

Georgian economy in the first half of 2021

Georgian economy reached two-digit growth thanks to base effect:

- The rapid estimates of economic growth show that the economic activity has exceeded even the pre-pandemic 2019-level amid fiscal stimulus and credit growth. Following y-o-y output decrease of 4.5% in the first quarter, accelerated recovery and base effect in the second quarter led to a 12.7% growth in the first half of 2021;
- Manufacturing, financial & insurance activities, transportation, trade, hotels & restaurants, real estate activities and construction contributed positively to y-o-y economic growth in June 2021. Meanwhile, a contraction was experienced in mining sector. Taxpayers' turnover y-o-y growth was at 37.5% in June, resulting from the 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 approached two-digit level due to higher prices in international markets:

- Consumer prices increased by 0.7% m-o-m in June and annual inflation stood at 9.9%, which is above the central bank target of 3%. Transmission of higher prices from international markets, the end of the utility bill subsidy program and depreciation of lari were the main factors that fuelled inflation in the first half of 2021;
- Annual core inflation* amounted to 5.9%, while the annual core inflation without tobacco** stood at 5.8%, implying that the current level of annual headline inflation may be temporary;
- In the breakdown of annual inflation:
 - ✓ Food & non-alcoholic beverages turned out to be the major contributor to the overall 9.9% annual inflation. The prices increased by 8.8%, adding 2.78 percentage points (p.p.). Rise in international food prices was the main driver;
 - ✓ Transport prices rose by 22%, contributing 2.54 percentage points to the annual inflation. Personal transport equipment had the largest impact in this segment increasing by 33.4%;
 - ✓ Prices of housing, utilities and other fuels surged by 10.5%, pulled inflation up by 1.59 percentage points. The prices went up for electricity, gas & other fuels (14%), maintenance & repair of the dwelling (7.3%) and water supply & services related to dwelling (4.5%);
- Meanwhile, the domestic PPI (DPPI) increased by 19.7% compared to June 2020. The DPPI for manufactured products increased by 19.9% compared to the same month of 2020, resulting in a 15.05 p.p. contribution to the overall annual DPPI change;
- Almost one-third (30.1%) of annual domestic PPI change comes from food products, which went up by 17.9% y-o-y;

- The Import Price Index (MPI) increased by 26.4% y-o-y. Import prices of coke & refined petroleum products surged by 74.2%, while machinery & equipment rose by 46.5%, putting upward pressure on headline inflation.

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Exports slightly exceeded the pre-pandemic level, while imports approached that level:

- In the first half of 2021, the external merchandise trade turnover of Georgia expanded by 20.7% y-o-y amounting to \$6209.7 mln.;
- The exports equaled \$1884.7 mln. (25.2% increase), while the imports stood at \$4325 mln. (18.9% increase);
- The trade deficit rose by 14.4% and amounted to \$2440.3 mln. Its share in external trade turnover constituted 39.3% (Jan-Jun 2020: 41.5%);
- The exports to the EU countries stood at \$321.3 mln. (5%↓ compared to Jan-Jun 2020) and constituted slightly less than a fifth of total exports. Meanwhile, the imports equaled \$998.9 mln. (15.8% increase) with 23.1% share in total imports;
- The exports to the CIS countries amounted to \$866.5 mln. (33.1%↑) and constituted about 46% of the total exports, while the imports amounted to \$1280.3 mln. (13.7%↑) with a 29.6% 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 58.4%. The top partners were China (15.4%), Russia (14%) and Azerbaijan (13%);
- The share of the top five trading partners by imports account for almost half of the total imports (49.2%). The top partners were Turkey (18%), Russia (10.8%), and China (8.4%).

Both consumer and corporate loans grew* in the first half of 2021:**

- As of end of June 2021, total assets of the commercial banks decreased by approximately 1.6% compared to end-2020 and stood at GEL 56 bln.;
- The total loan portfolio grew by 4.7% y-t-d and amounted to GEL 38.4 bln. In y-t-d terms, loans to households (exc. individual entrepreneurs) went up by 5.9% (GEL 19.6 bln.), while the consumer loans experienced a 9.9% y-t-d growth and accounted for GEL 5.1 bln.;
- The corporate loan portfolio (exc. individual entrepreneurs) grew by 3.5% y-t-d and stood at GEL 18.8 bln. The main drivers of the rise were loans to construction (1.4 p.p. contribution), trade (0.7%), and hotels & restaurants (0.5%);
- The share of non-performing loans in total loans realized as 6.7%, which is 1.5 percentage point lower comparing to end-2020. The recovery from the pandemic showed its impact on NPL;

- The deposit portfolio of non-financial borrowers (individuals & legal entities) expanded by 1.8% y-t-d to GEL 35.3 bln. The main drivers were demand deposits of individuals in FC and demand deposits of legal entities in NC, growing by 8.3% and 9.4%, respectively. Time deposits of legal entities decreased by 4.6% (NC: 3.7%; FC: 6.8%), while time deposits of individuals expanded by 4.2% (NC: 10.6%; FC: 2.4%);
- Dollarization of the total deposits stood at 60.6% (2020: 62.1%), while it was 75.2% (2020: 75.7%) for individuals' deposits and 44% (2020: 47.2%) for legal entities;
- During the reporting period, the Return on Assets ratio (ROA) of the sector stood at 4% (2020 Jan-Jun: -2.2%), while Return on Equity ratio (ROE) was 37.3% (2020 Jan-Jun: -21.4%). 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 (Aug 4, 2021), the NBG increased the policy rate by 0.5 percentage points to 10% based on accelerating inflation and recovery of aggregate demand:

- National Bank of Georgia (NBG) raised the policy rate from 9.5% to 10%, as of 4th of August. NBG has increased the policy rate by 2 percentage points since the beginning of 2021;
- NBG stated that the unexpectedly high inflation is a result of the sharply increased prices of food and oil in international markets and has a temporary nature;
- According to the latest NBG forecasts, inflation on average will be higher than 9% in 2021 and then decline in 2022 gradually approaching the target (3%);
- The NBG emphasized that it will maintain contractionary monetary policy in order to ensure that recent price increases do not result in high inflation expectations;
- The next meeting of the Monetary Policy Committee is scheduled for September 15, 2021.

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