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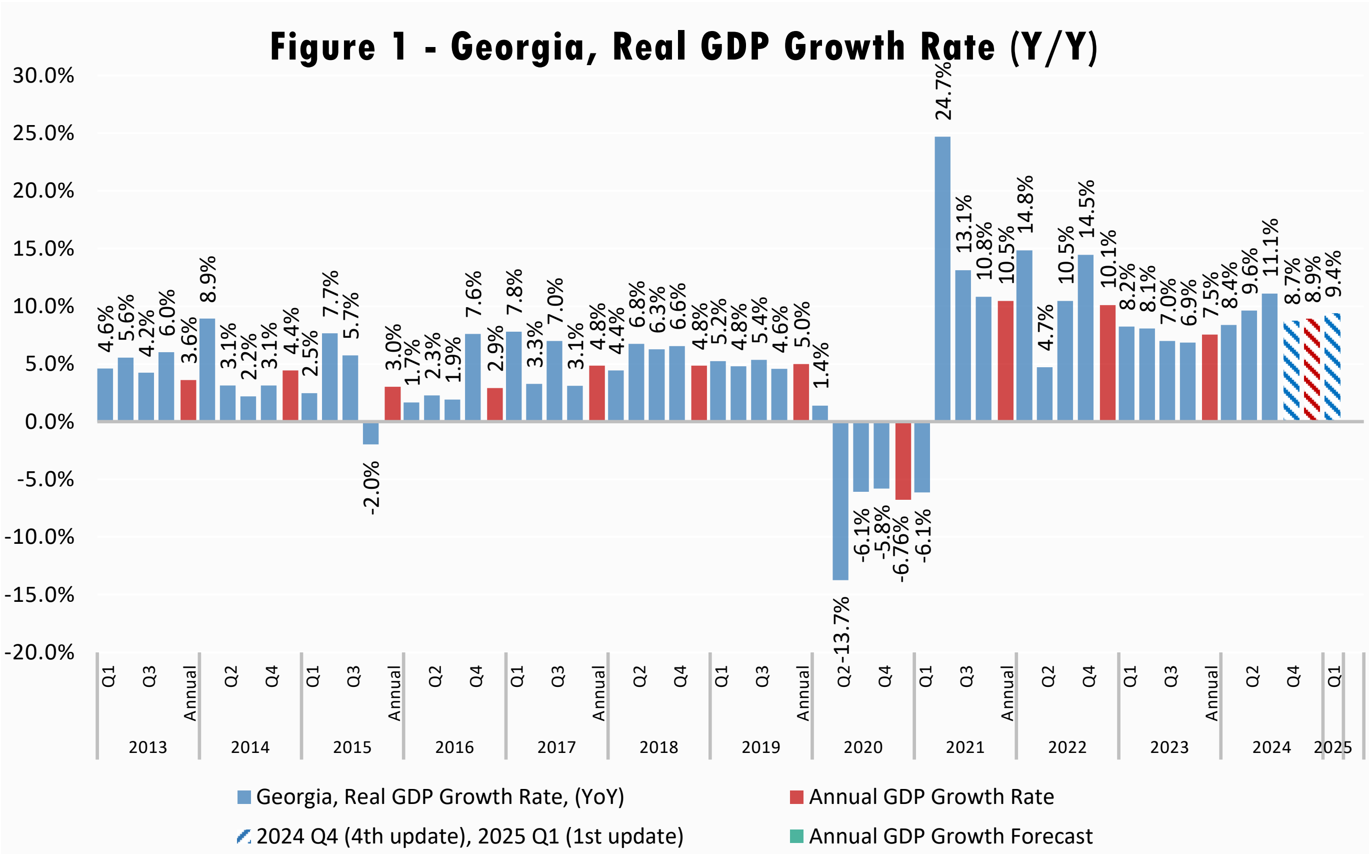
ECONOMIC GROWTH ANCHORED BY LENDING AND TRADE, CHALLENGED BY CURRENCY DEPRECIATION



ISET-PI has updated its real GDP growth forecast for the fourth quarter of 2024 and first quarter of 2025. Here are the highlights of this month's release.

HIGHLIGHTS:

- Geostat has published its preliminary estimate of real GDP growth for September 2024, which stands at 8.3%. In addition, the estimated growth for the first, second, and third quarters of 2024 reached 8.4%, 9.6%, and 11.1%, respectively. Consequently, the average real GDP growth from January to September 2024 reached 9.8%.
- ISET-PI forecasts Georgia's economy to grow by 8.7% in the fourth quarter of 2024 and 9.4% in the first quarter of 2025. However, given recent trends, the growth projections for the fourth quarter of 2024 is conservative estimate, and actual growth could surpass expectations.
- Based on September data, the annual growth for 2024 is projected to be 8.1%.

VARIABLES INFLUENCING THE GDP GROWTH FORECAST BASED ON THE SEPTEMBER 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. Almost all major categories of national currency deposits showed annual growth. Specifically, national currency demand deposits increased by 19.4% year-over-year, while time deposits rose by 36.4% annually. As a result, total national currency deposits grew by 19.9% on an annual basis. *Overall, national currency deposits still had a negative contribution to the real GDP growth forecast.*

Total foreign currency deposits increased by 15.1% compared to the same month of the previous year. In the same period, foreign currency current accounts and demand deposits increased by 7.1% and 4.8%, respectively, in annual terms. Furthermore, foreign currency time deposits saw a significant annual increase of 33.1%. *However, according to our model, variables related to the foreign currency deposits still had a negative contribution to the real GDP growth forecast.*

Merchandise Trade. In September, Georgia's exports experienced a 17% annual increase. This upsurge was primarily driven by a significant increase in the export/re-export of motor cars (increased by 43.9% YoY), undenatured ethyl alcohol, spirits, liqueurs and other spirituous beverages (increased by 41.8% YoY), precious metal ores and concentrates (increased by 132.9% YoY), and Hazelnuts and other nuts (increased by 29.9% YoY).

During this period, the import of goods decreased by -0.3% year-over-year, driven by an annual decrease in the import/re-import of motor cars (fell by 17.3% YoY). In contrast, there was an increase in the import/re-import petroleum and petroleum oils (increased by 1.5% YoY), Medicaments put up in measured doses (increased by 21.7% YoY), and Other bars and rods of iron or non-alloy steel (increased by 176% YoY). **Consequently, the trade deficit decreased by 11% year-over-year, amounting to 762 million USD.** *Overall, trade-related variables had a positive influence on the GDP growth forecast.*

Remittances. In September, remittances decreased by 1.1% year-over-year, reaching 283 million USD. The primary contributors to this decline were the Russian Federation (down 40% YoY, -8.3 percentage points), Kazakhstan (down 55.9% YoY, -3.6 percentage points), and Turkey (down 3.1% YoY, -0.1 percentage points). Conversely, money inflows increased from the United States (up 17.7% YoY, 2.6 percentage points), Italy (up 13.5% YoY, 2.1 percentage point), Germany (up 18.4% YoY, 1.4 percentage points), Greece (up 18.7% YoY, 1.4 percentage points), and Israel (up 20.4% YoY, 1.2 percentage points). The reduction in money inflow can still be 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. *Overall, money transfers had negative influence on the growth forecast according to our model.*

Exchange Rate. In September, the Georgian Lari depreciated against the **Dollar** (1.4% in monthly terms), **Euro** (2.3% in monthly terms), and **Turkish lira** (1.1% in monthly terms), and appreciated against the **Ruble** (0.5% in monthly terms). Furthermore, **REER depreciated by 0.5% monthly and depreciated by 9.2% yearly.** The depreciation of the Georgian Lari negatively 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 increases the competitiveness of exports. Overall, REER-*related variables had no influence on the real GDP growth projections.*

Consumer Credit. In September**, the total volume of commercial banks' consumer credit increased by 26.7% year-over-year.** The volume of short-term consumer credits rose significantly by 84.9% annually, driven mainly by increases in both domestic and foreign currencies, which grew by 30.3% and 365.6%, respectively, on a yearly basis. Furthermore, the volume of long-term consumer credits provided by commercial banks increased by 25.2% annually. *However, according to our model, the variables related to consumer credit had a negative impact on the growth forecast.*

Inflation. In September, **the annual inflation rate for consumer prices was 0.6%, 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. It is also worth noting, that **oil prices on the global market (Euro Brent Spot Price) decreased by 21.0% year-over-year.** However, inflationary risks persist. *Overall, CPI-related variables have not had a considerable 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.