Ministry of Finance of Georgia

General Government Debt Management Strategy 2023-2026

Tbilisi, 2023

Contents

1. Introduction

The General Government Debt Management Strategy document covers the main areas and objectives of government debt management for 2023-2026 years. The strategy reflects the plan of the Government of Georgia, which should ensure the implementation of efficient debt management policies and achieve the objectives of debt management. The document also outlines the measures taken by the Government of Georgia to achieve the goals of the 2022-2025 strategy (Annex).

According to the “Law on Public Debt” of Georgia, borrowing on behalf of Georgia and issuing state guarantees under other loan agreements are undertaken by the Ministry of Finance, with the consent of the Government of Georgia and in consultation with the National Bank of Georgia. The government of Georgia obtains funds from bilateral and multilateral creditors1 as well as from the issuance of government securities on international and domestic financial markets.

The government of Georgia borrows to finance investment projects and to promote government-planned reforms.

It should be noted that according to the World Bank classification, Georgia is currently included in the group of upper middle-income countries[2]. Georgia is expected to have access to concessional funding[3] in the medium term, but in the long run, as the country's economy grows, access to concessional funding will gradually decline. Alongside decreasing access to financial resources from bilateral and multilateral creditors, they will be replaced by local market instruments. At the same time, it is important to increase country awareness in the international capital market for the diversification of access to financial resources.

The Government Debt Management Strategy is a public document that ensures the transparency of the government debt management policy and increases the awareness to creditors, investors, credit rating agencies and society on this issue.

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[1] International Financial Institutions and Partner Countries.

[2] https://data.worldbank.org/country/georgia

[3] Concessional loans have lower interest rates compared to the market rates.

2. Strategy Scope and Objectives

The Government Debt Management Strategy Document covers the debt indicator, which includes:

1. The debt of the Government of Georgia, as defined by the Organic Law of Georgia on Economic Freedom. In particular, it covers a) Public Debt, as defined by the Law of Georgia on Public Debt, except for liabilities undertaken by the National Bank of Georgia, and b) debt undertaken by budgetary organizations, except the debt undertaken from budgetary organizations.
2. Public-private partnership (PPP) liabilities, which is the fair value[4] of the liabilities made within the framework of the basic principles of public-private partnership and the relevant projects of the criteria of PPP provided by "Law of Georgia on Public-Private Partnership".

In 2020, together with the deterioration of the macroeconomic parameters of the country caused by COVID-19, the ratio of the government debt to the gross domestic product (GDP) exceeded the 60% threshold, defined by Georgian legislation[5] and reached 60.2%. As a result, government debt management faced new challenges and new strategic directions were outlined in the government debt management strategy.

In 2021, the macroeconomic indicators improved because of the restoration of tourism and economic recovery. The economy grew by 10.5% in 2021 after a 6.8% contraction in 2020, and the ratio of the consolidated budget deficit to GDP decreased from 9.3% to 6.1%. The ratio of government debt to GDP also improved. By the end of 2021, compared to the end of 2020, the ratio of government debt to GDP decreased from 60.2% to 49.7%, and the ratio of government net debt to GDP decreased from 52.9% to 45.7%. For 2022, as of the end of December, the debt-to-GDP ratio has decreased to 39.5% (45.4% if the exchange rates are maintained at the same level as at the end of 2021), and the net debt-to-GDP ratio – 36.1%. In the same period, the share of debt denominated in local currency (GEL) in the total debt portfolio increased to 25.0%.

As a result, we can conclude that the first goal identified in the previous debt management strategy - reducing the debt to a safe level - has already been achieved, even though this goal seemed difficult to achieve even in the medium term. However, the high dollarization rate

[4] This component is taken into consideration only in the calculation of the Debt-to-GDP ratio.

[5] Organic Law of Georgia on Economic Freedom.

(75.0%) remains to be a significant challenge, which makes government debt significantly vulnerable to exchange rate fluctuations. Another demonstration of this vulnerability is the significant share of exchange rate effects in recent debt reduction. Accordingly, the main task of the medium-term period is to maintain the debt at a safe level, for which the main tools are the government debt portfolio structure improvement and currency risk reduction.

Based on the above, the strategic directions of the government debt management strategy are the following:

1. Maintaining the government net debt to GDP ratio at the safe level;
2. Increasing GEL-denominated debt share in the government debt portfolio;
3. Increasing the focus on development-oriented external loans;
4. Cost and risk optimization of the government total debt portfolio;
5. Government securities market development.

The strategy focuses on the five directions listed above, defines the target indicators for each direction, and sets the plan to achieve them.

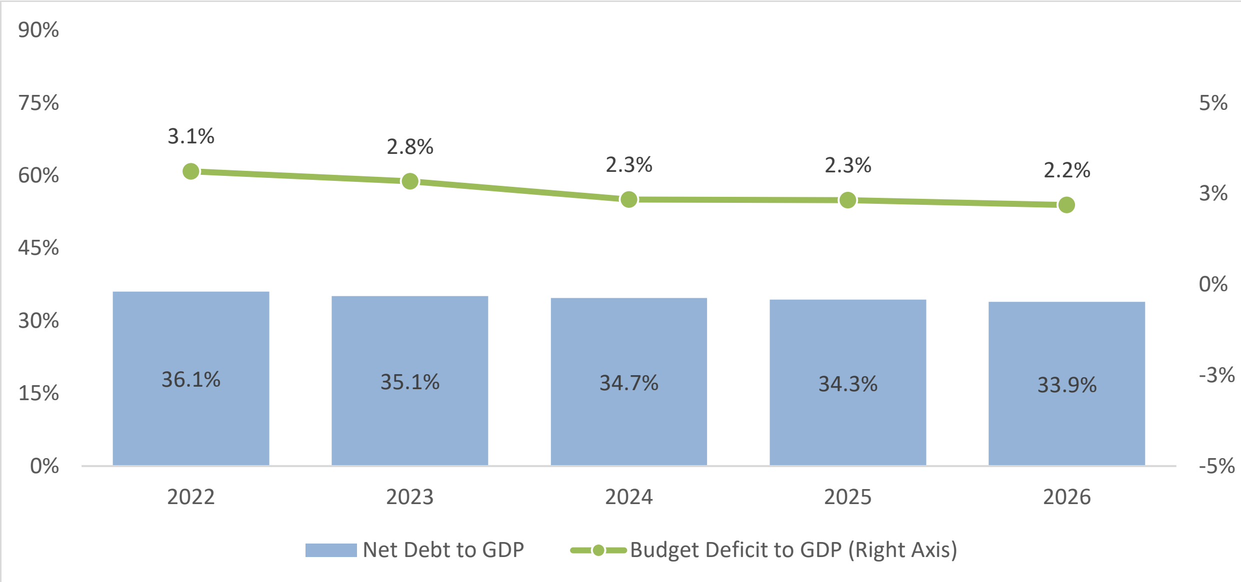
Direction 1. Maintaining the Government Net Debt[6] to GDP Ratio at the safe level

After the economic shock caused by the pandemic, one of the main goals of the government debt management strategy for 2022-2025 was to return the debt-to-GDP ratio to the pre-crisis level. During 2021, the economic upswing had a positive effect on the strengthening of the local currency, which significantly reduced the volume of the government external debt in local currency. As a result, at the end of 2021, the ratio of the government net debt to GDP decreased to 45.7%, which was determined as an intermediate indicator of the government debt management strategy for 2022-2025. According to the preliminary estimate for 2022, the ratio of the government net debt to GDP is 36.1%.

Based on the above, the goal of the first direction of the government debt management strategy for 2023-2026 is <u>to maintain the ratio of the government net debt to GDP within 40%.</u>

[6] Defined as the difference between total government debt and the balance of deposits

Figure 2.1 Projected dynamics of government net debt and budget deficit to GDP ratios for 2022-2026

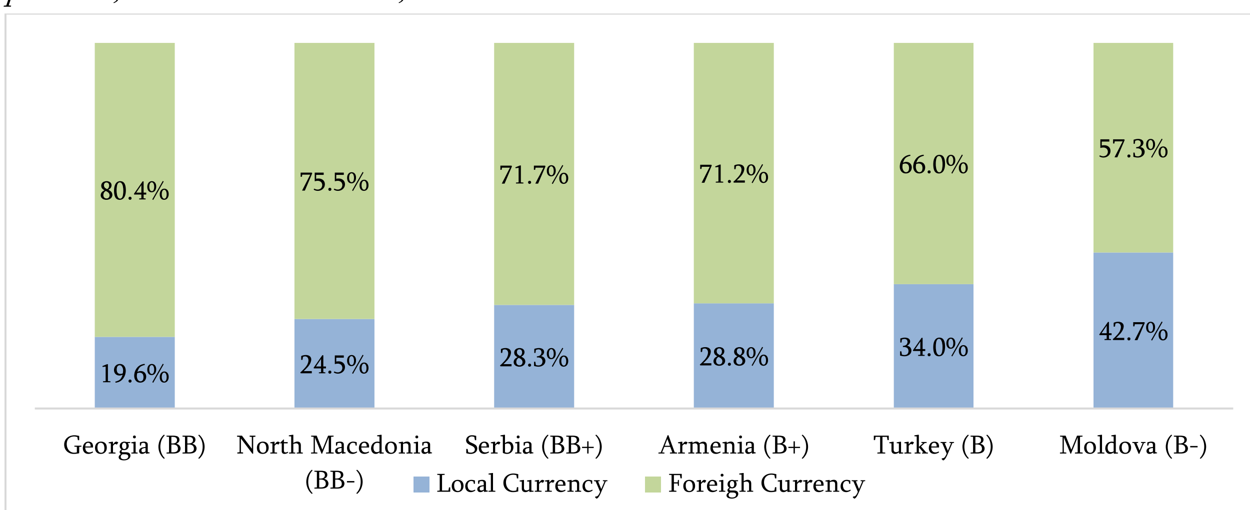


Source: Ministry of Finance of Georgia

Direction 2. Increasing GEL-denominated debt share in the government debt portfolio

The main problem of the Government Debt portfolio is historically large share of foreign currency denominated debt. At the end of 2021, foreign currency denominated debt accounted for 80.4% of the total debt portfolio, which is one of the highest level compared to the regional and other comparable countries (Figure 2.2).

Figure 2.2 The share of local and foreign currency denominated government debt in the total debt portfolio, for different countries, as of the end of 2021



Source: Ministries of Finance of the respective countries

The government debt to GDP ratio is one of the main indicators affecting country's credit rating. However, in this regard, the share of foreign currency denominated debt in the total portfolio is a much more important factor. Most of the developed countries have a high debt to GDP ratio, but due to the local currency denomination of a significant portion of the debt portfolios, the issue of their creditworthiness is not questionable.

According to the methodology applied by credit rating agencies, the share of debt denominated in foreign currency in the government debt portfolio negatively affects the sovereign rating of the country. Thus, the high level of external debt (80.4% as of the end of 2021) in Georgia's government debt portfolio significantly hinders the effectiveness of debt management policy and the ability of Georgia to improve its credit rating.

In recent years, foreign currency denominated loans have had lower interest rates. However, it should be noted that this difference is only optical and a direct comparison of interest rates in different currencies is not valid. There is also a difference between interest rates in global currencies. For example, interest rates on EUR-denominated loans in 2014-2019 were, on average, about 1.5 percentage points lower compared to the interest rates on USD-denominated loans. However, the explicit conclusion that borrowing in EUR is cheaper than borrowing in USD would not be fair, given the difference between the USD/EUR spot and forward exchange rates in the financial markets.

In this direction, the target indicators of the debt management strategy are a) reduction of the external debt to GDP ratio to 30%, and b) reduction of the external debt share in total debt below 70%.

The following net increases in the domestic and external debt are planned to achieve the targets set above:

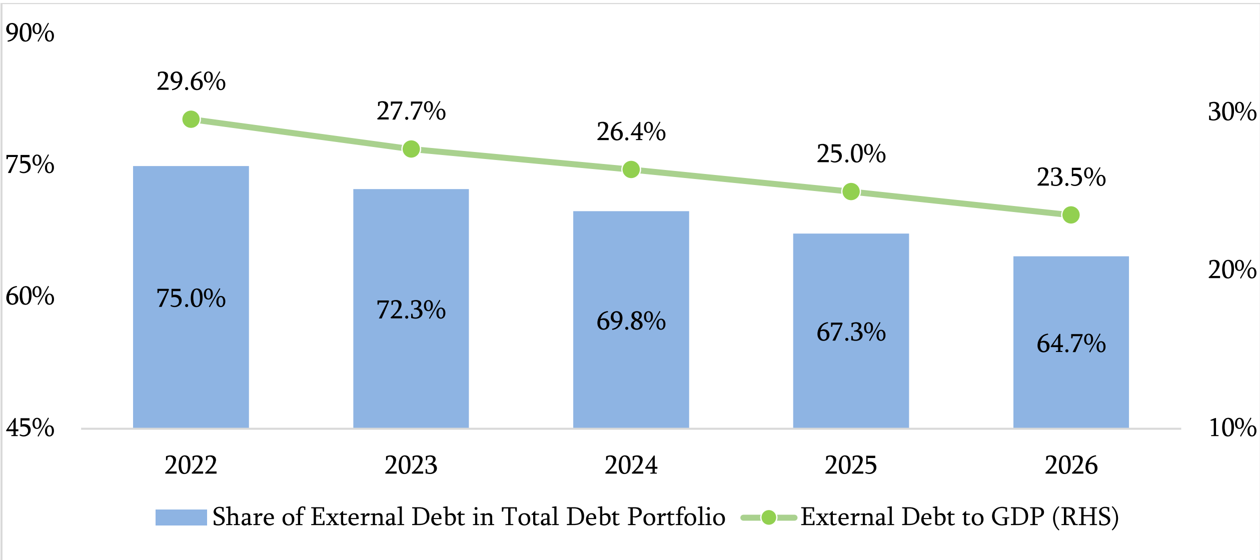
Table 2.1 *Projected annual changes in the domestic and external debt and deposit balance for 2022-2026 (Million GEL)*

	2022	2023	2024	2025	2026
Net increase of treasury securities	1,300	1,400	1,500	1,600	1,700
Net increase of external debt	1,337	1,074	720	600	400
Change of the balance of deposits	113	122	122	-48	-193

Source: *Ministry of Finance of Georgia*

Given the above and the macroeconomic assumptions of the strategy (Table 3.2), the projected dynamics of the share of external debt in the portfolio and the external debt to GDP ratio are presented in the diagram below.

Figure 2.3 *Projected dynamics of external debt share in the total debt portfolio and external debt to GDP ratio for 2022-2026*



Source*: Ministry of Finance of Georgia*

Both targets are ambitious and largely depend on exchange rate fluctuations. However, it is worth noting the fact that by 2026 Georgia's 500 million USD Eurobonds will expire and its refinancing with debt denominated in local currency will allow the country to reduce the share of foreign debt in the total debt portfolio below 65%.

Direction 3. Increasing the Focus on the Development-oriented External Loans

The government of Georgia takes two types of loans from Multilateral and Bilateral creditors: Investment Loans, which are directly connected to certain projects, and reform-supporting loans such as Program Loans.

Due to the domination of foreign currency-denominated loans and debt Larization goal, the strategy‘s objective in this direction represents to be focused on the loans having a high transformational effect. However, in the medium-term foreign currency loans will remain major source of funding gross financing needs.

To achieve this strategic objective, a loan will be taken under the following principles:

For investment loans:

- **Investment loans will be taken only for large and complex[7] projects.** These are projects that require the support of development partners in the project implementation process to achieve a high standard of performance, and which are accompanied by expertise and knowledge sharing. The main benefit of taking an investment loan is not only the attraction of financial resources but also the support that should facilitate the project implementation with the relevant standards. <u>Consequently, the government will not take (submit a new application) investment loans for projects that can be implemented with the same success and efficiency using budget resources;</u>
- **There must be a positive evaluation of project's efficiency under each investment loan**. Investment loans can be initiated only for projects that have passed the pre-assessment stage according to the investment/capital project management methodology[8] and have received a positive decision from the Economic Council[9]. Therefore, it is a necessary precondition for the beneficiary ministry or municipality to have a public investment management system in place to initiate an investment loan. In addition, investment projects that are not subject to review by the rules defined by the investment/capital project management methodology will be selected by the Fiscal Council of the Ministry of Finance of Georgia.
- **On-lending to state-owned enterprises will take place only if the enterprise expresses its readiness to make reforms**. To meet the minimum standard of reform, a state-owned enterprise must express readiness: a) to implement corporate governance practices according to the corporate governance code compatible with the OECD standard approved by the government; and b) to undergo the reform according to the standard agreed with the International Monetary Fund and approved by the Minister of Finance of Georgia;
- **For fully corporatized enterprises, the government will stop on-lending practices**. By doing so, the government will encourage companies to enter the private equity market and attract financial resources independently. It is important that the investments required for the company are not part of the budget process and are independent of

[7] The ministry of finance, gradually, will elaborate measurable indicators to assess project complexity.
[8] Resolution # 65 of the Government of Georgia of February 16, 2023 "On the Approval of the Investment/Capital Project Management Methodology".
[9] The Commission established by the Government of Georgia's resolution, which makes decisions at various stages of an investment project according to the Resolution # 65 of the Government of Georgia of February 16, 2023 "On the Approval of the Investment/Capital Project Management Methodology".

budgetary constraints, which in turn will increase investments in the country's economy; at the same time, the government will convert the loans already lent to companies into marketable instruments. That will increase the liquidity of the instruments issued by companies and create fiscal space.

For program loans:

- **From 2022, external borrowing is available only for significant transformational reforms.** Under such programs, a significant technical assistance is provided to support the implementation of reforms in line with international best practices. It is important to focus on and implement reforms with a highly transformative nature. Program loans will be taken only for significant government reforms, for which the outcome will be assessed in advance and approved by the government. The degree of transformability of the reform will be assessed by the Fiscal Board of the Ministry of Finance of Georgia. For the program loans, an annual limit of $250 million is set.

Direction 4. Cost and Risk Optimization of the Government Total Debt Portfolio

This direction includes refinancing risk management issues for the total debt portfolio and important factors to consider when taking foreign loans.

Refinancing risk. To manage refinancing risk, it is important to maximize the average time to maturity of the portfolio and control the amount of debt maturing within a year relative to total debt in order to avoid peaks in the government debt repayment schedule. Therefore, to manage this risk, it is important that

- **The average time to maturity (ATM) of the government total debt portfolio** should not fall below 5.5 years, while this indicator for the domestic debt portfolio should be maintained at least 3 years;
- **The share of the debt maturing within 1 year** should not exceed 15.0% of the total debt portfolio.

This direction concerning foreign loans means achieving the optimal level of costs and risks associated with a loan when selecting the terms of the loan. To achieve the optimal level, the key parameters considered are the following:

- **Grant Element.** The grant element is the difference between the present value of servicing the loan from development partners and the cost of servicing an alternative loan with market terms. The higher the grant element the more preferable the loan. When selecting the loan terms, priority is given to the option with a higher grant element, which in most cases is achieved by selecting the maximum maturity and grace period;

- **Loan currency**. The long-term analysis of the dynamics of the GEL exchange rate against the main currencies of the government debt portfolio shows that the GEL is less volatile against the EUR. At the same time, due to the ongoing economic and political convergence with the Euro area, an increase in the share of EUR-denominated loans in the external debt portfolio reduces the currency risk. Accordingly, EUR-denominated loans are preferred when choosing a loan currency;
- **Type of interest rate**. Choosing between fixed and variable interest rates implies solving the dilemma of minimizing cost and refinancing risk. For interest rate risk management purposes, it is important that the share of fixed interest rate debt in the external debt portfolio not to fall below 50%.

Direction 5. Treasury Securities Market Development

According to international best practices, the developed local securities market reduces the budget servicing cost on loans and the risks for the medium and long term.

A developed market allows the government to respond quickly to financial needs and to manage cash efficiently.

The developed securities market is a critical factor in achieving the goal of debt portfolio Larization.

The developed treasury securities market is fundamental for the country's capital market. It also plays an important role in shaping and enlarging the investor base. Government securities create a benchmark for other corporate securities, overall allowing corporate issuers to attract investors more effectively.

In this regard, the objectives of government debt management strategy are <u>a) increase of the market liquidity, and b) diversification of the investor base.</u>

To achieve the stated objectives, it is important to take the following steps:

To increase the market liquidity:

- **Increase the securities volume**. The increased volume of securities in circulation increases the investors' interest. Large market size reduces the risks for investors to enter and exit the market;
- **Secondary market development.** A developed secondary market is an important factor for investors. To develop the secondary market, in November 2020, the Ministry of Finance of Georgia, in consultation with the International Monetary Fund and the World Bank, launched a Market Making Pilot Program (MMPP). To bring the mentioned pilot program closer to the fully-fledged system, by the decision of the primary dealers working group, the enhancement of the program began on November 1, 2022, and 2-year benchmark bonds were added to the program along with 5-year benchmark bonds. For further development, from 2023, the MMPP will be further expanded to include additional 10-year treasury bonds originally issued in 2018. In accordance with the readiness of the market, which is assessed by a joint analysis of various criteria (activity in the primary market, turnover in the secondary market, frequency of pricing in the secondary market, the size of the spread, activity of non-bank investors and non-resident investors in the local market), MMPP will be transformed into a fully-fledged primary dealer system;
- **Strong benchmark**. The strength of a benchmark is measured by its volume. In 2018, the Ministry of Finance of Georgia started issuing benchmark bonds with a volume of GEL 240 mln. Currently, the volume of the largest benchmark is GEL 1,064 mln, which is quite a significant achievement. For portfolio improvement, portfolio concentration on strong benchmarks with various maturities is essential. Therefore, it is important to gradually create large benchmarks. It should be noted that the size of the market and the size of the benchmark are one of the main criteria for Georgia to enter the international indices of government securities issued in local currency (JP Morgan GBI-EM, FTSE Frontier Emerging Markets Government Bond Index, etc.). Accordingly, by strengthening the portfolio, it will be possible to meet the mentioned criteria for the medium term.

To diversify the investor base:

- **Increase the share of non-resident investors**. High share of non-resident investors will diversify the investor base, which will reduce the cost of GEL-denominated debt and increase the currency inflows in the country. For this purpose, in 2022, the Ministry of Finance of Georgia developed the Investors Relation Strategy, which will help attract non-resident investors to the country through regular and effective communication with market participants (including periodic roadshows). At the same time, inclusion in the international index will increase the activity of non-resident investors in the local market. By 2025, the target for the share of non-resident investors in treasury securities holders is set at 25%;

- **Create a market for retail investors**. Creating a market for retail investors will help to increase public awareness of financial markets and to improve the level of financial education. The implementation of this is appropriate in the medium term and requires the creation, implementation, and maintenance of an appropriate platform before the creation of the retail investor market.

Considering all the above-mentioned strategic directions, the following tables provide risk indicators and relevant targets:

Table 2.2 *Strategic Targets for 2026*[10]

Types of Risk	Indicators	2021 (Actual)	2022 (Preliminary data)	2026 (Target)
Refinancing Risk	Debt maturing within 1 year (% of total) for total government debt	9.2%	7.4%	Max. 15.0%
	ATM for total government debt	7.9	7.5	Min. 5.5
	ATM for government domestic debt	3.0	2.8	Min 3.0
Interest Rate Risk	Share of fixed-interest external debt in government external debt	54.3%	52.0%	Min 50.0%
Exchange Rate Risk	Share of government domestic debt into total government debt	19.6%	25.0%	Min 30.0%
Solvency Risk	Government net debt to GDP ratio	45.7%	36.1%	Max. 40.0%

[10] These strategic directions assume that there will be no internal or external shocks during the strategy period, which will significantly change the macroeconomic environment and will not apply in the cases provided in Article 2, Paragraph 7 of the Organic Law of Georgia on Economic Freedom.

Table 2.3 Operational Targets by 2026[11]

Indicators	2021 (Actual)	2022 (Preliminary data)	2026 (Target)
Limit on External Program Loans*	-	277 mln USD	250 mln USD
Conversion of on-lent resources into market instruments	-	-	900 mln GEL
PIM-based investment loans*	-	100%	100%
Program loans approved by the Fiscal Board of the Ministry of Finance	-	100%	100%
Participation of non-resident investors in the local market	9.6%	4.2%	25%
Compliance with international indices inclusion requirements	42.8%	52.4%	100%

**-Indicators are based on the operations carried out within a year*

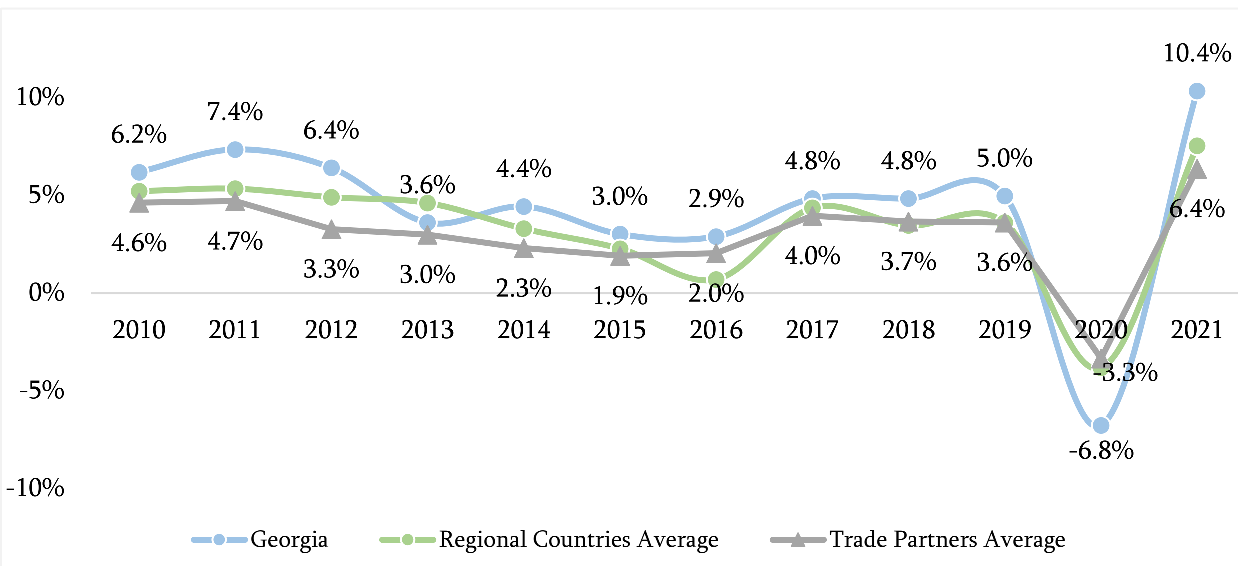
[11] These strategic directions assume that there will be no internal or external shocks during the strategy period, which will significantly change the macroeconomic environment and will not apply in the cases provided for in Article 2, Paragraph 7 of the Organic Law of Georgia on Economic Freedom.

3. Macroeconomic Outlook

The global COVID-19 pandemic at the end of 2019 had a significant negative impact on both global and Georgian macroeconomic indicators. There were both demand-side and supply-side shocks. As a result, economic growth by 2020 was recorded at -6.8%. From the beginning of 2021, the economy began to recover rapidly. Annual economic growth in 2021 amounted to 10.5%, which exceeded by 3.0% to the same indicator for 2019. The main contributor to the recovery was tourism, which in nominal terms accounted for 38% of the 2019. Simultaneously, with the gradual opening of the economy, consumption increased significantly along with the foreign sector, which played an important role in achieving double-digit economic growth.

The high rate of economic recovery was maintained during 2022 as well. Despite global and regional risks caused by Russia's invasion of Ukraine, economic growth in January-October amounted to 10%. Economic growth for the current year is projected to 10%.

Figure 3.1 *Real Economic growth of Georgia, regional and trading partner countries*[12] *for 2010-2021*



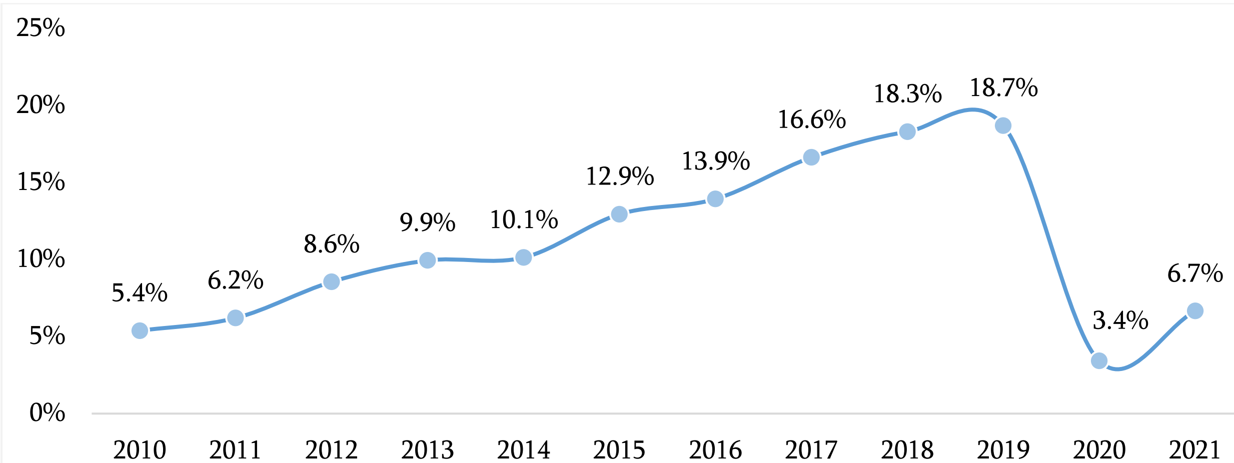
Source*: National Statistics Office of Georgia, International Monetary Fund*

One of the main contributors to economic growth in 2022 was the tourism sector. According to the January-October data, the income received from tourism exceeded the same indicator

[12] Regional Countries: Azerbaijan, Turkey, Russia, Georgia, Armenia.
Trading Partners: : Azerbaijan, USA, Bulgaria, Eurozone, Turkey, Poland, Russia, Armenia, Ukraine, China.

of 2019. The consumption and investments were important contributors to the economic growth. The significant increase in investments is particularly noteworthy.

Figure 3.2 *Tourism Revenues to GDP ratio for 2010-2021, Seasonally Adjusted*

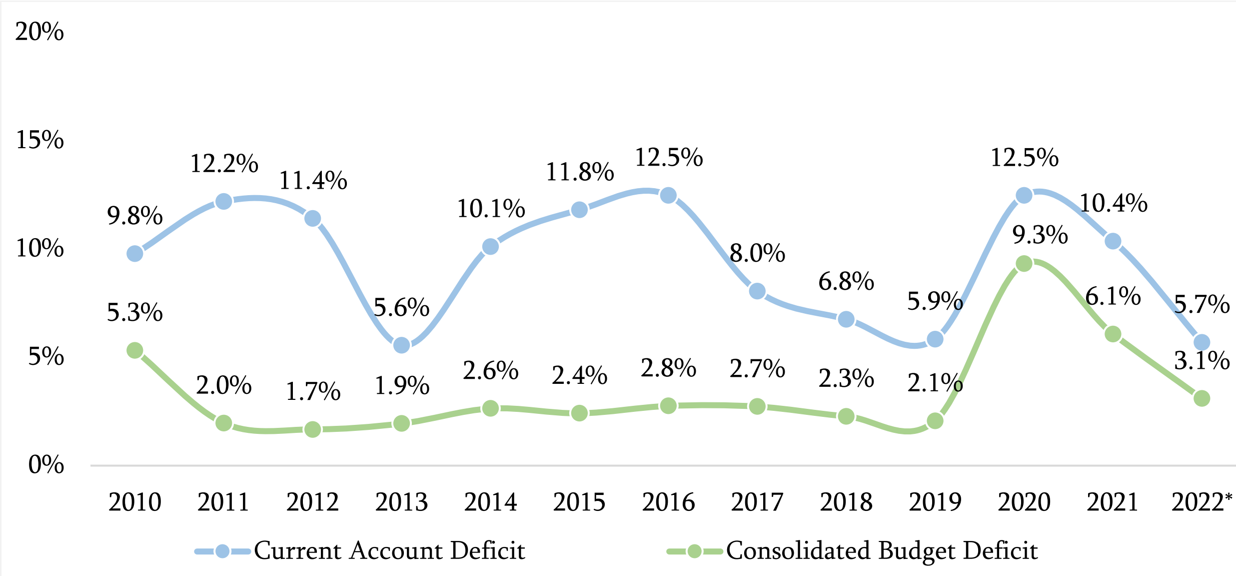


Source: *National Statistics Office of Georgia, National Bank of Georgia, Ministry of Finance of Georgia*

The budget deficit (9.3% of GDP) that increased during the pandemic began to decrease from 2021 and amounted to 6.1% by the end of December. This was partly due to stronger than expected economic activity, as well as the reduction of costs required for pandemic response support measures. The mentioned pace of fiscal consolidation was maintained during 2022. Along with increased economic growth, improved fiscal parameters and effective distribution of expenditures aimed at responding to existing challenges made it possible to sharply reduce the deficit. By the end of 2022, the deficit is expected to decrease to 3.1%.

In 2021, the current account deficit (10.4%) has improved compared to 12.5% in 2020. The improvement came from the tourism recovery, a significant increase in remittances, and a sharp improvement in the trade balance. Against the background of substantial improvements in the same indicators, it is expected that by 2022 the current account deficit will significantly decrease and return to the pre-pandemic level.

Figure 3.3 *Consolidated budget deficit and current account deficit to GDP ratios for 2010-2022*



Source: *National Statistics Office of Georgia, National Bank of Georgia*

The disruption of global supply channels during the pandemic had a significant impact on the rise in global inflation. On the one hand, global inflation and, on the other hand, the domestic demand shock had a negative impact on the local inflation. From the beginning of 2021, inflation continued to grow and maintained at a double-digit rate, the mentioned trend continued in 2022 as well. While the increase in inflationary pressure in 2021 was caused by global events, such as the breakdown of supply chains and the increase in the prices of raw materials (oil and gas) on the international market, by 2022 these factors were further exacerbated by the deteriorating environment due to the Russia-Ukraine war. According to the National Bank of Georgia's projections, inflation will remain above the target level in the short term, and will return to the target level of 3% in the medium term.

As for Georgia's sovereign ratings, according to the rating agency Fitch, Georgia's rating improved from "BB-" stable to "BB" stable in 2017-2019, which was mainly due to high-quality macroeconomic management, high economic growth and low government debt; In addition, the current account deficit and fiscal sustainability significantly improved during the mentioned period. In their reports, international rating agencies often highlighted the reforms implemented in the country and reduced vulnerabilities, which had a positive impact on the country's sovereign ratings. Similar to Fitch, in 2019 Standard & Poor's (S&P) also upgraded Georgia's sovereign rating to "BB" stable. According to S&P, the improvement of the credit rating, despite the deterioration of external factors, was associated with the relatively high growth of the Georgian economy in recent years. In 2020, Fitch downgraded Georgia's credit rating outlook, however, in 2021, due to higher-than-expected economic growth and improved macroeconomic parameters, it upgraded the rating again at "BB" stable. However, in 2021, Standard & Poor's downgraded the country's sovereign rating to "BB" negative, which was mainly due to the sanctions imposed on Russia as a result of the Russia-Ukraine war and Georgia's vulnerability to the Russian economy. In 2022, S&P upgraded this rating again to "BB" stable level. As for the rating agency Moody's, during the pandemic, Georgia's rating was kept unchanged, at "Ba2" stable. However, after Russia's invasion of Ukraine and the sanctions imposed on Russia, due to the high dependence on the Russian economy and the risks arising from it, Moody's changed Georgia’s sovereign rating from "Ba2" stable to "Ba2" negative.

Table 3.1 *Sovereign credit ratings of Georgia assessed by rating agencies y-o-y*

Credit Rating Agencies	2018	2019	2020	2021	2022
Fitch	BB- Positive	BB Stable	BB Negative	BB Stable	BB Stable
Standard & Poor’s	BB- Stable	BB Stable	BB Stable	BB Negative	BB Stable
Moody’s	Ba2 Stable	Ba2 Stable	Ba2 Stable	Ba2 Stable	Ba2 Negative

Source: *Ministry of Finance of Georgia*

Target indicators of Government Debt Management Strategy for the medium and long term are based on the following fiscal and macroeconomic assumptions:

Table 3.2 Projected data of macroeconomic indicators for 2022-2026

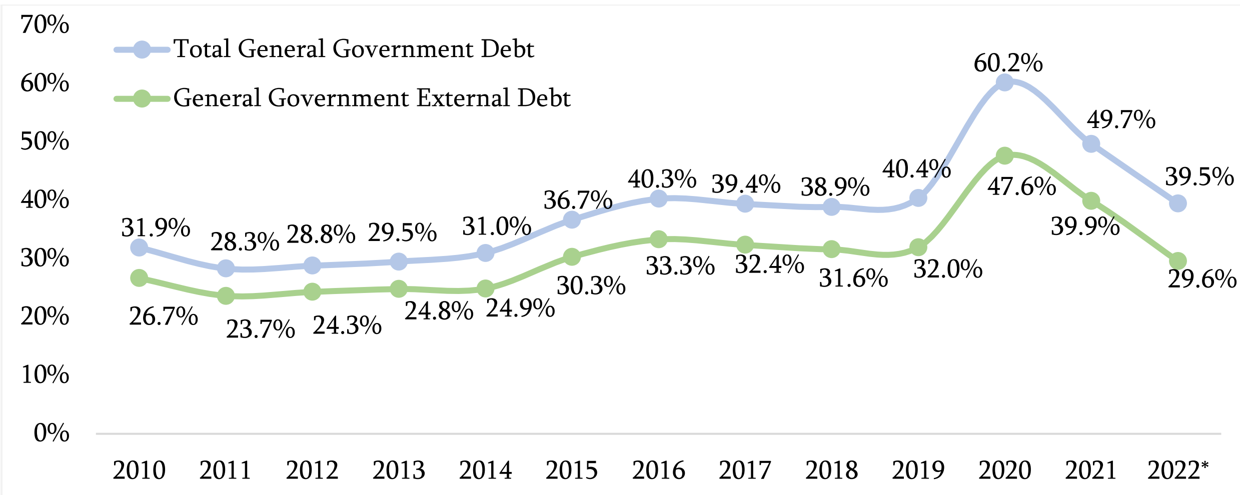
Indicators (mln GEL)	2022	2023	2024	2025	2026
Common Budget Revenues	19,217	20,805	22,076	23,794	25,704
Common Budget Expenses	15,743	17,416	18,364	19,832	21,357
Net growth of Non-Financial Assets	5,485	5,770	5,610	6,010	6,440
Net growth of Financial Assets	240	-120	120	120	120
Modified Budget	-2,251	-2,261	-2,018	-2,168	-2,213
Gross Financing Needs	-4,786	-4,811	-5,248	-5,168	-6,882
Domestic	1,200	1,300	1,420	1,520	1,620
Borrowing	2,730	2,680	3,270	3,020	3,290
Redemption	-1,530	-1,380	-1,850	-1,500	-1,670
External	1,337	1,074	720	600	400
Borrowing	2,342	2,244	2,100	2,100	3,400
Redemption	-1,005	-1,170	-1,380	-1,500	-3,000
Change of the Balance of Deposits	286	113	122	-48	-193
Balance of Deposits[13]	2,479	2,592	2,714	2,666	2,473
Government Gross Debt	28,538	30,539	32,679	34,799	36,819
Government Net Debt	26,059	27,947	29,965	31,133	34,346
Nominal GDP	72,276	79,685	86,343	93,558	101,183
Real GDP Growth	10.0%	5.0%	5.2%	5.2%	5.0%
Change in GDP Deflator	9.5%	5.0%	3.0%	3.0%	3.0%
Percent to GDP					
Modified Deficit	-3.1%	-2.8%	-2.3%	-2.3%	-2.2%
Gross Financing Needs	-6.6%	-6.0%	-5.6%	-6.2%	-7.2%
Balance of Deposits	3.4%	3.3%	3.1%	2.8%	2.4%
Government Gross Debt	39.5%	38.3%	37.8%	37.2%	36.4%
Government Net Debt	36.1%	35.1%	34.7%	34.3%	33.9%

[13] The balance for the forecast years is adjusted for the change in the balance on the consolidated budget deposits.

4. General Government Debt Portfolio Description

By the end of 2021, Georgia's general government debt amounted to 29,812[14] mln GEL. The mentioned figure for 2022 is 28,538 million GEL of which foreign currency denominated debt amounts to 21,392 million GEL, and local currency denominated debt amounts to 7,146[15] million GEL. As a result of the economic recovery in 2021-2022, the debt to GDP ratio, according to the preliminary estimate of 2022, is 39.5%, of which foreign currency denominated debt to GDP ratio constitutes 29.6%.

Figure 4.1 *General Government Debt Dynamics (% of GDP)[16] for 2010-2022*



Source: *Ministry of Finance of Georgia*

As of the end of 2021, 80.4% of the government total debt portfolio was denominated in foreign currency. As of the end of 2022, this indicator decreases to 75.0%. Despite the downward trend, the above-mentioned indicator remains at a high level.

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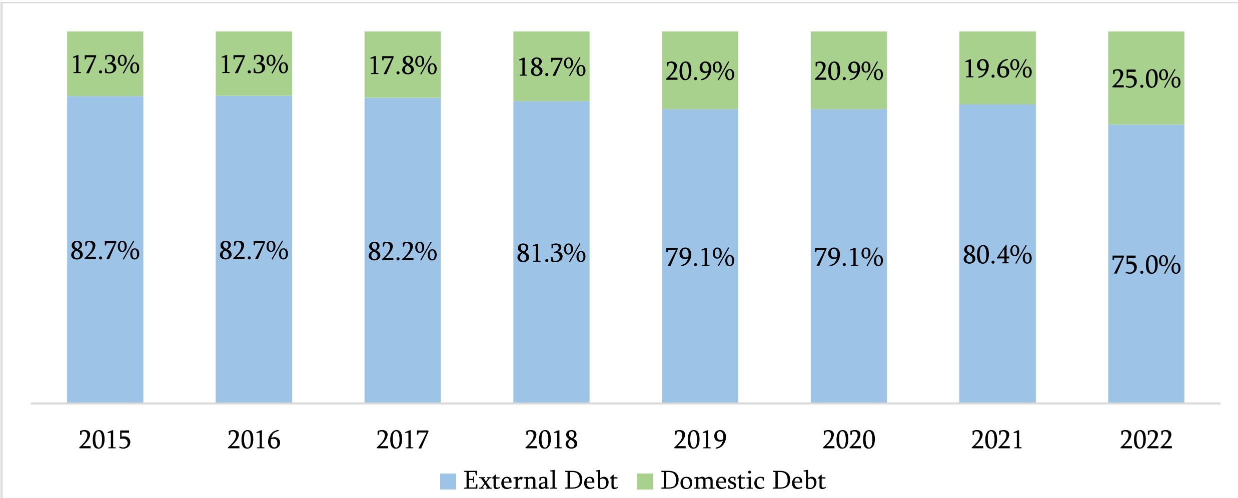
[14] The strategy document does not include the so called Domestic "Legacy Debt"; includes debt of budgetary organizations, except the debt taken from budgetary organizations.

[15] Includes debt of budgetary organizations, except the debt taken from the budgetary organizations.

[16] The general government debt to GDP ratio, including the PPP liabilities, amounted to 50.3% by the end of 2021 (Amount of the PPP liabilities was 384.6 mln GEL by the end of 2021).

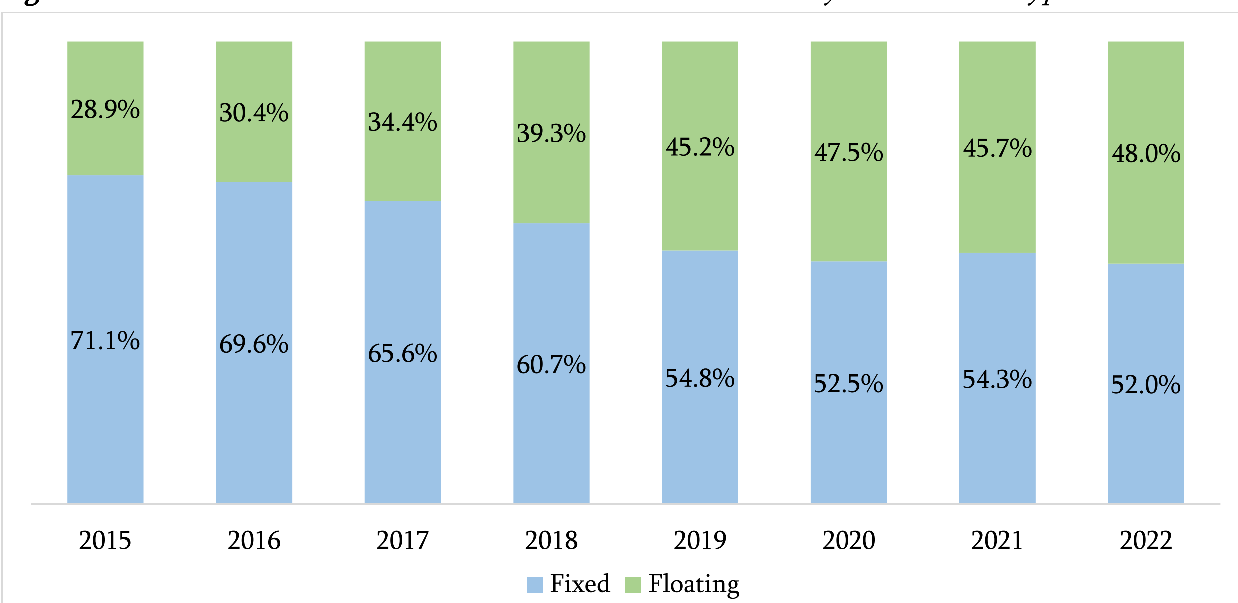
Figure 4.2 General Government Debt Portfolio Structure for 2015-2022



Source: Ministry of Finance of Georgia

By the end of 2022, 64.0% of the government debt portfolio bears a fixed interest rate. For the government foreign debt portfolio, the mentioned indicator is 52.0%.

Figure 4.3 General Government External Debt Portfolio Structure by Interest Rate Type for 2015-2022

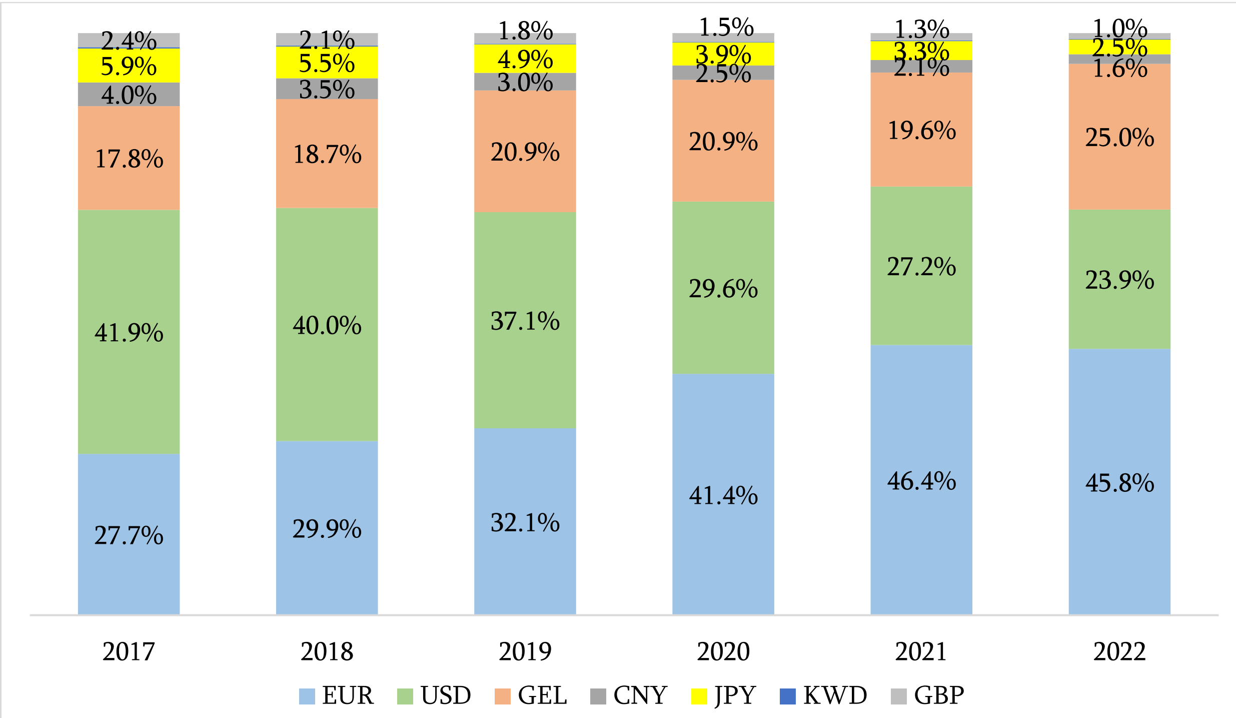


Source: Ministry of Finance of Georgia

By the end of 2022, according to preliminary estimates, 23.9% of the government debt portfolio is denominated in USD. It is notable, that the share of the USD denominated debt has been declining due to the increase in the shares of debt denominated in EUR (45.8%) and GEL

(25.0%). The remaining 5.3% of the portfolio is denominated in other currencies - JPY, KWD, CNY and GBP.

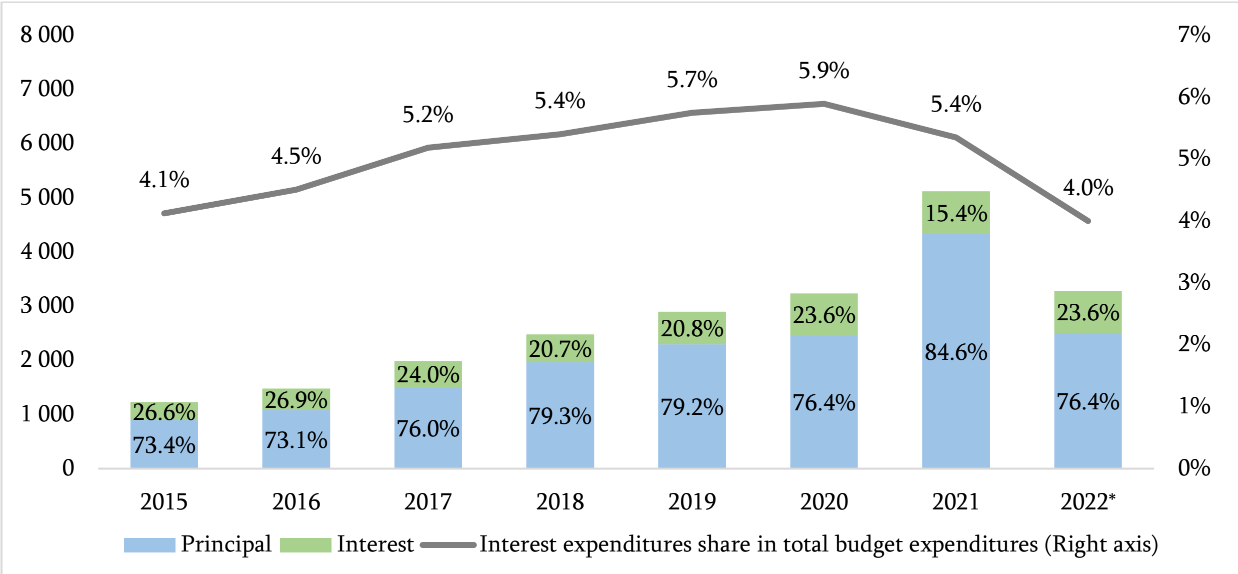
Figure 4.4 *Currency Composition of the General Government Debt Portfolio for 2015-2022*



Source: *Ministry of Finance of Georgia*

While taking new loans, debt portfolio service schedule (based on stock) is taken into account. The loans comprising the external debt portfolio usually have long-term repayment schedule and long grace period, which ensures the equal distribution of debt service, and therefore, does not impose the significant pressure on budgetary expenditures, neither the expenses are concentrated on short-term period. By the end of 2022, the interest rate expenditures of the general government debt portfolio amounted to 4% of the total budget expenditures.

Figure 4.5 *General Government Debt Service for 2015-2022 (mln GEL)*



Source*: Ministry of Finance of Georgia, National Statistics Office of Georgia*

According to preliminary estimates for 2022, the weighted average interest rate of the government debt portfolio increased in 2022 compared to 2021 and amounted to 3.97%. This indicator is 9.20% for the domestic debt portfolio, and 2.23% for the foreign debt portfolio. The increase in the weighted average interest rates of the government debt portfolio is mainly due to the sharp increase in the interest rates on the local and international markets. The weighted average interest rate on the newly borrowed local currency debt throughout the last year amounted to 9.76%, the same indicator for foreign currency denominated debt amounted to 2.72%.

Table 4.1 Weighted Average Interest Rates on the General Government Domestic and External Debt Portfolios

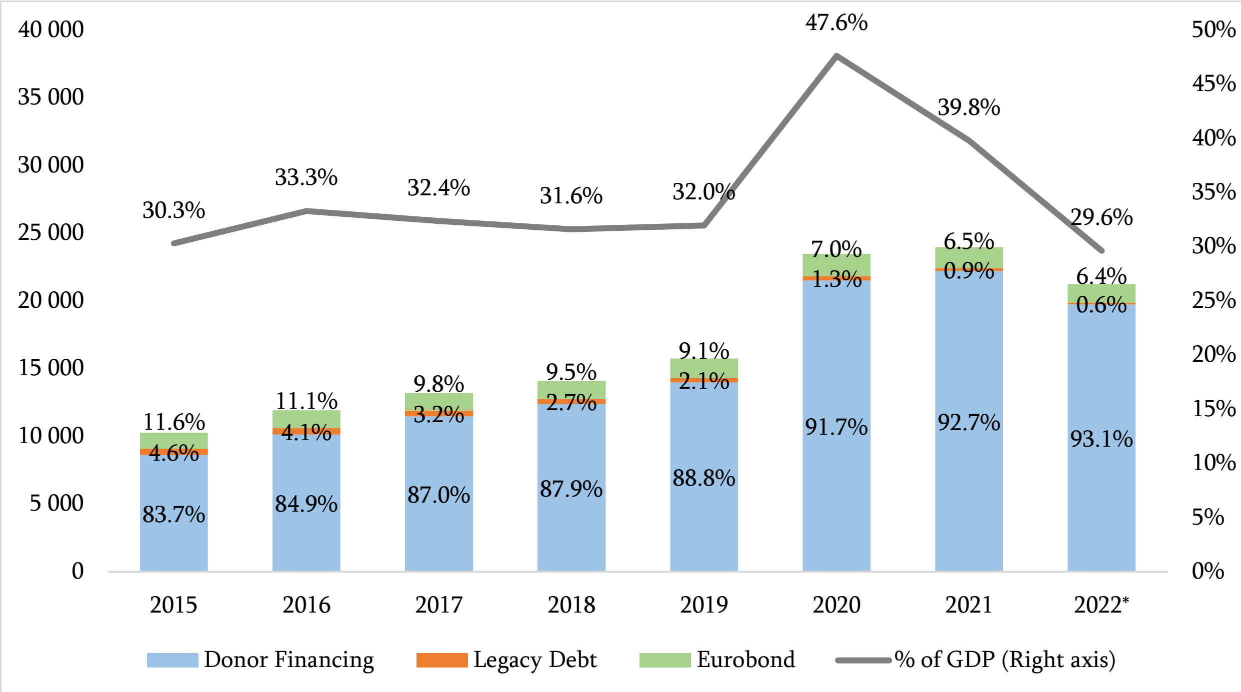
	Weighted Average Interest Rate of the Portfolio		Weighted Average Interest Rate of Last Year	
	2021	2022*	2021	2022*
Domestic Debt	**8.83%**	**9.20%**	**8.91%**	**9.76%**
6m T-Bills	9.39%	10.17%	9.06%	10.34%
12m T-Bills	9.03%	9.99%	9.03%	9.99%
2y T-Bonds	8.76%	9.62%	8.94%	9.84%
5y T-Bonds	8.49%	8.86%	9.09%	9.69%
10y T-Bonds	9.56%	9.48%	8.85%	9.29%
Government Bonds	8.64%	9.04%	8.14%	9.54%
External Debt	**0.95%**	**2.23%**	**1.56%**	**2.72%**
Donor Financing	0.81%	2.18%	0.36%	2.72%
Legacy Debt	3.54%	3.60%	-	-
Eurobond	2.75%	2.75%	2.75%	-

***Source**: Ministry of Finance of Georgia*

By the end of 2022, according to preliminary estimates, 93.1% of the government external debt is composed of the funds attracted from the multilateral and bilateral creditors. Most of these loans have concessional terms. Eurobond represents 6.4% of the foreign debt portfolio, while the remaining 0.6% is “Legacy Debt”[17], which will be fully repaid by 2025.

[17] Existing and other restructured loans to the former republics of the USSR.

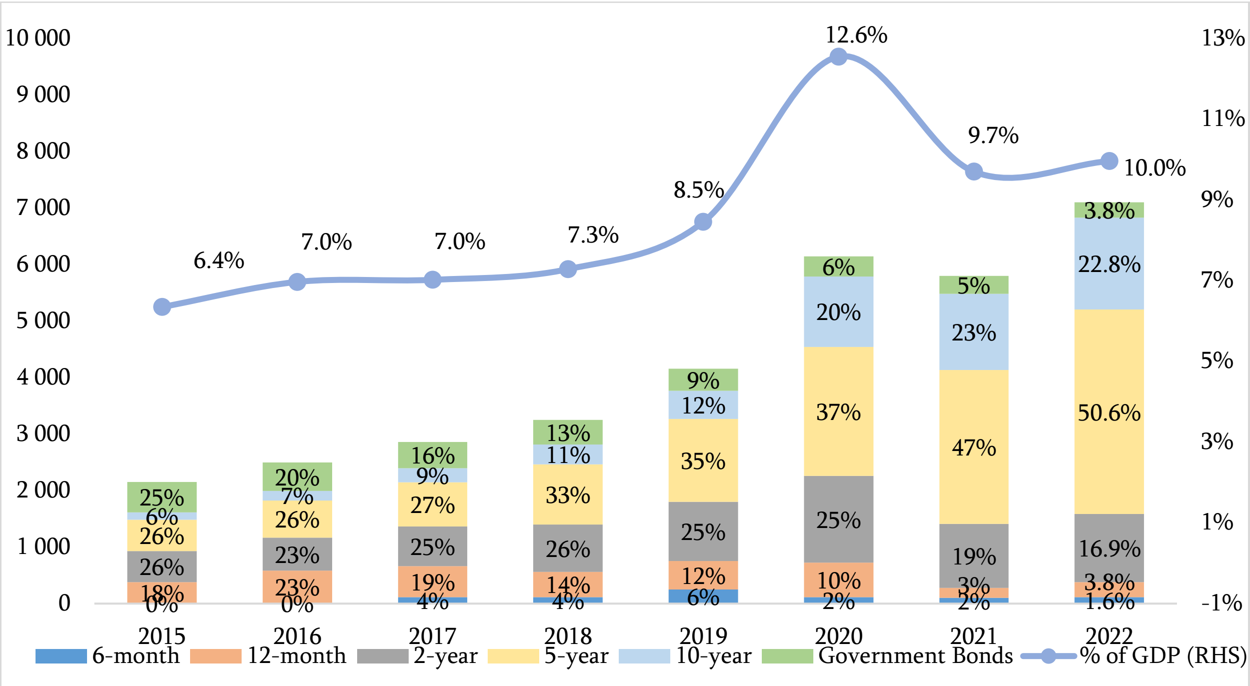
Figure 4.6 General Government External Debt Structure for 2015-2022 (mln GEL)



***Source:** Ministry of Finance of Georgia*

The general government domestic debt has increasing trend in recent years. By the end of 2021, domestic debt to GDP ratio amounted to 9.7%, and according to the preliminary data for 2022, it is 10.0%. Significant portion of domestic debt constitutes of treasury bonds: 2-year, 5-year and 10-year treasury securities issued on behalf of the government. Considering the current issuance plan until the end of 2022, treasury bonds hold 90.8% of the portfolio. As for treasury bills, which include 6 and 12 month securities, the mentioned indicator represents 5.4% of the portfolio. The remaining share of the domestic debt portfolio, 3.8%, is represented by government bonds (the government debt to the National Bank).

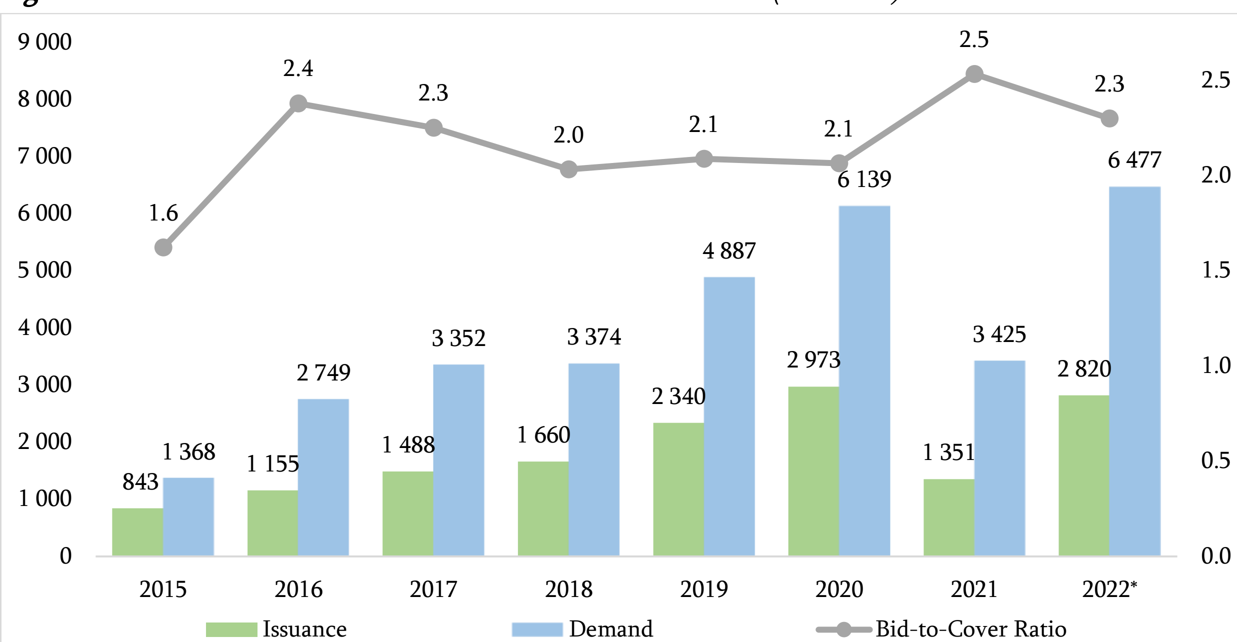
Figure 4.7 General Government Domestic Debt Portfolio Structure for 2015-2022



Source: Ministry of Finance of Georgia, National Statistics Office of Georgia

Despite the increasing issuance of government securities, demand significantly exceeds issue sizes. Bid-to-cover ratio amounted to 2.5 for 2021 and 2.3 for 2022.

Figure 4.8 Domestic Debt Issuance and Demand for 2015-2022 (mln GEL)



Source: Ministry of Finance of Georgia

Annex

The following key actions have been taken to achieve the objectives defined under General Government Debt Management Strategy 2022-2025:

- **Enhancement of Primary Dealers Pilot Program:** The Primary Dealers Pilot Program, which included 5-year Treasuries, was expanded to include 2-year Treasuries in November 2022. Also, from January 1, 2023, 10-year treasury bonds originally issued in January 2018 will be added to the program;
- **Development of investor relations strategy**: In 2022, the Ministry of Finance of Georgia developed an investor relations strategy, which aims to create a framework for regular communication with investors. The document includes the main principles of relations with investors and measures to be implemented in order to improve investors relations;
- **Monthly government debt report**: From July 2022, in order to improve relations with investors and increase transparency, the Ministry of Finance of Georgia started publishing the monthly government debt report;
- **Strong benchmark**: The size of the benchmark is one of the main criteria for Georgia to be included in the international index. For this purpose, it is planned to increase the volumes of benchmark securities. Based on the above, from November 2022, the Ministry of Finance of Georgia has reopened the issuance of the 10-year benchmark bond, which was originally issued in January 2018;
- **Increase in supply, transparency and predictability of securities:** From 2022, the Ministry of Finance of Georgia started publishing the aggregated indicators of the annual plan for the issuance of securities.
- **Establishment of retail securities market**: International best practices are being studied for creating a retail securities market. By 2023, with the support of international organizations, several visits to countries with successful practices are planned to gain experience and develop retail securities market domestically.