

## Georgian Economy in the January-March period of 2021

### Georgian economy contracted in the first quarter of 2021:

- The rapid estimates of economic growth show that the economy has not reached the pre-pandemic level yet but the recovery path continues. Following y-o-y output decreases in January (11.5%) and February (5.1%) the economy expanded by 4% in March due to the low base effect. Overall, real GDP fell by 4.2% in the first quarter of 2021;
- Financial and insurance activities, trade, manufacturing, transportation and ICT contributed positively to y-o-y economic growth in March 2021. Meanwhile, a contraction was experienced in construction, mining and entertainment sectors. Taxpayers' turnover y-o-y growth was at 21.5% in March, resulting from the low base effect of 2020. This indicator is used in rapid estimates of economic growth suggesting the economy is on a recovery path from the pandemic.

### Inflation started acceleration since the beginning of 2021:

- Consumer prices increased by 4.2% m-o-m in March and annual inflation stood at 7.2%, which is above the central bank target of 3%. Depreciation in GEL, higher international commodity prices and the end of state subsidies for utilities led to a jump in inflation in March 2021;
- Annual core inflation\* amounted to 6.9%, while the annual core inflation without tobacco\*\* stood at 6.6%, implying that the current level of annual headline inflation may persist throughout the year;
- In the breakdown of annual inflation:
  - ✓ Food & non-alcoholic beverages turned out to be the major contributor to the overall 7.2% annual inflation. The prices increased by 5.7%, adding 1.86 percentage points (p.p.). Rise in international food prices was the main driver;
  - ✓ Prices of housing, utilities and other fuels surged by 7.6%, pulled inflation up by 1.24 percentage points. The prices went up for maintenance & repair of the dwelling (7.9%), electricity, gas & other fuels (7.8%) and water supply & services related to dwelling (4.5%);
  - ✓ Prices in the health sector rose by 13.6%, contributing 1.03 percentage points to the headline inflation. Medical products, appliances & equipment prices increased by 21.3%, while prices of outpatient services went up by 12%;
- Meanwhile, the domestic PPI (DPPI) increased by 17.1% compared to March 2020. The DPPI for manufactured products increased by 17.6% compared to the same month of 2020, resulting in a 13.14 p.p. contribution to the overall annual DPPI change;

- More than one-third (33.9%) of annual domestic PPI change comes from food products, which went up by 17.1% y-o-y;
- The Import Price Index (MPI) increased by 21.4% y-o-y. Import prices of coke & refined petroleum products surged by 41.5%, while machinery & equipment rose by 34.6%, putting upward pressure on headline inflation.

\*The core inflation is calculated by excluding food and non-alcoholic beverages, energy, regulated tariffs, and transport (specific tariffs) from the consumer basket.

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#### **The trade deficit decreased thanks to shrinking imports and rising exports:**

- In the first quarter of 2021, the external merchandise trade turnover of Georgia shrank by 0.3% y-o-y amounting to \$2773.2 mln.;
- The exports equaled \$820.6 mln. (5.2% increase), while the imports stood at \$1952.6 mln. (2.4% decline);
- The trade deficit abated by 7.3% and amounted to \$1131.9 mln. Its share in external trade turnover constituted 40.8% (Jan-Mar 2020: 43.9%);
- The exports to the EU countries stood at \$156.6 mln. (5.4%↓ compared to Jan-Mar 2020) and constituted slightly less than a fifth of total exports. Meanwhile, the imports equaled \$441 mln. (8.2% drop) with 22.6% share in total imports;
- The exports to the CIS countries amounted to \$366.7 mln. (2.7%↑) and constituted about 44.7% of the total exports, while the imports amounted to \$609.3 mln. (0.2%↑) with a 31.2% share in total imports;
- The export market concentration is high: the share of the top five trading partners by exports in the total exports amounted to 56.7%. The top partners were China (13.4%), Russia (13.3%) and Azerbaijan (12.7%);
- The share of the top five trading partners by imports account for more than half of the total imports (52.4%). The top partners were Turkey (17.6%), Russia (11.3%), and China (9.4%).

#### **Consumer loans grew\*\*\* while corporate loans fell\*\*\*, especially due to foreign currency:**

- As of end of March 2021, total assets of the commercial banks increased by approximately 2.3% compared to end-2020 and stood at GEL 58.2 bln.;
- The total loan portfolio contracted by 0.5% y-t-d and amounted to GEL 38.2 bln. In y-t-d terms, loans to households (exc. individual entrepreneurs) went up by 0.7% (GEL 16.8 bln.), while the consumer loans experienced a 1.8% y-t-d growth and accounted for GEL 4.8 bln.;
- The corporate loan portfolio (inc. individual entrepreneurs) fell by 1.4% y-t-d and stood at GEL 21.5 bln. The main drivers of the contraction were loans to industry (65.6% of the fall), trade (26.9%), and real estate (18.5%);

- The share of non-performing loans in total loans realized as 8.3%, which is 0.1 percentage point higher comparing to end-2020. The pandemic-induced decline in income of households and businesses showed its impact on NPL;
- The deposit portfolio of non-financial borrowers (individuals & legal entities) expanded by 1.2% y-t-d to GEL 35.9 bln. The main drivers were demand deposits of legal entities in FC and time deposits of individuals in NC, growing by 7.3% and 8.4%, respectively. Demand deposits of legal entities increased by 5% (NC: 2%; FC: 7.3%), while time deposits of individuals expanded by 2.4% (NC: 8.4%; FC: 0.8%);
- Dollarization of the total deposits stood at 63.9% (2020: 62.1%), while it was 76.7% (2020: 75.7%) for individuals' deposits and 50% (2020: 47.2%) for legal entities;
- During the reporting period, the Return on Assets ratio (ROA) of the sector stood at 2.9% (2020 Jan-Mar: -7.1%), while Return on Equity ratio (ROE) was 27.8% (2020 Jan-Mar: -64.4%). The significant increase in profitability is driven by low base effect resulting from pandemic-induced restrictions. Profitability measures show that the banking sector started recovery from the pandemic.

\*\*\*In this section, all growth rates exclude the effect of the exchange rate depreciation

**In the latest MPC meeting (Apr 28, 2021), the NBG increased the policy rate by 1 percentage point to 9.5% amid depreciation of GEL and rising inflation:**

- National Bank of Georgia (NBG) raised the policy rate from 8.5% to 9.5%, as of 28<sup>th</sup> of April. NBG has increased the policy rate by 1.5 percentage points since the beginning of 2021;
- NBG stated that inflation is on an upward trend and is not expected to revert to the target within 2021;
- According to the NBG forecasts, inflation will remain on average around 6.5% in 2021 and then gradually approach the target (3%). NBG noted a significant increase in prices in the international commodity markets and currency depreciation in trading partner economies puts pressure on inflation;
- The NBG emphasized that tight monetary stance is essential to ensure price stability;
- The next meeting of the Monetary Policy Committee is scheduled for June 23, 2021.



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Holding**

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