- *The economic recovery moderated in July but remains robust.*
- *COVID-19 infections rose sharply in July and August, posing a downside risk to the recovery.*
- *Inflation spiked further to 12.8 percent yoy in August, driven by food and fuel prices and earlier lari volatility.*
- *Lari remained stable in August through mid-September.*
- *Trade deficit widened in August, as import growth outweighed export performance.*
- *Credit growth remained strong in August, while deposit growth decelerated slightly.*
- *The fiscal deficit widened in July, as increased expenditures offset strong tax collections.*

The economy expanded by a robust 9.9 percent year on year (yoy) in July, as per GEOSTAT's rapid estimates of economic growth. This was slower than in May and June, and cumulatively, in the year-to-July, growth is estimated at 12.9 percent yoy. The construction and mining sectors were the only drag on growth, contracting on a yoy basis in July. Growth was particularly strong in financial sectors and manufacturing. Service sector growth was supported by pick-up in tourist arrivals for the summer tourist season (up by 500 percent yoy) with easing of entry restrictions and increase in flights. However, the number of international tourists remained 75 percent below pre-COVID 2019 levels in July and August. Nearly 4,270 new enterprises were registered in the country in July, which is 8.5 percent higher than in the same period last year.

COVID-19 infections picked up sharply until mid-August posing a risk to the recovery. COVID-19 infections peaked at around 6,000 daily infections in mid-August, prompting a reintroduction of selected restrictions in late August, including the suspension of public transport in cities and limiting the late working hours of restaurants. The average number of daily infections has since fallen to 2,500 by early September, with a marginal decline also in the test positivity rate, from over 10 percent in mid-August to 8 percent by mid-September. Meanwhile, vaccination efforts have picked up, and, as of mid-September, 32 percent of the population had received at least one shot of the vaccine and 22 percent were fully immunized.

Inflation increased further to 12.8 percent yoy in August, the highest rate in over a decade. Food products, transport and utilities contributed the most (9.5 ppt) to the overall price increase. In addition to pass-through from the earlier volatility of the lari, the key driver was a sharp increase in prices of food and oil in global commodity markets, which led to 16.5 percent yoy increase in the price of imported food products. The price of transportation increased by 22.5 percent yoy, reflecting higher fuel prices. Core inflation, excluding food, alcohol, transport and administrative prices, also went up by 0.3 ppt to 6.7 percent in August. Following the 50 basis points increase in the monetary policy rate in August, NBG kept the policy rate steady at 10 percent in September.

The trade deficit widened by 35 percent yoy in August, as import growth considerably outweighed export performance. Trade turnover increased by 23 percent yoy in August, as exports increased by 14.3 percent yoy and imports by 26.0 percent yoy. Cumulatively, in the year to August, the deficit widened by 17.2 percent yoy. Until July, export growth was driven by ferroalloys, vehicles, as well as exports of wine, fruits and mineral waters, mainly to China, Russia, Azerbaijan, Ukraine, Turkey and Armenia. The export of copper ores also made a significant contribution to export growth in July, supported by higher global prices. In the year to July, imports increase was driven by imports of oil products and of cars.

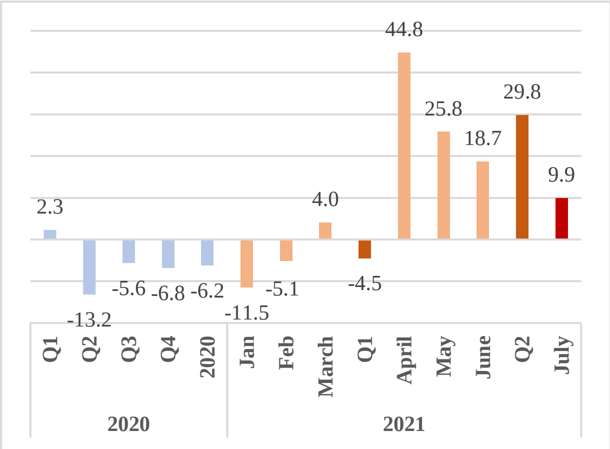
Foreign Direct Investments (FDI) fell in the first half of 2021 (H1 2021) when compared to earlier years. Georgia saw FDI inflows of 2 percent of GDP in H1 2021, as compared to 2.6 percent of GDP in H1 2020 and 3.2 percent in H1 2019. Reinvestment accounted for close to three-quarters of the inflows. On a sectoral basis, the financial sector accounted for half of the inflows while the energy sector attracted 29 percent. UK was the main country of origin contributing 45 percent of FDI.

Lari was stable in August through to mid-September. 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 and kept the lari stable in August through mid-September. Reserves were boosted by the receipt of reserve assets from the IMF as part of Special Drawing Rights (SDR) allocation, offsetting a decline on account of swap operations with commercial banks. At USD4.1 billion, as of end-August, reserves provided a comfortable 5.5 months of goods import cover.

Credit growth remained robust in August, while deposit growth decelerated slightly. Credit growth (excl. FX effect) accelerated to 14.2 percent yoy in August, as compared to 12.8 percent yoy in July. Lari loans grew strongly by 27 percent yoy, prompting a reduction in dollarization rate. Deposit growth slightly decelerated to 13.6 percent as compared to 14 percent yoy in July. The banking sector remained profitable in July. The share of non-performing loans (more than 90 days overdue) remained low at 2.4 percent in July.

The fiscal deficit widened in July. Total revenues increased by 15 percent yoy, as increased economic activity translated to higher tax collections, but were offset by a 16 percent yoy increase in spending, pushing the deficit up by 1 ppt in July. By end-July, the fiscal deficit reached 4 percent of GDP, as compared to the annual target of 7.6 percent of GDP.

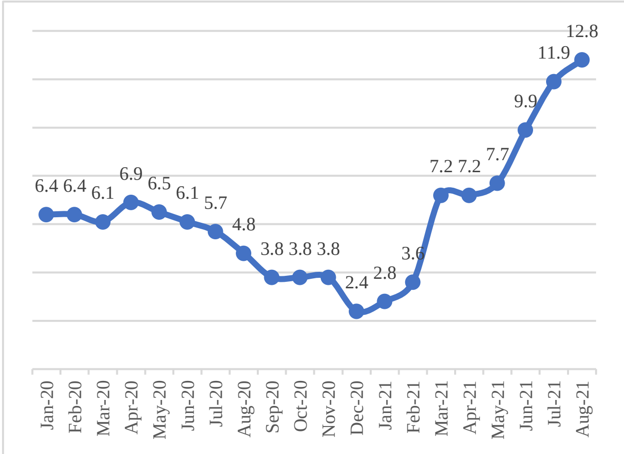
Figure 1. The pace of economic recovery moderated, but remains robust
(year-on-year, in %)



Source: Geostat

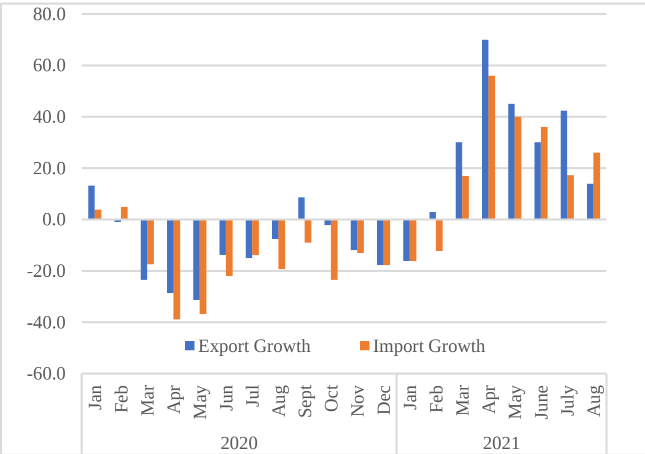
Figure 2. Inflation spiked to record levels in August

(year-on-year, in %)



Source: Geostat

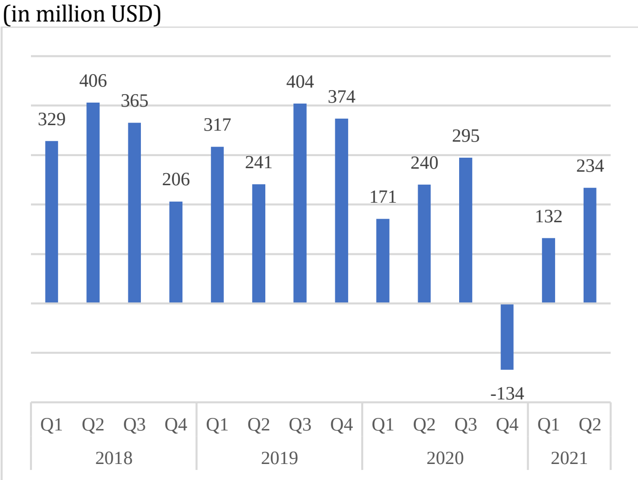
Figure 3: The trade deficit widened in July, as both imports and exports grew fast
(year-on-year, in %)



Source: Geostat

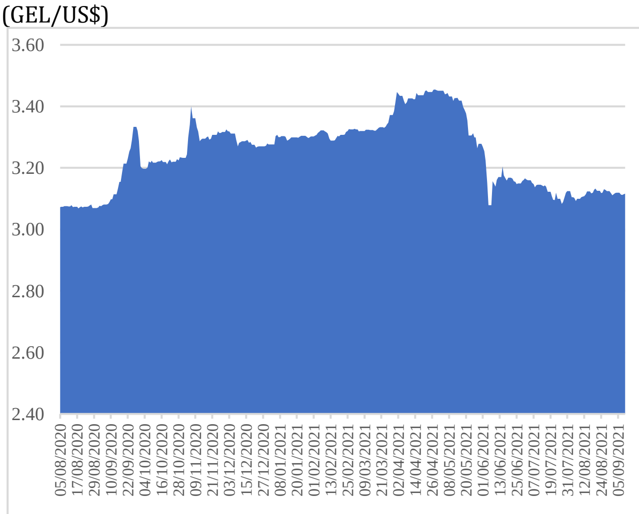
Figure 4. FDI inflows dropped in H1, 2021

(in million USD)



Source: Geostat

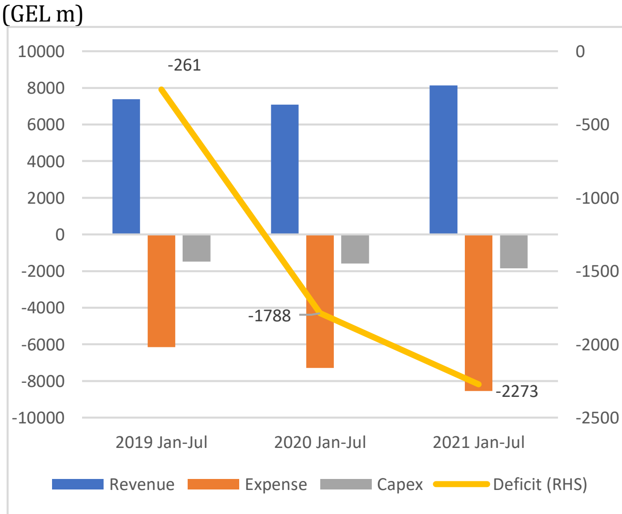
Figure 5: The lari remained stable in August through early-September
(GEL/US$)



Source: NBG

Figure 6: Fiscal deficit widened in July

(GEL m)



Source: MOF