The World Bank Group - Georgia Partnership Program Snapshot

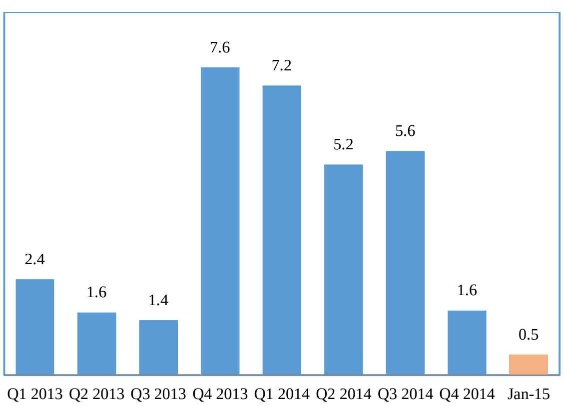
April 2015

RECENT ECONOMIC AND SECTORAL DEVELOPMENTS

Growth and External Performance

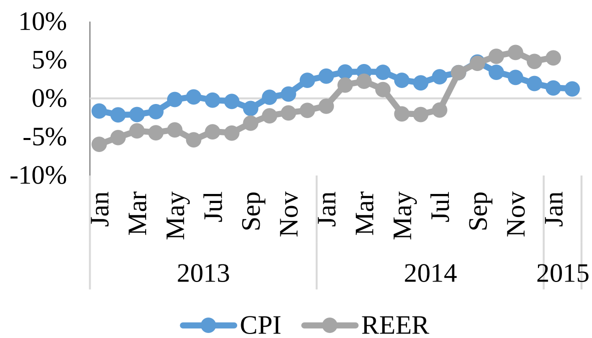
GDP growth was 4.8 percent in 2014, representing a recovery after the slowdown in 2013, though the effects of the Russia crisis started to hit the economy in the fourth quarter of the year. Growth in 2014 was largely due to recovering private investment and domestic demand. A brisk expansion in construction, which grew by 16.3 percent, spurred overall investment to increase to 28.5 percent of GDP at the end of the third quarter in 2014, the highest since the 2008 crisis. However, the spillover effects from the slowdown in Russia in the last quarter of 2014 led to a significant drop in exports, remittances, and tourism. As a result, despite the beneficial impact of the decline in oil prices, the current account deficit is estimated to have widened to 9.7 percent of GDP in 2014 with net foreign direct investment (FDI) at 6.6 percent of GDP.

Figure 1. Quarterly GDP Growth (percent)



There are significant downside risks to growth in 2015 stemming from the external environment. Growth is now projected at 2 percent, mainly because of deteriorating export prospects and slowing investment. Exports in January 2015 were close to the levels in January 2012, a fall of 30 percent year-on-year (y-o-y). As the external accounts worsened and in response to the depreciating currencies of Georgia's trading partners, the Georgia lari (GEL) depreciated by 26.7 percent against the U.S. dollar between November 2014 and March 2015. In real terms, however, as of end-January 2015, the lari had appreciated by 51 percent y-o-y against the ruble and by 8 percent y-o-y against the euro, while depreciating by 8 percent y-o-y against the U.S. dollar. The overall real effective exchange rate (REER) appreciated by 5.3 percent y-o-y. Inflation has remained low, at 1.3 percent y-o-y as of end-February 2015 (well below the inflation target of 5 percent), largely because of the decline in oil prices and the appreciation of the REER. The National Bank of Georgia (NBG) has retained its commitment to a flexible exchange rate regime.

Figure 2. Inflation and Real Exchange Rate (y-o-y %)



Source: Geostat, NBG, and staff calculations.

Fiscal Developments

The Government is likely to submit an amendment to the 2015 budget. The planned 2015 budget, passed by Parliament in December 2014, was based on a growth projection of 5 percent. General government revenues in 2014 exceeded the previous year's collections by 8.3 percent. Indirect taxes increased by 14.9 percent (import-led value added tax [VAT] increased by 16 percent) and direct taxes grew by 1.3 percent. Further improvements in revenue collections were envisaged for 2015 through improved tax administration; however, this is unlikely now because of shrinking aggregate demand and falling growth.

Georgia's public debt remains sustainable. Total public sector debt increased from 32.2 percent of GDP in 2013 to 33.3 percent in 2014. About 80 percent of public debt in 2014 was external and dominated by long-term multilateral (70 percent) and bilateral (20 percent) debt. Given the highly concessional nature of public debt, interest payments average at around 1 percent of GDP a year. Nearly 75 percent of external public debt is at fixed interest rates, thereby reducing interest rate risk. During 2014, the Government issued securities of GEL 898.5 million in order to finance the fiscal deficit, increasing domestic public debt by GEL 554 million (2 percent of GDP) to 6.5 percent. Domestic financing of the deficit, which eases exchange market pressures, will continue in 2015.

Medium-Term Outlook

Economic growth is projected to average 3.6 percent a year over the medium term, but downside risks to growth remain. GDP growth is expected to increase to 3.0 percent in 2016. The Deep and Comprehensive Free Trade Area (DCFTA) and the Association Agreement with the European Union (EU) are likely to improve market access, exports, and FDI in the medium term. However, in the short term, this will involve costs, as producers upgrade their facilities to meet required quality standards. Georgia receives little FDI from Russia or Ukraine and energy imports are mainly from Azerbaijan, but spillover effects are likely from geopolitical uncertainties and potential longer-term stagnation in the EU.

The authorities are committed to prudent fiscal management over the medium term, anchored in an International Monetary Fund (IMF) program that remains on track. During 2015, some increase in revenues is likely from the tobacco excise tax and the introduction of an excise tax on international calls. There will be a modest increase in expenditures on health (drug coverage under universal health care) and education (increased teacher salaries), while other current expenditures will be held constant. Various measures are under consideration to improve fiscal outcomes over the medium term. These include increased expenditure efficiencies in social benefits, reforms in public investment management, and limits on other nonessential expenditures. The large infrastructure deficit necessitates large capital spending in Georgia, which is expected to be 5–6 percent of GDP. The Government has an efficient tax administration and cannot easily increase tax rates; hence, fiscal consolidation will come from the expenditure side.

Lower domestic demand, the decline in investment, and the lari depreciation's impact on imports are likely to reduce the current account deficit in 2015. In addition, lower oil prices will also reduce the import bill. Georgia's exports are expected to remain subdued in 2015 because of lower demand from its key trading partners. In addition, there are downside risks to tourism receipts (the main tourist arrivals are from Turkey, Armenia, Azerbaijan, and Russia) and remittances, nearly 35 percent of which originated in Russia in January 2015 (compared to 50 percent in 2014). In 2016, some deterioration of the current account is likely, with a pickup in investment-related imports and domestic demand but a limited increase in exports. From 2017 onward, external sustainability will be supported by a recovery in export markets and some gains from the continued focus on competitiveness.

Public Financial Management (PFM)

Georgia has significantly advanced in public sector management practices. The success stories of public financial reforms, such as strengthened cash management, comprehensive control systems that avoid the accumulation of arrears, a transparent public procurement system, improved systems of external audit and oversight, and a strong e-governance focus—all are examples of how consolidated government efforts can achieve tangible results. At the same time, for macroeconomic stability, centralized decision making has been instrumental in enforcing fiscal rules and budget discipline. These topics, with reliable fiscal reporting, comprise the basics for initiating a second generation of financial and fiscal reforms.

The Ministry of Finance is in the process of increasing its capacity to monitor the cash management of local self-governments, legal entities of public law (LEPLs), and nonprofit legal entities (NPLEs). This will be undertaken through integrating them into the Public Financial Management Information System (PFMIS), which will help to monitor and manage their cash balances throughout the budget cycle. It will also help promote better management of intergovernmental transfers.

Strong financial and fiscal management systems are especially important due to the increased fiscal risks from state-owned enterprises (SOEs) and emerging social and pension obligations. The lack of adequate central monitoring systems for SOEs and of reporting standards and a framework for non-budget operations is a bottleneck to fiscal transparency and accountability. The Government has identified this issue as one of the critical challenges in the PFM framework and has been addressing them with World Bank support through the Inclusive Growth Development Policy Operation (DPO) series and the Programmatic PFM and Governance Task.

The coverage and quality of the internal audit function have been improved. Twenty-nine internal audit units in 12 ministries accounting for 54 percent of total state budget expenditures have been established. The Internal Audit Methodology, standards, and code of ethics are in line with international standards.

The Bank's ongoing support to the public administration sector in Georgia includes a series of DPOs and a Programmatic PFM and Governance Task that covers the FY15–17 period, and a Strengthening Accountability and the Fiduciary Environment (SAFE) grant–funded project on IT Audit Development in the State Audit Office of Georgia.

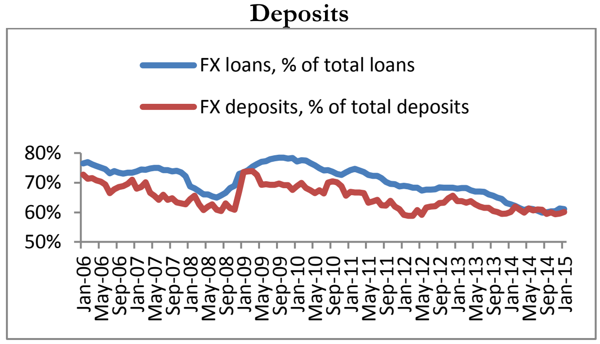
Financial Sector Performance

The banking sector continued to grow rapidly in 2014. As of July 2014, banking sector assets had grown by 19 percent (versus 26 percent asset growth in 2013), reaching 73 percent of GDP compared to 64 percent of GDP in 2013 (y-o-y) and 70.5 percent of GDP compared to 66.1 percent of GDP at the end of that year. Total loans (excluding interbank loans) increased by 18 percent and reached 44 percent of GDP compared to 37 percent of GDP at end-2013. Total deposits grew by 21 percent and reached 44 percent of GDP compared to 38 percent of GDP a year before.

The financial sector remains sound and well capitalized. However, banking sector performance needs to be carefully monitored in light of the potential growth of nonperforming loans (NPLs) and subsequent capital erosion due to foreign exchange and growing credit risks. The aggregate banking sector capital adequacy ratio (CAR) increased to 17.4 percent from 17.2 percent at the end of 2013, well above the minimum regulatory requirement of 12 percent. Return on equity (ROE) and return on assets (ROA) surged to 14.8 percent and 2.6 percent, respectively. NPLs as calculated based on NBG methodology slightly increased from 7.5 percent in 2013 to 7.6 in 2014. Export growth reduction and lower domestic demand might exert pressures on local firms' growth and debt service capacity. In addition, a nearly 50 percent reduction in the flow of remittances from Ukraine and Russia in December 2014 may also jeopardize the capacity of households in credit repayment.

Currency depreciation raises concerns about potential credit and refinancing risks for the highly dollarized credit portfolio. Despite the increased share of GEL lending, 61 percent of the loan portfolio remains denominated in foreign currency (figure 3), while the vast majority of borrowers do not have foreign currency revenues, especially nonexporting micro, small, and medium-sized enterprises (MSMEs) and households. This exposes banks to significant currency-induced credit risk, as evidenced by the recent decision of some larger banks to restructure/extend maturities for their foreign exchange–denominated loans to smooth the higher debt costs for borrowers. To foster local currency lending, the NBG increased the volume of long-term GEL refinancing in 2013–14. The program of NBG mortgage lending support resulted in a reduction in the household foreign exchange–denominated loans from their peak of 71 percent in 2009 to 43 percent in 2014. Still, 78 percent of corporate loans remain foreign currency denominated.

Figure 3. Share of Foreign Currency Loans and Deposits



Source: NBG.

The banking sector has sufficient liquidity, supported by the growth of client deposits and access to international lending markets. During the period of July 2013–July 2014, client deposits on the books of banks grew by 22 percent, reaching 42 percent of GDP in July 2014 compared to 39 percent at end-2013. Liquid assets to total assets slightly decreased to 24.7 percent in July 2014 (from 27.5 percent at end-2013) due to lending growth.

The Georgian financial system remains heavily bank dominated, with a negligent non-bank financial services market and a dormant private securities market. Twenty-one private commercial banks, including two branches of foreign banks, hold more than 90 percent of total financial sector assets. Growth of the non-bank financial sector is constrained by the lack of funds in the absence of deposits and capital markets and by the limited access to international lending due to the sector's small size.

The Financial Sector Advisory Program (FSAP) 2014 Update Report suggested that Georgia's sustainable growth outlook strongly depends on increasing national savings and investments and enhancing the competitiveness of exports. Thus, the financial sector needs to play a much more proactive role both in savings mobilization and financial intermediation to cater to the needs of the real economy.

The World Bank group supports improving the liquidity and capital of the banking sector and enhancing access to finance for SMEs. The Bank program includes analytical and advisory works, completing a comprehensive survey of 500 SMEs to assess their financial demands and identify constraints in access to finance.

To respond to the crisis and provide counter-cyclical support, during fiscal years 2009-2014, International Finance Corporation (IFC) provided about $280 million in long-term finance, including debt and equity investments, to Georgia's financial sector. In addition, IFC worked with three leading banks to provide trade finance guarantees for export-import operations. IFC has adjusted its product mix to better respond to the needs of the economy by offering trade financing and swaps (for interest rate and foreign currency risks) to its clients. In 2014, the IFC Capitalization Fund, a fund managed by the IFC Asset Management Company, invested US$65 million in the Bank of Georgia, the country's largest bank, to help the bank increase domestic access to finance and foster sustained economic growth. IFC has also provided advisory services to the financial sector to strengthen its risk management capacity and thereby reduce the country's vulnerability to future economic downturns.

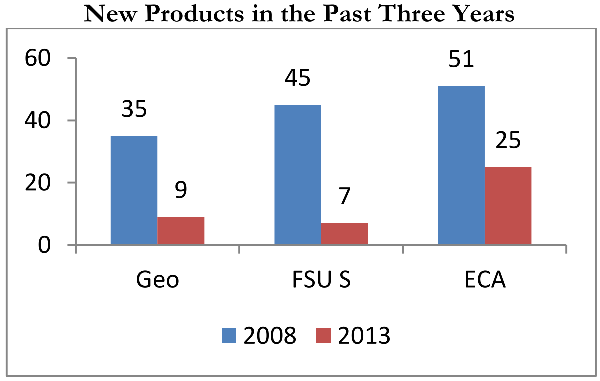
IFC supported microfinance lending by providing a US$4 million loan to FINCA Georgia, a leading microfinance institution in the country, to increase lending to micro and small businesses, thus creating jobs, boosting the economy, and reducing poverty, especially in rural areas.

Private Sector Development

Georgia has undergone extensive public sector and business environment reforms over the past several years, as recognized by its *Doing Business* rankings, especially in such areas as business entry, deregulation and construction permits, and tax and customs reforms. This has attracted a large influx of FDI, spurred robust tourism growth, and facilitated new business entry.

However, the favorable business environment has so far had only a moderate impact on the country's competitiveness. FDI has largely been concentrated in non-tradables and tourism and has been associated with a high propensity to import. Although Georgia significantly increased export diversification during 2000–10, adding more than 200 new products to its export bundle, the export basket remains fairly unsophisticated, with low value added and high labor intensiveness. Moreover, according to the 2013 World Bank Enterprise Survey, only 9 percent of surveyed entrepreneurs indicated that their firm had introduced new or substantially improved products or services in the previous years. More than 90 percent of surveyed firms had had no research and development (R&D) expenditures in the previous five years and did not envision spending on R&D in the next two years.

Figure 4. Percentage of Firms that have Developed New Products in the Past Three Years



Source: World Bank Enterprise Survey.

While globally the SME sector is the main source of private sector growth, innovation, and jobs, in Georgia it remains small and underdeveloped. Although SMEs account for nearly 94 percent of registered firms in Georgia and 38 percent of formal employment, they bring less than 20 percent of gross value added and account for less than 18 percent of turnover. The growth of SMEs is constrained by the poor skills match, low technological preparedness, restricted access to infrastructure, and underdeveloped value chains and local suppliers markets. The productivity of Georgian firms, especially SMEs, remains inadequate, particularly in agriculture, due to poor technological preparedness and low business sophistication and innovation.

Still, access to finance is named as the largest constraint to firms' growth. The share of SME lending in Georgia is only 8 percent of GDP compared to 16 percent for the middle-income countries and 21 percent for the Europe and Central Asia (ECA) region on average. Loans to SMEs represent only 20 percent of banks' private sector loan portfolio.

A new series of private sector development DPOs is included in the World Bank's current Country Partnership Strategy (CPS), which is aimed at supporting efforts to spur inclusive economic growth through second generation business environment reforms, financial sector deepening and diversification, and initiatives to increase firms' capacity to innovate and export, thus fostering private sector growth, access to finance, and export competitiveness. IFC continues its support to the private sector through direct equity investments and lending, a trade facilitation program, and the South Caucasus Growth Fund (created jointly with the European Bank for Reconstruction and Development [EBRD] and other donors and managed by the Small Enterprise Assistance Fund [SEAF]).

Poverty and Shared Prosperity

Poverty rates have considerably decreased since the peak observed in 2010. The poverty rate at US$2.5 per day (purchasing power parity corrected) fell from a peak of 47 percent in 2010 to 36 percent in 2013. The poverty rate at US$5 per day followed the same trend, falling from 81 to 73 percent in the same period. Using a poverty line developed for national analysis (GEL 70.8 per adult equivalent per month in 2007 prices), a notable reduction is also visible, with poverty falling from 18 to 14.8 percent between 2010 and 2012. Extreme poverty rates based on the national food poverty line have also decreased considerably in the same period, falling from 6.7 percent in 2010 to 3.7 in 2012.

In spite of the considerable poverty reduction observed in recent years, rural areas still lag behind and register poverty rates almost twice as large as urban areas. Using the US$2.5 per day line (2013), poverty was estimated to affect almost one in every two rural households. In urban areas, in contrast, poverty was considerably lower, affecting one out of every four households. Poverty estimations based on the national poverty line show a similar result (2012), with poverty rates of almost 20 percent in rural areas but close to 10 percent in urban centers.

Compared to other members of the Commonwealth of Independent States (CIS), Georgia is still among the countries with the highest poverty rates. Under ECA poverty lines of US$2.5 and US$5 per day, Georgia's poverty rates are close to Armenia and the Kyrgyz Republic, emerging as one of the poorest countries in the region.

Social assistance has played an important role in poverty reduction in recent years. Social spending has recently increased and has been an important driver in lifting households out of poverty. Pension benefits were raised for pensioners above 67 from GEL 70 in 2009 to GEL 100 in 2011, GEL 125 in September 2012, and GEL 150 in September 2013. Coverage and benefits have also increased for the targeted programs, both the targeted social assistance (TSA) and the Medical Insurance Program (MIP). In the case of TSA, the household benefit doubled in 2013. Also in 2013, the Government introduced the Universal Health Coverage (UHC) program, oriented to provide coverage for the large segment of the population without any health insurance. In addition, in 2013, the Ministry of Agriculture provided GEL 300 vouchers to about 600,000 farmers for work during the spring harvest. These actions are estimated to have helped the poor, especially in rural areas.

Picture 1. Social Service Agency at Mtatsminda Branch in Tbilisi

Employment has played only a limited role in poverty reduction, and high unemployment is persistent (14.6 percent in 2013). High unemployment in Georgia is caused primarily by weak labor demand, as firms expand more from productivity improvements than from increasing employment. However, there are also problems on the supply side. Despite high unemployment, including among university graduates, many firms find it difficult to recruit workers with the right skills. Addressing the skills gap is thus one of the key challenges facing the education and training systems. In addition, low-productivity employment, especially in agriculture, is the main factor behind the high incidence of in-work poverty in Georgia.

Overall, Georgia has fared poorly on the World Bank Group's measure of shared prosperity, with some gains in recent years. The consumption of the bottom 40 percent of the distribution grew at only 0.7 percent per year compared to 2 percent for the overall population over 2006–08. During the 2008–09 financial crisis, the picture worsened considerably, as the consumption of the bottom 40 percent of the population contracted by almost 5 percent per year in this period compared to a contraction of only 2 percent for the overall population. With an annual growth in consumption of 5.4 percent between 2010 and 2012, the bottom 40 percent fared better post-crisis, as they benefited from a fiscal stimulus, improved earnings, and falling food and energy prices.

Inequality in consumption has changed little over time. In Georgia, the Gini coefficient was 39.1 in 2007 and 38.8 in 2012. Another measure of inequality, the ratio of mean consumption expenditures of the top 10 percent (90th percentile) and the bottom 10 percent, has remained between 5.8 and 6.1 over the same period. Consumption inequality is consistently greater in rural than in urban areas. For example, in 2011, the rural Gini was 39.32 while the urban Gini was lower at 38.03; moreover, the ratio of the top 10 percent's consumption to that of the bottom 10 percent was 6.21 for rural residents and 5.66 for urban residents.

Health

Trends in Georgia's health indicators point to steady improvement. Considerable progress has been observed in terms of achieving the Millennium Development Goals (MDGs) for health; for example, the under-5 mortality per 1,000 live births dropped from 47 in 1990 to 13.0 in 2013. The maternal mortality rate fell from 50 deaths per 100,000 live births in 1990 to 41 in the same period. Life expectancy increased from 70.3 years in 1995 to 75.2 years in 2012.

High private expenditures on health remain a challenge. Total private health expenditures have significantly increased in recent years and represent 10 percent of GDP, which is almost twice that of comparable countries. Over 70 percent of total health expenditures are out-of-pocket, and the leading causes of household impoverishment in Georgia were costs related to hospitalization and the treatment/management of chronic diseases and acute health conditions. In 2014, the budget for health was doubled in nominal terms, an increase by 75 percent when measured as a share of the budget or as a share of GDP. The ratio of health spending to GDP is expected to rise to over 2 percent in 2015, though this is still lower than the ECA regional average.

Georgia is rapidly moving toward achieving universal health coverage, thus improving the financial protection of its citizens. Since the introduction of the UHC program, Georgia now has a foundation of universal entitlements within its health system. The World Bank, the U.S. Agency for International Development (USAID), and the World Health Organization (WHO) conducted a stock-taking exercise of these reforms that indicated that a majority of the Georgians surveyed view the program positively and are satisfied with the planned out-patient care.

The Bank continues to support the health sector in Georgia through technical assistance and development policy lending. Currently, the Bank, together with the USAID and WHO, is supporting a Health Utilization and Expenditure Survey, providing the analytic underpinnings for the future improvement of the UHC and other health policies. Bank support will also focus on improving the delivery and quality of health care, aiming at increased primary care utilization and improved health outcomes for all Georgian citizens.

Education

Georgia compares well to comparator countries in the ECA region in terms of enrollment rates at basic education levels, despite relatively modest levels of public expenditure at approximately 2.9 percent of GDP in 2013. Notwithstanding the fact that education spending in Georgia is considerably lower than the ECA average of 4 percent, gross enrollment for basic education is almost universal. For upper secondary education, the gross enrollment rate remains low at 73 percent. Gender parity has generally been achieved at all levels of education enrollment.

Improving the quality of education and student learning outcomes is a key challenge facing Georgia, based on international student assessment results. The majority of students in Georgia demonstrate below average levels of performance in reading, mathematics, and science. Over 60 percent of 15-year-old Georgian students were found to be three years behind their peers on the reading scale compared to Organisation for Economic Co-operation and Development (OECD) average scores in the Program for International Student Assessment (PISA) 2009 plus. The education outcomes also indicate important differences between students from various socioeconomic backgrounds and places of residence. Similarly, according to the Trends in International Mathematics and Science Study (TIMSS) and Progress in International Reading Literacy Study (PIRLS) 2011 results, the academic performance of Georgian students in key learning domains (literacy, mathematics, and science) remains low compared to CIS, Central and East European (CEE), and Western European countries.

Recent Government initiatives to address the quality constraints in education include the formulation of a strategic vision for the sector's development called "Main Directions for Education and Science Development, 2014–2024." Other efforts include continued reform of school curricula, improved focus on teacher qualifications through reforming the existing teacher policy framework, a new teacher evaluation and professional development system, updated school-leaving examinations using Computer Adaptive Testing (CAT), and an enhanced focus on reforming the vocational education and training (VET) sector and improving quality assurance in higher education.

Picture 2. Jugaani School in Kakheti, One of the Seven Schools Built with World Bank Assistance

The Bank supports the quality of Georgia's general education through the Growth and Competitiveness Development Policy Operation. In addition, the Bank mobilized Institutional Development Fund (IDF) grant funding to support capacity building in teacher and school principal evaluation. Most recently, the Bank conducted a detailed review of education public expenditure as part of the broader Public Expenditure Review (PER) in 2014 and a comprehensive Education Sector Policy Review (2014) aimed at supporting the Ministry of Education and Science in developing a strategic plan in preparation for the next phase of sector reforms. The Bank has also provided technical assistance through Programmatic Education Sector Support to inform policy dialogue in strategic areas identified as priorities by the Government.

Agriculture

The share of agriculture in total GDP has significantly declined from 12.8 percent in 2006 to 9.3 percent in 2013, but it remains an important sector. Agricultural production accounts for 45 percent of rural household income, and subsistence agriculture accounts for 73 percent of rural employment. Agriculture also makes a significant contribution to exports.

The agriculture sector is still recovering from the 2006 collapse. At that time, the cultivated area fell from around 525,000 to 325,000 hectares, largely caused by the Russian trade embargo, which was followed by the dismantling of public services in agriculture (such as extension and veterinary services) and low levels of public investment in agricultural infrastructure (particularly irrigation) up to 2011. Wine, fruit, nuts, and mineral water are currently driving agricultural export growth.

Weak land markets and poor access to irrigation are two key factors impeding private investment in agriculture and undermining growth. During the past 25 years, the irrigated area has declined from 386,000 hectares in 1988 to 25,000 hectares in 2013 due to weak investment in irrigation infrastructure and institutions. In addition, while Georgia has a modern national registration agency, it is estimated that only 15–20 percent of land titles are registered.

The current Government has attached a high priority to agricultural sector development, with a strong focus on rebuilding irrigation and other agricultural services, promoting land market development, and developing a strategy to harmonize food safety legislation with EU requirements in line with the Association Agreement. In 2010, Georgia started implementing food safety provisions that had been suspended since 2006. The Food Safety Law was amended to extend inspections and traceability to all food and feed operators and the country developed a training program for inspectors in 2011.

The Bank has supported the agriculture sector of Georgia through analytical work and investment operations. A US$50 million irrigation and land market development project, aimed at establishing land rights and improving irrigation and drainage agencies and infrastructure, is currently under implementation.

IFC is supporting the agriculture sector through advice and targeted investments. IFC has committed two loans (US$1.5 million and US$2 million) to Georgian wine producer and exporter Tbilvino. Following receipt of the first loan in 2011, Tbilvino's farmer-suppliers more than tripled. With the new loan, this number is expected to increase further, creating employment opportunities in rural areas and benefiting small farmers.

The IFC *Georgia Food Safety Improvement Project* has helped improve food safety practices among Georgian food producers, boosting competitiveness and sales.

Picture 3. A Mushroom Production Company

Road Infrastructure

Georgia's geographical location positions the country at the center of East-West (Black Sea and Caspian Sea) and North-South (between Russia and Turkey) transit routes. Trade with neighboring countries is therefore an important driver of the economy. Once completed, the East-West Highway will help Georgia emerge as a regional transport hub, providing direct access to 2.2 million people, or around half of the country's population, and reducing travel time by an average of 40 percent. The completion of the East-West Highway project will also contribute to improving Georgia's Logistics Performance Index (LPI).

Nevertheless, Georgia still has significant challenges ahead to improve its logistics and competitiveness. Georgia's infrastructure deficits are still a major component of this lower performance.

Road rehabilitation has been a key Government priority since 2004. Sizable investments have been made in the rehabilitation and upgrade of the East-West Highway and the improvement of the secondary and local road network. The Bank has provided over US$600 million to the road sector of Georgia, and plans to continue this financing in the coming years. Ongoing Bank-financed investments in the East-West Highway include upgrading the E-60 highway from Ruisi to Agara and the Agara-Zemo-Osiauri road sections, and constructing the Agara bypass. In addition, the Bank finances the rehabilitation and improvement of up to 200 kilometers of various sections of the secondary and local road network throughout Georgia and the piloting of a new contracting methodology for the road network in the Kakheti region.

Picture 4. A Section of the East-West Highway

Energy

Georgia has developed a stable and reliable energy sector that delivers services to customers in a sustainable manner, resulting from a series of reforms that included unbundling, privatization, and tariff adjustments to a cost-recovery level. Recent economic growth translated into a 3 percent increase in the demand for electricity in 2013, and in that year, Georgia continued to be fully self-sufficient in electricity. However, it still relies on seasonal electricity exchanges with a single neighboring country, which undermines the security of its supplies and poses a risk of seasonal electricity shortages.

Georgia has vast hydropower resources that are underutilized but have enormous potential. At present, only 12 percent of Georgia's hydropower potential is being utilized. Georgia generated about 10 terawatt hours (TWh) of electricity in 2013, about 82 percent of which was generated by hydropower stations. Several new hydropower stations are under construction, which will increase the country's installed capacity by about 16 percent.

The Bank's support to the energy sector includes analytical work (a regional analytical study has been concluded to assess power trade and demand in the South Caucasus and Turkey), reforms under the Competitiveness and Growth DPO series, and a US$60 million investment project aimed at strengthening the country's transmission grid and electricity exchange systems.

IFC is helping Georgia realize its significant renewable energy potential by investing US$40.5 million in the Paravani hydropower plant.

Together with Clean Energy Group and Tata Power, IFC has also participated in the early development of the Shuakhevi hydropower project, part of the Adjaristsqali Cascade, through IFC InfraVentures, an early stage project developer. The US$250 million debt financing arranged by IFC for the Shuakhevi project, represents the largest private hydropower investment in Georgia, consisting of two US$90 million long-term senior loans, one each from the Asian Development Bank (ADB) and EBRD, and US$70 million from IFC. IFC's total investment in this project is US$104 million, which includes a US$34 million equity investment in the project company, Adjaristsqali Georgia, a joint venture between Tata Power and Clean Energy Invest (40 percent each), and IFC (20 percent).

The Shuakhevi project is the first hydropower plant in Georgia certified by the United Nations Framework Convention on Climate Change for carbon emission reductions. It is expected to produce about 450 gigawatt hours of power annually and reduce greenhouse gas emissions by more than 200,000 tons per year. The project will develop the 187-megawatt Shuakhevi hydropower scheme, consisting of the Shuakhevi and Skhalta hydropower plants located in the Adjara region in southwest Georgia. Work on the plant began in September 2013 with a target to start producing electricity in 2016.

The Shuakhevi hydropower plant will satisfy electricity demand during winter, reducing dependence on imported fuel and increasing renewable energy output. It will also foster cross-border electricity trading at other times of the year by exporting electricity to Turkey through a transmission line financed by the European Bank for Reconstruction and Development(EBRD). The project will benefit local communities by helping create jobs, boosting municipal incomes, and upgrading area roads.

IFC's investment will be complemented by World Bank financing of the power transmission line, which will connect the plant to Georgia's national grid and improve power supply to the Adjara region.

Municipal and Regional Development

Georgia's municipal and regional development faces three main challenges: wide regional disparities, insufficient municipal infrastructure, and incomplete decentralization. The Government's priorities include support for decentralization, comprehensive local self-government reforms, democratic governance, and more efficient public service delivery. A Decentralization Strategy setting out a sound and transparent framework for the public financing of municipal and regional development has been prepared, and an amendment to the Organic Law of Local Self-Governments (LSGs) was adopted by the Cabinet and the Parliament in February 2014. The new law paves the way for a more decentralized service delivery mechanism, increased LSG accountability, and institutional capacity building to establish an effective LSG system.

Georgia has adopted a State Strategy for Regional Development to create a favorable environment for regional socioeconomic development and to improve living standards. These two goals are to be achieved through the adoption of balanced socioeconomic development policies, increased competitiveness, and greater socioeconomic equality among the regions. In regions with low income per capita or high rates of poverty, the state has focused on social issues; in others, it has chosen to focus on infrastructure bottlenecks.

The Government recognizes the importance of building local infrastructure, not only to increase the well-being of the population but also as a key element in promoting growth. The urban and rural roads, water, and sanitation infrastructure has remained in need of substantial rehabilitation in most of the country. Today, only slightly more than half of Georgian households in rural areas have indoor bathroom facilities, only 78 percent of urban households are connected to a piped water and sewerage system, and only five out of 29 wastewater treatment plants have marginal functionality.

Tourism Development

One of the potential drivers of economic growth in cities and regions is tourism, which has seen rapid growth in Georgia over the past decade and has become an important source of job creation and foreign exchange income. The number of visitors increased from 560,000 in 2005 to 5 million in 2013, with 6.3 million expected in 2015. An integrated and demand-driven approach to regional development has been designed with the support of the Bank and is currently seen as critical to spurring growth and job creation in historic cities and cultural villages.

Picture 5. Dartlo Village, Tusheti

The Bank supports regional development through a multi-sectoral approach. The first *Regional Development Project* (RDP, US$60 million), focuses on the Kakheti region, and the second *Regional Development Project* (RDPII, US$30 million), focuses on the Imereti region. The Swedish International Development Cooperation Agency (SIDA) has provided an additional US$10 million grant to address issues of wastewater treatment in the two regions to ensure the promotion of sustainable and responsible tourism.

The Bank's regional development activities bring direct benefits to residents. The number of hotel beds as well as of SME points of sales (tickets, souvenirs shops, restaurants, hotels, guest houses, and family houses) in renovated tourism and culture heritage sites and cities has increased by about 25 percent since 2011. In addition, residents are directly benefiting from an improved water supply (from eight to 24 hours per day) and reduced vehicle operating costs as a result of rehabilitated, safer, and well-lit streets.

Picture 6. Urban Regeneration in Telavi, Kakheti Region

The regional development program has all the prerequisites of becoming one of the flagships of Georgia's cooperation with the World Bank. The program is designed to improve the quality of life of the local population, create job opportunities, and generate public-private partnerships (PPPs) in collaboration with IFC.

Environment

Environmental management remains a challenge, but efforts are being made to improve the situation. Georgia's public policies to protect the environment and natural resources were initially driven by excessive deregulation, resulting in the unsustainable use of natural resources and environmental damage. The outlook for enhancing the policy and regulatory framework improved with recent institutional reforms, and a number of important pieces of environmental legislation are under preparation, including a waste law, a water law, and a forest code.

The World Bank, in partnership with the International Union for Conservation of Nature (IUCN) and the World Wildlife Fund (WWF), is implementing the EU-funded *European Neighborhood and Partnership Instrument East Countries Forest Law Enforcement and Governance Program (FLEG) II* in Georgia, which is one of the seven beneficiary countries of this program. The Bank-financed Country Environmental Analysis explored public environmental expenditure, the cost of environmental degradation, and an institutional framework for environmental management in Georgia.

THE WORLD BANK PROGRAM IN GEORGIA

The Country Partnership Strategy (CPS) for FY14–17 envisages a new lending envelope of about US$1.18 billion, roughly 30 percent higher than the program delivered under the previous CPS (US$823 million in FY10–13). Georgia graduated from the International Development Association (IDA) as of the end of the IDA 16 Replenishment period.

The objectives of the CPS are to reduce poverty and support inclusive growth focused on job creation. These objectives are fully aligned with the Government's Socioeconomic Development Strategy. The CPS objectives are supported through two areas of focus: (i) strengthening public service delivery to promote inclusion and equity, and (ii) promoting job creation and competitiveness to enable private sector–led inclusive growth.

The current portfolio consists of 10 active investment projects financed by IDA credits/IBRD loans for a total of US$670 million, of which US$200 is IDA. About US$303 million is undisbursed. In addition to IDA/IBRD operations, there is an active program of four recipient-executed Trust Fund operations for about US$12.8 million, of which about 92 percent is undisbursed. Analytical and Advisory Activities (AAA) further contribute to program implementation. The AAA program of the current fiscal year is on track and includes activities in various sectors and complements the lending program.

INTERNATIONAL FINANCE CORPORATION

Georgia became an IFC member and shareholder in 1995. As of December 31, 2014, IFC has provided a total of about US$665 million[1] in long-term finance, including US$272 million mobilized from partners, supporting 51 projects in the financial, agribusiness, manufacturing, services, and infrastructure sectors. In addition, IFC has supported trade flows worth more than $292 million[2] through its trade finance program. IFC has also implemented a number of advisory projects focused on private sector development.

IFC Strategy in Georgia
The new World Bank Group Country Partnership Strategy for financial years 2014-2017—approved by the Board in May 2014—has two pillars: strengthening public service delivery to promote inclusive growth and enabling private sector-led job creation through improved competitiveness.

Within this Country Partnership Strategy, IFC works to:

- Contribute to greater financial intermediation and increase access to finance for MSMEs through the provision of trade finance, risk management products, longer term senior and subordinated debt, and equity;
- Promote sustainable private sector-driven growth through increased trade and increased competitiveness of local companies;
- Help develop the country's significant renewable energy potential;
- Support improvements in productivity for agricultural processing and food safety;
- Foster the development of public-private partnerships.

1 Starting on July 1, 2014, IFC shifted from reporting its cumulative commitment volume as a sum of short-term trade finance and long-term finance to reporting only long-term commitments. Short-term finance is now reported as the average annual outstanding portfolio balance in a given fiscal year.

2 Total trade supported is measured as all trade transactions in which the given country is either the country of import or the country of export.

ONGOING PROJECTS

THIRD EAST-WEST HIGHWAY IMPROVEMENT PROJECT

Key Dates:
Approved: September 10, 2009
Effective: November 3, 2009
Closing: June 30, 2016 (Additional Financing)
Financing in million US Dollars:

Financier	*Financing*	*Disbursed**	*Undisbursed*
IDA Credit	43.00	27.41	10.81
IBRD Loan	147.00	147.00	0.00
Government of Georgia	47.87		
Total	**237.87**	**174.41**	**10.81**

***World Bank Disbursements as of April 2, 2015**
Note: Disbursements may differ from financing due to exchange rate fluctuations at the time of disbursement.

The Project Development Objectives are to (i) contribute to the gradual reduction of road transport costs and improve access, ease of transit, and road safety along the central part of Georgia's East-West corridor, and (ii) strengthen the capacity of the Government, the Roads Department, and other relevant government entities to plan and manage the road network and improve traffic safety. The project builds on the Bank's past projects and addresses some of the remaining policy and investment gaps in the road sector. Specifically, the project envisages an upgrade of the 15-kilometer segment of the E60 East-West Highway from Sveneti to Ruisi to a dual carriageway. The East-West Highway will be selected to implement a holistic approach to traffic safety along part of the E60 corridor, which will integrate ambulance services, police, first aid training, and other safety measures under the corridor safety management plan. As a result of the project, road users will get a better road quality and level of service, avoid costly congestion, experience better road safety, and save on travel time. With the Additional Financing in the amount of US$43 million, the existing Ruisi-Agara road section will be upgraded and the Agara Bypass will be constructed as a dual carriageway road. Overall 34 kilometers of road will be upgraded.

Results achieved to date:

- Construction work for a 15-kilometer segment of the E60 Highway from Sveneti to Ruisi is complete. The road, two tunnels, and the bridge over Liakhvi River are open for traffic.
- Institutional strengthening and road safety components have begun to be implemented, and road safety audits have been conducted. Monitoring and evaluation outputs have recently improved.
- Transit time from Sveneti to Ruisi has decreased from 12 to 8.1 minutes.
- Vehicle operating costs from Sveneti to Ruisi have decreased to US$0.17 per kilometer for cars and to US$0.71 per kilometer for trucks—target overachieved.
- Transit time from Sveneti to the Agara Bypass has decreased from 27 to 23.2 minutes.
- Vehicle operating costs from Sveneti to the Agara Bypass have decreased to US$0.19 per kilometer for cars and to US$0.74 per kilometer for trucks.
- Road fatalities on the East-West Highway from Senaki to Tbilisi have been reduced by 43 percent.
- Around 50 percent of works are completed on the Ruisi to Agara Bypass financed under the Additional Financing.

Key Government Partners: Ministry of Regional Development and Infrastructure (MRDI), responsible for policy setting; Roads Department under the MRDI, responsible for implementing the project; and the Transport Reform and Rehabilitation Center (TRRC), responsible for financial management and disbursement functions within the project.

Key Development Partners: Japan International Cooperation Agency (JICA), Asian Development Bank (ADB), Millennium Challenge Corporation (MCC), European Commission (EC), European Investment Bank (EIB), and the Kuwait Fund, which have been financing (or plan to finance) different sections of Georgia's road network.

FOURTH EAST-WEST HIGHWAY IMPROVEMENT PROJECT

Key Dates:
Approved: May 6, 2013
Effective: August 5, 2013
Closing: February 28, 2018
Financing in million US Dollars:

Financier	*Financing*	*Disbursed**	*Undisbursed*
IDA Credit	37.00	15.06	18.74
IBRD Loan	38.00	0.95	37.91
Government of Georgia	18.75	--	--
Total	**93.75**	**16.01**	**56.65**

*** World Bank Disbursements as of April 2, 2015**
Note: Disbursements may differ from financing due to exchange rate fluctuations at the time of disbursement.

The Project Development Objectives are to (i) contribute to the gradual reduction of road transport costs and improve road safety along the section upgraded under the project; and (ii) strengthen the capacity of the Roads Department (RD) and the Ministry of Regional Development and Infrastructure (MRDI) to plan and manage the road network and improve road traffic safety. The project development objectives are similar to those used in the current East-West Highway projects supporting the improvements to the E60 highway since they contribute to the achievement of the overall objective of improving the E60 East-West Highway Corridor westward from Tbilisi.

The project is designed to upgrade the existing East-West Highway through the construction of a two-lane dual carriageway from Agara to Zemo Osiauri. The length of the section of the E60 to be upgraded is about 12 kilometers and contains two interchanges, two bridges, several overpasses and underpasses, and approximately 3.4 kilometers of riverbank protection. The project will also finance maintenance of the E60 two-lane dual carriageway between Natakhtari and Ruisi (approximately 67 kilometers) through a multiyear maintenance contract to assure the continued serviceability of this section of the E60.

Results to be achieved:

- Transit time from Agara to Zemo Osiauri will be reduced by three minutes, or 30 percent
- Vehicle Operating Costs from Agara to Zemo Osiauri (cars) will be reduced by 10 percent to US$0.18/kilometer
- Vehicle Operating Costs from Agara to Zemo Osiauri (trucks) will be reduced by 5 percent to US$0.72/kilometer
- Number of road fatalities will be reduced by 25 percent

Key Government Partners: Ministry of Regional Development and Infrastructure (MRDI), responsible for policy setting; Roads Department under the MRDI, responsible for implementing the project; and the Transport Reform and Rehabilitation Center (TRRC), responsible for financial management and disbursement functions within the project.

Key Development Partners: Japan International Cooperation Agency (JICA), Asian Development Bank (ADB), Millennium Challenge Corporation (MCC), European Commission (EC), European Investment Bank (EIB), and the Kuwait Fund, which have been financing (or plan to finance) different sections of Georgia's road network.

SECOND SECONDARY AND LOCAL ROADS PROJECT

Key Dates:
Approved: March 15, 2012
Effective: May 24, 2012
Closing: June 30, 2017
Financing in million US Dollars:

Financier	*Financing*	*Disbursed**	*Undisbursed*
IDA Credit	40.00	39.30	0.00
IBRD Loan	30.00	10.86	19.14
Government of Georgia	17.50	--	--
Total	**87.50**	**50.16**	**19.14**

*** World Bank Disbursements as of April 2, 2015**
Note: Disbursements may differ from financing due to exchange rate fluctuations at the time of disbursement.

To boost the country's economy and diversify sources of growth, Georgia is focusing on developing selected sectors, including infrastructure, agriculture and agro-industries, and tourism, with the expectation that this would create jobs. Rehabilitating secondary and local roads and improving local connections are also known to stimulate agricultural development. Further, reduced transport costs would lower agriculture sector costs, thus making agricultural products more competitive.

The Project Development Objective is to improve local connectivity and travel time for selected secondary and local roads and to strengthen the capacity of the Roads Department (RD) to manage the road network. The project envisages rehabilitating and improving up to 200 kilometers of various sections of the secondary and local road network throughout Georgia. As a result of the project, travel time will be reduced by 20 percent on the targeted road sections. A Performance-Based Contract (PBC)/Output- and Performance-based Rehabilitation Contract (OPRC) will be piloted.

Out of 225 kilometers of secondary and local roads to be rehabilitated under the project, about 182 kilometers of roads have been rehabilitated.

Results achieved to date:

- Travel time on rehabilitated sections has decreased on average by 44 percent, affecting over 150,000 direct beneficiaries
- Roads in good and fair condition as a share of total classified roads has improved from 30 to 33 percent
- 19 safety audits have been conducted

Key Government Partners: Ministry of Regional Development and Infrastructure (MRDI), responsible for policy setting; Roads Department under the MRDI, responsible for implementing the project; and the Transport Reform and Rehabilitation Center (TRRC), responsible for financial management and disbursement functions within the project.

Key Development Partners: Japan International Cooperation Agency (JICA), Asian Development Bank (ADB), Millennium Challenge Corporation (MCC), European Commission (EC), European Investment Bank (EIB), and the Kuwait Fund, which have been financing (or plan to finance) different sections of Georgia's road network.

THIRD SECONDARY AND LOCAL ROADS PROJECT

Key Dates:
Approved: July 3, 2014
Effective: November 6, 2014
Closing: September 30, 2018
Financing in million US Dollars:

Financier	*Financing*	*Disbursed**	*Undisbursed*
IBRD Loan	75.00	7.87	67.13
Government of Georgia	18.75		
Total	**93.75**	**7.87**	**67.13**

*** World Bank Disbursements as of April 2, 2015**
Note: Disbursements may differ from financing due to exchange rate fluctuations at the time of disbursement.

The Secondary and Local Roads Projects (SLRP) have contributed to improving the condition of roads and building the technical and management capacity of the Roads Department. A total of 1,054 kilometers of secondary and local roads were rehabilitated by 2012 under SLRP I and 225 kilometers will be rehabilitated by 2017 under the ongoing SLRP II. This has contributed to bridging the road rehabilitation backlog and increasing the share of secondary and local roads in good and fair condition from 45 to 49 percent and from 16 to 17 percent, respectively.

The Project Development Objective is to reduce transport costs on project roads and improve the sustainability of road asset management in the secondary and local project road network. The Third SRLP will improve 200 kilometers of key regional and local road sections, which will provide better access to three major towns (Telavi, Samtredia, and Tsalenjikha), 126 villages, and around 45,600 households, totaling a population of roughly 138,000 inhabitants.

Expected Results:

- Travel time on rehabilitated sections will decrease: average speed will increase by 20 kilometers per hour
- Vehicle operating costs will decrease on average by 22 percent for cars and 27 percent for trucks
- Improved condition of project roads (as measured by international roughness index - IRI) from 12 to 3
- Roads in good and fair condition as a share of total classified roads will improve by 2.4 percentage points

Results achieved to date:

- All 10 road sections of the first-year program have been contracted out.

Key Government Partners: Ministry of Regional Development and Infrastructure (MRDI), responsible for policy setting; Roads Department under the MRDI, responsible for implementing the project; and the Transport Reform and Rehabilitation Center (TRRC), responsible for financial management and disbursement functions within the project.

Key Development Partners: Japan International Cooperation Agency (JICA), Asian Development Bank (ADB), Millennium Challenge Corporation (MCC), European Commission (EC), European Investment Bank (EIB), and the Kuwait Fund, which have been financing (or plan to finance) different sections of Georgia's road network.

KAKHETI REGIONAL ROADS IMPROVEMENT PROJECT

<u>**Key Dates:**</u>
Approved: November 10, 2009
Effective: December 8, 2009
Closing: August 30, 2015
<u>**Financing in million US Dollars:**</u>

Financier	*Financing*	*Disbursed**	*Undisbursed*
IBRD Loan	30.00	29.40	0.00
Government of Georgia	7.50	--	--
Total	**37.50**	**29.40**	**0.00**

*** World Bank Disbursements as of April 2, 2015**
Note: Disbursements may differ from financing due to exchange rate fluctuations at the time of disbursement.

Roads are a lifeline for the economic activities of most Georgians, and even in the main foreign trade road corridors, up to 90 percent of the traffic is local users. In the Kakheti region, the main activities are the wine industry and tourism. A reliable transport network is essential to stimulating both of these activities as well as to reducing poverty in rural areas.

The Project Development Objective is to reduce transport costs and improve access and traffic safety for Kakheti regional roads. The project entails (a) rehabilitating the 65-kilometer Vaziani-Gombori-Telavi (VGT) road, mainly along its existing alignment; (b) rehabilitating the 17 kilometer Sasadilo-Sioni road under a design-build contract; (c) implementing traffic safety improvement measures on the VGT road and along the existing alignment of the Vaziani-Sagarejo-Bakurtsikhe-Gurjaani-Telavi road; (d) strengthening the operational effectiveness of the Sagarejo Regional Office of the Roads Department; and (e) conducting the Roads Safety Awareness and Education Campaign in the Kakheti region.

Results achieved to date:

- 75 kilometers of roads have been rehabilitated
- Traffic volume for trucks between Vaziani and Telavi via Gombori has increased about five times
- Travel time to Vaziani and Telavi via Gombori has decreased from 120 to 50 minutes
- Vehicle operating costs have decreased significantly, from US$0.36 to US$0.25 for cars and from US$1.05 to US$0.72 for trucks
- The number of road crashes with fatalities along the Vaziani-Sagarejo-Bakurtsikhe-Gurjaani-Telavi road has declined by 52 percent.

Key Government Partners: Ministry of Regional Development and Infrastructure (MRDI), responsible for policy setting; Roads Department under the MRDI, responsible for implementing the project; and the Transport Reform and Rehabilitation Center (TRRC), responsible for financial management and disbursement functions within the project.

Key Development Partners: Japan International Cooperation Agency (JICA), Asian Development Bank (ADB), Millennium Challenge Corporation (MCC), European Commission (EC), European Investment Bank (EIB), and the Kuwait Fund, which have been financing (or plan to finance) different sections of Georgia's road network.

REGIONAL DEVELOPMENT PROJECT – 1 (Kakheti)

Key Dates:
Approved: March 20, 2012
Effective: May 31, 2012
Closing: December 31, 2016
Financing in million US Dollars:

Financier	*Financing*	*Disbursed**	*Undisbursed*
IBRD Loan	60.00	53.62	6.38
Government of Georgia	15.00		--
Total	**75.00**	**53.62**	**6.38**

*** World Bank Disbursements as of April 2, 2015**
Note: Disbursements may differ from financing due to exchange rate fluctuations at the time of disbursement.

In response to global economic uncertainties, the Government of Georgia is trying to ensure that its economic reform program is also backed by a strong public investment program. The Government has therefore launched several regional development initiatives to attract private sector investors to various areas. Georgia, however, has not yet fully tapped its potential to promote sustainable tourism in promising regions, such as Kakheti, which has long been at the heart of Georgia's ancient culture and economy. The tourism strategy proposes to develop Kakheti as a high-quality destination year-round. It seeks to attract both domestic and international tourists, building on its cultural heritage and biodiversity.

The Project Development Objective is to improve infrastructure services and institutional capacity to support the development of a tourism-based economy and cultural heritage circuits in the Kakheti region. The activities envisaged under the project are expected to bring benefits to the residents and tourists in Kakheti. The implementation of the project is expected to improve access to, and the quality and reliability of, public infrastructure; increase the volume of private sector investment in the region; and increase points of sales in renovated cultural heritage sites and cities. The Government will benefit from the improved institutional capacity of selected agencies and LSGs. Overall, the population is expected to see improved welfare and revenues.

Results achieved to date:

- 210 building facades have been rehabilitated in Telavi and Kvareli
- Water supply, sewage networks, 71,613 square meters (m^2) of asphalt road/sidewalks, 20,824 m^2 of cobblestone paving, 530 lighting posts, and three public parks rehabilitated in central Telavi and Kvareli
- Volume of private sector investments has reached US$10 million (end-of-project target: US$50 million)
- 40,400 people in urban areas provided with access to all-season roads within a 500-meter range under the project
- Weighted average number of hours per day of piped water services in project areas increased from eight hours/day to 12 (end target: 24 hours/day)
- Weighted average vehicle operating costs due to improved urban roads have been reduced by 10 percent (end target: 25 percent)
- Number of hotel beds in circuit route increased by 69 percent from 1,610 to 2,719, well above the target of 1,932 beds
- Number of points of sales in renovated cultural heritage sites and cities increased by 21 percent from 248 to 300 (end target: 323)
- About 3,500 new jobs have been created.

Key Government Partners: Ministry of Regional Development and Infrastructure (MRDI), Ministry of Finance (MoF), Ministry of Economy and Sustainable Development (MoESD), Municipal Development Fund (MDF), Cultural Heritage Fund, Agency for Cultural Heritage Preservation, Protected Areas Agency, National Tourism Administration, United Water Supply Company (UWSC), and Kakheti regional and local governments.

Key Development Partners: Swedish International Development Cooperation Agency (SIDA), European Union (EU), German Technical Cooperation Agency (GiZ), U.S. Agency for International Development (USAID), and the Swiss Agency for Development and Cooperation (SDC).

REGIONAL DEVELOPMENT PROJECT – 2 (Imereti)

Key Dates:
Approved: November 6, 2012
Effective: January 29, 2013
Closing: June 30, 2017
Financing in million US Dollars:

Financier	*Financing*	*Disbursed**	*Undisbursed*
IDA Credit	30.00	16.21	11.07
Government of Georgia	7.50		--
Total	**37.50**	**16.21**	**11.07**

*** World Bank Disbursements as of April 2, 2015**
Note: Disbursements may differ from financing due to exchange rate fluctuations at the time of disbursement.

Georgia intends to fully tap into its potential to promote sustainable tourism in attractive regions such as Kakheti and Imereti. Bank involvement under the proposed programmatic approach to regional development will ensure continued support to (a) growth in the tourism sector, (b) growth of underdeveloped areas, and (c) the leveraging of public and private investment. The Imereti spatial economic analysis 2 and Imereti Regional Development Strategy 3 have identified tourism, industry, and trade as the main drivers of economic growth in the region. Imereti is home to several cultural heritage sites, as well as to significant natural and protected areas.

The Project Development Objective is to improve infrastructure services and institutional capacity to support the increased contribution of tourism to the local economy of the Imereti region. Project activities are expected to benefit Imereti's residents and tourists. They are also expected to improve access to, and the quality and reliability of, public infrastructure; increase the volume of private sector investment in the region; and increase small and micro enterprises in renovated cultural heritage sites and cities. The Government will benefit from the improved institutional capacity of selected agencies and the improved capacity to operate and maintain assets.

Results achieved to date:

- Number of hotel beds in circuit route areas increased by 48 percent (from 2,661 to 3,943)
- Number of hours per day of piped water services in Tskaltubo increased from eight to 12 (end target is 18)
- Number of household water connections that are benefiting from rehabilitation works: 2,000 (end target is 5,000)
- Energy efficiency of street lights has improved by 20 percent

Expected Results:

- Volume of private sector investments will increase by US$20 million
- Revenues from tickets sold at Vani museum will increase from US$10,500 to US$89,000 per annum

Key Government Partners: Ministry of Regional Development and Infrastructure (MRDI), Ministry of Finance (MoF), Ministry of Economy and Sustainable Development (MoESD), Municipal Development Fund (MDF), Cultural Heritage Fund, Agency for Cultural Heritage Preservation, Protected Areas Agency, National Tourism Administration, Georgian National Museum, United Water Supply Company (UWSC), and Imereti regional and local governments.
Key Development Partners: Swedish International Development Cooperation Agency (SIDA)*, European Union (EU), German Technical Cooperation Agency (GiZ), U.S. Agency for International Development (USAID), and the Swiss Agency for Development and Cooperation (SDC).

**The World Bank leveraged a US$10 million grant from the Swedish International Development Cooperation Agency to address environmental issues in Tskaltubo and Telavi (Kakheti region) through the rehabilitation of wastewater treatment plants.*

IRRIGATION AND LAND MARKET DEVELOPMENT PROJECT

Key Dates:
Approved: May 23, 2014
Effective: Not yet effective
Closing: July 31, 2019
Financing in million US Dollars:

Financier	*Financing*	*Disbursed**	*Undisbursed*
IDA Credit	50.0	0.0	44.70
Total	**50.0**	**0.0**	**44.70**

*** World Bank Disbursements as of April 2, 2015**
Note: Disbursements may differ from financing due to exchange rate fluctuations at the time of disbursement.

Agriculture remains an important sector in Georgia, given that over 50 percent of the population works in agriculture, which constitutes about 25 percent of exports. Subsistence agriculture accounts for 75 percent of rural employment and 45 percent of rural income. However, the share of agriculture to GDP has significantly declined (from 25 percent in 1999 to about 8 percent in 2012), though it has started to increase again due to the Government's focus on the sector, recording 8.2 percent in the first six months in 2013. The Government's draft Socioeconomic Development Strategy 2020 recognizes the poor condition of agriculture and focuses strongly on rebuilding services for small farmers, promoting cooperative development, and restoring infrastructure. The Government is increasing public funding to agriculture, either through specific funds (to promote private sector participation) or subsidies to small-holder farmers. Two key constraints to investment in agriculture are poor irrigation and weak land markets. During the past 25 years, the irrigated area has declined from 386,000 hectares in 1988 to 25,000 hectares in 2013 due to weak investment in irrigation infrastructure and institutions. While Georgia has a modern national registration agency, it is estimated that only 15–20 percent of land titles are registered.

The Project Development Objective is to improve the delivery of irrigation and drainage services in selected areas and develop improved policies and procedures as a basis for a national program of land registration.

Expected Results:

About 31,000 farming households cultivating approximately 26,000 hectares of agricultural land on which irrigation and drainage services will be improved will benefit directly from increased agricultural productivity under the project. Up to 10 percent of these households are headed by a female and about 78 percent of all households were employed in agriculture in 2012. Additionally, about 19,000 households holding unregistered agricultural land plots in pilot areas for land registration will benefit from the improved policies and procedures generated under the project and the opportunity to register their land. In the longer term, all rural households in Georgia holding unregistered agricultural land plots (approximately 640,000 households) will similarly benefit.

Key results expected:

- 50,000 farmers will benefit from the project
- 26,000 hectares will be provided with improved irrigation and drainage services
- 31,000 water users will be provided with new or improved irrigation and drainage services
- A national irrigation and drainage strategy will be prepared and endorsed
- Recommended policies and procedures for a national program of land registration will be submitted to the Government

Key Government Partners: Ministry of Agriculture (MOA), Ministry of Justice (MOJ), United Amelioration Service Company for Georgia (UASCG), and the National Agency for Public Registry (NAPR).

TRANSMISSION GRID STRENGTHENING PROJECT

<u>**Key Dates:**</u>
Approved: May 13, 2014
Effective: December 29, 2014
Closing: March 31, 2019
<u>**Financing in million US Dollars:**</u>

Financier	*Financing*	*Disbursed**	*Undisbursed*
IBRD Loan	60.0	0.75	59.25
Government of Georgia	1.88		
Total	**61.88**	**0.75**	**59.25**

*** World Bank Disbursements as of April 2, 2015**
Note: Disbursements may differ from financing due to exchange rate fluctuations at the time of disbursement.

Affordable and reliable clean energy is essential for Georgia's private sector to compete, grow, and contribute to the kind of job creation necessary for boosting shared prosperity. Although Georgia has no overall shortage of supply, it is highly dependent on imported power to meet seasonal demand, raising concerns over the security of supply. Without major investments in domestic seasonal generation, the security of the power supply will diminish even further as Georgia's economy grows. Even with a major increase in power generation capacity, the weak parts of the transmission grid will impede the security of supply. The proposed Transmission Grid Strengthening Project (TGSP) will address the following key issues: (i) the lack of a hydropower development plan optimized for enhancing the security of supply, realizing the economic benefits of hydropower assets, and minimizing adverse environmental and social impacts; and (ii) inadequate infrastructure for a major increase in the power trade.

The Project Development Objective is to provide reliable power transmission to the southwestern part of the grid, upgrade electricity exchange systems, and provide economically efficient and environmentally and socially sustainable electricity sector planning.

Expected Results:
All power consumers of Georgia will benefit either directly or indirectly from an adequate and more reliable electricity supply transmitted from a cleaner source of power. The power consumers in the Ajara region will be direct beneficiaries of an improved quality of power supply, particularly Batumi. The power from new hydropower stations on the Adjaristsqali river will provide an important additional flow of revenues to Georgia's economy.

Key results expected:
- 142 kilometers of transmission lines will be constructed or rehabilitated
- Total duration of outages in Batumi will decrease from 136 hours to 0.5 hours per annum
- Total electricity evacuated from the newly developed power generation stations in southwestern Georgia through the grid will reach 400 gigawatt hours (GWh) by the end of the project.

Key Government Partners: Ministry of Energy, Ministry of Environment, and Georgia State Electrosystem (GSE).

Key Development Partners: International Finance Corporation (IFC), Asian Development Bank (ADB), European Bank for Reconstruction and Development (EBRD), and the U.S. Agency for International Development (USAID).

INTERNATIONAL FINANCE CORPORATION

IFC SUPPORTS BANK OF GEORGIA IN EXPANDING LENDING TO SMALLER BUSINESSES AND FEMALE ENTREPRENEURS

Key Dates:

Approved: June 25, 2012
Signed: June 28, 2012

IFC financing (US Dollars):

Financier	*Amount*	*Fiscal Year (starts July 1)*
Loan	25 million	2012

The Challenge

The fact that many financial institutions in emerging markets do not tailor financial products and services to women entrepreneurs represents a missed opportunity and constrains private sector development. Providing women with access to finance from the Georgian finance sector represents a largely untapped market opportunity.

IFC supports female entrepreneurship as an important part of its mission to foster sustainable private sector growth in developing countries. IFC works with financial institutions to expand financial services to women entrepreneurs through specialized credit lines, market analyses, and capacity building. IFC launched its Banking on Women program in Europe and Central Asia in 2011 to support lending to women through financial intermediaries.

The Project Development Objective

IFC has provided the Bank of Georgia, its long-term partner, with a US$25 million loan to expand lending to smaller businesses, especially those owned by women, supporting financial inclusion and improving the competitiveness of Georgia's economy. The IFC loan is supporting the lender in reaching out to female entrepreneurs, who face more challenges accessing credit than their male counterparts. Through the bank's network of 164 branches, the program is expected to help small and medium-sized enterprises (SMEs) inside and outside the capital expand and modernize.

This is IFC's first loan in Georgia under its Banking on Women program, which helps women to play a greater role in the economy.

Key Expected Results:

The project is expected to:

- Support SMEs in Georgia by providing them with much-needed long-term financing, boosting economic growth
- Encourage lending to women-owned businesses, helping improve the lives of many
- Have a strong demonstration effect, leading to increased international funding for the Georgian market

WORLD BANK GROUP AND IFC ADVISORY SERVICES PROJECTS IN GEORGIA

WORLD BANK GROUP
TRADE AND COMPETITIVENESS

Georgia Investment Climate Project (2013–16)

Donor Partners: Austria's Federal Ministry of Finance, BP and its Oil and Gas Co-venturers, and the Norwegian Trust Fund for Private Sector and Infrastructure.

The Challenge
Georgia has undertaken sweeping economic reforms in recent years, improving the investment climate. The Government's priorities are now focused on further improving the investment climate and strengthening investor confidence to attract more foreign investment and boost economic growth. Reforms in the tax system, investment policy, and trade logistics are expected to contribute to increased transparency and investor confidence. These are crucial for growth in a small, open economy like Georgia and are high on the Government's agenda.

The World Bank Group Approach
The IFC Georgia Investment Climate Project aims to improve the investment climate in Georgia by increasing the efficiency of regulations in three key areas: tax, trade logistics, and investment policy.
The project will work on:

- **Taxation:**
    - Improving the legal framework and efficiency of administration of international taxation procedures, with a focus on transfer pricing[1]
    - Aligning Georgian tax legislation and implementation practices with global standards following the guidelines of the Global Forum on Transparency and Exchange of Information[2]
    - Simplifying value added tax (VAT)–related administrative procedures and harmonizing them with the legislation of European Union
- **Trade logistics:**
    - Supporting an upgrade of customs automation system
    - Supporting the simplification of import and export procedures
- **Investment policy:**
    - Enhancing the legal and regulatory framework for investment in Georgia

The IFC Georgia Investment Climate Project is implemented by the World Bank Group Trade and Competitiveness Global Practice.

Results achieved to date:
- Transfer pricing legislation has been adopted, which will help increase revenues from transfer pricing audits
- Customs automation system has been upgraded, which will help reduce the administrative burden for businesses

[1] Transfer pricing occurs when two related companies—a parent company and a subsidiary, or two subsidiaries controlled by a common parent—trade with each other.
[2] The Global Forum is the multilateral framework within which work in the area of transparency and exchange of information has been carried out by both the Organisation for Economic Co-operation and Development (OECD) and non-OECD economies since 2000. Georgia became a member of the Global Forum in 2011.

IFC ADVISORY SERVICES PROJECTS IN GEORGIA

Agribusiness Standards Advisory Program in Eastern Europe and Central Asia (2013–16)

Donor partner: The Ministry of Finance of Austria

The Challenge
The agribusiness industry is a vital contributor to the economies of Europe and Central Asia. However, inadequate food safety standards keep the region's agribusiness industry from advancing, while food companies are shut out of the modern food value chains, potentially aggravating global food security.

The IFC Approach
The IFC program assists local companies in applying food safety standards throughout the agribusiness value chain while also strengthening the capacity of local consultants. Improved standards will help agribusiness firms meet regional and export market requirements while building a foundation to mobilize investments and help the agribusiness industry realize its full potential.

Expected Results
The IFC program is expected to:

- increase the number of companies with food safety management systems in place, boosting their competitiveness, investment attractiveness, and export opportunities;
- facilitate an increase in domestic and export sales by client companies;
- facilitate investments as a result of improved food safety management;
- build capacity among local consultants and firms;
- create a demonstration effect for how to do business more sustainably, across the region and globally.

Corporate Governance Program in Europe and Central Asia (2012–15)

Donor partners: the Swiss State Secretariat for Economic Affairs (SECO) and the Development Bank of Austria (OeEB).

The Challenge
Good corporate governance helps companies and financial institutions to enhance their sustainability, access capital, and improve their performance. Yet many companies and financial institutions in Europe and Central Asia lack the knowledge and experience necessary to strengthen their governance practices so as to realize the real benefits such practices can bring. Local consultants and institutions also lack the skills needed to help businesses improve their corporate governance. In addition, the corporate governance framework in many countries is in need of further enhancement.

The IFC Approach
The program provides in-depth advice to companies and financial institutions on implementing good corporate governance practices, strengthens the capacity of local partner institutions to deliver director-focused training and corporate governance services, and contributes advice on the corporate governance aspects of laws, codes, regulations, and other tools.

Expected Results
The program aims to help its partners in Europe and Central Asia raise US$180,000 in sales revenue through corporate governance work in order to improve the performance of 32 companies through corporate governance improvements and to help 24 companies access financing totaling US$100 million.

Resource Efficiency Program in Europe and Central Asia (2010–15)

Donor partner: the Ministry of Finance of Austria

The Challenge
The efficient use of energy, raw materials, and water along a company's value chain not only helps conserve resources and reduce waste, pollution, and greenhouse gas emissions, but also reduces operating costs. Yet many firms in Europe and Central Asia remain unaware of the potential cost savings and environmental benefits. As a result, firms are reluctant to invest the upfront costs needed to identify and take advantage of resource-efficiency opportunities.

The IFC Approach
The program works at the firm and sector levels to stimulate investment in resource-efficient technologies and best practices, improve management and operational practices across industries, raise awareness among policy makers and financial institutions, and drive market transformation through sector studies, such as benchmarking and assessment tools.

Expected Results
The program aims to facilitate the investment of US$90 million and reduce carbon dioxide emissions by 120,000 tons of CO_2 annually in Europe and Central Asia.

Bank Advisory Program in Europe and Central Asia (2009–15)

Donor partners: the Development Bank of Austria, the Government of Luxemburg, and the Swiss State Secretariat for Economic Affairs

The Challenge
The Europe and Central Asia region was among the hardest hit by the global financial crisis, and many financial institutions remain vulnerable to further instability and lack the confidence to restart lending to the SME sector in particular. That is a byproduct of insufficient knowledge about how to manage risk, best practice SME lending skills, and the high rates of nonperforming loans (NPLs).

The IFC Approach
The program provides in-depth advice to help financial institutions strengthen their NPL and risk management capabilities and increase lending to SMEs. It also supports the development of a market for distressed assets, increases awareness of best international practices in risk and NPL management, and supports the development of SME banking with a focus on gender finance.

Results to Date
The project has helped clients in Europe and Central Asia release more than US$51 million for new lending and facilitated a further US$17 million in new financing to clients.

MULTILATERAL INVESTMENT GUARANTEE AGENCY

GeoCapital, Georgia

Key Project Data:

Project name: GeoCapital, Georgia
Fiscal year: 2013
Status: Active
Guarantee holder: Principals of a microfinance organization operating in Georgia
Investor country: United States
Sector: Banking
Project Board date: May 28, 2013
Gross exposure: US$1.8 million
Project type: SIP
Strategic priority area: IDA

Project Description

On May 29, 2013, MIGA issued guarantees totaling US$1.8 million covering equity investments and shareholder loans by two individual American investors in GeoCapital, Georgia. The coverage is for a period of up to three years against the risks of transfer restriction, expropriation, and war and civil disturbance.

The project involves investment in the creation and subsequent expansion of operations of GeoCapital Microfinance Organization LLC (GC), a fast-growing microfinance institution in Kutaisi (Imereti region), Georgia. GC offers small loans primarily to individuals but also to micro and small businesses. The purpose of the loans is to provide working capital for small businesses, house remodeling/repairs, education and medical expenses, and other general purposes. These loans are extended to the large population of households and businesses that have had no or only limited access to credit.

In Georgia, access to finance is one of the main constraints for both companies and individuals. GC is helping a part of the "unbankable" population gain access to credit and loans for purposes ranging from home equity loans to medical, educational, and income-generation loans. As a large portion of these loans are extended to individuals, they enhance Georgians' capacity to pay for social services.

GC's loans carry a lower interest rate than other microfinance institutions operating in the country. This competition has resulted in other institutions reducing their rates by an annual average of 20 percent—to the benefit of low-income consumers.

Since its establishment in 2011, GC has opened three branches and employs 30 people. The company has plans to open 17 new branches within the next three years.

The World Bank Group Country Partnership Strategy for Georgia recognizes that credit constraints are severe in the country, and the project addresses this concern. MIGA's support for this investment is also aligned with the agency's strategy of supporting investments in countries eligible for concessional lending from the International Development Association.

The project is underwritten through MIGA's Small Investment Program.

ProCredit Group Central Bank Mandatory Reserves Coverage

Key Project Data:

Project name: ProCredit Group Central Bank Mandatory Reserves Coverage
Fiscal year: 2011
Status: Active
Guarantee holder: ProCredit Holding
Investor country: Germany
Sector: Banking
Project Board date: November 23, 2010
Gross exposure: US$9 million
Project type: non-SIP

ProCredit
HOLDING

Project Description

On December 22, 2010, MIGA issued a guarantee of US$9 million to ProCredit Holding (PCH) covering its investment in its subsidiary in Georgia. The coverage is for a period of up to 10 years against the risk of expropriation of funds for mandatory reserves held by the subsidiary in the central bank of its jurisdiction.

This project is part of a master contract that MIGA has issued. PCH is headquartered in Germany and is the parent company of 21 banks (ProCredit group). The ProCredit group is a provider of finance to some 750,000 micro, small, and medium-sized enterprises (MSMEs) in Latin America, Eastern and Central Europe, and Africa. Throughout the world, banks are required to maintain mandatory reserves with the central banks of their respective jurisdictions. The ProCredit group's capital adequacy ratio (CAR) is calculated according to the German Banking Act. Under this act, at a consolidated level, reserves deposited at the various central banks can attract a risk weighting of 100 or even 150 percent, depending on the country. This risk weighting determines the amount of equity required to maintain a specified CAR in accordance with the German Banking Act.

The guarantee issued by MIGA will help PCH obtain capital relief from the CAR requirements. By obtaining MIGA's insurance against the risk of expropriation of funds, the risk weighting for mandatory reserves held at the central bank can be reduced. A lower risk weighting will allow PCH to free up equity currently tied up for CAR maintenance purposes, thereby allowing these funds to be injected into its subsidiary banks. This in turn will allow PCH's emerging market subsidiary banks across its network to increase their lending activities.

MIGA's support will help PCH optimize its capital management across its 21 banks, allowing PCH to direct equity to subsidiaries with the greatest need. These banks will be able to offer additional financial services to MSMEs at a time of macroeconomic challenges. Supporting productive small businesses will help stimulate growth, generate employment, and reduce poverty.

MIGA's support for this project is aligned with the World Bank Group's microfinance strategy, which includes improving the supply of microfinance in large but underserved markets; enhancing deposit capacity by assisting microfinance institutions in savings mobilization; promoting capacity building; creating and shaping markets; and fostering innovation.

MULTILATERAL INVESTMENT GUARANTEE AGENCY

ProCredit Group Central Bank Mandatory Reserves Coverage

Key Project Data:

Project name: ProCredit Group Central Bank Mandatory Reserves Coverage
Fiscal year: 2012
Status: Active
Guarantee holder: ProCredit Holding AG & Co. KGaA
Investor country: Germany
Sector: Banking
Project Board date: December 1, 2011
Gross exposure: US$13.5 million
Project type: non-SIP

Project Description

On December 22, 2011, MIGA issued a guarantee of US$13.5 million to cover an investment by ProCredit Holding AG & Co. KGaA in its subsidiary in Georgia. The coverage is for a period of up to 10 years against the risk of expropriation of funds for mandatory reserves held by the subsidiary in the central bank of its jurisdiction.

MIGA provided coverage of US$9 million under the project in FY11. This additional coverage brings MIGA's exposure under the project to US$22.9 million.

This project is part of a master contract that MIGA has issued. ProCredit Holding AG & Co. KGaA is headquartered in Germany and is the parent company of 21 banks (ProCredit group). The ProCredit group is a provider of finance to some 750,000 MSMEs in Latin America, Eastern and Central Europe, and Africa. Throughout the world, banks are required to maintain mandatory reserves with the central banks of their respective jurisdictions. Currently, the ProCredit group's capital adequacy ratio (CAR) is calculated according to Basel II, but in the future it will also be calculated according to the German Banking Act. Under this act, at a consolidated level, reserves deposited at the various central banks can attract a risk weighting of 100 or even 150 percent, depending on the country. This risk weighting determines the amount of equity required to maintain a specified CAR in accordance with the German Banking Act.

ProCredit Holding AG & Co. KGaA approached MIGA to obtain capital relief from the CAR requirements. By obtaining MIGA's insurance against the risk of expropriation of funds, the risk weighting for mandatory reserves held at the central bank can be reduced. A lower risk weighting would allow ProCredit Holding AG & Co. KGaA to free up equity currently tied up for CAR maintenance purposes, thereby allowing these funds to be injected into its subsidiary banks. This in turn will allow ProCredit Holding AG & Co. KGaA's emerging market subsidiary banks across its network to increase their lending activities.

MIGA's support will allow ProCredit Holding AG & Co. KGaA to direct equity to subsidiaries with the greatest need. The additional services these banks will be able to offer will help stimulate growth, generate employment, and reduce poverty.

MIGA's support for this project is aligned with the World Bank Group's microfinance strategy, which includes improving the supply of microfinance in large but underserved markets; enhancing deposit capacity by assisting microfinance institutions in savings mobilization; promoting capacity building; creating and shaping markets; and fostering innovation.