

MINISTRY OF FINANCE OF GEORGIA



CURRENT ECONOMIC OUTLOOK

10/31/2019

The Department of Macroeconomic Analysis and Fiscal Policy Planning prepares the outlook.

Analytical information presented in the outlook does not represent official statistics.

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FitchRatings has improved Georgia's sovereign credit ranking from "BB-" to "BB" with stable outlook in February, while S&P has improved perspective to „BB" stable from „BB-" positive in October (p. 37);

The current account deficit has improved to 3,2 percent in 2019 Q2. First time in the history, there was a positive current account balance in the third quarter of 2018 (p.11);

Real growth of the Gross Domestic Product is 4.5 percent in 2019 Q2 (p.4);

Unemployment rate has decreased by 1.2 points and reached 12.7 percent (p.11);

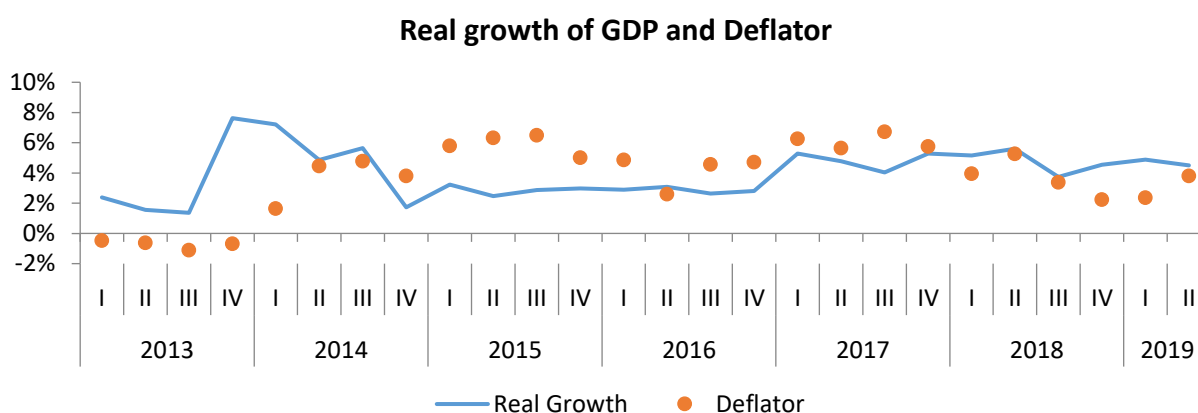
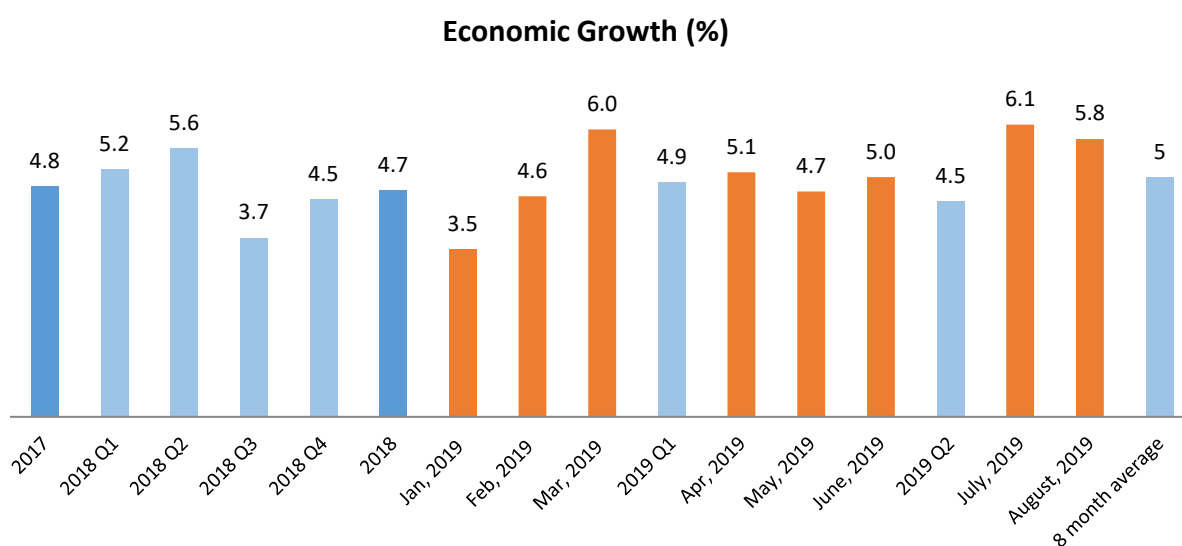
Fully automated VAT refund system started operating in February 2019 (p.23).

Real Sector

Gross Domestic Product

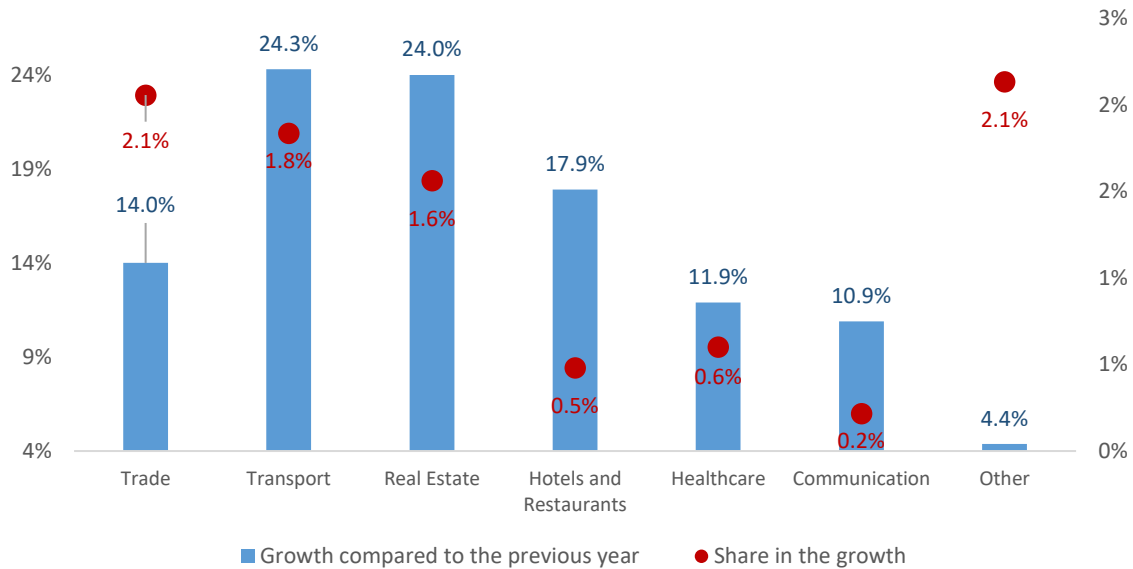
Economic growth

2018 started with increased economic activity and according to the preliminary estimation, economic growth in 2018 is 4.7 percent. Economic growth in January 2019 is 3.5 percent, in February – 4.6 percent, in March – 6.0 percent and growth rate in the first quarter of 2019 was 4.9 percent. Economic growth in second quarter of 2019 was 4.5 percent. In August economic growth was 5.8 percent and average growth rate during the first 8 months was 5.0 percent.



There was high economic growth in the following sectors of the economy during 2018: trade, manufacturing, operations with real estate, services, transport and financial activity. In the first quarter of 2019, main driving sectors of economic growth were: education, hotels and restaurants, transport and communication. At the same time, in the second quarter, high growth was driven by growth in following sectors: operations with real estate, hotels and restaurants, transport and communication and services.

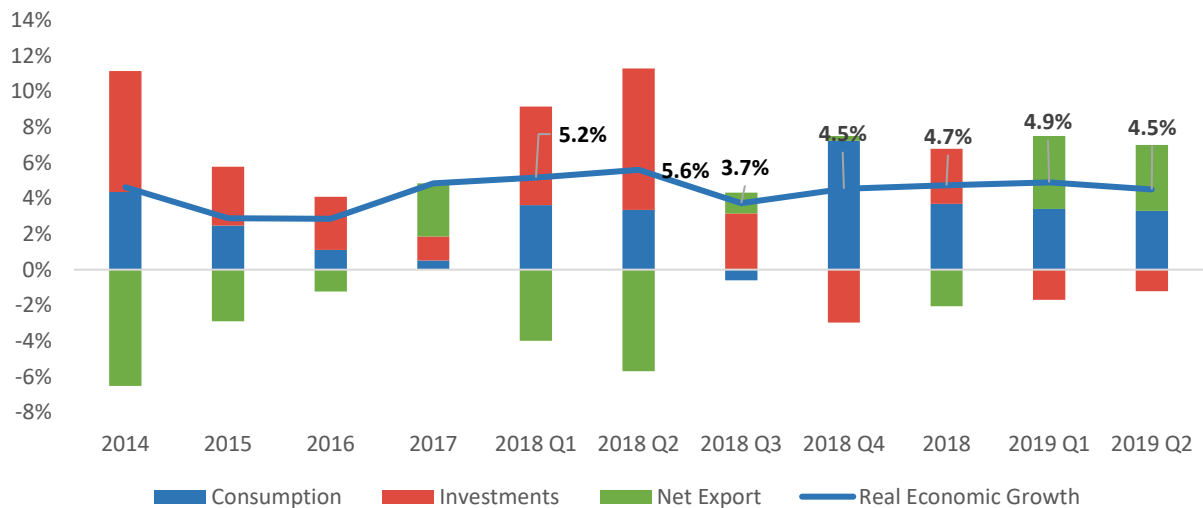
Growth of Sectors (2019 Q2)



The structure of economic growth

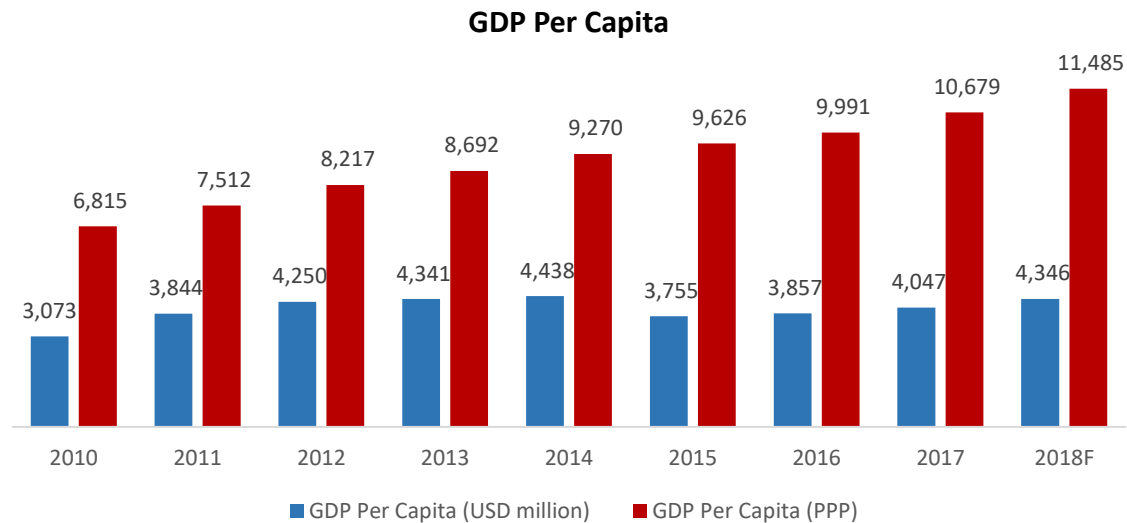
Investments and changes in inventories were the main contributors to the economic growth during 2018. The share of net exports in economic growth in the first half of 2018 was negative compared to the same period of 2017 and was a result of significant increase in imports relative to exports. In the third quarter of 2018 net exports has improved and positively contributed to the growth. The main contributors in 4.7 percent economic growth of 2018 were consumption (3.7 percent) and investments and changes in inventories (1.0 percent), while share of net export was negative. Net export has the highest contribution in the economic growth in the second quarter of 2019, however, share of investments was negative unlike 2018. Net exports is expected to be the main driver of economic growth in the medium run. In addition, global economic recovery is likely to be trade driven. Another important determinant of growth in the medium run is investments. Economic reforms in Georgia are directed towards improving saving and investments in the country.

Economic Growth Decomposition



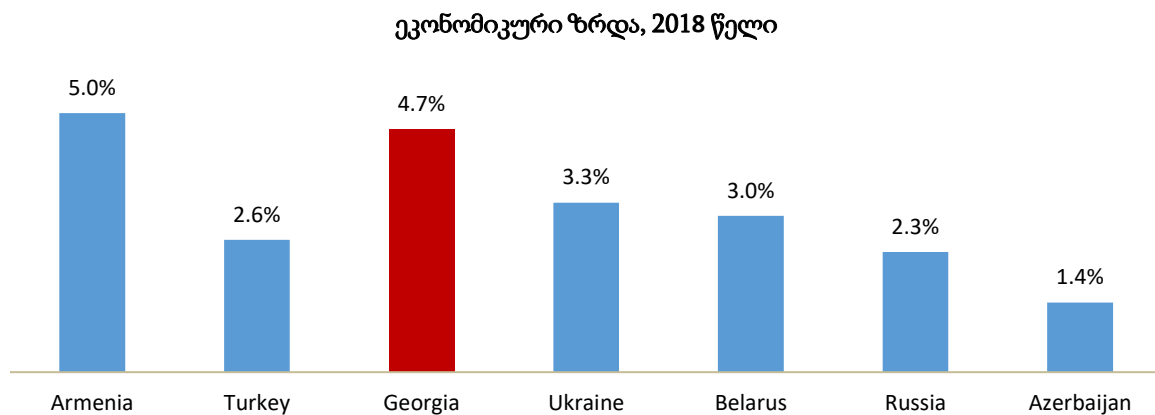
Gross Domestic Product per capita

GDP per capita has an increasing trend. According to the preliminary projections, GDP per capita was GEL 11,014 (USD 4,346 million) in 2018. According to the IMF estimations, GDP per capita in PPP is USD 11,485.



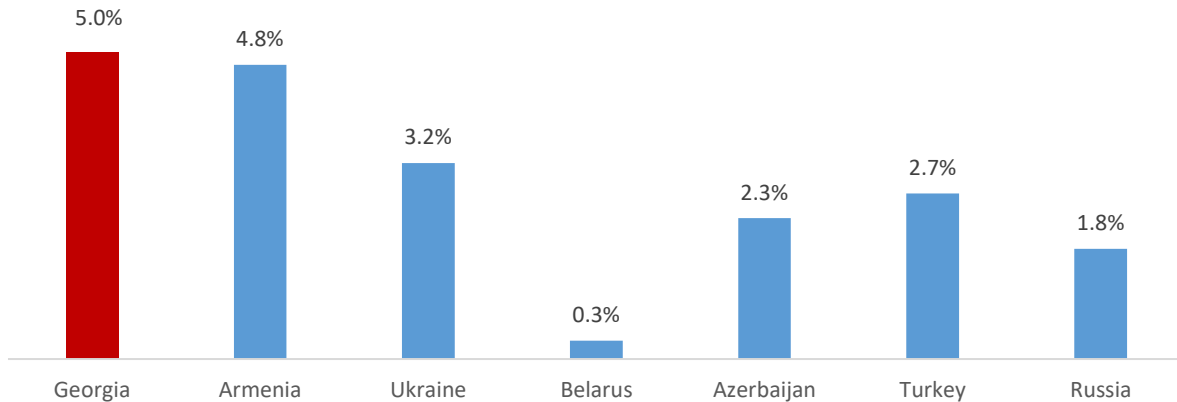
Economic growth in Georgia and neighboring countries

Georgia was growing faster than its trade partners during recent years. Georgia showed impressive resilience in the period of economic slowdown in the region during 2014-2016. Georgian economy was growing about 3.4 percent on average (4.6 percent in 2014, 2.9 percent in 2015 and 2.8 percent in 2016), while all neighboring countries were experiencing negative growth. In 2017 and 2018, there was significant improvement represented by increase of economic growth to 4.8 and 4.7 percent respectively. Consistent reaction of the macroeconomic policy to the external shocks made Georgian economy one of the leading countries in the region.



According to the IMF estimation, Georgia will still continue being the leading country in the region in terms of economic growth in the medium run. Forecast of economic growth is 5 percent during 2019-2024, which is higher than region countries.

Real GDP growth 2019-2024

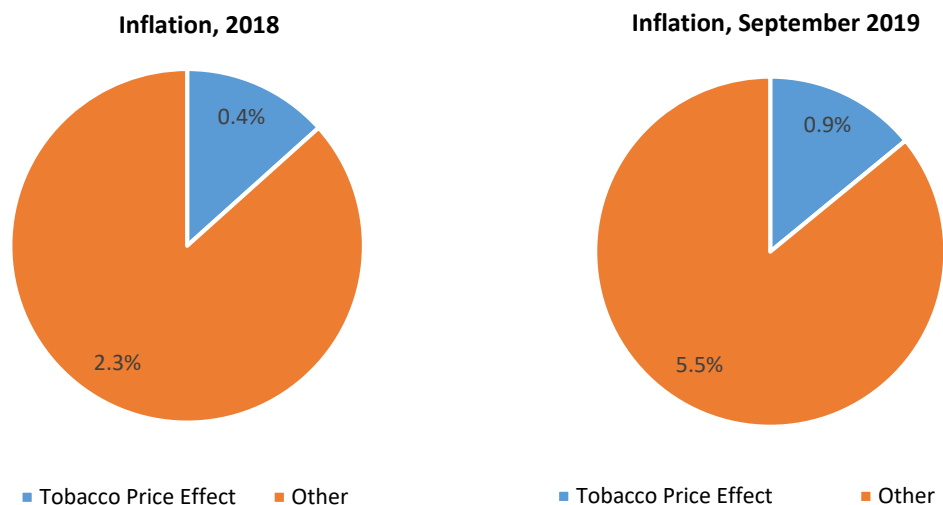


Prices

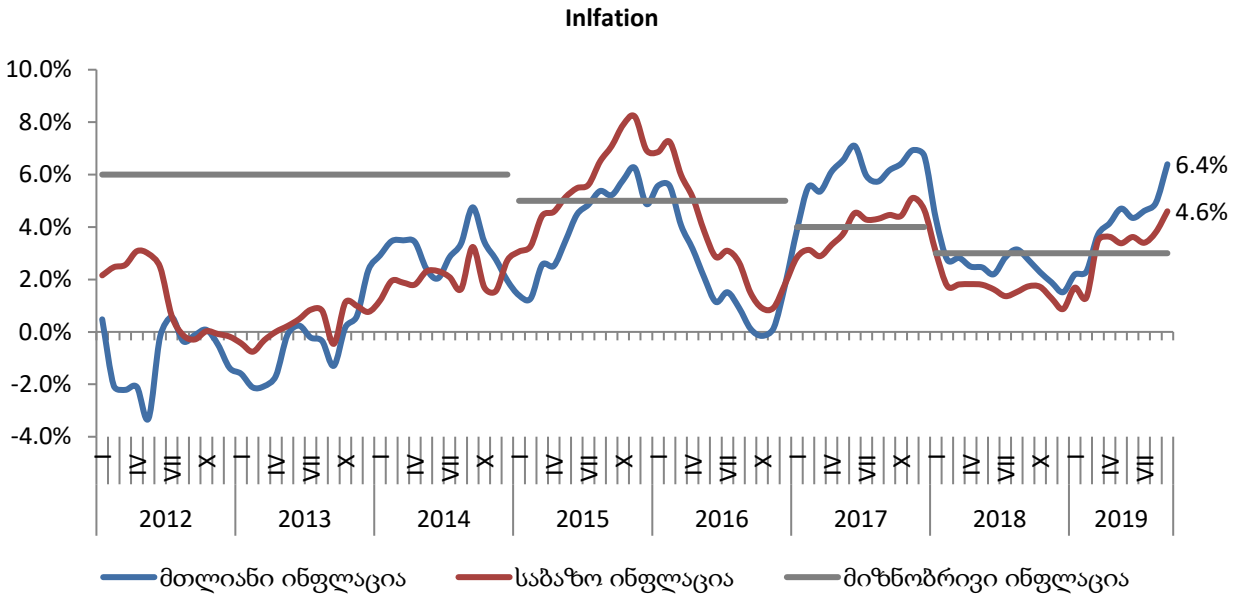
The National Bank of Georgia (NBG) follows the inflation-targeting regime in the conduct of its monetary policy. After the impact of excise has faded out, inflation started to stabilize and was around targeted 3 percent in 2018. In September of 2019, inflation was 6.4 percent (higher than the target) compared to the same period of 2018. Core¹ inflation was at 4.6 percent.

Average annual rate of inflation in 2018 was 2.6 percent, which is lower than the target of 3 percent. As for 2017, annual rate of inflation was 6.0 percent, higher than the target of 4 percent. However, the deviation from the target was attributed to one-off factors related to the change in the excise tax (on tobacco, fuel, motor cars etc.) under the new fiscal reform implemented in 2017. Core inflation was fluctuating around the target level during the entire year.

Recent change in tobacco excise tax will be reflected on the inflation rate of 2019. The effect of price change on tobacco in August of 2019 amounts to 0.9 points of inflation.



¹ Inflation excluding food and energy prices

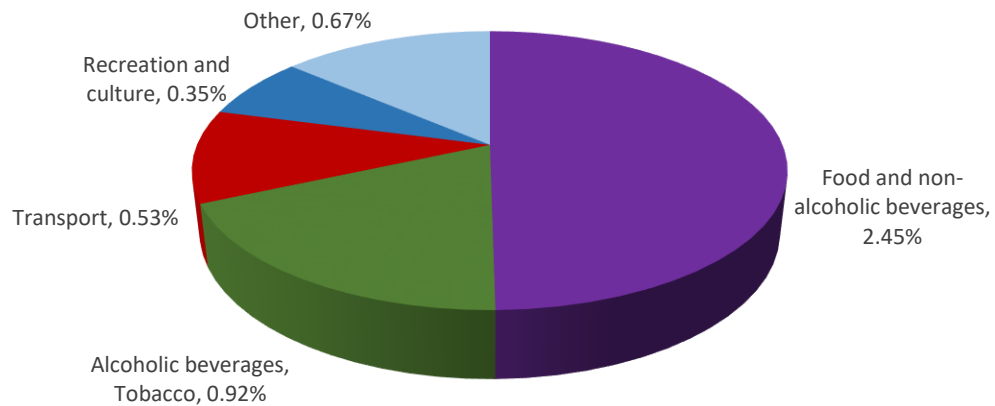


Price change on the following groups² of products contributed to formation of yearly inflation in July 2019:

- Food and non-alcoholic beverages: the prices within the group increased by 11.7 percent, contributing 3.49 percentage points to the overall annual inflation rate. Within the group the prices were higher for the following subgroups: fish (16.1 percent), milk, cheese and eggs (14.6 percent), sugar, jam, honey, chocolate and confectionery (13.2 percent), meat (12.6 percent), bread and cereals (10.8 percent), vegetables (10.1 percent), mineral waters, soft drinks, fruit and vegetable juices (7.6 percent) and oils and fats (3.0 percent);
- Alcoholic beverages and tobacco: the prices increased by 14.6 percent, with a relevant contribution of 0.97 percentage points to the overall annual CPI growth. The prices increased for tobacco (29.0 percent);
- Transport: the prices increased by 3.9 percent, which resulted in a 0.47 percentage point contribution to the overall annual inflation rate. The prices were higher mainly for purchase of vehicles (9.1 percent), operation of personal transport equipment (4.0 percent) and transport services (2.0 percent);
- Recreation and culture: the prices went up by 6.9 percent, contributing 0.39 percentage points to the overall annual inflation rate. The prices in the group increased for recreational and cultural services (6.6 percent);
- Health: the prices went up by 4.0 percent, contributing 0.32 percentage points to the overall annual inflation rate. The prices increased for the following subgroups: medical products, appliances and equipment (6.6 percent), out-patient services (3.7 percent) and hospital services (1.1 percent).

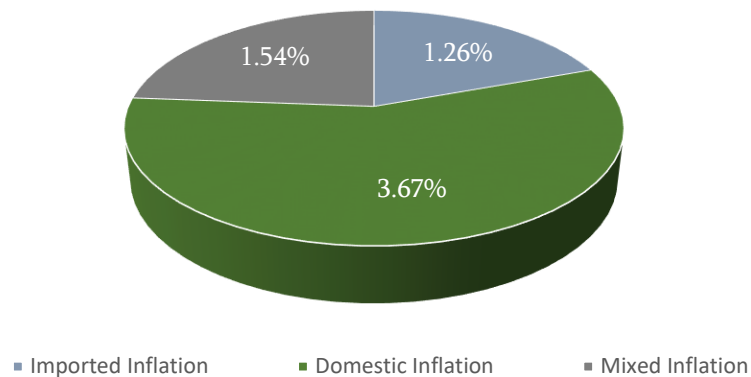
² Source: National Statistics Office of Georgia

Inflation decomposition (September 2019)

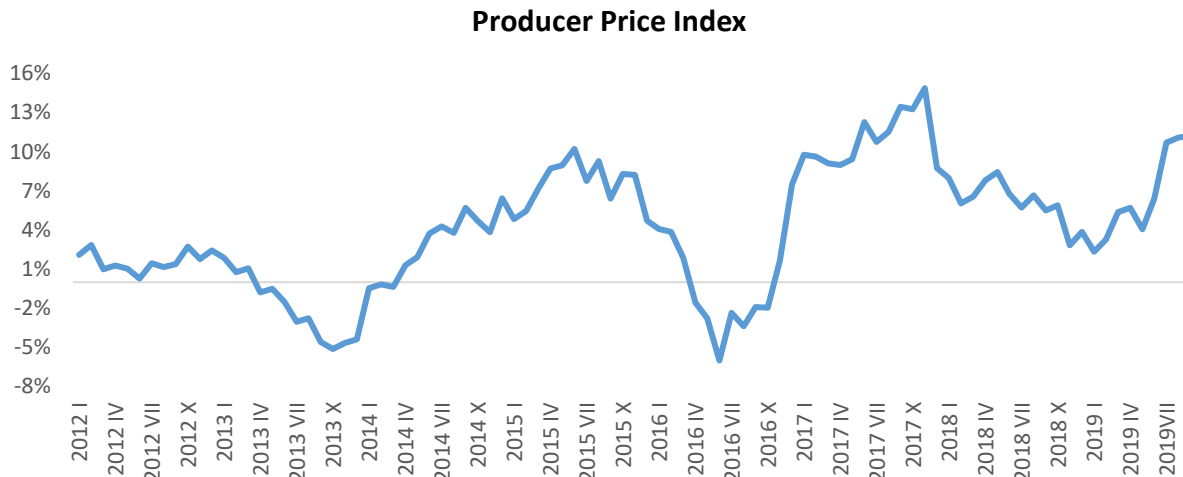


Decomposition of inflation by domestic and imported inflation is as follows: domestic inflation – 3.7 percent, imported inflation – 1.3 percent, mixed inflation – 1.5 percent.

Decomposition of Inflation, August 2019



In September of 2019 compared to the same period of 2018, change of Producer price index (PPI) was 11.2 percent and was mainly driven by the increase in prices in manufacturing industry. Average PPI on industrial production in 2018 was 6.2 percent.



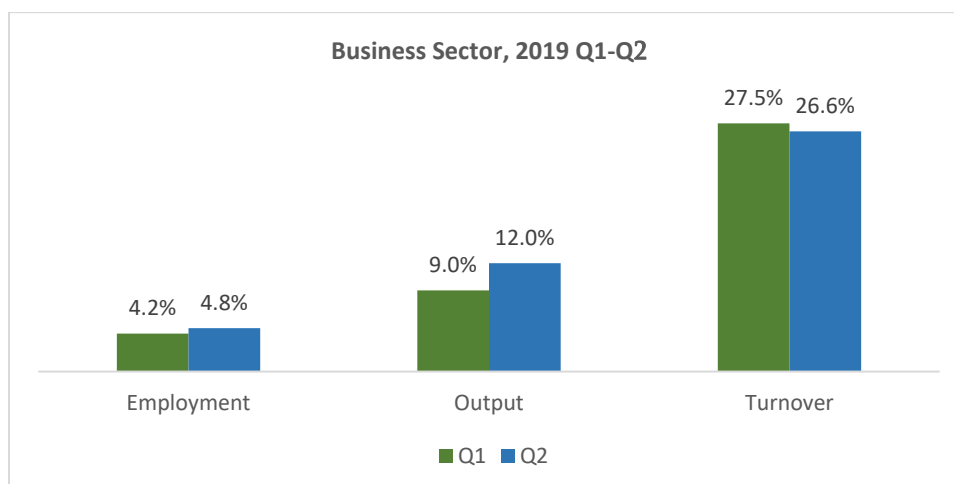
Price change on the following groups of products contributed to formation of PPI in September 2019:

- Manufactured products: the prices increased by 11.9 percent, contributing 9.58 percentage points to the overall annual index growth. There was an increase in the prices for food products, beverages and tobacco products (12.6 percent), basic metals and fabricated metal products (9.5 percent), also for pulp, paper and paper products (42.4 percent);
- Products from mining and quarrying: the prices were 21.5 percent higher, contributing 1.38 percentage points to the overall annual index growth;
- Electricity energy, gas, steam and hot water: the prices increased by 1.9 percent and contributed 0.27 percentage points to the overall annual PPI change.

Business Sector

Private sector historically had a leading role in economic growth of the country and the trend continued in 2018 as well.

Turnover of the business sector increased by 19.5 percent in 2018 compared to 2017. The output was 10.5 percent higher and employment grew by 3.7 percent (or 24,458 new jobs). Total number of employees in business sector was 684,517. As for the first quarter of 2019, business sector turnover has increased by 26.6 percent, output – by 12.0 percent and employment has increased by 4.8 percent. Number of employees in business sector in the first quarter was 687,9.

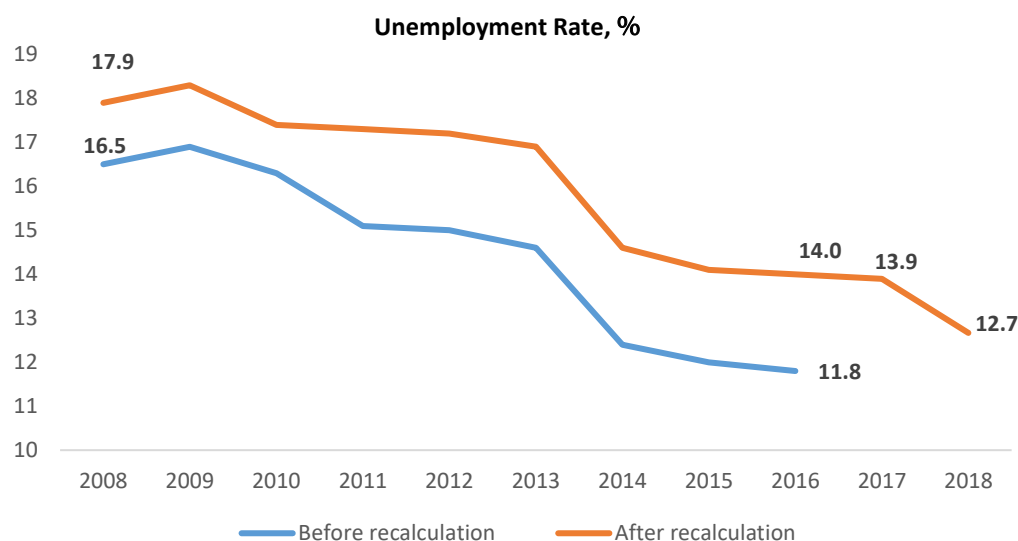


Unemployment Rate

Unemployment rate reduced to 12.7 percent in 2018, which is the lowest during last years. In 2017, unemployment rate was 13.9 percent. In first quarter of 2019, unemployment rate was equal to 18.8 percent, while in the second quarter it was equal to 11.4 percent.

As a result of population census conducted in 2014, there was an absolute decrease in the country's population. The labor force data was recalculated, which resulted into a different rate of unemployment. Recalculated unemployment rate is higher than before the recalculation but the trend is similar and the declining during 2017-2018.

As of 2018, unemployment rate was 12.7 percent: urban unemployment rate was 19.3 percent, while rural unemployment rate was 5.8 percent. According to data from second quarter of 2019, urban unemployment rate was 17.5 percent, while rural unemployment rate was 5.1 percent. Age groups 15-24 and 25-34 are characterized with the highest rate of unemployment compared to other age groups.



External Sector

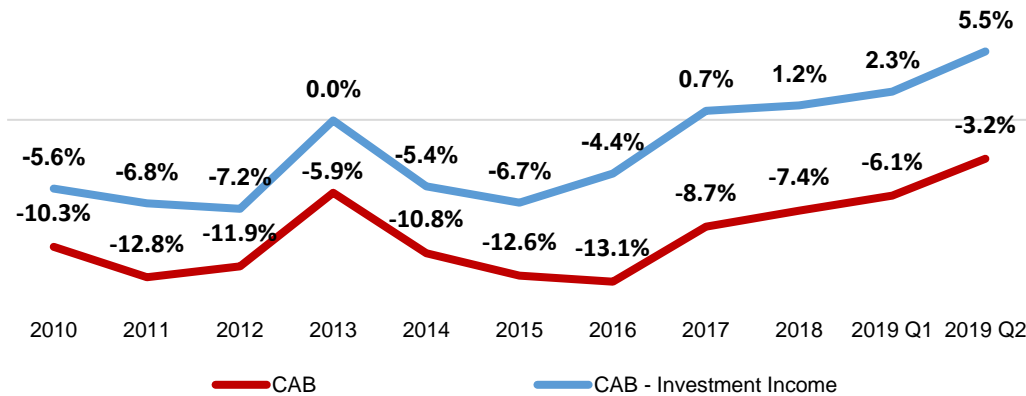
Current Account Deficit

High current account deficit is one of the main vulnerabilities of the Georgian economy. Government of Georgia initiated set of reforms to promote savings, increase productivity and export and gradually close saving-investment gap which means to achieve balanced current account.

In the second quarter of 2019 current account deficit was 3.2 percent, which is significant improvement compared to corresponding value of -8.2 percent in second quarter of previous year. Decline of deficit was mainly due to the decrease of negative goods balance, which is the result of export improvement.

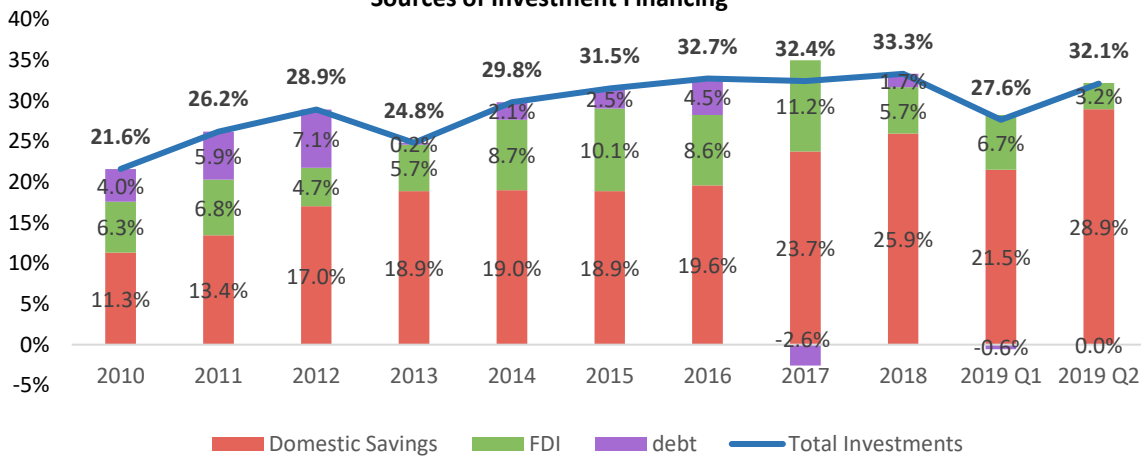
Declining tendency of current account deficit that started in 2017 is continuing in 2018 as well. In the first quarter of 2018, current account deficit amounted to 11.9 percent, in the second quarter it was -8.8 percent, while in the third quarter there was current account surplus at 0.2 percent, which is historical best, in the fourth quarter current account deficit amounted to 10.9 percent. As a result, current account deficit decreased to 7.7 percent in 2018. The improvement was mainly due to a significant increase of positive service balance.

Current Account Balance as % of GDP

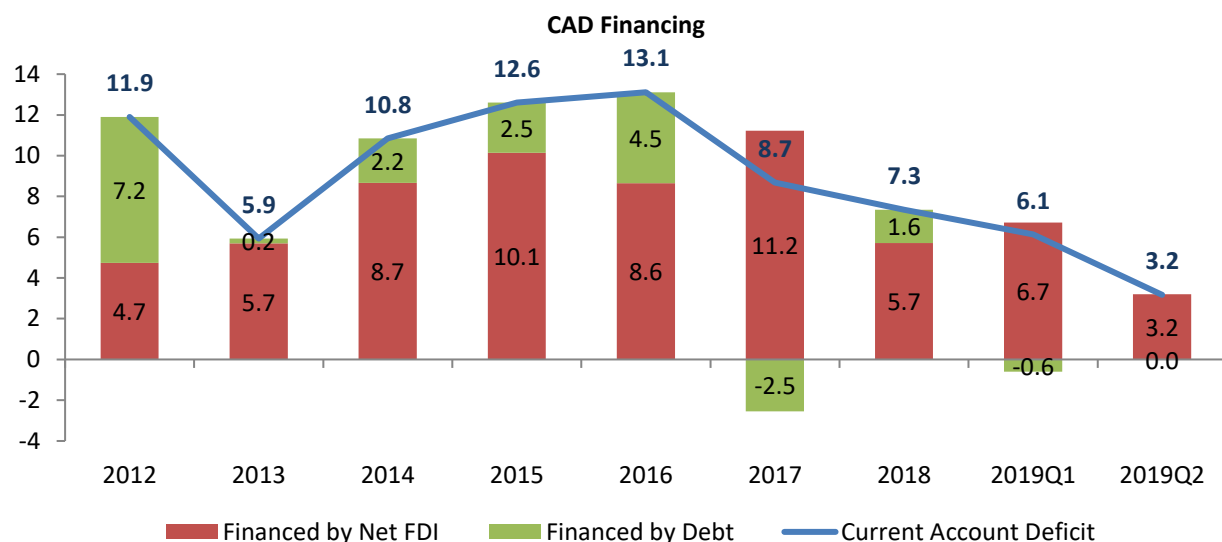


It is important to note that the improvement in current account balance during last few years was driven by an increase in savings. This increase was a result of CIT tax reform implemented in 2017 according to which reinvested corporate profit is no longer subject to taxation.

Sources of Investment Financing



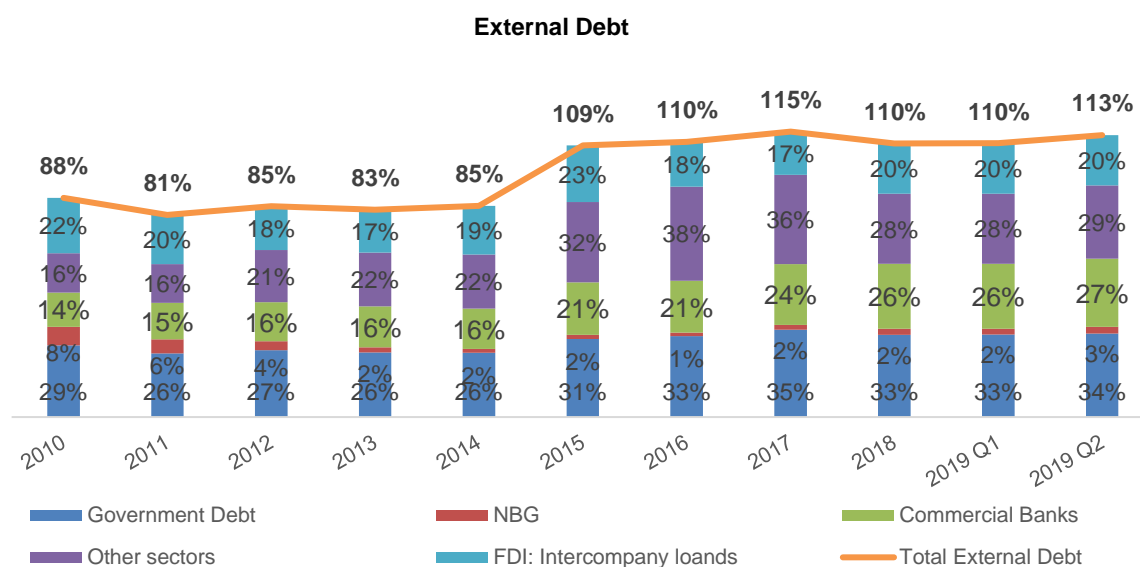
Current Account Deficit is financed through debt and foreign direct investments (FDI). Debt financing means more borrowing and, thus, more interest payments. Therefore, it is more favorable to finance current account deficit through increased FDI. In 2017, current account deficit was fully financed through FDI. In the third quarter of 2018 there was a positive balance of 0.2 percent: financing through FDI contributed to 6.3 percent, while debt financing contributed negative 6.6 percent. As for 2018, deficit is financed by the FDI and debt as well. In the second quarter of 2019, current account deficit has significantly decreased to 3.2 percent, while deficit was mainly financed by investment contributing to 3.2 percent, while contribution of debt financing was close to 0.



External Debt

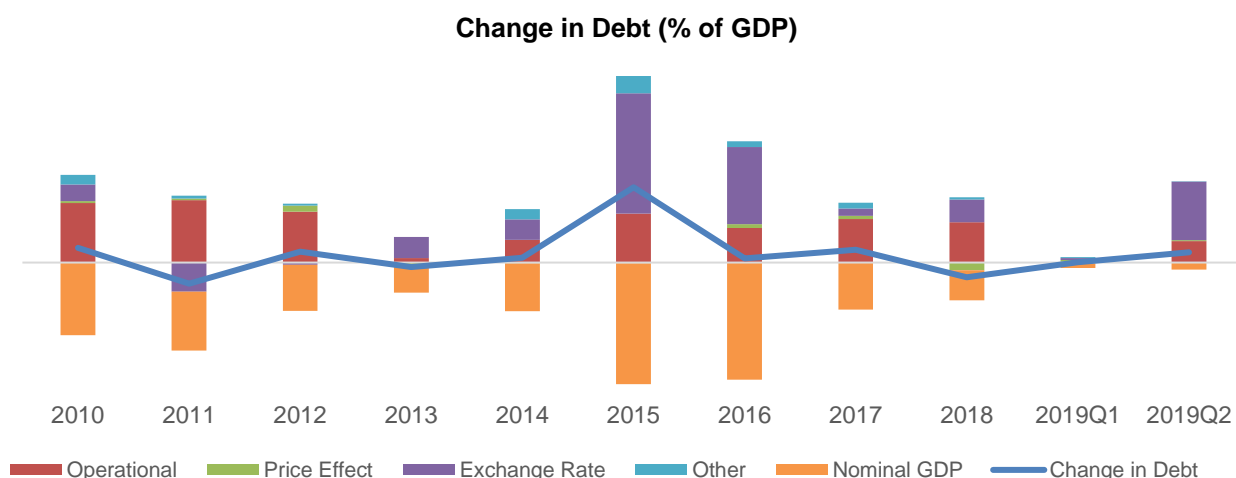
External debt is another vulnerability for Georgia. External debt consists of government debt on one the hand and commercial debt, debt of the NBG and intercompany loans on the other hand.

Total external debt has declined in 2018 compared to 2017 and amounted to 110 percent of GDP, while in 2017 it was 115 percent of GDP. In the third quarter of 2018, it has reduced and constituted to 107 percent of GDP. The reduction was mainly due to reduced government debt and intercompany loans. External debt remained to 113 percent of GDP in the first half of 2019.



Change in external debt can be decomposed into operational change (new debt) and price effect, exchange rate effect and nominal GDP effect. During 2015 and 2016, depreciation was the main driver of increasing external debt, while change in GDP was positively contributing towards its reduction. In 2018, operational and exchange rate effects were source of increase the external debt, however, growth of nominal GDP and price effects caused debt to decline. As for the second

quarter of 2019, external debt has increased by 3.3 percent and the main contributor of the debt change was exchange rate effect, while decrease of the new debt and economic growth has contributed to reduce the external debt.

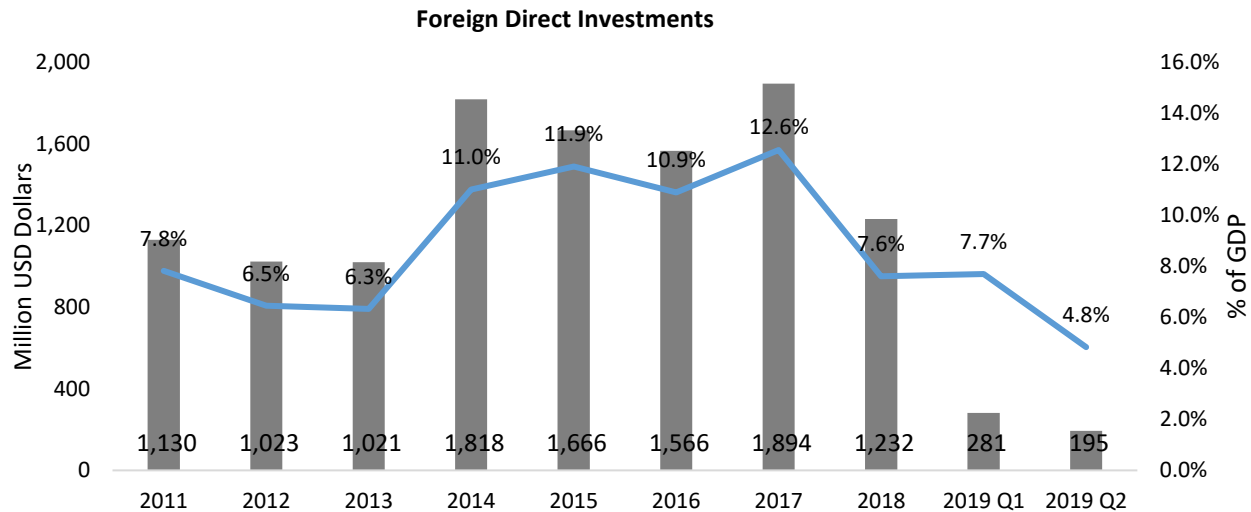


Foreign Direct Investments

FDI amounted to USD 194.5 million in the second quarter of 2019, which means 30.8 percent decrease compared to the previous period. The main reasons for decreasing the FDI included completion of a pipeline project and transferring of ownership in some companies from non-resident to a resident units. Direct investor countries in the second quarter were Netherlands (31.1 percent), Turkey (19.2 percent) and the United States (14.7 percent). As for the sectors, FDI in the other community, energy sector, reached 34 percent, while in manufacturing sector it was 20.5 percent and foreign direct investments from hotels and restaurants amounted to 15 percent.

FDI has amounted to 7.6 percent of GDP in 2018. In the first quarter of 2018, FDI was 8.2 percent of GDP, in the second quarter - 9.4 percent of GDP, in the third quarter - 8.2 percent, while in the fourth quarter it amounted to 4.7 percent of GDP. The largest foreign direct investments were made in the following sectors in the fourth quarter of 2018: Financial sector - 42.7 percent, transport and communication - 10.7 percent, manufacturing - 10.4 percent. For the whole 2018 investments were made in the financial sector - 22.5 percent, transport and communication - 14.2 percent and energy sector - 12.8 percent.

During the last four years, Foreign Direct Investments has improved significantly in Georgia and steadily amounts 10 percent of GDP. In 2018 there was slight decline in FDI due to the completed pipeline project, transferring of ownership in some companies from non-resident to a resident units and reduction of liabilities to non-resident direct investors. In the third quarter of 2018 FDI amounted to USD 345 million, which amounted to 8.2 percent of GDP. In the fourth quarter FDI was USD 197 million and in 2018 FDI was USD 1,232 million, which is less than the investments made the recent period.

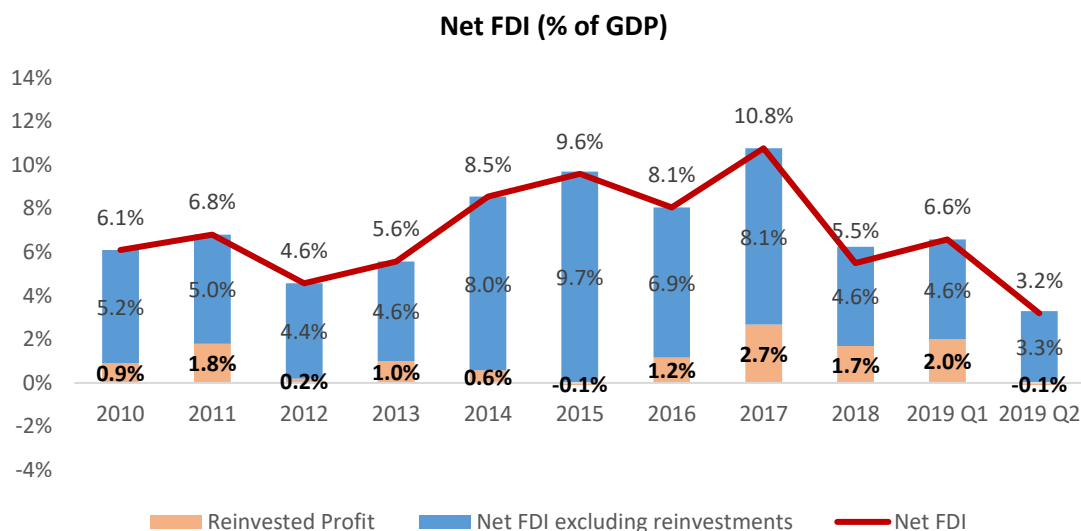


The major part of foreign direct investment in 2017 was made in transport and communication sector and was 25.8 percent, while it amounted 16.0 percent in financial intermediation sector, construction – 14.9 percent, energy sector – 11.8 percent, real estate – 9.6 percent, manufacturing – 5.2 percent, hotels and restaurants – 3.8 percent, and mining – 2.7 percent.

There is improvement in FDI diversification through investments in new sectors. For instance, in 2015, there was a rapid growth of investments in healthcare compared to the previous years. In 2016, FDI has increased in communication sector, where investments share of total FDI amounted 3.8 percent. In 2017, there was a significant increase in financial and construction sectors. In financial sector, investments amounted 16.0 percent of total FDI, while in construction sector investments were 14.9 percent of total FDI. The same trend continued in the beginning of 2018. However, in the second quarter of 2018, investment has increased in the energy sector, which amounted to 28.0 percent of total investments, while in the first three quarter it was financial sector where FDI amounted to 19.7 percent of total FDI, transport – 17.3 percent and energy sector – 15.4 percent.

The biggest investors by FDI in Georgia for 2018 were Azerbaijan with 19.5 percent, the UK with 16.5 percent and Netherlands with 13.6 percent shares. Should be mentioned, that investments made from the EU countries are increased from 40.5 percent to 46.2 percent in 2018 compared to 2017.

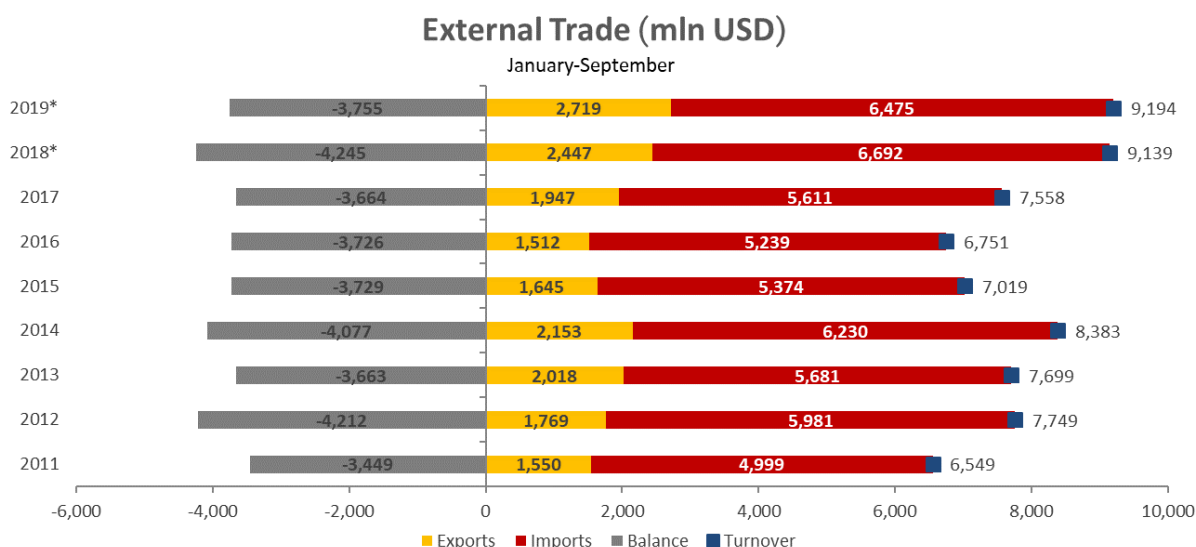
In 2016, the highest indicator was recorded in reinvestments amounting to 32 percent of total FDI which increased to 43.9 percent in 2017 and demonstrates that the government's economic policy and improved business environment is positively perceived by investors and more investors decided to extend their business plans in Georgia. The current economic policies and the reforms are prerequisites for maintaining high levels of reinvestment in subsequent periods and for increasing it in the medium and long term. Increasing share of reinvestments can be linked with CIT reform, so called “Estonian Model”, under which reinvested profits are exempt from taxation.



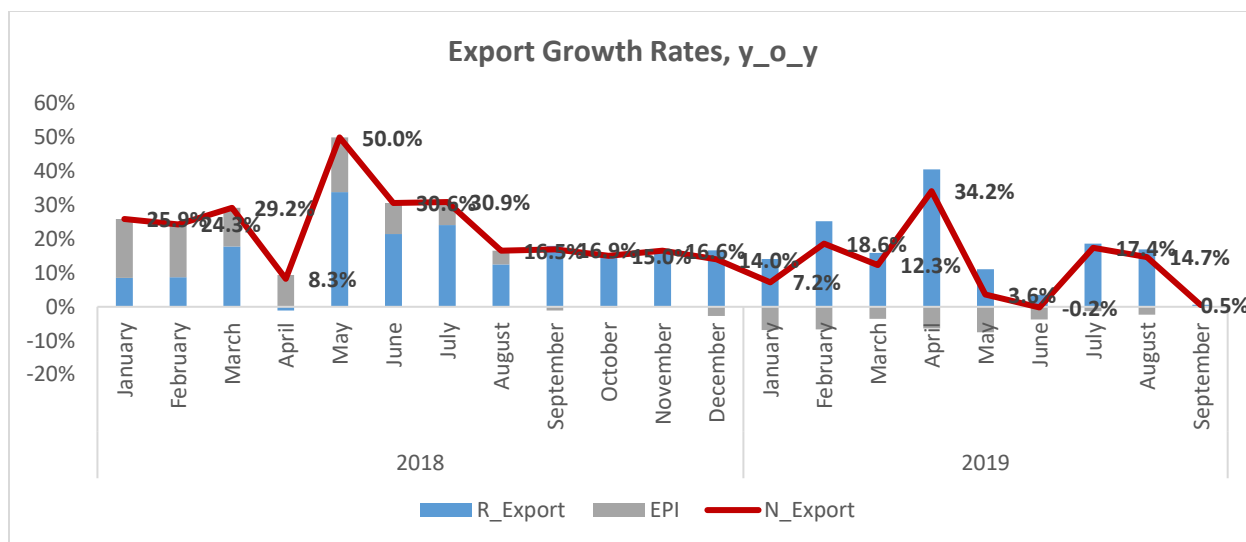
External Trade

In September of 2019, export has increased by 0.5 percent, while import has reduced by 4.0 percent and trade deficit was increased by 6.6 percent relative to previous year. In January-September export growth amounted to 11.1 percent, import decline was – 3.3 percent.

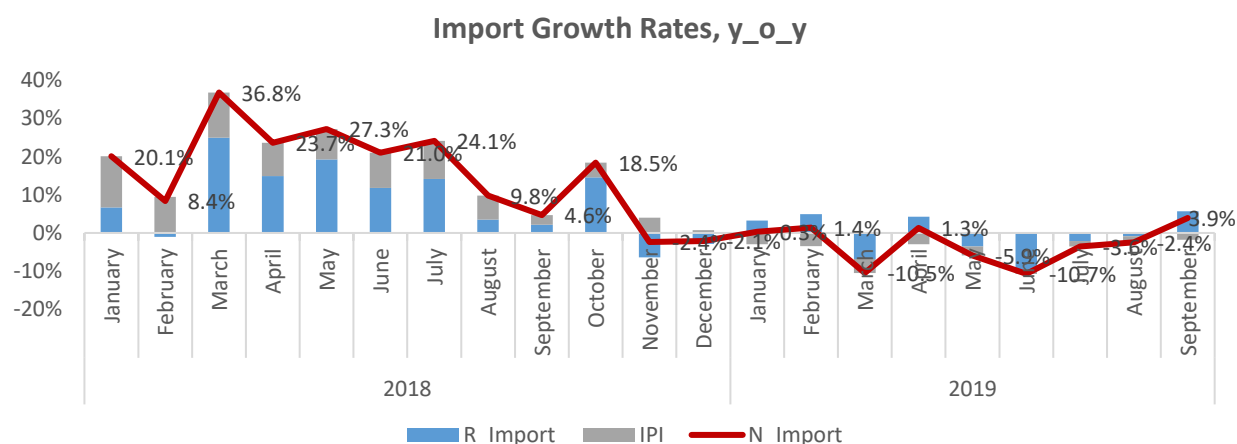
In 2018, both export and import increased by 22.6 percent and 14.9 percent respectively, resulting in deterioration of trade balance by USD 561 million. As for the first quarter of 2019, increase in export was 12.7 percent and decrease of import was 3.9 percent, as a results, trade balance improved by USD 174 million compared to the same period of 2018.



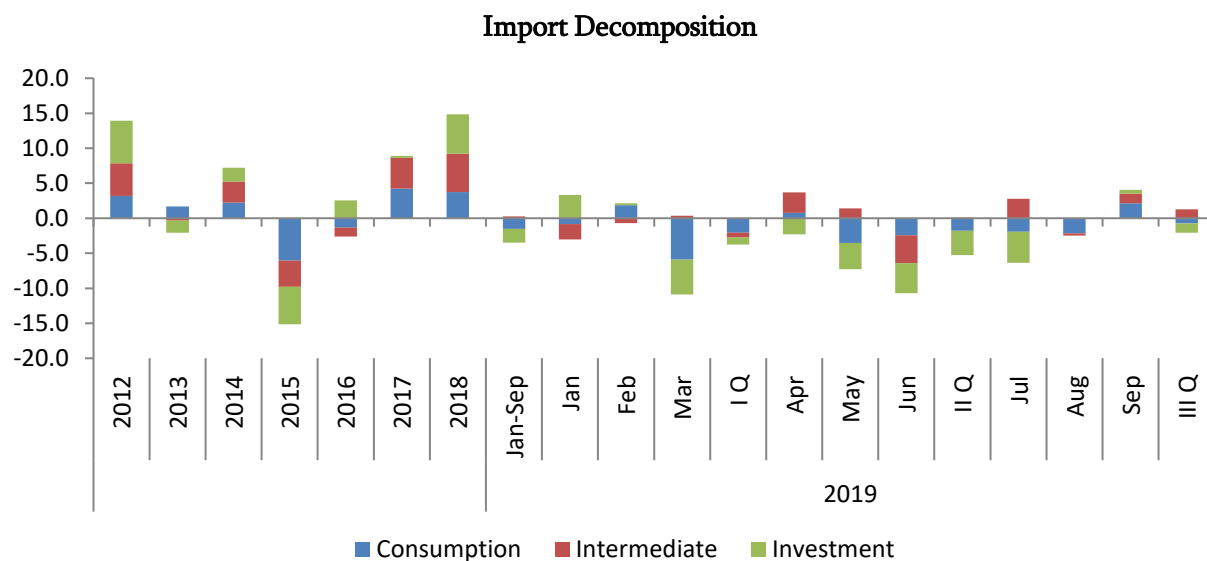
It is important to differentiate between real and price change effects when analyzing external trade. Real growth of export has improved in the first half of 2018. Moreover, starting from September 2018, the effect of price change on export was negative, thus, making the real change of exports greater than the nominal change. This tendency has also continued in 2019. In September 2019, real growth of export amounted 0.6 percent, while its nominal growth was 0.5.



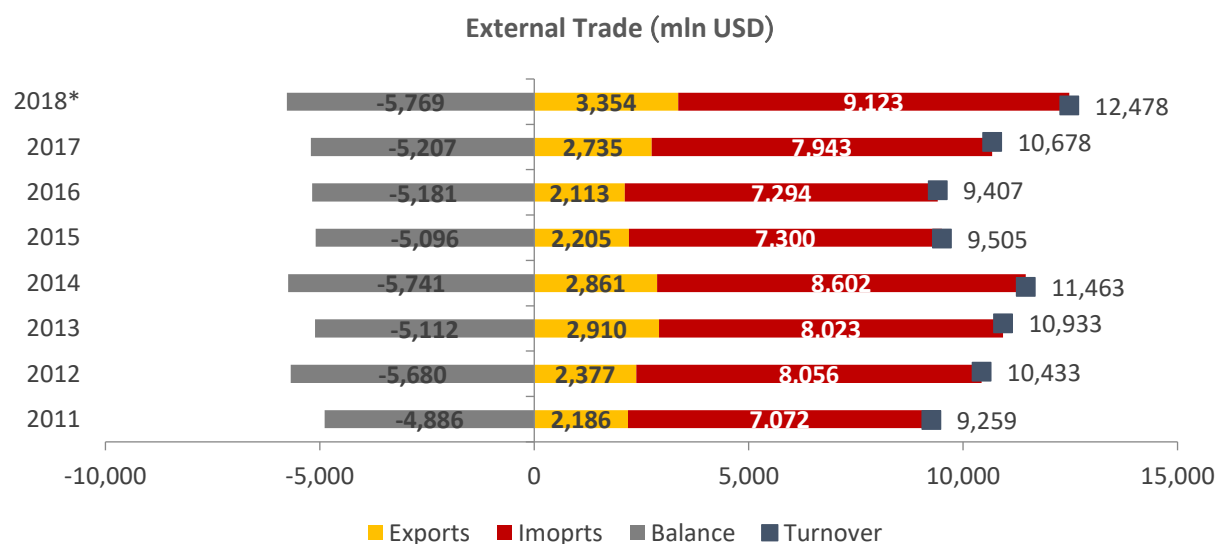
As for the growth in import, the effect of price change has a significant share in its nominal growth in 2018. Real import has reduced during November and December of 2018, while in January-February of 2019, real growth of import was greater than its nominal growth. In September 2019, real growth of import amounted 5.7 percent, while its nominal growth was 3.9 percent.



In total, export increased by 22.6 percent in 2018, while import increased by 14.9 percent out of which 11.1 percent was due to increase in import of capital and intermediate goods. Import of investment goods has also increased compared to previous years. As for 2019, in January-September import of investment goods has decreased by 2.0 percent and import of consumption goods – by 1.5 percent, while import of intermediate goods has increased by 0.2 percent.



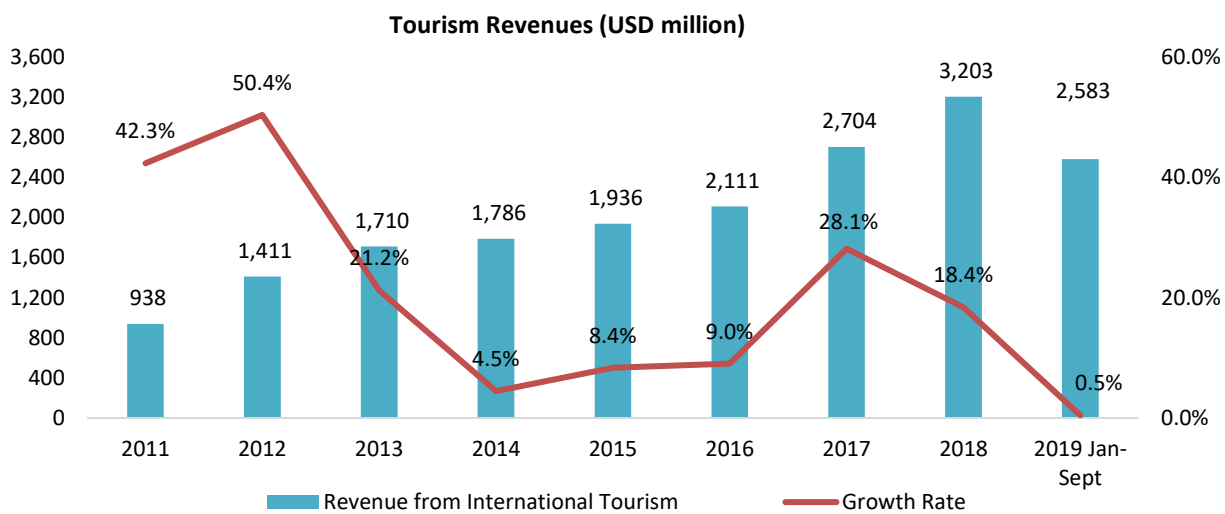
Contributions in growth of exports of 2018 by sectors is as follows: cars – 6.4 percentage points, cigarettes – 3.9 percentage points, copper ores – 3.0 percentage points, ferroalloys – 1.7 percentage points, wine – 0.9 percentage points. Share of products in the export growth during January-May of 2019 is following: cars – 6.6 percentage points, copper ores – 6.2 percentage points, medicaments – 3.1 percentage points, centrifuges – 0.9 percentage points, mineral water – 0.7 percentage points,



Tourism

During last years, tourism has formed as one of the most important sectors of the economy. The number of visitors has increased by 15.1 percent in September 2019 and amounted to 839 thousand, while revenues from tourism was 318 million USD, 4.9 percent less compared to September of last year. It should be noted that change in number of visitors was mainly due to 0.6 percent increase in a number of touristic trips, while there was 7.7 percent increase in number of one day trips.

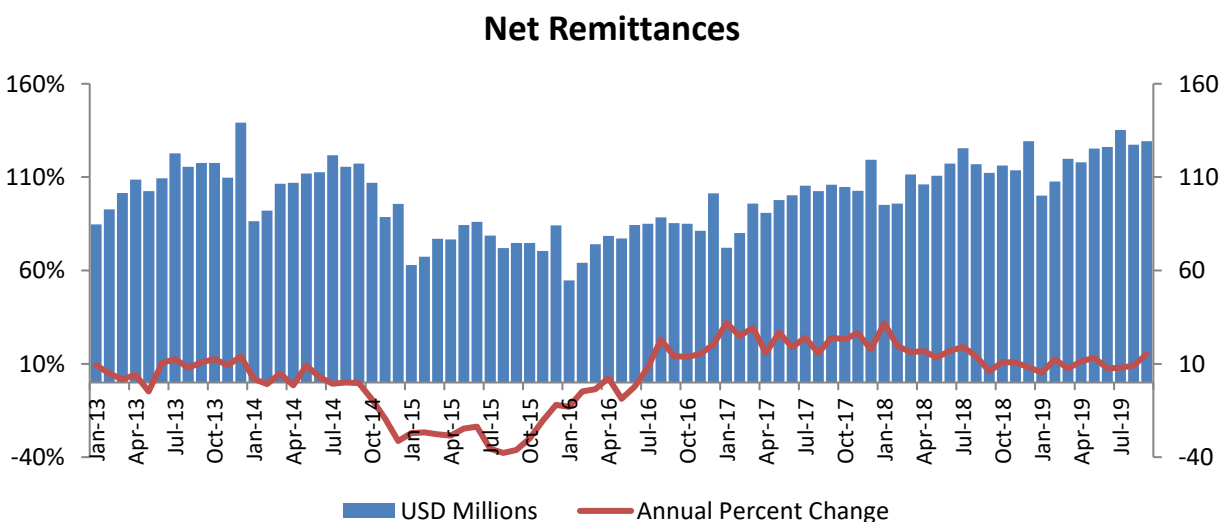
2018 started with increasing trend of visitors. There were 8,326 thousand visitors in Georgia throughout 2018 which is 10.2 percent greater than in 2017. Revenues from tourism increased by 19.1 percent and amounted USD 3,222 million.



Transfers

From the beginning 2019 net money transfers in a month were higher than USD 100 million, which was higher compared to the same period of the previous year. In September transfers amounted USD 129.3 million, which is 15.2 percent higher than in previous year. Remittances have increased significantly from the Italy (3.4 percentage share of the total increase), from Ukraine (1.5 percentage share of the total increase), from Greece (1.3 percentage share of the total increase) and from the USA (0.9 percentage share of the total increase) in September, while they have decreased from Russia (-1.1 percentage share of the total increase).

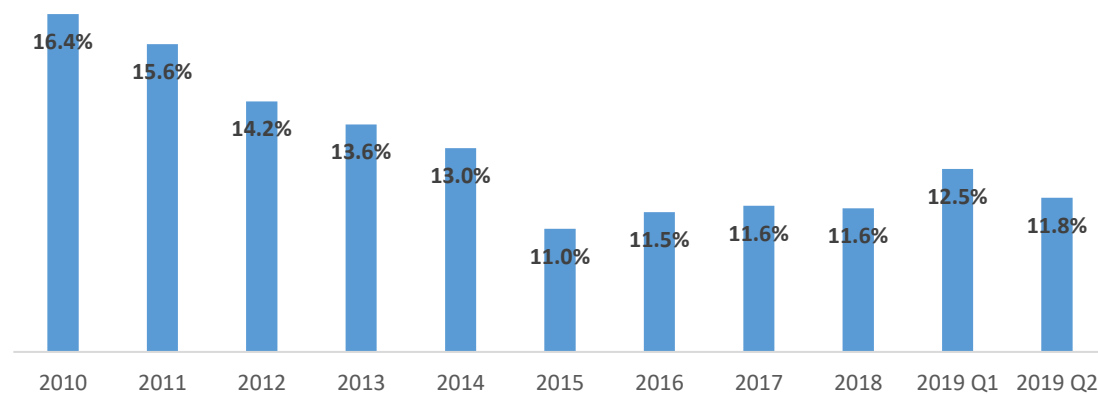
There was a significant increase in money transfers in 2018. In January 2018 there was 34.7 percent annual increase in money transfers, which is the maximum percentage increase in recent years. Increase in money transfers in the following months roughly between 14-20 percent. Growth of money transfers was lower from September, which is due to the high amount of money inflow at the end of 2017.



Overall, inflow of foreign currency that amounted USD 1,321 million in 2018 was driven by increase in export, tourism and transfers, while outflows determined by import amounted USD 1,183 million. The impact to the current account was positive and amounted USD 137 million. Inflow of foreign currency driven by increase in export, tourism and transfers, in January-September increased by USD 381 million (6.2 percent higher relative to previous year), while outflows determined by import decreased by USD 222 million (less by 3.3 percent compared to previous year).

Despite the fact that money transfers have increased as a result of exhaustion of external shocks during recent years, dependence of the economy on such transfers declines through years and can be explained by rapid growth of export and tourism. However, this dependence has increased in the first quarter of 2019 in addition to the increase of export and tourism.

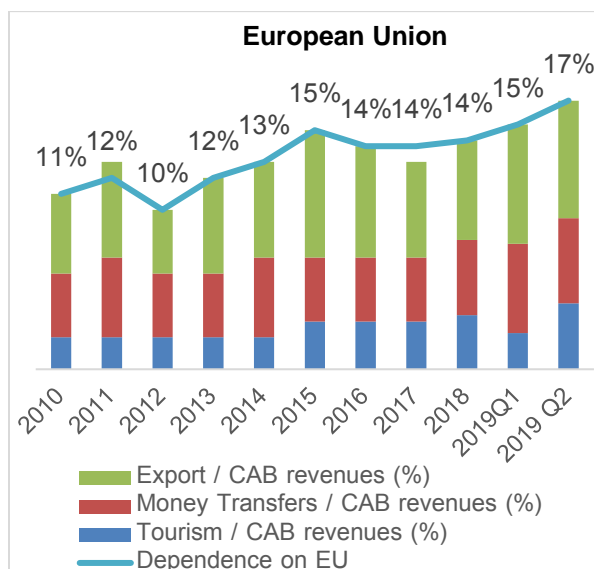
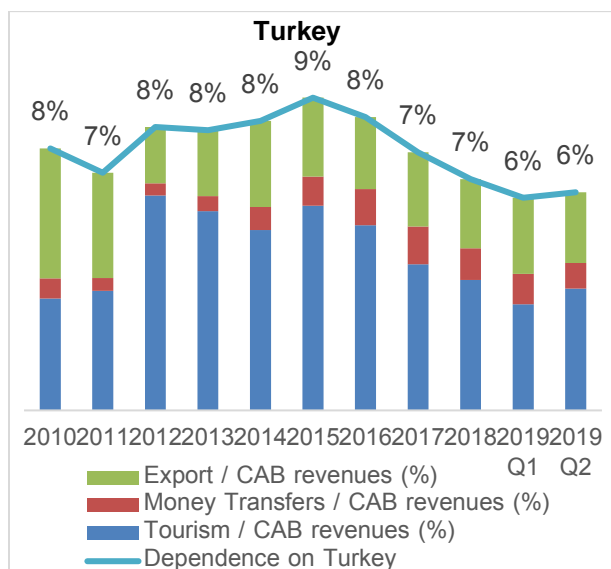
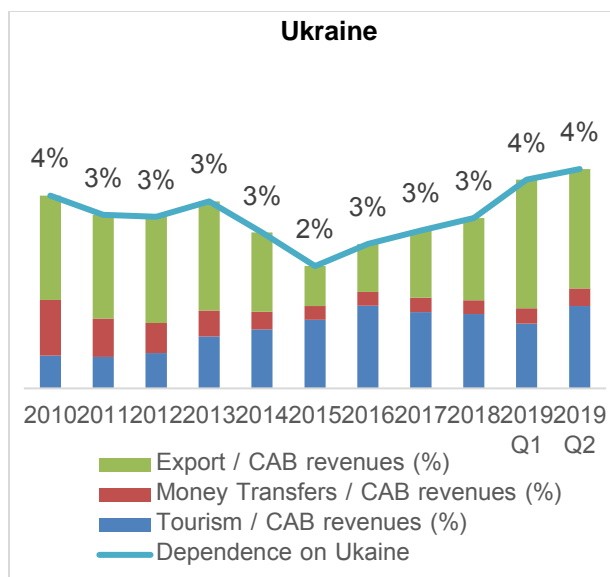
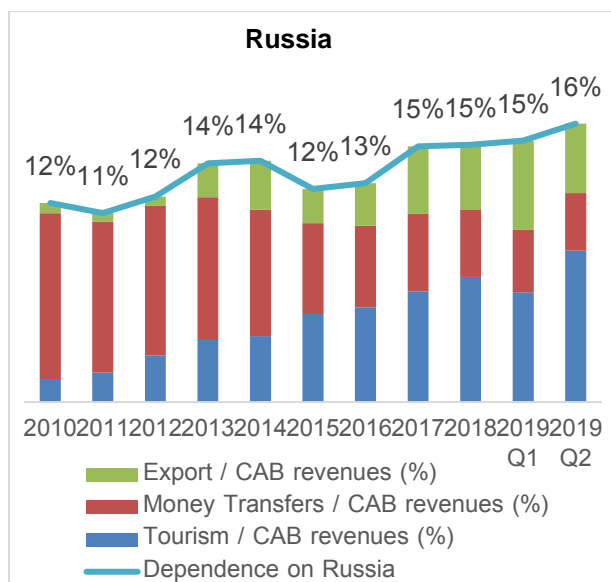
Money Transfers as a percent of CA inflows



Dependence on other countries

Georgian economy is diversified in terms of dependence on other countries. Based on shares of exports, tourism and transfers in current account deficit, it can be concluded that Georgia has tight relationships with Russia, Turkey, Ukraine and European Union.

Dependence on Ukraine and EU has increased in the first half of 2019, while based on the 2018 data, total dependence on Russia is almost unchanged, however, compared to the previous years, it is increased in 2017-2018; dependence on Turkey has slightly reduced, while dependence on Ukraine and European Union has increased. There is also change in composition of dependence. There has been a declining tendency in the share of transports and increase in the share of tourism from Russia, Turkey and Ukraine during recent years. The share of exports, in turn, has been increasing in the case of Russia and Ukraine, while being almost unchanged in the case of Turkey and European Union.

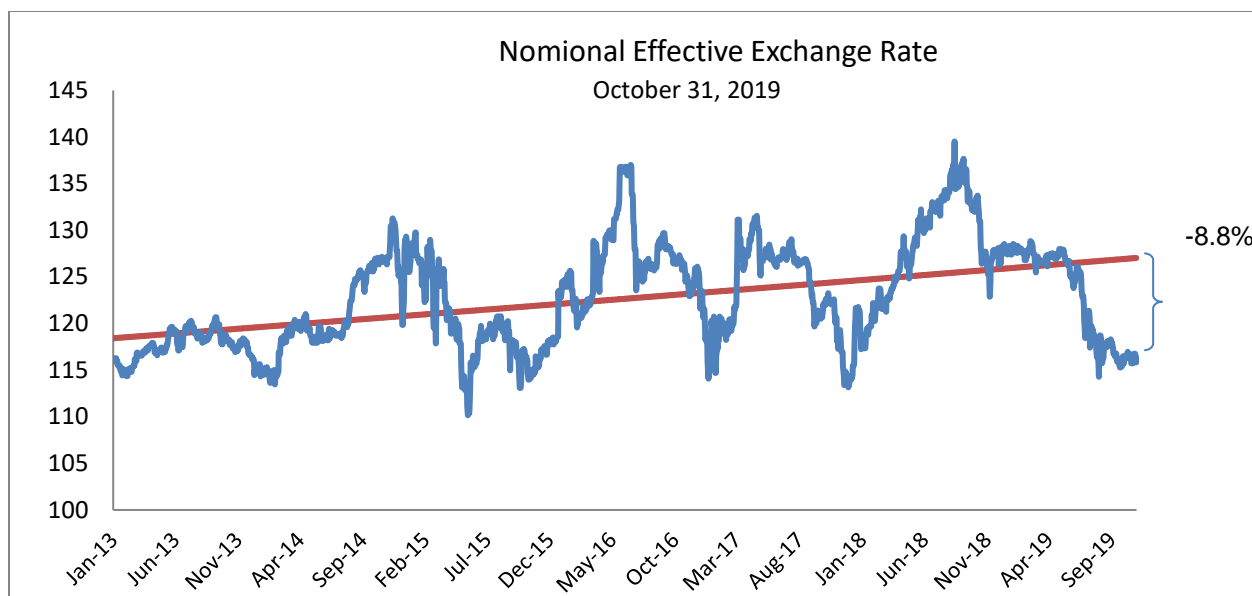


Exchange rate

On October 31 of 2019, nominal effective exchange rate of Georgian Lari depreciated by 9.4 percent compared to January 1 of 2019 and there was 2.0 percent depreciation compared to January 1 of 2018. Real exchange rate depreciated by 3.9 percent compared to January of the last year and by 7.1 percent compared to the January of 2018.

Nominal effective exchange rate of Lari is depreciated by 6.2 percent from its medium-run trend.

	October 31, 2019	Oct 31, 2019 - Jan 1, 2019	Oct 31, 2019 - Jan 1, 2018
Euro	3.2963	▼ -15.2%	▼ -20.7%
US Dollar	2.9632	▼ -10.7%	▼ -19.1%
Turkish Lira	0.5158	▲ 45.5%	▲ 58.8%
Russian Ruble	0.0464	▼ -7.4%	▼ -30.0%
NEER	115.83	▼ -9.4%	▼ -2.0%
REER (September 2019)	111.07	▼ -7.1%	▼ -3.9%



Fiscal sector

Budget of 2018

Actual budget revenues of 2018 exceeds budget revenues of 2017 by 8.3 percent and amounts to GEL 903.3 million. Actual budget revenues constitute to 101.0 percent of planned revenues and the excess amounts to GEL 122.7 million. Excess revenues will promote savings and will be directed towards VAT refunds, strengthening fiscal buffers and reducing the deficit. In 2018, total VAT refunds amounted to GEL 521 million, which is historically the highest and exceeds VAT refunds of 2017 by Gel 200 million.

Total tax revenues of 2018 amounts to GEL 10,506.3 million which 7.4 percent greater (GEL 727.4 million) than tax revenues in 2017. The forecast of tax revenues of 2018 is GEL 10,500.0 million. Actual tax revenues exceed the forecast by 0.1 percent (GEL 6.3 million).

Budget deficit maintains a declining tendency. Based on preliminary estimation, deficit of 2018 is 2.5 percent, which is 0.3 points less than forecasted deficit.

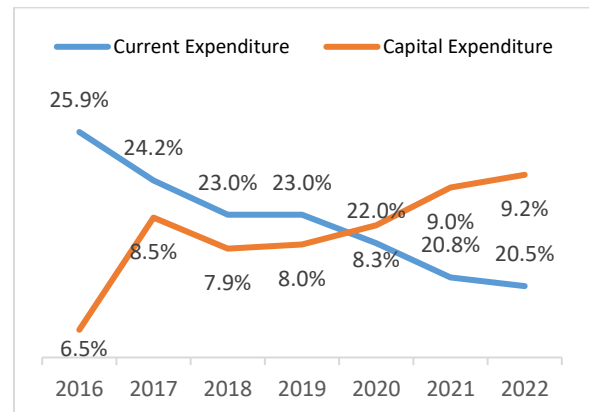
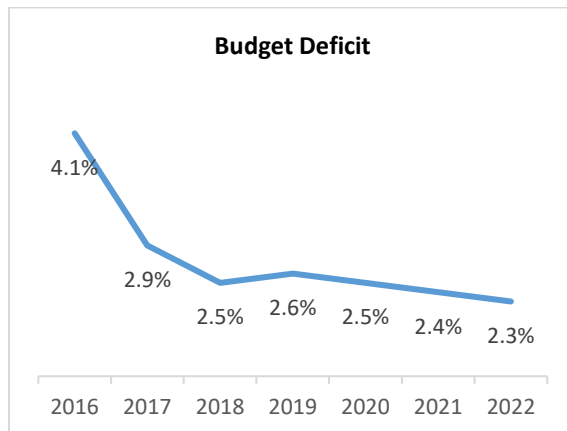
Budget of 2019

Forecast of budget revenues of 2019 is GEL 12,578.0 million including: tax revenue – GEL 11,280.0 million, grants – GEL 448.0 million, other revenues – GEL 850.0 million.

Forecast of tax revenues of 2019 is based on 4.5 percent economic growth and 3.5 inflation rate. In addition, legislative changes, change of tax base, administrative improvements and current economic tendencies were taken into account when forecasting tax revenues. These include:

- Pension reform (GEL -70.0 million);
- Change in tax regime for small businesses (GEL -25.0 million);
- Including LEPLs and other organizations into “Estonian model” (GEL -30.0 million);
- BP’s payment (GEL 140.0 million);
- Abolishing the golden list (GEL 100.0 million);

Budget deficit of 2019 is forecasted at 2.6 percent, which is 0.1 points greater than the deficit of 2018.



During recent years, there has been an increasing tendency in capital expenditure, while current expenditure has been decreasing. Capital expenditure is expected to increase to 8 percent in 2019, while current expenditure decreases to 23 percent. Compensations to employees is forecasted at 3.9 percent (4.1 percent in 2018).

Budget Revenues

Forecast of tax revenues in January-June 2019 was GEL 5 421.5 million, which is 1.3 percent (GEL 71.8 million) less than actual tax revenue.

- Income tax revenue amounts to GEL 1 699.3 million (greater than the forecast by 0.2 percent);
- Profit tax revenue amounts to GEL 470.1 million (greater than the forecast by 12.5 percent);
- VAT revenue amounts to GEL 2 288.4 million (less than the forecast by 3.7 percent);
- Excise tax revenue amounts to GEL 544.2 million (less than the forecast by 16.3 percent);
- Import tax revenue amounts to GEL 34.1 million (less than the forecast by 18.2 percent);
- Property tax income amounts to GEL 34936 million;
- Other tax revenue amounts to GEL 36.2 million.

Automated VAT Refund System

Starting from February 2019, taxpayers will have an opportunity to use fully automated VAT refund system. Automated VAT refund system allows taxpayers to receive their VAT refunds upon submitting declaration using new simplified system.

Starting from January 2019 and onward, evaluation of declarations will be based on automated VAT refund system.

Low risk declarations (at least 90 percent of submitted declarations) will be reflected on VAT refund card on a monthly basis. High risk declarations (at most 10 percent of submitted declarations), in turn, will be reviewed manually. The refundable amount will either be edited or reflected on the refund card unchanged.

VAT refund can be transferred to taxpayer's personal account on the web-portal of Revenue Service Authority by clicking the respective button. The process is fully based on the modern experience of advanced tax organs and risk-based methodology.

Taxpayers were refunded GEL 521 million of VAT refund in 2018.

Government Debt

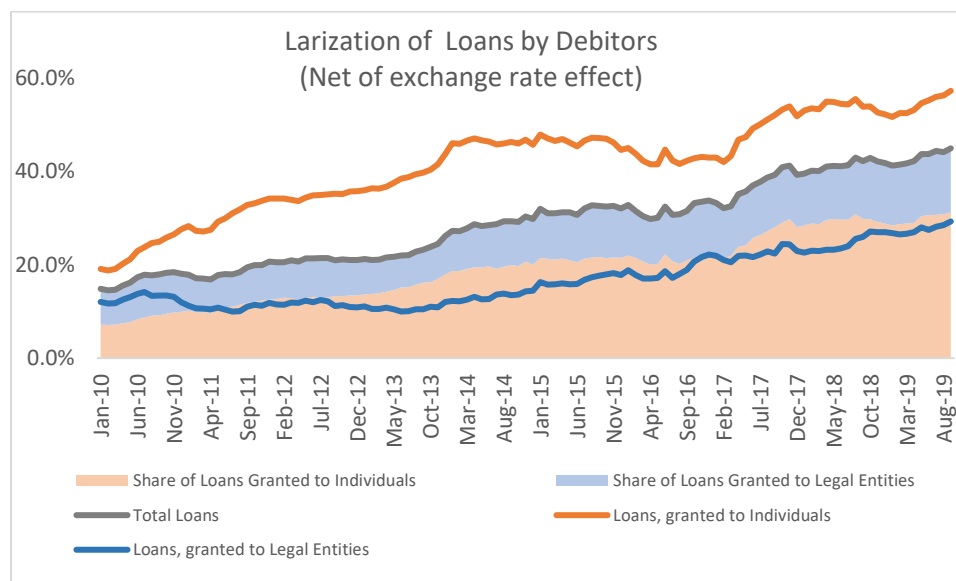
- Government debt was 42.1 percent of GDP as of the end of 2018 (out of which external debt was 34.2 percent of GDP). In 2017 the debt amounted 42.4 percent of GDP (external debt – 34.9 percent of GDP), in 2016 – 42.4 percent of GDP (external debt – 35.1 percent of GDP), and in 2015 – 39.2 percent of GDP (external debt – 32.4 percent of GDP);
- Increase in government debt in 2015 and 2016 was driven by the change in exchange rate;
- Debt to GDP ratio will be stabilized at around 40 percent in the medium run.

There will be increase in issuance of treasury bills along with development of capital market. This will decrease the need for external financing and increase the share of domestic debt in total government debt.

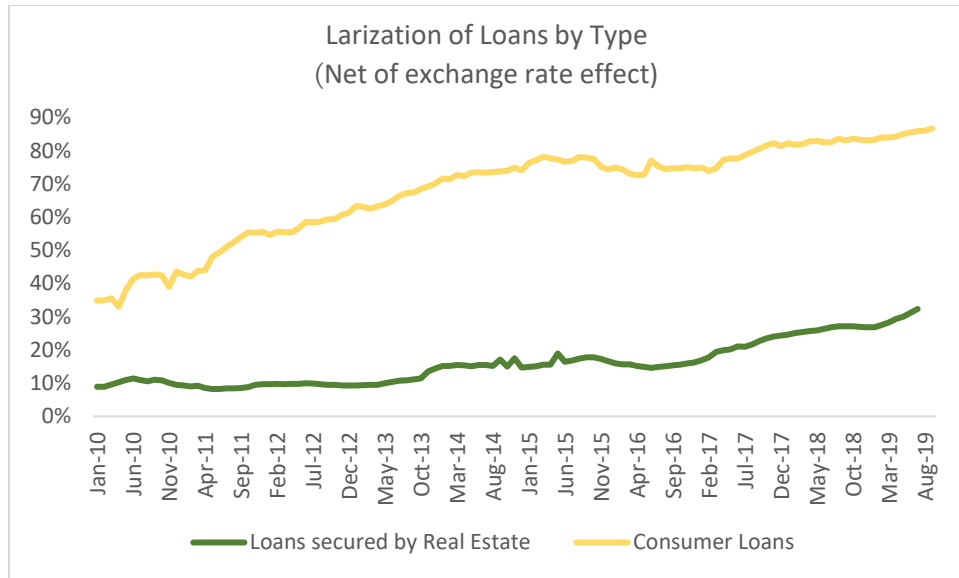
Monetary Sector

Dollarization of the Private Sector

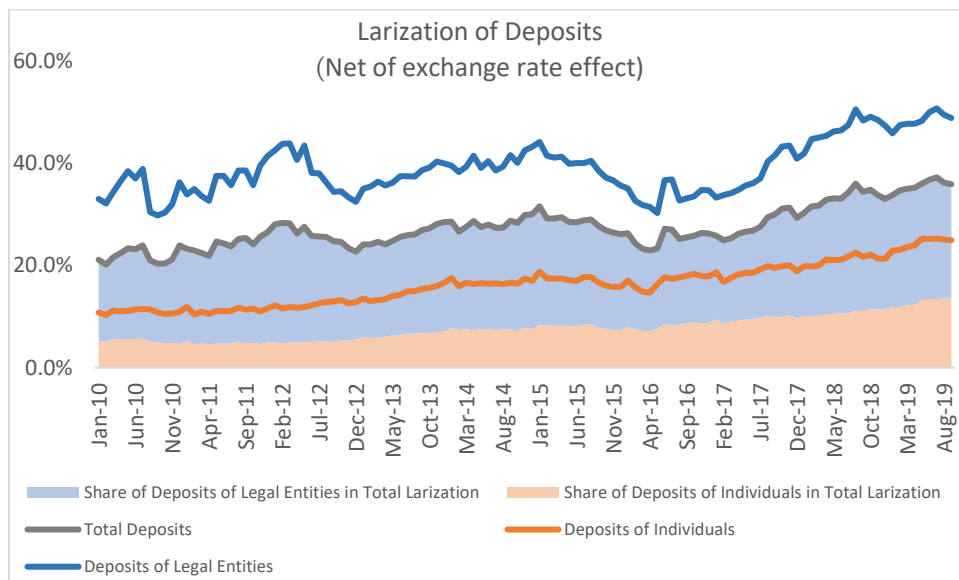
Loan larization has an increasing trend. Larization of total loans is mainly driven by larization of individual loans. As of September 2019, larization of individual loans amounted 57.3 percent, while larization of corporate loans is 29.3 percent. Larization of total loans amounted 45 percent in the given period.



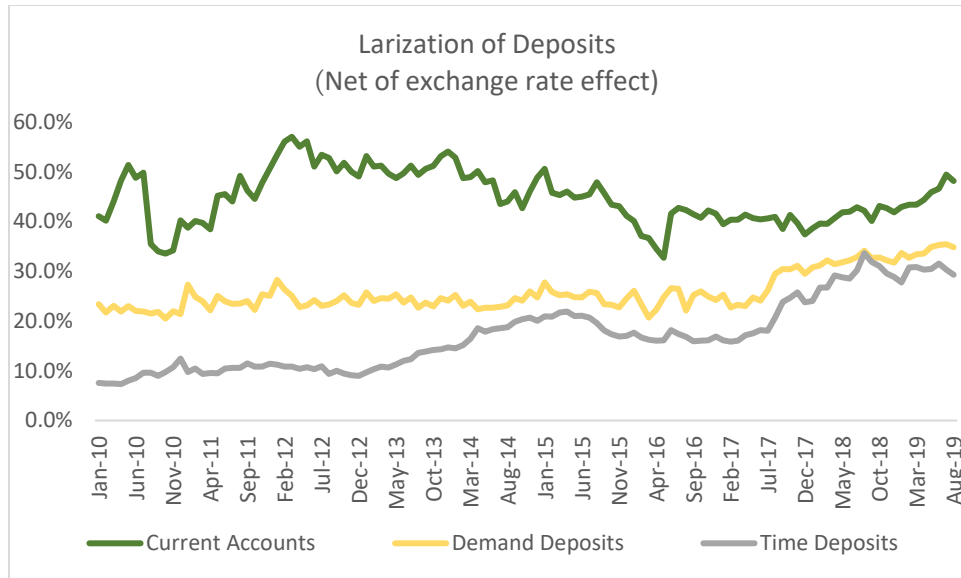
There is an increasing trend of larization of loans secured by real estate as well as consumer loans but the latter is significantly higher than the former. Larization of consumer loans was 86.7 percent in September 2019, while larization of loans secured by real estate increased by 1 percentage points compared to previous month and amounted 33.3 percent in August 2019.



Larization of deposits is mainly driven by corporate deposits. Larization of total deposits was 35.9 percent in September 2019. Larization of deposits of individuals was 24.9 percent during the same period, while larization of corporate deposits decreased by 0.6 percentage points compared to previous month and amounted 48.8 percent.

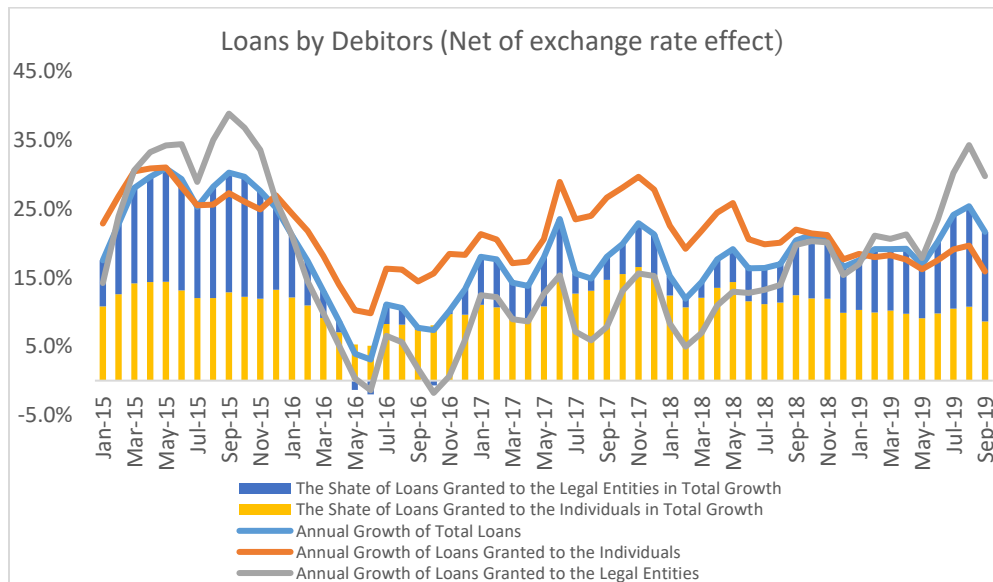


Larization of time deposits increased by 0.5 percentage points compared to previous month and in September 2019 amounted 29.8 percent, in the same period larization of demand deposits was 34.5 percent and larization of current accounts decreased by 1.8 percentage points compared to previous month and amounted 46.4 percent.

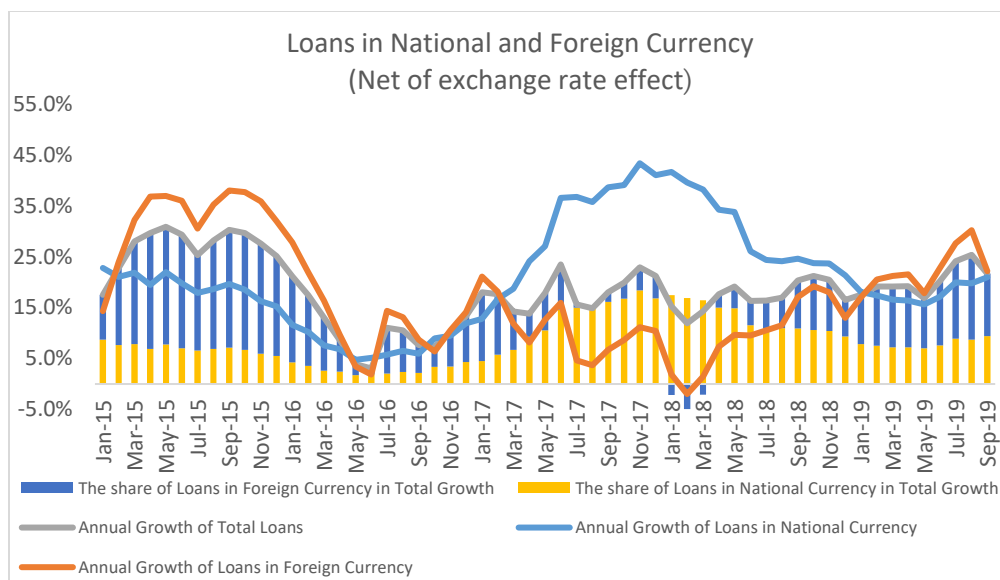


Overview of Loans

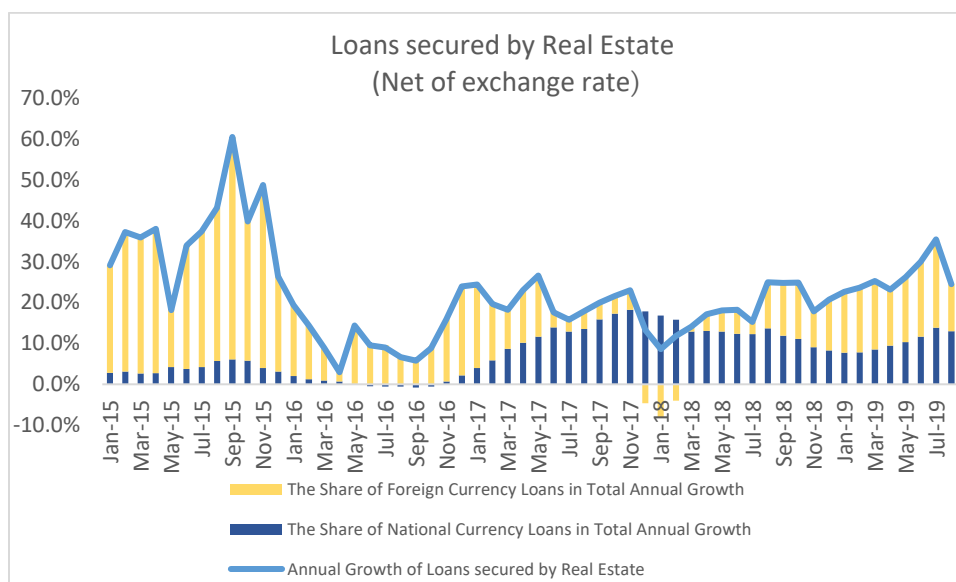
In September 2019, loans granted to individuals increased by 15.9 percent compared to September 2018. In the same period annual growth rate of corporate loans decreased by 4.6 percentage points compared to previous month and amounted 29.7 percent, while annual growth rate of total loans decreased by 3.7 percentage points compared to previous month and amounted 21.7 percent.



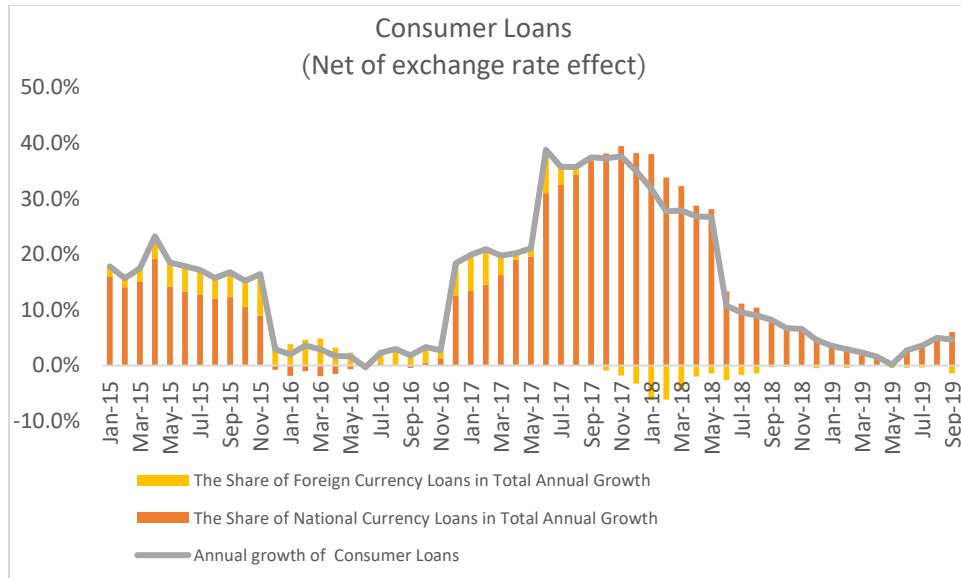
In September 2019, annual growth rate of foreign currency denominated loans decreased by 8 percentage points compared to previous month and amounted 22.2 percent growth compared to the same period of the previous year, while loans in national currency grew by 21 percent. Total loans grew by 21.7 percent. Since 2018 contribution of foreign currency loans growth in total growth is increasing.



In August 2019, annual growth of loans secured by real estate was 24.5 percent, it is important to note that compared to previous month it decreased by 11 percentage points. Since 2018 contribution of foreign currency loans growth in total growth of loans secured by real estate is increasing.

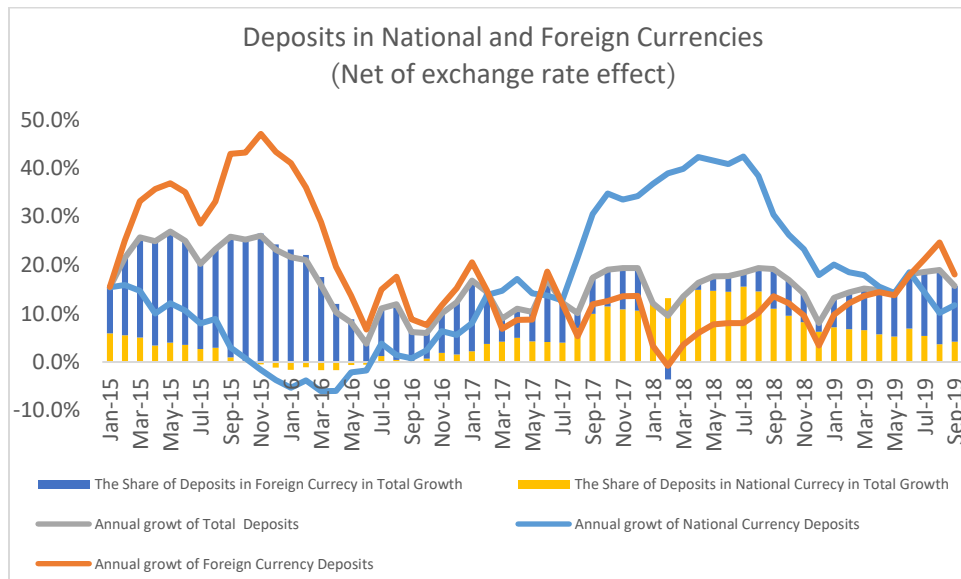


As for consumer loans, in August 2019, the annual growth rate decreased by 0.3 percentage points compared to previous month and amounted 4.6 percent. Since 2017 increase in consumer loans was mainly driven by growth of loans denominated in national currency.

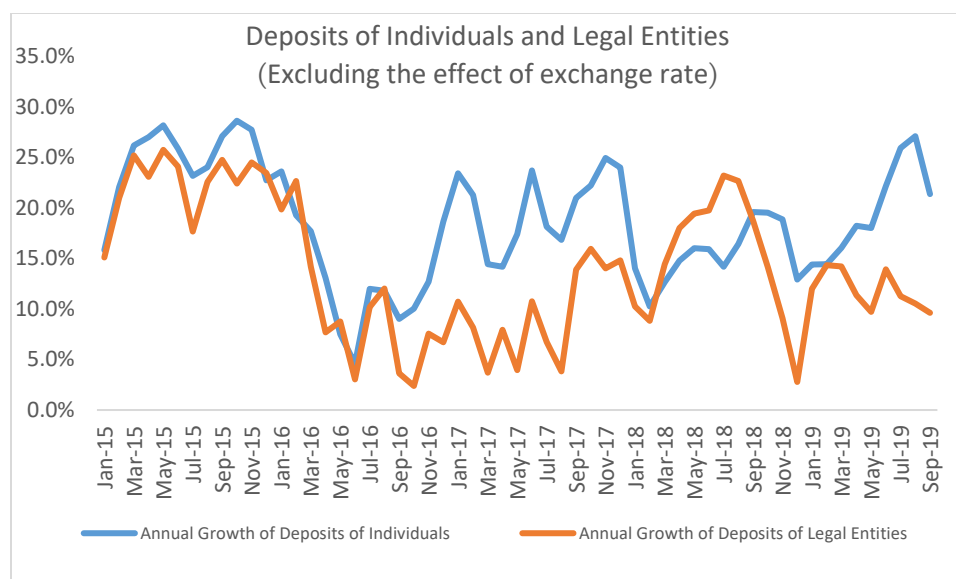


Overview of Deposits

In September 2019, the annual growth rate of national currency denominated deposits increased by 1.6 percentage points compared to previous month and reached 11.7 percent, while deposits in foreign currency grew by 18 percent compared to the same period of 2018, annual growth rate of total deposits was 15.7 percent.



In September 2019 annual growth rate of deposits of individuals decreased by 5.7 percentage points compared to previous month and reached 21.4 percent, while annual growth rate of deposits of legal entities in the same period amounted 9.6 percent.



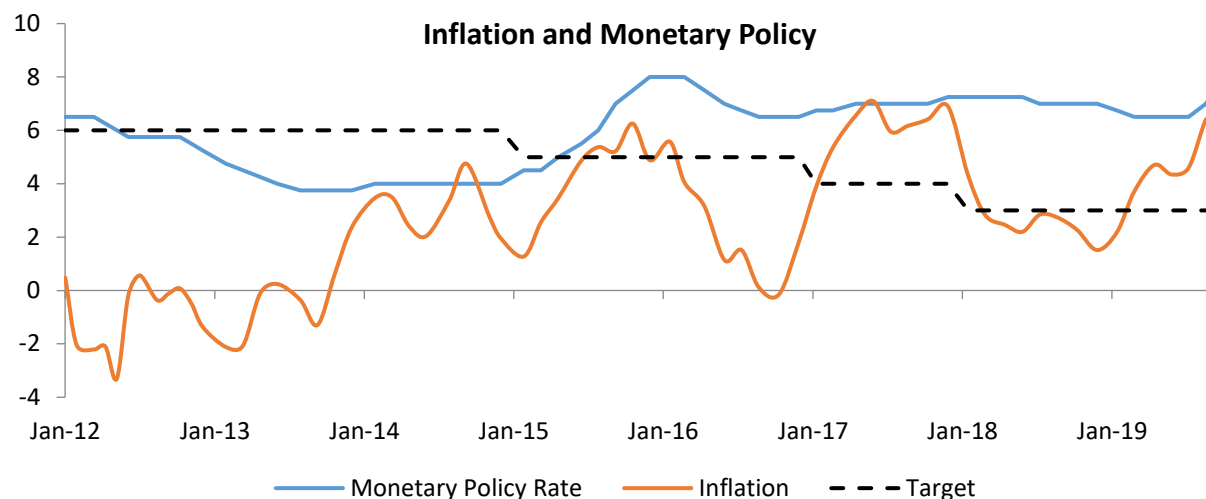
Monetary Policy Rate

Monetary policy rate was at 7.50 percent at the end of September. The Monetary Policy Committee cut the refinancing rate from 7.0 percent by 25 basis points on January 30 and then on March 13 by 25 basis points. The main reasons were: the weakening risks coming from the external risks and weak demand-side inflation pressure. National Bank of Georgia was planning to gradually ease monetary policy, but the pass through of the exchange rate depreciation to inflation increased in recent periods and inflations stood above the target, so in September 2019 the Monetary Policy Committee of the National Bank of Georgia decided to raise refinancing rate by 0.5 percentage points twice, on September 4, from 6.5 to 7 percent, and on September 25 at extraordinary meeting, from 7 to 7.5 percent. Policy tightening is expected to continue until the pressure on the exchange rate are eliminated.

The Monetary Policy Committee increased the policy rate by 25 basis points three times in 2017, which was explained by the increase in excise taxes as well as worsening of nominal effective exchange rate, which affected the inflation pressure. According to NBG, together with the increase in global oil prices, inflation expectations have also risen and larger than expected improvement in economic activity decreased the downside pressure on inflation coming from demand side. Therefore, the Committee decided to increase the policy rate. Once the impact of those factors has faded out, the inflation was expected to decrease from the beginning of 2018, which has happened.

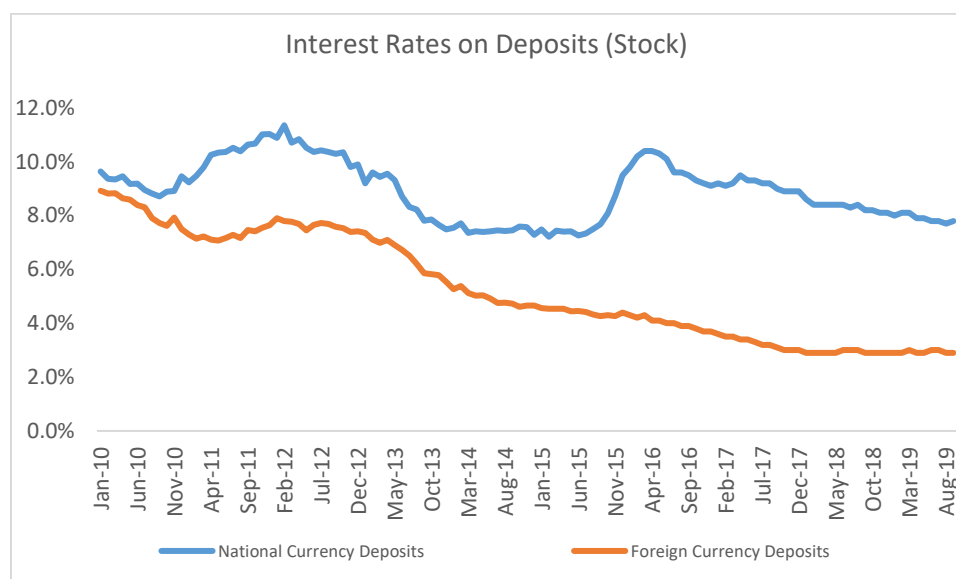
Starting from January 2018, the Monetary Policy Committee kept the refinancing rate unchanged at 7.25 percent, which was mainly derived by nominal effective exchange rate appreciation and the fact that aggregate demand remained below its potential level which has a downward pressure on inflation.

On July 25th 2018 monetary policy committee has cut the refinancing rate by 25 basis points, to 7.0 percent. The main reasons were: decline in annual inflation, which is close to the target level; higher than expected appreciation of nominal exchange rate, which reduced inflationary pressure. Monetary policy easing will continue at a slower pace than expected due to the recent improvement in aggregate demand and faster than expected closing of the output gap, which declined downward pressure on inflation.

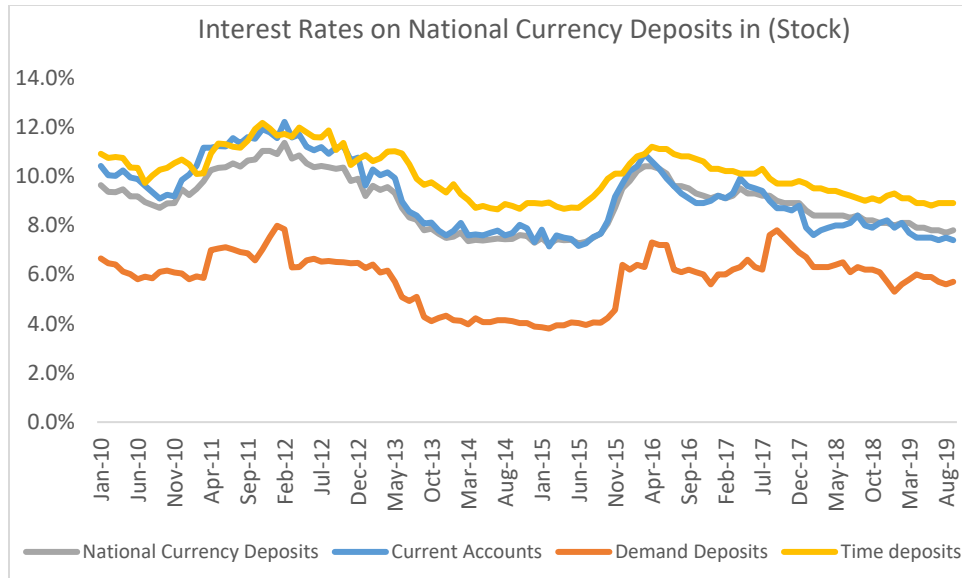


Interest Rates

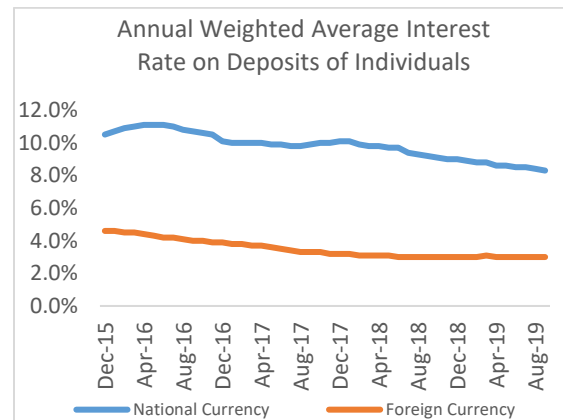
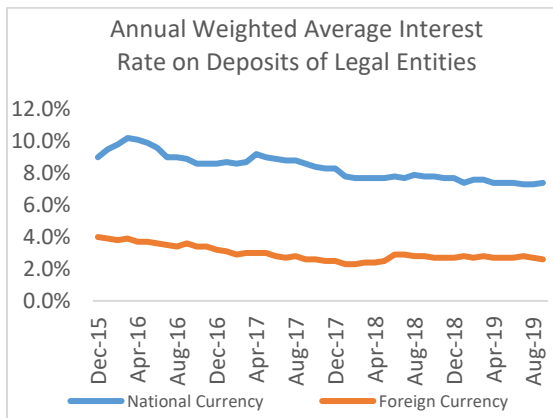
Interest rate on local currency deposits in September 2019 reached 7.8 percent, while on foreign currency deposits it was 2.9 percent.



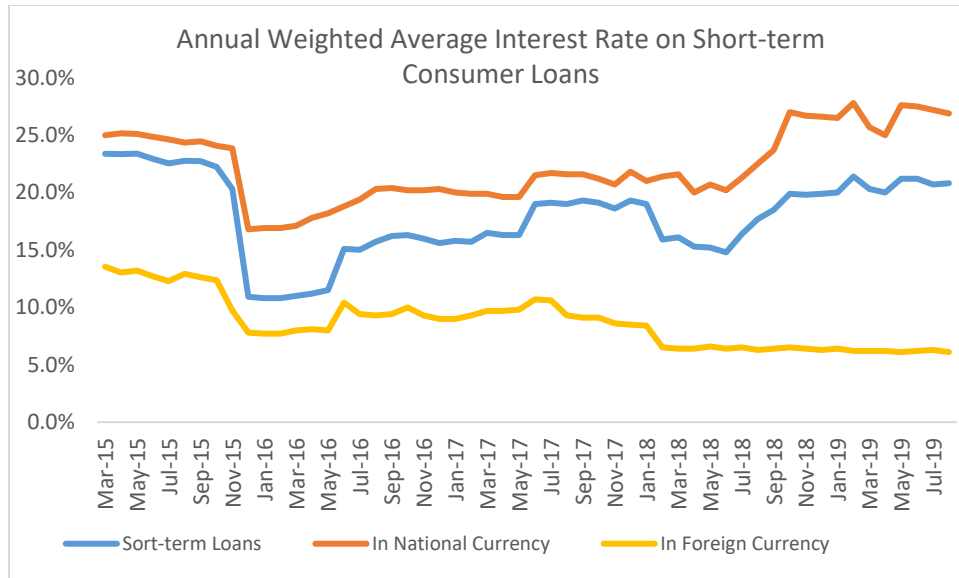
In September 2019, interest rate on current accounts denominated in local currency changed insignificantly compared to previous month and amounted 7.4 percent. During the same period, interest rate on time deposits was 8.9 percent, while on demand deposits it was 5.7 percent.



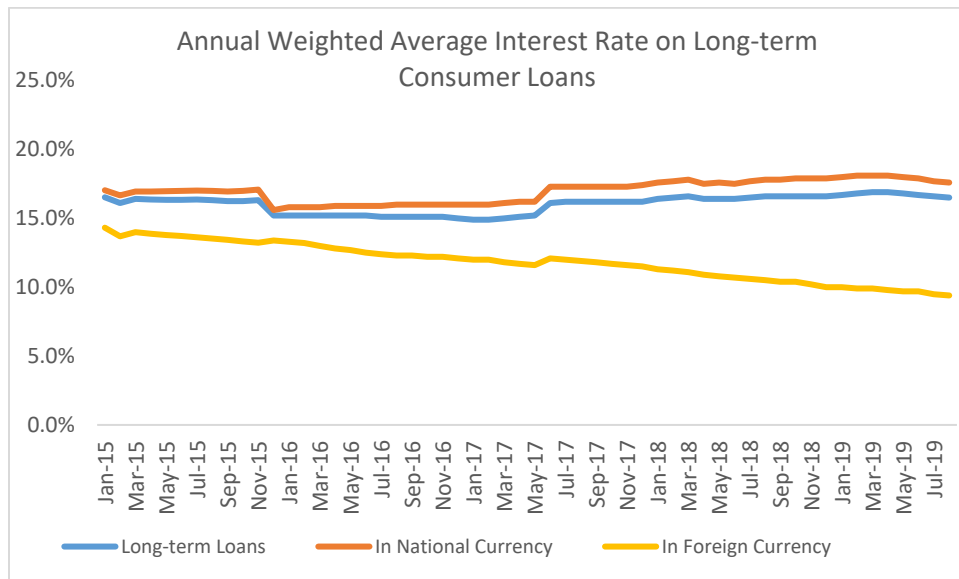
In September 2019, annual weighted average interest rate on national currency deposits of legal entities reached 7.4 percent, while on foreign currency deposits it was 2.6 percent in the same period. As for deposits of individuals, annual weighted average interest rate on national currency deposits reached 8.3 percent, while in foreign currency it was 3 percent.



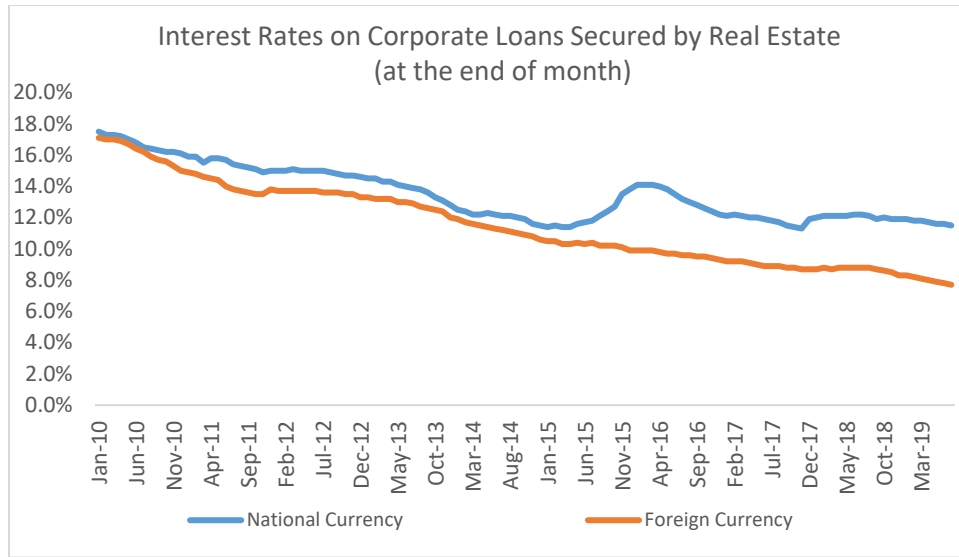
In September 2019, annual weighted average interest rate on short-term consumer loans reached 21.1 percent. In the same period annual weighted average interest rate on short-term consumer loans in national currency was 26.9 percent, while on foreign currency loans it was 6.1 percent.



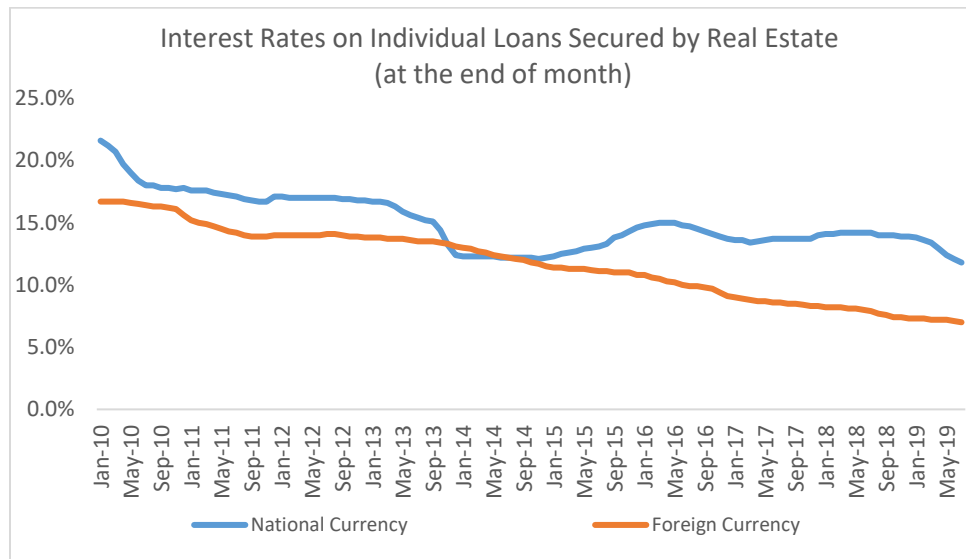
Annual weighted average interest rate on long-term consumer loans was mainly determined by national currency loans. In September 2019 it reached 17.5 percent on national currency loans, 9.4 percent on foreign currency loans and 16.4 percent on total long-term consumer loans.



At the end of August 2019 interest rate on corporate loans secured by real estate denominated in local currency was 11.5 percent, while on foreign currency loans is was 7.6 percent.



In the same period interest rate on national currency individual loans secured by real estate decreased by 0.2 percentage points compared to previous month and amounted 11.6 percent, while in foreign currency it reached 7 percent.



State Securities Market

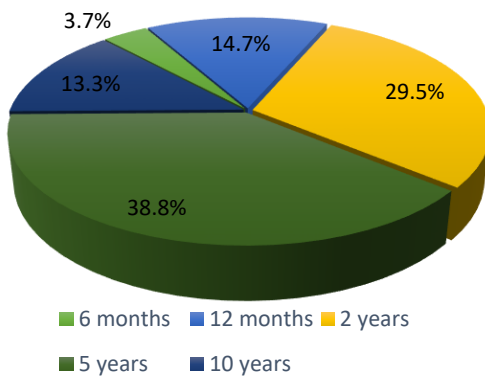
In September 2019, 4 auctions were held with total issuance volume of 170 million GEL. The weighted average interest rate amounted to 7.525%.

There were issued treasury bills with maturities of 6 months and 12 months; Treasury bonds with maturities of 2 years and 5 years. Treasury securities with total amount of 60 million GEL were redeemed.

	6M	12M	2Y	5Y	Total
Issuance Volume	20	40	60	50	170
Average weighted interest rate	7.021	7.055	7.414	8.235	7.525
Redemption	20	40	0	0	60
Difference	0	0	60	50	110

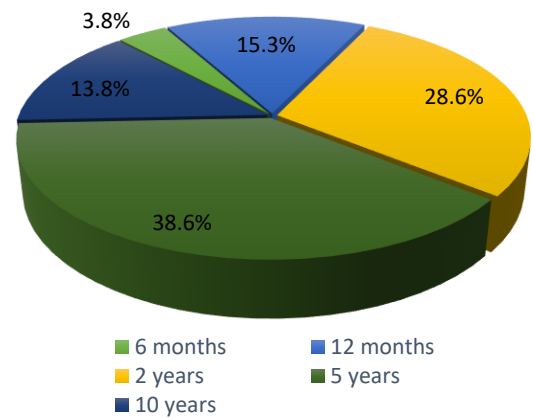
The structure of treasury securities portfolio has changed slightly:

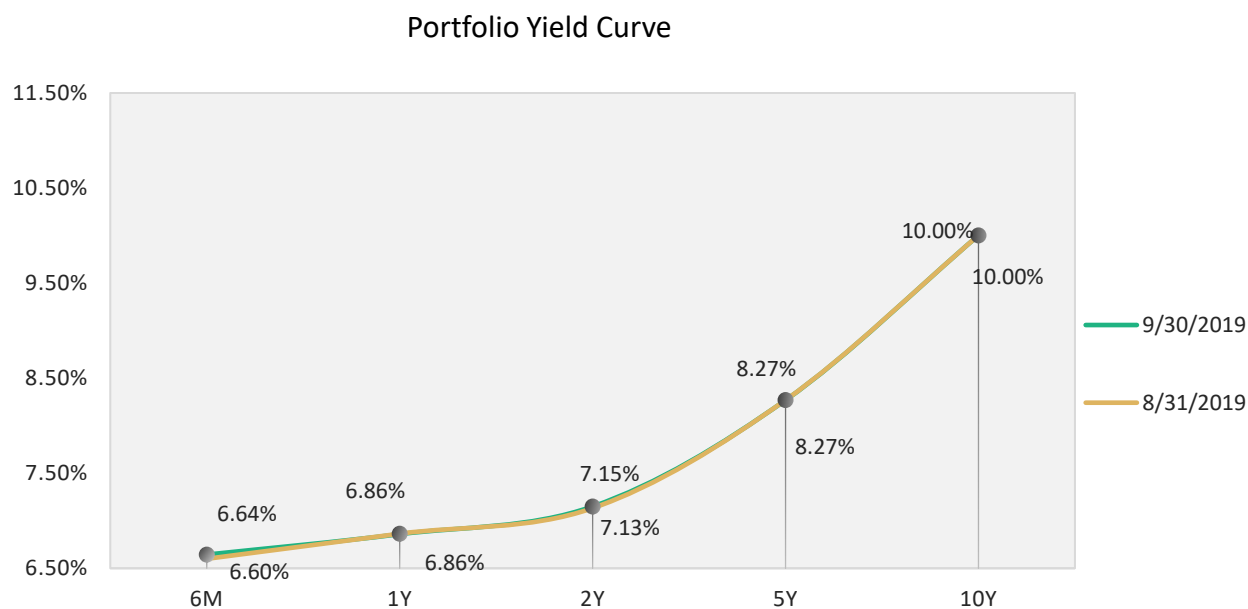
Portfilio Structure as of 31.09.2019



The portfolio yield has slightly changed.

Portfilio Structure as of 31.08.2019



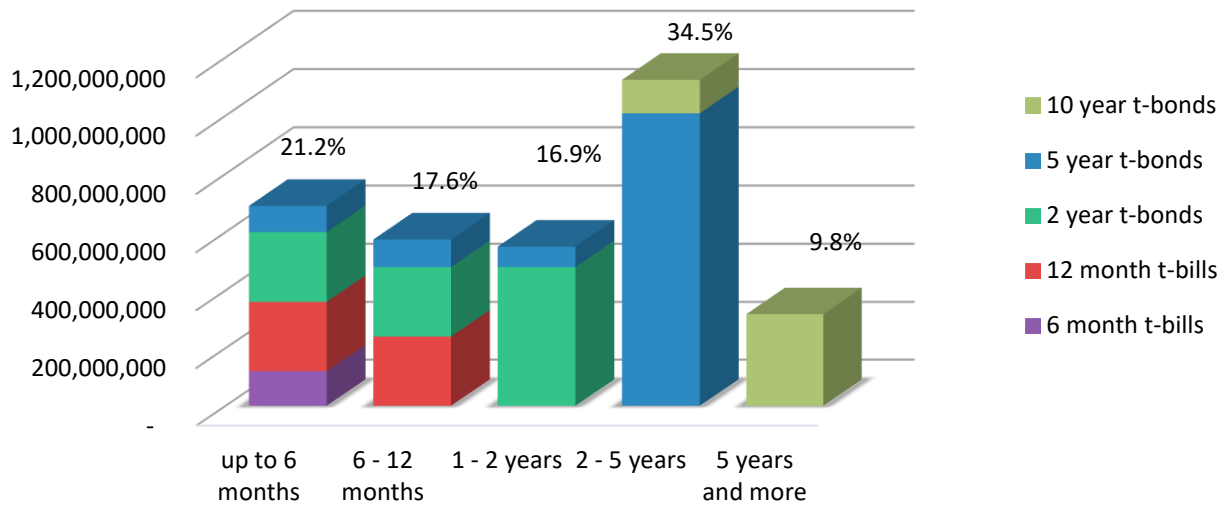


Average Time to Maturity (ATM) for all securities forming the portfolio has decreased compared to the previous month's value.

Average Time To Maturity (Years)			
2019	July	August	September
6 month t-bills	0.24	0.24	0.24
12 month t-bills	0.47	0.47	0.47
2 year t-bonds	1.09	1.04	0.92
5 year t-bonds	3.06	3.04	3.03
10 year t-bonds	6.98	6.41	6.33
Total	2.48	2.43	2.37

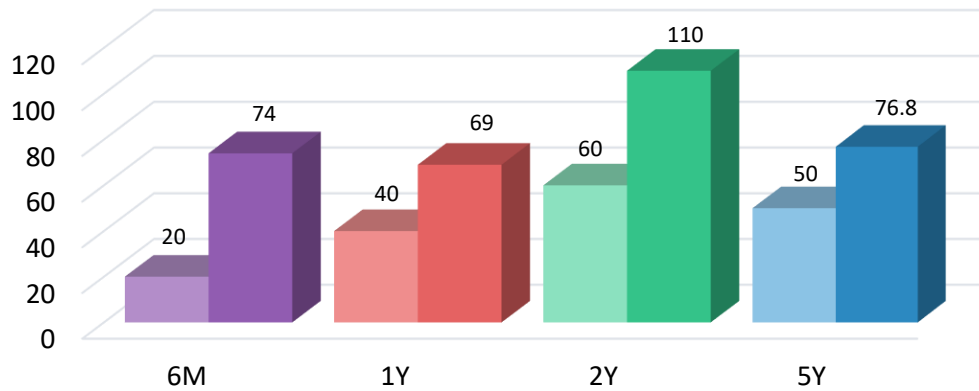
As of September 30, 2019, 38.8% of treasury securities portfolio is composed of securities whose maturity date is due for the next 1 year. Securities' distribution by time to maturity is shown below:

Portfolio Forming Securities Composed by Time to Maturity

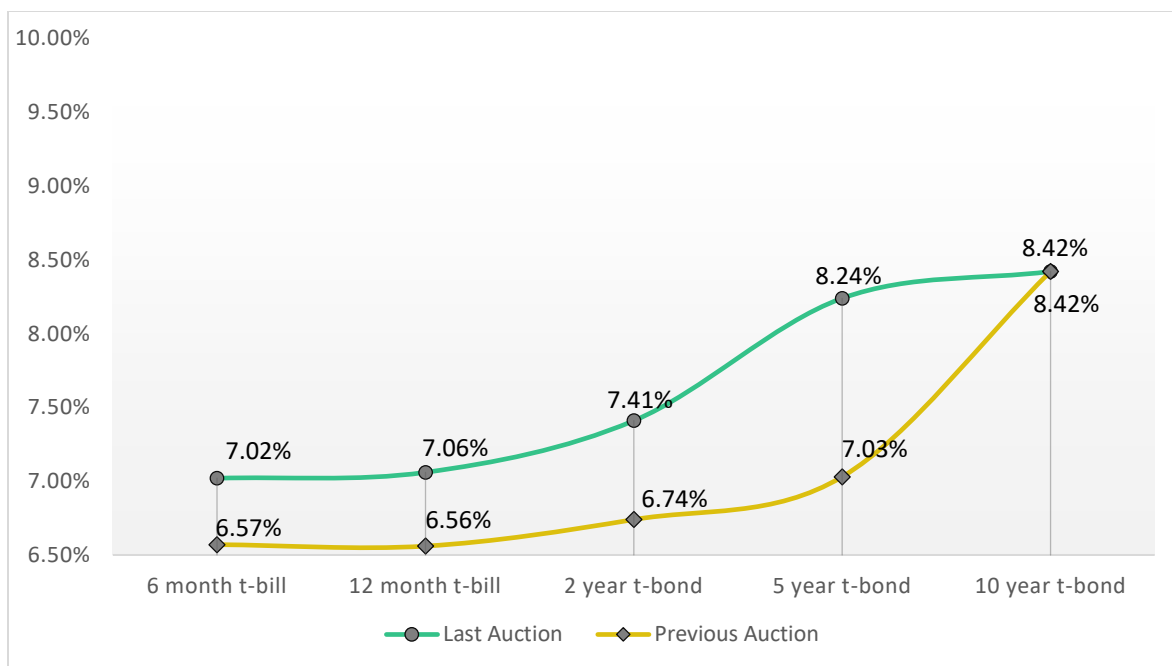


Bid-to-cover ratio has decreased compared to the previous month's value (August 2.09) and is 1.94.

Issuance and Demand
million GEL



Weighted average interest rates from the last month's auctions: *



*- If there was not issued any of the given maturity securities in the last month, previous results will be shown on the chart instead.

Credit Ratings

Georgia continues to cooperate with the international rating companies Standard & Poor's, Fitch and Moody's. The country not only maintains stable ratings, but improves it as well. Based on evaluation of 2019, Fitch has increased Georgia's sovereign rating outlook from "BB-" positive to "BB" stable. Given increase was mainly driven by high economic growth and low government debt compared to BB country group; also, by significant improvement in current account deficit and fiscal sustainability. Country perspective has improved by Standard & Poor's in 2019 and according to their evaluation, Georgia has "BB-" positive rating from stable "BB-". Georgia has "Ba2" stable rating according to Moody's evaluation. On the other hand, there was a deterioration of the ratings in the countries of the region, credit ratings have started to improve in neighbor countries from the end of 2017. However, in 2018, there was a significant deterioration of Turkey's credit rating.

According to Fitch and S&P, Azerbaijan's credit rating is "BB+" stable, while according to Moody's, rating is "Ba2" stable. S&P and Fitch worsened ratings of Azerbaijan in 2016 and changed from "BBB+" to "BB+" negative. However, outlook has improved from negative to stable at the beginning of 2018 according to both companies. Moody's decreased the rating from "Baa3" to "Ba1" in 2016 and from "Ba1" to "Ba2" in the previous year.

According to Fitch, Armenia's current rating is "B+" positive, while according to Moody's the rating is "Ba3" stable. Moody's has decreased rating of Armenia from "Ba3" negative to "B1" stable in 2016, while in 2018 outlook has improved from stable to positive and in August 2019 it improved to "Ba3" stable.

S&P and Moody's deteriorated Russia's credit rating and Compared to 2014, Russia's credit rating deteriorated from "Baa1" to "Ba1" according to Moody's and from "BBB-" to "BB+" according to S&P. According to S&P, Russia's credit rating now is at "BBB-" stable, according to Moody's Russia's rating is improved to "Baa3" with stable outlook, while in August 2019 it improved from "BBB-" positive to "BBB" stable according to Fitch.

Turkey credit rating is "BB-" negative according to Fitch, „B+“ stable according to S&P and „B1“ negative according to Moody's. Moody's decreased rating of Turkey from "Baa3" to "Ba1" in September 2016 and from stable to negative in March

2017. In 2018, the rating has deteriorated to “Ba2” and then to “Ba3” and finally in June 2019 it decreased to “B1” negative. S&P decreased Turkey’s rating from “BB+” to “BB” in 2016, to “BB-” in 2018 and later to “B+” stable, while Fitch decreased the rating from “BBB-” to “BB+” and then to “BB” negative and in July 2019 it reached current level of “BB-” negative.

Georgia’s rating upgrade and stable outlook are supported by rating agencies’ view that the Georgian economy has shown strong resilience towards shocks that started in 2014 and the country demonstrated its economic and institutional strength. Furthermore, ongoing economic reforms supported by the International Monetary Fund will mitigate some of Georgia’s underlying credit weaknesses further boosting credit strength over time. However, external vulnerability risks continue to constrain the rating.

Ongoing economic reforms are positively perceived by Moody’s: “Credible new reforms will further support credit strength”. The 3-year program with IMF has improved credibility of the reforms:

“The program emphasizes structural reforms to generate higher and more inclusive growth. The focus will be on improved education, road infrastructure investment, more efficient public administration, and further improvements in the business climate to boost the private sector’s role as a growth driver.”

Moody’s emphasized following positive factors including strong institutions and agreement with EU, diversified export markets and trade agreements, which will facilitate maintaining FDI to GDP ratio at 10 percent on average, increase export in the medium run and accelerate economic growth.

S&P emphasizes the following factors as the main positive movements in Georgia: structural reforms, strong institutional framework, economic growth, improvement of international trade conditions and current IMF program.

According to Fitch report about the rating of Georgia, positive contributors of rating were: high economic growth, significant improvement in current account deficit, strengthening of fiscal sustainability. Fitch positively evaluates ongoing cooperation with the International Monetary Fund. According to the rating agency, current progress is meeting benchmarks aimed at strengthening of financial sector and will contribute towards further improvement of structural indicators and stimulating investment and savings.

The main weaknesses of Georgian economy remain high Dollarization and external vulnerability. Nevertheless, Larization process is positively assessed by rating agencies. Saving promoting reforms are encouraged by the agencies and reduction of saving-investment gap is considered as potential for improving ratings further.

Overall, despite the deteriorated economic environment in the region, Georgia has maintained stable outlook and improved credit rating, which is the result of the correct policy (flexible exchange rate, inflation targeting, counter-cyclical fiscal policy, removal of trade barriers and export diversification, agreement with EU), low risks and medium-term perspectives.

Cooperation with the International Monetary Fund

On April 12 of 2017, the IMF Executive Board Approved USD 285.3 million Extended Arrangement under the Extended Fund Facility for Georgia.

The IMF shares and welcomes the economic policies of the Government of Georgia that ensure sustainable economic growth for the country. The program is based on the Government’s new four-point reform agenda. Within the program, the IMF will be Georgia’s partner in carrying out Government’s economic policies.

The economic and structural reforms approved by IMF aim to support macroeconomic stability and economic growth.

2019 budget, as well as the government’s medium-term budgetary plans, qualitatively represent continuation of the fiscal policy developed by the government and includes:

- Reducing administrative costs;
- Creating tax-system customized to economic growth;
- Increasing effectiveness of the budget programs;
- Increasing investments in infrastructure projects.

During 2017-2020, the country's road infrastructure backbone will be finished, which will allow full utilization of logistical and touristic potential. Development of infrastructure will improve communication between the regions, which will increase their involvement in country's economic development.

During 2017-2020, capital expenditures foreseen under the budget will increase from 5.6 percent of GDP to 9 percent of GDP. Meanwhile, administrative costs will be reduced from 26.5 percent to 21.7 percent.

Government of Georgia plans to carry out the most important structural reforms within the program that will support economic growth. Reforms include:

- Pension Reform;
- Capital Market Reform;
- Establishment of Deposit Insurance System;
- Establishment of Public-Private Partnership (PPP) System;
- Establishment of insolvency legislative framework;
- Land Reform;
- Insurance System Reform;
- Measures for improving the Public Finance Management;
- Others.

The decision of the Government of Georgia is to return the Financial Sector Supervision function to the National Bank of Georgia.