GEORGIA

The economy posted double-digit growth in 2022, reflecting strong exports and an influx of Russian citizens. Growth should moderate in 2023 and 2024. Demand-side factors raised inflation despite tight monetary policy and a smaller fiscal deficit. Slowing domestic demand and tighter macroeconomic policies should trim inflation. Strong foreign inflows substantially narrowed the current account deficit, which will likely widen again in 2023 and 2024. It is critical to address climate change to minimize losses from disasters and promote green growth.

Economic Performance

In 2022, the economy performed strongly, as expected adverse spillover from the Russian invasion of Ukraine failed to materialize. Growth was estimated at 10.2% in 2022, little changed from 10.5% in 2021, driven mostly by industry (Figure 2.3.1). Industry growth accelerated from 3.2% in 2021 to 15.4%, led by gains in mining at 21.2%, construction 6.2%, and utilities 48.9%. Despite sharp recovery in tourism and strong expansion in information and communication at 36.8% and transport at 27.2%, growth in services slowed from 15.0% in 2021 to 9.6% as growth moderated to 22.5% in accommodation and food services, 5.4% in financial and insurance services, and 18.7% in arts, entertainment, and recreation. Health and social work shrank by 3.3%. Favorable weather and increased demand for food boosted expansion in agriculture from 1.4% in 2021 to 4.2%.

Both domestic and external demand lifted growth. Private consumption grew by 9.7%, little changed from 9.5% in 2021, largely on spending by an influx of Russian migrants. Meanwhile, private investment reversed a decline in 2021 to grow by 5.9%. After flatlining in 2021, net exports of goods and services expanded by 10.8% on higher exports of both merchandise and services related to travel and transport.

Inflation remained elevated, reflecting strong domestic demand. Inflation accelerated from 9.6% in 2021 to 11.9% on a sharp rise in consumption, mainly by Russian migrants, and higher wages. Inflation rose from 10.9% in 2021 to 17.9% for food, from 7.1% to 8.9% for other goods, and from 6.9% to 6.8% for services (Figure 2.3.2). However, core inflation moderated in the second half of 2022 as fuel and transportation costs abated. The Georgian lari appreciated in 2022 by 27.1% in nominal terms and 18.8% in real effective terms, easing inflation (Figure 2.3.3).

Figure 2.3.1 Supply-Side Growth

Double-digit growth continued in 2022, led by industry and services.

Source: National Statistics Office of Georgia.

This chapter was written by George Luarsabishvili of the Georgia Resident Mission, ADB, Tbilisi.
continued to expand but more slowly, driven mostly by local currency lending as foreign currency loans became more expensive, and as the central bank implemented new macroprudential measures to curb unhedged borrowing (Figure 2.3.5). Bank deposits, mainly by nonresidents, increased by 11.8%. Nonperforming loans remained under 2% of all loans despite a rise in restructured loans in the hospitality industry. The financial position of banks remained sound, with high liquidity and substantial profitability thanks to strong returns on assets at 3.8% and equity at 30.2%.

Revenue overperformance sharply narrowed the budget deficit from the equivalent of 6.1% of GDP in 2021 to 2.8% in 2022 (Figure 2.3.4). Revenue increased by 27.0%, rising from 25.4% of GDP in 2021 to 26.6%. Fiscal consolidation helped cut current expenditure from 25.6% of GDP in 2021 to 23.0% despite a 10% rise in the public wage bill. Total expenditure declined from 31.5% of GDP in 2021 to 29.4%, with capital spending sustained at about 7% of GDP. Public debt declined from 49.7% of GDP in 2021 to 39.6%.

The National Bank of Georgia, the central bank, has maintained its policy rate at 11% since March 2022 to control inflation. Broad money grew by 11.6%, little changed from 11.3% in 2021. Credit growth slowed with tight monetary policy.
The balance of payments strengthened on buoyant tourism revenue, a surge in financial inflows, and higher transit trade. The current account deficit narrowed sharply from the equivalent of 10.4% of GDP in 2021 to 3.2% despite the merchandise trade deficit widening because of higher imports of petroleum products, automobiles, and intermediate inputs such as metals. Growth in merchandise exports accelerated from 27.4% in 2021 to 32.3% on increased vehicle reexports and exports of fertilizer and of copper ore and concentrates. Higher commodity prices in the first half of 2022 and strong domestic demand boosted import growth from 24.2% in 2021 to 31.6%. Tourism inflows exceeded the pre-pandemic 2019 peak by 7.6%, while inward money transfers surged by 86.1% to a record 17.7% of GDP, mainly as multiple waves of Russian settlers brought capital into Georgia. Money transfers from the US and European Union also increased (Figure 2.3.6). These favorable conditions enabled the central bank to rebuild gross international reserves to a record high of $4.9 billion, cover for 4 months of imports of goods and services. External public debt declined from the equivalent of 39.9% of GDP at the end of 2021 to 29.8% a year later. Foreign direct investment almost doubled to $2.0 billion in 2022, mainly reflecting reinvested earnings.

Economic Prospects

Growth is forecast to slow considerably. In 2023, growth will decelerate to 4.5% as migrant and financial inflows are expected to subside, and as slower growth or recession in trade partners inhibits export growth and cuts money transfers (Figure 2.3.7 and Table 2.3.1). Growth should reaccelerate to 5.0% in 2024 with continued gains in services. On the supply side, industry is forecast to expand by 3.9% in 2023 and 4.9% in 2024, with continued increases in construction. Services are projected to grow by 5.2% in 2023 and 5.7% in 2024 from continued expansion in service exports and tourism. Agriculture is expected to grow in both 2023 and 2024, reflecting government investment in modern farm technologies.

**Table 2.3.1 Selected Economic Indicators, %**

<table>
<thead>
<tr>
<th></th>
<th>2021</th>
<th>2022</th>
<th>2023</th>
<th>2024</th>
</tr>
</thead>
<tbody>
<tr>
<td>GDP growth</td>
<td>10.5</td>
<td>10.2</td>
<td>4.5</td>
<td>5.0</td>
</tr>
<tr>
<td>Inflation</td>
<td>9.6</td>
<td>11.9</td>
<td>6.0</td>
<td>4.0</td>
</tr>
</tbody>
</table>


Domestic demand will grow more slowly, assuming no more waves of Russian migrants. On the demand side, growth in private consumption is expected to moderate to 4.9% in 2023 because of tight monetary policy and reduced consumer purchasing power as inflation remains elevated, then reaccelerate somewhat to 5.6% in 2024. Investment is projected to expand by 5.5% in 2023 and 3.5% in 2024 as business confidence continues to improve. A widening trade deficit is expected to drive net exports down by 8.1% in 2023 and 8.0% in 2024.
Inflation is projected to slow to single digits in 2023 and 2024. Tight monetary policy, weaker domestic demand, and improved supply chains are expected to cut inflation to 6.0% in 2023 and further to 4.0% in 2024, approaching the central bank’s 3.0% target (Figure 2.3.8). An assumed lack of further waves of migrants should trim inflation. Broad money is projected to grow by 11.5% in 2023 and 11.1% in 2024, reflecting expected increases in credit growth to 13.3% in 2023 and 12.4% in 2024 with higher private sector investment.

The budget deficit is projected to decline to the equivalent of 2.7% of GDP in 2023 and 2.5% in 2024. This will reflect strengthened revenue administration, sound debt management, and fiscal consolidation to ensure compliance with a rule that limits Georgia’s fiscal deficit to 3% of GDP. Revenue is forecast to equal 26.0% of GDP in 2023 and 25.8% in 2024. Expenditure is projected at 28.7% of GDP in 2023 and 28.3% in 2024 as current expenditure is kept in check and capital expenditure is maintained, with infrastructure spending targeted at about 7% of GDP to support growth. Public debt is projected to decline to 39.0% of GDP in 2023 and 38.5% in 2024, barring an unlikely major depreciation of the local currency (Figure 2.3.9). Structural reform could support fiscal sustainability by incorporating climate resilience issues into the public investment management framework and quantifying fiscal risks that stem from natural hazards.

The current account deficit is forecast to widen to equal 5.0% of GDP in 2023 and 6.0% in 2024 as the trade deficit deepens. Export growth is expected to decelerate to 10.7% in 2023 as slower expansion in the euro area and recession in Russia could affect external demand and supply chains, then edge up to 11.2% in 2024. Import growth is also expected to diminish to 11.6% in 2023 and 6.2% in 2024 in line with slowing domestic economic expansion. Services should rise by 18.8% in 2023 before moderating to 11.2% in 2024 as tourism and transportation services revive and subsequently slow. Money transfers are forecast to fall to $2.5 billion in each year as external inflows from migrants moderate, possibly creating exchange rate pressures. Gross reserves are projected at $4.6 billion in 2023 and $4.7 billion in 2024. Public external debt is projected to fall to the equivalent of 28.0% of GDP at the end of 2023 and 27.5% a year later, and total external debt to 73.1% and then 68.4%.

Risks skew to the downside. A prolonged Russian invasion of Ukraine would hinder global recovery and stoke inflation, possibly shrinking external demand and new investment, driving down production, and stemming inflows from tourism. On the other hand, a strong upturn among key trading partners, increased transit trade, and further inward migration from Russia could boost growth but also inflation.
Policy Challenge—Addressing Climate Change to Mitigate Disasters and Promote Green Growth

Georgia is highly susceptible to floods, droughts, forest fires, landslides, and mudslides under climate change. Worsening floods have destroyed property and crops and damaged infrastructure. Droughts and forest fires in eastern Georgia have degraded soils and fertility, undermining harvests and food security. Less snowfall in the mountains has hindered winter tourism and the hospitality industry, which provide nearly 20% of GDP. In addition, mudslides and landslides have required the government to fund the rehabilitation of affected infrastructure.

Georgia joined the Paris Agreement in 2015 and committed to achieving carbon neutrality by 2050. Georgia has allocated more than $1 billion to meet its climate targets in a national climate strategy for a just transition to low-emission, climate resilient development. The country strives to increase the share of renewable hydro, wind, and solar energy to 87% of electricity production by 2030. Under its revised nationally determined contributions, Georgia committed to reducing greenhouse gas emissions by at least 15% below business as usual by 2030, including reductions of 15% in transportation and in electricity generation and transmission, and 5% in agriculture and industry.

The government has developed sector initiatives. Programs address carbon emissions from the energy sector, which contributes about 60% of Georgia’s carbon footprint; agriculture with 20%; manufacturing and transport 11%; and waste management 9%. Georgia currently uses only an estimated quarter of its rich hydropower resources, and the country aims to generate 100% of its electricity consumption from renewable sources by 2050 by expanding renewable energy generation capacity. The government has taken measures to ensure responsible energy consumption by supporting climate resilient housing projects, with the ultimate goal of housing stock in full compliance with new building code standards requiring 100% thermal insulation. Georgia takes advantage of technological know-how such as remote sensing to map agricultural land and prevent crop failure by matching climate-resilient crop variates with local climatic conditions, as well as climate smart irrigation and agriculture, using modern, innovative technologies. It aims to limit growth in carbon-intensive industries and bolster energy-efficient transport such as electric vehicles with a wide network of charging stations. Georgia has made efforts to reduce emissions through recycling and improved waste management, strengthen forest management in support of a clean ecosystem and green tourism, and streamline practices for natural resource extraction and sustainable rural development.

To preserve biodiversity for sustainable eco- and agri-tourism, Georgia should further strengthen its environmental policies. Disaster and climate risks could be mainstreamed by including in the government’s framework for managing public investment quantified fiscal risks stemming from climate change and natural hazards and by targeting expenditure for greenfield and brownfield investment. Benefits would accrue from cost–benefit analyses of new tax incentives that promote green growth and introduce climate-smart technologies in agriculture, and from identifying suitable policy options to shift toward greener transport alternatives, such as redirecting freight from road to rail transport.

Georgia can explore other ways to accelerate its transition to green growth without jeopardizing its development goals or growth prospects. These include accelerating trade digitalization, as a significant portion of global greenhouse gas emissions stem from trade and supply chains linked to company operations. Georgia can further benefit from decarbonization by trading emissions through global market mechanisms to support appropriate incentives for energy use and increase revenue for low-emitting firms. Georgia will thus be able to join an emerging cohort of climate-conscious countries that promote a green economy based on clean energy. The government should also do more to engage the private sector in its climate-friendly policies and provide climate financing incentives with shared risk, to ensure greener and more sustainable private sector development.