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GEORGIA'S ECONOMIC GROWTH POWERED BY TRADE AND CREDIT, AMID POLITICAL CHALLENGES

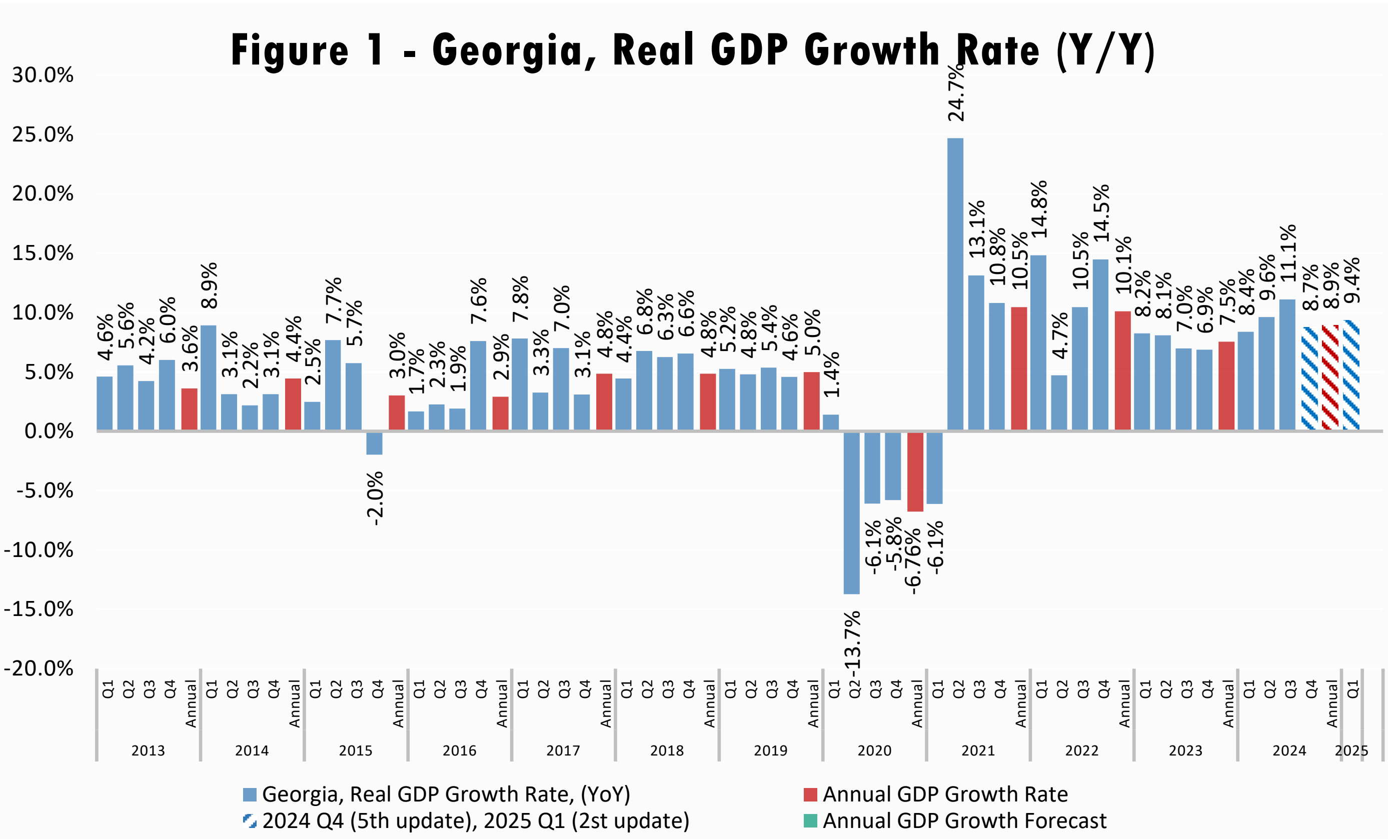

Figure 1 - Georgia, Real GDP Growth Rate (Y/Y)

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 October 2024, which stands at 11%. In addition, the estimated growth for the first, second, and third quarters of 2024 reached 8.7%, 9.7%, and 11%, respectively. Consequently, the average real GDP growth from January to October 2024 reached 10%.
- 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. Nevertheless, recent developments, including the severe political crisis in Georgia, are not yet reflected in the available data. As a result, the growth forecast for the first quarter of 2025 is likely to be overestimated.
- Based on October data, the annual growth for 2024 is projected to be 8.9%[1].

[1] Notably, the average growth rate for the first 11 months of 2024 stands at 9.4%.

VARIABLES INFLUENCING THE GDP GROWTH FORECAST BASED ON THE OCTOBER 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 10.5% year-over-year, while time deposits rose by 29.7% annually. As a result, total national currency deposits grew by 14.2% 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 16.9% compared to the same month of the previous year. In the same period, foreign currency current accounts and demand deposits increased by 14.2% and 6.3%, respectively, in annual terms. Furthermore, foreign currency time deposits saw a significant annual increase of 29.6%. *However, according to our model, variables related to the foreign currency deposits still had a negative contribution to the real GDP growth forecast.*

Official Reserve Assets: In October, the official reserve assets decreased by 13.3% compared to the previous month and by 20.2% relative to the same month in the previous year. Reserve assets serve as a critical buffer for external shocks and play an important role in ensuring macroeconomic stability. Their contraction not only reflects reduced capacity to address external vulnerabilities but may also signal weakened investor confidence or challenges in managing balance-of-payments dynamics, contributing to the downward pressure on the GDP growth outlook. *Therefore, this significant decline in reserve assets has had a negative impact on the GDP growth forecast.*

Merchandise Trade. Trade dynamics have also influenced the GDP growth forecast, with exports showing a remarkable annual increase of 39% and imports rising by 9.1% during the same period. It is noteworthy that domestic exports (excluding re-exports) surged by 70.7% in October compared to the same month in the previous year. Consequently, the trade deficit decreased by 7.7%, reaching 803.6 million USD. This reduction may signal a modest improvement in external imbalances. *Overall, trade-related variables had a positive influence on the GDP growth forecast.*

Consumer Credit. In October, the total volume of commercial banks' consumer credit increased by 27% year-over-year, reflecting robust credit activity. Short-term consumer credit rose sharply by 78% annually, driven by significant increases in both domestic and foreign currency loans, which grew by 31.7% and 265.8%, respectively. In addition, the volume of long-term consumer credits provided by commercial banks increased by 25.6% annually. This surge in consumer credit activity suggests higher borrowing and spending capacity, which supported domestic demand and partially offset some of the negative factors impacting the GDP growth forecast. *However, according to our model, the variables related to consumer credit had only slight impact on the growth forecast.*

Inflation. In October, **the annual inflation rate for consumer prices was 0.3%, 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 16.5% year-over-year.** However, inflationary risks still persist. Low inflation expectations can also have a negative impact on investment decisions[2]. *Overall, CPI-related variables 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.

[2] Low inflation expectations typically support investment by creating a stable economic environment and reducing borrowing costs. However, they could negatively affect investment in scenarios involving deflationary pressures, reduced demand, or rising real interest rates.