



Central Bank
of Armenia

2025 March
Executive
Monetary
Policy
Statement

Published March 18, 2025

A. Executive Monetary Policy Statement

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

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

Annual CPI inflation approached the target level, reaching 2.5% in February 2025. Meanwhile, core inflation has also remained at low levels, at 1.5% year-over-year in February.

In Q1 2025, the risks of slower economic growth and accelerated inflation in global markets and Armenia's key partner countries have significantly increased. In particular, the risks of price increases and potential disruptions to supply chains in international commodity markets and key partner countries have intensified, driven by growing tensions in international trade relations and ongoing geopolitical uncertainties. Uncertainty related to fiscal expansion in US over the medium term and resulting increase in debt and long term interest rates increased significantly recently. At the same time, sticky prices in key trading partner economies continue to remain relatively elevated, while labor market conditions continue to be tight. In this context, key trading partner central banks will continue to gradually lower policy rates at a slower pace than previously expected, while still maintaining a relatively tight stance in the near term. Consequently, weak deflationary effects from the external sector on the Armenian economy continue to persist.

Since the beginning of the year, economic activity in Armenia remained close to estimated sustainable long term growth rate, continuing to be largely driven by meaningful growth in construction, services and trade. The latter has been affected by certain short-term factors, posing significant uncertainty with respect to the sustainability of economic growth and its long-term outlook, as well as the strength of domestic demand and consumption conditions. External demand for services continues to decline, while the overall demand environment is assessed as neutral from an inflationary perspective. In this context, labor market conditions continue to cool, as reflected in the gradual stabilization of wage growth, non-traded sticky price inflation and inflation expectations. At the same time, risks for demand pressures stemming from fiscal policy continue to persist.

In order to manage possible risks stemming from conditions of high uncertainty, the Board considers multiple scenarios during its deliberations. On the one hand, the Board discussed scenarios where possible underlying developments would require a higher path for the policy rate relative to current market expectations to ensure price stability. This includes scenarios related to the risk premium of Armenia, amid the geopolitical developments, and the resulting macroeconomic effects. On the other hand, the Board discussed scenarios related to the risks of prolonged uncertainty over US economic policy, the decline in global economic confidence, and the resulting risks of reduced growth and weakened demand in Armenia. This would imply a more rapid and aggressive downward path for the policy rate than what is currently priced in markets in order to sustainably bring inflation back to target in the medium-term horizon.

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

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Approved by the Board of the Central Bank of Armenia
March 18, 2025

Governor

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Deputy Governors

Armen Nurbekyan

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Board Members

Hasmik Ghahramanyan

Davit Nahapetyan

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B. Summary of Economic Conditions

Global Economy

In Q1 2025, economic activity among Armenia's main trading partners has been mixed. In the US, the strong economic growth and wealth accumulation observed in recent quarters create preconditions for continued expansion driven by consumption. However, uncertainty surrounding economic policy outlooks in recent months may restrain private demand in the near future. In Russia, high economic activity persists, largely supported by strong domestic consumption, particularly in services. Meanwhile, economic activity in China is showing signs of slowing, driven by weakening domestic demand. In the Eurozone, economic growth remains at a low level. Overall, risks of a slowdown in global economic activity persist.

Uncertainty continues to surround economic fundamentals in the US. Uncertainty has increased particularly regarding economic policies—especially trade and fiscal policies—which has contributed to heightened financial market volatility and some asset price adjustments in recent months. Despite strong consumption growth in recent quarters supporting high economic growth (with GDP growing by 2.3% in Q4 2024, of which approximately 2.8 percentage points came from personal consumption expenditures), the rising uncertainty around economic policies poses risks of consumption and investment delays, potentially slowing economic growth. While headline inflation is gradually approaching the target, some core inflation indicators—such as sticky-price goods inflation and wage growth—remain significantly above target. At the same time, trade and fiscal policies under the new U.S. administration pose substantial risks of an expansionary inflationary environment, which could further complicate the Federal Reserve's trade-off between price stability and full employment objectives. Beyond the short-term inflationary effects, a more expansionary fiscal policy stance in the medium term also raises risks of a higher debt trajectory and an increase in the neutral rate. This could impact both the future course of Fed policy and long-term interest rates, as well as capital flows to emerging markets. These developments continue to challenge monetary authorities in their efforts to bring inflation sustainably to target and ensure price stability.

In March 2025, the European Central Bank (ECB) further lowered its policy rate by 25 basis points, setting it at 2.65%. After a temporary acceleration in 2024 driven by external demand factors, economic growth at the beginning of the year remains generally weak, with growth prospects and structural composition—particularly in the industrial sector—continuing to raise concerns. Headline inflation is declining due to weaker goods inflation, while services inflation remains elevated, reflecting a deepening divergence in economic developments across different sectors. This presents a significant challenge for the ECB in terms of calibrating the pace of policy

adjustments while ensuring the achievement of its inflation target.

Risks of persistently weak domestic demand in both the Eurozone and China, along with uncertainty surrounding economic policies and geopolitical developments, remain key factors contributing to the outlook for slower global economic growth.

Economic growth in Russia remains strong, supported by both expansionary fiscal policy and a significant increase in private spending. In this environment, intensifying competition for labor between the military-industrial sector and the private sector—amid tight labor market conditions—could heighten inflationary risks. Despite the Bank of Russia's substantial tightening of policy conditions, meaningful progress in stabilizing inflation has yet to be observed. On the other hand, stricter and more targeted Western sanctions, combined with a significantly tighter monetary policy stance, pose risks to Russia's medium-term economic outlook. At the same time, the likelihood of a near-term resolution to the Russia-Ukraine conflict has increased, introducing mostly upside risks to short- and medium-term economic growth.

The inflationary environment in global commodity markets continues to remain weak, though upside risks exist. Heightened geopolitical tensions in the Middle East, which show few signs of easing, continue to threaten both higher and more volatile energy prices as well as potential disruptions to global supply chains. At the same time, food prices continue to remain below the high levels of the previous two years.

In global commodity markets, food prices have stabilized in recent months but remain at higher levels compared to the previous year. However, significant uncertainty persists regarding the medium-term trajectory of commodity markets. Rising geopolitical tensions in the Middle East continue to pose risks of increased oil price volatility and potential disruptions to global value chains. Conversely, if global demand weakens further, deflationary pressures could emerge.

Domestic Demand Conditions

In the fourth quarter of 2024, economic growth in Armenia continued to slow, approaching the estimated level of long-term sustainable growth. The construction, trade, and services sectors made significant contributions to growth. These trends in economic activity persisted in January 2025, with growth accelerating slightly to 7.1%. It is worth noting that alongside the stabilization of economic growth, concentration has also weakened. Nevertheless, due to the structure of growth, high uncertainty remains regarding the relative position of aggregate supply and aggregate demand.

The robust external demand observed since 2022 has been gradually weakening in 2024, as reflected in the stabilization of both real expenses per tourist and tourist arrivals.

Considerable uncertainty continues to surround current domestic demand conditions. On the one hand, strong growth in retail trade, consumer credit, domestic tourism, and other services points to strong domestic demand. On the other hand, recent economic growth has been fairly concentrated in certain sectors, remittances have continued to decline, and labor market conditions have eased somewhat. These factors, coupled with the overall weak inflationary environment for several successive quarters, could point to weaker demand conditions in the economy.

Uncertainties also surround the outlook and future trajectory of domestic demand conditions. Key uncertainties relate to the reduced debt burden (given higher incomes); the future utilization of accumulated savings in the private sector; slowing wage growth; and geopolitical and regional uncertainties. For example, depending on how and in which direction savings are spent (consumption vs. investment), this could have different implications on the relationship between aggregate demand and aggregate supply in the economy.

Additionally, risks for modest demand pressures stemming from fiscal policy continue to persist. This is driven by risks of revenue underperformance, as well as high current expenditures given the imperative for various social support programs. The risks of expenditure underperformance, as well as their structure, also remain significant, potentially exerting a more restrictive impact on aggregate demand.

Labor Market & Inflation

Uncertainty regarding the labor market conditions persists. The household survey-based unemployment rate in Q3 2024 moderated to 13.3%, which is 1.2% higher compared to the same quarter in previous year. Considering uncertainty surrounding the level of unemployment, it is important to continue to monitor potential development scenarios and their consequences. On the one hand, the increase in the unemployment rate compared to previous year could reflect arguments for weakening demand conditions across the economy, given that the uptick in unemployment has been driven by increases in the number of unemployed rather than increases in labor supply. This is also in line with a certain outflow of foreign workers and a slowdown in wage growth rates during 2024. On the other hand, the total number of registered employees, per State Revenue Committee data, continued to increase by around 34 thousands. This could suggest that labor conditions are tighter than what the household survey suggests. Alternatively, the growth in registered employees could reflect gradual, structural declines in the shadow labor market in favor of formal employment.

In recent months, wage growth in the private sector has accelerated. However, it remains below the level consistent with productivity growth and the inflation target. In the medium and long term, a potential expansion in labor supply

could serve as an additional factor in easing labor market conditions and reducing market-driven pressures. The main uncertainty here is related to the high uncertainty surrounding Russia's economic growth prospects, the flow of Armenian labor migrants to Russia, participation in the domestic labor market, and the integration of economically inactive populations into the workforce.

In the first quarter of 2025, the economy continues to experience a low-inflation environment, largely driven by ongoing deflationary pressures from the external sector and a weakening of foreign demand for certain domestic services. In this context, 12-month inflation has remained below the target since April 2023, reaching 2.5% in February 2025. Non-traded sticky price inflation, which primarily reflect domestic demand-driven price behavior, remained stable at 2.2% year-over-year in February. The increase in global food prices has not yet been fully reflected in domestic prices. On the other hand, the decline in prices for imported non-food goods continues, mainly due to falling producer prices in China. At the same time, prices for certain services have continued to decrease amid weakening external demand. Under these conditions, inflation expectations have also continued to decline, approaching the target level. This is evidenced by both the persistently low inflation environment and household survey results.

Monetary Policy

Market expectations of the CBA policy rate path have adjusted very slightly downward since the latest decisions, and continue to reflect expectations of a gradual reduction in the policy rate over the next eight decisions. The yield curve has shifted downward to some extent, reflecting also to some extent the gradual adjustment of inflation expectations following the reduction in the inflation target. At the same time, per CBA estimates, it is likely that, besides market expectations about the future policy rate, the yield curve also reflects certain other risk factors.

In recent months, Armenia's country risk premium has declined to some extent and remains significantly below the long-term stable level determined by the country's fundamentals. However, it still reflects uncertainties related to debt sustainability, geopolitical risks—including border tensions—and regional developments. In this context, a potential upward adjustment of the country risk premium poses risks for a revision of the neutral rate to the upside, which, all else being equal, could create inflationary pressures due to a more accommodative monetary policy stance. At the same time, Armenia's macroeconomic stability and strong economic growth provide certain positive factors for a possible reassessment of the country's risk premium and a potential reduction in the neutral rate.

Considering the persistence of numerous types of uncertainty, the CBA builds and evaluates several different scenarios for future economic developments in order to manage possible risks stemming from these key areas of uncertainty. The Illustrative Case A Scenario presented in this report (which

requires a higher policy rate path compared to market expectations) is based on the assumption that a possible resolution of the Russia-Ukraine conflict and potential positive developments in Russia's economic outlook could create additional inflationary pressures. These pressures may arise from increased external demand, seasonal migration from Armenia to Russia, and higher inflow of remittances to Armenia. In this scenario, a tighter monetary policy stance compared to market expectations would be more appropriate for the Central Bank of Armenia, considering the potential formation of strong domestic demand and the associated inflationary risks in the near future.

The illustrative Case B scenario presented in this report (which requires a lower policy rate path compared to market expectations) is based on the assumption that significant uncertainties surrounding the economic policies of the new U.S. administration lead to a sharp decline in confidence among households and businesses. As a result, consumer and investment spending is postponed, and economic growth slows significantly.

Given the scale of the U.S. economy, these developments would also contribute to a deflationary environment in global commodity markets and a decline in consumer and business confidence worldwide. Consequently, in the presence of weak external demand and deflationary pressures from the external sector, Armenia would face risks of prolonged weak demand and a low-inflation environment.

In such a situation, the Central Bank would prefer a more aggressive reduction in the policy rate compared to market expectations to stimulate demand in the medium term and bring inflation closer to the target.

In the context of the latent risks and uncertainties in the current period, the CBA builds and discusses various scenarios, summarized in the Taxonomy of Scenarios, with the aim of managing possible risks and assessing sources of uncertainty. At the same time, the MPR includes a deeper dive into two illustrative scenarios, which reflect illustrative future paths of the economy that would require either a higher path for the policy rate (Case A) or a lower path of the policy rate (Case B) relative to current market expectations. These illustrative scenarios do not represent a most-likely future, assign weight or probability to outcomes, or include all possible risks and uncertainties.



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