



Central Bank
of Armenia

2025 Q2

**Executive
Monetary
Policy
Statement**

Published June 17, 2025

A. Executive Monetary Policy Statement

The Board of the CBA decided today to keep the Refinancing Rate unchanged at 6.75%.

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%.

In the second quarter of 2025, 12-month headline inflation accelerated, reaching 4.3% in May. Meanwhile, 12-month core inflation edged up slightly, standing at 2.8%

In the second quarter of 2025, risks associated with a further slowdown in global demand and in Armenia's key partner economies increased, while inflationary pressures intensified in the US. Uncertainty surrounding US economic policies—particularly trade policy and its macroeconomic implications—remains elevated. On the other hand, heightened tensions in international trade relations, along with the sharp escalation of geopolitical conflicts—particularly in the Middle East—have significantly increased the risks of potential disruptions to supply and value chains. Significant uncertainty persists regarding the medium-term implications of US fiscal policy—particularly the magnitude of aggregate demand stimulus, the consequent increase in public debt, and the potential upward pressure on long-term interest rates. In this context, given still-tight labor market conditions in partner countries and persistently elevated inflation environment, it is likely that central banks in major economies will either maintain or ease tight monetary conditions at a gradual pace.

In the second quarter of 2025, economic activity in Armenia moderated, primarily due to the gradual fading of certain short-term, non-structural growth drivers. The continued strong growth in the construction and services sectors has remained a key driver of overall economic activity. At the same time, uncertainty remains elevated regarding the sustainability of this growth, its long-term trajectory, and the future path of domestic demand—largely reflecting the structural nature of the ongoing expansion. External demand for services has continued to decline. The impact of aggregate demand on inflation is assessed to be neutral, while the recent acceleration in inflation is largely driven by certain supply-side factors. In this context, labor market conditions are showing signs of cooling, as evidenced by the gradual stabilization of wage growth, sticky price inflation in non-tradable sectors, and inflation expectations. Simultaneously fiscal policy poses primarily inflationary risks over the medium term.

In the context of current macroeconomic developments, financial market participants in Armenia broadly anticipate that the Central Bank of Armenia will gradually lower the refinancing rate over the coming year, aiming to reach a level of 6.25 percent.

Amid the elevated risks and heightened uncertainty, the Board has assessed multiple scenarios, consistent with its mandate to ensure price stability. On the one hand, the Board considered scenarios (Case A) — including those related to geopolitical developments and fiscal policy dynamics in the US and Armenia — that could lead to an increase in Armenia's neutral interest rate. These scenarios would require a higher path for the policy rate relative to market expectations to ensure the price stability. On the other hand, scenarios (Case B) that involve risks related to a continued normalization of external demand, which could lead to an uneven slowdown across certain sectors of the economy and further weakening of aggregate demand. This requires a monetary policy trajectory characterized by a more rapid and pronounced reduction in interest rates relative to market expectations, with the objective of moderating demand and anchoring inflation near the target over the medium term.

Consequently, emphasizing the build-up of Case A-type risks and underscoring the imperative to manage their macroeconomic implications, the Board of the Central Bank of Armenia decided to keep the refinancing rate unchanged for the current period. 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
June 17, 2025

Governor

Martin Galstyan

Deputy Governors

Armen Nurbekyan

Hovhannes Khachatryan

Board Members

Hasmik Ghahramanyan

Davit Nahapetyan

Artak Manukyan

Narek Ghazaryan

B. Summary of Economic Conditions

Global Economy

In the second quarter of 2025, global economic growth prospects have deteriorated. In the United States, the strong economic growth observed in recent quarters, fueled by an expansion in domestic private consumption, began to slow early in the year due to rising uncertainty surrounding economic policy. Nevertheless, following a moderate contraction in the first quarter of 2025, the U.S. economy is expected to rebound in the second quarter, almost fully offsetting the weak growth observed in the previous period. However, uncertainty remains elevated both regarding the current state of the economy and, more notably, its future outlook. Despite these developments, some major economies—most notably the Eurozone and China—experienced a slight acceleration in growth, likely driven by a short-term increase in orders from the US. However, structural challenges within these economies persist.

Uncertainty surrounding the outlook for US economic policies—particularly trade and fiscal policy outlook—remains elevated. In recent months, this uncertainty has contributed to increased volatility in financial markets and has triggered price corrections across various asset classes, including long-term government bonds. Given the current highly expansionary fiscal stance and expectations of its continuation, significant risks have emerged regarding a potential rise in long-term interest rates. Such developments could impact not only the future course of the Federal Reserve's monetary policy but also influence the neutral interest rate and capital flows to emerging markets.

In recent quarters, there has been significant progress toward easing inflationary pressures in the United States. Nevertheless, several core inflation indicators—such as sticky-price inflation and wage growth—remain significantly above target levels. Concurrently, the trade and fiscal policies implemented by the new U.S. administration pose notable risks of fostering a more inflationary environment, potentially complicating the Federal Reserve's trade-off between maintaining price stability and achieving full employment. The extent and nature of any potential inflationary acceleration will largely depend on domestic demand conditions. The current restrictive migration policy is also a tangible factor that may pose challenges for monetary authorities in sustainably returning inflation to target while reinforcing their commitment to long-term price stability.

In June 2025, the European Central Bank reduced its policy rate by an additional 25 basis points, bringing it down to 2.15%. Headline inflation continues to decline, driven by falling prices of industrial goods, while services inflation—despite some moderation—remains elevated, reflecting polarization across different sectors of the economy. Structural challenges in the Eurozone and China, along with the risk of prolonged

weak domestic demand, remain a key sources of uncertainty in the global economic outlook. On the other hand, the implementation of planned programs aimed at expanding defense and infrastructure capacities in the Eurozone could serve as a significant stimulus for the overall economy, particularly by revitalizing certain productive sectors.

Volatility in the international oil market has increased significantly. Amid slowing global demand and a deteriorating outlook, oil prices have gradually declined in recent months. These trends have been accompanied by both actual and anticipated increases in supply. On the other hand, the sharp escalation of tensions in the Middle East has contributed to a significant recent increase in oil prices. While rising geopolitical risks may further dampen global demand, they also pose substantial risks of disruptions to supply chains. In this context, the primary uncertainty revolves around the duration and scale of the conflict.

Economic activity in Russia has significantly weakened, signaling a gradual adjustment from an overheated economic state. Nevertheless, the primary driving forces remain the expansionary fiscal policy and the growth in private consumption. The labor market continues to exhibit significant tightness. On the other hand, optimistic expectations regarding a resolution to the Russia-Ukraine conflict have led to a significant appreciation of the ruble, which has also contributed to a moderation of inflationary pressures. In this context, in June 2025, the Bank of Russia lowered its policy rate by 1 percentage point, signaling the beginning of a monetary easing cycle. Nevertheless, signals of a sustained decline in inflationary pressures remain weak, and managing the persistently strong domestic demand environment continues to pose a challenge.

Domestic Demand Conditions

In recent quarters, economic activity in Armenia continued to weaken, largely due to the gradual fading of certain short-term, non-structural growth factors, stabilizing around its estimated long-term sustainable level. Nonetheless, the services and construction sectors remained the primary drivers of economic expansion. Sectoral concentration—particularly within specific service industries—has moderated to some extent, though it remains elevated. Encouraging signs also emerged from the manufacturing sector, especially in select sub-sectors that recorded strong growth in output, exports, and production capacity. The current structure of growth continues to generate considerable uncertainty regarding the balance between aggregate demand and aggregate supply. However, it can be noted that the extent of these imbalances has markedly declined in recent quarters.

Since 2022, Armenia has experienced a gradual, natural slowdown in external demand, particularly evident in declining tourism flows. Uncertainties persist regarding seasonal

migration trends to Russia and the channels through which remittances are transferred. On the one hand, if the ruble maintains its current value or strengthens further—particularly with a potential resolution of the Russia-Ukraine conflict—this could increase incentives for migration from Armenia to Russia. However, uncertainties surrounding the outlook and tightening migration policies may act as limiting factors, potentially curbing the growth of migration flows, thereby supporting an increase in labor supply within Armenia and contributing to the easing of inflationary pressures.

Uncertainty continues to surround domestic demand conditions. Strong growth in imports, consumer loans, inbound tourism, and services points to robust domestic demand. However, the persistence of somewhat concentrated economic growth, coupled with its slowing pace, along with the stabilization of core inflation measures below the target, raises concerns about a relatively weak demand environment.

There is considerable uncertainty regarding the impact of fiscal policy on aggregate demand, primarily due to the risk of underperforming tax revenues in 2025, despite the current strong performance of tax collections. Additionally, concerns persist about the potential increase in current expenditures required to fund social support programs. In this context, a higher public debt trajectory may also raise concerns about debt sustainability, contributing to an increase in the country's risk premiums. On the other hand, there are notable risks associated with underperforming capital expenditures and the structural characteristics of these expenditures, which could exert a restrictive effect on demand.

Labor Market & Inflation

The decline and stabilization of the unemployment rate at around 13%, along with steady wage growth in the private sector (ranging from 5–6%), may indicate more balanced labor market conditions.

Nevertheless, surveys on labor market conditions and the actual increase in registered formal sector employment continue to send mixed signals regarding labor market developments. The household survey-based unemployment rate in Q4 2024 stood at 12.9%, closely aligning with the figure from the same quarter of the previous year. A decline in employment was also observed, with a year-on-year decrease of approximately 22 thousand. On one hand, the increase in the unemployment rate compared to 2022-23 may reflect weakening demand conditions and adjustments within the economy. This aligns with a noticeable outflow of foreign workers and a slowdown in wage growth rates during 2024. On the other hand, data from the State Revenue Committee indicate that the total number of registered employees increased by approximately 36.8 thousand over the year. This, along with the still robust wage growth in certain sectors of the economy, may indicate the presence of potentially tighter conditions in the labor market. Alternatively, this growth in registered employees could signal a gradual, structural decline in the shadow labor market in favor of formal employment.

In recent months, wage growth in the private sector has stabilized, although it remains slightly below the level consistent with productivity growth and the inflation target. 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 uncertainty in this context relates to the high degree of uncertainty surrounding Russia's economic growth prospects, the flow of Armenian labor migrants to Russia, domestic labor market participation, and the integration of economically inactive populations into the workforce.

Under these conditions, the 12-month inflation accelerated to 4.3% during January-May 2025, primarily driven by a significantly higher seasonal increase in food prices compared to historical levels for the corresponding months. However, this reflects a significant price increase concentrated in a limited number of goods and does not represent a broad-based inflationary trend. It is worth noting that of the approximately 0.3% month-on-month inflation recorded in May, about 0.1 percentage points were attributable to seasonal food products, particularly potatoes (0.3 percentage points).

Deflationary pressures transmitted from the external sector on non-food goods persist. Simultaneously, amid ongoing adjustments in external demand, prices for certain services have either continued to decline or increased significantly below the overall inflation rate. Nevertheless, the Non-Traded Sticky Price Inflation, which captures domestically driven demand dynamics, has stabilized within the 2–3% range. In this context, inflation expectations have continued to steadily decline, approaching the target level, supported by a prolonged low-inflation environment.

Monetary Policy

Market expectations of the CBA policy rate path have remained unchanged since the latest decisions, and continue to reflect a gradual reduction in the policy rate to 6.25% over the next eight decisions. Considering the above, along with minimal changes in expectations regarding economic fundamentals, the yield curve has remained largely unchanged following the previous decision and communication.

In recent months, Armenia's sovereign risk premium has remained below the long-term stable level determined by the country's fundamentals. However, it is important to note that upward risks to the country's risk premium have increased lately. This reflects uncertainties surrounding Armenia's fiscal policy—particularly debt sustainability—as well as geopolitical risks, including border tensions and regional developments. In this context, a potential upward adjustment of the country risk premium poses 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. At the same time, Armenia's macroeconomic stability and strong economic growth provide certain positive factors for a possible reassessment of the country's risk premium and a potential reduction in the neutral rate.

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 outlined in the Monetary Policy Report, which necessitates a policy rate path higher than market expectations, is grounded in the assumption that a significantly more expansionary fiscal stance may emerge in the United States as a result of a potential weakening in fiscal discipline. Under this scenario, rising concerns over public debt and its sustainability could exert upward pressure on neutral interest rates globally, including in emerging markets such as Armenia, thereby necessitating a higher trajectory for the policy rate.

The illustrative Case B scenario outlined in the Monetary Policy Report, which assumes a lower policy interest rate path compared to market expectations, is grounded in the

assumption that, in recent years, the high debt burden in Armenia's private sector, particularly in certain segments, combined with the continued and gradual adjustment in external demand may lead to a more "cost-sensitive" environment. Specifically, although the aforementioned trend of a natural deceleration in growth within these sectors is expected, the accumulated debt, along with the potential further adjustment in incomes, poses risks of a disproportionate decline in investment, employment, and the consumption of intermediate goods and services in those areas.

In the context of the latent risks and uncertainties in the current period, the CBA builds and discusses various scenarios, summarized in the Taxonomy of Scenarios, with the aim of managing possible risks and assessing sources of uncertainty. At the same time, the MPR includes a deeper dive into two illustrative scenarios, 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 include all possible risks and uncertainties.

