
CBA Board Considers It Expedient To Reduce Gradually Interest Rates

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At the January 13 sitting, the Board of the Central Bank of Armenia (CBA) made a decision to reduce the CBA refinancing rate by 0.25% to 7%. The interest rates of attracted deposits and lombard credits were established at 4% and 10% respectively.

The decision was made based on the situation report, which assessed, by using new information, the forecasts about the current situation, the risks and the new macroeconomic forecasts as well the possible risks related to these forecasts. The situation report also contained new results received by using the CBA quarterly forecast model, and these results continue bearing evidence of the tendencies to deepening deflation environment.

The CBA PR Service reported that only 0.1% inflation was recorded in December on November 2008, as a result of which the 12-month inflation fell by 1.4 percentage points and made 5.2%, ensuring the target level of inflation. The fall in inflation rates was mainly conditioned by the continuous fall of prices in international markets of goods and raw materials because of the global recession and became apparent in domestic markets of these goods as well. Following the fall in November, a 15% fall in diesel fuel prices and a 3.5% fall in gasoline prices was recorded in Armenia in December. On the whole, the inflation recorded based on the results of the year was due to a growth in prices of food commodities (including alcoholic drinks and cigarettes) - 3.3% nonfood commodities - 0.2% and a growth in tariffs of services - 11.4%.

The members of the CBA Board agreed that the external inflation pressures continued to weaken due to the tendencies to a decline in global economic growth rates and became apparent in the domestic markets of food and nonfood commodities, resulting in a considerable fall in overall inflation rates. In the opinion of the CBA Board, although the uncertainty of foreign and domestic economic developments has increased, the clarifications to the forecasts on economic growth in foreign countries, especially Armenia's trade partners, show that the external deflation environment continues to remain. Under these conditions it is expected that in mid 2009 inflation will form in the lower part of the target interval.

The CBA Board discussed the risks concerning a fall or growth of forecast inflation. As a result, the risks towards a decline were considered as prevailing in the overall balance of risks.

The Board also discussed in detail the possible impact of consequences of the global economic crisis on domestic economic developments in 2009. It was mentioned that the prospects of external demand continue to become worse, which will have its impact, especially on the export sector of domestic economy, leading to further decline in production volumes in the exporting branches. The impact of the global economic crisis will also be seen in construction because of declining inflow of financial resources from abroad and the delay in financing of some investment programs. The slowing rates of inflow in the form of noncommercial transfers will be conditioned by Russian economy's capacities to overcome the consequences of the economic crisis. At the same time, it was mentioned that the forecast domestic economic developments will depend very much on the scale and directions of the additional economic programs that the government plans to implement.

Underlining the importance of the situation that has formed in conditions of the global financial and economic crisis, the members of the CBA Board focused on two possible scenarios of mitigating the monetary and credit conditions: 0.25% and 0.5% reduction of the refinancing rate. In this connection the Board has repeatedly stressed the necessity of conducting such a monetary and credit policy that will allow to combine efficiently the tasks of ensuring price stability and financial stability. There were arguments that the current interest rates continue being attractive for capital inflow. At the same time, a sharp reduction of interest rates at this moment is likely not to have desirable consequences for interest rates of the interbank market, therefore for the monetary and credit transfer chain. The Board attached great importance to an increase of credits for implementation of measures and to improvement of credit accessibility. On the other hand the continuous fall in inflation rates and the existence of risks towards a fall was put forward as the main argument for sharper reduction in interest rates. As a result, the CBA Board considered the version of gradually reducing the interest rates as most well-founded.

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