



# Georgia

Country Report March 2019

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# **1.0 Executive summary**

**Georgia, the small South Caucasus country of 3.9mn, expanded by 4.8% y/y in Q4 from Q3's 3.7% y/y, meaning the country expanded by 4.8% y/y in 2018 overall.** That compares to 2017's 5% advance and is not far from Georgia's performance over the medium term, which has remained robust in recent years. This year the government expects the country, increasingly a popular tourist destination, to see growth of 4.5%. Central bank governor Koba Gvenetadze told Reuters last month that he expected the economy to grow by at least 5% in 2019.

**Among the reasons behind the expansion in growth are improved domestic and external demand due to significant foreign capital inflows** - mainly from exports, tourism and remittances - and improved business sentiment, credit growth and capital spending by the government. **However, structural imbalances continue to plague Georgia's macroeconomy**, most notably its large trade deficit, which is financed partly with external borrowing, and its unpredictable currency, the exchange rate of which has varied widely.

**Georgia's trade gap widened by 10% y/y despite exports rising at a robust rate, above that of imports.** Exports rose by 22.9% y/y to \$3.36bn while imports advanced by 14.9% y/y to \$9.12bn in the year. The negative trade balance was \$5.76bn in 2018. Reducing the foreign trade and overall current account deficit has been an ongoing concern in Tbilisi. An oil and gas-importing country, Georgia has struggled to expand its manufacturing base enough to make up for its sizeable energy imports and for its imports of higher added-value goods.

The country saw its current account deficit falling further this year. Georgia posted its first ever current account surplus of \$5.7mn in the third quarter of 2018, swinging from the \$135.2mn deficit it recorded in the same period of 2017.

**Meanwhile, Georgia's central bank expecting strong economic growth and a pick-up in consumer demand this year**, plans to gradually ease interest rates towards 5-6% from the current refinancing rate of 7% over the next two years. Headline inflation is predicted to hover around 3% per annum during 2019-2021, the central bank added. Georgian current account dynamics and Georgian lari exchange rate is not expected to fluctuate much and the central bank would continue to purchase foreign currency on the market this year.

The national lender purchased \$197.5mn on the market in 2018 and has not sold dollars since the start of 2017, increasing the level of its international reserves to \$3.29bn by the end of December from \$3.04bn a year ago.

Georgia's banking sector achieved high profitability in 2018, while, Georgia's London-listed TBC Bank is [presently under investigation](#) for "facts of the legalization of illicit income", according to the Prosecutor's Office of Georgia. TBC rejected the allegations. Resigned chairman and co-founder of TBC Bank, Mamuka Khazaradze, on February 26 was reported as saying that he and his deputy Badri Japaridze were forced to step down following pressure from the Georgian government amid investigations related to operations carried out by the lender in 2007-2008, which allegedly involved conflicts of interest.

## **2.0 Politics**

### **2.1 Georgia's Prosecutors reveal alleged frauds of TBC Bank founders**

**The Prosecutor's Office of Georgia has publicised facts it says have been established so far in investigations related to alleged fraud perpetrated by the co-founders, and until recently top managers, of TBC Bank.**

The [statement](#) referring to Mamuka Khazaradze and Badri Japaridze was issued "to address the public interest", the Office said.

Prosecutors claim that the bank issued two loans worth \$17mn each that indirectly went to the pair. The bank is said to have quickly declared the two credits as non-performing debts, while not proceeding to attempt to recover the money. If the two used the money to increase bank's capital as previously speculated, then the legal implications of the action would be major.

Khazaradze and Japaridze in principle would risk losing part of the shares subject to a subsequent court decision.

Prosecutors claim that TBC Bank extended the two loans in April-May 2008 to two companies: Samgori M Ltd and Samgori Trade Ltd. The companies belonged to "a businessman close to Mamuka Khazaradze", their statement said.

On the same day, the money was transferred to Khazaradze and Japaridze's personal accounts, prosecutors claim. The prosecutors do not state whether there were lending contracts signed between the two companies and the two bank officials—but further details revealed by them indicate that there were such inked contracts.

In October-November 2008, the deadline for the loan repayment was increased for one year without any particular reason. No principal or interest had been paid by that time. By the end of 2008, the loans were declared non-performing without any particular reason, it is said. Before the terms established by the bank regulations, TBC Bank wrote off the loans, meaning that they "were moved to an external balance account", according to the prosecutors.

TBC Bank did not demand a refund of the money from guarantors. It did not withdraw the money from the accounts of the two companies or confiscate properties used as mortgages for the loans.

Prosecutors claim that normal crediting operations were carried out in relation to the two firms during the whole process.

"It should be highlighted that despite the fact that the loans given to Samgori Trade Ltd and Samgori M Ltd were classified as bad loans, TBC Bank continued crediting the companies of the businessman close to Mamuka Khazaradze and gave them other loans on the basis of other loan agreements," the press release on the statement reads.

In a final step, TBC Bank replaced the two debtors with a company registered in an offshore region, with no prior activity in Georgia and with no collateral. “An agreement had been signed with the company registered offshore according to which this company undertook the obligation to pay the loan in the amount of \$17mn instead of Samgori M Ltd and Samgori Trade Ltd and obtained the right to demand money from Khazaradze-Japaridze,” the release further reads.

Prosecutors avoid explaining why the two were mentioned in the “agreement”. The sole logical explanation is that the two companies further lent the money to the two bank officials in line with separate lending contracts, but even so it remains unclear why the offshore companies’ claims on the two were mentioned in the “agreement” between TBC, the initial debtors (Samgori companies) and the unnamed offshore companies (the final creditors). However, such documents (the “agreement”) if shown as evidence by the prosecutors, might be a strong element of the case against TBC Bank’s founders.

At the same time of the signing of the agreement with the offshore companies, TBC Bank exempted immovable properties mortgaged for loan insurance.

It should be noted, prosecutors said, that the trustee of the offshore company was a citizen of Georgia, P. Gh, who was a member of the credit committee during the providing of the loans to Samgori M Ltd and Samgori Trade Ltd and who held a high managerial position at TBC Bank when these companies were replaced by the company registered offshore.

## 2.2 Three MPs quit Georgian Dream in row over appointing lifetime judges

**Three MPs of the ruling Georgian Dream party—including the influential Eka Beselia, a former head of the committee charged with appointing lifetime judges under the new Constitution’s provisions—quit the party last week leaving it with only 112 lawmakers in the 150-seat parliament.**

Significantly, this is less than the 3/4 majority required for enforcing constitutional amendments, although the reduction in seats poses no essential risk to the government’s stability.

A day after MP Levan Gogichaishvili announced he was quitting Georgian Dream, Beselia and Beka Natsvlishvili also declared they were leaving the party.

Several other lawmakers of Georgian Dream have been expelled from the party, InterPressNews [reported](#), citing unofficial sources.

Lawmakers who voted in favour of the draft law on the suspension of appointing lifetime judges were reportedly expelled from Georgian Dream. That places serious question marks over the ruling party’s good faith on this topic, critics said.

Beselia resigned last autumn from the parliamentary committee charged with appointing lifetime judges to the High Court, claiming that the procedures

should be thoroughly revised in order to appoint judges with the best credibility. The nominees have been broadly criticised for their political bias under previous regimes.

Georgian Dream has asked the Venice Commission, an advisory body of the Council of Europe, to get involved in the consultations on the appointment procedure lawmakers will draft for lifetime judges, Irakli Kobakhidze, executive secretary of the party, announced on February 20. But one day later, most of the party members refrained from supporting the key bill regarding the postponement of appointing lifetime judges, a bill that would have made time for broad consultations on the appointment procedures.

Attempts to regulate this issue, after the new Constitution came in effect at the end of last year, prompted conflicts within the ruling party and criticism from the civil society organisations that fear the appointment of politically-biased judges.

“We express our full readiness to prepare the proposals for the lifetime appointment of judges, which will be in compliance with the Constitution of Georgia and the recommendations of the Council of Europe. For this purpose, we are addressing the Venice Commission to get involved in the process,” Kobakhidze said.

## **2.3 Georgia’s economy 16th freest on Heritage’s Economic Freedom Index 2019**

**Georgia’s score on The Heritage Foundation’s 2019 Index of Economic Freedom is 75.9, making its economy the 16th freest of the 180 assessed, the US-based conservative think tank said on January 30.**

The country’s overall score has decreased by 0.3 of a point compared to its performance on the 2018 index, with a sharp drop in judicial effectiveness and lower scores on government integrity and monetary freedom exceeding a big gain in financial freedom, Heritage said. Georgia is ranked 8th among 44 countries in the Europe region, and its overall score is well above the regional and world averages.

Since the 2003 “Rose Revolution,” reforms by successive administrations have reduced petty corruption, cut regulation, simplified taxes, opened markets, and developed transport and energy infrastructure, the think tank said, adding: “The government hopes that further reductions in regulation, taxes, and corruption will attract foreign investment and stimulate growth. Its maintenance of monetary stability and overall sound fiscal health has fostered macroeconomic resilience. Nonetheless, deeper and more rapid institutional reforms to enhance judicial independence and effectiveness are still needed to ensure dynamic and lasting economic development.”

Georgia was forcibly incorporated into the Soviet Union in 1921 and regained its independence in 1991. Russia invaded in 2008 and continues to occupy territory in Georgia’s South Ossetia and Abkhazia regions. Georgia’s economy has improved noticeably after years of economic downturn, Heritage said. Agriculture or related industries employ over half of the workforce. Georgia signed an Association Agreement with the European Union in 2014 and is an

official aspirant for Nato membership.

For Georgia in the rule of law category on the index, Heritage said: “Property rights are recognized, and the government has made property registration easier. Only a quarter of private landowners hold clear title to their property. Although the constitution and laws provide for an independent judiciary, political pressure threatens impartiality. Georgia has made great progress in fighting petty corruption, but high-level corruption by public officials remains a problem.”

For Georgia’s government size, it stated: “The flat income tax rate is 20 percent, and the flat corporate tax rate is 15 percent. Other taxes include value-added and dividends taxes. The overall tax burden equals 25.8 percent of total domestic income. Over the past three years, government spending has amounted to 29.6 percent of the country’s output (GDP), and budget deficits have averaged 1.1 percent of GDP. Public debt is equivalent to 44.9 percent of GDP.”

Looking at Georgian regulatory efficiency, Heritage said: “Georgia’s economy has maintained strong momentum in liberalizing economic activity. It takes only two procedures and two days to start a business, and no minimum capital is required. The nonsalary cost of hiring a worker is not burdensome, but the labor market lacks dynamism. The government is increasing subsidies for green energy and transport projects.”

In its open markets conclusions for Georgia, the think tank noted: “The combined value of exports and imports is equal to 112.6 percent of GDP. The average applied tariff rate is 0.7 percent. As of June 30, 2018, according to the WTO, Georgia had 66 nontariff measures in force. There are some restrictions on foreign ownership of agricultural land. With the banking sector growing, access to financing has improved. Capital markets continue to evolve, but the stock exchange remains small.”

## **2.4 Georgia “faces democratic backsliding, making it vulnerable to high-level corruption”: Transparency International**

**Georgia “faces democratic backsliding, making it both vulnerable to high-level corruption and a country to watch moving forward,” Transparency International (TI) said on January 29 after releasing the 2018 edition of its Corruption Perceptions Index (CPI).**

Although the small nation fared better than any other country in the Eastern Europe & Central Asia region—it placed 41st of 180 assessed countries with 58 points compared to 46th in the 2017 survey with 56 points (the points scale runs from 0 which represents “highly corrupt” to 100 which represents “very clean”)—it has come in for some firm criticism from TI.

In a [press release](#) on the CPI results, TI said: “Despite an urgent need to investigate cases of corruption and misconduct in the government, Georgia has failed to establish independent agencies to take on this mandate.

“Impunity contributes to public distrust. According to a [recent poll](#) conducted by

our chapter, [Transparency International Georgia](#), 36 percent of citizens believe that public officials abuse their power for personal gain. This is up from only 12 per cent in 2013. Progress in anti-corruption will continue to stall and reverse if the Georgian government does not take immediate steps to ensure the independence of institutions, including the judiciary, and support civil society, which enhances political engagement and public oversight.”

## 2.5 Georgia retains “Partly Free” ranking: Freedom in the World 2019 survey

Georgia has again been [categorised as “Partly Free”](#) by the annual **Freedom in the World survey**. However, the 2019 edition of the ranking shaves a point off the country’s Aggregate Freedom Score. It now stands at 63/100 (100 = Most Free).

The latest survey, issued by US-based watchdog Freedom House late on February 4, makes no changes to Georgia’s scores in the sub-categories of Freedom Rating, Political Rights and Civil Liberties. Georgia again scored 3/7 for each (7 = Least Free).

Freedom House was yet to release the report detailing the reasoning behind the latest scorecard for Georgia.

The organisation entitled its latest report “Democracy in Retreat” in a reflection of events around the world last year.

On February 4, Laura Linderman, a representative of the Atlantic Council, said in an interview with the Voice of America that [if democratic progress in Georgia is reversed the country will disappear from the agenda of many western countries](#), including the US.

Her remarks came with Georgia’s authorities preparing to appoint members of the Supreme Court. Lifetime members of the court will be appointed for the first time under procedures outlined in the country’s new Constitution, which came into force in December. The High Council of Justice will nominate the members who are to be endorsed by Parliament.

“Georgia is distinguished with democratic characteristics in the region and beyond it... If democracy is reversed, Georgia will lose its main component. Georgia is in a difficult neighbourhood, in a difficult situation in terms of security, the economy is growing, but it is not so great compared to other countries. If Georgia loses its democracy, it will disappear from the agenda of many western countries, including the United States,” Linderman said.

## 2.6 Polls & Sociology

**Jobs, poverty top Georgians’ agenda**

**Finding a job is ranked by 51% of Georgians as among their top three issues, followed by poverty (32%) and rising prices (28%), with all three major concerns demonstrating households’ poor economic conditions, according to a US National Democratic Institute (NDI) poll carried out in December.**

Support for Georgia taking Nato and EU membership remains robust, but the issue of joining the bloc is seen as rather unimportant, the survey also

concluded. Nato membership was mentioned among the top issues by only 4% of respondents, while European Union membership ranked even lower at 2%.

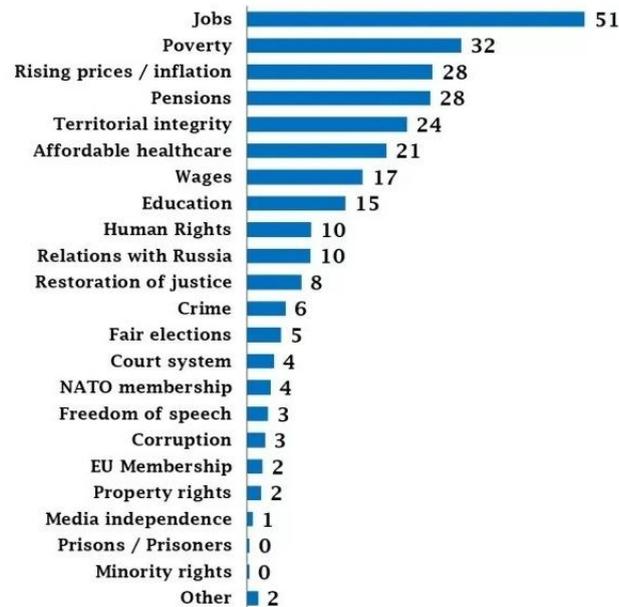
Territorial integrity was seen as a much more important problem, regarded by 24% of respondents as a key issue, given that Georgia has breakaway territories that are defended by Russian armed forces.

Notably, issues related to democracy were mentioned by rather few respondents. Only 4% saw problems related to the court system, although 8% wanted a revamp of the judiciary. Primary concerns related to poverty were the pressing matters.

Some 83% of respondents supported Georgia's integration into the EU, with 9% against. As for Nato, 78% supported membership while 13% did not.

The majority of those responding to the opinion poll said the judiciary was developing in the wrong direction. A total of 30% said there had been no changes in the judiciary they could point to, and only 16% thought that the system was developing in the right direction.

**Georgia: Most important national issues. Name up to three (q1)**



## 3.0 Macro Economy

Georgia - Main Macro Indicators	2012	2013	2014	2015	2016	2017	1Q18	2Q18
GDP real growth (y/y, %)	6.4	3.4	4.6	2.9	2.7	5.0	5.3	5.6
GDP (per capita, \$)	3,523.4	3,599.6	3,676.2	3,766.6	3,864.6	4,078.5	987.1	/
GDP: Final consumption expenditure, (GEL mn)	23,733.2	23,671.8	25,570.7	27,318.7	28,241.5	30,381.7	7,581.2	7,462.8
GDP: Gross capital formation, (GEL mn)	7,575.4	6,652.9	8,688.8	10,004.3	10,999.8	12,133.3	2,842.4	3,190.9
GDP: Exports, (GEL mn)	9,982.9	11,997.9	12,518.3	14,206.8	14,837.8	19,177.3	4,549.7	
GDP: Imports, (GEL mn)	15,124.2	15,475.2	17,627.3	19,774.3	20,187.5	23,650.1	6,022.9	

Source: bne IntelliNews, CEIC

### 3.1 Macroeconomic overview

#### Georgia's GDP up 3.5% in January

Georgia's estimated GDP growth rate in January was 3.5%, the country's statistics office said on February 28.

Real growth in January compared to the same month of last year was posted for the following sectors: trade, hotels and restaurants, financial intermediation and real estate, renting and business activities. Declines in growth were recorded for manufacturing and construction.

#### Georgia's 2018 GDP growth recorded at 4.8% after Q4 acceleration

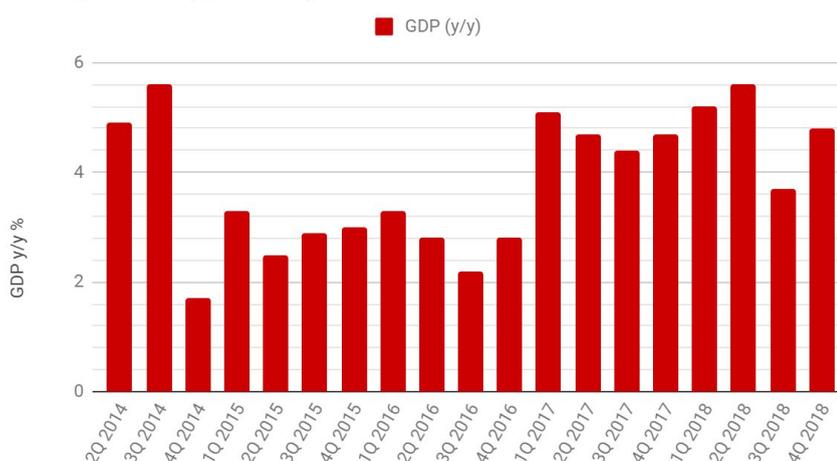
Georgia's GDP growth accelerated to 4.8% y/y in Q4 from Q3's 3.7% y/y, meaning the country's expanded by 4.8% y/y in 2018 overall.

That compares to 2017's 5% advance and is not far from Georgia's performance over the medium term, which has remained robust in recent years.

This year the government expects the country, increasingly a popular tourist destination, to see growth of 4.5%.

Central bank governor Koba Gvenetadze told Reuters last week that he expected the economy to grow by at least 5% in 2019.

Georgia GDP (quarters)



## Turnover in Georgia's business sector up 17.3% y/y in Q3

The aggregated turnover in Georgia's business sector rose by 17.3% y/y to GEL21.8bn (\$8.2bn) in Q3, statistics office Geostat has announced.

Growth was driven by companies in the arts, entertainment and recreation sector (+93.8% y/y). The sector has been the main driver throughout the year. |Real estate firms also increased their business in the third quarter (+17.9% y/y), despite the negative performance posted by construction.

For the whole January-September period, total business turnover soared by 18.4% y/y to GEL59.7bn (\$22.5bn).

The largest turnover was reported in retail (and services to households), namely at GEL26.8bn (nearly half of the total) in January-September. The rise for this sector was 12.0% y/y (14.9% y/y in Q3 alone). In construction, in contrast, turnover increased by only 3.4% y/y in January-September (and contracted by 4.4% y/y in Q3).

The number of employees increased by 3.3% y/y to 665,500 in Q3.

Business Turnover [GEL mn]	Q3 18	Jan-Sep 18	y/y	Q3 y/y
By kind of economic activities, total	21,829	59,732	18.5%	17.3%
Agriculture, forestry and fishing	102	319	9.6%	2.9%
Mining and quarrying	194	559	15.5%	5.3%
Manufacturing	2,332	6,676	9.9%	0.4%
Electricity, gas, etc	715	2,375	12.2%	14.4%
Water supply; sewerage, etc	72	196	10.2%	5.1%
Construction	1,874	4,988	3.4%	-4.4%
Wholesale and retail trade; services to households	9,610	26,825	14.9%	12.0%
Transportation and storage	1,409	3,820	12.5%	11.3%
Accommodation and food service activities	531	1,328	14.7%	11.9%
Accommodation	269	614	14.2%	8.8%
Food and beverage service activities	263	713	15.1%	15.2%
Information and communication	435	1,249	2.8%	2.0%
Real estate activities	315	883	18.6%	17.9%
Professional, scientific and technical activities	369	1,012	10.9%	10.2%
Administrative and support service activities	389	910	16.2%	13.0%
Education	72	269	11.6%	9.6%
Human health and social work activities	252	777	9.5%	7.1%
Arts, entertainment and recreation	3,120	7,435	93.8%	136.6%
Other service activities	39	111	17.6%	9.0%

Source: Geostat

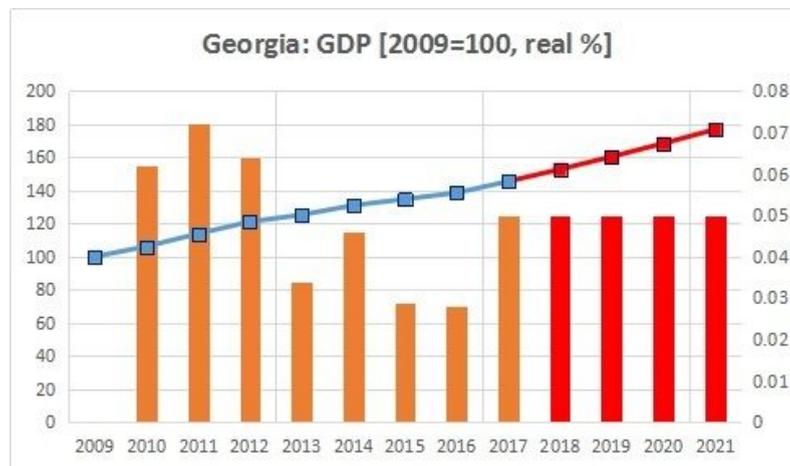
## 3.2 Macro outlook

### Georgia's central bank baseline scenario sees 5% GDP growth across 2019-2021

Georgia's GDP will rise by 5% per annum during 2019-2021, under a [baseline scenario](#) published by its central bank.

Headline inflation will hover around 3% p.a. under the baseline scenario (2.9% in 2019), allowing the regulator to ease its policy rate by 0.5pp in 2019 and 2020 and by 0.25pp in 2021. The nominal Georgian lari exchange rate versus the US dollar will remain steady, resulting in the currency strengthening in real terms.

Under a scenario with a negative external shock formulated by the central bank, Georgian GDP would only rise by 2% in 2019, 2.5% in 2020 and 3.5% in 2021. Under a compiled strong demand scenario, the growth rate would accelerate to 6% in 2019 and gradually ease to 5% in 2021.



**World Bank sees robust, steady 5% GDP growth in Georgia from 2018 to 2021**

**The World Bank has revised its estimate for Georgia’s GDP growth in 2018 upwards to 5% from the 4.2% it anticipated last June.** It added in the latest edition of its Global Economic Prospects report, released late on January 8, that it now expects the country to maintain the same robust growth rate from 2019 to 2021.

The revised outlook is slightly more optimistic for 2019, as it adds 0.2pp to the growth expectation versus the June 2018 forecast.

Among the risks, the World Bank spots possible spillover effects from Turkey’s economic downturn via the flow of FDI to Georgia.

The International Monetary Fund in its latest World Economic Outlook issue, released last October 9, revised its forecast for Georgia’s 2018 GDP growth to 5.5% from the 4.5% it projected in April. Independent projections put the country’s expected growth this year at above 6%, but caution is shown when it comes to possible strengthening adverse effects stemming from the Turkish lira crisis.

Georgia’s GDP growth was estimated at 4.9% y/y for January-September 2018 by the country’s statistics office, while it improved to 5.1% y/y for January-October. But the monthly GDP estimates are volatile, and are subject to deep revisions. On a broader perspective, growth rates of around 5% as seen in 2017 and 2018 have not yet resulted in visible improvements in the standard of living in Georgia.

# 4.0 Real Economy

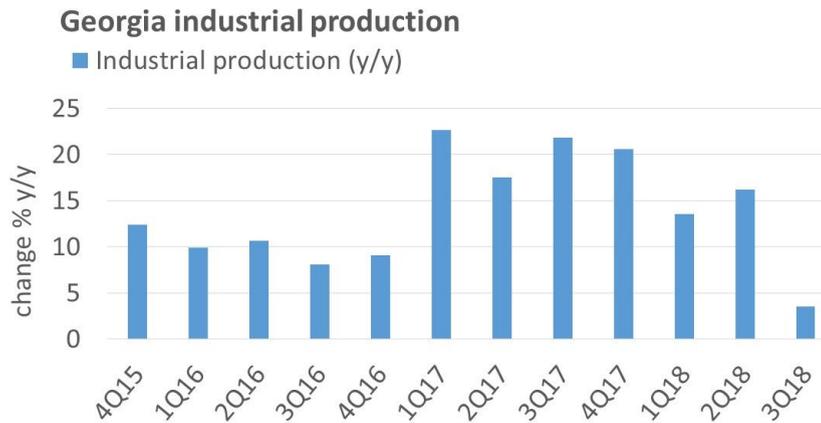
## 4.1 Industrial production

**Industrial production rises 3.5% y/y in 3Q18**

**Georgia's industrial production increased 3.5% y/y in the third quarter of 2018, slowing from a 16.2% y/y in the previous quarter,** according to the National Statistics Office of Georgia.

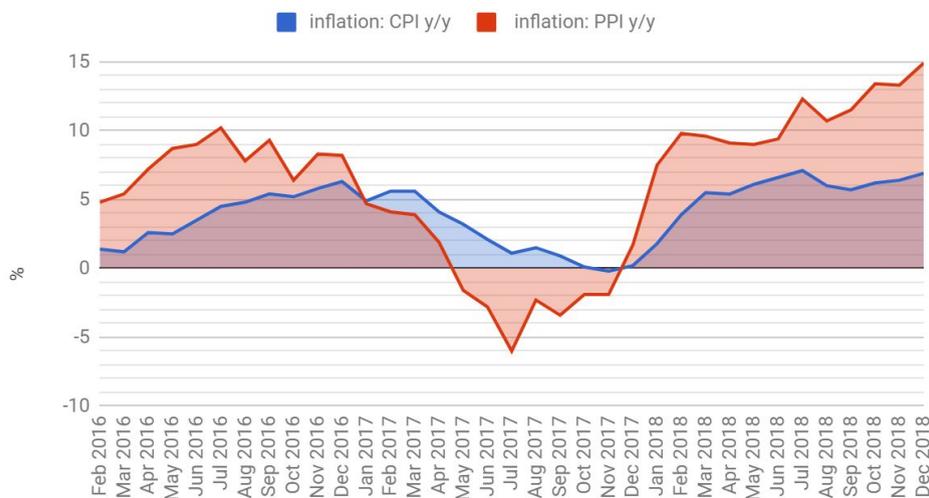
It was the weakest growth rate since the first quarter of 2015 as production expanded slowly for all sectors: for mining and quarrying (5.2% in 3Q18 from 30.5% in 2Q); electricity, gas, steam and air conditioning supply (14.4% in 3Q18 from 16.6% in 2Q); manufacturing (0.4% in 3Q18 from 15.1% in 2Q) and water supply sewerage, waste management and remediation activities (5.1% in 3Q18 from 11.9% in 2Q).

Industrial production y/y in Georgia averaged 13.0% from 2000 to 2018.



## 4.2 Inflation

Georgia inflation: CPI vs PPI



## 4.2.1 CPI dynamics

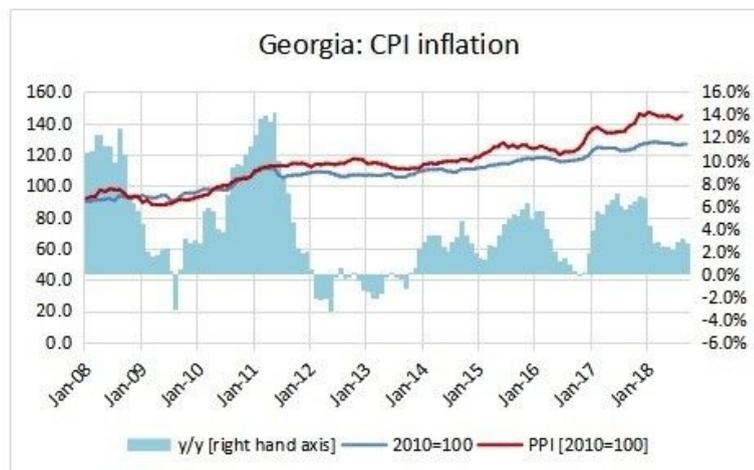
### Headline inflation eases in Georgia

Consumer prices in Georgia increased by 1.5% y/y in December, easing from the 2.7% y/y rise seen in September, the national statistics office reported. Headline inflation has thus dropped to its lowest level in nearly two years with prices hovering at a steady level throughout this year.

The monetary board of the National Bank of Georgia on January 30 cut its refinancing rate by 25bp to a still restrictive rate of 6.75%. Annual inflation in Georgia decreased at the beginning of 2018 and, in line with previous forecasts, remains within the target rate of 3%, the central bank said. According to current forecasting, inflation both this year and in the medium term will fluctuate around the target rate.

According to central bank estimates, there is still the necessity of policy normalisation—that is, gradual policy easing. However the speed of normalisation will depend on how fast the output gap closes on the one hand and how strongly increased regional macroeconomic risks are transmitted to the Georgian economy, on the other.

Despite the slight disinflation seen as of October, the prices of individual goods have changed significantly both directions.



## 4.2.2 PPI dynamic

### Georgia's PPI for industrial products up 3.8% y/y in Dec consolidate disinflationary trend

Georgia's Producer Price Index (PPI) for industrial products increased by 3.8% y/y in December, decelerating from 6.6% y/y in August, according to the national statistics office.

The rise in food, metal and energy prices contributed the most to the prices' dynamics. The industrial price figures consolidate the disinflationary trend (with the consumer price inflation easing below the 3% y/y target level), justifying central bank's decision of lowering the monetary policy interest rate to 6.75%. Nonetheless, higher energy and food prices might pass through to consumer prices posing inflationary pressures. The import prices rose more than export prices on a longer-term upward trend.

**GEORGIA: PRODUCER PRICE INDEX FOR INDUSTRIAL PRODUCTS**  
(THE SAME MONTH OF THE PREVIOUS YEAR =100)



### 4.3 Fixed investment

Georgia -Fixed capital investment	2012	2013	2014	2015	2016	2017	1Q18	2Q18
Gross fixed investment capital formation (GEL mn)	3,936.1	3,540.5	4,260.5	3,951.7	4,358.8	4,481.7	989.6	1,304.6
Gross fixed capital formation (% of GDP)	28.8%	24.6%	29.5%	31.3%	32.4%	31.6%	31.1%	35.8%

Source: CEIC

#### EIB lends Georgia €250mn to improve infrastructure

The European Investment Bank (EIB) and the Georgian government signed a deal on a €250mn loan to finance infrastructure projects in Georgia on 19 February, Georgia Today reported. Georgian Prime Minister Mamuka Bakhtadze and vice-president of the EIB, Vazil Hudak, signed the deal in Tbilisi.

The money will be used for “vitaly important” infrastructure projects, said the government of Georgia, such as the construction and renovation of the Rustavi-Red Bridge-Sadakhlo highway.

“Such highways significantly increase Georgia’s transit role,” stated Bakhtadze. “EIB is the financial instrument of the EU and our activities for Georgia confirm that you are part of Europe. The loan will provide opportunities for Georgia to come closer to the EU and use its geopolitical location to connect Europe with Asia,” said Hudak.

Bakhtadze said he considers the EIB an important partner in Georgia’s development. The new infrastructure projects should also create new jobs in Georgia.

## 4.4 Labour and income

### 4.4.1 Unemployment, income dynamics

**Georgia's unemployment rate inched down in 2017**

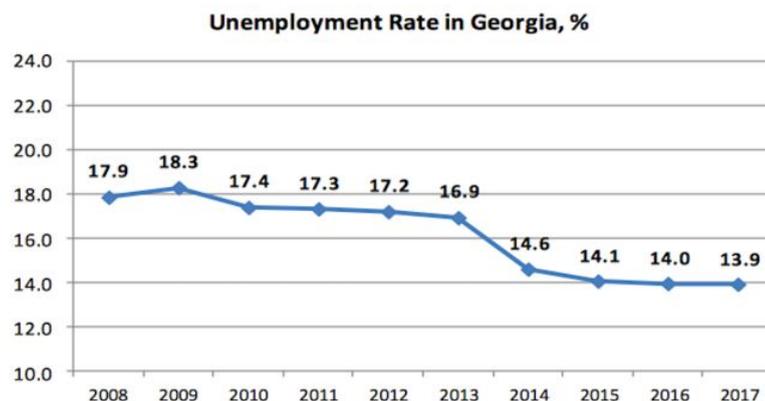
**Georgia's unemployment rate dropped by 0.1 of a percentage point (pp) to 13.9% in 2017, continuing the downtrend of the last eight years, data from the state statistics office Geostat shows.** Unemployment remained highest among young people, reaching as high as 29.6% for 20-24 year olds, even though it declined by 3.2pp for this age group compared to 2016.

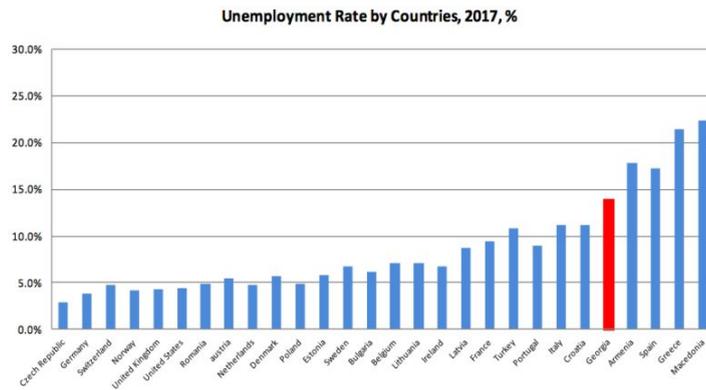
The unemployment rate declines steadily as ages increase though, as Geostat points out, the low level for the 65+ age group is due to the high inactivity rate in this age group.

By region, Geostat reports an increase in the unemployment rate in the capital Tbilisi (by 1.6pp), and in regions Shida Kartli (2.0pp), Kvemo Kartli (3.5pp) and Imereti (1.2pp). The largest declines were in Adjara and Samegrelo-Zemo Svaneti, where unemployment fell by 5.8pp and 3.4pp respectively.

Georgia's unemployment rate is higher than the rates of most EU countries, though below the rates of crisis-hit Spain and Greece, most of the Western Balkan countries, and neighbouring Armenia.

Geostat made fundamental changes to how it compiles its labour force statistics in 2017, after new data in the population dynamics and the population's geographic distribution in the country were revealed by the 2014 census. At the same time, new measures were taken with support from the World Bank and other international organisations and partners to improve the labour indicators.





Source: International Labour Organization.

### Job creation lags behind economic growth in Georgia

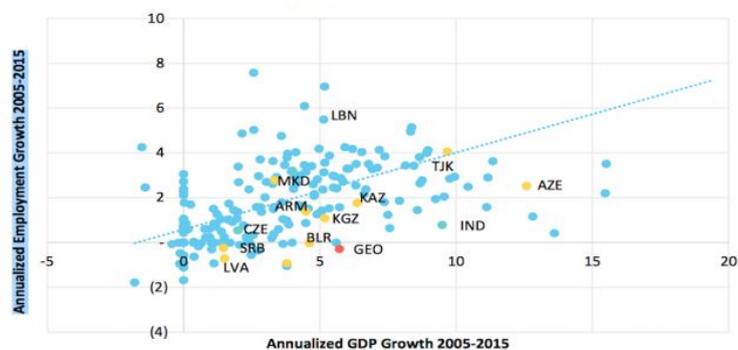
**Georgia has achieved sustained economic growth over the past two decades, despite a dip during the crisis of the late 2000s, but while this has increased prosperity and reduced poverty, job creation has failed to keep up with economic growth, a World Bank report said.** This has worrying implications for the future, as lack of employment opportunities is a key contributor to emigration.

The report reveals that most Georgian firms are small and struggle to grow. As a result, employment is concentrated in larger and relatively older firms. “Georgia has done a tremendous job in creating the environment for firm entry, but more reforms are needed to help firms increase productivity, grow, and thrive in an increasingly competitive global environment,” commented Mohamed Ihsan Ajwad, World Bank Senior economist and one of the lead authors of the report. “Our analysis shows that small and individual firms fail to grow to medium-sized firms.”

The “missing middle” is revealed by employment data. While individual firms represented over 70% of total registered firms, they accounted for just 11% of employment in registered firms. Private sector employment is concentrated in small firms with fewer than 20 employees, or large firms with more than 100 employees.

World Bank economists also point out that while Georgia has made considerable progress putting business-friendly policies in place — the country soared to ninth place on the latest Doing Business index — “political instability remains a significant challenge for firms”.

**Figure E55. Growth has not created employment in Georgia**  
Relationship between GDP and employment growth, 2005-2015



Source: authors using WDI. Notes: The linear fit for the period 2005-2015 is  $E = 0.3428 \text{ GDP} + 0.5877$

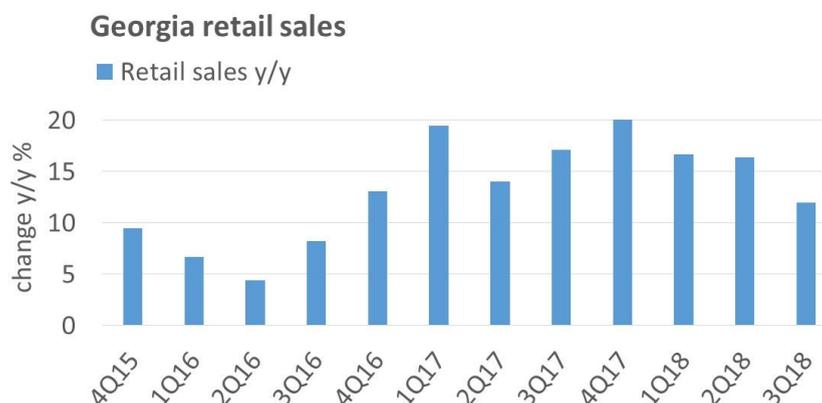
## 4.4.2 Retail sector dynamics

Retail sales rises at a slower rate of 12% y/y in 3Q18

Retail sales in Georgia increased 12% y/y in the third quarter of 2018, easing from the 16.4% y/y rise in the previous quarter, according to CEIC data.

In 2017, retail trade turnover reached GEL9,929.8mn, up from GEL8,101.9mn last year. Retail sales, which has been growing at a strong double-digit pace for several years, grew by only 8-9% in 2015-16 as wage growth slowed and unemployment rose.

Retail sales y/y in Georgia averaged 16.5% from 2000 to 2018.



## 5.0 External Sector & Trade

### 5.1 Balance of payments, current account

Georgia - External Trade	2012	2013	2014	2015	2016	2017	2018*	2019* Jan
External trade turnover (\$ mn)	10,433	10,933	11,463	9,505	9,408	10,675	12,473.4	826.8
Export (FOB) (\$ mn)	2,377	2,910	2,861	2,205	2,113	2,735	3,354.3	238.8
Import (CIF) (\$ mn)	8,056	8,023	8,602	7,300	7,295	7,939	9,118.5	588.0
Balance (\$ mn)	-5,680	-5,112	-5,741	-5,096	-5,181	-5,204	-5,763.6	-349.2
Export excluding re-export (\$ mn)	1,606	1,812	1,873	1,637	1,657	2,070	2,297.1	158.9
Current account BPM6 (\$ mn)	-1,853.0	-934.7	-1,763.6	-1,684.3	-1,934.9	-1,311.1	/	/
Current account to GDP (%)	-11.7%	-5.8%	-10.7%	-12.2%	-12.9%	-8.8%	/	/

Source: Geostat

## 5.1.1 Import/export dynamics

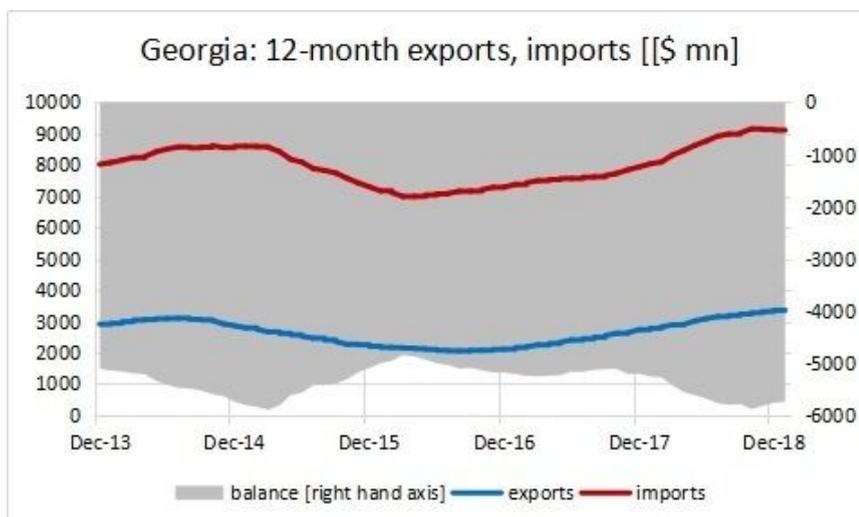
**Georgia's trade gap narrows as imports shrink in Nov-Jan**

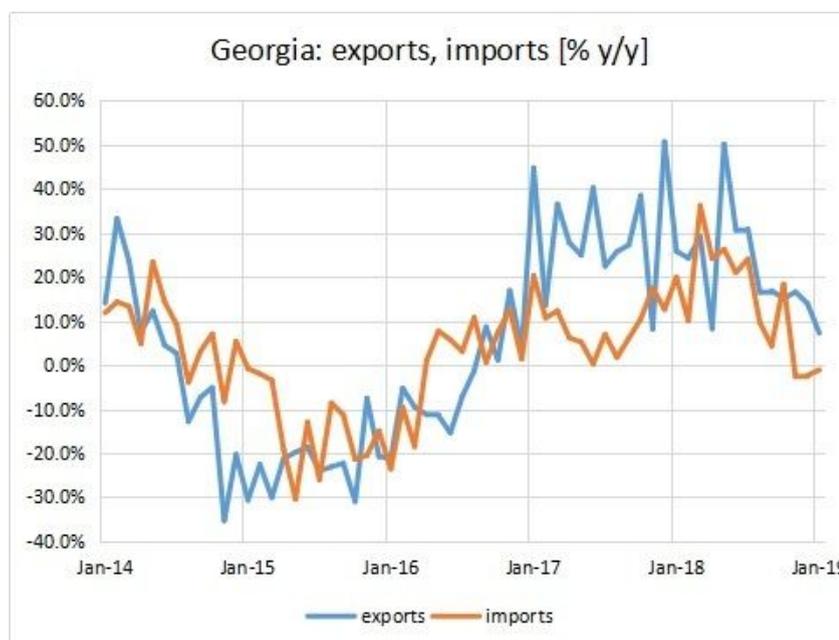
**Georgia's trade gap contracted by double-digit rates in November and December and by 6% y/y in January, as imports posted negative dynamics in each of the three months.** But the trade deficit remains a threat to the country's macroeconomic stability, say economists.

The improvement comes after the country's trade gap widened by 15% y/y to \$5.9bn (some 37% of the country's GDP in 2018) in the 12-month period as of October 2018. The annual rise in the rolling 12-month trade gap eased to 9.2% y/y as of January already.

The trade and current account deficits are a major threat to Georgia's macroeconomic stability and exchange rate. Georgia's central bank has managed to avoid any significant depreciation through 2018, though.

Exports increased by robust rates of 14%-17% y/y in November and December and by 7.3% y/y in January, the statistics office informed. The 12-month exports as of January were 21.2% up y/y, having increased visibly faster than the imports that advanced by only 13.3% y/y under the same metrics. In fact, exports have increased faster than imports since April 2017 and exports' performance (measured as the differential between exports' and imports' annual growth rates) has been as high as 20pp in some of the months -- but the volume of imports is so much higher than the exports (\$9.1bn versus \$3.3bn in the 12-month period ending January) that even moderate growth in imports results in wide supplementary trade deficits.





## 5.1.2 Current account dynamics

**Georgia's current account deficit narrows marginally in Jan-Sep**

**Georgia's current account surplus amounted to \$11.9mn (GEL30.1mn) in Q3, 2018, the central bank reported under BPM5 methodology (the surplus was \$9.9mn under BPM6).**

The trade of goods and income account made a negative contribution, but services and current transfers offset this, the monetary authority noted. In the whole January-September period, the current account balance produced a \$783mn deficit—1% smaller than in the same period of 2017.

The net import of goods widened by 14% y/y to \$3bn. The net export of services rose impressively, by 15% y/y to \$1.9bn in the three-quarter period, but it barely covered two-thirds of net imports.

The current transfers covered the remaining part of the trade gap: they increased by 11% y/y to over \$1bn. Out of this, \$639mn (17% up y/y) was formed by wage remittances. The official reserves at the central bank improved by \$142mn in the year-to-date period—which, however, translated into a 38% smaller advance compared to the first three quarters of 2017.

Net foreign direct investments in Q3 amounted to \$262.5mn accounting for 6.3% of the quarter's GDP, the central bank said. The largest investment inflows were directed to the manufacturing, energy, transport and real estate sectors.

## 5.1.3 Capital flows

**12-month net remittance to Georgia 20% up y/y to \$1.3bn in Aug**

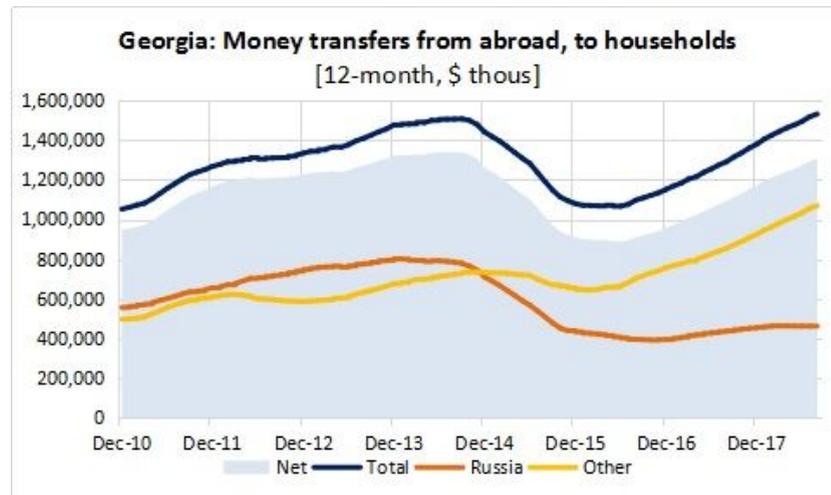
**Net money transfers from abroad to Georgian households (largely wage transfers) in the 12 month-period ending August increased by nearly 20% y/y to \$1.30bn according to *bne Intellinews* calculations based on central bank data.**

Gross inflows were up 19% y/y to \$1.53bn, equivalent to roughly 10% of the country's GDP. Wage remittances finance the largest part of the current

account gap that exceeded 10% of GDP last year and remains a key problem this year as well.

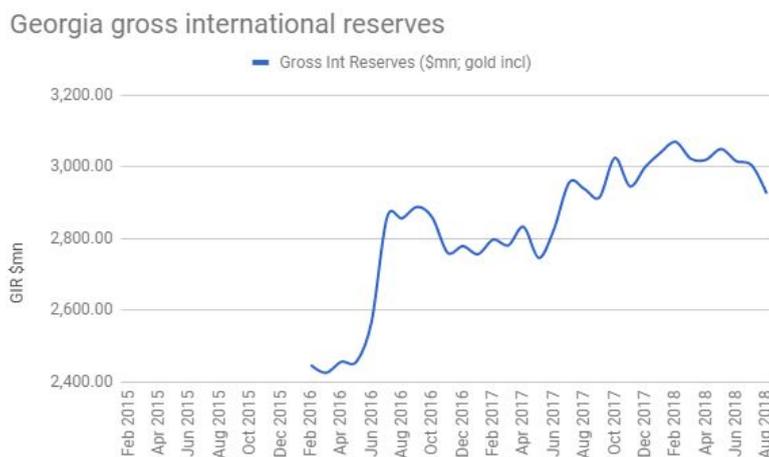
Georgia's GDP is set to rise from some \$15bn in 2017 to \$16bn this year. Of the \$1.53bn gross transfers in the rolling 12 months, \$463mn (up 5.7% y/y) were transfers from Russia. Gross transfers from other countries surged by 25% y/y to \$1.07bn. Since January 2015, transfers from countries other than Russia exceeded remittances from Russia.

In August alone, the volume of money transfers from abroad to Georgia rose by 11.4% y/y to \$135.6mn. In the same month, \$18.9mn (down 2.5% y/y) was transferred out of the country.



## 5.1.4 Gross international reserves

**Gross international reserves in Georgia amounted to USD3,289.82mn in December 2018, up from USD3,152.59mn in September, according to the National Bank of Georgia. Of which, foreign currency reserves made up the majority at USD3,089.07mn in December.**



## 5.2 FDI

Georgia - FDI	2011	2012	2013	2014	2015	2016	2017	2018 Q1	2018 Q2	2018 Q3
FDI (\$ mn)	1,130.3	1,022.9	1,020.6	1,817.9	1,652.5	1,565.8	1,894.5	287.0	389.1	322.6
FDI (% of GDP)	7.51	5.25	5.93	10.84	11.89	11.27	11.88	7.5		

Source: Geostat, CEIC

### European investors push up Georgia's FDI

The value of foreign direct investment in Georgia across the rolling four quarters ending June increased by 19.4% y/y to \$1.82bn and accounted for an impressive ratio of approximately 12.2% of period's GDP, according to data released by the national statistics institute on September 10.

The growth rate remained close to last year's 21% y/y advance, to \$1.89bn or 12.5% of GDP.

European investors poured into Georgia during the four-quarter period, delivering 2.4 times more capital than one year earlier, and they accounted for half of the period's total FDI in the country (\$900mn). Beside activity in the investments hubs where multinationals from the Netherlands and the UK base their headquarters, investors from Czechia (\$206mn, 234% up y/y) were particularly active. Chinese investors also doubled their contribution, taking it to \$79mn.

On a broader perspective, FDI in the rolling four-quarter period remained above 10% of GDP, where it increased to starting with Q3, 2014. In value terms, the FDI returned to the pre-crisis period (before 2008) but as a percentage of GDP it still lags behind the peak value of 19% seen in Q2, 2008.

By economic sector, the financial sector (\$400mn in the four-quarter period) as well as the sectors of transport (\$365mn) and energy (\$315mn) concentrated half of the FDI. The investments in the country's financial sector soared 4.2 times y/y in the period, while those in the energy sector increased by 3.5times.



FDI in Georgia by sector ['000 \$]	Q2, 2018	2017 y/y	Q1 y/y	Q2 y/y	4Q ending June	y/y
Total	389,198	21.0%	-27.1%	9.4%	1,821,249	19.4%
of which:						
Agriculture, fishing	6,920	48.3%	-230.9%	72.6%	14,082	22.7%
Mining	17,616	4.1%	85.0%	25.3%	65,561	38.8%
Manufacturing	22,233	-21.5%	211.8%	21.7%	130,163	0.2%
Energy sector	108,798	54.6%	-23.4%	651.5%	315,729	246.8%
Construction	29,144	67.8%	27.1%	-56.3%	260,283	11.2%
Hotels and restaurants	7,622	35.9%	233.4%	-69.6%	75,441	-5.0%
Transports and communications	77,028	-23.0%	-108.0%	-33.3%	313,755	-40.3%
of which:					-	
Transports	64,869	-18.0%	-46.6%	-45.1%	365,150	-29.0%
Communications	12,159	-71.6%	-748.0%	-550.1%	-51,395	-561.9%
Health and social work	1,617	-75.5%	12366.0%	99.6%	16,402	-3672.2%
Real estate <sup>1</sup>	34,254	259.4%	-131.9%	-23.7%	85,976	-40.1%
Financial sector <sup>2</sup>	64,063	114.4%	45.3%	3171.7%	399,238	318.0%
Source: NSI of Georgia, bne Intellinews						

## **6.0 Public Sector**

### **6.1 Budget**

**Georgian parliament passes 2018 budget law**

**With 111 votes in favour out of 150, the Georgian parliament passed the country's 2018 budget on December 13, according to agenda.ge. The budget stipulates an 8.5% increase in spending to GEL12bn (€4bn) compared to the 2017 budget.**

Meanwhile, revenues will amount to GEL10.5bn. Some GEL9.5bn of the revenues will arrive in the form of taxes, while the rest will be covered from grants and loans from donors.

Large budget deficits have been an issue for the small country in the South Caucasus for years, particularly because the government has used loans to finance them. Contributing to the 2018 budget deficit is an expected shortfall in corporate tax collections as a result of a tax reform passed in 2017 that lowers corporate tax in order to boost private investment.

Three ministries will account for more than half the spending: healthcare (GEL3.5bn), infrastructure (GEL1.85bn) and education (GEL1.18bn). Universal healthcare coverage has been one of the main electoral promises with which the ruling Georgian Dream party has based its campaigns since 2012.

Meanwhile, infrastructure development is the strategy that the government has chosen to spur economic activity, particularly in the logistics and tourism sectors, and particularly with a focus on rural development.

The 2018 budget law envisions an economic growth level of 4.5% in 2018.

<b>Georgia State Budget Figures</b>					
<b>(GEL mn)</b>	<b>2016 Actual</b>	<b>2017 Plan</b>	<b>2017 Actual</b>	<b>2018 Q1</b>	<b>2018 Q2</b>
<b>Revenues</b>	<b>8,580.0</b>	<b>9,489.5</b>	<b>9,750.4</b>	<b>2,635.1</b>	<b>2,384.7</b>
Tax revenues	7,986.8	8,820.0	8,991.3	2,380.0	2,136.8
Grants	296.8	284.46	289.9	173.3	49.1
Other revenues	296.4	385.0	469.2	81.8	198.8
<b>Expenditures</b>	<b>8,741.8</b>	<b>9,121.22</b>	<b>9,372.1</b>	<b>2,093.8</b>	<b>2,309.6</b>
Compensation for employees	1,452.3	1,393.51	1,385.4	322.4	339.5
Use of goods and services	1,117.8	1,144.27	1,248.5	257.6	304.8
Interest Expense	397.7	503.04	476.6	128.4	123.5
Subsidies	359.3	419.97	541.4	95.5	114.6
Grants	935.1	1,020.28	968.6	229.2	206.4
Social benefits	3,150.1	3,313.18	3,324.3	832.2	846.5
Other expense	1,329.5	1,326.98	1,427.3	228.5	374.3
<b>Net operating balance</b>	<b>-161.8</b>	<b>368.23</b>	<b>378.3</b>	<b>541.3</b>	<b>75.1</b>
<b>Change in nonfinancial assets</b>	<b>416.1</b>	<b>909.04</b>	<b>874.2</b>	<b>277.4</b>	<b>245.6</b>
<b>Total balance</b>	<b>-577.9</b>	<b>-540.81</b>	<b>-495.9</b>	<b>263.9</b>	<b>-170.5</b>

Source: Finance Ministry

## 6.1.1 Budget dynamics - tax issues

**BAT director responds to sales effects of tax hikes and smuggling in Georgia**

**Tobacco producers sales in Georgia dropped by almost 30% during a single month after tax hikes, British American Tobacco (BAT) corporate business director Zviad Skhvitaridze has said.**

The country hiked the value-added tax (VAT) and excise taxes for cigarettes and tobacco, which resulted in end-user prices rising by one US dollar per 20-cigarettes compared to prices found in neighbouring countries. The cost of a pack of Winston cigarettes moved up from Georgian lari (GEL) 4.30 (\$1.61/€1.41) to GEL4.80 (\$1.80/€1.57), while the price of a packet of Camel cigarettes increased from GEL 4.00 (\$1.50/€1.31) to GEL 4.50 (\$1.68/€1.47).

Skhvitaridze said that the sales decline was prompted by rising black market sales but he said that he expected the situation to improve during the year as smuggling was tackled.

Akaki Zoidze, head of the parliament's health committee and a lawmaker of the ruling Georgian Dream party, [played down](#) the impact of the smuggling, saying that the illegal market covered less than 1% of total sales.

"In the regional context we see that the excise taxes in Armenia, Russia and Azerbaijan are radically low. The difference is more than one dollar [per package]. This fact is quite a great temptation for people engaged in illegal

trade. Accordingly, the share of illegal trade may increase. This process has already begun in recent years. Illegal trade and consumption on the lower-end products have reflected in our sales,” he said.

Zoidze added that consumers were obtaining raw tobacco, which is seven to eight times cheaper than imported cigarettes, but was not subject to quality checks. Smuggling and use of raw tobacco would significantly affect the government’s budget, the lawmaker noted.

Cigarette prices increased by an average of 50 tetri (\$0.19/€0.16) in Georgia following amendments to the tax code that came into play on January 1.

## 6.2 Debt

Georgia - Gross external debt	2Q16	3Q16	4Q16	1Q17	2Q17	3Q17	4Q17	1Q18	2Q18	3Q18
Gross external debt (\$ mn)	15,281	15,697	15,872	16,042	16,660	16,881	17,250	17,759	17,416	17,225
	2011	2012	2013	2014	2015	2016	2017	2018		
Gross external debt (% GDP)	32.46	32.53	33.92	35.38	41.28	41.6	/	/		

source: CEIC, World Bank

**The gross external debt of Georgia decreased to \$17,225mn in the third quarter of 2018 from \$17,417mn in the previous quarter. External debt averaged \$11,420.4mn from 2007-2017**, according to the National Bank of Georgia. Gross external debt include both public sector (general government, public corporations and national bank) and private sector (banking and other sectors) external debt.

**Georgia’s government debt is expected to inflate to 3.5% of GDP in 2017-2019**, in part due to the depreciation of the Georgian lari and the high level of dollarisation of Georgia's external debt. **External government debt is expected to peak at 43% of GDP in 2018.**

**The country's high current account deficit, which reached 13% of GDP at end-2016, is one of the important sources of external debt.**

## 7.0 FX

Georgia - Foreign exchange rate	2012	2013	2014	2015	2016	2017	2018 Q1	2018 Q2	2018 Q3
Currency (units per EUR) (average)	2.123	2.209	2.346	2.520	2.617	2.832	3.054	2.918	2.940
Currency (units per USD) (average)	1.651	1.663	1.766	2.270	2.367	2.509	2.485	2.446	2.529

**Georgia’s central bank attempts to smooth exchange rate “volatility”**

**Recent exchange rate fluctuations in the Georgian lari are not related to economic fundamentals, Georgia’s central bank stated in a note on November 6, in an attempt at moderating depreciation that has accelerated recently.**

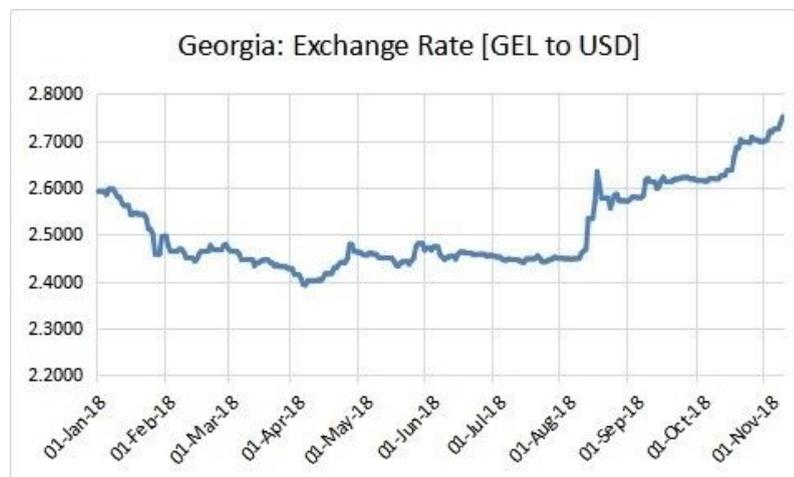
While the country's chronic current account deficit is safely financed by wage remittances and the central bank's reserves are actually increasing, vulnerabilities make the exchange rate of the lari particularly sensitive to political developments—the outcome of the presidential election which has gone to a runoff is highly unpredictable. Slower than expected growth in Q3—at 4.0% y/y from 5.5% y/y in Q2—has added additional downward pressure the currency.

“The floating exchange rate regime, which is currently employed in Georgia, is characterised by short-term fluctuations on the FX market”, the monetary authority said.

Based on the information available, recent exchange rate fluctuations should be seen as unrelated to economic fundamentals, the central bank underlined. The current exchange rate dynamic is negatively affected by the environment surrounding the presidential election, it added. “The National Bank strongly encourages public figures and experts to abstain from ungrounded statements and forecasts about the exchange rate dynamics to avoid the emergence of misleading expectations”, added.

However, what the National Bank of Georgia claims to be “volatility” seems to be moderate depreciation, and the deep current account deficit is a significant fundamental behind this.

The current account gap is expected to grow to 10.5% of GDP this year from 8.9% of GDP in 2017 and to remain in the double digits at 10.2% of GDP in 2019, according to the International Monetary Fund's October 9 World Economic Outlook edition. Earlier, in April, the Fund expected the country's external deficit to narrow to 9.5% of GDP.



## 8.0 Financial & capital markets

Georgia - Commercial banks lead indicators (as of)	Jan-Dec' 18	Sep-18	Jun-18	Mar-18	Dec- 2017	Dec-2016
Interest income (GEL mn)	296.86	278.43	274.15	269.49	275.70	227.44
Net profit / loss (GEL mn)	914.72	602.34	410.4	234.2	869.80	679.11
Bank assets (GEL mn)	39,682.98	37,782.32	35,665.08	34,272.35	34,593.50	30,149.32
Bank deposits (GEL mn)	18,273.92	16,698.19	15,563.09	15,346.53	15,717.54	13,662.0
Bank loans (GEL mn)	25,473.45	23,700.85	22,388.53	21,708.98	21,761.90	18,512.30
ROA (%)	3.0%	2.7%	3.0%	3.0%	3.1%	3.1%
ROE (%)	23.3%	21.2%	22.6%	22.6%	23.3%	22.1%
CAR (%)	18.4%	17.6%	18.9%	19.0%	19.1%	15.1%
NPL (%)	2.7%	2.7%	2.4%	2.4%	2.8%	3.4%

Source: National Bank of Georgia

### 8.1 Bank sector overview

#### 8.1.1 Earnings

##### Georgian banks' achieve high profitability in 2018

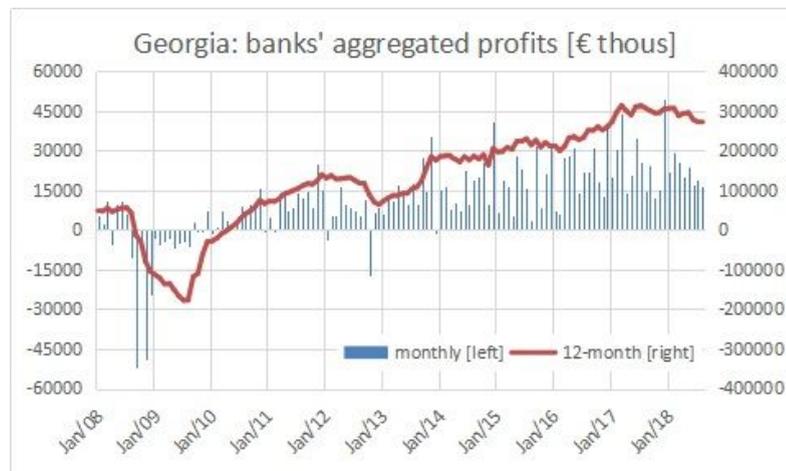
**The aggregate net profits of Georgia's banks rose by 5.3% y/y to GEL915mn (€340mn) in 2018**, resulting in a return on assets (ROA) ratio of 2.5% and a return on equity (ROE) ratio of 20%, according to central banks reports.

The banks' incomes increased by 16.4% y/y to GEL4.2bn driven by a 19% rise in interest incomes to GEL3.29bn. Expenses rose as well, moving up by 17.4% y/y to GEL3.06bn.

Provisions for asset losses climbed 45% y/y to a still moderate level of GEL396mn. Provisions for loan losses surged by 87% y/y to GEL377mn.

**The Georgian banking sector is dominated by TBC Bank and Bank of Georgia, two lenders that are listed on the London Stock Exchange and that, together, account for two thirds of total banking assets.** In total, 16 commercial banks operate in the country, after TBC Bank merged with Bank Republic, the country's fifth largest lender, last October. The sector has performed well in recent years, but financial services penetration in the market remains modest.

Georgian banks constantly posted rising profits from 2010 to 2017, following the losses incurred in 2009. But their profitability stagnated in 2017 and the lenders have struggled in 2018.



## 8.1.2 Loans

**Bankers say tighter regulations to constrain lending by 3.5%-4%**

**Forecasts of the Georgian Banking Association show the effect of new retail lending regulations across the next 12 months will reflect negatively on Georgia's total credit portfolio, reducing it by 3.5-4%, Interpress News [informed](#).**

The latest tightening in lending constraints comes on top of others, which have not passed through the financial intermediation mechanism, and will result in a significant economic slowdown, the bankers' association warned.

The tighter regulations are in principle needed, but excessive provisions and complicated procedures will result in an excessively negative impact on small businesses, bankers cautioned. Thus, the new regulations will push down GDP as well (by 3%, the association anticipates), since small businesses account for a significant share of economic activity in the country.

Georgian banks and financial organisations will have to stick to local currency denominations when issuing loans of up to GEL200,000 (€69,000) under a regulation enacted by the government in September. Foreign currency loans accounted for 53% of total non-government loans in Georgia as of the end of June. The regulation was first introduced as of January 2017, when the threshold was set at GEL100,000.

Starting from May, commercial banks in Georgia were restricted in issuing a loan without a meaningful analysis of consumer solvency, under another step toward financial discipline. The total amount of these loans must not exceed 25% of the supervisory capital of commercial banks. Also, the total amount of loans guaranteed by real estate must not exceed 15% of the bank's supervisory capital without an analysis of client solvency, while the loan to value ratio must not exceed 50% when issuing a loan.

**Financial intermediation gains momentum in Georgia by real 19.4% y/y at end-Aug**

**The stock of bank loans in Georgia increased by 22.4% y/y (19.4% y/y in CPI-deflated terms) to GEL23.7bn (€7.85bn) at the end of August, according to *bne IntelliNews* calculations based on official data from the Georgian central bank. The real growth rate accelerated from 16.0% y/y at the end of July and stands at the highest level since January 2016.**

Financial intermediation marked significant expansion over the past year. The stock of bank loans accounted for 61.4% of GDP (according to latest available

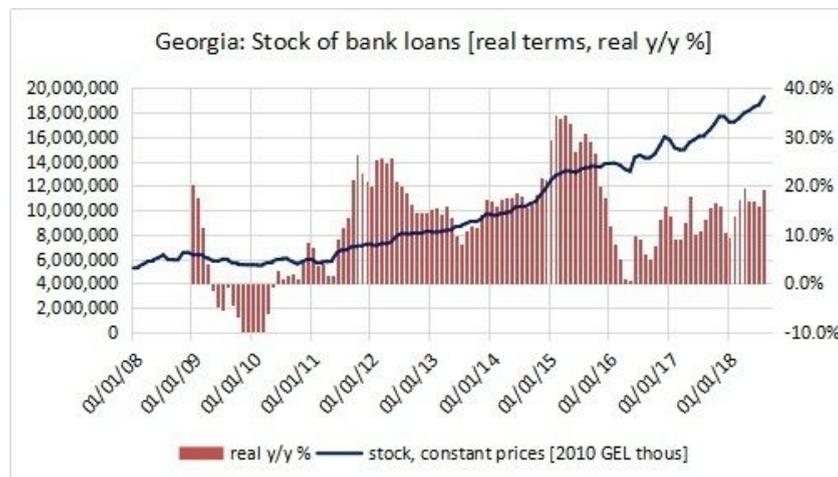
four-quarter GDP, calculated at the end of June) at the end of August, up from 55.3% one year earlier. The robust GDP growth, at over 5% y/y in the past three quarters ending June 2018, contributed to higher investor confidence.

The stock of loans has increased by real rates of over 15% y/y for the past six months. But on a broader perspective, the growth rates are far from the record performances seen in 2015. After the lending decelerated abruptly in 2016 amid weak economic growth in 2015 and 2016, the banks have gradually recovered to deliver outstanding performances in 2017 and 2018.

Amid an upward stage in the economic cycle, lending gained momentum particularly this year while the quality of banks' portfolios improved. Nonetheless, the central bank has urged lenders to not slacken when it comes to financial discipline since such an improvement in credit quality is typical for this stage of the economic cycle (while hiding potential threats). In fact, new, tighter regulations were enforced.

The stock of loans was pushed up as of the end of August by mortgage lending to households, with that accounting for a significant share of total loans: 32.7% at the end of August up from 29.3% one year earlier. In nominal terms, the stock of mortgage loans to households increased by 36.8% y/y (33.8% y/y real terms), well above the average.

A high growth rate was posted by the transport and communication sector. It saw growth of 84.6% y/y (nominal terms), and went from 1.5% of total loans one year earlier to 2.2% at the end of August. The stock of loans to industry accounted for 11% of total loans after having increased by 22.7% y/y.



### 8.1.3 NPLs

**Georgian banks have weathered the depreciation well, with non-performing loans (NPLs) at a manageable rate of 2.8% of total loan portfolio at end-2017**, compared with a ratio of 3.4% at end-2016, according to the National Bank of Georgia. NPLs account for around 3% of total lending. Banks are well capitalised and positioned to absorb a moderate deterioration in their loan portfolios, according to Fitch ratings agency.

## 8.1.4 Banks specific issues

**Georgia's TBC Bank claims "dark PR" as it fights laundering probe**

**Georgia's London-listed TBC Bank is under investigation for "activities [that] clearly showed the characteristics of legalization of illegal income, i.e. money laundering, and other illicit acts", according to a statement from the Office of the Prosecutor General (POG) of Georgia.**

Largest Georgian lender TBC—included in the London Stock Exchange's FTSE 250 Index since June 2017—responded to the announcement by saying it is the target of "dark PR" and a "deliberate attempt to discredit and tarnish its reputation".

POG is probing events said to have occurred more than a decade ago. It said that in May 2008 two companies, Samgori Trade LLC and Samgori M LLC, received a loan worth \$17mn from TBC, without the provision of any security and through an accelerated procedure. "As soon as the loaned funds were credited in the accounts of the companies, [TBC co-founder and chairman] Mamuka Khazaradze and [TBC co-founder and deputy chairman] Badri Japaridze borrowed the same amount which TBC Bank had lent to the aforementioned companies for the purpose of financing working capital," POG added.

**Loans written off 'without grounds'**

By the end of 2008, said POG, TBC wrote off the loans to the Samgori companies without any grounds and earlier than stipulated by banking regulations, prior to moving them to an external balance account and, in 2012, exempting the companies from liabilities owed when agreeing to transfer the liabilities to an offshore company. The offshore entity was said to have not yet made any repayment on the loan.

The loans "were written off in such a manner that these companies have not paid any commissions and these loans have not been repaid to the bank", the prosecutors said.

Statements made by Khazaradze's lawyer show that the bank chairman has stated that the loan made to him and Japaridze has been repaid from borrowings provided by unspecified natural persons. But, without explaining the point further, POG noted that Khazaradze and Japaridze were yet to repay a loan from the Samgori firms.

**"Rumors... are nonsense"**

"The rumors about money laundering are nonsense. The operation was absolutely open and transparent," Zviad Kordzadze, Khazaradze's lawyer, argued in comments reported by Georgia Today on January 9. He confirmed to the publication that Khazaradze had been questioned by POG representatives several days prior to the new year.

The owner of the Samgori companies, Vakhtang Tsereteli, said in a Facebook post quoted by commersant.ge that the borrowing of \$17mn from TBC and the transfer of the lending contract to make the offshore company the debtor was legitimate business.

**Regulatory fine**

TBC Bank subsidiary TBC Bank JSC, meanwhile, on January 9 released a statement through the London Stock Exchange saying it had been fined Georgian lari (GEL) 1mn (GBP295,000) by Georgia's central bank, the National Bank of Georgia, over historic "certain transactions" in 2007 and

2008.

It said the regulator claimed that these transactions, which the regulator believed were related to the chairman and deputy chairman of TBC, did not comply with relevant Georgian law concerning conflicts of interest.

TBC Bank JSC added that these transactions took place before its 2014 initial public offering and were already subject to a National Bank of Georgia inspection in 2008, which did not result in any action being taken at that time.

It was "unclear" if further sanctions would be imposed, TBC Bank JSC said, noting TBC had already challenged the fine in the Georgian courts and an injunction suspending the fine's payment had been issued.

The POG was also investigating the 2007 and 2008 transactions and TBC Bank's subsidiary, while denying the allegations, planned to "vigorously defend its position".

"It is not currently expected that these matters will result in any material consequences for the group," TBC Bank JSC said.

TBC Bank, together with its subsidiaries, says it is the leading universal banking group in Georgia, with a total market share of 38.4% of loans and 40.3% of non-banking deposits as of 30 September 2018, according to data published by the National Bank of Georgia.

## 8.1.5 SMEs finance

### **EBRD assists SMEs in Georgia under Trade Ready programme**

**The European Bank for Reconstruction and Development (EBRD) on October 16 [announced](#) it has launched its trade support initiative *Trade Ready* in Georgia to help the country's small and medium sized enterprises (SMEs) win their way to improving their competitiveness and succeed on international markets.**

The EBRD is thus boosting the support it already extends to the country's SME entrepreneurs, while other international financial institutions also work in the same direction.

The initiative offers trade finance training and trade-related business advice for SMEs, networking opportunities with local banks, as well as policy dialogue to facilitate improvements in the regulatory environment. The support initiative is already operational in Serbia and will be implemented gradually in other EBRD countries.

Trade Ready will extend the outreach of the EBRD's pioneering Trade Facilitation Programme (TFP) and dedicated business advice through the Bank's Small Business Initiative.

While banks can expect to attract new clients with the introduction of new trade finance products, businesses will benefit from better access to finance and the chance to expand to international markets.

Earlier in March this year, the EBRD and the European Union extended their support to SMEs in Georgia, Moldova and Ukraine, with a total of almost

€1.1bn in credit lines and trade finance and €58.3mn in EU grants. The EU4Business-EBRD credit line has allowed SMEs in sectors such as manufacturing, retail, agriculture and food processing, transport, services and healthcare to improve their products, strengthen their export potential and adopt EU standards and technical norms, she explained. Other international financial institutions extended their support for Georgia's SME sector.

The European Investment Bank (EIB) has [announced](#) that it has extended a €30mn loan to Georgia's largest bank TBC Bank to improve access to financing for local small and medium sized enterprises (SMEs). The loan is part of the EU4Business initiative, designed to support SMEs in the six Eastern Partnership countries (Armenia, Azerbaijan, Belarus, Georgia, Moldova and Ukraine). Funding within the scope of the project is expected to benefit approximately 600 Georgian SMEs.

Financial intermediation marked significant expansion over the past year in Georgia (+19.4% y/y as of August). But the banks particularly focus on mortgage lending. Robust GDP growth, at over 5% y/y in the past three quarters ending June, has contributed to higher investor confidence. SMEs make up more than 90% of Georgian businesses and are thus a critical component of economic growth and development. It is the EIB's fourth loan provided to TBC Bank since 2012, with the credits totalling €85mn.

## 8.1.6 Bank news

**EIB extends \$34mn in loans to Georgia's TBC Bank**

**Georgia's biggest retail lender TBC Bank Group, registered in the UK, announced on February 28 that its corporate subsidiary TBC Bank has received a \$34mn loan from the European Investment Bank (EIB), Reuters [reported](#).**

TBC Bank JSC, which has been in a dispute with the National Bank of Georgia over issues including lending that took place more than a decade ago, said the EIB's five-year loan facility would primarily be used to finance small and medium sized enterprises in Georgia.

"This loan will further contribute to the positive development of the bank and our SME clients in various sectors of the economy, boosting job-creation and long lasting benefits for the country," CEO Vakhtang Butskhrikidze said.

The bank has settled its dispute with NBG, but its founding members, who are also shareholders, said that they would continue legal action brought against the central bank's move to remove them from TBC Bank's managing board. The two remain CEO and deputy CEO of TBC Bank Group.

**Co-founder of Georgia's TBC Bank stepped down 'after government pressure'**

**Resigned chairman and co-founder of Georgia's TBC Bank, Mamuka Khazaradze, on February 26 was reported as saying that he and his deputy Badri Japaridze were forced to step down last week following pressure from the Georgian government.**

The two were formally asked by the National Bank of Georgia to resign amid investigations related to operations carried out by the London-listed lender in 2007-2008, which allegedly involved conflicts of interest.

“We took a forced step when we left the bank, but we will not yield our worth and justice,” Khazaradze, who still serves as chairman of the board of TBC Bank Group, Georgia’s biggest retail banking group, told Reuters.

Georgia’s central bank president Koba Gvenetadze has refused to hold public talks on the accusations raised against TBC Bank in relation to the operations more than a decade ago. NBG said that such discussions would harm the country’s banking sector.

But Khazaradze, invited by lawmakers to parliament on February 26, said he remained open to public debates and has nothing to hide.

“As you know it, today, I was not allowed to say a thing. We are ready to arrive in the relevant parliamentary committee again, to express our position from the public tribune. We are waiting for an invitation from the Parliament in the nearest future. I hope, the truth will be revealed and there will not be the situation that could result in misunderstanding and speculations,” he wrote in a Facebook post.

In [a statement](#) issued on February 21, the National Bank of Georgia explained again the situation. The operations in 2007-2008, by which they took \$16.7mn loans by intermediary companies and never paid back, caused damages to TBC Bank. The bank had already provisioned and taken the loan out of the balance sheet by the time it listed its shares on London Stock Exchange in 2012, the central bank explained.

The central bank’s statements and the resignation of the two had a positive impact on the bank’s shares: their price increased by 8.6% on the LSE. When the central bank asked the two to step down, TBC’s shares dropped by 7%.

TBC and National Bank of Georgia signed an agreement to iron out the disagreements, after the former announced plans to sue the later in court. TBC will pay the GEL1mn fine and will cooperate with the central bank to investigate the deeds in 2008.

But the two founders might still sue the central bank on their own behalf. “I made a decision to leave TBC bank where I spent 27 years of my life,” reads the statement posted by Khazaradze on Facebook.

“I will not repeat what kind of attack our bank is facing. As a result, our international shareholders suffered a loss of 200 million dollars in one month, so our country has been seriously damaged. Without any investigation or court decision, they seriously stained our reputation by accusing us of alleged money laundering, non-existence of which has been internationally recognised ... I realised that the goal was to discredit me, I realised that they are fighting against our success, I realised that the company's growth should be limited in Georgia,” he wrote.

## 8.2 Central Bank policy rate

**Georgia cuts policy rate by 25bp to 6.75%**

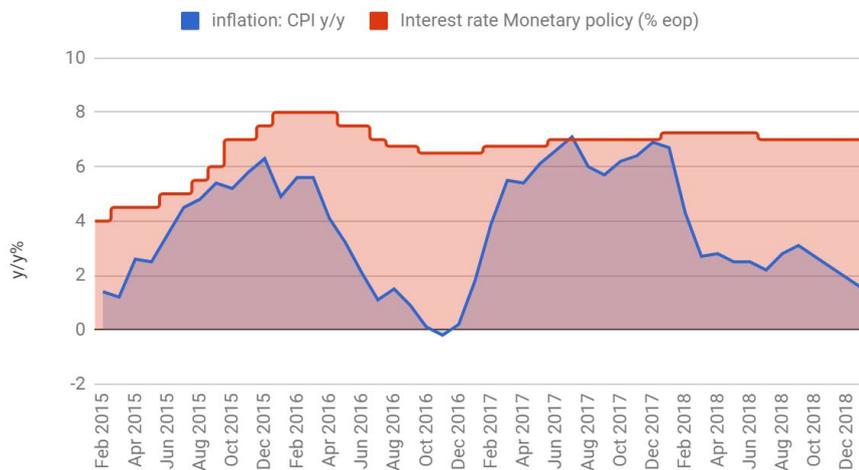
**The Monetary Policy Committee of the National Bank of Georgia on January 30 cut its refinancing rate by 25bp to a still restrictive rate of 6.75%. The central bank sees headline inflation around 3% in the medium**

term.

In December, the annual inflation rate was 1.5% y/y. According to existing forecasts, inflation will move around the 3% y/y target rate in the medium term. The central bank said in a press release that it plans another rate cut during this year.

External demand strengthened during 2018 with a positive impact on growth, but the Georgian economy lost momentum during H2, the central bank noted. The annual increase in the export of goods was 23% in 2018, while tourism revenues grew by 18% in the same period.

Georgia monetary policy rate vs inflation



## 8.3 Stock market

### Georgian central bank announces new regulations as part of capital market reform

**The National Bank of Georgia said on July 18 that it has drawn up two new regulations governing brokerage companies.**

The aim of the regulations — the Rule of Licensing and Regulation of Brokerage Company and the Additional Rule of Regulation of Brokerage Companies Involved in High-Risk Financing Instruments — is to raise standards of service in the sector, and to protect investors' interests and allow them to make well-informed decisions. They were drawn up as part of ongoing capital market reforms.

"It is noteworthy that the established requirements fully address the challenges in the sector and also reflect the principles of the EU Directives, International Organisation for Securities Commissions (IOSCO) and European Securities and Markets Commission (ESMA) regulations," the NBG said in a [July 18 statement](#).

The rules are mandatory for all licensed brokerage companies, but due to their complexity active brokerage companies have been given a transition period during which they have to bring their work into compliance with the legislation.

When [outlining his governing programme](#) on July 15, Prime Minister Mamuka Bakhtadze said the government will work with the central bank on capital market reforms.

The Georgia Stock Exchange (GSE) recorded a turnover value of GEL8,787.65 in June, declining from GEL103,819.70 in the previous month, according to CEIC data.

Georgian Stock Exchange: Index



## 8.4 International ratings

Georgia - Rating agency	as of February 2019
Bond rating: Moody's	Ba2 (Stable)
Bond rating: Fitch	BB (Stable)
Bond rating: S&P	BB- (Stable)

**Fitch upgrades Georgia to BB on sound external balance, fiscal performance**

**International rating agency Fitch Ratings on February 22 upgraded Georgia's sovereign rating (associated with risk on default on long-term, foreign currency debt) to BB/stable from BB-**, citing the country's resilience to regional turmoil and progress in terms of fiscal consolidation and improving its external balance.

The progress was confirmed by Georgia's smooth completion of quarterly reviews under the programme carried out with the International Monetary Fund, Fitch said in a [press release](#).

The rating keeps Georgia in the non-investment class, above Serbia (which is more risky) but below Hungary (a better risk profile) in terms of sovereign risk.

The Georgian economy proved sturdy in the face of negative developments in 2018. Economic growth remained robust, the currency was relatively stable and the National Bank of Georgia (NBG) central bank built reserves despite a severe economic shock in Turkey and heightened sanctions risk in Russia, Fitch commented.

External imbalances are gradually easing. Georgia's current account deficit is structurally high, but Fitch estimated that it narrowed to 7.5% of GDP in 2018, despite the testing external environment.

Fitch forecast a further narrowing of the current account deficit as the recently launched funded pension pillar will likely encourage savings and the implementation of macro-prudential measures will lead to a deceleration in

consumer lending, reducing pressure on imports.

Growth remained robust at an estimated 4.8% in 2018, with the five-year average at 5.0%, which compares favourably with the current median for peers of 3.1%.

The 2018 fiscal outturn, an estimated augmented deficit of 2.5% of GDP, including budget on-lending, outperformed the authorities' 2.8% initial target and current BB median, due to strong revenue performance and delayed implementation of infrastructure projects, meaning public capex was subdued.

Fiscal policy is consistent with a gradual decline in gross general government debt (GGGD)/GDP, which Fitch forecasts at 42.5% of GDP in 2019, lower than the current BB median of 48.1%. With 81% of total GGD external, it is vulnerable to exchange rate fluctuation.

## 8.5 Fixed income

### 8.5.1 Fixed income - bond news

**Georgia Capital PLC acquires remaining 40% stake in Tbilisi luxury hotel**

**Georgia Capital PLC said it has acquired the remaining 40% stake it didn't already own in a luxury hotel in Tbilisi, Georgia, for \$5.2mn, Alliance News reported on February 6.**

m2 real Estate, a subsidiary of Georgia Capital and owner of the Hospitality & Commercial Real Estate business, first acquired a 60% interest in the hotel in December 2017.

The payment reportedly consists of \$300,000 in cash and \$4.9mn settled through local bonds issued by the Hospitality & Commercial Real Estate unit. At the end of 2018 \$30mn in local bonds were placed with a three-year tenor, backed by the rental income stream from commercial properties with an annual coupon rate of 7.5%.

**EBRD issues €600mn global green bond**

**The European Bank for Reconstruction and Development (EBRD) issued its debut €600mn euro-denominated global green bond at the beginning of January.** "This transaction represents the EBRD's inaugural benchmark Green Bond in the EUR market, and its fourth benchmark-sized Green Bond," the bank said in a January 4 [statement](#).

The latest bond, issued on January 3, pays a coupon of 0.000% and priced with a spread of 13bps through mid-swaps, equivalent to +39.9 bps over the OBL 0.000% October 2023, the bank said. The issue will mature on January 10, 2024.

The offer was oversubscribed, with the order book exceeding €680mn, well above the €500mn originally targeted, in response to which the EBRD raised the size of the transaction to €600mm to satisfy demand, while still tightening the pricing.

"For EBRD to effectively open the benchmark new issue market in EUR SSAs [sub-sovereigns and agencies] for 2019 might have been considered a surprise by some, however, the combination of a compelling credit story, a well-established reputation in the SSA market, and the added attraction of the

Green Bond format proved to be a compelling formula to galvanise investors at the start of the new year, and EBRD was dynamic enough to take advantage of a relatively quiet window in the market,” the bank said in a statement.

Over two-thirds of the final deal was allocated to investors with a sustainable and responsible investment focus, which, the development bank said, “welcomed this opportunity to add the EBRD name to their EUR portfolios”. The bank also reported demand from other “high quality Central Bank and Bank Treasury investors”.

Proceeds from the EBRD’s green bonds are invested into a dedicated portfolio of environmentally and socially sustainable projects, spanning investments in five areas: Energy Efficiency, Renewable Energy, Water Management, Waste Management and Air Pollution Prevention & Sustainable Transport.

Since the EBRD started issuing green bonds back in 2010, its green project portfolio has grown to include 379 projects worth a total €4.1bn as of September 30, 2018.

BofA Merrill Lynch, Crédit Agricole CIB and Morgan Stanley were joint bookrunners for the issue.

## **9.0 Industry & Sectors**

### **9.1 Sector news**

#### **9.1.1 Oil & gas sector news**

**The Trans Adriatic Pipeline (TAP) project to provide the final leg of a 3,500-km-long set of interconnected pipelines that will deliver Azerbaijani gas to Italy at the end of an Azerbaijan-Georgia-Turkey-Greece-Albania-Adriatic Sea route has announced its financial close.**

It has secured €3.9bn from public and private lenders, its managing director, Luca Shieppati said in a January 11 statement.

The sum is the largest amount of finance agreed for a European infrastructure project last year. The biggest creditor is the European Investment Bank (EIB), which provided a €700mn loan, while the second biggest is the European Bank for Reconstruction and Development (EBRD) with a loan of €500mn provided on its own account and €500mn syndicated to a group of 16 commercial banks.

TAP is a priority project of the European Union (EU) and the Energy Community, an international organisation which brings together the EU and its neighbours to create an integrated pan-European energy market.

The 878-kilometre pipeline will start at the Greek/Turkish border, cross Albania and, after passing under the Adriatic Sea, terminate in southern Italy. It constitutes the final segment of the Southern Gas Corridor (SCG), a supply route to transport gas from the Caspian Sea to Europe.

With an initial annual capacity of 10bn cubic metres—equivalent to the energy consumption of approximately seven million households in Europe—the pipeline will make a significant contribution to the diversification of Europe’s energy supply, the EBRD said in a press release. The first delivery of gas is

expected in 2020.

It will also make energy supply for consumers more reliable and achieve significant CO2 reductions by offering an alternative to more polluting energy sources, supporting the transition to low-carbon economies in line with the EBRD's new energy sector strategy.

Nandita Parshad, EBRD managing director for sustainable infrastructure, said: "The Trans Adriatic Pipeline will set the foundation for an integrated gas market across southeastern Europe and enhance the region's strategic status as an energy hub. We believe that gas remains an important transition fuel in this region that can help displace coal and facilitate penetration of renewables."

With exit points along the route, TAP has the potential to support new gas infrastructures, integrating markets across Southeastern Europe and enhancing the region's strategic status as an energy gateway, the EBRD said.

## 9.1.2 Automotive sector news

**Leading Chinese carmaker Guangzhou Automobile Group will open an office in Georgia by the end of 2019**, the Georgian government announced after Prime Minister of Georgia Mamuka Bakhtadze met Guangzhou Automobile Group chairman Zeng Qinghong on January 23.

After opening the office, the company will study the country's environment further prior to making decisions on investing and building plants.

"Guangzhou Automobile Group is China's leading carmaker with more than 84,000 employees. The group manufactures passenger cars and commercial vehicles, motorcycles, and auto parts. It is also engaged in the areas of finance and insurance. The group's fixed capital exceeds 18 billion USD," the PM's press office said.

## 9.1.3 Transport sector news

**The European Commission and the World Bank have announced the development of a new Indicative trans-European Transport Network (TEN-T) Investment Action Plan.** It identifies priority projects in Armenia, Azerbaijan, Belarus, Georgia, the Republic of Moldova and Ukraine. Georgia will receive €3.5bn of the programme's €13bn, Georgia Today [reported](#), quoting government officials.

"This is an important decision since Georgia's integration into European structures is the main priority of our foreign policy... We welcome this move," the Georgia's Minister of Foreign Affairs David Zalkaliani stated

The programme is aimed at covering almost 100 projects involving investments of almost €13bn by 2030. It foresees a total of 4,800 kilometres of road and rail, six ports, and 11 logistics centres.

The agreement on the maps extending the TEN-T to the Eastern partnership countries entered into force on 9 January.

"The completion of the Indicative TEN-T Investment Action Plan is a joint commitment to deliver tangible results for citizens across the region. The Plan will assist decision-makers in prioritising strategic investments in transport infrastructure with the aim of completing the TEN-T network defined as one of the 20 deliverables for 2020 in the Joint Declaration of the last Eastern Partnership Summit in Brussels," EU Commissioner for European Neighbourhood Policy Johannes Hahn said.

"Enhanced transport connectivity both within the Eastern Partnership region, and between the Eastern Partnership region and the EU has the potential to

bolster economic growth and create job opportunities. The Plan shall also serve to highlight the importance of road safety as well as digital solutions in new projects, and to align design standards with current EU practices," added EU Commissioner for Transport Violeta Bulc.

**Passenger traffic at Georgia's three international airports rose 23% y/y during January-October, the Georgian Civil Aviation Agency has reported.** A 28% y/y increase in the number of tourists visiting Georgia to more than 8mn was the major driver. The increases amount to a gain when it comes to tackling the country's wide current account that stands at around 10% of GDP.

Georgia was ranked in fourth position among the world's fastest-growing tourism destinations in the World Tourism Organisation's (UNWTO's) [2017 report](#).

The passenger traffic figure covers Georgia's three main airports: Tbilisi Shota Rustaveli International Airport, Batumi International Airport and Kutaisi David Aghmashenebeli International Airport.

Kutaisi International Airport saw the greatest expansion: 39% to 512,386 passengers. That most likely followed the launching of routes to popular destinations like Berlin and London by low-cost airline Wizz Air.

With 3,286,344 passengers, Tbilisi International Airport remained the largest airport in the country. Its increase equates to 21% y/y. Batumi International Airport registered a 19% y/y gain, serving 555,693 passengers.

#### 9.1.4 Tourism sector news

**Foreign tourists spent \$164.5mn in Georgia in January, marking a fivefold increase year on year, the Georgian National Tourism Administration (GNTA) of the Ministry of Economy of Georgia announced, according to agenda.ge.**

About \$3.2bn was generated from tourism in Georgia in 2018. That was \$498mn more compared to 2017, said the GNTA. Meanwhile, in all of 2017 international tourism revenue reached \$2.7bn, which was \$594mn more compared to 2016.

Some 8,679,544 international visitors arrived in Georgia during 2018, 25% more than in 2017 and a national record, Prime Minister Mamuka Bakhtadze announced on January 4.

"This is truly a unique success for a country of our size... Visitors are learning about our country and seeing that our unique culture is part of a common European civilisation," said Bakhtadze.

Georgia is increasingly celebrated as a "newly discovered destination" in international travel media.

#### 9.1.5 Infrastructure and construction sector news

**Georgia's regional development and infrastructure ministry managed to spend only GEL627mn of GEL1bn earmarked for the first three-quarters of the year, deputy minister Mzia Giorgobiani said on October 10, as quoted by IPN.**

The financing from international institutions was secured and all procedures were completed, but there were problems the tenders, he reportedly added. For the whole year, the ministry was earmarked a total budget of GEL1.8bn, or some 4.5% of Georgian GDP.

Despite the problems outlined by Giorgobiani, new projects are being

launched. The construction of six new cable installations at the Gudauri ski resort was announced by the economy ministry, [reported](#) IPN. The ski slopes' area will increase by 20%.

More infrastructure investment is needed in mountainous areas of Georgia to allow for tourism development, Prime Minister Mamuka Bakhtadze said during a visit to the resort of Beshumi (altitude 2,000 metres) in the Ajara region back on August 5. Many of Georgia's summer and winter resorts are unprepared when it comes to coping with the growing number of tourists visiting the South Caucasus country, Bakhtadze observed on August 29.

Georgia reported 6.9mn international visitor arrivals in 2017, up 20.2% from the previous year, according to state statistics office Geostat. A further increase is expected this year. The country's profile as a tourist destination is reaching new heights and Georgia is also served by a growing number of airlines, including budget carriers.

The Infrastructural Development Strategy of Georgia for 2017-2020 envisages the implementation of 2,500 major modernising infrastructure projects worth GEL10bn. They include building a 1,000-km road, providing water supplies for 500,000 people and solving problems with solid waste and landfills in the country.

**Georgia and Asian Development Bank (ADB) have signed a contract under which the international financial institution is extending a \$300mn loan to the South Caucasian country for the construction of the 12.2-kilometre Rikoti-Zestaponi pass road, which will be part of the East-West Highway (EWH).**

The document was signed on October 5 by Minister of Finance Ivane Machavariani and ADB regional director Ileshi Elhan Kaialar. The new road infrastructure will ensure efficient and safe driving, cut driving time and develop tourism business, the development bank said.

"Georgia's geographic location puts the country at the heart of trading and logistics activities not only in Central Asia, but in the rest of Europe and Asia, which opens up a lot of growth opportunities for the economy," said ADB senior transport specialist for Central and West Asia Valerie Lisack.

The EWH, an integral part of one of the six key corridors connecting member countries of the Central Asia Regional Economic Cooperation (CAREC), currently carries about 60% of Georgia's foreign trade despite representing only about 2% of the country's entire road network length.

The 410-km highway, which serves about 13,000 vehicles per day with a traffic growth rate of over 10% annually since 2005, is not only crucial for the connectivity of international trade between the Caspian Sea and the Black Sea, but also essential for Georgia's global market access and socioeconomic development.

The ADB previously financed the construction of the Kobuleti and Batumi bypass roads and the reconstruction of Kvesheti-Kobi, together with the European Bank for Reconstruction and Development (EBRD) and the construction of the Dzirula-Kharagauli-Moliti-Pona-Chumateleti roads.

## 9.1.6 TMT sector news

**The World Bank, in collaboration with the Georgian economy ministry, will develop a National Innovation Ecosystem in the country in order to foster the digital economy and innovative start-ups.** The World Bank will finance the project, which is estimated to cost \$40mn. Countries in the South Caucasus, including Georgia, have been seeking to develop their value-added

sectors, such as information technology, in recent years. Armenia is a leader in this sector in the region, with IT and technology accounting for 5% of GDP, and a sizable qualified workforce that has attracted the likes of Microsoft to open up innovation centres in the country. Meanwhile, Azerbaijan has been working on digitising its public services and installing fibre-optic Internet connections across the country. Following in their footsteps, Georgia is also working on Internet connectivity and promoting tech start-ups. The project will comprise four parts, namely the development of an innovation infrastructure through the creation of a network of innovation hubs in selected cities and towns; the provision of innovation services; ensuring financing through technical assistance and matching grants; and project implementation support.

## 9.1.7 Retail sector news

**New bank regulations enacted in Georgia since January 1 have substantially cut durable consumer goods sales in the country, two large retailers have estimated, [bpn.ge](#) reported.**

Turkish-owned brand Beko has reportedly cut prices and the Techno Boom retailer has closed some outlets in the regions in the wake of the sales downturn. Retailers are seeking a solution, but the National Bank of Georgia is yet to properly assess the impact of its new regulations.

Under the regulations, lenders must estimate each customer's capacity to repay a loan.

The instant impact of the changes have pushed Beko brand sales down by 50% in Georgia, with its general director telling [bpn.ge](#) that the decline is steeper outside the capital Tbilisi.

"Most of the population in the regions [outside Tbilisi] is self-employed and therefore it is very difficult to show a document confirming any income to the financial institution. Because of this, most of them will not be extended loans," noted Mehmed Melek.

"The banking regulations are quite strict, and our work was stopped immediately. We were forced to reduce prices to make products available to consumers. Of course, it is at the expense of reducing our profit margin," Melek added.

The Techno Boom retailer also said the regulations were behind a 50% drop in its sales. Anzor Kokoladze, founder of the company, was cited as saying that it had to close 4 stores.

Central bank president Koba Gvenetadze said in parliament on February 27 that it was too early to evaluate the impact of the regulations.

"The statistical information that we have today does not provide the basis for a profound analysis of this issue. We think that it is too early to talk about this issue until the first quarter figures will be presented," he said.

The regulations, on the upside, were consolidating the country's financial stability, Gvenetadze argued.

On February 22, Fitch upgraded Georgia's credit rating. Its press release mentioned the regulations as boosting financial stability.

**Negotiations between Swiss global giant Nestle and the IDS Borjomi International mineral water producer and bottler that operates in Georgia, Ukraine and Russia, have failed after half a year of talks with the parties unable to agree on a price, [BusinessPressNews](#) has reported.** At this stage, IDS Borjomi carries no negotiations.

Information about the possible sale of IDS Borjomi first emerged last October. Russian daily *Kommersant* wrote that Alfa Group, held by Mikhail Fridman and

German Khan, was negotiating the sale not only with Nestle but also with Coca-Cola.

IDS Borjomi is a leading producer and bottler of fine mineral waters with production facilities in Georgia, Ukraine, and Russia. The company says it is a leader in the marketplace in the CIS and Baltics and has been exporting products to 40 countries since it was established in its present form in 2002. Alfa Group bought IDS Borjomi in 2013 from Boris Berezovsky's business partner, Badri Patarkatsishvili's foundation, owned by Salford Capital Partners Inc. Now, according to Forbes, Alfa Group owns 55.8% of IDS Borjomi and heirs of Patarkatsishvili 37.2%, with the rest belonging to small shareholders in Georgia, Russia and Ukraine.

### 9.1.8 Renewable energy sector news

**The board of the European Bank for Reconstruction and Development (EBRD) will discuss on November 28 a \$30mn loan that the Turkish group Anadolu would use to develop a \$88.7mn hydropower plant in Georgia, Kheledula HPP. The project was agreed in December 2016.**

Anadolu in 2014 completed the largest hydropower plant built in Georgia for 40 years: a 85MW plant, at a cost of \$200mn, located on Paravani river in the southern part of the country close to Turkey. The EBRD approved at that time a \$52mn loan to support financing the power plant. The World Bank Group's International Finance Corporation contributed \$40.5mn and another \$23mn was raised from commercial banks.

Of relatively small size and using environmental-friendly technology, the new Kheledula HPP project was rated by the EBRD as Class A for its moderate environmental and social impact.

The EBRD's loan would be part of a \$60mn financing package with the remaining part mobilised from third parties.

The borrower is a special purpose vehicle established in Georgia to develop, construct and operate the project. It is majority-owned and controlled by the Anadolu Group, a large Turkish conglomerate partially listed on the Istanbul Stock Exchange.

The power plant with a capacity of 51MW is to be developed on the Kheledula River located in the Racha-Lechkhumi and Kvemo Svaneti regions. Georgia, already having robust power generation capacities (some 80% of its electricity is generated in hydropower plants) and being an established regional exporter, plans to build a large number of dams because its generation capacities largely matching consumption tend to fall short of growing consumption.

Turkey is among the largest investors in Georgia and a significant export market for Georgia's electricity. Environmental NGO Bankwatch, however, has questioned the plans for more hydropower plants in the absence of a broader energy sector strategy. Furthermore, the environmental impact of the planned dams is major, Bankwatch has warned.

### 9.1.9 Utilities sector news

**Georgia is to privatise its postal services run by Georgian Post, economy minister Giorgi Kobulia said in a Bloomberg interview, after which he explained the policy to local media.**

The country's railway transport company will be unbundled, its railway transport market will be opened up to private operators and the electricity system privatisation might resume, he also reportedly said.

The privatisation option was under consideration for the railway company

Georgian Railway, but only after a company reorganisation including the unbundling of the railway infrastructure and transport functions, Kobulia added. As part of the railway transport system restructuring, the government wants to encourage more involvement of private railway operators, while the infrastructure management company would operate separately.

Georgia has to restructure its railway transport and electricity systems under the EU-Georgia Association Agreement. It must also implement EU directives on railway transport, which require the infrastructure segment to be segregated by 2022.

Similar restructuring plans are envisaged for the Georgian electricity distribution. Under the Association Agreement and the Energy Community Treaty, Georgia has to implement the Third Energy Package into its national legal framework.

"We need to increase the efficiency of these companies in order to privatise them," said Kobulia in relation to Georgian Railway and State Electrosystem. According to Kobulia, the plan is to eventually privatise State Electrosystem. Its selloff was suspended in 2011 in the face of "challenges" on the market.

## 9.2 Major corporate news

### 9.2.1 Oil & gas corporate news

**Azerbaijan has moved further into securing more value from its huge gas resources with the launch of the country's first urea plant by the State Oil Company of the Azerbaijan Republic (SOCAR).**

Production at the €800mn installation in Sumqayit Industrial Zone outside Baku began on January 16, according to officials. Around 70% of the plant's urea (aka carbamide) production is likely to be exported to Turkey, Georgia and other Black Sea markets and Mediterranean markets. The remainder is to be sold on the domestic market, saving Azerbaijan around \$90mn on urea imports. The production targets are 1,200 tonnes per day of ammonia and 2,000 tonnes per day of granular urea. Around 435mn cubic metres of natural gas as raw material is to be consumed.

Urea is usually used as a nitrogen-release fertilizer.

Construction of the plant began as long ago as 2011. There were several project realisation delays.

Samsung Engineering Co. won an international open tender to provide engineering, procurement, construction and pre-commissioning services for the facility.

Azerbaijan is directing gas into several petrochemical projects, with a couple of units already open at Sumqayit.

### 9.2.2 Transport corporate news

**Smartlynx Airlines is to start charter flights between Estonian capital Tallinn and Batumi in Georgia in the summer,** business executive and politician Tornike Rizhvadze, head of the government of the Autonomous Republic of Adjara in southwest Georgia, said during a visit to Estonia. Flights would be operated with 180-seat Airbus A320 aircraft from Tallinn Airport, the Adjara government's press office added.

The flights would boost tourist inflows from Europe, boosting tourism development in Adjara on the Black Sea coast, Rizhvadze said.

The number of visitors from Estonia arriving in Adjara last year rose 80%.

The tourist potential of the region is currently represented by a special stand at the Tourist 2019 event in Tallinn.

### 9.2.3 Healthcare corporate news

**Georgia's largest medical services and insurance provider Georgia Healthcare Group has reported a robust 25% y/y Ebitda gain to GEL33mn (\$22mn) in Q3 broadly in line with expectations.** But the London Stock Exchange listed company's GEL10mn (\$3.7mn) net income remained flat, at around 25% below the consensus forecast by the market.

Georgia Healthcare Group has a market capitalisation of nearly \$400mn. The company's management is working on plans to capture a higher share of the medical tourism market, including in neighbouring counties. Georgia Healthcare Group has raised awareness of available medical facilities throughout the region, capturing GEL 1.7mn of inbound medical tourism revenues in the first nine months of the year.

Company revenues increased by 13% y/y to GEL202mn, below investors' expectations by around 6%.

In the January-September period, the company performance was stronger in terms of net profit. Ebitda soared by 23.4% y/y to GEL77.3mn (\$28mn) while the bottom line expanded by 12% y/y to GEL34.0mn (\$12.6mn) for reported total revenues worth GEL622mn, 13% up y/y.

Results were good across all three of the company's businesses, the company's management commented in a press release. The pharmacy and distribution business performed particularly well with double-digit revenue growth and an Ebitda margin in excess of 10% in the third quarter. Results in the healthcare services business are consistently improving and the medical insurance business delivered a strong third quarter, with moderate revenue growth and a significant improvement in the loss ratio leading to a profit before tax of GEL2.6mn in the quarter.