- *A gradual recovery is ongoing as COVID-19 related restrictions were gradually removed.*
- *Inflation rose sharply to 7.2 percent yoy in March prompting a 50bps hike in the main policy rate.*
- *Lari depreciated sharply in March.*
- *Trade deficit narrowed by 19 percent yoy in February reflecting robust exports and slowly recovering imports.*
- *Credit growth continues to slow, while soundness indicators remain robust.*
- *Despite robust revenues, the fiscal deficit widened considerably in the first two months of 2021 as spending increased sharply.*

The pace of contraction is easing as COVID-19 related restrictions are gradually phased out. The economy contracted by 5.1 percent yoy in February as compared to 11.5 percent yoy in January. Construction, hotels and restaurant, transport and cultural activities declined the most, while financial sector, trade, water supply and waste management grew in February. High-frequency data point to further recovery more recently as restrictions (except curfew) were gradually removed since late February. Mobility in Tbilisi went up from an average of 51 percent of pre-COVID levels in February to an average of 67 percent of pre-COVID in March. Electricity consumption and flight availability also increased. Growth is projected to recover to 4 percent in 2021[1], contingent on control of COVID-19 infections, stronger pace of vaccination, and pick up in global and regional economic activity.

With the easing of restrictions, the number of infections increased. While test positivity rates remain low, Georgia registered more than 600 infections per day in early April, compared to around 300 a month earlier. Meanwhile, COVID-19 vaccination has had a slow start with only 14,200 persons vaccinated as of April 7.

Inflation spiked to 7.2 percent yoy in March, the highest rate in over five years. An increase in global food and oil prices, pass-through from depreciation of the lari and the expiration of the temporary state utility subsidy period in February, were the key drivers of the inflation spike. Food prices increased by 5.7 percent yoy and contributed 1.9 percentage points (pp) to the overall inflation rate. Transport prices continued to increase in March as global oil prices rose. Core inflation, excluding food, alcohol, transport and administrative prices, increased considerably to 6.9 percent yoy in March. The National Bank of Georgia (NBG) increased the policy rate by 50 bps to 8.5 percent in March, driven by concerns of inflationary pressures.

The lari depreciated by 3.6 percent month on month (mom) against the USD in March and continued to weaken in April. Recovering demand and depreciation of the Turkish lira against the USD in March may have been a contributing factor. The National Bank of Georgia (NBG) sold USD67.5 million in March and April 1, to smooth the exchange rate adjustment. Reserves, supported by the disbursements of the EU grants, increased since the beginning of the year and at USD4.1 billion as of end-March provided 5.5 months of goods and services import cover.

The goods trade deficit narrowed by 21 percent yoy in February, as exports recovered, and imports remained weak. Exports grew by 2.9 percent yoy in February, with exports of domestic products (excluding re-exports) growing by 23 percent yoy driven by strong export of copper ores, ferroalloys and nuts. The recovery of imports has been more gradual with imports down 12.2 percent yoy, compared to 16 percent yoy decline in the previous two months. Remittances from abroad were up by 17.5 percent yoy in the first two months of 2021, which could also reflect increased formalization of transfers. Tourism revenues remained depressed.

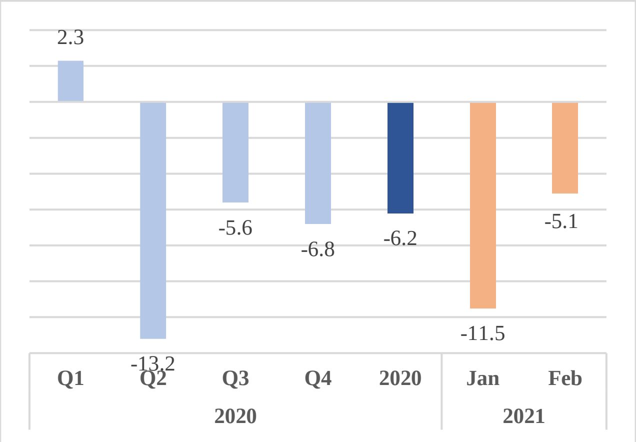
The current account deficit widened significantly to 12.2 percent of GDP in 2020 from 5.5 percent of GDP in 2019. This was driven by lost income from inbound tourism, partially offset by lower tourism related outflows and weak imports. The deficit was financed largely by official borrowing while net FDI covered less than third of the deficit (3.7 percent of GDP). Higher official borrowing contributed pushed the external debt to 127 percent of GDP in 2020 (including intercompany loans) as compared to 106 percent of GDP in 2019.

Credit growth moderated to 8.9 percent yoy (excl. FX effect) in March. Lari loans grew by 21 percent yoy, while FX lending growth eased to 1.7 percent yoy in March, helping to lower the credit dollarization rate marginally. Deposits grew by 21 percent yoy in March, similar to the February rate, with deposits in lari increasing by 37 percent yoy. Banking sector profits increased by 25 percent yoy in nominal terms in January and February, with 11 banks out of 15 showing positive returns. The share of non-performing loans fell slightly to 2.6 percent; however, increasing confiscated assets could signal concerns.

The fiscal deficit widened to almost 1 percent of GDP in the first two months of 2021. Social spending increased by 21 percent yoy and total current spending by 15 percent yoy in the first two months of 2021. Tax collections recovered to the last year's level in nominal terms. Higher inflows of external grants, mainly from EU, further supported revenues. As a result, revenue collection increased by 10 percent yoy. Public debt increased to 61.7 percent of GDP as of end-February.

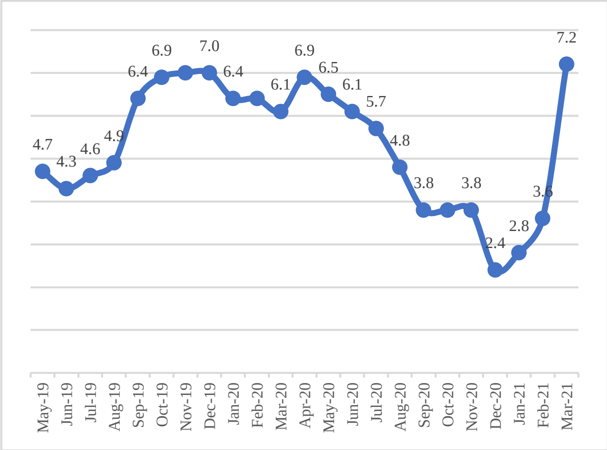
[1] See latest World Bank projections at: https://openknowledge.worldbank.org/bitstream/handle/10986/35273/9781464816987.pdf?sequence=4&isAllowed=y

Figure 1. The pace of contraction eased in February
(year-on-year, in %)



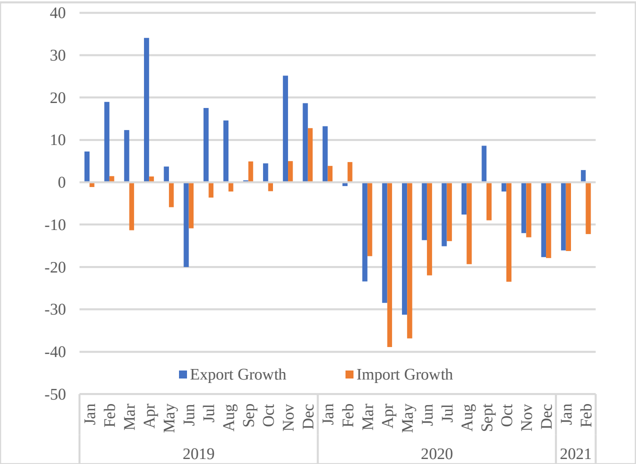
Source: Geostat

Figure 2. Inflation increased sharply in March
(year-on-year, in %)



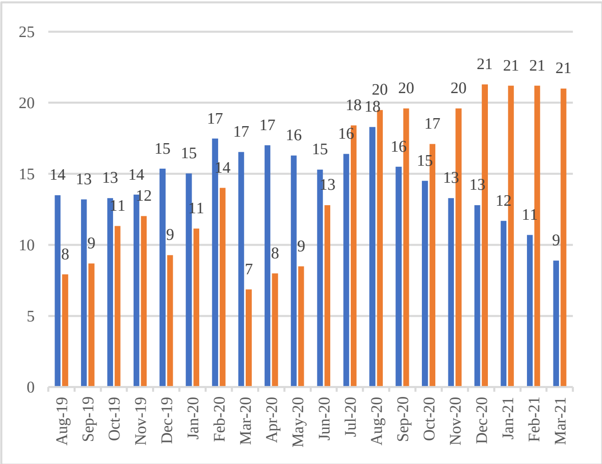
Source: Geostat

Figure 3: The trade balance continued to improve, with recovering exports and weak imports
(year-on-year, in %)



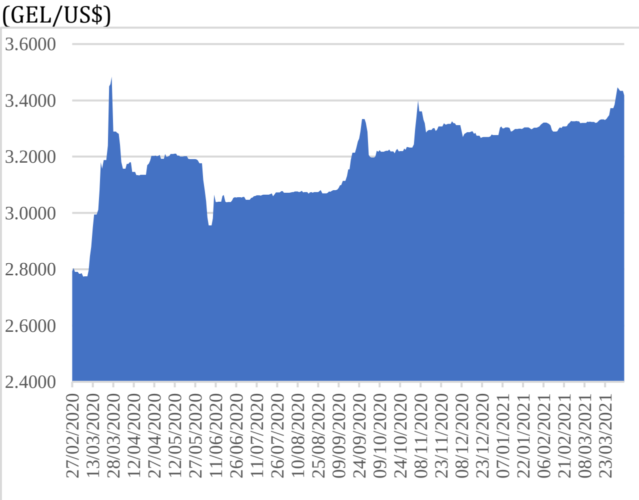
Source: Geostat

Figure 4. Credit growth moderated, while deposit growth remained strong
(year-on-year, in %)



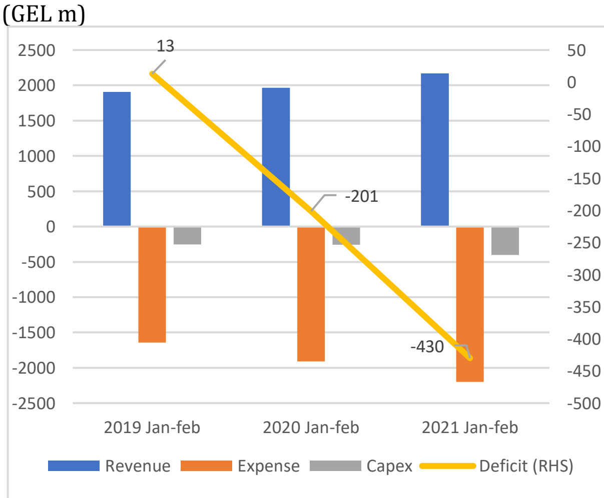
Source: NBG

Figure 5: The lari depreciated in March against the USD
(GEL/US$)



Source: NBG

Figure 6: Fiscal deficit widened further in early 2021
(GEL m)



Source: MOF