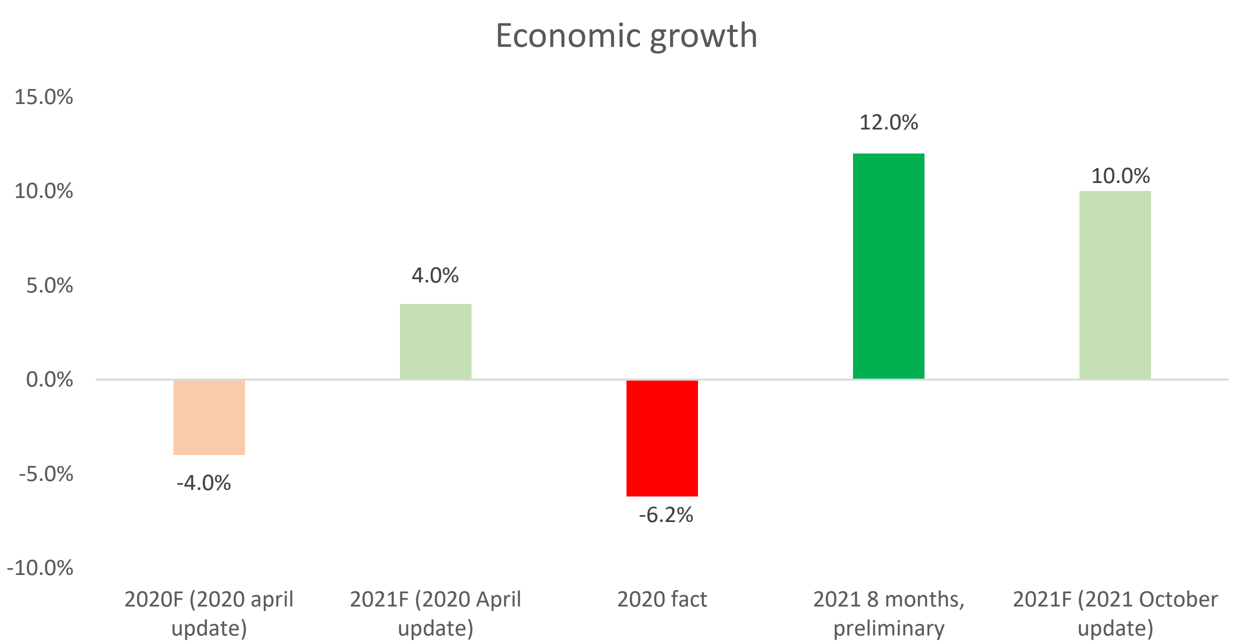
Ladies and gentlemen,

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.

The process of overcoming the pandemic in the world has turned out to be longer and more difficult than initially expected. This, in turn, hindered the recovery of foreign demand for Georgia, especially tourism. The pandemic is not over yet, however, the world economy copes better with Covid-19 in 2021, which, amid the gradual lifting of restrictions, is accompanied by a process of economic recovery. The recovery process in Georgia is going much faster than expected. While the Georgian economy shrank by 6.2 percent in 2020, in the first eight months of this year, according to preliminary data, real economic grew by 12 percent. According to the current forecast, a total GDP growth of about 10 percent is expected in 2021.

Diagram 1 Economic growth

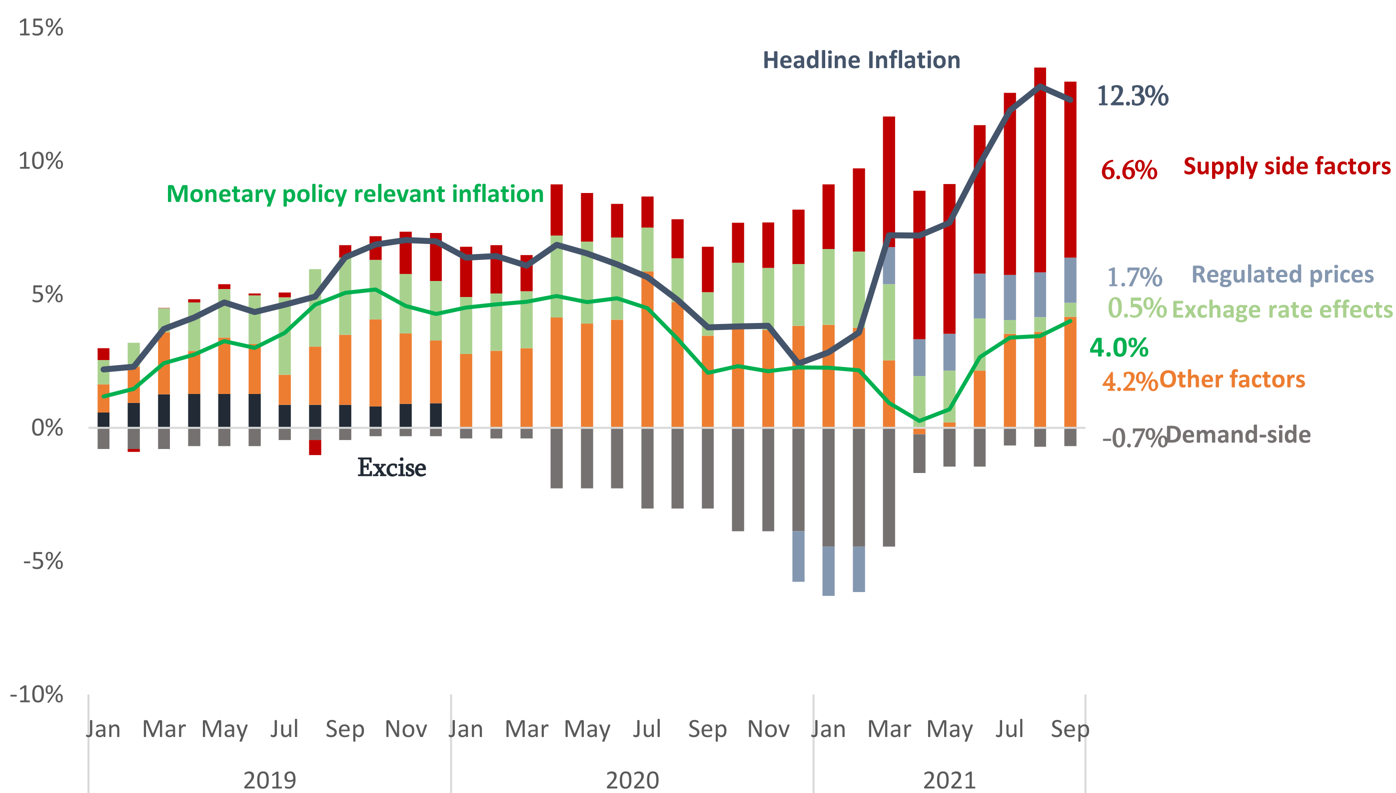


The acceleration of the process of economic recovery and pent-up demand, against the background of still limited production, have significantly increased inflationary pressure in the world, including Georgia. Rising global inflation is one of the main topics of discussion among the International Monetary Fund, the World Bank and other international organizations.

Monetary policy is based on a comprehensive analysis of the current inflation and its forecast dynamics. In this process, it is important to assess the impact of one-off factors in order to better see the expected outlook for inflation. Due to the extraordinary situation caused by the pandemic, the exogenous factors are particularly active globally in 2020-2021.

Now you see the inflation chart on the screen. The NBG estimates that the impact of temporary factors in September 12.3 percent annual inflation is around 8 percentage points. A large share of these factors, about 6.6 percentage points, comes from supply factors such as the sharp rise in the USD commodity prices and global shipping costs(Diagram 2).

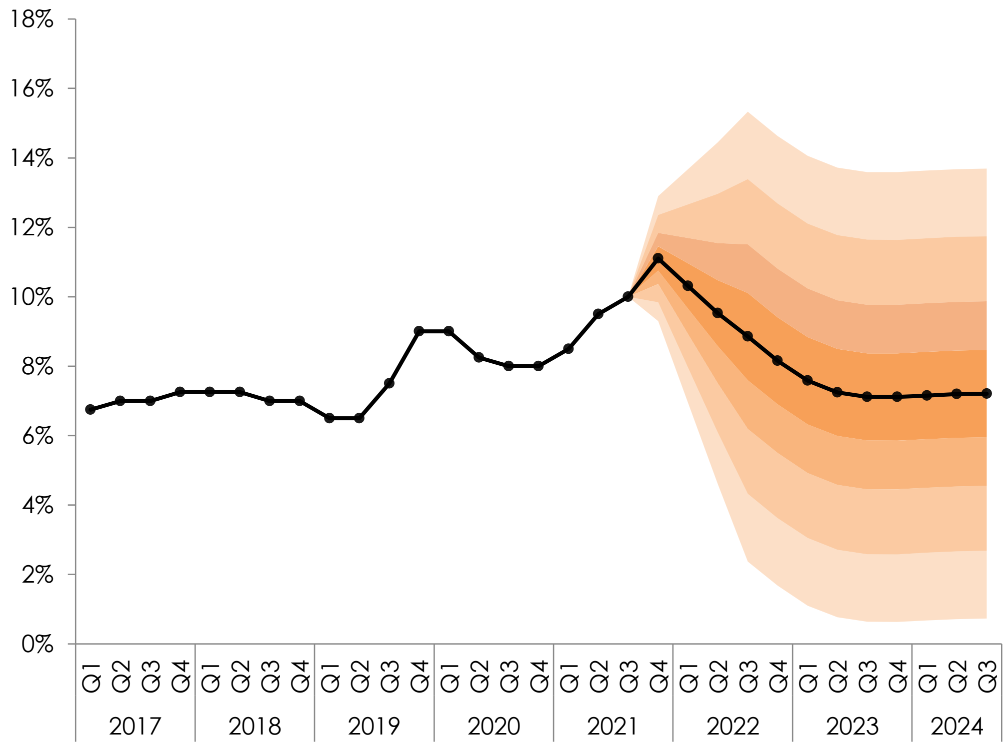
Diagram 2 Monetary Policy Relevant Inflation



As mentioned, assessing the impact of one-off factors is important, since the monetary policy changes the future outlook of inflation and not its current level. This is the reason why the central banks respond to one-off factors only in case when an impact is so strong, that it also affects long-term inflation expectations. In other words, tightening monetary policy has a limited impact, for example, on prices of fuel or food expressed in US dollars and, without taking this into account, tightening of monetary policy may lead to unnecessary shrinkage of the economy and increase in unemployment.

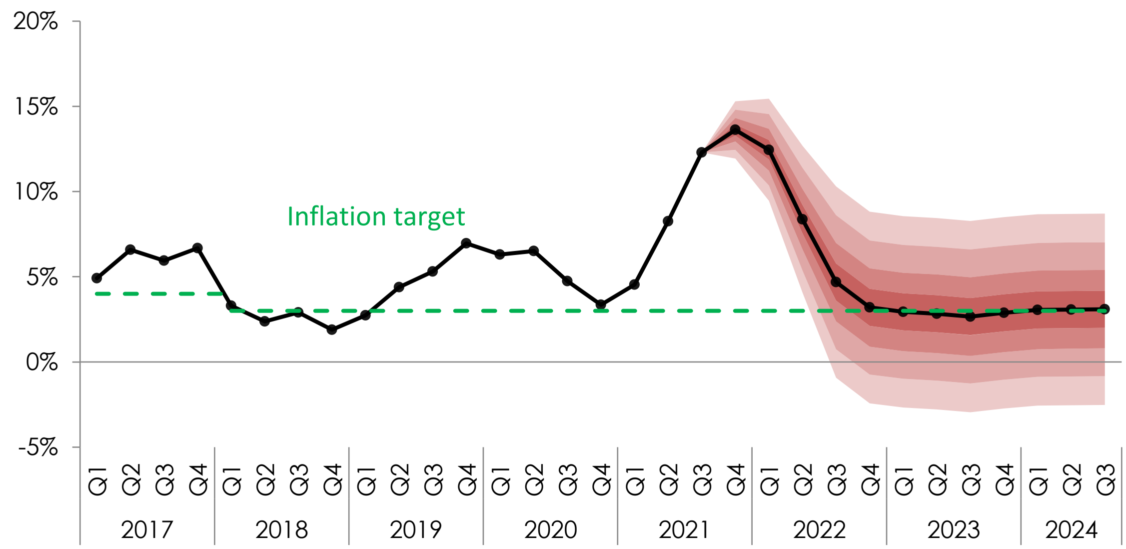
The inflation will remain high for the rest of the year. Given that the contribution of temporary factors to inflation will continue to be a driving force and, at the same time, monetary policy stance is tight, the Committee decided to keep the policy rate at the current level. Nevertheless, in the face of strong supply shocks, the threat of inflation expectations accelerating is still relevant. In addition, inflationary risks persist and the materialization may warrant further tightening of monetary policy (Diagram 3). In the increased crediting the higher contribution of foreign currency loans is particularly noteworthy.

Diagram 3 - Forecast of the Monetary Policy Rate



Against the background of the expected depletion of exogenous factors, according to the forecast on the screen, inflation will begin to decline in 2022 and gradually approach its medium-term target. This process will be underpinned by the expected longer tightened monetary policy stance (Diagram 4)

Diagram 4 – Forecast of the Inflation



It should be highlighted once again that the monetary policy rate forecast is not a commitment to future decisions made by the NBG. Rather, it is the expected trajectory of the policy rate, assuming that all exogenous factors incorporated into the forecast materialize as expected. With the receipt of new data, the policy is re-analyzed, which affects the macroeconomic forecast, and consequently, the future decisions of the NBG.

The NBG continues to monitor the developments in the economy and financial markets and it presents to the public the overview of economic conditions and updated macroeconomic forecasts in the Monetary Policy Report. Thank you for your attention!