

# NEWSLETTER

## Partial recovery in tourism drives strong growth

Georgia's economy grew strongly by 10.6% in 2021. The pre-crisis level was exceeded. Growth was driven by all components. GDP growth of 5.5% is forecast for 2022. Tourism remains a crucial factor in the recovery, with revenues from the sector at 38% of 2019 levels in 2021 and expected to reach 75-85% in 2022.

The Lari has appreciated to around 3 GEL/USD. FX interventions have declined. However, inflation was very high at 13.9% at year-end 2021. The National Bank therefore raised its policy rate four times to 10.5%.

Fiscal consolidation has started, the deficit has been reduced to 6.7% of GDP in 2021. A further decline to 4.4% in 2022 and 3.0% in 2023 (compliance with the fiscal rule) is expected. The debt ratio fell to around 50% in 2021 and will remain stable at about this level.

Downside risks to growth remain in the tourism sector due to the pandemic. Furthermore, the significant exposure vis-à-vis Russia and Ukraine poses an additional potential challenge.

### Strong recovery driven by consumption and exports

Real GDP in Georgia grew by 10.6% in 2021, far exceeding initial expectations. Particularly noteworthy is the very high growth in Q2 (29% yoy), which can only partially be explained by a base effect. Importantly, GDP now exceeds the pre-crisis level. While regional peer countries also recorded strong growth last year, Georgia's recovery stands out.

#### Selected economic indicators

	2021	2022	2023
Real GDP growth, % yoy	10.6	5.5	5.0
Inflation, % yoy (end of period)	13.9	2.5	3.0
Current account balance, % of GDP	-8.4	-7.6	-6.6
Budget balance, % of GDP	-6.7	-4.4	-3.0
Gross government debt, % of GDP	51.5	51.5	50.2

Sources: Geostat, Ministry of Finance; forecast

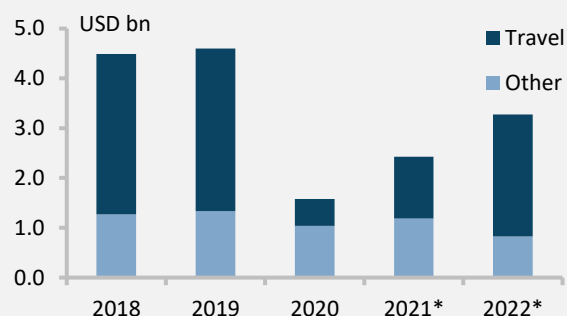
Growth in 2021 was broad-based and supported by all demand components. Consumption contributed the strongest, with pent-up demand playing an important role. The continuation of the strong trend in remittances (+24.6% yoy after an already strong 2020) provided additional income. Noteworthy is the increase in

exports, fuelled by the partial recovery in tourism. Stronger investments also supported growth. For 2022, a continuation of the overall trend is expected with GDP estimated to grow by 5.5%, still slightly above the pre-crisis trend of around 4.5 to 5%. However, growth prospects are still closely linked to the development of the COVID-19 pandemic, especially due to the importance of the tourism sector for Georgia.

### Recovery in tourism begins

In 2020, the shock to tourism was a major driver of the recession. The development in 2021 was thus a crucial factor for growth. Last year, revenues from tourism increased by 130% yoy from a low base, reaching 38% of the 2019 level. This is a promising figure, but still leaves room for improvement, also due to the low base of the first three months. The partial recovery was the main driver for the increase in services exports and a key factor for the high growth. The outlook for this year is positive: Georgian experts expect the recovery to continue at about 75%-85% of the 2019 level. Whether the potential for further recovery can be tapped will be a crucial factor for Georgia's economic outlook this year.

#### Revenues from services exports



Sources: NBG, Ministry of Finance, TBC Capital, German Economic Team; \*forecast

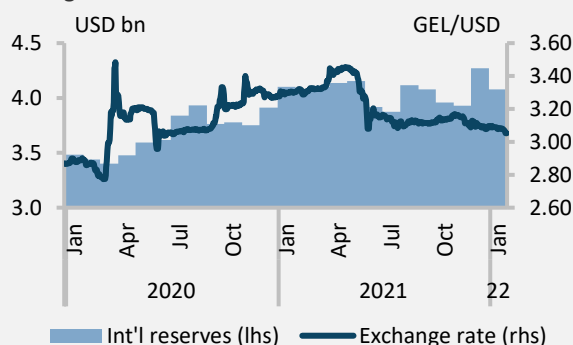
### Goods trade gains traction

The dynamics in goods trade also gained traction in 2021. Exports increased by 26.9%, driven by ferro-alloys, cars and fertilisers. Imports also increased sizeably by 25.1% on the back of higher imports of oil products, copper ores (for re-export) and machinery. For 2022, a continuation of the positive dynamics is forecast, with growth rates of 13.3% and 11.5% for exports and imports, respectively. Overall, the current account deficit narrowed to 8.4% of GDP (2020: 12.4%). This year, the deficit is projected to fall to 7.6% of GDP.

## Stable Lari, but high inflation

After an initial period of depreciation in early 2021, the Lari overall appreciated by 6% against the US dollar. In February 2022, the exchange rate appreciated to below 3 GEL/USD for the first time since June 2020. FX sales by the NBG have been decreasing in 2021, reaching only USD 333 m (2020: USD 873 m), with most of the interventions conducted in the early months. FX reserves increased on the back of the SDR allocation (USD 286 m) by the IMF in August and government FX operations. The development of inflation was more concerning. Reaching 13.9% yoy in December 2021, it was far above the NBG's 3% target. Most of the increase can be explained by a supply shock of rising international commodity prices. The shock is thus likely to be temporary, with inflation forecast to converge towards target in the course of 2022. However, in order to prevent a rise in inflation expectations, the NBG raised its policy rate four times by a total of 2.5 percentage points to the current rate of 10.5%, thus maintaining its stability-oriented policy.

### Exchange rate and FX reserves



Source: NBG

## Budget deficit and debt ratio decreasing

The public deficit amounted to 6.7% of GDP in 2021 due to the continuation of fiscal stimulus, albeit at a lower level than in 2020. In the coming years, further budget consolidation is to be expected. In 2022, the deficit is forecast to reach 4.4% of GDP as a result of fading fiscal stimulus, rising tax revenues and a larger GDP base. The fiscal rule is to be observed again in 2023, with a projected deficit of 3.0% of GDP. This is the maximum value allowed under the fiscal rule, which will become active again as mandated when the escape clause activated during the pandemic will expire. Strong GDP growth also helped in reducing the debt ratio from around 60% of GDP in 2020 to currently approx. 50% of GDP. This value is forecast to remain stable in the next years, but lies approx. 10 percentage points above pre-crisis level.

## Outlook

2021 turned out to be a positive year for the Georgian economy. For 2022, tourism will remain a key factor. In January, tourism revenues reached 69% of the 2019 level, offering a positive first indication. However, the number of COVID-19 cases in Georgia remains very high and the global outlook regarding the pandemic uncertain, presenting a downside risk for the growth prospects. The conflict between Russia and Ukraine poses an additional risk. While the risk spread of government debt in foreign currency ("eurobond") only increased slightly in recent months, Georgia's exposure towards Russia and Ukraine should not be underestimated. Inflows stemming from goods exports, tourism and remittances re equivalent to approx. 10% of GDP. The recent escalation of the crisis thus poses significant risks.

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[This newsletter is based on the 15<sup>th</sup> issue of our Economic Monitor Georgia.](#)

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