The World Bank Group - Georgia Partnership Program Snapshot

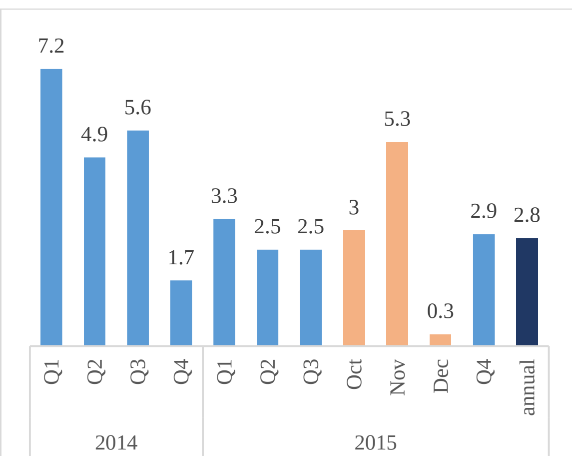
April 2016

RECENT ECONOMIC AND SECTORAL DEVELOPMENTS

Growth and External Performance

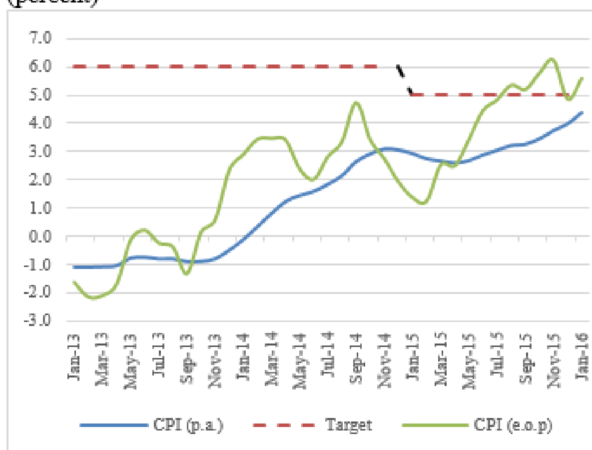
Growth decelerated to 2.8 percent in 2015, largely because of a weaker external environment. The recession in Russia and slower growth in other trading partners impacted Georgia through lower exports and reduced remittances, particularly from Russia and Greece. The tradable sector suffered the most, as industrial production contracted by 1.2 percent in 2015. As a result, growth moderated from 4.8 percent in 2014 to 2.8 percent in 2015. Despite the overall slowdown, growth was supported by non-tradables such as construction, which grew at 16 percent, and services (growth of 3 percent). Foreign direct investment (FDI) and tourism proceeds remained stable, which also helped increase employment by 20 percent and real wages by 4.7 percent in 2015. The largest increases in wages were in construction, real estate, and health.

Figure 1. Quarterly GDP Growth (percent change)



Lower exports and remittances put strong depreciation pressure on the exchange rate, which was allowed by the National Bank of Georgia (NBG) to float and absorb the shock. The almost 30 percent depreciation since December 2014 has raised inflation expectations, leading the NBG to increase the policy rate from 4 percent in February 2015 to 8 percent in December. The tightening of monetary policy, together with lower oil prices, helped contain inflation during 2015 to 4.9 percent. The floating exchange rate, limited interventions, and independence of the NBG helped to achieve both nominal and real exchange rate realignment and maintain scarce international reserves. Prudent financial sector supervision ensured the stability of the banking sector and the low level of nonperforming loans (NPLs) at 2.3 percent in 2015. At the same time, the large total external debt of over 100 percent of GDP and the high rate of dollarization of 65 percent are sources of vulnerability.

Figure 2. Inflation (y-o-y) and Policy Rate
(percent)



Sources: Geostat

Fiscal Developments

In an environment of weak external demand, the Government supported growth through a 17 percent increase in capital expenditures. This was coupled with a 9 percent increase in current spending, raising the fiscal deficit to 3.8 percent of GDP in 2015 compared to a budgeted deficit of 3 percent. The deviation was mainly driven by an overrun in current spending on health care, wages, goods, and services and also on-lending to municipalities.

In 2016, the Government is planning to adopt the Estonian tax model in the area of corporate income taxes. The authorities' rationale for this change is to encourage the reinvestment of corporate profits, which will boost growth. However, the impact on growth will come with a lag, while tax revenues will go down immediately. Under this scenario, and with the increasing health and social expenditures, containing the fiscal deficit at 3 percent of GDP in 2016 will require cuts in other expenditures. The authorities would therefore need to undertake major cuts in current expenses in order to maintain the current level of capital expenditures.

Public debt has increased because of the valuation effects from the exchange rate depreciation as well as higher borrowing, with a wider fiscal deficit. The lari depreciated by 29 percent against the U.S. dollar during 2015 in nominal terms. With 78 percent of public debt denominated in U.S. dollars, the stock of public debt increased to 42 percent of GDP in 2015, up from 36 percent in 2014.

Medium-Term Outlook

Growth is projected to remain at a modest 3 percent in 2016, with parliamentary elections scheduled for October 2016 and the weakness in external markets likely to persist. The spillover effects from the Russia-Ukraine crisis and the slowdown in Georgia's other main trading partners are likely to result in a current account deficit of 10 percent of GDP in 2016. Greater policy certainty in the post-election environment, some recovery in external markets, and continued FDI inflows (particularly the British Petroleum pipeline expansion, the upcoming Anaklia deep-sea port, and hydropower plants) are likely to raise growth to 4.5 percent in 2017 and 5 percent in 2018. The current account deficit is also expected to go down gradually in the coming years. Political and policy uncertainty emanating from the October parliamentary elections, along with the existing geopolitical risks, could weaken consumer and business confidence and dampen the pace of reforms. However, a rapid return to normal is likely, as both the ruling and opposition parties are equally committed to Georgia's European integration aspirations and business friendly policies.

The fiscal deficit is likely to increase in the short to medium term with the expected decline in revenues. This is because of the adoption of the Estonian tax model, which will replace the corporate profit tax with a dividend tax. This measure could boost growth in the medium term, but tax revenues will decline immediately. In addition, pensions will rise by 12.5 percent in July 2016 and teachers' salaries will be increased in April. Thus, total expenditures are expected to stay above 30 percent of GDP in 2016, and the fiscal deficit is projected to increase to 4–5 percent of GDP, assuming that the Estonian tax model is adopted. The decline in tax revenues is likely to persist over the medium term, which will keep the deficit level elevated compared to the past. The stock of public debt is likely to increase to 45 percent of GDP in 2016.

Low growth, a large current account deficit, high external debt, an increasing fiscal deficit, elevated rural poverty, and continuing high unemployment are the main risks to the economy and to poverty reduction. With low domestic savings, Georgia relies on foreign savings to finance its investments, which has led to persistently high current account deficits that have raised the external debt to over 100 percent of GDP. Lower exports and remittances, a high level of dollarization at 65 percent, and the low level of reserves (three months of imports) have heightened foreign exchange risks. Mitigating factors include the floating exchange rate, market access, and support by international financial institutions (IFIs). Fiscal risks stem from the reduction in corporate tax revenues, further increases in recurrent spending, and contingent liabilities arising from the power purchase agreements. The Government needs to manage aggregate demand through lower deficits and put in place an adequate mechanism to monitor and reduce contingent liabilities. The contribution of social benefits to poverty reduction would need to be better balanced with net job creation and labor participation.

Public Financial Management (PFM)

Georgia has significantly advanced in public sector management practices. The success stories of public financial management (PFM) 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—are all 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. The Ministry of Finance has initiated a 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 was undertaken through integrating them into the Public Financial Management Information System (PFMIS), which helps to monitor and manage their cash balances throughout the budget cycle. It also helps to promote better management of intergovernmental transfers.

In October 2015, the Parliament approved a new law on the civil service. The objective of the law (in line with the framework) is to create a merit-based system that protects the rights of civil servants, promotes ethical and non-corrupt behavior, is transparent in its hiring and promotion, outlines clear disciplinary processes, and promotes public confidence in the civil service. The time line for the new law was expedited as it is a prerequisite for making progress on the visa liberalization scheme with the European Union (EU). Although it is essentially a framework law and does not explicitly incorporate many key provisions, checks and balances are envisaged in the form of secondary legislation and through the Law on Conflict of Interest. Many of the details are expected to be firmed up in this secondary legislation. Earlier in 2015, the Government adopted a comprehensive framework for civil service reform, which formed the basis for the new civil service law. The current structure of the public sector was formed as a result of significant changes made since 2004, with the conversion of many civil service institutions into LEPLs and NPLEs. These changes were not adequately reflected in the existing law and made it difficult to ensure uniformity in hiring policies, career development, remuneration packages, and the rights and responsibilities of the employees. The status of the public servant was also only vaguely defined in the old law.

There are increased fiscal risks from state-owned enterprises (SOEs) and emerging social and pension obligations. For the purpose of monitoring the fiscal risks emanating from SOEs, the Government is creating a detailed financial database of large SOEs. The Ministry of Finance has made a list of all the SOEs operating in Georgia, which yielded a total of 1,853 entities. The ministry focused on those that had a turnover of over GEL 200,000 or a total wage bill of more than GEL 15,000 annually. This cutoff yielded a list of 386 SOEs, which constituted 98 percent of the total turnover of these entities. The ultimate objective of this data collection and analysis is to provide the Parliament with an aggregated picture of these companies as part of the budget preparation and execution process.

Improving the public investment management (PIM) agenda is critical to closing the infrastructure gap to accelerate and sustain economic growth, as fiscal space for public investment is shrinking. In this context, the Government is committed to adopting and implementing a framework for systematic capital investment identification, preparation, appraisal, and selection, for both the central and the local governments. This framework will include guidelines as well as a manual. The key ministries that will be impacted by the new framework include the Ministry of Regional Development and Infrastructure, the Ministry of Energy, and the Ministry of Education and Science. Improving the performance of the procurement system is another of the Government's priorities, and to that end, a Procurement Performance Assessment study was recently initiated.

The World Bank's ongoing support to the public administration sector in Georgia includes a series of Development Policy Operations (DPOs), a Programmatic PFM and Governance task that covers the FY15–17 period, a grant-funded project on Strengthening Accountability and the Fiduciary Environment (SAFE), as well as another grant-funded project on the Supreme Audit Institution Capacity Development Fund (SAICDF).

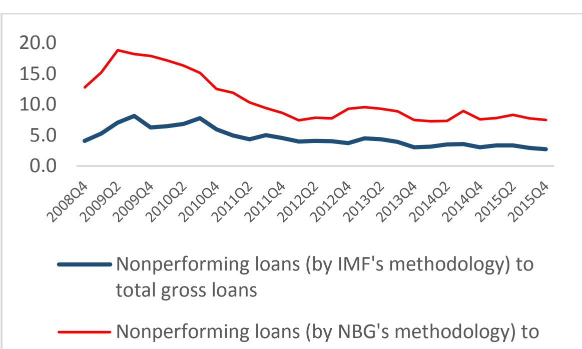
Financial Sector Performance

Despite the unfavorable external environment and lower economic growth, the banking sector recorded high growth and record profitability in 2015. This is largely explained by the rising dollarization on the assets and liabilities side of the banks' balance sheet and the nominal growth of the loan portfolio as reported in local currency at the back of the GEL devaluation. The lending portfolio increased by 23 percent to 50 percent of GDP; however, if adjusted for the foreign exchange effect, the loan growth was modest. Corporate deleveraging reduces banks' lending support for the economy. Unlike in neighboring countries, banks in Georgia recorded high profitability, with return on equity (ROE) and return on assets (ROA) at 15.4 percent and 2.3 percent, respectively, in 2015.

The Georgian financial system remains heavily bank dominated, with a negligible non-bank financial services market and fairly small private securities market. Nineteen private commercial banks, including two branches of foreign banks, hold more than 90 percent of total financial sector assets. In 2015, banking sector assets grew by 22 percent (year-on-year) to 85 percent of GDP, and client deposits in banks grew by 23 percent in nominal terms to 48 percent of GDP. The growth of the non-bank financial sector is constrained by the lack of liquidity access in the absence of deposits and shallow capital markets.

Despite the rising number of NPLs, the financial sector remains sound and liquid thanks to significant capital buffers. The aggregate banking sector capital adequacy ratio (CAR) stood at 17.5 percent as of December 2015, well above the minimum regulatory requirement. NPLs, as calculated based on NBG methodology, remained at 7.5 percent, similar to 2014. NPLs under the methodology of the International Monetary Fund (IMF) (Financial Soundness Indicator [FSI] methodology) were reported at 2.7 percent (figure 3), indicating streamlined NPL write-off procedures against the loan loss provisions. Nonetheless, vulnerabilities exist due to the high portfolio dollarization, especially to unhedged borrowers, and the credit concentration, including in real estate and household lending. Banks' liquid assets slightly increased to 23.4 percent of total assets.

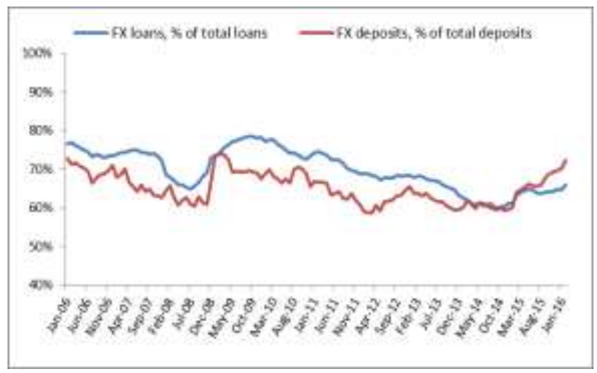
Figure 3. Nonperforming Loans



Source: NBG, IMF FSI.

The high dollarization of banks' balance sheets makes them vulnerable to currency-induced credit risk and local currency funding constraints. Foreign currency–denominated deposits jumped from 60 percent in December 2014 to 70 percent of total deposits by end-2015. During the same time frame, the share of loans denominated in foreign currency increased from 61 to 65 percent of total loans (figure 4). The net open foreign currency position was reported to be negative at the end of 2015, exposing banks to devaluation risks.

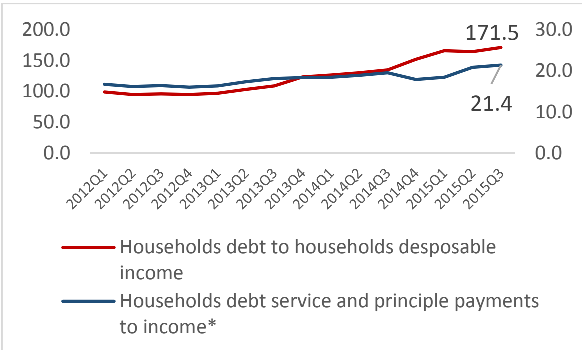
Figure 4. Share of Foreign Currency Loans and Deposits



Source: NBG.

The rapid growth of the retail portfolio, especially in foreign currency to unhedged borrowers, presents an increasing credit risk for the banking sector and significant social risks. The retail loan portfolio surged from 21 percent of GDP in 2014 to 27 percent of GDP at end-2015. The consumption boom in 2010–14 and GEL devaluation in 2014–15 rapidly increased personal indebtedness, with household debt equal to nearly 171.5 percent of disposable household income and 21.4 percent to total income (figure 5). Although banks have offered debt restructuring to their clients to mitigate losses and reduce debt service costs, significant risk remains, especially in the light of the 40 percent remittances reduction and lower real income. On top of that, the rising number of shadow banking activities (including micro finance lenders, pawnshops, and other street or digital lenders) pose severe risks for household debt service capacity. To mitigate the financial sector and social risks, the consumer protection framework and regulation of non-bank credit and deposit institutions need to be significantly strengthened.

Figure 5. Household Debt to Income



Source: NBG

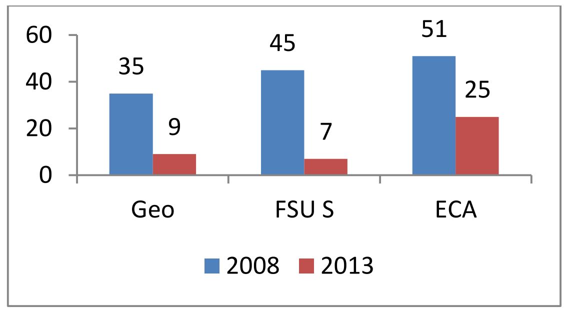
The World Bank supports deepening the financial sector and enhancing access to finance for small and medium-sized enterprises (SMEs). The Bank program includes lending as well as analytical and advisory work. In 2015, the Bank completed a comprehensive survey of 500 SMEs to assess their financial demands and identify constraints in access to finance. The Bank is also working with the authorities on implementation of the financial sector reform agenda (capital markets, pension, insurance, and deposit insurance) supported by the series of Private Sector Competiveness DPOs. The Bank provides advisory support through the Austrian Government–supported grant from the Vienna Center for Financial Sector Advisory Services (FinSAC); it is also developing a new extensive program of financial sector reform support under the Financial Sector Reform and Strengthening (FIRST) Initiative.

Private Sector Development

Georgia has a consistent track record with regard to improving the business environment. The business deregulation, anticorruption, legal, tax, and trade reforms that Georgia put in place in the past decade made the country a more attractive destination for FDI and brought it global recognition as a top reformer. In the 2015 *Doing Business* report, Georgia ranked 15th.

However, the favorable business environment has so far had only a moderate impact on the country's competitiveness. Its Global Competitiveness ranking improved from 90th place in 2008–09 to 69th in 2014–15; however, investment has largely been concentrated in non-tradables and tourism and has been associated with a high propensity to import. According to the 2013 World Bank Enterprise Survey (the latest available), only 9 percent of surveyed entrepreneurs indicated that their firm had introduced new or substantially improved products or services in the previous years. Majority 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 6. Percentage of Firms that have Developed New Products in the Past Three Years



Source: World Bank Enterprise Survey.

Although globally the SME sector is the main source of private sector growth, innovation, and jobs, in Georgia it remains underdeveloped. SMEs account for nearly 94 percent of registered firms in Georgia and 38 percent of formal employment, but they account for only 20 percent of gross value added and less than 19 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 supply markets. The productivity of Georgian firms, especially SMEs, remains inadequate due to poor technological preparedness and low business sophistication and innovation.

A series of programmatic Private Sector Competitiveness DPOs are supporting private sector development as a central element of the World Bank's current Country Partnership Strategy (CPS). The DPOs are 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.

The International Finance Corporation (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 in 2014 continued the decreasing trend started in 2010, although considerable disparities persist between urban and rural areas. The poverty rate at US$2.5 per day (purchasing power parity corrected) fell from 47 percent in 2010 to 32 percent in 2014. The poverty rate at US$5 per day followed the same trend, falling from 81 to 69 percent in the same period. Measures of poverty intensity, such as, for instance, the average distance to the poverty line for the poor population, also show considerable improvements in this period (19 to 11 percent of the poverty line between 2010 and 2014). However, regional differences are still considerable and persistent. Although both urban and rural poverty have decreased significantly, poverty continues to be much higher in rural than in urban areas. In 2014, poverty in urban areas was half what it was in rural areas, registering 21 percent of the population against 43 percent in rural areas.

Social assistance and labor income earnings outside agriculture have played the most important roles in the poverty reduction observed between 2010 and 2014. Labor earnings have played a more substantial role in urban regions, while both labor earnings and social transferences share responsibility for the fall observed in rural areas. The role of social assistance is consistent with continuous increases in social spending between 2010 and 2013. Pension benefits were raised for pensioners above the age of 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. The role of labor earnings in reducing poverty is consistent with the increases in wages observed across the board during 2010–13, with all industries recording annual wage growth rates above 6 percent and half of them recording two-digit annual increases.

Employment creation has played only a minor role in poverty reduction. Although unemployment decreased in 2014 (12.4 percent in 2013), urban unemployment is still considerable (22 percent) and low-productivity employment among the poor is prevalent. 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 (agriculture employs two-thirds of the working poor).

Picture 1. Social Service Agency at Mtatsminda Branch in Tbilisi

Georgia has reversed the trend from past years and now fares well on the World Bank Group's measure of shared prosperity, with solid gains in recent years. The consumption of the bottom 40 percent of the distribution grew 8.3 percent per year compared to 6.4 percent for the overall population in the period 2010–14. Initial estimates of shared prosperity showed that the bottom 40 percent lagged behind the rest of society in consumption growth between 2006 and 2012. However, more recent estimates based on the 2010–14 period show that the bottom of the distribution has been increasing its level of consumption at a faster pace than the overall population, consistent with the decrease in poverty described above and with evidence that growth in this period has been widespread along the income distribution (2015 Georgia Poverty Assessment).

Inequality in Georgia fell between 2010 and 2014. Inequality in per capita consumption fell between 2010 and 2014, as measured by the Gini coefficient, from 42.1 to 40. Observing a Gini by location (39.4 in rural areas and 38 in urban areas) that is lower than the national Gini indicates that differences in living standards between urban and rural areas do much to explain national inequalities. Other indicators designed to better capture changes at specific locations of the welfare distribution also show inequality decreasing.

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.

The UHC program introduced in 2013 has led to a major expansion in population entitlement to publicly financed health services. As a result, coverage has expanded substantially and rapidly from 29.5 percent of the population in 2010 and around 40 percent at the end of 2012 to 99.9 percent in 2014. Most of those benefiting from the UHC program are being covered for the first time; in 2014, just over half of those covered by the UHC program (51.4 percent) were previously uninsured.

In 2014, the budget for health was doubled in nominal terms, an increase of 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 Europe and Central Asia (ECA) regional average. The World Bank, the U.S. Agency for International Development (USAID), and the World Health Organization (WHO) worked with the Ministry of Health on an analysis of the Household Utilization and Expenditure Survey. The results show substantial improvements in utilization of and access to services.

The Bank continues to support the health sector in Georgia through technical assistance and development policy lending. In FY16, the Bank will carry out an analysis of financing options for health care, which will include an analysis of potential savings through improvements in efficiency.

Education

Georgia compares well to comparator countries in the ECA region in terms of enrollment rates at basic education levels, despite a relatively modest level 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 the Commonwealth of Independent States, 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 DPO. In addition, the Bank mobilized Institutional Development Fund (IDF) grant funding to support capacity building in teacher and school principal evaluation and technical assistance through Programmatic Education Sector Support to inform policy dialogue in strategic areas identified as priorities by the Government. In 2014, the Bank conducted a detailed review of public expenditure on education as part of the broader Public Expenditure Review (PER) and a comprehensive Education Sector Policy Review aimed at supporting the Ministry of Education and Science in developing a strategic plan in preparation for the next phase of sector reforms.

Agriculture

The share of agriculture in total GDP significantly declined from 12.8 percent in 2006 to 9.2 percent in 2014, 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 and low levels of public investment in agricultural 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. The irrigated area declined from 386,000 hectares in 1988 to 25,000 hectares in 2013. While Georgia has a modern national registration agency, it is estimated that only 15–20 percent of land titles are registered.

The Government has attached a high priority to agricultural sector development as outlined in its Strategy for Agricultural Development 2014-2020, which strongly focuses on rebuilding irrigation and other agricultural services, promoting land market development, and harmonizing food safety legislation in line with the EU Association Agreement.

The Bank is supporting the agriculture sector of Georgia through a US$50 million irrigation and land market development project aimed at establishing land rights and improving irrigation and drainage agencies and infrastructure.

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 to overcome before it can improve its logistics and competitiveness. Georgia's infrastructure deficits are still a major component of this lower performance.

Picture 3. A Section of the East-West Highway

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 sections from Ruisi to Agara (19 kilometers) and from Agara to Zemo-Osiauri (12 kilometers) and preparing the project to upgrade the section from Zemo-Osiauri to Chumateleti (14 kilometers). 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.

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 6.4 percent increase in the demand for electricity in 2014, and in that year, Georgia continued to rely 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.

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.

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 between 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 urban and rural roads, water, and sanitation infrastructure has remained in need of substantial rehabilitation in most of the country.

Picture 4. Dartlo Village, Tusheti

Tourism development is one of the expanding drivers of economic growth in cities and regions. It has seen rapid growth in Georgia over the past decade and has become an important source of job creation and hard currency income. The number of international arrivals increased from 560,000 in 2005 to 5.9 million in 2015. An integrated and demand-driven approach to tourism and 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. A National Tourism Strategy has been prepared with Bank support, which defines a Vision 2025 and an action plan.

The regional development program is one of the flagships of Georgia's cooperation with the World Bank and brings direct benefits to residents. 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. The first *Regional Development Project* (RDP, US$60 million) focuses on the Kakheti region, the second *Regional Development Project* (RDPII, US$30 million) focuses on the Imereti region, and the third *Regional Development Project* (RDPIII, US$60 million), focuses on the two regions of Mtskheta-Mtinatenti and Samtekhe-Javakheti. The Swedish International Development Cooperation Agency (SIDA) has provided an additional US$10 million trust fund grant to address issues of wastewater treatment in the two regions to ensure sustainable and responsible tourism.

The Bank also supports municipal development and decentralization through a series of *Regional and Municipal Infrastructure Development Projects* (RMIDP). The first Project (RMIDP, US$90 million and US$3.7 million EU trust find grant) closed in December 2014 and fully achieved its expected results. The second project (RMIDPII, US$30 million and US$5.0 million trust fund grant from the Swiss Agency for Development and Cooperation) aims to improve the efficiency and reliability of targeted municipal services and infrastructure. This is being achieved by investing in high-priority local infrastructure improvements and by supporting local self-governments in enhancing their capacity and systems for service delivery.

Picture 5. Urban Regeneration in Telavi, Kakheti Region

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 the signing of the EU-Georgia Association Agreement and recent institutional reforms.

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 (FLEG) Program 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. Delivered in 2015, this study equips the Government with valuable information on environmental priority-setting, planning, and budgeting.

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). At the end of FY14, Georgia graduated from the International Development Association (IDA), which was also 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 13 active investment projects financed by IDA credits/International Bank for Reconstruction and Development (IBRD) loans for a total of US$920 million, of which US$200 is IDA. About US$525 million is undisbursed. The two DPO series (Programmatic Inclusive Growth DPO and Private Sector Competitiveness DPO) are also part of the ongoing program.

In addition to IDA/IBRD operations, there is an active program of seven recipient-executed trust fund operations of about US$18 million, of which about 91 percent is undisbursed. Advisory Services and Analytics (ASA) further contribute to program implementation. The ASA program of the current fiscal year is on track and includes activities in various sectors and complements the lending program.

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	36.5	2.48
IBRD Loan	147.00	147.00	0.00
Government of Georgia	47.87		
Total	**237.87**	**183.50**	**2.48**

***World Bank Disbursements as of March 31, 2016**
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. In addition, 34 kilometers of road have been upgraded on the Ruisi-Agara section.
- 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 22 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.

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	27.44	6.71
IBRD Loan	38.00	0.95	37.91
Government of Georgia	18.75	--	--
Total	**93.75**	**28.39**	**44.62**

***World Bank Disbursements as of March 31, 2016**
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 achieved:

Three out of twelve kilometers have been completed.

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.

EAST-WEST HIGHWAY CORRIDOR IMPROVEMENT PROJECT (EWHCIP)

Key Dates:
Approved: December 3, 2015
Effective: Not yet effective
Closing: December 31, 2020
Financing in million US Dollars:

Financier	*Financing*	*Disbursed**	*Undisbursed*
IBRD Loan	140.00	0.00	140.00
Government of Georgia	24.00		
Total	**164.00**	**0.00**	**140.00**

***World Bank Disbursements as of March 31, 2016**
Note: Disbursements may differ from financing due to exchange rate fluctuations at the time of disbursement.

The Project Development Objectives are to (i) reduce road user costs along the East-West Highway Corridor section upgraded under the project; and (ii) strengthen the capacity of the Roads Department (RD) and the Ministry of Economy and Sustainable Development to manage the road network and provide an enabling environment to improve logistics services, respectively.

The project is a part of a larger international financial institution (IFI)-coordinated effort to support the Government in completing the East-West Highway Corridor Program. This phase consists of the upgrading of the existing two-lane East-West Highway from Zemo-Osiauri to Chumateleti, totaling 13.8 kilometers. EWHCIP refers to the project cofinanced by the Government and the World Bank. The European Investment Bank (EIB) will finance in parallel the upgrading of the first 5.8 kilometers from Zemo-Osiauri to Zemo-Osiauri to a two-lane dual carriageway road, including four bridges. The total cost estimate is US$48.9 million, including US$39.1 million EIB financing and US$9.8 million from government cofinancing. The World Bank (the project) will finance the remaining 8.0 kilometers from Zemo-Osiauri to Chumateleti. The project will also strengthen the capacity of RD's Intelligent Transport Systems (ITS) Unit in setting up and managing ITS systems applications to improve traffic control and road safety and timely communication with road users along the East-West Highway Corridor, and also the capacity of RD's Monitoring Unit to assess and inform the general public and beneficiaries about the impacts of improving the East-West Highway Corridor.

Expected results:

- Travel time from Zemo-Osiauri to Chumateleti will decrease from 12 to six minutes
- Vehicle operating costs from Zemo-Osiauri to Chumateleti will decrease from US$/km 0.24 to 0.21 for cars and from US$/km 0.63 to 0.50 for trucks
- Asset value of the East-West Highway Corridor from Tbilisi to Sarpi will increase from GEL 812 million to GEL 4,880 million.

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), European Commission (EC), and European Investment Bank (EIB) 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, 2019
Financing in million US Dollars:

Financier	*Financing*	*Disbursed**	*Undisbursed*
IDA Credit	40.00	39.30	0.00
IBRD Loan	30.00	13.77	16.23
Government of Georgia	17.50	--	--
Total	**87.50**	**53.07**	**16.23**

***World Bank Disbursements as of March 31, 2016**
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 will create jobs. Rehabilitating secondary and local roads and improving local connections are also known to stimulate agricultural development. Moreover, reduced transport costs will 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.

Results achieved to date:

- Out of 200 kilometers of secondary and local roads to be rehabilitated under the project, about 198 kilometers have been rehabilitated.
- Travel time on rehabilitated sections has decreased on average by 42 percent, affecting over 150,000 direct beneficiaries.
- The number of roads in good and fair condition as a share of total classified roads has improved from 30 to 62.3 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	16.94	58.06
Government of Georgia	18.75		
Total	**93.75**	**16.94**	**58.06**

***World Bank Disbursements as of March 31, 2016**
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 will create jobs. Rehabilitating secondary and local roads and improving local connections are also known to stimulate agricultural development. Moreover, reduced transport costs will lower agriculture sector costs, thus making agricultural products more competitive.

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.

Results achieved to date:

- 52.2 kilometers of secondary roads and 5.7 kilometers of local roads have been rehabilitated.
- Travel time on rehabilitated sections has decreased and average speed has increased by 5 (out of the planned 20) kilometers per hour.
- Vehicle operating costs have decreased on average by 19 percent for cars and for trucks (target: 22 and 27 percent, respectively).
- Condition of project roads has improved (as measured by international roughness index, IRI) from 12 to 10.8 (target: 3).
- Roads in good and fair condition as a share of total classified roads have improved by 0.9 percentage points (target: 2.4).

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.

SECONDARY ROADS ASSET MANAGEMENT PROJECT

Key Dates:
Approved: March 18, 2016
Effective: Not yet effective
Closing: April 30, 2022
Financing in million US Dollars:

Financier	*Financing*	*Disbursed**	*Undisbursed*
IBRD Loan	40.00	-	40.00
Government of Georgia	8.00		
Total	**48.00**	**-**	**40.00**

***World Bank Disbursements as of March 31, 2016**
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 will create jobs. Rehabilitating secondary and local roads and improving local connections are also known to stimulate agricultural development. Moreover, reduced transport costs will lower agriculture sector costs, thus making agricultural products more competitive

The Project Development Objectives are (i) to improve road user access to social services and markets through the project roads in a sustainable manner, and (ii) to enhance road asset management for the secondary road network in Georgia.

Expected results:

- 160 kilometers of roads will be rehabilitated
- Share of secondary road network in good and fair condition will increase from 60 to 65 percent
- Travel time to socioeconomic centers or district centers on Guria OPRC roads will decrease from 320 to 255 minutes
- Travel time to socioeconomic centers or district centers on project roads under design-build contracts will decrease from 135 to 100 minutes

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	56.31	3.69
Government of Georgia	15.00		--
Total	**75.00**	**56.31**	**3.69**

***World Bank Disbursements as of March 31, 2016**
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 local self-governments (LSGs). Overall, the population is expected to see improved welfare and revenues.

Results achieved to date:

- 217 building facades have been rehabilitated in Telavi, Kvareli, and Dartlo
- 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 have been rehabilitated in central Telavi and Kvareli
- Volume of private sector investments has reached US$17 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 14 (end target: 24 hours/day)
- Weighted average vehicle operating costs due to improved urban roads have been reduced by 20 percent (end target: 25 percent)
- Number of hotel beds in circuit route has increased by 76 percent from 1,610 to 2,838, well above the target of 1,932 beds
- Number of points of sales in renovated cultural heritage sites and cities increased by 25 percent from 248 to 310 (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	24.50	3.35
Government of Georgia	7.50		--
Total	**37.50**	**24.50**	**3.35**

***World Bank Disbursements as of March 31, 2016**
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 and Imereti Regional Development Strategy 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 59 percent (from 2,661 to 4,224)
- Number of hours per day of piped water services in Tskaltubo increased from 8 to 16 (target revised from 18 to 16)
- 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 30 percent in Tskaltubo (end target met)
- Nine out of targeted 11 buildings have been restored/constructed.
- Six thousand people in urban areas provided with access to all-season roads within a 500 meter range under the project

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.

REGIONAL DEVELOPMENT PROJECT – 3 (Samtskhe Javakheti and Mtskheta-Tianeti)

Key Dates:
Approved: July 1, 2015
Effective: October 15, 2015
Closing: December 31, 2019
Financing in million US Dollars:

Financier	*Financing*	*Disbursed**	*Undisbursed*
IBRD Loan	60.00	5.15	54.85
Government of Georgia	15.00		--
Total	**75.00**	**5.15**	**54.85**

***World Bank Disbursements as of March 31, 2016**
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 Samtskhe-Javakheti and Mtskheta-Mtianeti spatial economic analysis and Regional Development Strategies have identified tourism, agriculture, and trade as the main drivers of economic growth in the regions. Samtskhe-Javakheti is home to several cultural heritage sites and nature attractions, while the Mtskheta-Mtianeti region is a major tourism destination, including the UNESCO World Heritage Site of Mtskheta city and an exceptional portfolio of cultural heritage and natural products with a year-round appeal for foreign and domestic visitors.

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 Samtskhe-Javakheti and Mtskheta-Mtianeti regions. The project activities are expected to benefit the residents, tourists, and enterprises in the Samtskhe-Javakheti and Mtskheta-Mtianeti regions. They are expected to receive improved access to and quality of public infrastructure; an increased volume of private sector investment in the region; and an increased number of small and micro enterprises in renovated cultural heritage sites and cities. The Government will benefit from increased overall tourism spending and satisfaction, expanded job creation, improved institutional capacity within selected agencies, and an improved capacity to operate and maintain assets.

Expected results:

- Number of hotel beds in circuit route areas will increase by 40 percent (from 10,939 to 15,277)
- Number of hours per day of piped water services in project areas will increase from eight to 18
- 1,280 persons in urban areas will be provided with access to all-season roads within a 500 meter range
- Number of jobs created by activities linked to supporting the tourism industry will increase by 27 percent (from 63,787 to 81,410)
- Number of visitors at project sites will increase by around 28 percent
- Volume of private sector investments will increase by US$30 million

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 Samtskhe-Javakheti and Mtskheta-Mtianeti 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).

SECOND REGIONAL AND MUNICIPAL INFRASTRUCTURE DEVELOPMENT PROJECT

Key Dates:
Approved: July 3, 2014
Effective: December 16, 2014
Closing: June 30, 2019
Financing in million US Dollars:

Financier	Financing	Disbursed*	Undisbursed
IBRD Loan	30.0	7.90	22.10
Government of Georgia	11.0		
Financial Intermediaries	12.93		
Swiss Development Cooperation	5.0	0.40	4.60
Total	**37.50**	**8.30**	**26.70**

***World Bank Disbursements as of March 31, 2016**
Note: Disbursements may differ from financing due to exchange rate fluctuations at the time of disbursement.

The World Bank has been supporting the improvement of municipal service delivery and infrastructure since 1997. The Government of Georgia has requested the World Bank's continued support under this project in addressing local self-government (LSG) reforms and investments needs. This project will support the decentralization agenda in line with the overall government reform strategy through financing the investment priorities identified under the regional development strategies, prepared with technical assistance from the EU, GiZ, and UNDP.

The Project Development Objective is to improve the efficiency and reliability of targeted municipal services and infrastructure. This will be achieved by investing in high-priority local infrastructure improvements and by supporting LSGs in enhancing their capacity and systems for service delivery.

Results achieved to date:

- 17 kilometers of rural and 2.5 kilometers of non-rural roads have been rehabilitated.

Expected results:

The primary project beneficiaries are the residents of towns and villages, who currently experience substandard municipal service quality. The project is expected to improve the quality and reliability of municipal services and therefore positively affect the living conditions of the beneficiaries. The project is also expected to benefit small and micro enterprises and to attract new enterprises to beneficiary municipalities. As a result, the project will contribute to income generation and job creation. Improvements in living conditions and the creation of jobs will contribute to a reduction in poverty and to increased shared prosperity. More specifically, key results expected from the project are:

- 30 percent reduction in energy consumption per cubic meter of water or wastewater pumped (KWh/m3) in selected municipalities;
- Increase in the average number of hours per day of piped water service from seven to 12 in selected municipalities;
- volume (mass) of biological oxygen demand (BOD) pollution loads removed by the treatment plant supported under the project (153 tons/year);
- 60 percent of LSGs with improved asset management and accounting system.

Key Government Partners: Ministry of Regional Development and Infrastructure (MRDI), Ministry of Refugees and Accommodation (MRA), Ministry of Finance (MoF), local self-governments, Tbilisi Capital, and Municipal Development Fund (MDF).

Key Development Partners: European Union (EU), German Technical Cooperation Agency (GiZ), and United Nations Development Programme (UNDP).

IRRIGATION AND LAND MARKET DEVELOPMENT PROJECT

Key Dates:
Approved: May 23, 2014
Effective: March 13, 2015
Closing: July 31, 2019
Financing in million US Dollars:

Financier	*Financing*	*Disbursed* *	*Undisbursed*
IDA Credit	50.0	2.00	43.15
Total	**50.0**	**2.00**	**43.15**

***World Bank Disbursements as of March 31, 2016**
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 and the sector constitutes about 25 percent of exports. Subsistence agriculture accounts for 75 percent of rural employment and 45 percent of rural income. However, although the share of agriculture to GDP has significantly declined (from 25 percent in 1999 to about 8 percent in 2012), it has started to increase again due to the Government's focus on the sector, recording 8.2 percent of GDP 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. Moreover, although 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

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

Financier	*Financing*	*Disbursed **	*Undisbursed*
IBRD Loan	60.0	13.58	46.42
Government of Georgia	1.88		
Total	**61.88**	**13.58**	**46.42**

***World Bank Disbursements as of March 31, 2016**
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).

GEORGIA NATIONAL INNOVATION ECOSYSTEM PROJECT

Key Dates:
Approved: March 18, 2016
Effective: Not yet effective
Closing: April 30, 2021
Financing in million US Dollars:

Financier	*Financing*	*Disbursed **	*Undisbursed*
IBRD Loan	40.00	-	40.00
Local Beneficiaries	2.00		
Total	**42.00**		**40.00**

***World Bank Disbursements as of March 31, 2016**
Note: Disbursements may differ from financing due to exchange rate fluctuations at the time of disbursement.

The weak performance of micro, small, and medium-sized enterprises (MSMEs) is at the root of Georgia's innovation, productivity, and competitiveness challenges. MSMEs in Georgia represent 94 percent of registered businesses and more than 47 percent of formal jobs, but they account for less than 20 percent of GDP as compared to global averages of 40–50 percent and 60 percent in the ECA region. Most of this is due to their poor productivity, which is three times lower than that of large enterprises, and to their low rates of innovation.

Since the early 2000s, Georgia has been implementing far-reaching reforms to improve the business environment, spur investment, and shake off the lingering rigidities of a centrally planned economy. These reforms have helped to kick start GDP growth, but the economy has still not fully returned to its pre-transition size, and unemployment remains a significant public policy concern. The sustainability of this growth in the medium term is tenuous, amidst slowing productivity growth, depressed external demand, and declining export competitiveness. Prospects for a resurgence in productivity growth and exports are constrained by low levels of innovation, human capital development, and entrepreneurship. The rural economy is also lagging behind, trapped by low productivity in agriculture. To address these challenges, the Government seeks to promote inclusive growth and develop an innovation-driven and knowledge-based economy, which is the focus of this project.

The Project Development Objective is to increase the innovative activities of firms and individuals in the Borrower's territory and their participation in the digital economy. The project will help to increase jobs, productivity growth, and export competitiveness in Georgia.

The Innovation Infrastructure component will support the development of a hub-and-spoke network of innovation centers across Georgia, as well as increase the use of broadband Internet services among rural households and MSMEs. The Innovation Services component will support innovation competitions, digital economy skills development, and innovation capacity building for firms and individuals. The Innovation Financing component will provide matching grants to start-ups and firms to undertake innovative projects.

Expected results:

- 200 new/improved products or services introduced by project beneficiaries
- 340 start-ups launched by project beneficiaries
- Access to broadband Internet increased from 39 to 50 subscribers per 100 people
- 400 beneficiary MSMEs selling via e-commerce platforms

Key Government Partners: Ministry of Economy and Sustainable Development, and Georgia Innovation and Technology Agency.

Key Development Partners: Private sector, including firms, Internet service providers, training providers, etc.

FIRST PROGRAMMATIC INCLUSIVE GROWTH DEVELOPMENT POLICY OPERATION

(IG DPO1)

Key Dates:
Approved: April 28, 2015
Effective: June 12, 2015
Closing: December 31, 2015

Financier	*Financing*	*Disbursed**	*Undisbursed*
IBRD Loan (US$ million)	60.0	60.0	0.00
Total (US$ million)	**60.0**	**60.0**	**0.00**

***World Bank Disbursements as of March 31, 2016**

The main development challenge facing by Georgia is the need to achieve more inclusive growth, which will require investments in human capital and improvements in private sector competitiveness. So far, a decade of strong economic growth in Georgia, briefly interrupted by the 2008 conflict with Russia and the global financial crisis, has not succeeded in making a significant dent in the unemployment rate. This is largely explained by low net job creation and gaps in skills and overall human capital development. The Government was successful in attracting foreign investors through significant improvements in the business environment. Net job creation, however, remained weak. With economic transformation in Georgia, some of the older industries died, shedding their labor force. New industries grew during the same period but have not been able to absorb the workforce as effectively. New growth sectors, especially in tourism and other service sectors, have not been able to generate sufficient formal employment. In addition, the existing educational system is not in line with the demands of the private sector and student performance ranks low. Moreover, although life expectancy in Georgia has improved significantly over the past decade, it has stalled at 74 years since 2010. The high levels of neonatal mortality and the poor quality of reproductive health, coupled with premature deaths due to noncommunicable diseases (NCDs), are among major factors contributing to the stagnation in life expectancy. Making growth more inclusive will therefore require investments in human capital as well as reforms to support competitiveness.

The **Project Development Objective** is to support the Government in its efforts to improve public service delivery and strengthen fiscal oversight. Pillar I supports greater fiscal oversight of public institutions (including municipalities, legal entities of public law, non-profit legal entities, and state-owned enterprises [SOEs]) and improvements in the budgeting and framework for civil services. Pillar II supports improvements in the coverage and targeting of social expenditures, the quality of education and health care services, and the monitoring of outcomes.

Expected results:

- Real-time availability of budget and execution data for municipalities, legal entities of public law, and nonprofit legal entities
- Improved capital budgeting framework reflected in the selection criteria for new capital projects in six municipalities and two central ministries
- Availability of comprehensive financial data on SOEs
- Pre-qualification test taken by first-time entrants to the civil service according to the new hiring rules
- Increased share of the bottom decile receiving targeted social assistance (TSA)
- Reduced pharmaceutical expenses as percent of out-of-pocket (OOP) expenses on health
- Reduced maternal mortality rate
- Reduction in the proportion of teachers in Category 1 in general public schools
- Increased number of preschool educational institutions using the new pre-school curriculum
- Quarterly publication of data on poverty and unemployment

Key Government Partners: Ministry of Finance (MoF), Ministry of Labor, Health, and Social Affairs (MoLSHA), Ministry of Economy and Sustainable Development (MoESD), Ministry of Education and Science (MoES), the National Statistics Office, the National Agency for State Property, and the Civil Service Bureau.

Key Development Partners: International Monetary Fund (IMF), European Union (EU), and the United Nations Children's Fund (UNICEF).

FIRST PROGRAMMATIC PRIVATE SECTOR COMPETITIVENESS DEVELOPMENT POLICY OPERATION (PSC DPO1)

Key Dates:
Approved: April 28, 2015
Effective: June 12, 2015
Closing: December 31, 2015

Financier	*Financing*	*Disbursed**	*Undisbursed*
IBRD Loan (US$ million)	60.0	60.0	0.00
Total (US$ million)	**60.0**	**60.0**	**0.00**

***World Bank Disbursements as of March 31, 2016**

Although the business environment reforms implemented in the past decade contributed to Georgia's robust economic growth, boosting long-term competitiveness and employment remains a significant public policy concern. The Government's inclusive growth agenda foresees policy reforms to strengthen the private sector's competitiveness and productivity, thereby reducing the economy's reliance on public investment as the main source of growth. Long-term growth prospects will also depend on Georgia's ability to leverage the benefits of membership in the Deep and Comprehensive Free Trade Area (DCFTA) and the Association Agreement (AA) with the European Union (EU), both of which will improve market access and encourage trade and foreign direct investment (FDI). Harnessing the gains from deeper integration with the EU will require promoting the reallocation of capital and labor to more productive industries, building the capacity in domestic firms so they can cope with the compliance costs associated with the harmonization of the legal and regulatory frameworks, and upgrading state institutions to improve trade facilitation, reduce technical barriers to trade, protect intellectual property rights, and develop the country's human capital.

The **Project Development Objective** is to support the Government in its efforts to increase private sector competitiveness. The operation contains a series of policy actions that are structured around three pillars. Pillar 1 will support second-generation business environment reforms as a way to stimulate private sector–led growth. Pillar 2 will support financial sector reforms and pension reforms that are essential to increasing savings and mobilizing the investment needed to enhance competitiveness. Pillar 3 will support measures to increase firms' capacity to innovate and to export, including the upgrading of broadband Internet services in Georgia.

Expected results:

- Enhancing the public-private dialogue mechanisms in the business environment
- Developing an institutional framework for entrepreneurship and small and medium-sized enterprise (SME) support
- Increasing the number of users of public procurement and the number of public tenders that are successfully completed
- Strengthening the financial safety net through the implementation of a Deposit Insurance System (DIS)
- Adopting the legal framework that will underpin the comprehensive pension reform, including the establishment of a new contributory pension system
- Developing capital markets and the insurance market
- Improving efficiency, competition, and access in telecommunications and Internet services
- Promoting widespread access to broadband services, especially in rural and underserved areas
- Increasing the number of innovative Georgian firms, entrepreneurs, and academic institutions
- Improving access to international markets for Georgian firms through improvements in the national quality infrastructure

Key Government Partners: Ministry of Finance (MoF), Ministry of Economy and Sustainable Development (MoESD), the Economic Council, the State Procurement Agency, the Entrepreneurship Development Agency (EDA), the National Bank of Georgia, the Georgian National Communications Commission (GNCC), and the Georgian Innovation and Technology Agency (GITA).

Key Development Partners: International Monetary Fund (IMF), European Union (EU), the Asian Development Bank (ADB), and the European Bank for Reconstruction and Development (EBRD).