Ministry of Finance of Georgia

Georgia – The Outlook

April 2018
The Government of Georgia’s long-term strategy seeks sustained and inclusive growth that is based on macroeconomic stability.

- The Government aims to maintain a sound macroeconomic environment, backed by prudent fiscal, monetary and financial policies.
  - Structural reforms to improve governance, encourage employment, and reduce poverty are priorities on the agenda.

- The Authorities are striving to deliver reforms aiming at promoting the formation of a robust and free private sector assisted by an efficient and fully transparent government.
  - Fostering a vibrant, competitive private sector, both on an internal and external levels, is perceived as a top priority for the Georgian authorities.

- In that regard, Georgia set a two-legged long term growth strategy (Georgia 2020 and sectoral development policies) aiming to achieve a profound transformation of the country’s macroeconomic framework. Goals of these two strategic plans are highlighted below.

<table>
<thead>
<tr>
<th>THREE MAIN AXES OF GEORGIA 2020 STRATEGY</th>
</tr>
</thead>
<tbody>
<tr>
<td>PRIVATE SECTOR COMPETITIVENESS</td>
</tr>
<tr>
<td>HUMAN CAPITAL DEVELOPMENT</td>
</tr>
<tr>
<td>ACCESS TO FINANCE</td>
</tr>
</tbody>
</table>

### GA**R**IA 2020: SOCIAL-ECONOMIC DEVELOPMENT STRATEGY OF GEORGIA

- Fostering inclusive economic growth through
  - Reduced unemployment
  - Improved labor and living conditions
  - Establishment of social protection system
  - Human capital development

### SECTORAL DEVELOPMENT POLICIES

- Fostering exports through selected key sectors with high growth and export potential
  - Tourism
  - Hydro Power
  - Agriculture
  - Transport

Source: Ministry of Finance
Four-Point Plan
For Rapid Development of The country

**Education Reform**
- Promotion of Professional Education
- General Education Reform
- Fundamental Reform of Higher Education

**Infrastructure Development**
- Road Infrastructure
- Land Reform
- Expansion of the South Caucasus Pipeline through Azerbaijan and Georgia
- Spatial development

**Improve Business Environment**
- Deposit Insurance
- Pension Reform
- PPP Framework
- Capital Market Reforms
- Insolvency Legislation
- Public Investment Management Reform

**Promoting Open Governance**
- Inclusive Governance – Involvement of the Private Sector in Legislative Process
- Building physical and virtual space for one stop service
- Public Finance Management Reform

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Economic Structure and Trends
Economic Structure and Trends
Reform-driven economic success: story in numbers

GDP: 2008-2009 crisis had temporary impact on steady growth

Rapidly growing GDP per capita – PPP and Nominal

Economic growth comparison across countries, 2017

Broad-based and diversified nominal GDP structure, 2017

Growth rates are from IMF WEO April, 2018
*Indicates estimates for 2017
The Historic Signing of the EU-Georgia Association Agreement is a huge step forward in Georgia’s external relations

The EU-Georgia Association Agenda, signed on 27 June 2014, deepen and strengthen the political, economic and cooperative relations between the EU and Georgia

- The Association Agreement establishes a long-term foundation for future EU-Georgia relations, based on set of jointly agreed priorities for the period 2014-2016, including a Deep and Comprehensive Free Trade Area (“DCFTA”)

- The Association Agreement creates a practical framework for achieving EU-Georgia political association and economic integration
  - The Association Agreement incorporates political elements, reforms to strengthen democratic institutions, cooperation on foreign and security policy, amongst others
    - All axes will have significant positive impacts in strengthening Georgia’s economy, institutions and external perception
    - The agreement with the EU will also help to reduce the perception of geopolitical risk, as cooperation on a security level is also a priority
    - Russia has not sent the same negative signals after Georgia signed EU cooperation agreement, contrary to what it did for Ukraine and Moldova
    - The recent lift of the Russian ban is symbolic of a new trend of commercial relations between Georgia and Russia

- The Association Agenda also includes economic and trade elements, including a dedicated DCFTA chapter and cooperation in a number of sectors such as energy, transport, employment and social policy

- The signing of the Agenda will allow for EU financial support, technical expertise and advice, information sharing, and capacity building, all of which will support Georgia in its economic development

- The signing of the Association Agreement with the EU on June 27th sends a very positive message to the markets, and helps to promote exports to the area from 2014-2015 onwards

- The strengthening of EU-Georgia ties will help to contribute to economic recovery and growth, and will help to better integration of the Georgian economy within the world markets

- The signing of the Agreement proves Georgia’s commitment to sustainable growth, democracy and transparency, will add momentum to the consolidation of Georgia’s stance as an interesting country for investment
Economic Structure and Trends
Liberalized trade, diverse partners, significant and growing network of free trade agreements

- Simple tax and customs policy and user friendly procedures
- No quantitative restrictions or tariff barriers
- Genuine commitment to trade liberalism and openness
- Free trade agreement signed with neighboring countries
- Deep and Comprehensive Free Trade Agreement (DCFTA) with the EU was ratified by many members of the EU
- Georgia has returned to Russian market
- Free trade agreement signed with China

Export Structure by Country 2018
January - March

Import Structure by Country 2018
January - March

Export Structure by Product 2018
January - March

Import Structure by Product 2018
January - March

- Excluding import of medicaments from Canada and Ireland (medicaments for c hepatitis)
- Excluding import of medicaments for c hepatitis

Simple tax and customs policy and user friendly procedures
No quantitative restrictions or tariff barriers
Genuine commitment to trade liberalism and openness
Free trade agreement signed with neighboring countries
Deep and Comprehensive Free Trade Agreement (DCFTA) with the EU was ratified by many members of the EU
Georgia has returned to Russian market
Free trade agreement signed with China
Fiscal Framework and Public Debt Performance
Fiscal Framework and Public Debt Performance

Strong fiscal consolidation path driven by sustainably high revenues and prudent government spending

Fiscal Consolidation

Fiscal Balance as a percentage of GDP

Composition of the 2017 State Budget Outlays
Fiscal Framework and Public Debt Performance
Strategic Infrastructure Projects with Significant Positive Externalities and Strong Spillovers into the Rest of the Economy

- Energy Infrastructure
  - Rehabilitation/construction of transmission line network
  - Rehabilitation/ Construction of HPPs

- Roads Infrastructure
  - Construction of the East-West Highway
  - Rehabilitation of regional road networks, secondary and local roads

- Municipal and Regional Infrastructure
  - Regional Municipal and Urban Infrastructure Development Projects
  - Water supply, sanitation and storm water projects
  - Solid waste management projects

- Agriculture
  - Rehabilitation of irrigation and drainage systems
Debt Indicators are at Comfortable level

- Total Public Debt to Nominal GDP (%)
- External Public Debt to Nominal GDP (%)

Public Debt Ratios are Stable and Annual Repayment Volumes are Easily Affordable

- In 2015, public debt increased to 41.4% of GDP and external public debt to 32.5%. The growth of total public debt to GDP ratio was driven mostly by depreciation of Georgian Lari. In 2016 both public debt and external public debt have increased to 44.4% of GDP and 35.1% of GDP respectively, while for 2017, according the preliminary data, these indicators are: 44.6% and 35.3%.

- Based on the IMF Debt Sustainability Analysis, the public debt ratio would remain sustainable under the most standard shocks.
- Average Weighted Interest Rate (AWIR) on External Public Debt is around 2%.
- The bulk of External Public Debt portfolio is owed to official multilateral and bilateral development partners, mainly on concessional terms 70% of the external public debt portfolio carries fixed interest rate. This keeps Georgia’s external public debt service parameters to a large extent shielded from exogenous interest (base) rate fluctuations and ensures that external public debt service costs remain low and affordable despite global economic uncertainties.
- No refinancing risk exists in the foreseeable future.

Government External Debt Service

External Public Debt Currency Composition
Fiscal Framework and Public Debt Performance
External Public Debt Situation

Affordable Public Debt Stock and Very Low Interest Rate on External Public Debt

- Domestic 21%
- External 79%
- Multilateral 58.9%
- Bilateral 12.6%
- Eurobond 7.6%
- Average Weighted Interest Rate of External Public Debt Portfolio: 2.0%

External Public Debt by Interest Type: Interest Rate Risk Brought to a Minimum

- Fixed 64.5%
- Variable 35.5%
- Domestic 21%
- Multilateral 58.9%
- Bilateral 12.6%
- Eurobond 7.6%
- External 79%

Georgian Sovereign Eurobond 2021

- Price
- Yield

Georgian Sovereign Eurobond 2021

- Spread to UST
Fiscal Framework and Public Debt Performance
Eurobonds Issued by the State Owned Enterprises (As for December, 2016)

Georgian Oil and Gas Company Eurobond 2017

- Price
- Yield

Georgian Railway Eurobond 2022

- Price
- Yield
- Spread to UST

Georgian Oil and Gas Company Eurobond 2017

- Price
- Yield
- Spread to UST

Georgian Railway Eurobond 2022

- Price
- Yield
- Spread to UST

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## Fiscal Framework and Public Debt Performance

### Taxation is Simple, Low, Efficient and Fair

<table>
<thead>
<tr>
<th>Taxes</th>
<th>Rate (%)</th>
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<tbody>
<tr>
<td>VAT</td>
<td>18%</td>
</tr>
<tr>
<td>Income Tax</td>
<td>20%</td>
</tr>
<tr>
<td>Corporate Income Tax</td>
<td>15%</td>
</tr>
<tr>
<td>Dividend &amp; Interest Income Tax</td>
<td>5%</td>
</tr>
</tbody>
</table>

- ✔ No payroll tax or social insurance tax
- ✔ No capital gains tax
- ✔ No wealth tax, inheritance tax or stamp duty
- ✔ Foreign-source income of individuals fully exempted
- ✔ A new CIT model has launched since January 1, 2017, which means that reinvested profit will be free from taxes until distribution of dividends
- ✔ Very strong political commitment to low and simple taxation and improvement of services
- ✔ Significantly streamlined tax and customs administration geared towards provision of maximum comfort to businesses and investors
- ✔ Georgia has double taxation avoidance treaties with 54 countries

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External Sector
External Sector
Current Account funding structure 2017

Goods and Current transfers exclude transactions regarding medicaments for c hepatitis
External Sector

Balance of payments - in sustainable equilibrium

Current Account Deficit (% of Nominal GDP)

FDI Breakdown by Sectors 2017

- Hotels and Restaurants: 9%
- Real Estate: 16%
- Energy: 10%
- Other Sectors: 12%
- Financial Sector: 16%
- Manufacturing: 4%
- Transports and Communications: 28%

Foreign Direct Investment Dynamics

Note: 2006-2008 spikes are due to large privatization
External Sector
Current Account - steadily growing external revenues

Rapidly Growing Contribution of the Tourism Sector, with significant untapped potential

Current transfers (net)

Gross International Reserves

Million USD

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Monetary and Banking Sector
Monetary and Banking Sector

**World Food Prices**

FAO Food Price Index in nominal and real terms

- Nominal
- Real*

**Average Inflation Rate**

Average Inflation Rate
(12 month average over the previous 12 month average, percentage change)

- Jan-11: 4.4%
- Mar-11: 4.8%
- May-11: 4.2%
- Jul-11: 3.4%
- Sep-11: 2.4%
- Nov-11: 2.0%
- Jan-12: 2.1%
- Mar-12: 2.8%
- May-12: 3.6%
- Jul-12: 4.5%
- Sep-12: 6.1%
- Nov-12: 5.8%
- Jan-13: 5.6%
- Mar-13: 5.3%

**Core (net of food and energy)**

**Headline**

**Core (net of food)**

**Annual Inflation Rate**

Annual Inflation Rate in Georgia
(Year-on-Year Change)

- Jan-11: 5.6%
- Mar-11: 4.1%
- May-11: 2.1%
- Jul-11: 1.5%
- Sep-11: 0.1%
- Nov-11: 1.8%
- Jan-12: 3.9%
- Mar-12: 5.5%
- May-12: 6.1%
- Jul-12: 7.1%
- Sep-12: 5.7%
- Nov-12: 6.4%
- Jan-13: 6.7%
- Mar-13: 4.3%
- May-13: 2.8%
- Jul-13: 2.5%
Shift to the inflation targeting mode has provided an enhanced exchange rate flexibility.

Floating exchange rate has increased resilience of the economy. Central Bank participation at the market is limited.

Banks well-capitalized with low NPLs

- Banking system shows resilience with respect to general and bank specific shocks.
- Banks highly capitalized with average Basel I capital adequacy ratio of 23% (15% by local standards) and liquidity ratio of 37%; NPLs are around 3% (by IMF definition) as of February, 2018.
- ER depreciation had only a minor effect on NPLs.
- Borrowings from IFIs represent large share of the banking sector’s non-deposit funding.
- Banking system privately owned since 1995; no restrictions on foreign ownership.
Monetary and Banking Sector
Sound Performance of the Banking Sector

Traditionally High Capital Adequacy Ratio (NBG and Basel I Definition)

High Profitability as Measured by ROE

Total Bank Deposits and Loans – moving in tandem

Sound Non-Deposit Funding Structure as of February-2018
Monetary and Banking Sector
Credit growth at a healthy rate

Assets of the Banking Sector as % of GDP

Commercial Bank Lending, GEL mln

Banking Sector Liquidity Ratios – Ample Liquidity Buffers

Banking Sector Dollarization – on the Downward Path

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International Rankings of Georgia
International Rankings of Georgia
Sovereign Credit Ratings

**STANDARD & POOR’S**

**BB- Stable**
(Affirmed in May 2018)

**FitchRatings**

**BB- Positive**
(Affirmed in March 2018)

**Moody’s INVESTORS SERVICE**

**Ba2 Stable**
(Affirmed in March 2018)
International Rankings of Georgia
Consistently outperforming sovereign peers

Georgia - one of the most liberal labor environments, according to the Heritage Foundation, 2017 (score)

<table>
<thead>
<tr>
<th>Country</th>
<th>Score</th>
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</thead>
<tbody>
<tr>
<td>USA</td>
<td>91.4</td>
</tr>
<tr>
<td>Kazakhstan</td>
<td>86.8</td>
</tr>
<tr>
<td>Georgia</td>
<td>77.3</td>
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<tr>
<td>Czech Republic</td>
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<td>UK</td>
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<td>Azerbaijan</td>
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World Bank Doing Business, 2018: Registering Property

<table>
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<tr>
<th>Country</th>
<th>Rank</th>
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<tbody>
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<td>Ukraine</td>
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<tr>
<td>Serbia</td>
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<td>UK</td>
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<td>USA</td>
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<td>Czech Republic</td>
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<td>Ukraine</td>
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<td>Estonia</td>
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<td>Georgia</td>
<td>3</td>
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<tr>
<td>Lithuania</td>
<td>1</td>
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</table>

World Bank Doing Business, 2018: Starting a Business

<table>
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<th>Rank</th>
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<tbody>
<tr>
<td>Czech Republic</td>
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<td>Georgia</td>
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Crime Index, 2018 (ranking)

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<td>Ukraine</td>
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International Rankings of Georgia
Improved positions

<table>
<thead>
<tr>
<th>WB Doing Business: Ease of Doing Business (ranking from 2006 to 2018)</th>
</tr>
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<tbody>
<tr>
<td>Transparency International: Corruption Perception Index (ranking from 2004 to 2016)</td>
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<tr>
<td>Fraser Institute: Economic Freedom Index (ranking from 2004 to 2017)</td>
</tr>
<tr>
<td>Heritage Foundation: Economic Freedom Index (ranking from 2004 to 2018)</td>
</tr>
</tbody>
</table>
International Rankings of Georgia
Consistently outperforming sovereign peers

Economic Freedom Trend (Economic Freedom Index, 2018)

ECONOMIC FREEDOM SCORE

NOTABLE SUCCESSES:
Fiscal Policy, Regulatory Efficiency, and Trade Freedom

CONCERNS:
Rule of Law

OVERALL SCORE CHANGE SINCE 2014:
+6.5

FREEDOM TREND

Economic Freedom Index, 2018 (Heritage Foundation)

<table>
<thead>
<tr>
<th>Country</th>
<th>Score</th>
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</thead>
<tbody>
<tr>
<td>Ukraine</td>
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