

Overview

- High economic growth of 5.0% in 2017 and 5.5% in Jan-Apr 2018
- Demand side: balanced growth based on consumption, investment and net exports
- Positive development in services and industry in 2017, but decline in agriculture
- Inflation decreases to 2.5% in May 2018; largely price stability
- Lari appreciation since late 2017, after depreciation in autumn 2017 caused by seasonal fluctuations
- Exports increased by 29% in 2017 and 28% in Jan-May 2018
- Reduction of budget deficit in 2017 to 2.9% thanks to higher revenues
- 27 June: IMF decided to disburse the third tranche of its programme amounting to USD 43.6 bn

Topics

- **Mining of cryptocurrencies.** Own estimation of contribution to GDP
- **Mid-term fiscal plan.** Higher public investment combined with a lower budget deficit
- **Banking sector.** Stability and concentration
- **De-dollarisation.** Partial success in 2017

Basic indicators

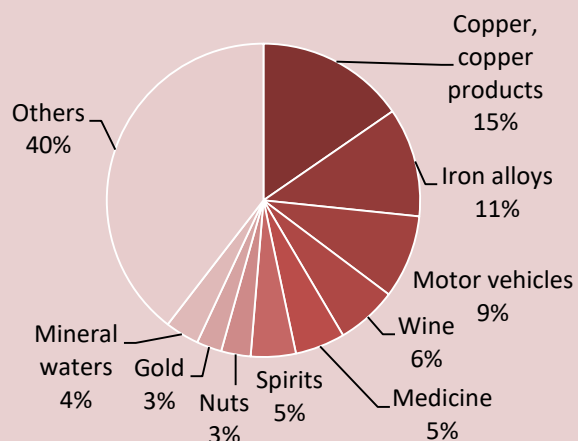
	Georgia	Moldova	Belarus	Ukraine	Russia
GDP, USD bn	16.1	9.2	59.2	119.1	1,719.9
GDP/capita, USD	4,370	2,596	6,300	2,821	11,947
Population, m	3.7	3.5	9.4	42.2	144.0

Source: IMF World Economic Outlook Apr 2018, forecast 2018

Trade structure

Export

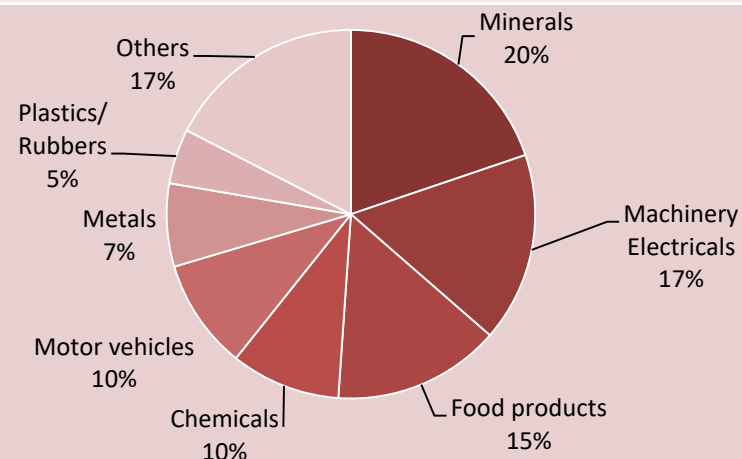
EU 24% | CIS 43% | Others 33%



Source: Geostat, 2017; Note: trade in goods

Import

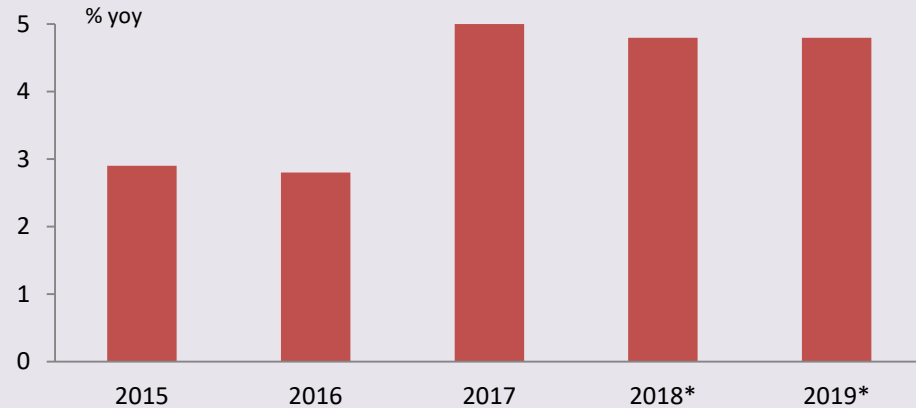
EU 28% | CIS 30% | Others 42%



Source: Geostat, 2017; Note: trade in goods

Economic growth

Real GDP growth



Source: IMF June 2018; *Forecast

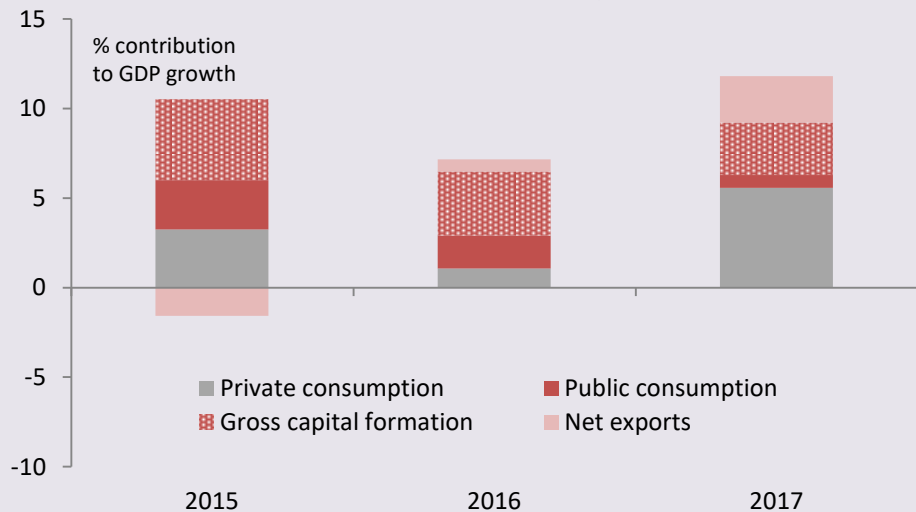
GDP 2017

- Economic growth: 5.0%
- Drivers:
 - Private consumption
 - Investment
 - Net exports
- Demand side: balanced growth

GDP 2018

- Jan-Apr yoy: 5.5%
- Forecast for 2018
 - IMF: 4.8%
 - Galt & Taggart Research: 5.4%

Contribution to economic growth (nominal)



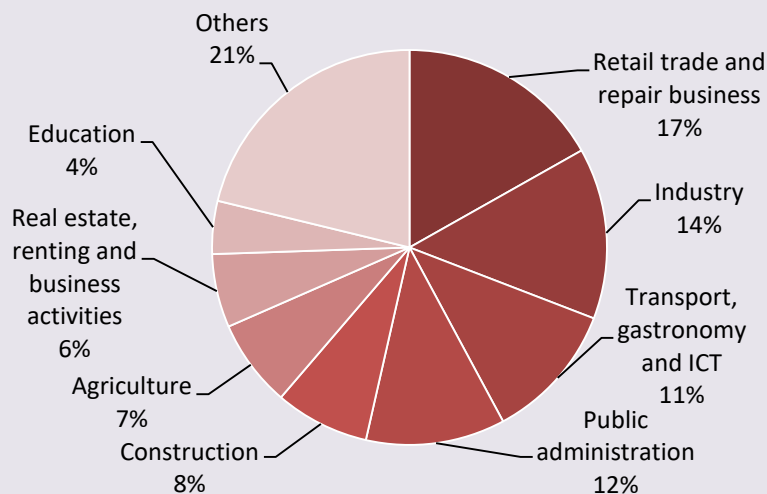
Source: Geostat

Conclusion

- High economic growth
- Growth broad based

Sectoral perspective

Composition of GDP



Source: GeoStat, 2017

Agriculture

- Decrease by 2.7% in 2017
- Disappointing development reveals structural problems

Industry

- Positive development: 4.5% in 2017
- As in 2016 important contribution to GDP

Services

- Increase by 6.0% in 2017
- Tourism and construction have increased by ca. 11%, respectively

Sectoral dynamic



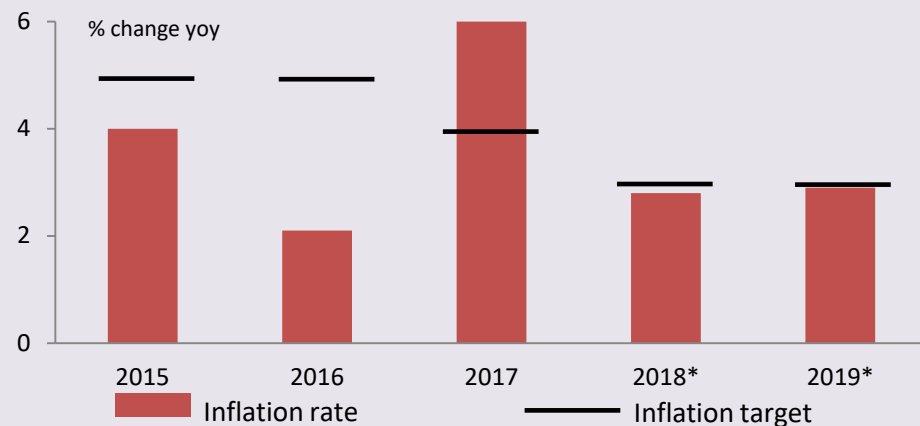
Source: Geostat

Conclusion

- Services still most important driver of economic growth
- Also positive development of industry
- Agriculture remains problematic

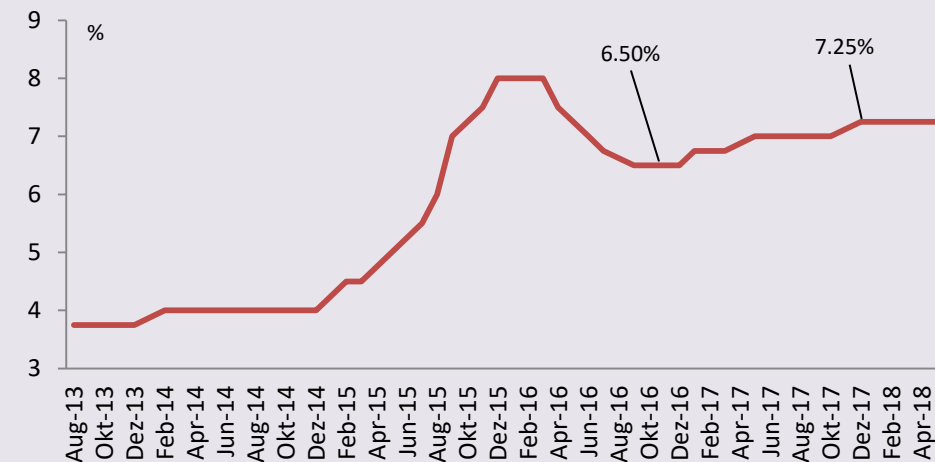
Inflation and monetary policy

Inflation rate and inflation target



Source: IMF Country Report June 2018, *forecast; Note: Annual average (consumer prices)

NBG policy rate



Source: National Bank of Georgia

2017

- Inflation: 6.0% yoy
- Thus: higher than target of 4.0%
- Reason: not monetary, but fiscal
- In detail: increase in excise taxes for mineral oil, cars, tobacco and gas in beginning of 2017

2018

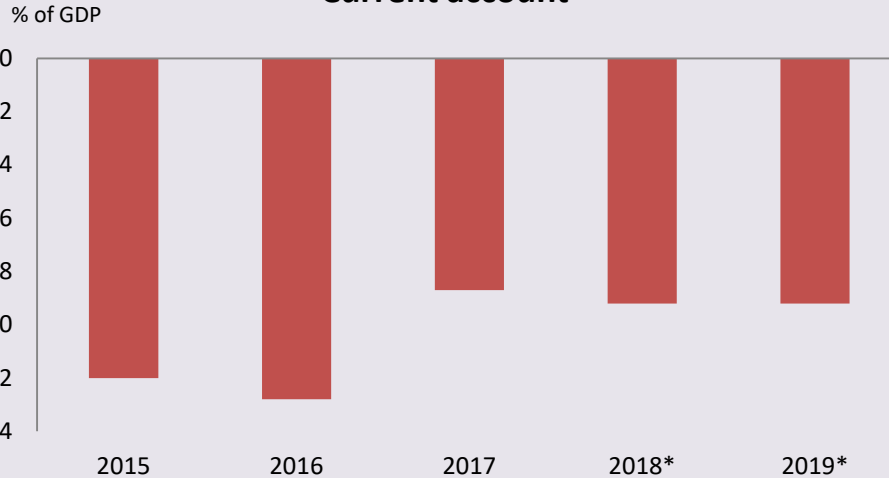
- Inflation May 2018: 2.5% yoy
- Reasons for decline in inflation
 - One-off fiscal effect ceases
 - Increase in policy rate in 2017
- Inflation target National Bank: 3.0%
- Forecast IMF: 2.8%

Conclusion

- Inflation at appropriate levels
- Stability orientated monetary policy of National Bank („inflation targeting“)

Current account and exchange rate

Current account



Source: IMF Country Report June 2018; *Forecast

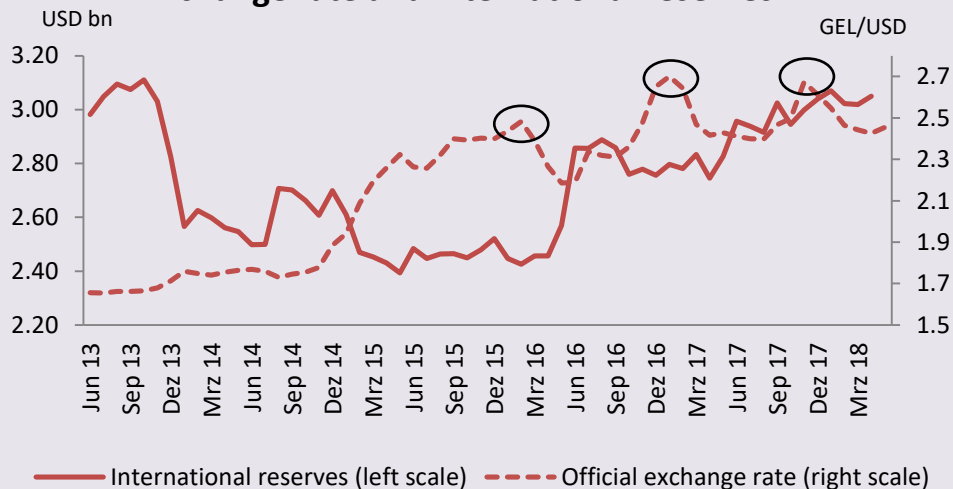
Current account deficit

- Decline of the deficit from 12.8% in 2016 to 8.7% of GDP in 2017
- Positive, but deficit still high

Exchange rate

- Aug 2017: 2.4 GEL/USD
- Nov 2017: 2.7 GEL/USD
- Jun 2018: 2.5 GEL/USD
- Typical fluctuation caused by seasonality of tourism and energy trade
- No reason for NBG intervention

Exchange rate and international reserves



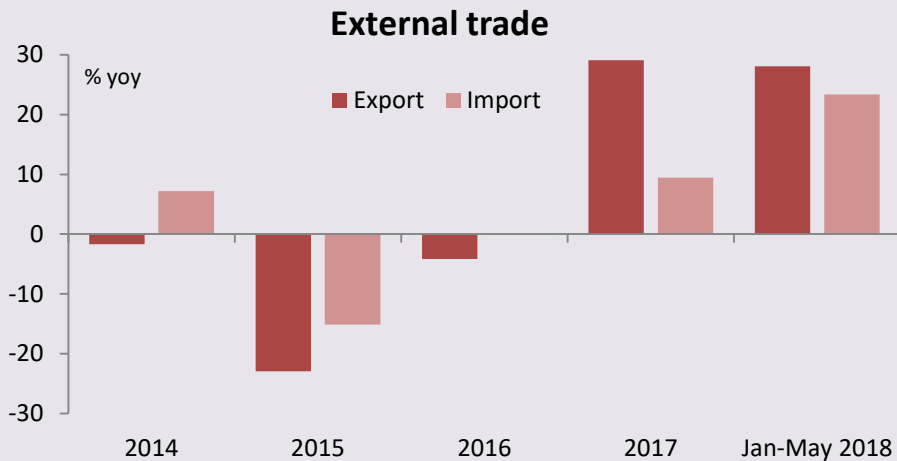
International reserves

- Apr 2018: increase to USD 3.0 bn; equivalent to ca 3.5 month of import coverage

Conclusion

- National Bank's flexible exchange rate policy important for external stability

External trade



Source: Geostat

Dynamic

- 2017: increase in exports by 29.1%, imports increase by 9.4%; positive
- Jan-May 2018: continuation of positive dynamic

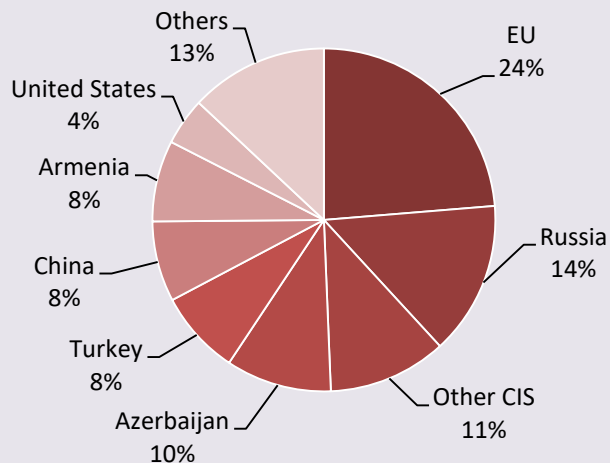
Export dynamic by countries Jan-May 2018

- AZE: +156.5%
- UKR: +92.7%
- ARM: +36.0%

- EU: +13.7%
- RUS: +13.2%

→ Exports spurred by regional recovery

Export by countries

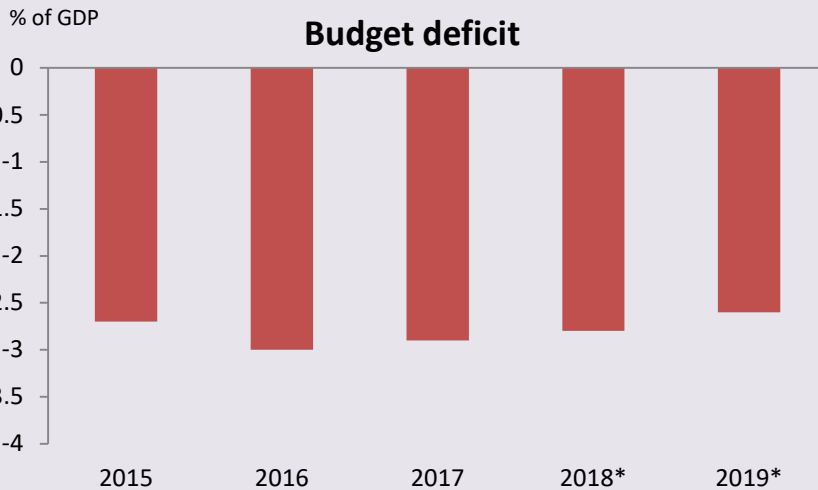


Source: Geostat, 2017; Note: trade in goods

Conclusion

- Regional recovery, especially in AZE, UKR and ARM, supports Georgian exports

Public finances and government debt



Source: IMF Country Report from June 2018; *Forecast; Note: GFSM 1998-Definition

Budget deficit 2017/2018

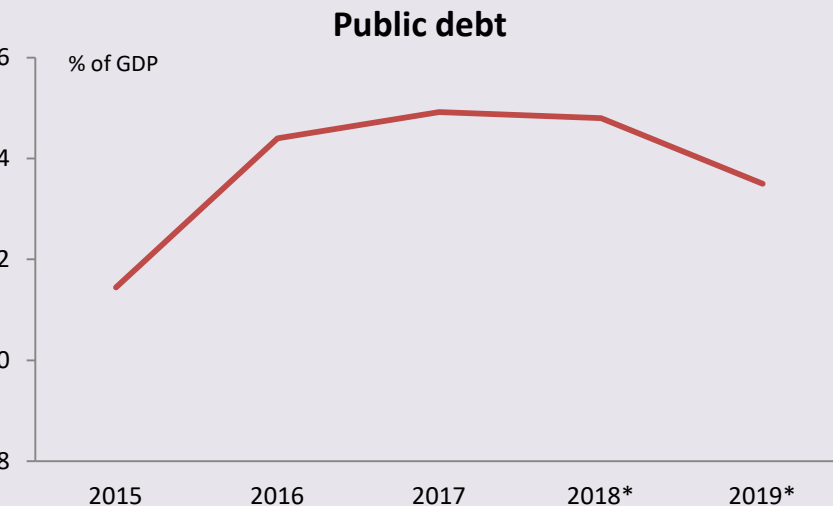
- 2017: deficit of 2.9% of GDP
- Less than planned (3.6%) and in line with IMF
- Main reason: higher revenues
 - Higher economic growth
 - Reform of corporate tax: Revenue shortfalls only 1.1% of GDP; 1.5% planned
- 2018: Deficit of 2.8% of GDP

Medium-term planning

- Reduction of deficit to 2.3% of GDP in 2022
- Simultaneously: higher public investments
- How possible? See slide 11

Conclusion

- Good fiscal position
- Important factor for smooth implementation of IMF programme
- 27 June: IMF Executive Board decided to disburse third tranche amounting to USD 43.6 bn



Source: IMF Country Report from June 2018; *Forecast

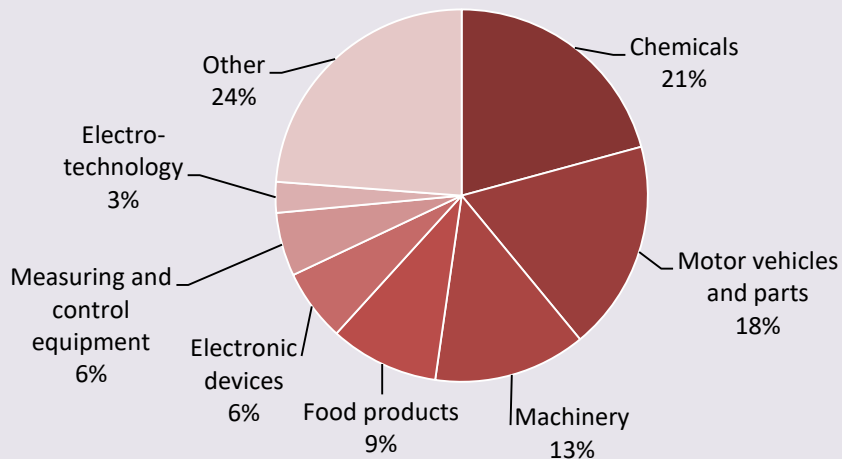
Bilateral trade between Germany and Georgia

German trade with Georgia



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

German exports to Georgia



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

Trade volume

- Trade volume between Georgia and Germany in 2017 amounted to EUR 423 m

Exports to Georgia

- 2017: increase by 5.2%
- Jan-Apr 2018: +12.1%

Imports from Georgia

- 2017: decrease by 19.2%
- Jan-Apr 2018: increase by 8.8%

Conclusion

- Good development of German exports
- Imports from GEO start to recover

Mining of cryptocurrencies

Georgia: one of the biggest miners of cryptocurrencies world-wide

Reasons: low electricity costs, good business climate and tax exemptions in free industrial zones

Economic relevance: unknown so far, barely covered by official statistics

GET Georgia: own estimation of contribution to GDP in 2017

Contribution of crypto-mining to GDP in 2017 (preliminary)

Electricity consumption	1,680,000 MWh
Electricity/BTC	23.01 MWh
Number of BTC	81,043 BTC
Revenue = quantity * price	USD 324 m
Costs of inputs	
Electricity	USD -84 m
Processors, hardware	USD -30 m
Other inputs	USD -40 m
Contribution to GDP	USD 170 m
% of GDP	1.1%

Comparable to: mining and quarrying (1.1%), manufacture of alcoholic beverages (1.2%), restaurants,.... (1.6%)

Mid-term fiscal plan

Mid-term planning

- Higher public investments combined with a lower budget deficit

Possible?

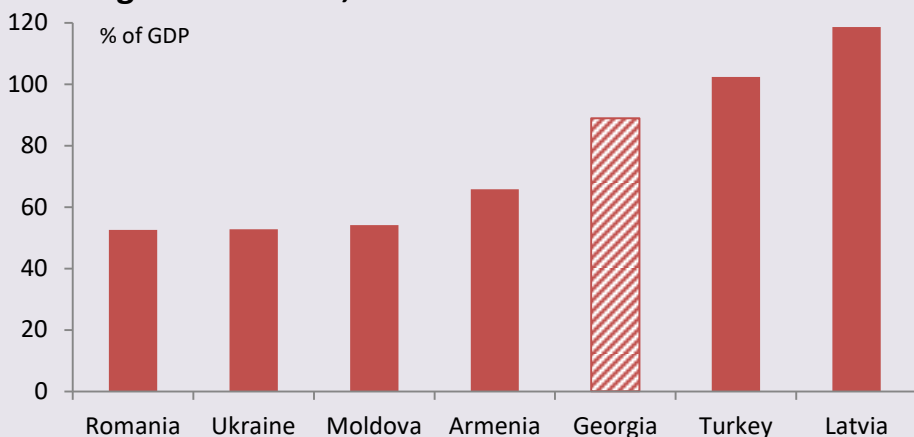
- Yes, because consumptive expenditure (as % of GDP) shall be markedly reduced
- From 25.9% in 2016 to 20.8% of GDP in 2022
- Areas: public wages and administration, efficacy of health sector, framework for public-private-partnership
- Realistic? Yes, as long as high economic growth continues

% of GDP	2016	2017*	2018**	2019**	2020**	2021**	2022**
Revenues	28.3	29.0	27.9	27.3	27.2	27.2	27.1
Expenditures	29.9	29.6	29.5	29.6	29.5	28.8	28.5
Current expenditures	25.9	24.2	23.1	22.5	21.7	20.8	20.8
Capital expenditures	4.0	5.4	6.4	7.1	7.8	7.9	7.8
Net lending/ borrowing (before adjustment)	-1.6	-0.5	-1.6	-2.3	-2.3	-1.5	-1.4
Unidentified measures	0.0	0.0	0.0	0.8	0.8	0.0	0.0
Net lending/ borrowing (after adjustment)	-1.6	-0.5	-1.6	-1.5	-1.5	-1.5	-1.4
Budget lending	1.4	2.4	1.2	1.1	1.0	0.9	0.9
Deficit***	-3.0	-2.9	-2.8	-2.6	-2.5	-2.4	-2.3

Source: IMF report June 2018 (second programme review); *preliminary data; **projection; ***Augmented net lending / borrowing

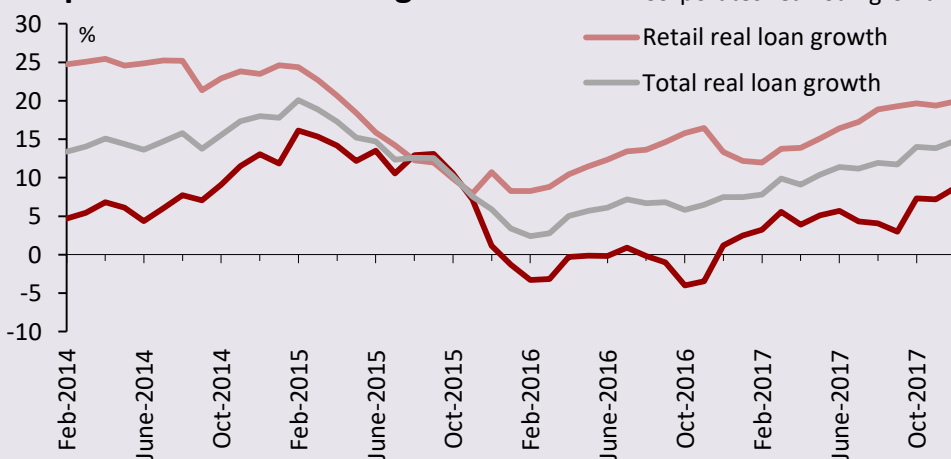
Banking sector: stability and high concentration

Banking sector assets, 2016



Source: National Banks, eop, data for 2016

Corporates vs retail loan growth

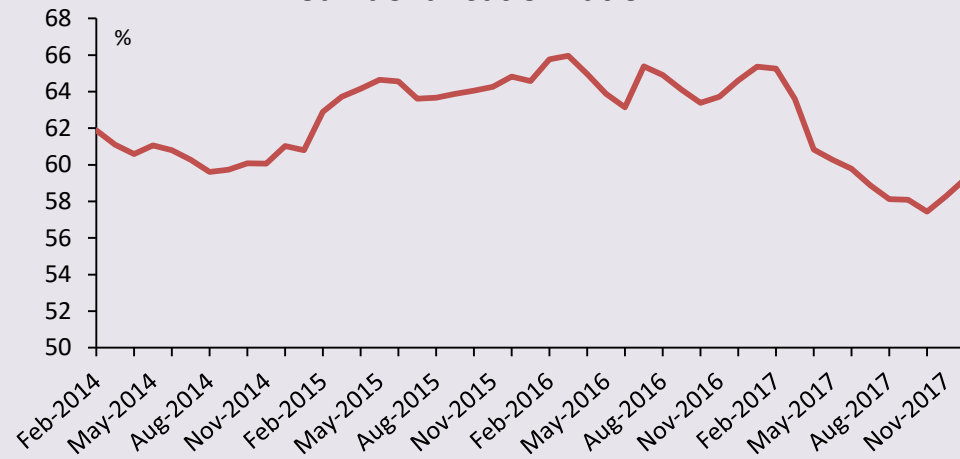


Source: NBG, own calculations

- Banking sector is well developed in regional comparison and loan access for households and SMEs is good
- Equity ratio with 16% continues to be very high
- Risks lie in dollarisation and resulting from it in open currency positions
- However, non-performing loans (NPLs) are low
- Concentration in the banking sector remains high, with 77% of assets in 3 banks. High profitability remains controversial
- Two biggest banks have good governance standards due to London listing and there is almost no state interference in the financial system
- The systemic relevance (“too-big-to-fail”) of the two banks produces disincentives and requires a resolutions framework

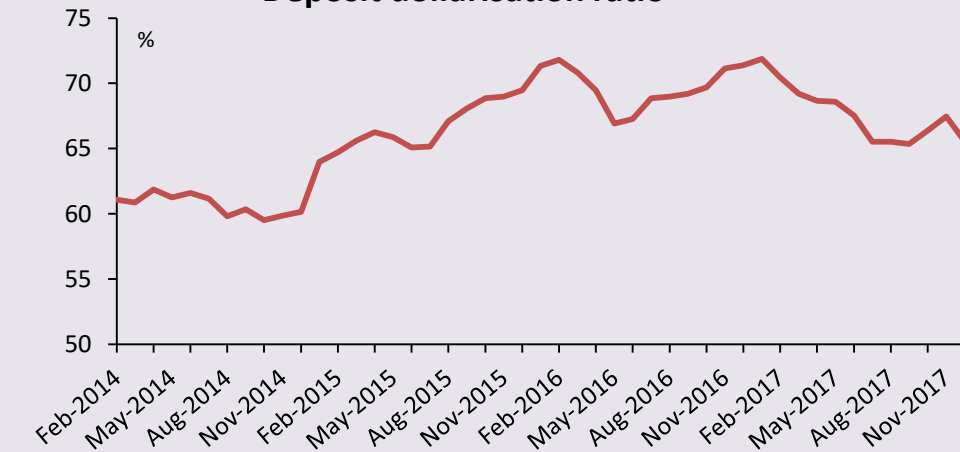
De-dollarisation: partial success in 2017

Loan dollarisation ratio



Source: NBG; excl. interbank deposits

Deposit dollarisation ratio



Source: NBG; excl. interbank deposits

- Significant decline in loan dollarisation in 2017, likely helped by prohibition of loans in foreign currency under GEL 100,000
- Also reduction in deposit dollarisation
- However: deposit dollarisation cannot be addressed by administrative measures alone
- Additionally: foreign currency still widely regarded as a sounder store of value

→ **Some progress in fighting dollarisation in 2017**

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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