Ladies and gentlemen,

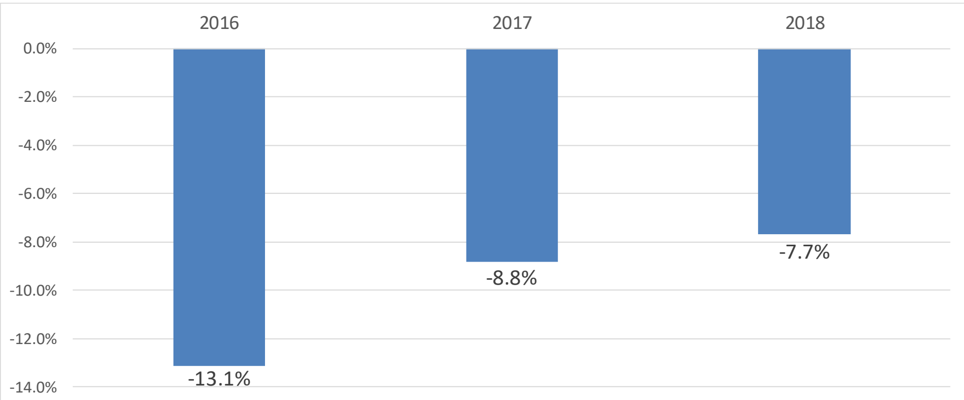
The National Bank of Georgia (NBG) publishes quarterly Monetary Policy Report, providing detailed forecasts of inflation and other macroeconomic indicators, which play a key role in the formation of monetary policy.

As you all know, the main objective of the NBG is to maintain price stability, which, in turn, is a necessary precondition for long-term economic growth and maximum employment.

According to preliminary information, economic growth was at 4.7% in the first quarter of 2019. The main driver of the growth are export revenues, among them – tourism revenues. At the same time, domestic demand, which is the main determinant of inflation, remains weak.

In recent periods, current account deficit has a declining trend and it stood at 7.7% in 2018. Current account shows a balance between expenditures and revenues from the external sector. The expenditures include imports, or dividends and interest payments to foreign investors, while the revenues are mainly composed of proceeds from merchandise exports and tourism, money transfers, etc. Other things equal, improvement in the current account deficit reduces inflationary pressure coming from the exchange rate. According to the preliminary data, improvement of the current account deficit continued in the first quarter of 2019 as well.

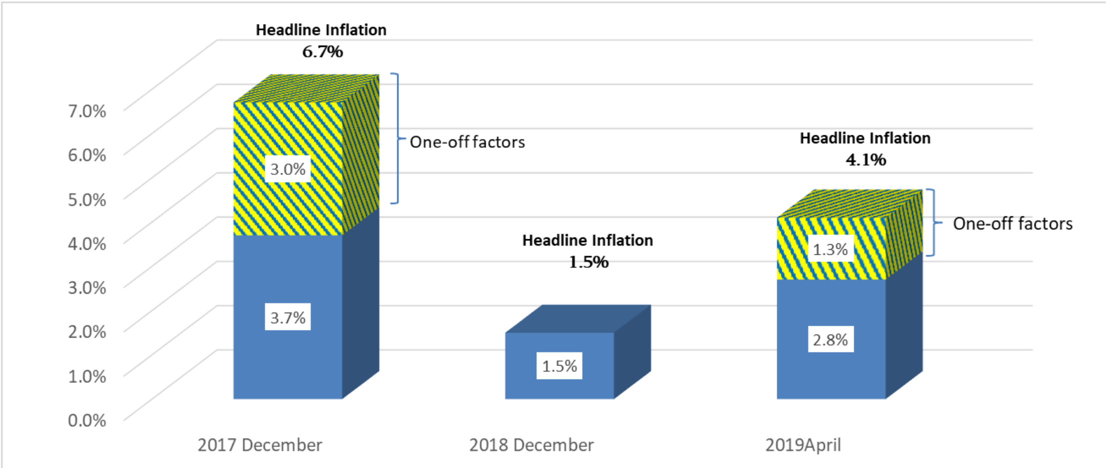
Graph 1 - Current Account Deficit to Gross Domestic Product, 2016-2018



Source: National Bank of Georgia

Since the beginning of the year inflation has been moving around the target rate of 3%. In April headline inflation increased to 4.1% with a significant contribution from one-off factors. Particularly, the increase in excise taxes on tobacco products at the beginning of the year contributed 1.3 percentage points to annual inflation in April, and without it, you can see from the Graph 2, that inflation is 2.8%. One-off factors, such as increase in excise taxes, have a temporary effect and central banks do not react to them. As you well know, increase in excise tax had a significant influence on inflation in 2017 as well. However, this effect was then neutralized from the beginning of 2018 and inflation rate declined down to the target, as was constantly communicated by us before. According to the current forecast, other things equal, the inflation will move towards the target level once the one-off (exogenous) factors fade away. Note that, the core inflation, which excludes volatile food, energy and tobacco prices, stood at 1.4% in April. Taking core inflation into account is important as it provides valuable information about long-term trend of prices changes.

Graph 2 – One-off Factors in Headline Inflation

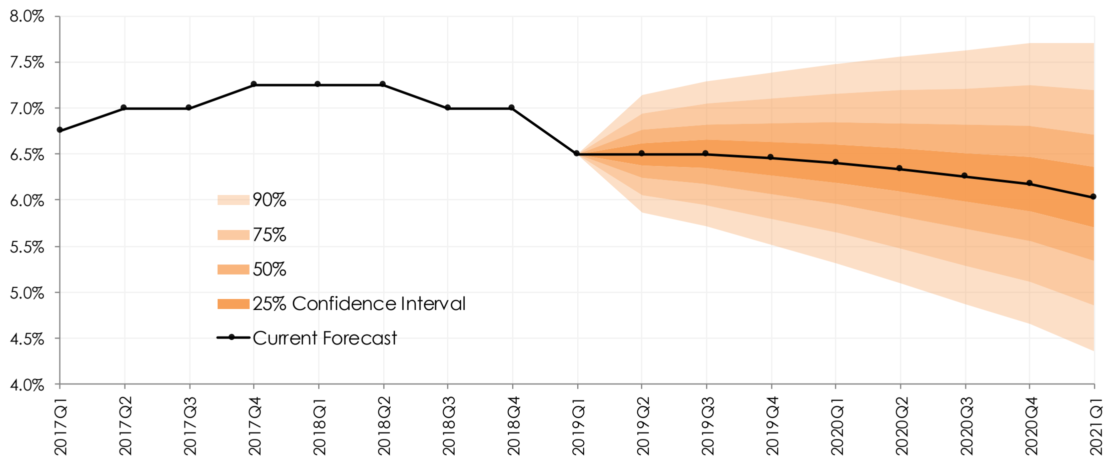


Source: National Bank of Georgia

Along with external risks softening, in the first quarter of 2019 the NBG continued the process of gradual exit from moderately tightened monetary policy (normalization process). However, despite the fact that aggregate demand remains below the potential level of output, considering the still-material risks from external sector, the normalization process is expected to be implemented gradually. Therefore, the MPC deemed it necessary to leave the policy rate unchanged at 6.5% at this stage.

As earlier, I want to add that the monetary policy rate forecast is not a commitment to future decisions made by the National Bank of Georgia. Rather, it is the expected trajectory of the policy rate, assuming that all exogenous factors incorporated into the forecast materialize as expected.

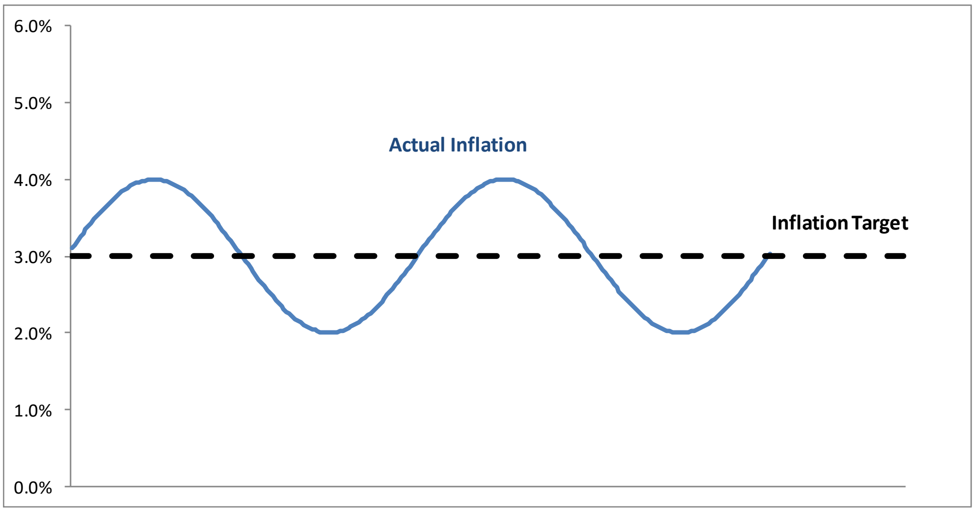
Graph 2 - Forecast of the Monetary Policy Rate



Source: National Bank of Georgia

I also would like to remind you that the inflation target in the medium term is 3% starting from 2018. Focusing on the medium term is the key, since exogenous shocks always affect the economy and, hence, move inflation away from the target: at any moment it may be higher or lower than the target level of 3%. However, as a result of the policy pursued by the NBG, inflation will always move towards the target over the medium term (see Graph 3). Moreover, inflation target does not mean the upper bound of inflation. In particular, when we state that inflation target is set at 3%, we do not mean inflation from 0 to 3%; rather we mean an inflation level close to 3% - either above or below - in the medium term. Under the inflation targetin,g the price stability is achieved arguably with the lowest social cost, while the economic growth is the highest compared to existing alternative frameworks.

Graph 3 - Variation of Inflation around its Target



Source: National Bank of Georgia

The NBG continues to monitor the developments in the economy and financial markets and will use all means and instruments at its disposal to ensure price stability.

Thank you for your attention!