



TBC CAPITAL

UPDATE FROM THE CHIEF ECONOMIST

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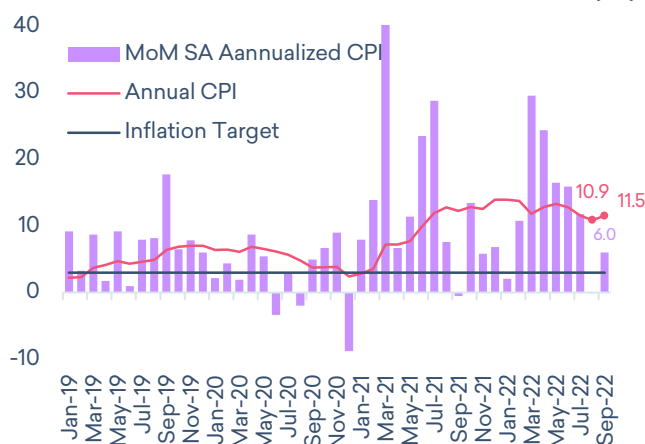
September inflation print came in at 11.5% YoY and 6.0% MoM annualized seasonally adjusted. This is above [our expectations](#) as our nowcasting framework pointed to a continuation in the normalization path of consumer prices. While a much slower normalization in domestic goods and services was well expected, the decline in imported inflation was only a fraction compared to what international dynamics in commodities would imply. In particular, the prices of key consumer basket categories such as fuel, sunflower oil, sugar and probably to some extent cereals are still expected to retreat. This should mean that we are leaving our earlier 2022 year end CPI projection of 7.4% broadly unchanged, however, taking into account the very recent dynamics the outlook is up to around 9.4% for the following reasons. First, a number of key commodity prices have recovered last week, though to note that even now, relatively less, but still sizable, expected deflationary pass through on the local market is a baseline. Second, there is evidence of a worse than anticipated harvest in the number of locally grown groceries such as potatoes, corn and the impact to a large extent will show up in October.

INFLATION BY PRODUCT GROUPS, SEP-22

	Sep-22/Aug-22		Sep-22/Sep-21	
	Growth, %	Contribution, PP	Growth, %	Contribution, PP
Total	0.8	0.8	11.5	11.5
Food and non-alcoholic beverages	1.7	0.6	17.6	5.7
Alcoholic beverages and tobacco	-0.3	0.0	7.9	0.5
Clothing and footwear	1.5	0.1	3.0	0.1
Housing, water, electricity, gas and other	0.0	0.0	12.2	1.1
Furnishings, household	0.4	0.0	10.1	0.5
Health	-2.0	-0.2	-1.1	-0.1
Transport	-1.3	-0.1	14.1	1.8
Communication	0.0	0.0	0.4	0.0
Recreation and culture	3.9	0.1	10.4	0.4
Education	7.5	0.4	6.4	0.3
Restaurants and hotels	0.5	0.0	15.7	0.9
Miscellaneous goods and services	1.1	0.1	11.7	0.6

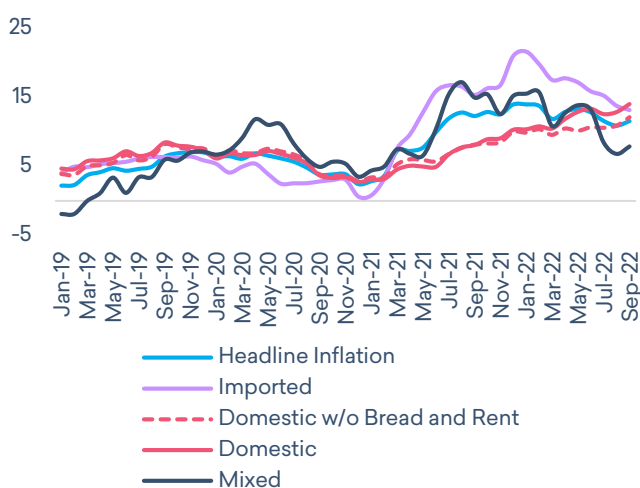
Source: Geostat

ANNUAL AND SEASONALLY ADJUSTED ANNUALIZED MONTHLY INFLATION (%)



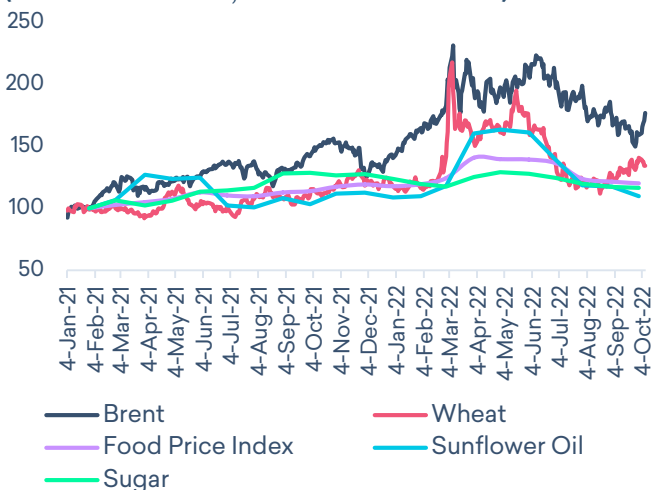
Source: Geostat, TBC Capital

CPI INFLATION BY FINAL PRODUCT ORIGIN (YoY, %)



Source: Geostat, NBG, TBC Capital

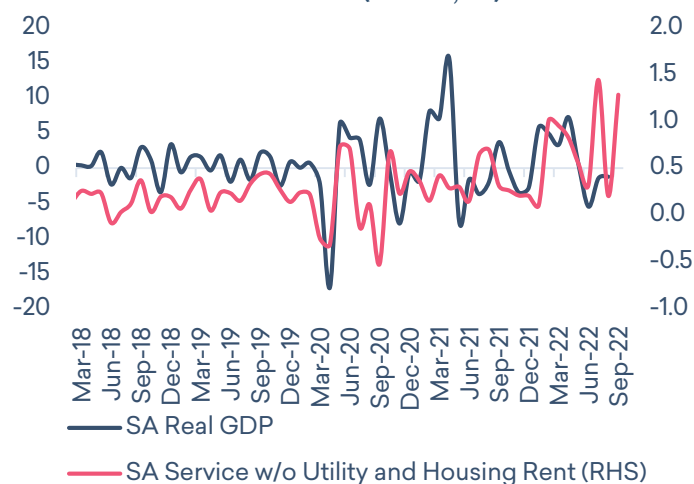
SELECTED COMMODITY PRICE INDICES (Jan-2021 = 100, As of 7-Oct-2022)



Source: CME, ICE, FAO

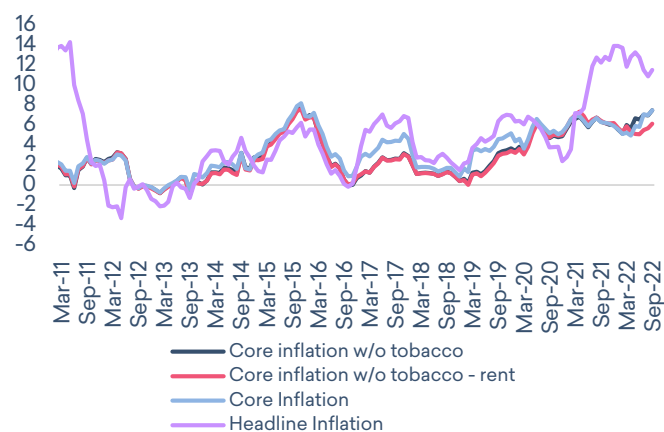
As for the inflationary pressures on the domestic demand side, [the assessment](#) is broadly unchanged mainly except for the housing rentals as after the announcement of the partial mobilization in Russia, another wave of migrants entered the country. Therefore, we stick to our view that an expected normalization in growth should bring elevating domestic inflation back on track. As in local production a large number of imported intermediate inputs are used, e.g. bread, probably the domestic services alone are a better indicator in this regard. In fact, when having a rather simple look, historically services look to be better aligned with the growth pattern the later in coming months to stay negative MoM seasonally adjusted the 2022 full year growth to reach [our bullish 10.6%](#), while in 2023 above trend GDP outlook is not our baseline. Furthermore, due to the global slowdown and high base effect, and assuming the migration inflows peak already this year, our recent estimates point to a 3.9% growth in 2023. In addition, trimmed measures of service inflation look only relatively, but still subdued.

SEASONALLY ADJUSTED SERVICE INFLATION W/O UTILITY AND HOUSING RENT AND REAL GDP (MoM, %)



Source: Geostat, NBG, TBC Capital

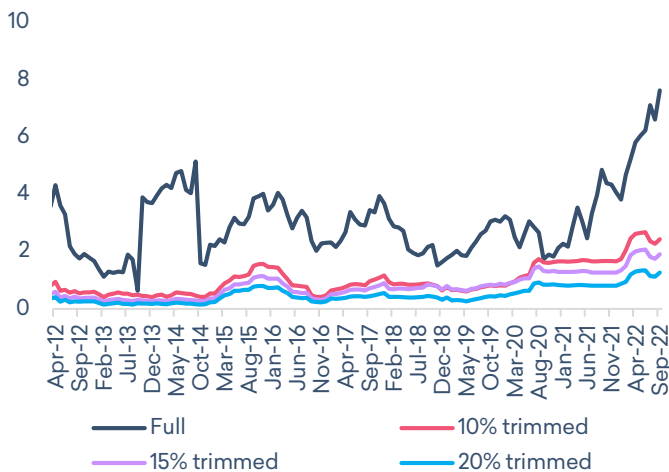
HEADLINE AND CORE INFLATION (YoY, %)



Note: Core inflation is calculated by excluding the following groups of goods and services from the consumer basket: food and non-alcoholic beverages, energy, regulated tariffs, transport (specific tariffs).

Source: Geostat, TBC Capital

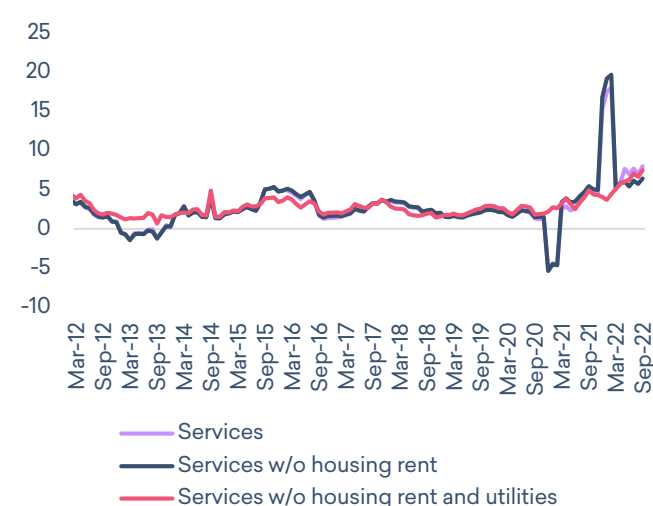
FULL AND TRIMMED SERVICE INFLATION W/O HOUSING RENT AND UTILITIES (YoY, %)



Note: Trimmed service CPI series excludes X% of the CPI components with the highest and lowest price changes from each tail of the price-change distribution

Source: Geostat, TBC Capital

SERVICE INFLATION (YoY, %)

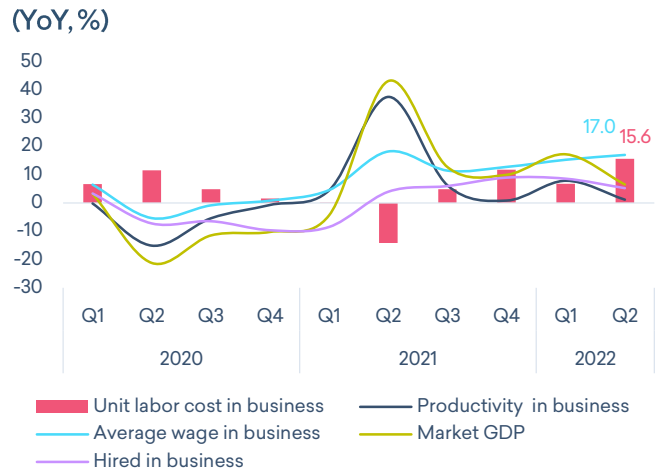


Source: Geostat, TBC Capital

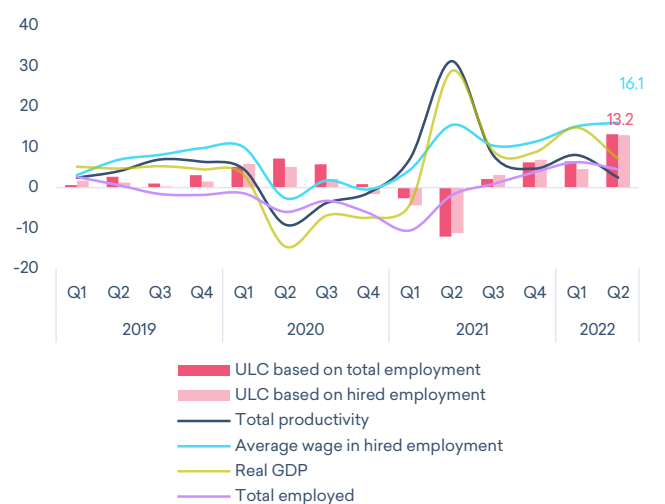
On the unit labor costs side, our [previous assessment](#) is unchanged as we still expect the wages to cool down as the demand and importantly inflation is back to the trend. Also, Geostat number of jobs estimates indicate to an ongoing recovery being not an argument for an inflation pressures. However, the latest emigration data is not available and the level of natural unemployment in Georgia is highly uncertain. On the other hand, besides stronger domestic demand on the back of the immigration, the later also results in higher labor supply domestically which is not yet included in the labor market data.

What does this imply for the GEL policy rate and an exchange rate? We postpone [the first rate cut](#) outlook from the end of this year to the beginning 2023. Here we note, that even if 2022 year end headline CPI inflation stands at 10.5%, instead of our new baseline of 9.4%, this implies October-December MoM seasonally adjusted annualized inflation to be on 3% target. However, for sure, domestic and various measures of core inflation are watched more closely by the NBG.

UNIT LABOR COST BASED ON MARKET GDP



UNIT LABOR COST BASED ON TOTAL GDP (YoY, %)

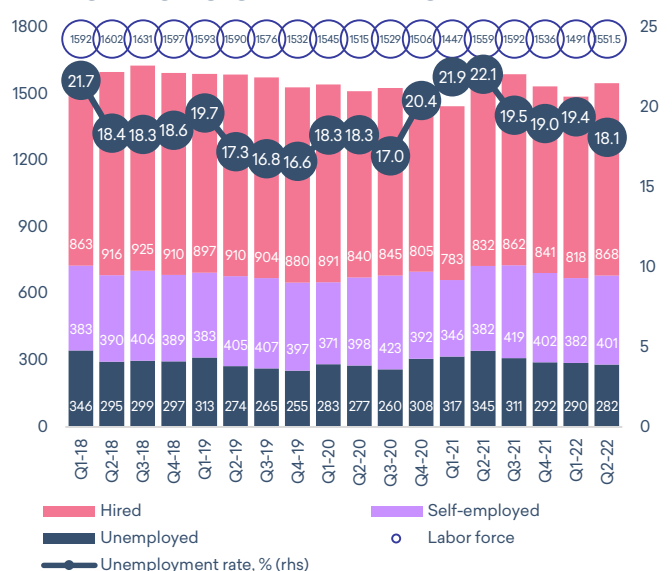


EMPLOYMENT, REAL GDP AND WAGE DYNAMICS

(%, compared to the same period of 2019)



INDICATORS OF THE LABOR MARKET

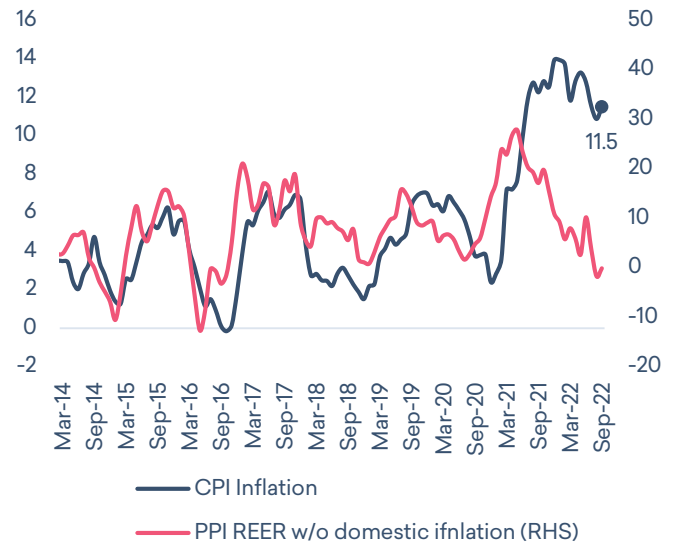


Note: Labor statistics do not include current migration dynamics
Source: Geostat, TBC Capital

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Source: Geostat

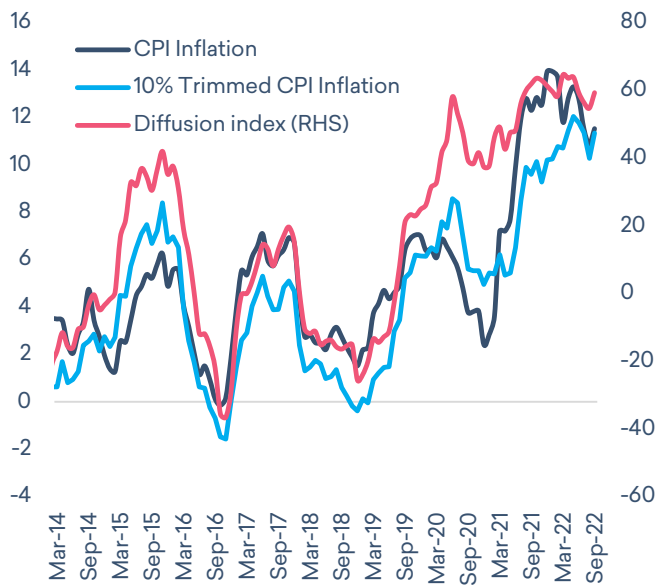
On the GEL exchange rate side, we continue to believe that the [excess FC liquidity in the banking system](#) has to show up at the FX market. Furthermore, the worsened inflation outlook is also certainly the GEL supportive, though, recent dollar strength has to be counted as well as postponed, but still cooling inflation outlook. Therefore, we stick to [our view](#) that unless the greenback weakens, unlikely in the coming months, higher NBG reserves look more reasonable rather than a materially stronger GEL.

INFLATION (YoY, %) AND PPI REER EXCLUDING DOMESTIC INFLATION (YoY, %, increase means GEL depreciation)



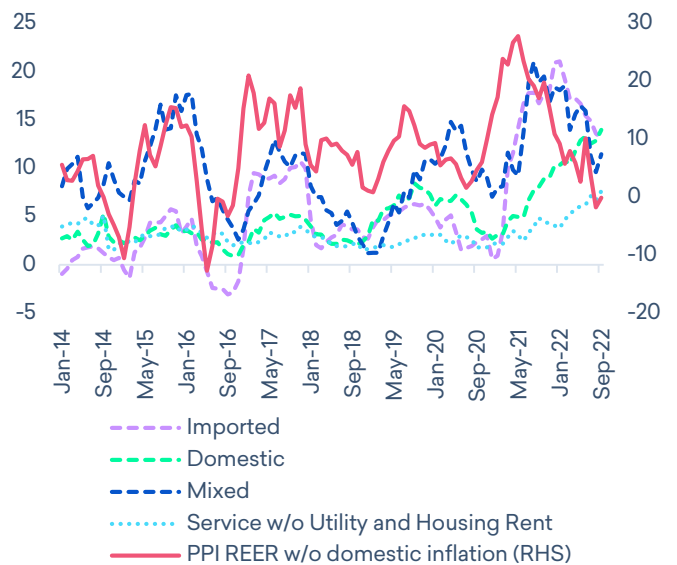
Source: Geostat, NBG, TBC Capital

DIFFUSION INDEX AND CPI INFLATION (YoY, %)



Source: Geostat

INFLATION (YoY, %) AND PPI REER EXCLUDING DOMESTIC INFLATION (YoY, %, increase means GEL depreciation)



Source: Geostat, NBG, TBC Capital

Data releases to watch this week:
October 10 – Central Bank Survey, Sep-22;
October 13 – External Trade Express Data, Sep-22.

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