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RAEX-Europe confirmed at 'B+' the credit ratings of Armenia. The rating outlook is stable.

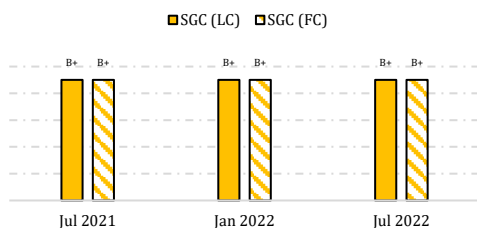
RAEX-Europe confirmed the sovereign government credit ratings (SGC) of Armenia at 'B+' (moderately low level of creditworthiness of the government) in national and at 'B+' (moderately low level of creditworthiness of the government) in foreign currency. The rating outlook is stable, which means that in the mid-term perspective there is a high probability of maintaining the rating score.

Ratings

Sovereign Government Credit (LC)	B+
Sovereign Government Credit (FC)	B+
Outlook (LC)	Stable
Outlook (FC)	Stable

* These ratings are unsolicited

Ratings dynamics



Main Economic Indicators of Armenia

Macro indicators	2019	2020	2021
Gross gov. debt, AMD bn	3278	3924	4210
Nominal GDP, AMD bn	6543	6182	6983
Real GDP growth, %	7,6	-7,4	5,7
Gross gov. debt/GDP, %	50,1	63,5	60,3
Deficit (surplus)/GDP, %	-1,0	-5,4	-4,6
Inflation rate, %	0,7	3,7	7,7
External debt, USD bn	5,8	5,6	7,0
Development indicators	2021		
Inequality adj. HDI	0,70**		
GDP per capita, USD th	14,7		
Default indicator	8.01.2021		
10Y Gov Bond Yield, %	9,07***		

Source: RAEX-Europe calculations based on data from the IMF, WB, UN, Armenia Ministry of Finance, CBA.

*Preliminary figures ** Figure from 2019 ***Maturity in 2029

Summary

The ratings of Armenia were confirmed at 'B+' and the outlook remains stable. This mainly reflects the rebound of the economy after the initial effects of the COVID-19 outbreak and decrease in the budget deficit and debt levels by the end of 2021. On the other hand, growth of the inflation rate, slow progress of the vaccination campaign in 2021, sanctions imposed on the country's main trade partner Russia and such inherent factors as demographic pressure and high level of dollarization, are negatively affecting the rating assessment.

Armenian economy experienced a rebound in 2021. As of the end of 2021, the real GDP grew by 5,7% y-o-y which is a considerable increase after a 7,4% pandemic-related contraction of the economy in 2020 (see graph 1). This growth accelerated mainly in 4Q 2021 due to the strong performance of construction, manufacturing and trade sectors of the economy, as well as the increase in metal ore exports due to the strong external demand and high copper prices.

Further economic growth will depend on three major factors. At first, on the development of the pandemic in the country and effectiveness of epidemiological measures and vaccination campaign that drive household consumption and development of the tourism industry. Secondly, although at the current moment the situation in the Nagorno-Karabakh region is stabilized, the potential tensions may lead to financial instability and undermine growth. Last but not least, the military conflict in Ukraine and sanctions imposed on Russia represent a threat to the Armenian exports and lead to the decrease of remittances from the largest trade partner Russia which in turn negatively affects private consumption. Taking these factors in consideration, we expect the growth of Armenian economy to shrink to 1,5% in 2022.

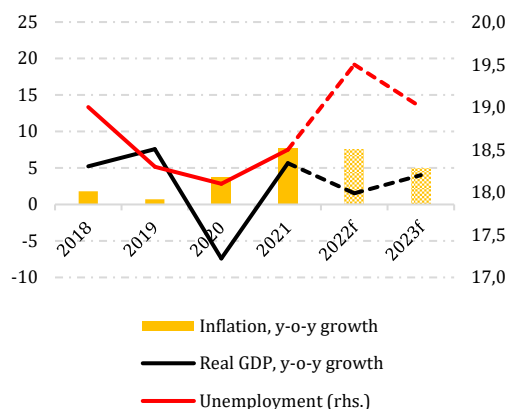
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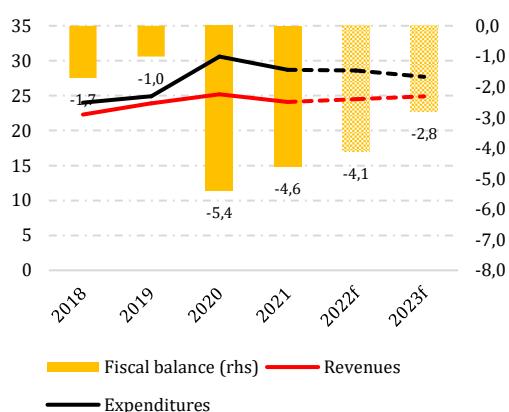
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Graph 1: Macroeconomic indicators, %

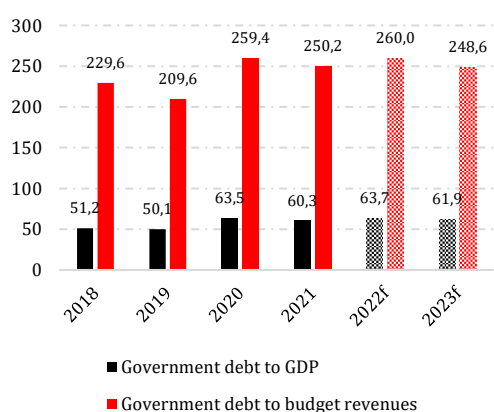


Source: RAEX-Europe calculations based on data from the IMF

Graph 2: Fiscal budget dynamics, % of GDP



Graph 3: Government debt dynamics, %



Source: RAEX-Europe calculations based on data from the IMF and Ministry of Finance of the Republic of Armenia

Fiscal deficit and debt load decreased in 2021. By the end of 2021, government expenditures decreased to 28,7% of GDP and government revenues to 24,1% of GDP which led to a decline of the current account deficit by 0,8p.p to 4,6% of GDP. We expect the deficit to decrease further down to 4,1% of GDP in 2022 and reach the government fiscal consolidation target of 3% of GDP not earlier than in 2023 due to the effects of the Russia-Ukraine conflict (see graph 2).

In 2021, the level of central government debt showed a slight decrease by 3,2p.p. to 60,3% of GDP after the pandemic-induced rapid increase in 2020. Relative to budget revenues it declined to around 250% and we expect it to go up to 260% in 2022 (see graph 3).

The IMF has completed its fourth and fifth reviews of Armenia under the SBA. The amount of funds within this program is about USD 72 m (SDR 51,32 m) bringing total disbursements to just below USD 400 m. These money will help the Armenian economy recover from the heavy economic implications of the Covid-19 pandemic and advance the government's 2021-2026 economic program focused on the export orientation and investment drivers.

The inflationary pressure is still high. By November 2021 CPI reached its peak of 9,6% and then decreased to 7,7% by the end of the year. It is still significantly higher than the CBA target of 4% and outside of the target interval of 4±1,5%.

As a response, CBA raised the refinancing rate three times in 2021 and, due to persisting inflationary environment, it was raised again in February 2022 by 0,25p.p. to 8% (see graph 4). The efficiency of the transmission mechanism of the monetary policy is, however, weakened by the high level of financial dollarization: as of May 2022, FX deposits constituted 42,4% of total deposits and FX loans – 41,7% of total loans (see graph 5).

The banking sector is showing signs of strengthening. The banking sector of Armenia remains sufficiently capitalized: capital adequacy ratio is stable: it slightly increased from 16,9% in 1Q 2021 to 17,2% in 1Q 2022. ROA has been gradually declining from 1,6% to 0,8% in 2Q 2021 and then marginally grew to 0,9% in 3Q 2021 and to 1,1% in 4Q 2021. In 1Q 2022 it reached a long-time peak of 2,3%. NPLs to total loans have also been showing a positive dynamics: the metric decreased to 1,9% in 4Q 2021 and to 1,8% in 1Q 2022. Concentration of the banking system on the three largest banks (Ameriabank, Armbusinessbank and Ardshinbank) remains high.

External position is recovering from the pandemic. In 2021 exports showed a slightly better dynamics than imports supported by shipments

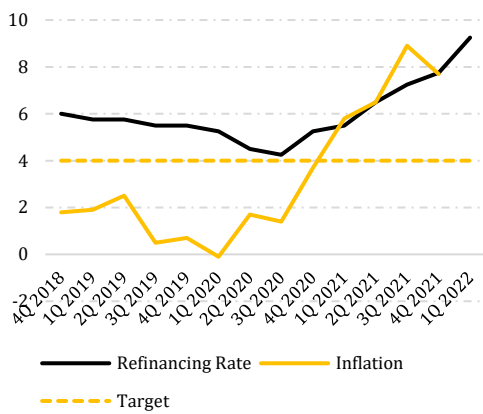
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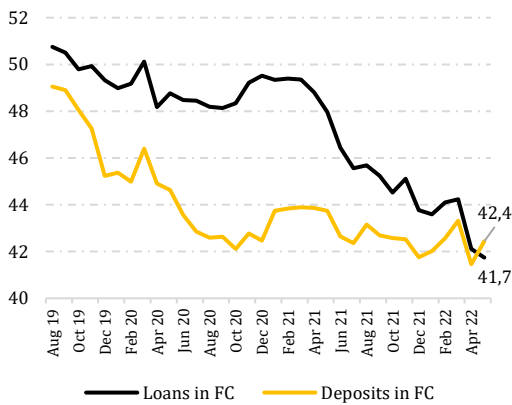
Graph 4: Target vs inflation rate, %



Source: RAEX-Europe calculations based on data from the CBA, IMF and EBD

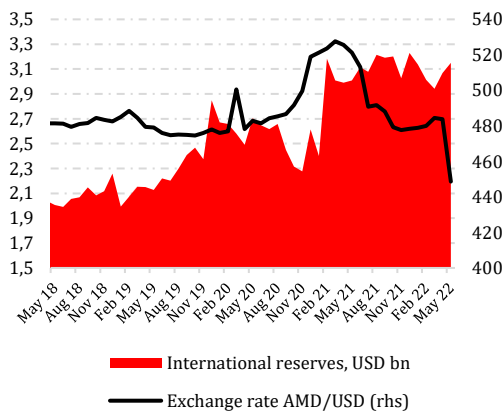
of metals and textile products due to higher international prices. Foreign exchange reserves increased from 2,6 to 3,2 bn USD between December 2020 and December 2021 and remained at the same level in the 1Q 2022. The overall amount of FX reserves currently covers about 5,6 months of Armenia’s imports. The AMD was strengthening in 2021 and reached its pre-pandemic level of about 480 AMD/USD in the end of 2021 and strengthened even further to about 400 AMD/USD in the 2Q 2022 (see graph 6).

Graph 5: Financial dollarization, % of total



Source: RAEX-Europe calculations based on data from the CBA

Graph 6: International reserves and exchange rate



Source: RAEX-Europe calculations based on data from the WB, IMF and CBA

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Stress factors:

- Financial dollarization remains high; loans and deposits in FX were equivalent to 41,7% and 42,4% of total loans and deposits respectively as of May 2022 (weak stress-factor);
- The escalation of the conflict with Azerbaijan for the Nagorno-Karabakh and the probability of its further development as well as sanctions imposed on Armenia's largest trade partner Russia due to the military conflict in Ukraine are another downside risks affecting the ratings.

The following developments could lead to an upgrade:

- Faster and stronger than expected recovery of the global economy, as well as the main trade partners, including Russia, which can lead to an improvement of the external position of Armenia and a faster recovery from the current crisis;
- Substantial decrease of the public debt and deficit metrics on a recovery phase of the economic cycle;
- Consistent reduction in the dependence on external factors combined with a steep decrease in levels of financial dollarization.

The following developments could lead to a downgrade:

- Continued lock-down measures in the country and longer period of turbulence in the global economy, including the second wave of COVID-19 pandemic, which would lead to a further deterioration of the external position, as well as a deeper contraction of local economy;
- Higher than expected increase of the government debt and deficit metrics due to the need of additional financing for the government expenses, and underperforming of tax and external revenues;
- Substantial deterioration of the stance of the banking system with sharp growth of NPLs levels, a drop of profitability and capitalization metrics, combined with a lack of liquidity in the system.

ESG Disclosure:

Inherent factors

- Quality of fiscal policy; quality of monetary policy; natural resources; natural and climatic threats; environmental threats; level of corruption, CPI; Government Effectiveness Index; quality of the business environment; position in Doing Business Ranking; level of investment in human capital, adjusted for inequality; Rule of Law Index; transparency of government policymaking Index; level of information transparency of the government; Political Stability and Absence of Violence/Terrorism Index; natural disasters, constant exposure to difficult natural conditions.

Drivers of change factors

- None.

Next scheduled rating publication: TBD. The full sovereign rating calendar can be found at [Sovereign Rating Calendar 2022](#).

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RATING HISTORY:

Date	Review reason	SGC		Outlook	
		National currency	Foreign currency	National currency	Foreign currency
07.01.2022	Scheduled revision of both types of ratings for the country	B+	B+	Stable	Stable
09.07.2021	Scheduled revision of both types of ratings for the country	B+	B+	Stable	Stable
08.01.2021	Scheduled revision of both types of ratings for the country	BB-	BB-	Negative	Negative
10.07.2020	Scheduled revision of both types of ratings for the country	BB-	BB-	Stable	Stable
10.01.2020	Scheduled revision of both types of ratings for the country	BB-	BB-	Positive	Positive
12.07.2019	Scheduled revision of both types of ratings for the country	BB-	BB-	Positive	Positive
18.01.2019	Scheduled revision of both types of ratings for the country	BB-	BB-	Stable	Stable
20.07.2018	Scheduled revision of both types of ratings for the country	BB-	BB-	Stable	Stable
26.01.2018	Scheduled revision of both types of ratings for the country	BB-	BB-	NA	NA
28.07.2017	Scheduled revision of both types of ratings for the country	B+	B+	NA	NA
03.02.2017	Scheduled revision of both types of ratings for the country	B+	B+	NA	NA
05.08.2016	Scheduled revision of both types of ratings for the country	B+	B+	NA	NA
04.03.2016	First assignment of both types of ratings for the country	B+	B+	NA	NA

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Minute's summary

The rating committee for Armenia was held on 8 July 2022. The quorum for the rating committee was present. After the responsible expert presented the factors, which influenced the rating assessment, the members of the committee expressed their opinions and suggestions within the framework of the Sovereign methodology. The chairman of the rating committee ensured that every member of the committee expressed his/her opinion before proceeding to the voting.

The following methodology was used for the rating assessment: [Methodology for Assigning Sovereign Government Credit Ratings – Full Public Version \(from April 2022\)](#). Descriptions and definitions of all rating categories can be found under the [Rating scale](#) section. The user of the rating shall read the methodology in order to have a full understanding of the rating procedure.

The definition of default can be found on the Agency's website in the section for [Internal policies](#).

These ratings are unsolicited. The rated entity did not participate in the rating process.

Main sources of information: IMF, World Bank, Central Bank of Armenia, Ministry of finance of Armenia.

ESG Disclosure

We consider Environmental, Social, and Governance (ESG) risks and opportunities in the creditworthiness analysis of our Sovereign entities. The disclosure document can be found on the Agency's website in the section: [ESG factors in RAEX-Europe's Credit Ratings](#)

Limits of the Credit Rating

During the rating assignment process, Rating-Agentur Expert RA GmbH (the Agency) used publicly available information that was considered to be reliable, complete and non-biased. The responsible expert performed the rating assessment of the country with information considered as the most reliable and up to date in accordance to the overall position of the country and the Agency's internal criteria for selecting data providers. The information and data used for this specific assessment can be considered as of sufficient quality.

Regulatory use

SGC ratings can be used for regulatory purposes according to the ESMA definition.

Conflict of interest

The responsible expert was neither influenced nor biased by third parties during the rating assessment. All employees involved in the rating assessment and revision of the rated entity have reported absence of conflicts of interests before initiation of the rating process.

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The office responsible for the preparation and issuance of this credit rating is the office of Rating-Agentur Expert RA GmbH in Frankfurt am Main, Germany.

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Rating-Agentur Expert RA GmbH applies the Code of Conduct Fundamentals for credit rating agencies issued by the International Organization of Securities Commissions (IOSCO Code) and includes the basic principles of IOSCO Code in its Code of Conduct.

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