
Central Bank Of Armenia Lifts Interest Rate Further As Inflation Accelerates

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The Board of the Central Bank of Armenia (CBA) in their 2 April meeting decided to lift the CBA's annual refinancing rate by a further 25 basis points, ARKA News reports. This move takes the main policy rate to 6.5%. The interest rate was increased by a similar magnitude in March as well as February, having been left unchanged in January. The Board indicated that high and accelerating inflation in international food markets over the first quarter of the year has been reflected in Armenian food prices, further leading to rising cost of non-food goods and services.

Indeed, ARKA News further reports that consumer prices in Armenia in March increased by 1.4% month-on-month (m/m), leading to the annual inflation rate shooting up to 9.6%. The corresponding rates in February registered 1.1% m/m and 7.5% year-on-year (y/y). Compared with the end of 2007, Armenian consumer prices increased by 4.8% by the end of March, further data from the National Statistical Service show. The CBA board pledges gradual further tightening of monetary and credit policy in order to contain near term inflationary pressures, to allay inflation expectations and to counteract the secondary effects that risk arising from the external inflation forces. Armenian consumer price inflation ended year 2007 at 6.6%, averaging 4.4% for 2007 (see Armenia: 2 January 2008:).

Significance: The CBA's inflation-targeting policy has proved relatively successful over recent years, even if implying strong appreciation of the dram exchange rate, in conditions of strong foreign remittance and FDI inflows. However, over March, the exchange rate of the dram against the U.S. dollar was reported to have remained virtually stable, while the first quarter of the year witnessed weakening of the dram. In addition to Armenian inflation being pushed upwards from the cost side due to high prices of food, also demand side price pressures persist, as the robust GDP growth has proved somewhat more reluctant to cool than we previously expected. Domestic demand is partly boosted by fiscal spending.

Adding these recent overheating signs to the effect of persistently high food and energy prices, inflation pressure in Armenia is likely to remain considerable in the near term, making achieving the target specified by the CBA at 4% (with 1.5% on either side) a challenging task.
