

# DEVELOPMENT OF THE MAIN MACROECONOMIC INDICATORS AND THE FINAL CRISIS

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## Abstract

On the background of global financial crisis, the successful solution of economic and social problems Georgia is facing is linked to the qualitative changes in the macro-economic efficiency, which is based on the construction of a market economy in Georgia. The reality of monetary policy developed by the National Bank and practical value is determined by how well it takes into account the results of country development of the and future objectives, the macroeconomic environment in the region, the ongoing processes in the world market. Established tendencies in Financial and foreign exchange markets, pricing changes and the factors affecting them, the hazards and their prevention, opportunities for adaptation to the changing environment in this policy. The paper analyzes and evaluates basic macroeconomic indicators of Georgia and gives positive and negative results of economic policy.

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**Keywords:** Monetary policy, macroeconomic indicators, balance of payments, inflation targeting

## Introduction

On the background of global financial crisis, the successful solution of economic and social problems Georgia is facing, is linked to the qualitative changes in the macro-economic efficiency, which is based on the construction of a market economy in our country.

Table # 1 Basic Macroeconomic Indicators of Georgia 2005-2014

	Unit of Measurement	Years				
		2010	2011	2012	2013	2014
1.real sector Nominal GDP	Million Lari	20,74	24,34	26,16	26,84	29,18
		3.4	4.0	7.3	7.4	7.0
Industry production	Million Lari	5,855.3	7,458.7	8,019.2	8,493.4	9,193.6
Agricultural production	Million Lari	2,396.7	2,396.7	3,018.7	3,393.6	3,579.0
Real GDO growth rate	%	106,3	107,2	106,4	103,3	104,8
2.investments	Million USD	<b>814.5</b>	<b>1 117.2</b>	<b>911.6</b>	<b>941.9</b>	<b>1 758.4</b>
3. Foreign trade	Million USD	<b>6935</b>	<b>9225</b>	<b>10413</b>	<b>10921</b>	<b>11454</b>
Export	Million USD	<b>1677</b>	<b>2187</b>	<b>2376</b>	<b>2910</b>	<b>2861</b>
Import	Million USD	<b>5257</b>	<b>7038</b>	<b>8037</b>	<b>8012</b>	<b>8593</b>
4.State budget Income	Million Lari	5,421.5	6,388.8	7,058.2	6,808.1	7,377.2
Expanses(Costs)	Million Lari	5,466.5	5,926.9	6,641.5	6,514.5	7,447.7
Balance Surplus(+) Deficit(-)	Million Lari	-918.6	-293.9	-121.0	-393.8	-687.77
5. Inflation Consumer Price index	%	111.2	102.0	98.6	102.4	102.0
6.Unemployment level	%	16,3	15,1	15,0	14,6	12,4
7. Gross Foreign debt	Million US dollars	10,102.8	11,578.7	13,242.8	13,459.8	

Analysis of data Table #1 shows that over the past 9 year period, the economy was characterized by a certain inequality. The real GDP rate growth of 1005-2012 is significantly million reduced in 2013-2014 that is mainly explained on the one hand by the influence of negative external global economic factors, on the other hand, by election-related uncertainty expectation factors of entrepreneurs, especially investors. The situation is particularly significant in 2014, which is characterized by fluctuation of global economic, that negatively affected our country's economy. In 2014 geopolitical crisis (the Russian-Ukrainian conflict, and economic sanctions of EU and US against Russia), the global financial and economic crisis, the heavy legacy of the international markets of tradable goods (especially oil, metal and food) prices' decline and the growth of the US dollar exchange rate negatively impacted not only economically undeveloped, but on the figure of economic growth performance of developed countries. The IMF

estimates the 2014 global economic growth of 3.3%, which is almost no different from the figure of 2013.

Doubt raises about the global economy in the years 2015 and 2016, respectively 3,5 and 3,7% percent growth.<sup>1</sup> This year the growth of domestic product of Euro zone increased by 0.8%. The IMF predicts growth of 1.2% in 2015 to 1,4% in 2016, which is a very low figure.<sup>2</sup> Apart from Euro zone different picture is observed in the US, where in 2014 the GDP growth amounted to 2.4% and was more than expected.

The weakening of economic activity around the world to strengthen the dollar against foreign currencies in many countries, including Georgia was due to the weak inflation (see Table №1) particularly notable is the fall in prices of oil, metals, food products).

Geopolitical conflict between Ukraine and Russia and the related economic results negatively impact on the economy of Georgia and of many trading partners. International economic sanctions imposed on Russia and deterioration of trading conditions could not compensate the 85% devaluation of Russian ruble against the dollar which is reflected in higher inflation and reduced the real income.

This has a negative impact on exports from Georgia, its amount decreased in 2014. As the case shows it is real, that the negative trends will continue in 2015 as well, which will be reflected on the economy of Georgia, especially if the government and the private sector do not find alternative markets and do not provide the development of already existing ones. The conflict has negatively affected the situation in Ukraine (in 2014, its economy decreased by about 8%, and the local currency - the hryvnia has depreciated by 98% to the US dollar.). The economic situation of Armenia as an important trade partner of Georgia, has deteriorated (which is reflected in its close economic ties with Russia) There is a prediction that in 2015 the economy of Armenia will have a 0% increase. Difficulties are seen also in Azerbaijan, as well as an important economic partner of our economies, but to a lesser extent, due to the energy exports. Better perspectives are seen in case of our closest and the main economic partner Turkey economy growth amounted 2.9% in 2014 (the same growth is forecast for 2015), which is a good for our country trade turnover and other kinds of economic ties.

The indicator of the country import dependence is important while the country export does not exceed the quarter, such balance causes the shortage nature of the country payment balance, the outflow of foreign exchange resources; it also adversely affects the stability of our currency and the domestic consumer goods prices.

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<sup>1</sup> WEO update, Jan. 2015

<sup>2</sup> WEO update, Jan. 2015

The low rate of agricultural products, from real economic sector deserves attention which is perfectly not adequate to the country natural abilities and problem solving tasks in the food industry. Compared to 2005 under the conditions of industry growth by 2,9 times, the output of agricultural products increased by only 38\$.

As for the previous year 2014, the economic activity and development trends appears to be instable. In 2014 real growth of domestic products related to 2013 amounted 4.8%, but it is lower than the indicator of 2010-2012 years. During the year, the speed of economic growth was uneven. The first 3 quarters of the year was relatively of a high growth amounted 5.9%. In the fourth quarter GDP growth was reduced and amounted only 1.8% due to the decline of market orders compared to previous three quarters. The main reason for this are negative foreign factors. Reduced demand for the country export products had a negative impact on the processing industry, where a large part of the export products is produced (if during the first 3 quarters of the year average growth was apparent, in the fourth quarter there was 6.9% drop).<sup>3</sup>

Deteriorating economic conditions in the countries of trade partners adversely affected the other areas, in the fourth quarter reduced the number of visitors and the flow of foreign remittances, which had a negative impact on the 2014 economic growth indicators.

The main objectives of the National Bank is to insure price stability in the country and to maintain purchasing power of national currency. Georgia, in its short history of independence not once has suffered from severe inflationary consequences. It should be noted that until 1995 inflation had a less controlled nature, in the following period, in proportion to economic recovery, especially after the reform of money inflation processes subsequently got manageable character. The opportunity of this was largely due to the creation of financial and banking legislative framework, monetary policy of National Bank, taking fixed exchange rate of the national currency-Lari to a free-floating rate, inflation targeting regime since 2009, relatively effective enforcement of monetary policy instruments. It is also very important if government makes positive changes in social sector, in budget fiscal policy. However under the influence of various objective factors price fluctuations not only by years, but in whole, according to individual types of market products is often crucial. In Georgia many factors are the reasons of inflationary processes, including the low level of economic development and its unstable growth rate, the economy dependence on imports and significant lack of export growth, high level of economy dollarization, not eligible efficiency of budget fiscal policy and the other reasons as well.

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<sup>3</sup> www. Statistics. ge

Table2 The consumer price index ( inflation) 2010-2014 years <sup>4</sup>

#	Years				
	2010	2011	2012	2013	2014
The annual average to the previous average annual	107,1	108,1	99,1	99,5	103,1
December to the previous year December	111,2	102,0	98,6	102,4	102,0

Data analysis of the abovementioned table shows that in Georgia there have been significant fluctuations in the Consumer Price List. Besides there is some regularity in the abovementioned changes in the inflation rate. The inflation rate is higher in those years when there is the growth in economy activity, and in the years when it is reduced (2012, 2013, 2014).

We have approximately the same picture in case of investments made in the country as well. Foreign direct investment in 2011 amounted to 11172 million US\$, in 2012- 911,6 - million US\$, in 2013- 941.9 mln. US\$, 2014- 127.2 million US\$. Inflation change rate is adequate for this period (growth-reduction). In 2012-2014 among the reasons for economic growth and inflation squeeze was reduced markets and a decline in investment on the basis of Russian-Ukrainian conflict, some confusion caused by elections and expectation factor from entrepreneurs and investors side, oversea transfer decline, also, inefficient state regulation in tourism field. Some other low inflation rate, together with the affecting factors from delivery side, was supported by the negative factors as well. The evidence of it is the reduction of import growth rate. If in 2011 comparing to previous years the growth rate of imports amounted 28,8% in 2012-15.7% and in 2013 it was reduced up to 4,1% . Thus, 2012-2014, compared to the previous three years in Georgia, was characterized by deflation processes, which has a negative impact on the country economic activity. For this purpose, the actual inflation rate is significantly less than the inflation target of central bank for 2012-2014.

In 2014 because of internal and external factors, food prices grew slowly. In spite of the fact that in the end of the year exchange rate of Lari declined significantly, according to data for December, annual inflation of consumer food basket amounted 2.7%, while its impact on the overall index amounted 0.8 percentage points. The impact of fuel price dynamics on the changes of general price level was very important. Since the second half of 2014 began the decline in fuel prices in the local market. By the end of 2014, the annual reduction in fuel prices amounted 5-6 percent, and its contribution to overall price level was 0.3 percentage points.

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<sup>4</sup> www. statistics. ge

The price movement dynamic on imported goods, which has its significant share in the consumer basket, influences on low inflation.

The Ongoing Economic Processes are fully reflected in regularity changes of payment balance.

Table3

Title	2010	2011	2012	2013	2014
<b>Current account</b>	-1,193	-1,841	-1,855	-930	-1,611
Goods	-2,590	-3,494	-4,216	-3,493	-4,225
Export	2,462	3,254	3,502	4,246	4,073
Import	-5,052	-6,748	-7,718	-7,738	-8,299
Service	513	747	1,101	1,405	1,341
Credit	1,599	2,008	2,544	2,964	3,019
From here-Tourist income	659	955	1,411	1,720	1,787
Debit	-1,085	-1,261	-1,443	-1,559	-1,678
Incomes(net)	-215	-423	-147	-308	-158
Of which interest payments	-252	-311	-395	-377	-375
Transfer(net)	1,098	1,329	1,408	1,466	1,432
Of which public sector	174	144	118	91	54
Of which remittance credit	417	618	712	786	761
Of which other private transfers credit	534	583	587	600	636
<b>Capital Account</b>	206	153	134	134	115
<b>Financial Account</b>	1,019	1,672	1,744	824	1,546
Direct investments(net)	679	902	614	829	1,077
Of which direct investment in Georgia	814	1,048	911	949	1,279
Portfolio investments(net)	250	133	848	-37	210
Financial derivatives(net)	1	5	5	-2	8
Other investments(net)	297	1,205	314	-12	218
Of which public sector	336	278	398	490	355
Reserve assets	-208 -	572	-38	45	33
Net errors and omissions	-33	15	- 23	-28	-50

Source: [www.nbg.ge](http://www.nbg.ge) The National Bank Of Georgia, Annual report 2014, p. 9

The analysis of abovementioned chart shows that the current account of payment balance in the process of analysis is characterized by deficiency, and in whole, over the years there is no significant change, although because of influence of various factors we have a different picture. The picture is particularly noteworthy since 2013-2014. If in 2012 the current account deficit of GDP was 11.7% in 2013 it amounted 5.8% as it is seen it reduced by up to 5,9 percentage points. (Mainly at the expense of export, services, transfers, direct investment, net revenue growth). In 2014 the situation

reversed. The current account deficit amounted to 9.7% of GDP, which is higher in 4,0 percentage points than the figures of previous(2013) year. The current account deficit, in absolute figures, increased by \$ 681million and amounted to1,611 billion Dollars. In 2014, in the second half of the year external shocks contributed to the increase of deficit. Deficit deepening was mainly caused by the deterioration of the balance of goods trade. The assessment of deficit of trade in goods to GDP amounted to 25,6%, which is 3.9 percent higher than the figure of 2013. Already mentioned deterioration is mainly caused by the crisis in main trading partner countries. In 2014, exports of registered goods in these countries compared to last year decreased by 1.7%.

From some largest commodity groups, 26,4% the decrease of automobile exports is noteworthy. Reduced spirits (-4,7%), steel semi(-24,5%), gold(-46,3%), cattle(-36,8) and the export of trucks. The decrease in export of abovementioned commodity groups more or less was balanced by the increase in export of ferroalloys(+24,3%),cooper concentrates(+53,5), hazelnut(+ 10.0%), wine(+41,4%), mineral water(+28,3%), drugs(+76,8%),textiles(+76,2%)and electricity (+114,9%).<sup>5</sup>

As for the export geography, in 2014 export increased by 2.1% in the direction of EU and amounted to 620.8million US dollars. Export decreased by 9.6% in the CIS, which was mainly due to decrease in exports ; Azerbaijan(-23,3%), Ukraine(-27,3%), Armenia(-8,7%) and Moldova (-67,5%). At the same time, exports increased to Russia by 44,5%. In other countries, exports grew by 13.9%, mainly in Turkey it reached (+30,9), USA(+52,1) and China(+166,9%) at the expense of gross export.<sup>6</sup>

Despite the decline in export markets, Azerbaijan and Armenia still remain as the largest export markets for Georgia. Among the top three export markets there appeared Russia in 2014, which replaced Ukraine.

In 2014 increase of import in registered goods mainly was due to the annual growth of consumer(13,1%) and intermediate type of goods (+9,1%). 2% increase in import of investment goods was also apparent, although its contribution to the overall growth of import is small.

National Bank is responsible for the monetary policy in Georgia. According to main monetary and foreign exchange policy approved by Parliament, which is the key document for the National Bank activities, inflation rate for 2014 is determined to be 6 percent of level, by 2015-2016-5 percent of level and by 2017 it would be reduced to 4 percent for long-term period. The reality of monetary policy and practical value, developed by the National Bank, is determined by how it takes into account the results and

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<sup>5</sup> www. Ststatistics.ge

<sup>6</sup> www. Ststatistics.ge

future objectives of county development, macroeconomic environment in the world and in region, the ongoing processes in the world markets. Established trends in financial and foreign exchange markets, pricing changes and the factors affecting them, hazards and their prevention, opportunities for adaptation to the changing environment in this policy.

Since 2008, the activities of National Bank is highly appreciated from the side of international financial and monetary organizations as well as from rating organizations. It is considered to be a model for other countries. However, this doesn't mean that his work was not the flows of errors.(Inadequate attitude in some bank's activity, the delayed effects towards the exchange rate fluctuations in 2014and etc.) In 2012-2014, the country recorded inflation below at its target level. From the second half of 2012 from the side of supply, reduction of aggregate demand was added to the negative impact of prices, although from the second half of 2013 to the end of 2014 economic growth indicator a little, but still increased. This allowed National Bank start gradually exit from accommodative monetary policy, which is confirmed by the increase of monetary policy rate up to 4% (0.25percentage points). But these trends cannot be sustained. In 2014 inflation gradually strengthened. Negative factors in trading partner economies, decrease in prices on imported goods and oil, tourism flow decline and other unfavorable economic trends reflected the economy of Georgia; weakened foreign demand, together with export decrease, the decline in fixed remittances inflow was apparent. Despite the depreciation of the dollar against the gel, its nominal effective exchange rate hasn't decreased as the trading partner countries' currencies have experienced a higher devaluation. This stopped the growth of imported inflation. Under such circumstances, it was impossible to make inflation rate closer to the target level of 5 %. The rate did not changed it remained in the 4%. By the end of the year it became more distant. Consumer prices grew by 2%. As in previous years, the low level of economic Larization still remained the main obstacle in increasing the efficiency on monetary policy. Under the conditions of high dollarization the impact of interest rate transmission mechanism is weakened, because the exchange rate changes are much more transmitted to inflation which prevents exchange rate flexibility, causes currency exchange rate fluctuation which in its side causes price changes, particularly in the consumer basket components. In low Larization process increase the risk of exchange rate fluctuation for disadvantaged economic operators, especially for borrowers of commercial banks who receive the income in the currency-Lari and loans are taken in foreign currency. Classical example f all these is our country, where strengthening the dollars against the Lari in 2015 (and thereafter) make people detrimental who had loans denominated in dollars. Therefore, the development of Lari market is

of a paramount importance of monetary-exchange policy of the National Bank. Compared to 2014 the rate of Gel in case of deposits improved by 1,7% and amounted to 39,8%, in case of loans it increased by 3,3% and amounted to 39,2%.<sup>7</sup>

Analysis shows that in recent years the volume of trade in the securities market significantly increased. In 2014 compared with 2010 circulation of Treasury securities balance increased 3 times and in previous years the growth amounted to 80%. As the growth for secondary market, it was contributed by the growth of repo operations with securities. If in 2013 only 4 repo deals was signed, in 2014 their number reached 86.<sup>8</sup>

As the result of monetary policy pursued by the National Bank, in recent years activity of commercial banks in the money market has increased. In 2014, the volume of transactions in the national currency increased by 39% from the previous year and amounted to 18.9 billion GEL. In order to get the monetary policy rate the national bank developed operational framework, which consists of monetary instruments such as refinancing loans, overnight loans, overnight deposits, certificates of deposit and minimum reserve requirements. Effective use of these instruments significantly provided stability and liquidity of the banking sector, protection from the risks and shocks which took place in the international market.

In the period of analysis the development of monetary market was supported with Treasury bills and Treasury bonds by the Ministry of Finance which is the form of funds mobilization for the needs of the State. Their portfolio amounted to 1.3 billion GEL by the end of 2014, which is 4.5% of GDP. They may be purchased by physical as well as by legal entities. As for government bonds, by December 2014 the National Bank owned 80 million Lari, and commercial banks 53 million government bonds. Unfortunately, in 2014 compared to 2013 in the secondhand market of Treasury bills. If in 2013 there were concluded 22 treasury transaction deals with the amount of 56 million, therefore in 2014 there were 8 treasury transaction deals which amounted to 35,4 million Gel. Treasury bonds was concluded 67 deals in 2013 with amount of 248.9 million GEL, while in 2014, respectively, the amount of deals reached to 10 with 21.5 million GEL.<sup>9</sup> Certificates of deposits of the National bank are in great demand in securities market, which are circulated for 3 and 6-month maturity segment. IN 2014 there were 505 million GEL deposit certificate in the circulation. In 2014 in the second hand market of CDs 5 deals with 66.5 million Gel of total amount was signed.

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<sup>7</sup> www.nbgov.ge, annual report of the National Bank of Georgia, 2014 p. 42

<sup>8</sup> www.nbg.ge The National Bank Of Georgia ,Annual report 2014, p. 42

<sup>9</sup> www.nbg.ge The National Bank Of Georgia ,Annual report 2014, p. 50

To measure the value of the securities market, we can see that it is one of the weakest developed segment of Georgian economy and therefore cannot effectively perform the functions of economic regulation and growth. US

The main objective of the National Bank monetary policy is to ensure the stability of the national currency and to increase effectiveness of the regulation of its exchange rate mechanism. In Georgia we have a floating exchange rate regime of the national currency, which is considered the optimal exchange rate regime. The character of the regime is exchange rate fluctuations (often important) in the short-term, but due to its inherent flexibility, it maintains stability in the long-term and is adequate to economic conjuncture changes. Table 4 highlights the changing nature of Lari rate in 2008-2014.

Table 4 Lari exchange rates (period, average) <sup>10</sup>

	2008	2009	2010	2011	2012	2013	2014	2015
US Dollars/Lari	1,4902	1,6705	1,7829	1,6860	1,6513	1,6634	1,7494	
Euro/Lari	2,1886	2,3307	2,3644	2,3473	2,1232	2,2094	2,3969	

## Conclusion

The National Bank has no target index of exchange rate, in such circumstances the course is determined by the demand and the supply of the currency in the foreign exchange market, which is affected by both the fundamental economic factors as well as by a temporary, short-term fluctuations. In such circumstances, in order to prevent significant changes in the exchange rate The National Bank uses the instruments of monetary policy, including foreign exchange intervention. In 2008-2014 the instrument of the National Bank intervention was foreign exchange auction mechanism. In January 2013 in order to extinguish the inflation expectations, the National bank sold 220 million dollars, but then in February and August he carried out interventions in reverse-procurements, which served to increase foreign exchange reserves. In 2014 the National Bank carried out foreign exchange intervention 18 times, which increased the circulation of Lari mass. In 2014 exchange rate of Lari to dollars is decreasing and these trends significantly strengthened in the first quarter of 2015. Throughout 2014 in the world foreign exchange market the strengthening of dollar is observed, which was caused by the 2013 Federal Reserve System decision about gradual completion of quantitative easing policy introduced in 2008; as a result the dollar began to strengthen against foreign currencies, which affected our country, its economic and the currencies of our trade partner.

<sup>10</sup> www. Ststatistics.ge

This process reflected GEL exchange rate relatively late and The National Bank has several reasons for it:

1. A large amount of foreign direct investment inflow during the first three quarters of 2014, especially in the third quarter;

2. Seasonal increase of foreign currency inflow, concerning the summer tourist season;

3. As far as the dollar touched a stick in the first place those countries where the financial market is relatively developed, later as a result of devaluation of partner countries' currencies the balance of payment of current account fell to convey. As a result, the restraining factors of the Lari nominal exchange rate depreciation has been weakened.

As for the end of 2014 the specific reasons of Lari depreciation are of several types, including primary: the global strengthening of the dollar exchange rate to other currencies, including Georgian currency and the currencies of its trading- partner countries; reduction of exports and tourist flow; A significant increase in the realization of social programs; Increase of salaries, bonuses and other benefits in State structure; visa restrictions and complicated regulations towards some of the partner countries; Inequalities in the state budget fulfillment for the last month of the year; the reduction of Investment growth; GEL mass growth in calculation; Decline of money transfers from abroad; Reduction of investment growth rate; An increase of inflation expectations; The delay(the prevention) of adequate response on Lari depreciation by the National Bank.<sup>11</sup>

Depreciation doesn't occur at once, the symptoms were evident in 2013 which is confirmed also by interventions of the National Bank, when in January it sold 220 million US dollars.<sup>12</sup> Refinancing loans which were given in December to commercial banks to fill liquidity negatively impacted on the growth of Lari mass in circulation. In 2014 the National bank carried out intervention only two times which was not enough. For this action the National Bank has the following arguments: During floating exchange regime due to the shocks the depreciation of exchange rate is natural reaction. In this process currency intervention carried out by the National Bank is counterproductive, as on the one hand it prevents to correct foreign misbalance existed in economic, and on the other hand, it supports appearing speculative expectation. Accordingly, the foreign currency policy of the National Bank was leading policy of less interference, so that to correct foreign misbalance quickly. In abovementioned period the National Bank carried out only two interventions in foreign exchange market, which mainly was a signal for the market that mentioned rate misbalance tremors wasn't

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<sup>11</sup> www.nbg.ge The National Bank Of Georgia ,Annual report 2014, p. 55

<sup>12</sup> www.nbg.ge The National Bank Of Georgia ,Annual report 2014, p. 54

the result of out of control process.<sup>13</sup> Unfortunately the reality was controversial. Lari rate falling kept going on during the fourth month of 2015 and only after that it became stable on its high benchmark. As for the reserves of international currency by the end of December 2014 it amounted 2,7 billion US dollars, which is less by 4,4% to the same indicator of 2013. During 2014 with the help of currency auctions the National bank net sales amounted to 100 million US dollars. In the same year our country got 188,4 million US dollars as the loan in total and grants from donor organizations to finance various programs. (EU-18,8 million dollar; The World Bank- 91,1 million dollars; Asia Development Bank- 73,5 million dollars; the other- 40 million dollars), projects and loans for projects amounted- 238,4 million US dollars (the World Bank – 54,4 million dollars, Europe investment Bank- 75,5 million dollars; Japan-47,8 million dollars, Asia Development Bank- 17,8 million dollars , the other-42,9 million dollars). The past year was marked by coverage of important debts of the national Bank and the government which amounted to 429.4 USD.<sup>14</sup>

The trends in the economy of the country in 2013-2014, and the process of foreign debt service caused abovementioned reduction of the international reserves.

Consumer confidence index as business confidence index provide qualitative information useful for monitoring the current economic situation and advance warning of turning points in economic activity. Consumer confidence is the degree of optimism that consumers feel about the overall state of the economy and their personal financial situation. How confident people feel about stability of their incomes determines their spending activity and therefore serves as one of the key indicators for the overall shape of the economy. In essence, if consumer confidence is higher, consumers are making more purchases, boosting the economic expansion. On the other hand, if confidence is lower, consumers tend to save more than they spend, prompting the contraction of the economy.

The U.S. consumer confidence index (CCI) is an indicator designed to measure consumer confidence, which is defined as the degree of optimism on the state of the economy that consumers are expressing through their activities of savings and spending. Global consumer confidence is not measured. Country by country analysis indicates huge variance around the globe. In an interconnected global economy, tracking international consumer confidence is a lead indicator of economic trends. In the United States consumer confidence is issued monthly by The Conference Board, an independent economic research organization, and is based on 5,000

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<sup>13</sup> www.nbg.ge www.nbg.ge The National Bank Of Georgia ,Annual report 2014, p. 56

<sup>14</sup> www.nbg.ge The National Bank Of Georgia, Annual report 2014, p. 57

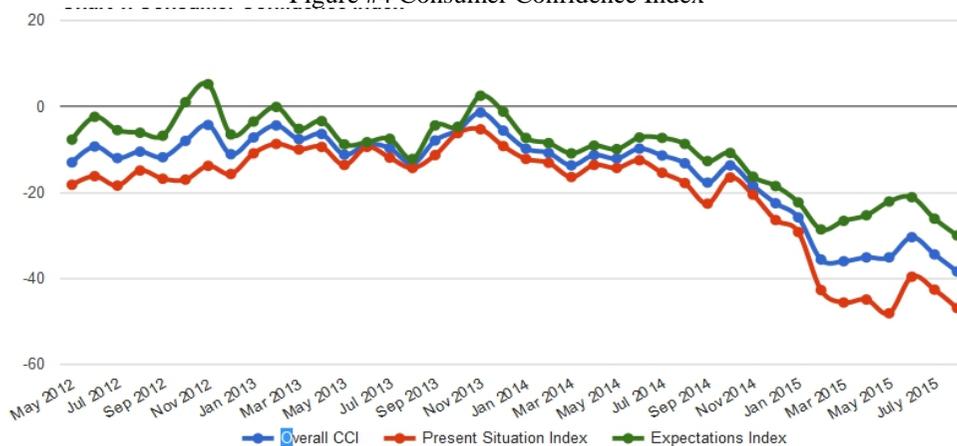
households. Such measurement is indicative of consumption component level of the gross domestic product. The Federal Reserve looks at the CCI when determining interest rate changes, and it also affects stock market prices.

The consumer confidence index was started in 1967 and is benchmarked to 1985=100. This year was chosen because it was neither a peak nor a trough. The Index is calculated each month on the basis of a household survey of consumers' opinions on current conditions and future expectations of the economy. Opinions on current conditions make up 40% of the index, with expectations of future conditions comprising the remaining 60%.

OECD also calculate The Index each month on the basis of a household survey of consumers' opinions on current conditions and future expectations of the economy. OECD data is regularly published for OECD countries, index is estimate for OECD overall. There are Consumer Confidence Index as well as Business Confidence Index.

Consumer Confidence Index for Georgia is calculated since 2012. Consumer Confidence Survey by ISET follows the standard EU methodology - There are randomly sample 300-350 individuals on a monthly basis and question them about the past, current and future financial situation of their families and the country as a whole. The chart below shows that after several months of incremental improvements, Consumer Confidence Index dropped 4.1 points in August 2015, to reach a new historical minimum of -38.4 points. Data are available through the ISET survey.

Figure #4 Consumer Confidence Index



The survey measures how optimistic or pessimistic consumers are with respect to the economy in the near future, consequently we see consumers' pessimism. **The results of survey reflect people's**

**dissatisfaction with the GEL continuing to lose in value against the US dollar.** It also means that consumers are mainly concerned about future prices, a worsening in unemployment and the general economic situation.

Another well-established index that measures consumer confidence is the University of Michigan Consumer Sentiment Index, run by University of Michigan's Institute for Social Research.

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