Strong economic recovery continued in June as COVID-19 related restrictions eased. Rising COVID-19 infections in July and August pose a significant downside risk to the recovery even as the pace of vaccination improves. Inflation increased further to 11.9 percent yoy in July, driven by food and fuel prices, prompting a 50bps increase in the policy rate. Lari remained stable in July through mid-August. Trade deficit widened in July as import growth outweighed strong export performance. Credit growth remained strong in July, while deposit growth decelerated slightly. The fiscal deficit widened in June, as increased expenditures offset strong tax collections.

The economy grew at a robust pace of 18.7 percent year on year (yoy) in June, as per GEOSTAT's rapid estimates of economic growth. This continued the strong performance in April and May and cumulatively, growth in the first half of the year was estimated at 12.7 percent yoy. Further, economic output was 9.5 percent higher than the output in the corresponding pre-pandemic period in 2019, which may reflect the strength of the recovery. Growth was broad-based, with manufacturing, financial sector, trade, construction, real estate and restaurant sales all showing robust growth. Only the mining sector showed declining output, driven by a decline in the extraction of non-ferrous metal ores. Nearly 4,900 new enterprises were registered in the country in June, which is 13 percent higher than in the same period last year. The broad-based growth was supported by a further easing in COVID-19 restrictions in June, a pick-up in mobility and easing of restrictions on border crossings contributing to a pick-up in tourist arrivals. The number of arrivals for tourism purposes almost quadrupled in June yoy and increased five-fold in July. However, the number of international tourists remained 80 and 74 percent below pre-COVID19 levels respectively in June and July.

However, the rate of COVID-19 infections worsened in July and August, posing a significant risk to the recovery. The easing of restrictions and increased mobility have coincided with a significant increase in COVID-19 infections in July and August. The average number of daily infections exceeded 5,000 in mid-August as compared to 1,500 in end-June, and the test positivity rate exceeded 8 percent in mid-August (7-day average as of August 11) as compared to less than 5 percent in end-June. Meanwhile, vaccination efforts have recently picked up, albeit from a low base, and as of August 11, up to 19 percent of the population had received one shot of the vaccine and 5.7 percent were fully immunized.

Inflation increased further to 11.9 percent yoy in July, the highest rate in over a decade. While all commodity groups experienced price increases, food products, transport and utilities contributed the most (8.7 ppt) to the overall price increase. The key driver was a sharp increase in prices of food and oil in global commodity markets, which led to 18.4 percent yoy increase in price of imported products. The price of domestic products increased by 7.2 percent yoy, with the pass-through from earlier depreciation of the lari a key contributing factor. Core inflation, excluding food, alcohol, transport and administrative prices, also went up by 0.5 ppt to 6.4 percent in July. In response to price developments, on August 4, the National Bank of Georgia (NBG) tightened monetary policy and increased the policy rate by 50 bps to 10 percent.

The trade deficit widened by 2.6 percent yoy in July, as import growth slightly outweighed strong export performance. Preliminary statistics reported that trade turnover increased by 24.5 percent yoy in July, as exports increased by 42.2 percent yoy and imports by 17.7 percent yoy. Trends from January-June suggest that export growth was driven by ferroalloys, vehicles, as well as exports of wine and mineral waters, while import growth was driven by oil products and cars.

Lari was stable in July through to mid-August. A partial pick-up in tourism proceeds, healthy remittances and the stabilization of the political environment helped offset the impact of the widening trade deficit, to keep the Lari stable in July through to mid-August. The nominal effective exchange rate appreciated by 1.6 percent in July on month on month (mom) basis and by 0.8 percent yoy. Reserves declined slightly in July and early August, due to swap operations with commercial banks, but the level remained robust. At USD 3.7 billion as of mid-August, reserves provided a comfortable 5 months of goods import cover.

Credit growth remained robust in July, while deposit growth decelerated slightly. Credit growth (excl. FX effect) remained robust at 12.4 percent yoy in July as compared to 13 percent yoy in June. Lari loans grew strongly by 26 percent yoy in July, and, as a result, dollarization declined by 0.6 ppt to 51.9 percent in July. Deposit growth decelerated slightly to 14 percent yoy in July as compared to 18 percent yoy in June. The banking sector remained profitable, outperforming 2019 levels in the first six months of 2021. The share of non-performing loans (more than 90 days overdue) remained low at 2.3 percent in June.

Government revenues and spending both increased in June. General government tax collections increased by 26 percent yoy, driven by VAT collections, which increased sharply by 36 percent yoy, reflecting the pick-up in economic activity. Government spending increased by 26.5 percent yoy, counteracting the revenue increase and pushing the deficit up marginally by 0.7 ppt in June.
Figure 1. Economic recovery continued in June (year-on-year, in %)

Figure 2. Inflation spiked to record levels in July (year-on-year, in %)

Figure 3. The trade deficit widened in July, as both imports and exports grew fast (year-on-year, in %)

Figure 4. Credit growth remained robust, while deposit growth decelerated slightly in July (year-on-year, in %)

Figure 5: The lari remained stable (GEL/US$)

Figure 6: Fiscal deficit widened marginally in June (GEL m)

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