NEWSLETTER

Issue No. 1 | November - December 2014

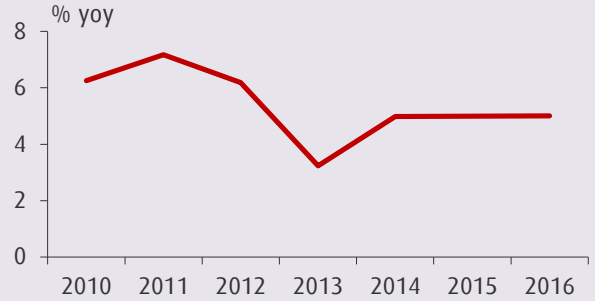
Great challenges in spite of stable macroeconomic situation

The economic situation of Georgia is stable. The gross domestic product is growing, public finances are in sound condition and inflation is low. However, two fundamental problems persist: The economy's export weakness leads to a significant current account deficit and the economic growth rate is too low considering the country's income level and excellent basic conditions for growth. Supporting the growth of export-oriented, highly productive economic sectors should be the main focus of economic policy in the coming years.

Stable growth, but at too low rates

Due to a policy of economic reform, Georgia's economy has grown constantly in the past decade. In the first few years after the "Rose Revolution" of 2003, annual real GDP growth rates of around 10% were attained. After a temporary lull in growth during the change of government in 2012/2013, annual growth rates around 5% are expected for the coming years.

Real GDP growth



Source: IMF, 2014: Estimate, 2015-2016: Forecast

Although a growth rate of 5% seems high at first, considering the good conditions for economic growth in the country, higher growth rates should be possible. In the "Doing Business" ranking by the World Bank for 2015, Georgia scores an impressive 15th position, just one position behind Germany.

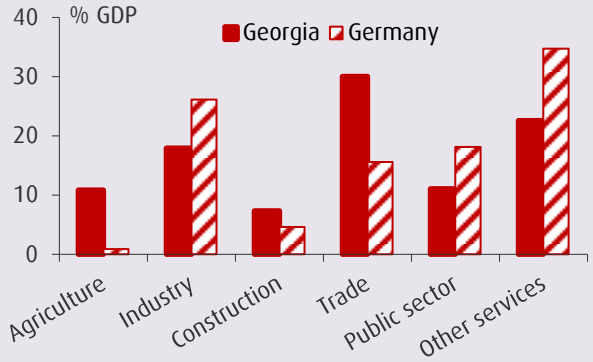
As GDP per capita is still at a very low level of USD 3,600 per annum and unemployment is high at 16%, the permanent strengthening of the growth rate will continue to be considered a central challenge for the government.

Structural change still to come

Consumption expenditures of the private sector have been the principal demand-side driver of economic growth in the past years, contributing 70-75% to GDP growth. Private and public investments contributed to a smaller extent, whereas the growth contribution of the external sector has been negative due to the current account deficit of -13 to -20% of GDP.

In a sectoral view, agriculture and trade – in which typically relatively low productivity and hence low wages are to be expected – make up a comparatively high share of GDP in comparison with high income countries. The share of trade, transport and tourism in GDP is circa twice as high in Georgia as it is in Germany, whereas the GDP shares of industry and business services are significantly lower.

GDP shares of economic sectors in Georgia and Germany, 2013



Source: Geostat

The growth contribution of the industrial sector has been substantial and relatively constant over the last years, whereas e.g. the agricultural sector did not significantly contribute to growth. Therefore, a larger shift in the relative sizes of economic sectors should be expected for the medium term.

Export weakness...

The relative weakness of Georgia in industry also contributes to significant trade and current account deficits.

Current account deficit

Source: National Bank of Georgia

In 2013, Georgia imported goods to a value of 58% of GDP, whereas exports made up only 45% of GDP. In spite of high remittances, this gave rise to a high

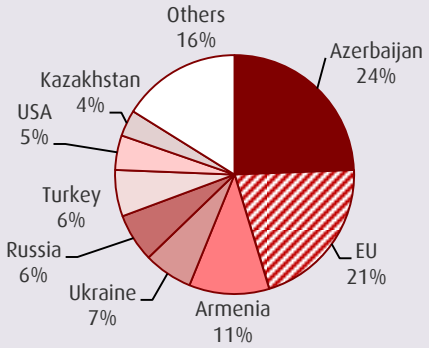
current account of 6% of GDP. In past years, even higher deficits of up to 20% had existed. As foreign direct investments only partly suffice to finance the current account deficit, the stock of Georgia's foreign debt now amounts to around 85% of GDP.

... but diversified structure of trade partners

The regional structure of the foreign trade of Georgia is remarkably diversified. In particular, due to the problematic relationship in past years, no significant dependency on Russia as a trade partners exists, which is a common feature of the trade structure of other countries in the region. Only in the foodstuffs sector (wine, spirits and water in particular), Russia has again become the destination of the majority of exports after the ban on Georgian food imports was lifted in 2013.

The EU, as destination of 21% of Georgian exports in 2013 is the second most import market for exports. The first place of Azerbaijan among the destination countries of Georgian exports (24% in 2013), is however mostly due to re-exports of used cars, with limited economic relevance.

Destinations of Georgian exports, 2013

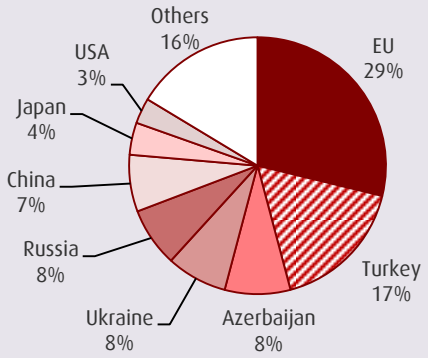


Source: Geostat

Among EU countries, Bulgaria, as destination of 5.2% of Georgian exports is the most important market, followed by Italy (2.8%) and Germany (2.5%). The role of the EU as a trade partner should continue to grow in the near future due to the implementation of the recently signed free trade agreement.

In the domain of imports, the EU, accounting for 29% of imports, is already the most important trade partner for Georgia. Among the EU countries, Germany, with 5.7% of imports, is the most important source country, followed by Romania (4.1%) and Italy (2.8%). Turkey is the most important single source country for imports with 17% of 2013 imports originating from Turkey.

Source countries of Georgian imports, 2013



Source: Geostat

Conclusion

After the change of government in 2012, doubts existed, whether Georgia would stay on the course of economic reform taken by the previous government. These doubts have been largely allayed by now. Social policy and distributive justice are priorities of the new government, but are embedded in a framework of market-oriented economic reform policy.

The macroeconomic situation of Georgia on a whole is stable, with the only significant vulnerability existing in the substantial current account deficit. Sound public finances and an independent monetary policy provide a good foundation for an economic policy focused on fostering growth. Within this policy, supporting the growth of highly productive, export-oriented industries should be prioritised in order to reduce the current account deficit and raise the standard of living.

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Note: This is a translation of the November – December issue of the German newsletter.

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GET Georgia advises the Georgian government on a wide range of economic policy issues since 2014. The project is financed by the German Federal Ministry of Economics and Energy under the TRANSFORM programme and its successor.

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