



GEORGIA

Highlights

- **Economic recovery is gaining momentum in the first half of 2021.** Renewed growth is benefiting from a supportive external environment but risks to the recovery remain, in particular the slow vaccination rate and potentially extended travel restrictions.
- **A new insolvency framework aims to address a long-standing business environment vulnerability.** It could also help resolve Covid-19 pandemic-related bankruptcies in a more efficient way.
- **The government has presented a 10-year country socio-economic development vision.** The vision is supported by ministry-specific strategies, which will set out development goals, financial needs and planned instruments.

Key priorities for 2022

- **Strengthening governance standards needs to remain a top priority.** An impartial, independent, transparent, efficient and accountable formal and informal public institutional framework is key to maintain the trust of businesses and the general public.
- **The authorities should ensure that economic recovery is tilted to green, including by creating an enabling environment for non-hydro renewables.** Exploiting Georgia's great renewable energy potential would help ensure sustainable growth and increase the country's energy self-sufficiency and competitiveness.
- **Georgia should continue pursuing critical structural reforms such as education and state-owned enterprise (SOE) reform.** Pledges to reform the education sector and to bring corporate governance closer to best practices should be pushed forward to ensure the availability of skills and to increase competitiveness of the economy.

Main macroeconomic indicators %

	2017	2018	2019	2020	2021 proj.
GDP growth	4.8	4.8	5.0	-6.2	7.5
Inflation (average)	6.0	2.6	4.9	5.2	9.3
Government balance/GDP	-0.5	-0.8	-1.8	-9.2	-6.5
Current account balance/GDP	-8.0	-6.8	-5.5	-12.4	-10.0
Net FDI/GDP [neg. sign = inflows]	-10.5	-5.6	-6.0	-3.5	-3.9
External debt/GDP	106.6	101.3	106.7	129.7	n.a.
Gross reserves/GDP	18.7	18.7	20.1	24.6	n.a.
Credit to private sector/GDP	52.2	56.8	61.7	74.4	n.a.

Covid-19: macroeconomic implications

The economy strongly contracted in 2020 as tourism and global demand plummeted.

Following an average growth of 4.9 per cent in 2017-19, gross domestic product (GDP) declined by 6.2 per cent in 2020 as the economy was hit by the Covid-19 pandemic shock. The hospitality sector and exports of goods suffered an immediate blow. In 2020 exports of services contracted by 65.6 per cent and exports of goods by 12.1 per cent, investment activity shrank by 4.8 per cent while repeated lockdowns weighed on consumption and many small service providers. Nonetheless, household consumption posted 5.4 per cent growth. Inbound money transfers grew by 8.8 per cent in the same period as strong growth in the second half of the year outpaced the initial fall in the second quarter. Many indicators point to a strong recovery from January to September 2021: money transfers grew by 27.8 per cent and nominal goods exports by 24.0 per cent, both year-on-year, the latter driven largely by increased trade with China and neighbouring economies. As a result, high-frequency economic data point towards a strong growth of 11.3 per cent year-on-year from January to September 2021. As Georgia lifted restrictions on international air travel in February 2021, tourism started to recover slowly but it remains far below the levels seen before the Covid-19 pandemic. In the first nine months of 2021, the number of international travellers was just 18.0 per cent of the figures for the same period in 2019.

The downturn in 2020 led to higher public debt and inflation. Increased spending on the Covid-19 crisis response, shrinking budget revenues and reduced economic activity deepened the budget deficit from an average of 1.0 per cent of GDP in 2017-19 to 9.2 per cent in 2020. On the back of the new borrowing needed to cover the fiscal gap, currency depreciation and economic contraction, this resulted in a steeply rising public debt, from 40.4 per cent of GDP in 2019 to 60.0 per cent in 2020. Upon repaying the 10-year Eurobond in April 2021, the authorities issued a five-year US\$ 500 million Eurobond at a historically low coupon of 2.75 per cent, with demand exceeding supply by a factor of four. Together with official lending, this helped to maintain international reserves at high levels, amounting to US\$ 4.1 billion in September 2021 and covering approximately 5.4 months of imports, despite the National Bank of Georgia's (NBG) occasional interventions on the foreign exchange market to smooth out currency volatility. Earlier depreciation and rising commodity prices raised inflation pressures in the first half of the year. Consumer price index growth stood at 12.3 per cent year-on-year in September 2021, compared with 2.4 per cent year-on-year in December 2020. To combat inflation, the NBG raised the refinancing rate three consecutive times, from 8 per cent in March 2021 to 10 per cent in August 2021.

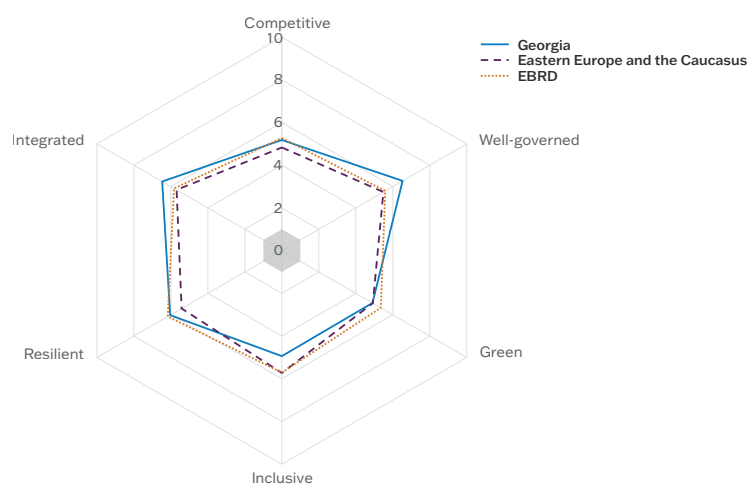
Recovery prospects are cautiously optimistic. GDP growth is forecast to recover to 7.5 per cent in 2021 and accelerate to 5.5 per cent in 2022. The main driver for the overall economic recovery remains the return of tourism, which is a lifeline for many businesses in Georgia. Major risks stem from the slow vaccination rate and potentially extended travel restrictions because of more infectious variants of the Covid-19 virus spreading. Maintaining macro-economic policy discipline, in particular in relation to adherence to the fiscal rule, will be a challenging task.

Policy response to Covid-19

The government implemented a comprehensive package of measures to support the economy in 2020. The total fiscal support package amounted to 3.8 per cent of GDP (Lari 1.86 billion). Economic support measures included the postponement of tax payments, subsidised interest payments on loans and scaling up of the credit guarantee scheme. The central bank lowered capital and liquidity requirements and relaxed regulatory requirements to support loan restructuring.

The fiscal support package for 2021 is expected to reach 2.3 per cent of GDP (Lari 1.2 billion). Previous measures were reintroduced during the second lockdown, including the coverage of utility fees for smaller household users and the exemption from income tax for those in low-paid jobs. In addition, employees in the hard-hit tourism sector are fully exempt from property tax in 2021. The Covid-19 policy response in 2021 is supported by external financing, including the International Monetary Fund programme finalised in April 2021 and Eurobond issue in early 2021.

Assessment of transition qualities (1-10)



Structural reform developments

Despite significant political volatility, the government presented a new 10-year development plan for Georgia. Repeated disruptions to the economy and a difficult environment on the domestic political scene, on top of Covid-19 pandemic-related uncertainties, have reduced the space for reforms. Despite this, in July 2021 the government produced an overarching medium-term development vision to advance the socio-economic development of Georgia. The development plan is supported by ministry-specific strategies setting out development goals, financial needs and planned instruments for the next 10 years.

A new insolvency framework is in place. After adopting the Law on Rehabilitation and Collective Satisfaction of Creditors in parliament in September 2020, the new framework entered into force in April 2021. Before the reforms, the legislation was focused on swift liquidation of debtors in financial difficulties, thus essentially neglecting other restructuring possibilities and the interests of some stakeholders. The new law introduces a new profession of licensed insolvency practitioners and creates incentives to use other restructuring possibilities at an early stage, even before getting to the point of bankruptcy liquidation. It also introduces the possibility of reaching a regulated agreement outside of court. Thereby it is intended to offer adequate protection of creditor rights, ensure timely and efficient insolvency processes and provide an effective rehabilitation framework in line with best international standards. The new regulation is expected to strengthen Georgia's economic and financial system and help resolve Covid-19 pandemic-related bankruptcies more efficiently.

Labour reform law aims to unify interests of workers and employees and bring their rights into line with international standards. A comprehensive labour law reform package was adopted in autumn 2020. It includes extending the scope of the labour supervisory body to the full range of labour rights, prohibiting discrimination and regulating internships and overtime. Labour inspectors will be able to achieve compliance through proactive steps and by giving them the necessary enforcement tools. The new laws bring Georgia's labour legislation into line with relevant international labour standards of the International Labour Organization and European Union Directives and aim to strike a better balance between the rights and interests of workers and employers.

Significant improvements have been made in tax administration and reducing outstanding value added tax (VAT) refunds. In October 2020 the government introduced fully automatic VAT refunds. This should help provide liquidity to the private sector and reduce the outstanding stock of VAT credits. The Georgia Revenue Service has been enhancing its risk-based approach to better identify non-compliant cases and inform individuals and legal entities at an early stage about inconsistencies. It is training its auditors to implement an audit case management system, which should improve productivity and timeliness of audits.

The authorities have completed secondary legislation to support the banking resolution framework. The new regulations, designed to enhance financial resilience, include legislation on resolution plans, a temporary administrator and special manager, recapitalisation tools, and temporary public support and emergency liquidity assistance backed by government guarantees.

The digital agenda has advanced. New electronic services (such as online applications for identity cards and passports, birth certificates, changes of name, new business and land title registrations) were integrated into the Unified Service Portal (www.my.gov.ge) throughout 2020 and 2021 to enable citizens to receive critical services without leaving their homes.