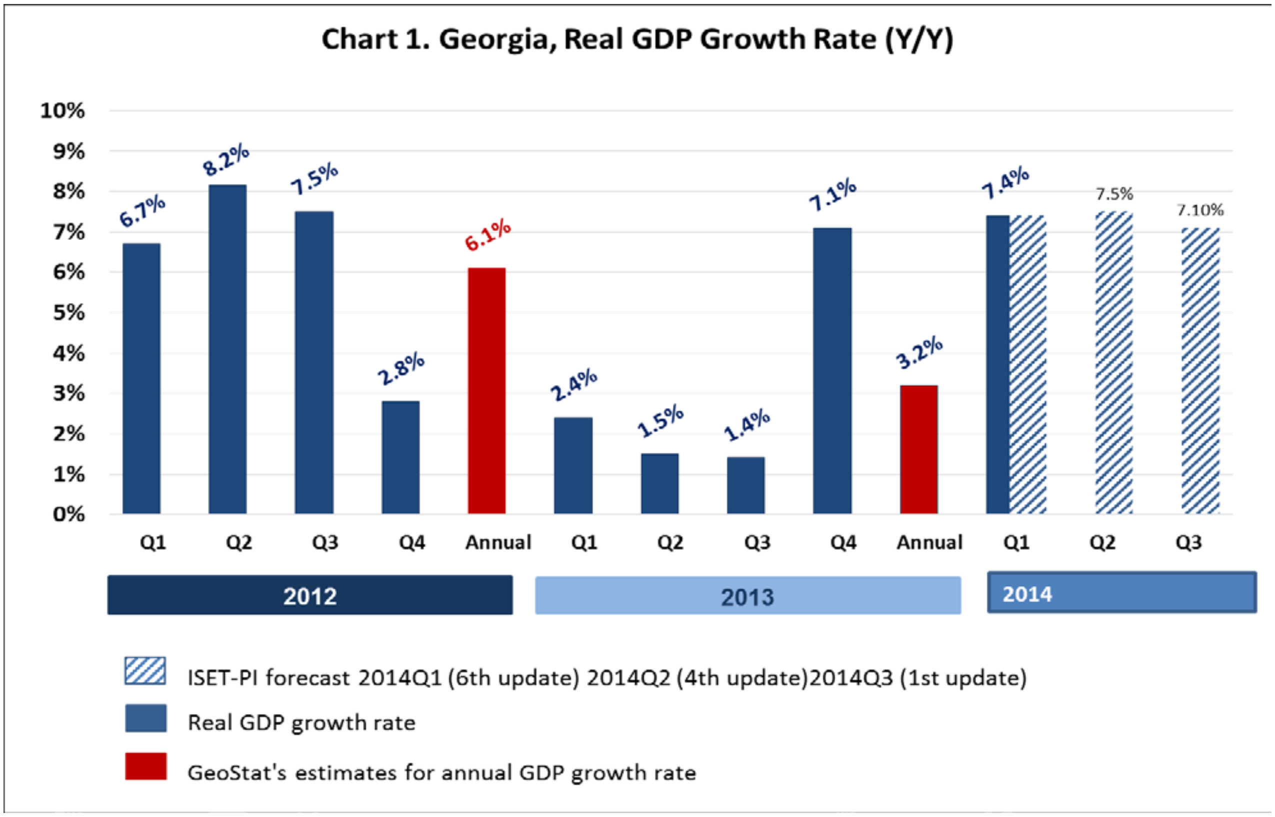
Leading GDP Indicator for Georgia

June 2014 report

Little has changed in quarterly growth patterns

ISET-PI has updated its forecasts for Georgia's real GDP growth rates using the April 2014 releases of various economic indicators.

- The growth forecast for the second quarter of 2014 has been revised downward from 7.7% to 7.45%.
- The growth forecast for the third quarter of 2014 has been targeted at 7.1%. Meanwhile, Geostat has released the GDP growth rate for the first quarter of 2014 and its preliminary estimates for April. These are 7.4% and 2.7% respectively. The April growth rate seems to be very low in relation to our forecast, but this low growth figure is most likely due to the relatively high GDP increase in April last year.
- Since the beginning of the year, we have been drawing some conclusions about the annual growth rate for 2014. The methodology that we use and the scenario description is explained in our February and January publications. Given these developments, we expect the annual growth rate in 2014 to be 6.2% at the very least, and it is more likely to be somewhere around 6.6%.



After gradually returning to a high growth rate, the Georgian economy seems to have slowed down once again – at least according to Geostat's preliminary estimates for April (GDP growth was 2.7% in y-o-y terms). Our forecast, however, is not as alarming. The forecasted quarterly growth rate (April-June 2014) has been revised downward, but still stands at 7.45%. Admittedly, if Geostat's estimates prove to be accurate, the monthly growth rates of May and June would have to be very high in order to catch up with our predicted quarterly growth.

Such a large difference in the estimates is mainly caused by the choice of underlying indicators the respective forecasts use. Geostat's forecast uses VAT payers' turnover to predict the growth rate for any given month. In April 2014, the VAT turnover level went down, and its year-on-year growth rate declined drastically from 19.6% in March to 4.8% in April.

This drop might have been caused by several factors. For one, the car import and re-export sector, which has been a very important part of the Georgian economy, has significantly slowed down in recent times. The slowdown is mainly a result of current and expected policy changes in Azerbaijan, Turkey and Armenia.

The more likely explanation for the decline of growth in April 2014, however, is the fact that April 2013 was a particularly good month for the Georgian economy. The government's plowing and agricultural voucher programs provided a temporary boost, after which growth rates reverted to the usual trend. The growth rate of April 2014 does not look impressive precisely because it is being compared to the relatively high GDP level of April 2013.

The indicators used in our forecast for the second quarter of 2014 show mild signs of economic weakening, but nothing so dramatic as to suggest a sharp slowdown of growth in the future.

On the negative side, the performance of the external sector has slowed down. In particular the y-o-y growth rate of exports stood at only 7.6% in April. By means of comparison, exports grew by as much as 23.8% in March 2014. In addition, electricity exports declined by 130% in April in y-o-y terms.

On the positive side, interest rates on different types of loans have declined, and money aggregates, as well as the volume of total credit, have increased. The Consumer Confidence Index has also risen, suggesting a slight improvement of both the expectations and current situation indices.

Moreover, inflation remained stable with the Consumer Price Index increasing by 3.4% in April as compared with the same month last year and by 0.3% compared to March 2014. The Khachapuri Index, however, recorded a bigger price increase: suggesting an increase of 12% compared to last April and 5% compared to March 2014.

Our forecasting model is based on the Leading Economic Indicator (LEI) methodology developed by the New Economic School, Moscow, Russia.[2] We constructed a dynamic model of the Georgian economy which assumes that all economic variables, including the GDP itself, are driven by a small number of factors, that can be extracted from the data well before the GDP growth estimates are published. For each quarter, ISET-PI produces five consecutive monthly forecasts ("vintages"), which increase in precision as time goes on. Our first forecast (1st vintage) is available about 5 months before the end of the quarter in question. The last forecast (5th vintage) is published in the first month of the next quarter.