Economic activity recovered marginally, with EAI contracting by 7.5 percent yoy in September compared to a 9.8 percent yoy decline in August. Industrial output grew by 1.8 percent yoy, benefiting from a 12.8 percent yoy growth in mining. Construction also posted a small positive growth (0.6 percent yoy), its first since the start of the pandemic. Services (excluding trade) remained in deep contractionary territory (18.3 percent yoy decline). Trade volumes were down 14.1 percent yoy. Agricultural output was relatively flat (0.4 percent decline in the third quarter). Year-to-September, the EAI has contracted by 6.6 percent, with sharp declines in private consumption amid stagnant wage growth, and weak investment offset only in part by import compression.

The recovery could be short-lived as COVID-19 infections spiked and the conflict and subsequent political tensions affect sentiments. The number of COVID-19 cases increased rapidly since late-September, coinciding with a lifting of the State of Emergency related to the COVID-19 pandemic, the subsequent opening of schools and more gatherings as the result of war in Karabakh. By early-November, daily new cases far exceeded the previous peak in early July. Consequently, weekly average mobility in Yerevan has declined sharply from 73 percent of pre-COVID-19 levels on September 30 to 52 percent by October 30. This, together with the month and a half long conflict with Azerbaijan and political turmoil following the November 10 agreement on cessation of hostilities will likely weigh on the economic recovery.

Inflation declined slightly to 1.3 percent yoy in October and remains below the CBA target band (4 +/- 1.5 percent). Food prices increased by 0.6 percent yoy while prices of alcoholic beverages and cigarettes grew by 9.7 percent yoy. Transport prices continued to recover, registering a 1.1 percent yoy increase in October as compared to a 0.4 percent drop in September. Despite subdued inflation, on October 27, 2020, the Central Bank of Armenia kept the policy rate at 4.25 percent, citing the need for accommodation to support economic recovery amid rising uncertainty and rising risk premia arising from intensified conflict.

The trade deficit narrowed in September, and the dram weakened slightly before stabilizing. Exports increased by 4.6 percent yoy in September, the first positive growth rate since the start of the pandemic and driven by a 16 percent yoy increase in mineral exports and a 7 percent yoy increase in exports of precious stones and metals. Imports remained weak, contracting by 22 percent yoy in September, with a sharp increase in machinery and equipment import (92 percent yoy increase) fully offset by declining imports across the board. The trade deficit narrowed to USD 154 million in September, a 43 percent improvement from a year ago. Inflow of money transfers (a proxy for remittances) increased by 7 percent yoy in September, helping partially offset lower services receipts, with tourist inflows yet to increase despite a limited re-launch of international flights since August. Reserves declined to USD 2.3 billion at the end of October, providing cover for around 5.7 months of imports. The dram weakened in the first month of the conflict (by 1.8 percent) but has stabilized in the last few weeks.

The budget deficit narrowed to AMD 20 billion in September, as spending growth decelerated. Current spending declined by 0.2 percent yoy, with increases in social payments and grants offset by declines in spending on goods and services. Capital spending increased by 9 percent yoy but remains well below the annual plan. Revenues declined by 9 percent yoy in September, weighed down by lower customs and VAT collections. The year-to-date deficit increased to 2.4 percent of projected annual GDP in September from 2.1 percent of GDP in August, financed by domestic borrowing. Government debt at the end of September reached 59.1 percent of projected annual GDP. The 2020 Budget was amended in October with the deficit projected at 7.4 percent of GDP reflecting the deteriorated outlook and higher conflict-related spending. The draft 2021 Budget is currently under discussion in the National Assembly.

Financial stability indicators improved in September. Non-performing loans (NPLs) declined to 6 percent of gross loans in September from 6.5 percent in August but remain above last year’s levels. Profitability remained flat and banks remain well capitalized. Credit grew by 1 percent in September over August, bringing the annual growth rate to around 14 percent (excluding exchange rate impact) from 18 percent yoy pre-COVID. Deposit growth also slowed (to 7.5 percent yoy) Dollarization remains high, with half of credits and more than half of deposits denominated in foreign currency.

Prepared by: Armineh Manookian, Economist, amanookian@worldbank.org
The economic recovery picked up pace in September…
(Economic activity index, yoy change, in %)

Figure 2. …but the outlook is weak due to rising COVID-19 cases and declining mobility
(COVID-19 new cases, 7-day mobility average)

Inflation remains subdued and well below the CBA lower target band
(CPI Inflation, y-o-y change, in %)

Trade deficit narrowed further with a pick up in exports
(in USD million)

The budget deficit increased marginally in September
(in AMD billion)

The dram weakened in the immediate aftermath of the conflict but stabilized recently
(index, March 2, 2020=100)