PASHA Holding

Georgian economy in 2020

Georgian economy contracted in 2020 due to pandemic:

- The pandemic-induced economic contraction continued in the last quarter of 2020. Intensification of the pandemic-related concerns and tight lockdown measuresled to a fall in economic growth by 6.5% in the fourth quarter of 2020. The real Gross Domestic Product (GDP) shrank by 6.1% YoY in 2020;
- Sectors driving the economic growth prior to the pandemic experienced contraction in 2020. Tourism, trade, manufacturing and transportation contributed negatively to economic growth. Taxpayers' turnover YoY growth was at -5.1% in December, higher than the level observed in the second quarter. This indicator is used in rapid estimates of economic growth suggesting the economy is performing better than it did in the second quarter. Finance, Utilies, ICT and Mining sectors experienced an economic growth despite the pandemic.

Despite rising in the second quarter inflation hovered around NBG's target at the year-end:

- Consumer prices decreased by 1% m-o-m in December and annual inflation stood at 2.4%, which is below the central bank target of 3%. Pandemic-induced fall in aggregate demand helped inflation to decrease in the second half of 2020;
- Annual core inflation* amounted to 5.3%, while the annual core inflation without tobacco** stood at 4.9%, implying that the decrease in annual headline inflation may be related to temporary factors;
- In the breakdown of annual inflation:
    - ✓ Food & non-alcoholic beverages turned out to be the major contributor to the overall 2.4% annual inflation. The prices increased by 6.8%, adding 2.19 percentage points (p.p.). Rise in international food prices was the main driver;
    - ✓ Prices of health services surged by 9.6%, pulled inflation up by 0.76 percentage points. The prices went up for medical products, appliances & equipment (13.6%) and out-patient services (11.9%);
    - ✓ Prices of alcoholic beverages & tobacco increased inflation by 0.56 p. p.;
- On the flip side,
    - ✓ Housing, utility & other fuels prices decreased by 21.7% attributable to the "Ordinance of the Government of Georgia On Approval of the Rules and Conditions for Subsidizing Utility Taxes" coming in force;
    - ✓ Transport dragged the headline down by 0.28 p.p., while recreation & culture sector prices contributed to a 0.11 p.p. fall;
- Meanwhile, the domestic PPI (DPPI) increased by 10.6% compared to December 2020. The DPPI for manufactured products increased by 13.1% compared to the same month of 2019, resulting in a 10.1 p.p. contribution to the overall annual DPPI change;

- More than half (52.6%) of annual domestic PPI change comes from food products, which went up by 14.6% YoY;
- The Import Price Index (MPI) increased by 10.9% YoY. Import prices of machinery & equipment rose by 26.4%, while prices of food products increased by 20.6% 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 triggered by constrained demand:

- In 2020, the external merchandise trade turnover of Georgia shrank by 14.8% YoY due to pandemic-induced restrictions and amounted to $11347.7 mln.;
- The exports equaled $3342.1 mln. (12% decrease), while the imports stood at $8005.6 mln. (15.9% decline);
- The trade deficit abated by 18.5% and amounted to $4663.4 mln. Its share in external trade turnover constituted 41.1% (2019: 42.9%);
- The exports to the EU countries stood at $717 mln. (13.2% ↓ compared to 2019) and constituted slightly more than a fifth of total exports. Meanwhile, the imports equaled $1920.6 mln. (17.3% drop) with 24% share in total imports;
- The exports to the CIS countries amounted to $1509.1 mln. (24.7% ↓) and constituted about 45.2% of the total exports, while the imports amounted to $2391.9 mln. (1.9% ↓) with a 29.9% 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 56.5%. The top partners were China (14.3%), Azerbaijan (13.2%) and Russia (13.2% in total);
- The share of the top five trading partners by imports account for slightly more than half of the total imports (50.6%). The top partners were Turkey (17.6%), Russia (11.1%), and China (8.9%).

Both consumer and corporate loans experienced a significant growth*, especially in national currency:**

- As of end-2020, total assets of the commercial banks increased by approximately 20.5% compared to 2019 and stood at GEL 56.9 bln.;
- The total loan portfolio rose by 12% YoY and amounted to GEL 37.4 bln. In YoY terms, loans to households (exc. individual entrepreneurs) went up by 12.1% (GEL 16.3 bln.), while the consumer loans experienced a 14.1% YoY growth and accounted for GEL 4.7 bln;
- The corporate loan portfolio (inc. individual entrepreneurs) grew by 11.9% YoY and stood at GEL 19.3 bln. The main drivers of the growth were loans to Hotels & Restaurants (19.6% of the growth), trade (18.1%), and construction (16.7%);

- The share of non-performing loans in total loans realized as 8.2%, which is 3.8 percentage point higher comparing to 2019. 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 20% YoY to GEL 35.4 bln. The main drivers were time deposits of legal entities in NC and time deposits of individuals in FC, constituting 53.7% and 11.9% of the growth, respectively. While 12.1% (NC: 5.6%; FC: 6.5%) of the total deposit growth was driven by individuals' demand deposits, demand deposits of legal entities comprised 15.4% (NC: 4.7%; FC: 10.6%) of the total growth;
- Dollarization of the total deposits stood at 62.1% (2019: 64.8%), while it was 75.7% (2019: 74.7%) for individuals' deposits and 47.2% (2019: 52.6%) for legal entities;
- During the reporting period, the Return on Assets ratio (ROA) of the sector stood at 0.2% (2019: 2.5%), while Return on Equity ratio (ROE) was 1.4% (2019: 20.3%). The significant decrease in profitability is driven by significantly higher loan loss provisions due to the COVID-19 and its economic effects. Profitability measures have improved compared to previous quarters in 2020 implying that the negative impact of the pandemic on the banking sector started to subside.

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

In the latest MPC meeting (Feb 3, 2021), the NBG maintained the current policy rate at 8% amid high uncertainty about the recovery dynamics of the economy and the growth rate of lending:

- National Bank of Georgia (NBG) kept the policy rate stable at 8%, as of the 3rd of February. NBG has not changed the policy rate since the August meeting;
- NBG stated that current downward movement of inflation is of a temporary nature and related to the government subsidy of utility bills;
- According to the NBG forecasts, inflation will remain on average around 4% in 2021 and then gradually approach the target (3%). NBG noted a significant increase in prices in the international commodity markets, pandemic-induced rising production costs and exchange rate depreciation as the main factors pulling inflation upwards;
- The NBG emphasized that tight monetary stance is essential to ensure price stability;
- The next meeting of the Monetary Policy Committee is scheduled for March 3, 2021.