საქართველოს ეროვნული ბანკი
National Bank of Georgia

MONETARY POLICY REPORT

MAY 2026

PREFACE

The primary objective of the National Bank of Georgia (NBG) is to ensure price stability, which, in turn, supports the country's long-term economic growth. In pursuit of this objective, the NBG operates within an inflation-targeting framework, which was formally adopted in 2009. Within this framework, the NBG conducts its monetary policy in a way that inflation approaches its target level of 3% in the medium term.

The primary tool of the NBG under its inflation-targeting framework is the monetary policy rate. When making decisions about the rate, the primary focus is on the inflation forecast, as the full economic impact of the decision takes time (4-6 quarters) to materialize. Therefore, macroeconomic forecasts are the key component in shaping monetary policy, and their effective communication is crucial for anchoring inflation expectations. Additionally, the communication of these forecasts plays an important role in the decision-making process of businesses and households.

In recent years, amid global developments, uncertainty has increased. Given the heightened unpredictability of future economic conditions and its broad scale, it is essential for central banks to make an optimal decision when conducting monetary policy to minimize economic losses in the event of any risk materializing. In a dynamic economic environment, a monetary policy approach focused on managing risks is critical for achieving optimal outcomes. This is evidenced by the experience of central banks in the post-pandemic period. Central banks, including the NBG, that made decisions based on the approach of minimizing the impact of risks, have managed the globally prevailing inflationary pressures with relatively greater success. Accordingly, policymakers are increasingly emphasizing the importance of a scenario-based approach, within which monetary policymakers make decisions based on the development of various relevant scenarios. This systematic assessment of scenarios and their impact enables policymakers to effectively navigate the inflation-output tradeoff.

The NBG adopted a new scenario-based approach to monetary policy communication, enhancing the transparency of its risk management and decision-making processes. This step marks another stage in the development of the NBG's monetary policy framework through which it improves the transparency and comprehensibility of the monetary policy reaction function, thereby strengthening the effectiveness of the policy transmission channels.

Under the scenario-based approach, the National Bank of Georgia publishes **three relevant scenarios**, given the existing uncertainty:

- **The Central Scenario**, which incorporates a broad set of current information, including assumptions on exogenous factors and economic transmission mechanisms. It reflects a monetary policy path that is calibrated by the policymaker through a careful assessment and balancing of heterogeneous risks.
- **The High-Inflation Risk Scenario**, which, compared to the central scenario, incorporates risks that are more inflationary over the monetary policy horizon.
- **The Low-Inflation Risk Scenario**, which, compared to the central scenario, incorporates more disinflationary risks over the monetary policy horizon.

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ISSN 1512-0767

MONETARY POLICY DECISION

The National Bank of Georgia raises the monetary policy rate by 0.25 percentage points to 8.25 percent.

On May 6, 2026, the Monetary Policy Committee of the National Bank of Georgia (NBG) decided to increase the monetary policy rate (refinancing rate) by 0.25 percentage point (pp). The monetary policy rate is 8.25 percent.

The escalation of geopolitical situation in the Middle East and the prolonged substantial disruptions to shipping through the Strait of Hormuz have created another supply-side driven inflationary shock to the global economy. The sharp increase in the prices of raw energy resources on international markets has already been reflected in rising global inflation. At the same time, the geopolitical situation is disrupting international transportation and heightening the risks of supply chain disruptions. This, in turn, increases production costs, which could become an additional source of inflation. The direct effect of the aforementioned increase in oil prices has already been reflected in fuel prices in the Georgian market. As a result of the combined direct and indirect effects of these supply shocks, headline inflation deviated from the 3 percent target in April, reaching 5.9 percent. At the same time, relatively sticky prices measures, which better capture long-term inflationary processes and inflation expectations, have recently accelerated, making the risks of a second-round effects more pronounced. However, despite the acceleration, they still remain close to the target. In particular, core inflation (excluding food, energy and tobacco) stood at 3.2 percent in April, while services inflation was 3.7 percent.

Despite severe geopolitical shocks, the Georgian economy remains resilient and economic growth stays high. According to preliminary data, economic activity grew by 10.7 percent in March 2026 and by 9.1 percent in the first quarter. At the same time, high-productive sectors remain a key driver of economic growth, which partially offsets demand-side inflationary pressures.

The NBG's updated central scenario assumes that the ongoing war in the Middle East will end in the second quarter. However, this assumption is conditional and subject to high uncertainty. Even if the geopolitical situation indeed de-escalate during this period, the pace of recovery in global supply capacity is subject to additional uncertainty. Consequently, high inflationary risks are more pronounced. However, there is also a possibility that the geopolitical situation will de-escalate more quickly than in the central scenario. Therefore, the Monetary Policy Committee (MPC), in addition to the central scenario, considered both high and low-inflation risk scenarios.

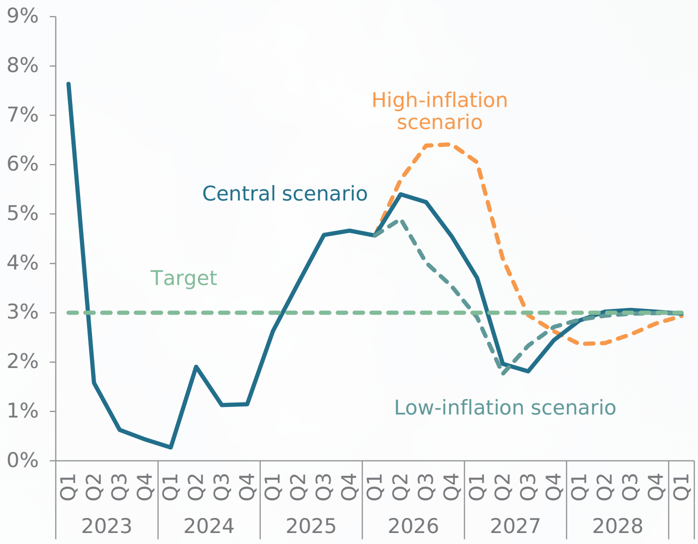
In the event of the realization of the high-inflation risk scenario, fundamental processes require a higher trajectory of the monetary policy rate than the central scenario. The high-inflation scenario assumes a more prolonged and intensified geopolitical situation. Against this backdrop, commodity prices in the international market will increase further and the disruption of supply chains will become widespread. As a result, the supply-side inflationary shock would exacerbate in Georgia, amplifying second-round effects, and ultimately inflation would be higher than in the central scenario.

On the other hand, under the low-inflation risk scenario considered by the MPC, the realization of the risks would allow a faster normalization of monetary policy stance compared to the central scenario. A rapid de-escalation of the severe geopolitical tension in the Middle East would ease price pressures in international commodity markets. At the same time, the risks of disruptions to global supply chains would decline significantly, which would be reflected in lower international transportation costs and, ultimately, a moderation of global inflationary pressures.

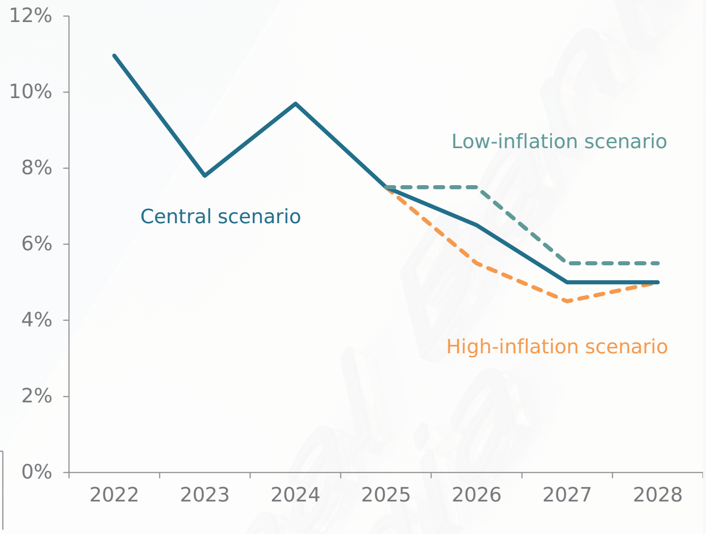
As a result of the ongoing macroeconomic analysis and consideration of existing risks, the MPC considered it optimal to increase the monetary policy rate by 0.25 pp to 8.25 percent. This decision is aimed at keeping inflation expectations firmly anchored at the target. The moderate tightening of monetary policy, in turn, reduces the risks of second-round effects and aims to ensure that, once the supply-side shock dissipates, inflation converges swiftly to the 3 percent target. The NBG continues to closely monitor ongoing developments and the intensity of their transmission to the domestic market. If inflationary shocks stemming from geopolitical tensions become even more prolonged and/or their magnitude would amplify the risks of second-round effects, the MPC will continue to moderately increase the monetary policy rate. Thereafter, once the inflationary shock dissipates, the NBG will begin a gradual normalization of the policy stance.

NBG's Macroeconomic Forecast Scenarios

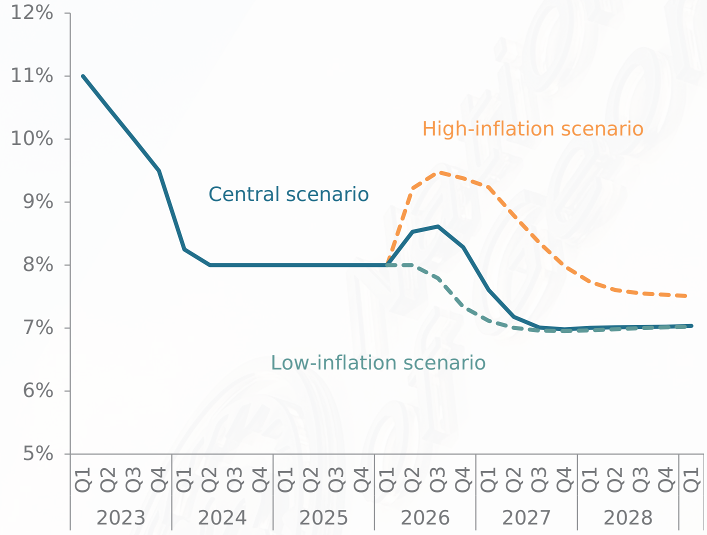
Inflation



Real GDP Growth



Monetary Policy Rate



1. OVERVIEW OF THE GLOBAL MACROECONOMIC ENVIRONMENT

Following the escalation of the conflict in the Middle East, the geopolitical risk index has increased again. For Georgia, as a small open economy, the global economic situation is transmitted through both direct and indirect channels.

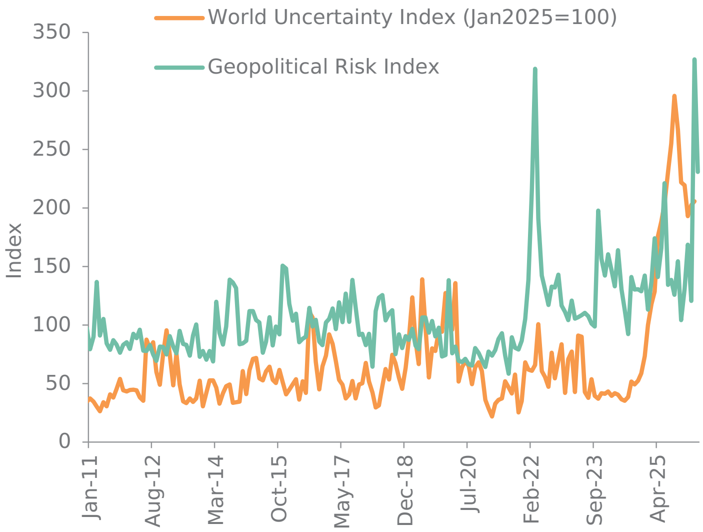


Figure 1.1. World Uncertanty and Geopolitical Risk Indices

Source: [Geopolitical Risk Index](); [https://worlduncertaintyindex.com/]().

The ongoing conflict in the Middle East represents a significant negative shock to the global economy, simultaneously slowing economic activity and increasing inflationary pressures, thereby strengthening stagflation risks, especially in developing economies.

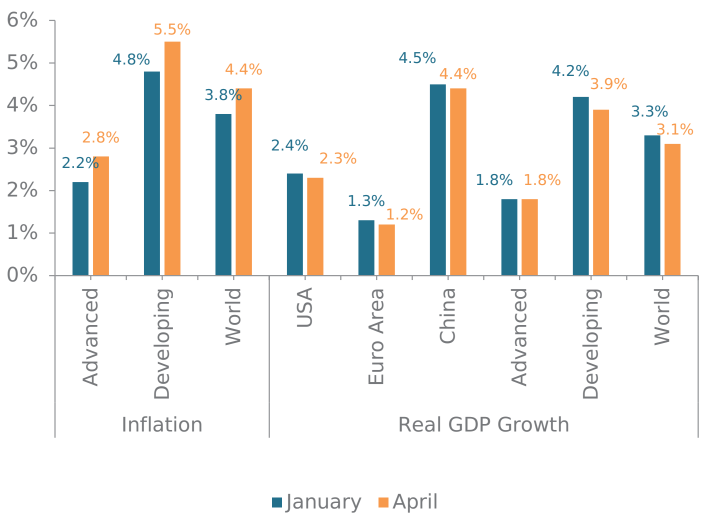


Figure 1.2. World Economic Overview (WEO), April 2026

Source: IMF.

The global economy is confronting a renewed and increasingly severe set of challenges amid the ongoing escalation of the conflict in the Middle East. In particular, disruptions to shipping flows through the Strait of Hormuz, a critical maritime corridor accounting for approximately one quarter of global seaborne oil trade alongside substantial volumes of liquefied natural gas (LNG) and fertilizers[1], have materially heightened risks to the global economic outlook. In the wake of the escalation, international commodity prices, particularly for oil, natural gas, and fertilizers, have increased markedly.

Against this backdrop, global uncertainty indicators, most notably the geopolitical risk index, have risen sharply (see Figure 1.1), exerting additional pressure on global economic activity and inflation dynamics. According to the International Monetary Fund (IMF), a one-standard-deviation geopolitical risk shock reduces global output by approximately 0.8 percentage points (pp), while increasing inflation by around 2.5 pp[2]. Reflecting the deterioration in the external environment, the IMF revised downward its 2026 global growth forecast in the April projections to 3.1%, from 3.3% in the January outlook, while the global inflation forecast was revised upward from 3.8% to 4.4%. Stagflationary pressures have become increasingly pronounced, particularly across emerging market economies relative to advanced economies (see Figure 1.2).

At the same time, elevated uncertainty has contributed to a rise in term premia which, in the context of persistent inflationary pressures, has further increased long-term government bond yields (see Figure 1.3). This development signals an additional tightening of global financial conditions.

Rising government bond yields are also amplifying fiscal vulnerabilities in both advanced and emerging economies, as external debt servicing costs remain elevated amid constrained fiscal space and limited access to financing. In this environment, higher energy, transportation, and food

1 UNCTAD.

2 იხ. https://www.imf.org/en/publications/weo/issues/2026/04/14/world-economic-outlook-april-2026 .

In the context of rising inflation expectations, tighter financial conditions and an increase in the term premium are reflected in higher yields on 10-year Treasury securities.

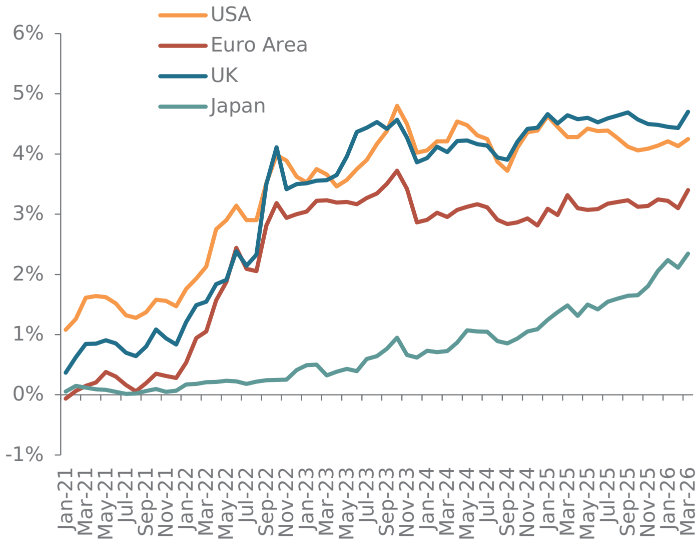


Figure 1.3. 10-year government bond yields

Source: FRED, ECB.

Following the escalation of the conflict in the Middle East, inflation expectations have increased amid rising prices of energy resources and other key commodities. As a result, financial markets have revised upward their expectations of the Federal Reserve's interest rate trajectory.

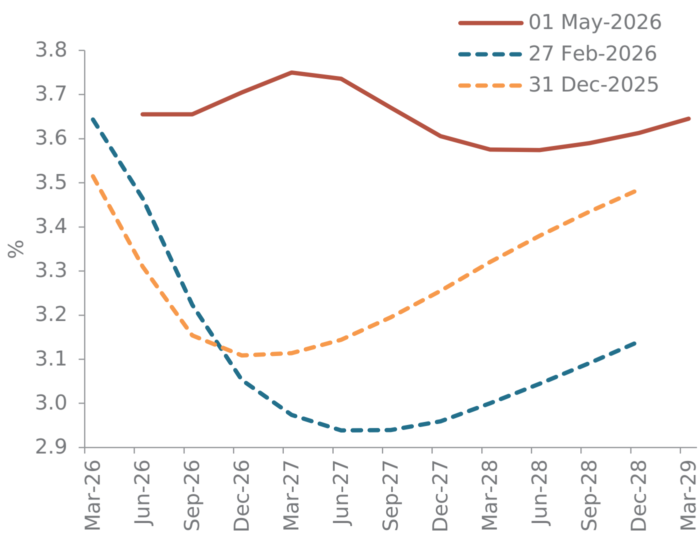


Figure 1.1.1: Market Expectations of Fed Funds Rate Path

Source: Atlanta Fed.

prices are simultaneously intensifying pressures on public finances and eroding households' purchasing power, particularly in economies highly dependent on imported energy resources and essential consumer goods.

Looking ahead, the magnitude and persistence of the economic implications stemming from the conflict in the Middle East, both globally and regionally, will depend critically on the duration, intensity, and geographic scope of the ongoing developments. Accordingly, close monitoring of evolving risks and transmission channels remains essential.

1.1. MAJOR ECONOMIES OF THE GLOBAL ECONOMY

In the **United States**, inflationary risks had already been elevated prior to the outbreak of the conflict, reflecting the gradual transmission of tariff and immigration policies introduced in 2025. Economic growth had also moderated amid weaker activity in the first and fourth quarters of 2025. Nevertheless, increased investment in artificial intelligence (AI) continued to provide important support to economic activity, contributing to the relative resilience of growth dynamics. The escalation of the conflict in the Middle East has further intensified inflationary pressures while simultaneously worsening expectations regarding economic growth and labor market conditions. Although signs of moderation in labor market activity have begun to emerge, the Congressional Budget Office estimates that excess demand conditions will persist throughout 2025 and into early 2026. This was also reflected in the dynamics of real consumer spending.

Consumer sentiment has weakened in recent months; however, private consumption continues to play a central role in supporting economic activity, underpinned by elevated asset prices. Notably, asset prices declined immediately following the escalation of the conflict but subsequently recovered toward pre-conflict levels. More broadly, the wealth effect associated with rising asset prices in the United States remains unevenly distributed, benefiting primarily higher-income households with significant financial asset holdings. As a result, divergences in consumption patterns across income groups have become more pronounced, contributing to increasingly "K-shaped"[3] dynamics in both consumer spending and overall economic activity.

Elevated inflationary risks have strengthened expectations that the Federal Reserve (Fed)

3 *Different sectors, industries, or income groups do not benefit equally from economic growth.*

The escalation of the conflict in the Middle East led to a strengthening of the U.S. dollar index, which exceeded the 100-point threshold. This is explained by the dollar's role as a "safe-haven asset" during periods of crisis. However, unlike previous crisis episodes, yields on U.S. Treasuries have increased. On the other hand, the euro index weakened, largely reflecting the strengthening of the dollar. However, in recent periods, the dollar has again been maintaining a relatively weaker position.

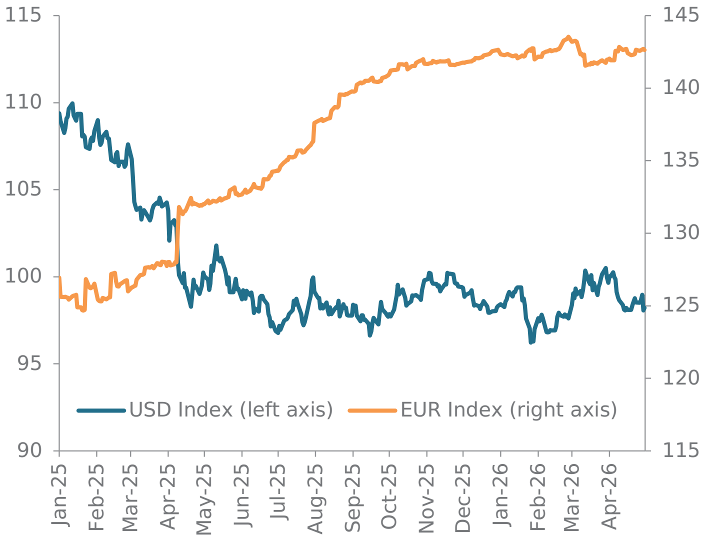


Figure 1.1.2. U.S. Dollar and Euro Indices

Source: investing.com.

Against the backdrop of ongoing hostilities in the Middle East and heightened uncertainty surrounding the Strait of Hormuz, oil prices have increased significantly. In the event that the Strait remains open, oil prices are expected to gradually normalize. However, if the conflict persists longer than anticipated, oil prices are likely to remain elevated for an extended period.

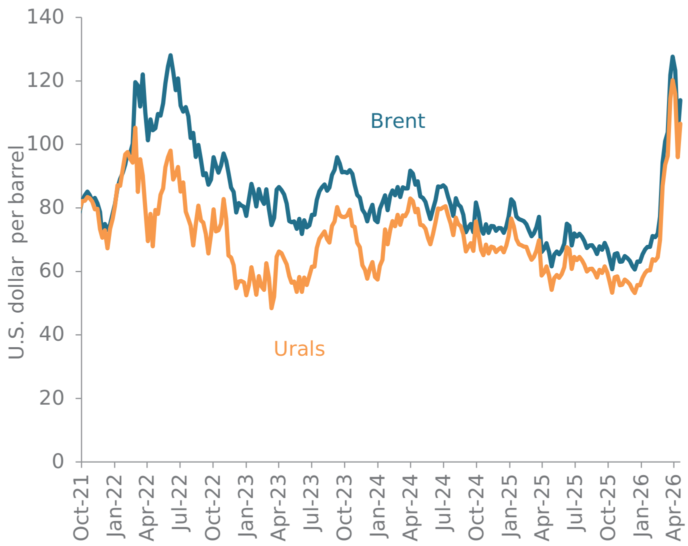


Figure 1.2.1. Brent and Urals oil prices

Source: FRED, Tradingeconomics.

will delay the normalization of monetary policy, with financial markets currently pricing in an unchanged policy rate through the end of 2026 (see Figure 1.1.1). Following the escalation of the conflict in the Middle East, the U.S. dollar index appreciated, reflecting the dollar's role as a safe-haven asset. During this period, the index temporarily exceeded the 100 mark, although it currently remains at a relatively weaker level compared to historical averages (see Figure 1.1.2). In contrast to previous crisis episodes, yields on 10-year U.S. Treasury securities increased, reflecting both heightened fiscal concerns and persistent inflationary pressures (see Figure 1.3).

The **euro area** continues to face challenges in maintaining an appropriate short-term balance between price stability and economic activity. At the beginning of 2026, the economy showed signs of cautious improvement, supported by stronger activity in Germany and France amid increased defense and infrastructure spending. However, uncertainty has subsequently increased and the economic outlook has deteriorated due to the energy shock associated with the conflict in the Middle East, alongside heightened global trade tensions. In the short term, the conflict has affected inflation primarily through higher energy prices. Headline inflation, which had recently fluctuated close to the 2% target, increased to 3.0% in April, largely reflecting higher oil prices resulting from the conflict. At the same time, relatively persistent inflation indicators, particularly services inflation, continued to signal elevated underlying inflationary pressures. Despite a slight moderation in April, services inflation remained elevated at 3.0%. Against this backdrop, the European Central Bank has maintained a cautious policy stance. Monetary policy settings remained unchanged at the April meeting; however, amid rising inflation expectations, both IMF and market expectations regarding the future policy rate path have shifted upward.

Amid the ongoing conflict in the Middle East and heightened geopolitical uncertainty, **China**'s economy demonstrated stronger-than-expected resilience, expanding by 5.0% in the first quarter of 2026. Growth was driven primarily by robust export performance and continued expansion in high-technology manufacturing. Nevertheless, structural vulnerabilities remain significant, particularly in the real estate sector, where declining investment continues to weigh on consumer confidence. External risks associated with the conflict in the Middle East also remain important. Although China maintains relatively substantial strategic oil reserves, volatility in energy prices and rising logistics costs are exerting additional

Against the backdrop of the conflict, the Global Supply Chain Pressure Index has risen, along with a modest increase in average international shipping costs. Other things being equal, these developments increase inflationary risks in international commodity markets.

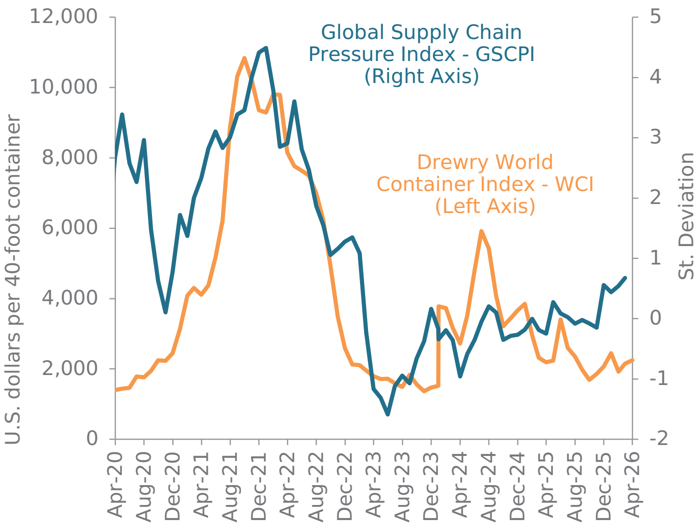


Figure 1.2.2. World Container Index and Global Supply Chain Pressure Index

Source: Drewry World Container Index (WCI), New York Fed, Global Supply Chain Pressure Index (GSCPI).

Amid supply chains disruptions, the FAO Food Price Index increased in March, driven by rises across all of its components, which carries inflationary risks.

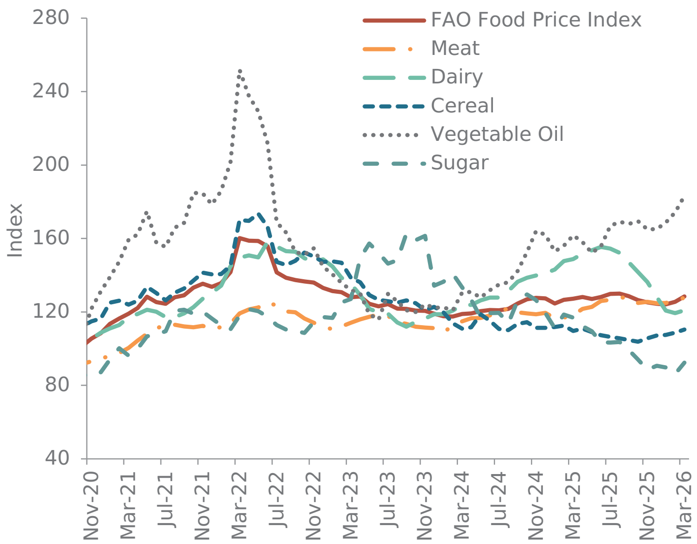


Figure 1.2.2. FAO Food Price Index, Dec-2019=100

Source: FAO, NBG's calculation.

pressure on production costs. Following a prolonged period of deflationary pressures, recent increases in industrial prices have partly reflected higher energy costs. At the same time, monetary policy transmission remains constrained, as credit demand continues to exhibit weak dynamics despite low interest rates. According to the IMF, China's long-term economic growth is expected to moderate to around 4.4% (see Figure 1.2).

In **Russia**, despite a modest reduction in the policy rate at the beginning of 2026, the central bank continues to maintain a tight monetary policy stance amid inflation remaining above target. Structural weaknesses within the economy also persist. According to the IMF, expectations for economic growth in 2026 improved slightly to 1.1%, largely reflecting higher oil prices and increased export revenues from energy resources amid the ongoing conflict in the Middle East.

1.2. INTERNATIONAL COMMODITY MARKETS

As noted, the outbreak of the war in the Middle East has caused significant disruptions to transit through the Strait of Hormuz. As a result of the de facto closure of the Strait of Hormuz, the prices of crude oil and petroleum products increased sharply in international markets. In April, U.S. crude oil averaged 116 U.S. per barrel and European Brent 122 U.S. per barrel, following a period at the beginning of the year when both fluctuated within the 60–70 U.S. range (see Figure 1.2.1). According to the U.S. Energy Information Administration (EIA), this increase is the highest in a single quarter since 1988 (in inflation-adjusted measures). Developments in international oil prices largely depend on uncertainty surrounding the Strait of Hormuz. If the disruptions related to the Strait of Hormuz are eliminated, oil prices are expected to decline gradually. However, if the conflict persists longer than anticipated, oil prices are likely to remain elevated for an extended period.

It is worth noting that since the conflict began, Urals prices have also increased markedly. The price of a barrel has risen to around 120 U.S. dollar, representing the highest level since the Global Financial Crisis (GFC)[4]. At the same time, upward pressure on Urals prices was also driven by the 30-day waiver period announced by the U.S. on Russian oil sanctions, which was further extended in April. In addition, Ukrainian drone periodic attacks on Russia's oil infrastructure continue to disrupt supply, creating additional pressure on prices. In turn, increased fuel prices in interna-

4 During the GFC, the price per barrel increased to approximately 140 U.S. dollar.

Amid logistical delays, the fertilizer price index has increased, which, other things being equal, carries risks of an increase in international food prices.

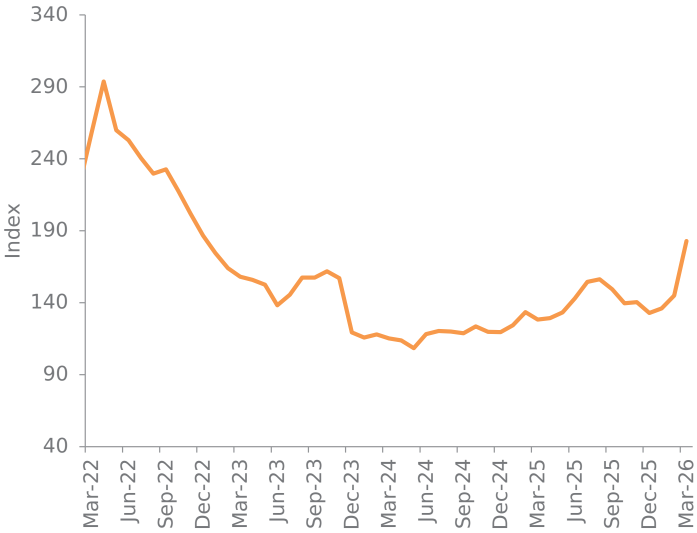


Figure 1.2.4. Fertilizer Price Index, 2010=100

Source: World Bank.

Since the onset of the conflict, gold prices have declined sharply; however, gold still records strong annual growth.

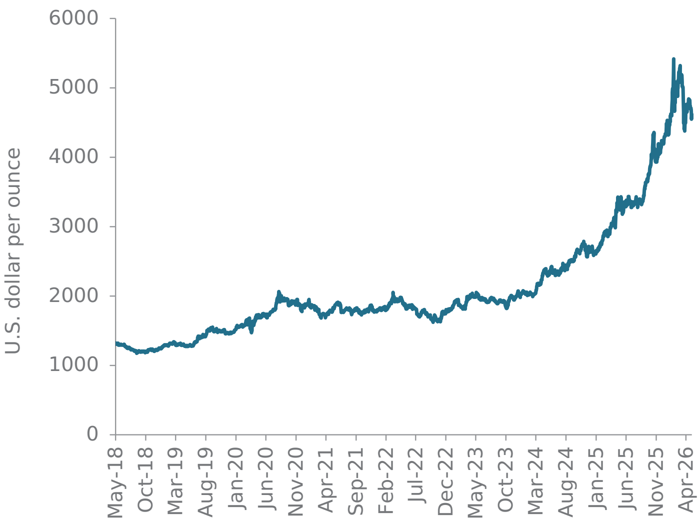


Figure 1.2.5. Gold Price, U.S. dollar per Ounce

Source: Bloomberg.

tional markets are also transmitted to the domestic market.

The Middle East conflict is causing disruptions to supply chains, which was reflected in the increase in the Global Supply Chain Pressure Index in March, reaching its highest level since January 2023 (see Figure 1.2.2). The average international shipping costs have also increased, although they remain significantly below the level observed in 2021 (see Figure 1.2.2). This, in turn, contributes to heightened inflationary risks in international commodity markets. Since the beginning of the year, the international food price index had been declining on an annual basis; however, in March it increased by 1.0% year-on-year and by 2.4% compared to February. Notably, prices of all major products increased on a monthly basis (see Figure 1.2.3), while mixed signals persist in annual terms. Upward pressure on international food prices is also being driven by disruptions related to fertilizer logistics. Approximately 30% of fertilizers transported by global maritime routes are shipped through the Strait of Hormuz. Thus, uncertainty surrounding the Strait and related shipping disruptions have pushed up fertilizer prices[5] globally. However, they are still well below their peak (observed in 2022) (see Figure 1.2.4). If geopolitically driven disruptions are resolved, these developments, other things being equal, are expected to exert downward pressure on prices. However, if such disruptions persist for a prolonged period, a moderation in price pressures is less likely.

Amid the escalating geopolitical tensions in the Middle East, gold prices declined in international markets (see Figure 1.2.5); however, gold still records strong annual growth. In recent years, central banks, including the National Bank of Georgia, have increasingly begun to diversify their international reserves by adding gold to their holdings. Amid the backdrop of global decline in gold prices, the aggregate value of central banks' international reserves decreased by approximately 600 billion U.S dollar, although, it still reflects a substantial increase compared to the time of acquisition. In Georgia's case, despite the decline in gold prices, as of March, the value of the gold in reserves remains approximately twice as high as at the time of acquisition. This underscores the soundness of reserve diversification strategies and serves as an important buffer against external shocks.

5 Compared to February 28, 2026, fertilizer price indices have increased noticeably, including the Urea Price Index, Fertilizers Price Index, and others.

2. OVERVIEW OF THE CURRENT MACROECONOMIC ENVIRONMENT IN GEORGIA AND FORECAST SCENARIOS

High-productive sectors remain the main drivers of economic growth.

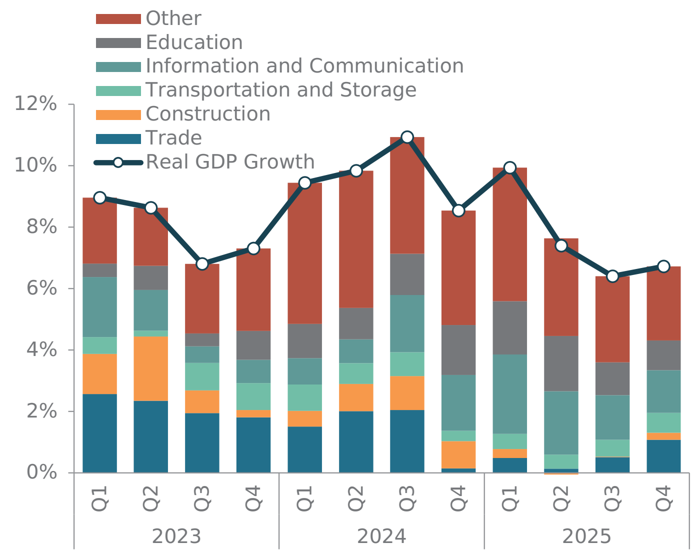


Figure 2.1.1. Sectoral Decomposition of Real GDP growth (Contribution to the Growth)

Source: NBG, Geostat.

High productivity growth is being maintained in the information and communications (ICT) and education sectors.

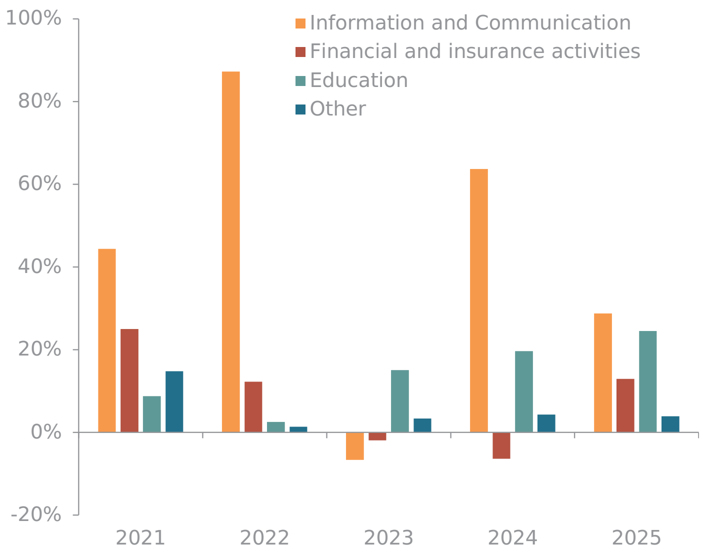


Figure 2.1.2 Annual productivity growth*

Source: NBG Estimations, Geostat.

* The data is calculated based on real GDP and sectoral employment indicators.

2.1. OVERVIEW OF THE CURRENT MACROECONOMIC ENVIRONMENT IN GEORGIA

Despite the outbreak of conflict in the Middle East, Georgia's economy continues to demonstrate strong growth momentum. According to the preliminary estimate, the high pace of economic growth (10.7%) was maintained in March as well, resulting in an average growth rate of 9.1% in the first quarter of 2026. Economic expansion continues to be driven primarily by high-productive sectors, with information and communication technology (ICT) and education making the largest contributions to growth (see Figures 2.1.1 and 2.1.2). These sectors are predominantly service-oriented and characterized by relatively low import intensity. Accordingly, the sustained contribution of less import-intensive sectors to real GDP growth reflects structural changes within the economy (see Figure 2.1.3). At the same time, several sectors, including construction, are exhibiting signs of gradual normalization following a period of exceptionally strong growth.

In recent periods, economic growth has been driven predominantly by strong domestic demand. By contrast, the contribution of external demand to growth in the first quarter of 2026 is expected to remain relatively moderate, reflecting the ongoing conflict in the Middle East and the cancellation of flights on the affected route in March.

Robust domestic demand has also been supported by accelerated credit activity. In particular, credit growth has increased in recent months, although it remains broadly close to its equilibrium level (13-15%) (see Figure 2.1.4). Financial conditions in domestic currency have eased somewhat, contributing to stronger growth in lari-denominated lending. As a result, growth in lari-denominated loans accelerated further to 16%. At the same time, amid the tightening of global financial conditions (see Chapter 1), interest rates on foreign currency loans in the domestic market have also increased; nevertheless, foreign currency lending continues to growth.

Simultaneously, as noted, amid less import-intensive economic growth, import growth has moderated compared to previous years. However, import dynamics vary significantly across categories. In particular, imports of investment goods declined in nominal terms, largely reflect-

Amid ongoing structural changes in the economy, economic growth is primarily driven by less import-intensive sectors.

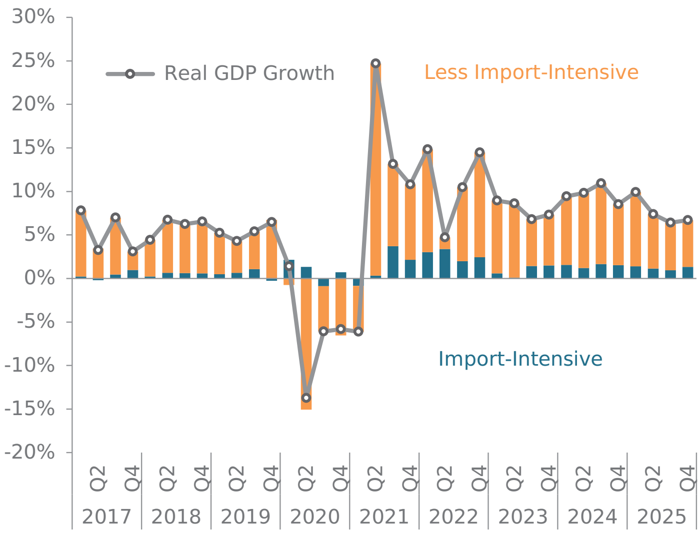


Figure 2.1.3. Sectoral Composition of Real GDP Growth by Degree of Import Dependence (Contribution to Growth)

Source: NBG, Geostat.

Recently, the pace of credit activity growth has accelerated, which is one of the factors driving strong domestic demand.

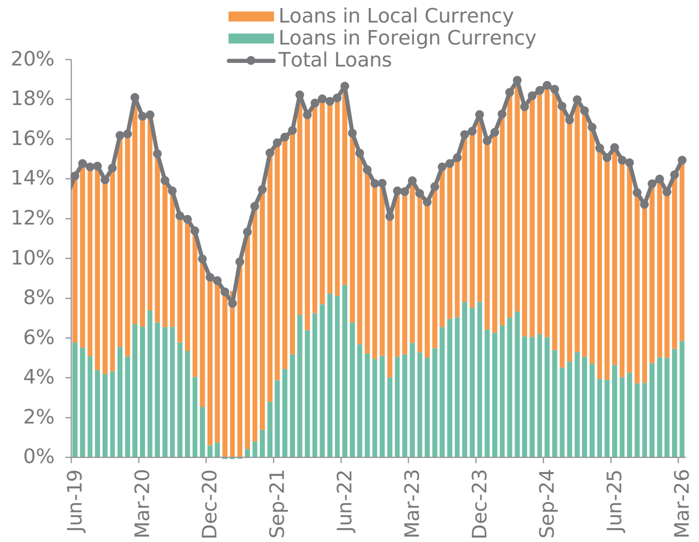


Figure 2.1.4: The annual growth rate of loans and the contribution of loans in local and foreign currency to it

Source: NBG.

ing lower prices for investment-related products (e.g. machinery and equipment). At the same time, within consumer imports, in the first quarter of 2026 imports of motor cars intended for re-export declined, which weighed on consumer import growth. Nevertheless, consumer-oriented imports excluding motor cars have shown renewed growth in recent months, including in real terms, which points to strong domestic demand (see Figure 2.1.4).

As for external demand, the ongoing heightened geopolitical tensions have already been reflected in a slowdown in tourism revenue growth. In particular, in the first quarter of 2026, tourism revenues increased by 0.5% year-over-year (YoY). If restrictions on air travel persist and airline ticket prices continue to rise, the adverse impact on travel-related revenues is expected to intensify further. At this stage, however, this effect is being partially offset by strong growth in goods exports and remittances, which increased by 23.3% and 14.2% on an year-over-year basis, respectively, in the first quarter of 2026. Notably, export growth was driven primarily by increased exports of domestically produced goods, partly reflecting higher global commodity prices amid the ongoing conflict. As a result, net inflows remain negative in the short term; however, they have not deteriorated in annual terms and continue to remain close to their equilibrium level (see Figure 2.1.7).

The share of Middle Eastern countries in Georgia's merchandise trade remains limited, while within the services balance the largest exposure is associated with Israel (see Box 1). Accordingly, the direct impact of the conflict on the current account remains contained and is broadly balanced by factors operating in opposite directions in nominal terms.

It is also noteworthy that, amid the structural transformation of the economy in recent years, Georgia's external position has improved significantly. In 2025, the current account deficit narrowed substantially to 2.6% of GDP (see Figure 2.1.7). In particular, alongside the significant improvement in the goods balance, strong growth in services exports also had a positive impact. Revenues from exports of computer and information services remained elevated, with their share to GDP reaching 3.0%. From an analytical perspective, the current account balance excluding net reinvested earnings better reflects the underlying dynamics of the current account. Excluding this factor, the current account recorded a surplus in 2025 (see Figure 2.1.8). As a result of the developments described above, despite heightened global uncertainty, and under the assumption that the conflict concludes in the second quarter

Against the backdrop of the ongoing conflict in the Middle East, financial conditions in the domestic market are moderately tight, mainly due to rising foreign currency interest rates. Meanwhile, financial conditions in the local currency (lari) have slightly eased in recent period.

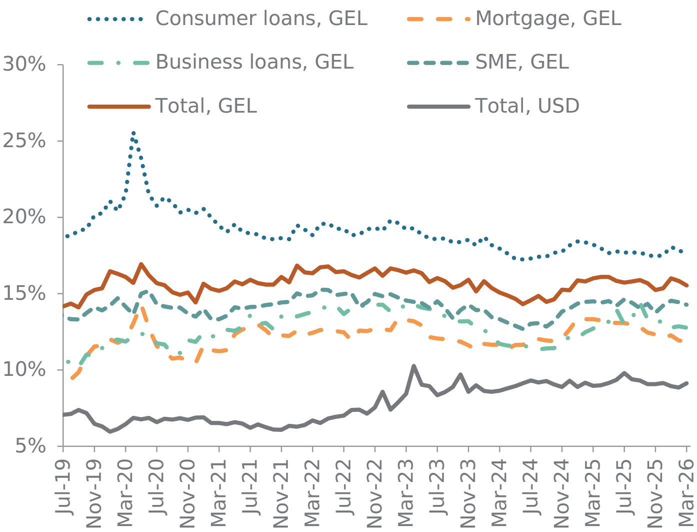


Figure 2.1.5. Interest Rates on Loan Flows in National and Foreign Currencies (Breakdown of Lari-denominated Loans by Purpose)

Source: NBG.

Although the overall growth rate of imports has slowed compared to previous years, the real growth of domestically consumed imports has recently accelerated, indicating strong domestic demand.

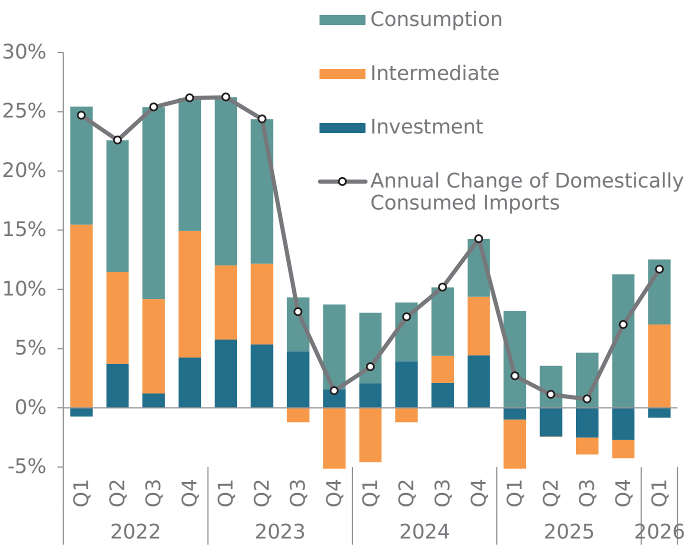


Figure 2.1.6: Real growth of domestically consumed imports

Source: NBG, Geostat.
* Goods imports excluding car imports, deflated using the import price deflator of Geostat (National Statistics Office of Georgia).

of 2026, the current account deficit is projected to remain close to its estimated equilibrium level of 5% in 2026.

The current account improvement supports lari stability. It is noteworthy that in the early stage of the Middle East war, the global strengthening of the U.S. dollar led to a cyclical depreciation of both the lari and the currencies of major trading partners against the U.S. dollar. However, the depreciation pressure on the lari was temporary, which was reflected in an appreciation of the nominal effective exchange rate in March. This, in turn, partially offset the depreciation of the real effective exchange rate, which is largely explained by inflation differentials between Georgia and its trading partners. According to the NBG's assessment, the current level of the real effective exchange rate remains close to its long-term equilibrium (see Figure 2.1.9). It is worth noting that the depreciation of the real effective exchange rate has a positive impact on the country's competitiveness in international markets, although it exerts upward pressure on inflation through the imported inflation channel.

The increasing dynamics of deposit larization also supported the stability of the exchange rate. Prior to the outbreak of the war, deposit dollarization had declined to a historical minimum (46.0%). However, amid heightened uncertainty, it increased slightly, mainly due to legal entities (see Figure 2.1.10). On the other hand, despite elevated global uncertainty associated with the ongoing war, the country's sovereign risk premium remains low and close to its equilibrium level (see Figure 2.1.11). This points to Georgias's economic resilience to shocks and has a disinflationary effect.

By the end of 2025, the labor market's disinflationary dynamics had weakened. In the second half of 2025, productivity growth decelerated somewhat, while wage growth remained at a relatively elevated. Against this backdrop, unit labor costs have approached the 3% target (see Figure 2.1.12). This development is driven by increasing labor market tightness, as reflected in the rising vacancy to unemployment ratio (see Figure 2.1.13).

The external and domestic factors discussed above highlight significant risks, among which the main ones are the direct and indirect effects of a renewed supply shock resulting from the war in the Middle East. The initial impacts of this war were reflected in a gradual increase in fuel prices in Georgia. As a result, it contributed significantly, by 0.8 pp, to the 5.9% inflation in April 2026 (see Figure 2.1.14). However, the full effect of oil price

In the context of the Middle East war, tourism revenues have declined; however, this has been offset by other types of inflows.

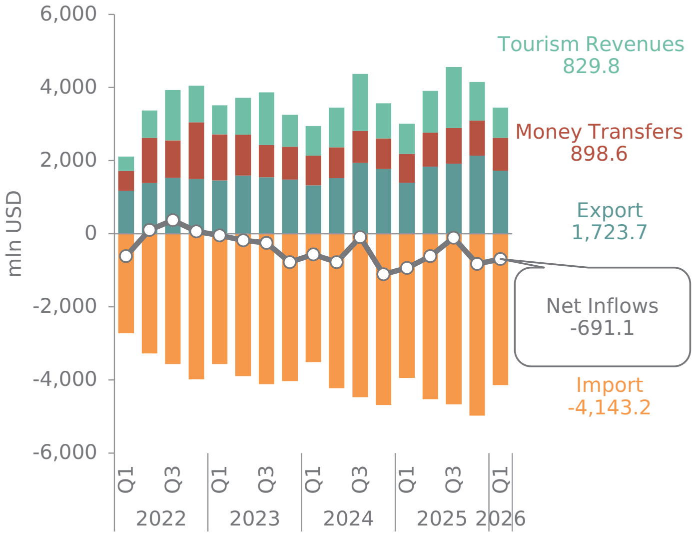


Figure 2.1.7 The dynamics of income from goods exports and imports, tourism, and remittances

Source: NBG, Geostat.

In 2025, the current account improved significantly, driven by structural changes in the economy. At the current stage, despite high uncertainty, the current account deficit in 2026 is expected to remain close to its equilibrium level.

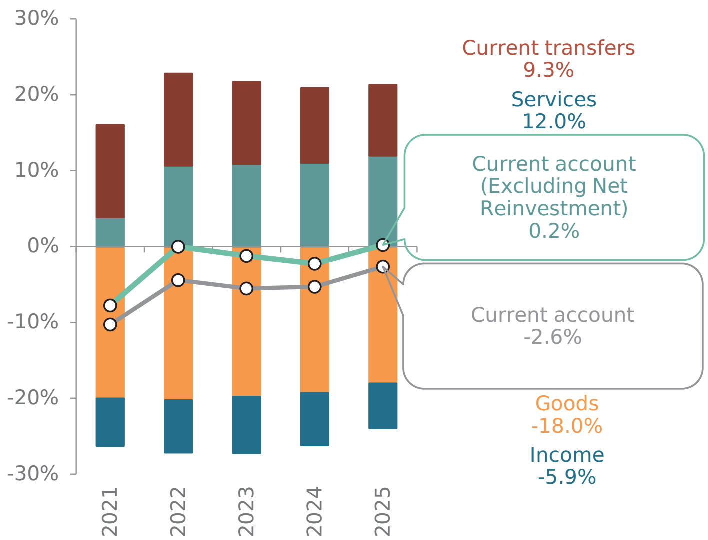


Figure 2.1.8: Current Account Balance Decomposition (% of GDP, according to BPM5)

Source: NBG.

increasing above 100 US dollar has not yet been reflected in current inflation. The future impact of fuel prices, other things being equal, will largely depend on developments around the Strait of Hormuz.

At the same time, energy prices are also being driven up by domestic increases in electricity tariffs, with a direct impact of 0.5 pp on April inflation. Meanwhile, the indirect effects depend on general macroeconomic conditions.

Apart from energy, food continues to be the main contributor to deviations of headline inflation from its target, with mixed signals persisting in international markets in this regard. However, its contribution in the domestic market has declined compared to recent months. It is noteworthy that, since March, the effects of the one-time upward adjustment in bread prices have been gradually fading, which has a disinflationary impact on both headline and sticky price inflation. At the same time, rising fuel prices and still-high food inflation are putting pressure on flexible prices (see Figure 2.1.15). If this tendency persists, the risk of higher long-term inflation expectations and therefore higher sticky-price inflation in the non-tradable sector increases.

Other measures of relatively sticky prices, which reflect the broad-based nature of inflationary processes, remain close to the target, however, they are characterized by an increasing dynamics. In particular, as of April 2026, core inflation stood at 3.2%, while services inflation amounted to 3.7%.

Overall, the external and domestic factors discussed above, along with heightened global uncertainty and supply chain disruptions, pose some risks of rising inflation expectations and include risks of strengthening so-called “second-round” effects, which warrants a moderately tighter monetary policy stance.

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The real effective exchange rate is close to its long-term equilibrium level, largely supported by relatively higher inflation among trading partners compared to Georgia.

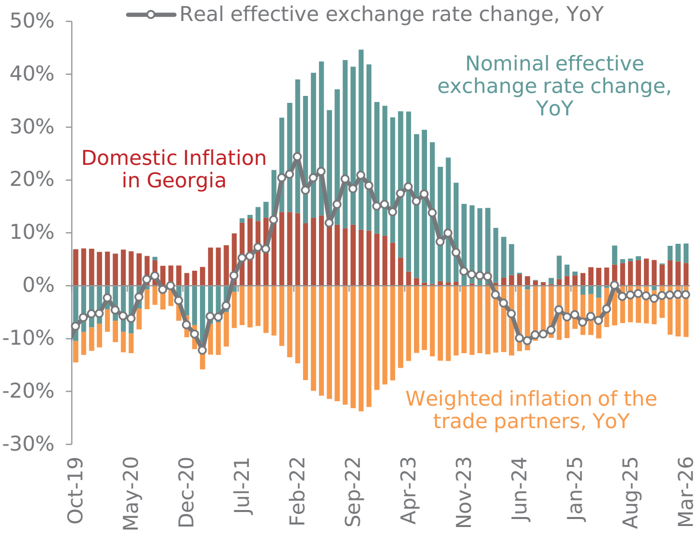

Figure 2.1.9. Decomposition of the Year-over-year Change in the Real Effective Exchange Rate of the Georgian lari*

Source: NBG, Geostat.

* The Real effective exchange rate and its components are presented in logarithmic terms, and, accordingly, their year-over-year changes are a first-order approximation of percentage changes.

Amid increased uncertainty, the deposit dollarization has increased, largely driven by legal entities.

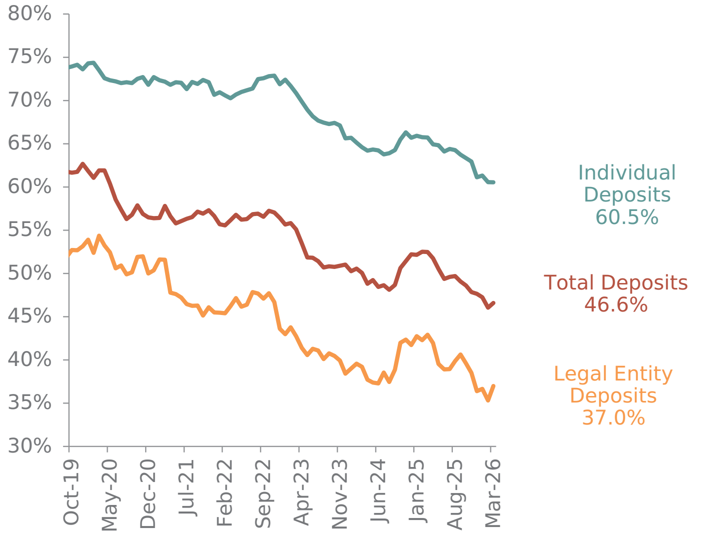

Figure 2.1.10. Deposit Dollarization (Excluding Exchange Rate Effects)

Source: NBG.

Despite elevated global uncertainty, Georgia's sovereign risk premium remains below its equilibrium level, indicating the country's strong macroeconomic fundamentals and favorable investor sentiment towards Georgia internationally.

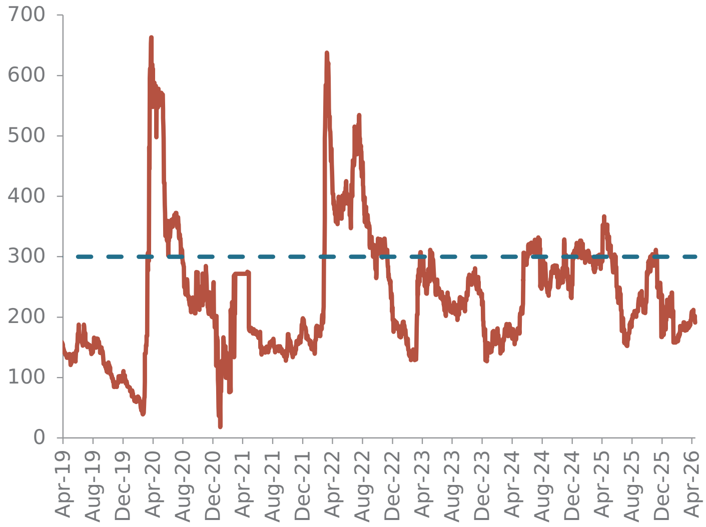

Figure 2.1.11. Spread Between 5-Year USD-Denominated Government Bond Yields of Georgia and the United States

Source: Bloomberg, NBG.

Amid a modest deceleration in productivity and an acceleration in wage growth, unit labor costs have approached the 3% target.

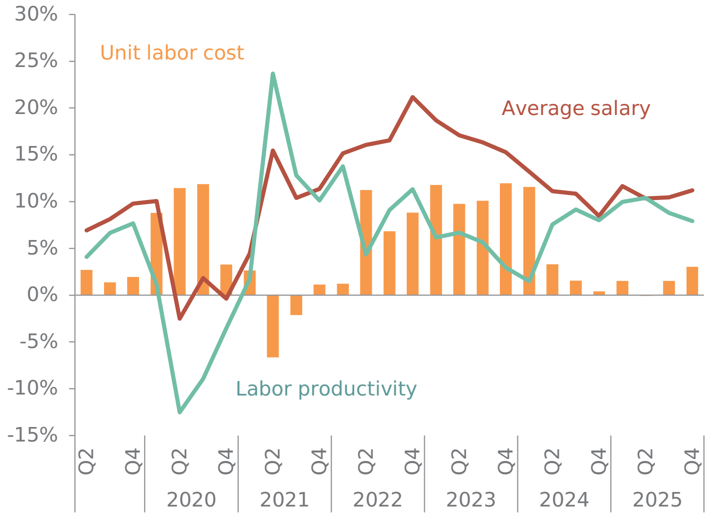

Figure 2.1.12. Average Wage, Labor Productivity, and Unit Labor Cost, Year-over-year Growth Rate

Source: Geostat, NBG.

Increased job opening to unemployment ratio indicates increased labor market tightness.

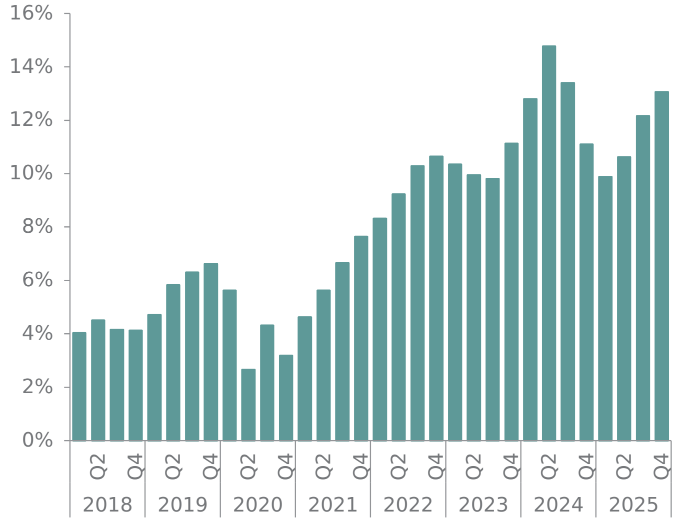

Figure 2.1.13. Jobs Opening to Unemployment Ratio, Seasonally Adjusted

Source: PMCG, Geostat.

Amid escalating geopolitical tensions, fuel prices have already increased, while risks of more persistent food inflation are also emerging. These developments intensify pressures on flexible prices, which, in turn, heighten the risk of rising long-term inflation expectations and, consequently, sticky prices.

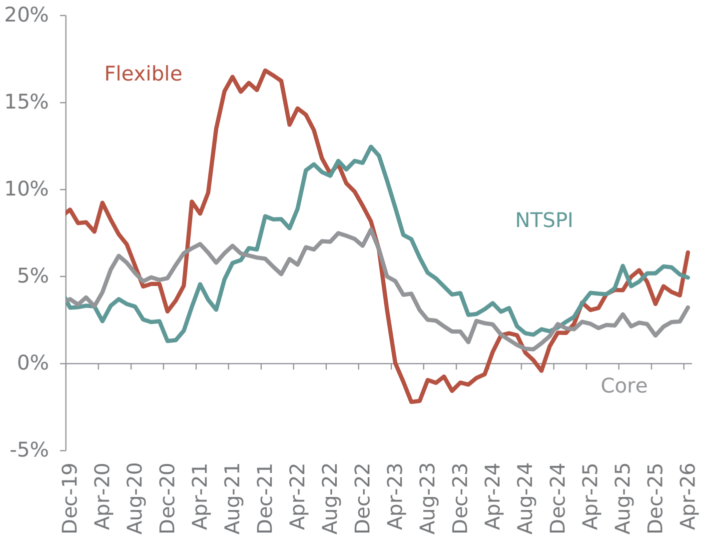

Figure 2.1.15. Core, Flexible and Non-Tradable Sticky Price (NTSPI) Year-over-year Inflation Measures.

Source: Geostat, NBG's Calculation.

Amid the war, rising global energy prices have made fuel prices inflationary. In addition, the direct effect of utility tariff adjustments was reflected in April inflation. Nevertheless, food prices continue to make the dominant contribution to headline inflation.

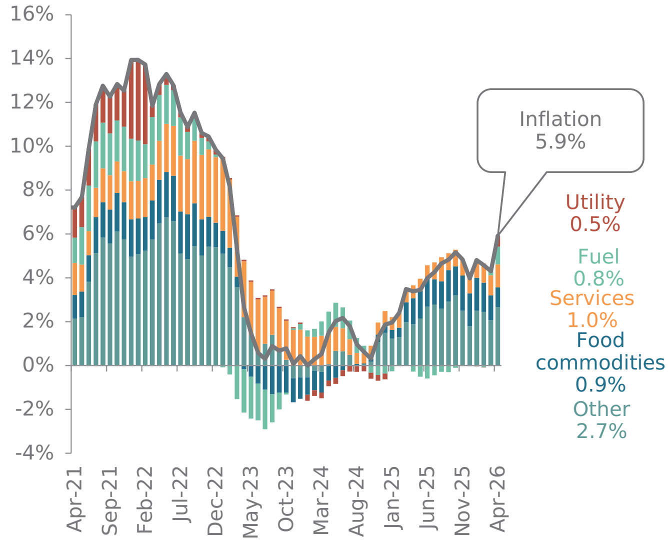

Figure 2.1.14. Inflation by Components

Source: Geostat, NBG.

2.2. CENTRAL SCENARIO

The marked deterioration in geopolitical conditions in the Middle East has triggered another supply shock to the global economy, sharply heightening uncertainty. Global economic developments have become increasingly dependent on war-related factors. Given that the duration, scale, and, consequently, the effects of the shock are difficult to predict in real time, a scenario-based approach has gained even greater importance. The National Bank of Georgia's **central scenario** incorporates a broad range of current information discussed in the preceding chapters, together with assumptions regarding exogenous factors and the channels through which they affect the domestic economy. Ultimately, it reflects a monetary policy path that, in line with the policymaker's preferences[6] and taking due account of the prevailing balance of risks, minimizes macroeconomic losses and ensures readiness in the event that alternative, yet equally relevant, scenarios materialize.

The current central scenario rests on the following key **assumptions**: hostilities are assumed to end within the current quarter, after which energy supply gradually recovers, with oil infrastructure only moderately damaged. International oil prices are assumed to peak in the current quarter at a quarterly average of USD 106 per barrel. In the following quarter, as de-escalation proceeds and supply capacity is gradually restored, prices decline significantly, bringing the annual average to USD 88 per barrel. Ultimately, although the rise in commodity prices was compounded domestically by higher electricity tariffs, the central scenario assumes only a moderate increase in inflation expectations, with elevated risks of second-round effects.

Regarding the outlook for **economic growth**, recent economic activity has proved stronger than expected, both domestically and globally. Georgia's economic growth continues to be driven primarily by service-oriented sectors, which are relatively less import-intensive (see Subchapter 2.1, Overview of the Current Macroeconomic Environment in Georgia). Under the central scenario, the direct impact of the escalation of the war in the Middle East on external demand is expected to be negative. However, geopolitical conditions may have heterogeneous effects across sectors. Ultimately, their net impact on economic growth is projected to be mildly negative. On the one hand, the war will put downward pressure on tourism revenues through cancellations of internation-

6 The National Bank of Georgia's priorities to anchor inflation expectations around the inflation target.

Despite stronger-than-expected growth momentum in the recent period, economic activity will normalize rapidly, with GDP growth standing at 6.5% in 2026 before returning to 5% thereafter.

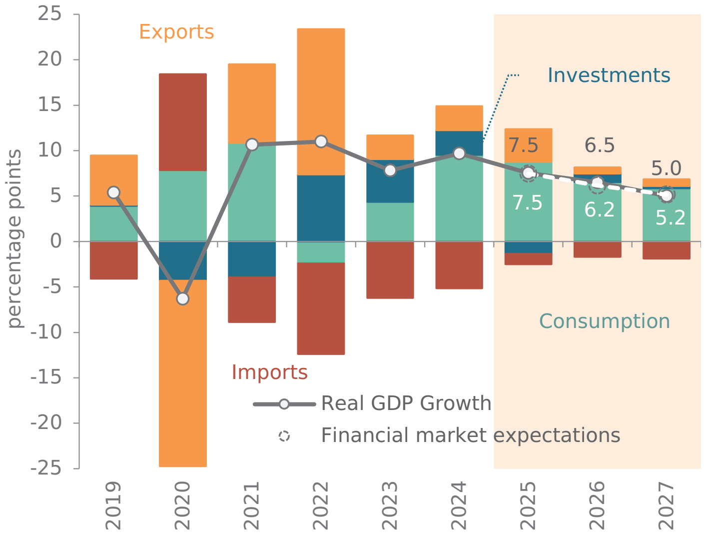

Figure 2.2.1. Central Scenario for Real GDP Growth and Financial Market Participants' Expectations of Economic Activity

Source: NBG, Financial Market Participants, Geostat.

al flights, heightened regional uncertainty, and weaker economic activity in the Middle East. In addition, higher energy prices will reduce households' purchasing power, which, together with tighter global and domestic financial conditions, is expected to slow the pace of aggregate demand growth to some extent. On the other hand, partly offsetting these effects, the escalation of the conflict has triggered a global commodity supply shock that will support growth in Georgia's mining and metallurgical exports while also strengthening demand from oil-exporting economies in the region. As a result, stronger-than-expected growth momentum in the recent period has prompted an upward revision to the 2026 growth forecast relative to the previous central projection. However, as the effects of the conflict materialize, economic activity will normalize relatively quickly, with **GDP growth ultimately reaching 6.5%.** Thereafter, growth will return to its long-term rate of 5% (see Figure 2.2.1).

In turn, **financial market expectations also point to the normalization of real GDP growth**. In particular, according to the average forecast of market participants, real GDP growth in 2026 and 2027 will amount to 6.2% and 5.2%, respectively.

Given the high share of oil products, food, and, more broadly, imported goods in the consumer price index, **global inflationary developments have a significant impact on inflation dynamics domestically**. Heightened volatility in international commodity markets has already fed through to headline inflation. Among these effects, the contribution of fuel prices is particularly noteworthy, adding 0.8 pp to annual inflation. However, the ultimate inflationary impact stemming from oil products will depend primarily on the duration of the Strait of Hormuz blockade and the scale of damage to energy infrastructure. At the same time, developments in the Middle East also shape both the extent of supply-chain disruptions and inflationary pressures stemming from selected food categories. In addition, higher diesel and fertilizer prices in international markets will increase intermediate input costs in the agricultural sector, both globally and domestically, which will also be reflected in final food prices.

Alongside external factors, increases in locally administered prices also warrant particular attention. The increase in electricity prices, together with higher excise taxes on cigarettes and car imports, is adding to inflationary pressure. However, high base effects from the previous year are exerting downward pressure on food inflation, including as the impact of last year's increase in wheat bread prices gradually fades.

Against the backdrop of higher global infla-

Against the backdrop of increased inflationary pressures, inflation will rise. However, as the supply-side shock is expected to be one-off in nature and amid the gradual normalization of exogenous factors, inflation will average 4.9% in 2026 and 2.5% in 2027, respectively.

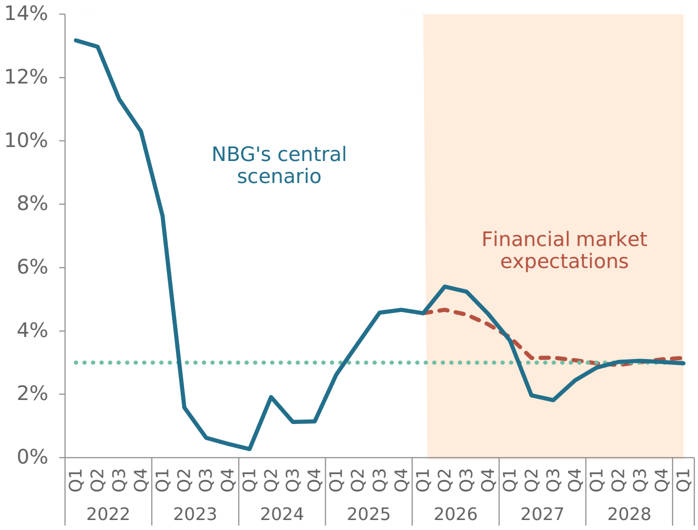

Figure 2.2.2. Central scenario of annual inflation and inflation expectations of financial market participants

Source: NBG, Financial Market Participants.

The fading of commodity price effects and base effects related to certain products will support inflation's gradual return to the target. At the same time, the normalization of aggregate demand will also exert downward pressure on inflation dynamics.

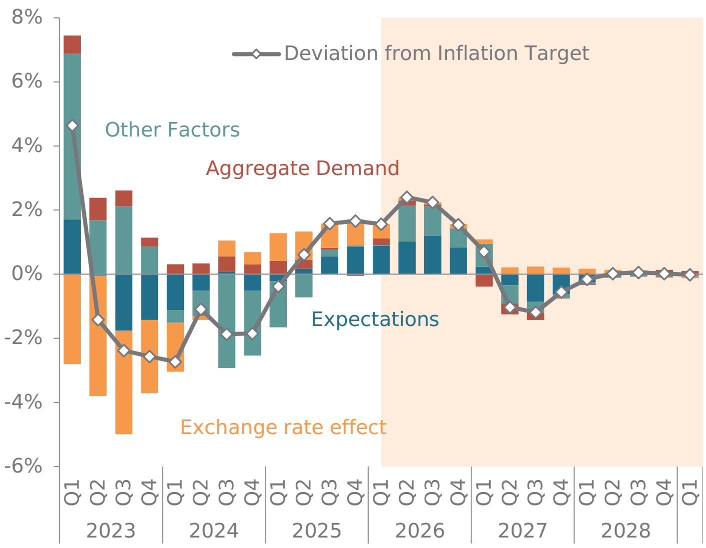

Figure 2.2.3. Decomposition of annual inflation deviations from target under the central scenario

Source: NBG, Geostat.

tion forecasts, monetary policy normalization in advanced economies has been significantly delayed, while year-end interest rate expectations have increased. As a result, global financial conditions have tightened significantly, and the risk of capital outflows toward safe-haven assets has increased. However, it is worth noting that Georgia's sovereign risk premium currently remains below its equilibrium level. This points to positive sentiment from international investors and, alongside the assumption that hostilities in the Middle East will have a limited direct impact on the current account balance, underpins the currently strong position of the exchange rate.

Overall, reflecting the strong but **one-off impact** of the supply shock, **headline inflation will rise to an average of 4.9% in 2026, before moving back toward the target and averaging 2.5% in 2027** (see Figures 2.2.2–2.2.3). In turn, the normalization of inflation toward the target will be supported by the fading of the exogenous shock, weaker aggregate demand, and the currently strong position of the exchange rate.

Compared with the previous central scenario, the inflation forecast for 2026 has been revised up by 1.2 pp, while the forecast for 2027 has been revised down by 0.3 pp, pointing to the one-off nature of the current increase in inflation. Overall, however, the inflation outlook has tilted toward the high-inflation scenario published in the previous quarter, in which rising energy prices were identified as one of the key risks. At the same time, it should be noted that the current oil price assumptions, which are based on futures prices, expectations regarding market fundamentals, and global consensus forecasts, are highly conditional amid elevated uncertainty. Accordingly, the risks embedded in the high-inflation scenario have gained even greater importance, as simultaneous strong supply shocks increase the risk of high inflation expectations and so-called second-round effects.

Compared with the previous survey, **financial market participants' inflation expectations** for 2026 have increased by 1.1 pp, to 4.5%, although they remain below the NBG's central scenario forecast. At the same time, the 2027 forecast has increased slightly, by 0.2 pp, to 3.3% (see Figure 2.2.2).

As noted above, the acute inflationary pressures stemming from exogenous shocks are expected to be transitory. At the same time, however, **they create significant risks** of de-anchoring medium- and long-term inflation expectations, especially against the backdrop of elevated headline inflation that has remained above the target for a relatively prolonged period. Central banks

Monetary policy will be moderately tightened to keep inflation expectations well anchored in the face of temporary but strong supply-side inflationary pressures.

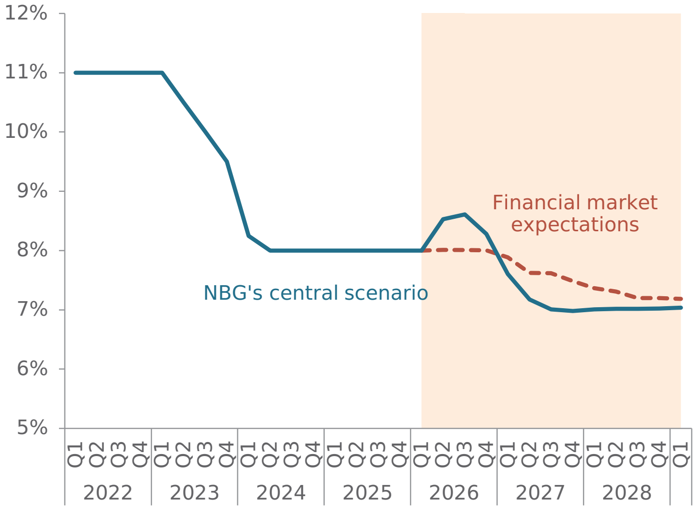

Figure 2.2.4. Central scenario of the monetary policy rate and expectations of financial market participants

Source: NBG, Financial Market Participants.

generally look through one-off supply shocks; however, when the above-mentioned risks become more pronounced, they stand ready to tighten monetary policy. Against the backdrop of a combination of supply-side inflationary shocks and prevailing uncertainty surrounding external conditions in the current period, the National Bank of Georgia considers a moderate tightening of monetary policy appropriate to keep inflation expectations anchored around the target (see Figure 2.2.4). The envisaged monetary policy tightening path is aimed primarily at keeping inflation expectations firmly anchored around the target, thereby limiting the propagation of so-called second-round effects. This, in turn, is particularly important in the face of a strong supply shock. As a result, the moderate tightening of monetary policy helps ensure that inflationary pressures do not broaden into more persistent high-inflation dynamics and that, once the effects of supply shocks fade, inflation returns to its 3% target. At the same time, amid prevailing uncertainty, upside risks to inflation remain more pronounced. Accordingly, the policy rate tightening path also reflects the National Bank's pre-emptive readiness to respond to the possible further materialization of upside risks to inflation. From a risk-management perspective, and given that the high-inflation scenario would be particularly costly for the economy, the current tightening also reduces the risk of inflationary pressures broadening into more generalized inflation dynamics should additional inflationary risks materialize. Once the transitory supply-side inflationary effects fade and inflation returns to the 3% target, the NBG will gradually exit from its tightened monetary policy stance.

2.3. HIGH-INFLATION SCENARIO

The high-inflation scenario is primarily based on a prolonged conflict in the Middle East, severe inflationary pressures stemming from petroleum products and food prices, and their second-round effects.

High-Inflation Risks	
◦ A significant escalation of geopolitical tensions in the Middle East. ◦ A substantial increase in international oil and domestic fuel prices and pronounced second-round effects. ◦ An increase in transportation costs and international food prices.	
Indicators of risk realization	**Impact on inflation**
Elevated domestic inflation driven by increases in international commodity prices.	↑
A deterioration of short-term inflation expectations.	↑
Deterioration of the current account balance amid strong imports on the one hand and declining tourism revenues on the other.	↑
In the short-run, an increase in the regional and country risk premiums.	↑
A reduction in investment and consumer spending.	↓

Impact size			
Neutral	Low	Medium	High

↑	Upward Pressure on Inflation
→	Same Level of Inflation
↓	Downward Pressure on Inflation

Table 2.3.1. Taxonomy of Risks in High-inflation Scenario

Source: NBG.

Amid high uncertainty, the **High-Inflation Scenario** is as relevant as the central scenario and considers the realization of the identified risks that would result in a higher inflation than in the central scenario. In particular, the scenario assumes a more pronounced materialization of both domestic and global inflationary risks identified in the current data, compared to the central scenario. In this context, one of the main risks is the prolongation of the conflict in the Middle East and, consequently, the strong inflationary pressures stemming from commodity markets (see Table 2.3.1). Accordingly, if these risks materialize, the NBG will pursue a tighter monetary policy compared with the central scenario to prevent a deterioration of long-term inflation expectations.

Existing heightened uncertainty and volatility in the global economy have further increased following the renewed conflict in the Middle East. The High-Inflation scenario assumes a further escalation and prolonged persistence of the conflict compared to the central scenario. The aforementioned, on the one hand, would inflict substantial damage on the region's oil infrastructure and postpone the reopening of the Strait of Hormuz, thereby significantly reducing the supply of oil to the global market and further increasing global petroleum product prices. Specifically, in this scenario, international oil prices are assumed to be, on average, 16% higher in 2026 compared to the central scenario (with the price of oil reaching USD 130 per barrel in the second quarter and averaging USD 100 over 2026). In addition, both disruptions to supply chains and elevated petroleum product prices will exert significant pressure on the production and transportation costs of food commodities, leading to a marked increase in food prices on international markets.

On the other hand, an extension of the conflict in the Middle East will raise both regional and country risk, dampen regional economic growth, and trigger capital outflows toward safe-haven assets. This would also worsen domestic investment sentiment and, in the context of the slowdown in regional economies, substantially reduce tourism revenues and foreign direct investment. Consequently, in **2026, economic growth will slow** compared to the central scenario and, **amid inertia in consumer spending, will average 5.5%** (see Figure 2.3.1). In addition, a decline in tourism revenues, together with higher costs of petroleum product imports, will worsen the current account deficit, which, amid capital outflows into safe-haven assets, will exert pressure on the effective exchange rate. Consequently, this, alongside the increase in international commodity

Amid slower external inflows and inertia in domestic demand, real GDP growth will be 5.5% in 2026, while in 2027, amid tighter monetary policy in response to inflationary pressures, it will stand at 4.5%.

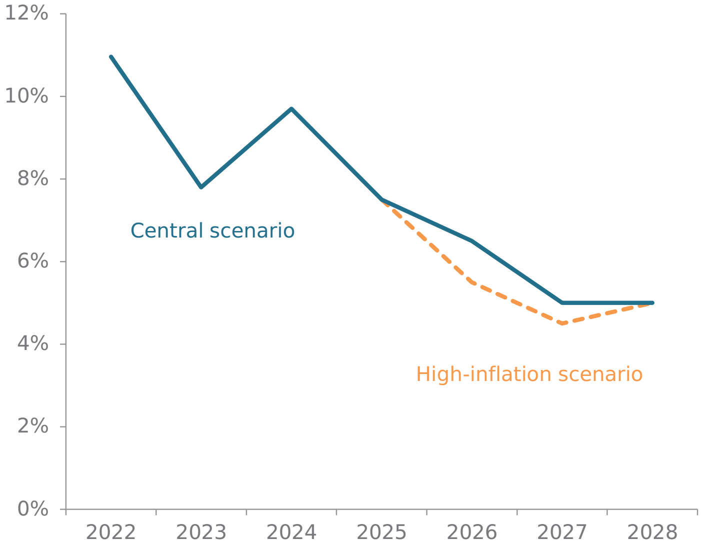

Figure 2.3.1. Real GDP Growth Under Central and High-Inflation Scenarios

Source: NBG, Geostat.

prices, will result in imported inflationary pressures, which will be transmitted to the domestic market through both direct and indirect channels. In addition, considering its severity and magnitude, the risk of the materialization of second-round effects also increases. Specifically, a prolonged period of inflation above the target strengthens inflationary pressures stemming from the labor market, which contributes to adjustment of relatively sticky prices and, ultimately, impedes the return of inflation to its target level. **Accordingly, in the high-inflation scenario, inflation will be higher by 0.9 pp and 1.4 pp in 2026 and 2027,** compared to the central scenario, **respectively averaging 5.8% and 3.9%** (see Figure 2.3.2). The NBG exhibits a low tolerance against rising inflation expectations and the materialization of second-round effects. Consequently, the above-mentioned developments would lead to a tightening of monetary policy. As a result of the effects of tighter monetary policy, **real GDP growth will amount to 4.5% in 2027** (see Figure 2.3.1).

Ultimately, **the monetary policy rate will be higher than in the central scenario by 0.6 pp in 2026 and by 1.4 pp in 2027**. Moreover, A globally high-inflation environment will lead to an increase in neutral interest rates in advanced economies, which in the medium term, **will be transmitted to the domestic neutral rate, driving it up to 7.5%.** Subsequently, the policy rate's normalization toward this level is expected to continue gradually, contingent on the stabilization of the inflationary environment (see Figure 2.3.3).

Instability on commodity markets, risks of second-round effects from elevated energy prices, and depreciation pressures on the exchange rate will significantly increase inflationary pressures over the monetary policy horizon and will delay the return of inflation to its target level for an extended period.

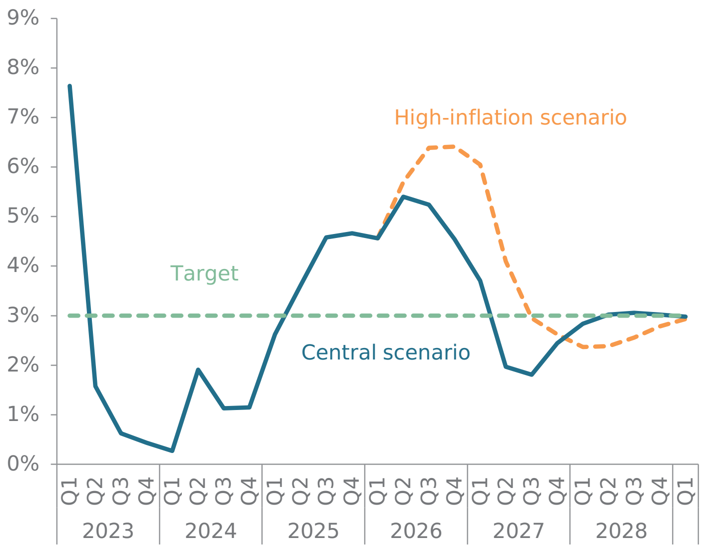

Figure 2.3.2. Year-over-year Headline Inflation Under Central and High-Inflation Scenarios

Source: NBG, Geostat.

The National Bank of Georgia has a low tolerance against the rise in inflation expectations. Consequently, the high inflationary environment in this scenario, compared to the central scenario, will lead to a tightening of monetary policy. Its normalization will begin at a gradual pace, contingent on the stabilization of the inflationary environment, towards 7.5% level.

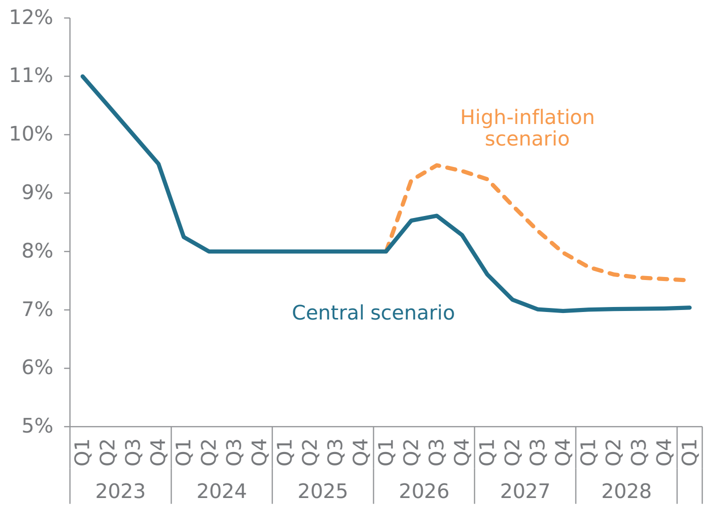

Figure 2.3.3. Monetary Policy Rate Under Central and High-Inflation Scenarios

Source: NBG.

2.4. LOW-INFLATION SCENARIO

The low-inflation scenario, relative to the central, envisions lower oil and food prices on international commodity markets, amid a rapid normalization of geopolitical tensions in the Middle East. In addition, the scenario considers the maintenance of high productivity growth.

Low-Inflation Risks	
◦ Amid a rapid de-escalation of the ongoing conflict in the Middle East, a decline in oil prices in international commodity markets and their full pass-through to the domestic market. ◦ Reallocation of global supply chains and the growing role of Georgia as the Middle Corridor country. ◦ Amid the slow normalization in the growth of highly productive sectors, their contribution to economic activity remaining at a relatively high level. ◦ The longer-than-expected weak position of the U.S. dollar.	
Indicators of risk realization	**Impact on inflation**
Low prices of petroleum products in the domestic market.	↓
The sustained high growth of economic potential.	↓
The maintenance of a low sovereign risk premium.	↓
Amid strong external inflows, the maintenance of an improved current account balance.	↓
Impact size	
Neutral, Low, Medium, High	
↑ Upward Pressure on Inflation	
→ Same Level of Inflation	
↓ Downward Pressure on Inflation	

Table 2.4.1. Taxonomy of Risks in Low-inflation Scenario

Source: NBG.

The Low-Inflation Scenario is as relevant as the high-inflation and central scenarios. It envisions the materialization of relevant risks that are less inflationary compared to the central scenario (see Table 2.4.1). Particularly, this scenario assumes a decline in international oil prices in commodity markets amid a rapid de-escalation of the ongoing conflict in the Middle East, and their full pass-through to domestic petroleum prices. Moreover, productivity is expected to remain at a relatively high level, which, in turn, will mitigate inflationary pressures stemming from strong aggregate demand. Furthermore, the scenario considers the maintenance of a weak U.S. dollar positions globally.

In recent years, Georgia's sustained strong economic growth has been primarily driven by structural changes, and accelerated the economy's potential growth. The low-inflation scenario assumes that even under the rapid de-escalation of the Middle East conflict, the accelerated global trade diversification process will be maintained. As a result, the realignment and regionalization of supply chains will further strengthen Georgia's role as a Middle Corridor country, additionally boosting the international transportation sector. Accordingly, high-productivity sectors including transportation and logistics, will continue to serve as the primary drivers of economic growth and the economy's potential growth is expected to remain at a high level.

High productivity will, in turn, offset the pressure stemming from positive output gap and, amid disinflationary effects from the supply side, will lead to a normalization of the policy rate. Meanwhile, despite heightened geopolitical risks, Georgia's sovereign risk premium has declined since the beginning of the year and remains at a low level. In the event of a de-escalation of geopolitical risks, a reduction in regional riskiness would further support this dynamic. This, coupled with improved financial conditions, will contribute to an increase in investment activity. Eventually, amid an improved economic outlook, **under this scenario, economic growth is projected to average 7.5% in 2026. Strengthened macroeconomic fundamentals lead to a revision of long-term potential growth to 5.5 percent, and economic growth in 2027 will stabilize around this level** (see Figure 2.4.1).

As noted above, assumptions around the international commodity markets continue to be key in the low-inflation scenario. In particular, this scenario assumes amid de-escalation of the ongoing conflict in the Middle East, a rapid decline in elevated oil prices and their full pass-through

Under the low-inflation scenario, amid rising external inflows, strong potential growth, and easing inflationary pressures, followed by the rapid normalization of monetary policy, real GDP growth in 2026 and 2027 will average 7.5% and 5.5%, respectively.

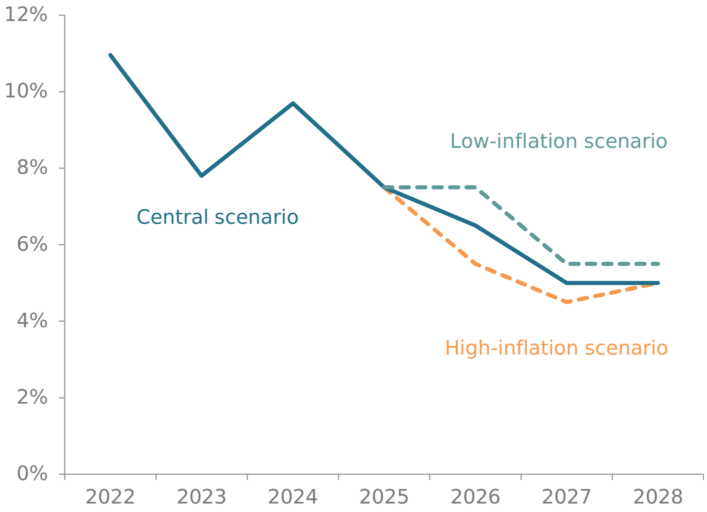

Figure 2.4.1. Real GDP Growth Under Central, High-Inflation, and Low-Inflation Scenarios

Source: NBG, Geostat.

Amid economic growth driven by strong fundamental factors and declining international commodity prices, inflation will average 4.3% and 2.4%, in 2026 and 2027, respectively. Over the long term, it will stabilize around its target level.

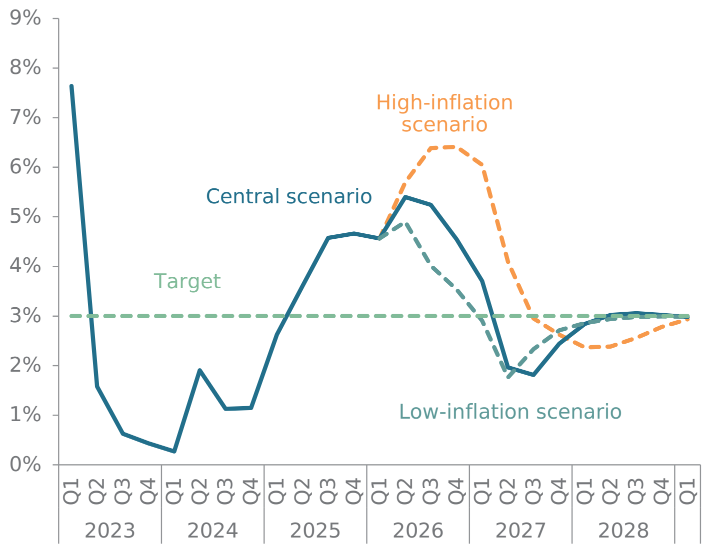

Figure 2.4.2. Year-over-year Headline Inflation Under Central, High-Inflation, and Low-Inflation Scenarios

Source: NBG, Geostat.

to domestic petroleum markets (with the price of oil reaching USD 100 per barrel in the second quarter and averaging USD 82 over 2026). This, in turn, will exert downward pressure on inflation and its expectations.

Meanwhile, a rapid normalization of the geopolitical risks and the maintenance of a low domestic risk premium, will support stronger external inflows. In particular, increased services exports (including tourism and transportation), will have a positive impact on the current account balance and contribute to the exchange rate appreciation. This will be further reinforced by the normalization of safe-haven demand amid easing turbulence, and accelerated de-dollarization tendency. All the aforementioned, ultimately, will significantly reduce headline inflation through the imported inflation channel.

Meanwhile, as a result of strong productivity growth and reduced inflation expectations, unit labor costs will have a disinflationary tendency, further reducing domestic inflation. Thus, under the realization of the abovementioned scenario, **headline inflation will be lower compared to the central scenario, averaging 4.3% in 2026. Meanwhile, by the end of 2027, inflation will stabilize around the target, averaging 2.4%** (see Figure 2.4.2).

Amid fading inflationary risks and the persistence of strong fundamental factors, monetary policy normalization will proceed at a faster pace relative to the central scenario. Particularly, a sharp decline in international oil prices and their full pass-through to domestic petroleum prices, as well as strong productivity growth alongside an appreciation of the exchange rate, will generate significant disinflationary pressures and reduce inflation expectations. Accordingly, **relative to the central scenario, the monetary policy rate is projected to be on average 0.6 pp lower in 2026 and to stabilize around its long-term neutral level of 7% in 2027** (see Figure 2.4.3).

Under the low-inflation scenario, amid disinflationary dynamics from the supply side, monetary policy will normalize toward its 7 percent neutral level more swiftly compared to the central scenario.

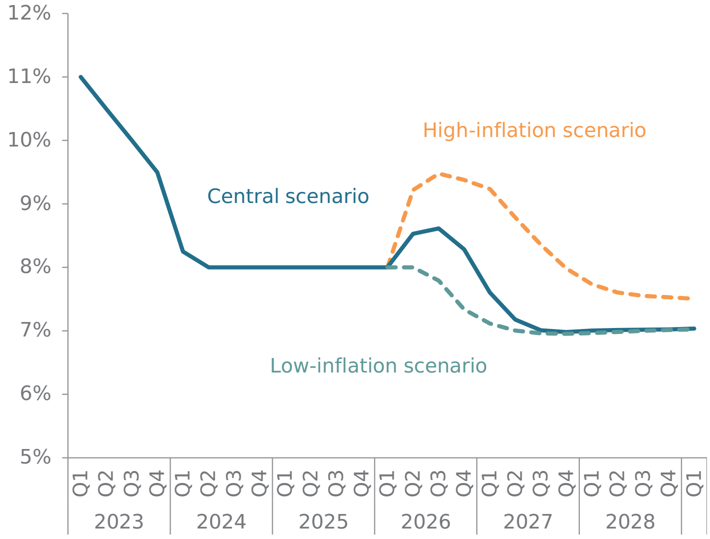

Figure 2.4.3. Monetary Policy Rate Under Central, High-Inflation, and Low-Inflation Scenarios

Source: NBG.

3. SPECIAL TOPICS

BOX 1. THE IMPACT OF THE ONGOING MIDDLE EAST CONFLICT ON GEORGIA'S ECONOMY

The ongoing conflict in the Middle East represents another severe global supply-side shock, increasing stagflationary risks. Its impact has already been reflected in international commodity prices (particularly energy resources, food, and fertilizers) as well as in financial markets. A particularly important risk factor is the blockade of the Strait of Hormuz, through which roughly one-third of the world's oil and fertilizer supplies, along with significant volumes of liquefied natural gas (LNG), are transported. Consequently, any disruption to this route would place substantial upward pressure on international commodity prices (see Chapter 1). At the same time, a closure of the Strait of Hormuz would heighten the risks of supply-chain disruptions and consequently, increase transportation costs. Notably, the impact of this shock is asymmetric across global economies; however, rising energy prices generate inflationary pressures worldwide.

Georgia is a small open economy and, therefore, remains vulnerable to external shocks. Consequently, it is important to assess both the direct and indirect transmission effects of the current shock on the Georgian economy. The assessment presented in this box is based on the central scenario assumption that the ongoing conflict will end in the second quarter. However, the overall economic impact of the war will depend significantly on its duration and intensity.

The direct impact of the war on Georgia's net external balance, through goods trade, tourism, and remittances, is moderate, reflecting the relatively small share of the Middle East in Georgia's overall trade structure. However, the war has led to a significant increase in international commodity prices, which has notably affected the domestic market. At the same time, heightened riskiness has resulted in tighter financial conditions globally, which are also being transmitted to the domestic financial market. In general, during periods of crisis, demand for safe-haven assets increases. This was reflected in the initial appreciation of the U.S. dollar at the onset of the war, which in turn created cyclical pressure on the Georgian lari (GEL) and the currencies of Georgia's main trading partners. Currently, the U.S. dollar maintains a relatively weak position, which is contributing positively to the stability of the GEL.

Among the direct transmission channels, one of the most tangible effects is observed in the tourism sector. Revenues from travel account for a significant share of the Georgian economy, amounting to 12.3% of GDP as of 2025. Against the backdrop of the conflict, restrictions on flights from Middle Eastern countries and India, together with rising airfare prices, have reduced tourist inflows, leading to a slowdown in the growth of tourism revenues (see Figure 3.1). As a result, the growth rate of travel revenues stood at 0.5% in the first quarter of 2026 (see Figure 3.1). In turn, the slowdown in tourism revenues also has a negative impact on the current account balance. Under the central scenario, if the conflict ends in the second quarter and flights from the Middle East and India gradually resume, the negative effect of travel export revenues on the current account balance during 2026 is expected to remain relatively limited (All else equal, the current account deficit-to-GDP ratio may widen by around 0.3–0.4 pp due to this effect). However, if the conflict is prolonged and airfare prices continue to rise, particularly amid higher jet fuel prices, global tourism activity

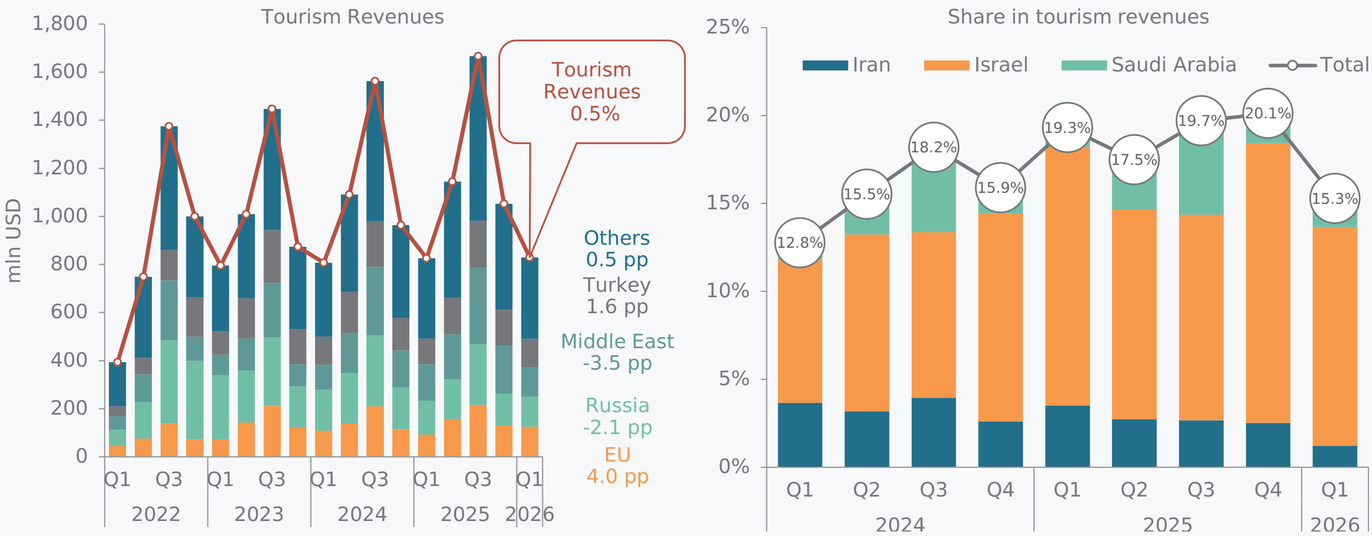

Figure 3.1. Dynamics of Tourism Revenues and the Share of Middle Eastern Countries in Total Tourism Revenues

Source: NBG, Geostat.

may weaken further. This could also slow the growth of tourism revenues from other countries. A slowdown in the tourism sector would also negatively affect related sectors, including hotels and restaurants, as well as transportation services.

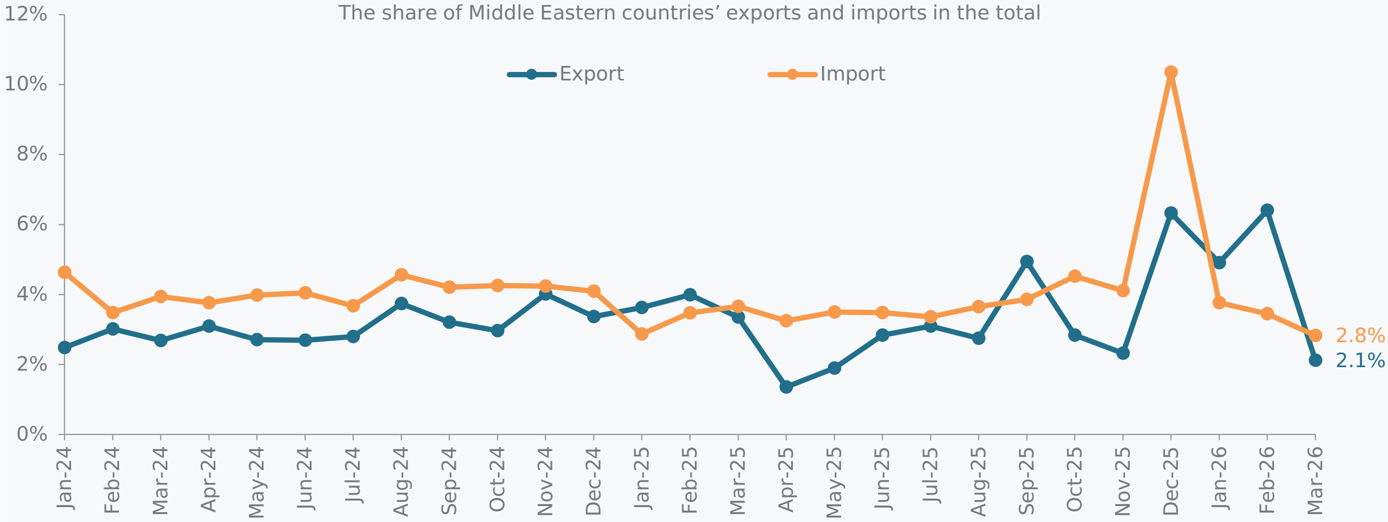

Figure 3.2. Share of Middle Eastern Countries in Total Exports and Imports.

Source: NBG, Geostat.

The effect of the Middle East war on remittances is mostly moderate and, in the short run, tends to have an upward impact. Notably, remittances from Iran are negligible for Georgia, whereas the share of Israel is significant. In the first quarter of 2026, the contribution of remittances from this region to total growth amounted to approximately 1.7 pp, which was largely explained by a 19.2% YoY increase in remittances from Israel (see Figure 3.3). Experience from previous periods suggests that at the initial stage of geopolitical shocks, remittances typically tend to increase. However, in the event of a deepening or prolonged conflict, risks rise: a slowdown in economic activity in remittance-source countries could negatively affect remittance volumes and, consequently, the current account balance. Accordingly, their dynamics are to some extent dependent on the duration and intensity of the geopolitical shock.

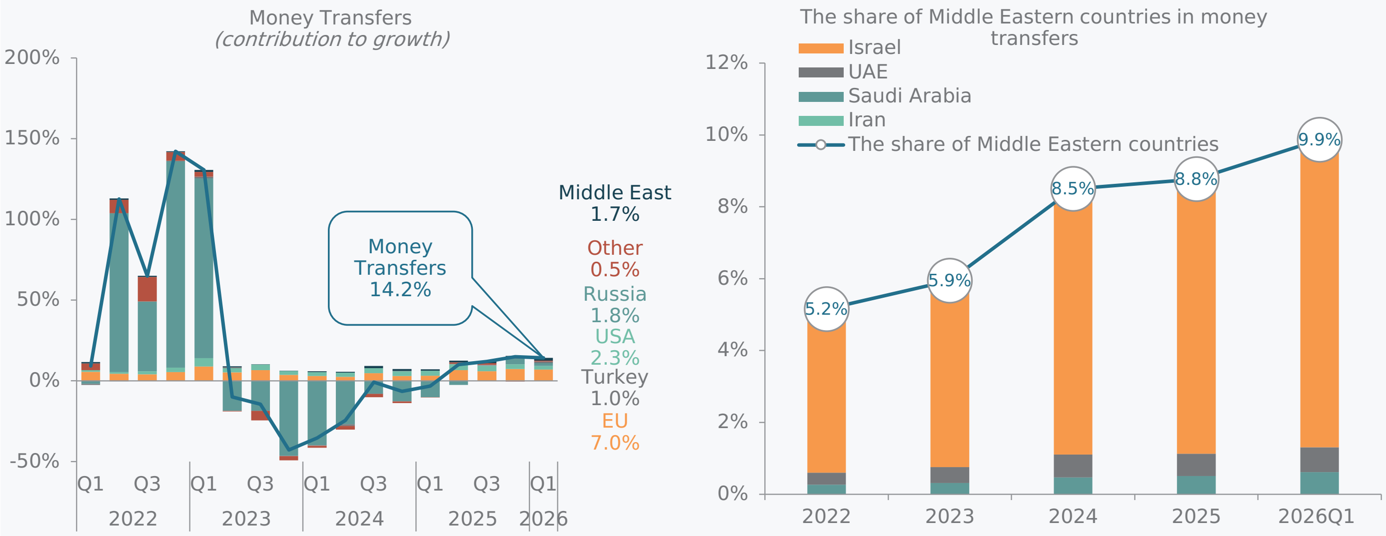

Figure 3.3. Dynamics of Remittances and the Share of Middle Eastern Countries in Total Remittances

Source: NBG, Geostat.

Ultimately, taking into account the above assumptions and transmission channels, under conditions of a relatively swift resolution of the conflict and accounting for the price effects, the additional effects on goods exports and imports and tourism revenues, would largely balance each other. As a result, the current account is expected to remain within its equilibrium level (5%). On the other hand, the impact of the net external balance on real GDP, all else being equal, would be approximately -1 pp.

Beyond the external channels discussed above, notable risks are also emerging regarding inflation. In particular, when assessing inflationary effects, the impact of this supply shock can be divided into three main channels: direct, indirect, and second-round effects. Through the direct channel, the rise in energy prices has already been reflected in inflation dynamics (see Chapter 2.1). Specifically, the increase in Brent crude oil prices to 100 U.S. dollars per barrel is reflected in April's inflation figures (see Figure 3.4, as well as Chapter 2.1). The further rise in oil prices to 120 U.S. dollars at the end of April is expected, all else being equal, to increase inflationary pressures in the coming months.

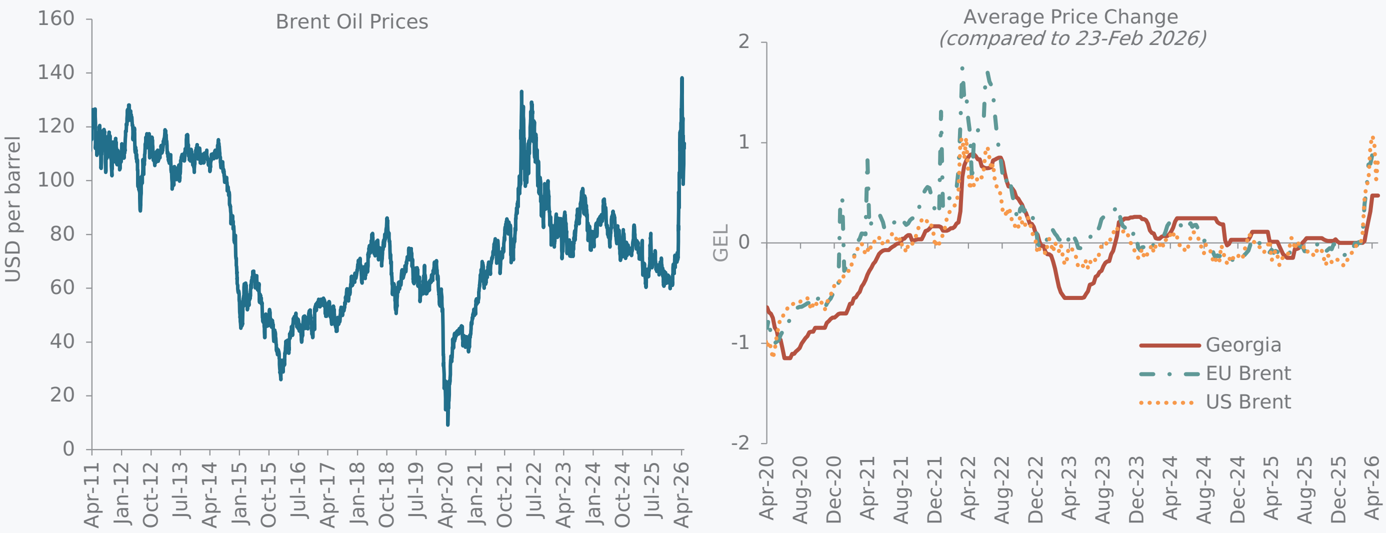

Figure 3.4. Brent Crude Oil Prices and the Fuel Price Index for Georgia

Source: FRED, NBG.

Through indirect channels, the rise in energy prices increases transportation costs and overall production costs, which are gradually transmitted to the prices of goods and services associated with fuel consumption. Higher production costs and price increases further intensify and prolong inflationary processes, including through the inertia component.

In terms of indirect effects, it should be noted that the Middle East conflict has also led to an increase in fertilizer prices, which, all else being equal, puts upward pressure on global food prices. This, in turn, strengthens the risk of higher imported inflation through the international food price channel (see Chapter 1.2).

In general, central banks typically do not respond to supply-side shocks, as their ability to influence supply conditions is limited. However, when a supply shock is strong and large-scale, the risk of so-called second-round effects increases. In particular, in an environment of rising inflation expectations, higher consumer spending can increase pressure in the labour market, which subsequently feeds into price increases for other goods and services. Accordingly, anchoring of inflation expectations becomes especially important. Therefore, when risks of second-round effects and rising inflation expectations emerge, central banks may respond to supply shocks by tightening monetary policy. The objective is to ensure that, once the impact of exogenous factors on inflation dissipates, inflation returns to its target level.

4. SUMMARY OF THE MACROECONOMIC FORECASTS OF THE NBG AND FINANCIAL MARKET PARTICIPANTS

SUMMARY OF THE MACROECONOMIC FORECASTS OF THE NATIONAL BANK OF GEORGIA*

	Fact	Central Scenario			High-Inflation Scenario			Low-Inflation Scenario		
	2025	2026	2027	2028	2026	2027	2028	2026	2027	2028
Inflation (%)	3.9	4.9	2.5	3.0	5.8	3.9	2.5	4.3	2.4	2.9
Real GDP Growth (%)	7.5	6.5	5.0	5.0	5.5	4.5	5.0	7.5	5.5	5.5
Monetary Policy Rate (%)	8.0	8.4	7.2	7.0	9.0	8.6	7.6	7.8	7.0	7.0

Table 4.1. Summary of the Macroeconomic Scenarios of the National Bank of Georgia

Source: NBG, financial market participants, Geostat.

* The table reports annual averages for the variables.

FORECASTS OF FINANCIAL MARKET PARTICIPANTS

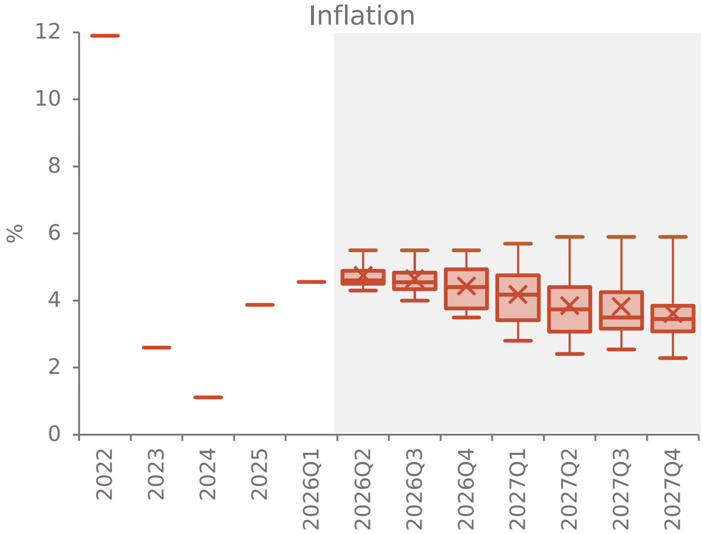

Figure 4.1. Actual average inflation and the distribution of market participants' forecasts

Source: NBG, financial market participants, Geostat.

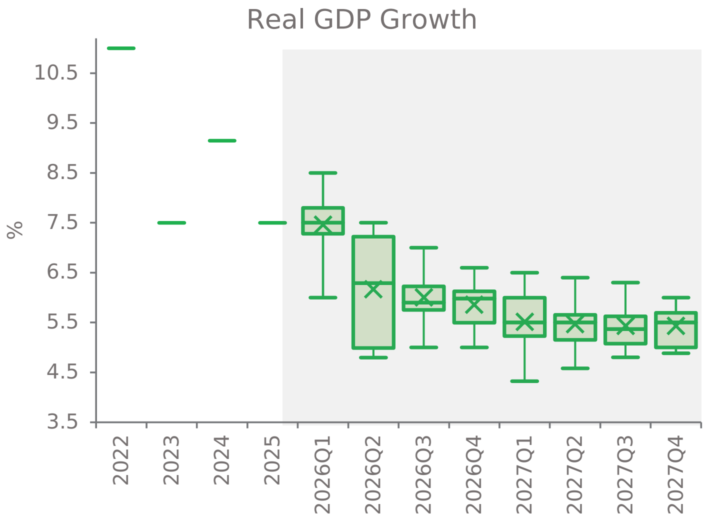

Figure 4.2. Actual real GDP growth and the distribution of market participants' forecasts

Source: NBG, financial market participants, Geostat.

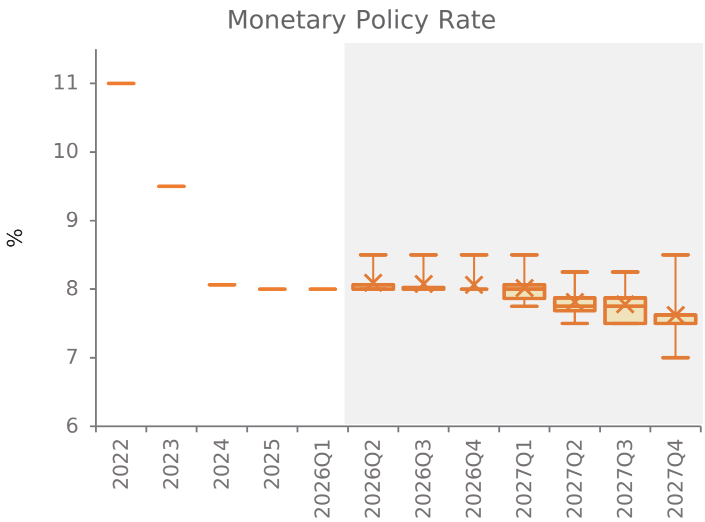

Figure 4.3. Actual monetary policy rate and the distribution of market participants’ forecasts

Source: NBG, financial market participants.

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