ARMENIA:

MONETARY POLICY AND ECONOMIC GROWTH "MONETARY POLICY AND ECONOMIC GROWTH" SEL

ASHOT MATEVOSYAN
TATEVIK AZATYAN

ARMENIA:

MONETARY POLICY AND ECONOMIC GROWTH

"MONETARY POLICY AND ECONOMIC GROWTH" SEL

ASHOT MATEVOSYAN
TATEVIK AZATYAN

"Armenia: Monetary policy and economic growth" is an electronic periodical which aims to analyse and briefly represent the overall view and trends of monetary policy and economic growth of RA.

This periodical is published by the team of scientific-educational laboratory "Monetary policy and economic growth" of ASUE. The opinions and conclusions expressed in the periodical belong to the authors and do not necessarily coincide with the official views of ASUE.

MONETARY POLICY IN ARMENIA SHOWS STABLE TREND

- Monetary policy is a set of measures by the state that aimed at regulating money supply or interest rate, which guarantees general economic objectives; price stability, economic growth rates, strengthening of national currency, lending capital market, non-cash payment order.
- Currently, the most widely used strategies are:
  - ✓ targeting of monetary aggregates
  - ✓ exchange rate targeting
  - ✓ inflation targeting.
- The primary goal of the CBA is prices stability, pursuant to the Constitution of Armenia, Article 83.3 and Law on Central Bank of Armenia, Article 4. Since January 1 2006, the CBA officially adopted an inflation targeting strategy which lays down that the forecast of the inflation level is an intermediate goal and the short-term interest rate is an operational goal. Moreover, the CBA is fully independent in the choice of the monetary policy strategy, interim and operational objectives.
- The Central Bank is conducting a freely floating exchange rate regime.
- The monetary policy instruments of CB of RA are:
  - ✓ Refinancing Rate
  - ✓ Lombard Repo Rate
  - ✓ Deposit Rate
- The following describes the current situation in the current monetary policy.

TABLE 1. *Inflation changes*

		Jul. 2016	Aug. .2016	Sep. 2016	Oct. 2016	Nov. 2016	Dec. 2016	Jan. 2017	Feb. 2017	Mar. 2017	Apr. 2017	May. 2017	Jun. 2017	Jul 2017
Inflation of RA		-1,3%	-1,9%	-1,9%	-0,9%	-0,6%	-1,1%	-0,6%	-0,2%	-0,1%	1,2%	1,6%	1,1%	0,9%

- In the fourth quarter of 2016 and the first quarter of 2017, in spite of deflationary risks, the 12-month inflation rate has notably increased to-0.1%, at the end of March (year 2016 ended with -1,1%), as was expected. It should be noted that inflationary developments in this period of time have mostly incurred the influence of expansionary monetary policy implemented by the Central Bank. expansionary monetary policy implemented by the Central Bank.
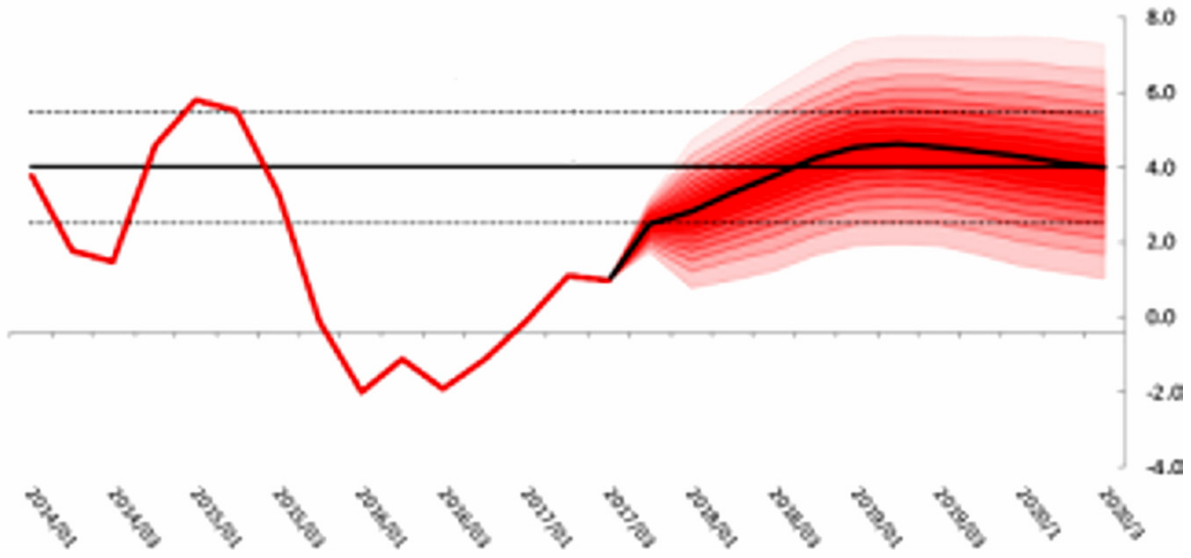
CHART 1. *Inflation (12 month) Forecast Probability Distribution Chart for 3-year horizon (Chart is taken from official website of Central bank of Armenia)*

- Inflation will continue rebounding in the medium term, starting from 2018 it will be within the confidence band, approaching the target. At the end of 2018 and during 2019 it will even slightly outstrip the 4% target, by the forecast of CB. From 2018 to the end of the forecast horizon, inflationary risks go upward, largely due to the expansion of the inflation environment in international commodity markets and the pace of recovery in domestic demand.
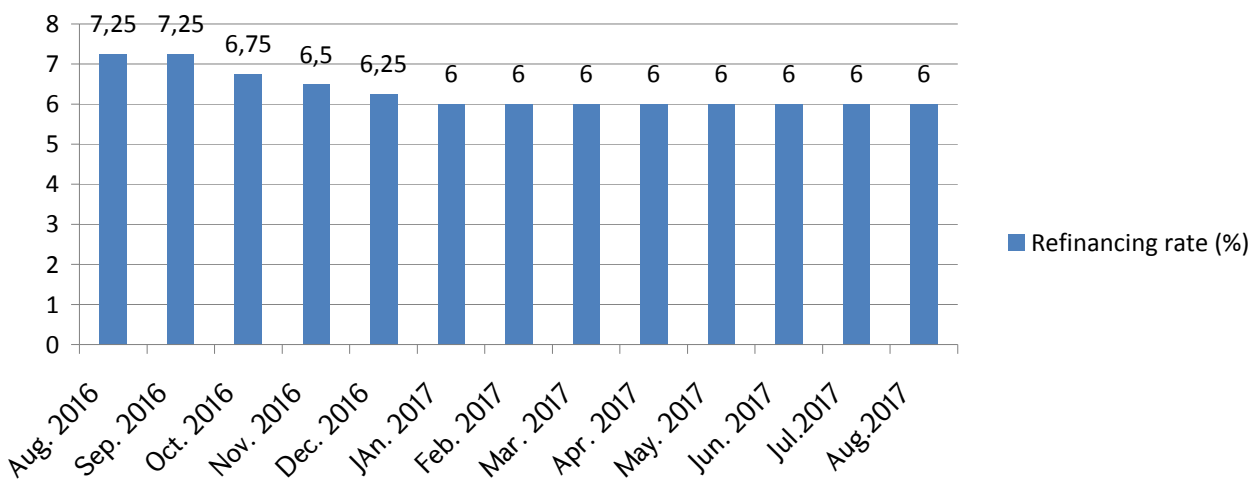

CHART 2. *Refinancing rate (%)*

- In consideration of the domestic demand persisted at a low between October 2016 and March 2017, th defletionary effects from the external sector transmitted onto food products and, later on, non food products, as well as anticipated impact of the Government's contractionary fiscal policy in 2017, the Central Bank continued in the mean time to mitigate the lending terms by reducing the refinancing rate by 0,75 pp to 6,0% at the end of February.
- In such a situation, the CB reckons, the monetary policy previously proved rather expansionary for the inflation to

recover and would still have its impact transmitted by the end of the year. Therefore, the Central Bank left the monetary conditions unchanged during the second and the third quarters, keeping the refinancing rate at 6%. In the fourth quarter, as the inflation environment expanded and inflation expectations grew, the central Bank again left refinancing rate unchanged, yet the financial market has already been signaled that stimulating monetary conditions would need to be abolished gradually in the light of forecast developments.
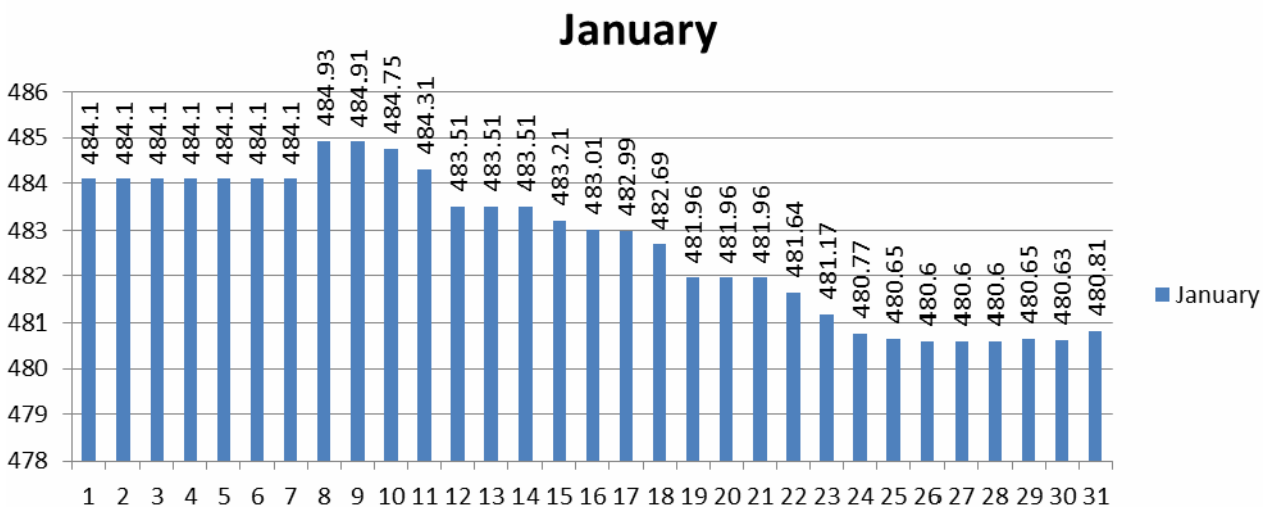

CHART 3. *Calculated exchange rate of 1 US dollar / AMD set by the Central Bank of Armenia for January*

- The minimum exchange rate of 1 US dollar / dram set by the Central Bank of Armenia was 480.60 in January, the

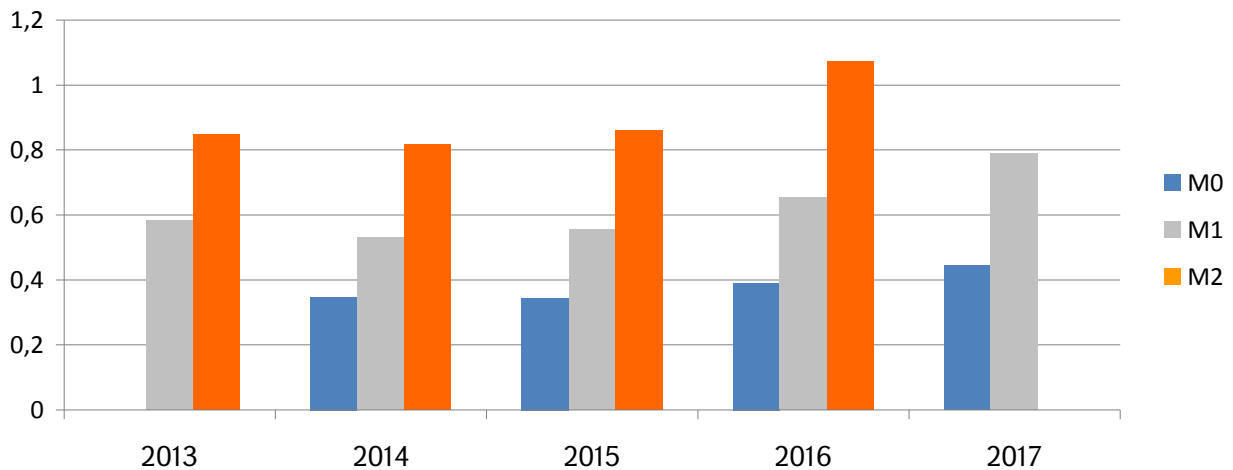maximum was 484.93 and the average was 482.74.

CHART 4. *Change of monetary aggregates in 2013-2016*

- In the Republic of Armenia for 2013-2016 M0 increased by 1.6%, M1 increased by 12.23%, M2 increased by 26.6%.

TABLE 2. *Comparison of Mathematical Trends of Armenian Monetary Aggregates in 2005-2016*

	R^2			Y		
	M_0	M_1	M_2	M_0	M_1	M_2
RA	0.6	0.7	0.8	0,1269 ln(x)+0,1769	0,2361 ln(x)+0,2269	0,4547 ln(x)+0,2141

- The level of monetization shows the increase in money supply and GDP ratio. It should be understood that the analysis of money demand also affects the monetization.
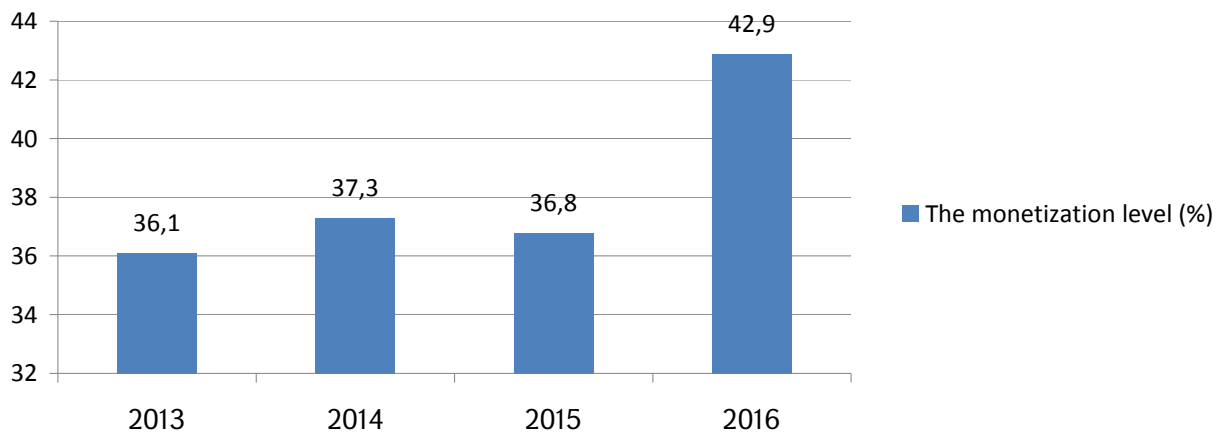

CHART 5. *Level of Monetization in the Republic of Armenia (%) 2013-2017*

- Monetization factor is a function of national monetary demand. In 2016 the level of monetization in Armenia was 42.9%.
- The Indicator of Economic Activity (IEA) is a monthly aggregate indicator of the actual volumes' changes of output in the country's economy. It covers all types of economic activity and is initially calculated at the average annual prices of the previous year, which allows to have a real change in the volume of output for the month of the previous month compared to the same month of the previous year and to create

chronological series of chains of indexes. For each month, it is an aggregate index for the entire economy, as an index. The behavior of the index of economic activity in the Republic of Armenia for 2017 is presented in Chart 6. In the observed period, the highest value recorded in economic activity index was up 117.2 percent in October, over the corresponding period of the previous year. It should be noted that in January to December, the index of economic activity against the corresponding period of the previous year has shown an upward trend– 7.7 %.
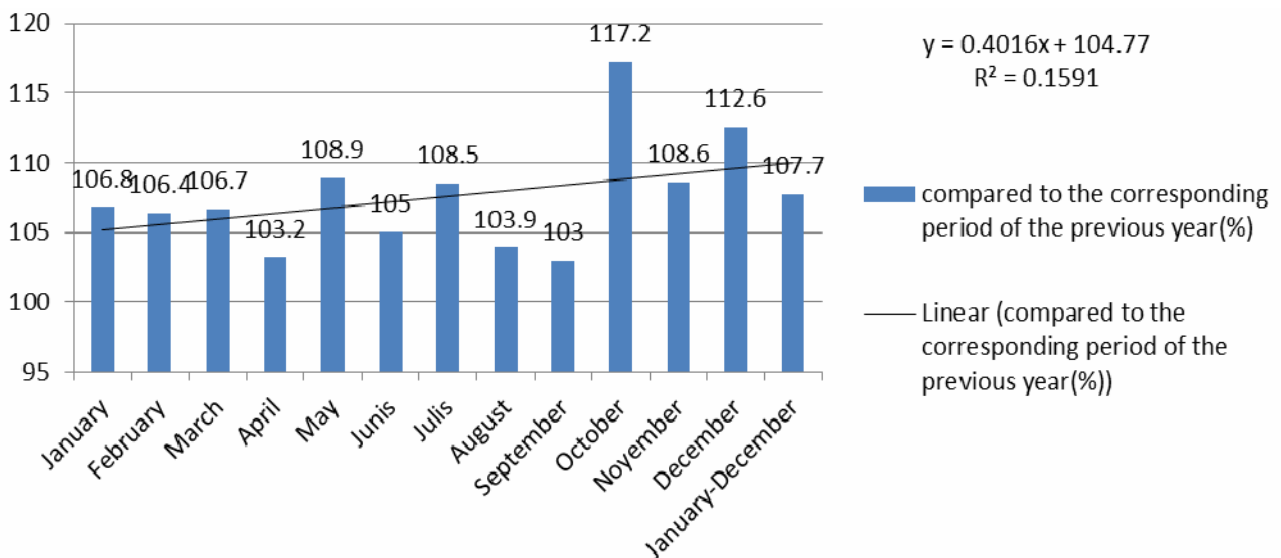

$$y = 0.4016x + 104.77$$
$$R^2 = 0.1591$$

CHART 6. *The behavior of the index of economic activity in 2017 January to December*

- The behavior of Economic Growth in Armenia in 2004–2017 is presented in Chart 7. This indicator had the highest value in the observed period in 2005 – 13.9%, and the lowest value in 2009 –

14.1%. The economic growth in the Republic of Armenia has dropped by 3.3% including 2012 year. In October of 2017, the economic growth in the Republic of Armenia was 3.5%.
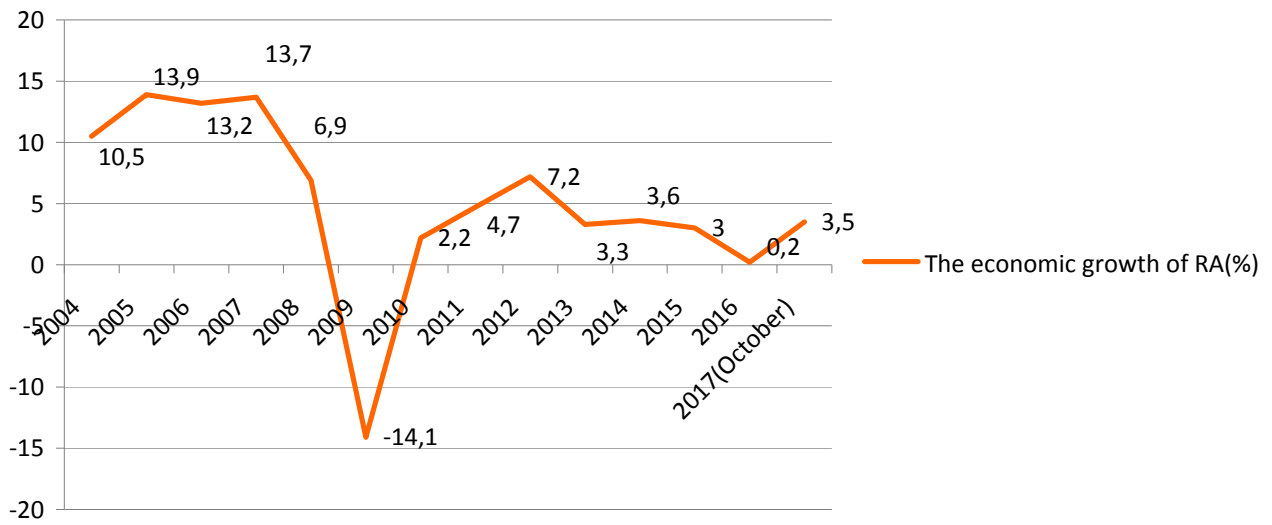
CHART 7. *The economic growth of RA (%) in 2004-2016.*