**Medium-term forecast Reconciliation**

# **Basic Macroeconomic and Fiscal Indicators**

The following forecast has prepared as a part of 2020 budget project and it is an updated version of the forecasts attached on the 2019 budget low and 2020-2023 Basic Data and Directions (BDD) document.

The updated forecast is compared to the tables attached to the last year's budget law. Several factors contributed in the change of forecasts. One of the most important was to observe actual figures in the model for the last year instead of estimations and it has an impact on the entire medium-term period. Difference between the forecasts of previous period and actual figures is mostly contributed by introducing of a new methodology of the National Accounts System (SNA 2008), which caused recalculation of GDP data for the past years and respectively caused increase of forecast values. Based on an analysis of current trends and the consultations with various international organizations and IMF mission, some key assumptions were also revised.

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| --- | --- | --- | --- | --- | --- |
| **Table 1. Basic Expectations and Assumptions** |  |  |  |  |  |
|   | **2018** | **2019** | **2020** | **2021** | **2022** |
|   | Actual | Expected | Forecast | Forecast | Forecast |
| Growth of Real GDP, % |   |   |   |   |   |
| Previous Forecast | 5.0% | 4.5% | 5.0% | 5.5% | 6.0% |
| Updated Forecast | 4.8% | 4.8% | 4.5% | 5.0% | 5.0% |
| Difference | -0.2% | 0.3% | -0.5% | -0.5% | -1.0% |
| Percentage Change of GDP Deflator |   |   |   |   |   |
| Previous Forecast | 4.5% | 3.5% | 3.0% | 3.0% | 3.0% |
| Updated Forecast | 4.4% | 5.0% | 3.5% | 3.0% | 3.0% |
| Difference | -0.1% | 1.5% | 0.5% | 0.0% | 0.0% |
| Interest Rates on Loans, % |   |   |   |   |   |
| Previous Forecast | 15.7% | 14.7% | 13.7% | 12.7% | 11.7% |
| Updated Forecast | 16.0% | 15.0% | 14.0% | 13.0% | 12.0% |
| Difference | 0.2% | 0.3% | 0.3% | 0.3% | 0.3% |
| Interest Rates on Deposits, % |   |   |   |   |   |
| Previous Forecast | 8.3% | 7.8% | 7.3% | 6.8% | 6.3% |
| Updated Forecast | 7.9% | 7.4% | 6.9% | 6.4% | 5.9% |
| Difference | -0.3% | -0.3% | -0.3% | -0.3% | -0.3% |

Table 1 reveals the differences in major underlying assumptions. The table also shows the actual values for 2018 in order to present more clearly the effect of the adjustments caused by the changes in the base year. As we can see, the expected value of the real GDP growth in 2019 has increased slightly, however, the forecast for 2022 has decreased by 1.0 percentage point which is related to the revision of global economic growth forecasts. As for the current account balance, given the latest trends, the forecast has improved. A faster than expected improvement of the current account balance is related to a sharp increase in savings in the economy since 2017, driven by recent saving enhancing reforms, such as income tax reform, pension reform, etc.

As Ministry of Finance of Georgia uses a macroeconomic model for forecasting. Changes in the initial period data and adjustment of the initial variables affect the final results, as reflected in the macroeconomic forecasts.

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| --- | --- | --- | --- | --- | --- |
| **Table 2. Change in Nominal GDP** |  |  |  |  |  |
| (Million GEL) | 2018 | 2019 | 2020 | 2021 | 2022 |
|   | Actual | Expected | Forecast | Forecast | Forecast |
| **Previous Forecast of Nominal GDP** | **41,527.2** | **44,914.8** | **48,575.3** | **52,784.4** | **57,630.0** |
| **Total change in Nominal GDP** | **3,072.1** | **4,162.3** | **4,505.2** | **4,622.3** | **4,455.3** |
| **Updated Forecast of Nominal GDP** | **44,599.3** | **49,077.1** | **53,080.6** | **57,406.6** | **62,085.3** |

Table 2 shows the previous and updated forecasts of nominal GDP. As we can see, the new methodology of accounting has increased both actual and projected values of nominal GDP.

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| --- | --- | --- | --- | --- | --- |
| **Table 3. Change in Real GDP** |  |  |  |  |  |
|  | 2018 | 2019 | 2020 | 2021 | 2022 |
|   | Actual | Expected | Forecast | Forecast | Forecast |
| **Previous Forecast of Real GDP** | **16,822.9** | **17,579.9** | **18,458.9** | **19,474.1** | **20,642.6** |
| **Total change in Real GDP** | **21,562.6** | **22,648.1** | **23,579.4** | **24,666.1** | **25,704.7** |
| **Updated Forecast of Real GDP** | **38,385.5** | **40,228.0** | **42,038.3** | **44,140.2** | **46,347.2** |

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| **Table 4. General Government Budget** |  |  |  |  |  |
| (Million GEL) | 2018 | 2019 | 2020 | 2021 | 2022 |
|  | Actual | Expected | Forecast | Forecast | Forecast |
| **Previous Forecasts of Revenues** | **11,624.0** | **12,578.0** | **13,402.0** | **14,250.0** | **15,340.0** |
| **Total Changes** | **198.2** | **127.0** | **210.0** | **501.0** | **465.0** |
| **Taxes** | **6.3** | **30.0** | **173.0** | **282.0** | **367.0** |
| **Grants** | **86.9** | **72.0** | **-63.0** | **3.0** | **18.0** |
| **Other Revenues** | **104.9** | **25.0** | **100.0** | **216.0** | **80.0** |
| **Updated Forecasts of Revenues** | **11,822.2** | **12,705.0** | **13,612.0** | **14,751.0** | **15,805.0** |
| **Previous Forecast of Expenses and Acquisition of Nonfinancial Assets** | **12,201.0** | **13,698.0** | **14,550.0** | **15,409.0** | **16,625.0** |
| **Total Changes** | **151.7** | **214.0** | **549.0** | **785.0** | **795.0** |
| **expenses** | **-92.2** | **106.0** | **700.0** | **1,415.0** | **1,595.0** |
| Wages and Salaries | -8.2 | 23.0 | 86.0 | 162.0 | 150.0 |
| Use Goods and Services | 43.8 | 28.0 | 177.0 | 222.0 | 174.0 |
| Interest | -39.4 | 0.0 | 111.0 | 155.0 | 130.0 |
| Subsidies | 20.9 | 24.0 | 121.0 | 154.0 | 143.0 |
| Grants | -42.4 | -16.0 | 12.0 | -9.0 | -12.0 |
| Social Benefits | 6.5 | 23.0 | 146.0 | 571.0 | 637.0 |
| Other Expenses | -73.3 | 24.0 | 47.0 | 160.0 | 373.0 |
| **Acquisition of Nonfinancial Assets** | **243.9** | **108.0** | **-151.0** | **-630.0** | **-800.0** |
| **Updated Forecast of Expenses and Acquisition of Nonfinancial Assets** | **12,352.7** | **13,912.0** | **15,099.0** | **16,194.0** | **17,420.0** |

The changes in the General Government Budget forecasts are shown in Table 4. As we can see, the updated forecasts of the General Government Budget revenues have increased. The forecasts of budget revenues is estimated based on the projections of macroeconomic indicators. It also considers expected changes in the national tax policy and an improvement in tax administration. The current medium-term fiscal forecast is developed in consultation with the IMF and reflects the costs associated with major policy change related to education reform.

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| **Table 5. Balance of Payment** |  |  |  |  |  |
| Current Account | 2018 | 2019 | 2020 | 2021 | 2022 |
| **(Million US Dollar)** | Actual | Expected | Forecast | Forecast | Forecast |
| **Previous Forecast of Current Account** | **-1,652.4** | **-1,440.1** | **-1,424.2** | **-1,406.2** | **-1,368.7** |
| Total Changes | 459.6 | 720.2 | 797.0 | 778.4 | 709.4 |
| Goods | 494.1 | 981.9 | 1,195.0 | 1,221.9 | 1,302.5 |
| Export of Goods | -61.0 | -39.0 | -17.3 | -54.1 | -124.9 |
| Import of Goods | -555.2 | -1,021.0 | -1,212.3 | -1,276.0 | -1,427.4 |
| Services | -236.2 | -463.6 | -514.6 | -644.7 | -859.1 |
| Export of Services | -308.3 | -502.0 | -530.2 | -605.9 | -766.6 |
| Import of Services | -72.1 | -38.4 | -15.6 | 38.8 | 92.5 |
| Primary Income | 148.4 | 227.8 | 277.1 | 346.4 | 429.7 |
| **Secondary Income (Transfers)** | **53.3** | **-26.0** | **-160.5** | **-145.3** | **-163.7** |
| **Updated Forecast of Current Account** | **-1,192.7** | **-720.0** | **-627.2** | **-627.8** | **-659.3** |

The forecast of the current account balance of the country has also been updated. Specifically, projections for both export and import have been reduced. However, reduction in imports is higher than in exports, which leads the balance of goods and services to improve. Changes in export and import forecasts depict recent trends and outcomes, when the economy showed higher resilience to foreign shocks and net export figures have increased, while having shrinked foreign demand.

Factor income forecasts have increased. Income forecasts have been influenced by 2018 trends. In particular, gross external debt is reduced and international investment position is improved, which reduces current factor payments abroad. At the same time, current transfers slightly reduced, but the overall effect on the current account balance is positive.

The forecast of monetary indicators has also adjusted. Given the current and 2018 trends, it is likely that the broad money forecast for 2019 will exceed its initial forecast. There are also changes in the composition of the banking sector assets. Given the broad money forecast, achieving the inflation target will require managing domestic assets, which can only be done by adjusting the claims on the rest of the economy. However, under the updated forecast, an adjustment of the claims on private sector will not repress the private sector from the credit market and the banking sector will be able to lend to the private sector in order to provide it with the enough financial resources, needed for economic development.

| **Table 6. Review of Depositary Corporations** |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| (Million GEL) | **2018** | **2019** | **2020** | **2021** | **2022** |
|  | **Actual** | **Expected** | **Forecast** | **Forecast** | **Forecast** |
| **Previous Forecast of Broad Money M3** | 21,864.5 | 24,733.6 | 28,171.6 | 32,477.3 | 37,893.8 |
| Changes |   |   |   |   |   |
| Net Foreign Assets | -2,244.7 | -3,544.7 | -3,886.4 | -3,777.3 | -3,617.3 |
| Foreign Assets | -927.9 | 226.4 | 765.5 | 1,023.3 | 1,138.6 |
| Foreign Liabilities | 1,316.8 | 3,771.1 | 4,651.9 | 4,800.6 | 4,755.9 |
| Domestic Assets | 1,504.9 | 4,577.3 | 5,178.5 | 4,818.3 | 3,854.3 |
| Government Net Debt | 432.0 | 419.0 | 51.0 | -190.0 | -413.0 |
| Other Economic Sectors Debt | 1,194.4 | 4,828.5 | 6,355.3 | 6,837.4 | 6,742.9 |
| **Other Components Net** | **-121.5** | **-670.3** | **-1,227.9** | **-1,829.2** | **-2,475.6** |
| **Broad Money M3** | **-739.8** | **1,032.6** | **1,292.1** | **1,041.0** | **237.0** |
| **Updated Forecast of Broad Money M3,**  | **21,124.7** | **25,766.2** | **29,463.7** | **33,518.2** | **38,130.7** |

# **Fiscal Framework**

***(Million GEL)***

|    | **2019** | **2020** | **2021** | **2022** | **2023** |
| --- | --- | --- | --- | --- | --- |
| **Expected** | **Forecast** | **Forecast** | **Forecast** | **Forecast** |
|  |
| **Revenue** |  |
| 2019-2022 Forecast | 12 578,0 | 13 402,0 | 14 250,0 | 15 340,0 |  |
| 2020-2023 Forecast | 12 705,0 | 13 612,0 | 14 751,0 | 15 805,0 | 17 056,0 |
| Difference | 127,0 | 210,0 | 501,0 | 465,0 |  |
|    |
| **Decrease in Non-Financial Assets** |  |
| 2019-2022 Forecast | 150,0 | 130,0 | 130,0 | 130,0 |   |
| 2020-2023 Forecast | 160,0 | 230,0 | 200,0 | 217,0 | 235,0 |
| Difference | 10,0 | 100,0 | 70,0 | 87,0 |   |
|  |
| **Decrease in Financial Assets** |   |
| 2019-2022 Forecast | 110,0 | 90,0 | 100,0 | 110,0 |   |
| 2020-2023 Forecast | 100,0 | 115,0 | 105,0 | 90,0 | 90,0 |
| Difference | -10,0 | 25,0 | 5,0 | -20,0 | 90,0 |
|   |
| **% of GDP** |
| **Revenue** |   |
| 2019-2022 Forecast | 28,0% | 27,6% | 27,0% | 26,6% |   |
| 2020-2023 | 25,9% | 25,6% | 25,7% | 25,5% | 25,3% |
| Difference | -2,1% | -1,9% | -1,3% | -1,2% |   |
|    |
| **Decrease in Non-Financial Assets** |    |
| 2019-2022 Forecast | 0,3% | 0,3% | 0,2% | 0,2% |   |
| 2020-2023 Forecast | 0,3% | 0,4% | 0,3% | 0,3% | 0,3% |
| Difference | 0,0% | 0,2% | 0,1% | 0,1% |   |
|    |
| **Decrease in Financial Assets** |   |
| 2019-2022 Forecast | 0,2% | 0,2% | 0,2% | 0,2% |   |
| 2020-2023 Forecast | 0,2% | 0,2% | 0,2% | 0,1% | 0,1% |
| Difference | 0,0% | 0,0% | 0,0% | 0,0% |   |

There are no substantial changes in the revenue forecasts for the 2020-2023 projections compared to the 2019-2022 forecasts. Revenue forecasts have been adjusted as a result of adjustments for economic growth, including actual figures for 2018, and reflect current performance trends in terms of taxes and other revenues, as well as forecasts of receivables from privatization and decrease in financial assets. It should be mentioned that, the composition of tax revenues has changed this year. Accordingly, amendments to the 2019 Budget Law have been made.

Changes in Revenue forecasts as percent of GDP is caused by the change of the base GDP data related to the introducing new methodology by the National Statistics Office. While, revenues as ratio to GDP declined by almost 2 percentage points, in fact, the revenue forecast remains stable at the same level - on average, up to 25.5% of adjusted (increased) nominal GDP.

***(Million GEL)***

|   | **2019** | **2020** | **2021** | **2022** | **2023** |
| --- | --- | --- | --- | --- | --- |
|   | **Expected** | **Forecast** | **Forecast** | **Forecast** | **Forecast** |
| **Expenditures** |   |
| 2019-2022 Forecast | 10 326,0 | 10 710,0 | 10 979,0 | 11 835,0 |   |
| 2020-2023 Forecast | 10 432,0 | 11 410,0 | 12 394,0 | 13 430,0 | 14 622,0 |
| Difference | 106,0 | 700,0 | 1 415,0 | 1 595,0 |   |
|   |
| **Capital Expenditures** |   |
| **Increase in Non-Financial Assets** |   |
| 2019-2022 Forecast | 3 372,0 | 3 840,0 | 4 430,0 | 4 790,0 |   |
| 2020-2023 Forecast | 3 480,0 | 3 689,0 | 3 800,0 | 3 990,0 | 4 160,0 |
| Difference | 108 | -151 | -630 | -800 |   |
| **Increase in Financial Assets** |   |
| 2019-2022 Forecast | 323,0 | 290,0 | 410,0 | 390,0 |   |
| 2020-2023 Forecast | 230,0 | 177,0 | 360,0 | 360,0 | 340,0 |
| Difference | -93,0 | -113,0 | -50,0 | -30,0 | 340,0 |
|   |
| **% of GDP** |
| **Expenditures** |   |
| 2019-2022 Forecast | 23,0% | 22,0% | 20,8% | 20,5% |   |
| 2020-2023 | 21,3% | 21,5% | 21,6% | 21,6% | 21,7% |
| Difference | -1,7% | -0,6% | 0,8% | 1,1% |   |
|   |
| **Capital Expenditures** |   |
| **Increase in Non-Financial Assets** |   |
| 2019-2022 Forecast | 7,5% | 7,9% | 8,4% | 8,3% |   |
| 2020-2023 Forecast | 7,1% | 6,9% | 6,6% | 6,4% | 6,2% |
| Difference | -0,4% | -1,0% | -1,8% | -1,9% |   |
|  |
| **Increase in Financial Assets** |   |
| 2019-2022 Forecast | 0,7% | 0,6% | 0,8% | 0,7% |   |
| 2020-2023 Forecast | 0,5% | 0,3% | 0,6% | 0,6% | 0,5% |
| Difference | -0,3% | -0,3% | -0,1% | -0,1% |   |

Significant changes in spending compared to 2019-2022 projections are caused by education reform spending which has affected 2019 medium-term forecasts. In particular, the current spending was influenced by the costs of compensation of retired teachers and remuneration increase of certified teachers. Reform also affects capital spending for education infrastructure and equipment.

The spending also reflected the costs of social policies, such as increase of pensions for elderly and social benefits for people with disabilities, including higher increase for elderly above 70 from July 2020.

Considering the ongoing complex infrastructural projects (including the East-West Rikoti highway), forecasts of execution of non-financial assets, is reflected in the coming medium-term projection.

Capital expenditure was also affected by the classification issues. Introducing new GFSM 2014 classification and reclassifying contributions to state-owned enterprises (SOE) from lending to current or capital spending affected the distribution.

Reduction of both current and capital expenditure, as percent of GDP are caused by the methodological changes in Statistics (explained above).

By 2023, fiscal policy will keep current spending low (below 22%) and capital expenditure within 7%. The policy of retaining current spending and deficit low and focusing on capex while implementing education reform and social policies are reflected by both (2020-2023 and 2019-2022) macroeconomic and fiscal forecasts for medium-term.

|   | **Consolidated Budget** | **General Government Budget** |
| --- | --- | --- |
|   | **2019** | **2020** | **2021** | **2022** | **2023** | **2019** | **2020** | **2021** | **2022** | **2023** |
|   |
| **Total balance** |   |
| 2019-2022 Forecast | -970,0 | -1 018,0 | -1 029,0 | -1 155,0 |   | -1 070,0 | -1 140,0 | -1 150,0 | -1 276,0 |   |
| 2020-2023 Forecast | -1 047,0 | -1 257,0 | -1 243,0 | -1 398,0 | -1 491,0 | -1 146,7 | -1 333,4 | -1 323,7 | -1 481,5 | -1 577,4 |
|   |
|  **Modified deficit (IMF program)** |  |
| 2019-2022 Forecast | -1 183,0 | -1 218,0 | -1 339,0 | -1 435,0 |   | -1 283,0 | -1 340,0 | -1 460,0 | -1 556,0 |   |
| 2020-2023 Forecast | -1 177,0 | -1 319,0 | -1 498,0 | -1 668,0 | -1 741,0 | -1 277,0 | -1 395,6 | -1 578,7 | -1 751,5 | -1 827,4 |
|   |
| **% of GDP** |
| **Total balance** |   |
| 2019-2022 Forecast | -2,2% | -2,1% | -1,9% | -2,0% |   | -2,4% | -2,3% | -2,2% | -2,2% |   |
| 2020-2023 Forecast | -2,1% | -2,4% | -2,2% | -2,3% | -2,2% | -2,3% | -2,5% | -2,3% | -2,4% | -2,3% |
|   |
| **Modified deficit (IMF program)** |   |
| 2019-2022 Forecast | -2,6% | -2,5% | -2,5% | -2,5% |   | -2,9% | -2,8% | -2,8% | -2,7% |   |
| 2020-2023 Forecast | -2,4% | -2,5% | -2,6% | -2,7% | -2,6% | -2,6% | -2,6% | -2,8% | -2,8% | -2,7% |

Both the consolidated budget and the general government budget deficit are kept below 3% and accordingly, it fully meets the parameters of the Organic Law of Georgia on Economic Freedom. Deficit growth in nominal terms is due to projections in 2019-2022, with reforms planned in education and social protection and by maintaining high capital costs. The deficit with respect to GDP is reduced compared to the previous fiscal framework. This was influenced by the growth of the nominal GDP base, because of the new methodology. However, even without the changes of this methodology, the general government budget deficit were projected to be below 3% (close to 2.5%).

Current fiscal policy, while incorporating the policy reforms on spending side and financing major infrastructure project, still retains low by 2023, as set by the Organic Law of Georgia “On Economic Freedom” (3%).

# **Government Debt**

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| Government Debt | ***2019*** | ***2020*** | ***2021*** | ***2022*** | ***2023*** |
| 2019-2022 (million GEL) | 19,126 | 20,676 | 21,971 | 23,466 |  |
| % of GDP | 42.6 | 42.6 | 41.6 | 40.7 |  |
| 2020-2023 (million GEL) | 20,050 | 22,579 | 24,274 | 26,225 | 28,315 |
| % of GDP | 40.9 | 42.5 | 42.3 | 42.2 | 42.0 |

Change in projected government debt indicators, which are defined by the Organic Law of Georgia on “Economic Freedom” compared to last year’s projected indicators are mainly caused by the GEL exchange rate fluctuations against foreign currencies in the government debt portfolio and by the expected credit disbursements of investment projects. Projections show that for 2023 government debt fully meets the requirement of the organic law (60%). The parameter is also, close to safe debt level of 40% and it is expected that after medium term period (as major investment projects are completed) government debt will fall below the 40% level.