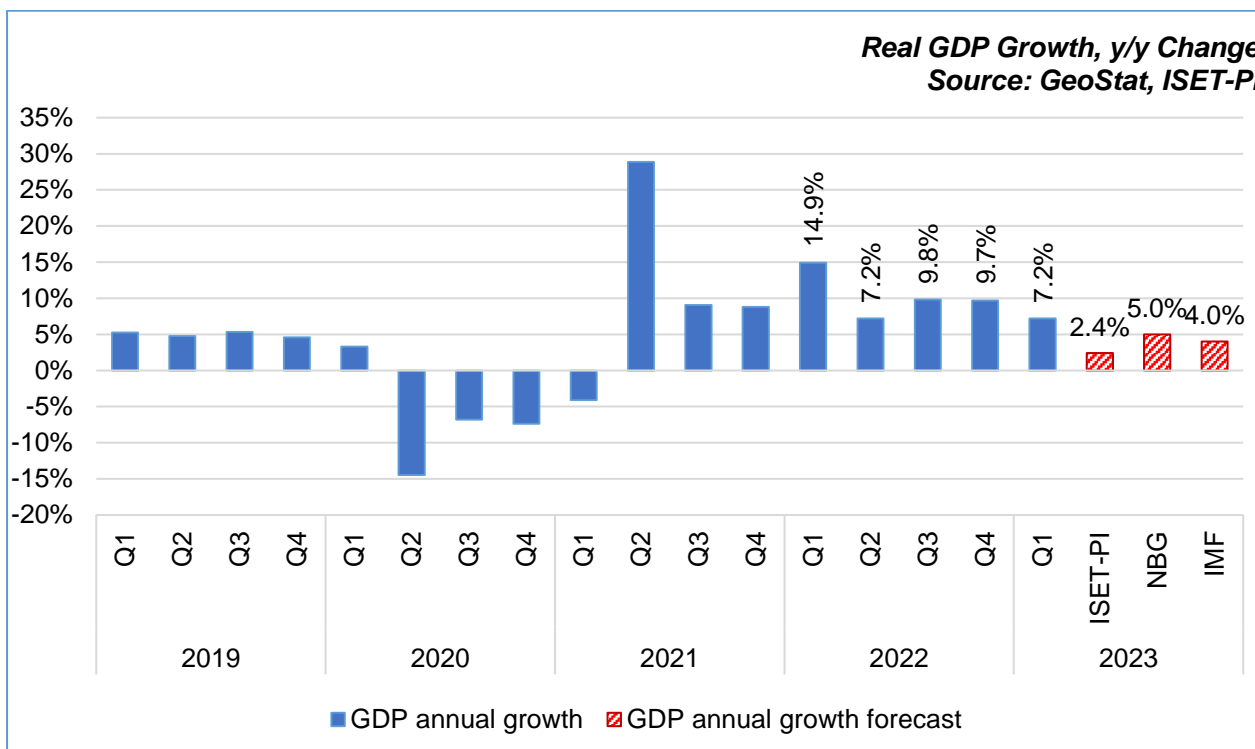




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GEORGIAN ECONOMY GOING STRONG, BUT FEARS OF GLOBAL HEADWINDS MAR THE START OF 2023



SUMMARY

The global economy remains in a volatile state amid the prolonged effects of the combined negative shocks of the pandemic, Russia’s invasion of Ukraine, high inflation and the tightening monetary policy. Although the global economy remained resilient at the beginning of the year, the situation is expected to worsen. In 2023 global economic activity is expected to slow down despite several major economies showing stronger than expected economic growth, despite a rapid reopening of China and robust consumption in the United States. While China is expected to recover, the growth in advanced economies is likely to decline. The growth of global output, estimated at 3.4% in 2022 is expected to decline to 2.8% in 2023. This is the lowest growth rate observed since 2001 (excluding the 2008 global financial crisis and during the critical phase of the COVID-19 pandemic) ([IMF, April 2023](#)).

Given these global challenges, Georgia and the South Caucasus have been affected as well. Georgia’s neighbors are expected to show moderate to weak growth for 2023: [Armenia](#) (+5.5% y/y), [Azerbaijan](#) (+3% y/y), and [Türkiye](#) (+2.7% y/y). The [Russian](#) economy, surprisingly, is also expected to show positive, albeit weak economic growth (+0.7% y/y). The output in emerging markets and developing economies (EMDEs) is expected to grow by 3.9%, on pace with 4% growth observed in 2022.

[According to GeoStat’s latest GDP growth estimates](#), due to recovering tourism, increasing migration, financial inflows, and increased demand, the Georgian economy grew by 7.7% y/y in the first quarter of 2023. Moreover, it is expected that improved investment dynamics will persist,



hence, the National Bank of Georgia adjusted the real GDP growth expectations for 2023 to 5% ([NBG, May 2023](#)), compared to the previous estimate of 4% ([NBG, February 2023](#)).

ISET-PI's GDP forecast placed the 2023 annual real GDP growth at 2.6% y/y (see Figure 1 above) ([May 2023](#)). However, these numbers may be underestimated by the model at the current point in time. This is due to the fact that ongoing large-scale in-migration had not had relevant analogues in the Georgian data in the past.

INFLATION

According to recent [GeoStat](#) data, annual inflation in the Consumer Price Index (CPI) stood at 7.6% in Q1 2023, 4.6 pp higher than the targeted 3%. The gradual phasing out of the negative effects of the Russia-Ukraine war on the international commodity prices along with a strong inflow of Russian migrants into Georgia and tightened monetary policy have strengthened the GEL exchange rate and reduced inflationary pressure. On the other hand, the increased demand for services from foreigners pushed the prices for the rentals and HORECA sectors up, driving the quarterly inflation rate. To continue with the statistics, higher food prices showed a 13.6% y/y increase, contributing 4.5 pp to the annual inflation. The following notable contributors to inflation were housing, water, electricity, gas, and other fuel prices. These products combined added 1.1 pp to the overall inflation rate with a 12.2% y/y increase. The actual rentals for housing increased by 37.9% y/y and contributed 0.7 pp to the overall inflation rate.

In the end, even though international commodity prices showed a decreasing tendency, due to the increase in unit labour cost, the National Bank of Georgia is expected to keep decreasing the monetary policy rates at a considerably slower pace ([NBG, May 2023](#)). According to the NBG's latest monetary policy report ([NBG, May 2023](#)), the medium-term inflation rate is forecasted to stay close to the targeted 3% in 2023.

EXTERNAL SECTOR: TRADE, TOURISM, REMITTANCES, FDI

In Q1 2023 Georgia's external merchandise trade expanded by 28.9% y/y, with both exports and imports having increased, and exceeded the numbers observed back in Q1 2019, before the pandemic ([GeoStat, 2023](#)). After deteriorating in Q4 2022, the trade balance improved somewhat, reaching 2,094 million USD in Q1 2023.

The registered export of goods increased by 24.7% y/y ([GeoStat, 2023](#)), which was mostly attributed to rising exports of goods in real terms, with prices of export goods being moderately lower ([NBG, May 2023](#)). The major drivers behind increased exportation were exports to Armenia (+12.1 pp y/y), Kazakhstan (+8.4 pp y/y), Kyrgyzstan (+7.7 pp y/y), Russia (+5.7 pp y/y) and Azerbaijan (+4.7 pp y/y). On the other hand, declining exports to China (-7.4 pp y/y), United States (-5.8 pp y/y), and Ukraine (-2.3 pp y/y) had a negative effect on the growth of exports.

The higher price of consumer goods was the major contributor to increased export in Q1 ([NBG, May 2023](#)), followed by the increased export of investment goods. The rise in the export of consumer goods was driven by a greater re-export of motor cars (mainly to Armenia, Kazakhstan and Kyrgyzstan). The export of motor cars rose by 333% – contributing 27 pp y/y to the overall rise in export ([GeoStat, 2023](#)). The exports of alcoholic beverages (+1.43 pp y/y) and cigarettes (Cigars, cheroots, cigarillos and cigarettes) (+1.38 pp y/y) also were the main contributors to growing exports. According to the NBG, lower exports of intermediate goods was a result of declining exports of ferro-alloys to the USA and Italy declining exports of copper ores and concentrates to China and lower exports of chemical fertilizers to Ukraine ([NBG, May 2023](#)). When



it comes to investment goods, increase (re)exports of motor vehicles for the transport of ten or more persons (+1.71 pp y/y) and automatic data processing machines (+1.32 pp y/y) also were top contributors in overall growth of exports.

Imports rose by 30.7% y/y ([GeoStat, 2023](#)), driven by rising internal demand. Imports from USA were the main contributors to the overall growth of all imports (+8.9 pp y/y), outweighing the effect of imports from EU (+8.8 pp y/y). Imports from Russia still remain at a high level, contributing 8pp y/y to growth of imports, just behind USA and EU. From regional countries, only Türkiye made a reasonable contribution to growth of imports (+4.1 pp y/y). Contribution from Armenia was only slightly positive, while imports from Azerbaijan declined. (-1.2 pp y/y).

Consumer and intermediate goods were the primary contributors to the overall growth of imports. Motor cars (+17.2 pp y/y) medicaments (+1.09 pp y/y) and telephone sets (+0.9 pp y/y) were the largest drivers behind increased import of consumer goods. While petroleum gases and other gaseous hydrocarbons (+1.5 pp y/y), coal (+0.38 pp y/y) and iron/steel parts (+0.37 pp y/y) were the major drivers of imports of intermediate goods ([GeoStat, 2023](#)).

Due to the ongoing war in Ukraine, Georgia saw an increase in the number of international visitors. In the first quarter of 2023, the total number of visitor trips reached 1.066 million (a 109.6% increase over the same period in 2022). ([GNTA, 2023](#)). The most visitors came from Russia (+257.7% y/y), Turkey (+108.5% y/y) and Armenia (+209.6% y/y). Given the increased number of international trips, income from foreign travel has risen correspondingly, reaching almost 795.4 million USD – more than double the amount observed in the same period of 2022 ([NBG, 2023](#)).

According to [NBG](#) statistics, total money transfers to Georgia amounted to 1.26 billion USD in Q1 2023, a 130.3% annual increase. The increased inflow of Russian migrants to Georgia tremendously increased instant money transfers from Russia (851.3% y/y) contributing 111 pp to the overall increase in the quarterly money transfers. Other main contributors to the increase in the money inflow were the following countries: USA (+41.8% y/y) – 5.1 pp, Italy (+19.1% y/y) – 3.6 pp, Germany (+47.6% y/y) – 2.7 pp, Kazakhstan (+39.8% y/y) – 2 pp, Kyrgyzstan (+96.5% y/y) – 1.5 pp and Israel (+13.6% y/y) – 1.1 pp. On the other hand, money transfers from Ukraine to Georgia decreased by 98.6% y/y and so did Azerbaijan (21.4% y/y).

According to [GeoStat](#) (2023), foreign direct investment in Georgia amounted to 496.6 million USD in Q1 2023, recording a 13.7% decrease compared with the preliminary data from Q1 2022. FDI was mainly directed towards manufacturing (45.6%), trade (18.3%), transport (8.7%), information and communications (8.5%), energy (7.9%), construction (3.5%), art, entertainment and recreation (3.2%). Netherlands was the top investor for Georgia with 239.6 million USD, followed by Japan – with 63.2 million USD, the United States – with 54.7 million USD, Türkiye – with 47 million USD, and Russia – with 28.2 million USD.

PUBLIC FINANCES

The total revenue of the general budget amounted to 5.1 billion GEL, a rise of 12.4% y/y that was mainly driven by increased tax collection (+12.6% y/y). It should be noted that the collection of tax on goods and services (+23.8% y/y), income, profit and capital gains (16.2% y/y) primarily contributed to this growth ([Ministry of Finance of Georgia, 2023](#)).

Current governmental expenditures also rose by 10.5% y/y in the reported quarter (amounting to 4.2 billion GEL). From this expenditure, spending on grants has been reduced by 15.4% (y/y), while spending on the following categories has been increased: subsidies (+31.5% y/y), use of



goods and services (+7.7% y/y), compensation for employees (18.4% y/y), and interest (+72.2% y/y). Additionally, the net acquisition of non-financial assets increased by 15.1% y/y, amounting to 742.2 million GEL in Q1. The first quarter of 2023 recorded a budget surplus of 98.4 million GEL. Governmental debt decreased by 2.6% from 28.5 billion GEL and amounted to 27.7 billion GEL. This was mainly driven by the reduction in foreign debt (-3.8%). The share of foreign debt in the total figure stood at 74.2% indicating the higher exposure of the Georgian economy to exchange rate volatility ([Ministry of Finance of Georgia, 2023](#)).