

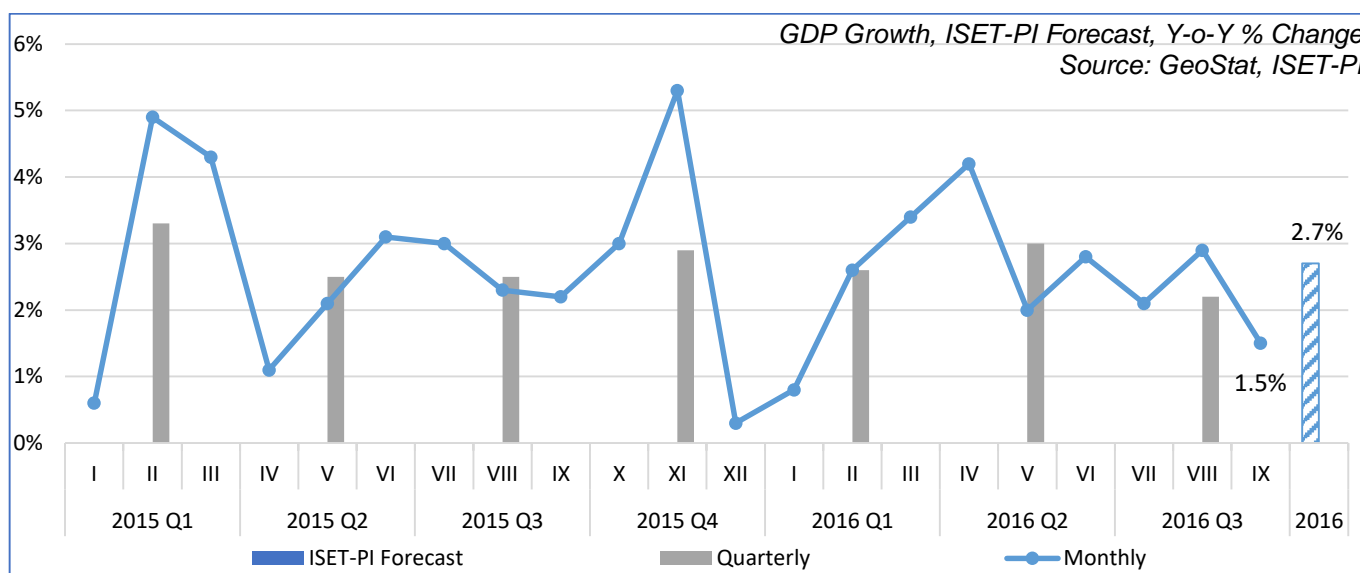


Authors: Yaroslava Babych and Giorgi Mzhavanadze

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Georgia's economy was weaker than expected in September, but exports showed an annual increase for the first time since July 2014.

GDP growth trends and forecasts



According to Geostat's rapid estimates, real GDP grew by 1.5% in September 2016, while the growth rate for Q3 stood at 2.2% year over year (YoY). The estimated third quarter growth was thus 1.3 percentage points lower than ISET-PI's GDP forecast for the quarter. One should note that the data from September are likely to include a very high services component (revenues from the tourism sector). Therefore, the quarterly growth number is likely to be revised upward in the future as more data comes in.

Despite low economic performance in the third quarter, the NBG still predicted 3.5% year-over-year real GDP growth for 2016 in its Monetary Policy Report published on 2 November. According to the NBG's forecast, fiscal stimuli and the normalization of monetary policy will be the main drivers of investment and consumption in 2016-2017, while negative net exports will continue to deter economic growth.

Based on new information, the ISET-PI forecast for Q4 has been downgraded from 4.1% to 2.9%. The estimated real GDP growth for the first nine months of 2016 was 2.6% YoY, while ISET-PI's annual GDP forecast stood at 2.7%

According to ISET-PI forecast for first and second quarter of 2016 is 2.9% and 3.5% correspondingly, while recent updated forecast predicts 3.3% year-over-year real growth in 2016.

Prices

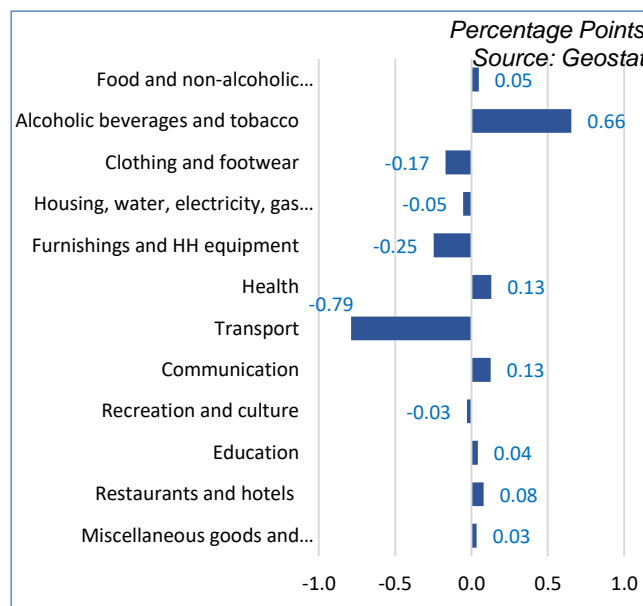
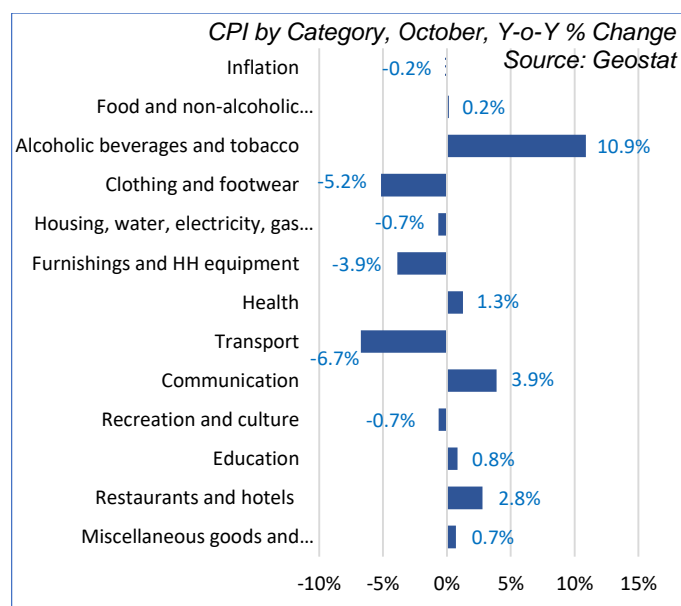
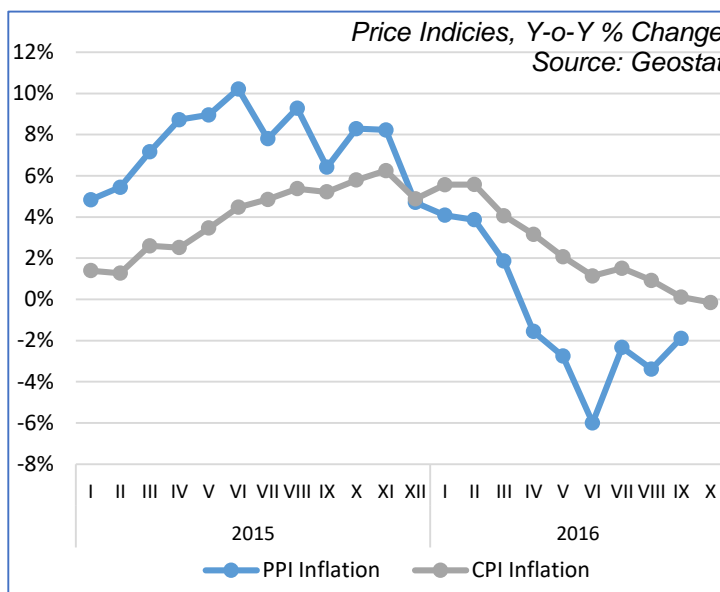
According to Geostat, in October the annual inflation rate was negative (-0.15% YoY) for the first time since September 2013. The annual inflation rate was well below its target level in the first ten months of 2016, reaching 2.4% on average. Month-over-month (MoM) prices increased by 0.5% in October. Among the reasons for low inflation rates were weak aggregate demand, a decrease in inflation expectations and a decline in commodity prices on the world market.



However, at its meeting on 26 October, the NBG’s monetary policy committee decided to keep the monetary policy rate at 6.5%. The NBG argued that the “reduction in the policy rate implemented in the previous periods has not completely passed on to the economy, so it is expedient to implement the normalization policy in a gradual manner. According to the current forecast, other things being equal, the monetary policy rate can be expected to decrease to 6% in the coming two quarters.”

The decomposition of the consumer price index for October shows that as many as five product categories saw a year-over-year price decline. Transport prices were down by 6.7% and drove inflation down by 0.79 percentage points. The categories of clothing and footwear (-5.2% YoY); housing, water, electricity, gas and other fuels (-0.7% YoY); furnishings and household equipment (-3.9% YoY); recreation and culture (-0.7% YoY) together contributed -0.5 percentage points to total inflation.

Alcoholic beverages and tobacco (+10.9% YoY) was the main category that pushed total inflation upward, contributing +0.66 percentage points. The increase in prices in this category was mainly due to the higher excise tax introduced in January this year.



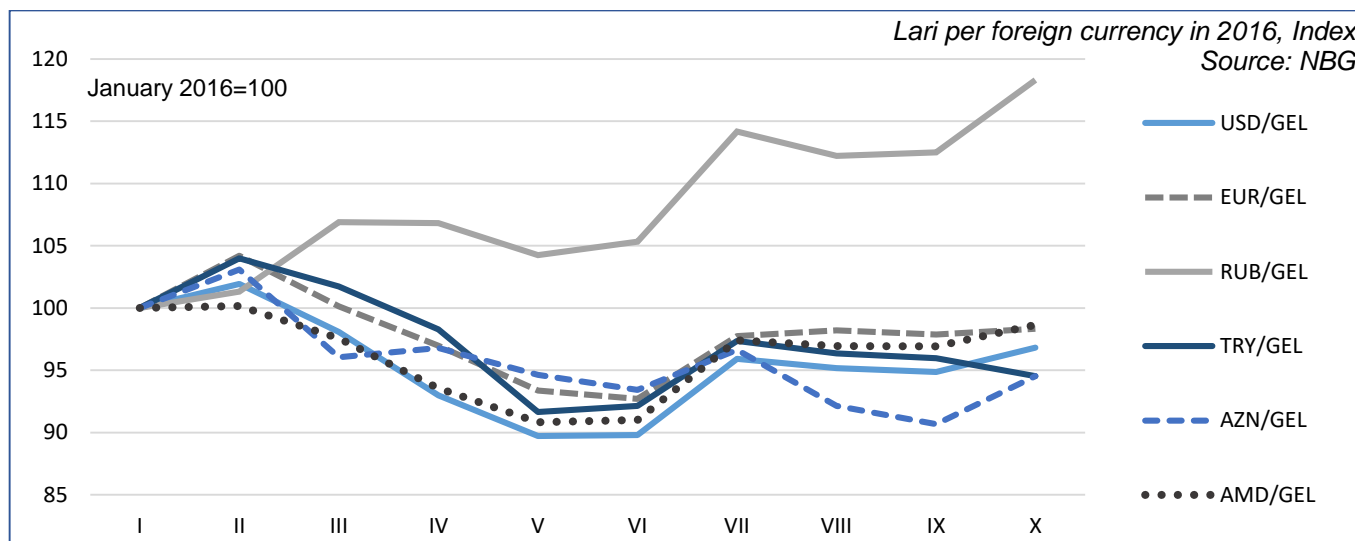
Generally, the decrease in prices is positive news for consumers in the short run because of their greater purchasing power; however, in the long run it has a severe negative effect on the overall economy, causing lower production, higher unemployment and lower economic growth. Although -0.15% YoY inflation is not a serious concern, it may be a sign for the NBG to start easing monetary policy more aggressively. Especially considering that producer prices have been clearly on the decline in the second and third quarters of the year, reflecting low aggregate demand conditions as well as lower input prices.

Currency

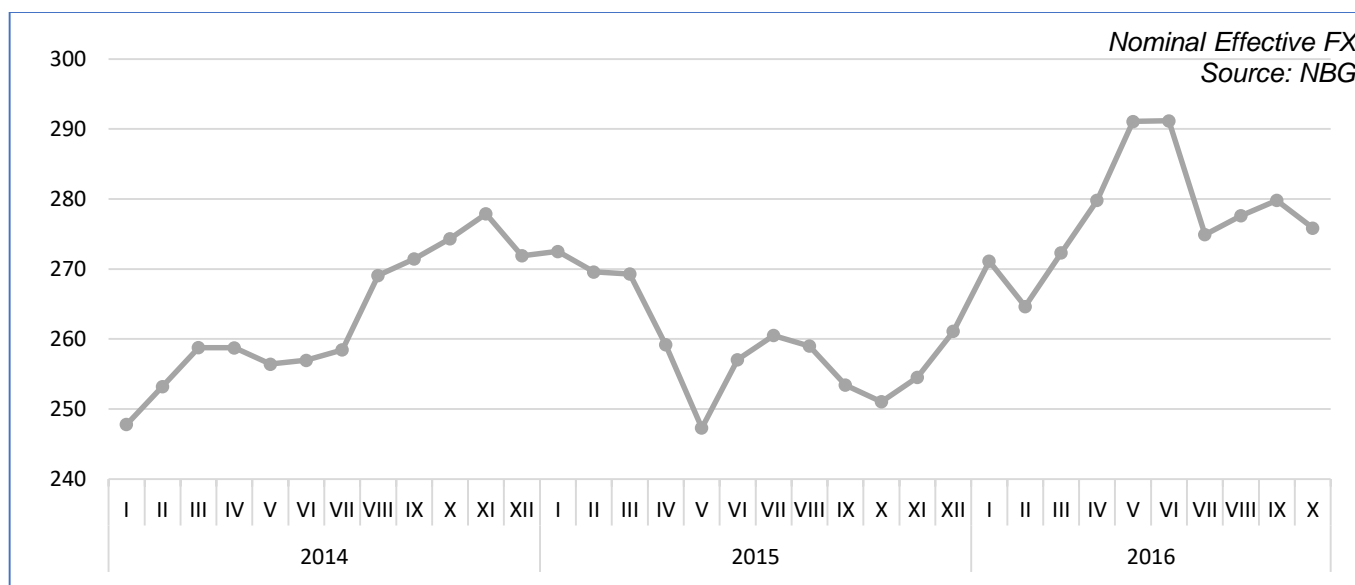
In October, the lari depreciated against the US dollar (-2.0% MoM) and the euro (-0.5% MoM). The lari also weakened against the Russian ruble (-5.2% MoM), Azerbaijani manat (-4.3% MoM) and Armenian dram (-1.8% MoM). The Turkish lira was the only currency in Georgia’s neighborhood against which the



lari gained in October, rising by 1.5% MoM. The depreciation trend of October can be explained by the expectations effect of the upcoming parliamentary elections as well as several large transactions conducted between Georgian and foreign companies.



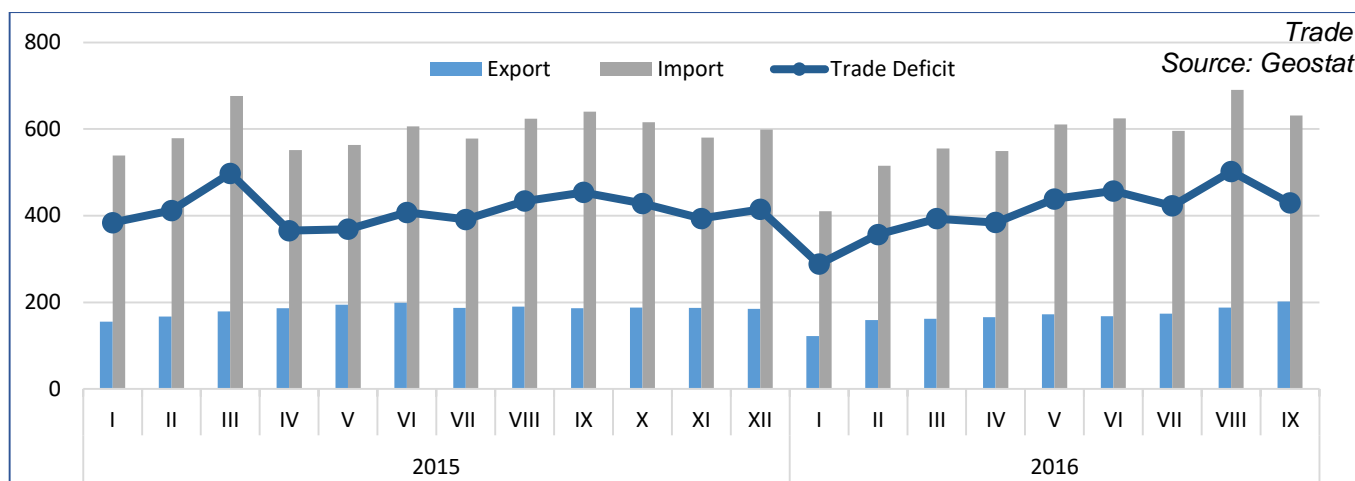
Georgia's nominal effective exchange rate thus showed a month-over-month depreciation of 1.4% in October. However, in annual terms, the lari nominal effective exchange rates still appreciated by 9.9%. This means that the country's trading partners experienced higher year-over-year depreciation than recorded in Georgia.



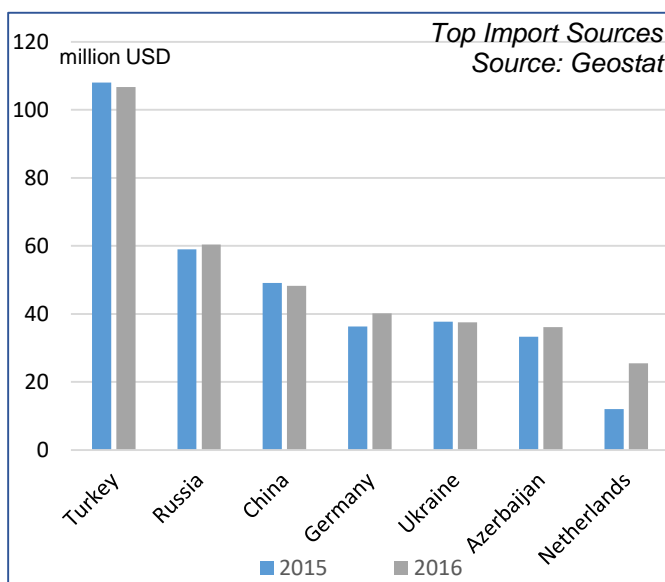
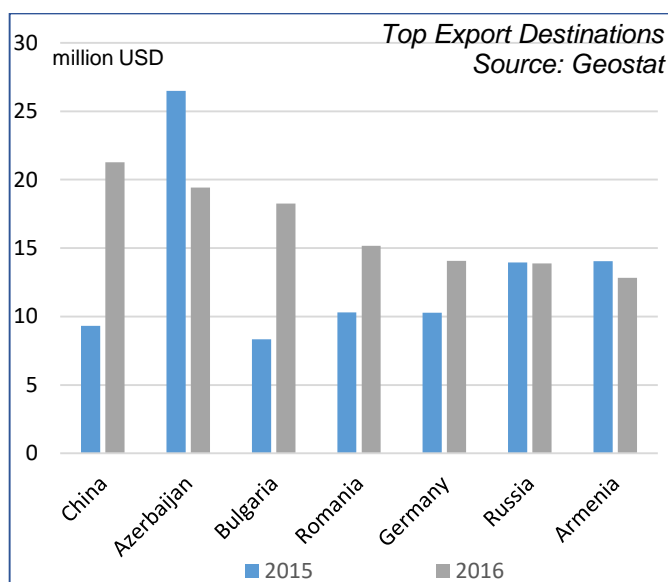
External Trade

Georgian exports amounted to 201.7 million USD in September, an 8.3% YoY increase. **This is the first time exports have showed a YoY increase since July 2014.** Most of this increase came from EU countries (+24.3% YoY), while exports to CIS countries showed an 8.3% YoY decline; exports to other countries increased by 13.8% YoY.

The main drivers of the exports increase were copper (+173% YoY), nuts (+19% YoY), cars (+9% YoY) and crude oil (+7% YoY). At the same time, exports of ferro-alloys (-6.4% YoY), wine (-14.4% YoY) and pharmaceuticals (-15.6% YoY) had a negative effect on total exports in September.



Imports to Georgia amounted to 631.1 million USD in the reported month. **Imports showed a 1.4% YoY decline** (excluding the donation of hepatitis C medicines). Imports of petroleum (-8.4% YoY) and gases (-43.5% YoY) were the main drivers of the decrease of imports, while imports of cars (+14% YoY) and copper (+21% YoY) drove import numbers up in September.



As a result, in September 2016 the **trade deficit decreased** by 5.4% YoY, and amounted to 429.3 million USD.

In the first nine months of 2016, the trade deficit was down by 1.1% YoY (to the level of 3.7 billion USD), as imports decreased by 3.3% YoY and exports fell by 8.1% YoY. The donation of hepatitis C medicines constituted about 840 million USD in September (and 2.4 billion USD in the first nine months of 2016).

Tourism

In October, the number of international visitors coming to Georgia increased by 4.5% YoY. A total of 527,157 international visitors entered the country in October. Of these, 80.1% arrived by land (-1.1% YoY), 17.9% by air (+44.6% YoY), 0.7% by sea (-35% YoY) and 0.7% by rail (6.2%).

The number of visitors who stayed in Georgia for 24 hours or more increased by 20.9% year-over-year. Such visitors comprised slightly less than a third (28.2%) of total arrivals.

Once again, Asia was the leader in terms of the year-over-year increase of international visitors: Iran (+344% YoY), Israel (+82% YoY), India (+130 YoY), and Kazakhstan (+37% YoY) were among the fastest growing international visitor countries. The number of visitors from Russia and Ukraine increased by 13%



and 16% respectively, while tourist numbers from Belarus increased significantly (42%) compared to October last year.

International Arrivals (October 2016)

Source: GNTA

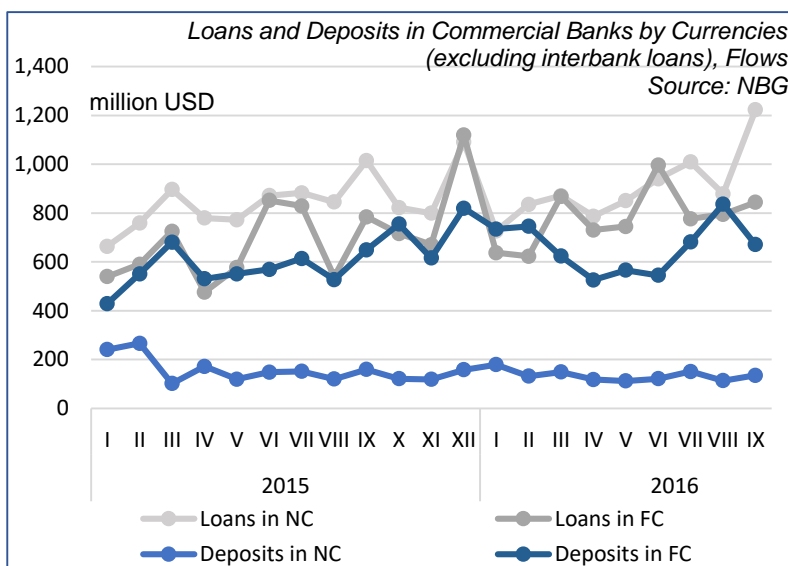
	Country	2015: October	2016: October	Change	Change %	Share %
1	Armenia	128403	125665	-2738	-2%	24%
2	Azerbaijan	108931	119967	11036	10%	23%
3	Turkey	121876	101621	-20255	-17%	19%
4	Russia	78080	88192	10112	13%	17%
5	Ukraine	12736	14742	2006	16%	3%
6	Iran	2443	10854	8411	344%	2%
7	Israel	5845	10652	4807	82%	2%
8	Germany	3639	4817	1178	32%	1%
9	Poland	2873	3918	1045	36%	1%
10	India	1480	3407	1927	130%	1%
11	Kazakhstan	2317	3184	867	37%	1%
12	U S A	3213	3115	-98	-3%	1%
13	Belarus	1995	2836	841	42%	1%
14	United Kingdom	1952	1791	-161	-8%	0%
15	China	1469	1662	193	13%	0%

Overall, in the first ten months of 2016 there were 5.4 million international arrivals, an 8.1% YoY increase. Of these, 81.2% arrived by land, 17.2% by air, 1.0% by sea and 0.7% by rail.

Banking Sector

In September, commercial banks granted loans totaling 2.066 billion GEL (excluding interbank loans), which represents a 14.9% year-over-year increase (+23.5% MoM).

Nearly half of these loans (54.5%), were granted to legal entities, while 45.5% went to individuals. 59.2% of the total loans granted in this period were denominated in the national currency. This was driven by a jump in lari denominated loans to individuals. Overall, national currency denominated loans grew by 20.5% year on year. Foreign currency denominated loans only grew by 3.3%.



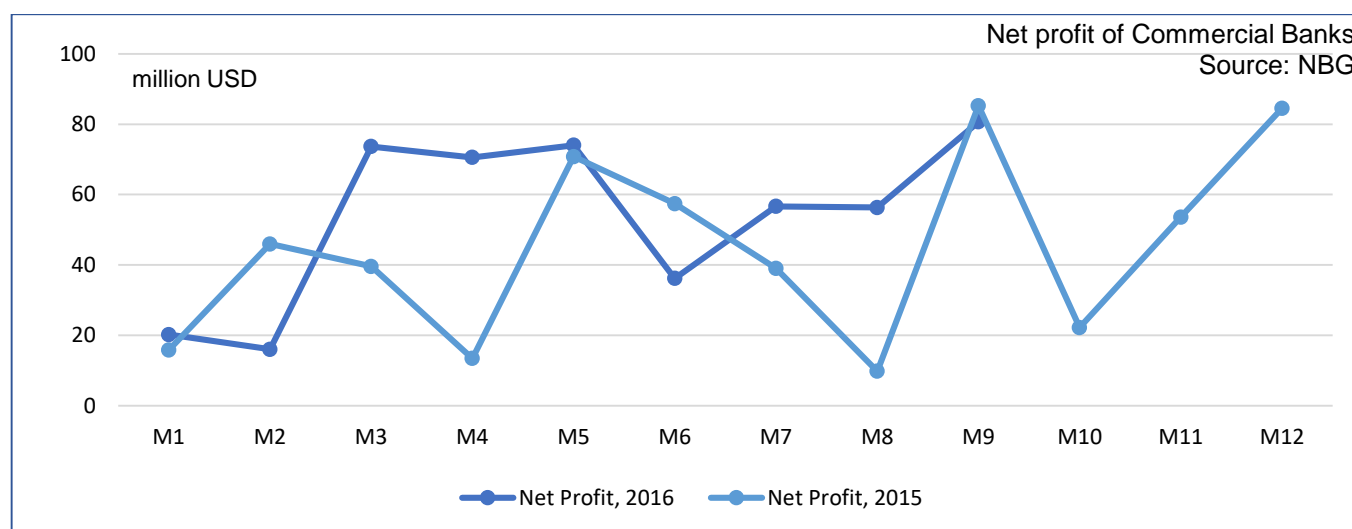
Total deposits in commercial banks amounted to 809.5 million GEL in September, which represents a 1% year-over-year decrease (-15.3% MoM). Only 17% of these deposits were denominated in the national currency. Individuals were the main owners of deposits in the reported month – accounting for 72.4% of total deposits.

Despite large fluctuations on foreign exchange markets during the last two years, the **dollarization rate of stocks of both loans and deposits remained high**. Dollarization of loans constituted 64.1%, while 66.7% of deposits were dollarized in September. The IMF recommended that the Georgian government and the NBG conduct de-dollarization policy actions and promote operations denominated in lari, especially on the highly dollarized real estate and automobiles markets.

The net profits of the banking system amounted to 80.7 million USD in September, a 5.4% year-over-year decrease. However, this annual decline can be explained by the high fluctuation of net profits in the



previous year; in the first nine months of 2016, banks' profits increased by 28.4% to 484.3 million USD.

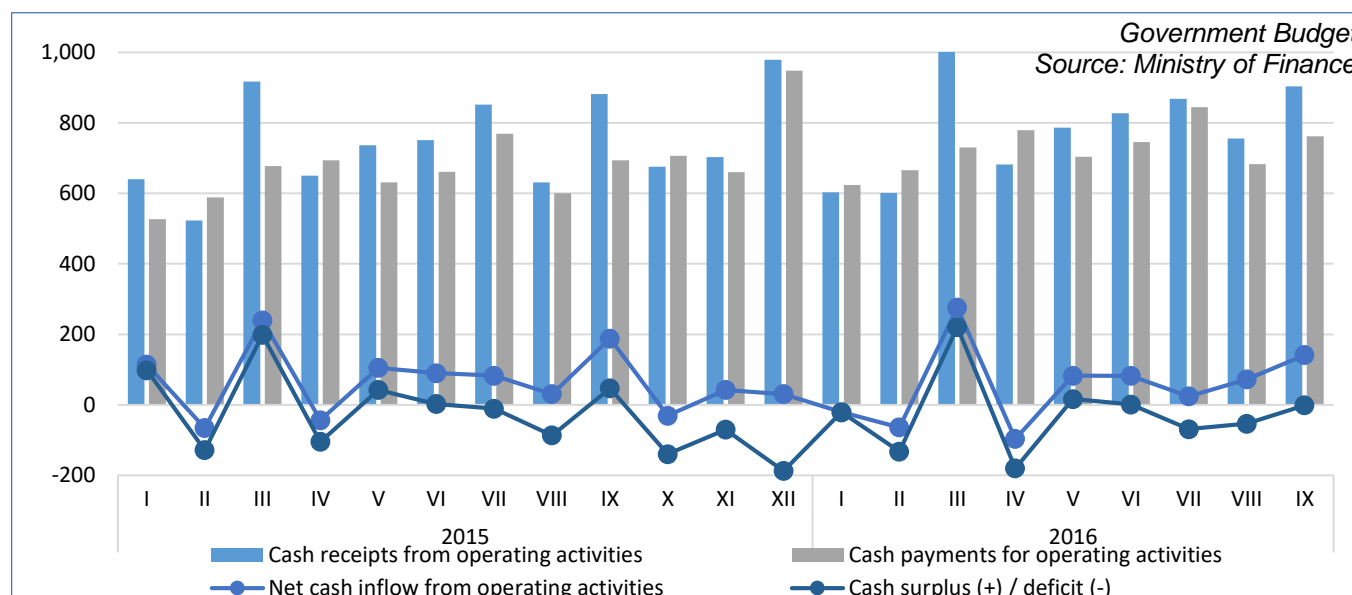


Government budget trends

Government revenues increased by 2.5% YoY and constituted 903.5 million GEL in September (income from taxes rose by 8% YoY in the same period, reaching 819.9 million GEL).

Total expenditure increased by 9.9% YoY and constituted 762.1 million GEL. There was an increase in social benefits (+8.4% YoY), compensation of employees (+ 7.7% YoY), and other payments (+17% YoY).

The overall government budget, despite the pre-election period, was only 1.3 million USD in deficit in September; however, in the same period of the previous year, it showed a 46.8 million USD surplus. In September, **total government debt amounted to 13.3 billion GEL (a 4.7% YoY increase)**.



According to the Ministry of Finance, in the first nine months of 2016, government revenues constituted 6.285 billion GEL, which was 100.5% of the planned target. Government expenditures constituted 6.256 billion GEL, which was 96.6% of the planned target. As a result, the budget deficit in the first nine months of 2016 amounted to 255 million GEL, instead of the projected 605 million GEL. Due to corporate tax reform and its expected negative effect on budget revenues, the IMF has recommended that the Georgian government undertake a fiscal consolidation policy.