MINISTRY OF FINANCE OF GEORGIA

CURRENT ECONOMIC OUTLOOK

3/1/2019

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 (p. 35);

The current account deficit has improved to 7.7 percent in 2018. 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 4.7 percent in 2018 (p.4);

Unemployment rate has decreased by 1.2 points and reached 12.7 percent (p.10);

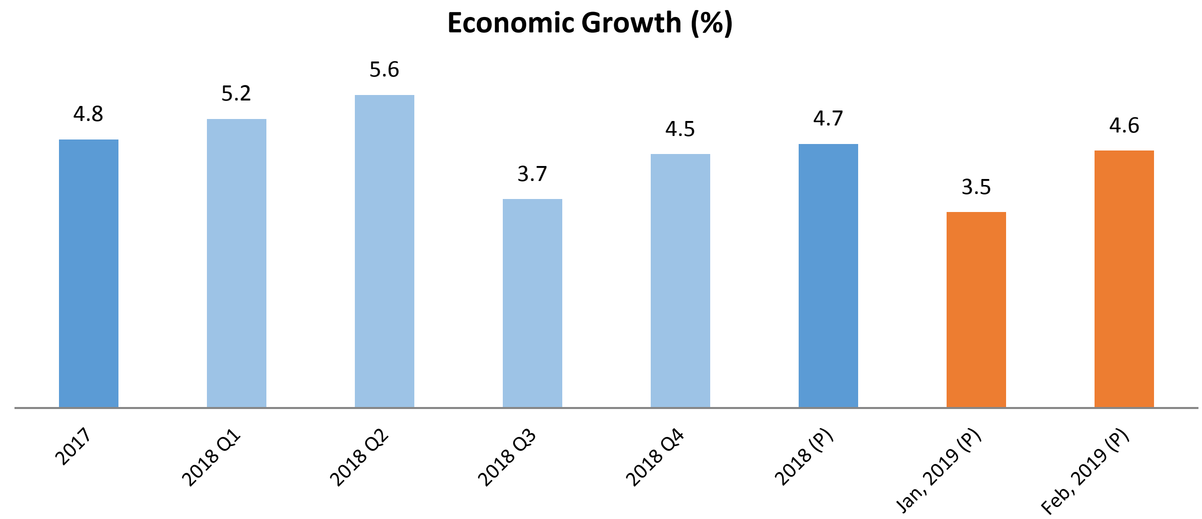
Fully automated VAT refund system started operating in February 2019 (p.22).

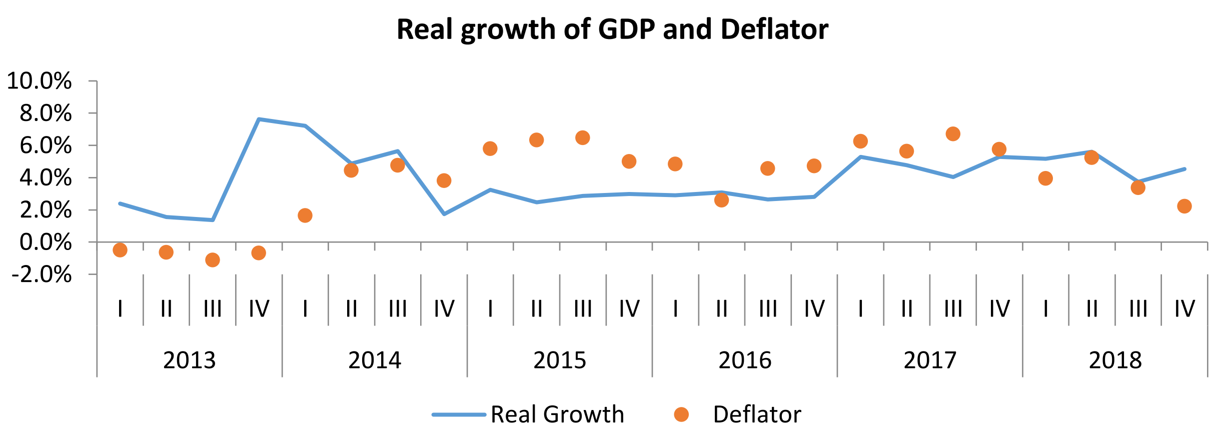
Real Sector

Gross Domestic Product

Economic growth

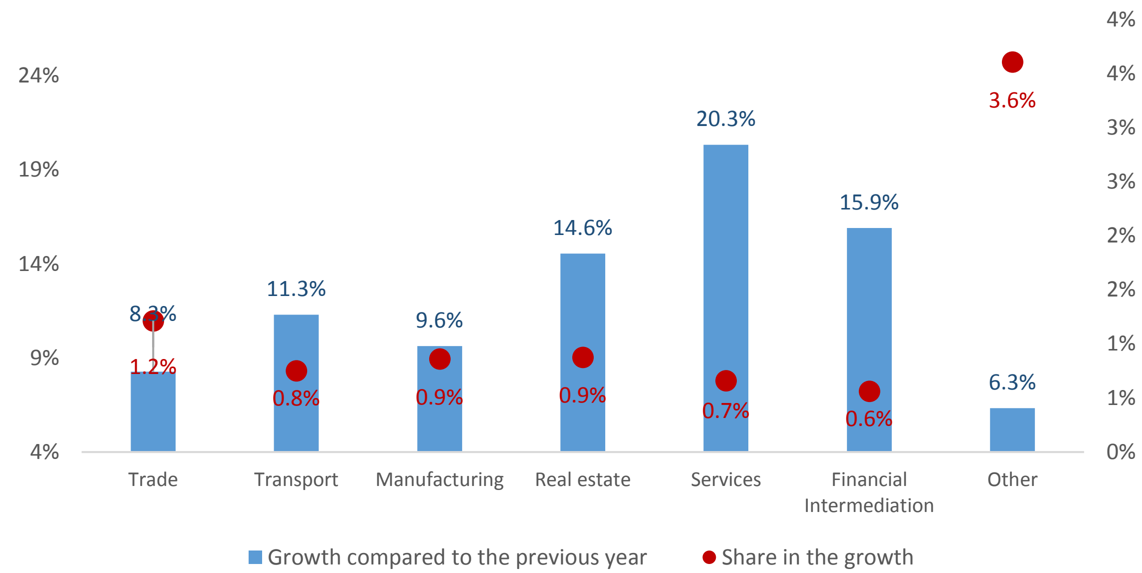
2018 started with increased economic activity. Economic growth was 5.2 percent in the first quarter, 5.6 percent in the second quarter, 3.7 percent in the third quarter and 4.5 percent in the fourth quarter. According to the preliminary estimation, economic growth in 2018 is 4.7 percent. Economic growth in January is 3.5 percent and in February – 4.6 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.

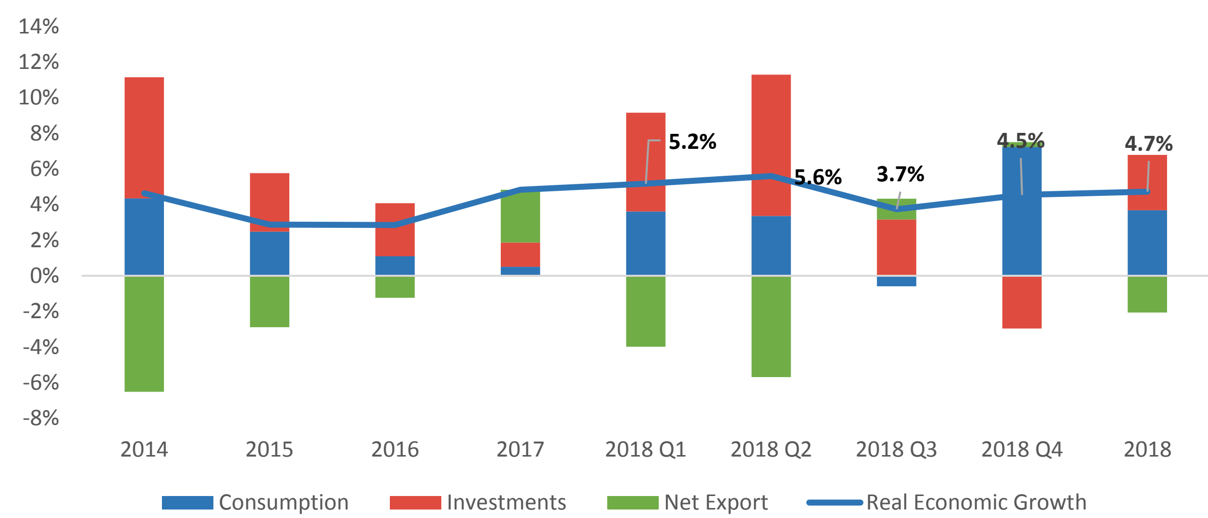
Growth of Sectors (2018)



The structure of economic growth

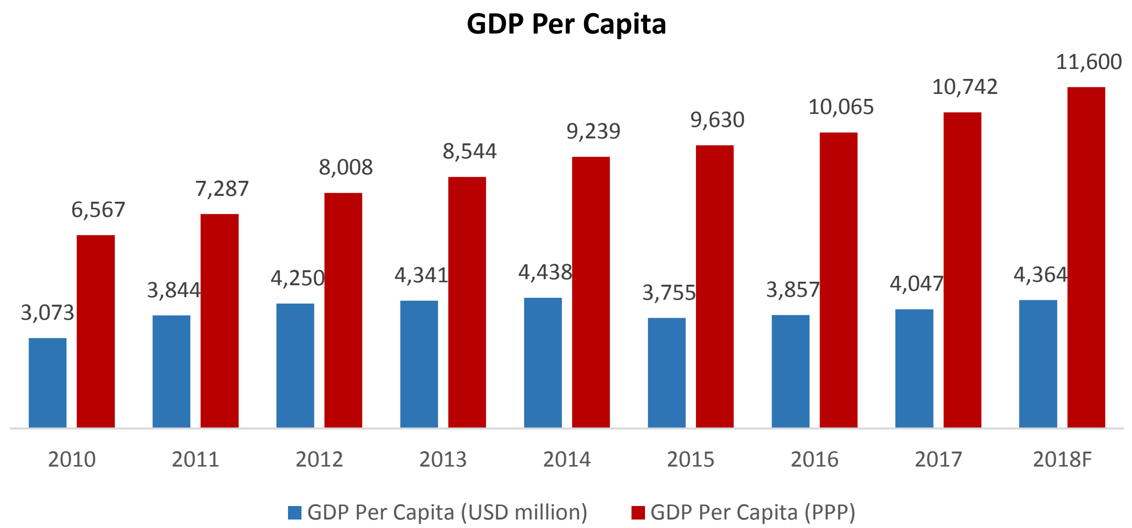
Investments and changes in inventories were the main contributors to the economic growth during 2018. The share of net exports in economic growth in the first half of 2018 was negative compared to the same period of 217 and was a result of significant increase in imports relative to exports. In the third 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 (3.1 percent), while share of net export was negative. 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



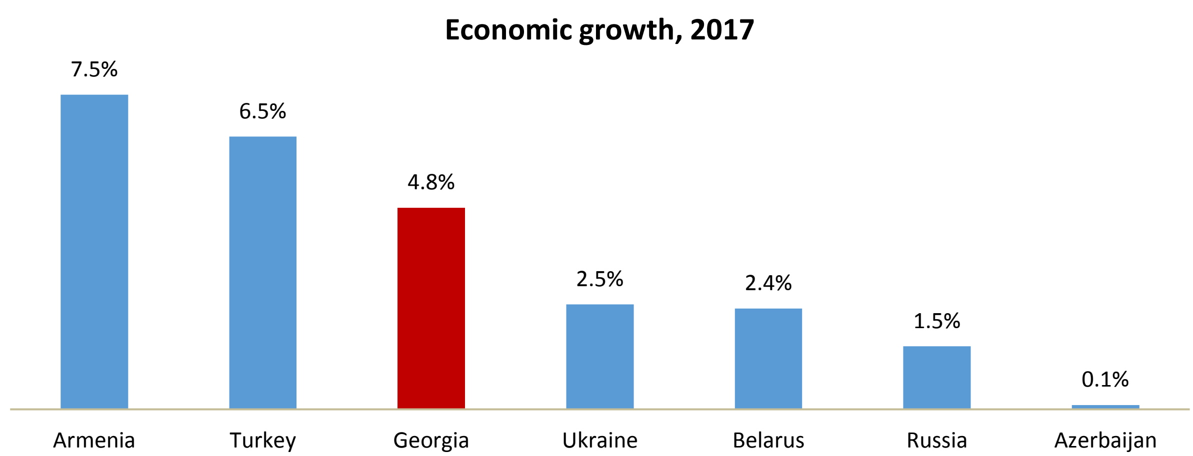
Gross Domestic Product per capita

GDP per capita has an increasing trend. According to the preliminary projections, GDP per capita was GEL 11,059 (USD 4,364 million) in 2018. According to the IMF estimations, GDP per capita in PPP is USD 11,600.

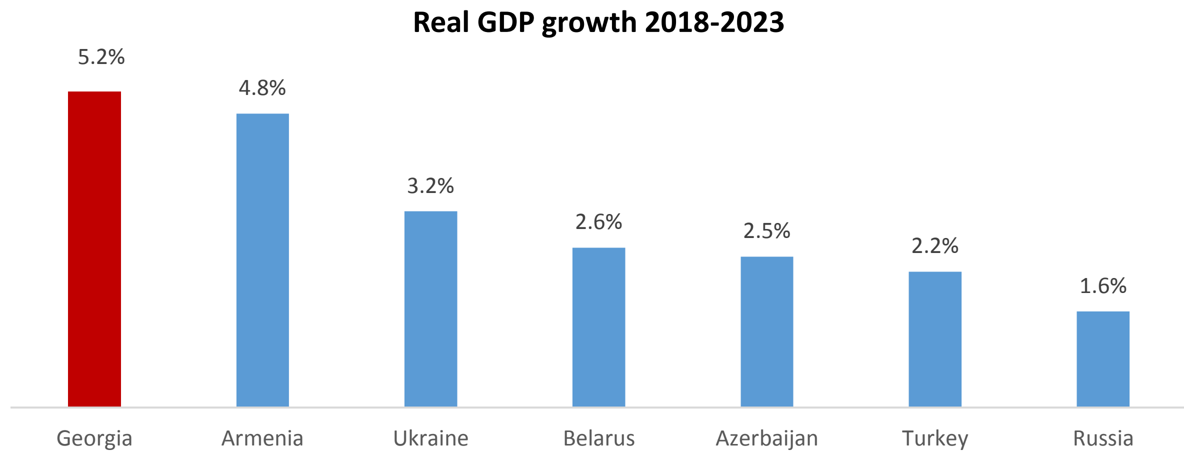


Economic growth in Georgia and neighboring countries

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. 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 continue being the leading country in the region in terms of economic growth in the medium run. Forecast of economic growth is 5.2 percent during 2018-2023, which is higher than region countries.

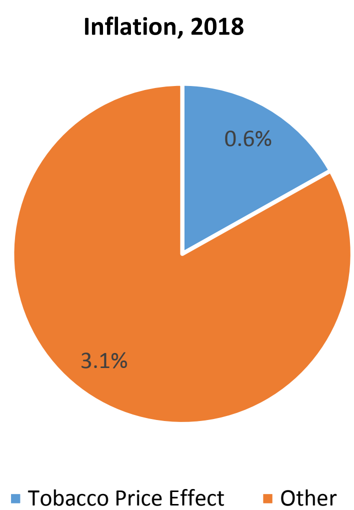


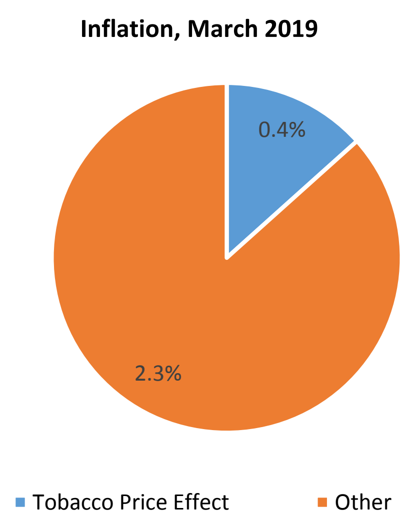
Prices

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 March of 2019, inflation was 3.7 percent (higher than the target) compared to the same period of 2017. Core[1] inflation was at 3.5 percent.

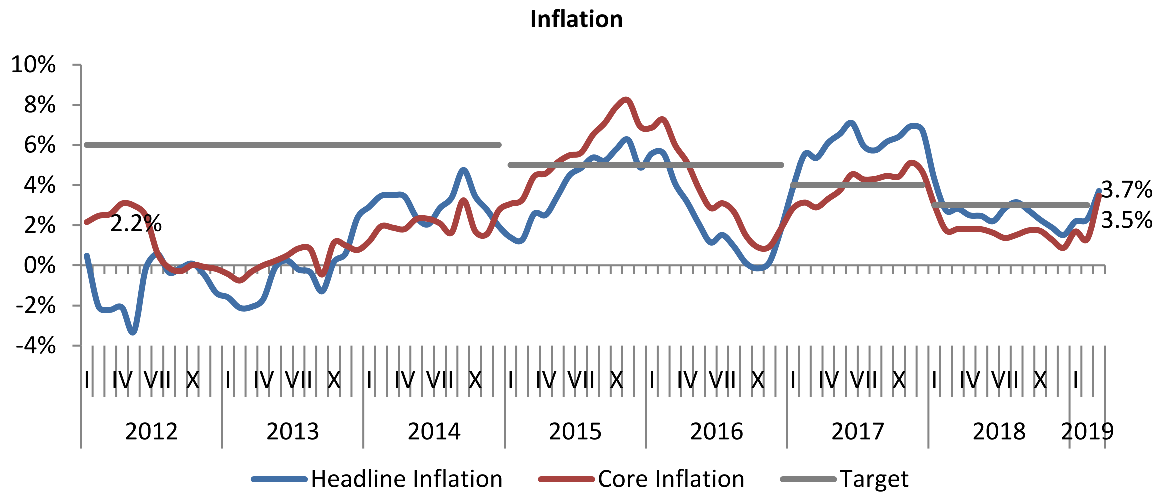
Average annual rate of inflation in 2018 was 2.6 percent, which is lower than the target of 3 percent. As for 2017, annual rate of inflation was 6.0 percent, higher than the target of 4 percent. However, the deviation from the target was attributed to one-off factors related to the change in the excise 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 March of 2019 a mounts to 0.6 points of inflation.



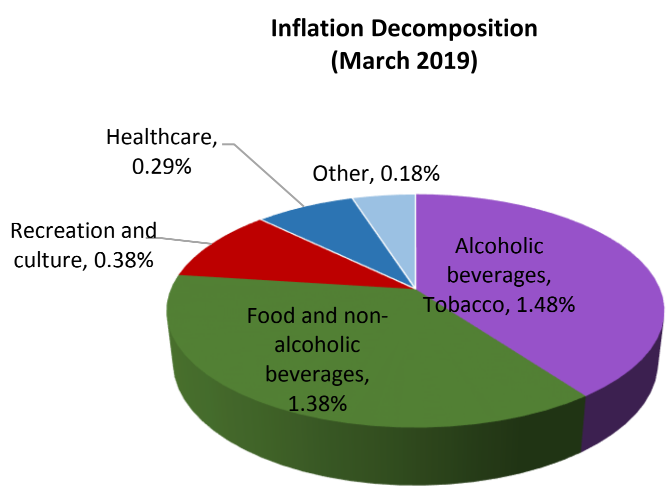


[1] Inflation excluding food and energy prices



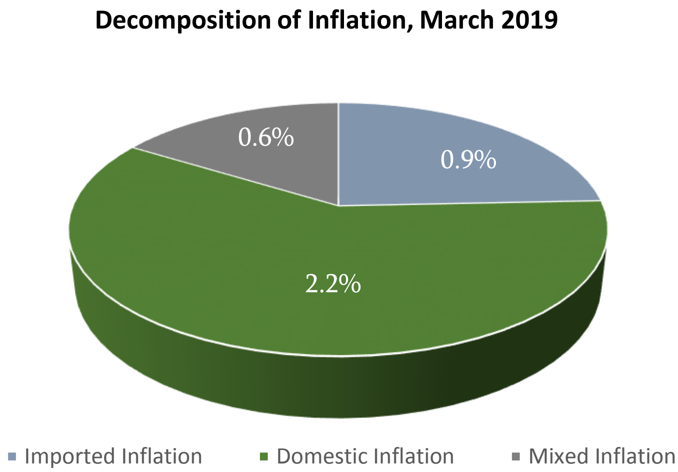
Price change on the following groups[2] of products contributed to formation of yearly inflation in March 2019:

- Food and non-alcoholic beverages: the prices within the group increased by 4.8 percent, contributing 1.5 percentage points to the overall annual inflation rate. Within the group the prices were higher for the following subgroups: vegetables (19.8 percent), fish (12.9 percent), bread and cereals (10.9 percent), meat (4.2 percent), also mineral waters, soft drinks, fruit and vegetable juices (3.5 percent). Meanwhile, the prices decreased for fruit and grapes (-23.3 percent);
- Alcoholic beverages and tobacco: the prices increased by 20.8 percent, with a relevant contribution of 1.36 percentage points to the overall annual CPI growth. The prices increased for tobacco (43.7 percent);
- Recreation and culture: the prices went up by 6.7 percent, contributing 0.38 percentage points to the overall annual inflation rate. The prices in the group increased for recreational and cultural services (7.1 percent). Meanwhile, the prices decreased for audio-visual, photographic and information processing equipment (-5.0 percent);
- Health: the prices increased by 3.6 percent, which resulted in a 0.3 percentage point contribution to the overall annual inflation rate. The prices were higher for the following subgroups: out-patient services (3.8 percent), medical products, appliances and equipment (5.6 percent) and hospital services (1.4 percent).

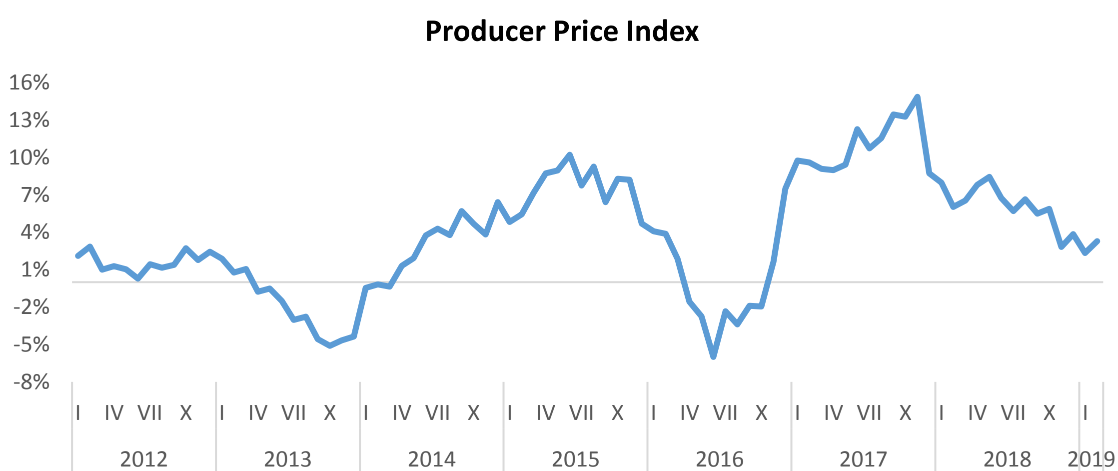


[2] Source: National Statistics Office of Georgia

Decomposition of inflation by domestic and imported inflation is as follows: domestic inflation – 2.2 percent, imported inflation – 0.9 percent, mixed inflation – 0.6 percent.



Producer price index (PPI) was 3.3 percent in February of 2019 compared to the same period of 2018 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 February 2019:

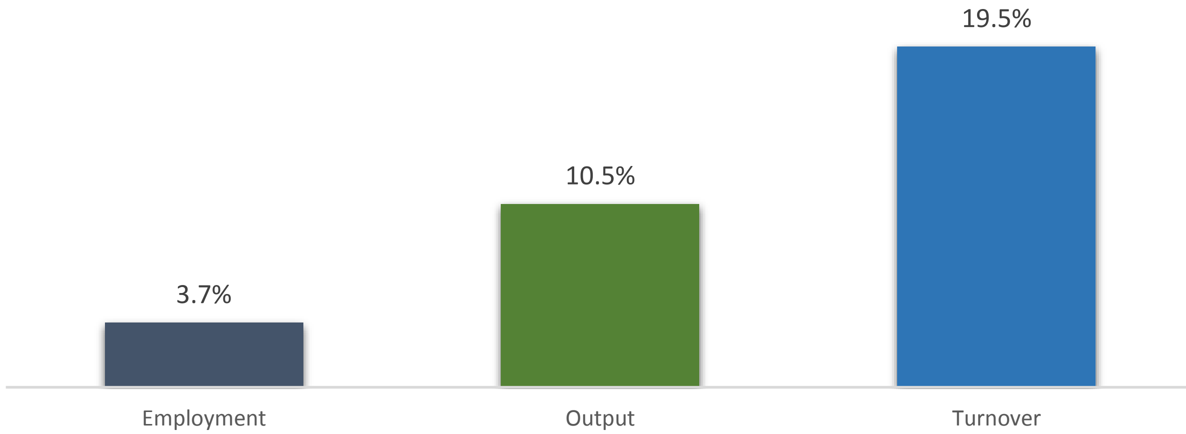
- Manufactured products: the prices increased by 4.0 percent, contributing 3.18 percentage points to the overall annual index growth. There was an increase in the prices for food products, beverages and tobacco products (4.5 percent), also for basic metals and fabricated metal products (5.1 percent);
- Electricity energy, gas, steam and hot water: the prices increased by 1.1 percent and contributed 0.14 percentage points to the overall 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.

Business Sector, 2018



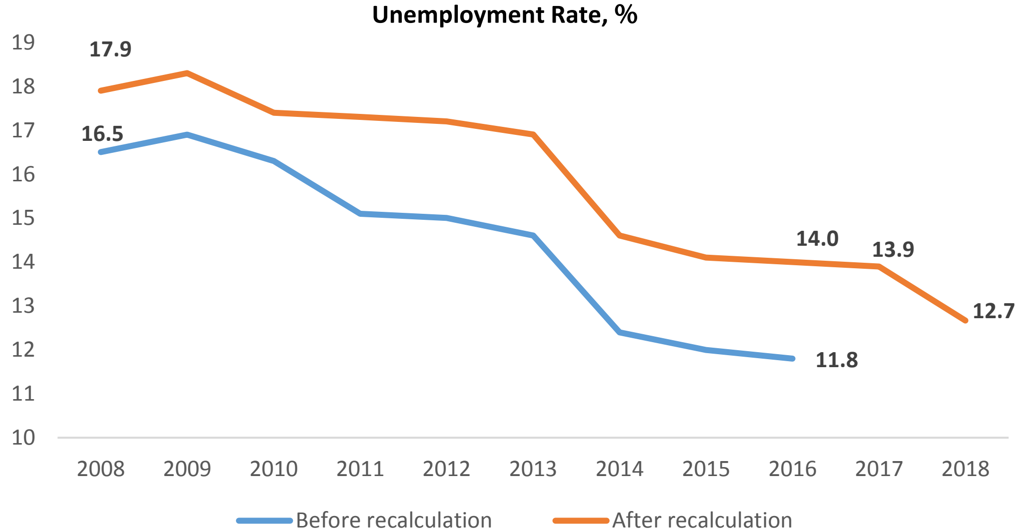
Unemployment Rate

Unemployment rate reduced to 12.7 percent in 2018, which is the lowest during last years. In 2017, unemployment rate was 13.9 percent.

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 2017, unemployment rate was 13.9 percent: urban unemployment rate was 22.8 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.

Unemployment Rate, %

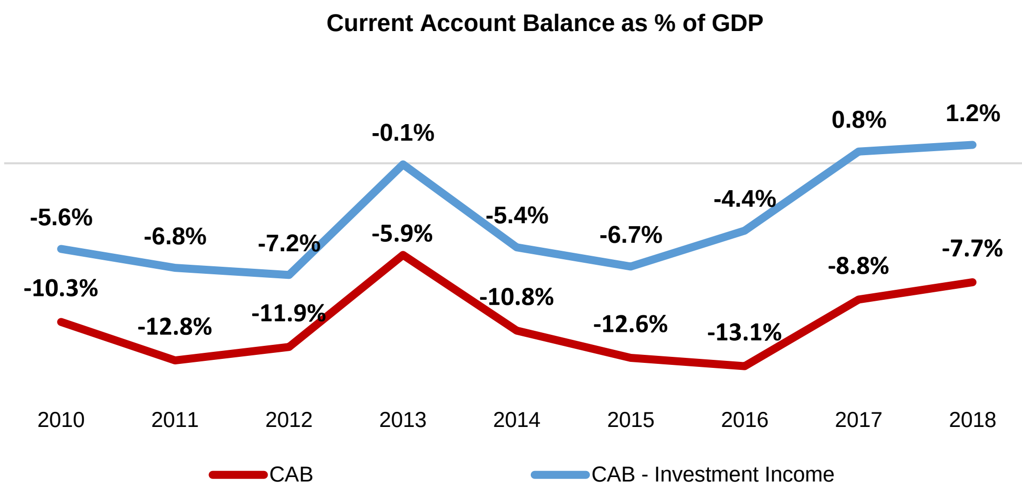


External Sector

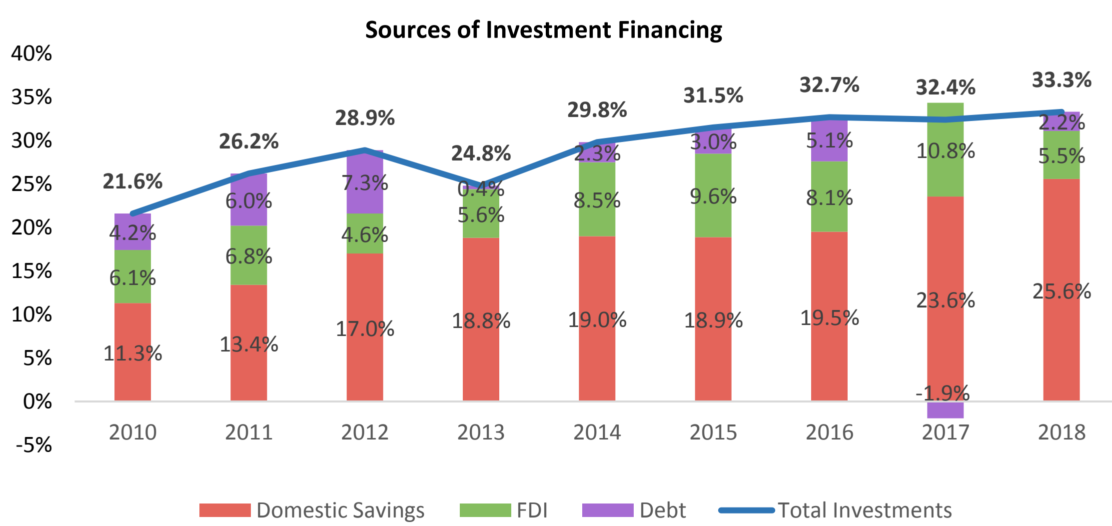
Current Account Deficit

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.

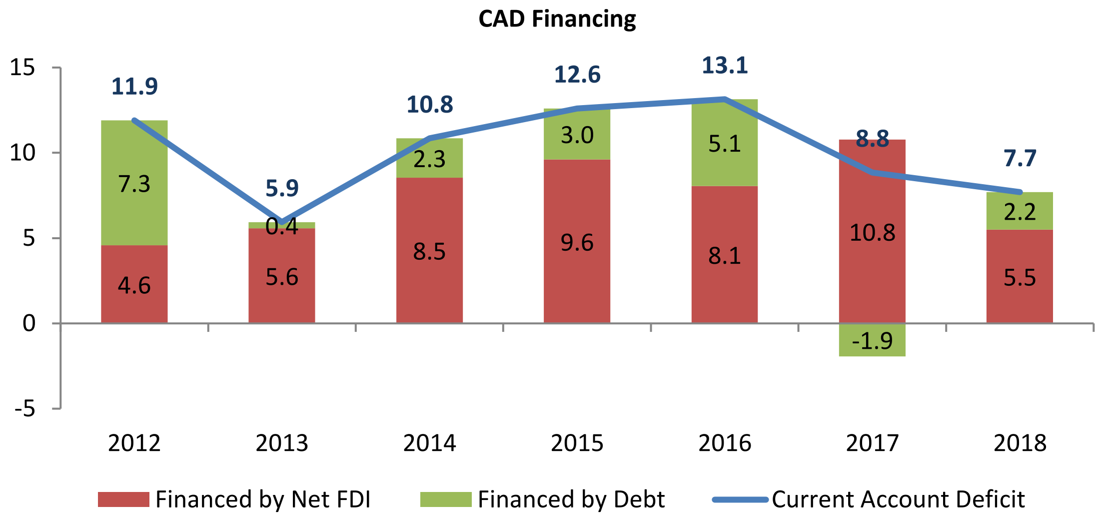
Declining tendency of current account deficit that started in 2017 is continuing in 2018 as well. In the first quarter of 2018, current account deficit amounted to 11.9 percent, in the second quarter it was – 8.8 percent, while in the third quarter there was current account surplus at 0.2 percent, which 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.



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.



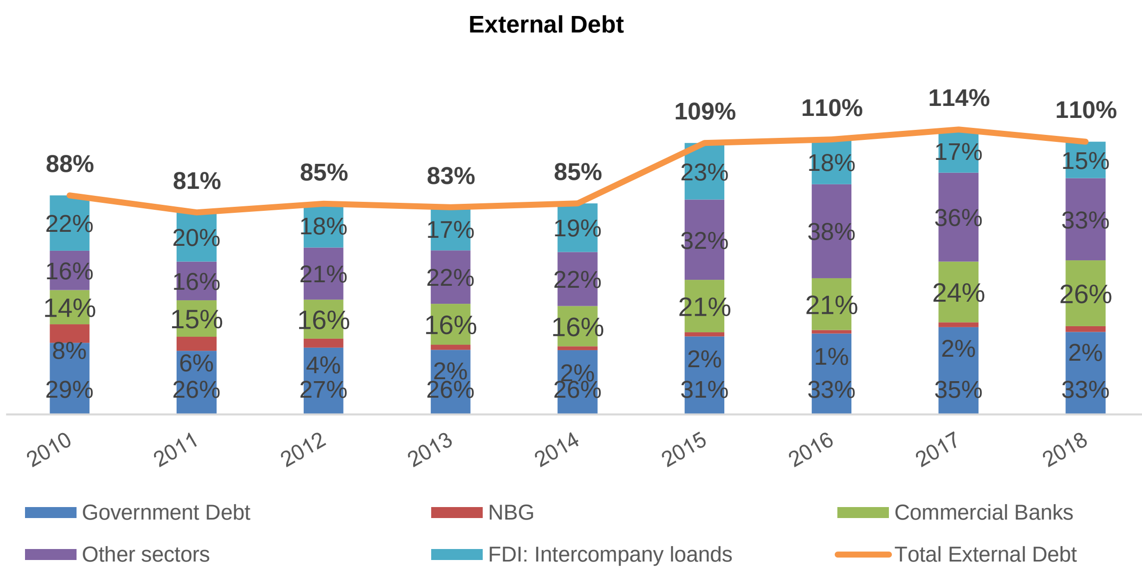
Current Account Deficit is financed through debt and foreign direct investments (FDI). Debt financing means more borrowing and, thus, more interest payments. Therefore, it is more favorable to finance current account deficit through increased FDI. In 2017, current account deficit was fully financed through 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.



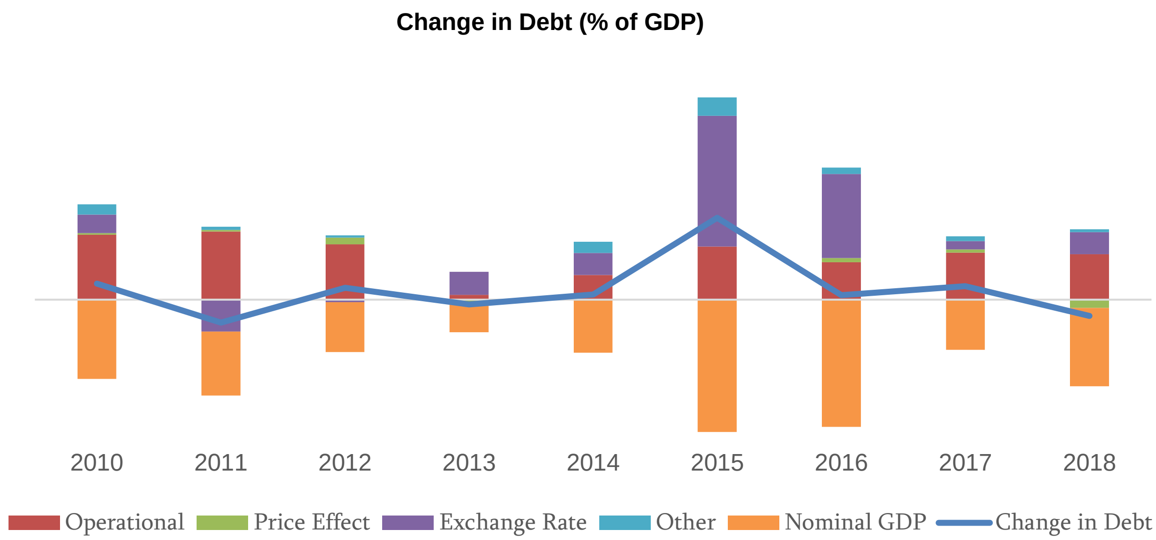
External Debt

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 114 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.



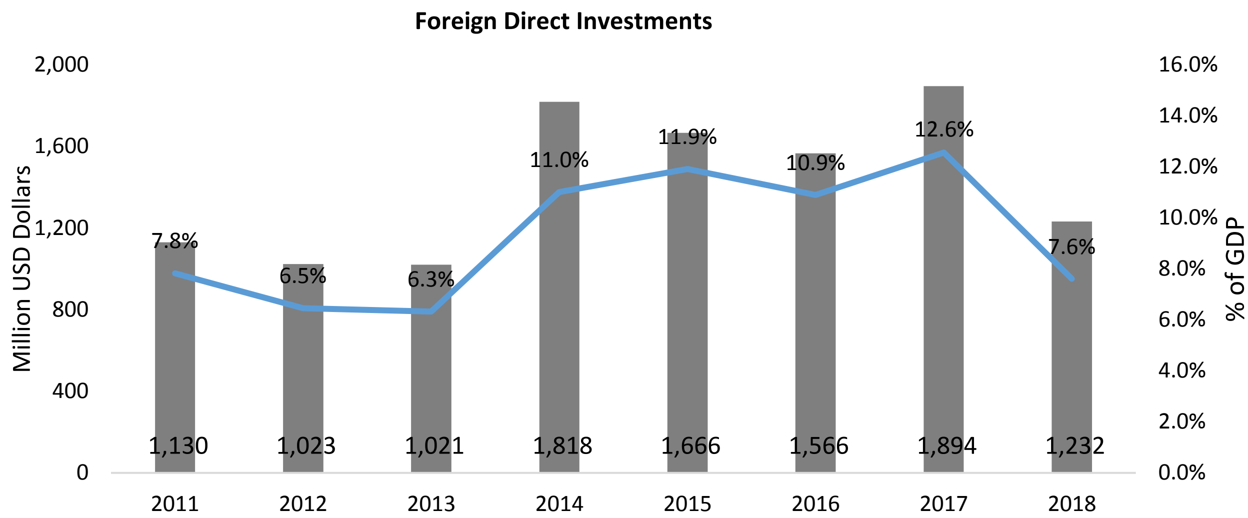
Change in external debt can be decomposed into operational change (new debt) and price effect, exchange rate effect and nominal GDP effect. During 2015 and 2016, depreciation was the main driver of increasing external debt, while change in GDP was positively contributing towards its reduction. In 2018,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



Foreign Direct Investments

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.

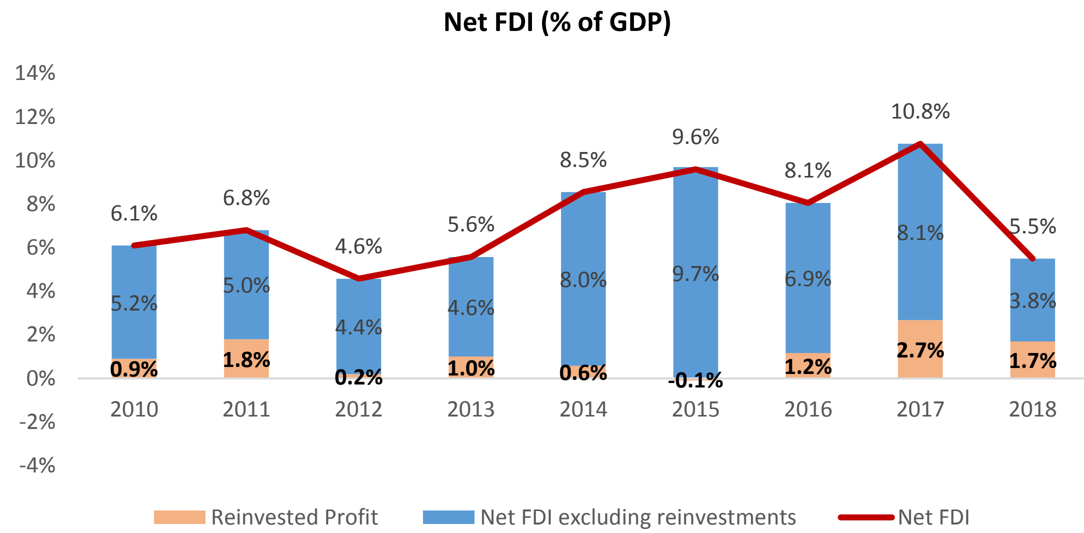


The major part of foreign direct investment in 2017 was made in transport and communication sector and was 25.8 percent, while it amounted 16.0 percent in financial intermediation sector, construction – 14.9 percent, energy sector – 11.8 percent, real estate – 9.6 percent, manufacturing – 5.2 percent,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

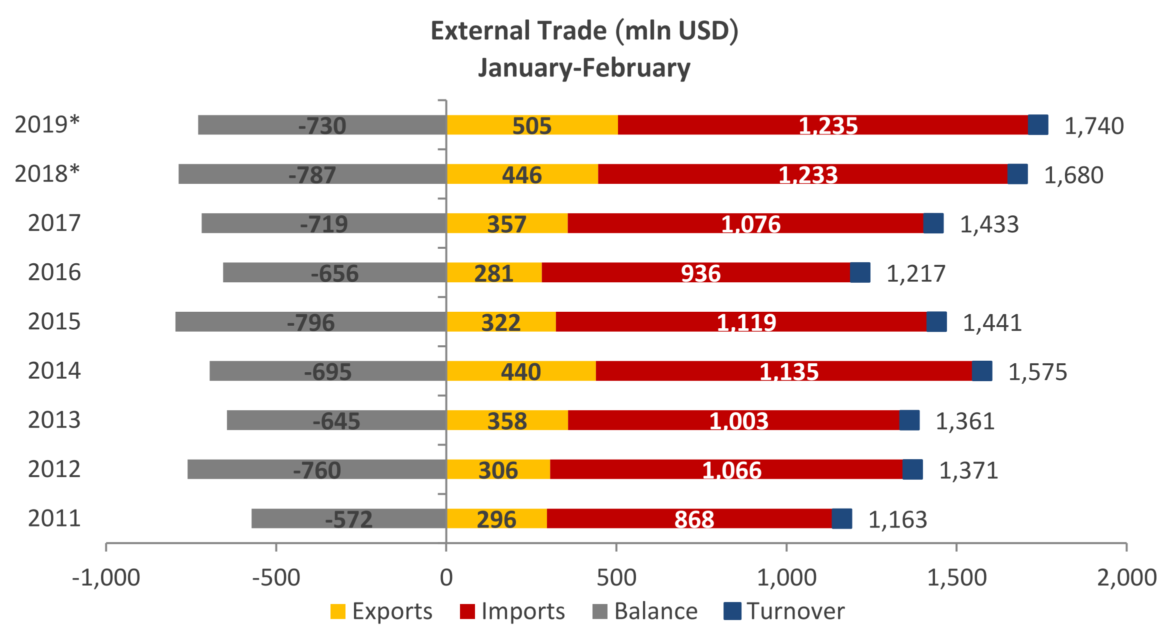
In 2016, the highest indicator was recorded in reinvestments amounting to 32 percent of total FDI which increased to 43.9 percent in 2017 and demonstrates that the government's economic policy and improved business environment is positively perceived by investors and more investors decided to extend 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.



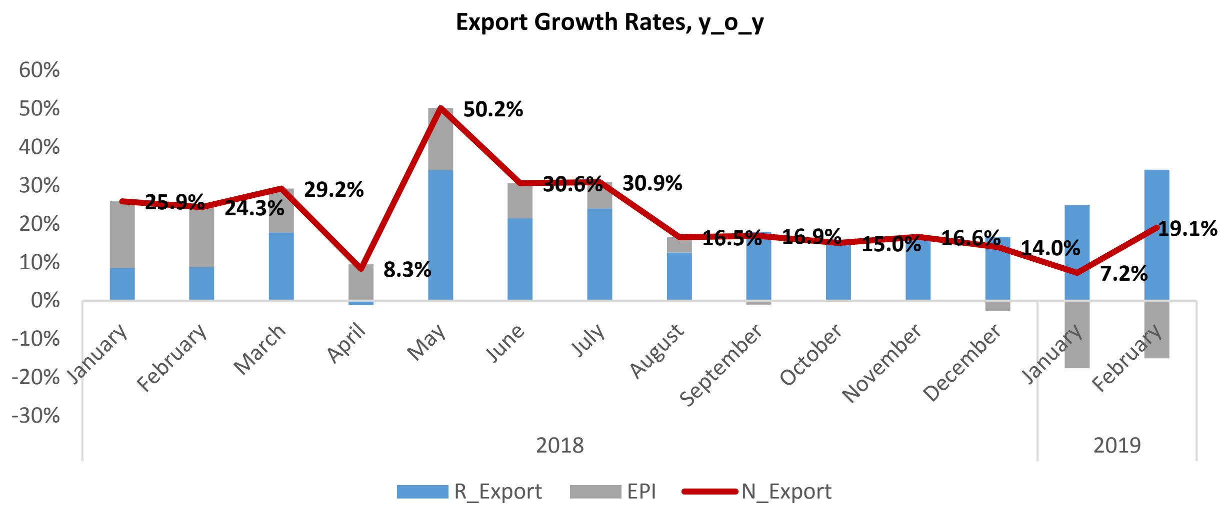
External Trade

In January of 2019, export has increased by 7.2 percent, while import has reduced by 0.4 percent and trade balance has improved. In February export has increased by 19.1 percent, while import has increased just by 0.6 percent. This is an illustration of the fact that economic recovery in region strongly affected Georgian export.

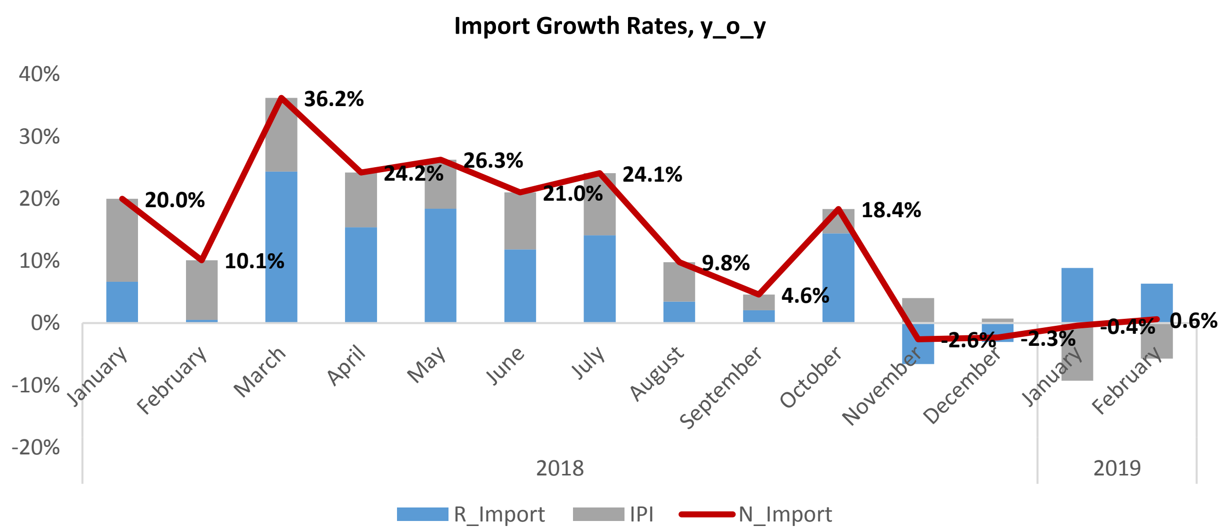
In 2018, both export and import increased by 22.6 percent and 14.9 percent respectively, resulting in deterioration of trade balance by USD 560 million. As for the fourth quarter of 2018, increase in export and import was 16.0 percent and 4.2 percent respectively and trade balance improved by USD 24 million compared to the same period of 2017.



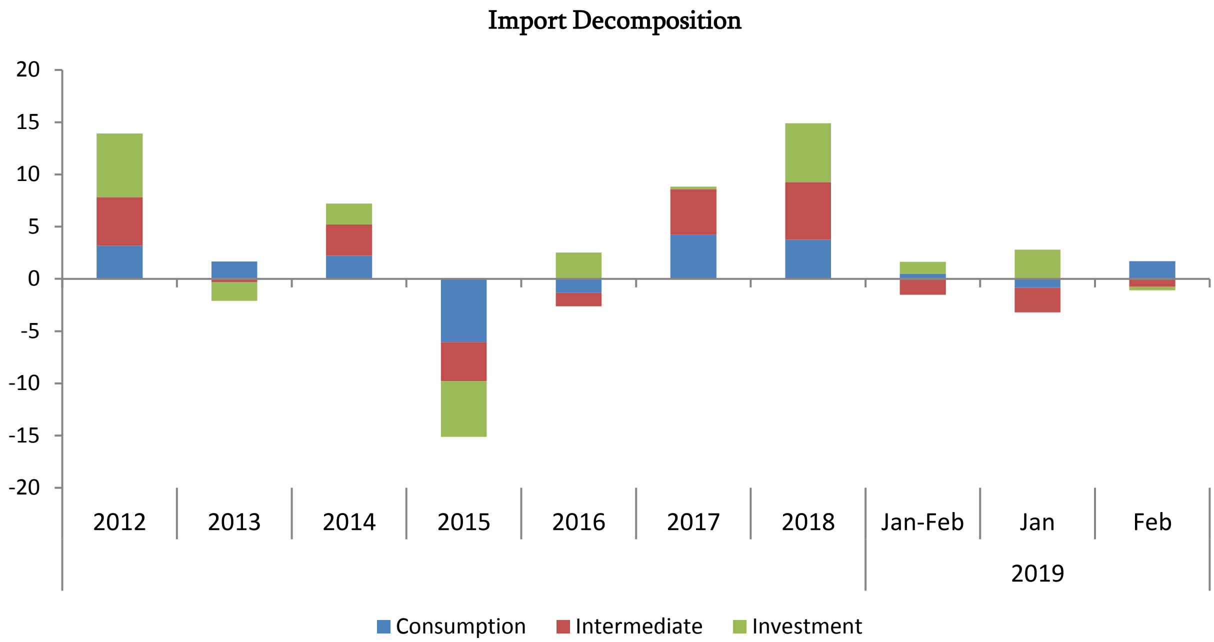
It is important to differentiate between real and price change effects when analyzing external trade. Real growth of export has improved in the first half of 2018. Moreover, starting from September 2018, the effect of price change on export was negative, thus, making the real change of exports greater than the nominal change. In February 2019, real growth of export amounted 34.1 percent, while its nominal growth was 19.1 percent.



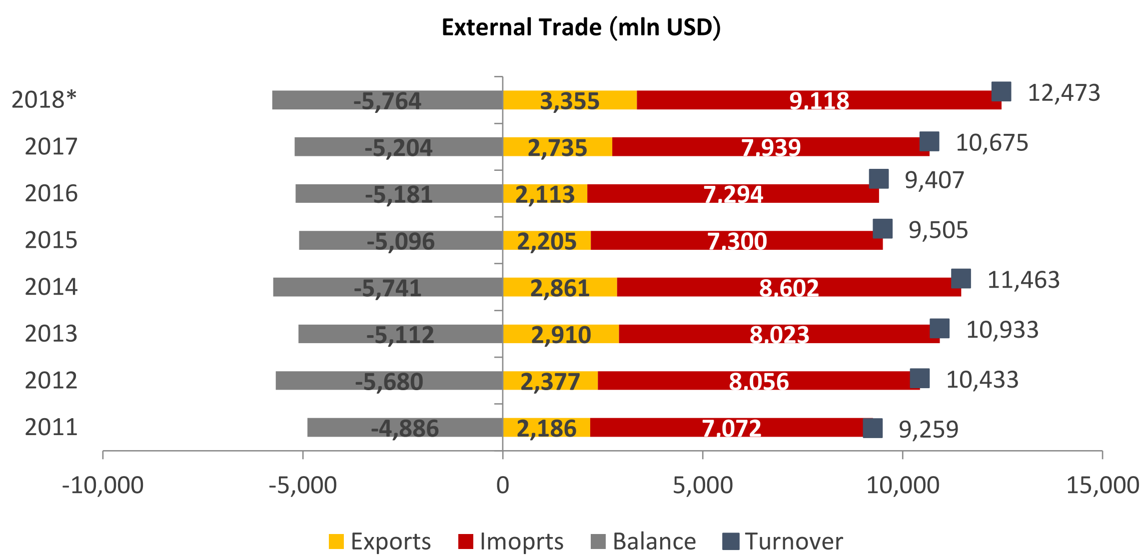
As for the growth in import, the effect of price change has a significant share in its nominal growth. Real import has reduced during November and December of 2018. In January 2019, real growth of import was greater than its nominal growth. In February 2019, real growth of import amounted 6.3 percent, while its nominal growth was 0.6 percent.



In total, export increased by 22.6 percent in 2018, while import increased by 14.9 percent out of which 11.2 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-February import of investment goods has increased by 1.2 percent and import of consumption goods – by 0.5 percent, while import of intermediate goods has decreased by 1.5 percent.



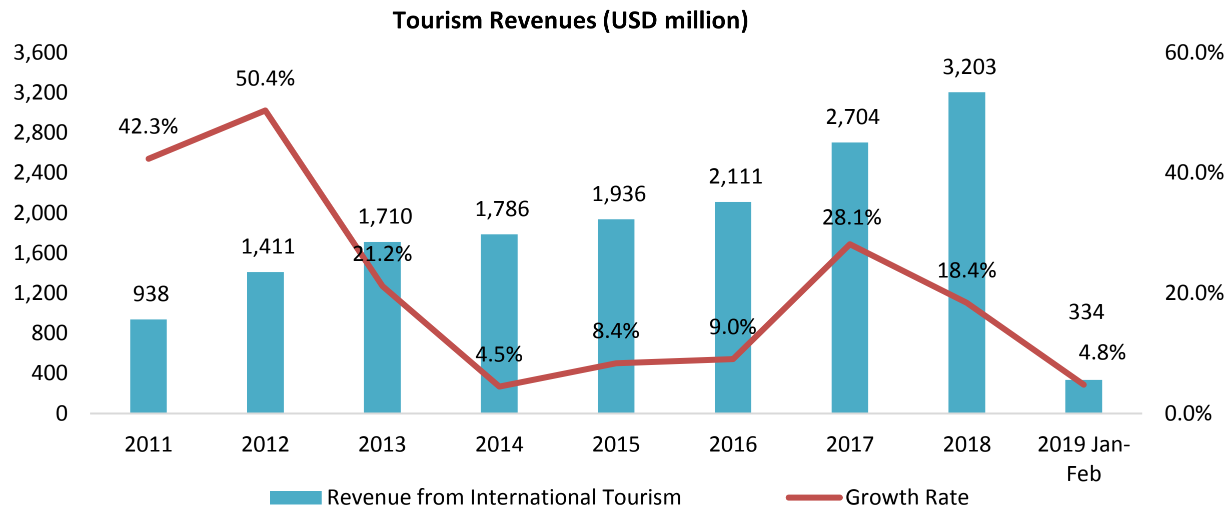
Contributions in growth of exports of 2018 by sectors is as follows: cars – 6.4 percentage points, cigarettes – 3.9 percentage points, copper ores – 3.0 percentage points, ferroalloys – 1.7 percentage points, wine – 0.9 percentage points.



Tourism

During last years, tourism has formed as one of the most important sectors of the economy. The number of visitors has decreased by 0.8 percent in February 2019 and amounted to 444 thousand, while revenues from tourism was 169 million USD, 4.6 percent higher compared to February of last year. It should be noted that decrease in number of visitors was due to 10.7 percent decline in number of one day trips, while number of touristic trips increased by 5.1 percent.

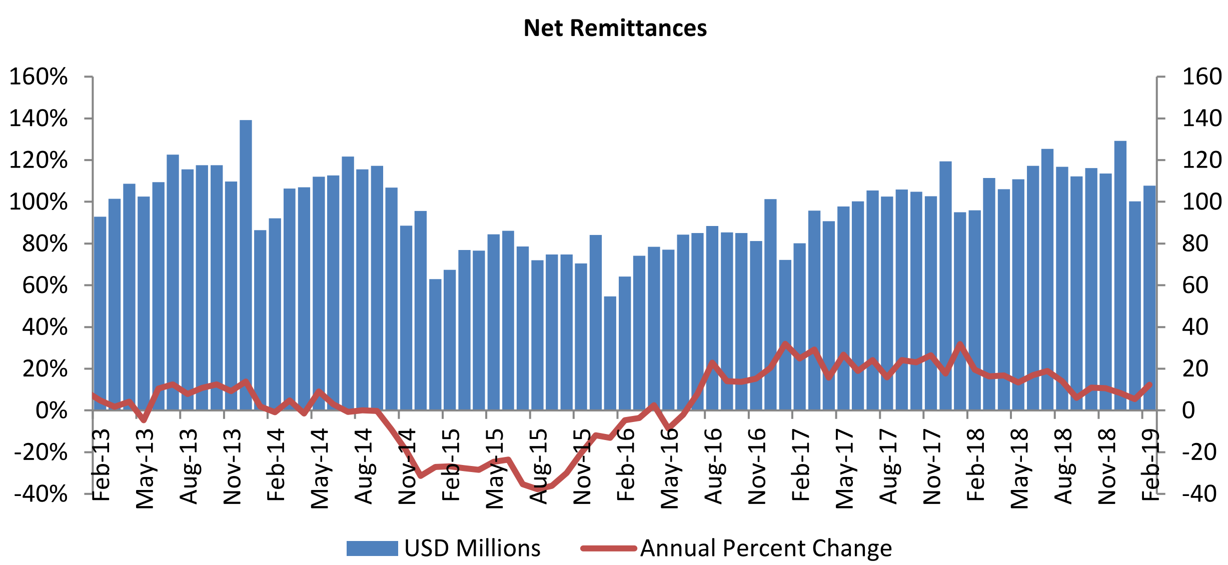
2018 started with increasing trend of visitors. There were 8,326 thousand visitors in Georgia throughout 2018 which is 10.2 percent greater than in 2017. Revenues from tourism increased by 19.1 percent and amounted USD 3,222 million.



Transfers

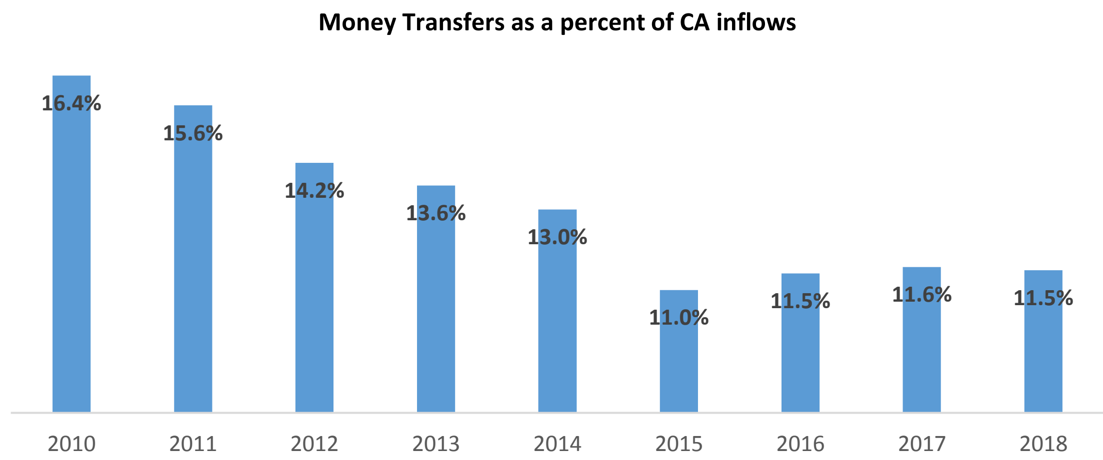
In January 2019 net money transfers amounted USD 100.2 million, which is 5.4 percent higher compared to January of the previous year. In February money transfers amounted USD 107.7 million, which is 12.4 percent higher than in February 2018. Remittances have increased significantly from the USA (4.5 percentage share of the total increase) and from Italy (3.5 percentage share of the total increase) in February, while they have decreased from Turkey (-2.8 percentage share of the total increase) and from Russia (-0.6 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 1,301 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 118 million. Inflow of foreign currency driven by increase in export, tourism and transfers, in January-February increased by USD 91 million, while outflows determined by import increased by USD 1 million.

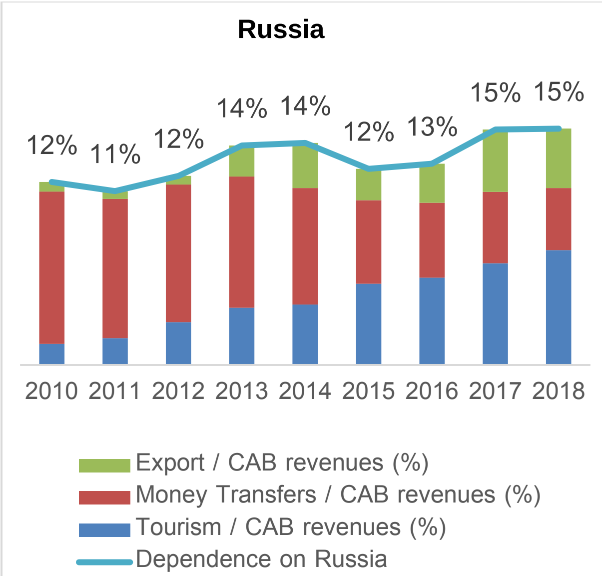
Despite the fact that money transfers have increased as a result of exhaustion of external shocks during recent years, dependence of the economy on such transfers declines through years and can be explained by rapid growth of export and tourism.

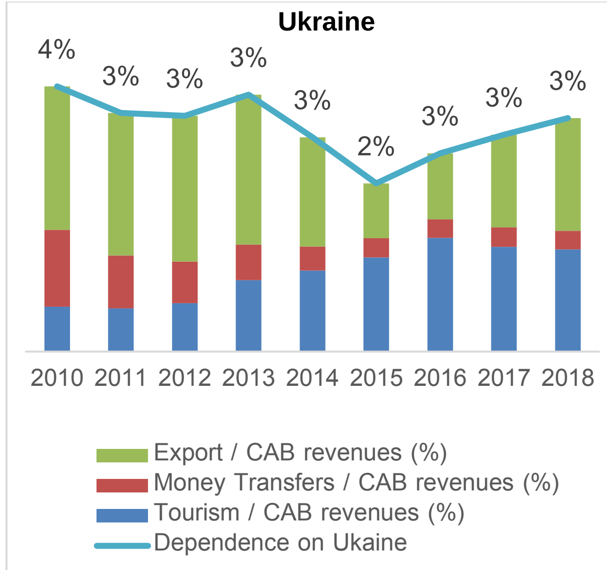


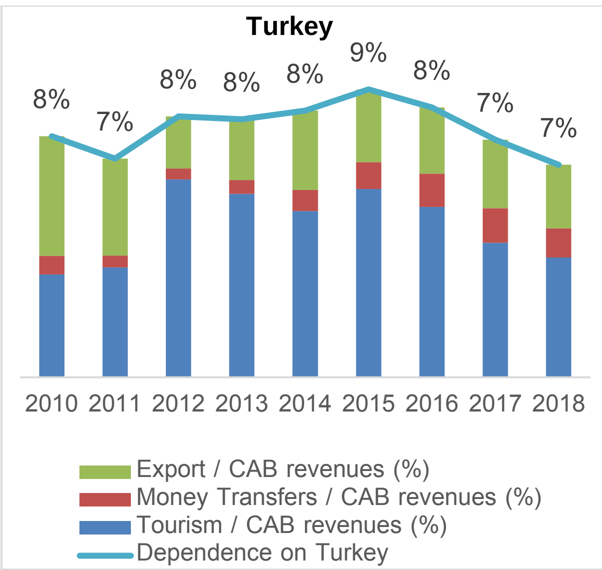
Dependence on other countries

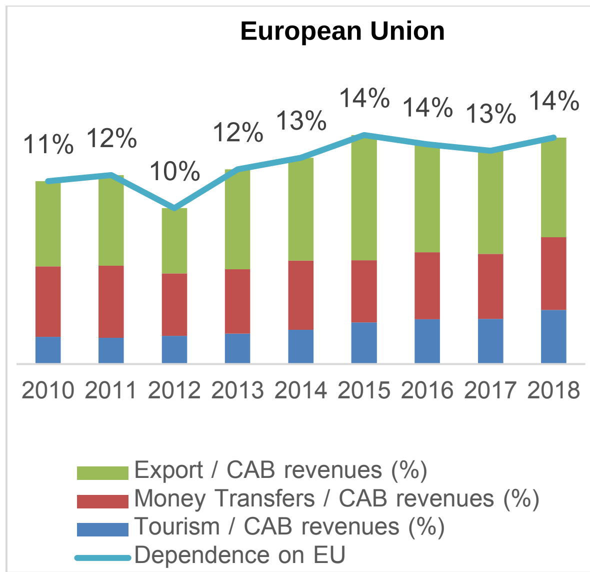
Georgian economy is diversified in terms of dependence on other countries. Based on shares of exports, tourism and transfers in current account deficit, it can be concluded that Georgia has tight relationships with Russia, Turkey, Ukraine and European Union.

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.







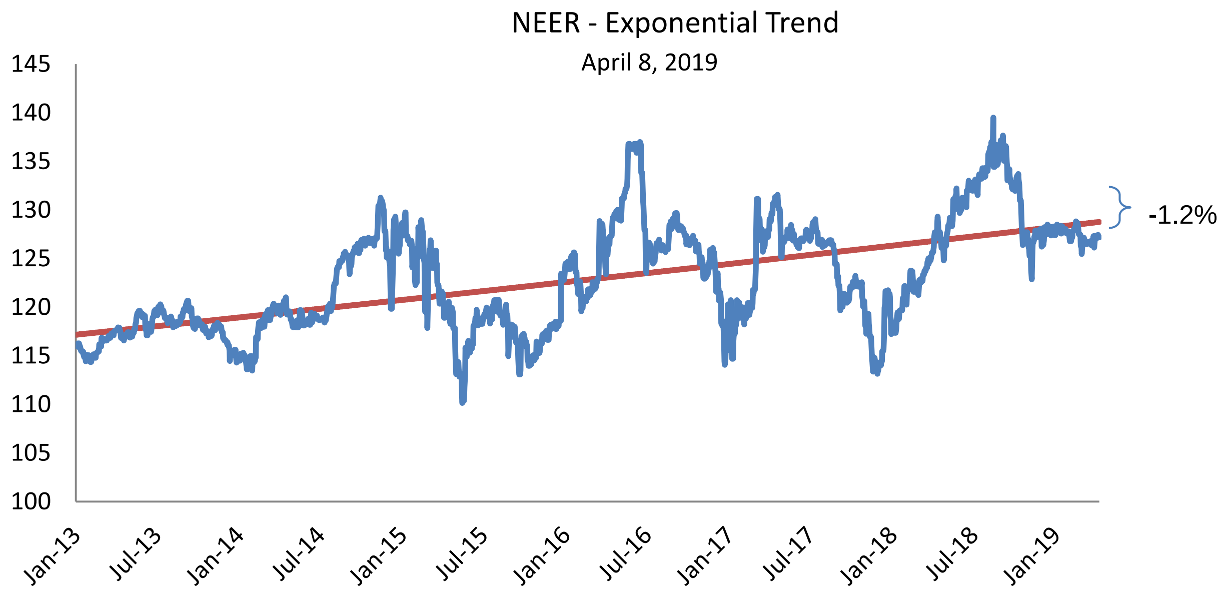


Exchange rate

On April 8 of 2019, nominal effective exchange rate of Georgian Lari depreciated by 0.5 percent compared to January 1 of 2019. There was 7.6 percent appreciation compared to January 1 of 2018. Real exchange rate appreciated by 4.0 percent compared to January of the last year and appreciated by 0.5 percent compared to the January of 2018.

Nominal effective exchange rate of Lari is depreciated by 1.2 percent from its medium-run trend.

	8 April, 2019	8 Apr 2019 - 1 Jan 2019	8 Apr 2019 - 1 Jan 2018
Euro	3.0212	▲ 1.3%	▲ 2.8%
US Dollar	2.6903	▼ -0.7%	▼ -3.6%
Turkish Lira	0.4811	▲ 5.1%	▲ 42.9%
Russian Ruble	0.0411	▼ -6.7%	▲ 9.2%
NEER	127.17	▼ -0.5%	▲ 7.6%
REER (February 2019)	120.27	▲ 0.5%	▲ 4.0%



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

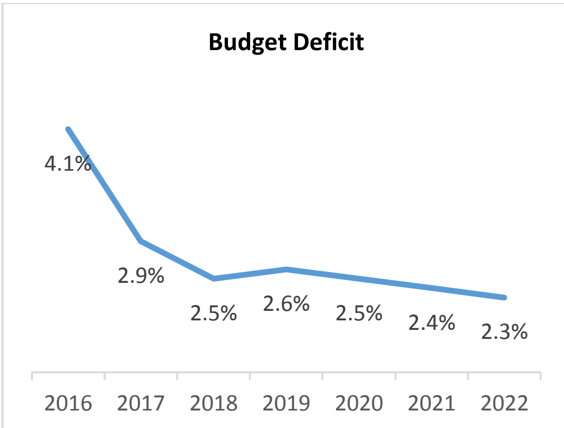
Forecast of budget revenues of 2019 is GEL 12,578.0 million including: tax revenue – GEL 11,280.0 million, grants – GEL 448.0 million, other revenues – GEL 850.0 million.

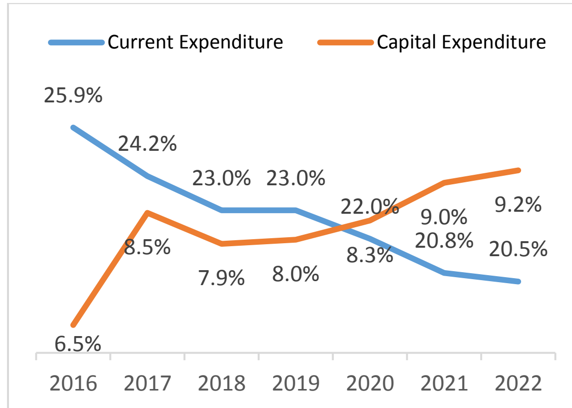
Forecast of tax revenues of 2019 is based on 4.5 percent economic growth and 3.5 inflation rate. In addition, legislative changes, change of tax base, administrative improvements and current economic tendencies were taken into account when forecasting tax revenues. These include:

- 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);
- Equalizing excise tax on domestic and imported tobacco; increasing ad-valorem tax from 10 percent to 30 percent (GEL 70.0-80.0 million).

Budget deficit of 2019 is forecasted at 2.6 percent, which is 0.1 points greater that 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-March 2019 was GEL 2 577.0 million, which is 0.6 percent (GEL 14.3 million) less than actual tax revenue.

- Income tax revenue amounts to GEL 817.3 million (greater than the forecast by 0.2 percent);
- Profit tax revenue amounts to GEL 279.2 million (greater that the forecast by 12.6 percent);
- VAT revenue amounts to GEL 1 092.5 million (less than the forecast by 4.7 percent);
- Excise tax revenue amounts to GEL 285.4 million (less than the forecast by 4.9 percent);
- Import tax revenue amounts to GEL 15.5 million (less than the forecast by 26.0 percent);
- Property tax income amounts to GEL 4.1 million;
- Other tax revenue amounts to GEL 98.1 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 VAR 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

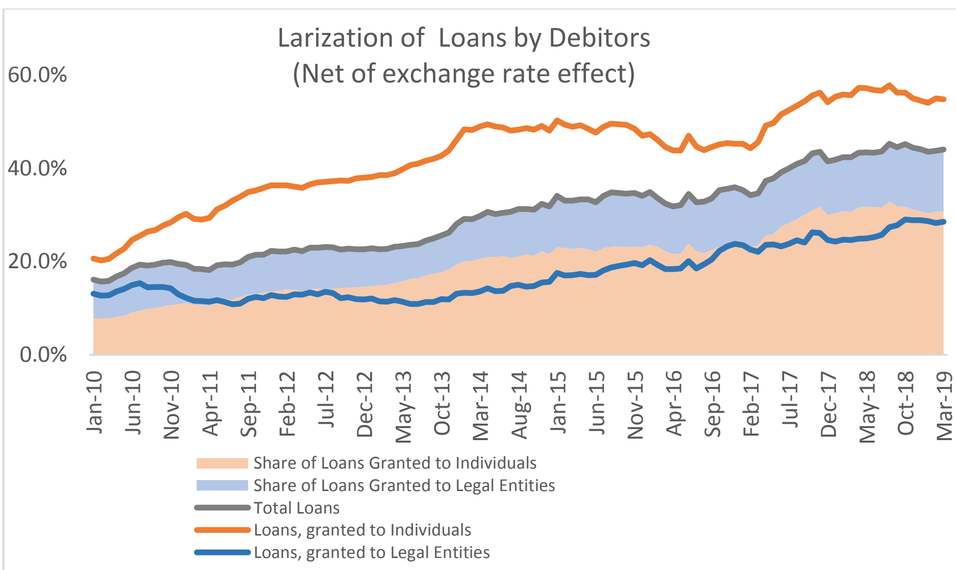
- Government debt was 42.1 percent of GDP as of the end of 2018 (out of which external debt was 34.2 percent of GDP). In 2017 the debt amounted 42.4 percent of GDP (external debt – 34.9 percent of GDP), in 2016 – 42.4 percent of GDP (external debt – 35.1percent of GDP), and in 2015 – 39.2 percent of 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.

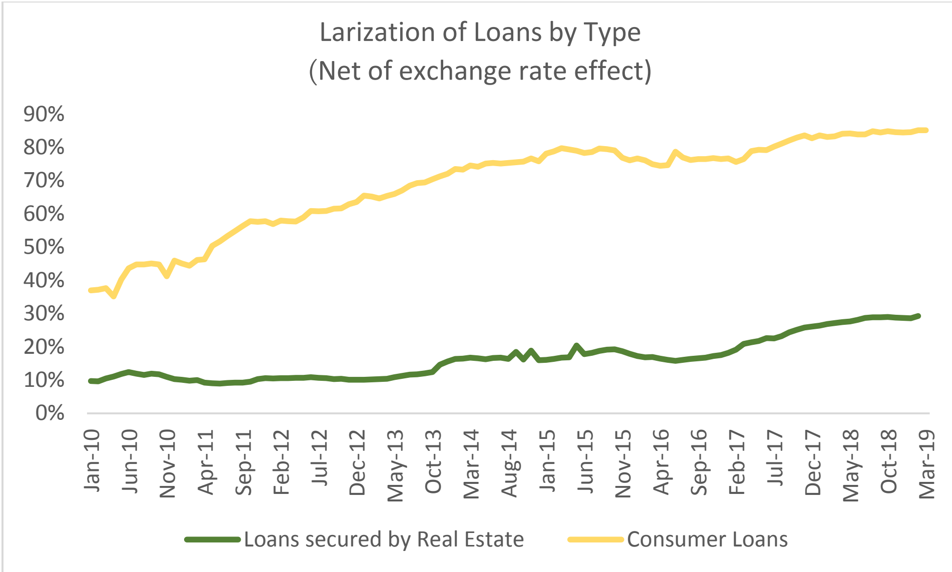
Monetary Sector

Dollarization of the Private Sector

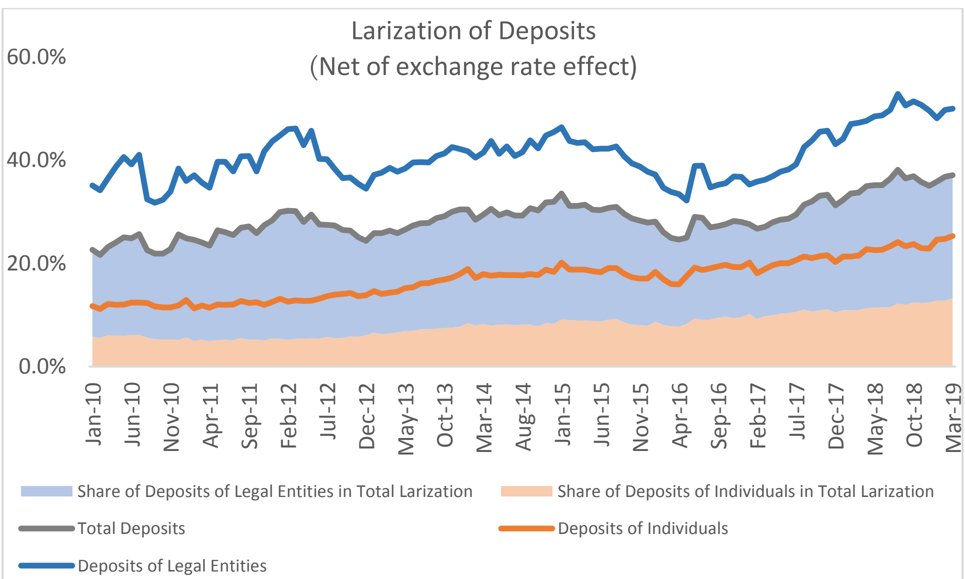
Loan larization has an increasing trend. Larization of total loans is mainly driven by larization of individual loans. As of March 2019, larization of individual loans is 54.8 percent, while larization of corporate loans is 28.5 percent. Larization of total loans is 44 percent in the given period.



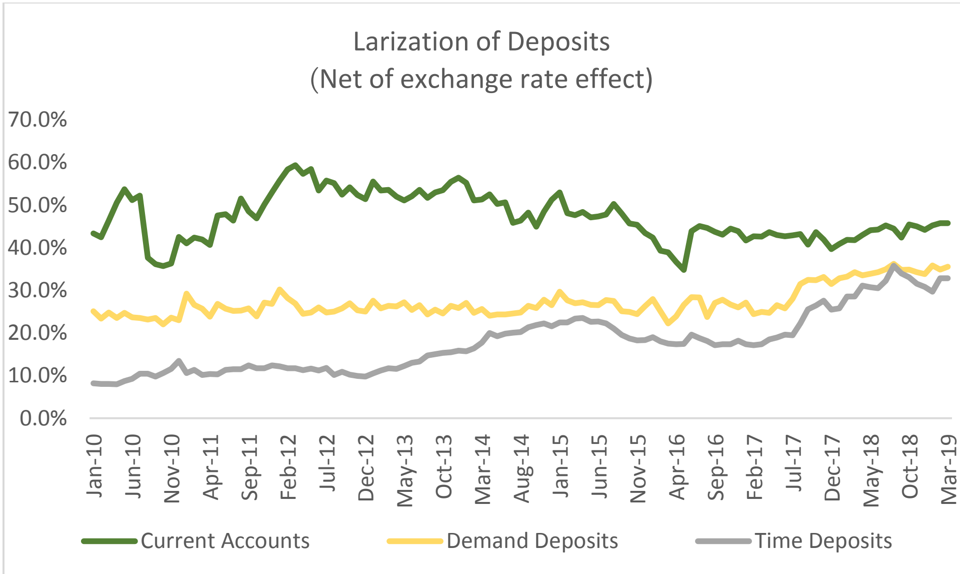
There is an increasing trend of larization of loans secured by real estate as well as consumer loans but the latter is significantly higher than the former. Larization of consumer loans was 85.2 percent in March 2019, while larization of loans secured by real estate was 29.3 percent in February 2019.



Larization of deposits is mainly driven by corporate deposits. Larization of total deposits was 37.1 percent in March 2019. Larization of corporate deposits was 50 percent during the same period, while larizarion of individual deposits improved by 0.6 percentage points in March 2019 compared to February 2019 and amounted 25.3 percent.

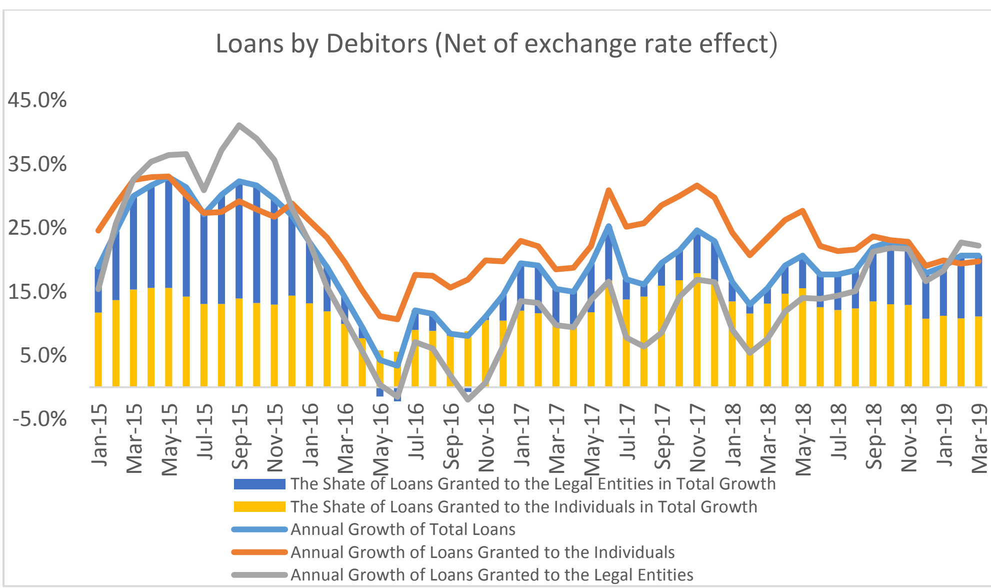


Larization of current accounts was 45.7 percent in March 2019, larization of demand deposits was 35.5 percent and larization of time deposits was 32.9 percent.

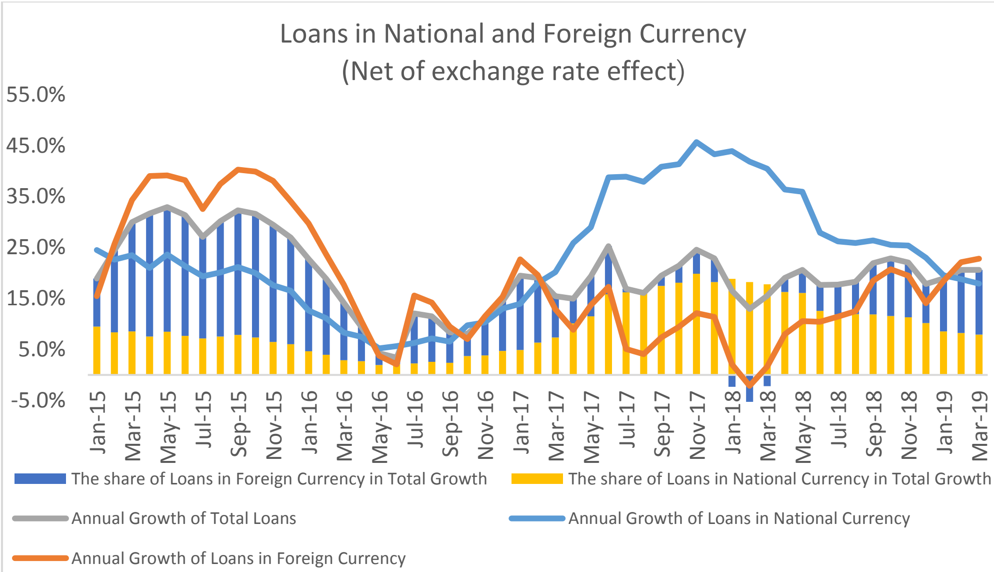


Overview of Loans

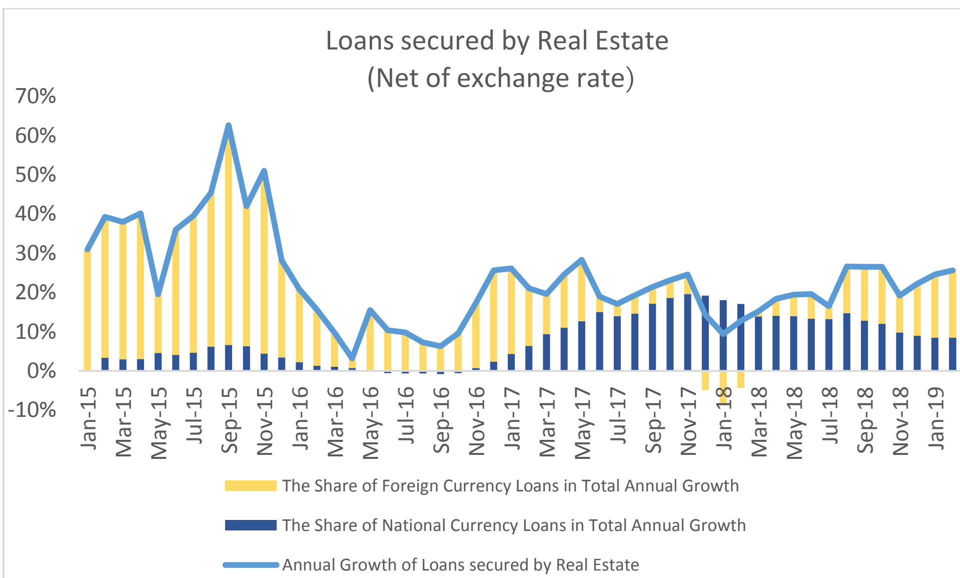
In March 2019, loan portfolio increased by 20.6 percent (net of exchange rate effect) compared to March 2018. In the same period annual growth of corporate loans reached 22.2 percent, while annual growth rate of loans granted to individuals was 19.7 percent. The following sectors contributed to the growth of loan portfolio: trade, hotels and restaurants, manufacturing and transport and communications; whereas increases in credit in agriculture, forestry, fishing and education were insignificant.



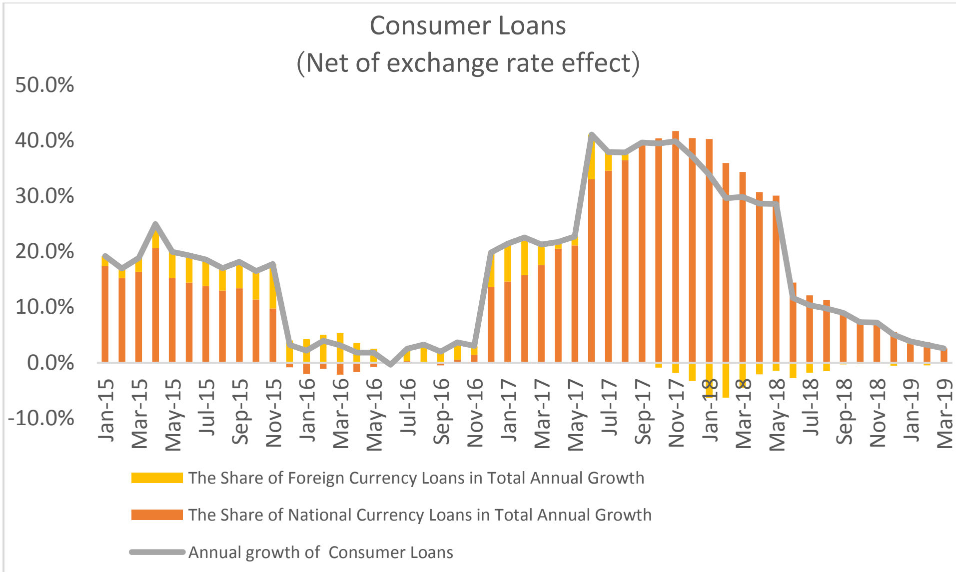
In March 2019, the growth rate of foreign currency denominated loans increased by 0.7 percentage points compared to previous month and reached 22.8 percent growth compared to the same period of the previous year, while loans in national currency grew by 17.9 percent. Total loans grew by 20.6 percent. Since 2018 contribution of foreign currency loans growth in total growth is increasing.



In February 2019, annual growth of loans secured by real estate was 25.7 percent, it is important to note that compared to previous month it increased by 1.1 percentage points. Since 2018 contribution of foreign currency loans growth in total growth of loans secured by real estate is increasing.

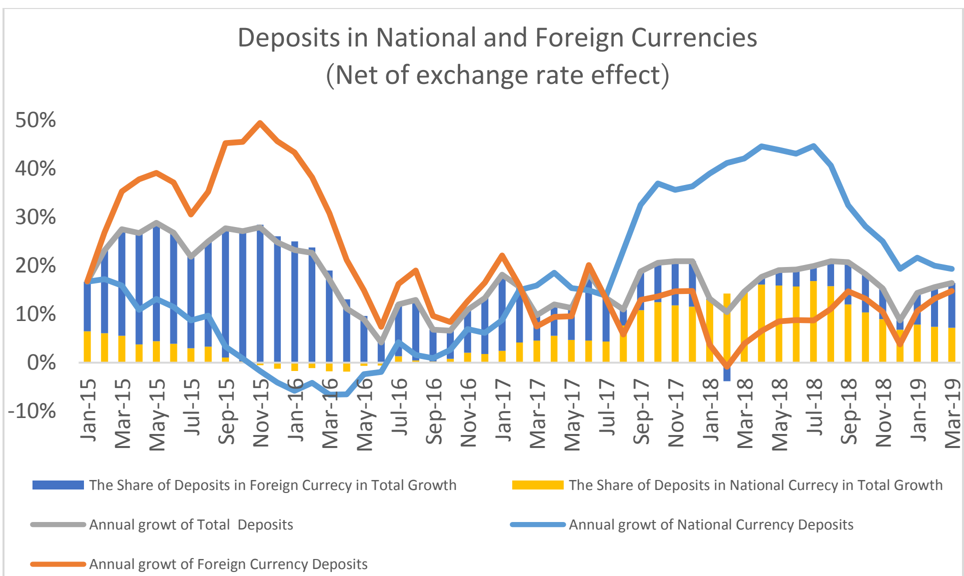


As for consumer loans, in March 2019, the annual growth rate was 2.6 percent. Since 2017 increase in consumer loans was mainly driven by growth of loans denominated in national currency.

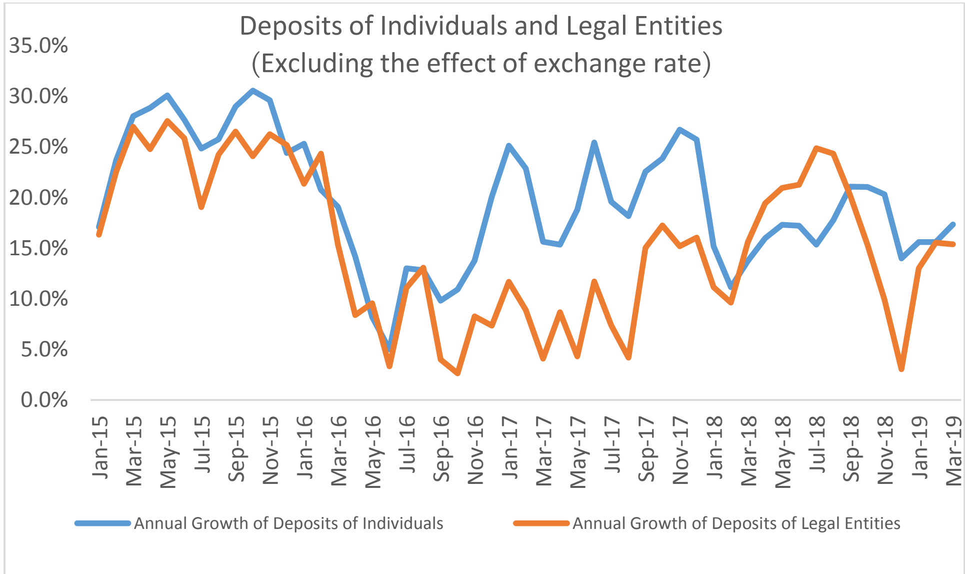


Overview of Deposits

In March 2019, the annual growth rate of foreign currency denominated deposits increased by 1.6 percentage points compares to previous month and reached 14.8 percent, while deposits in domestic currency grew by 19.3 percent compared to the same period of 2018, annual growth rate of total deposits was 16.4 percent.



In March 2019 annual growth rate of deposits of individuals increased by 1.8 percentage points compared to previous month and reached 17.4 percent, while annual growth rate of deposits of legal entities in the same period was 15.4 percent.



Monetary Policy Rate

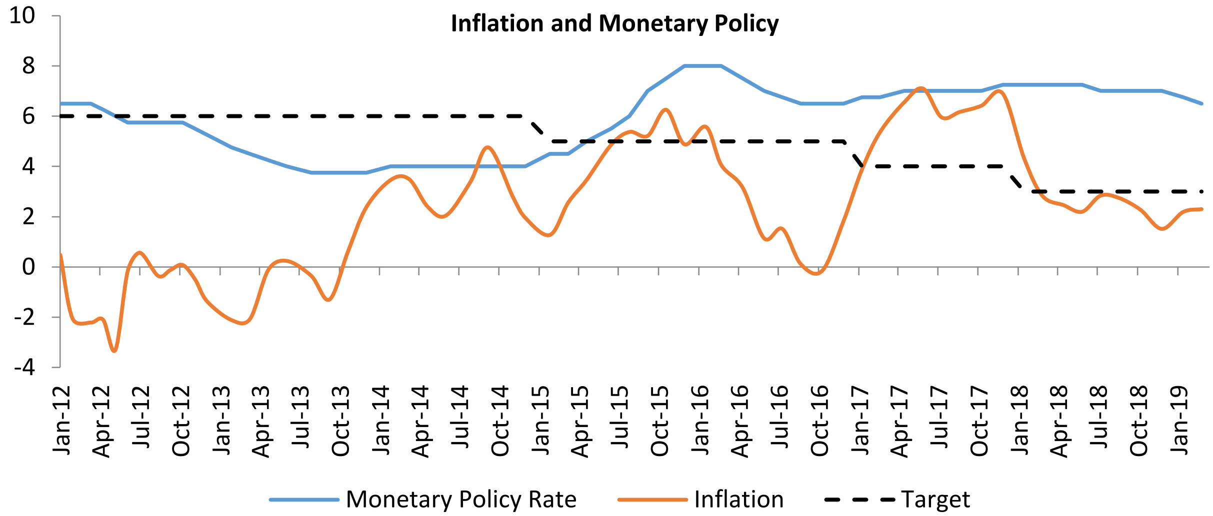
Monetary policy rate is at 6.50 percent. The Monetary Policy Committee cut the refinancing rate from 7.0 percent by 25 basis points on January 30 and then on March 13 by 25 basis points. The main reasons were: the weakening risks coming from the external risks and weak demand-side inflation pressure. National Bank of Georgia is planning gradual policy easing. The speed of normalization will depend on how fast the output gap will close on one hand and how strongly the increased regional macroeconomic risks will be transmitted to Georgian economy – on the other.

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.

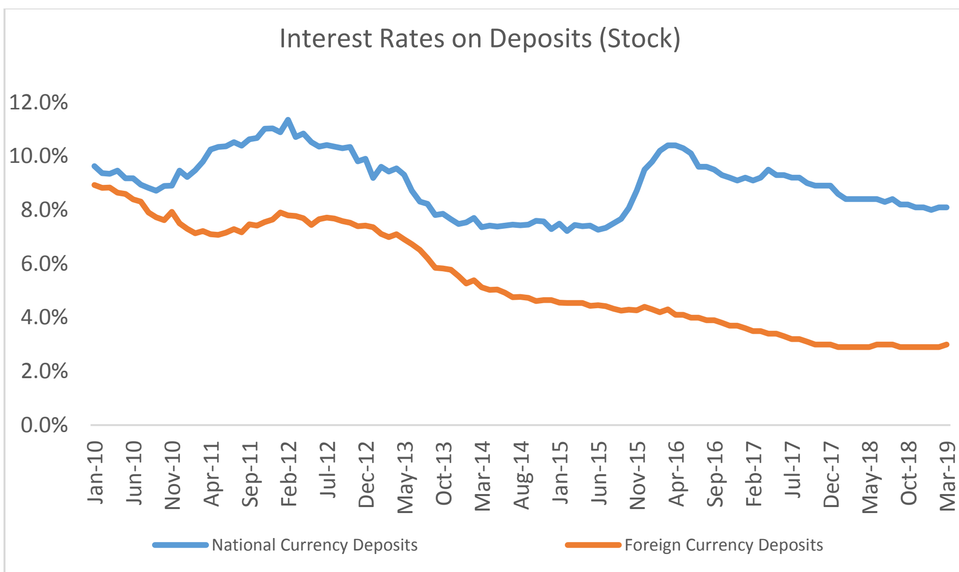
On July 25th monetary policy committee has cut the refinancing rate by 25 basis points, to 7.0 percent. The main reasons were: decline in annual inflation, which is close to the target level; higher than expected appreciation of nominal exchange rate, which reduced inflationary pressure. Monetary policy 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.

Now the monetary policy rate is at 6.5 percent.

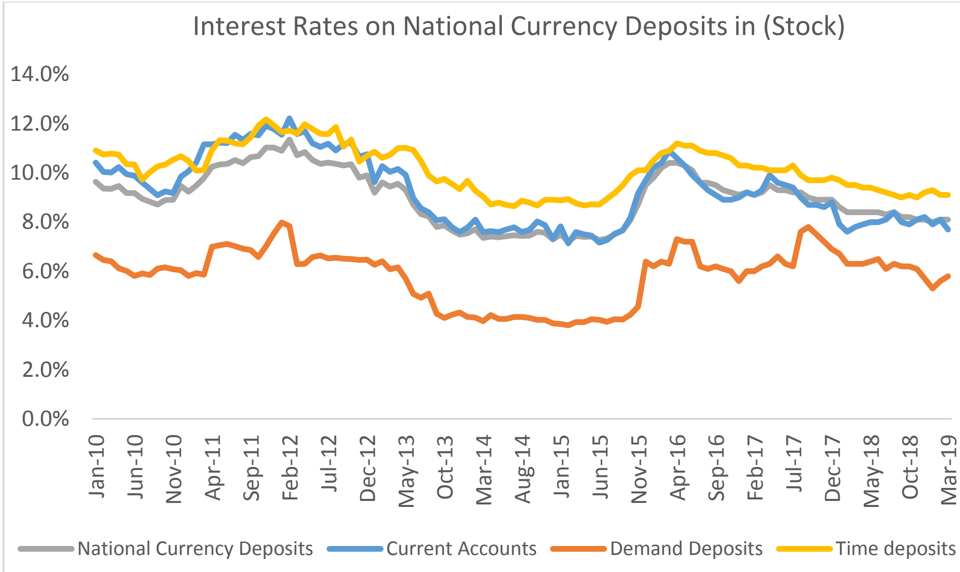


Interest Rates

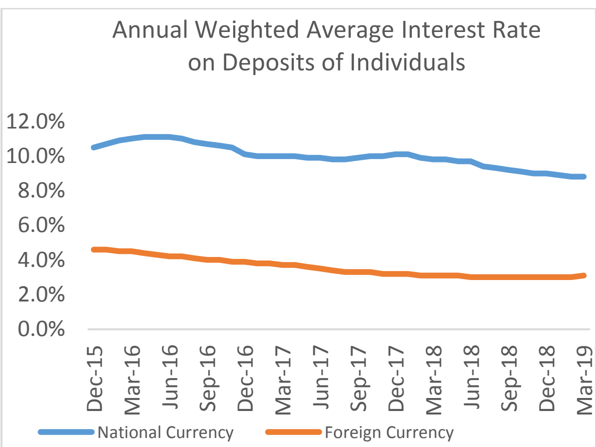
Interest rate on local currency deposits in March 2019 reached 8.1 percent, change in foreign currency deposits was insignificant and reached 3 percent.

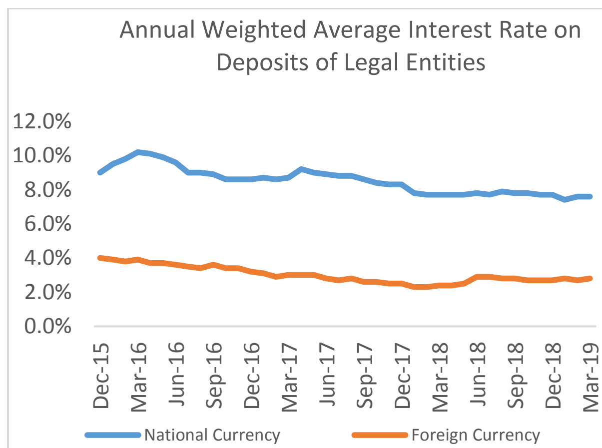


In March 2019, interest rate on demand deposits denominated in local currency was 5.8 percent. During the same period, interest rate on current accounts decreased by 0.4 percentage points compared to previous month and reached 7.7 percent, while on time deposits it was 9.1 percent.

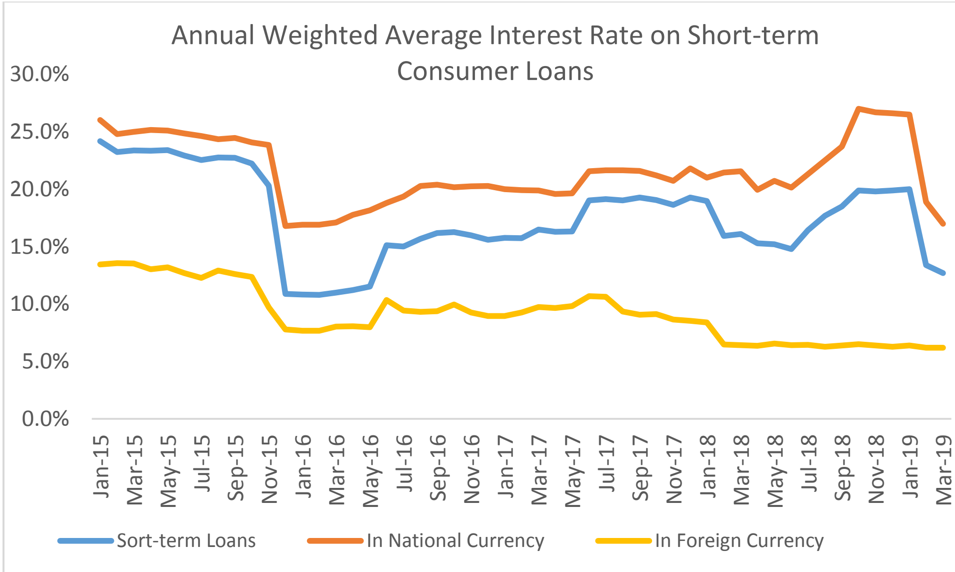


In March 2019, annual weighted average interest rate on national currency deposits of legal entities reached 7.6 percent, while on foreign currency deposits it was 2.8 percent in the same period. As for deposits of individuals, annual weighted average interest rate on national currency deposits reached 8.8 percent, while in foreign currency it was 3.1 percent.

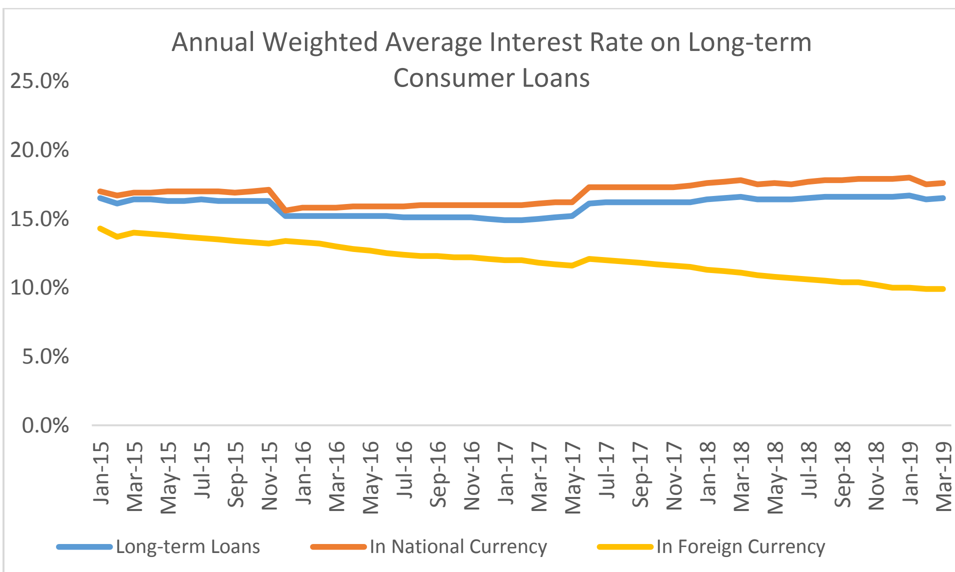




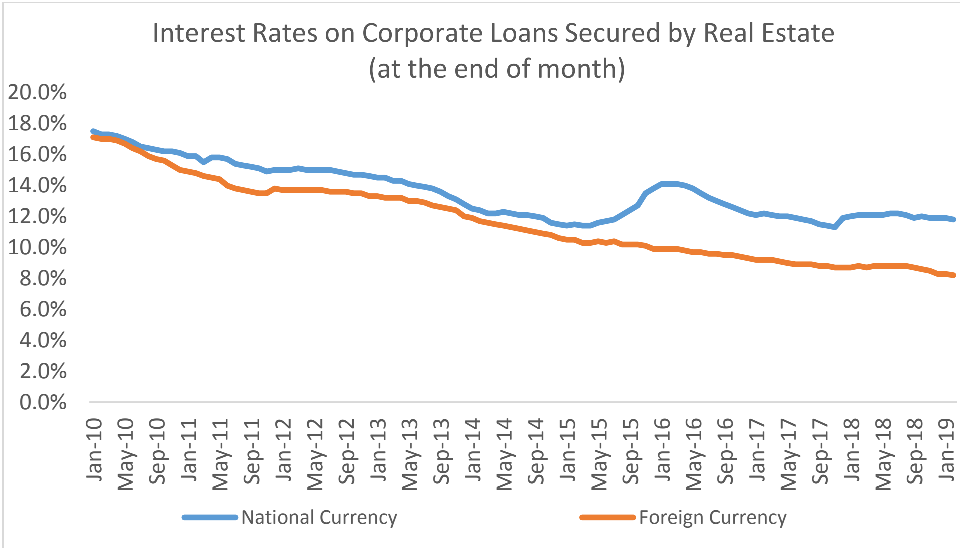
In March 2019, annual weighted average interest rate on short-term consumer loans decreased by 0.7 percentage points compared to previous month and reached 12.7 percent, this decrease was caused by decrease of local currency loans interest rate by amount of 1.9 percentage points. In the same period annual weighted average interest rate on short-term consumer loans in national currency was 17 percent, while on foreign currency loans it was 6.2 percent.



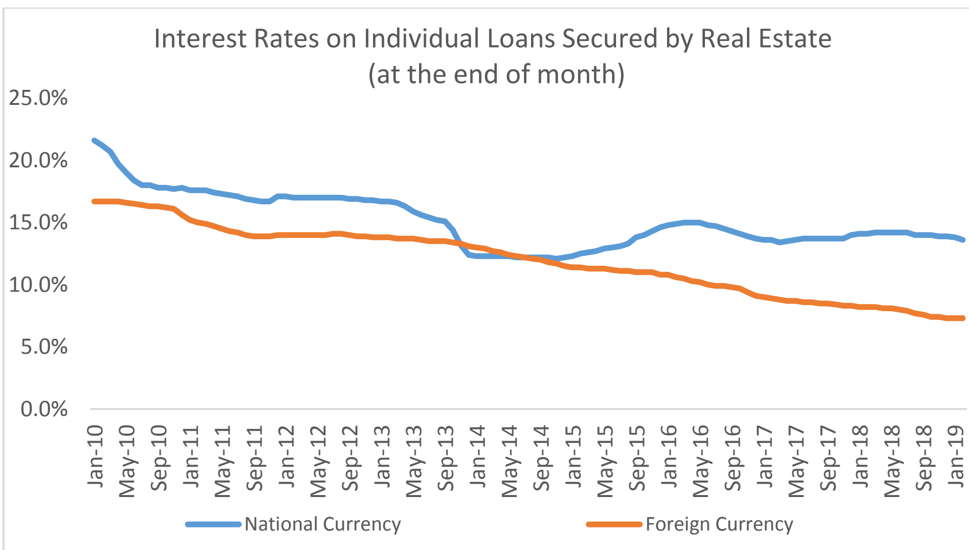
Annual weighted average interest rate on long-term consumer loans was mainly determined by national currency loans. In March 2019 it reached 17.6 percent on national currency loans, 9.9 percent on foreign currency loans and 16.5 percent on total long-term consumer loans.



At the end of February 2019 interest rate on corporate loans secured by real estate denominated in local currency was 11.8 percent, while on foreign currency loans is was 8.2 percent.



In the same period interest rate on foreign currency individual loans secured by real estate was 7.3 percent, while in national currency it reached 13.6 percent.



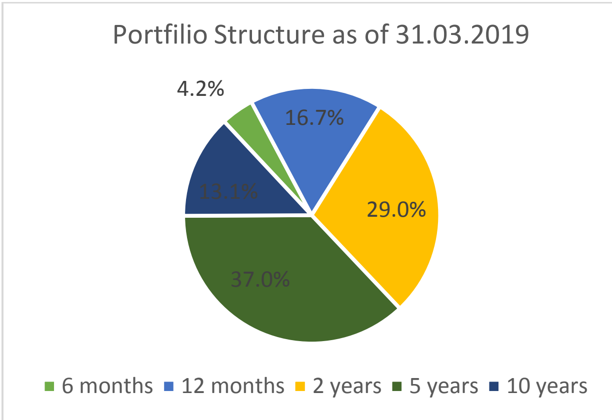
State Securities Market

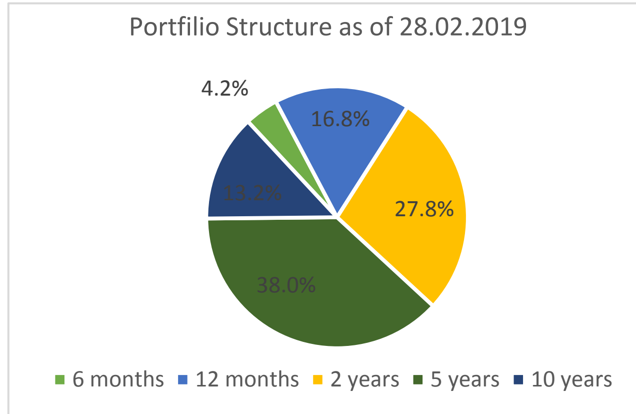
In March 2019, 4 auctions were held with total issuance volume of 130 million GEL. The weighted average interest rate amounted to 6.966%.

There were issued treasury bills with maturity of 6 months and 12 months; Treasury bonds with maturity of 2 years and 5 years. Treasury securities with total amount of 112 million GEL were redeemed.

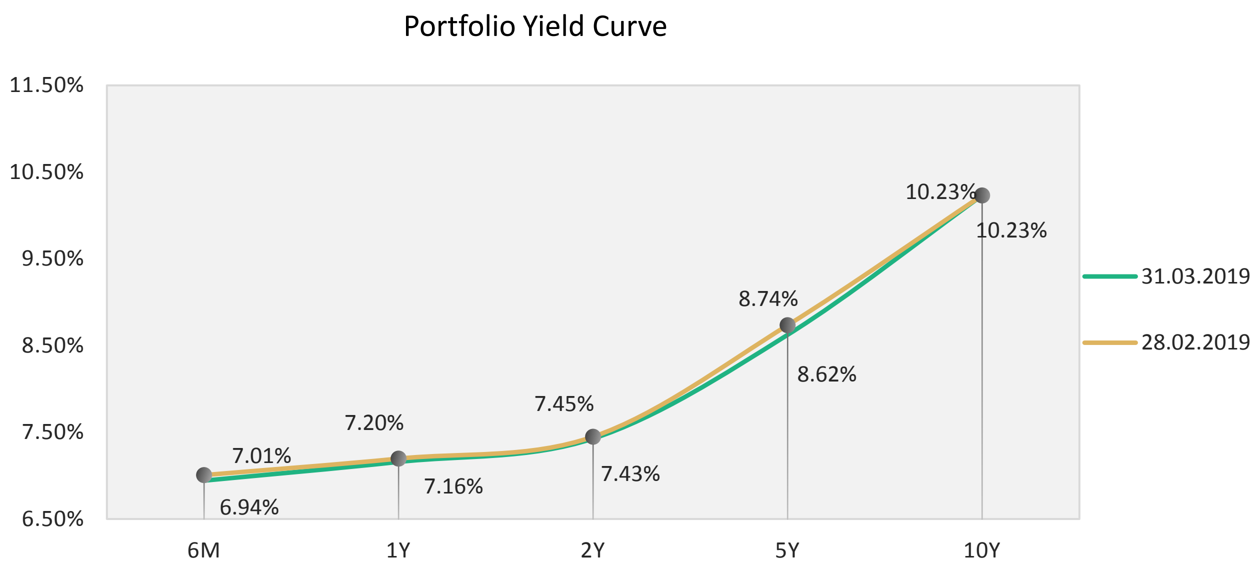
	6M	12M	2Y	5Y	Total
Volume of Emission	20	40	40	30	**130**
Average weighted interest rate	6,755	6,876	7,019	7,155	**6,966**
Coverage	20	40	0	52,417	**112**
Difference	0	0	40	-22,417	**18**

The structure of treasury securities portfolio has changed slightly:





The portfolio yield almost has not changed.

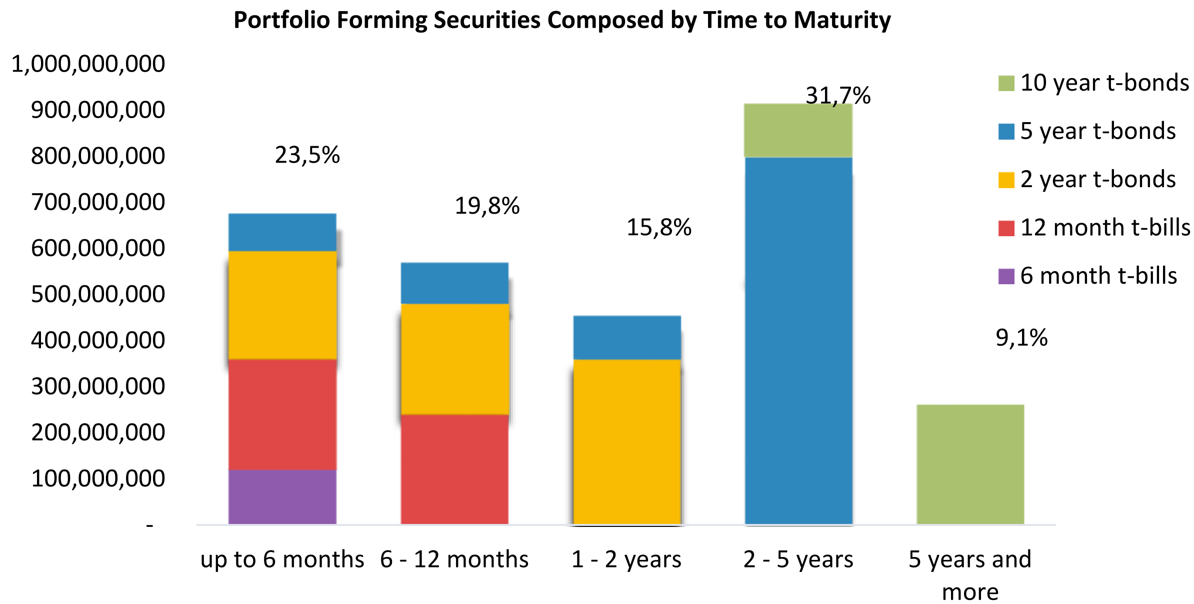


Time to Maturity (ATM) for all securities forming the portfolio has slightly increased compared to the previous month's value.

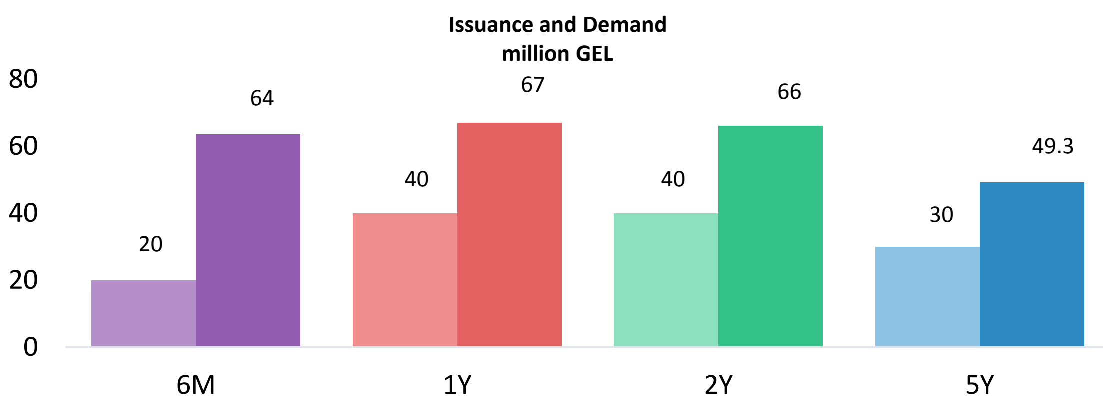
Average Time To Maturity (Years)			
	31.01.2019	28.02.2019	31.03.2019
6 month t-bills	0,24	0,25	0,33
12 month t-bills	0,47	0,47	0,56
2 year t-bonds	0,97	0,94	0,99

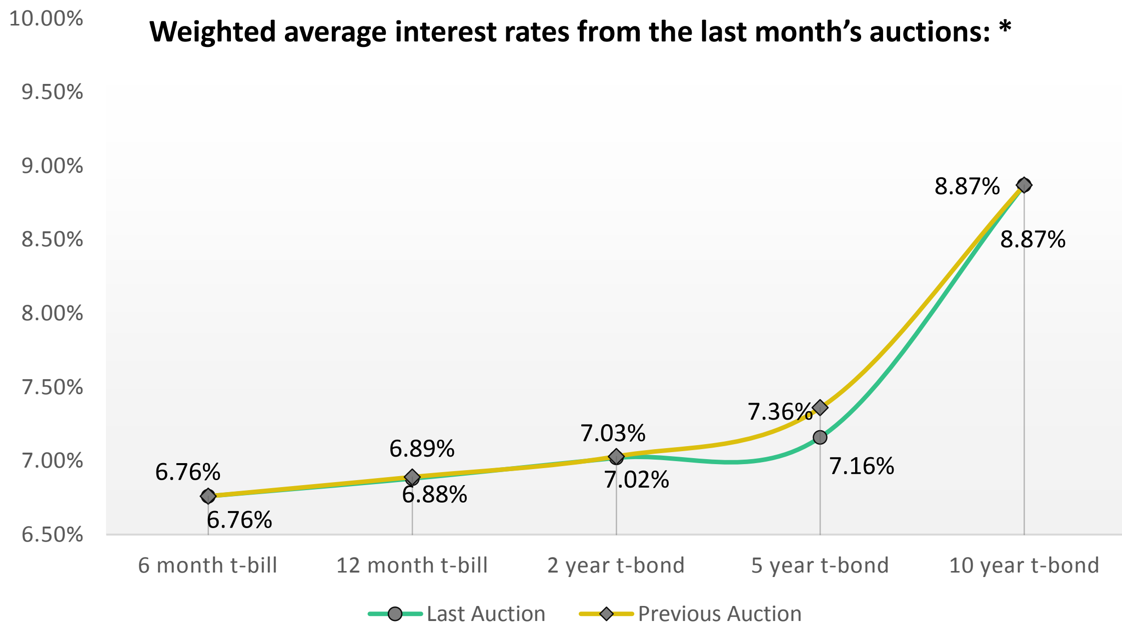
5 year t-bonds	2,80	2,77	2,96
10 year t-bonds	6,71	7,10	6,63
Total	**2,32**	**2,30**	**2,39**

As of March 31, 2019, less than one-fourth of treasury securities portfolio is composed of securities whose maturity date is due for the next 6 months. Securities' distribution by time to maturity is shown below:



Bid-to-cover ratio has decreased compared to the previous month's value (February 2) and is 1.89.





*- If there was no issuance of 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 maintains stable ratings. 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.

Georgia has stable "BB-" rating according to Standard & Poor's evaluation and "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.

S&P and Fitch worsened ratings of Azerbaijan and affirmed to "BB+" negative, which was changed from "BBB+" in 2016. 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. Moody's also decreased rating of Armenia from "Ba3" to "B1". According to Fitch, Armenia's current rating is "B+" positive.

According to S&P and Moody's, Russia's credit rating deteriorated as well. Compared to December of 2014, Russia's credit rating deteriorated from "Baa3" to "Ba1" according to Moody's and from "BBB-" to "BB+" according to S&P. As for the beginning of 2018, Russia rating remained "BBB-" stable according to S&P, while it is "BBB-" positive according to Fitch.

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". 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.

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.