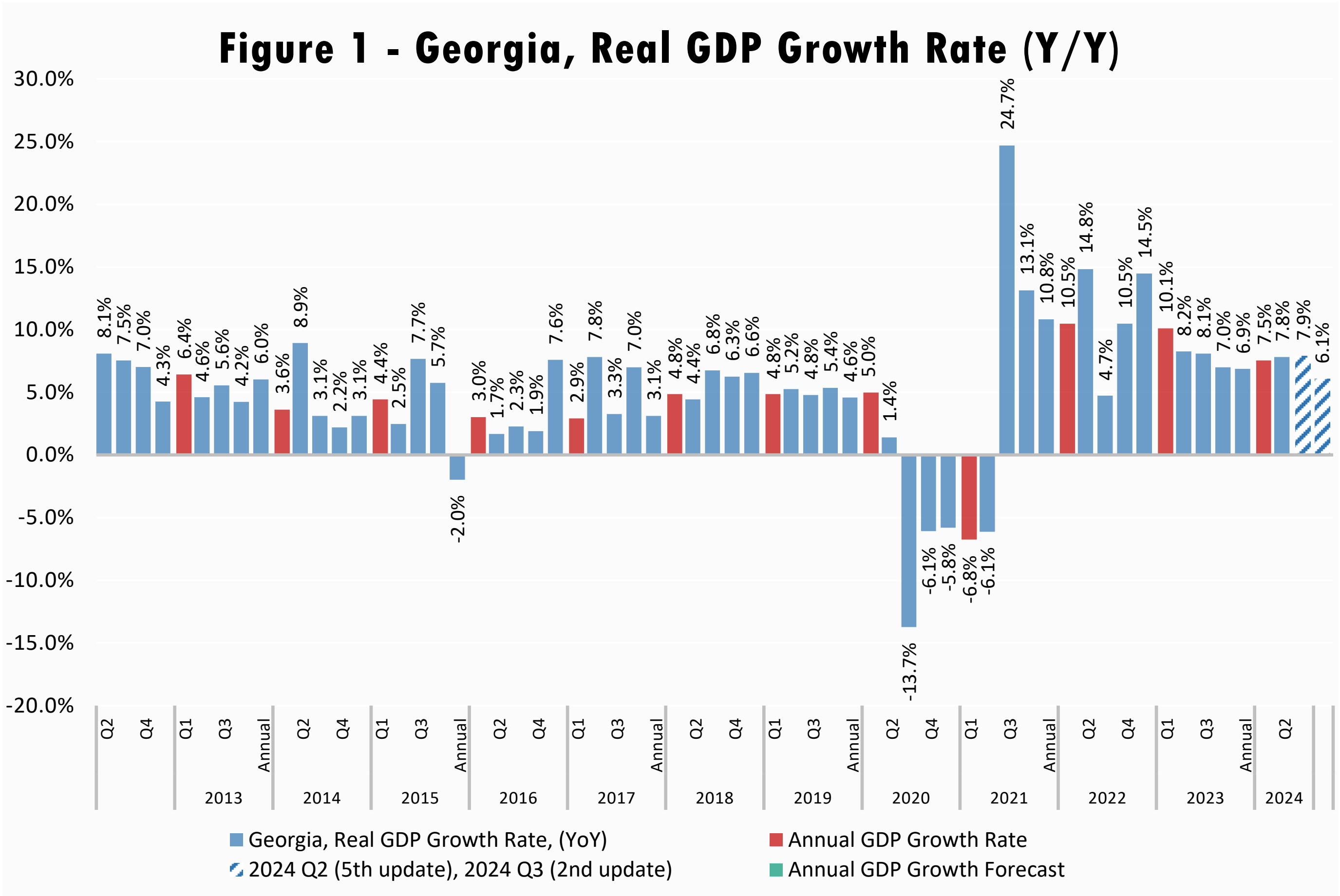
Authors: Tornike Surguladze and Davit Keshelava

Resilient GDP growth forecast despite trade and remittance challenges in April



ISET-PI has updated its real GDP growth forecast for the second and third quarters of 2024. Here are the highlights of this month's release.

HIGHLIGHTS:

- Geostat has published its preliminary estimate of real GDP growth for April 2024, which stands at 11.8%. In addition, the estimated growth for the first quarter of 2024 reached 7.8%.
- ISET-PI forecasts Georgia's economy to grow by 7.9% in the second quarter and 6.1% in the third quarter of 2024.
- According to April data, the annual growth in 2024 is projected to be 7.1% in the worst-case scenario and 8.8% in the best-case or average long-term growth scenario. Our median

scenario, reflecting the average growth from the past four quarters, forecasts an 8.2% increase in real GDP.

Variables behind the GDP growth forecast based on the April data:

National and Foreign Currency Deposits. The first set of variables with a moderate impact on our forecast pertains to national and foreign currency deposits in commercial banks. All major categories of national currency deposits showed annual growth. Specifically, national currency demand deposits increased by 29.1% year-over-year, while time deposits rose by 35.8% annually. As a result, total national currency deposits grew by 29.4% on an annual basis. *Overall, national currency deposits had a positive contribution to the real GDP growth forecast.*

Total foreign currency deposits increased by 15.9% compared to the same month of the previous year. In the same period, foreign currency current accounts and demand deposits increased by 8.5% and 0.9%, respectively, in annual terms. Furthermore, foreign currency time deposits saw a significant annual increase of 39.5%. *Consequently, variables related to foreign currency deposits contributed only moderately to the real GDP growth forecast according to our model.*

Merchandise Trade. In April, Georgia's exports experienced a 12.6% annual decrease. This decline was primarily driven by a significant reduction in the export/re-export of motor cars, which fell by 27.5% year-over-year. On the other hand, there was an annual increase in the export/re-export of wine of fresh grapes (up by 94.1% YoY) and undenatured ethyl alcohol, spirits, liqueurs, and other spirituous beverages (up by 64.8% YoY).

During this period, the import of goods increased by 13.8% year-over-year, driven by an annual increase in the import/re-import of petroleum and petroleum oils (up 100% YoY) and medicaments put up in measured doses (up 57.9% YoY). In contrast, there was a drop in the import/re-import of motor cars (fell by 23.2% YoY) and petroleum gases and other gaseous hydrocarbons (up 32.7% YoY). **Consequently, the trade deficit increased by 32.1% year-over-year, amounting to 957 million USD.** *Overall, trade-related variables had a slight negative influence on the GDP growth forecast.*

Remittances. In April, remittances decreased by 25.2% year-over-year, reaching 278.5 million USD. The primary contributors to this decline were the Russian Federation (down 69.3% YoY, -29.8 percentage points), Kazakhstan (down 38.0% YoY, -2.0 percentage points), Turkey (down 13.3% YoY, -0.3 percentage points), and Azerbaijan (down 22.7% YoY, -0.3 percentage points). Conversely, money inflows increased from the United States (up 34.1% YoY, 3.2 percentage points), Italy (up 11% YoY, 1.2 percentage points), Germany (up 12.9% YoY, 0.6 percentage points), and Greece (up 6% YoY, 0.3 percentage points). The reduction in money inflow can be again attributed to the base effect. In 2022, there was a substantial surge in the influx of Russian citizens relocating to Georgia following Russia's war in Ukraine, and they subsequently remitted funds for their expenditures. As the transient impact of this event diminishes, Georgia is observing a return to more typical patterns in money transfers. *However, money transfers still have a slight positive contribution to the growth forecast according to our model.*

Exchange Rate. In April, the Georgian Lari appreciated against the **Dollar** (0.4% in monthly terms), **Euro** (1% in monthly terms), **Ruble** (1.1% in monthly terms), and **Turkish lira** (0.5% in monthly terms). However, **REER depreciated by 3.3% yearly.** The appreciation of the Georgian Lari positively impacts the Georgian population due to heavy reliance on imports and significant levels of debt dollarization (a notable portion of businesses having income and liabilities in different currencies). However, it simultaneously decreases the competitiveness of exports. Overall, REER-*related variables had a negative influence on the real GDP growth projections.*

Consumer Credit. In April, the total volume of commercial banks' consumer credit increased by 28.9% year-over-year. The volume of short-term consumer credits rose significantly by 82.3% annually, driven mainly by increases in both domestic and foreign currencies, which grew by 29.2% and 343%, respectively, on a yearly basis. Furthermore, the volume of long-term consumer credits provided by commercial banks increased by 27.6% annually. *Despite these increases, the variables related to consumer credit had a small positive impact on the growth forecast.*

Inflation. In April, **the annual inflation rate for consumer prices was 1.5%, which is significantly lower than the targeted 3%.** Stable international commodity prices have played a key role in mitigating inflationary pressures. It is expected that inflation will gradually realign with the medium-term target. **Oil prices on the global market (Euro Brent Spot Price) increased by 6.3% year-over-year.** Consequently, inflationary risks persist. *Overall, CPI-related variables still have had a negative 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.