



Central Bank
of Armenia

Monetary Policy **Accountability** **Report**

Monetary Policy Program
Implementation Report, 2025

Published 31 March 2026

Message from the Board of the Central Bank

The Board of the Central Bank of Armenia (CBA) is pleased to present the Monetary Policy Accountability Report for 2025, part of our continuous commitment to enhancing and strengthening the Central Bank's transparency and accountability in matters of monetary policy. This report is the first in a series of accountability reports, to be published annually in the first quarter of each year.

The Board of the Central Bank of Armenia, in our Statement of Long-Run Monetary Policy Objectives, emphasizes the importance of clear and effective communications, transparency, and accountability as a key priority for the CBA as an independent, public-sector institution. This report is an important part of our commitment to the public to ensure that our policy decisions are clearly understood and effective. It also encourages us to continuously strive to improve the quality of our analysis, communications, and decisions. Together, these values constitute an important foundation of our commitment to achieving price stability, which we understand as a means to support the broader goal of improving the welfare of our nation.

The report is intended to describe the CBA's approach to maintaining price stability in 2025. It provides a concise overview of economic developments, followed by an exposition of each of the eight monetary policy decisions made in the year. This includes a comprehensive discussion of the different scenarios policymakers considered when making their decision and their assessment of policy trade-offs in the context of our "least regrets" decision-making model. Building on our commitment to individual Board member accountability, the report considers how each Board member's thinking around policy-relevant issues evolved over the year. Finally, given our commitment to ensuring the policy framework and decisions are accessible and easily understood for the public, the report responds to commonly asked questions about monetary policy in 2025.

Additionally, this report conforms to the requirements proscribed in the Law on the Central Bank of Armenia, which stipulates that the CBA prepare and publish a report in the first quarter of each year, outlining the implementation of monetary policy over at least the preceding twelve month period.

This report was compiled by the staff of the Central Bank of Armenia's Monetary Policy Department, with guidance and insights from members of the CBA Board. Because monetary policy decisions impact the economy with lags, this annual report constitutes an *ex-ante* assessment of policy that seeks to understand how and why policymakers arrived at their decisions in real time, without the benefit of hindsight.

The Board fully endorses the findings of this report, particularly its focus on the challenges faced amidst economic uncertainty and the strategic steps taken to mitigate risks.

The Board of the Central Bank of Armenia remains committed to upholding and strengthening our priorities of high transparency and accountability. We look forward to the dialogue and feedback that this report will generate.

Governor

Martin Galstyan

Deputy Governors

Hovhannes Khachatryan

Armen Nurbekyan

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Report Structure

Accountability report begins with a summary of global and domestic economic developments in Armenia. As in the Monetary Report, the focus of the summary is to elucidate the two ingredients essential for economic analysis: where was the economy, and what were the underlying forces driving the economy, in the context of key risks and uncertainties.

Section II presents an overview of the conduct of monetary policy in 2025, focusing on how the CBA managed risks through a framework of “least regrets.” The section begins with an annual taxonomy covering the different types of scenarios that policymakers considered throughout the year, reflecting a summary of the universe of major issues the Board and Staff of the CBA, as well as external stakeholders, were concerned about. The section then proceeds to assess how the Board arrived at and communicated their policy rate decisions, what trade-offs they managed, and how Board members’ concerns regarding key risks, uncertainties, and trade-offs evolved over the year.

Section III presents the assessment of how financial markets reacted to policy rate decisions and communications. Section IV provides comprehensive assessment on monetary policy outcomes. Section V provides responses to common questions on the conduct of monetary policy in 2025, drawing upon frequent questions or comments raised by members of the media, academia, financial markets, and the general public over the course of the year. The purpose of this section is to better clarify the objectives, purpose, and conduct of monetary policy; address potential misconceptions; and explain important topics relevant to understanding monetary policy conduct.

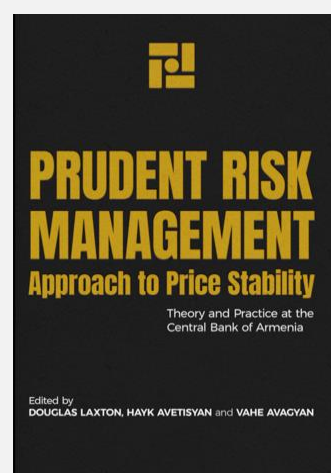
Disclaimer

The information presented in this report is based on actual data, 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.

In line with the CBA’s Accountability Framework, the Monetary Policy Accountability Report is published on an annual basis, at the end of the first quarter of each year. The MPAR 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 prior year.

As a succinct document covering economic developments and the conduct of policy in the preceding calendar year, the MPAR avoids excessive detail about specific economic developments. The reader is referred to the quarterly Monetary Policy Reports, and the Executive Monetary Policy Statements that accompany each decision, for greater detail on economic developments in each quarter, which are published on the CBA website.

All Monetary Policy Accountability Reports which have been published to date are available on the CBA’s website (www.cba.am), which also contains quarterly Monetary Policy Reports, all press releases, working papers, and other monetary policy-related publications.



The Board of the Central Bank of Armenia is pleased to announce the forthcoming publication of the book “Prudent Risk Management Approach to Price Stability,” which lays out the theoretical and practical underpinnings of the innovative monetary policymaking framework developed by the CBA. Geopolitical tensions, economic fragmentation, fiscal unsustainability, and climate risk have become defining features of a new economic reality characterized by high and persistent uncertainty. Rising uncertainties and risks represent a new reality and a profound challenge for central banks, one that demands a fundamental rethinking of the prevailing approach to monetary policy design and communications. The Prudent Risk Management Approach to monetary policy effectively incorporates, communicates, and addresses these challenges. Under this framework, the monetary policy decision-making process is guided by the construction and consideration of multiple scenarios for the development of the Armenian economy. These scenarios (two or more) imply a path for the policy rate that is either above or below current market expectations. They embody concrete and actionable monetary policy directions, rather than describing abstract or implausible risks. The framework has given rise to the development and implementation of the highest global standards for monetary policy communications and transparency.



Central Bank
of Armenia

01 |

Economic
Developments
and Context

A. Global Economic Environment

United States Economy

In the post-pandemic period, the stronger-than-expected recovery of demand conditions was accompanied by a broadening of inflationary pressures. Amid a delayed monetary policy response to early inflationary pressures, inflation in the US ticked up to levels not seen in decades. By late 2024, following significant interest rate hikes, inflation moderated markedly but still remained above target. At the same time, while there were emerging signs of easing in labor market conditions, high debt levels as well as questions about the strength of the real economy left the economy entering 2025 with elevated uncertainty and accumulating vulnerabilities.

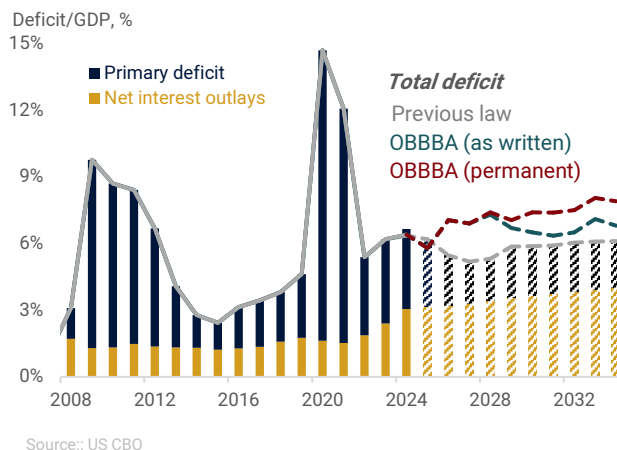
Economic growth in the United States in 2025 was marked by pronounced volatility and uncertainty. Growth slowed in early 2025 amid heightened trade policy uncertainty and a surge in imports ahead of anticipated tariff increases. Over the course of the year, consumption—increasingly concentrated among high-income households and supported by elevated financial asset prices—as well as AI-related investment activity remained the primary drivers of growth. Nevertheless, underlying demand conditions showed uneven signs of weakening, reflected in rising household credit delinquencies, and a notable deterioration in labor market indicators. The structure of growth, coupled with rising income inequality, raised uncertainty regarding the sustainability of the expansion. Moreover, the risk of a correction in potentially overvalued asset markets (given elevated P/E ratios) emerged as a key downside risk to both domestic consumption and demand conditions as well as global demand.

While headline inflation moderated early in the year, sticky prices remained persistently above target, raising concerns about elevated inflation expectations. As the year progressed, inflation re-accelerated, driven in part by the gradual pass-through of tariffs into consumer prices as well as elevated domestic demand conditions. Labor market developments were mixed: although payroll and wage growth weakened substantially, unemployment remained stable, while tighter labor supply conditions linked to restrictive migration policies posed potential medium-term inflationary risks.

Monetary policy was confronted with increasingly difficult trade-offs amid heightened uncertainty. The Fed faced “last mile” challenges in returning inflation sustainably to target while avoiding an undesirable sharp weakening in demand. At the same time, the prospect of a more expansionary fiscal stance, widening fiscal deficits, and rising public debt intensified risks of higher long-term interest rates and a higher neutral rate, with implications for U.S. debt sustainability, global capital flows, and emerging market financial conditions.

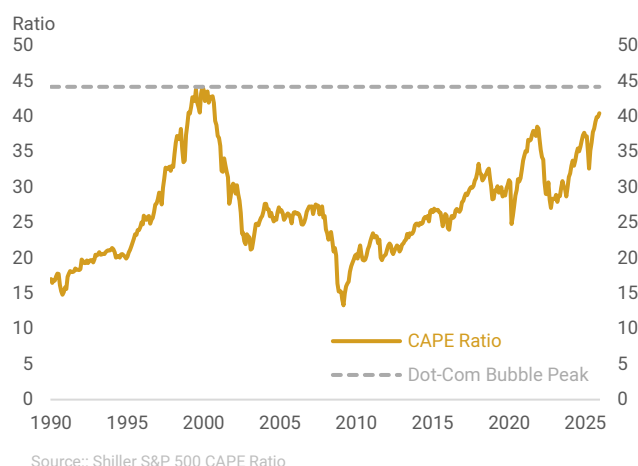
Expansionary fiscal policy threatens meaningful increases in deficit and higher public debt trajectory

Figure 1.A.1. US deficit projections



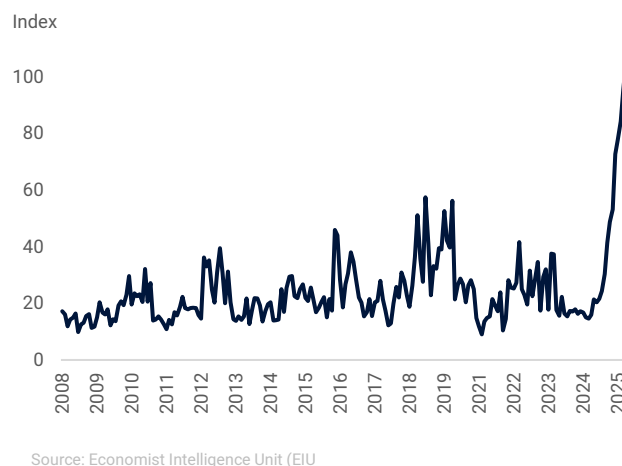
Possible overvaluation in financial asset prices adds uncertainty to medium-term consumption and growth outlook

Figure 1.A.2. Cyclically adjusted price to earning ratio



Uncertainty surrounding US trade policy and its macroeconomic implications remains elevated

Figure 1.A.3. Global Uncertainty Index



Eurozone Economy

In recent years, structural challenges, including competitiveness concerns, energy-related constraints, as well as sectoral and geographical imbalances, have heightened uncertainty surrounding the economic outlook. In 2025, these factors continued to weigh on economic activity, while geopolitical tensions and uncertainty related to economic policies generated additional pressures on investment activity, business sentiment, and growth prospects. Throughout 2025, the services sector remained the primary driver of growth, whereas structural headwinds continued to constrain activity in the manufacturing sector. The temporary acceleration in growth at the beginning of the year largely reflected short-term factors, notably a sharp increase in exports to the United States amid expectations of higher tariffs. Nevertheless, persistent structural challenges and the conclusion of an asymmetric trade agreement with the United States had negative impacts on business and investment activity over 2025.

Following surging post-pandemic inflation in 2022 and 2023, headline inflation softened by 2024 and largely stabilized around target levels in 2025. However, declining inflation was primarily driven by low or negative goods (particularly imported goods) inflation, while services inflation continued to remain well above target. The latter could reflect relatively strong domestic demand as well as tight labor market conditions, with unemployment remaining at historically low levels even as wage growth showed signs of moderating towards year-end. In this context, the ECB continued to gradually reduce the key policy rate in H1 but held rates steady at 2.15% beginning in July, highlighting its challenge in balancing sluggish and uneven growth with tight labor market conditions and high underlying inflation.

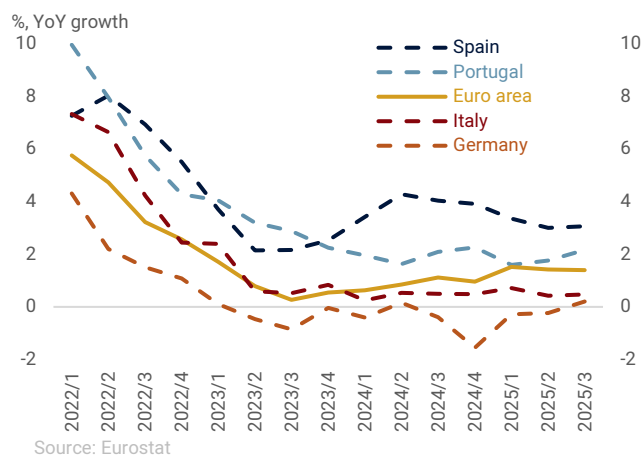
Russian Economy

The Russian economy, which had remained remarkably resilient in the post-2022 period, slowed considerably in 2025. Industrial activity remained in positive territory, largely driven by expanding defense spending. However, demand conditions deteriorated in 2025, reflected in weak services and retail trade activity. Meanwhile, slowing household lending and rising non-performing corporate loans reflected risks of a weak demand environment taking hold. Amid low global oil prices (compounded by targeted sanctions on Lukoil and Rosneft in late 2025) and slowing economic activity, fiscal revenues weakened considerable. Meanwhile, the planned tightening of tax rates (including VAT) to offset weak oil and gas revenues in 2026 pose risks to the growth outlook and overall consumer sentiment.

Amid sustained excess demand conditions in the economy post-2022, inflation and inflation expectations remained persistently elevated. However, weakening demand and tight monetary policy contributed to softening inflationary pressures in H2, with CPI declining to 5.6% Y-o-Y in December, compared to 10.3% in March. At the same time, labor market conditions remained tight amid labor shortages, which could be worsened by tightening migration policies, potentially generating sustained inflationary pressures. In this context, the CBR faced a challenging dilemma of managing weakening demand on the one hand and persistent labor market conditions and elevated inflation expectations on the other, cautiously lowering interest rates by 500 bps throughout 2025 but nonetheless maintaining a tight monetary stance.

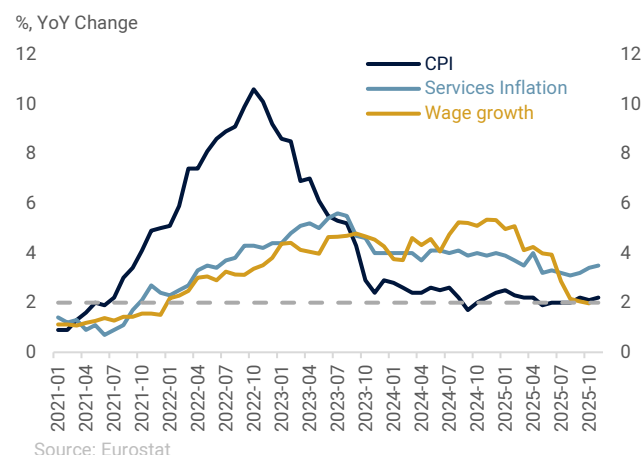
Southern European economies (e.g. Spain) have emerged as the main driver of Eurozone growth, while the outlook for traditional, leading economies like Germany continues to worsen, particularly in the industrial sector

Figure 1.A.4. Real GDP Growth, Euro Area



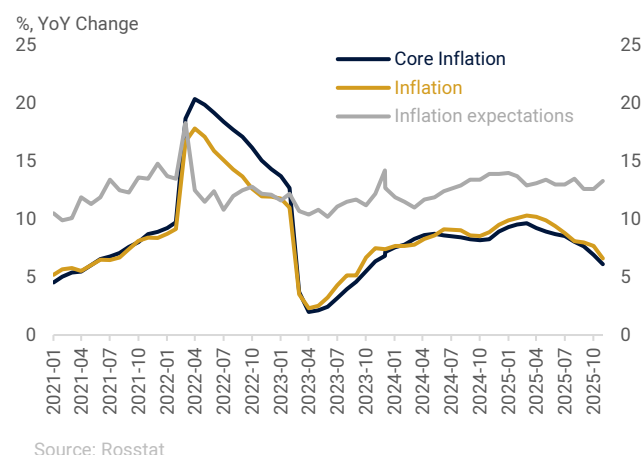
Inflationary pressures from the labor market have persisted even as wage growth has slowed since the end of the year.

Figure 1.A.5. Underlying Inflation Measures, EU Area



High inflation expectations and tight labor market conditions have significantly complicated the task of returning inflation durably to the target

Figure 1.A.6. Inflation Indicators in Russia



Commodity Markets

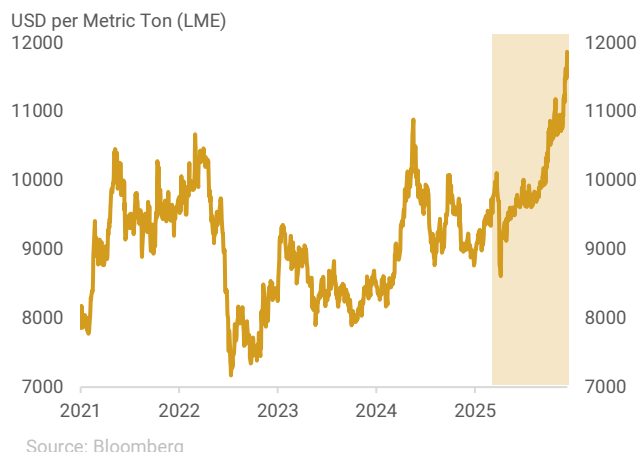
Copper: Copper prices increased sharply throughout 2025, particularly in the second half of the year, settling over \$12,500 per metric ton by year-end. This strong growth reflects both short-term and fundamental factors. This includes on the one hand significant uncertainty about US tariff policy (leading to surging imports and inventory stockpiling) as well as disruptions in several large global copper mines; and, on the other hand, growing global demand linked to the green energy transition, AI, data centers, and increased infrastructure and defense spending that continued to drive current and expected demand for copper. The outlook for copper prices continued to be weighed down by risks of oversupply conditions forming once short-term tariff-related and/or speculative factors fade.

Oil: Oil prices exhibited considerable volatility throughout 2025 but generally exhibited a downward trend, with Brent crude oil prices declining from a peak of \$84 per barrel in mid-January to a low of \$60 in mid-December. Weak oil prices continued to be impacted primarily by global production outpacing consumption. Production cuts by OPEC+ countries were not enough to offset this imbalance, while strategic stockpiling in China cushioned the extent of downward price movements. At the same time, geopolitical tensions added meaningful volatility to oil price movements, with oil prices temporarily surging midyear amid a sharp uptick in geopolitical tensions in the Middle East, but nonetheless continuing to decline throughout the rest of the year as these tensions eased.

Food: Following a dramatic surge in global food prices in 2022 amid supply disruptions related to the pandemic and Russia-Ukraine conflict, global food prices declined considerably in 2023. However, beginning in Q2 2024 and continuing through Q3 2025, food prices began to rise again, driven by adverse weather conditions and supply disruptions, particularly in cereals, dairy, and vegetable oils. Despite this uptick, food prices in general still remained well below the levels seen in 2022. Beginning in September, many of these supply-side factors, including adverse weather conditions, reversed, supporting sustained declines in global food prices through year-end. At the same time, geopolitical and climate risks continue to present upside risk for potentially higher and/or more volatile global food prices, including for food imports into Armenia.

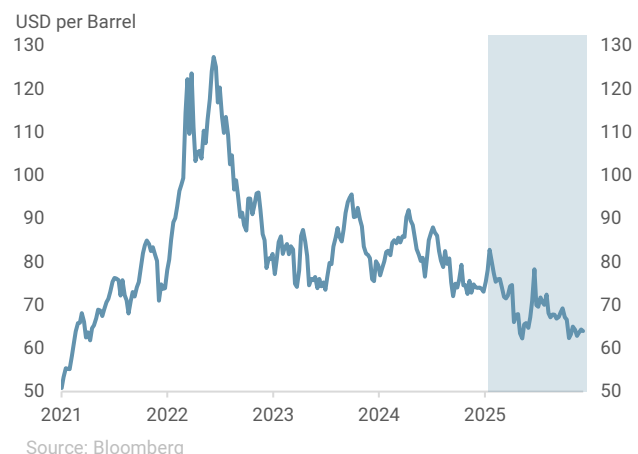
The continued growth in global demand for copper has been a source of upward pressure on prices

Figure 1.A.7. Copper Prices



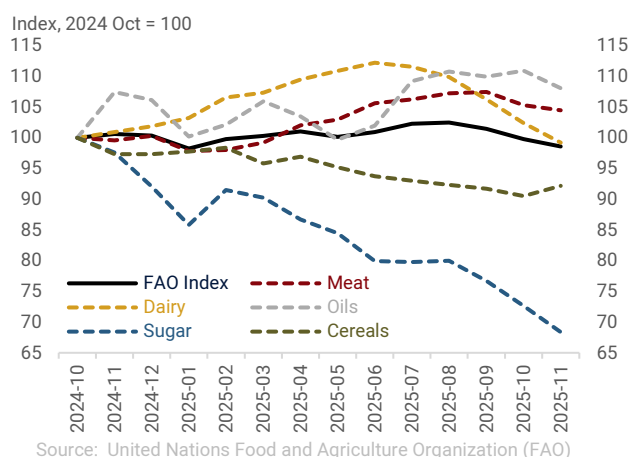
Global oil supply has continued to exceed demand, exerting downward pressure on prices

Figure 1.A.8. Brent Crude Oil Prices



Supply-side factors have been a source of upward pressure in global food price developments

Figure 1.A.9. Food Price Index of the Food and Agriculture Organization (FAO)



B. Domestic Economic Environment

Aggregate Demand Conditions

Following robust growth in 2022–23, economic growth in Armenia gradually slowed over 2024, reaching 3.7% in the fourth quarter. The services and construction sectors continued to be the main drivers of growth. Nevertheless, the structural characteristics of growth and its uneven nature created uncertainty regarding its long-term sustainability and the strength of aggregate demand conditions in the economy. Global geopolitical uncertainties, a gradual weakening of external demand, and sector-specific challenges (particularly in IT) additionally remained major sources of uncertainty throughout the year.

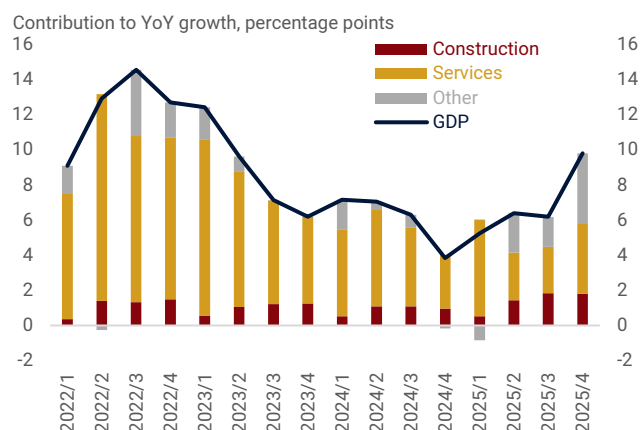
During 2025, economic growth accelerated, reaching 9.8% Y-o-Y in the fourth quarter and 7.2% annually. Growth remained concentrated in a limited number of sectors, giving rise to uncertainties regarding the interpretation of the strength of domestic demand conditions on the one hand and the medium-term growth outlook on the other. In 2025, the construction sector grew at a rapid pace, exceeding the already elevated levels recorded in previous years. At the same time, the potential for a gradual adjustment in real estate prices posed risks of threatening growth in adjacent sectors, contributing to weakening demand conditions, and posing deflationary pressures. Strong growth in the services sector was largely driven by expansion in financial and IT services; however, throughout the year, statistical issues created some uncertainty in interpreting the data. At the same time, growth for other services that are sensitive to domestic demand conditions accelerated, possibly pointing to an expansion in aggregate demand conditions. Following a slowdown in the beginning of the year, growth in the industrial sector accelerated sharply from the second half of 2025, largely in response to the reemergence of short-term, non-structural factors. Meanwhile, “traditional” industrial subsectors continued to expand at a high rate.

Private consumption, after remaining subdued relative to economic growth in previous years, showed signs of acceleration from the beginning of the year, supported by continued strong credit growth for both households and the private sector. At the same time, investment activity in the economy also picked up, driven by growth in both private (real estate) and public (infrastructure) investments. Nevertheless, uncertainty regarding the strength of domestic demand conditions and its outlook persisted throughout the year. This uncertainty reflected, on the one hand, the potential for spending of accumulated savings and accelerating lending activity, and on the other, relatively muted retail trade activity. Meanwhile, remittances in recent years have come to play an increasingly smaller role in driving domestic demand. Although remittances accelerated since the beginning of the year, their volume remains at low levels compared to historical trends.

External demand, which had weakened somewhat in the beginning of the year, rebounded to high levels in 2025. After a record-setting increase in 2023, tourist flows to Armenia slowed considerably in 2024 and through Q1 2025, reflecting slowing flows from Russia and declining per capita tourist expenditures. However, beginning in Q2 2025, tourist flows to Armenia sharply increased, driven partly by structural changes in source markets, including growing tourism from non-traditional markets. Additionally, although external trade flows had slowed in the beginning of the year, throughout the year external demand for domestic goods and particularly services proved to be strong. In this context, both IT and financial services exports remained at high levels (comprising 7.0% of GDP in Q3 2025).

Structural characteristics of growth posed uncertainty about its underlying strength and outlook

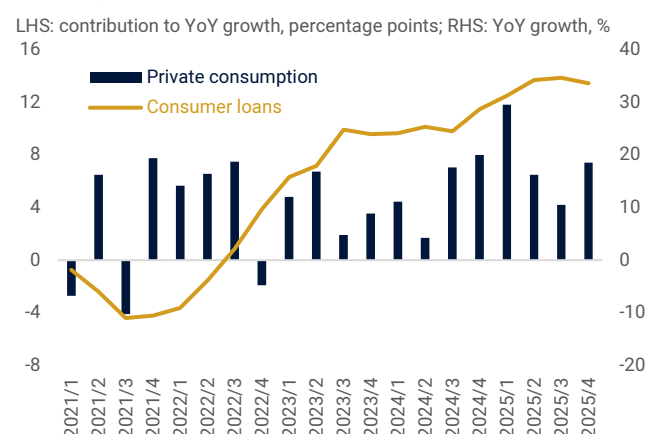
Figure 1.B.1. Real GDP Growth by Production Components



Source: Statistical Committee of the Republic of Armenia (SCRA)

Statistical questions raise uncertainty about the underlying strength of domestic demand conditions

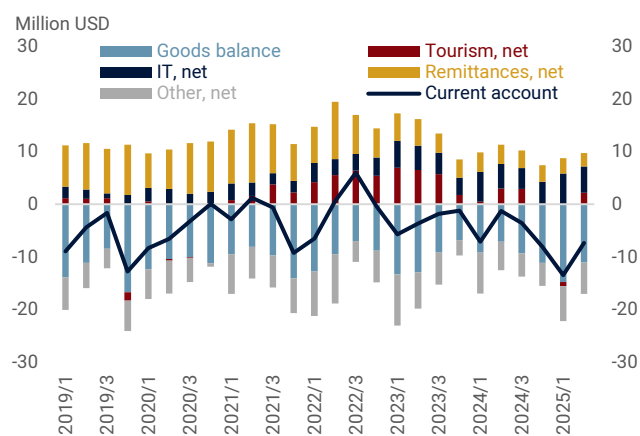
Figure 1.B.2. Private consumption and consumer lending activity



Source: SCRA, CBA

External demand for domestic goods and especially services remained elevated throughout 2025

Figure 1.B.3. Current account



Source: CBA

The external demand shock of 2022-23, experienced amid the Russia-Ukraine conflict, contributed to an expansion of aggregate demand conditions and expanding inflationary pressures. While excess demand conditions in 2022 primarily reflected the impacts of this external demand shock, they gradually subsided in 2023-24 as external demand pressures stabilized. Consequently, in the period that followed, uncertainty about domestic demand conditions and underlying potential output growth added an additional layer of complexity to assessing the output gap.

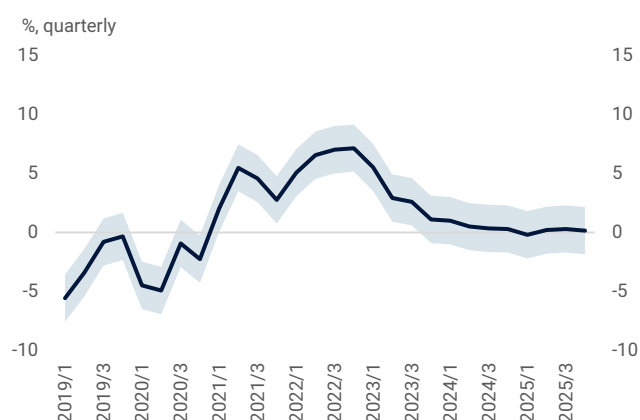
Over the course of 2025, various signals pointed to a primarily closed output gap. At the same time, however, the structural characteristics of growth and uneven developments across sectors added uncertainty to the assessment of the relative position of aggregate supply and demand. On the one hand, high lending growth and private consumption, as well as the concentration of growth in demand-driven sectors, posed upside uncertainty. On the other hand, the continued concentration of growth; stabilized labor market conditions, weakening imports of final consumption and capital goods; persistently low services and NTSPI inflation; as well as slowing retail trade activity posed downside uncertainty.

In interpreting and assessing the output gap, it is equally important to understand developments in potential output and the factors driving its long-term sustainable level. Productivity and productive capacities have grown considerably since 2022, as evidenced by the growing share of exportable goods and services exports in GDP, as well as strongly rising output per worker in sectors highly dependent on high-quality human capital and innovation (e.g. IT, financial services, and others). This, in turn, can imply a more productive economy in structural terms, contributing to some increase in the long-term sustainable level of potential output. At the same time, it is worth emphasizing that there exists considerable uncertainty about the *scale* of this impact, somewhat complicating efforts to estimate the long-term, sustainable level of potential output.

In this context, amid the external demand shock of 2022 and sustained capital inflows, recent years saw a meaningful appreciation of the real exchange rate. This, in turn, raised uncertainty about the sustainable, “trend” level of the real exchange rate. One interpretation supporting stronger trend appreciation is the argument that appreciation since 2022 has been primarily driven by the aforementioned growth in productivity, productive capacities, and a higher level of potential output. An alternative interpretation, however, places less emphasis on these fundamental factors and argues that appreciation has been instead primarily driven by short-term, cyclical factors.

The structural characteristics of growth have added to uncertainties surrounding the relative position of aggregate demand and supply in the economy

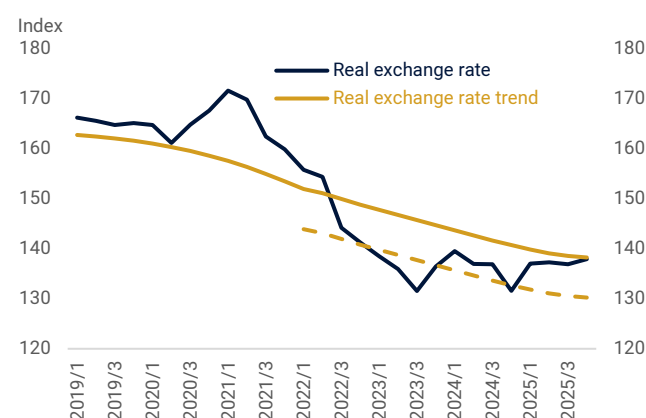
Figure 1.B.4. Output gap



Source: CBA

Significant uncertainty surrounding the equilibrium level of the real exchange rate persisted

Figure 1.B.5. Real effective exchange rate



Source: CBA

Fiscal Policy

In 2020–21, against the backdrop of the COVID-19 pandemic and geopolitical developments, the public debt burden increased moderately as a result of the stimulus measures implemented during that period. Nevertheless, against the backdrop of strong economic growth in 2022–23 and the implementation of a relatively more restrictive fiscal policy, the budget deficit declined significantly, and public debt also decreased, stabilizing in the 40–50% of GDP. In 2024, due to some underperformance of tax revenues and the need to meet ongoing social expenditures, fiscal policy had a mildly expansionary effect on aggregate demand conditions.

At the beginning of 2025, key uncertainties regarding fiscal policy were related to potential revenue underperformance and expenditure growth, which, compared with previous years, could have resulted in a stronger fiscal impact on aggregate demand and a widening of the budget deficit. By year-end, these risks had moderated significantly, reflecting strong revenue performance, under-execution of expenditures, and the planned fiscal consolidation in 2026. Over the course of 2025, fiscal policy was characterized by strong revenue performance, with improvements in tax administration contributing to a significant increase in budget revenues compared with the previous year, and even a slight overperformance relative to the plan. At the same time, the execution of current expenditures largely followed historical trends, while strong performance in capital spending contributed to a significant improvement in the expenditure structure. As a result, in 2025, fiscal policy had a somewhat restrictive effect on aggregate demand.

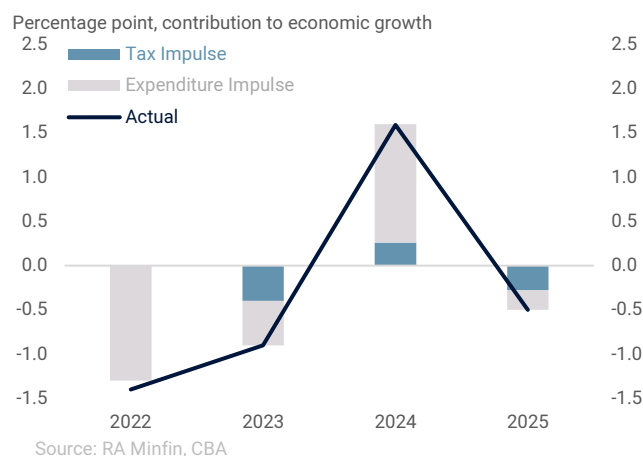
Labor Market Conditions

During 2022–23, amid strong demand and a positive output gap, labor market conditions tightened significantly, as reflected in declining unemployment and a sharp acceleration of wage growth, exerting some upward pressure on inflation. Since 2024, against the backdrop of stabilizing demand conditions and an increase in labor supply, labor market imbalances gradually eased.

Despite mixed signals from the labor market during 2025, labor market conditions showed a marked improvement toward gradual normalization. After seasonal increases in the first quarter, the unemployment rate declined, reaching 11.2% in the third quarter. Over the course of the year, uncertainty around employment growth estimates has led to differing interpretations of labor market conditions. Specifically, the number of formally registered employees grew at a steady pace during 2025, reflecting both the influence of certain structural factors and the persistence of strong labor demand. Nevertheless, according to labor force survey results, employment indicators have largely remained stable, which is not fully consistent with the strong economic growth and sustained wage increases observed in the economy. Over the course of the year, private sector nominal wage growth remained at relatively stable levels of 5.0%–7.0% Y-o-Y, while the concentration of growth declined markedly, which may suggest more balanced labor market conditions and a reduction in structural imbalances in the economy.

In 2025, fiscal policy exerted a moderately restrictive effect on aggregate demand

Figure 1.B.6. Impact of fiscal policy on aggregate demand



Over the course of the year, labor market imbalances have declined, pointing to an overall improvement in labor market conditions

Figure 1.B.7. Private sector nominal wage growth

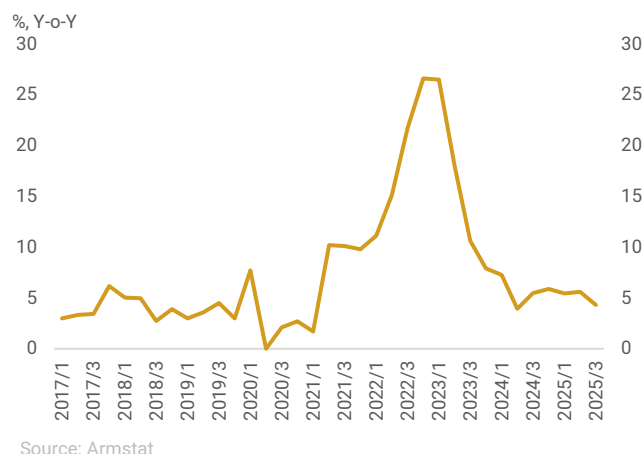
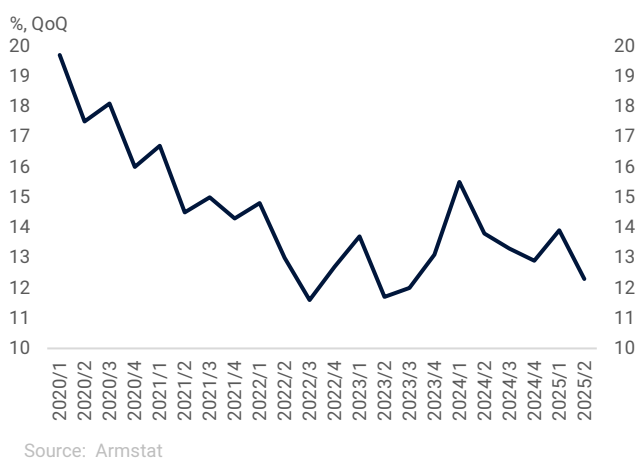


Figure 1.B.8. Unemployment rate



Inflation and Underling inflation

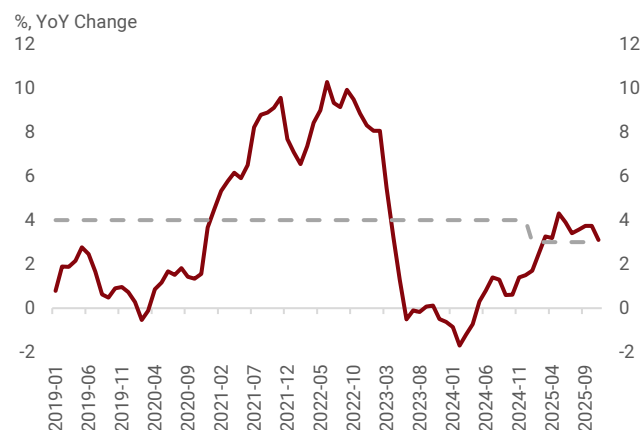
In the post-pandemic period, persistent global supply chain disruptions and supply constraints, together with the rapid recovery in domestic demand and economic activity, contributed to a significant broadening of the inflationary environment. Thanks to the early monetary policy response by the Central Bank of Armenia, inflation showed signs of moderation at the beginning of 2022. However, in the context of the Russia–Ukraine conflict, a positive external demand shock contributed to an expansion in aggregate demand conditions in Armenia’s economy and an acceleration of inflationary pressures. Against this backdrop, headline inflation in Armenia moderated significantly from early 2023, reflecting the cumulative effects of monetary policy tightening as well as an easing of inflationary pressures stemming from the global economy, in line with the normalization of global supply chains.

Since end-2024 and through 2025, global supply-side pressures have broadened and inflationary spillovers from the global economy have intensified, as also reflected in developments in the FAO Food Price Index. This contributed to an acceleration of imported inflation and a broadening of the inflationary environment. However, from the end of 2025, a gradual unwinding of the aforementioned supply-side factors was observed, with headline inflation stabilizing at 3.3% by year-end. In this context, the key uncertainties have related to the persistence of these trends and, against this backdrop, the speed and magnitude of domestic price adjustment. Since the beginning of the year, services inflation has shown signs of acceleration, largely driven by elevated price pressures in air transport. However, services inflation excluding air transport has remained below the target, hovering in the 2.0%–2.5%. The non-traded sticky price index, which captures demand-driven price dynamics, remained relatively stable in the range of 2.0%–2.5%. While these developments may suggest the absence of excess demand pressures in the economy over the course of the year, an acceleration of core inflation was observed in the final months of the year, which, although largely reflecting the influence of certain short-term factors, may nonetheless contain early signals of broadening demand pressures.

According to the Central Bank of Armenia’s household inflation expectations survey, elevated inflation expectations continued to decline over the course of 2025, while uncertainty remained high. At the same time, the share of respondents expecting low and stable price growth remained relatively unchanged. These developments reflect a gradual anchoring of inflation expectations around the target, supported in large part by the sustained low-inflation environment over the prior year. Furthermore, in January 2025 the Central Bank reduced the inflation target to 3%. In this context, the key uncertainties over the course of the year have related to the speed of adjustment of inflation expectations toward the new target (see Chapter 4).

The acceleration in inflation has been primarily driven by the growing impact of supply-side factors.

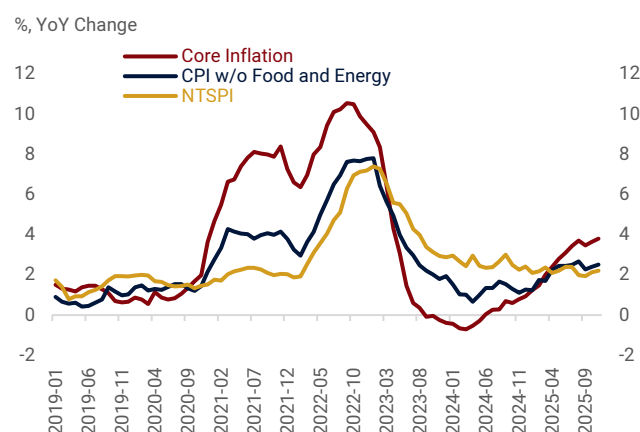
Figure 1.B.9. Inflation



Source: Armstat

The stabilization of NSTPI may indicate the absence of excess demand pressures in the economy.

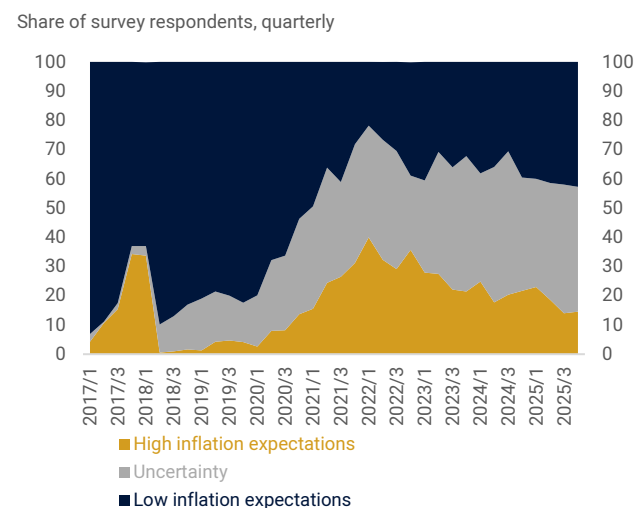
Figure 1.B.10. Underlying inflation measures



Source: Armstat, CBA

Elevated inflation expectations have declined, while heightened uncertainty has persisted.

Figure 1.B.11. Inflation expectations survey



Source: CBA

Financial Conditions

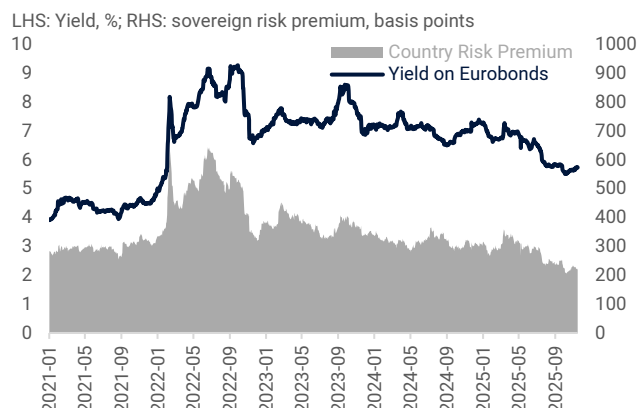
High uncertainty continued to surround the neutral interest rate and its individual components (global neutral rate, sovereign risk premium, inflation expectations, and real exchange rate appreciation) in 2025. Over the course of the year, questions about public debt sustainability in advanced economies, as well as the persistence of a high inflationary environment, posed upside pressure on **global neutral rates**. This, in turn, added a layer of uncertainty to assessing neutral rates in emerging market economies. Further, **Armenia's sovereign risk premium** declined throughout 2025, reflecting both global and country-specific factors. Issues stemming from fiscal and trade policies in advanced economies, coupled with long-term, structural reforms in emerging market economies, contributed to improving investor sentiment toward emerging market bonds. Amid this broad decline in emerging market risk premia, Armenia's sovereign risk premium declined as well. At the same time, although trends in Armenia's sovereign risk premium closely followed this broader trend in emerging market risk premia, several country-specific factors—especially expectations of a decline in geopolitical risk following August 8—additionally contributed to declines in Armenia's risk premium. Additionally, uncertainty has surrounded the pace and scale at which **inflation expectations** declined commensurate to the reduction of the new inflation target from 4% to 3% in January 2025. However, several factors—including persistently low and stable non-traded sticky price inflation, declines in long-term yields throughout the year, as well as CBA surveys of households and financial market participants—support the argument that inflation expectations have declined to the new target at a rather brisk pace. This, in turn, could support a lower level of the neutral rate (see Section 4). At the same time, stronger growth in exports and productive capacities relative to trading partners in recent years has supported **trend appreciation in the real exchange rate**, exerting further downward pressure on the neutral interest rate.

Lending volumes continued to grow at a rapid pace in 2025, reflecting high credit demand. Specifically, high consumer lending growth could point to relatively high domestic demand conditions. Further, although mortgage growth slowed somewhat, it nonetheless remains at elevated levels. This implies that demand for real estate (whether for residential or investment purposes) remains elevated in both Yerevan and in surrounding regions, even as some modest adjustments are taking place. Additionally, business lending activity has continued to grow at a high rate, which could in turn reflect a positive investment climate and improved business sentiment. Market interest rates have largely held constant throughout the year. However, several indicators (including credit availability, lending volumes, borrower composition, and changes in the credit maturity structure) could point to an overall easing in financial conditions in 2025.

Throughout 2025, the dram appreciated slightly versus the US dollar, driven by a confluence of several factors including growing capital inflows as well as depreciation of the dollar relative to currencies of both advanced and emerging market economies. At the same time, the ruble appreciated against the dram, primarily reflecting Russia's tight monetary policy, weakening demand environment and declining imports.

Armenia's sovereign risk premium declined in 2025

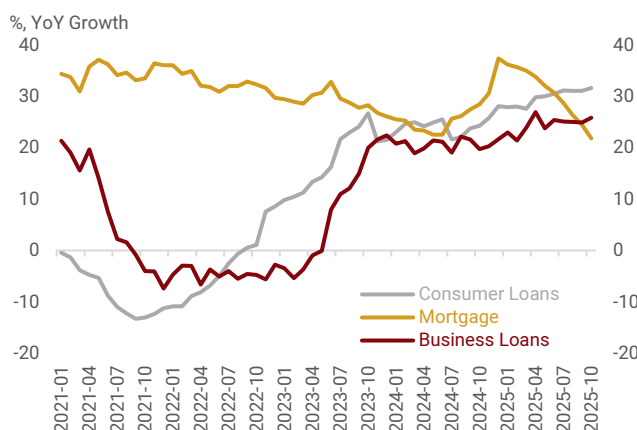
Figure 1.B.12. Republic of Armenia sovereign risk premium



Source: CBA

Credit demand has continued at an accelerating pace

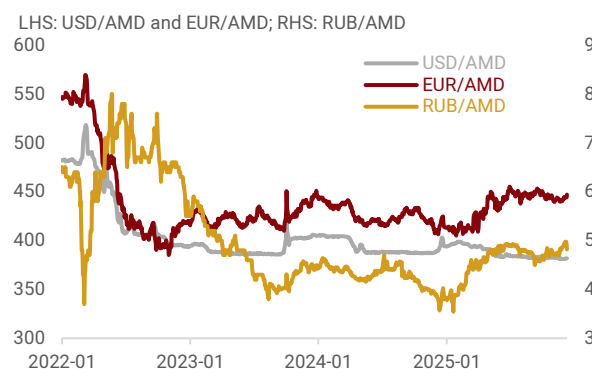
Figure 1.B.13. Change in volume of loans extended by commercial banks to households and legal entities



Source: CBA

The dram appreciated slightly against the US Dollar in 2025 but depreciated somewhat against the Ruble and Euro

Figure 1.B.14. Nominal exchange rate versus USD, Euro and Ruble



Source: CBA

C. Markets' View on Economic Outlook

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.

To determine market expectations, we 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. This section responds to the question of how market expectations of the macroeconomic outlook changed in response to changing economic conditions and central bank policy actions.

At the beginning of 2025, against the backdrop of gradual normalization of economic conditions in Armenia, as well as growing uncertainty stemming from global economic policies and risks of worsening in the global growth and demand outlook, financial market participants expected that economic activity would gradually normalize toward long-term sustainable levels—around 5%. Importantly, in markets' assessment, the normalization of growth toward long-term sustainable levels was expected to occur gradually and in an orderly manner, rather than through a sharp correction in the real economy. Against this macroeconomic backdrop, markets expected inflation to remain below target in the near term, gradually converging toward target levels over the medium-term horizon. In this context, market participants expected the CBA Board to continue gradually reducing the policy rate, converging over the medium-term horizon toward what they assessed to be the neutral rate—around 6.25%.

In the second quarter of 2025, external demand showed signs of moderation, reflected in slowing tourism and trade flows, declining per-tourist spending (for further details, see Chapter 1). These developments were accompanied by growing uncertainty surrounding global economic policies and a worsening outlook for global growth and demand, prompting market participants to revise their near-term growth projections somewhat downward. At the same time, from the second quarter of the year onward, inflation had shown some signs of acceleration, driven largely by a pickup in inflationary pressures transmitted from the global economy amid broadening supply-side factors. In Q2, market participants adjusted their near-term inflation expectations upward. Amid uncertainty stemming from global economic policies and some acceleration in inflation, markets expected the policy rate to continue to decline gradually, albeit at a somewhat slower pace relative to the previous survey.

However, in Q3 and Q4, tourist inflows accelerated sharply, exports continued to grow steadily, and uncertainty over the potential effects of tighter U.S. trade policy eased somewhat. In parallel, market participants revised up their short-term growth forecasts. In this context, they continued to expect growth to gradually stabilize around 5% over the medium term. At the same time, the supply-driven inflationary pressures observed in Q2 remained meaningful through the second half of the year. As a result, market participants revised their near-term inflation projections somewhat upward. Importantly, however, despite the upward shift in near-term inflation expectations, medium-term inflation expectations gradually converged toward the CBA's new inflation target. The remarkably rapid adjustment of inflation expectations toward the new target—fully reflected in Q3 expectations—serves as an important indicator of the effectiveness of the CBA's communications and its credibility (for further details, see Chapter 4). Against this backdrop, market participants continued to expect a gradual reduction in the policy rate, but at a slower pace than they had expected at the beginning of the year. In the first quarter survey, the policy rate was expected to stabilize at 6.25% in early 2026. By the fourth quarter survey, stabilization at 6.25% was expected only by the end of 2027.

This likely reflected the gradual influence of the factors noted above, especially the volatility of the global inflation environment driven by supply side factors, uncertainty stemming from global economic policies, and expectations of relatively strong economic activity and aggregate demand. Against this macroeconomic backdrop, market participants also continued to expect a mild depreciation of the nominal exchange rate during 2025. At the same time, with each successive quarter, they expected a lower, that is, more appreciated, fundamental level of the nominal exchange rate. These expectations regarding the medium-term level of the exchange rate reflect the view that, in the market's assessment, the appreciation of the exchange rate in recent years has been driven by fundamental factors and has not been solely the result of short-term cyclical factors. In particular, the substantial inflow of highly skilled labor and capital in 2022 made a significant contribution to strong and sustained growth in the productive capacities and competitiveness in tradable sectors, implying a fundamentals driven appreciation of the real exchange rate.

Figure 1.C.1. Market Reference Scenario

Y-o-Y, %

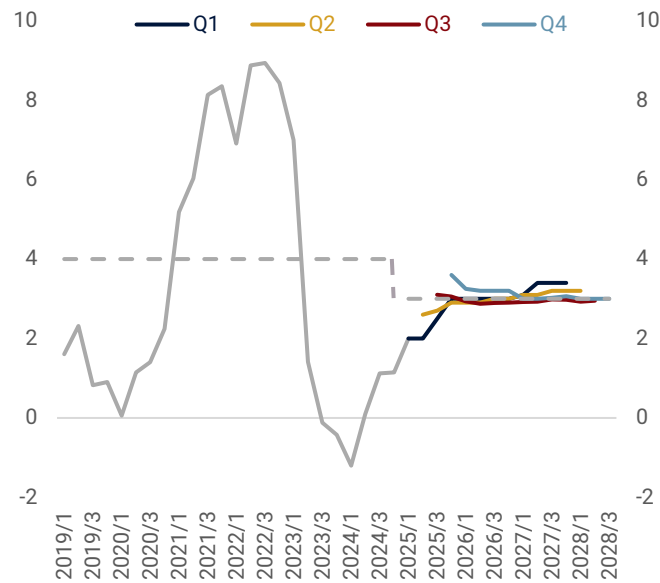


Figure 1.C.2. Market reference Scenario

Expected path of policy rate, %

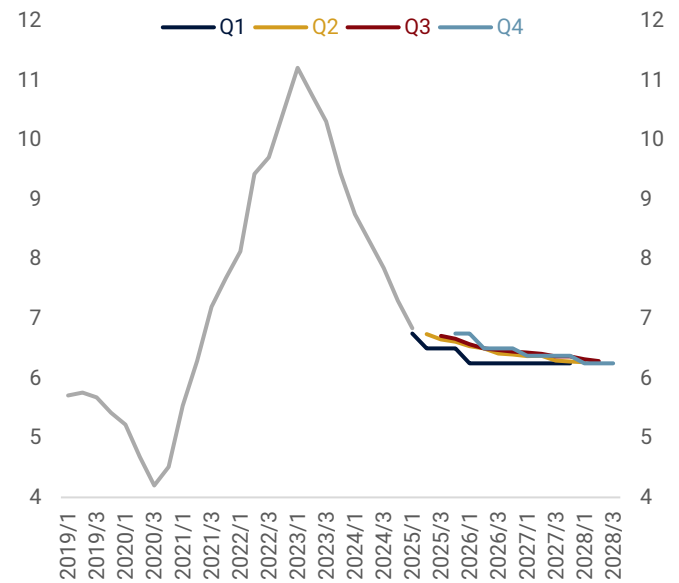


Figure 1.C.3. Market Reference Scenario

Real GDP Growth, %

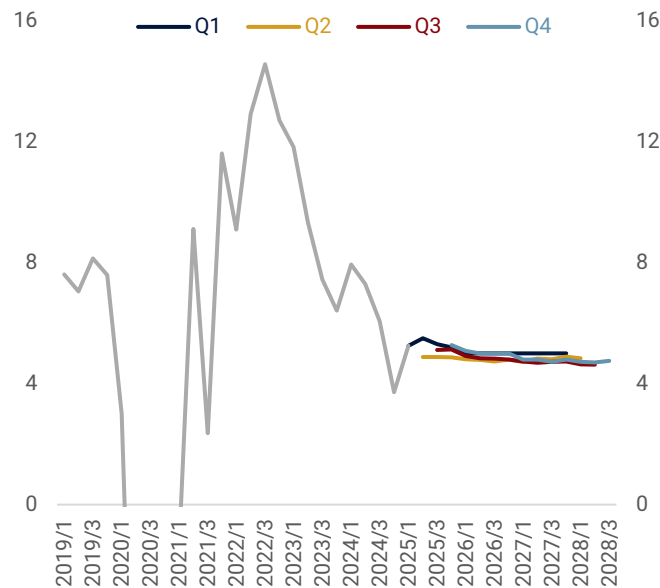
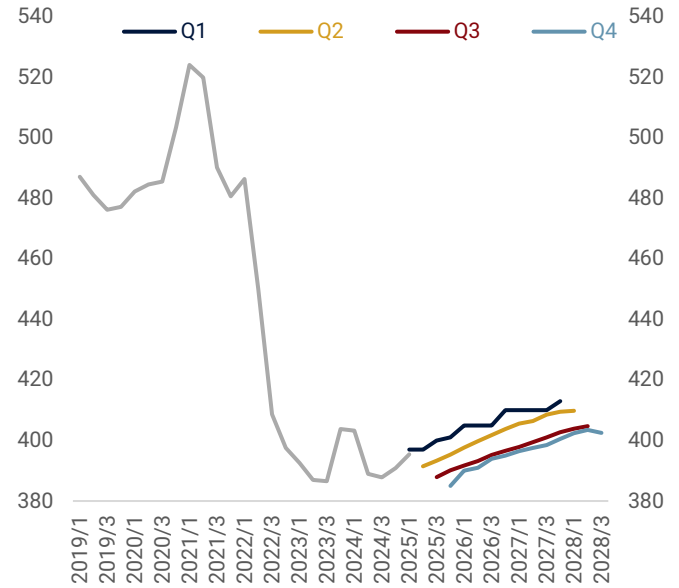


Figure 1.C.4. Market Reference Scenario

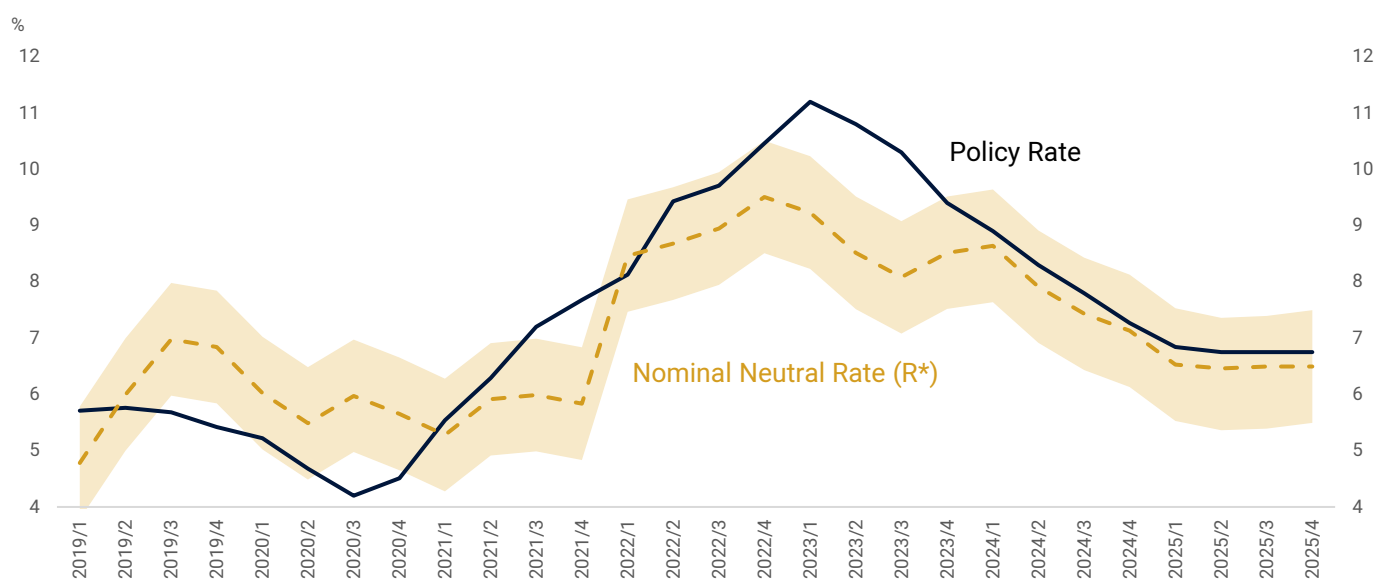
AMD-USD Nominal Exchange Rate



D. Monetary Policy

In response to the inflationary pressures stemming from the Covid-19 pandemic and the subsequent external demand shock, the CBA implemented a restrictive monetary policy stance beginning in December 2020, resulting in a gradual unwinding of supply and demand imbalances in the economy and a significant easing of the inflationary environment. It is worth noting that the CBA was among the very first central banks in the world to raise the policy rate at the end of 2020, in order to preempt an undesirable acceleration of inflation expectations and the potential buildup of excess demand conditions. In the context of these developments—taking into account, on the one hand, the significantly decelerating twelve-month inflation, and, on the other, the still-prevailing elevated demand and inflation expectations—the CBA kept the policy rate unchanged through the first half of 2023, up to June. Over the course of the above-described monetary policy tightening cycle, the CBA raised the policy rate by a cumulative total of 6.5 percentage points.

Figure 1.D.1: Policy rate and nominal neutral rate



Source: CBA

From June 2023 to the end of the year, amid the continued softening of the inflationary environment driven by deflationary pressures stemming from the global economy and an easing of inflationary pressures from the domestic labor market, the CBA gradually eased monetary conditions, lowering the policy rate by a cumulative 1.5 percentage points.

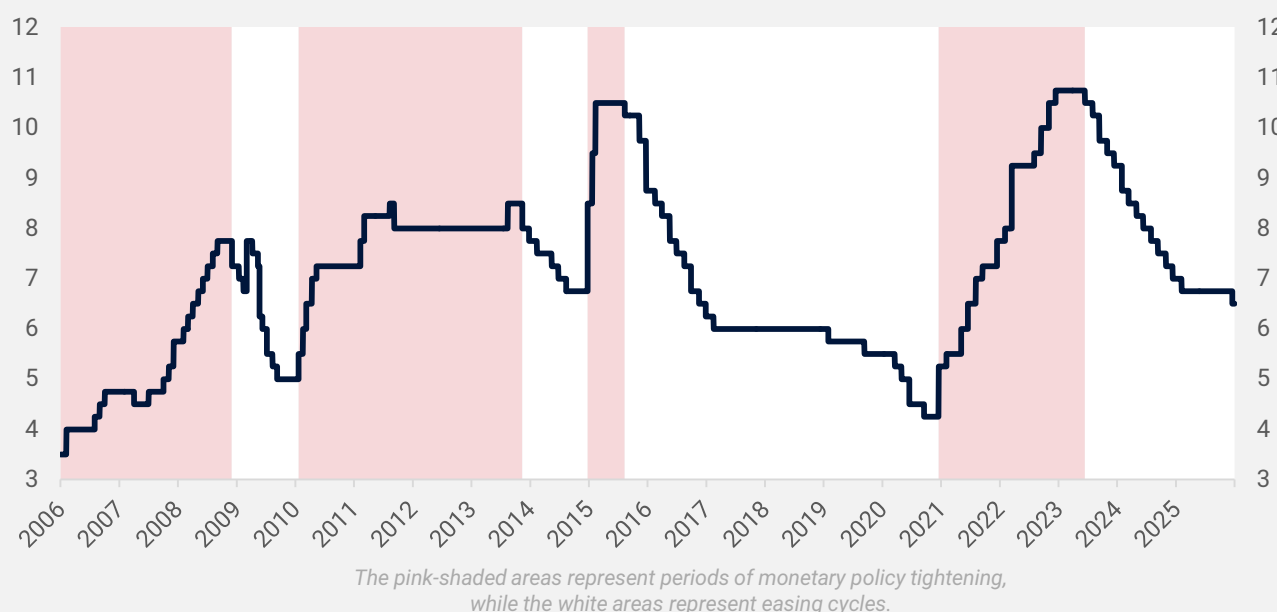
In 2024, the CBA continued to gradually reduce the policy rate by a cumulative 2.25 percentage points, setting it at 7.0% in December. Through the third quarter, balancing risks in both directions, the Board deemed a gradual easing of the policy stance in line with market expectations to be the most appropriate course of action, while in the fourth quarter—alongside the increased likelihood of Case B scenarios materializing—the Board emphasized the necessity of managing the material risks stemming from Case A scenarios. As a result, against the backdrop of the above-described developments and the monetary policy stance maintained during the reporting period and the period preceding it, twelve-month inflation increased by 2.1 percentage points over the course of 2024, standing at 1.5% at year-end, while twelve-month underlying inflation rose by 1.3 percentage points, closing the year at 0.9%.

In the interest of prudently managing the risks stemming from prevailing uncertainties, the CBA gradually eased monetary conditions at a measured pace over the course of 2025, by a cumulative 0.5 percentage points. Following the decision to reduce the policy rate by 0.25 percentage points in February, the policy rate remained unchanged through the March–November period. In December 2025, the Board reduced the policy rate by a further 0.25 percentage points (for a more detailed discussion, see Chapter 2). The broadly neutral position of demand conditions, alongside labor market conditions and the inflationary environment, indicated that the policy stance remained close to neutral throughout 2025.

Box 1: Economic Developments in Armenia and the Monetary Policy Response Since the Adoption of the Inflation Targeting Strategy

This box presents the economic developments in Armenia and the monetary policy response since the adoption of the inflation targeting strategy. Since the adoption of inflation targeting in 2006 and the gradual incorporation of FPAS Mark I, the CBA has dealt with a continuous succession of macroeconomic and geopolitical crises that required swift policy action. With a view to effectively managing the implications of future challenges amid continuously evolving economic realities, the CBA has made significant investments in the development of a monetary policy framework oriented toward prudent risk management. Amid rising uncertainties and multi-layered risks, the Central Bank's institutional reforms, including the introduction of the new monetary policy framework, further reinforce the Central Bank's institutional capacity to ensure price stability over the medium term.

Figure B.1.1. Central Bank of Armenia's Policy Rate Developments, %



2006-2009: Double Digit Growth

In the years preceding the Global Financial Crisis, the global economy was in an expansionary phase, which exerted inflationary pressures on international food and commodity prices. During this period, inflationary impulses emanating from global commodities were transmitted to the Armenian economy in the form of imported goods inflation. In parallel, significant capital inflows to emerging economies were generating currency appreciation pressures in the domestic economy and driving above-average growth in non-tradeable sectors, particularly construction. During 2006–2008, the Armenian economy recorded double-digit economic growth and substantial foreign capital inflows, accompanied by a significant appreciation of the dram. Throughout the second half of the 2000s, Armenia's real estate market experienced unprecedented growth, while the share of the construction sector in GDP was on the rise. Against the backdrop of inflationary pressures transmitting from the global economy, expanded aggregate demand conditions, significant capital flows, an appreciated exchange rate, and the newly introduced monetary policy strategy, the primary challenge for monetary policy was the stabilization of inflation expectations and their anchoring around the 4% target.

2009–2014: Global Financial Crisis, Sluggish Growth, and Elevated Risk Premium

The contraction in global demand brought about by the Global Financial Crisis had significant consequences for the Armenian economy. As in other emerging market economies, a significant reappraisal of the country risk premium in Armenia led to a sudden stop in capital flows and a contraction in aggregate demand. As a result, a double-digit economic contraction was recorded in 2009. In the years that followed, the accumulation of debt to sustain high levels of consumption and support economic growth – which was characterized by structural problems – allowed consumption to be maintained, but economic growth continued to remain subdued owing to the slow structural adjustment of the economy. Moreover, the accumulation of public and private debt to support economic growth resulted in rising debt levels, reflected in a persistently elevated country risk premium. In this situation, the CBA's monetary policy was aimed at balancing the two-sided risks stemming from uncertainties around the relative position of demand amid the structural adjustment of the economy.

2014-2020: Opportunistic Disinflation

The slow recovery marred by the European Debt Crisis and numerous supply shocks was followed by a new wave of challenges. In 2014, geopolitical conflicts in Crimea and the Donbas, along with the sharp decline in global oil prices, had adverse consequences for the Russian economy. The sharp depreciation of the Russian ruble spilled over to regional currencies, including the Armenian dram. Depreciation pressures on the national currency and the rise in the general price level in the economy led to a destabilization of inflation expectations. This, in turn, resulted in a sharp increase in demand for goods and foreign currency in the economy, further amplifying inflationary pressures and jeopardizing the credibility of the CBA. In this situation, the monetary policy response was immediate and sharp, with a substantial tightening of financial conditions, which helped to contain inflationary pressures and stabilize the financial system. Nonetheless, given the elevated level of uncertainty, risks of destabilization of the economy continued to persist. Despite the disinflation trend observed from 2015 onwards, risks of a destabilization of inflation expectations at elevated levels remained. As a result, beginning in 2015, the CBA adopted an opportunistic disinflation stance, which ensured a significant deceleration in inflation expectations. This played an important role in building and reinforcing public trust and credibility in monetary policy.

2020–2024: Post-Pandemic and Post-War Period

In the early 2020s, the Armenian economy faced an unprecedented succession of crises. The disruption to global supply chains brought about by the Covid-19 pandemic, coupled with social distancing requirements, represented major supply shocks. At the same time, parallel negative demand shocks manifested amid consumer hesitation to maintain pre-pandemic levels of spending and restrictions on freedom of movement. Against the backdrop of the pandemic, in the autumn of 2020, these shocks were further compounded by the 44-day war. The combination of war and pandemic resulted in a sharp contraction in aggregate demand, which in turn exerted deflationary pressures on the domestic economy. The double shock also had consequences for aggregate supply and potential output.

By end-2020, a key monetary policy risk was identified as a quicker-than-anticipated recovery of aggregate demand on the back of pent-up consumption and the resulting potential destabilization of inflation expectations. In this situation, although inflation was below the target level, the CBA raised the refinancing rate by one percentage point in December 2020. As a result of this and subsequent actions, the CBA succeeded in containing the sharp rise in prices and ensuring a relatively stable environment, and by end-2021 inflation began to exhibit a certain downward trend.

The sharp escalation of the Russia-Ukraine conflict in February 2022 represented a new source of challenges for monetary policy and the Armenian economy. There existed significant uncertainty regarding the potential economic consequences of the Russia-Ukraine conflict for the Armenian economy. Taking into account Armenia's close economic ties with Russia and the experience of 2014, one view held that the conflict would manifest as a negative external demand shock for the Armenian economy. According to an alternative view, the conflict represented a source of positive growth opportunities and could result in significant increases in capital, labor, and tourism flows. Amid elevated uncertainty, the CBA adopted a cautious policy stance, clearly communicating to markets the sources of prevailing risks and uncertainties and their potential implications. Over the course of 2022–2023, Armenia recorded a significant inflow of international visitors and capital. This broad external demand shock drove above-average growth in services, construction, information technology, and exports, while simultaneously becoming a new source of inflationary pressures and overheating in labor market conditions.

The exchange rate served as the automatic stabilizer for the external demand shock, appreciating to absorb the bulk of the inflationary pressures emanating from external demand. Nonetheless, the aforementioned developments warranted a continued tightening of the policy stance, with a view to containing the broadening of domestic demand conditions and preempting a potential de-anchoring of inflation expectations. In this context, between December 2020 and December 2022, the CBA raised the policy rate by a cumulative total of 6.5 percentage points, bringing the refinancing rate to 10.75% by end-2022. Over the course of 2023, the inflationary environment in Armenia continued to ease, driven primarily by the transmission of the restrictive effects of the CBA's monetary policy, as well as the continued slackening of demand and inflationary pressures amid risks of a global economic slowdown. As a result, from April 2023 onwards, inflation in Armenia fell below the target level, entering negative territory. Notwithstanding these inflation developments, indicators characterizing underlying inflation in the economy — such as the Non-Traded Sticky Price Index (NTSPI) — continued to remain elevated, which posed certain risks regarding the persistence of inflation expectations at comparatively elevated levels and their potential destabilization. Taking into account the aforementioned and numerous other potential risks and uncertainties, over the course of 2023 the CBA embarked on a gradual policy rate reduction cycle. As a result of this policy, by early 2024 it became possible to bring down and anchor sticky-price inflation, wages, and inflation expectations around the target level. Throughout 2024, a low inflationary environment persisted in the economy, while a gradual adjustment of aggregate demand and an easing of labor market conditions were observed, leading to a deceleration in wages, non-traded sticky price inflation, and inflation expectations. In this situation, also taking into account the growing risks conducive to the persistence of a low inflationary environment, the Central Bank continued to gradually ease monetary conditions.



Central Bank
of Armenia

02 |

Conduct of
Monetary Policy
in 2025

A. Policy-Relevant Risk and Uncertainty

What were the key sources of risk and uncertainty that policymakers considered in 2025? How did the taxonomy of scenarios evolve?

Annual Taxonomy of Scenarios: 2025¹

Table E.2: Annual Taxonomy of Scenarios: 2025

Case A-Type Considerations Expansionary Demand	Case B-Type Considerations Contractionary Demand
- Higher trajectory for deficit and debt levels raises questions about fiscal sustainability and exerts upward pressure on the U.S. neutral interest rate, with potential spillover effects on the neutral rates of developing economies, including Armenia. (Q1 Q2 Q3 Q4) - Due to the under-collection of tax revenues and the need to implement social and other expenditures (which do not contribute to domestic growth), there is a risk of a significant increase in the debt burden compared to expectations in the medium term, potentially leading to an upward adjustment of the country risk premium toward its fundamental level. (Q1 Q2 Q3 Q4) - The high economic growth recorded in the domestic economy may reflect higher levels of productivity, an increase in the marginal cost of capital and a rise in the neutral interest rate. In this case, there are risks of continued acceleration of demand and increased inflationary pressures. (Q1 Q2 Q3 Q4) - Persistent uncertainties around domestic demand conditions, particularly regarding the emergence and potential persistence of excess demand conditions: - Economic growth that is above estimated long-term potential and concentrated in primarily demand-driven sectors could point to excess demand conditions in the Armenian economy. (Q1 Q2 Q3 Q4) - 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. (Q1 Q2 Q3 Q4) - The adoption of a more expansionary fiscal stance than previously anticipated present risks of further intensifying domestic demand pressures. (Q1 Q2 Q3 Q4) - Recent increases in tourism flows, as well as sustained strong demand for Armenian goods and especially services, could generate additional demand and inflationary pressures. (Q1 Q2 Q3 Q4) - Uncertainty regarding the trajectory of the Russian-Ukrainian conflict, coupled with the tightening sanctions regime against Russia, may further bolster capital inflows into the Armenian economy, thereby amplifying domestic demand and reinforcing inflationary pressures. (Q1 Q2 Q3 Q4)	- 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. (Q1 Q2 Q3 Q4) - 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. (Q1 Q2 Q3 Q4) - Given risks of weakening U.S. economic activity and labor market conditions, as well as potential overvaluation in financial assets, a potential sharp correction in financial asset prices could generate deflationary pressures both globally and within the Armenian economy. (Q1 Q2 Q3 Q4) - As Western sanctions gradually become more effective, combined with tightening of economic policy stances, domestic demand in Russia may weaken substantially. Simultaneously, the expansion of alternative trade routes for imports and exports may reduce Armenia's integration into Russia's foreign trade flows, thereby exacerbating the anticipated decline in revenues stemming from weakened external demand. (Q1 Q2 Q3 Q4) - 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. (Q1 Q2 Q3 Q4) - Headline inflation remains persistently below the target for a long period, which could lead to a sustained decline in long-term inflation expectations and contribute to restrained consumption patterns. (Q1 Q2 Q3 Q4) - 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. (Q1 Q2 Q3 Q4) - Persistently low inflation in services and non-traded sticky prices; slowing retail trade and final consumption goods imports; weak wage growth; and the structural characteristics of growth could lead to risks of subdued demand and deflationary conditions forming. (Q1 Q2 Q3 Q4)

¹ 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 annual taxonomy of risk scenarios is derived by consolidating the quarterly scenarios. The parentheses next to each scenario indicates whether that scenario was considered by the Board in a given quarter; a yellow value indicates that it was considered, while a black strikethrough indicates that it was not considered.

Case A-Type Considerations Expansionary Demand (Continued)	Case B-Type Considerations Contractionary Demand (Continued)
- Under conditions of persistent uncertainty surrounding inflation (or exchange rate) expectations, various potential shocks could lead to scenarios where these expectations become unanchored in an upward direction. (Q1 Q2 Q3 Q4) - In the event of a potential increase in military expenditures by several major economies, the rise in prices of certain metals could lead to higher export revenues for Armenia and stimulate domestic demand. (Q1 Q2 Q3 Q4) - Inflationary trends from the global economy, especially for food and basic necessities, could lead to an undesirable increase in inflation expectations in Armenia. (Q1 Q2 Q3 Q4) - A possible cooling of regional geopolitical tensions could pose risks of accelerating capital inflows, which could contribute to an expansion in demand conditions. (Q1 Q2 Q3 Q4)	- Uncertainty about neutral rate fundamentals in Armenia: - 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. (Q1 Q2 Q3 Q4) - 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. (Q1 Q2 Q3 Q4) - 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. (Q1 Q2 Q3 Q4) - 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. (Q1 Q2 Q3 Q4) - A sharp slowdown in demand conditions and real incomes in Russia could significantly curtail tourism flows to Armenia, negatively impacting services growth and generating deflationary pressures. (Q1 Q2 Q3 Q4)
Case A-Type Considerations Contractionary Supply	Case B-Type Considerations Expansionary Supply
- Risks associated with disruptions in global supply chains. - The potential for further escalation and worsening of regional conflicts (Middle East, Russia-Ukraine conflict) creates risk in terms of disrupting global supply chains (including oil and food) that can feed through to higher global inflation. This could result in, on the one hand, a tighter-than-expected policy stance in advanced economies, and on the other hand, higher prices being transmitted to the domestic economy through the imported goods channel. (Q1 Q2 Q3 Q4) - 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. (Q1 Q2 Q3 Q4) - A significant decline in external trade flows to Armenia could occur in the context of targeted sanctions on Russia, enhanced effectiveness of third-country controls, and/or Russia's identification of alternative markets and trade routes. (Q1 Q2 Q3 Q4)	- 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. (Q1 Q2 Q3 Q4) - In the event of a significant tightening of U.S. foreign trade policy, an excess supply of goods and services (such as freight transportation) may emerge in the medium term within the global economy among several leading economies, creating risks of associated deflationary pressures for smaller economies. (Q1 Q2 Q3 Q4) - A sharper-than-expected slowdown in Russian demand conditions could represent a negative external demand shock for Armenian goods exports, thereby increasing domestic supply in select goods markets and generating broad-based deflationary pressures. (Q1 Q2 Q3 Q4)

Case A-Type Considerations Contractionary Supply (Continued)	Case B-Type Considerations Expansionary Supply (Continued)
• In the event of a resolution to the Russia-Ukraine conflict and the full or partial lifting of sanctions, Armenia may face a significant outflow of capital and labor. This could result in a substantial reduction in aggregate demand, while simultaneously heightening the risks of broader inflationary pressures. (Q1 Q2-Q3-Q4) • Due to regional and geopolitical uncertainties, developing economies, particularly Armenia, may face a scenario marked by an increase in country risk premiums and a slowdown in investment activity. (Q1 Q2 Q3-Q4) • 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. (Q1-Q2 Q3 Q4)	

B. Monetary Policy Response

How did the Board make their policy rate decisions? What were the key trade-offs policymakers managed in the context of “least regrets”? How did the Board arrive at and communicate its decisions?

Board Decisions on the Refinancing Rate, 2025

Eight times per year, at fixed action dates, the Board of the Central Bank of Armenia decides on monetary policy and sets the policy rate. On an alternating basis, four of the eight decisions (one per quarter) follow a full projection round, the details of which are presented below. The remaining four decisions, referred to as “interim” decisions, follow a more streamlined process. In any economic situation, the Board designs and implements a program of current and future monetary policy actions that is intended to guide inflation and inflation expectations to the target with the minimum possible economic costs. This report presents a summary of monetary policy decisions from two perspectives:

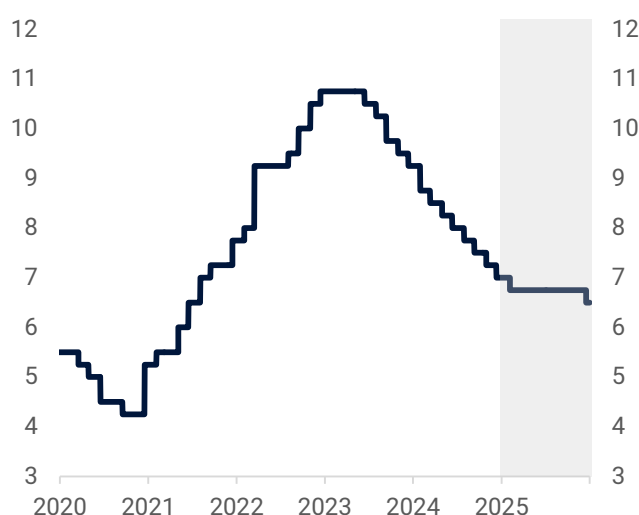
The first approach, presented in this section (B), addresses the discussions underpinning the Board's decision on the refinancing rate, covering the risks and uncertainties that informed that decision. It treats the Board of the CBA as a single collegiate body, examining how the Board has, from an institutional perspective, reached, explained, and communicated its decisions. In this way, this section emphasizes the content of the Board's deliberations, affording the reader the opportunity to understand not only the rationale underpinning each decision, but also the thinking of Board members – and, at times, their divergence of views – on the key uncertainties. The summary of each decision presents the Board's decision and its rationale, a concise description of the Board members' deliberations, as well as a figure summarizing the risks and sources of uncertainty discussed. **The second approach**, presented in Section C, presents how both the individual views of Board members and their assessment of the balance of risks have evolved over the course of the year.

Note: The analyses in this section are based exclusively on information published in the CBA's Monetary Policy Transparency Report. The Transparency Report – which includes the attributed minutes of the policy rate meeting, the attributed voting record, and the vote rationale of each Board member – affords the public a direct and comprehensive understanding of the discussions, arguments, and rationale underpinning the Board's decision at each policy rate meeting. For more detailed information, refer to the CBA's Monetary Policy Transparency Reports. For a more detailed description of economic developments and underlying conditions, refer to Section 1 of this document.

Summary of Board Decisions in 2025

Over the course of the year, the Board of the CBA gradually reduced the policy rate by a total of 0.5 percentage points. Following a reduction of 0.25 percentage points in February, the rate was held unchanged over the course of the year, with a further reduction of 0.25 percentage points in December. A discussion of the risks and uncertainties underlying each decision, as well as the corresponding risk management approaches, is presented below.

Figure 2.B.1. CBA Refinancing Rate



Date	Decision
February 4	↓25 bps
March 18	Unchanged
May 6	Unchanged
June 17	Unchanged
August 5	Unchanged
September 16	Unchanged
November 4	Unchanged
December 16	↓25 bps

Source: CBA

Figure 2.B.2. February decision. Most pressing risks identified by the CBA Board

The Board of the Central Bank of Armenia decided to decrease the policy rate by 0.25 percentage points, setting it at 6.75%.

In order to prudently manage risks stemming from key uncertainties, the CBA Board considered various scenarios in its deliberations. In the context of **Case A-type scenarios**, the Board discussed the risks of a possible expansion of the inflationary environment in the global economy, as well as the risks of interest rates remaining at elevated levels for in the long- term. These types of scenarios are primarily related to the more expansionary fiscal stance in the United States; the uncertainties surrounding the U.S. long-term neutral interest rate; the tightening of external trade policies by leading economies and the expansion of the scope of countries subject to such policies; global and regional geopolitical developments; the formulation of a more expansionary fiscal policy stance in the RA; and other risks. On the other hand, the Board also discussed scenarios where underlying developments would require the policy rate to follow a more rapid and aggressive downward path than what is currently priced in markets in order to sustainably bring inflation back to target in the medium-term horizon (**Case B-type scenarios**). These types of scenarios include the gradual slowdown of economic growth in Armenia, weakening demand, and the prolonged persistence of a low-inflation environment. They also encompass risks related to the further weakening of global demand, the deterioration of labor market conditions in the domestic economy, an undesirable decline in inflation expectations due to inflation remaining low for an extended period, as well as uncertainties and risks regarding the impact on aggregate demand amid slowing activity in the real estate market.

In the context of deliberations around these scenarios, Board members offered varying perspectives about how to prudently manage the key medium-term risks. Board members Levon Sahakyan and Hasmik Ghahramanyan considered it prudent to keep the policy rate unchanged at this stage to mitigate risks associated with Case A-type scenarios. Meanwhile, Martin Galstyan, Armen Nurbekyan, Davit Nahapetyan, Narek Ghazaryan, and Artak Manukyan, seeking to balance both A-type and B-type risks, advocated for a continued gradual reduction of the policy rate in alignment with market expectations. As a result, **seeking to minimize the losses that could stem from Case A and Case B scenarios materializing, and balancing the aforementioned risks in both directions, the Board finds it appropriate to continue to gradually ease the policy stance.**

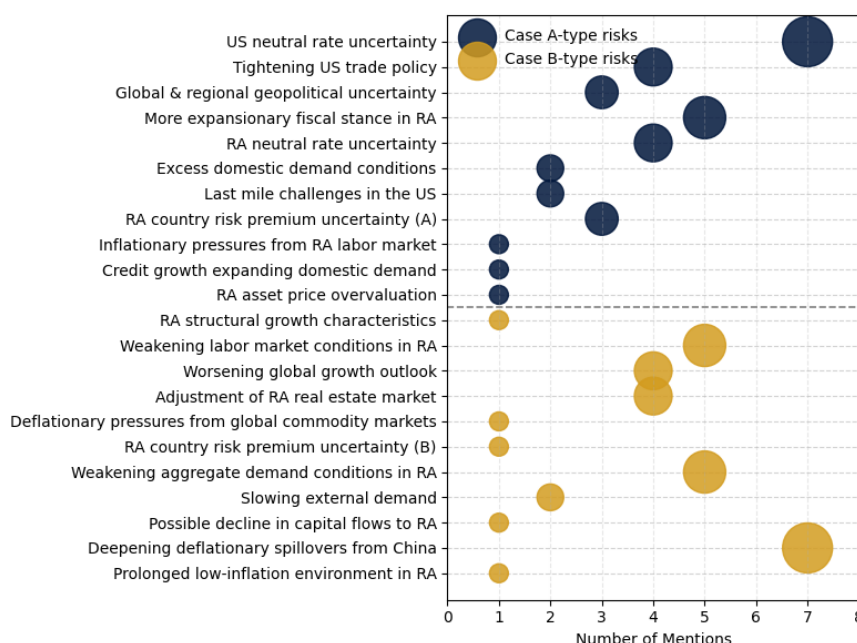
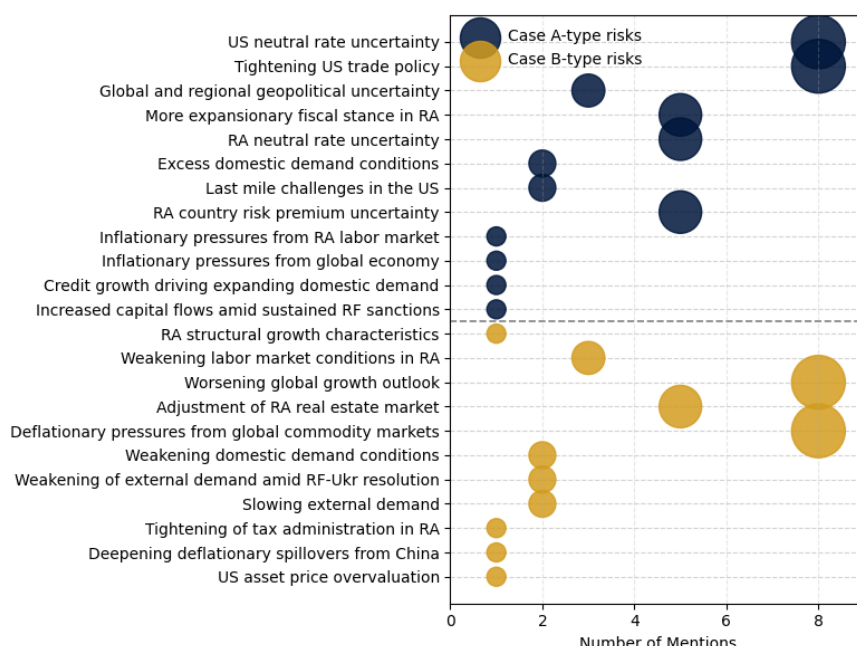


Figure 2.B.3. March decision. Most pressing risks identified by the CBA Board

The Board of the Central Bank of Armenia decided to keep the policy rate unchanged at 6.75%.

In its deliberations, the CBA Board considered various scenarios that, relative to market expectations, could require a higher or lower policy rate path. In the context of **Case A** risks, the Board emphasized the following scenarios: a possible increase in the U.S. long-term neutral interest rate amid prospects of rising public debt in the United States; the tightening of trade policy in the United States and a possible expansion of the global inflationary environment; rising global and regional geopolitical uncertainties; the formulation of a more



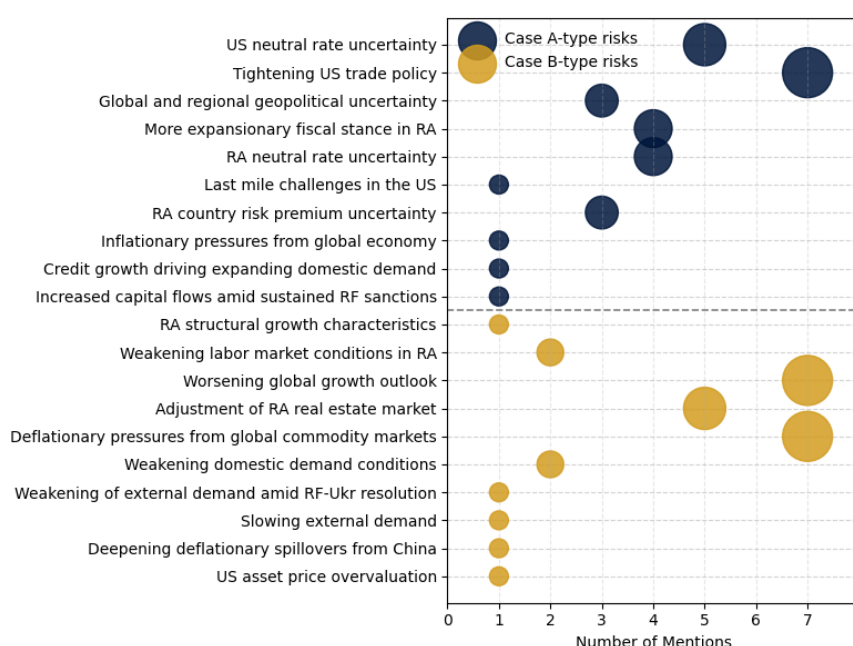
expansionary fiscal stance in the RA; increasing uncertainty surrounding Armenia's country risk premium and neutral interest rate; and other scenarios. In the context of **Case B-type** scenarios, the Board discussed risks connected to the worsening of the global economic outlook and a further slowdown in demand; the deepening of deflationary spillovers from global commodity markets; uncertainties and risks regarding the impact on aggregate demand amid slowing activity in the real estate market; the weakening of labor market conditions in the domestic economy; and other scenarios.

In the context of deliberations around these scenarios, the CBA Board was in unison that the current level of the policy rate best balances the need to manage risks in both directions. As a result, **seeking to minimize the losses that could stem from these and other scenarios materializing, and balancing the aforementioned risks in both directions, the Board finds it appropriate to keep the policy rate unchanged in a line with market expectations.**

Figure 2.B.4. May decision. Most pressing risks identified by the CBA Board

The Board of the Central Bank of Armenia decided to keep the key policy rate unchanged at 6.75%.

Amid the elevated risks and heightened uncertainty, the Board has assessed multiple scenarios, consistent with its mandate to ensure price stability. In discussions around **Case A-type** scenarios, the Board considered scenarios related to uncertainties surrounding the U.S. long-term neutral interest rate; the tightening of external trade policies by leading economies and the expansion of the scope of the affected countries; global and regional geopolitical developments; the potential resolution of the Russia-Ukraine conflict and the resulting risks for Armenia; the formation of a more stimulative fiscal policy stance in the RA; a possible increase in Armenia's country risk premium; and other risks. At the same time, in discussions around **Case B-type** scenarios, the Board considered risks connected to a further slowdown in global demand and the emergence of a deflationary environment in commodity markets; an undesirable softening of domestic labor market conditions; and uncertainties regarding the impact on aggregate demand amid adjustments in real estate prices; and other risks.



In the context of deliberations around these scenarios, Board members offered varying perspectives about how to prudently manage the key medium-term risks. Martin Galstyan, Armen Nurbekyan, Hovhannes Khachatryan, and Hasmik Ghahramanyan, while acknowledging the higher likelihood of Case B-type scenarios materializing, also emphasized the importance of managing the significant macroeconomic implications stemming from Case A-type scenarios. Narek Ghazaryan, Davit Nahapetyan, and Levon Sahakyan preferred to balance both Case A-type and Case B-type risks and to proceed in alignment with market expectations. **While the Board believed that though there was a greater likelihood of Case B-type scenarios materializing, it emphasized the importance of minimizing the potential macroeconomic losses that could stem from the Case A-type risks. As a result, the Board decided to keep the Policy Rate unchanged.**

The Board of the Central Bank of Armenia decided to keep the key policy rate unchanged at 6.75%.

In the course of its deliberations, the CBA Board considered a number of policy scenarios. On the one hand, the Board considered **Case A-type** scenarios related to the broadening of the inflationary environment in the United States; the anchoring of interest rates at elevated levels over the long term; the escalation of tensions in the Middle East; a more expansionary impact of fiscal policy on demand conditions in

the RA; a possible increase in Armenia's country risk premium; as well as the potential resolution of the Russia-Ukraine conflict and the resulting risks for Armenia. On the other hand, the Board considered Case B-type scenarios related to a further slowdown in global demand and the emergence of a deflationary environment in commodity markets; a possible weakening of labor market conditions; as well as uncertainties and risks regarding the impact on aggregate demand amid adjustments in real estate prices.

Figure 2.B.5. June decision. Most pressing risks identified by the CBA Board

Noting the increased prominence of Case A-type risks and emphasizing the importance of managing their potential macroeconomic implications, Board members Martin Galstyan, Armen Nurbekyan, and Narek Ghazaryan assessed, that over the medium term, a higher interest rate path compared to market expectations would be necessary. Artak Manukyan, pointing to the significant intensification of Case A-type risks and the urgency of addressing them, argued that it would be necessary to raise the policy rate already in the current phase. On the other hand, Board members Hovhannes Khachatryan, David Nahapetyan, and Hasmik Ghahramanyan, while agreeing on the increase in Case A-type risks, believed that in the context of persisting Case B-type risks, no immediate policy adjustment was necessary, and that under current conditions it would be appropriate to proceed in line with market expectations. 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.**

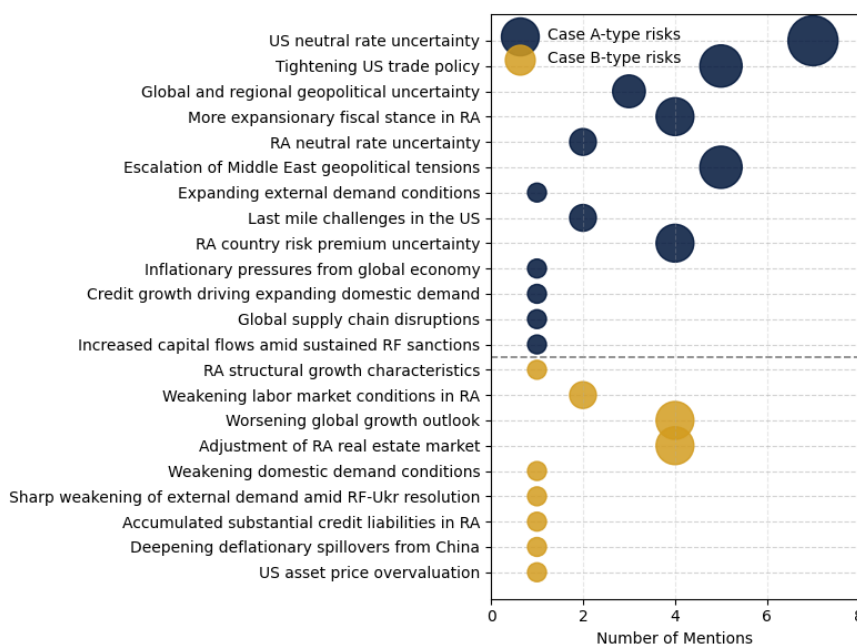
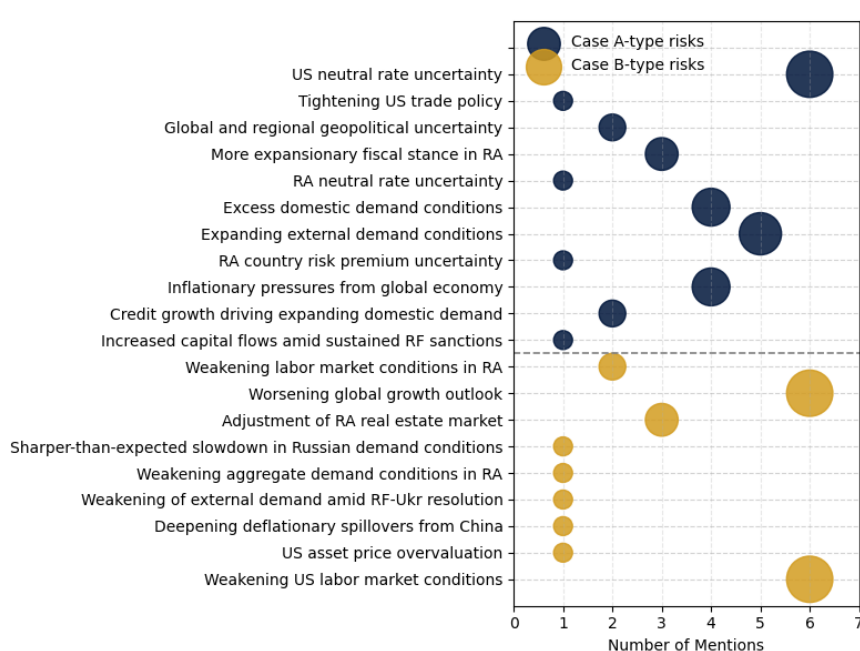


Figure 2.B.6. August decision. Most pressing risks identified by the CBA Board

The Board of the Central Bank of Armenia decided to keep the key policy rate unchanged at 6.75%.

In order to prudently manage risks stemming from key uncertainties, the CBA Board considered various scenarios in its deliberations. **Case A-type** scenarios were primarily related to risks of rising global and domestic neutral interest rates; a possible acceleration of inflationary pressures transmitting from the global economy; a possible expansion of external demand; uncertainty surrounding the country risk premium and regional geopolitical developments; the formation of excess demand conditions in the economy; and other risks. On the other hand, **Case B-type** scenarios were primarily related to the worsening of the global economic growth outlook and a possible weakening of demand conditions; a possible weakening of labor market conditions in the United States; as well as the weakening of labor market conditions in the RA; and other risks.



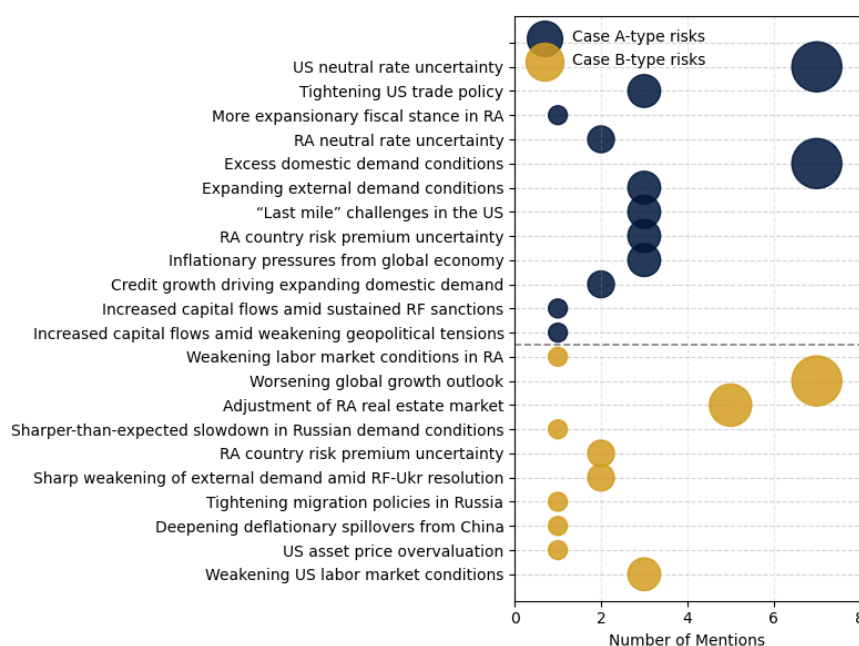
Considering the aforementioned risks and uncertainties, Board members were in unison that the concerns stemming from Case A-type risks continued to dominate. One group of Board members, including Armen Nurbekyan, Davit Nahapetyan, Hasmik Ghahramanyan, Levon Sahakyan, and Narek Ghazaryan, argued that while the current policy stance remained appropriate amid uncertainty, the policy rate may need to follow a higher path over the medium term relative to market expectations in order to ensure the price stability objective. On the other hand, Artak Manukyan suggested that an immediate rate increase would be necessary in order to minimize the losses that could emerge from the Case A-type scenarios materializing. As a result, **emphasizing the buildup of Case A-type risks and seeking to minimize the losses that could stem from these and other scenarios materializing, the Board finds it appropriate to keep the policy rate unchanged.**

Figure 2.B.7. September decision. Most pressing risks identified by the CBA Board

The Board of the Central Bank of Armenia decided to keep the key policy rate unchanged at 6.75%

In the course of policy deliberations, the CBA Board considered various scenarios that, relative to market expectations, could require a higher or lower policy rate path.

Case A-type scenarios were primarily related to risks of rising global and domestic neutral interest rates; uncertainty surrounding the country risk premium and regional geopolitical developments; risks of excess demand conditions forming in the domestic economy; an acceleration of inflationary pressures from the global economy; and other risks. In the context of **Case B-type** scenarios, the Board discussed risks and uncertainties related to the worsening of the global growth outlook; the formation and deepening of a weak demand environment in the economy amid a gradual decline in real estate prices; and the weakening of labor market conditions in the United States.

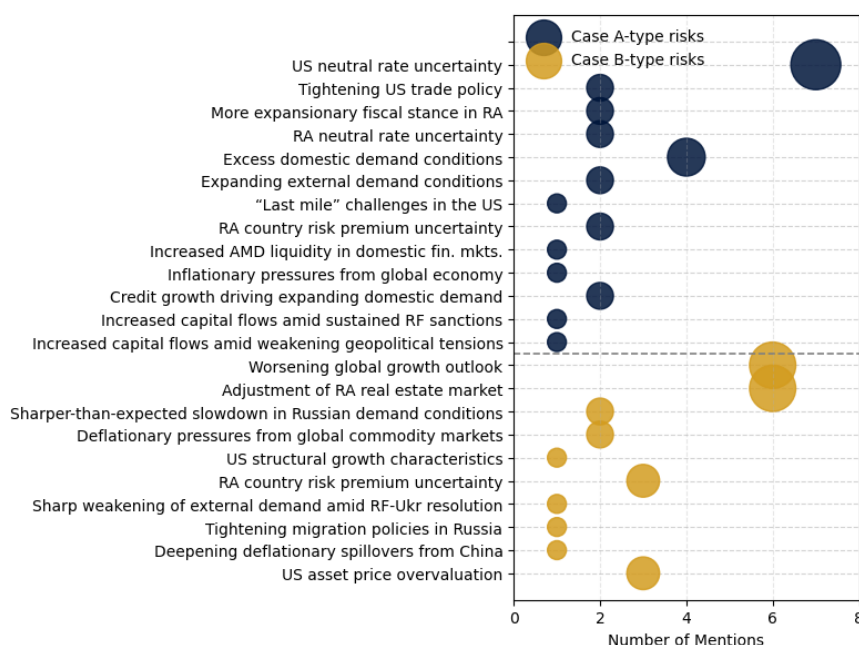


Considering the aforementioned risks and uncertainties, Board members were in unison that the concerns stemming from Case A-type risks continued to dominate. All Board members agreed that while leaving the policy rate unchanged in the current decision remained appropriate amid uncertainty, the policy rate may need to follow a higher path over the medium term relative to market expectations in order to ensure the price stability objective. **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**

Figure 2.B.8. November decision. Most pressing risks identified by the CBA Board

The Board of the Central Bank of Armenia decided to keep the key policy rate unchanged at 6.75%.

In the course of policy deliberations, the CBA Board considered various scenarios. On the one hand, the Board discussed **Case A-type** scenarios, primarily relating to risks of rising global and domestic neutral interest rates; the potential formation of excess demand conditions in the domestic economy; uncertainty surrounding the country risk premium and regional geopolitical developments; as well as a loosening of financial conditions in the domestic economy; and other risks. At the same time, the Board discussed **Case B-type** scenarios relating to uncertainties surrounding the outlook for global economic growth; the potential formation and deepening of a weak demand environment in the economy amid a gradual adjustment in real estate prices; a worsening of the growth outlook in Russia and a sharp weakening of demand conditions; the possible overvaluation of financial asset prices in the United States; as well as risks of deflationary pressures forming in global commodity markets; and other risks.



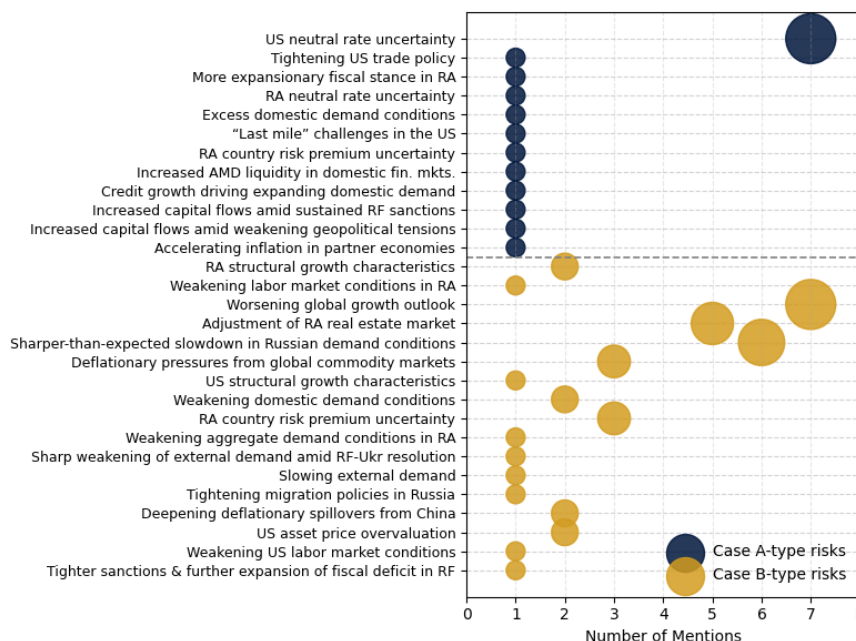
The Board agreed that the greatest policy imperative lies in accurately assessing which types of risks are most relevant and dangerous in terms of their scale and impact on the economy, and what types of policy errors the Board is most focused on avoiding from a least regrets perspective. On the whole, the Board members were in unison that the main risks that had been

discussed in prior rounds—especially dark corner tail risks—had somewhat softened. At the same time, several Board members, including Martin Galstyan, Armen Nurbekyan, Artak Manukyan, and Narek Ghazaryan emphasized the need to manage the losses that could stem from the Case A-type scenarios materializing. In this context, they argued that while the decision to leave the policy rate unchanged remained appropriate amid uncertainty, the policy rate may need to follow a higher path over the medium term relative to market expectations in order to ensure the price stability objective. On the other hand, another group of Board members, including Hovhannes Khachatryan, Levon Sahakyan, and Armen Ktoyan argued that the risks were largely balanced in both directions. **Seeking to manage the macroeconomic implications that could stem from Case A-type scenarios materializing, the Board decided to keep the policy rate unchanged.**

Figure 2.B.9. December decision. Most pressing risks identified by the CBA Board

The Board of the Central Bank of Armenia decided to decrease the key policy rate (refinancing rate) by 25 basis points, setting it at 6.50%

In order to prudently manage risks stemming from key uncertainties, the CBA Board considered various scenarios in its deliberations. In the context of discussions around **Case A-type** scenarios, the Board considered risks of higher global neutral rates; uncertainty about the long-term sustainable level of the country risk premium; risks of increasing aggregate demand conditions; a loosening of financial conditions in the domestic economy; and other risks. In discussions around **Case B-type** scenarios, the Board considered overall concerns about global growth outlook; risks of subdued demand conditions forming in the domestic economy; a gradual adjustment to real estate prices leading to a weak demand environment forming and deepening in the economy; a sharp weakening of demand conditions in Russia; an acceleration of deflationary pressures stemming from global commodity markets; uncertainty surrounding the long-term sustainable level of the country risk premium in Armenia; and other risks.



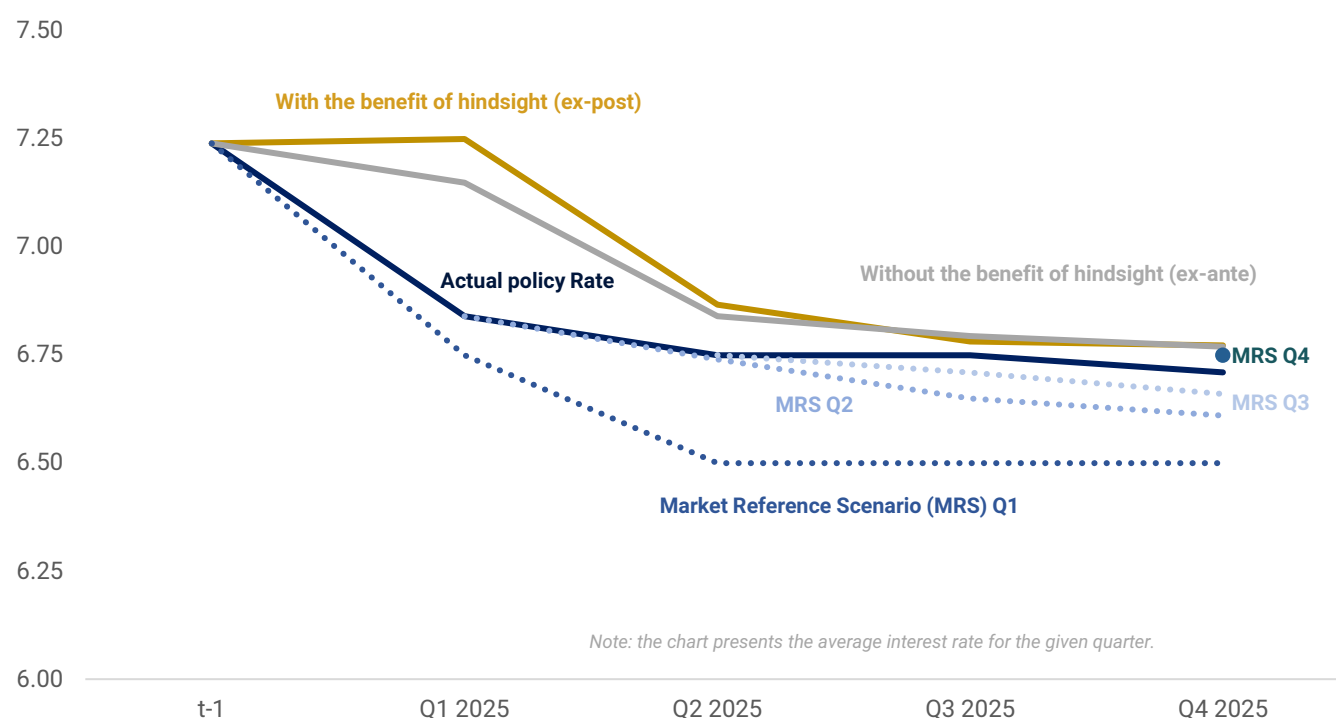
Summarizing their views, the Board agreed that the greatest policy imperative lies in accurately assessing which types of risks are most relevant and dangerous in terms of their scale and impact on the economy, and what types of policy errors the Board is most focused on avoiding from a least regrets perspective. On the whole, the Board members were in unison that the main risks that had been discussed in prior rounds—especially dark corner tail risks—had somewhat softened. At the same time, Board members expressed a diversity of views about the most prudent approach for managing these risks. One group of Board members, including Armen Ktoyan, Artak Manukyan, Davit Nahapetyan, and Martin Galstyan, argued that a 25 bps reduction in the policy rate, in line with market expectations, would best balance the risks at hand. In this context, Armen Ktoyan and Artak Manukyan emphasized the importance of managing the macroeconomic implications stemming from the Case B-type risks, while Davit Nahapetyan and Martin Galstyan found the risks to be largely balanced in both directions. On the other hand, Narek Ghazaryan, Levon Sahakyan, and Hovhannes Khachatryan noted that the current policy stance continued to remain appropriate amid existing uncertainties. Narek Ghazaryan placed greater emphasis on needing to manage the macroeconomic implications stemming from the Case A-type risks materializing, while Levon Sahakyan and Hovhannes Khachatryan argued that the Case A and B-type risks were largely balanced. **Balancing the aforementioned risks in both directions, the Board finds it appropriate to decrease the policy rate in line with market expectations.**

Against the backdrop of prevailing risks and uncertainties, the Board gradually reduced the policy rate at a measured pace, in order to ensure that the price stability objective of 3 percent inflation over the medium-term horizon is met. In the first decision of the year, balancing the risks in both directions, the Board decided to reduce the policy rate by 25 basis points. Over the course of the subsequent six decisions, the Board voted to keep the policy rate unchanged. Nonetheless, against the backdrop of evolving economic conditions and a shifting balance of risks, the rationale underlying these decisions reflected differing approaches to risk management. Specifically, over the course of the year, the Board emphasized the build-up of Case A-type risks and the need

to minimize the losses that could stem from those scenarios materializing. In this context, the Case A-type risks were primarily associated with a possible increase in the long-term neutral interest rate amid rising public debt in the United States; the tightening of external trade policies by advanced economies and their extension to a broader set of countries; a more expansionary fiscal policy stance; the expansion of aggregate demand conditions in the domestic economy; as well as uncertainty surrounding the fundamental drivers of the neutral interest rate in Armenia. At the same time, the Board also expressed concerns regarding a number of Case B-type risks, primarily associated with a worsening global growth outlook; a gradual adjustment to real estate prices leading to a weak demand environment forming and deepening in the economy; a weakening of external demand; the possible overvaluation of asset prices in the United States; the structural characteristics of economic growth in Armenia and the potential weakening of demand conditions; and related risks. Over the course of the year, alongside a softening of certain Case A-type risks, the Board noted growing concerns surrounding a number of Case B-type risks, particularly relating to a worsening global demand and growth outlook; a possible acceleration of deflationary pressures from the global economy; and a sharp weakening of demand conditions in Russia. As a result, at the end of the year, emphasizing the need to manage both Case A and Case B-type risks, the Board decided to reduce the policy rate by 25 basis points.

To better illustrate the nature of risk management-based decision-making, Figure 2.B.10 presents a comparison of the actual path of the policy rate over the course of 2025 with the path implied by a simple policy rule (Taylor rule type). To construct the path implied by the simple policy rule, two approaches have been applied: one with the benefit of hindsight (ex-post) and one without the benefit of hindsight (ex-ante). The ex-post approach illustrates the path that would have been implied had policy decisions been made with perfect foresight regarding economic developments, while the ex-ante approach presents the path that would have been implied in real time, using only the information that was available and accessible at the time of each decision. The simple policy rule equation has been drawn from the analytical work of Mkrtchyan and Stepanyan (2006)². It is worth noting that the simple rule does not imply an optimal or more precise policy path. The primary purpose of this analysis is to illustrate the logic of decision-making under the risk management approach, where the path implied by the simple rule has been used as a benchmark for comparison.

Figure 2.B.10. Comparison of the Actual Policy Rate Path with the Path Implied by a Simple Policy Rule (Taylor Rule Type)*



² We estimate the paper's Taylor rule with interest-rate smoothing on monetary-policy decision dates. The economic assumption is that, at each decision, the Board has an implicit "desired" policy rate determined by the neutral nominal rate, inflation pressure, and the output gap, but it adjusts the actual policy rate only gradually from the previous decision. Starting from the paper's smoothed Taylor rule, $i_t = m_1 i_{t-1} + (1 - m_1)(i_t^{eq} + m_2 X_t^\pi + m_3 Y_{gt})$ we subtract the previous decision's rate i_{t-1} from both sides to express the rule in terms of the policy change $\Delta i_t = i_t - i_{t-1}$. This yields an "error-correction" representation in which the policy change is proportional to the gap between last decision's rate and the desired rate implied by fundamentals: $\Delta i_t = (1 - m_1)(i_t^{eq} + m_2 X_t^\pi + m_3 Y_{gt} - i_{t-1})$. We then estimate the expanded reduced-form version of this equation by OLS (optionally including inflation targeting period dummies and interactions) and use HAC/Newey-West standard errors to allow for serial correlation and heteroskedasticity across decision dates. Finally, we recover the paper's structural parameters from the estimated coefficients: the speed of adjustment is $\lambda = 1 - m_1$ (so m_1 measures gradualism(persistence)), while m_2 and m_3 measure the response of the desired(fully forward looking) policy rate to inflationary pressures and the output gap, respectively.

Based on the results of the analysis presented, during the first half of 2025 the policy rate followed a somewhat lower path than that implied by the simple policy rule. The difference between the policy rate paths reflects the distinction between a simple rule-based and a risk management-based approach to monetary policy. Specifically, from the end of 2024 a certain acceleration in inflation was observed, largely driven by external, supply-side factors. Against this backdrop, the simple policy rule implied maintaining the policy rate at a higher level in order to prevent a further acceleration of inflation. In contrast, while this factor featured prominently in the Board's deliberations (see the first section of this chapter), the Board's decisions were grounded in the need to manage a considerably broader set of Case A and Case B-type risks and uncertainties. As a result, the decision to reduce the policy rate by 25 basis points, followed by the decision to keep the rate unchanged in the subsequent decision, best balanced the need to manage the prevailing risks and the macroeconomic implications stemming from their materialization. Over the course of the second half of the year, alongside a gradual easing of supply-side factors, inflationary pressures transmitted from the global economy moderated and, by year-end, gradually neutralized. Against the backdrop of these developments, the simple policy rule implied a reduction in the policy rate and its stabilization at levels close to the actual policy rate. It is also important to note that the simple rule does not incorporate forward-looking judgments. Consequently, it is unable to reflect the medium-term risks and scenarios that the Board sought to manage in its decision-making over the course of the second half of the year — for example, uncertainty surrounding the fundamental drivers of the long-term neutral interest rate in the United States and in Armenia. In this context, noting the build-up of Case A-type risks and emphasizing the need to minimize the losses that could stem from those scenarios materializing, the Board decided to keep the policy rate unchanged over the course of the June through November decisions, implying a somewhat higher path relative to market expectations. Nonetheless, by year-end, alongside a softening of certain Case A-type risks, a degree of build-up in Case B-type risks was observed, including risks of a sharp weakening of external demand, a worsening global demand and growth outlook, and other risks. As a result, the reduction in the policy rate balanced the need to manage both Case A and Case B-type risks. In summary, over the course of the year, the path implied by the simple rule gradually converged toward the actual policy rate path.

C. Decision-Making Dynamics

How did individual Board members arrive at their decisions, and how did their concerns regarding key risks, uncertainties, and trade-offs evolve over the year?

Since the beginning of 2024, the Central Bank has implemented the key elements of the communications and transparency framework under the Prudent Risk Management Approach to Monetary Policy. The key elements of the monetary policy transparency framework are consolidated in the "Transparency Report" – a document published by the Central Bank concurrently with each monetary policy decision. The latter encompasses the following components:

- the attributed minutes of policy deliberations, which allow the reader to gain a comprehensive understanding of the discussions underlying each decision,
- the attributed voting record on the policy rate decision,
- the vote explanation of each Board member, which includes a concise description of the key risks and uncertainties underlying each Board member's decision. This allows the public to gain a better understanding of each Board member's individual perspective, the risks and concerns underlying the decision, and their assessment of the balance of risks. Furthermore, the introduction of vote explanations serves to enhance the individual accountability of Board members.

This section presents how each Board member's individual perspective, as well as their assessment of the balance of risks, has evolved over the course of the year. Most importantly, this section focuses on the key trade-offs that each Board member took into consideration when arriving at their decision. To this end, an annual summary table is presented for each Board member. For each decision, the table enumerates the key risks and uncertainties that each Board member identified – in their individual vote explanation – as most pressing and as having played a significant role in their decision-making process.

Summary of Board Members' Votes on the Refinancing Rate During 2025

Table 2.C.1. Monetary Policy Decision-Making Calendar for 2025

Decision	1	2	3	4	5	6	7	8
Date	February 4, 2025	March 18, 2025	May 6, 2025	June 17, 2025	August 5, 2025	September 16, 2025	November 4, 2025	December 16, 2025

Table 2.C.2. Summary of Attributed Voting Results*

Decision	1	2	3	4	5	6	7	8
Martin Galstyan	↓0.25 pp	Unchanged	Unchanged	Unchanged		Unchanged	Unchanged	↓0.25 pp
Armen Nurbekyan	↓0.25 pp	Unchanged	Unchanged	Unchanged	Unchanged	Unchanged	Unchanged	
Hovhannes Khachatryan		Unchanged	Unchanged	Unchanged		Unchanged	Unchanged	Unchanged
Hasmik Ghagramanyan	Unchanged	Unchanged	Unchanged	Unchanged	Unchanged		-	-
Davit Nahapetyan	↓0.25 pp	Unchanged	Unchanged	Unchanged	Unchanged	Unchanged		↓0.25 pp
Artak Manukyan	↓0.25 pp	Unchanged		↑0.25 pp	↑0.25 pp	Unchanged	Unchanged	↓0.25 pp
Levon Sahakyan	Unchanged	Unchanged	Unchanged		Unchanged	Unchanged	Unchanged	Unchanged
Narek Ghazaryan	↓0.25 pp	Unchanged	Unchanged	Unchanged	Unchanged	Unchanged	Unchanged	Unchanged
Armen Ktoyan	-	-	-	-	-	-	Unchanged	↓0.25 pp
Policy Decision	↓0.25 pp	Unchanged	Unchanged	Unchanged	Unchanged	Unchanged	Unchanged	↓0.25 pp

* Cells shaded in grey indicate that the Board member was not present at the policy rate meeting.

↓ The Board member voted to decrease the policy rate.

↑ The Board member voted to increase the policy rate.

Governor Martin Galstyan

At the beginning of the year, Martin Galstyan's decisions were characterized by a balanced approach to managing upside and downside risks. In the context of Case A-type risks, the primary concerns were associated with the tightening of U.S. trade policy, as well as the potential re-assessment of fiscal sustainability and the neutral interest rate in the United States. At the same time, uncertainties surrounding global and regional geopolitical developments, as well as the direction and magnitude of the impact of fiscal policy on demand conditions in Armenia, constituted key sources of upside risk. On the other hand, Case B-type risks were associated with a potential weakening of economic growth and demand conditions in Armenia. In his May 2025 decision, Martin Galstyan noted that, while the probability of Case B-type scenarios materializing – stemming from a potential deterioration in global and domestic economic prospects – was assessed as greater, it remained important to manage the significant macroeconomic implications that could arise from Case A-type scenarios. In subsequent decisions, as Martin Galstyan noted an intensification of Case A-type risks, he placed greater emphasis on the need to minimize potential losses arising from Case A-type scenarios. The primary Case A-type risks were associated with a potential upward re-assessment of the neutral interest rate in the United States and in developing economies, as well as an expansion of external and domestic demand conditions in Armenia. Toward the end of the year, taking stock of the growing significance of Case B-type risks alongside the persistence of the aforementioned Case A-type risks, Martin Galstyan's decision reflected a balanced approach to managing risks in both directions.

Table 2.C.3. Summary of key risks mentioned by Governor Martin Galstyan in rationale for each vote

Decision	1	2	3	4	5*	6	7	8
Case A-type risks								
In the US, higher trajectory for deficit and debt levels exerts upward pressures on US neutral interest rate								
Tightening of trade policies in the US								
Global and regional geopolitical uncertainty								
More expansionary fiscal stance in RA								
Uncertainty regarding the neutral rate fundamentals in RA								
Escalation of geopolitical tensions in the Middle East								
Excess demand pressures in the domestic economy								
Expansion of external demand conditions								
Case B-type risks								
The structural characteristics of growth pose uncertainty regarding the sustainability of current trends and the underlying strength of domestic demand conditions in RA								
Possible weakening of labor market conditions in RA								
Worsening of global growth outlook								
Gradual adjustment of the real estate market in RA								
Weakening of external demand amid a deteriorating economic outlook in Russia								
Voting Record	↓25 bps	Un-changed	Un-changed	Un-changed	-	Un-changed	Un-changed	↓25 bps

* The Board member was not present at the policy rate meeting.

Deputy Governor Armen Nurbekyan

At the beginning of 2025, Armen Nurbekyan's decisions were characterized by a balanced approach to managing risks in both directions. In this context, Armen Nurbekyan assessed that global and domestic structural factors were predominantly associated with Case A-type risks, while cyclical factors constituted Case B-type risks. From the external sector, the primary Case A-type risks were associated with uncertainties surrounding the neutral interest rate amid a potential increase in public debt in the United States, the tightening of U.S. trade policy, as well as the implications for Armenia's country risk premium — and consequently the neutral interest rate — under conditions of persistent global and regional geopolitical tensions. Within the domestic economy, the primary Case A-type uncertainties were associated with the potentially more expansionary impact of fiscal policy on demand conditions, as well as the risk of an increase in the country risk premium driven by a potential rise in public debt. On the other hand, Case B-type risks were primarily associated with the emergence of subdued demand conditions in the global economy and in Armenia. In May 2025, having noted a greater probability of Case B-type scenarios materializing, Armen Nurbekyan nonetheless emphasized the importance of managing the significant macroeconomic implications that could arise from Case A-type scenarios. However, from mid-2025 through the end of the year, Armen Nurbekyan's decisions reflected exclusively the need to manage the aforementioned Case A-type risks.

Table 2.C.4. Summary of key risks mentioned by Deputy Governor Armen Nurbekyan in rationale for each vote

Decision	1	2	3	4	5	6	7	8*
Case A-type risks								
In the US, higher trajectory for deficit and debt levels exerts upward pressures on US neutral interest rate								
"Last mile" challenges in the US								
Tightening of trade policies in the US								
Global and regional geopolitical uncertainty								
Uncertainty regarding the neutral rate fundamentals in RA								
Uncertainty regarding the long-term sustainable level of country risks premium in RA								
Excess demand pressures in the domestic economy								
More expansionary fiscal stance in RA								
Expansion of external demand conditions								
Case B-type risks								
Worsening of global growth outlook								
Possible weakening of labor market conditions in RA								
Gradual adjustment of the real estate market in RA								
Deflationary pressures stemming from global commodity markets								
Voting Record	↓25 bps	Un- changed	Un- changed	Un- changed	Un- changed	Un- changed	Un- changed	-

* The Board member was not present at the policy rate meeting.

Deputy Governor Hovhannes Khachatryan

In the beginning of the year, Hovhannes Khachatryan found the Case B-type risks, particularly those related to a weakening global and domestic demand outlook, to be dominant. As the year progressed, the continued dominance of these Case B-type risks began to be countered in his May and June decisions by the need to manage potential losses stemming from the Case A-type risks, particularly those related to neutral rate and global trade policy uncertainty. As US trade policy uncertainty eased while risks of expanding aggregate demand conditions in Armenia increased, Hovhannes Khachatryan's September decision placed greater emphasis on managing losses that could stem from the Case A-type risks materializing. His final two decisions, however, were driven by the need to balance risks in both directions. From a Case A perspective, these included sustained upside risk to US neutral rates as well as a potential easing of domestic financial conditions, while the Case B risks reflected concerns about weakening demand globally, downside uncertainty to the country risk premium, and growing concerns about the structural characteristics of domestic growth.

Table 2.C.5. Summary of key risks mentioned by Deputy Governor Hovhannes Khachatryan in rationale for each vote

Decision	1*	2	3	4	5*	6	7	8
Case A-type risks								
In the US, higher trajectory for deficit and debt levels exerts upward pressures on US neutral interest rate								
Tightening of trade policies in the US								
Uncertainty regarding the long-term sustainable level of country risks premium in RA								
Excess demand pressures in the domestic economy								
Increased AMD liquidity in domestic financial markets may lead to looser financial conditions and an expansion of domestic demand								
Case B-type risks								
Worsening of global growth outlook								
The structural characteristics of growth in the US								
Gradual adjustment of the real estate market in RA								
Weakening of domestic demand conditions								
Uncertainty regarding the long-term fundamental level of country risks premium in RA								
The structural characteristics of growth pose uncertainty regarding the sustainability of current trends and the underlying strength of domestic demand conditions in RA								
Voting Record	-	Un- changed	Un- changed	Un- changed	-	Un- changed	Un- changed	Un- changed

* The Board member was not present at the policy rate meeting.

Board Member Hasmik Ghahramanyan

Hasmik Ghahramanyan's February decision was motivated by the need to manage Case A-type risks. In this context, the primary Case A type risks she sought to manage related to risks of rising inflationary pressures from the labor market, expansionary fiscal policy, as well as uncertainty about the country risk premium and neutral rate, while the sole Case B risk she emphasized related to a possible slowing of domestic demand conditions. In the following decision, her approach shifted to the need to balance the risks that could stem from both types of scenarios, specifically risks of tightening US trade policy (Case A) and risks of slowing demand and inflationary environment amid a possible resolution of the Russia-Ukraine conflict (Case B). In May and June, however, her decision-making shifted to greater emphasis on the Case A type risk. Specifically, in June, she emphasized risks stemming from a worsening of geopolitical tensions in the Middle East and growing concerns about US government debt sustainability. Finally, in August, emphasizing risks of expanding inflationary pressures from the global economy on the one hand and risks of weakening domestic demand conditions on the other, she emphasized the need to balance the losses that could stem from risks in either direction.

Table 2.C.6. Summary of key risks mentioned by Board member Hasmik Ghahramanyan in rationale for each vote

Decision	1	2	3	4	5	6*	7**	8**
Case A-type risks								
Inflationary pressures stemming from the domestic labor market								
Uncertainty regarding the neutral rate fundamentals in RA								
Uncertainty regarding the long-term sustainable level of country risks premium in RA								
Tightening of trade policies in the US								
More expansionary fiscal stance in RA								
In the US, higher trajectory for deficit and debt levels exerts upward pressures on US neutral interest rate								
Global trade tensions								
Inflationary pressures stemming from the global economy								
Expansion of domestic demand conditions driven by sustained credit growth								
Case B-type risks								
Possible weakening of aggregate demand conditions in RA								
Possible resolution to the Russia-Ukraine conflict could result in substantial reduction in aggregate demand in RA								
Weakening demand conditions in key trading partner economies								
Deflationary pressures stemming from global commodity markets								
Worsening of global growth outlook								
Weakening labor market conditions								
Voting Record	Un- changed	Un- changed	Un- changed	Un- changed	Un- changed	-		

* The Board member was not present at the policy rate meeting.

**Board member's term ended

Board Member Davit Nahapetyan

In the first half of the year, Davit Nahapetyan's decisions were motivated by the view that risks were balanced in both directions, though the specific risks and associated losses that he sought to manage evolved somewhat during this period. In January, Davit Nahapetyan was most concerned about country risk premium and neutral rate uncertainty (Case A), which were balanced by the need to manage risks of weakening external demand, a potential adjustment in the real estate sector, and disinflationary pressures from the global economy (Case B). In March and June, as global economic policy uncertainty increased, concerns of higher US neutral rates and the combination of a worsening global growth outlook in tandem with rising global inflationary pressures began to play a growing role in his decisions. By the August and September decisions, however, his decisions were motivated by the need to manage the losses associated with Case A-type scenarios. Specifically, these Case A-type considerations related to expanding domestic demand conditions, a more expansionary stance for fiscal policy, and sustained global inflationary pressures, even as he noted emerging Case B-type risks including a weakening labor market and a worsening global growth outlook. However, as global inflationary pressures began to ease toward the end of the year, his balance of risks shifted, emphasizing the need to manage risks in both directions.

Table 2.C.7. Summary of key risks mentioned by Board member Davit Nahapetyan in rationale for each vote

Decision	1	2	3	4	5	6	7*	8
Case A-type risks								
Uncertainty regarding the neutral rate fundamentals in RA								
Uncertainty regarding the long-term sustainable level of country risks premium in RA								
In the US, higher trajectory for deficit and debt levels exerts upward pressures on US neutral interest rate								
Tightening of trade policies in the US								
Inflationary pressures stemming from the global economy could lead to undesirable increase in inflation expectations in RA								
More expansionary fiscal stance in RA								
Excess demand pressures in the domestic economy								
Expansion of external demand conditions								
Case B-type risks								
Weak external demand for domestic services								
Gradual adjustment of the real estate market in RA								
Worsening of global growth outlook								
Accumulated substantial credit liabilities in RA								
Weakening of labor market conditions								
Deflationary pressures stemming from global commodity markets								
Voting Record	↓25 bps	Un- changed	Un- changed	Un- changed	Un- changed	Un- changed	-	↓25 bps

* The Board member was not present at the policy rate meeting.

Board Member Artak Manukyan

In Q1 2025, Artak Manukyan's decisions were driven by the view that the need to manage the losses associated with the Case A- and B-type scenarios materializing were largely balanced in both directions. Specifically, in January, key Case A-type considerations including risks of higher-for-longer interest rates in the US, a more expansionary fiscal policy stance, and elevated demand conditions domestically. Meanwhile, the Case B-type considerations included risks of weakening capital flows, a gradual adjustment to the real estate market, and weakening labor market conditions. In March, while he continued to emphasize the need to balance risks in both directions, his Case A-type risks were augmented by uncertainty about the country risk premium, while the Case B-type risks he sought to manage were dominated by risks of weakening external demand and tightening tax administration. In June and August, Artak Manukyan placed greater emphasis on the need to manage potential losses stemming from the Case A-type risks, supporting successive votes in favor of increasing the policy rate by 25 basis points. Specifically, his June decision placed almost no emphasis on Case B-type considerations, instead prioritizing the need to manage risks associated with rising geopolitical tensions in the Middle East, an elevated policy stance in the US, and country risk premium uncertainty, while his August decision was primarily motivated by the need to manage risks associated with excess domestic and external demand conditions forming. Beginning in September, he began to call attention to Case B-type risks related to a deteriorating Russian economic outlook, tightening Russian migration policy, and downside uncertainty to the country risk premium amid easing geopolitical tensions, even as his decision-making continued to stem from the need to manage the Case A-type risks. By December, however, as risks of excess aggregate demand conditions meaningfully subsided while risks to the Russian economic outlook continued to grow, Artak Manukyan's decision-making shifted, emphasizing the need to manage the Case B-type scenarios.

Table 2.C.8. Summary of key risks mentioned by Board member Artak Manukyan in rationale for each vote

Decision	1	2	3*	4	5	6	7	8
Case A-type risks								
"Higher for longer" in the US								
More expansionary fiscal stance in RA								
Excess demand pressures in the domestic economy								
Uncertainty regarding the long-term sustainable level of country risks premium in RA								
Global and regional geopolitical uncertainty								
Supply chain disruptions in the global economy								
Expansion of external demand conditions								
Case B-type risks								
Possible decline in capital flows to RA								
Uncertainty regarding the long-term sustainable level of country risks premium in RA								
Gradual adjustment of the real estate market in RA								
Weakening of labor market conditions								
Weakening of external demand conditions								
Tightening of tax administration in RA								
A sharper-than-expected slowdown in Russian demand conditions								
Tightening migration policies in Russia								
Voting Record	↓25 bps	Un- changed	-	↑25 bps	↑25 bps	Un- changed	Un- changed	↓25 bps

* The Board member was not present at the policy rate meeting.

Board Member Levon Sahakyan

In his February decision, Levon Sahakyan placed greater emphasis on the Case A-type risks, specifically those related to higher neutral rates in the US and in Armenia as well as uncertainty stemming from US fiscal policy. In his view, the need to manage the potential losses stemming from these Case A risks outweighed the sole Case B risk of a weakening global economic outlook. In his March decision, however, Levon Sahakyan found that the aforementioned Case A type risks were balanced by the Case B-type risks of a weakening global and domestic demand outlook. This balanced approach continued to dominate his thinking in the May decision, where the Case B-type risks were augmented by concerns about a gradual adjustment in the real estate sector. Beginning in August, his decision again reflected the need to manage Case A-type risks, and in particular, risks of expanding demand conditions in Armenia as well as US neutral rate uncertainty. By the end of the year, his final two decisions shifted to a more balanced assessment, with the need to manage Case A-type risks associated with a higher US neutral rate balanced out by the need to manage risks of adjustments in the real estate market and downside uncertainty regarding the country risk premium, to which in December he also emphasized concerns about weakening external demand.

Table 2.C.9. Summary of key risks mentioned by Board member Levon Sahakyan in rationale for each vote

Decision	1	2	3	4*	5	6	7	8
Case A-type risks								
In the US, higher trajectory for deficit and debt levels exerts upward pressures on US neutral interest rate								
Tightening of trade policies in the US								
Uncertainty regarding the neutral rate fundamentals in RA								
Excess demand pressures in the domestic economy								
Case B-type risks								
Uncertainty regarding the domestic demand outlook in RA								
Worsening of global growth outlook								
Gradual adjustment of the real estate market in RA								
Uncertainty regarding the long-term sustainable level of country risks premium in RA								
Weakening of external demand conditions								
Voting Record	Un- changed	Un- changed	Un- changed	-	Un- changed	Un- changed	Un- changed	Un- changed

* The Board member was not present at the policy rate meeting.

Board Member Narek Ghazaryan

In the first three decisions of the year, Narek Ghazaryan's votes were motivated by the need to balance the risks stemming from both the Case A and Case B scenarios. In the January decision, the main Case A-type considerations related to growing global geopolitical and trade tensions, a more expansionary fiscal policy stance domestically, and accelerating lending activity and high asset prices supporting high domestic demand. These risks were balanced by Case B-type considerations related to deflationary pressures from China, weakening growth in the Euro Area and Great Britain as well as in countries impacted by trade wars, slowing wage growth, a rapid adjustment in the real estate market, and the persistence of a low inflationary environment in Armenia. In the March and May decisions, balancing of these risks continued to dominate Narek Ghazaryan's decisions, although some risks gradually faded out (high asset prices in Armenia and a persistence of a low inflationary environment) while other risks were added to the mix (overvalued asset prices in the US and uncertainty related to sanctions on Russia). However, beginning with the June decision and continuing through the end of the year, Narek Ghazaryan's decisions were motivated by the need to manage potential losses associated with the aforementioned Case A-type risks. Several Case B-type risks, including those related to weakening wage growth, a negative growth outlook for the EU and GB, and downside uncertainty stemming from sanctions on Russia, gradually faded out throughout the year. At the same time, the Case A-type risks evolved as well, with risks related to US trade policy and global geopolitical tensions gradually easing while new risks stemming from positive regional geopolitical developments and a potential acceleration of inflation in trading partner economies gaining relevance by year-end.

Table 2.C.10. Summary of key risks mentioned by Board member Narek Ghazaryan in rationale for each vote

Decision	1	2	3	4	5	6	7	8
Case A-type risks								
Tightening of trade policies in the US								
Global geopolitical uncertainty								
More expansionary fiscal policy stance in RA								
Expansion of domestic demand conditions driven by sustained credit growth								
Potential overvaluation of asset price in RA								
Sustained sanctions against Russia could result in increased capital flows to RA								
Inflationary pressures stemming from the global economy								
Sustained robust economic activity in RA								
Regional geopolitical developments								
Acceleration of inflationary environment in partner economies								
Case B-type risks								
Deepening deflationary spillovers from China								
Weaker growth outlook in EU & UK								
Slowing wage growth in RA								
Gradual adjustment of the real estate market in RA								
Prolonged low-inflation environment in RA								
Slowing economic activity in countries involved in global trade tensions								
Potential overvaluation in financial asset prices in the US								
Possible resolution to the Russia-Ukraine conflict could result in substantial reduction in aggregate demand in RA								
Possible resolution to the Russia-Ukraine conflict could result in substantial reduction in aggregate demand in RA								
Voting Record	↓ 25 bps	Un- changed	Un- changed	Un- changed	Un- changed	Un- changed	Un- changed	Un- changed

Board Member Armen Ktoyan

Armen Ktoyan's November decision was motivated by the need to balance the Case A and Case B-type risks. Specifically, he emphasized Case A-type risks related to ongoing US trade policy, an expansionary fiscal stance in the US, and risks of sustained inflationary pressures in global food markets. In his view, these risks were balanced by key Case B-type risks including a potential weakening of the construction and real estate sectors and a worsening growth outlook for the Russian economy. In his December decision, however, Armen Ktoyan placed greater emphasis on managing the losses associated with the Case B-type scenarios materializing. Specifically, these included risks of worsening labor market conditions and an asset price correction in the US, a weakening in domestic demand conditions, and a further worsening of economic fundamentals in Russia, in addition to the aforementioned B-type risks.

Table 2.C.11. Summary of key risks mentioned by Board member Armen Ktoyan in rationale for each vote

Decision	1	2	3	4	5	6	7*	8
Case A-types risks								
Tightening of trade policies in the US								
More expansionary fiscal policy stance in the US								
Inflationary pressures stemming from the global economy								
Case B-type risks								
Gradual adjustment of the real estate market in RA								
A sharper-than-expected slowdown in Russian demand conditions								
Weakening labor market conditions in US								
Potential overvaluation in financial asset prices in the US								
Tighter sanction against Russia & further expansion of fiscal deficit								
Weakening demand conditions in RA								
Voting Record							Un- changed	↓25 bps

*First decision following the appointment as a Board member



Central Bank
of Armenia

03 |

Market
Response
to Policy
Decisions

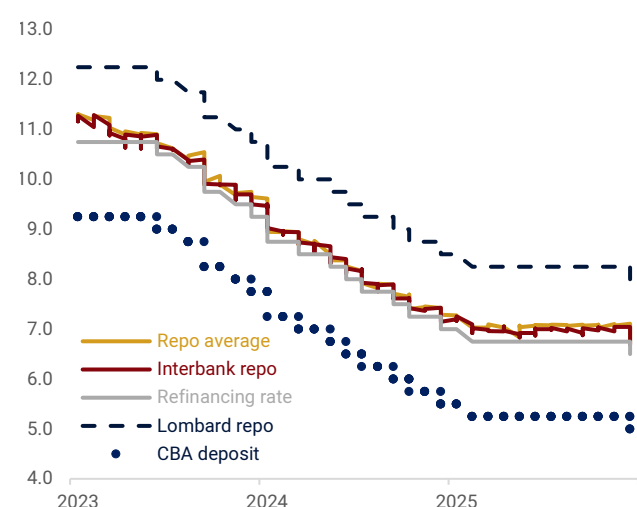
Market Response to Policy Decisions

How did financial markets react to policy rate decisions and communications?

A. Monetary Policy Operations

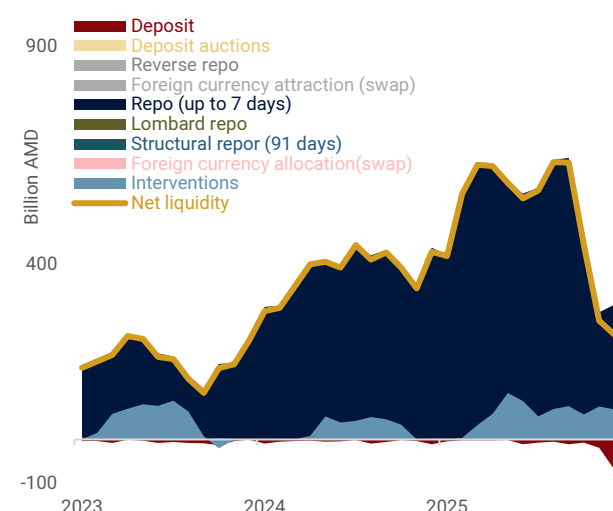
In 2025, market interest rates were largely formed around the Central Bank's operational objective — the policy rate. Specifically, the interbank repo rate deviated by an average of approximately 23 basis points from the policy rate, reflecting a close alignment between market dynamics and the Central Bank's monetary policy stance. This also reflects the stability of the financial system and the presence of adequate and sufficient liquidity, as no significant interest rate volatility was observed in the market during the period under review. In this context, with a view to ensuring the normal functioning of financial markets, the CBA participated in the foreign exchange market on a situational basis, primarily conducting foreign currency purchase operations.

Figure 3.A.1. CBA Refinancing Rate and Interbank Repo Rate



Source: CBA

Figure 3.A.2. Monetary policy operations



Source: CBA

B. Market expectations of the future path of the policy rate

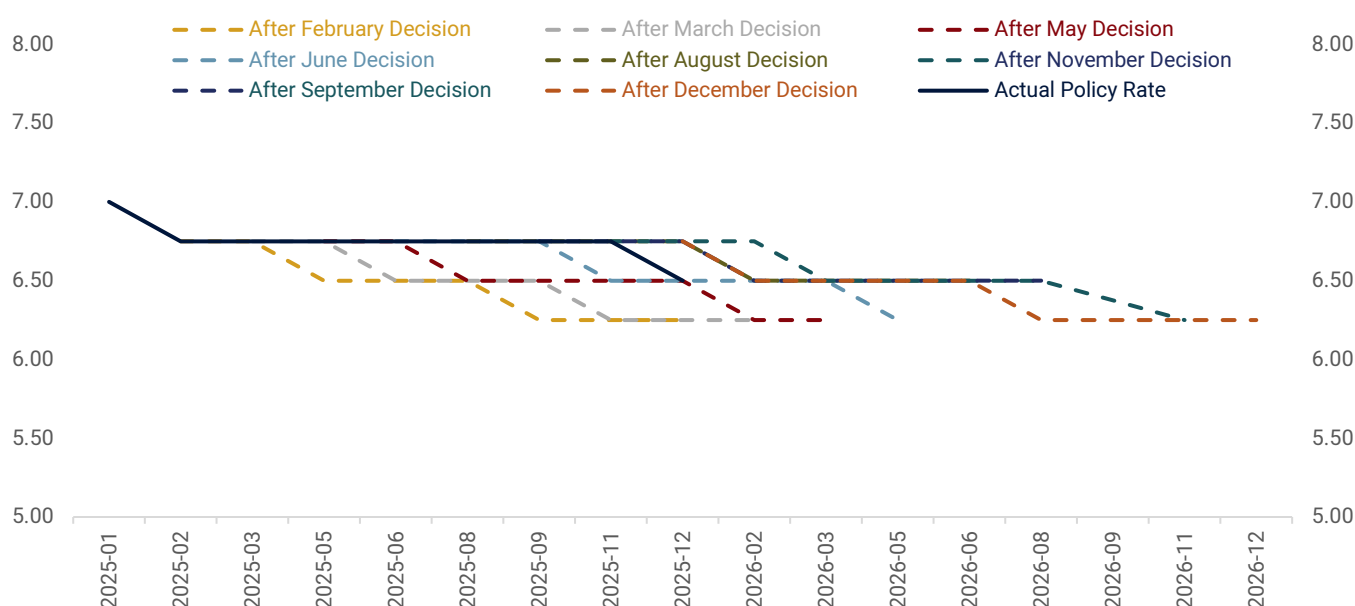
This sub-section presents the evolution of market expectations regarding the future path of the policy rate over the course of 2025, in the context of monetary policy decisions, the Central Bank's forward guidance, and changing economic conditions.

In order to construct a comprehensive and informed picture of market expectations regarding the expected path of the policy rate, this sub-section also draws on the results of the CBA's relatively high-frequency surveys of financial market participants (dealers of commercial banks and investment companies) regarding the expected path of the policy rate. These surveys are conducted before and immediately after each monetary policy decision, enabling an examination of the immediate impact of monetary policy decisions and communications on market expectations, as well as an identification of changes over time in the key factors driving the formation of those expectations.

At the start of 2025, financial market participants expected the CBA to continue reducing the policy rate, albeit at a more gradual pace relative to previous quarters. Over the course of the year (and particularly following the February decision), market expectations remained broadly unchanged, reflecting a path of gradual reduction in the policy rate at a measured pace over the subsequent eight decisions. While market participants' assessments regarding the magnitude and pace of policy rate reductions remained broadly unchanged, participants continuously pushed back the expected timing of rate reductions, shifting them to subsequent quarters. Specifically, following the reduction of the policy rate by 25 basis points in February 2025, the refinancing rate remained unchanged through November. Beginning with the June decision and through November, the decisions to keep the policy rate unchanged reflected the need to manage Case A-type risks (a detailed description of the Case A and Case B-type risks considered by the CBA Board in the decision-making process is presented in Chapter 2). The communications underlying the above-mentioned decisions differed significantly from those of prior decisions, signaling to markets a shift in the risk management approach. It is important to note that, in the context of this shift in communications, the market appropriately internalized the approach underlying the Board's decision and its forward guidance, and adjusted its expectations accordingly. In its December 2025 decision, the CBA Board decided to reduce the policy rate by 25 basis points. In this context, whereas in prior

decisions the Board had emphasized the need to manage Case A-type risks — which could have required a higher policy rate path relative to market expectations over the medium term — the risk management approach underlying the most recent decision reflected a more balanced approach, emphasizing the need to manage the macroeconomic implications stemming from Case B-type scenarios as well.

Figure 3.B.1. Evolution of market expectations regarding the future path of the policy rate



Prior to the February 2025 decision, financial market participants expected a gradual reduction of the policy rate over the next eight decisions. In this context, the majority of market participants expected a cumulative reduction of the refinancing rate by 100 basis points over the course of the year, with the rate settling at around 6.00% by end-2025. In these surveys, market participants also provided narratives explaining the key considerations and risks underpinning their expectations. In this context, the key downside considerations mentioned by participants related to the persistence of a low inflation environment in the Armenian economy, a further weakening of demand conditions in the domestic economy, a deteriorating global economic outlook, softening labor market conditions in Armenia, and other factors. At the same time, the key upside considerations were associated with a possible escalation of global and regional geopolitical tensions, a widening of the fiscal deficit and a potential increase in the country risk premium, uncertainty surrounding US economic policies, and other risks.

Figure 3.B.2a. Expected path of the CBA Policy Rate.

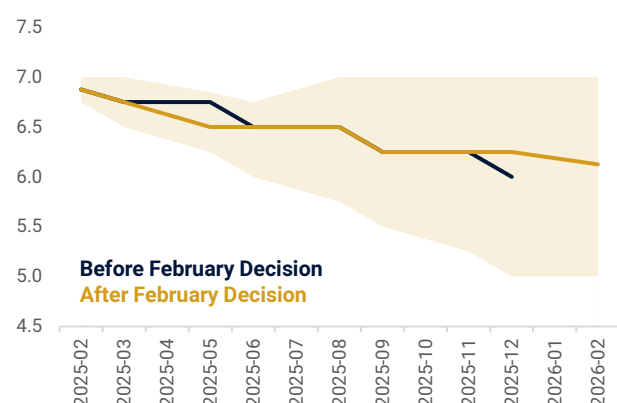
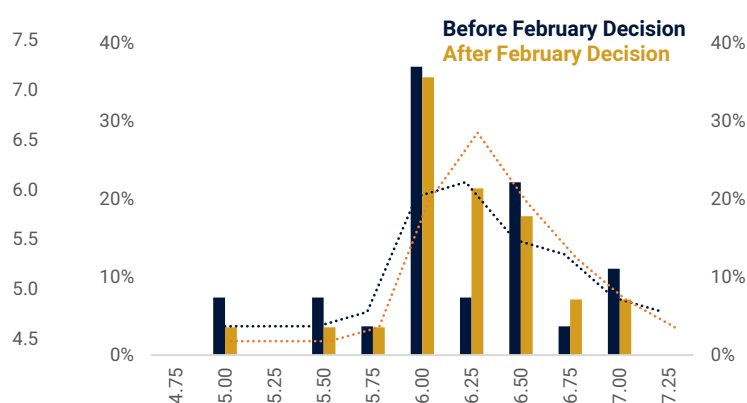


Figure 3.B.2b. Evolution of market expectations for the one-year ahead policy rate



In its February 4, 2025 decision, the Board of the Central Bank of Armenia decided to continue the gradual reduction of the policy rate at a measured pace, communicating that a reduction of the policy rate by 25 basis points best balanced the need to manage Case A and Case B-type risks. This messaging sent a clear signal to markets that the CBA's actions reflected a balanced approach to the assessment of risks, and that a gradual and measured reduction of the policy rate was consistent with market expectations. In the survey conducted immediately following the February decision, the expected path of the policy rate remained broadly unchanged, while the distribution of participants' assessments of the one-year ahead policy rate showed a slight but notable shift. Specifically, compared to the previous survey, a slight upward shift was observed in the expected one-year ahead policy rate. Whereas prior to the decision, the majority of participants (55%) expected the policy rate to settle at 6.00% or below by year-end, following the decision a significant decline was observed in the share of participants expecting the rate to settle at lower levels.

This could suggest that market participants absorbed the Board's communication regarding its balanced risk management approach, implying that in reaching its decision, the Board sought to manage, in equal measure, the potential losses stemming from both upside and downside risks.

Figure 3.B.3a. Expected path of the CBA Policy Rate

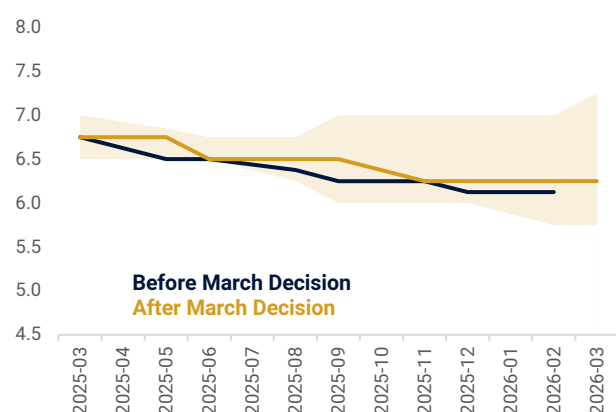
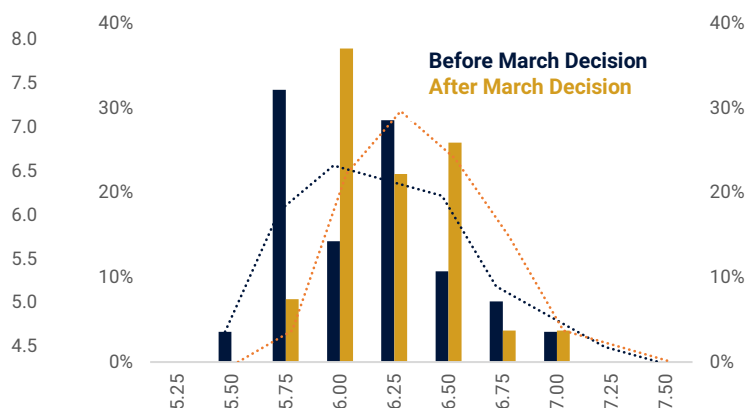


Figure 3.B.3b. Evolution of market expectations for the one-year ahead policy rate



Even as CBA communications gave markets greater confidence about future rate reductions, the survey conducted prior to the March 2025 decision continued to reflect some uncertainty about the pace and scale of rate cuts in the near term. In this context, market participants expressed a degree of divergence in their views regarding the expected one-year ahead policy rate; approximately 30% of respondents expected the rate to settle at around 5.75%, while a comparable share of around 30% anticipated a higher level of around 6.25%. This could suggest that markets were broadly aligned on the direction of future rate changes, while no clear consensus had emerged regarding whether the pace and scale of rate reductions would be more aggressive, or more moderate and gradual. At the same time, this could also suggest that some market participants assigned greater weight to downside risks in forming their expectations, while others, placing greater emphasis on upside risks, anticipated a more conservative pace of rate reductions. In this context, market participants continued to express concerns about Case A-type risks, such as a potential expansion of demand conditions in the domestic economy, a more expansionary fiscal policy stance, uncertainty surrounding the country risk premium, and other risks. At the same time, the key Case B-type risks highlighted in previous surveys – relating to the persistence of a low inflation environment in Armenia, a deteriorating global economic outlook, softening labor market conditions in Armenia, and a potential adjustment in the real estate market – continued to remain on the horizon.

In its March 18, 2025 decision, the Board of the Central Bank of Armenia decided to keep the policy rate unchanged in line with market expectations, communicating that this decision best balanced the need to manage Case A and Case B-type risks. This messaging sent a clear signal to markets that the policy direction remained unchanged, and that a gradual and measured reduction of the policy rate best balanced the need to manage the prevailing risks. In the survey conducted immediately following the March decision, the expected path of the policy rate remained broadly unchanged, reaffirming market expectations of a gradual reduction of the policy rate at a measured pace. In this context, compared to the previous survey, the share of participants expecting a lower one-year ahead policy rate declined significantly, with around 80% of participants expecting the rate to stabilize in the range of 6.0%–6.5%. This suggested that market participants were broadly aligned in their view that the next steps in the policy rate path would be gradual and measured.

Figure 3.B.4a. Expected path of the CBA Policy Rate

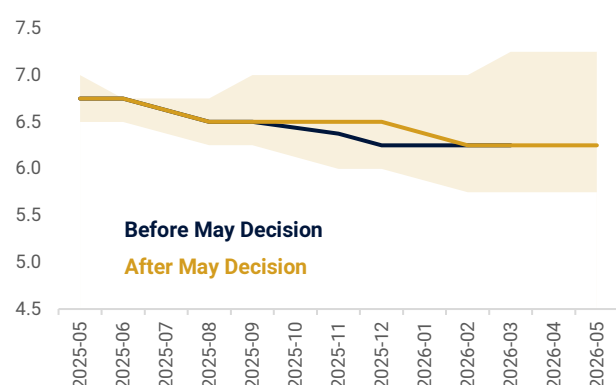
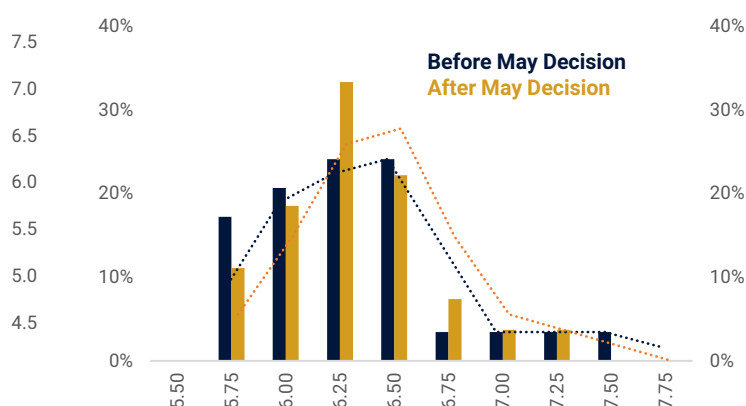


Figure 3.B.4b. Evolution of market expectations for the one-year ahead policy rate



Prior to the May 2025 decision, financial market participants continued to expect a gradual reduction of the policy rate at a measured pace over the one-year ahead horizon. The upside considerations underpinning market expectations related to a potential escalation of global and regional geopolitical tensions, the formation of elevated demand conditions in Armenia, global neutral rate uncertainty, an acceleration of inflationary pressures stemming from the global economy, and other factors. At the same time, the key downside considerations related to the persistence of a low inflation environment in Armenia, a deteriorating global growth outlook, a weakening of demand conditions in the domestic economy, and other related factors. As presented in Figure 3.B.4b, a degree of divergence among market participants regarding the pace and scale of policy rate reductions persisted.

In its May 6, 2025 decision, **noting a greater likelihood of Case B-type scenarios materializing, while also emphasizing the need to manage the macroeconomic implications stemming from Case A-type scenarios**, the Board of the Central Bank of Armenia decided to keep the refinancing rate unchanged. The communications underlying the current decision differed significantly from those of prior decisions, signaling to markets a shift in the risk management approach. In this messaging, the Board emphasized that while there was a greater likelihood of scenarios materializing that would imply a lower policy rate path relative to market expectations, the Board nonetheless found it appropriate to maintain a degree of caution, taking into account the potential macroeconomic implications stemming from Case A-type scenarios. The survey conducted following the May decision indicated that the expected path of the policy rate remained broadly unchanged. In other words, markets continued to expect a gradual reduction of the policy rate, with the rate stabilizing at around 6.25% over the one-year horizon. This pattern in the evolution of expectations suggests that the current rate decision and forward guidance did not come as a surprise to financial markets and had already been priced into their expectations.

Figure 3.B.5a. Expected path of the CBA Policy Rate

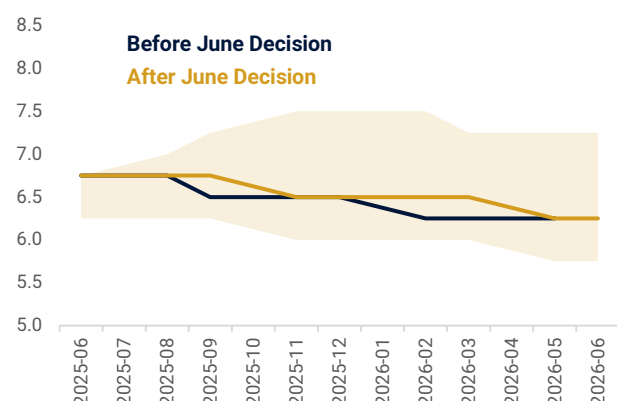
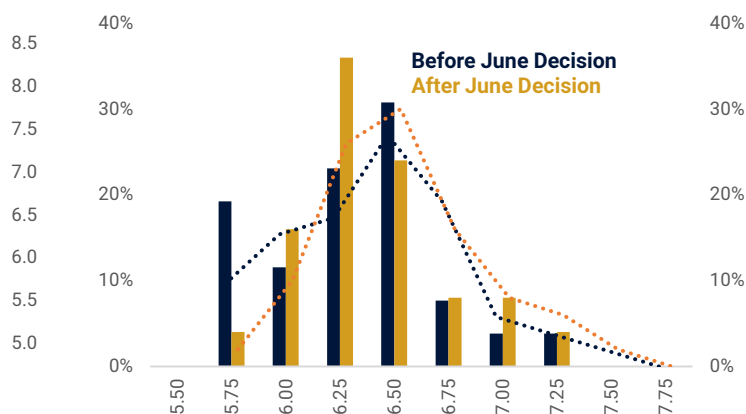


Figure 3.B.5b. Evolution of market expectations for the one-year ahead policy rate



Prior to the June decision, financial market participants continued to expect a gradual reduction of the policy rate at a measured pace. The key upside considerations underpinning the expected path of the policy rate related to uncertainty around Armenia's country risk premium, risks of a highly expansionary fiscal stance, a possible acceleration of inflationary pressures transmitted from the global economy, a potential escalation of geopolitical tensions, and other related factors, while the key downside considerations were primarily associated with expectations of a deteriorating global economic outlook, as well as risks of a potential weakening of domestic demand conditions.

In its June 17, 2025 decision, **noting the build-up of Case A-type risks and emphasizing the need to minimize the losses that could stem from those scenarios materializing**, the Board of the Central Bank of Armenia decided to keep the refinancing rate unchanged. This messaging by the CBA sent a clear signal to markets that the need to manage Case A-type risks warranted a higher policy rate path over the medium-term horizon relative to market expectations. Even as market expectations regarding the expected path of the policy rate remained broadly unchanged immediately following the June decision, the share of participants expecting a lower one-year ahead policy rate declined compared to the previous survey. This likely suggests that markets absorbed the rationale underlying the Board's decision and its forward guidance, and adjusted their expectations accordingly. In this context, the majority of market participants expected the policy rate to stabilize at around 6.25%–6.50% over the one-year horizon.

Prior to the August decision, financial market participants continued to expect a gradual reduction of the policy rate, with the rate stabilizing at around 6.25%–6.50% over the one-year horizon. In this context, the key upside considerations cited by financial market participants were associated with an escalation of tensions in geopolitical and international trade relations and rising overall economic uncertainty, while the key downside considerations — primarily relating to a slowdown in demand conditions in Armenia — continued to remain relevant.

Figure 3.B.6a. Expected path of the CBA Policy Rate

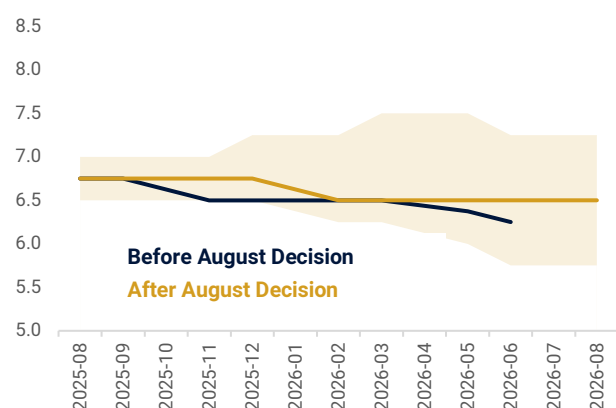
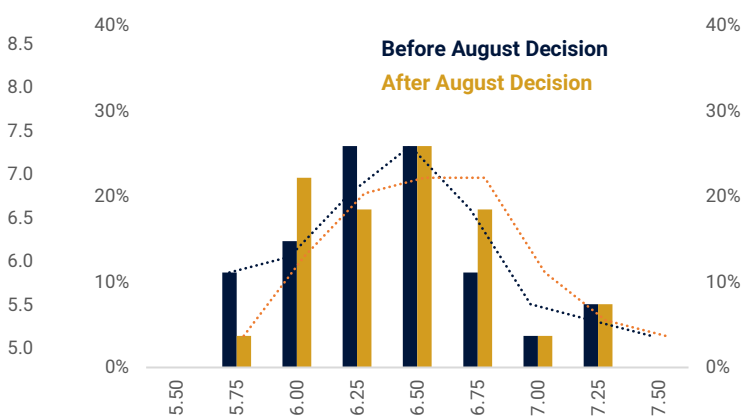


Figure 3.B.6b. Evolution of market expectations for the one-year ahead policy rate



In its August 5, 2025 decision, **noting the build-up of Case A-type risks and emphasizing the need to minimize the losses that could stem from those scenarios materializing**, the Board of the Central Bank of Armenia decided to keep the refinancing rate unchanged. This messaging by the CBA continued to signal to markets that the need to manage Case A-type risks warranted a higher policy rate path over the medium-term horizon relative to market expectations. The survey conducted immediately following the decision indicates that markets responded promptly to the CBA's forward guidance, with the expected path of the policy rate shifting upward, reflecting expectations of the rate stabilizing at a higher level of 6.50% over the one-year horizon. It is worth noting that while the majority of market participants priced in a moderate reduction of the policy rate in their expectations regarding the policy rate path, a group of participants nonetheless expected the rate to remain at its current level or even increase somewhat relative to the current level. This could reflect growing concerns among market participants regarding Case A-type risks.

In the survey conducted prior to the September 2025 decision, market participants continued to broadly expect a gradual easing of the policy rate, with the rate stabilizing at around 6.25% over the one-year horizon. In this context, while the majority of respondents expected a gradual easing path, around 20% of participants expected a reduction of the policy rate by 25 basis points over the one-year horizon, while a comparable share of around 20% expected the rate to remain at its current level. The divergence among market participants regarding the future trajectory of the policy rate could be attributable to differing interpretations of current economic developments and underlying conditions prevailing in the market. Specifically, the key upside considerations cited by market participants in the survey related to risks of expansionary fiscal stance in Armenia, uncertainty around the country risk premium, a broadening of inflationary pressures transmitted from the global economy, the persistence of geopolitical tensions, the potential formation of excess demand conditions in the domestic economy, and other related factors. On the other hand, the key downside considerations related to a deteriorating global growth outlook, a slowdown in external demand, a correction in the real estate market, and other related factors.

Figure 3.B.7a. Expected path of the CBA Policy Rate

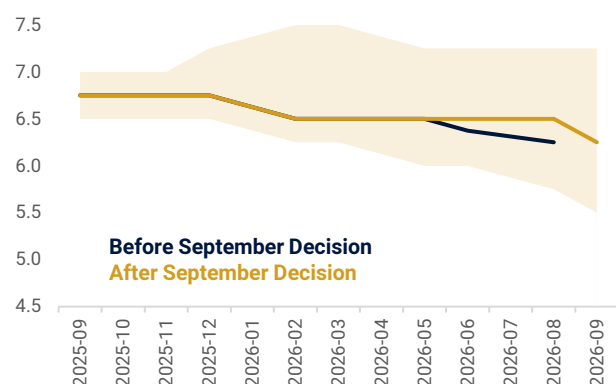
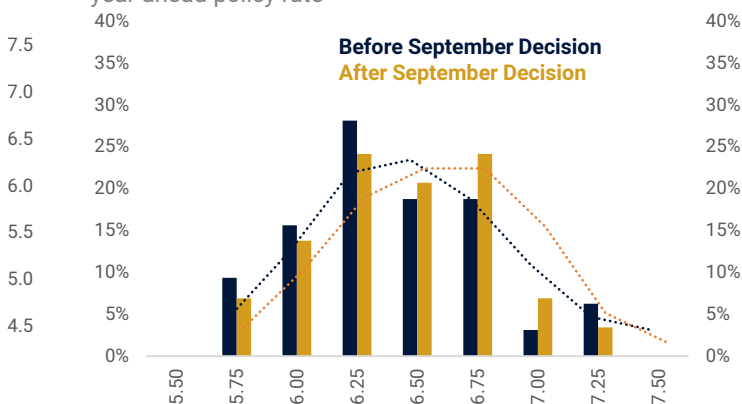


Figure 3.B.7b. Evolution of market expectations for the one-year ahead policy rate



In its September 16, 2025 decision, **emphasizing the need to minimize the losses that could stem from Case A-type scenarios materializing**, the Board of the Central Bank of Armenia decided to keep the refinancing rate unchanged. In this context, the Board continued to communicate that the need to manage Case A-type risks warranted a higher policy rate path over the medium-term horizon relative to market expectations. The survey conducted following the decision indicates that, alongside a decline in the share of participants expecting a path of gradual and measured easing, an increase was observed in the share of participants expecting the policy rate to remain at its current level or, in some cases, to increase – which could suggest that the CBA's communications were effective and clearly conveyed to the market.

Figure 3.B.8a. Expected path of the CBA Policy Rate

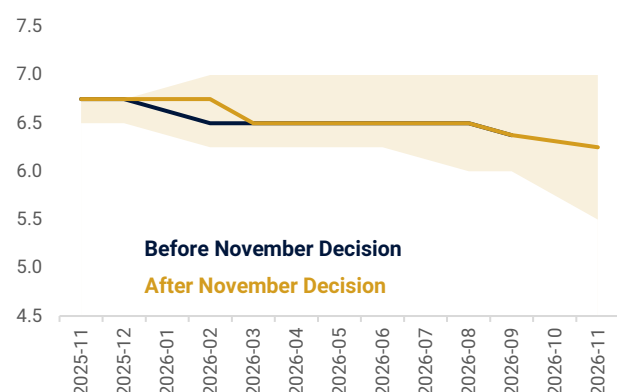
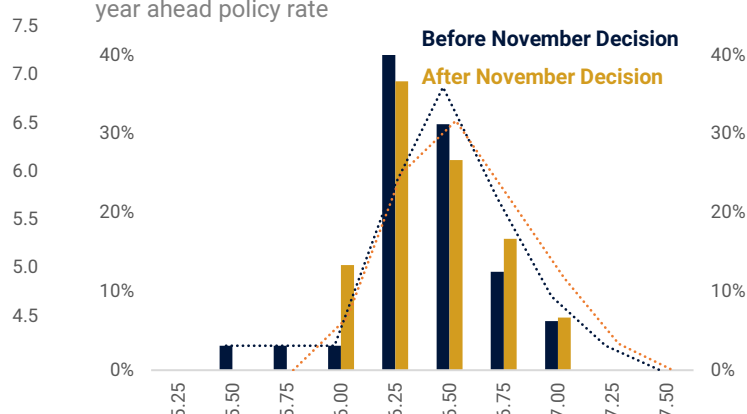


Figure 3.B.8b. Evolution of market expectations for the one-year ahead policy rate



The survey conducted prior to the November decision shows that financial market participants expected a gradual easing of the policy rate at a measured pace over the one-year horizon, with the rate stabilizing at around 6.25%. While market participants were broadly aligned in expecting a reduction of the policy rate by 25–50 basis points over the course of the year, a smaller subset of participants nonetheless anticipated a more significant reduction, while some participants did not rule out a modest increase relative to the current level. The key upside considerations underpinning the above assessments related to an acceleration of the inflationary environment in the domestic economy, the formation and deepening of excess demand conditions in the economy, uncertainty around the country risk premium, the persistence of geopolitical uncertainties, and other related factors. On the other hand, the key downside considerations were associated with a deteriorating global growth outlook and a potential weakening of external demand.

In its November 4, 2025 decision, **emphasizing the need to minimize the losses that could stem from Case A-type scenarios materializing**, the Board of the Central Bank of Armenia decided to keep the refinancing rate unchanged at the current policymaking cycle. Over the course of the recent decisions, the Board continued to communicate that the need to manage Case A-type risks warranted a higher policy rate path over the medium-term horizon relative to market expectations. In this context, compared to the previous survey, the expected path of the policy rate remained unchanged, reflecting expectations of the rate stabilizing at around 6.25%–6.50% over the one-year horizon. As reflected in Figure 3.B.8b, the majority of market participants continued to expect a path of gradual and measured easing, while distinct groups remained inclined toward scenarios of the policy rate remaining at its current level or, in some cases, a possible increase.

Figure 3.B.8a. Expected path of the CBA Policy Rate

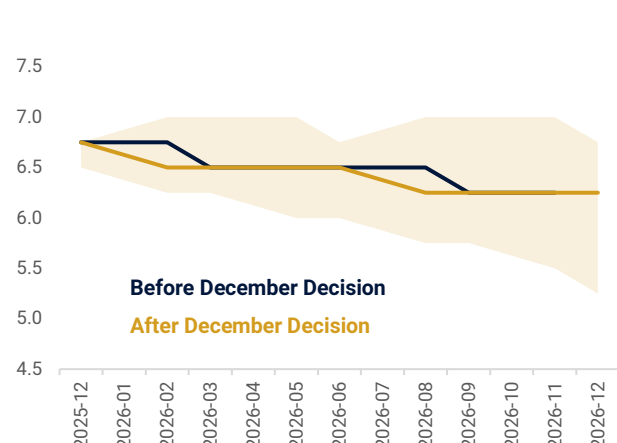
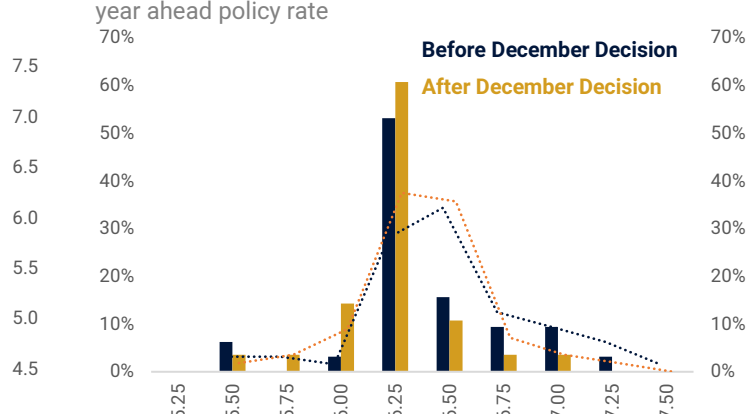


Figure 3.B.8b. Evolution of market expectations for the one-year ahead policy rate



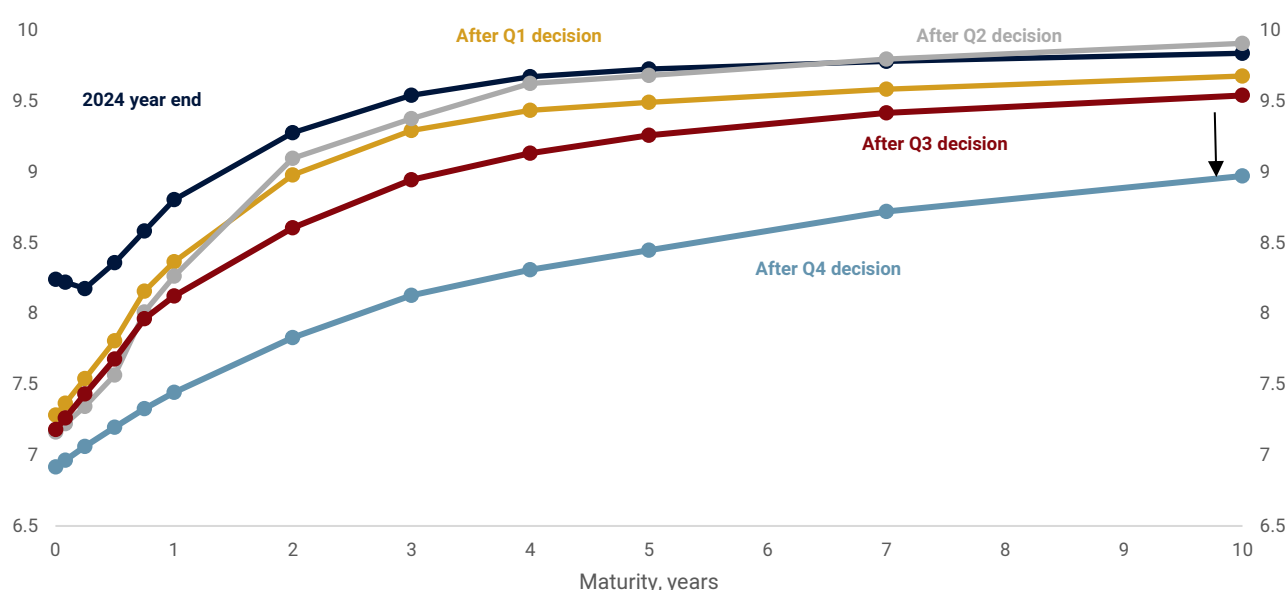
The survey conducted prior to the December decision shows that market participants expected a gradual easing of the policy rate at a measured pace, with the rate stabilizing at around 6.25% over the one-year horizon. While the majority of participants expected a path of gradual rate reductions, around 40% of respondents nonetheless anticipated a slower pace of easing or did not rule out a possible increase relative to the current level. This suggests that a growing share of market participants assigned greater weight to scenarios of a broadening inflationary environment in the economy, accordingly placing a higher probability on the possibility of a more conservative or even tightening policy path. In this context, the key upside considerations were associated with a broadening of inflationary pressures transmitted from the global economy and an expansion of demand conditions in the economy. At the same time, the key downside considerations were associated with a deteriorating global growth outlook and a potential weakening of external demand.

In its December 16, 2025 decision, balancing the need to manage Case A and Case B-type risks, the Board of the Central Bank of Armenia decided to reduce the policy rate in line with market expectations. This marked the first change in official communications since the preceding four decisions, signaling a shift in the risk management approach. Specifically, whereas in prior decisions the Board had emphasized the need to manage Case A-type risks – which could have required a higher policy rate path relative to market expectations over the medium term – the risk management approach underlying the most recent decision reflected a more balanced approach, emphasizing the need to manage the macroeconomic implications stemming from Case B-type scenarios as well. This messaging sent a clear signal to markets that the CBA's actions reflected a balanced approach to the assessment of risks, and that a gradual and measured reduction of the policy rate was consistent with market expectations. The survey conducted immediately following the December decision shows that the share of participants expecting a slower pace of rate reductions or even a possible increase relative to the current level declined significantly compared to the previous survey, from 38% to 18%. This suggests that the CBA's communications were effective and clearly absorbed by markets. At the same time, the majority of participants (around 60%) expected the policy rate to stabilize at around 6.25% over the one-year horizon, suggesting that market participants were broadly aligned in their view that the next steps in the policy rate path would be gradual and measured.

C. Yield Curve

Over the course of 2023, against the backdrop of the external demand shock, an elevated inflationary environment, as well as geopolitical developments and expectations of a more expansionary fiscal stance, the yield curve shifted upward. Over the course of 2024, alongside the gradual neutralization of the above-mentioned factors, the gradual adjustment of inflation expectations, and the continued reduction of the policy rate, the yield curve declined considerably across all maturities. In Q1 2025, the yield curve shifted downward. This reflected, on one hand, a reduction in market participants' expectations regarding the refinancing rate trajectory, and on the other hand, a possible reevaluation of macroeconomic risks. This, in particular, may reflect a reconsideration of risks related to debt stabilization and financing of the fiscal deficit, as well as certain external factors, such as uncertainties surrounding long-term interest rates in the United States, a reduction in risk premiums due to recent geopolitical developments, and so on.

Figure 3.C.1. Developments in the Yield Curve in 2025



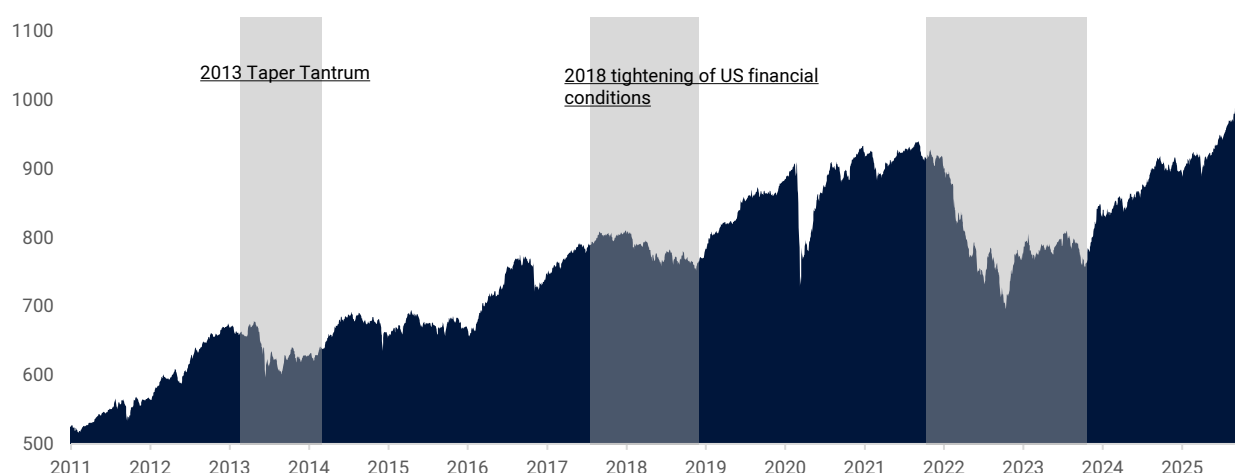
Source: CBA

Over the course of the second quarter, the yield curve remained broadly stable, though modest upward shifts were observed in the longer-term portion of the curve. This may reflect expectations of a slight increase in long-term interest rates, as well as a possible reassessment of perceptions related to macroeconomic risks. In the third and particularly the fourth quarter, a significant downward shift was observed across all maturities of the yield curve, most pronounced in the longer-term portion of the curve. These developments in the yield curve reflected the impact of a number of factors, including:

- a) **Improvement in overall sentiment toward emerging market economies (EMEs):** Against the backdrop of heightened policy uncertainty in advanced economies, and ongoing structural reforms in EMEs, country risk premia have declined significantly. In this context, key uncertainties relate to whether the compression in EME risk premia reflects an improvement in economic fundamentals or is instead driven by overoptimism. Historically, EMEs have exhibited greater sensitivity to global economic shocks. Nevertheless, in recent years most emerging market economies have demonstrated considerable resilience in the face of economic shocks, as reflected in lower volatility of output and

inflation. In this context, institutional and structural reforms undertaken in EMEs, increased credibility of monetary policy, and fiscal sustainability have provided a solid foundation for maintaining macroeconomic stability. At the same time, the development of domestic capital markets has contributed to reducing reliance on foreign capital, as reflected in a significant increase in the share of local currency-denominated bond issuance, thereby somewhat mitigating countries' vulnerability to global economic shocks. In addition, the application of macroprudential tools and improvements in financial regulatory frameworks have significantly helped to contain the potential impact of capital outflows and exchange rate volatility risks. In 2025, the tightening of trade policy by the new U.S. administration, the planned widening of the fiscal deficit, and concerns regarding debt sustainability have become significant sources of concern about a broadening global inflation environment and a possible increase in the U.S. long-term neutral interest rate. As a result, traditional "safe haven" assets for investors, including government bonds of the United States and other advanced economies, have become less attractive. Amid such uncertainties, overall sentiment toward emerging market economies with stable macroeconomic environments, strong financial systems, and more effective economic policies has improved. Although these fundamental reforms have played a major role in supporting the improvement in sentiment toward EMEs, the possibility cannot be ruled out that the observed improvement in sentiment and the decline in risk premia are driven by cyclical or opportunistic factors. In this context, it is worth noting that developments over the past decades indicate that historically, advanced economies have been quite vulnerable to global economic shocks. During periods of global economic turbulence, sentiment has historically deteriorated sharply, accompanied by capital outflows and increases in risk premia (see Figure 3.C.2).

Figure 3.C.2. The EMBI index during periods of tightening global financial conditions



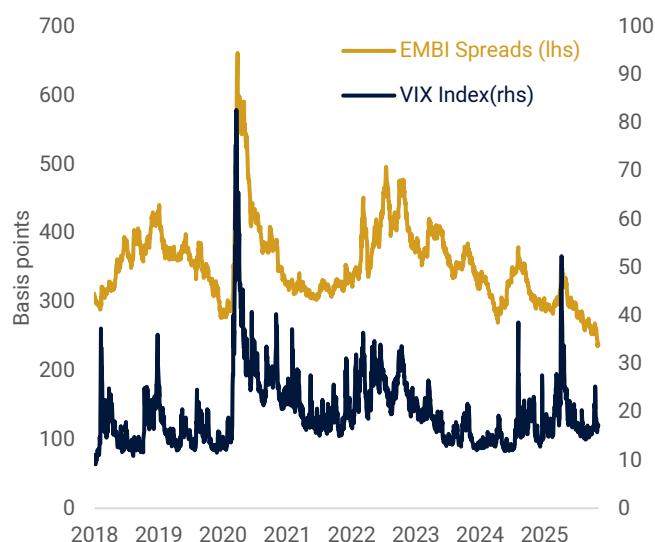
Source: Bloomberg

b) Impact of domestic factors: structural and long-term determinants, including:

- Adjustment of long-term inflation expectations due to the reduction of the inflation target since the beginning of the year:** Recent developments and achievements in Armenia's economy and monetary system have provided a solid foundation for the Central Bank of Armenia to continue strengthening public confidence in monetary policy, developing the monetary policy framework, and implementing broad-based, long-term reforms. This includes setting a lower inflation target consistent with both the perception of price stability and the current structure of the financial system. In this context, in 2025 the Central Bank of Armenia reduced the inflation target from 4% to 3%. Since the adjustment of the inflation target, various indicators—including measures of inflation expectations and underlying inflation—suggest that the shift toward the new target occurred relatively quickly (see Chapter 4 for more details). The reduction in the inflation target, together with the corresponding adjustment in market participants' inflation expectations, may have contributed to a downward shift in the yield curve.
- Expansion of the tradable sector's capacities and fundamental appreciation of the exchange rate:** Since 2022, strong and sustained growth in production capacity and competitiveness indicates the emergence of a new equilibrium level in the economy. In this context, strong growth in productivity and export capacities has contributed to an acceleration in potential GDP growth. Moreover, numerous studies (see Lee and Tang, 2003) indicate that in small, open economies, growth in productivity and export capacity—when accompanied by improvements in the investment climate and stable, robust capital inflows—can support the fundamental (trend) real exchange rate appreciation in the economy (see Chapter 1, Section A) and contribute to a downward shift in the yield curve.

Against the backdrop of policy uncertainty in advanced economies on the one hand, and structural reforms in emerging market economies on the other, risk premiums across emerging markets declined substantially.

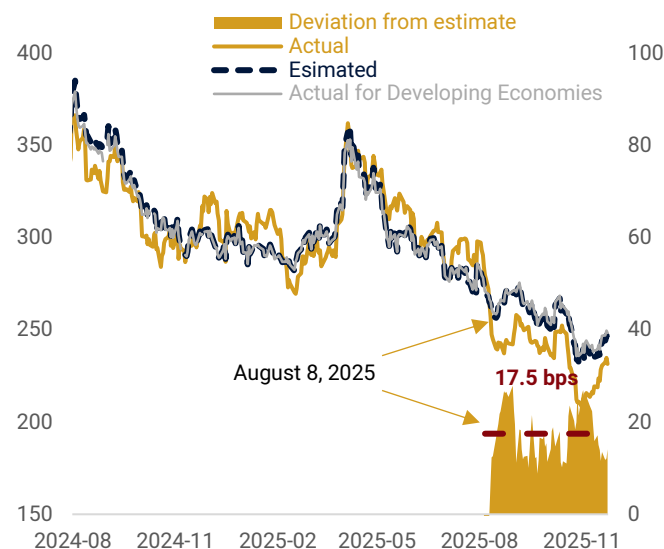
Figure 3.C.3. EMBI spread



Source: Bloomberg, FRED

Developments in Armenia's country risk premium have been broadly in line with trends observed across emerging market economies, though the influence of Armenia-specific factors has also been evident

Figure 3.C.4. Developments in Armenia's country risk premium



Source: CBA

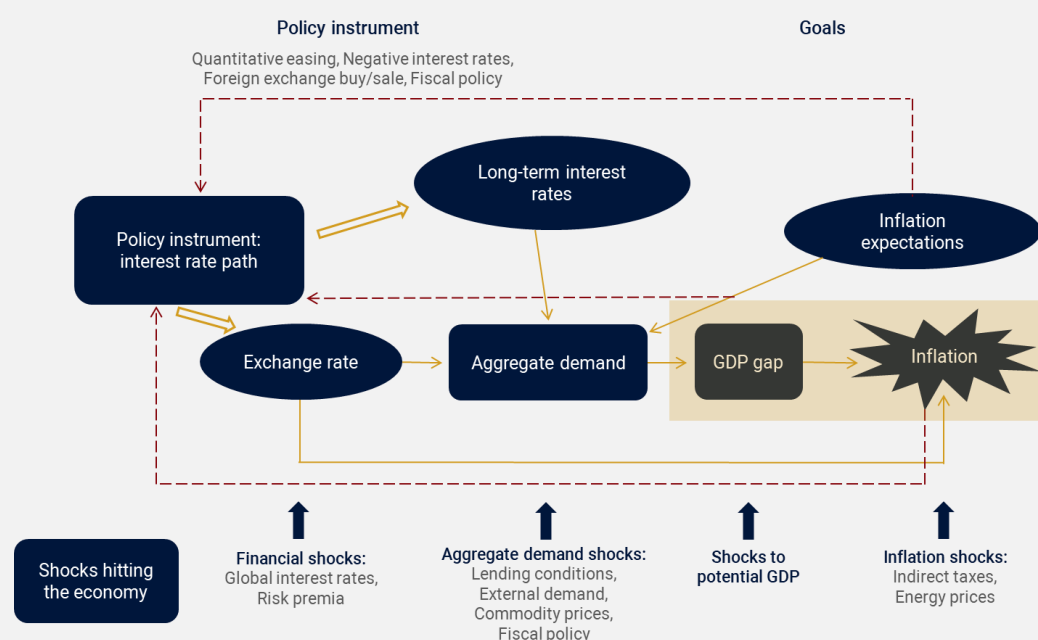
* CBA estimates based on 2023–2025 developments

- **An improvement in expectations regarding the trajectory of public debt.** Over 2025, the key uncertainties surrounding fiscal policy were linked to potential revenue underperformance and expenditure growth, which could have resulted in a more expansionary fiscal impulse on aggregate demand and a widening of the budget deficit. This, in turn, could have exerted upward pressure on the country risk premium and long-term government bond yields. Over the course of the year, robust revenue performance supported by improvements in tax administration, a significant improvement in the composition of expenditures, as well as the fiscal consolidation planned from 2026, substantially alleviated concerns surrounding fiscal policy. As a result, the improvement in expectations regarding the trajectory of public debt may have exerted a favorable influence on the downward shift of the long end of the yield curve
 - **The gradual transmission of monetary policy to the economy** (see Box 2 and Box 3).
- c) Impact of Armenia-specific factors, *non-structural factors*, such as the **increase in AMD liquidity in the financial market resulting from a reduction in the reserve requirement**. An increase in AMD liquidity in the financial market may have contributed to greater demand for government bonds, thereby putting downward pressure on yields. Unlike structural factors, the impact of these factors may prove to be temporary.

Box 2. Monetary Policy Transmission mechanism

Monetary policy involves making decisions regarding the policy tools, while the monetary transmission mechanism describes how these instruments impact the economy. Monetary policy decisions influence other interest rates in the economy, which in turn affect the behavior and decisions of economic agents through various channels, ultimately feeding through into developments in aggregate demand and inflation. It is worth noting that changes in the expected path of policy rates are transmitted to the economy gradually, and therefore the full impact of monetary policy on the economy and inflation takes time to materialize. In pursuit of their primary objective of ensuring price stability, central banks may adopt various monetary policy regimes, including inflation targeting, exchange rate targeting, monetary aggregate targeting, and others. Under an inflation targeting regime, central banks consistently adjust the policy rate in order to anchor inflation and inflation expectations over the medium-term horizon. The primary channels through which monetary policy influences the economy are the interest rate, exchange rate, and inflation expectations channels (see Figure B.2.1).

Figure B.2.1. MP transmission mechanism



The interest rate channel is an important component of the monetary policy transmission mechanism. Expectations regarding the policy rate have a significant impact on long-term interest rates. When the CBA makes a decision regarding the refinancing rate, it influences short-term interbank interest rates, which in turn, as the price of liquidity, can be transmitted to short-term deposit and lending rates. In this context, expectations regarding the policy rate are of critical importance, as they directly influence long-term interest rates, thereby affecting the decisions of households and firms.

The exchange rate channel is of particular importance for small open economies such as Armenia. Changes in interest rates influence the returns on financial assets, including the currency exchange rate. A higher policy rate typically makes local currency-denominated bonds more attractive, leading to an appreciation of the national currency. This, in turn, influences the trade balance and inflation through changes in import and export prices, as well as external demand. This channel becomes particularly important in economies where a significant share of domestic consumption goods is imported. In such cases, exchange rate fluctuations have a direct impact on inflation, as changes in the exchange rate are rapidly passed through to the prices of imported goods. This also underscores the sensitivity of such economies to external shocks.

Inflation expectations, which are also dependent on confidence in the central bank, represent another important element of the transmission mechanism. The success of monetary policy depends to a significant extent on the inflation expectations of economic agents. These reflect the perceptions of individuals, households, businesses, and financial markets regarding the anticipated level of future inflation. These expectations play an important role in the economic decision-making process. Through its monetary policy decisions and communications, the central bank can influence the inflation expectations of the public, and thereby exert an impact on aggregate demand and inflation. In this context, the Central Bank pays close attention to inflation expectations, as they directly influence the effectiveness of monetary policy. When inflation expectations are well-anchored, it is easier to manage inflation through adjustments to the policy rate and other policy instruments – which is also consistent with the concept of credibility. Conversely, when inflation expectations are significantly above the inflation target, the central bank must resort to more restrictive measures in order to bring inflation under control.

Box 3. How does Monetary Policy Impact Some Market Rates?

A government bond yield curve represents the relationship between the yields on sovereign bonds and their maturities at a given point in time. It is essentially a graphical illustration of how markets price the cost of borrowing over different time horizons, combining information about expected future short-term interest rates and compensation for holding longer-term risk. While short-term instruments are closely tied to domestic monetary conditions, longer-term yields embed expectations about the future path of monetary policy, long-term inflation expectations, as well as underlying structural factors in the economy, such as productivity growth, fiscal sustainability, and broader risk factors. Developments in the yield curve therefore provide an important lens into financial conditions in the economy over the year.

Monetary policy affects the economy through several channels. A detailed discussion of the monetary policy transmission mechanism—including the interest rate channel, credit channel, exchange rate channel, and others—can be found in Box 2 and Section 5 of this report. In this section, we focus only on the general aspects of transmission that are most relevant for understanding and interpreting movements in the yield curve.

The central bank most directly influences the short end of the yield curve, where interest rates closely reflect the current policy rate and the price of short-term liquidity, such as yields on short-term government securities or deposit rates. The cost of short-term liquidity, however, has only a limited effect on long-term yields, which are shaped more by expectations about the future path of policy rates, the equilibrium (neutral) interest rate, long-term inflation expectations, term premium, and other structural and risk factors. Consider a credible central bank that responds aggressively to economic shocks by implementing short-term policy adjustments aimed at maintaining price stability over the longer horizon. When inflation expectations are well anchored, changes in short-term interest rates may produce little to no movement in long-term yields. This means that many of the fundamental factors that drive long-term yields—including long-term inflation expectations and the neutral rate—do not exhibit volatility in the face of short-term economic shocks, a relationship that is explored in greater detail in Section 4. In other words, the absence of large movements in long-term rates is a sign of an effective and credible monetary policy regime.

International evidence supports this maturity-specific pattern. In advanced economies such as the United States (especially pre-2020), as well as in several emerging markets with credible monetary frameworks, temporary adjustments in policy rates have often led to modest or negligible movements in long-term yields. This reflects the strong anchoring of inflation expectations, market confidence in the central bank's commitment to price stability, and the forward-looking nature of long-term rates. In the United States, this pattern is supported by high-frequency event studies of monetary policy. These studies show that surprise changes in the policy rate have the largest effects on short-term yields, while the impact diminishes progressively along the yield curve as maturities increase. This evidence reinforces the view that long-term yields are largely determined by expectations of the future path of the policy rate, medium- and long-term inflation, and term premia, rather than by contemporaneous, short-term rate adjustments in response to idiosyncratic shocks. Such findings are consistent with empirical, international experience in economies with credible and transparent central banks (see table B.3.1).

Table B.3.1. Estimated effects of changes in the federal funds rate, forward guidance, and LSAPs on U.S. Treasury yields.

The estimated effects of changes to 3 distinct MP tools on treasury yields (1999-2020)					
	6 Months	2 Years	5 Years	10 Years	30 Years
$\Delta \text{FFR } (\beta_1)$	4.22***	3.65***	2.03*	0.89	0.03
$\Delta \text{FG } (\beta_2)$	2.11**	4.49***	4.60***	3.58***	2.28**
$\Delta \text{QE } (\beta_3)$	0.51*	0.08	-3.22***	-5.28***	-4.31***

Table B.3.2. Estimated effects of changes in the federal funds rate, forward guidance, and LSAPs on U.S. Treasury yields post the zero lower bound (ZLB) constraint period³

The estimated effects of changes to 3 distinct MP tools on treasury yields (2016-2020)					
	6 Months	2 Years	5 Years	10 Years	30 Years
$\Delta \text{FFR } (\beta_1)$	3.12***	4.45***	2.88*	0.69	-1.31
$\Delta \text{FG } (\beta_2)$	1.79**	4.79***	5.12***	3.58***	1.26**
$\Delta \text{QE } (\beta_3)$	0.25	-0.88	-4.08***	-4.92***	-4.21***

The belly of the yield curve, typically representing medium-term maturities, is particularly sensitive to market expectations about the future path of the policy rate. In practice, these expectations can shift meaningfully in response to central bank communications and forward-looking signals that indicate a likely change in the trajectory of monetary policy over coming quarters. As a result, movements in the medium segment of the curve can often reflect how markets interpret the central bank's forward guidance, anticipated policy adjustments, and evolving macroeconomic conditions.

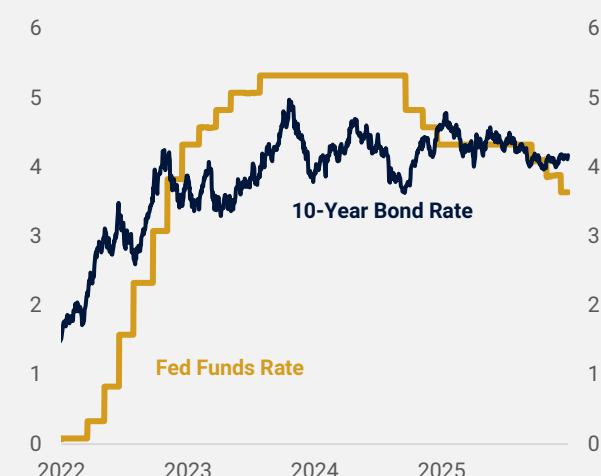
³ Using and extending the high frequency event study framework of Gurkaynak, Sack, and Swanson (2005), the analysis decomposes FOMC announcement surprises into three orthogonal factors: (i) unexpected changes in the federal funds rate target ("target factor"), (ii) forward guidance shocks affecting the expected future path of short term rates ("path factor"), and (iii) large scale asset purchase (QE) shocks. These shocks are identified from changes in interest rate futures and Treasury yields within narrow intraday windows around each FOMC announcement. The estimated shocks are then regressed on changes in Treasury yields across maturities to quantify the immediate effects of conventional and unconventional monetary policy tools on the yield curve.

Interpretation of magnitudes (units): Note: Coefficients from regressions $Y_{m,t} = \beta_1 Z_{1,t} + \beta_2 Z_{2,t} + \beta_3 Z_{3,t} + \epsilon_t$, where t indexes announcements, Y denotes yields for different maturity (m) treasuries. Z_1 , Z_2 , and Z_3 denote the surprise component of changes to the three monetary policy tools. Coefficients are in units of basis points per standard deviation change in the monetary policy instrument. Asterisks ***, **, and * denote statistical significance at the 99, 95, and 90 percent confidence levels respectively. An alternative and simpler way of interpreting the coefficients: multiply the rows of FED FUNDS RATE and FORWARD GUIDANCE by 3 and 4.4 to get the coefficients in units of basis points per 25 basis point exogenous shocks to the changes to respective policy announcement.

Moreover, because the *expected* path of the policy rate and long-term inflation expectations play such a fundamental role in determining medium- and long-term yields, credible central banks place a very high degree of emphasis on providing maximum transparency about central bank policy actions. High transparency helps markets develop better-informed expectations and reduces uncertainty about *policy* itself, in this sense helping to minimize volatility in long-term yields. Further, the long end of the yield curve is influenced not only by expectations of future short term rates but also by term premia and risk compensation demanded by investors. In advanced economies, large-scale asset purchase programs or quantitative easing have at times been used to explicitly influence longer term yields through this channel. In Armenia, such central bank balance sheet tools are not part of the standard monetary policy toolkit, which implies that longer term yields may be relatively more influenced by movements in various risk premia, global conditions, and longer run expectations than by the policy rate alone.

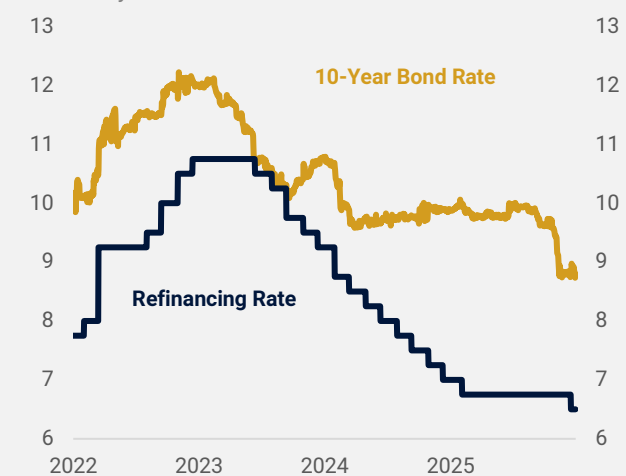
Movements in Long-Term Government Bond Yields Can Convey Important Messages about Policy Credibility

Figure B.3.1. United States: 10-Year Bond Rate and Fed Funds Rate



Source: FRED

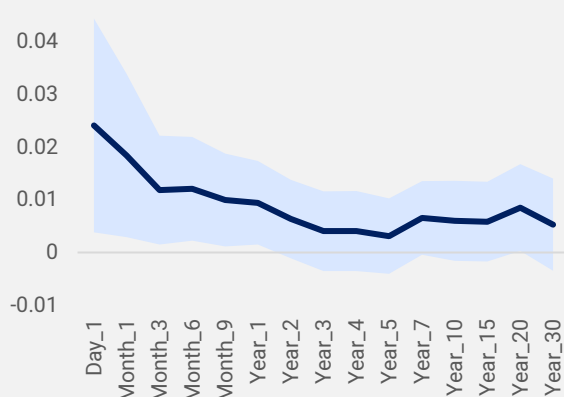
Figure B.3.2. Republic of Armenia: 10-Year Bond Rate and CBA Policy Rate



Source: CBA

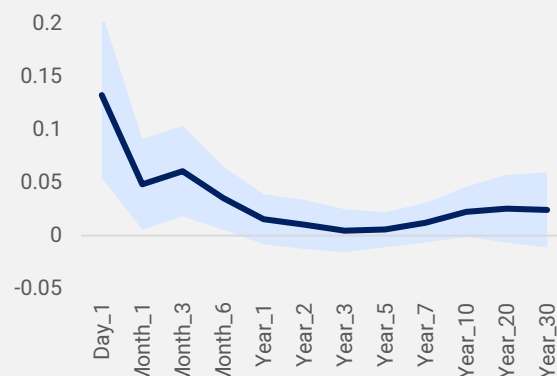
Long-term government yields in many advanced and emerging market economies had drifted meaningfully upward in response to the global inflationary surge post-Covid, which was compounded in Armenia by a significant external demand shock in 2022-23 as well as regional geopolitical tensions. The fact that long-term yields increased across the board could reflect a number of factors, including upward drifts in inflation expectations as well as expectations of higher long-term neutral rates. Beginning in 2023, as the economic condition stabilized in Armenia and the Central Bank of Armenia began its loosening cycle, long-term bond rates began to decline considerably as well. This spoke to the credibility and efficacy of the monetary policy regime: while inflation expectations had indeed increased post-2020, contributing to a rise in long-term bond yields, they quickly re-anchored in response to a forceful policy response and a clear commitment to the price stability mandate. On the other hand, in many advanced economies such as the United States, this dynamic did not hold, and when the Federal Reserve entered a loosening cycle in late 2024, 10-year bond rates remained stubbornly elevated. Several hypotheses could explain this development, namely: (1) longer-term inflation expectations were not fully anchored to the target even as the central bank entered a loosening cycle, reflecting sustained difficulty in the “last mile”; (2) the long-term neutral rate had drifted meaningfully upward, largely in response to concerns about rising government debt and a more persistent inflationary environment; and (3) concerns about perceived “riskiness” of these assets, in response to US economic policy and concerns about fiscal sustainability.

Figure B.3.3. Armenian yield volatility reaction to monetary policy decisions



Source: CBA Calculations

Figure B.3.4. Kazakhstan's yield volatility reaction to monetary policy decisions



Source: CBA Calculations

Over the past year, movements in the short end of the yield curve were broadly consistent with the central bank's ability to influence short-term market conditions through policy decisions and credible communications. At the beginning of 2025 the short end of the yield curve declined in response to the policy rate reduction, as markets adjusted their expectations regarding the near-term trajectory of monetary policy.

The easing occurred in an environment of moderate inflation, stabilizing inflation expectations in line with the reduction of the target for inflation from 4% to 3%, stabilizing labor market conditions, and cooling external demand, all of which helped alleviate concerns about sustained demand pressures. As the year progressed and the policy rate was kept unchanged, short term yields remained broadly stable, reflecting balanced risks: inflation temporarily increased due to supply-side factors, but domestic demand conditions were assessed as largely neutral and expectations rather quickly anchored to the new target. In the fourth quarter, short term yields declined again in line with the December policy rate cut. By that time, inflation had moderated, external risks to growth had intensified, and short to medium term domestic demand pressures had softened. Overall, movements in the short end of the yield curve during 2025 closely followed monetary policy decisions and evolving expectations regarding the near term policy path.

To assess the responsiveness of the short end of the yield curve in a way that is easy to interpret, it is useful to compare market behavior around monetary policy decision dates with market behavior on other days. The evidence from Armenia indicates that the repricing activity around decisions is concentrated at shorter maturities. In particular, estimates of decision day yield volatility responses decline sharply with maturity and appear most clearly positive for very short horizons, suggesting that market participants reassess near term interest rate expectations most actively around monetary policy decisions. This pattern aligns with international evidence, and with evidence from similar countries like Kazakhstan (Figure B.3.3), that interest rates react primarily to the unexpected component of policy decisions and that the strongest effects are generally found at short maturities (Figure B.3.4)⁴

Taken together, developments at the short end over the year suggest that monetary policy actions and communications continued to provide an effective and stabilizing anchor for the economy through short-term market interest rates. In addition, the timing and maturity profile of market reactions indicates that monetary policy decisions play an outsized role in shaping near term expectations, while longer maturities are less tightly linked to monetary policy decisions.

⁴ We estimate the impact of monetary policy (MP) decision dates on yield volatility separately for each maturity along the Armenian yield curve (Day_1, Month_1, ..., Year_30) in order to see which segments of the curve (short end, belly, and long end) react to MP decisions. For each maturity m , we construct a simple, "volatility" proxy as the absolute daily yield change:

$$X_{m,t} = |\Delta y_{m,t}| = |y_{m,t} - y_{m,t-1}|$$

We then run a maturity by maturity event study regression:

$$X_{m,t} = \alpha_m + \beta_m MP_t + \varepsilon_{m,t},$$

where $MP_t = 1$ on policy decision dates and the first trading day after the decision, and $MP_t = 0$ otherwise; standard errors are heteroskedasticity robust. The figure plots the estimated β_m across maturities (solid line), with the shaded band showing the corresponding 95% confidence interval. A positive β_m implies that the typical day to day move in yields at maturity m is larger on MP event windows than on non event days. The key policy relevant result is that this response is concentrated at the short end of the yield curve, while the belly and long end show small effects that are typically not distinguishable from zero, implying that monetary policy decisions primarily move near term rates and transmit only weakly to medium and long term yields.

Interpretation of magnitudes (units): The coefficient β_m is in the same units as the yield series, because $X_{m,t} = |y_{m,t} - y_{m,t-1}|$. Yields are recorded in percentage points (e.g., 7.50), then $\beta_m = 0.025$ means that, on MP decision days (and the next trading day), the average absolute daily yield change at maturity m is about 0.03 percentage points larger, i.e. roughly 3 basis points, than on other days. The average non event $|\Delta y_{m,t}|$ for the 1 month maturity bonds is 0.053 and the estimated $\beta_{1\text{month}} = 0.0183$, then the typical daily move rises to about 0.072 on MP event windows—an increase of 2 bps, or about 35% relative to the non event baseline.

D. Financial Market Rates

Over 2025, financial market rates remained broadly unchanged. During this period, the central bank's policy rate declined gradually by a cumulative 50 basis points. Long-term interest rates are generally less sensitive to monetary policy decisions (see Box 3). It is important to note that several factors play a greater role in influencing the pricing of financial products. These include demand for financial products, competition among commercial banks, perceived borrower risk, inflation expectations, the broader economic outlook, and the country risk premium. Consequently, central bank actions alone, or expectations of future actions, may have only a limited impact on the formation of long-term interest rates. A decline in lending rates is one manifestation of easing financial conditions, but not the only one, as financial conditions may become more accommodative through changes in other indicators of the credit market. In this context, loan volumes expanded over the course of the year across several segments, including consumer loans, credit card lending, and loans financing household purchases, which could point to greater credit availability and an easing of financial conditions. The average maturity of loans extended by 2.2 months, which could point to an improvement in effective borrowing conditions even where nominal rates remained stable. Furthermore, lending to borrowers relying on collateralized loans, as well as to non-resident borrowers, also increased, which could point to a broadening of credit access – this too is indicative of an easing of financial conditions. In this context, developments in Armenia's credit market suggest that borrowing conditions in the economy eased over the course of the year, even though this was not fully reflected in corresponding changes in average lending rates (see Chapter 5, Section 1 for a more detailed discussion).

Figure 3.D.1. Financial Market Interest Rates: AMD Loans to Households

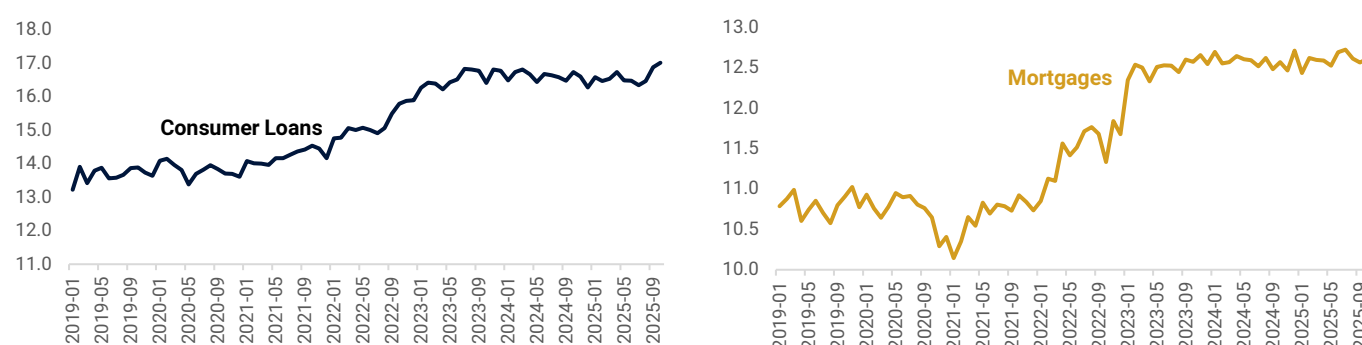


Figure 3.D.2. Financial Market Interest Rates: AMD Loans to Legal Entities (3-Month Moving Average)

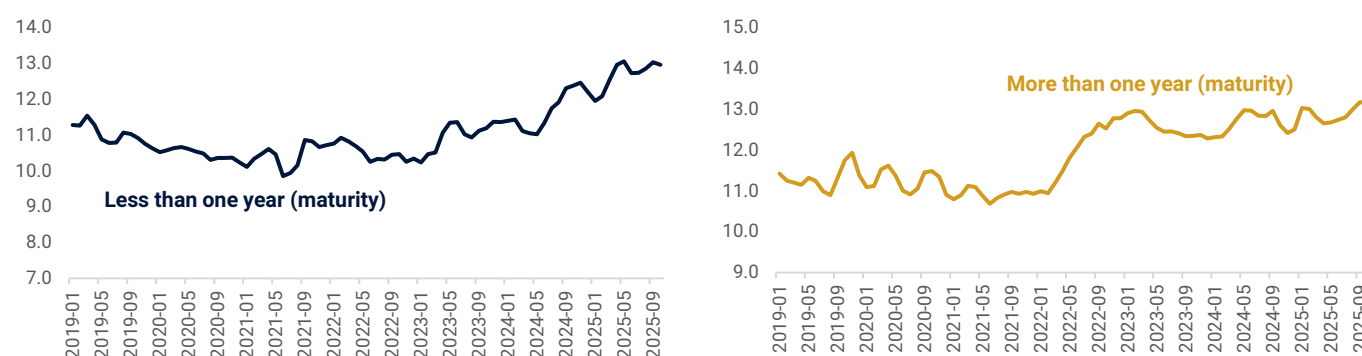
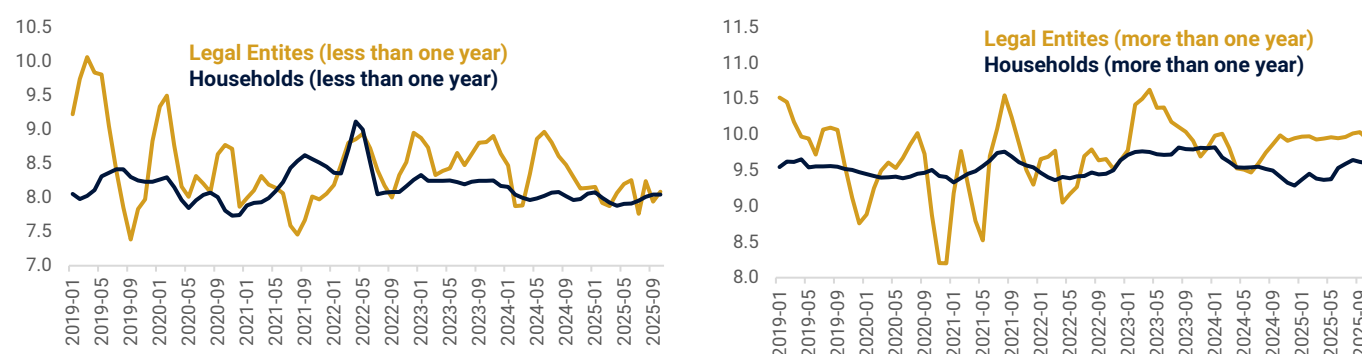


Figure 3.D.3. Financial Market Interest Rates: AMD Deposits (3-Month Moving Average)





Central Bank
of Armenia

04 |

Monetary Policy
Outcomes

Monetary Policy Outcomes

How did inflation expectations evolve over the past year? What does this indicate about the central bank's credibility and the effectiveness of its communication strategies?

Anchored inflation expectations play a critical role in ensuring the effectiveness of monetary policy and, at the same time, inflation expectations remain one of the key factors to measure the success of monetary policy. Since 2006, the Central Bank of Armenia has operated under an inflation-targeting framework. Within this framework, the extent to which the public's inflation expectations are well anchored serves as a key indicator of the Bank's credibility and the effectiveness of its monetary policy. In this context, if expectations are not well-anchored, inflation shocks may have persistent effects, undermining price stability and policy transmission.

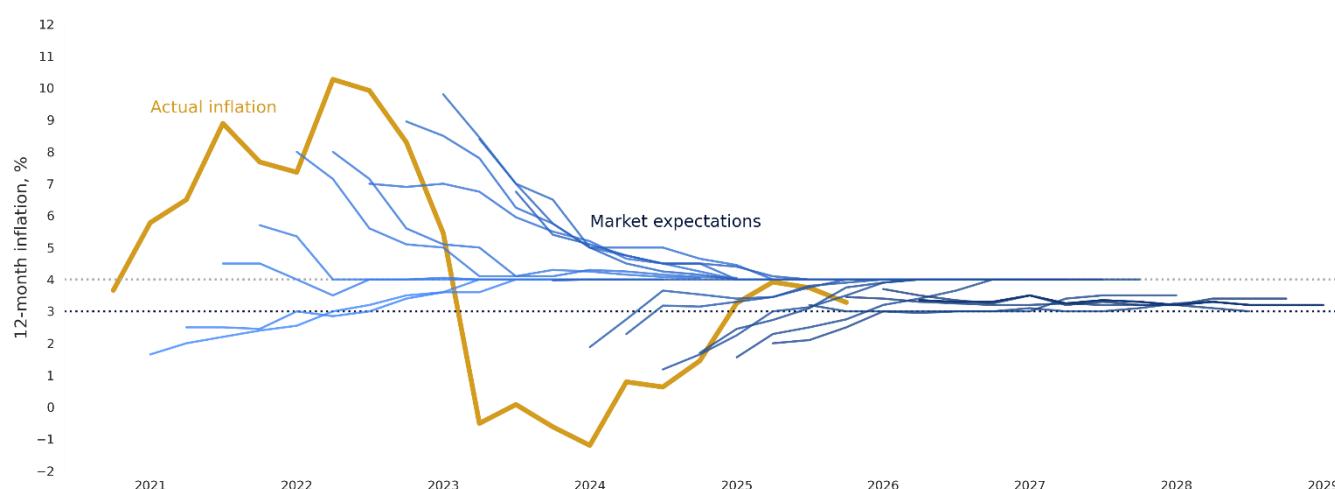
This section presents how inflation expectations have evolved over the past year and what this indicates about trust in the Central Bank and the effectiveness of its communication strategy. Since expectations play a decisive role in shaping central bank credibility, the analysis begins by examining the inflation expectations of financial institutions and households. The analysis then turns to the measurement of credibility itself, presenting two methodological approaches. The first is based on financial dollarization indicators and households' inflation expectations, while the second relies on the non-tradable sticky price index. The latter approach makes it possible to capture underlying inflation dynamics as a slowly adjusting, forward-looking indicator that reflects monetary policy communication and its effectiveness.

Although there is no single definition of the anchoring of inflation expectations, several approaches highlight specific aspects of anchoring. These approaches consider: a) whether financial institutions expect inflation to converge to the target over the long term; b) the degree of dispersion among expectations; c) the extent to which long-term expectations are sensitive to short-term expectations.

For the purpose of conducting the aforementioned study, the results of the Central Bank's quarterly surveys, regularly conducted among financial market participants, were examined. The main objective of these surveys is to collect information from financial market participants (banks, credit institutions, insurance and investment companies, etc.) regarding the macroeconomic environment, economic outlook, and the expected path of the policy interest rate.

Figure 4.1 presents actual inflation developments and the median of inflation expectations of financial market participants from Q1 2021 to Q1 2026. The survey results show that, over a one-year horizon, inflation expectations have been continuously revised in line with changing economic conditions and new information, suggesting that short-term inflation expectations are more sensitive to economic shocks and current events. Nonetheless, even amid high economic uncertainty, medium-term inflation expectations have largely remained stable, centered around the target, which sends a positive signal regarding the credibility and effectiveness of monetary policy.

Figure 4.1. Financial Market Expectations Regarding the Medium-Term Inflation Outlook



Since the transition of the 2025 inflation target from 4% to 3%, market inflation expectations have adjusted fairly quickly toward the new target level. Specifically, having stabilized around the previous 4% target in the fourth quarter of 2024, the median of medium-term inflation expectations gradually declined from around 3.5% starting in the first quarter of 2025, reaching 3.2% by

the first quarter of 2026. Expectations may not yet be fully anchored around the new target, which is consistent with the standard behavioral adjustment mechanism; the speed of their adjustment toward the new target reflects the high credibility of monetary policy and the effectiveness of communication strategies surrounding the change in the target.

Box 4. Inflation target in Armenia

This article presents the main conclusions of the 2024 analytical paper "Inflation Target in Armenia" by H. Avetisyan, H. Igityan, and A. Papikyan.

In order to define and achieve its price stability mandate, the Central Bank of Armenia is guided in the medium term by the inflation target which is consistent with this mandate. However, ensuring price stability is not limited to setting a numerical target. It is a dynamic and continuous process that requires a comprehensive, forward-looking monetary policy strategy, a well-developed and flexible toolkit, high standards of transparency, communication, and accountability, as well as an effective policy transmission mechanism.

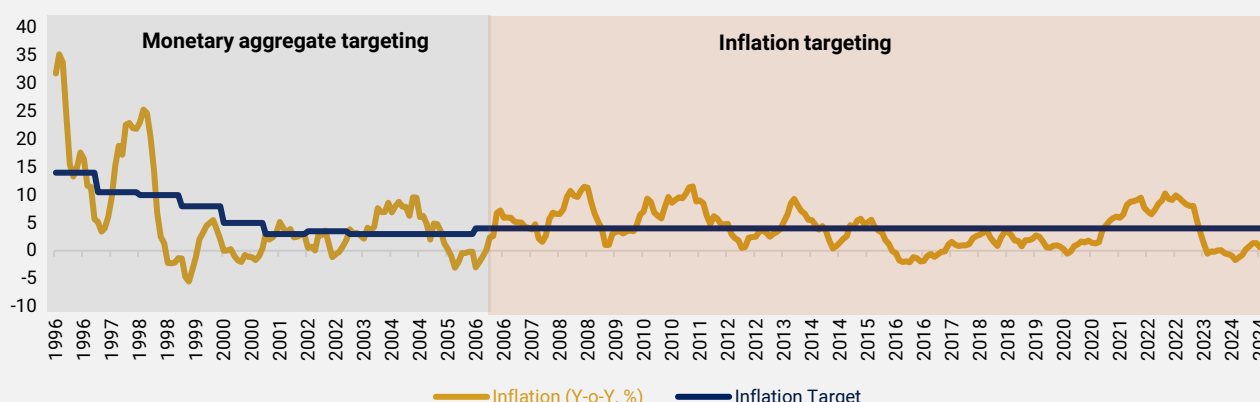
In this context, a reliable and clearly communicated inflation target is an important benchmark for businesses in decisionmaking, setting contracts, and forming inflation expectations. At the same time, the selection of the inflation target should reflect the specific characteristics of the RA economy, and take into account issues associated with accurately measuring inflation. Over time, the Central Bank may consider it necessary and appropriate to revise the inflation target to best reflect the long-term structural characteristics of the economy, its driving forces, and the vision for the country's future economic development and improvement of the country's wellbeing.

Modern economic literature asserts that an inflation target of zero is the best and most optimal mediumterm inflation target that is consistent with price stability. However, the literature also identifies a number of arguments that can explain why a low positive target is chosen in practice. These include factors relating to the zero lower bound of the nominal interest rate, downward rigidities for prices of factors of production (especially wages), and statistical errors in calculating inflation. Taking these factors into account, a low, positive inflation target is considered an acceptable and optimal solution.

Since the adoption of the inflation targeting strategy in 2006, the Central Bank has consistently achieved the proposed 4% inflation target. As such, between 2006 and 2024, the average year-over-year rate in Armenia has stood at approximately 4.0%. This is the most important indicator of the success and effectiveness of the CBA's monetary policy. However, it is important to note that this has not fully translated to the public perceiving price stability, as during various regional and internal shocks, the Armenian economy often faced risks of inflation and deanchored inflation expectations. The prevalence of similar situations over the course of Armenia's monetary policy history may offer signals that the 4% target may currently not be consistent with the definition of true price stability, or that maintaining price stability in line with a 4% target may come at the expense of significant social costs.

Since the independence of the Republic of Armenia, the country's economy and economic situation have improved significantly, becoming more robust, diversified, and globally interconnected. Parallel to this economic growth and development, the central bank's framework and strategy for price stability and monetary policy have also undergone fundamental changes and developed in several stages, providing a stronger and more robust foundation for prudently managing a growing layering of risks and uncertainties. In recent years, the Armenian economy has benefitted from consistent structural and institutional improvements, while the financial system has made significant strides in becoming more developed and robust, whether in terms of its depth, diversity of sectors, or significant expansion of its toolkit. It is also worth mentioning that with the successes achieved in the fields of monetary and macroeconomic policy as well as in developing robust policymaking frameworks, Armenia is currently "classified" by international experts and investors as a country with a leading monetary policy framework. Therefore, setting a lower and consistent inflation target is also an important factor from the perspective of Armenia's international reputation and rating.

Figure B.4.1. Developments in 12-Month Inflation and the Inflation Target, 1996–2024



Source: Armstat

According to various studies and the extensive monetary policy experience of other central banks, lowering the inflation target significantly reduces uncertainties related to monetary policy and price developments. This, in turn, ensures low macroeconomic volatility and provides a foundation for long-term investment growth, increased consumer confidence, sustained high economic growth, and the formation of low nominal interest rates. Under these conditions, economic agents can plan their consumption and savings decisions more effectively. Moreover, low and stable inflation mitigates the impact of inefficient boom-and-bust cycles on economic agents, supporting the stability of real incomes and wages.

By promoting the growth of long-term savings, a stable low-inflation environment creates the conditions for a societal shift from a borrowing-oriented model to one focused on saving and investment. By providing a more predictable macroeconomic and fiscal environment, it also reduces volatility in currency and financial markets and enhances the Republic of Armenia's reputation in international credit and investment arenas.

Thus, the recent developments and achievements in the Armenian economy and monetary system have established a solid foundation for the Central Bank of Armenia to continue strengthening public confidence in monetary policy, developing the core monetary policy framework, and implementing broad, long-term reforms. This includes, since 2025, setting a lower 3% inflation target consistent with both the public's perception of price stability and the current structure of the financial and economic system.

The analytical work examines Armenia's transition from a 4% inflation target to 3% and shows that macroeconomic spending and the speed of adjustment of inflation expectations critically depend on the level of credibility of the central bank's monetary policy. Under conditions of perfect credibility, inflation expectations immediately anchor around the new 3% target, resulting in a relatively smooth reduction in inflation, with only a small and temporary negative output gap. Under more realistic, imperfect and endogenously determined credibility, expectations adjust more slowly. This requires a tighter and more prolonged monetary policy, which leads to a deeper GDP gap and greater welfare losses.

Figure 4.2. Disagreement Among Financial Institutions' Inflation Expectations

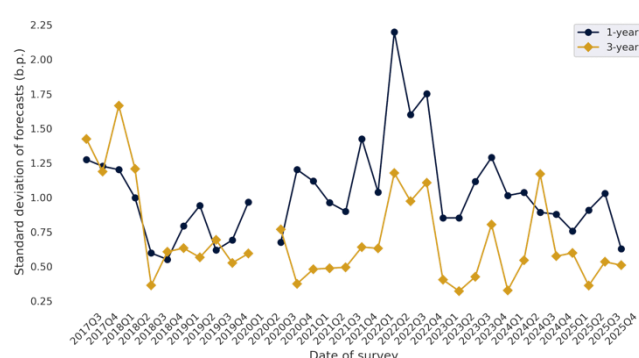
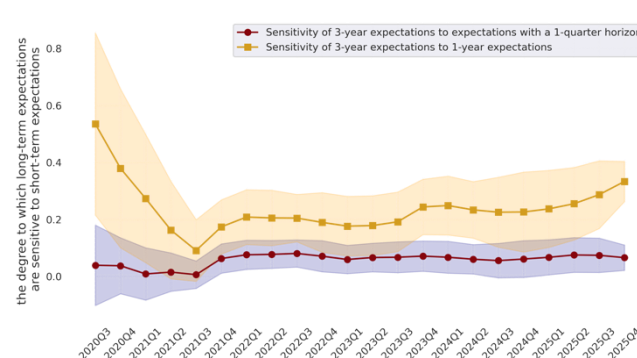


Figure 4.3. Time-Varying Sensitivity of Long-Term Inflation Expectations



According to another interpretation of the anchoring of inflation expectations in the economy, low dispersion of inflation expectations can indicate a higher degree of anchoring, reflecting a lower level of disagreement among financial market participants regarding future inflation. Figure 4.2 shows that short-term inflation expectations exhibit higher volatility and greater dispersion compared with medium-term (three-year horizon) expectations. This suggests that short-term inflation expectations are more sensitive to economic shocks and current events, whereas medium-term expectations remain relatively stable. The stable, low sensitivity of medium-term expectations to short-term shocks is an important indicator of the effectiveness of forward-looking monetary policy guidance. Notably, dispersion among both short-term and long-term inflation expectations was particularly high in 2022–2023, during periods of elevated uncertainty caused by external demand shocks. As the economy gradually stabilized, dispersion has declined over the past year, reflecting more stable expectation trends. During 2025, the increase in dispersion among short-term expectations mainly reflected disagreement over the projected trajectory of inflationary pressures driven primarily by supply factors in the global economy. Nevertheless, dispersion among medium-term expectations remained consistently low throughout the year, reflecting the market's strong confidence in the Central Bank's ability to maintain price stability over the medium term.

According to another approach, the long-term inflation expectations of financial institutions, which should reflect the Central Bank's inflation target, should be clearly distinct from short-term expectations, which are more vulnerable to short-term economic fluctuations. Therefore, under well-anchored expectations, the linkage between short-term and long-term inflation expectations of financial institutions is expected to be weak.

As shown in Figure 4.3, the results of a rolling bilateral regression indicate that long-term (three-year horizon) inflation expectations of financial institutions respond less to short-term (one-quarter) expectations than to one-year expectations. This relatively weak linkage reflects the anchoring of long-term expectations and their insulation from temporary fluctuations. It suggests that financial institutions form their long-term inflation expectations primarily based on the Central Bank's target rather than recent economic developments. Under fully anchored expectations, the corresponding coefficient should be close to zero, and the estimates for the most recent quarters are statistically near this level.

Alongside the inflation expectations of financial institutions, it is important to consider the inflation expectations of households. Studying household inflation expectations provides valuable insights into the overall formation of inflation expectations, their trends, and perceptions of the inflationary environment in the economy. Therefore, a joint analysis of both financial institutions' and households' expectations allows for a comprehensive understanding of the degree of expectations anchoring and the effectiveness of monetary policy.

The results of the Central Bank's quarterly surveys on household inflation expectations (over a one-year horizon) are summarized in Figure 4.4. The forward-looking monetary policy implemented by the Central Bank to mitigate the inflation shocks of 2014–2015 significantly reduced and stabilized elevated inflation expectations during 2015–2017. However, starting in 2018, household inflation expectations have been characterized by a notable increase in the share of uncertainty, primarily reflecting geopolitical developments and pandemic-related uncertainties. Following the high post-COVID inflation episode, elevated inflation expectations have gradually eased, recently giving way to lower inflation expectations.

Despite temporary fluctuations in overall inflation, household inflation expectations remained relatively stable throughout 2025. In the first quarter of the year, as uncertainty decreased, the share of high inflation expectations increased slightly, reflecting public perceptions of persistently high prices in certain small product categories. At the same time, the weight of respondents expecting slower inflation grew, consistent with a low-inflation environment. In the second and third quarters, high inflation expectations continued to decline, even amid some acceleration in overall inflation, while uncertainty fluctuated somewhat, driven by perceptions of prices for certain goods, particularly food. In the fourth quarter, expectations largely remained stable, with a slight increase in the share of respondents anticipating low inflation. In this context, the Central Bank's monetary policy credibility indicator, which was calculated based on inflation expectations, showed a steady and gradual increase, reflecting the public's relatively stable and well-anchored inflation expectations (Figure 4.5)⁵.

Figure 4.4. One-Year-Ahead Household Inflation Expectations in Armenia

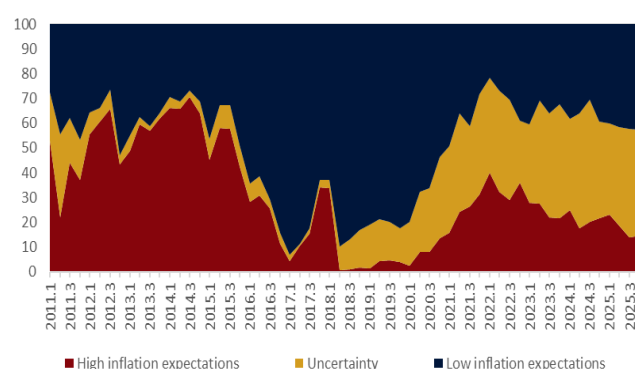
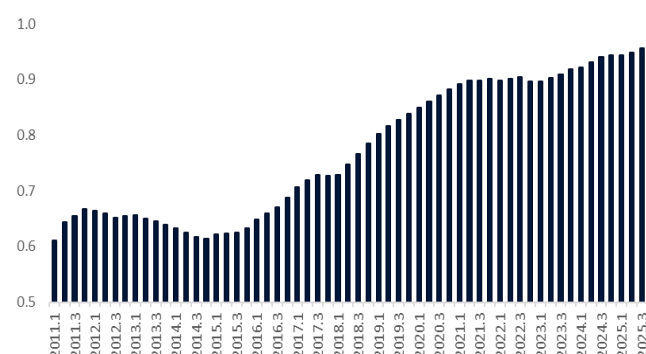


Figure 4.5. Central Bank Monetary Policy Credibility Level Based on Household Expectations



Long-term inflation expectations are a key indicator of the success of monetary policy and the credibility of the central bank. At the same time, inflation expectations help define the potential social costs that may arise in the pursuit of price stability in the economy. In the short term, central banks often face a trade-off between inflation and economic growth. How central banks manage this trade-off largely determines their authority and public confidence. For example, central banks with high credibility can often choose not to respond to short-term supply shocks, as long-term inflation expectations remain anchored and do not react to these temporary developments. The credibility of a central bank can be assessed using several indicators, such as the degree of dollarization, inflation expectations, and the achievement of the inflation target.

The level of dollarization in the economy can provide important information about the credibility of the central bank. In small open economies, financial dollarization has a dual significance: on one hand, it can serve as a tool for hedging risks, while on the other hand, excessively high dollarization may indicate low confidence in the national currency and weak trust in monetary policy. Various studies estimate that the optimal level of dollarization for Armenia is around 30%⁶. Dollarization above this level may signal low confidence in the central bank and poorly anchored inflation expectations.

Sharp increases observed during the 2008 global financial crisis and the 2014 inflation shocks reflected rising uncertainty and declining trust in the domestic currency. Since then, dollarization has gradually declined, partly thanks to Central Bank policies, and by 2025 it had stabilized in the 30–35% range (Figure 4.6). Specifically, over the year, the share of residents' foreign currency deposits and borrowings decreased by 3.5 percentage points, stabilizing near the optimal level of around 33%, while the share of loans extended to residents in foreign currency remained largely stable, fluctuating around 31%. These trends reflect a restoration of confidence in the national currency and an improvement in the effectiveness of monetary policy.

⁵ Using household inflation expectations survey data, we construct a measure of credibility based on the assumption that deviations of inflation expectations in either direction from the target indicate weakly anchored expectations. Accordingly, the credibility flow is defined as inversely related to the shares of households expecting high and low inflation, with low inflation expectations assigned a smaller weight to reflect that negative deviations from the target are considered less detrimental than positive deviations. The credibility flow is defined as: $Cred_t^{Flow} = 1 - Share_t^{High} - 0.5 Share_t^{Low}$. The credibility stock evolves according to a partial adjustment process: $Cred_t = 0.9Cred_{t-1} + (1 - 0.9)Cred_t^{Flow}$, where the initial level of credibility is assumed to be around 0.6.

⁶ Grigoryan, V., & Dallakyan, A. (2007). "Equilibrium real exchange rate model of Armenia" (Working Paper No. 080701E),

The results of the credibility measure based on excess dollarization, presented in Figure 4.7, suggest that credibility is at its maximum when dollarization is at its optimal level and declines linearly once it exceeds that threshold. To eliminate distortions arising from exchange rate fluctuations, fixed exchange rate adjustments are applied in the calculations.

The resulting indicator is almost a mirror image of dollarization dynamics, reflecting the gradual restoration of credibility following the low levels observed during the 2008–2015 shocks. According to the estimates, in 2025 the credibility indicator stood at around 91–94% based on the D2 dollarization measure and 95–97% based on the D5 measure, which may be characterized as a high degree of credibility of the Central Bank's monetary policy.

Figure 4.6. Level of Dollarization in Armenia⁷

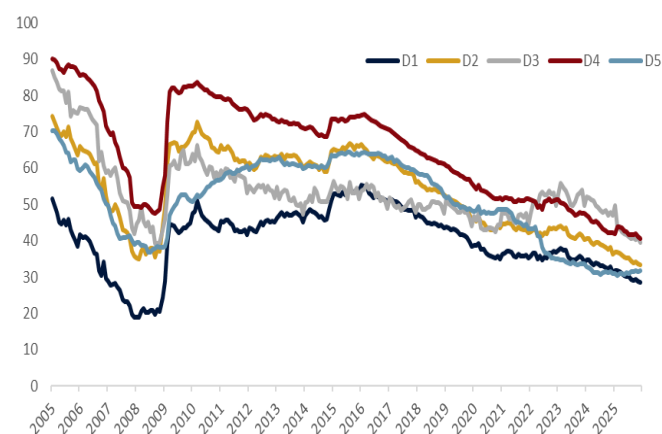
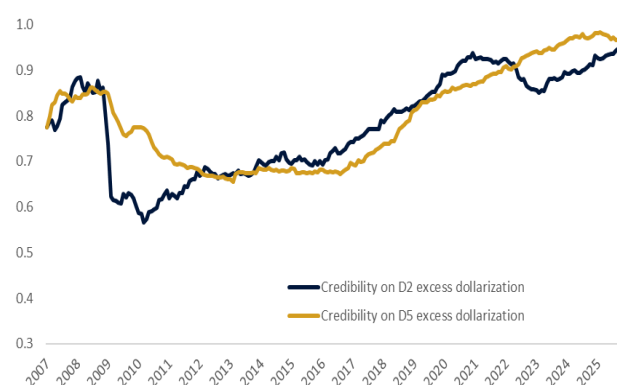


Figure 4.7. Credibility Levels Based on Dollarization Indicators

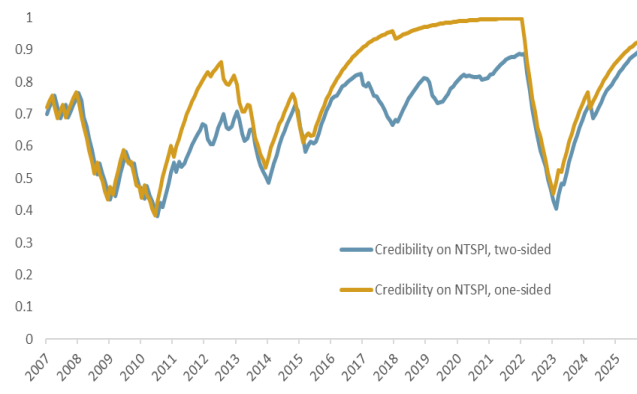


In the context of monetary policy implementation, the Non-Tradable Sticky Price Index (NTSPI) provides valuable insight into the underlying inflationary environment. These prices, which typically associated with non-tradable services that rely heavily on domestic labor, are more resilient to exchange rate fluctuations and supply shocks and adjust more slowly, thereby reflecting fundamental inflationary pressures in the economy⁸. The Central Bank's success in achieving its inflation target is considered a key condition for assessing monetary policy credibility. In this context, developments in the NTSPI are particularly important, as they indicate the degree to which expectations are anchored and the strength of public confidence in the central bank's commitment to maintaining price stability. Under a credible monetary policy, the index, reflecting firms' medium- to long-term pricing behavior, evolves gradually, signaling stable inflation expectations.

Figure 4.8. NTSPI, Y-o-Y, %



Figure 4.9. Credibility measures based on NTSPI



The NTSPI, which reflects core inflation, clearly captures historical key inflation episodes, such as the 2008 financial crisis, the 2014 oil price shocks and geopolitical tensions, as well as post-COVID inflationary pressures driven by high demand. Recent developments show a gradual stabilization of the NTSPI. In particular, throughout 2025, inflation for non-tradable goods with sticky prices continued to stabilize in the 2.0–2.5% range. This stabilization at low levels may also reflect the gradual anchoring

⁷ Note 1: Since 2012, the dollarization indicators have been compiled based on data from the Central Bank of Armenia, commercial banks, and credit organizations.

Note 2: D1 is the ratio of residents' FX deposits to broad money.

D2 is the ratio of residents' FX deposits to resident's total deposits.

D3 is share of FX demand deposits of resident households in total demand deposits of resident households.

D4 is share of FX term deposits of resident households in total time deposits of resident households.

D5 is ratio of FX loans provided to resident real sector to total loans provided to resident real sector.

⁸ Papikyan, Avetisyan, Laxton (2023), "Non-Tradeable Sticky Price Inflation: Developing Better Concepts for Monetary Policy Analysis",

of inflation expectations around the new 3% target following the early-year reduction in the inflation target. Credibility based on the NTSPI is constructed solely on the Central Bank's ability to maintain inflation at its target level⁹.

Thus, credibility is perceived as a stock accumulated over time, reflecting the Central Bank's cumulative performance in keeping inflation close to its target on average. When constructing the credibility indicator, two descriptive benchmarks are used to capture how inflation expectations form in high- and low-inflation environments^{10 11}. The above credibility measures reflect an important trend for Armenia. Following the economic shock of 2014–15, the Central Bank of Armenia was able to significantly enhance the credibility of its monetary policy through forward-looking inflation targeting, which stabilized inflation expectations and strengthened public confidence in the Bank's long-term commitments. Additional risks of destabilization emerged during 2020–22, a period characterized by high volatility and uncertainty, when the COVID-19 pandemic, the war, regional tensions, and the Russia–Ukraine conflict posed serious challenges to Armenia's macroeconomic stability. During this period, the Central Bank's monetary policy ensured macroeconomic stabilization and, in subsequent years, the restoration of monetary policy credibility. Institutional reforms by the Central Bank also played a key role in this process, particularly the development and implementation of a monetary policy framework based on prudent risk management, as well as the reduction of the inflation target. In 2024–2025, the economy entered a gradual adjustment phase, with 2025 characterized by robust and stable economic growth under inflationary pressures driven primarily by supply factors and a largely neutral impact of domestic demand. At the same time, since the 2025 reduction in the inflation target, various indicators, including the dynamics of inflation expectations and core inflation measures, show that the adjustment toward the new target occurred relatively quickly.

⁹ Laxton, Igityan, Mkhatrihshvili (2024), "Endogenous Credibility and Economic Modeling: Adapting the Forecasting and Policy Analysis System to Modern Challenges",

¹⁰ Papiqyan, Avetisyan, Laxton (2023), "Non-Tradeable Sticky Price Inflation: Developing Better Concepts for Monetary Policy Analysis",

¹¹ When constructing the credibility indicator, two descriptive benchmarks are used to capture how inflation expectations form in high- and low-inflation environments. The first benchmark represents "optimistic but cautious" expectations ($\Pi_t^{e,T}$), according to which inflation, while reflecting historical trends, gradually converges toward the target (Π^*) level. *Optimistic but cautious expectations*: $\Pi_t^{e,T} = \delta_1 \Pi_t + (1 - \delta_1) \Pi^*$, $\delta_1 > 0$

The second benchmark, "skeptical and history-driven," assumes that expectations are formed primarily based on historical trends, reflecting hypothetical higher (Π^{high}) or low (Π^{low}) inflation levels (after the 2025 target change, these correspond to 7% and -1%, respectively).

Skeptical Expectations, Oriented Toward a High-Inflation Regime $\Pi_t^{e,high} = \delta_2 \Pi_t + (1 - \delta_2) \Pi^{high}$, $\delta_2 > 0$

Skeptical Expectations, Oriented Toward a Low-Inflation Regime $\Pi_t^{e,low} = \delta_3 \Pi_t + (1 - \delta_3) \Pi^{low}$, $\delta_3 > 0$

Any deviation of actual inflation from optimistic expectations generates a positive probability (prob) that the economy will shift toward a higher- or lower-inflation regime. When actual inflation aligns with optimistic expectations, the probability of deviating from the target environment becomes zero.

Probabilities of Approaching High- and Low-Inflation Regimes.

$$prob_t^{high} = \frac{100 (\Pi_t - \Pi^*)^2}{(\Pi_t - \Pi^*)^2 + (\Pi_t - \Pi^{high})^2}, \quad prob_t^{low} = \frac{100 (\Pi_t - \Pi^*)^2}{(\Pi_t - \Pi^*)^2 + (\Pi_t - \Pi^{low})^2}$$

When actual inflation is lower than optimistic expectations, the probability of entering a high-inflation regime is assumed to be zero. Conversely, when actual inflation exceeds optimistic expectations, the probability of approaching a low-inflation regime becomes zero.

This framework illustrates how changes in expectations can guide the economy between high- and low-inflation regimes, highlighting the central role of monetary policy credibility in preventing extreme scenarios, such as excessively high and volatile inflation or deflationary traps. In particular, over time, the flow of credibility increases as the probability of deviation from the target decreases.

Credibility Flow Over Time: $C_t^{flow} = \frac{100 - prob_t^{high} - prob_t^{low}}{100}$

Open economies are generally less constrained by the zero lower bound on interest rates, as exchange rate depreciation through foreign exchange market operations provides an effective tool to avoid deflationary traps. In this context, for emerging economies that are more vulnerable to inflation shocks, a one-sided credibility indicator is typically used. This approach assigns a smaller weight to the probability of transitioning to a low-inflation regime, placing greater emphasis on inflation deviations above the target.

The credibility indicator (C_t), is constructed as a stock, accumulating over the previous level through the flow of credibility and the impact of shocks arising from external factors. *Credibility Index* $C_t = \delta_c C_{t-1} + (1 - \delta_c) C_t^{flow} + \varepsilon_t^C$, $\delta_c > 0$

Using the methodology described above and based on the NTSPI as a measure of underlying inflationary pressures, the Central Bank's credibility is calculated as an indicator of its success in achieving the inflation target. Another, hybrid credibility indicator combines fluctuations in the NTSPI and the level of dollarization, assigning respective weights of 70% and 30% to the effects of deviations from their balanced levels



Central Bank
of Armenia

05 |

Addressing Common
Questions on
Monetary Policy

Addressing Common Questions on the Conduct of Monetary Policy

In fulfilling its commitment to transparency and public engagement, the Central Bank of Armenia recognizes the importance of clearly communicating the objectives, tools, and outcomes of its monetary policy decisions. This section provides a valuable platform to foster dialogue between the Central Bank of Armenia and external stakeholders. By addressing common questions about monetary policy and other related topics, it supports the Bank's ongoing efforts to enhance transparency, promote public understanding, and strengthen engagement with the broader community.

Question 1. Why have lending rates not declined during the policy loosening cycle?

Monetary Policy Transmission

Understanding the relationship between short-term and long-term interest rates is essential for assessing the effectiveness of monetary policy transmission. It is sometimes argued that if policy rate adjustments do not immediately translate into comparable movements in long-term lending rates – such as loan or mortgage rates – the transmission mechanism must be impaired. However, this interpretation reflects a misunderstanding of how monetary policy operates through the financial system.

The policy rate primarily affects the cost of short-term financing and is thus more directly correlated with short-term interest rates, such as short-term bond rates or deposits. The cost of short-term liquidity for banks has a limited direct effect on long-term interest rates. What matters more is the expected path of the policy rate. Let's imagine a credible central bank responding aggressively to economic shocks, establishing short-term adjustments that reinforces long-term stability—such as keeping inflation expectations well-anchored— the short-term rates may rise substantially, while long-term rates may exhibit only minor changes. This case demonstrates effective monetary policy transmission, contrary to the notion that a lack of significant movement in long-term rates indicates a weak passthrough. For a more detailed description of the main channels through which monetary policy affects the broader economy, refer to Box 2 and Box 3.

While long-term interest rates should generally adjust in response to changes in short-term borrowing costs, factors that determine long-term interest rates are crucial for assessing the monetary policy transmission. **Competition among commercial banks, inflation expectations, demand for financial products, perceived consumer risk, economic outlook, and country risk premium** all play key roles in shaping the pricing of financial products. These drivers can sometimes obscure the direct link between policy rates and long-term rates, as discussed in greater detail below. In Armenia, long-term deposit, loan, and government bond rates have historically moved broadly in line with the policy rate across easing and tightening cycles, as shown in Figure 5.1.1 and Figure 5.1.2. However, for example during the post-COVID period, this relationship appeared somewhat distorted. As the CBA began lowering rates in early 2020 in response to the economic impact of COVID-19, long-term rates declined only slightly, reflecting heightened uncertainty and risk perceptions about the future amid an unprecedented global shock. This pattern is not unique to Armenia and is consistent with the international evidence on monetary transmission during periods of macroeconomic stress.

Figure 5.1.1. Change in policy rate and market interest rates, basis points

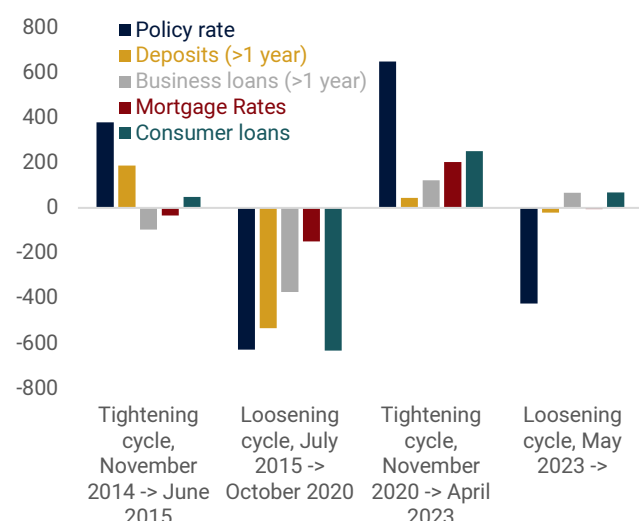
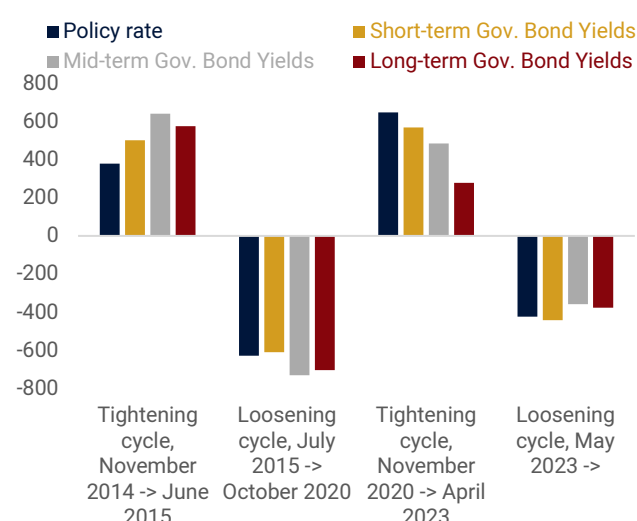


Figure 5.1.2. Change in policy rate and market interest rates in Armenia, basis points



Factors Impacting Long-term Market Interest Rates

Demand for financial products: The level of demand for credit and other financial products influences how lending rates are set. When demand for loans is strong, banks have less incentive to lower lending rates to attract borrowers, as their loan portfolios are already growing. Conversely, when credit demand is weak, banks may be more willing to reduce rates in order to stimulate borrowing. This means that even during an easing cycle, if credit demand remains robust, lending rates may not decline as quickly or as fully as the reduction in the policy rate might suggest. In this way, demand-side dynamics in the credit market can independently influence the pace and extent to which policy rate changes are reflected in retail lending rates.

In Armenia, a particularly relevant example of this dynamic, especially over the current monetary loosening cycle, is the mortgage interest rate subsidy program. This policy reimburses virtually the entire amount of mortgage interest payments from income taxes if the mortgage is used to purchase a newly built property. Essentially, the government pays back the borrower's income tax in an amount equivalent to the mortgage interest payments, making borrowers **almost insensitive to mortgage interest rates**. The policy's impact has been substantial, with mortgage lending volume increasing significantly since its inception. This elevated demand for long-term lending, with consumer indifference toward interest rates, has further contributed to this "temporary disconnect" and added a layer of complexity to the monetary policy transmission in Armenia.

Importantly, the effects of this policy may extend beyond the mortgage market itself. The purchase of a home often generates additional demand for credit to cover significant expenses related to home renovation, furnishing, and other durable goods consumption associated with the new property, especially since almost all new construction is delivered unfinished and unfurnished. Borrowers who take mortgage loans may therefore also seek additional loans for renovation works, furniture, major appliances, electronics, and other housing-related expenditures. Because the mortgage interest is effectively subsidized through the tax refund mechanism, the overall effective borrowing cost across the consumer's total loans (mortgage plus ancillary loans) becomes lower, which can sustain strong credit demand even when interest rates on individual loan products remain unchanged. In this way, strong mortgage demand can create spillover effects to other categories of lending, contributing to continued growth in credit volumes and limiting the downward adjustment of aggregate lending rates.

Competition among commercial banks: In theory, the degree of competition among banks plays an important role in shaping the pricing of lending and deposit rates. When competition is strong, banks have a strong incentive to pass on lower funding costs to their customers in the form of cheaper loans and better deposit rates. When competition is more limited, banks have greater flexibility in setting their rates and may adjust more slowly, particularly if there are specific downward rigidities in the lending market that disincentivize interest rate reductions, as described above.

Perceived consumer risk: When banks extend loans, they price not only the cost of their funding but also the risk that borrowers may fail to repay. This credit risk premium is an independent component of lending rates that does not necessarily move in line with the policy rate. During the current easing cycle, some increases in lending activity to segments with lower creditworthiness has been observed, generating further pressure against interest rate decreases in the aggregate. This is described in greater detail on the following pages.

Inflation expectations: Inflation expectations play an important role in determining long-term lending and deposit rates. When inflation expectations are well anchored around the central bank's target, banks and financial markets can price long-term products with greater confidence, and long-term rates tend to move in a more predictable and orderly manner in response to policy changes. For more information refer to Section 4.

Economic outlook: The broader macroeconomic environment is an important independent determinant of long-term lending rates. When the economic outlook is favorable — characterized by solid growth, low unemployment, and stable financial conditions — banks are more confident in the ability of borrowers to service their debts, which supports a gradual compression of lending rates over time. When the outlook is uncertain or deteriorating, banks tend to build additional buffers into their loan pricing to account for the possibility of weaker economic activity and higher default rates. The recent years have been characterized by the emergence of significant economic and policy uncertainty globally, with global and regional geopolitical tensions, trade wars, sanctions, climate risk, and other developments generating significant uncertainty for businesses and investors regarding the future economic outlook. In such an environment, banks, like other private enterprises, may exercise a greater degree of caution. For banks specifically, this more cautious attitude may manifest itself in a greater reluctance to adjust long-term lending rates downward, as loan pricing reflects forward-looking assessments of borrowers' repayment capacity over the entire life of the loan rather than only current economic conditions.

Country risk premium: The country risk premium reflects the additional compensation that investors and financial institutions require for operating in a particular economic and institutional environment. It captures a broad set of factors that influence the overall cost of financial intermediation in a given country. During the easing cycle, Armenia's country risk environment was influenced by broad external developments, including geopolitical uncertainty in the region, shifts in global financial conditions, and uncertainty surrounding the global economic outlook. Even as the sovereign risk premium declined markedly in Armenia

during this period, significant uncertainty continued to surround the long-term, sustainable, equilibrium level of the sovereign risk premium, a question that is far more relevant in the setting of long-term interest rates. For financial institutions operating in a small open economy, such factors affect the cost of long-term funding and the required return on financial assets. Even when domestic monetary policy becomes more accommodative, these external and country-specific risks may keep the required compensation for long-term lending elevated, thereby limiting the immediate decline in lending rates.

Other Channels Through Which Monetary Policy Influences Credit Conditions

Aggregate market interest rates represent only one dimension of monetary transmission. Changes in monetary policy may also influence credit conditions through adjustments in **credit availability, loan volumes, borrower composition, and the maturity structure of lending**. As a result, focusing solely on the behavior of aggregate lending interest rates may not fully capture how monetary policy affects credit markets.

Against this background, developments in Armenia's credit market since the beginning of the easing cycle in June 2023 warrant a closer examination. While aggregate lending rates have remained relatively stable as illustrated in Figure 5.1.3 and Figure 5.1.4, other indicators of credit market activity **suggest that monetary transmission may be operating through changes in the structure and allocation of credit rather than through an immediate decline in average lending rates**. The following section therefore looks beyond aggregate interest rates and examines how developments in credit volumes, borrower composition, and loan structures may help explain the observed patterns in lending conditions.

Figure 5.1.3. Policy rate and some market rates

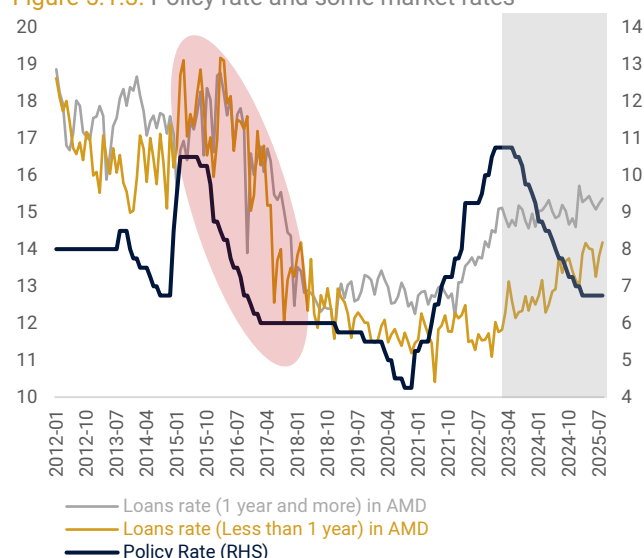
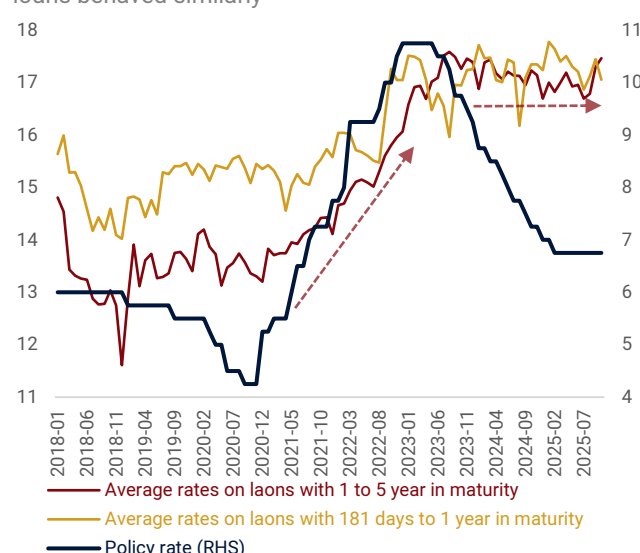


Figure 5.1.4. Average interest rates on most non-mortgage loans behaved similarly



Maturity composition of credit

The bank lending channel does not necessarily appear through changes in aggregate lending volumes or interest rate levels alone. It can also operate **through shifts in the maturity composition of credit**. Black and Rosen (2007, 2011) demonstrate that tighter monetary policy can reduce credit availability not only by contracting loan supply outright, but also by shortening the maturity of new loans – meaning that the effects of monetary policy on credit conditions may be visible in the structure of lending well before they appear in headline interest rates or volumes.

Evidence of these dynamics is visible in Armenia's credit market during the current easing cycle (Figure 5.1.5). While interest rates on loans with maturities of up to five years have remained broadly unchanged since the start of the easing cycle, credit conditions appear to have responded through shifts in the structure of lending rather than through a direct decline in nominal interest rates. In particular, the maturity composition of the loan portfolio has lengthened, with the average maturity of new loans extending by 2.2 months. All else equal, this shift implies an improvement in effective borrowing conditions – as borrowers are able to repay over a longer horizon without facing higher interest rates, the effective cost of credit declines even when headline lending rates remain stable. This pattern is consistent with the credit channel of monetary transmission, under which monetary policy influences not only the price of credit but also its terms and availability.

Figure 5.1.5. Shifts in the maturity structure of the loan portfolio in line with policy rate changes

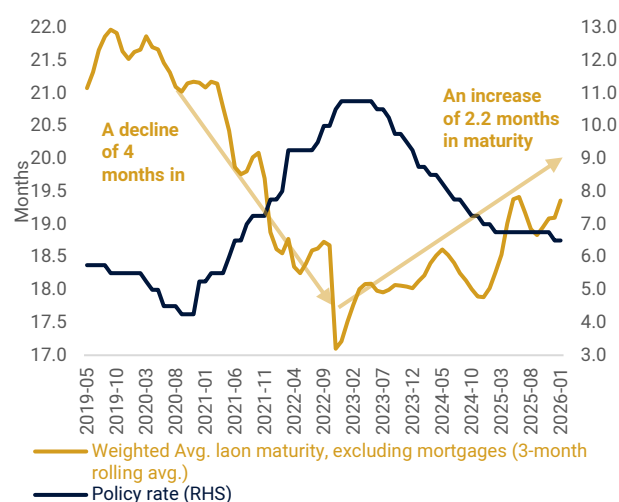
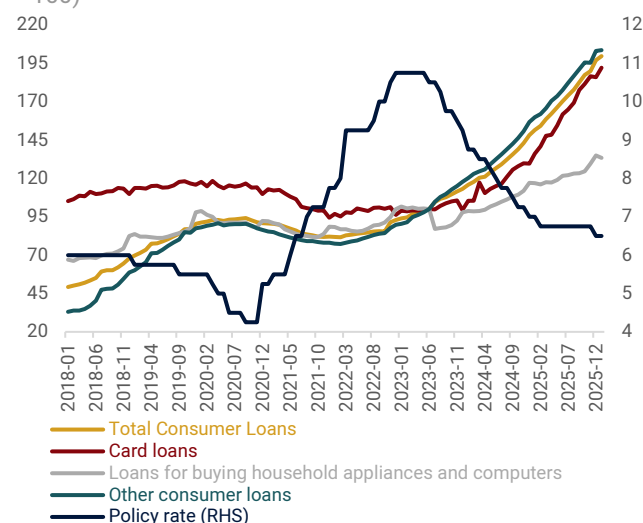


Figure 5.1.6. Consumer loans by category (index, June 2023 = 100)



Lending volumes

Developments in **loan volumes** provide further evidence that monetary transmission has been operating through the credit channel. As shown in Figure 5.1.6, the easing cycle has been accompanied by a clear expansion in several categories of lending, including consumer loans, credit card lending, and loans financing household purchases such as appliances and electronics. These categories are closely associated with segments of the economy that drive domestic demand and therefore represent an important margin through which monetary policy influences economic activity. The observed expansion in lending to these segments suggests that credit supply has responded positively to the easing of monetary conditions – a pattern consistent with the bank lending and bank capital channels of monetary transmission, under which expansionary policy improves banks' funding conditions and balance sheet strength, enabling them to extend credit more freely to households.

Figure 5.1.7. Gold collateralized loans grew markedly starting June 2023 as the easing cycle started

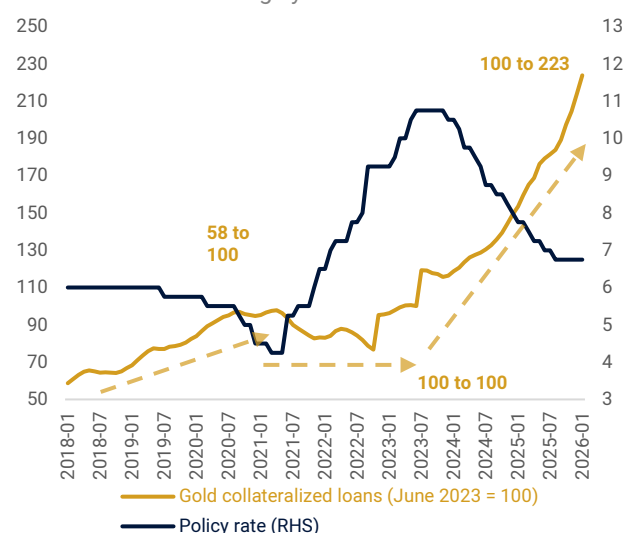
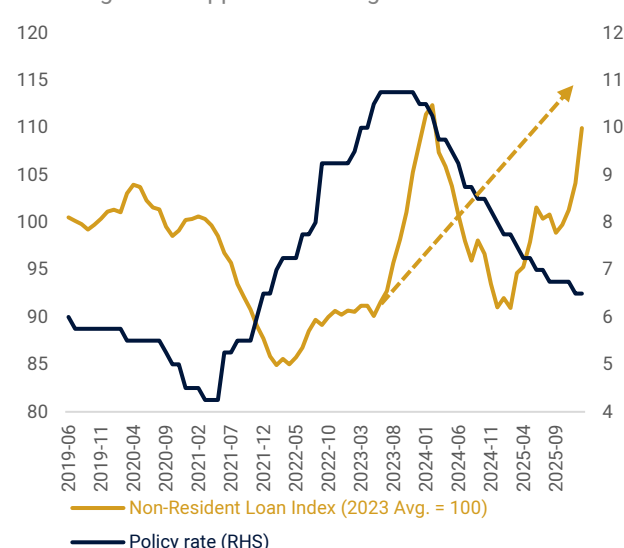


Figure 5.1.8. Moreover, loans to non-residents grew also, reflecting banks' appetite to taking on more risk



Borrower composition

Another part of the expansion in lending appears to reflect a shift in the composition of borrowers toward segments that are typically considered riskier by banks. In particular, lending has increased to borrowers who rely on collateralized loans, such as loans backed by gold or cash deposits (Figure 5.1.7). These borrowers often have limited credit history or would previously have had difficulty obtaining unsecured credit. In addition, lending to non-resident borrowers has also increased during the easing cycle (Figure 5.1.8). Because non-resident borrowers generally have less to no established financial history within the domestic banking system, banks may face greater uncertainty when assessing their creditworthiness. As a result, these types of loans are typically priced at higher interest rates. The expansion of credit to such borrower segments is consistent with the credit and risk taking channels of monetary policy, under which easier financial conditions encourage banks to extend credit to borrowers that

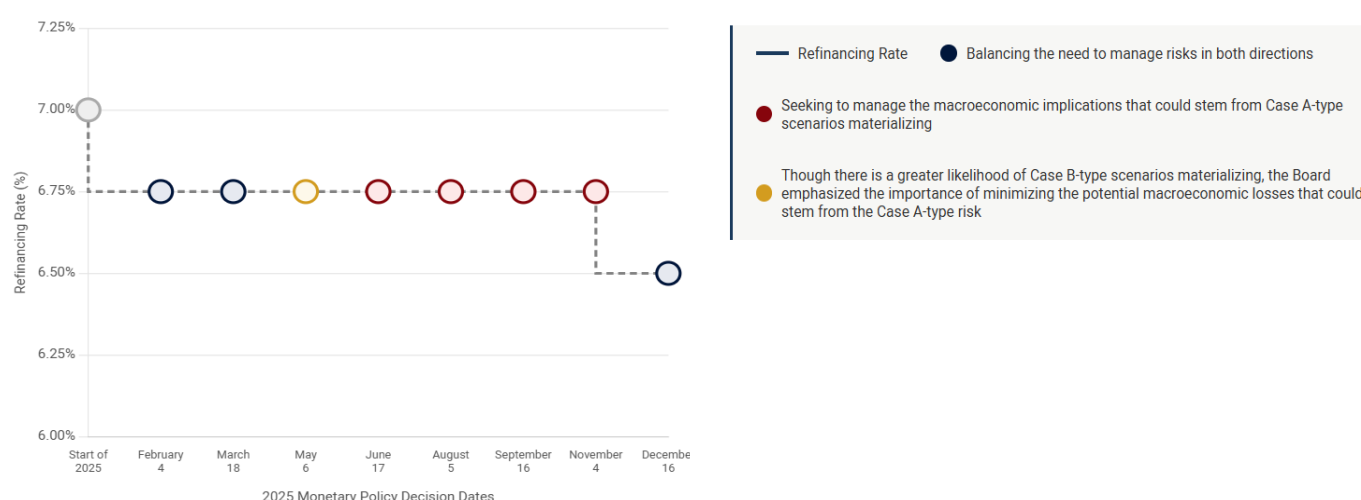
previously had limited access to financing. At the same time, the greater share of loans extended to these higher risk segments can keep the average interest rate across all loans elevated, even if lending conditions have eased for many borrowers.

In summary, while long-term interest rates can, as a general rule, adjust in response to changes in short-term interest rates, the factors underpinning long-term rates are nonetheless decisive for assessing the monetary policy transmission mechanism. Competition among banks, inflation expectations, demand for financial services, banks' assessment of customer risk profiles, expectations regarding the economic outlook, and the country risk premium play a pivotal role in the pricing of financial services.. As a result, policy rate adjustments do not always translate mechanically into equivalent changes in long-term loan rates. A decline in lending rates is one manifestation of easing financial conditions, but it is not the only one. Financial conditions can also become more accommodative through other dimensions of credit markets. On this front, developments in Armenia's credit market provide clear evidence of easing. During the recent easing cycle, lending volumes expanded in segments closely linked to domestic demand, banks extended credit to a broader set of borrowers, including riskier and previously underserved groups, and the maturity structure of loans lengthened, allowing borrowers to spread repayments over longer horizons. Taken together, these developments indicate that borrowing conditions in the economy have become more accommodative, even though this easing is not fully reflected in the behavior of aggregate lending rates.

Question 2. How should the Board's monetary policy decisions be interpreted within the risk management framework?

Clear and effective monetary policy communications help provide economic agents with clarity about the policy stance, its underlying rationale, and future directions. In this context, the main objective of monetary policy communication is to ensure transparency and comprehension among financial markets and the general public regarding how monetary policy decisions are made, with the ultimate goal of eliminating any uncertainty about the central bank's commitment to its price stability objective. Communications also play an integral role in shaping market expectations and ensuring that inflation expectations remain well-anchored to the medium-term inflation target. Over the past two years, the CBA has observed a marked increase in the interest of market participants, analysts, and the broader public in its monetary policy communications. The growing volume of analysis, commentary, and engagement with the CBA's policy decisions and publications is a welcome and encouraging development that reflects the deepening of monetary policy literacy in Armenia and the increasing recognition of the CBA's communications as a valuable source of insight into the economic outlook. In this context, the CBA finds it appropriate to elaborate on the logic of the risk management approaches underlying its monetary policy decisions.

Figure 5.2.1. Risk Management Approaches Underlying Monetary Policy Decisions in 2025



Under the Prudent Risk Management framework, the Board **does not anchor its communication to a single most-likely scenario**. Instead, it explicitly acknowledges that the economic outlook is surrounded by meaningful uncertainty and that responsible policymaking requires assessing the full distribution of plausible outcomes. As a structured overview of the policy-relevant scenarios considered by the Board, the CBA develops a taxonomy of scenarios which present the key issues that can impact policy decisions over a medium-term horizon in the context of a least regrets decision-making framework (see Chapter 2, Section A). These scenarios entail concrete monetary policy paths, rather than abstract or implausible risk narratives. The policy rate paths implied by these scenarios are presented relative to the Market Reference scenario. The Market Reference scenario reflects market participants' expectations regarding the future path of the policy rate, as well as their assessments of the economic outlook. **It does not represent the Central Bank's baseline forecast or the most-likely scenario.**

Under the Prudent Risk Management framework, decision-making is guided by the "least regrets" approach. When the CBA Board communicates that its decision is motivated by the need to manage Case A-type risks, this means that the Board is trying to mitigate the costs that could emerge in the event that the Case A-type scenarios materialize but the Board has made a policy error in selecting a different (i.e. lower) rate path. In other words, the Board's risk management places weight not on the scenario that is most likely to materialize, but rather, on the most dangerous scenarios—where a potential policy error that fails to adequately respond to this type of scenario leads to significant and costly macroeconomic consequences.

Under the Prudent Risk Management Approach, the conventional hawkish/dovish characterizations may be applied according to the following logic:

- An approach guided by the need to manage Case A-type risks may be interpreted as hawkish, as it implies a policy rate path that is higher relative to market expectations over the medium-term horizon. This does not necessarily imply a rate increase in absolute terms, but rather a policy rate path that is higher relative to market expectations.
- Similarly, an approach guided by the need to manage Case B-type risks may be interpreted as dovish, as it implies a policy rate path that is lower relative to market expectations over the medium-term horizon. This too does not necessarily imply a rate cut in absolute terms, but rather a policy rate path that is lower relative to market expectations.

Figure 5.2.2. Illustrative policy rate paths

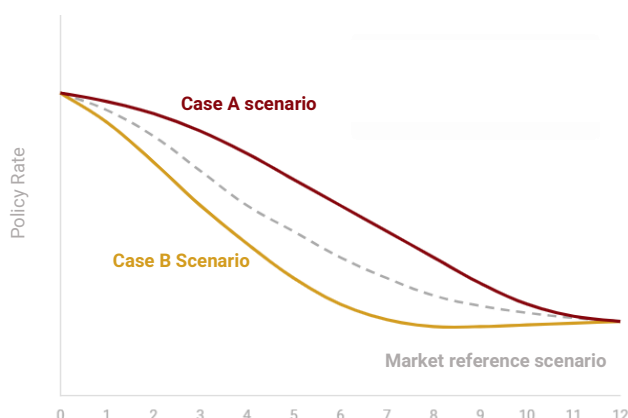
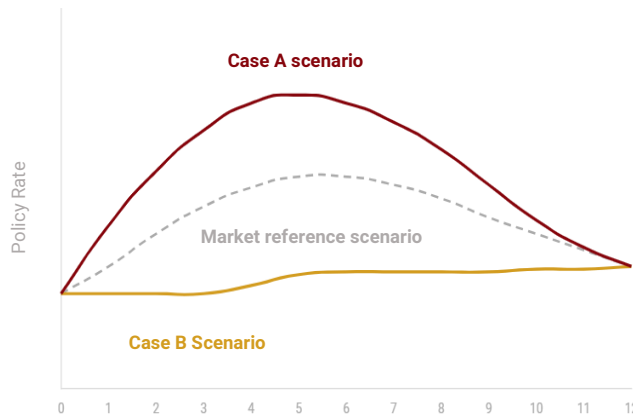


Figure 5.2.3. Illustrative policy rate paths



The September 16, 2025 policy decision provides a direct and instructive illustration of this distinction:

“...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.”

This means that managing Case A risks requires, over the medium-term horizon, a policy rate path that is higher relative to market expectations – in other words, it implies a hawkish approach. Nevertheless, a monetary policy decision guided by the need to manage Case A-type risks **does not necessarily imply an increase in the policy rate in absolute terms**. If financial market expectations reflect a declining policy rate path, there may be instances where Case A scenarios also imply a declining rate path albeit at a slower and more gradual pace relative to market expectations. This logic can be seen in the sequence of decisions taken throughout 2025. Across six consecutive meetings held between June and November, the Board opted to keep the policy rate unchanged. Four of these six policy decisions were underpinned by the need to manage Case A-type risks. Thus, the fact that several decisions cited the need to manage Case A-type risks without any sign of policy tightening demonstrates that such language does not imply an imminent rate increase, but rather a policy rate path that is higher relative to market expectations over the medium-term horizon.



Central Bank
of Armenia