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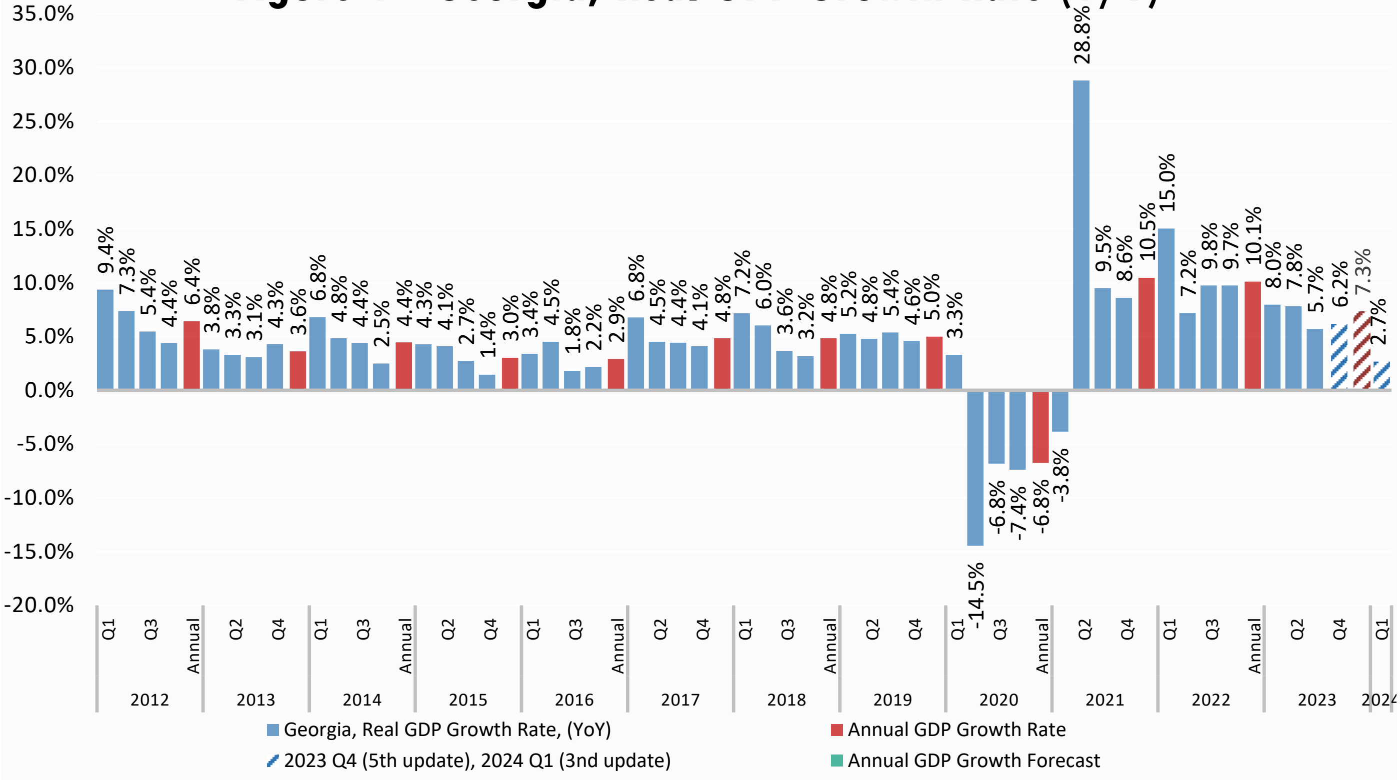
Analyzing economic trends in Georgia: moderate growth in foreign currency deposits, annual decline in exports, remittances adjust for migration impact, and below-target inflation

Figure 1 - Georgia, Real GDP Growth Rate (Y/Y)



ISET-PI has updated its real GDP growth forecast for the fourth quarter of 2023 and the first quarter of 2024. Here are the highlights of this month's release.

HIGHLIGHTS:

- Geostat has released its rapid estimate of real GDP growth for November 2023. The estimated growth stands at 5.9%, while the average real GDP growth for January-November 2023 reached 6.9%.
- In November, Geostat maintained its rapid estimate of economic growth for the first two quarters of 2023. The growth rate for Q1 is estimated to be 8.0%, and 7.8% for Q2. While the GDP growth for Q3 was adjusted upward from 5.4% to 5.7% by the end of January.
- ISET-PI predicted 6.2% and 2.7% growth for the fourth quarter of 2023 and the first quarter of 2024, respectively.
- Based on November data, the annual growth in 2023 is expected to be 7.3%.

Variables behind the GDP growth forecast:

National and Foreign Currency Deposits. The first set of variables with a moderate effect on our forecast relates to national and foreign currency deposits in commercial banks. All categories of national currency deposits experienced growth in annual terms. In particular, national currency demand deposits saw an annual increase of 43.7%, while time deposits increased by 31% annually. **Consequently, national currency total deposits increased by 34.9% yearly.** However, according to our model, *the national currency deposits had a negative contribution to the real GDP growth.*

In contrast to domestic currency deposits, **foreign currency total deposits increased relatively moderately by 5.2%** compared to the same month of the previous year. In the same period, foreign currency current accounts and demand deposits decreased by 1.6% and 0.1%, respectively, in annual terms. On the other hand, foreign currency time deposits increased by 18.3% yearly. The depreciation of the national currency partially drives the increase in the annual growth of foreign currency deposits. As a result, the dollarization ratio of deposits, included in Broad Money, increased by just 1 percentage point monthly, however, it decreased by 11.8 percentage points yearly. *Overall*, *foreign currency deposit-related variables had a relatively high negative contribution to real GDP growth based on our model.*

Merchandise Trade. In November, Georgia's exports experienced a 1.8% annual decrease. This was mainly driven by the decreased export/re-export of *copper ores and concentrates* (decreased by 76.5% YoY), *ferro-alloys* (decreased by 28.6% YoY), *mineral or chemical fertilizers, nitrogenous* (decreased by 61.6% YoY), and *wine of fresh grapes* (decreased by 27.4% YoY). On the contrary, the export/re-export of *motor cars* showed a significant annual increase (increased by 81.8% YoY).

During this period, the import of goods decreased by 6.8% yearly, driven by a decreased import/re-import of *motor cars* (decreased by 3.9% YoY), *petroleum gases and other gaseous hydrocarbons* (decreased by 33.1% YoY), and *telephone sets*, including *telephones for cellular networks or other wireless networks* (decreased by 6% YoY). In contrast, imports/re-import of *petroleum and petroleum oils* (increased by 24.9% YoY) and *medicaments put up in measured doses* (increased by 40.8% YoY) experienced an annual increase. **As a result, the trade deficit decreased moderately by 5.4% yearly and amounted to 740 million USD.** *Overall, trade-related variables had a slight positive influence on the GDP growth forecast.*

Remittances. In November, remittances decreased by 43.8% annually and reached 292.7 million USD. The main contributors to this decrease were the *Russian Federation* (decreased by 76.2% YoY, -46.2 ppts), *Turkey* (decreased by 9.8% YoY, -0.2 ppts), and *Azerbaijan* (decreased by 17.7% YoY, -0.1 ppts). Whereas money inflows increased from *Italy* (increased by 19.7% YoY, 1.4 ppts), *United States of America* (increased by 41.6% YoY, 2.3 ppts), *Germany* (increased by 32.2% YoY, 1 ppts), *Greece* (increased by 7.8% YoY, 0.3 ppt), *Kazakhstan* (increased by 71.3% YoY, 1.4 ppts), *Spain* (increased by 8.7% YoY, 0.1 ppts), and *France* (increased by 12.4% YoY, 0.1 ppts). The reduction in money inflow can be attributed to the base effect. In 2022, there was a substantial surge in the influx of Russian citizens relocating to Georgia in the aftermath of Russia's conflict in Ukraine, and they subsequently remitted funds for their personal expenditures. Consequently, Georgia is now observing a return to more typical patterns in money transfers as the transient impact of this event diminishes. To provide further clarity on this matter, it is worth noting that money inflow witnessed a remarkable 40% increase in the third quarter of 2023 when contrasted with the corresponding period in 2021. *As a result, money transfers still have a slight positive contribution to the growth forecast.*

Exchange Rate. In November, Georgian Lari depreciated against the **Dollar** (0.3% in monthly terms), **GEL/EUR** (4.1% in monthly terms), and **Ruble** (5.2% in monthly terms). However, the **GEL/TRY** exchange rate appreciated slightly by 2.1% monthly. Furthermore, **REER appreciated by 2.7% yearly, while it depreciated by 2.8% monthly. REER's yearly appreciation is mostly related to the relocation of Russian citizens.** While the depreciation of the Georgian Lari negatively impacts the Georgian population due to heavy reliance on imports and significant levels of debt dollarization (businesses having income and liabilities in different currencies), it simultaneously enhances the competitiveness of exports. This dual effect may contribute positively to Georgia's growth in the medium to long term. Overall, REER-*related variables had a significant negative influence on the real GDP growth projections.*

Money Supply. In November, all monetary aggregates including Narrow Money (M0) and Broad Money (M3), experienced notable growth in annual terms. Monetary aggregates M2 and M3 saw a yearly growth of 31% and 17.6%, respectively. The currency in circulation and Narrow Money (M0) increased by 15.4% and 20.4% in annual terms, respectively. However, *money supply-related variables had a negative contribution to the real GDP growth based on our model.*

Consumer Credit. In November, the total volume of commercial banks' consumer credit increased by 3.1% monthly and by 23.8% yearly. Furthermore, the credit volume of commercial banks' short-term consumer credits increased by 7.4% monthly and 30% yearly (the main drivers behind this positive trend in short-term consumer loans are domestic and foreign currencies, which went up by 18.2% and 97.8% respectively in yearly terms). Furthermore, the credit volume of commercial banks' long-term consumer credits increased by 3.0% monthly and 23.6% yearly. It is worth mentioning that the growth rate experienced a significant decline in comparison to the previous year. The average growth rate in the first eleven months of 2022 stood at 33.4%, whereas it dropped notably to 21.0% in 2023. *Overall, the variables related to consumer credit have had a small negative impact on the growth forecast.*

Inflation. In November, the annual inflation of consumer prices amounted to 0.1%, which is notably lower than the targeted 3%. The decreasing trend in CPI inflation is mainly related to exogenous factors, such as weakened pressure on prices resulting from the pandemic and the Russia-Ukraine war. It is also worth noting that **oil prices on the global market (Euro Brent Spot Price (COP) decreased by 9.3% yearly.** However, the depreciation of the Georgian Lari (GEL) contributes to an increase in the prices of imported goods. It is also crucial to acknowledge that there exist substantial risks pertaining to the potential elevation of inflation in the global commodity market, primarily stemming from the prevailing geopolitical circumstances. *Overall, CPI-related variables have had a negligible impact on the GDP forecast.*

Our forecasting model is based on the Leading Economic Indicator (LEI) methodology developed by the New Economic School, Moscow, Russia. We have constructed a dynamic model of the Georgian economy, which assumes that all economic variables, including GDP itself, are driven by a small number of factors that can be extracted from the data well before the GDP growth estimates are published. For each quarter, ISET-PI produces five consecutive monthly forecasts (or "vintages"), which increase in precision as time passes. Our first forecast (the 1st vintage) is available around five months before the end of the quarter in question. The last forecast (the 5th vintage) is published in the first month of the next quarter.