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NEWSLETTER GEORGIA

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High economic growth continues with gradual cool-down

Economic growth in 2023 is expected to remain high at 6.2%. The decrease compared with 2022 is mainly due to the fact that the special effect of the relocation of people from Russia and Belarus is slowly fading. This is also reflected in the normalisation of money transfers from Russia and the slight increase in the current account deficit. The lari has stabilised at approximately 2.70 GEL/USD, around the same level as at the beginning of the year. Lower international commodity and transport prices have caused inflation to fall strongly. Nevertheless, the National Bank remains cautious about policy rate cuts. The budget deficit and public debt ratio are expected to stabilise at below 3% and 40% of GDP, respectively. An open question is the continuation of the IMF programme which has been stalled since summer.

Relocation effect fades out, growth still high

Last year, relocation of people from Russia and Belarus, many of whom are high-skilled and have good incomes, was a key factor for the high economic growth (10.1% yoy). In 2023, as the initial shock gradually fades out, growth is expected to slow down to 6.2% yoy. For 2024, growth is forecast to reach 4.8%.

Selected economic indicators

	2022	2023*	2024*
Real GDP growth, % yoy	10.1	6.2	4.8
Current account balance, % of GDP	-4.0	-6.1	-5.8
Inflation, % yoy (end of period)	9.8	0.8	3.0
Budget balance, % of GDP**	-3.1	-2.8	-2.5
Gross government debt, % of GDP	39.8	38.4	38.2

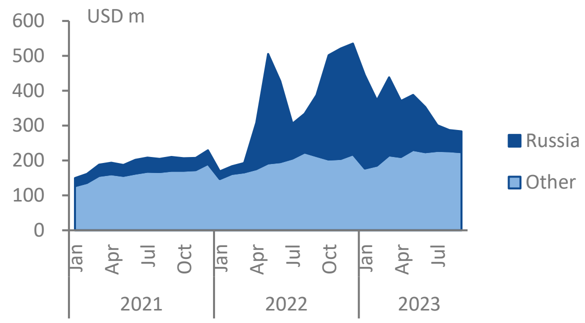
*Sources: Geostat, NBG, Ministry of Finance; *estimate/forecast, **IMF programme definition*

Whereas growth in 2022 was mostly driven by net exports (due to the fact that relocated persons are statistically treated as tourists in the first year), growth in 2023 and 2024 will mostly be driven by consumption, which is usually the main growth driver in Georgia.

Money transfers from Russia normalise

A key factor for the economy last year was the strong rise in money transfers from Russia due to relocation (totalling USD 2.1 bn). With the immediate effects of relocation fading, money transfers from Russia have started to normalise in recent months, although they are still elevated relative to past values. In 9M2023, they reached USD 1.3 bn (the increase of 16% yoy can be explained by a base effect).

Monthly money transfers



Source: NBG; Note: based on USD

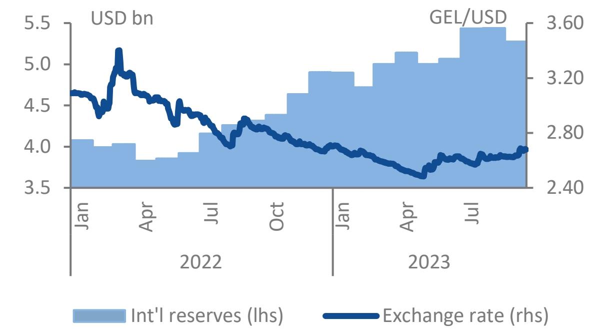
Slight increase in the current account deficit

The aforementioned rise in net exports and the high money transfers due to relocation were drivers for the strong reduction in Georgia’s current account deficit in 2022 (-4.0% of GDP). With the fading-out of this effect, dynamics of services exports is expected to slow down (although vacation tourism remains strong). Additionally, goods imports are forecast to rise stronger than exports, thus increasing Georgia’s negative goods trade balance. As a result of all these trends, the current account deficit is estimated to reach -6.1% of GDP this year. For 2024, a similar value (-5.8%) is forecast.

Lari appreciation slows down

In 2022, the lari appreciated strongly (14% yoy) as a result of strong money inflows and FDI inflows and the continuation of the recovery in the tourism sector. In the first months of 2023, this appreciation trend continued. However, since the summer, there has been a slight depreciation and the exchange rate has since stabilised around 2.70 GEL/USD (roughly the same level as at the start of the year). Compared to recent years, the lari has appreciated, which has enabled the National Bank to buy FX through interventions, thus raising the FX reserves to USD 5.3 bn.

Exchange rate and FX reserves

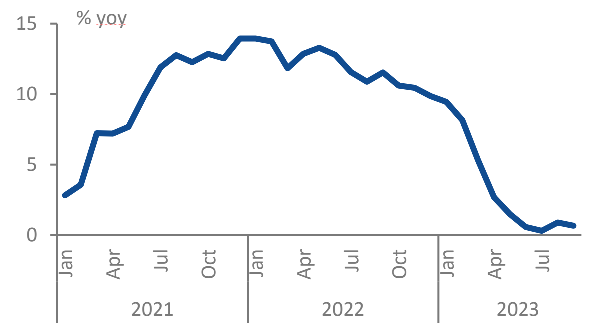


Source: NBG

Strong reduction in inflation, slight rate cuts

The appreciation of the lari has also been a factor in the strong slowdown of inflation by limiting the effect of imported inflation (pass-through effect). Additionally, lower commodity prices and transport costs have contributed to this development. In Sep-23, inflation reached 0.7% yoy (Sep-22: 11.5%).

Inflation dynamics



Source: NBG

While this value is far below the target level of 3.0%, the National Bank is still seeing some risks in potential volatility of food and energy prices (two main components of the CPI) and high aggregate demand. Therefore, it has only cautiously started to ease monetary policy, reducing the policy rate in three steps to 10.0% (-1.0 pp in the course of 2023). For 2024, a slow convergence towards the inflation target is anticipated.

Deficit and debt stable, IMF programme stalled

Boosted by high economic growth, tax revenues have risen more strongly than expenditures in recent years. In 2023, the budget deficit is expected to reach -2.8% of GDP, slightly lower than 2022 (-3.1%). For 2024, it is expected to decrease further to -2.5%. In general, the deficit can mainly be explained by investment projects (e.g. highway construction). The debt ratio will be around 38.4% of GDP in 2023 and is expected to stabilise around this level in the coming years.

Georgia's Stand-By Arrangement with the IMF has been stalled since summer over disagreements regarding changes in the management structure of the National Bank. Additional concern for the IMF was caused in September 2023 when the National Bank decided that international financial sanctions may only be applied to Georgian citizens and companies after prior conviction in local courts. As a result of this decision, three Vice Governors of the National Bank resigned.

Outlook

Overall, Georgia's economy continues to show a positive performance despite a difficult global environment. While the immediate effects of last year's relocation are fading out, the presence of (often high earning) immigrants still gives the economy some stimulus. Regarding trade, falling costs for energy imports and the strong tourism sector (part of services exports) provide some boost for the economy. An important question for the future will be the continuation of the IMF programme. While the authorities have not yet drawn on the funds, it should be noted that the programme not only provides financial resources but also serves as an important anchor for Georgia's sound macroeconomic framework.

This newsletter is based on the 18th edition of our Economic Monitor Georgia (forthcoming).

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