

## Overview

- Economic growth remains strong in 2018 (5.0%), despite a slowdown in 2H2018
- Growth mainly based on investment and consumption
- Industry and services continue to expand, while agriculture maintains its negative trend
- Stable inflation of 2.8% in 2018; in line with NBG's inflation target of 3%
- Decline in budget deficit to 2.3% of GDP in 2018; prudent fiscal policy
- Surge in current account deficit to 9.0% of GDP in 2018
- Recent depreciation of Lari due to seasonality, external factors and presidential elections
- Disbursement of USD 41.6 m as part of IMF programme

## Topics

- **Presidential elections.** New President has been elected
- **Banking.** Measures to curb household debt
- **Turkey.** So far only moderate effect of depreciation of Turkish Lira on Georgia
- **Pension reform.** Start on 1 January 2019

# Basic indicators

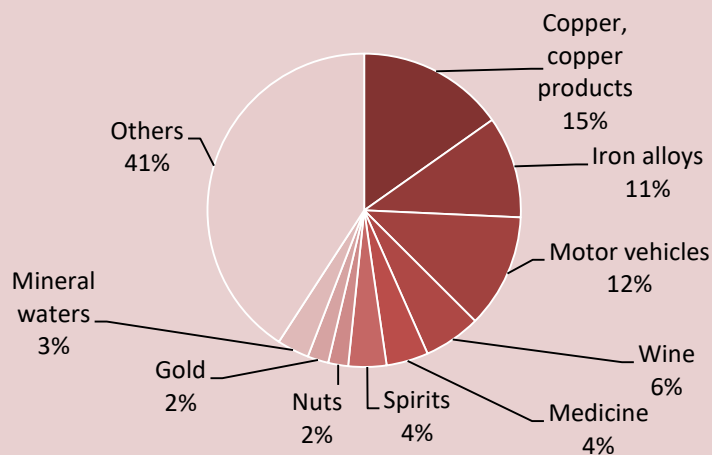
|                 | Georgia | Moldova | Belarus | Ukraine | Russia  |
|-----------------|---------|---------|---------|---------|---------|
| GDP, USD bn     | 16.7    | 11.4    | 56.9    | 126.4   | 1,576.5 |
| GDP/capita, USD | 4,506   | 3,227   | 6,020   | 2,964   | 10,950  |
| Population, m   | 3.7     | 3.5     | 9.5     | 42.6    | 144.0   |

Source: IMF World Economic Outlook October 2018, forecast 2018

## Trade structure

### Exports

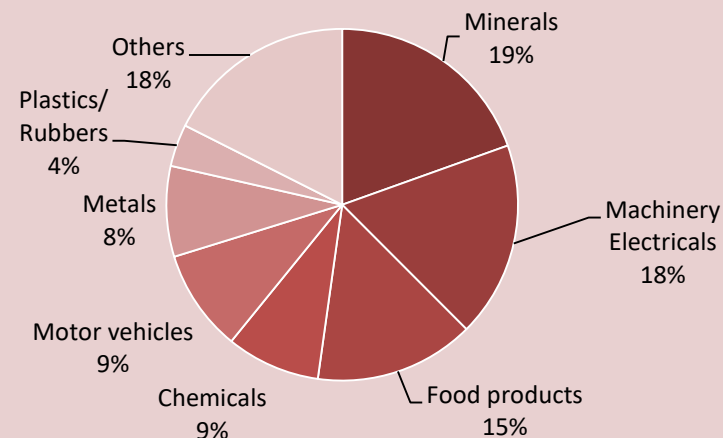
EU 22% | CIS 49% | Other 29%



Source: Geostat, Jan-Nov 2018; Note: Trade in goods

### Imports

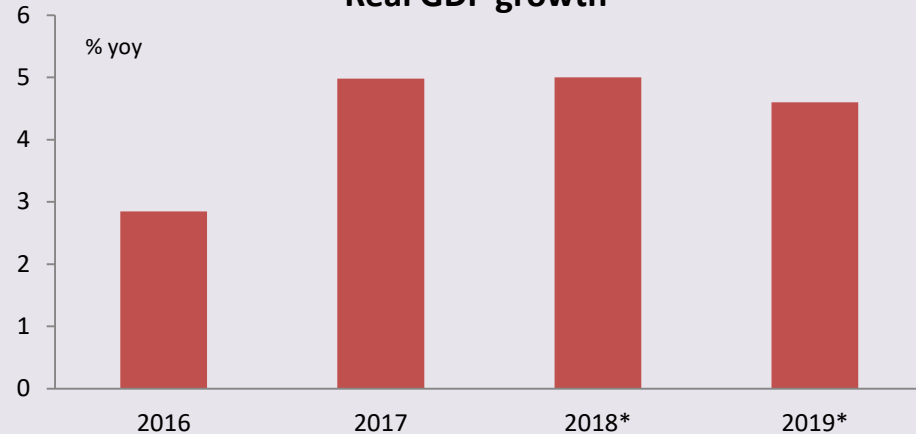
EU 28% | CIS 30% | Other 42%



Source: Geostat, Jan-Nov 2018; Note: Trade in goods

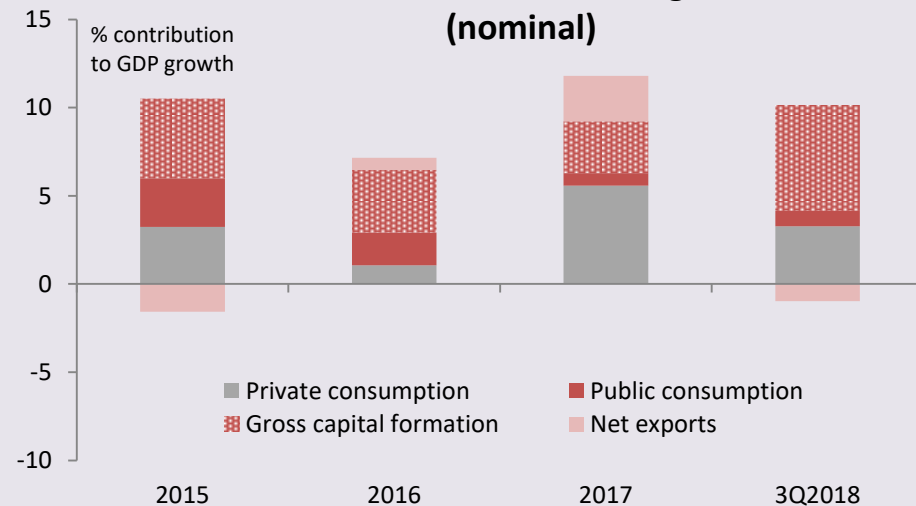
# Economic growth

## Real GDP growth



Source: IMF 2018; \*Forecast

## Contribution to economic growth (nominal)



Source: Geostat

## GDP 2018

- 1H2018: 5.4%
- Forecast 2018: 5.0%
- Thus: slowdown in 2H2018

## Growth drivers

- Private investment related to hotels, real estate and electricity generation
- But also sizeable contribution from private consumption in connection with higher remittances

## GDP 2019

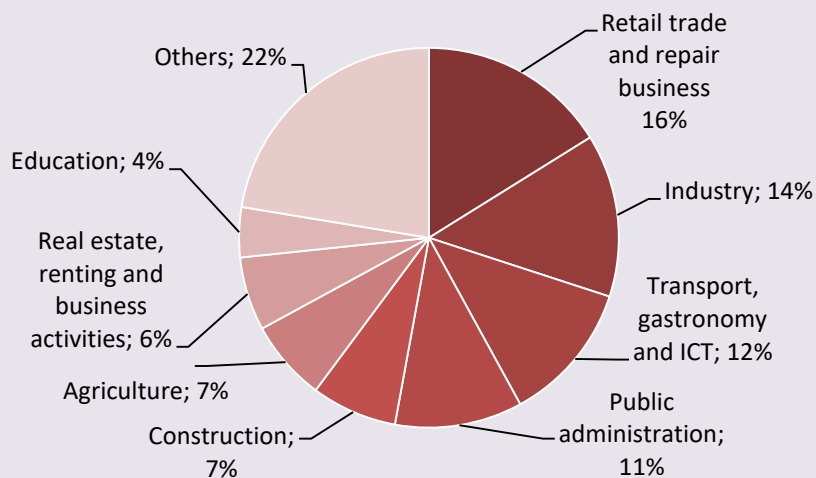
- Forecast: 4.6%
- Thus: slowdown will continue

## Conclusions

- Investment-led growth
- However: slowdown of economic activity observable

# Sectoral perspective

## Composition of GDP



Source: Geostat, 3Q2018

## Sectoral dynamic



Source: Geostat

## Agriculture

- 3Q2018: decrease by 0.6%
- Remains the weak point of the economy

## Industry

- Strong expansion: 4.7% in 3Q2018
- Positive contribution to GDP as in previous years

## Services

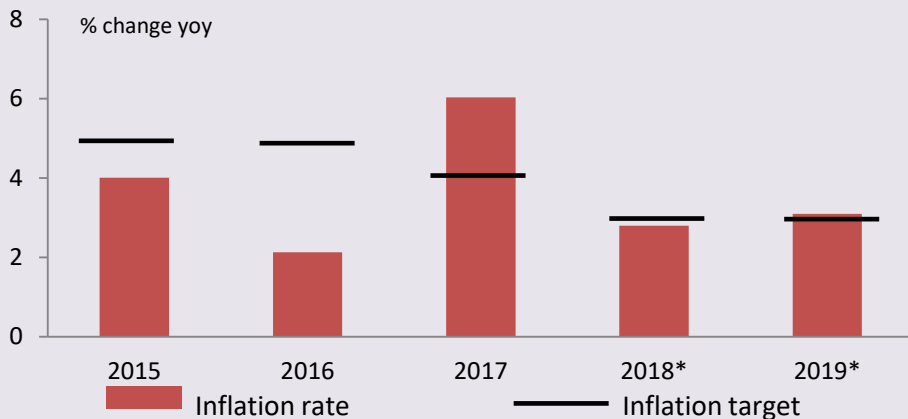
- Increase by 5.6% in 3Q2018
- Main driver of growth

## Conclusions

- Services lead sectoral growth
- Industry remains strong
- Agriculture still underperforming due to structural weaknesses

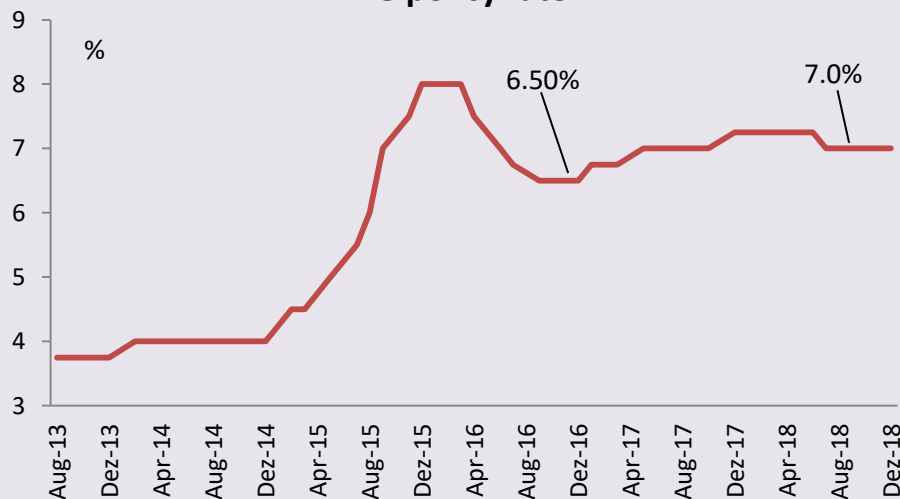
# Inflation and monetary policy

## Inflation rate and inflation target



Source: IMF 2018, \*forecast; Note: Annual average (consumer prices)

## NBG policy rate



Source: National Bank of Georgia

## Inflation

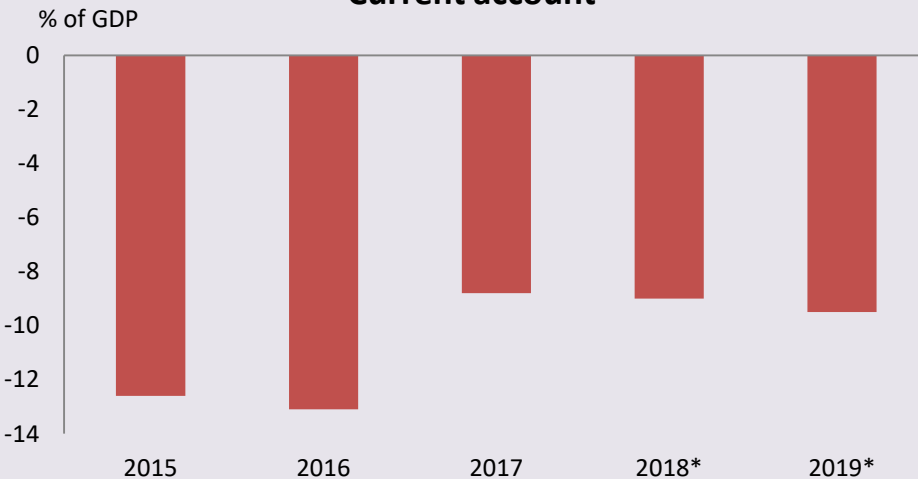
- 2018: 2.8% yoy
- Prudent monetary policy pays off
- National Bank (NBG) meets its inflation target of 3% in 2018
- 2019: slightly higher inflation but still under control
- Due to stable inflation NBG was able to slightly decrease its policy rate by 25 basis points to 7.0%

## Conclusions

- Inflation in line with target
- Stability orientated monetary policy of National Bank („inflation targeting“) has proven to be successful

# Current account and exchange rate

## Current account



Source: IMF 2018; \*Forecast

## Current account deficit

- Deficit widens to 9.0% of GDP in 2018; partly due to higher oil prices
- 2019: slight decline expected (9.5%)

## Exchange rate

- Typical seasonal depreciation in autumn
- On top: some pressure on Lari in the context of presidential elections
- However: no reason for sizeable NBG-intervention

## International FX reserves

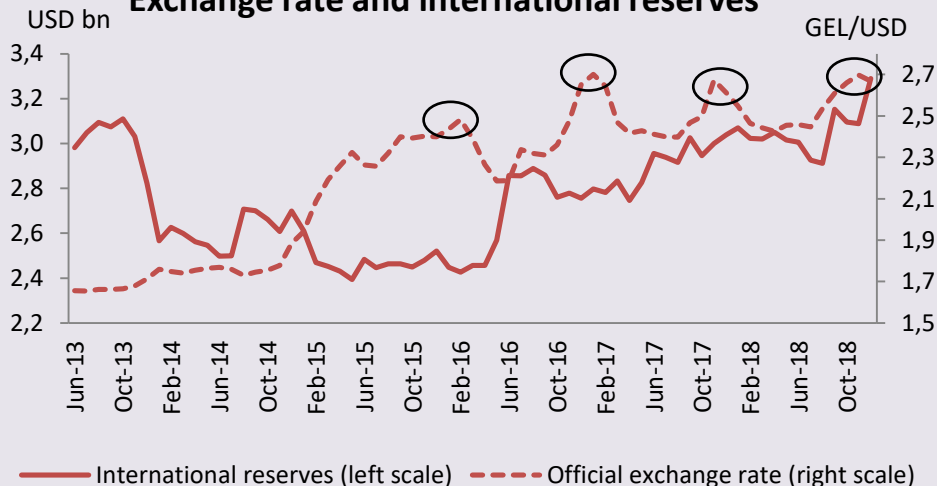
- December 2018: increase to USD 3.3 bn; equivalent to 3.3 months of imports

## Conclusions

- High current account deficit makes Georgia vulnerable to external shocks
- Recent Lari depreciation is not a reason for concern

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## Exchange rate and international reserves

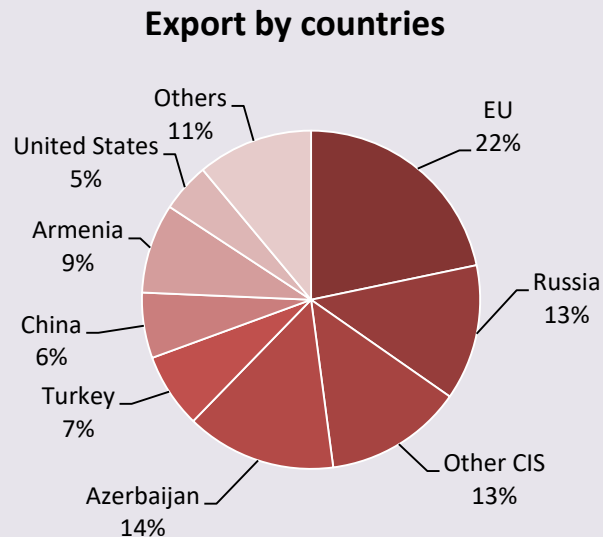


Source: National Bank of Georgia

# External trade



Source: Geostat



Source: Geostat, Jan-Nov 2018; Note: trade in goods

## Trade dynamics

- Jan-Nov 2018: increase in exports of goods by 24.0%; imports by 16.8%
- Positive trend

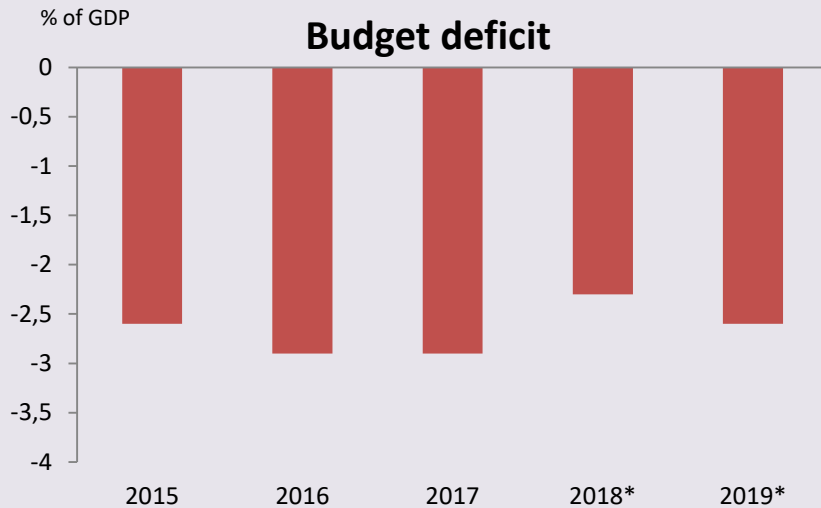
## Regional structure of exports

- Diversified trade structure
- Neighbours account for a major share of exports
- EU is the main export destination, with 22% of total exports in Jan-Nov 2018

## Conclusions

- Positive development of foreign trade
- Regional diversification helps Georgia to absorb negative shocks, e.g. due to depreciation of Turkish Lira

# Public finances and government debt



## Budget deficit

- 2018: deficit goes down to 2.3% of GDP due to higher-than-expected revenues, strong economic growth and delays in public investments

## Public debt

- 2018: Slight reduction to 43% of GDP
- Fiscal prudence likely to continue in 2019

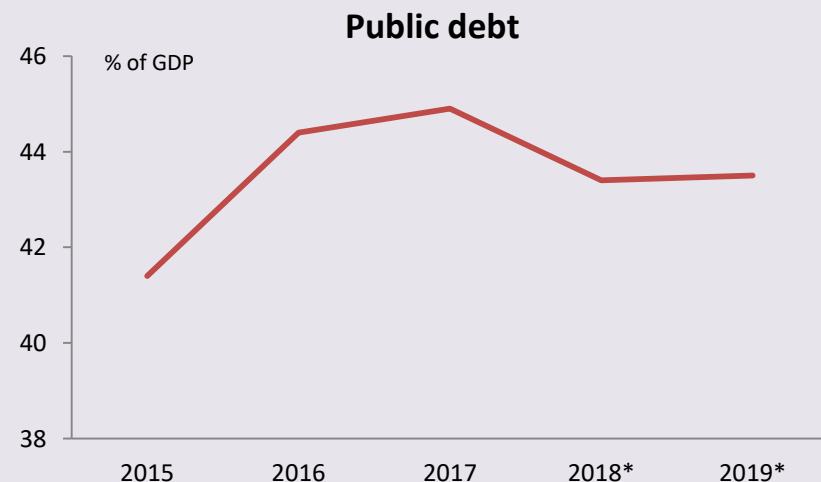
## IMF programme

- December 2018: agreement on the third review of the IMF programme
- Disbursement of ca USD 41.6 m

## Conclusions

- Stable fiscal situation
- High economic growth is essential for maintaining a low debt level as % of GDP

Source: IMF, \*Forecast; Note: programme definition



Source: IMF 2018; \*Forecast



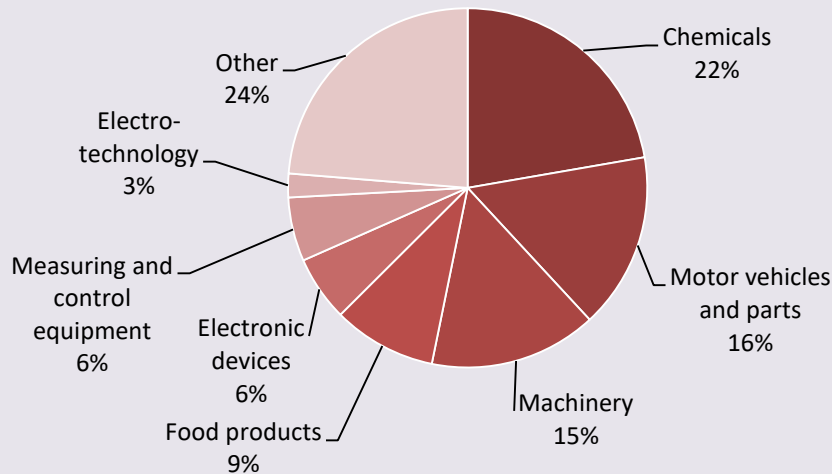
# Bilateral trade between Germany and Georgia

German trade with Georgia



Source: German Federal Statistics Office, Note: trade in goods

German exports to Georgia



Source: German Federal Statistics Office, Jan-Nov 2018, Note: Trade in goods

## Trade

- Trade between Georgia and Germany in Jan-Nov 2018 at EUR 398 m

## Exports to Georgia

- Exports from Germany to Georgia increased by 4.4% in Jan-Nov 2018

## Imports from Georgia

- Imports from Georgia increased by 4.5% in Jan-Nov 2018

## Conclusions

- Positive development of bilateral trade between Germany and Georgia
- Germany's traditional high bilateral trade surplus remains

# Presidential election: new president has been elected



## Election

- November 28: Salome Zourabichvili elected as new president
- With about 60% of the votes she prevails in a run-off against Grigol Waschadze
- The election was preceded by a polarizing election campaign in which Zourabichvili received massive support from the ruling party

## Importance

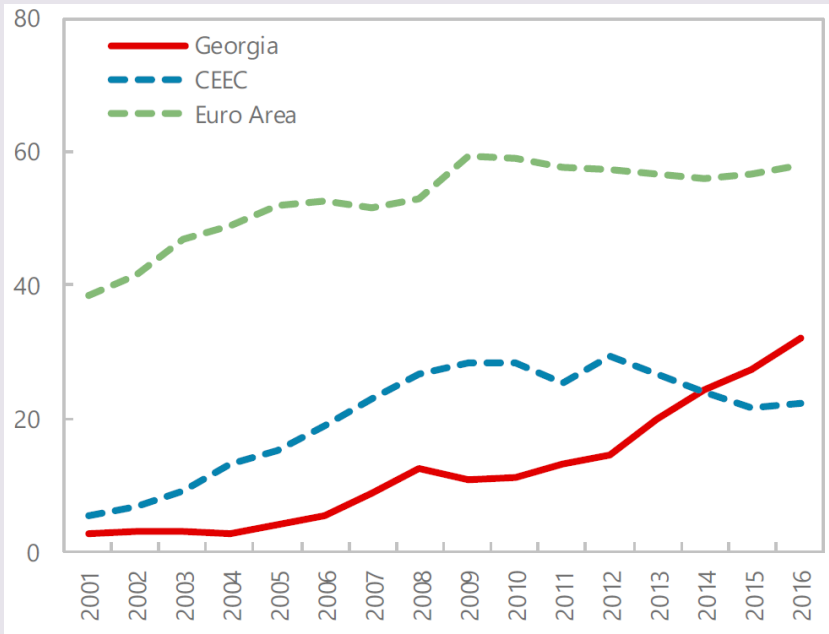
- Stands for a pro-European course
- Since the constitutional reform of 2017, the president mostly fulfills representative functions

## Conclusion

- Zourabichvili faces the challenge of reconciling society and regaining lost political trust

# Banking: measures to curb household debt

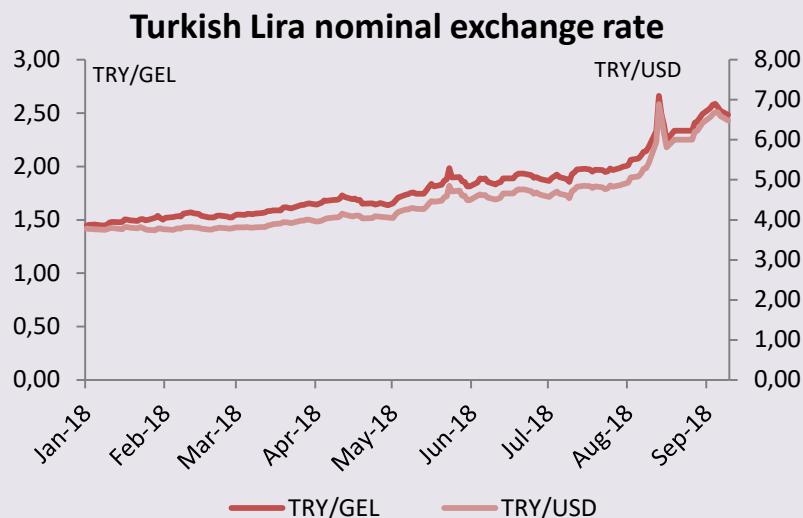
Household debt, % of GDP



Source: IMF Country Report June 2018

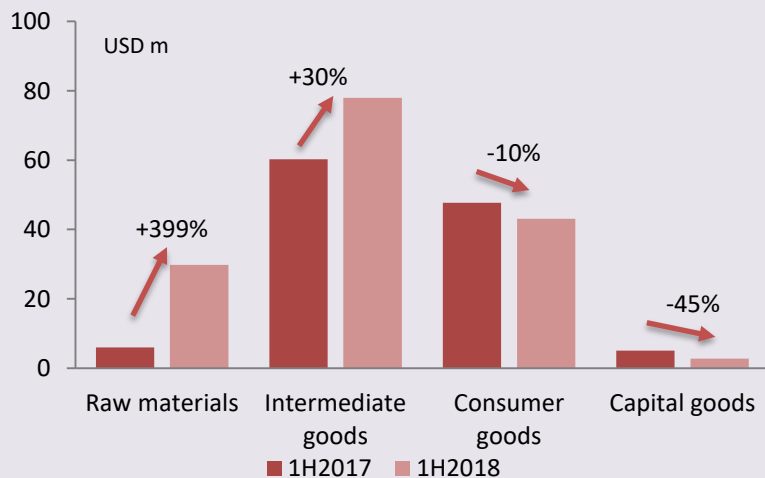
- Over-indebtedness of low-income households has become a growing problem; this was caused by weak regulation of credit companies in the past
- Additionally, total household debt increased significantly hovering slightly above the regional average; however, no signs of overheating so far, e.g. in housing market
- From January 2019: extensive measures to curb credit growth have come into effect; documentation of private income creates severe problems for households outside the formal sector
- Recent announcement of debt restructuring for households could set wrong incentives and could make loans more expensive
- High equity ratio and profitability continues to be positive for banking sector

# Depreciation of Turkish Lira: so far only moderate effect



Source: Central Bank of the Republic of Turkey

## Georgia's exports of goods to Turkey, 1H18 vs. 1H17



Source: UN ComTrade, WITS, authors' estimates

## Turkish Lira

- Depreciation by 42% against USD and GEL from Jan-Aug 2018
- However: trade flows depend on real, not nominal exchange rate
- Real depreciation Jan-Aug 2018: only ca. 20%; reduction of real depreciation recently

## Effect of Lira depreciation on Georgia

- Exports: consumer goods down, but raw materials and intermediary goods up; this shows the importance of global value chains
- Imports: growth in imports across all categories is in line with theory
- FDI, banking: little impact expected

## Conclusions

- So far only moderate effect
- However: this could change if further depreciation and/or recession in Turkey

# Pension reform: start on 1 January 2019

## Background

- July 2018: Parliament approved law on accumulative pension system which comes on top of the already existing flat-rate pension of 180 Lari per month
- From January 2019 each employee below age 40 contributes 2% of pre-tax salary; employer and government contribute each a further 2%
- Access to pension will be granted on retirement age (men: 60, women: 55)
- Participants have the option to invest in 3 different risk categories: low, medium and high

## Objective of reform

- Provide higher pension level which is more aligned to individual income
- Foster capital market development by investing funds in Georgia

## Challenges now

- Implementation of investment policy within the new pension fund
- Building capacity within the NBG in its new role as supervisor of this sector
- Engage employers and social partners to strengthen participation in the scheme, and limit opt-outs

# German Economic Team Georgia



The German Economic Team (GET Georgia) has been supporting the Georgian government in designing the necessary reform process since 2014.

In a dialogue with the Georgian Government, we identify existing economic problems and develop actionable policy recommendations to overcome them. Our advisory work is based on independent analysis and impartial recommendations.

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