In any economic situation, the CBA seeks to develop and implement monetary policy in a manner that brings inflation to the target in the medium-term (12 quarter) horizon, while minimizing associated social costs through a “least regrets” approach.

Effective monetary policy improves welfare by anchoring long-term inflation expectations and reducing the volatility of output and unemployment. Avoiding excessive volatility in the economy can result in substantial improvements in welfare by reducing average levels of unemployment and raising the productive capacity of the Armenian economy. The Bank emphasizes that placing weight on other near-term objectives must not be inconsistent with its primary responsibilities of achieving its three percent target in the medium term and maintaining price and financial stability.

The Board places great emphasis on the importance of communicating its policy and decision-making framework to the public in a clear and comprehensible manner. Clear and effective communication helps make policy more effective, and encourages financial markets, businesses, and the general public to better understand and manage risks and uncertainties. Moreover, this communications approach plays an important role in enhancing the transparency of monetary policy and central bank accountability, which is a key priority for the CBA as an independent public sector institution.

*The Board will review and renew the Statement of Long-Run Monetary Policy Objectives during the first decision-making round of each year.*

# Framework for Monetary Policy as Risk Management

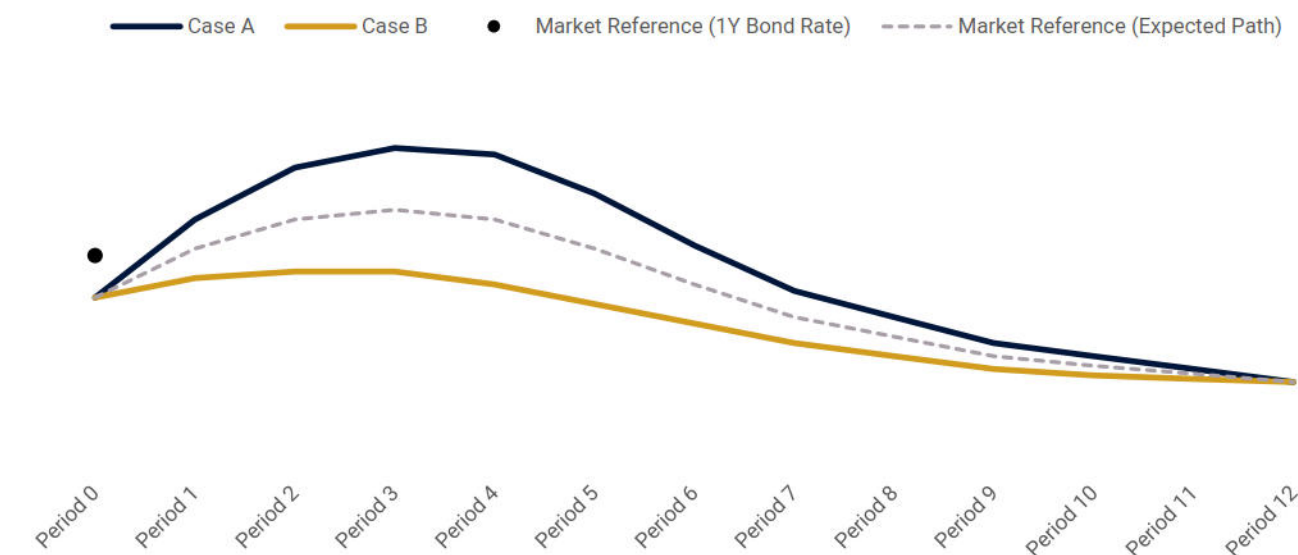
The CBA conducts monetary policy within a risk management framework to analyze and communicate the uncertainty surrounding the economic outlook more effectively. Our approach is to consider alternative scenarios for the evolution of the Armenian economy that have important implications for monetary policy. Elevated uncertainty is a reality that central banks must manage, and we do this by explicitly incorporating it into our framework and communication. We develop and analyze multiple scenarios that would imply a higher or lower path for interest rates than is currently priced in financial markets. At the same time, to steer the policy discussion and communication, we develop two or more illustrative scenarios. These scenarios should not be interpreted as pure risk scenarios, but are meant to represent plausible paths for the policy rate that could be consistent with managing monetary policy risks and concerns in an individual's economic scenario.

Market Reference is the expected path of the policy rate that is currently priced in financial markets. Ideally, if financial markets in Armenia were more developed, and there existed a derivative market for the policy rate, then we could construct an expected path based solely on market information. We therefore use the 1-year government bond yield, which should reflect the expected average policy rate over the next 12 months, plus some compensation for term premium. In addition, we conduct high-frequency surveys of market participants before, during, and following each decision-making cycle as another reference point for expectations of the policy rate.

Case A reflects a scenario that incorporates economic and financial developments that would require a higher interest rate path than what is currently priced in financial markets that is consistent with guiding the economy back to its long-run equilibrium and to achieve price stability objective.

Case B reflects a scenario that incorporates economic and financial developments that would require a lower interest rate path than what is currently priced in financial markets that is consistent with guiding the economy back to its long-run equilibrium and to achieve price stability objective.

**Figure 2.1: Alternative Paths for the Policy Rate**



Source: CBA

Note: For Illustrative Purposes Only

To learn more about the Central Bank of Armenia's approach to monetary policy, refer to the draft book, [Prudent Risk Management Approach to Monetary Policy: Theory and Practice of FPAS Mark II at the Central Bank of Armenia](#), edited by Douglas Laxton, Martin Galstyan, and Vahe Avagyan (2024).

## Report Structure

The MPR begins with the Executive Summary, which provides the Statement by the Board of the CBA as well as a high-level assessment of economic conditions and underlying forces. The Executive Summary is also issued as a standalone document, known as the Executive Monetary Policy Statement.

Section III presents in greater detail the CBA's implementation of this policymaking framework. It begins with an assessment of the first two ingredients essential for economic analysis: where is the economy now, and what are the underlying forces driving the economy. This section also communicates how the CBA is managing current risks through a framework of "least regrets." This includes a taxonomy of different types of scenarios that may be relevant in the current policy round, reflecting a summary of the universe of major issues the Board and Staff of the CBA, as well as external stakeholders, are concerned about. Against this context, the MPR presents two or more illustrative case scenarios representing what the CBA will do with its policy instruments in order to reach its objectives.

The statistical appendix is published as a separate file, known as the MPR Chart Pack, which contains charts and tables for relevant economic variables, as well as key projections from the illustrative case scenarios.

Importantly, the MPR of the CBA is published on the same day as the policy decision is made by the Board of the CBA. This is intended to provide the public with sufficient detail and narratives that describe the framework and analysis that led to the decision in a near-real-time manner. Following the decision and press conference, a separate Transparency Report is released, containing more detailed information about how the Board came to the specific decision during the Board meeting.

## Disclaimer

The information presented in this report is based on actual data available by September 12, 2025 as well as the results of the surveys conducted by the CBA and judgments made pursuant to the information on future developments of the macroeconomic environment.

The Monetary Policy Report serves as the chief monetary policy communications vehicle for the Central Bank of Armenia, and is published on a quarterly basis. The MPR has been designed to be a user-friendly document that covers key policy-relevant issues but remains accessible to technical and non-technical audiences alike. The report is structured to follow a narrative format that helps illustrate the key issues, risks, and uncertainties that drove the Board's thinking in the current decision-making round and how it arrived at its policy decision. Not all data, analysis, or issues can be reasonably included in the MPR in every quarter without overwhelming the reader or overshadowing key messages. For this reason, the MPR is supplemented with a Chart Pack that provides a complete and comprehensive overview of the current and underlying economic environment.

A decision made by the CBA Board today will affect inflation with a lag. The illustrative scenarios are chosen and designed by our Monetary Policy Department's economists to describe plausible paths of the economy under different risks. Importantly, the selected illustrative scenarios are two of many possible scenarios that the Board considers when making its decisions, which are represented in the Taxonomy of Scenarios in Section III. During each policymaking cycle, the Board is engaged in dynamic discussions and information-sharing with the Staff related to understanding the current position of the economy, its underlying drivers, and key sources of policy-relevant risk and uncertainty. These discussions, including the process through which the Taxonomy of Scenarios is developed and the illustrative scenarios are selected and quantified, are an important input for Board deliberations. The Taxonomy of Scenarios and the selected illustrative scenarios are produced four times a year and are a key, but not the only, input to the CBA Board's monetary policy decisions.

All monetary policy reports which have been published to date are available on the CBA's website ([www.cba.am](http://www.cba.am)), which also contains all press releases, working papers, and other monetary policy-related publications.



Central Bank  
of Armenia

03 |

Monetary Policy  
Outlook

# A. Global Economic Developments

## United States Economy

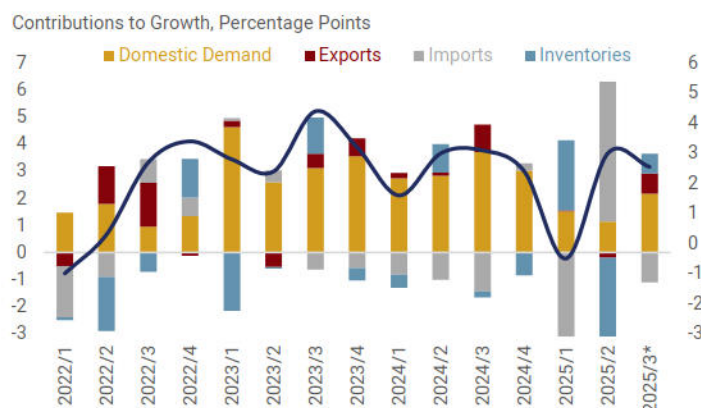
After weak growth in the U.S. in Q1 2025 amid a surge in imports in anticipation of tightening trade policies, growth recovered in Q2, reaching 3.3% Y-o-Y, as imports reversed and inventories gradually depleted. Nevertheless, uncertainties surrounding the underlying conditions of the economy persist. Consumption has slowed somewhat still remaining at relatively high levels. Labor market conditions weakened significantly in the second quarter, which may also indicate the signs of weaker demand. At the same time, stricter migration policy could contribute to tighter labor market conditions and the evolution of inflationary risks. However, there are still no clear signs of this risk materializing. Moreover, uncertainty around trade and fiscal policies remains elevated. Although current trade policy could substantially increase budget revenues through tariffs, estimates suggest that this will likely be insufficient to fully offset the considerable fiscal deficit generated by the new fiscal plan. Considering the substantial rise in the deficit and debt, risks of potential increases in long-term interest rates have intensified. These developments could affect the outlook for U.S. debt sustainability, raising the country's risk premium and implying a potentially higher path for interest rates.

In recent months, inflation has somewhat accelerated, reaching 2.9% Y-o-Y in August. Although the sharp increase in imports and inventories in Q1 2025 temporarily delayed the pass-through of tariffs into inflation, in recent months it has gradually passed through to inflation. Over the past three months, signs of accelerating inflation have been evident across nearly all tariff-sensitive categories. However, the full impact has yet to materialize due to the ongoing utilization of accumulated inventories. The persistence of current trends poses the risk of a more pronounced inflationary acceleration, though the scale and nature of such pressures will depend heavily on the outlook for domestic demand conditions. On the one hand, substantial downward revisions to labor market indicators in Q2 point to a significant weakening in labor market conditions. On the other hand, labor supply constraints stemming from restrictive migration policy could reduce labor supply even in the context of cooling demand.

Against the backdrop of a potential weakening of U.S. economic outlook, financial markets have priced in a further path of policy rate cuts. However, the scale of the inflationary impact from tariff policy and further conditions of domestic demand remain highly uncertain. Nevertheless, under potential stagflationary risks, the Fed's commitment to ensuring price stability and full employment has become increasingly problematic. On one hand, the weakening growth outlook, and on the other, the persistence of elevated inflation alongside the risk of de-anchoring expectations, pose significant challenges for the Fed. The situation is further complicated by risks of weakening central bank independence.

Uncertainty has grown surrounding the underlying conditions of the economy, including the strength of demand and consumption moving forward

Figure 3.A.1: Contributions to US Real GDP Growth

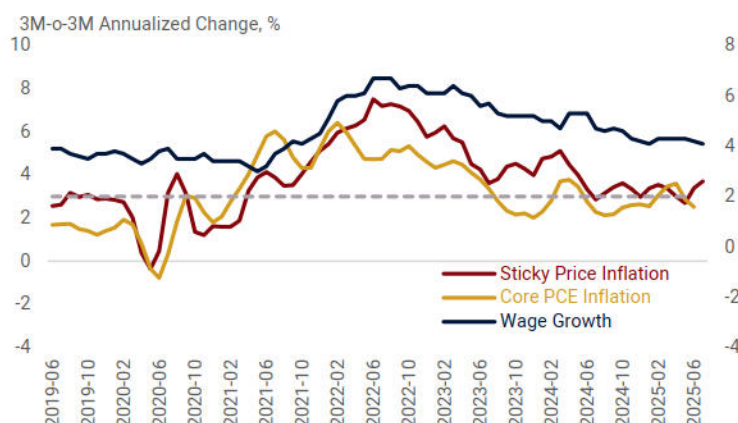


Source: US BEA; Atlanta Fed

Note: 2024 Q3 based on AtlantaFed's September 10, 2025 GDPNow Estimate

Inflation has ticked up in recent months, but the main risk is that tariffs have not yet fully transmitted to consumer prices

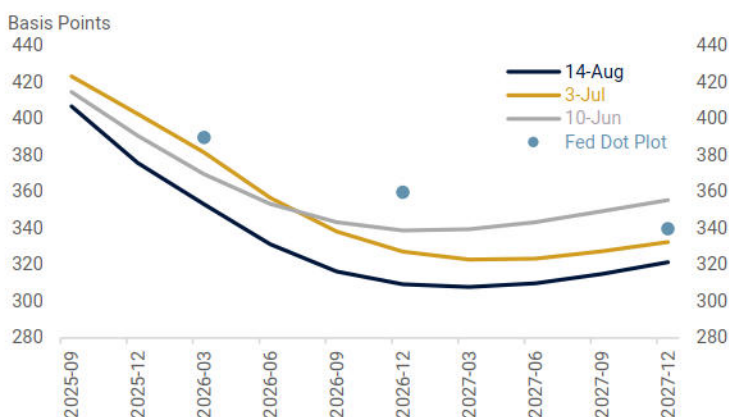
Figure 3.A.2: Underlying Inflation Measures, US



Source: BLS; BEA; Atlanta Fed

A potentially stagflationary environment complicates the Fed's task of meeting its dual mandate for price stability and full employment

Figure 3.A.3: Market Expectations of FED Funds Rate Path



Source: Atlanta FED, Federal Reserve Board

## Eurozone Economy

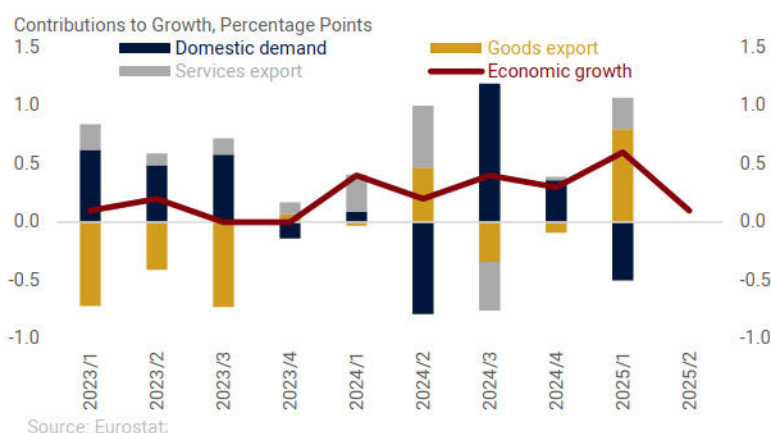
Economic growth in the Euro Area has decelerated considerably in the second quarter of 2025, with Q-o-Q real GDP growth easing to 0.1 percent, while the Y-o-Y growth rate moderated to 1.4 percent. This deceleration follows a relatively strong outturn in the first quarter, when Q-o-Q growth reached 0.6 percent, largely driven by a temporary surge in goods exports amid a front-loading of demand and inventory accumulation in the U.S. in anticipation of forthcoming trade restrictions. The recent loss of momentum reflects persistent structural headwinds, including subdued domestic demand and elevated uncertainty related to the global trade environment. In parallel, sectoral mismatches between aggregate demand and supply persist, particularly in the services sector, where resilient external demand contributes to sustained, albeit somewhat softened, inflationary pressures.

Uncertainty surrounding the medium- and long-term growth outlook remains elevated. Leading indicators of PMI readings point to an improvement in the services sector, supported by stronger inflows of new business. At the same time, the manufacturing sector shows signs of gradual stabilization, although overall momentum remains fragile due to persistent structural challenges. In this context, risks are twofold. On the one hand, continuous structural headwinds along with the imbalanced trade agreement with the U.S. continue to weigh on business sentiment and limit growth potential. On the other hand, fiscal stimulus measures aimed at addressing these structural issues are expected to provide targeted support to certain productive sectors, thereby partly offsetting these headwinds. However, the focus on increasing defense production may lead to uneven outcomes and add to inflationary pressures.

The inflationary environment has remained broadly stable with headline inflation converging towards 2% target for the past consecutive months. At the same time, broader measures of underlying inflation, despite moderating gradually, are still above the target, with 3.1% Y-o-Y services inflation recorded in July. Despite mixed signals of slight softening, labor market conditions still remain relatively tight, with the unemployment rate holding steady at a historically low 6.2%. At its July meeting, the ECB opted to keep policy rates unchanged, prompting markets to expect the easing cycle to end. Nevertheless, uncertainty surrounding the policy outlook persists, as stagflation-like risks emerge from persistent inflationary pressures arising from tight labor market alongside weakening growth amplified by structural challenges and trade restrictions.

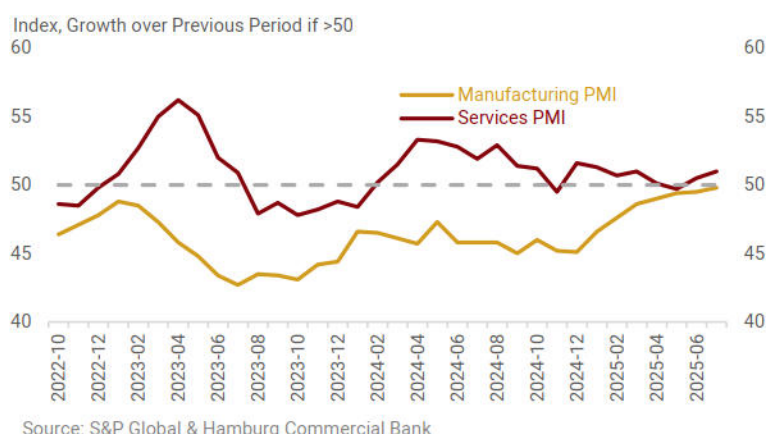
As the short-term factors that drove strong Q1 growth faded out, the growth outlook remains clouded by persistent structural challenges

**Figure 3.A.4: Contributions to Euro Area Real GDP Growth**



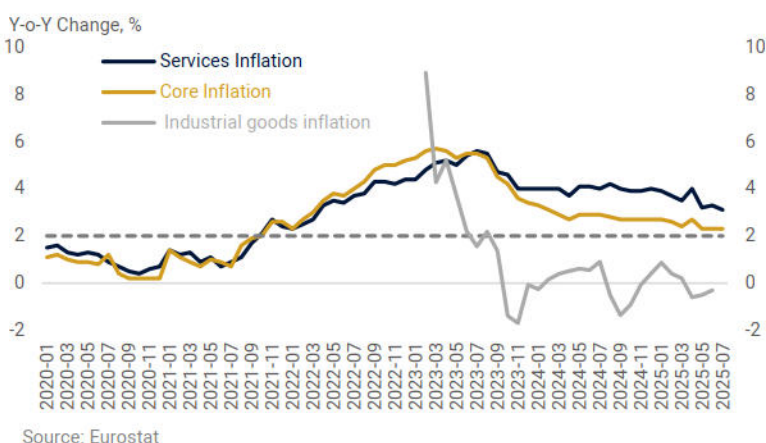
Services continue to drive economic growth, but structural challenges raise questions about the resilience of a recovery in manufacturing

**Figure 3.A.5: Composite Purchasing Managers Index (PMI), Euro Area**



Underlying inflation indicators suggest differing interpretations of the state of aggregate supply and demand conditions

**Figure 3.A.6: Underlying Inflation Measures, Euro Area**



## Russian Economy

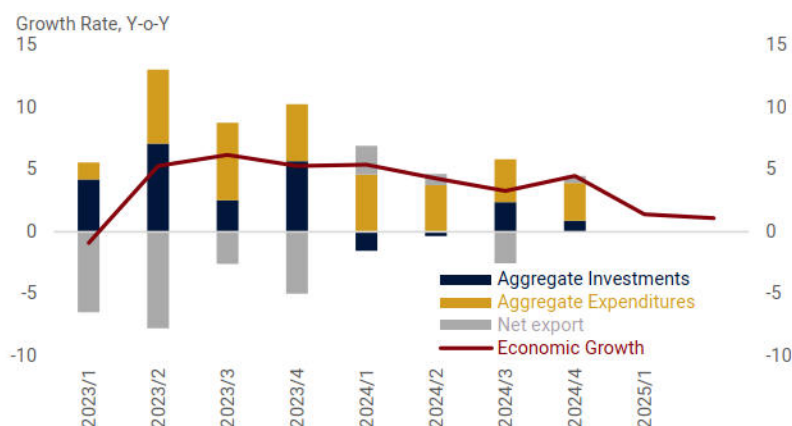
In Q2 2025, Russia's economic growth slowed significantly to 1.1% Y-o-Y. Signs of weakening demand are already evident across many sectors of the economy. Although growth in the industrial sector has decelerated, it remains in positive territory due to the expansion of military production. In recent months, both services and retail trade sectors have also shown signs of slowdown, while the moderation of lending further underscores the risks of a weak demand environment taking hold. Labor market conditions remain tight. Unemployment has stayed at historically low levels, standing at 2.2% in July 2025. At the same time, real wages have accelerated somewhat in recent months (Figure 3.A.8). These developments reflect sustained issues with labor shortages, which continue to generate additional inflationary pressures for the economy and pose risks of potentially limiting the further expansion of production capacities.

The high inflationary environment persists. Although inflation has somewhat slowed in recent months, it remains above the target, reaching 8.1% YoY in August (Figure 3.A.9). Inflation expectations also remain elevated, both in the short and medium term. Despite some easing of inflationary pressures in recent months against the backdrop of weakening demand, the continued tightness of the labor market and persistently high inflation expectations pose risks of potential acceleration in inflation. In this context, on the one hand, the rapid slowdown in demand, and on the other hand, the persistence of tight labor market conditions and elevated inflation expectations, pose serious challenges for the Bank of Russia in the short term in terms of effectively managing the inflation-growth trade-off, especially given that the Bank of Russia continues to lower the policy interest rate (in September by 100 basis points).

Uncertainty over Russia's economic growth outlook persists. On the one hand, the continuation of negotiations on resolving the Russia-Ukraine conflict and positive signals about the potential end of the conflict create grounds for a favorable medium-term outlook for the Russian economy. On the other hand, the persistence of a weak demand environment, as well as the imposition and continued tightening of targeted sanctions by Western countries, pose risks to Russia's medium-term growth prospects. At the same time, the Russian economy remains vulnerable to current developments in the oil market, where falling prices have reduced oil and gas revenues in the state budget, and the persistence of this downward trend carries risks for fiscal policy. Moreover, under the present conditions of slowing economic growth, uncertainties are also emerging regarding the outlook for collecting non-oil-and-gas revenues.

Weakening demand conditions poses risks to the medium-term economic growth outlook.

Figure 3.A.7: Russia Real GDP Growth

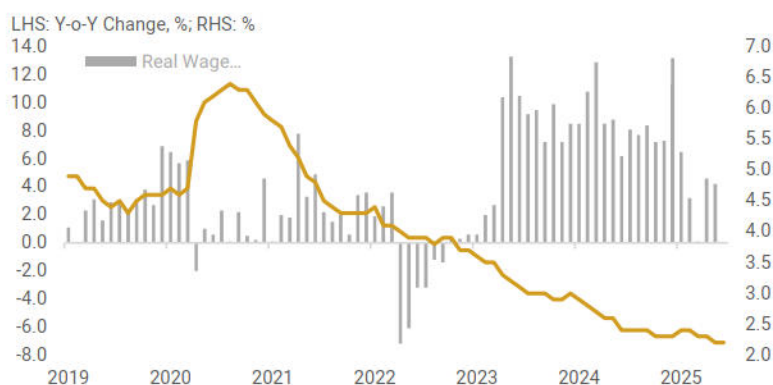


Source: Bank of Russia, Rosstat

Note: Data for 2025Q2 is a preliminary estimate.

Labor market conditions remain tight, exerting additional inflationary pressures on the economy.

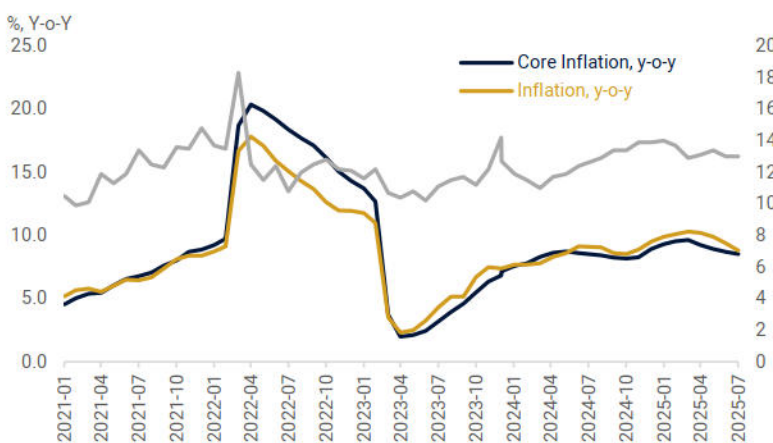
Figure 3.A.8: Unemployment Rate and Real Wage Growth, Russia



Source: Rosstat

Despite some slowdown in inflation, it remains above the target, while the persistence of elevated inflation expectations complicates the Bank of Russia's task of ensuring price stability.

Figure 3.A.9: Russian inflation indicators



Source: Rosstat

## Commodity Markets

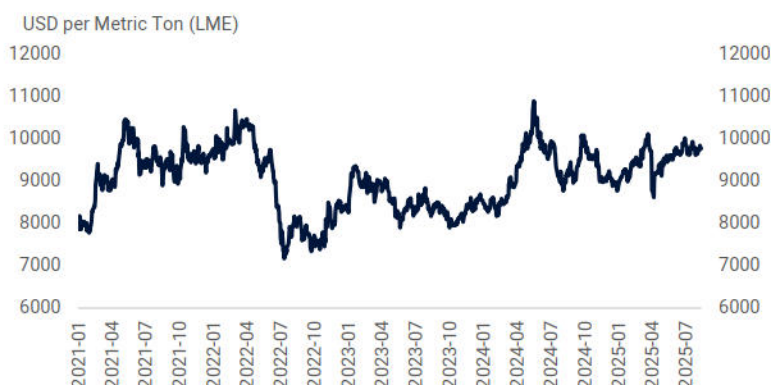
**Copper:** Since the announcement of a forthcoming 50% tariff in February 2025, copper demand has surged in the U.S., with increased front-loading imports and inventory stockpiling ahead of the August 1 implementation. This preemptive purchasing activity to secure supply resulted in a surge in copper prices, with the average price in August exceeding USD 9700 per metric ton (Figure 3.A.10). However, uncertainty surrounding the copper price outlook remains elevated. On the one hand, growing demand linked to the green energy transition and increased infrastructure and defense spending in the Euro Area pose upside risks to the prices. On the other hand, weakening global demand and the potential redirection of copper supply flows toward markets outside the U.S. exert downwards pressure on global prices.

**Oil:** Easing geopolitical tensions in the Middle East have somewhat stabilized oil prices near USD 70 per barrel, and markets continue to anticipate a sustained moderation in prices through 2026. Nevertheless, significant uncertainty surrounding the trajectory of oil prices persists. On the one hand, the increase in supply from OPEC+ countries, planned to reach approximately 2.5 million barrels per day in September, along with weakening global demand may reinforce the downward pressure on prices. On the other hand, the potential escalation of geopolitical tensions, combined with the risk of secondary sanctions against Russia, presents upside risks on prices by raising the likelihood of supply chain disruptions.

**Food:** International food commodity prices saw an approximately 7% Y-o-Y increase in July, reflecting diverging trends across major food categories. On the one hand, improved harvest prospects for cereals and improved sugar production outlook in key producer countries have contributed to easing price pressures in these segments. On the other hand, robust global demand for meat and vegetable oil exert upward pressures on prices. Despite slight moderation due to improved supply conditions, dairy prices remain elevated amid firm demand and lingering cost pressures. Nevertheless, uncertainty surrounding global food prices and the cost of food imports to Armenia persists, driven by supply chain disruptions related to geopolitical tensions and trade barriers on the one hand, and a weak global growth outlook on the other.

Copper prices have surged, reflecting both increased demand and tariff risks

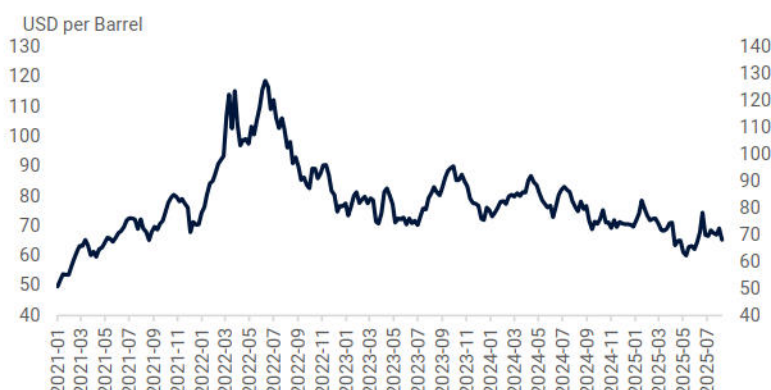
Figure 3.A.10: Copper Prices



Source: Bloomberg

Easing geopolitical tensions, coupled with a surge in production, have contributed to moderating oil prices. Nevertheless, both upside and downside risks remain prominent.

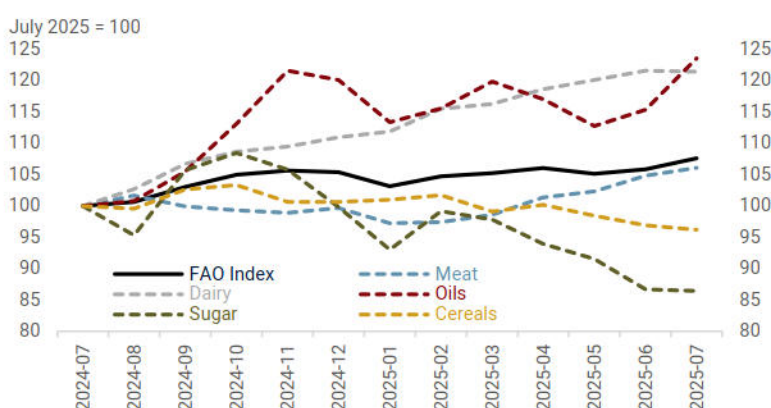
Figure 3.A.11: Brent Crude Oil Prices



Source: FRED

Global food prices continue to grow, which could serve as a source of future inflationary pressures in Armenia

Figure 3.A.12: FAO Food Price Index



Source: FAO

**Table 3.A.1: Third-Party Projections for Commodity Prices**

| Source/<br>Topic | Oil (Brent, Dollars per Barrel) |        |           | Copper (LME \$/t) |        |           | World Bank Food Price Forecasts (Ann. Growth) |        |            |
|------------------|---------------------------------|--------|-----------|-------------------|--------|-----------|-----------------------------------------------|--------|------------|
|                  | EIA                             | WB     | Consensus | WB                | REQ    | Consensus | Oils and Meals                                | Grains | Other Food |
|                  | Aug 25                          | Apr 25 | Sep 25    | Apr 25            | Jun 25 | Sep 25    | Apr 25                                        | Apr 25 | Apr 25     |
| 2025             | 67                              | 64     | 68        | 8200              | 9447   | 9471      | -6.8                                          | -10.5  | -4.6       |
| 2026             | 51                              | 60     | 63        | 8000              | 9793   | 9932      | 0.3                                           | -1.1   | -2.0       |

Source: US Energy Information Administration; World Bank; Australia Resources and Energy Quarterly (REQ); Bloomberg

**Table 3.A.2. Third-Party Projections for GDP Growth and Inflation in Key Trading Partner Countries**

| Source/<br>Date                    | United States |        |              |        |           | Euro Area |        |              |        |        |           | Russia |        |              |        |           |
|------------------------------------|---------------|--------|--------------|--------|-----------|-----------|--------|--------------|--------|--------|-----------|--------|--------|--------------|--------|-----------|
|                                    | IMF*          | WB     | OECD         | Fed    | Consensus | IMF*      | WB     | OECD         | EC     | ECB    | Consensus | IMF*   | WB     | OECD         | CBR    | Consensus |
|                                    | Apr 25        | Jun 25 | Jun 25       | Jun 25 | Sep 25    | Apr 25    | Jun 25 | Jun 25       | May 24 | Jun 25 | Sep 25    | Apr 25 | Jun 25 | Jun 25       | Jul 25 | Sep 25    |
| <b>GDP Growth (Annual Rate, %)</b> |               |        |              |        |           |           |        |              |        |        |           |        |        |              |        |           |
| 2024                               |               |        | 2.8 (Actual) |        |           |           |        | 0.8 (Actual) |        |        |           |        |        | 4.3 (Actual) |        |           |
| 2025                               | 1.8           | 1.4    | 1.6          | 1.4    | 1.6       | 0.8       | 0.7    | 1.0          | 0.9    | 0.9    | 1.1       | 1.5    | 1.4    | 1.0          | 1.4    | 1.3       |
| 2026                               | 1.7           | 1.6    | 1.5          | 1.6    | 1.7       | 1.2       | 0.8    | 1.2          | 1.4    | 1.1    | 1.1       | 0.9    | 1.2    | 0.7          | 1.6    | 1.4       |
| 2027                               | 2.0           | 1.9    | -            | 1.8    | 2.0       | 1.3       | 1.0    | -            | -      | 1.3    | 1.5       | 1.1    | 1.2    | -            | 1.8    | 1.5       |
| <b>Inflation (Annual Rate, %)</b>  |               |        |              |        |           |           |        |              |        |        |           |        |        |              |        |           |
| 2024                               |               |        | 3.0 (Actual) |        |           |           |        | 2.4 (Actual) |        |        |           |        |        | 8.4 (Actual) |        |           |
| 2025                               | 3.0           | -      | 3.2          | 3.0    | 2.8       | 2.1       | -      | 2.2          | 2.1    | 2.0    | 2.1       | 9.3    | -      | 9.7          | 9.1    | 9.1       |
| 2026                               | 2.5           | -      | 2.8          | 2.4    | 2.8       | 1.9       | -      | 2.0          | 1.7    | 1.6    | 1.9       | 5.5    | -      | 6.1          | 5.5    | 5.6       |
| 2027                               | 2.1           | -      | -            | 2.1    | 2.5       | 2.0       | -      | -            | -      | 2.0    | 2.0       | 4.0    | -      | -            | 4.3    | 4.5       |

Note: IMF inflation forecasts per April WEO.

Source: IMF; World Bank (WB); OECD; Fed; ECB; CBR; European Commission (EC); Bloomberg

## B. Domestic Demand Conditions

### Gross Domestic Product

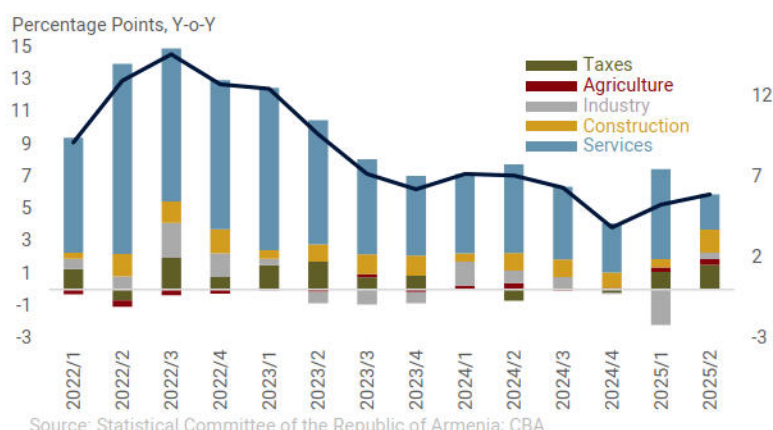
In Q2 2025, economic growth in Armenia accelerated somewhat, standing at 5.9% Y-o-Y, at the upper end of most estimates of its long-run sustainable level. Growth in Q2 was concentrated in demand-driven sectors including construction and services, which could pose risks to the future sustainability of growth and the long-term outlook. Construction continues to grow at a rapid pace, but persistent risks of a gradual adjustment in real estate prices could threaten growth in adjacent sectors, contribute to weakening demand conditions, and pose deflationary pressures. At the same time, while growth in services remains driven by IT and Financial Services (together contributing 2.0 p.p. to overall growth), signs of acceleration in other services subsectors could point to an expansion in aggregate demand conditions. Trade and industry continued to slow amid a gradual fading of certain short-term, non-structural factors. However, select sub-sectors of manufacturing and mining continued to show positive signs, with strong growth in output, exports, lending demand, & production capacity.

Following record inflows in 2023, tourist flows to Armenia in 2024 and through 2025 Q1 had substantially moderated. However, beginning in May, tourist flows to Armenia increased significantly to historically high levels, driven by a recovery in tourism from Russia as well as significant growth from other, non-traditional markets. The persistence of these trends could increase external demand pressures and exert inflationary impacts, especially on services exposed to external demand. Remittances have increased in recent months, potentially supported by a stronger ruble and labor shortages in Russia. At the same time, uncertainty for the external demand outlook persists in both directions, driven by a weakening global outlook as well as uncertainty about the persistence of the recent increase in tourism and remittances.

In this context, various signals point to a possible emergence of a positive output gap in Q2 2025 (Figure 3.B.3). However, the characteristics of recent growth, divergent developments across sectors, and mixed signals from various indicators add uncertainty regarding the relative position of aggregate demand and supply in the economy. On the one hand, strong loan growth, elevated private consumption, and high demand-driven growth indicate sustained excess demand pressures in the economy. On the other hand, the continued concentration of growth in certain sectors, along with stable labor market conditions and persistently low inflation in services and non-traded sticky prices (see Section C), may suggest weaker demand environment and the presence of a closed or slightly negative output gap in the economy.

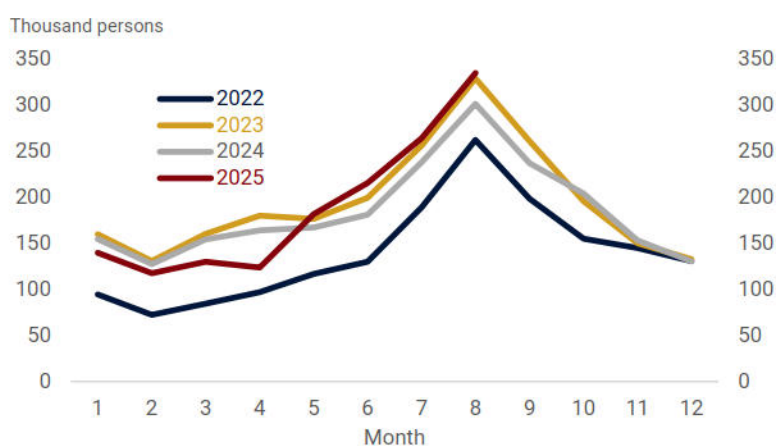
Economic growth picked up steam in Q2, with growth concentrated in demand-driven sectors

**Figure 3.B.1: Contribution to Real GDP Growth by Production Approach**



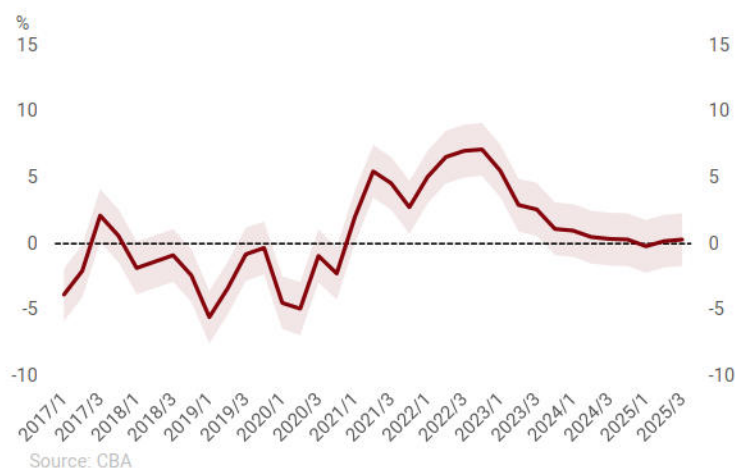
Strong rebound in tourism could point to growing external demand conditions

**Figure 3.B.2: Inbound Tourists Number**



Rebound in demand-driven growth and external demand could point to a possible emergence of a positive output gap

**Figure 3.B.3: The Output Gap**



## Consumption and Investment

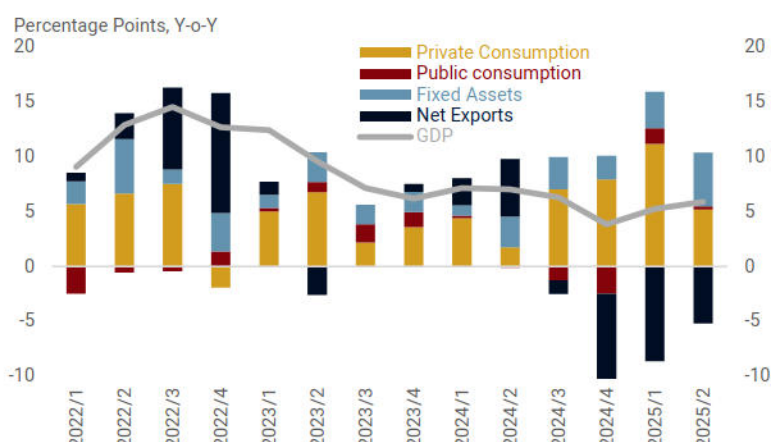
Private consumption has continued to grow at a strong pace since the second half of 2024, recording a Y-o-Y increase of 7.5% in Q2 2025 (Figure 3.B.4). Similarly, gross investment growth grew by 26.2% in Q2 2025, driven by growth in both private and public investment, particularly in real estate, investment goods, and infrastructure (Figure 3.B.5). The substantial increase in private spending may be attributed to continued strong growth in lending to households and the private sector, as well as the utilization of accumulated savings. Together, these factors could point to persistently strong domestic demand conditions within the economy.

Uncertainties remain regarding the outlook for domestic demand. On the one hand, domestic demand could grow on the back of spending from previously accumulated savings in the private sector in recent years, as well as sustained high credit growth. Such a scenario could fuel further excess demand pressures (particularly if the economy is operating at or slightly above its potential output), thereby increasing inflationary pressures. On the other hand, relatively muted growth in certain sectors of the economy and the absence of high wage growth conditions, (Figures 3.C.1 and 3.C.4) offer counterarguments against an excess demand environment forming. Moreover, the future trajectory of geopolitical tensions and regional uncertainties could have meaningful implications on private spending, in terms of both consumption and investment. A persistence of these trends could dampen the growth outlook, while a weakening in geopolitical tensions could pave the way for capital inflows and greater investment activity. Additionally, uncertainty regarding the stance of fiscal policy remains relevant from the perspective of domestic demand outlook.

Uncertainty remains regarding the number of Armenian labor migrants in the Russian Federation and the actual volume of remittances flowing into Armenia. The role of remittances in driving private demand has diminished considerably, given Armenia's strong economic growth and the substantial increase in household incomes. Nonetheless, remittances have accelerated in recent months, even as they remain at relatively low levels historically (Figure 3.B.6). Looking ahead, on the one hand, a strengthening ruble could increase incentives for labor migration to Russia. On the other hand, uncertainties surrounding the Russian economic outlook and tightening migration policies may act as limiting factors. The latter scenario could support an increase in labor supply within Armenia and contribute to easing inflationary pressures.

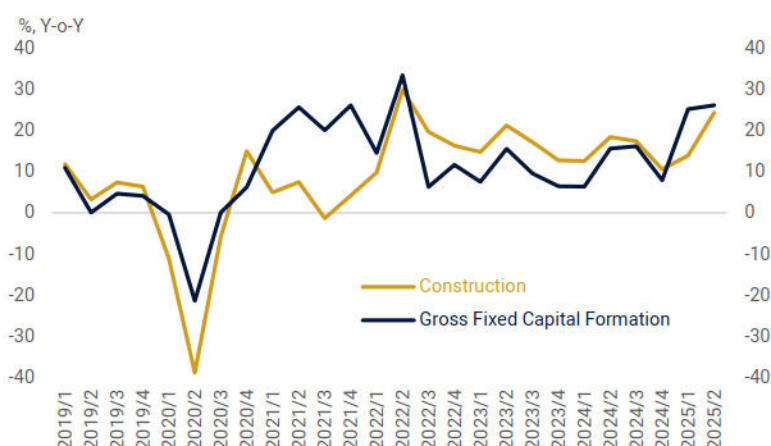
While data uncertainty remains, various signals point to strong consumption and investment, buoyed by sustained lending growth and high accumulated savings

**Figure 3.B.4: Contribution to Real GDP Growth by Expenditure Approach**



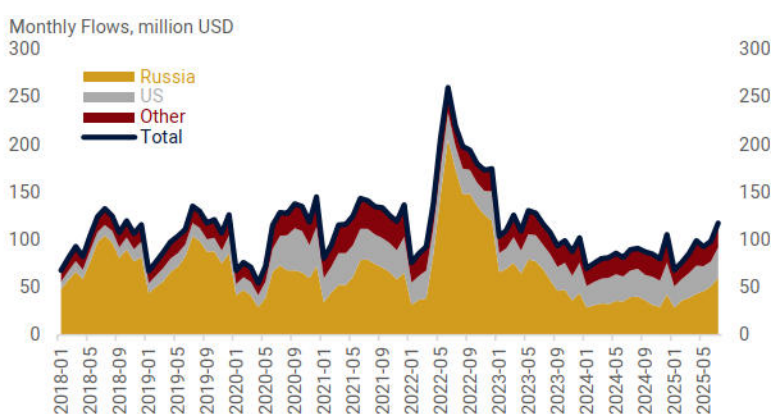
Investments in fixed capital are increasing, consistent with sustained high growth in the construction sector

**Figure 3.B.5: Investments in Fixed Assets and Growth of the Construction Sector in the Economy**



Remittances have increased substantially in recent months, particularly from Russia, but uncertainties around their future trajectory remains high

**Figure 3.B.6: Inflow of Non-Commercial Transfers to Armenia by Source Country**



## External Trade and Demand

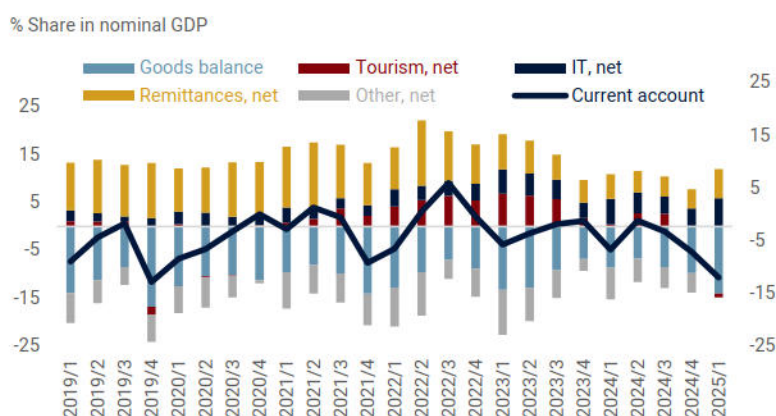
Armenia experienced a further deterioration in its current account in Q1 2025, as domestic demand gained momentum while external demand softened. The latter is reflected in a decline in external trade flows serviced by Armenia and its associated income, as well as a continued decrease in tourist arrivals to the country. However, tourism has significantly picked up in recent months (Figure 3.B.2), pointing to a potential strong rebound in Q2 that could compensate for the lost revenues in the sector in Q1. Together with robust domestic demand, these factors have pushed the current account somewhat closer to its sustainable level based on different estimates.

However, uncertainty looms around both the structure of the Armenian economy and the long-term sustainable level of its current account balance. On the one hand, although external trade flows have declined, Armenia continues to experience strong external and domestic demand for its goods and in particular for services. IT services exports continue growing relatively fast and as of Q1 2025 their exports reached around 6.5% of GDP. Financial services, is another category that speaks to the strong external demand pressures as its exports have expanded significantly in recent months reaching 2.7% of GDP in Q1. On the domestic front, a strong and steady consumption and investment appetite by households and businesses persists, clouding the near-term outlook for the current account position and rendering the economic spillovers from these forces uncertain (Figure 3.B.8). However, if these trends prove to be persistent, and if external demand in particular continues to rebound in a strong and persistent manner, this could serve as a source of further currency appreciation and/or inflationary pressures in the domestic economy.

At the same time, uncertainty around the fundamental level of real exchange rate leaves room for several interpretations. One such argument is that REER appreciation since 2022 reflects meaningful increases in productivity and potential output growth as evidenced by the increasing share of tradable goods and services exports in GDP and per capita productivity growth in those sectors (IT, financial services, etc....) that typically rely on human capital and innovation. This would suggest a structurally more productive economy with significantly enhanced long-term export potential and productive capacities (higher economic growth potential), supporting the case for a fundamental appreciation in the exchange rate (See Box XX). Alternatively, if these factors have been less pronounced, the REER appreciation would prove to be largely cyclical. Its eventual adjustment would likely be reflected in a corresponding correction of the current account balance.

Current account deterioration in Q1 reflects strong domestic and weak external demand, but a potential uptick in external demand could lead to improvement in Q2

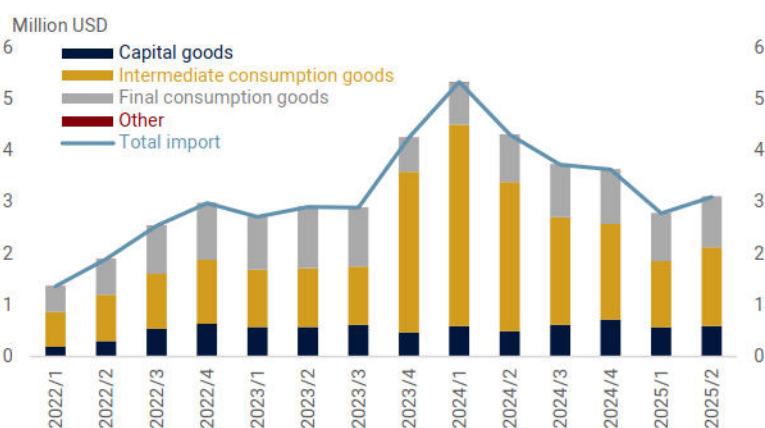
Figure 3.B.7: Current Account



Source: Statistical Committee of the Republic of Armenia; CBA

Persistently strong capital goods imports could point to a strong investment environment and support greater productive capacities in the economy

Figure 3.B.7: Value of Imports by Armenia by Broad Economic Category (BEC)



Source: Statistical Committee of the Republic of Armenia; CBA

Uncertainty regarding the cyclical position of the real exchange rate persists; stronger productivity growth could support a case for greater trend appreciation

Figure 3.B.8: Real Effective Exchange Rate and Trend for AMD against USD, EUR and RUB (Lower Value means Stronger Dram)



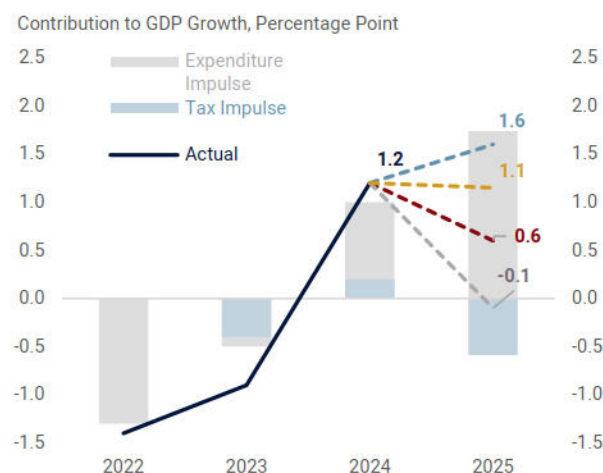
Source: CBA

## Fiscal Policy

The execution of the 2025 state budget reflects mixed trends. While tax revenues are slightly above planned levels, risks of under-collection remain. On the spending side, there are risks of over-performing current expenditures and, at the same time, under-performing in capital expenditures. As a result, uncertainties around the overall impact of fiscal policy persist. In the first half of 2025, tax revenues reached about 58% of the revised annual budget plan. This performance is largely driven by several factors: higher-than-planned nominal GDP growth, strong profits accumulated in some sectors during the previous year, an increase in completion acts in construction sector, boosting VAT collection, and some stricter tax enforcement. Nevertheless, last year's low tax base (a 7% underperformance), this year's ambitious targets, and the gradual fading of one-off factors could all pose risks of under-collection (Figure 3.B.11, Scenario 1). Regarding budget spending, the main uncertainty is related to its actual impact on demand conditions. On the one hand, both current and capital expenditures underperformed during January–July period, although execution has somewhat improved compared to historical trends. On the other hand, social spending needs could create pressure for higher current expenditures and utilization of the reserve fund (Figure 3.B.11, Scenario 1). If such pressures materialize, fiscal policy could prove more expansionary. This would deliver more demand-driven inflationary risks as well as concerns around public debt trajectory and the country's risk premium. Risks of under-execution of capital spending remains particularly relevant. The low base and weak execution in previous years, coupled with this year's higher targets (around 7% of GDP) and the economy's limited capacity to absorb such large scales of capital investment significantly increase the risk of underperformance (Figure 3.B.11, Scenario 2a). Furthermore, structural shifts in the composition of capital spending complicate the assessment of its impact on demand, further fueling uncertainty (Figure 3.B.11, Scenario 2b). Looking ahead, in the medium term the main risks refer to the sustainability of the deficit and debt dynamics. On the one hand, if revenue collection underperforms while expenditures remain elevated, this could deepen the deficit and increase financing pressures. On the other hand, tightening tax administration, as well as potential underperformance or a downward adjustment in current and capital expenditures, could negate risks of an increased debt burden and have less expansionary impacts on aggregate demand.

Uncertainties around fiscal policy impact stem from potential revenue under-collection, further use of reserve funds and underperformance in capital expenditures, exerting pressures on fiscal consolidation and debt sustainability

**Figure 3.B.10:** Scenarios for the Impact of Fiscal Policy on Aggregate Demand in 2025



Source: Ministry of Finance; CBA calculations

### Notes:

Scenario 1 – Underperformance of tax revenues, accompanied by a certain over-execution of current expenditures due to the necessity of increased social spending, along with the partial utilization of the reserve fund

Scenario 2a – Full implementation of the tax revenue plan; however, underperformance of capital expenditures in line with trends of previous years, largely because of limited capacity to implement large-scale projects.

Scenario 2b – Same as Scenario 2, but with an even weaker effect on aggregate demand, reflecting the structural characteristics of capital spending.

# C. Labor Market and Inflation

## Labor Supply and Demand

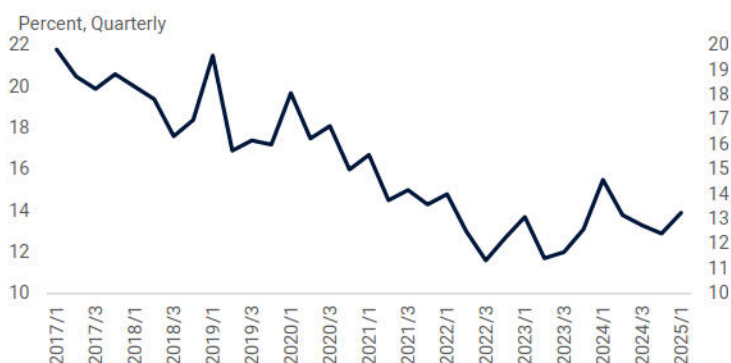
Uncertainties around labor market prospects persist, particularly regarding potential inflationary pressures driven by demand factors and possible shifts in labor supply. In the first quarter of 2025, Armenia's unemployment rate recorded a slight increase to 13.9%, partly due to seasonal factors (Figure 3.C.1). Nevertheless, it remains broadly consistent with its long-term equilibrium level. Overall, the labor market shows signs of gradually improving balance compared to previous years. Moreover, since 2024 the economy has experienced a significant expansion in labor resources and labor force. Both employment and labor force participation rates have been rising, consistent with the increase in officially registered employees reported by the State Revenue Committee (Figure 3.C.2). While these developments may suggest transition of labor from the informal to the formal sector, signals from the labor market still point to strong demand for labor.

Future trends in labor supply are largely linked to two key factors: the pace of labor market integration of forcibly displaced persons from Nagorno-Karabakh and the dynamics of labor migration flows to Russia. On the one hand, the narrowing wage gap between Armenia and Russia (compared to pre-2022 levels), risks surrounding Russia's economic outlook and tighter migration regulations in Russia may limit outbound migration, thus increasing domestic labor supply. On the other hand, remittance inflows from Russia have grown somewhat in recent months (Figure 3.C.3), potentially suggesting that an appreciated ruble and persistent labor supply issues in Russia outweigh these tail winds and have contributed to an increase in labor flows. To this end, recent ruble appreciation and positive expectations about a possible resolution of the Russia-Ukraine conflict could continue to support the recovery of migration flows.

In conclusion, various signals from the labor market point to demand for labor continuing to remain strong. However, the simultaneous increase in labor supply has helped absorb this demand and prevent the emergence of major inflationary pressures stemming from the labor market. Looking ahead, the key uncertainty relates to the future trajectory of labor supply growth, particularly if aggregate demand conditions accelerate. Further increases in labor supply in tandem with labor demand growth could prevent the emergence of any meaningful inflationary pressures from the labor market. At the same time, the potential for increased labor outmigration could contribute to tighter labor market conditions emerging, with accompanying inflationary implications.

Despite uncertainties around employment estimates, the labor market exhibits notable improvement towards equilibrium

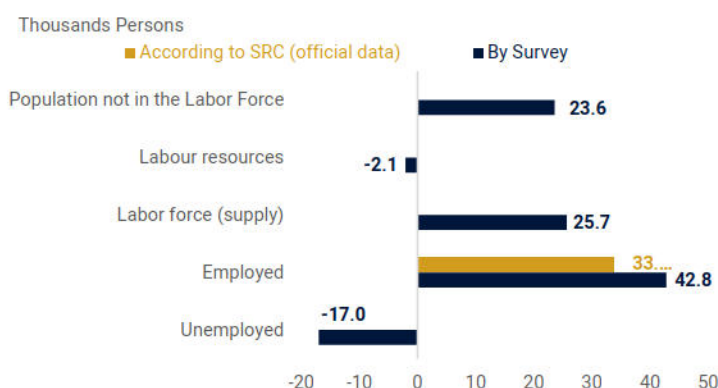
**Figure 3.C.1: Unemployment Rate, Armenia**



Source: Statistical Committee of the Republic of Armenia

The simultaneous increase in labor supply to meet demand has supported more balanced conditions in the labor market, preventing the emergence of significant inflationary pressures

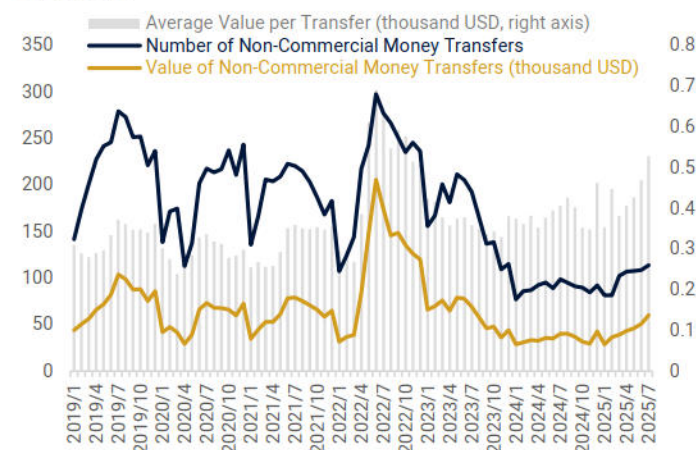
**Figure 3.C.2: The Change in RA Labor Resources, 2025Q1/2024Q1**



Source: Statistical Committee of the Republic of Armenia; CBA

Future uncertainties around labor market developments are shaped by migration trends and wage gaps between Armenia and Russia

**Figure 3.C.3: Non-Commercial Money Transfers from Russia to Armenia**



Source: CBA

## Wage Growth

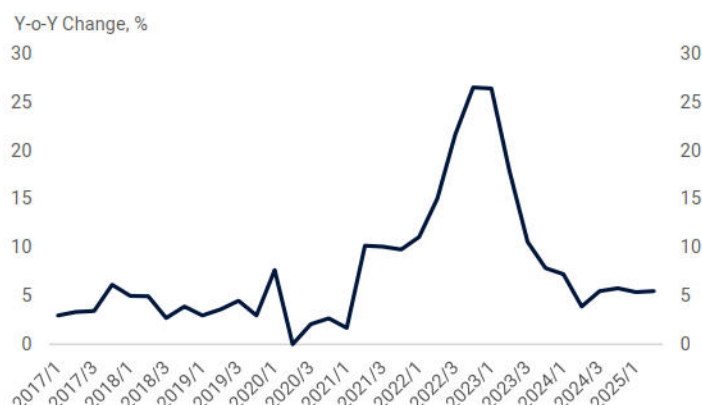
Nominal private sector wage growth continued to stabilize, reaching 5.6% year-on-year in Q2 2025 (Figure 3.C.4). Although in recent months there are notable signs that point to stronger labor demand, this stabilization could largely reflect supply-side factors. In particular, possible productivity gains in previous quarters, along with a significant expansion in labor supply, have helped maintain a relatively balanced labor market and easing inflationary pressures even amid accelerating demand. At the same time, as economic growth becomes less concentrated, wage growth is becoming more evenly distributed across sectors. While previously wage increases had been largely concentrated in services, and particularly in financial services, recently growth has become more broad-based. Moreover, some acceleration in economic activity and wage growth in other service sectors could suggest signals of demand-driven dynamics. Looking ahead, if these recent trends persist, wage-related inflation risks could intensify, especially if productivity growth slows and labor supply expansion lags behind (e.g. a slowing pace of labor market integration for Armenians from Nagorno-Karabakh).

## Inflation

Over 2025, inflation has shown some signs of accelerating, with CPI standing at 3.6% Y-o-Y in August. Since the beginning of the year, acceleration in annual inflation has been primarily driven by above-average increases in seasonal food prices, though its impact has been largely neutralized in June-August. At the same time, inflationary pressures from the global economy, particularly for imported food, have increased, reflecting increases in global food prices. Additionally, the deflationary pressures from non-food products observed earlier in the year have gradually subsided, and in August, year-on-year inflation stood at 1.1%. A persistence of global supply-side factors affecting imported goods prices could be a primary source of further increases in domestic inflationary pressures. Services inflation has increased somewhat in 2025, mainly due to high inflation for air transport services; excluding this subgroup, services inflation has remained stable and below target. At the same time, inflation for services highly exposed to external and domestic demand (e.g. hotels, restaurants, etc.) increased since May, consistent with increases in tourist inflows observed during this period. The persistence of these trends amid growing external demand could serve as a source of upward pressure moving forward. However, Non-Traded Sticky Price Inflation (NTSPI), which captures domestically-driven demand dynamics, has continued to remain stable, in the range of 2.0- 2.5% Y-o-Y. Conversely, core inflation has accelerated somewhat since the beginning of the year (3.7% Y-o-Y in August), primarily reflecting the above-described increases in imported non-seasonal food and certain exportable services.

Rising labor supply is offsetting inflationary pressures amid accelerating demand.

Figure 3.C.4: Nominal Private Wage Growth, Armenia



Source: Central Bank of Armenia

CPI has increased since the beginning of the year, primarily driven by supply factors globally and domestically

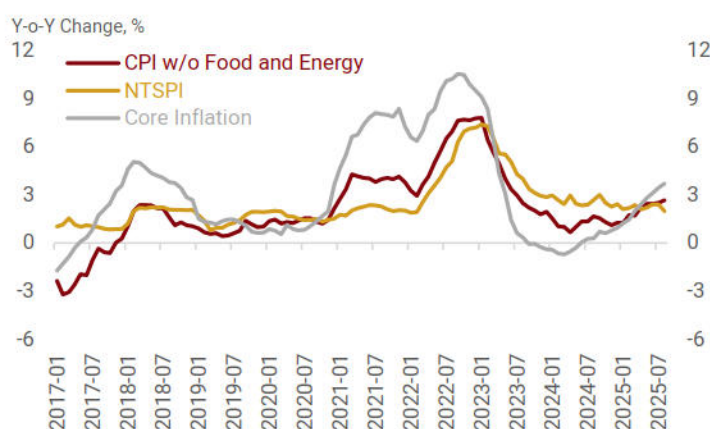
Figure 3.C.5: Y-o-Y CPI Inflation and the Target, Armenia



Source: Statistical Committee of the Republic of Armenia, CBA

Non-traded sticky prices have largely stabilized

Figure 3.C.6: Underlying Inflation Measures, Armenia



Source: Statistical Committee of the Republic of Armenia, CBA

## Box 1. Supply-Side Inflationary Pressures and the Role of Monetary Policy

Understanding the fundamental factors underlying inflation dynamics is a key component to the monetary policy decision-making process. In the short run, inflation can be influenced not only by demand-side factors but also by temporary price fluctuations stemming from supply-side factors—for example, variations in agricultural output due to weather conditions, disruptions in global supply chains, and so on. Over the past few years, supply-side factors have played an increasingly prominent role in shaping global inflation dynamics. The COVID-19 pandemic led to widespread disruptions in global supply chains and logistical bottlenecks, while escalating geopolitical tensions and the growing impact of climate change have further amplified these challenges. Together, these developments have significantly strengthened the influence of supply-side factors on inflation across economies. Driven by the above-mentioned factors, global food prices—as measured by the FAO Food Price Index—accelerated sharply during 2020–2022, recording an average year-over-year increase of 15.7%. In 2023–2024, inflationary pressures transmitted from the global economy gradually subsided, reflecting the easing of supply chain disruptions and a moderation of imbalances between global supply and demand. Consequently, global inflationary pressures eased, giving way to disinflationary trends. Since the end of 2024, deflationary trends in the global economy have gradually shifted to inflationary pressures, caused by several factors. These factors include agricultural production variability caused by climate change, rising prices of energy and other raw materials, the recovery of global demand, and other related influences. Over 2025, the effects of the aforementioned factors have been compounded by persistent geopolitical tensions and the risks stemming from trade restrictions. These developments currently represent additional sources of risks and uncertainty, contributing to the expansion of the global inflationary environment. Global inflation developments are transmitted to domestic inflation through several key channels:

- Changes in the prices of imported consumer goods directly affect the domestic consumer price index (CPI)
- Fluctuations in the prices of imported raw materials and intermediate goods used in domestic production lead to changes in production costs, which are often passed on to consumer prices.
- Competition between imported and domestically produced goods can lead to price adjustments in the local market as producers respond to changing relative prices.
- Changes in inflation expectations, which can lead to price adjustments in other goods and services within the economy

Imported food products comprise approximately 15% of Armenia’s consumer basket. Between 2020 and 2025, price movements of imported food products in Armenia have largely aligned with global inflationary trends (Figure B.1.1): In addition to imported goods, global price developments also affect domestic inflation through imported raw materials and intermediate goods used in domestic production. Rising global prices of raw materials—such as grains, fuel, and packaging materials—increase production costs, which are typically passed on to the prices of final goods. Additionally, competition between imported and domestically produced goods also influences price-setting behavior. In sectors where domestic goods compete with imports, changes in import prices can lead to adjustments in local prices, depending on the direction of the price changes. In this context, the increase in prices of imported food products during 2024–2025 has been accompanied by a rise in domestic food prices (Figure B.1.2).

In theory, monetary policy primarily responds to aggregate demand factors influencing overall inflation. However, in the case of inflation fluctuations driven mainly by supply-side factors—since these tend to be temporary and gradually dissipate over time—monetary policy typically does not react unless such supply-driven inflationary pressures significantly affect inflation expectations (Figure 3.C.7). Nevertheless, the persistent and prolonged presence of inflationary pressures primarily driven by supply-side factors may lead to undesirable developments in inflation expectations. Theoretically, to ensure price stability in an economy, such a scenario could require a prudent response from monetary policy (refer to the Statement on the Long-Term Objectives of Monetary Policy).

Figure B.1.1. FAO Food Price Index

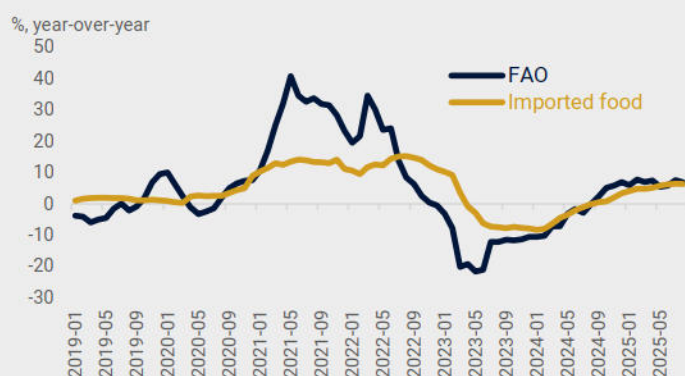
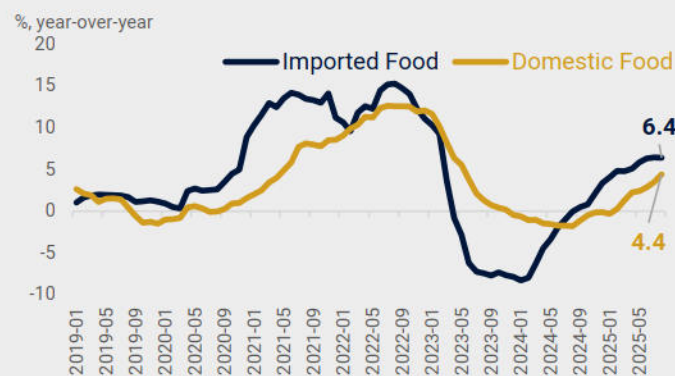


Figure B.1.2. Domestic and Imported food price index

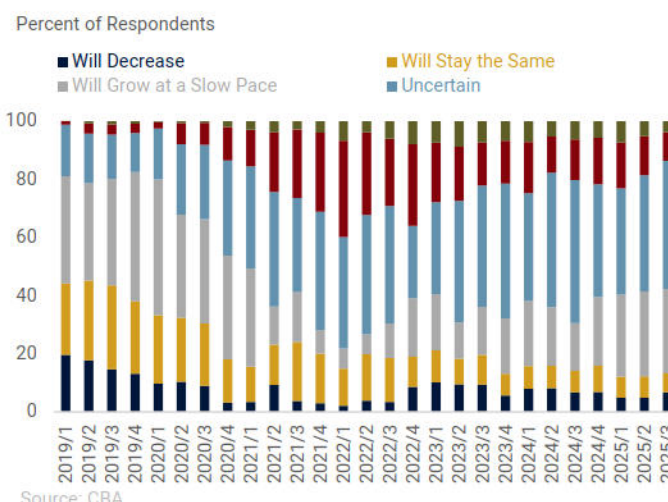


## Inflation Expectations

According to the results of the household inflation expectations survey conducted by the Central Bank of Armenia, in the third quarter of 2025, elevated inflation expectations have declined, but uncertainty has increased somewhat. Accordingly, the share of respondents expecting a slower pace of price increases has remained unchanged. These developments may reflect the gradual stabilization of inflation expectations around the target level, largely supported by the prolonged low-inflation environment in the economy. Nevertheless, the persistence and slight increase of high uncertainties may reflect public perceptions of sustained high inflation particularly for certain food products. At the same time, developments in the Non-Traded Sticky Price Index and private wage growth may point to low and stable inflation expectations.

### Uncertainty around inflation expectations persists

**Figure 3.C.7: Survey on Households' Inflation Expectations, Armenia**



## D. Financial Markets

### Market Expectations of Policy Rates

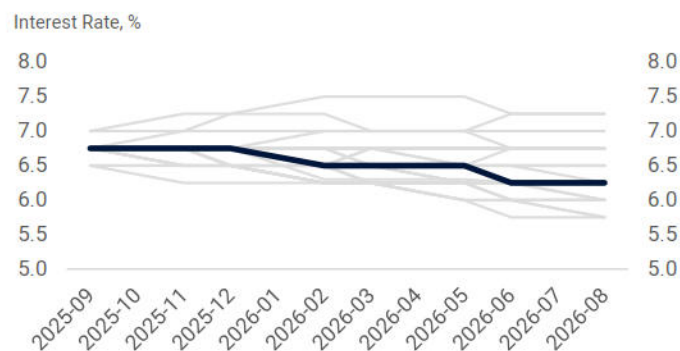
According to the latest survey conducted by the CBA among financial market participants, as of September 10, 2025, market participants on average expect the CBA to continue to very gradually decrease the policy rate over the course of the next eight decisions. This is generally consistent with the results from the CBA's Q3 Macro Survey (see Box 4), where participants expect a gradual reduction of the policy rate over the medium-term horizon to estimated long-term stable levels of roughly 6.25%. In line with participants' expected macroeconomic outlook, markets expect both growth and inflation to gradually stabilize around their long-term sustainable levels. In this context, the yield curve continues to remain largely stable, although some slight shifts have been observed. Overall, the slight shift in the long-term segments of the yield curve following the June 2025 monetary policy decision may reflect modest shifts in market participants' expectations regarding long-term interest rates, as well as a possible reassessment of perceptions related to macroeconomic risks. This may reflect a reassessment of risks related to Armenia's debt sustainability, US long-term interest rates, geopolitical uncertainties, and other factors. While those issues cannot be directly implied from survey results, they nonetheless pose significant uncertainty in terms of assessing the long-term neutral rates that are priced in financial markets.

### Neutral Interest Rate

Considering the general neutrality of economic demand, labor market conditions, and the inflationary environment, the current stance of the monetary policy can be assessed to be close to neutral. However, significant uncertainty remains regarding the underlying components of the neutral interest rate, including the US neutral rate, inflation expectations, the country risk premium, and fundamental exchange rate appreciation. In this context, a significant expansion of US debt and deficit levels could result in a higher neutral rate there, exerting upward pressure on neutral rates in emerging markets including Armenia. The country risk premium has continued to decline in the recent period. Regional geopolitical developments may have positive impacts on the long-term sustainable level of the country risk premium (Figure 3.D.6). However, a persistence of regional tensions could result in a higher fundamental risk premium level. Further, increases in Armenia's export and productive capacities in recent years, and the resulting trend appreciation of the real effective exchange rate point, could lead to a downward reappraisal of the neutral rate, particularly if productivity and potential export gains prove stronger than assumed (see the Illustrative Case B scenario). Moreover, considering the CBA's reduction in the inflation target to 3% beginning in January 2025, as well as persistently low inflation in non-traded sticky prices (see subsection C), inflation expectations may already be fully anchored at the new target, again contributing to a lower level for the nominal neutral rate.

Most market participants expect gradual declines in the policy rate over the next year

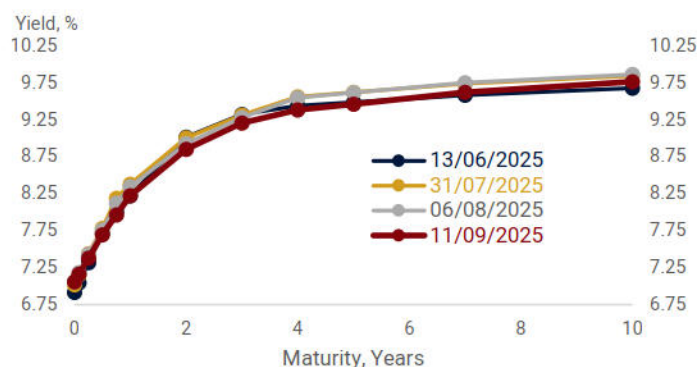
**Figure 3.D.1:** Financial Market Participants' Expectations of the CBA Policy Rate According to September 10, 2025 CBA Survey



Source: CBA

Yield curve has remained generally stable

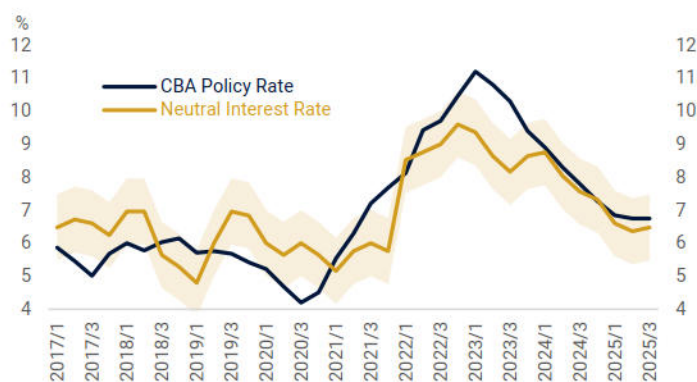
**Figure 3.D.2:** Yield Curve Dynamics, Armenia



Source: CBA

How Tight are Monetary Conditions?

**Figure 3.D.3:** CBA Policy Rate and Underlying Equilibrium Rate



Source: CBA

## Bank Lending Conditions

Bank lending continued to expand in Q2 2025, with Y-o-Y credit growth rates hovering around 30%, reflecting sustained high demand for credit in the economy. Strong growth in consumer loans to households could point to the potential for further growth in domestic demand conditions. In contrast, mortgage growth has softened somewhat but continues to grow at a strong pace. This suggests that demand for real estate (whether for housing or investment) continues to remain strong in both Yerevan and adjacent regions, even as some natural, gradual adjustments are taking place. CBA surveys suggest commercial banks continue to expect sustained demand growth in, and continued net easing of conditions for, consumer and business loans factoring overall economic conditions and increasing competition in the sector. The persistence of strong credit growth in the economy, especially if it starts to reflect the easing of supply conditions, could support sustained consumption and elevated demand conditions, potentially heightening inflationary pressures.

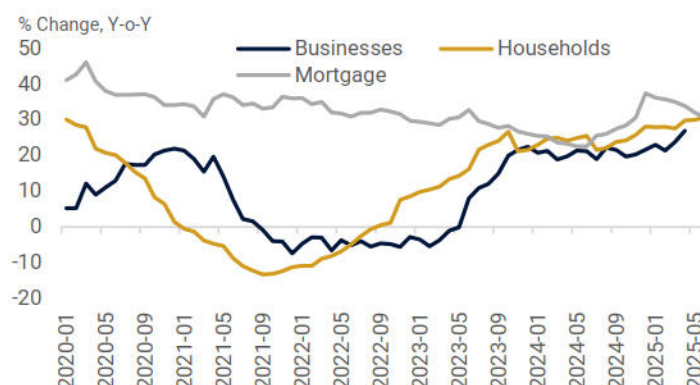
## Nominal Exchange Rate

In Q2 2025, the nominal appreciation of the Armenian dram against the US dollar (Figure 3.B.7) was driven by a combination of factors, including a moderate strengthening of capital inflows and a depreciation of the US dollar against the currencies of both advanced and emerging market economies. The U.S. dollar weakened by about 3% in the first half of the year, and despite a modest recovery in July, the delayed impact of tariffs, higher unemployment risks, and policy uncertainty could continue to raise questions about the strength of the Dollar, with investors increasingly hedging their exposure to U.S. assets. A high interest rate environment in Russia and improved expectations about conflict resolution have helped the Ruble appreciate against all currency groups.

Armenia's sovereign risk premium has declined further in recent quarters in tandem with broader improvements across emerging markets as well as country-specific factors (Figure 3.D.6). This decline could reflect a favorable reassessment of risks, supported not only by the easing of overall sentiment toward emerging markets but also by expectations of a cooling in immediate geopolitical risks in the South Caucasus. At the same time, slightly improved expectations of a potential de-escalation in the Russia-Ukraine conflict may have reinforced the improved outlook for the region and supported a more benign external environment. Nevertheless, the persistence of global and regional geopolitical uncertainty, coupled with uncertainty about future US economic policies, continue to present potential sources of volatility and the possibility of renewed upward pressure on Armenia's sovereign risk premium. In this context, several rating agencies note that the ultimate, fundamental adjustments in the country risk premium in response to the above developments would come only after the expected economic implications materialize.

Strong and sustained credit expansion could keep demand conditions and inflationary pressures elevated

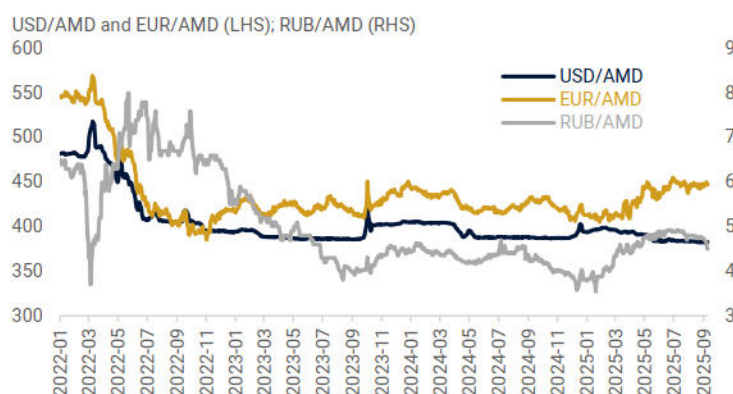
**Figure 3.D.4:** Change in Total Loans Provided by Commercial Banks to Households and Businesses, Armenia



Source: CBA

Nominal exchange rates impacted by sustained inflows and dollar weakness on the one hand, and strengthening Euro and Ruble on the other

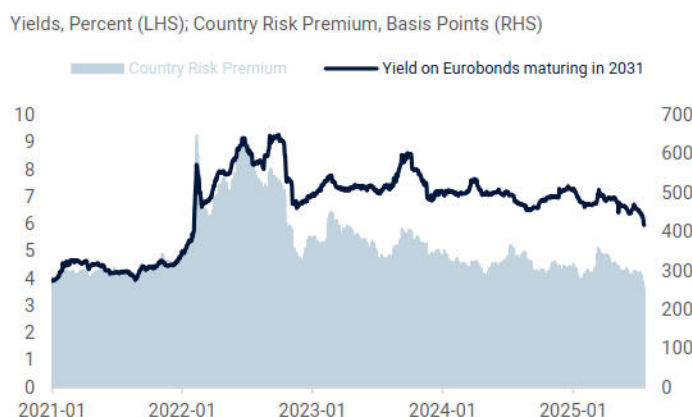
**Figure 3.D.5:** Nominal Exchange Rate for AMD against USD, EUR and RUB (Lower Value means Stronger Dram)



Source: CBA

While the country risk premium continues to decline, uncertainty regarding its fundamental, sustainable level persists

**Figure 3.D.6:** Yield on Armenian Eurobonds Maturing in 2029 and Estimated Country Risk Premium



Source: Ministry of Finance, CBA

## Box 2. Scenarios-Based Forward Guidance: The Role of Market Expectations

Approaching monetary policy through the lens of risk management under FPAS Mark II requires a different approach to the scenario-building process. Rather than treating its own central projections as the best piece of information and forcing market participants to coalesce around this singular view of unfolding economic conditions, the CBA instead utilizes market expectations for the central bank policy rate as a starting point for policy deliberations. Market expectations, by design, contain significant information about market views on current economic developments and possible behavior of monetary policy in the future economic environment.

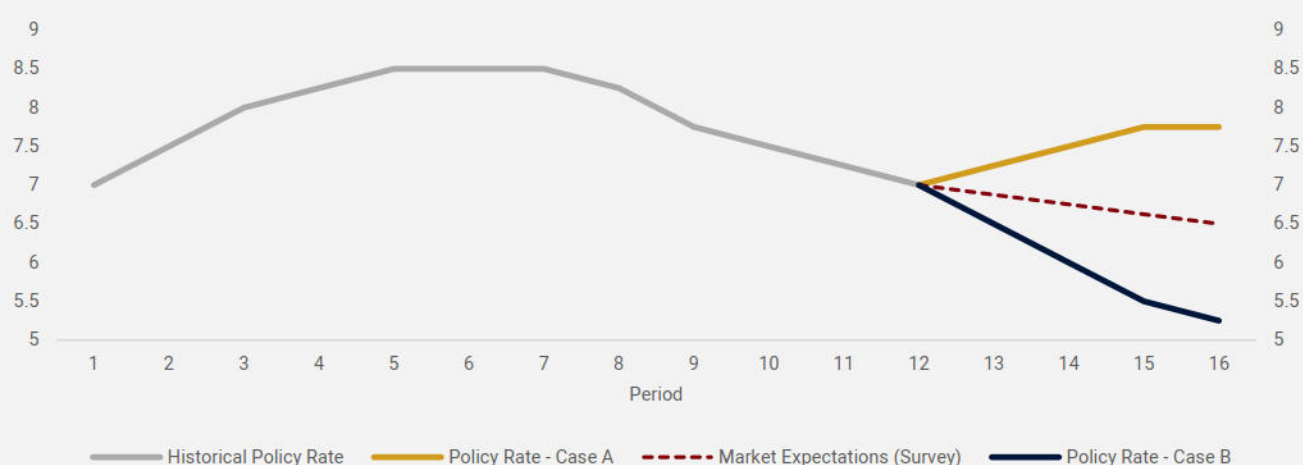
Before the development of flexible-inflation-targeting approaches, monetary policy communication predominantly focused on direct actions like the setting of short-term policy rates. However, short-term rates are not particularly relevant for most people; longer-term interest rates tend to hold greater significance as these are the types of maturities at which households and businesses typically borrow and lend. The two principal components that make up longer-term rates are the term and risk premiums and the expected path of the policy rate. Of these two components, the expected path of the policy rate is most significant. As inflation targeting regimes were adopted, transparency in communicating a central bank's perspective and rationale became a necessary precondition for the regime's efficacy. With greater central bank clarity, financial markets gain the agility to recalibrate efficiently between policy decisions. Importantly, on decision dates, policymakers do not merely set the current policy rate; they also provide insights into their monetary policy decisions, including how the policy rate may change in the future based on different narratives, scenarios, and assumptions.

In advanced economies with well-developed financial markets (including secondary bond markets), gleaned market expectations of the future path of the policy rate is a relatively straightforward task. For countries with less developed financial markets that lack options markets, such as Armenia, the task is less straightforward. It requires synthesizing multiple approaches, without resorting to "over-modeling" and attempting to ascribe a false degree of precision that is based on unreliable or incomplete information.

**Market Expectations of the Policy Rate:** We synthesize three approaches. First, we take as a starting point information from the spot market for shorter-term bonds (one year and less) and perfect foresight-based inferences about the term structure of the yield curve. We recognize that data from the spot market is imperfect and cannot paint a complete (or always accurate) picture about market expectations of the policy rate. For example, bond markets experience high term premium volatility, face frequent liquidity and other shocks, and so on, making it difficult to perfectly assess which price movements result from changes in expectations versus other factors. Second, considering this issue, we therefore also conduct a quarterly macro survey of financial markets (including commercial banks, institutional investors, asset managers, and others), who provide a macro-consistent projection of inflation, growth, policy rate, and exchange rate over the medium-term horizon, along with accompanying narratives supporting these scenarios. Recognizing that economists' projections may deviate from how financial participants actually behave, we finally dovetail this approach with a high-frequency survey of policy rate expectations among dealers in commercial banks and credit organizations.

**Scenarios-Based Forward Guidance:** To graphically illustrate our case scenarios relative to market expectations, we rely on the following approach (see the figure below). The grey line represents the CBA's refinancing rate historically. Market expectations are depicted with a red dashed line, representing the market's assessment of the most probable trajectory of the average policy rate over the course of the next 3 years. This provides a reference point around which the illustrative Case A (orange line) and Case B (blue line) scenarios for the policy rate are constructed.

**Figure B.3.1: Hypothetical** Example of Case Scenarios and Market Expectations under the Prudent Risk Management Framework  
Interest Rate, %



Source: CBA

# E. Taxonomy of Scenarios

## Purpose and Structure of the Taxonomy

The Taxonomy of Scenarios provides a comprehensive, structured assessment of the different types of risks, shocks, and sources of uncertainty that can affect the Armenian economy. It describes their potential impacts on inflation and economic environment in Armenia, as well as loosely illustrates implied monetary policy reactions by the CBA. As a structured summary of the various policy-relevant scenarios considered by the Board of the CBA, the Taxonomy presents the key issues that can impact policy decisions over a medium-term horizon in the context of a least regrets decision-making framework. The evolving Taxonomy of Scenarios is published in each quarterly MPR.

Table E.1: Taxonomy Structure

| Case A-Type Considerations                                                                                                                                                                                                                                                                                                                                | Case B-Type Considerations                                                                                                                                                                                                                                                                                                                                       |
|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <b>Expansionary Demand:</b><br><br>Shocks result in aggregate demand rising more than aggregate supply, increasing underlying inflation. This requires an increase in the policy rate path that is sufficiently aggressive to anchor inflation and inflation expectations.<br><br>Complications: credibility is fragile<br><br>Output +   Inflation +     | <b>Contractionary Demand:</b><br><br>Shocks result in aggregate demand rising less than aggregate supply, decreasing underlying inflation. This requires a decrease in the policy rate path that is sufficiently aggressive to anchor inflation and inflation expectations.<br><br>Complications: ELB, stuck in low inflation trap<br><br>Output -   Inflation - |
| <b>Contractionary Supply:</b><br><br>Nasty stagflationary shocks that require an aggressive upward adjustment in the expected path of the policy rate, resulting in a significant short-run tradeoff between inflation and other real objectives (e.g., unemployment)<br><br>Complications: Hard to hit the wounded economy<br><br>Output -   Inflation + | <b>Expansionary Supply:</b><br><br>Favorable supply shock(s) reduce inflation toward the target and results in higher growth as well as lower interest rates; is a policymaker's dream.<br><br>Complications: can be risky if this environment is extrapolated into the future<br><br>Output +   Inflation -                                                     |

The taxonomy is classified into those that can have Case A-type (expansionary demand, contractionary supply) and Case B-type (contractionary demand, expansionary supply) considerations. Although the classification of shocks can be done in different ways across different features, the one presented here is based on a typical distinction between supply and demand side forces and is particularly useful from policymakers' point of view as it provides a framework for analyzing the source of inflationary pressures and potential risks to the economy. By understanding the nature and magnitude of different types of shocks, policymakers can then design appropriate monetary policy responses to mitigate the negative impact of adverse shocks and leverage the benefits of positive shocks.

## Taxonomy of Scenarios: Q3 2025

Table E.2: Taxonomy of Scenarios: Q3 2025

| <b>Case A-Type Considerations</b><br><b>Expansionary Demand</b>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                         | <b>Case B-Type Considerations</b><br><b>Contractionary Demand</b>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                            |
|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <ul style="list-style-type: none"> <li>• In the United States, the reconfiguration of fiscal rules has heightened uncertainty regarding the magnitude of fiscal stimulus and, more critically, the trajectory of long-term public debt accumulation. This may exert upward pressure on the U.S. neutral interest rate, with potential spillover effects on the neutral rates of developing economies, including Armenia.</li> <li>• Persistent uncertainties around domestic demand conditions, particularly regarding the emergence and potential persistence of excess demand: <ul style="list-style-type: none"> <li>• Economic growth exceeding its estimated long-term potential and concentrated in primarily demand-driven sectors (tourism, finance, other services) could point to excess demand conditions in the Armenian economy.</li> <li>• Sustained growth in consumption driven by accumulated savings, wealth, and credit growth, as well as rising incomes linked to favorable export performance, may further amplify aggregate demand conditions.</li> <li>• Recent increases in tourism flows, as well as sustained strong demand for Armenian goods and especially services, could generate additional demand and inflationary pressures.</li> <li>• The adoption of a more expansionary fiscal stance than previously anticipated present risks of further intensifying domestic demand pressures.</li> </ul> </li> <li>• Ongoing negotiations to resolve the Russian-Ukrainian conflict, coupled with the continued enforcement of sanctions against Russia, may further bolster capital inflows into the Armenian economy, thereby amplifying domestic demand and reinforcing inflationary pressures.</li> <li>• Inflationary trends from the global economy, especially for food and basic necessities, could lead to an undesirable increase in inflation expectations in Armenia.</li> <li>• A possible cooling of regional geopolitical tensions could pose risks of accelerating capital inflows, which could contribute to an expansion in demand conditions.</li> </ul> | <ul style="list-style-type: none"> <li>• Subdued domestic demand—arising from structural challenges in the global economy, particularly within the Eurozone and China—may prove persistent, contributing to a prolonged period of low inflation in international commodity and raw material markets.</li> <li>• Prolonged elevated uncertainty surrounding U.S. economic policy could evolve into a broader crisis of confidence, sharply dampening consumer and investment activity both within the United States and across the global economy.</li> <li>• Expectations surrounding U.S. economic activity have moderated, while uncertainty has intensified. Under these conditions, a potential sharp correction in the prices of still-overvalued assets could generate deflationary pressures both globally and within the Armenian economy.</li> <li>• In the context of a gradual, natural adjustment in construction and real estate prices, related sectors of the economy may experience slowing growth, softening demand, and emerging deflationary effects.</li> <li>• In response to the strong external demand observed in recent years, the private sector in the Armenian economy—particularly in certain industries—accumulated substantial credit liabilities amid expectations of sustained high future income. Given risks of a worsening global economic outlook and a possible adjustment in external demand, these liabilities may become an additional constraining factor, potentially leading to a disproportionate tightening of income and expenditure dynamics, especially within the services sector.</li> <li>• The increase in certain tax rates and the tightening of tax administration, as well as a downward adjustment in current and capital expenditures, may exert additional dampening effects on investment activity, potentially contributing to higher unemployment and subdued demand.</li> <li>• In the event of a resolution to the Russian-Ukrainian conflict and the full or partial removal of sanctions, a substantial outflow of capital and labor from the Republic of Armenia may occur, posing risks of a marked weakening in aggregate demand and, more notably, a moderation of inflationary pressures.</li> <li>• Uncertainty about neutral rate fundamentals in Armenia: <ul style="list-style-type: none"> <li>• Growth in productive capacities and productivity in exportable sectors in recent years—in tandem with an improved investment climate, persistent capital flows, and an historical and expected appreciation of the real exchange rate trend—implies a lower level of the neutral rate.</li> <li>• A possible cooling of regional geopolitical tensions could contribute to a reappraisal of country fundamentals, including a lower country risk premium and thus a lower neutral rate.</li> </ul> </li> </ul> |

| <b>Case A-Type Considerations</b><br>Contractionary Supply                                                                                                                                                                                                                                                                                                                                                                                                                                                                                           | <b>Case B-Type Considerations</b><br>Expansionary Supply                                                                                                                                                                                                                                                                                          |
|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <ul style="list-style-type: none"> <li>• Amid the tightening of trade policies among major economies and the broader trend of de-globalization, disruptions in global supply chains may lead to higher production costs and a broadening of inflationary pressures in the global economy over the short to medium term.</li> <li>• An accumulation of stagflationary risks in the global economy could result in a higher path for interest rates in advanced economies if inflation expectations there prove to be imperfectly anchored.</li> </ul> | <ul style="list-style-type: none"> <li>• Continuous growth of labor supply in the Armenian economy, resulting from uncertainties about medium-term developments in the Russian economy and, notably, the persistent decline in seasonal migration from Armenia to the Russian Federation amid tightening migration policies in Russia.</li> </ul> |

### Box 3. Market Reference Scenario

Under the CBA Monetary Policy Framework (FPAS Mark II), the CBA does not prepare baseline projections. Instead, we rely on information from financial market participants (including commercial banks, fund managers, institutional investors, and so on)—compiled through quarterly surveys—to develop a macro-consistent “market reference scenario (MRS).” This MRS, in many ways, serves a similar purpose as a traditional baseline projection, in the sense that it represents the market’s rough estimation of the “most likely future,” given the information available to market participants at a particular point in time. The MRS can serve as a substitute for the baseline for those external stakeholders (e.g. IFIs, fiscal authorities, and others) who rely on exogenously-provided projections when making their own planning decisions. Through the use of the MRS, the CBA provides the opportunity to markets to not only understand third-party forecasts of the “most likely” future, but also pay attention to those types of risks, uncertainties, and scenarios that can pose risks from the perspective of monetary policy and price stability (which are presented in the preceding Taxonomy). At the same time, this provides an opportunity to effectively communicate the logic and rationale behind CBA’s policy decisions under the prudent risk management approach.

Note: The CBA Macro Survey is conducted on a quarterly basis by the CBA. For the purposes of informing the Market Reference Scenario, participants are each asked to provide a macro-consistent scenario, including a qualitative description of the narrative underlying the scenario and associated Case A- and B-type risks, as well as accompanying quantitative 12-quarter-ahead projections for CPI inflation, real GDP growth, the CBA policy rate, and the nominal AMD/USD exchange rate. The Q3 2025 survey was carried out in August 2025.

Figure B.3.1: CPI Inflation

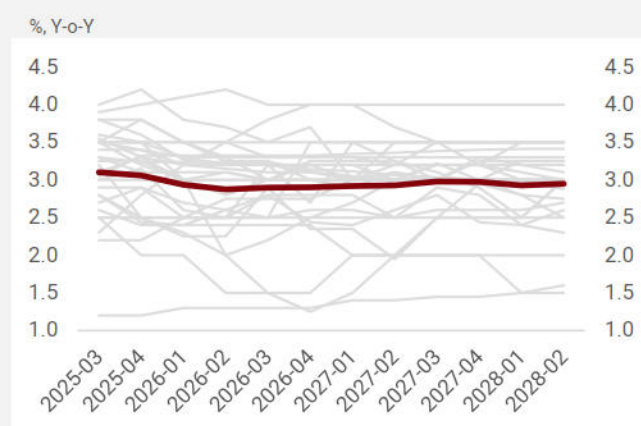


Figure B.3.3: Real GDP Growth Rate

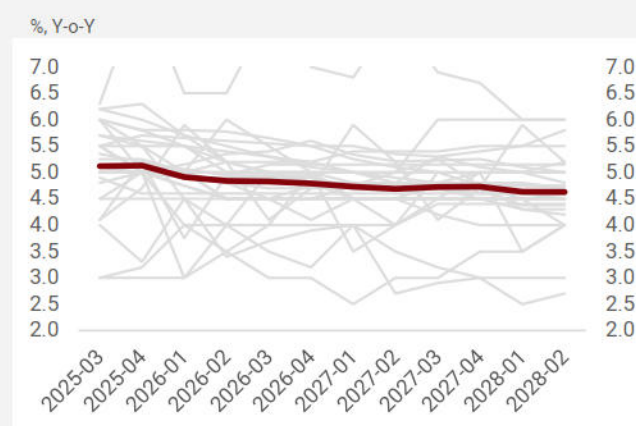


Figure B.3.2: CBA Policy Rate

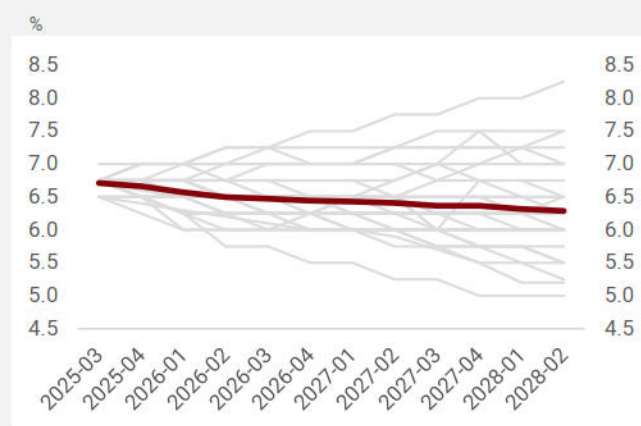
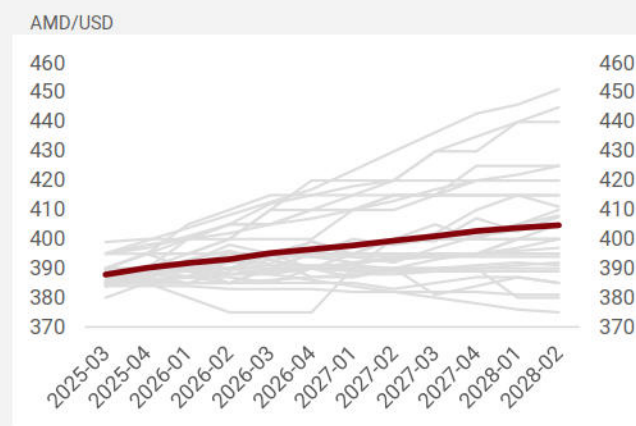


Figure B.3.4: Nominal AMD/USD Exchange Rate



\* Note: CBA Macro Survey shown as average of survey responses (line) and individual responses (grey lines).

Table B.3.1: Summary of Third-Party Projections

| Source<br>Date                     | IMF<br>Apr-25 | CBA Macro Survey<br>Q3 25 | Consensus<br>Sep-25 |
|------------------------------------|---------------|---------------------------|---------------------|
| <b>GDP Growth (Annual Rate, %)</b> |               |                           |                     |
| 2024 (Actual)                      |               | 5.9                       |                     |
| 2025                               | 4.5           | 5.1                       | 4.8                 |
| 2026                               | 4.5           | 4.8                       | 4.8                 |
| 2027                               | 4.5           | 4.7                       | 4.2                 |
| <b>Inflation (Annual Rate, %)</b>  |               |                           |                     |
| 2024 (Actual)                      |               | 0.3                       |                     |
| 2025                               | 3.2           | 3.2                       | 3.2                 |
| 2026                               | 3.0           | 3.0                       | 3.0                 |
| 2027                               | 3.0           | 3.0                       | 3.0                 |

Source: IMF, World Bank, ADB, CBA Macro Survey

## F. Monetary Policy Outlook

### Case A: Expansion in External Demand could Require Interest Rates above Market Expectations

The recent acceleration in tourism flows, along with persistently strong external demand for Armenian goods and especially services, may generate additional demand and inflationary pressures in the economy.

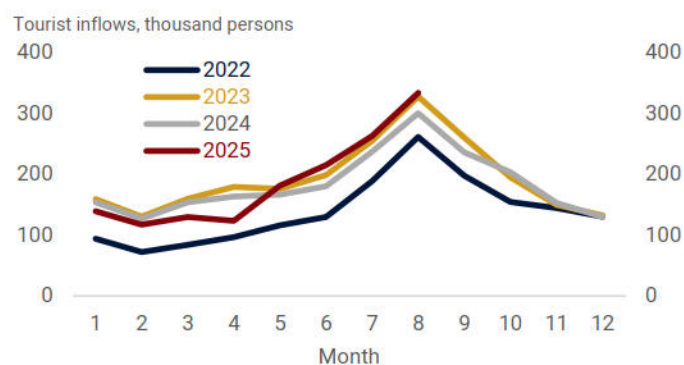
Beginning in Q2 2025, however, signs of an uptick in external demand have emerged. Since May 2025, Armenia has witnessed a sharp recovery and acceleration in tourism flows, reaching record-high levels. The composition of tourism has shifted, with Russian inflows recovering but not exceeding 2024 levels, while a surge in arrivals from new, non-traditional destinations has become the main driver of this acceleration. This resurgence has supported higher tourist spending, as shown by higher foreign card transactions in accommodation and food services, reversing the earlier trend of lower per-visitor expenditures and creating renewed inflationary pressures in sectors exposed to external demand, such as restaurant and hotel services. Beyond tourism, foreign demand for locally produced goods and services, particularly manufacturing exports and financial services, remains strong and continues to expand rapidly. In addition, remittance inflows have accelerated significantly in recent months, as reflected in increased transfers through the financial system. Cash ruble conversions have also grown, which could also point to rising remittances. This acceleration has likely been driven by Ruble appreciation and labor shortages in Russia.

These patterns support a scenario of a positive external demand shock. Under such a scenario, the free-floating exchange rate, as a shock absorber, would be expected to appreciate in order to absorb external demand and prevent inflationary pressures from transmitting to the domestic economy.<sup>1</sup> However, while the exchange rate appreciation would be expected to absorb much of the external demand shock, one of the main risks under this scenario is that localized inflationary pressures (e.g. in services highly exposed to external demand, such as restaurants and hotels) could lead to inflation expectations ticking upward. Therefore, under this scenario, the policy rate would also need to increase and follow a higher path relative to market expectations in order to prevent localized inflation pressures from translating into higher generalized inflation expectations.

<sup>1</sup> Evidence of the exchange rate's role as a shock absorber in Armenia can be seen in 2022, particularly when comparing Armenia's experience to peer countries that faced a similar shock. Countries that allowed their exchange rates to appreciate and absorb external demand pressures experienced a much milder inflationary

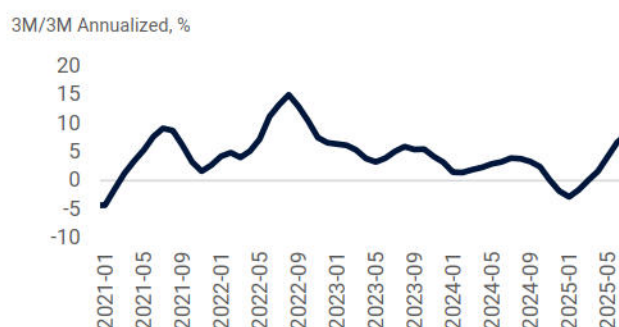
**Figure 3.F.1:**

**Panel A.** The recent acceleration in tourism flows may indicate an expansion of external demand



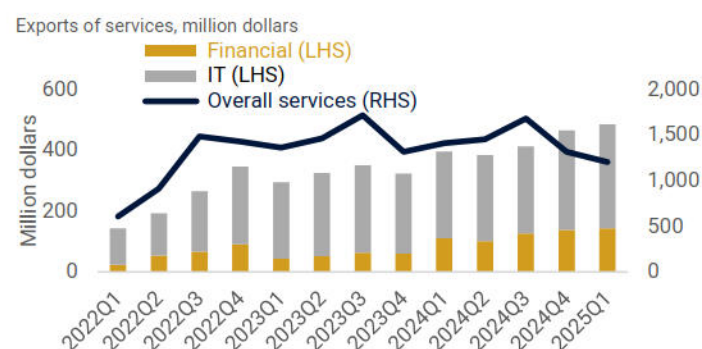
Source: Tourism Committee of the Republic of Armenia

**Panel B.** Inflation in restaurants and hotel services



Source: Statistical Committee of the Republic of Armenia

**Panel C.** External demand for Armenian goods and especially services remains robust



Source: CBA

environment, while those that kept exchange rates fixed allowed the external demand shock to generate high inflationary pressures in the economy and experienced significantly higher rates of inflation. See the Q2 2022 CBA Inflation Report.

## Case B: Growth in productive capacities and productivity in exportable sectors could imply a relatively lower level of neutral rate which would require Interest Rates below Market Expectations

Growth in productive capacities and productivity in exportable sectors in recent years—in tandem with an improved investment climate, persistent capital flows, and an historical and expected appreciation of the real exchange rate trend—could imply a lower level of the neutral rate

In 2022, massive inflows of highly-skilled human capital, businesses, and capital flows catalyzed a robust expansion in several sectors of the economy, most notably IT services. Prior to this, Armenia already benefitted from a booming tech ecosystem, with a thriving startup culture (including a homegrown unicorn), the presence of several global tech giants, and strong government incentives. The massive inflow of highly-skilled human capital—which was accompanied with new business formations and capital flows—accelerated this trend, contributing to an increasingly productive and globally competitive tech sector that has since emerged as a key driver of the Armenian economy. Output per worker increased by almost 39% from 2020 to 2025, while exports as a share of GDP increased from 2.8% to 6.4% during this period. In tandem with these developments in IT services, financial services similarly experienced remarkable growth. Amid strong and sustained capital and financial flows, Armenia's financial sector experienced strong growth, contributing, on average, 1.5 p.p. to GDP growth in each quarter since 2022. Output per worker more than doubled since 2020, while financial services exports have come to represent a meaningful 2.7% share of GDP in Q1 2025 (versus 0.7% in Q1 2020).

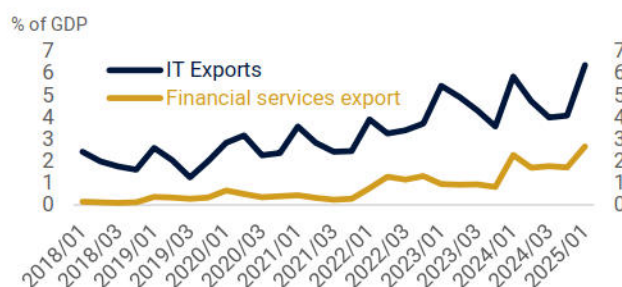
Manufacturing has experienced a similar surge in exports and potential. Restrictions on access to global goods in Armenia's largest trading partner in 2022 sparked a preference shift toward Armenian goods. In traditional subsectors including prepared food, beverages, and tobacco, Armenian producers capitalized on this opportunity to significantly increase their productive capacities and global competitiveness. Manufacturing exports, which between 2018 and 2022 averaged approximately 230 million dollars per month, have since increased by roughly 1.9x, averaging 440 million dollars per month since Q2 2022. Strong and sustained imports of capital goods point to consistently growing productive capacities.

Together, this significant and sustained growth in productive capacities and global competitiveness in Armenia's key tradeable sectors since 2022 could point to a new equilibrium forming in the economy. Strong growth in productivity and export potential could support a higher rate of growth for potential output. Moreover, research shows that in small open economies, rising productivity and export capacities, in tandem with a strong investment climate, leads to persistent capital flows which in turn support greater real exchange rate *trend* appreciation.<sup>2</sup> Greater fundamentals-driven appreciation of the real exchange rate, in its turn, would imply a lower level for the neutral rate. Under such a scenario, a lower neutral rate would suggest that the monetary policy stance has been tighter than initially assumed, especially since 2024. Moreover, a stronger level for potential output growth would indicate that the economy has been operating with a slightly negative output gap during this period, which could partly help explain the low inflationary environment observed in Armenia during 2023-2024. Given these assumptions, this scenario assumes that the policy rate would need to follow a lower path relative to market expectations in order to prevent a restrictive policy stance and stymie deflationary risks in this "new" economic reality.

<sup>2</sup> See, for example, Lee and Tang (2003).

**Figure 3.F.2:**

**Panel A: IT & Financial Services exports as share of GDP**



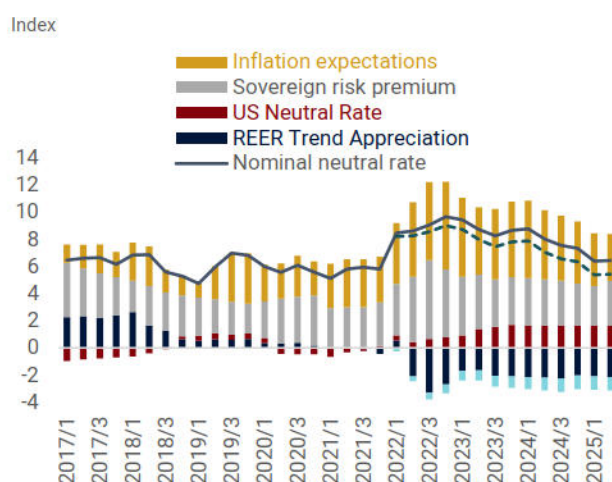
Source: Statistical Committee of the Republic of Armenia, CBA

**Panel B: Manufacturing exports and real effective exchange rate**



Source: Statistical Committee of the Republic of Armenia, CBA

**Panel C: Nominal neutral rate (hypothetical example)**



Source: Statistical Committee of the Republic of Armenia, CBA

## Summary of Illustrative Case A & Case B Macroeconomic Projections

Figure 3.F.3: Endogenous Interest Rate Path, %

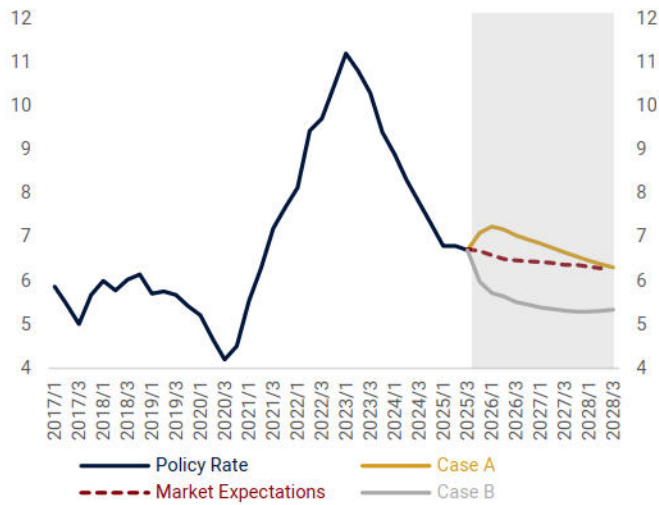


Figure 3.F.6: Non-Traded Sticky Price Inflation, Y-o-Y %

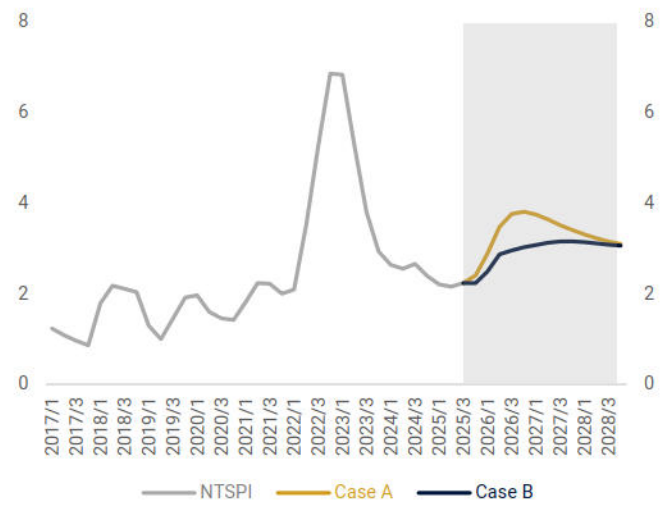


Figure 3.F.4: Real GDP Growth, Y-o-Y %

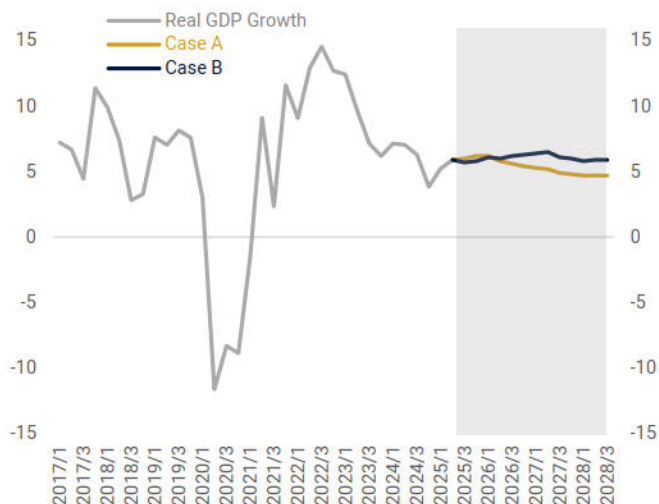


Figure 3.F.7: Output Gap, %

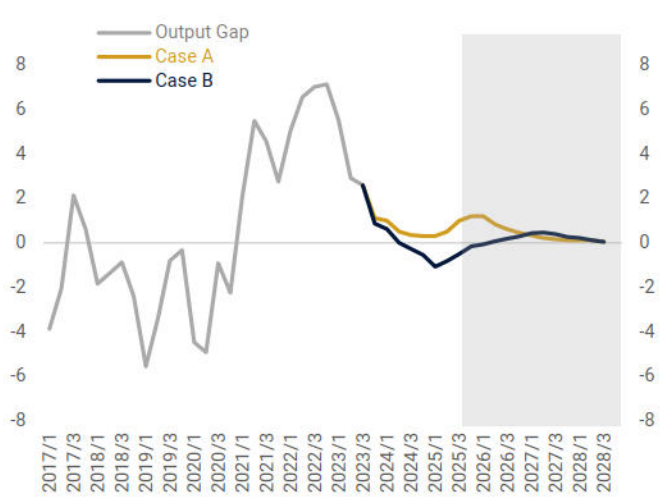


Figure 3.F.5: Headline CPI Inflation, Y-o-Y %

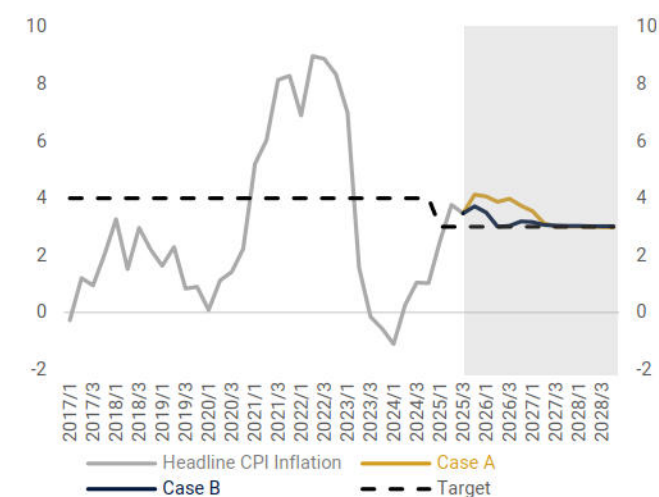


Figure 3.F.8: Real Interest Rate, %

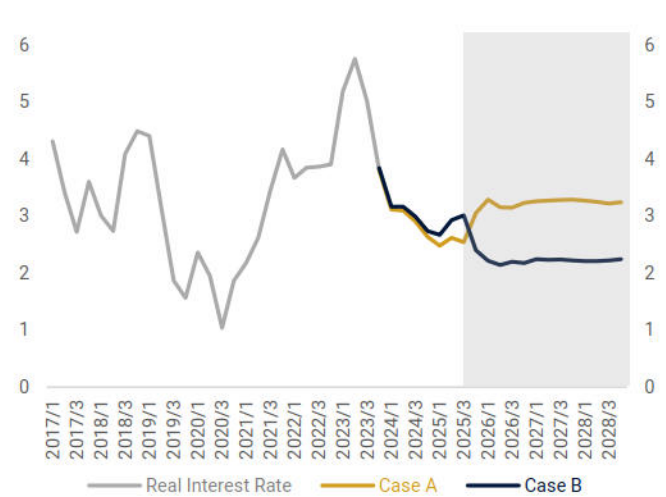


**Figure 3.F.9: Nominal Effective Exchange Rate, Index**

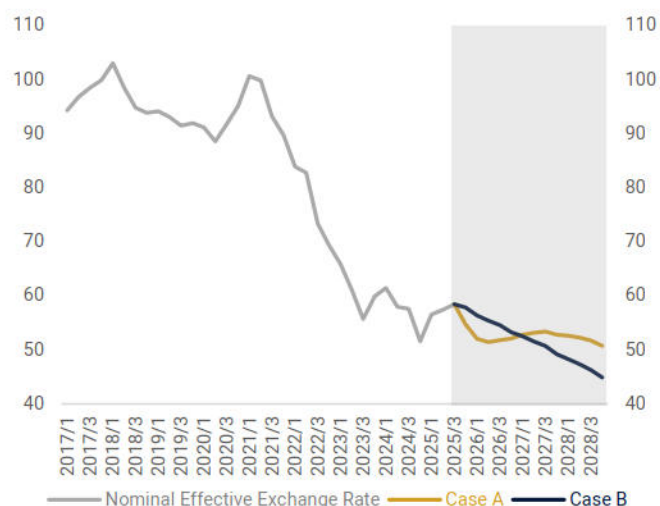


**Figure 3.F.11: Model-Based 1-Year Ahead Inflation Expectations, Y-o-Y %**

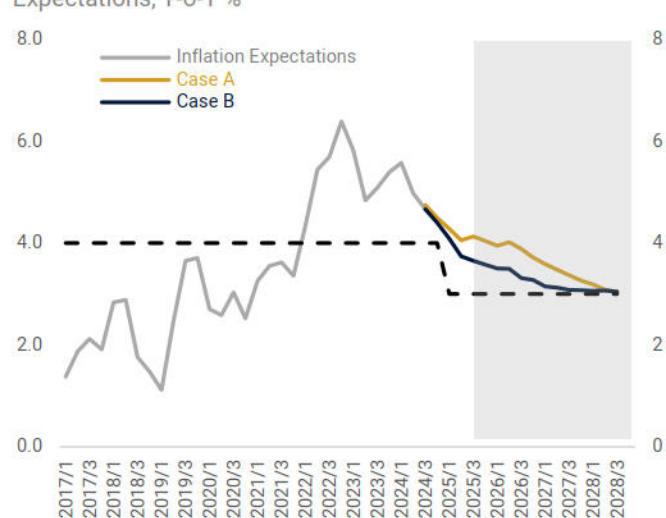


**Figure 3.F.10: Real Effective Exchange Rate, Index**

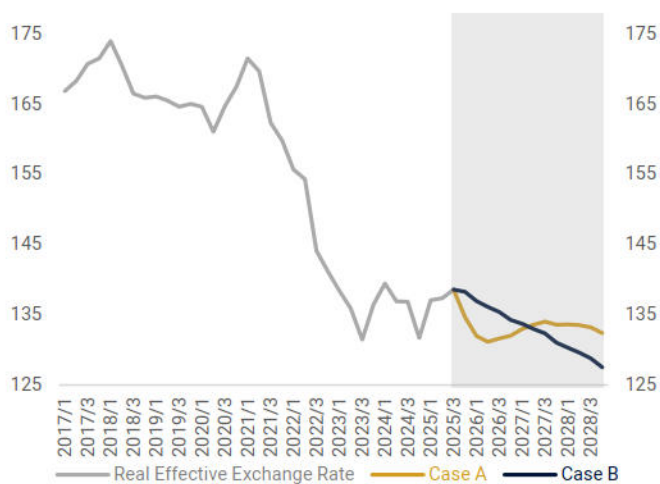


**Table 3.F.1: Summary of Illustrative Macroeconomic Projections**  
Historical Data and Illustrative Case A & B Scenario Projections

|                                   |                | 2023   | 2024    | 2025    |          | 2026    |          | 2027    |         | 2028    |         |
|-----------------------------------|----------------|--------|---------|---------|----------|---------|----------|---------|---------|---------|---------|
|                                   |                | Actual | Actual  | Case A  | Case B   | Case A  | Case B   | Case A  | Case B  | Case A  | Case B  |
| <b>Global Economy</b>             |                |        |         |         |          |         |          |         |         |         |         |
| USA economic growth               | real growth, % | 2.9    | 2.8     | 1.6     | 1.6      | 1.5     | 1.5      | 1.8     | 1.8     | 1.7     | 1.7     |
| Eurozone economic growth          | real growth, % | 0.4    | 0.9     | 1.2     | 1.2      | 1.1     | 1.1      | 1.4     | 1.4     | 1.2     | 1.2     |
| Russia economic growth            | real growth, % | 4.1    | 4.3     | 1.1     | 1.1      | 1.5     | 1.5      | 1.9     | 1.9     | 2.0     | 2.0     |
| USA inflation                     | average, %     | 4.1    | 3.0     | 2.8     | 2.8      | 2.8     | 2.8      | 2.3     | 2.3     | 2.0     | 2.0     |
| EU inflation                      | average, %     | 5.5    | 2.4     | 2.0     | 2.0      | 1.9     | 1.9      | 2.0     | 2.0     | 2.0     | 2.0     |
| Russia inflation                  | average, %     | 6.0    | 8.4     | 8.7     | 8.7      | 6.3     | 6.3      | 4.6     | 4.6     | 4.0     | 4.0     |
| Oil price                         | dollar/barrel  | 82.6   | 80.5    | 68.9    | 68.9     | 62.3    | 62.3     | 58.9    | 58.9    | 56.3    | 56.3    |
| Copper price                      | dollar/mt      | 8490.0 | 9142.1  | 9491.2  | 9491.2   | 9747.6  | 9747.6   | 10020.2 | 10020.2 | 10140.6 | 10140.6 |
| FAO food price index              | index          | 124.5  | 122.0   | 129     | 129      | 134.1   | 134.1    | 137.9   | 137.9   | 141.5   | 141.5   |
| <b>Domestic Economy</b>           |                |        |         |         |          |         |          |         |         |         |         |
| <b>Inflation</b>                  |                |        |         |         |          |         |          |         |         |         |         |
| Inflation                         | Y-o-Y, %, EOP  | -0.6   | 1.5     | 4.1     | 3.7      | 3.7     | 3.2      | 3.0     | 3.0     | 3.0     | 3.0     |
| CPI inflation                     | Y-o-Y, %, avg. | 2.0    | 0.3     | 3.5     | 3.4      | 3.9     | 3.2      | 3.2     | 3.1     | 3.0     | 3.0     |
| Non-traded sticky price inflation | Y-o-Y, %, avg. | 4.8    | 2.6     | 2.2     | 2.2      | 3.5     | 2.8      | 3.6     | 3.1     | 3.0     | 3.0     |
| <b>Gross Income</b>               |                |        |         |         |          |         |          |         |         |         |         |
| GDP                               | billion dram   | 9492.5 | 10193.4 | 11162.1 | 11140.75 | 12258.5 | 12210.08 | 13283.3 | 13381.7 | 14352.2 | 14596.3 |
| GDP                               | real growth, % | 8.3    | 5.9     | 5.8     | 5.7      | 5.7     | 6.2      | 5.0     | 6.3     | 4.9     | 5.9     |

Table continued on the following page.

## Historical Data and Illustrative Case A &amp; B Scenario Projections (continued from previous page)

|                                            |                 | 2023    | 2024    | 2025    |         | 2026    |         | 2027    |         | 2028    |         |
|--------------------------------------------|-----------------|---------|---------|---------|---------|---------|---------|---------|---------|---------|---------|
|                                            |                 | Actual  | Actual  | Case A  | Case B  | Case A  | Case B  | Case A  | Case B  | Case A  | Case B  |
| <b>Demand</b>                              |                 |         |         |         |         |         |         |         |         |         |         |
| <b>Consumption</b>                         | real growth, %  | 9.0     | 1.6     | 6.4     | 6.0     | 5.4     | 5.6     | 4.7     | 5.1     | 4.7     | 4.9     |
| Public consumption                         | real growth, %  | 28.3    | -22.3   | 9.6     | 9.6     | 4.1     | 4.1     | 1.1     | 1.1     | 2.5     | 2.5     |
| Private consumption                        | real growth, %  | 5.6     | 6.8     | 5.8     | 5.4     | 5.6     | 5.8     | 5.3     | 5.7     | 5.1     | 5.3     |
| <b>Gross accum. of fixed assets*</b>       | real growth, %  | 10.1    | 11.1    | 11.8    | 14.7    | 5.7     | 6.1     | 6.9     | 7.3     | 7.4     | 7.4     |
| Public investment**                        | real growth, %  | 27      | 1.5     | 21.9    | 21.9    | -1.1    | -1.1    | 4.4     | 4.4     | 6.1     | 6.1     |
| Gross accumulation of private fixed assets | real growth, %  | 3.6     | 15.2    | 7.5     | 11.7    | 8.8     | 9.5     | 7.9     | 8.5     | 7.9     | 7.9     |
| <b>Export of goods and services</b>        | real growth, %  | 30.7    | 35.6    | -30.4   | -36.8   | 2.7     | 4.4     | 3.6     | 4.0     | 3.2     | 3.8     |
| <b>Import of goods and services</b>        | real growth, %  | 30.2    | 31.4    | -32.1   | -32.7   | 3.1     | 3.4     | 4.3     | 4.7     | 4.2     | 5.3     |
| <b>Current Account</b>                     |                 |         |         |         |         |         |         |         |         |         |         |
| Balance of trade                           | million USD     | -1859.2 | -2340.6 | -2759.9 | -2675.4 | -3196.9 | -3119.7 | -3414.6 | -3087.4 | -3576.4 | -3307.8 |
| Balance of services                        | million USD     | 1711    | 2167.9  | 1565.8  | 1565.8  | 1831.8  | 1831.8  | 1879.2  | 1941.8  | 1926.3  | 2058.3  |
| Money transfers                            | million USD     | 1538.3  | 988.5   | 900.1   | 900.1   | 986.5   | 986.5   | 1033.8  | 1033.8  | 1083.4  | 1083.4  |
| Current account                            | million USD     | 151     | -476.7  | -1285.2 | -1200.7 | -1369.8 | -1292.6 | -1502.8 | -1113.0 | -1572.8 | -1172.2 |
| Balance of trade                           | share of GDP, % | -0.8    | -0.7    | -9.6    | -9.4    | -10.5   | -10.3   | -11.2   | -9.4    | -11.1   | -9.1    |
| Balance of services                        | share of GDP, % | 8.7     | 8.8     | 5.5     | 5.5     | 6.0     | 6.1     | 6.2     | 5.9     | 6.0     | 5.7     |
| Money transfers                            | share of GDP, % | 7.9     | 4       | 3.1     | 3.2     | 3.3     | 3.3     | 3.4     | 3.2     | 3.4     | 3       |
| Current account                            | share of GDP, % | 0.8     | -1.9    | -4.5    | -4.2    | -4.5    | -4.3    | -4.9    | -3.4    | -4.9    | -3.2    |
| <b>Public sector***</b>                    |                 |         |         |         |         |         |         |         |         |         |         |
| Revenues and grants                        | billion dram    | 2046    | 2358.6  | 2773.2  | 2773.2  | 3049.3  | 3049.3  | 3308.4  | 3308.4  | 3603.2  | 3603.2  |
| Tax revenue                                | billion dram    | 1926    | 2221.9  | 2655.9  | 2655.9  | 2934.9  | 2934.9  | 3206.1  | 3206.1  | 3503.3  | 3503.3  |
| Expenditures                               | billion dram    | 2243.5  | 2550.2  | 3376.9  | 3376.9  | 3584.7  | 3584.7  | 3755.4  | 3755.4  | 3994.5  | 3994.5  |
| Deficit                                    | billion dram    | -197.5  | -191.6  | -603.7  | -603.7  | -535.4  | -535.4  | -447    | -447    | -391.3  | -391.3  |
| Revenues and grants                        | share of GDP, % | 24.1    | 24.8    | 24.8    | 24.9    | 24.9    | 25.0    | 24.9    | 24.7    | 23.1    | 22.7    |
| Tax revenue                                | share of GDP, % | 22.7    | 23.4    | 23.8    | 23.8    | 23.9    | 24.0    | 24.1    | 24.0    | 22.3    | 22.0    |
| Expenditures                               | share of GDP, % | 26.4    | 26.8    | 30.3    | 30.3    | 29.2    | 29.4    | 28.3    | 28.1    | 26.2    | 25.7    |
| Deficit                                    | share of GDP, % | -2.3    | -2      | -5.4    | -5.4    | -4.4    | -4.4    | -3.4    | -3.3    | -3.1    | -3.1    |

\* The Central Bank only presents the indicator of gross fixed asset accumulation instead of gross accumulation, since the change in tangible working capital

