

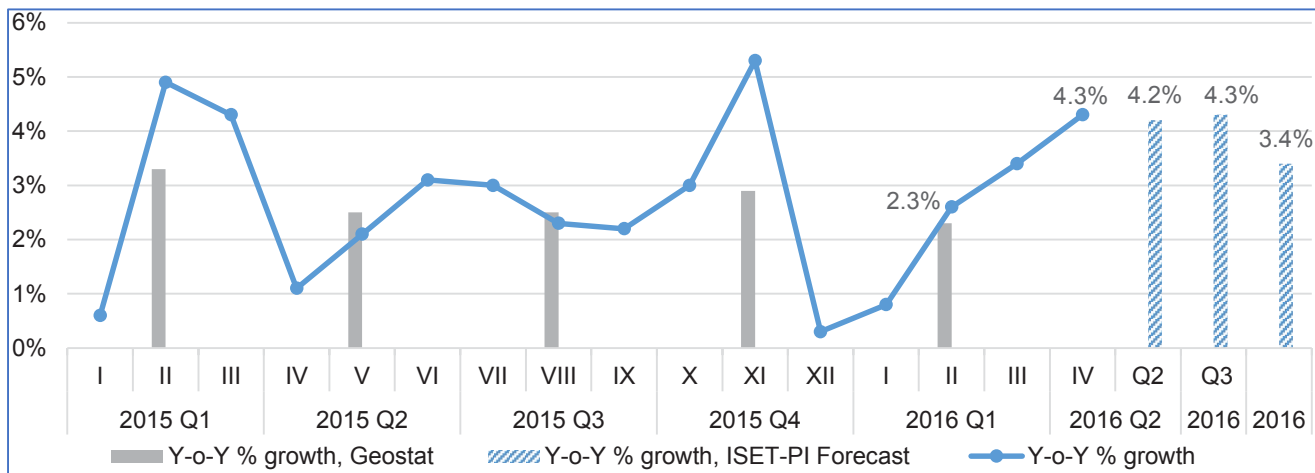


## Real Growth Rate in Georgia Stays on Track. Disappointing Export Data Reflects the High Shares of Metals and Car Re-Exports in Georgia's External Trade

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Figure 1: GDP Growth, ISET-PI Forecast, %

Source: GeoStat, ISET-PI



According to Geostat estimates, real GDP grew by 4.3% year over year (YoY) in April 2016. Although the growth rate showed an upward trend from the beginning of the year, the ISET-PI forecast for Q2 and Q3 has remained at 4.2% and 4.3%, the same as in previous predictions. This means that the **real growth rate is expected to stabilize at the 4-4.5% level in the next months**. The positive dynamic in the real GDP growth rate has been complemented with increasing trends in the consumer and business confidence indices in recent months. Unlike last quarter, the second quarter increase in the BCI was mostly driven by a significant improvement in performance rather than in business expectations, which kept rising albeit at a marginal pace. In terms of the CCI, the current situation component increased, but this was somewhat tempered by lowered expectations. Despite this, the overall CCI still climbed, resulting in the highest CCI level since January 2015 (see these links for the full reports: [CCI](#), [BCI](#)).

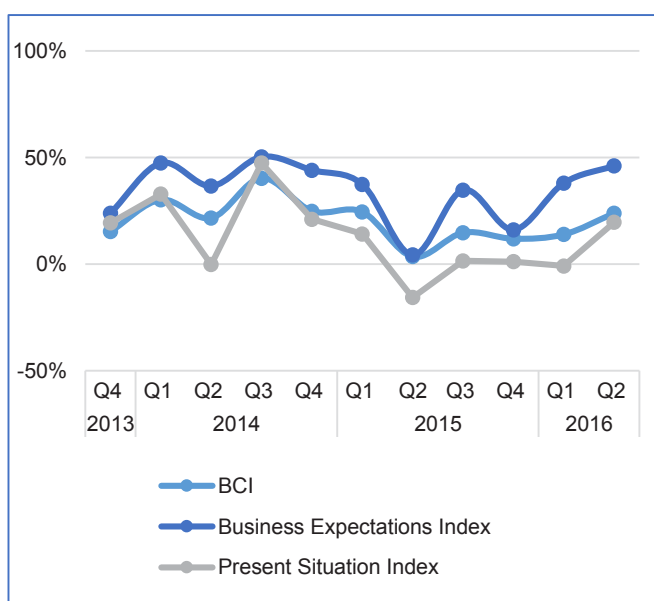
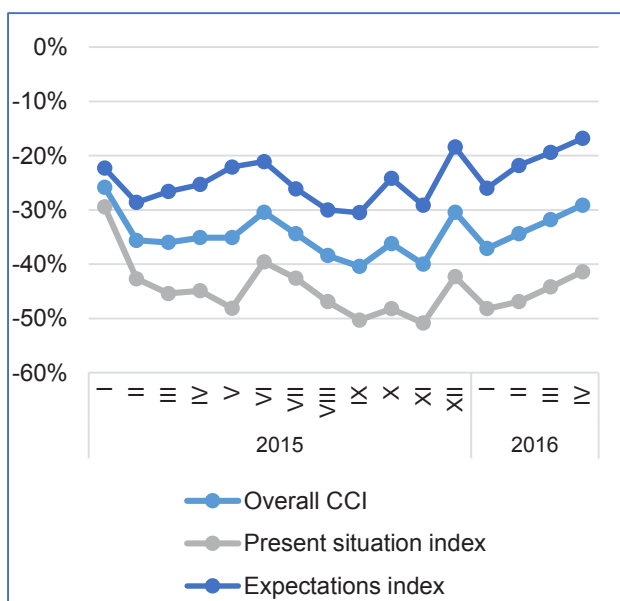
**Unemployment on the decline.** Positive news came from Geostat's recent publication on the Georgian labor market – the YoY **unemployment rate decreased by 0.4 percentage points to 12% in 2015**, and the share of self-employed in total employment decreased by 3.5 percentage points to 57.5%. However, breaking

Figure 2: Consumer Confidence Index

Source: ISET-PI

Figure 3: Business Confidence Index

Source: ISET-PI



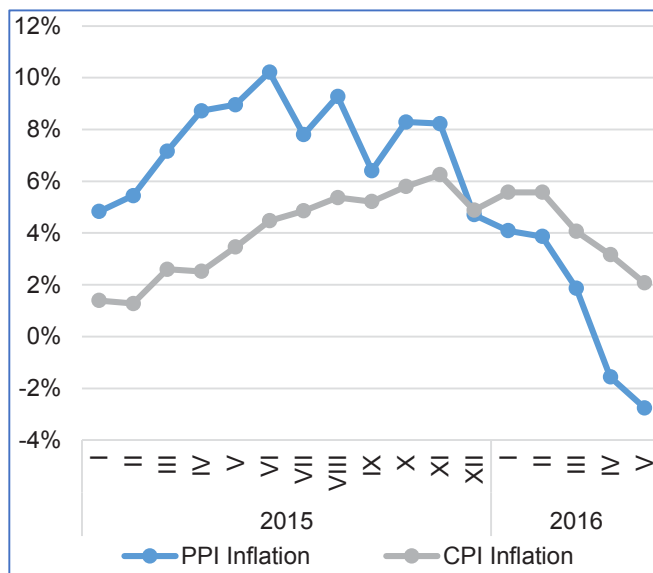


down unemployment by age indicated **high youth unemployment** in Georgia: 26.2% of people in the 15-19 age group category, 32% in the 20-24 category and 20.7% in the 25-29 category are unemployed. Serious shortcomings with the Georgian education system, which lacks a strong vocational education and training (VET) component, could be to blame.

**Low consumer prices growth, and declining producer prices**

Figure 2: Inflation Rates, YoY Change Source: GeoStat

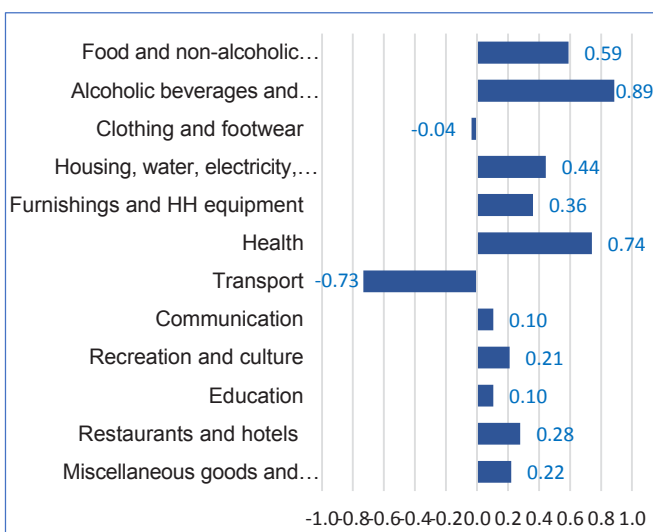
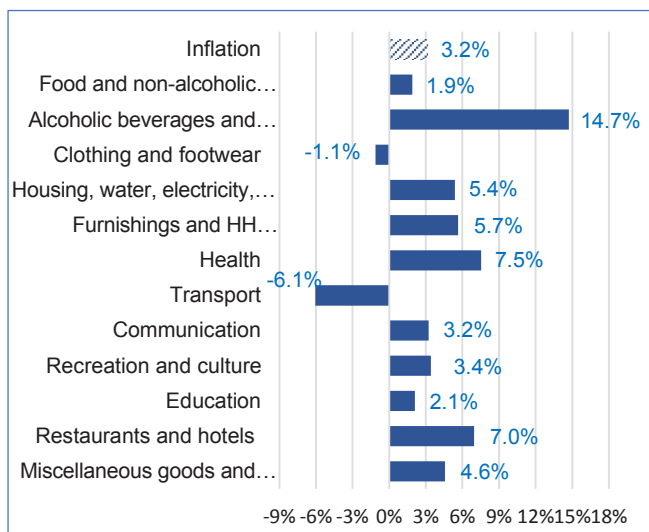
Inflation, as measured by the consumer price index, decreased by 0.6% month over month (MoM) and increased by 3.2% YoY in April 2016. The declining trend continued in May (-0.4% MoM and only 2.1% YoY). The producer price index showed deflation. **Producer prices fell year on year in April and May by 1.6% and 2.8% respectively.** Inflation in producer prices was driven down by low prices of oil and the declining prices on imported goods caused by the recent GEL appreciation against the USD. The tightening of monetary policy by the NBG throughout 2015 also affected inflation. On 27 April and 15 June, the NBG reduced the refinancing rate by 50 basis points, reaching 7%. “According to the current forecast the annual inflation will decrease at moderate rate in the coming quarters, temporarily keeping below the current target value and will reach the latter by the end of the year”- said the NBG.



The products whose prices increased the most in the reported months were **alcoholic beverages and tobacco, which saw a 14.7% YoY increase** that contributed 0.89 percentage points to overall inflation. The other important drivers of inflation were health (prices increased by 7.5% and contributed 0.74 percentage points to inflation) and **restaurants and hotels, the latter increased by 7% YoY in April, reflecting the increased inflow of tourists.** The main factor driving the inflation rate down was transport, which saw a 6.1% YoY decrease in the reported month and contributed -0.73 percentage points to the overall inflation rate.

Figure 5: Inflation Rates by Category, YoY change, pp

Figure 6: Contribution to Inflation Rate by Category, pp



**The national currency appreciates for the third consecutive month in nominal and real terms**

Following the Georgian currency reaching a historic average monthly minimum of 2.48 GEL per USD, the GEL has been swinging back and has since appreciated three months in a row. In April and May 2016, the



GEL appreciated by 5.2% and 3.5% MoM respectively. The strengthening of the GEL reflected positive changes in FDI and tourist inflows into Georgia; expectations about further appreciation also had an effect.

This dynamic was also reflected in the effective exchange rates: **both the nominal and real effective exchange rates appreciated in April 2016, by 2.8% and 1.6% MoM respectively** (an 8.0% and 7.2% YoY change). In May, the effective exchange rates showed even higher numbers: 4% and 3.4% MoM appreciation respectively (17.7% and 15.7% YoY).

Because the steep appreciation of the GEL might harm exporters (by making Georgian products relatively more expensive abroad and imports cheaper for Georgian consumers), in order to smooth the appreciation, the NBG performed net purchases of 40 million and 140 million USD in April and May respectively.

Figure 7: Nominal Exchange Rates

Source: NBG

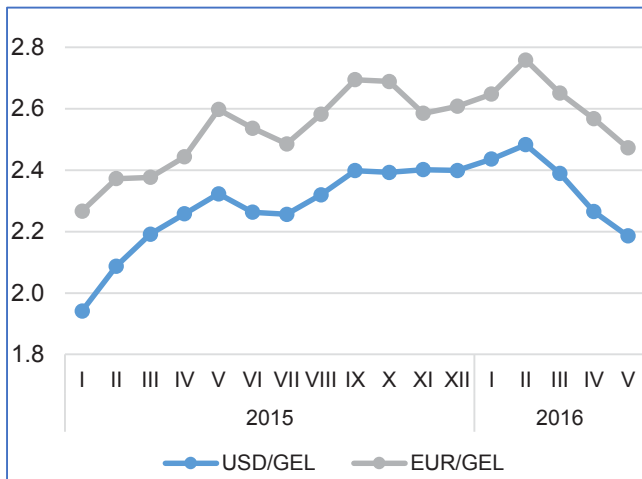
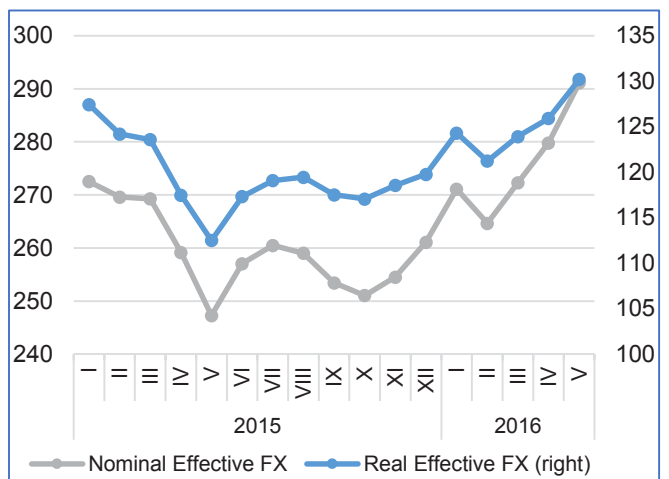


Figure 8: Effective Exchange Rates

Source: NBG



**Georgian trade data reflects the decline in metals, energy, and raw materials prices**

In April, according to Geostat’s preliminary statistics, trade turnover worsened by 3.1% YoY. Exports declined by 11.1% to 165.3 million USD, while imports fell by 0.5% to 549.3 million USD.<sup>1</sup> As a result, the trade deficit widened by 5% YoY to 384 million USD.

Figure 9: Trade Balance, mln USD

Source : GeoStat

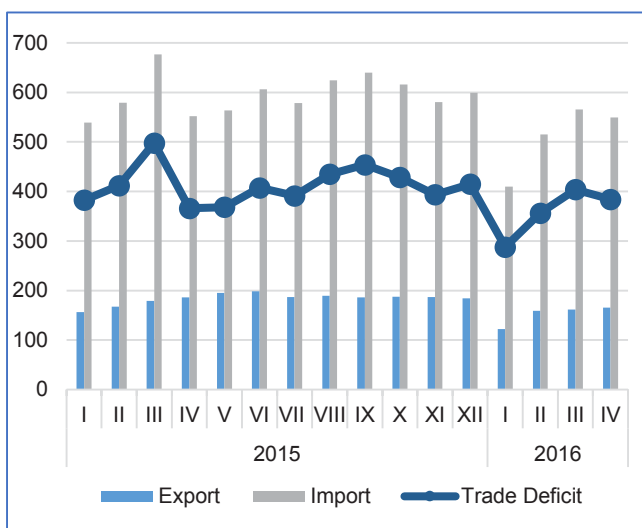
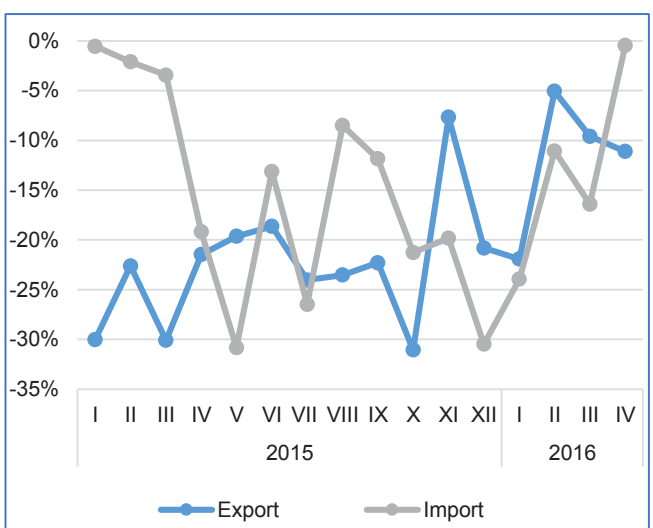


Figure 10: Trade, yoy Change

Source : GeoStat



<sup>1</sup> Trade statistics are calculated excluding the hepatitis C medicine provided to Georgia via international donations.



Exports were driven down by a **29% YoY decline in exports of both ferro-alloys and car re-exports**. Petroleum and gases, cars and copper ores **deterred import growth** in April. This could be due to a relative decrease in the prices of metals and energy products, which pushed import volumes down.

**Financial sector sees an uptick in non-performing loans**

The total stock of loans granted by commercial banks amounted to 16.1 billion GEL in April 2016, a 9.4% YoY increase (and a 1.5% MoM decline).

Total stock of deposits amounted to 15.4 billion GEL in the reported month, a 13.2% YoY increase (and a 3.3% MoM decline).

A total of 65% of loans were dollarized, while the dollarization of deposits stood at 66%. As we have mentioned in previous publications, dollarization rates were affected by the exchange rate depreciation; **adjusting for this effect shows that the dollarization rate was 57.5% for loans and 58.7% for deposits**.

According to recent NBG statistics, the **share of non-performing loans in total loans increased from 2.7% in Q4 2015 to 3.2% in Q1 2016**. The increase might be caused by the lagged effect of the GEL depreciation against USD on the cost of servicing foreign currency loans for people who have GEL denominated income.

Figure 12: Total Deposits and Loans, Stocks, bln GEL

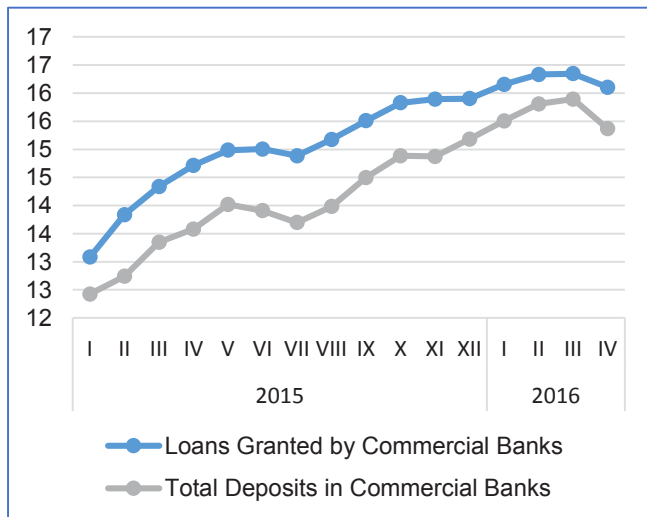
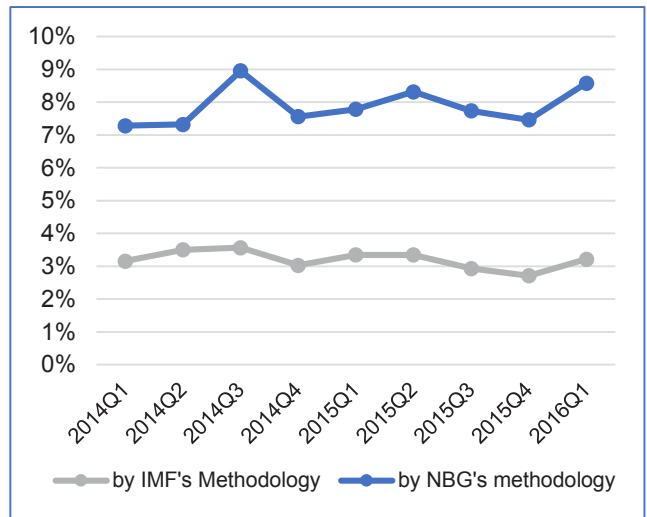


Figure 13: NPL Loans, Share in Total Loans Source: NBG



**Transfers from abroad increase in real terms**

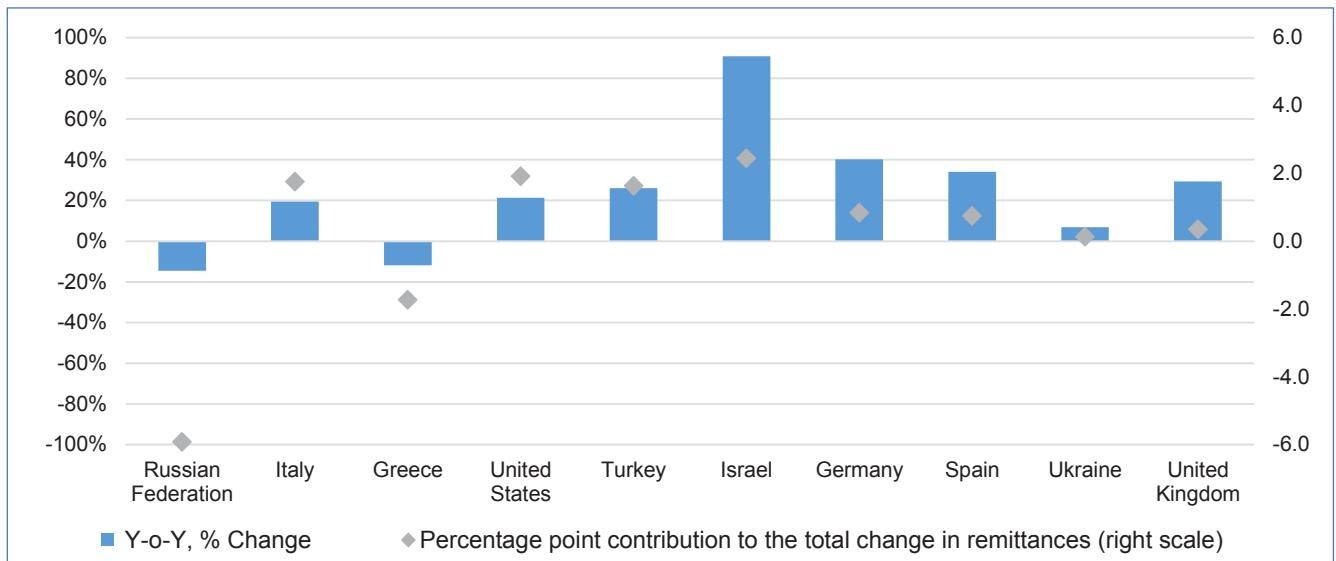
Remittances to Georgia equaled 94.8 million USD in April 2016, a 4% YoY increase. The main sources of the increase were Israel (+90.9% YoY), the United States (+21.3% YoY) and Italy (+19.5% YoY). The key countries driving money transfers to Georgia down in April were Russia (-14.6% YoY) and Greece (-11.8% YoY). Taken together, these two countries lowered the remittances growth rate by 7.7 percentage points.



**Remittances to Georgia measured in GEL terms and adjusted by CPI inflation also showed a 3.7% YoY increase in April 2016.**

Figure 14: Remittances by Country, April 2016, YoY Change

Source: NBG



### Tourism picks up early in the season

In April 2016, there were 462,500 international arrivals to Georgia, a 17.2% YoY increase. Of these, 84.3% arrived by land, 14.4% by air, 0.7% by sea and 0.7% by rail.

Visitors who stayed in Georgia for 24 hours or longer constituted 37% of total arrivals, or 171,200 people, a 20% YoY increase. The expected increase inflow of Russian tourists due to the strained Turkey-Russia relationship and visa liberalization with Iran indeed has already had positive effects on Georgian tourism. International arrivals from Russia increased by 26.7%, while those from Iran rose by 210.7% YoY in April. These numbers are expected to be much higher during the summer.

Figure 15: International Arrivals

Source: GNTA

	Country	2015: April	2016: April	Change	Change %	Share %
1	Turkey	103 504	115 887	12 383	12,0%	25,1%
2	Azerbaijan	89 855	105 695	15 840	17,6%	22,9%
3	Armenia	97 232	105 667	8 435	8,7%	22,8%
4	Russia	58 537	74 187	15 650	26,7%	16,0%
5	Ukraine	9 292	11 699	2 407	25,9%	2,5%
6	Israel	2 872	6 561	3 689	128,4%	1,4%
7	Iran	1 167	3 626	2 459	210,7%	0,8%
8	Poland	3 067	3 305	238	7,8%	0,7%
9	Kazakhstan	1 851	2 472	621	33,5%	0,5%
10	Germany	2 575	2 347	-228	-8,9%	0,5%
11	India	368	2 144	1 776	482,6%	0,5%
12	U S A	2 227	2 122	-105	-4,7%	0,5%
13	Belarus	1 311	1 780	469	35,8%	0,4%
14	Greece	1 408	1 434	26	1,8%	0,3%
15	UAE	1 272	1 412	140	11,0%	0,3%



**Government finances**

The general government budget income increased by 5% YoY in April and equaled 682.1 million GEL, while general government spending on operating activities increased by 12.1% and equaled 778.9 million GEL. Total **general government debts decreased by 5.5% YoY and constituted 12.7 billion GEL in April 2016**; of these, 22.4% were domestic debts while the rest were foreign debts.

Figure 16: General Budget, mln GEL

Source: MoF

