Economic growth was robust at 18 percent yoy in January, and broad-based. The COVID-19 outbreak began abating in late February.

- Inflation remained elevated at 13.7 percent yoy in January and further inflationary pressure is likely.
- External trade deficit widened in January by 33 percent yoy.
- Proceeds from tourism and remittances improved in January but may decline going forward as the war in Ukraine affects these inflows.
- The lari depreciated strongly in early March as the war in Ukraine affected expectations but has since recovered some of the losses.
- Credit and deposits remained stable in February and the banking sector is resilient.
- Revenue collections performed strongly in January, mirroring high economic growth.
- The economy will be adversely impacted by the Russian-Ukraine conflict, including through trade, remittances, commodity prices and currency developments.

Economic growth picked up to 18 percent yoy in January 2022 from 9.6 percent yoy in December 2021. Growth was broad-based, with robust growth in manufacturing, transport, energy, trade and tourism-related sectors while the construction and communication sectors contracted. On the demand side, private consumption and net export of services contributed positively to growth, while net export of goods, public consumption and investment are likely to have acted as a drag on growth. The fifth wave of the COVID-19 pandemic abated in late February, with new cases falling to 6 percent of peak levels on March 10th.

Inflation remained elevated at 13.7 percent yoy in February 2022. This reflected higher commodity prices as well as pass-through from earlier depreciation. Food and fuel prices contributed over 8 percentage points (ppt) to this increase.

Trade turnover increased and the trade deficit widened in January 2022. Exports grew by 48 percent yoy with sharp increases in nitrogen fertilizers (tripling yoy), wine exports (79 percent yoy increase) and mineral waters (31 percent yoy increase). Imports also grew sharply (39 percent yoy) driven by fuel imports (98 percent yoy increase) largely from Azerbaijan. Due to a higher base, imports outpaced exports and the trade deficit widened by 33 percent yoy in January. Inflows from remittances (12.7 percent yoy increase) and proceeds from tourism (10-fold increase) remained strong in January. The trade trends continued in February, with exports growing strongly by 60 percent yoy and imports by 53 percent yoy, with the trade deficit widening by 48 percent yoy.

Banking sector profitability indicators remained healthy. Return on assets (ROA) of the banking sector and return on equity (ROE) improved in January to 4.2 percent and 32.6 percent respectively. Non-performing loans remained low at 2.3 percent. Credit growth in the banking remained robust in February at 15 percent yoy (excluding FX effect). Deposits grew by 8 percent as of end-February with deposits in lari increasing by 9.9 percent.

The fiscal balance was positive in January supported by strong tax collection. General government revenues increased by 25 percent yoy in January, driven by a 36 percent yoy increase in tax collection. Spending also increased, with current spending increasing by 9 percent yoy and public investments up by 28 percent yoy. The surplus was around 0.2 percent of GDP in January.

Looking ahead, the conflict in Ukraine has created uncertainty on the outlook and is likely to impact the Georgian economy through several channels. The first channel of impact is through trade. Both Russia and Ukraine are among Georgia’s top trading partners and key destination for exports, including wine and beverages. In the short term, there is limited potential to divert some of the affected exports to alternative markets. In addition, Georgia is reliant on Ukraine and Russia on key imports, such as cereals. The second key channel is tourism. Russian and Ukrainian tourists accounted for 21 percent of visitors in 2021 and their number is likely to decline, although temporary relocation of people could result in increased arrivals. The third channel is through remittances, with Russia and Ukraine accounting for 21.5 percent of total remittances, which are at risk of declining sharply on account of economic contraction in the host countries, depreciation of the Ruble and potential challenges in executing transfers. The final channel is through elevated commodity prices, which have increased sharply since the beginning of the war due to uncertainty and commodity supplies from Russia and Ukraine are disrupted.

These impacts are likely to be felt in slowing growth, higher inflation, and widening external imbalance. Economic growth may slow to low single digits as compared to an initially expected recovery to over 5 percent in 2022. The current account deficit is expected to widen due to weaker exports and higher import prices. The lari has already depreciated by 16 percent mom as of March 8, 2022, though it regained some of the losses as the initial reaction subsided. Inflationary pressures are likely to increase due to higher commodity prices and potential regional supply disruptions. Having a long-term contract for its gas supply and a shared border with Russia may partially insulate Georgia from the spike in global prices, however, inflation is still likely to increase. On the other hand, recent developments provide an opportunity for Georgia to strengthen the transit potential of the Caucasus Transport Corridor.

Despite these pressures, Georgia enters the crisis with reasonable buffers and a credible macro-financial framework. The banking sector is entering the crisis in a relatively strong shape; however, high dollarization is a vulnerability. Fiscal discipline has been maintained over the last decade, although consolidation may be slower than planned in 2022 on account of the conflict related economic slowdown. Still, government deposits are sizeable, and debt is likely to remain below the 60 percent statutory level under the fiscal rule. Reserves remain adequate, at USD 4.0 billion as of end-February, providing 4.6 months of import cover.

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Figure 1. The economy grew strongly in January (year-on-year, in %)

Source: Geostat

Figure 2. Inflation remained elevated in January (year-on-year, in %)

Source: Geostat

Figure 3: The trade gap widened in January (year-on-year, in %)

Source: Geostat

Figure 4. Credit and deposit growth remained robust (year-on-year, in %)

Source: NBG

Figure 5: The lari depreciated since late February (GEL/US$)

Source: NBG

Figure 6: Fiscal balance turned positive in January (GEL m)

Source: MOF

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