- *Despite rising COVID cases, the economy grew by a robust 3.8 percent year on year (yoy) in March.*
- *The pace of vaccination has picked up, but remains slow, at an estimated 0.35 percent of the population as of May 7.*
- *Inflation continued to increase, to 6.2 percent in April, prompting the CBA to increase the policy rate by 0.5 percentage points.*
- *Foreign trade improved as domestic activity picked-up and external demand was robust.*
- *Despite a decent revenue performance, the budget deficit increased in March driven by higher spending.*
- *Banking sector intermediation remained sluggish in March.*

The economy grew by a robust 3.8 percent yoy in March, following a 5.3 percent yoy contraction in February. The Economic Activity Index (EAI) registered positive yoy growth for the first time since February 2020, reflecting, in part, a base effect as COVID related restrictions were introduced in March 2020. The pick-up was led by the construction sector (11 percent yoy growth), mining (19 percent yoy growth) and industry (3.8 percent yoy growth). In addition, while manufacturing continued to contract in March, by 4 percent yoy, this represents an improvement from February when it contracted by 14 percent yoy. Services, the hardest hit sector during the pandemic, picked up marginally (less than 1 percent yoy growth). On a cumulative basis, the EAI remains in negative growth territory, contracting by 2 percent yoy in the first quarter of 2021. On the demand side, recovering wages and resilient transfers from abroad added to consumption, while a faster recovery in exports meant a lower drag from net-exports.

The recovery appears to have continued despite intensity of the outbreak varying. COVID-19 cases picked up sharply in March and early-April, together with a pick-up in the daily test positivity ratio from an average of 5.5 percent at end-February to 21 percent at the peak in mid-April. The intensity of the outbreak has since eased, with new infections more than halving from their peak in early-April and test positivity rates declining to 12 percent in the first week of May. As no additional restrictions were imposed during the third wave, mobility was not impacted, remaining above 90 percent in this period in Yerevan compared with pre-COVID levels. The pace of vaccination has been slow – as of May 7, only 0.35 percent of the population (10,281 people) have received a vaccine shot. As of May 10, Armenia has received a total of 153,000 vaccines.

Inflation picked up further in April, prompting a further increase in the monetary policy rate. Inflation reached 6.2 percent yoy, exceeding the target range of the Central Bank of Armenia (CBA). Prices of food and non-alcoholic beverages increased sharply in April (8.3 percent yoy) driven by transmission from higher international food and oil prices and a weaker dram. The prices of other consumption items also grew in April, especially in transport (11 percent yoy). Taking into account the continued external inflationary pressures and emerging pressures from domestic sources, the CBA increased the policy rate by 0.5 percentage point in early May. At 6 percent, the policy rate is at the highest level since January 2019.

Goods foreign trade grew by 11 percent yoy in March, with both exports and imports increasing. Buoyed by domestic demand, imports grew by 5 percent yoy, with import of machines and equipment (up 26 percent yoy) growing sharply. Exports grew by 22 percent yoy, with two-thirds of the increase accounted for by higher copper exports, reflecting both higher volumes as well as higher prices. In the first quarter, in cumulative terms, exports grew by 3.4 percent while imports registered an 8.7 percent decline, implying a significant improvement in the trade balance (by 23 percent).

The pressure on the dram has eased since mid-April. By May 6, the dram appreciated by 2.5 percent against the USD as compared to a month ago. This reflected the smaller trade deficit, as well as a slight rebound in tourist arrivals and an increase in net transfers from abroad (by 2.5 times in March, yoy). After declining in March, international reserves were stable in April, and at USD3 billion provided 7 months of import cover.

The budget registered AMD 74 billion deficit in March, up from AMD 47 billion deficit in February. This brought the deficit in the first quarter of 2021 to AMD 55 billion (0.9 percent of annual projected GDP). The high deficit in March was driven by a sharp increase in spending (53 percent yoy increase). In terms of function, defense spending (over three-fold increase) and social spending (79 percent yoy) increased sharply. In terms of economic classification, capital expenditures showed a nearly eight-fold increase. Total revenues increased by 2 percent yoy in March, as robust collection of VAT, customs and environmental taxes offset weak performance of income taxes.

Banking sector intermediation was sluggish, while soundness indicators remain stable. Credit (adjusted for FX changes) remained flat on yoy basis, while deposits recovered slightly, by 1 percent yoy. The trend in growing non-performing loans was reversed in March, while profitability declined. Capital adequacy ratio, at around 17 percent, remained well above the 12 percent minimum threshold.

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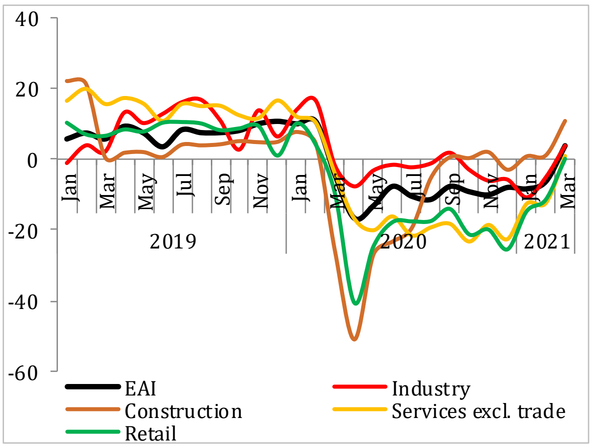
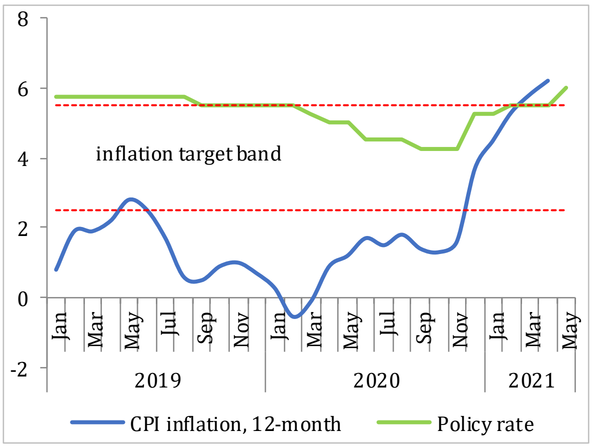
Figure 1. Economic recovery picked-up pace in March.
(Economic activity index, yoy change, in %)



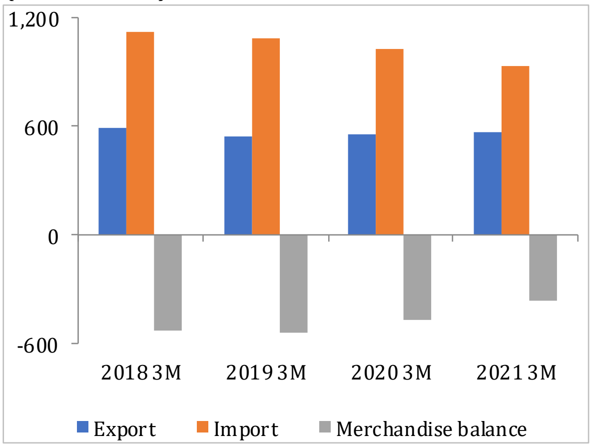
Source: Statistical Committee of RA

Figure 2. Inflation continued to rise, moving further away from the CBA target higher band
(CPI Inflation, y-o-y change, in %)



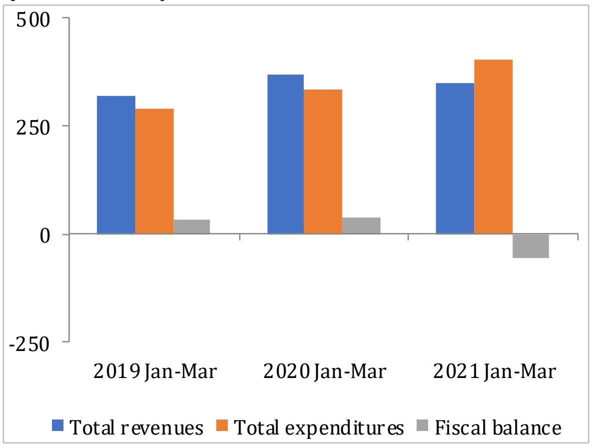
Source: CBA

Figure 3. Imports and exports grew in March, and the trade deficit narrowed
(in USD million)



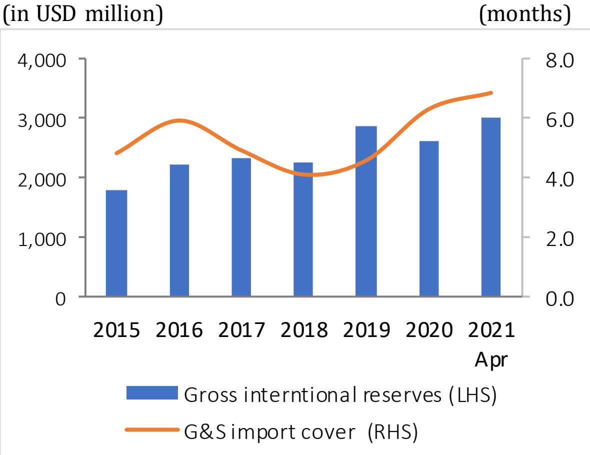
Source: Statistical Committee of RA

Figure 4. The budget registered a deficit in the first quarter due to higher expenditures
(in AMD billion)



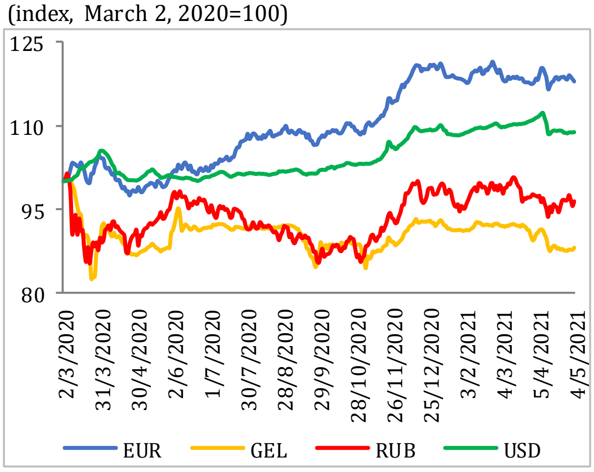
Source: MOF

Figure 3. International reserves were stable in April and provided 7 months of import cover
(in USD million) (months)



Source: CBA

Figure 4: The pressure on the dram has eased since mid-April
(index, March 2, 2020=100)



Source: CBA

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