
CBA Forecasts 5.4 Inflation for 2008

NOYAN TAPAN - 15/1/2008

According to forecasts of the Central Bank of Armenia (CBA), by the version of the unchanged level of interest rates, inflation will make 5.4% in Armenia in the 12-month period following December 2007 and 6.3% in the second quarter of 2008. The base scenario of inflation until the end of the second quarter 2008 includes the version that a growth in prices of bread products, butter and vegetable oil will contribute to the growth of the cumulative consumer price index by 3.8%, while the growth of gas prices due to the supposed end of budgetary subsidizing will contribute to the growth of this index by 1.2%. These forecasts were announced at the December 29 sitting of the CBA Board.

According to the CBA press service, by CBA's forecasts, the formation of higher international oil and food prices (including grain prices) than is expected may contribute to higher actual inflation than the forecast index, while the increase of oil prices will depend on both geopolitical and external economic developments. Besides, it may be also contributed by a higher than forecast growth of the consumption component in the overall demand and further positive deviation from the balanced level of consumption, as well as by higher than expected growth rates of crediting of the economy.

The registration of a lower actual inflation index than is forecast may be contributed by an increase in foreign currency amounts of exports (as a result of higher than forecast prices of base metals), as well as by a fall in prices of imported goods under conditions of greater capital inflow, as a result of appreciation of the dram.

At the same time, developments in the agricultural sector which mainly depend on climatic conditions may involve risks of both a fall and rise in prices.

Taking into account the developments in the fourth quarter of 2007 and the CBA's forecasts for the further 12-month period, the CBA Board registered that despite some stabilization of oil and food prices, the inflation pressures from the external environment remained at the end of the fourth quarter of 2007 and will remain in the forecast period. In case of absence of unexpected shocks in the external environment, these pressures will be milder than in the past period. The CBA Board also stated that the impact of the internal environment created smaller inflation pressures than was forecast - in the fourth quarter of 2007, while it is possible that combined with most expanding tax and budgetary policy, the high growth rates of private consumption will increase inflation pressures to some extent in the forecast period. In these conditions the CBA Board still sees risks in ensuring the 2008 target inflation index.

At the same time the CBA Board discussed the seasonal manifestations, which are typical of Armenia's economy and financial sector and are most pronounced at the beginning of a year, particularly a sharp decline in demand for money in January, due to which a rise in interest rates cannot have the desired effect on interest rates in the interbank market. It was underlined that the consistent tightening of the conditions of the monetary and credit policy by the CBA in recent months allows to refrain from raising the interest rates at the given moment.

Under conditions of various opinions about reduction of inflation pressures from the external environment, the deviation of inflation from the central position of the target interval, and the possible scenarios of further changes in interest rates, the CBA Board discussed the options of either raising the CBA refinancing interest rate or leaving it unchanged.

As a result, at the December 29 sitting the CBA Board made a decision to leave the CBA refinancing interest rate unchanged - 5.75%. The pawn credit and deposit interest rates were fixed at 8.75% and 2.75% respectively.

At the same time the CBA Board expressed a willingness to be consistent in the issue of correcting the interest rates if inflation pressures from the internal and external environments do not decline.
