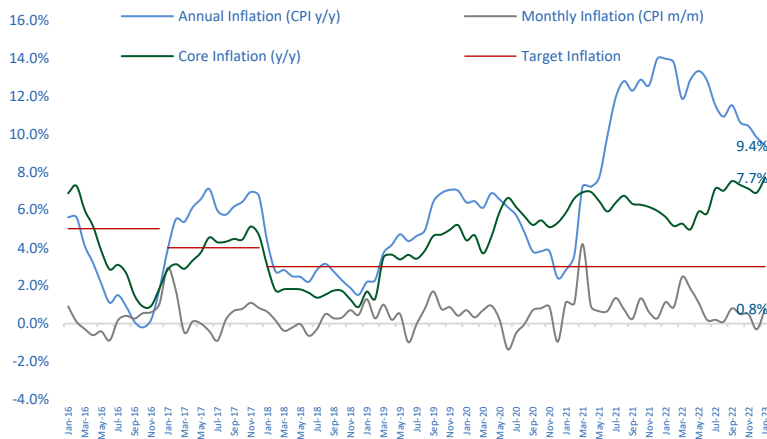


BasisBank Research

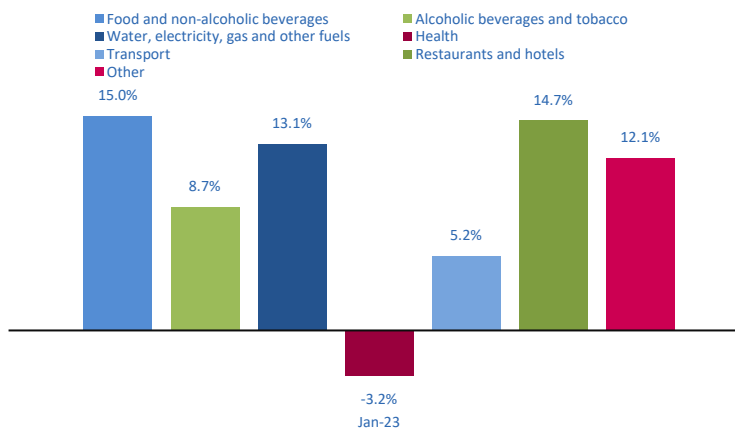
Economic Review

January 2023

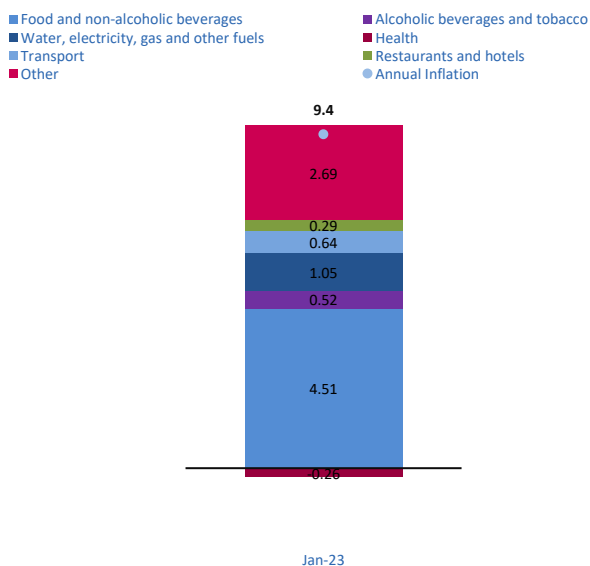
Inflation, Consumer Price Index



Y/Y changes of Groups (%)



Groups Shares in Annual Inflation



Inflation

The inflationary risks increased globally as a result of the Russian-Ukrainian war which slowed the projected pace of decline of high global inflation in the phase of post-pandemic recovery.

The Georgian Consumer Price Index (CPI) increased by 9.4% y/y (+0.8% m/m) in January 2023, while core inflation¹ increased by 7.7% y/y in the same period. So the Consumer Price Index remains high in Georgia compared to the target inflation (3%), but the peak has been overcome and the downward trend has been revealed.

The annual inflation in January 2023 was mainly affected by price changes in food and non-alcoholic beverages (+15% y/y, contribution +4.51 pp), housing, water, electricity, gas and other fuels (+13.1% y/y, contribution +1.05 pp) and transport (+5.2% y/y, contribution +0.64 pp).

The decrease of the annual inflation was partially affected by the decrease of imported inflation which is a result of decreased international shipping costs and commodity prices on a global level as well as the appreciation of Georgian currency. Moreover, energy prices, oil price as well as gas price have lowered globally.

Based on the Food and Agriculture Organization (FAO), *the international food price index (FFPI)* has been declining since April after the index hit the all-time high in March 2022. The index has fallen 17.9% after the peak in March 2022. *In January 2023 the index was down 0.8% from December, marking the tenth consecutive monthly decline.* The drop in the index in January was driven by declines in the price indices of vegetable oils, dairy and sugar, while those of cereals and meat remained largely stable.

The NBG expects that the inflation will average 5.4% in 2023 and will return to its target in the second half of the year (until then, the NBG keeps the monetary policy rate high, at 11%). Even though there are some positive global trends, inflationary risks remain high and with cautious optimism future dynamics is still characterized by high uncertainty.

It should be noted that the high inflation in Georgia is driven by demand side pressure promoted by migrated individuals amid the Russian-Ukrainian war, so the effect of the tight monetary policy followed by the NBG (coupled with the increased interest rates on USD and EUR funds) intended to mitigate demand side pressure on the price level is fair. On the contrary, higher interest rates increase the cost of funds for businesses while aggregate demand is not affected, which could further propagate the inflation.

Moreover, in Georgia, market wages are rising faster than productivity, so there is a significant increase of personnel costs per unit of production which further pressures the inflation from the labor market.

As for *the producer price index (PPI)* for industrial products, it increased by 1% in January 2023 compared to the previous month, while compared to the previous year the index growth amounted to 1.8%.

The annual producer inflation was mainly affected by price changes for the following products: products from mining and quarrying: -9.8% y/y, contributing -0.76 ppts to the overall annual index change; manufactured products: +3.2% y/y, contributing 2.58 ppts to the overall annual index growth; electricity, gas, steam and air conditioning: +1.6% y/y, contributing 0.13 ppts to the annual index change; water supply, sewerage, waste management and remediation services: -6% y/y, contributing -0.16 ppts to the annual index growth.

Exchange Rate

In January 2023, the **lari nominal effective exchange rate appreciated by 24.6% y/y** and by 0.9% YTD (compared to December 2022) while **the real effective exchange rate appreciated by 15.4% y/y** and depreciated a bit, by 0.1% in YTD terms.

The trend of appreciation of the nominal effective exchange rate in 2022 continued in 2023. The appreciation of the nominal effective exchange rate is driven by appreciation of lari against the main trading partners' currencies. In 2023², lari appreciated against the USD by 2.8%, against the EUR by 3.8%, GBP by 3.4%, Turkish lira by 3.6%, Chinese Yuan – 3.3%, Azerbaijan Manat – 3%, the Ukrainian hryvnia – 2.8%, Armenian Dram – 1.8%. As for the Russian Ruble, lari appreciated by 5% from December 31, 2022 to February 28, 2023.

Appreciation of the nominal effective exchange rate worsens a country's competitiveness on the international markets but at the same time reduces imported inflation.

Based on the chart, we can say that nominal effective exchange rate as well as the real effective exchange rate are above their long-term trends, so the exchange rate is somewhat appreciated even when the US dollar is very strong against all currencies. So, it is expected that in the long run lari will somewhat depreciate.

International Trade

Georgian external trade turnover amounted to \$1.46 billion in January 2022, which is a 29.1% increase compared to the same period of last year.

The value of exports increased by 38.5% y/y and amounted to \$459 million in the reported period, while imports also grew by 25.2% y/y, amounting to \$1 billion.

The negative trade balance widened to \$543.9 million (+\$74.2 mln, +15.8% y/y) in January 2023.

In January 2023 **Georgia's top partners by exports** were Russia (\$87.8 million, +105.7% y/y), Armenia (\$69.8 million, +235.6% y/y) and Azerbaijan (\$51.9 million, +11% y/y), while the top markets by imports were Russia (\$175.8 million, +104.5% y/y), Turkey (\$164.7 million, +14.3% y/y) and Azerbaijan (\$68.5 million, -11% y/y).

The exports in the EU decreased by 13.3% y/y in 2022, while the share of the EU in the total exports amounted to 16%. **Imports from the EU** increased by 30.1% y/y and the share amounted to 23.6%.

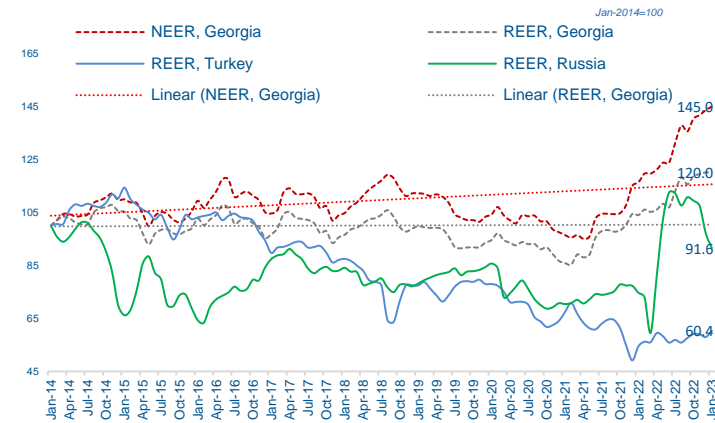
As for the CIS countries, the exports increased by 67.8% y/y and amounted to 60.3% of the total exports. **Imports from the CIS countries** increased by 33.1% and the share amounted to 30.9%.

In the reported period, **top import commodities** were petroleum gases (+40.3% y/y, 9.2% share of the total imports) followed by motor cars (-11% y/y, 8.6% share) and petroleum oils (+13.2% y/y, 8.2% share).

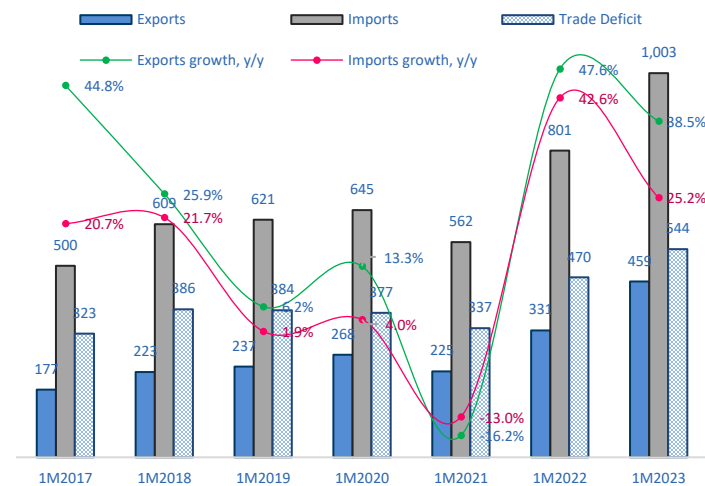
Furthermore, in January 2023, motor cars reclaimed the first place in **the list of top export items** (+186.6% y/y, 22.7% share of the total exports) followed by copper ores and concentrates (+2.7% y/y, 14.8% share) and the export of ferro-alloys (+61.8% y/y, 11.1% share).

Share of the domestic³ exports in the total exports constituted 56.4% and amounted to \$258.8 million in January 2023 which is 11.8% higher compared to the same period of 2022.

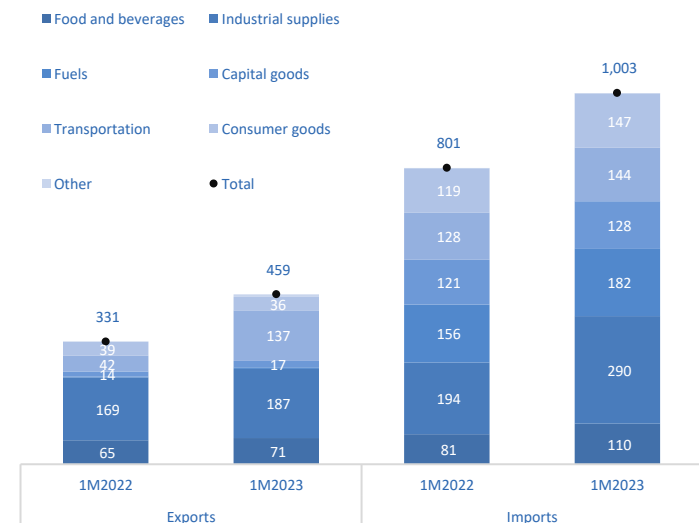
Effective Exchange Rate



International Trade, US\$ Mln



Exports/Imports (Broad Economic Categories), US\$ Mln



Export and Import Statistics, 1M 2023, US\$ Mln

Countries	Exports	Share	Change, y/y	Products	Exports	Share	Change, y/y
Total Exports	459		47.6%	Total Exports	459		47.6%
Russia	88	19.1%	105.7%	Cars	104	22.7%	186.6%
Armenia	70	15.2%	235.6%	Copper	68	14.8%	2.7%
Azerbaijan	52	11.3%	11.0%	Ferro-alloys	51	11.1%	61.8%
Kazakhstan	33	7.2%	433.5%	Fertilizers	21	4.5%	18.1%
China	32	6.9%	14.0%	Motor vehicles for the tra	18	3.9%	100.0%
Turkey	31	6.8%	13.7%	Wine	16	3.5%	8.1%
Bulgaria	26	5.6%	-48.3%	Spirituos beverages	13	2.8%	43.7%
Spain	19	4.2%	2332.1%	Gold	10	2.2%	49.4%
Peru	17	3.7%	24461.0%	Cigars, cheroots, cigarillos	8	1.7%	154.6%
Kyrgyzstan	16	3.6%	1031.8%	Nuts	8	1.6%	-1.8%
Germany	8	1.7%	53.9%	Mixed goods	7	1.5%	11070.4%
Other	67	14.7%	-30.1%	Other	137	29.7%	3.3%

Countries	Imports	Share	Change, y/y	Products	Imports	Share	Change, y/y
Total Imports	1,003		42.6%	Total Imports	1,003		42.6%
Russia	176	17.5%	104.5%	Gases	92	9.2%	40.3%
Turkey	165	16.4%	14.3%	Cars	86	8.6%	-11.0%
Azerbaijan	68	6.8%	-11.0%	Oils	82	8.2%	13.2%
China	65	6.5%	3.8%	Copper	72	7.2%	2816.8%
Germany	63	6.3%	93.7%	Telephones	28	2.8%	16.4%
United States	51	5.0%	18.2%	Medicaments	23	2.3%	-4.6%
Armenia	30	3.0%	153.7%	Vehicles for transport	15	1.5%	35645.2%
Indonesia	27	2.7%	4085.6%	Tractors	9	0.9%	55.5%
United Arab Emirates	23	2.3%	37.4%	Computers	9	0.9%	-51.7%
France	22	2.2%	105.3%	Motor vehicles	8	0.8%	42.5%
Chile	21	2.1%	100.0%	Other bars and rods of iron	7	0.7%	-21.7%
Other	292	29.1%	-0.9%	Other	571	56.9%	19.3%

Remittances

The volume of money transfers from abroad constituted about \$445 million in January 2023, which is 163.5% (\$276.1 million million) more than the amount in January, last year.

The top remittance senders in January 2023 were **Russia (60.1% of the total transfers, +1095.7% y/y)**, Italy (8.9% share, +18.9% y/y) and the USA (6.4% share, +40.8% y/y).

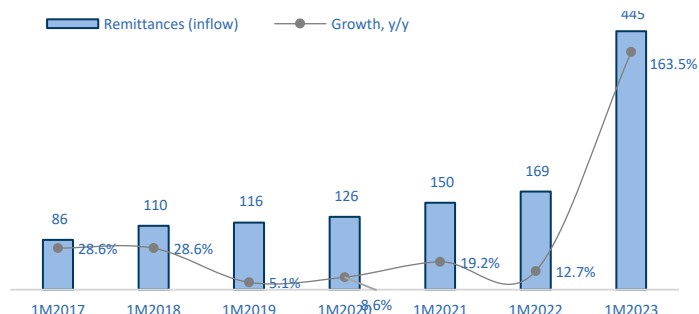
Russia was the major remittance sender to Georgia for years but the share had been decreasing over time. However, the volume of remittances from Russia increased significantly from April 2022. We see that the share of Russia started to increase as well starting April 2022 (with some decrease in July) and amounted to 60.1% in January 2023.

The increase of remittances from Russia might be related to the migrants who entered Georgia due to the Russia-Ukraine war as their family members might send money transfers to them to cover their living expenses in Georgia. Also, Georgians living in Russia might send more as they think about returning home.

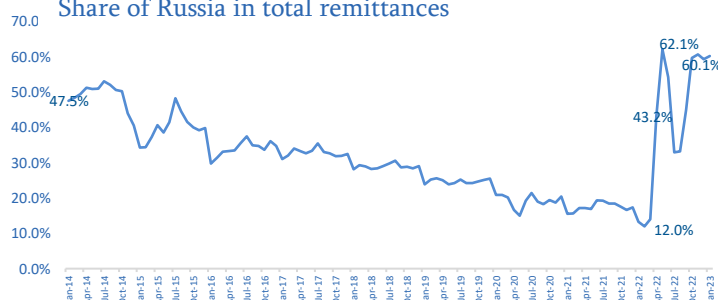
We exclude the exchange rate effect to see if increased remittances from Russia is linked to Ruble significant appreciation which has been the tendency after its quick and sharp depreciation in March 2022.

In January 2023, remittances from Russia increased 12 times year-on-year, while remittances from other countries excluding Russia increased by only 21.1%. Moreover, excluding the exchange rate effect, remittances from Russia increased 10.7 times. So we see that the exchange rate effect has no significant connection to remittance growth and in reality remittance growth from Russia is really remarkable.

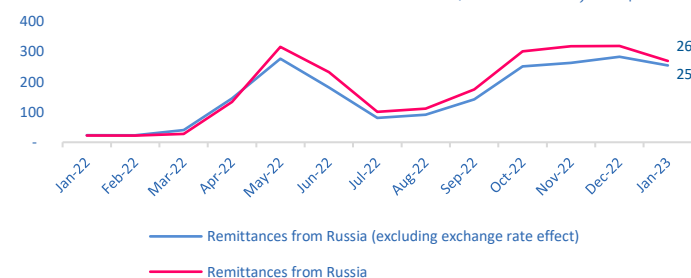
Remittance Statistics, 1M 2023, US\$ Mln



Share of Russia in total remittances



Remittances from Russia with and w/o fx effect, US\$ Mln



State Budget

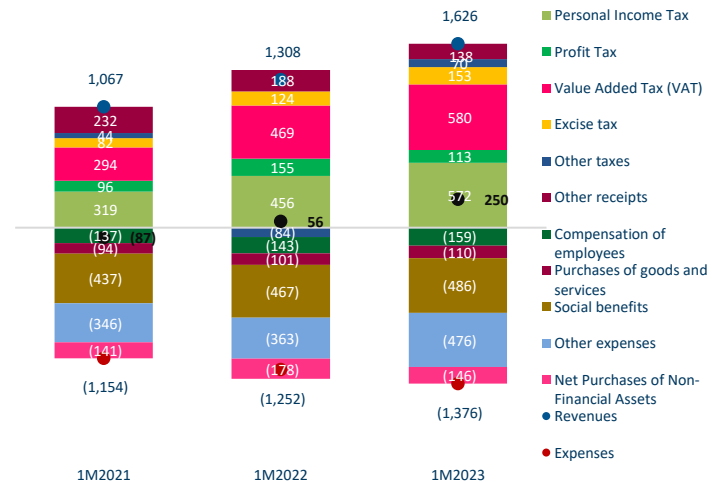
In January 2023, the state budget revenues increased by 24.3% y/y to 1.63 bln GEL, while the total expenses increased by 9.9% to 1.38 bln GEL.

The revenues from value added tax increased by 23.8% y/y to 35.7% of budget revenues, while revenues from excise and income taxes increased by 23.1% y/y to 9.4% of the total revenues and by 25.4% y/y to 35.2% of the total revenues, respectively. Meanwhile revenues from profit tax decreased by 27% y/y and amounted to 7% of the total revenues.

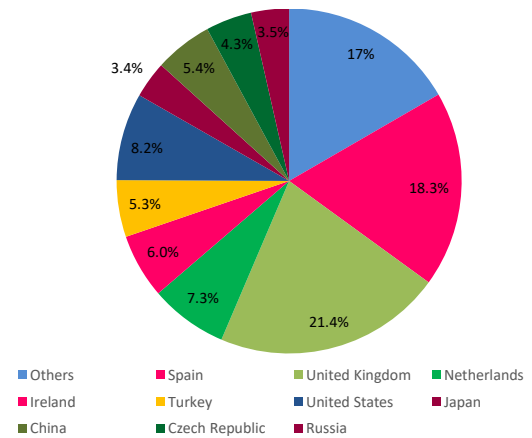
On the spending side, social benefits increased by 3.9% y/y to 35.3% of the total budget expenses in January 2023, while compensation of employees increased by 10.8% y/y to 11.5% of the total expenses and purchases of goods and services increased by 8.5% y/y to 8% of the total expenses.

As a result, the budget surplus in January 2023 expanded by 342.4% y/y from 56 mln GEL to 250 mln GEL.

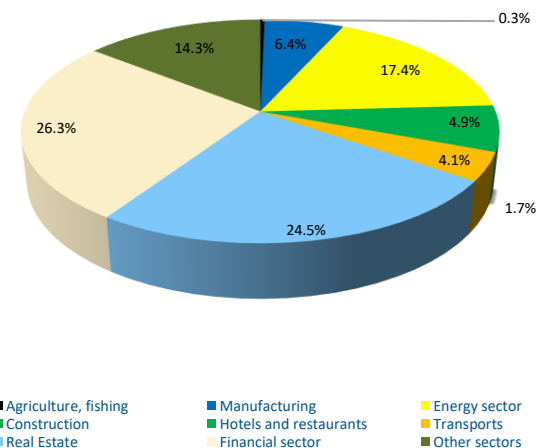
Budget Statistics, Mln GEL



Shares of countries in total FDIs in 2022



Shares of sectors in total FDIs in 2022



Foreign Direct Investments

Foreign direct investments (FDI) in Georgia amounted to \$324 million in the fourth quarter of 2022 which is 21% less compared to Q4 2021, while FDIs in 2022 as a whole increased by 61% compared to last year and by 48% compared to the pre-pandemic period of 2019. In total, FDIs amounted to about \$2 billion in 2022.

In 2022, the reinvestment of earnings (\$1.29 billion, up 67.5% y/y), which is the difference between profit/loss and dividends, was the major component with the share of 64.5% in total FDIs.

As for the classification by size of enterprises, more than ¾ of FDIs were invested in large size enterprises, so the share of large companies amounted to 77% of the total FDIs carried out in Georgia in 2022.

The highest share of FDIs in 2022 came from the United Kingdom (21%) followed by Spain (18%), USA (8%), Netherlands (7%) and Ireland (6%).

The financial sector contributed the highest share (26.3%) in 2022 in total foreign direct investments with 13% annual growth followed by the real estate sector (24.5% share) with 345% annual growth. The energy sector was in the third place with 17.4% share in total FDIs and with 87% annual growth.

¹Net of food and energy prices

²Estimated period: 31/12/2022 – 28.02.2023

³Exports excluding re-exports

⁴Visitor is a traveler aged 15 or above, non-resident of Georgia, took a trip outside his/her usual environment to Georgia for less than a year (except following categories: employment, diplomatic or consular officers accredited to Georgia, Armed Forces servants and their dependants and persons who frequently cross borders); International visitor trips include tourist (overnight visitor) trips and same day trips (same-day visitors)

⁵Total income in January-November 2022 over total number of visits from the country in the same period



BASISBANK
Hualing Group Member

1, Ketevan Tsamebuli Ave., Tbilisi, Georgia

Tel.: +995 322 922 922

www.basisbank.ge