

## Georgian Economy in Q2

### **Economic growth is still robust despite the external shocks:**

- The rapidly estimated real Gross Domestic Product (GDP) growth rate in June 2019 equaled 5.0% y-o-y. An average estimated y-o-y real GDP growth equaled 4.9% for the 1<sup>st</sup> half of 2019, while it was 5.7% for the same period of 2018;
- Compared to the same period of the previous year, the estimated real growth was recorded in the industry, real estate, construction, trade, transport, and hotels & restaurants sectors, while a decrease was registered in financial intermediation in June 2019.

### **Unemployment data indicates continuing easing in the labor market:**

- In the 2nd quarter of the current year the unemployment rate decreased by 0.7 percentage point compared to the corresponding period of the previous year and equaled 11.4%;
- This is attributable to the marginal drop in labor force participation and the tepid rise in the employment;
- The share of hired employees in total employed persons was 50.2%, which implies a 1.1 percentage point decline compared to the corresponding period of the previous year.

**Annual inflation is higher than the Central Bank target, however, the core inflation is subdued:**

- Consumer prices decreased by 0.02% m-o-m in July, which was significantly lower from the 1% decline experienced in June;
- Annual inflation rose to 4.6% from 4.3% in June, which is above the central bank target of 3%. However, core inflation\* increased to 1.9% from 1.4% in the prior month, implying that the increase in the annual inflation is only temporary;
- In the breakdown of annual inflation:
  - ✓ Food & non-alcoholic beverages turned out to be the major contributor to the overall 4.6% annual inflation, adding 2.3 percentage points (p.p.);
  - ✓ Alcoholic beverages & tobacco pulled inflation up by 0.9 p.p. in July driven by the increase in tobacco excises in January;
  - ✓ Transport was another driver, adding 0.5 p.p.;
- On the flip side,
  - ✓ Clothing & footwear dragged the headline down by 0.3 p.p.;
  - ✓ Communication costs reduced the headline by 0.1 p.p.;
- Meanwhile, Producer Price Index (PPI) for industrial products rose by 3.2% compared to June 2019, while the index growth amounted to 10.7% y-o-y. The PPI for manufactured products increased by 2% compared to the previous month, resulting in a 1.66 percentage points contribution to the overall monthly PPI change.

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

### **Trade deficit declines mainly driven by decreasing imports:**

- In January-July 2019, the external merchandise trade turnover of Georgia abated by 0.2% y-o-y and amounted to USD 7065.3 mln.;
  - The exports equaled USD 2102.2 mln. (12.4% growth)\*\*, while the imports stood at USD 4963.1 mln. (4.7% decline);
  - The trade deficit dropped by 14.2% and amounted to USD 2860.9 mln. Its share in external trade turnover constituted 40.5%;
  - The exports to the EU countries stood at USD 503.5 mln. (20.6% higher compared to January-July 2018) and reached a quarter of total exports, while the imports equaled USD 1280.2 mln. (12.6% drop) with 25.8% share in total import. The EU countries accounted for 27.2% of the overall trade deficit in the reporting period;
  - The exports to the CIS countries amounted to USD 1105.8 mln. (26.6% growth) and constituted half of the total exports, while the imports amounted to USD 1303.1 mln. (14.3% decline) with a quarter share in total imports. The CIS countries accounted for 6.9% of the trade deficit;
  - The export market concentration is higher: the share of the top ten trading partners by exports in the total exports amounted to 72.7%. The top partners were Russia (14.5% in total), Azerbaijan (12.7%), and Armenia (8.6%);
  - The share of the top ten trading partners by imports in the total imports account for 66%. The top partners were Turkey (17.4%), China (10.1%), and Russia (9.8%).
- \*\*The exports excluding re-exports expanded by 1.6% y-o-y and amounted to USD 1311.9 mln.

**A sluggish growth on consumer loans and a stronger one on the corporate side:**

- As of June 2019, total assets of the banking sector increased by 19.7% compared to the same month of 2018 and stood at GEL 43.1 bln.;
- The total loan portfolio rose by 23.2% and amounted to GEL 29.2 bln. In YoY terms, the consumer loans experienced a sluggish 3.5% growth and accounted for GEL 3.9 bln., while the corporate loan portfolio grew by 26.3%;
- The share of non-performing loans (CB methodology) in total loans realized as 5.7%, which is 0.2 percentage points higher comparing to December 2018;
- Non-bank deposit portfolio expanded by 21.8% y-o-y to GEL 25 bln. The main drivers were demand and term deposits in FX constituting 19% and 48% of the overall portfolio growth, respectively. Consequently, dollarization of the deposits stood at 62.8%, while it was 63.9% in December 2018;
- During the reporting period, Return on Assets ratio (ROA) of the sector stood at 2.1%, while Return on Equity ratio (ROE) was 16.2%.

**Central Bank's has maintained a hawkish 6.5% refinancing rate, after having cut it to 6.75% in January and 6.5% in March:**

- The Monetary Policy Committee (MPC) of the National Bank of Georgia (NBG) met on July 24, 2019, and decided to keep the refinancing rate unchanged at 6.5%;
- The decision based on two main factors:
  - (i) According to the NBG, in the medium-term, the weakened demand offsets the increasing inflationary pressure stemming from the exchange rate depreciation on the back of the external shock;
  - (ii) NBG estimates that current nominal effective exchange rate is undervalued more than the size of the current external shock would suggest. Hence, the expectations imply downward pressure on inflation due to the possible appreciation of the nominal effective exchange rate.

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