



Country Partnership Strategy

December 2014

Georgia 2014–2018

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Asian Development Bank

CURRENCY EQUIVALENTS

(as of 5 November 2014)

Currency unit	–	lari (GEL)
GEL1.00	=	\$0.5701
\$1.00	=	GEL1.754

ABBREVIATIONS

ADB	–	Asian Development Bank
ADF	–	Asian Development Fund
COBP	–	country operations business plan
CPS	–	country partnership strategy
GDP	–	gross domestic product
IDP	–	internally displaced person
IED	–	Independent Evaluation Department
IMF	–	International Monetary Fund
IOS	–	interim operational strategy
MFF	–	multitranches financing facility
MSME	–	micro, small, and medium-sized enterprises
O&M	–	operation and maintenance
PPP	–	public–private partnership
TA	–	technical assistance

NOTES

In this report, “\$” refers to US dollars.

Vice-President	W. Zhang, Operations 1
Director General	K. Gerhaeuser, Central and West Asia Department (CWRD)
Team leader	K. Julian, Country Director, Georgia Resident Mission (GRM), CWRD
Team members	<p>G. Abel, Senior Portfolio Management Specialist (Integrity), CWRD</p> <p>E. Araneta, Principal Operations Coordination Specialist, Private Sector Operations Department (PSOD)</p> <p>R. Barreto, Financial Sector Specialist, CWRD</p> <p>M. Beauchamp, Social Development Specialist (Safeguards), CWRD</p> <p>S. Campbell, Senior Social Development Specialist, CWRD</p> <p>F. Catacutan, Associate Programs Officer, CWRD</p> <p>I. Chkonia, Senior Project Officer, GRM, CWRD</p> <p>J. Farinha, Economist, CWRD</p> <p>B. Goalou, Urban Transport Specialist, CWRD</p> <p>R. Hartel, Principal Investment Specialist, PSOD</p> <p>T. Kanai, Senior Advisor, Office of Cofinancing Operations (OCO)</p> <p>G. Kiziria, Senior Project Officer (Infrastructure), GRM, CWRD</p> <p>G. Luarsabishvili, Associate Economics Officer, GRM, CWRD</p> <p>T. Luo, Senior Energy Specialist, CWRD</p> <p>W. Montealto, Operations Assistant, CWRD</p> <p>B. Mirbabaev, Senior Financing Partnerships Specialist, OCO</p> <p>T. Niazi, Principal Public Management Specialist, CWRD</p> <p>N. Nikuradze, Operations Assistant, GRM, CWRD</p> <p>T. Papuashvili, Associate Project Analyst, GRM, CWRD</p> <p>L. Schou-Zibell, Principal Economist, CWRD</p> <p>P. Seneviratne, Principal Transport Specialist, CWRD</p> <p>N. Singru, Senior Transport Specialist, CWRD</p> <p>V. Tan, Director, CWRD</p> <p>A. Torres, Senior Public–Private Partnership Specialist, CWRD</p> <p>T. Tran, Senior Environmental Specialist, CWRD</p> <p>L. Vavakis, Economist, CWRD</p> <p>X. Yi, Senior Financial Management Specialist, CWRD</p>
Peer reviewers	<p>K. Lao-Araya, Principal Results Management Specialist, Strategy and Policy Department (SPD)</p> <p>K. Nam, Senior Economist, Economics and Research Department</p> <p>R. Sabirova, Evaluation Specialist, Independent Evaluation Department</p> <p>W. Um, Deputy Director General, Regional and Sustainable Development Department</p> <p>B. Woods, Principal Results Management Specialist, SPD</p>

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COUNTRY AT A GLANCE

Economic^a	2008	2009	2010	2011	2012	2013
GDP (\$ billion, current)	12.8	10.8	11.6	14.4	15.8	16.1
GDP per capita (\$, current)	2,921	2,455	2,623	3,230	3,523	3,597
GDP growth (% , in constant prices)	2.3	(3.8)	6.3	7.2	6.2	3.2
Agriculture	(4.4)	(6.8)	(4.8)	8.0	(3.7)	9.8
Industry	(3.9)	(3.5)	9.1	9.4	9.5	1.9
Services	7.4	(3.4)	7.8	5.7	6.2	3.1
Gross domestic investment (% of GDP)	26.0	13.0	21.6	26.2	28.9	24.8
Gross domestic saving (% of GDP)	(2.7)	(6.1)	4.1	7.8	10.2	12.3
Consumer price index (average annual % change) ^b	10.0	1.7	7.1	8.5	(0.9)	(0.5)
Liquidity (M3) (annual % change)	7.9	7.7	30.1	14.5	11.4	24.5
Overall fiscal surplus (deficit) (% of GDP)	(6.3)	(9.2)	(6.8)	(3.6)	(3.0)	(2.7)
Merchandise trade balance (% of GDP)	(30.0)	(22.3)	(22.3)	(24.3)	(26.6)	(21.7)
Current account balance (% of GDP)	(22.0)	(10.5)	(10.3)	(12.7)	(11.7)	(5.9)
External debt service (% of exports of goods and services)	17.7	26.2	20.5	15.9	18.3	17.5
Gross external debt (% of GDP) ^c	44.3	61.3	65.1	60.3	66.7	65.3
Unemployment rate (%)	16.5	16.9	16.3	15.1	15.0	14.6

Poverty and Social	1990	2000	Latest Year
Population (million)	4.8	4.4	4.5 [2013]
Population growth (annual % change)	0.0	(0.8)	(0.3) [2013]
Maternal mortality ratio (per 100,000 live births) ^d	50.0	60.0	41.0 [2013]
Infant mortality rate (per 1,000 live births)	40.5	31.2	11.7 [2013]
Life expectancy at birth (years)	70.0	71.6	73.9 [2012]
Adult literacy (%)	99.7 [2012]
Primary school gross enrollment (%)	97.4	97.3	106.1 [2012]
Child malnutrition (% below 5 years old)	...	2.2	1.1 [2009]
Population below poverty line (%) ^e	21.4 [2013]
Poverty headcount ratio at \$2/day (PPP) (%)	...	38.6	35.6 [2010]
Population with access to improved water source (%)	85.0	89.2	98.7 [2012]
Population with access to improved sanitation (%)	96.5	95.4	93.3 [2012]

Environment	1990	2000	Latest Year
Carbon dioxide emissions (kilotons)	...	4,536	6,241 [2010]
Carbon dioxide emissions per capita (tons)	...	1.0	1.4 [2010]
Forest area (square kilometers)	27,790	27,678	27,372 [2012]
Urban population (% of total population)	55.0	52.6	53.1 [2013]

ADB Portfolio (sovereign loans, as of 31 December 2013)	OCR	ADF	Total
Total number of loans	3	8	11
Net loan amount (\$ million, cumulative)	261.9	555.3	817.2
Disbursements			
Total funds available for withdrawal (\$ million)	188.9	456.4	645.3
Disbursed amount (\$ million, cumulative)	6.5	215.8	222.3
Percentage disbursed (disbursed amount/total available)	3.5	47.3	34.5

... = not available, () = negative, [] = latest year for which data are available, ADB = Asian Development Bank, ADF = Asian Development Fund, GDP = gross domestic product, M3 = broad money, OCR = ordinary capital resources, PPP = purchasing power parity.

^a Data refer to fiscal year. GDP data in 2013 are estimates pending release of final GDP data in November 2014.

^b Refers to period average increase.

^c Excluding intercompany loans.

^d Modeled estimate based on regression model using information on fertility, birth attendants, and HIV prevalence. National estimate in 2012 is 22.9.

^e The proportion of the population living below the relative poverty line, equal to 60% of the median consumption (%).

Sources: ADB; International Monetary Fund; Ministry of Environment and Natural Resources Protection of Georgia; Ministry of Finance of Georgia; National Bank of Georgia; National Statistics Office of Georgia; United Nations Development Programme. 2013. *The UN Human Development Report 2013*. New York; United Nations. Millennium Development Goals Indicators. <http://mdgs.un.org/unsd/mdg/SeriesDetail.aspx?srid=749> (accessed 10 October 2014); World Bank. 2012. *Georgia Poverty Assessment*. Washington, DC; World Bank. 2011. *Georgia: Poverty Dynamics since the Rose Revolution*. Washington, DC; and World Bank. World Development Indicators Online. <http://data.worldbank.org/country/georgia> (accessed 13 September 2014).

I. DEVELOPMENT TRENDS AND ISSUES

A. Country Background

1. Georgia is located in the Southern Caucasus, at the crossroads of Europe and Asia. It is an important transit corridor for many countries in Central and West Asia, especially Armenia and Azerbaijan. Owing to economic and institutional reforms and sound macroeconomic policies, Georgia's economy expanded by 9.6% annually, on average, during 2003–2007, and withstood the effects of the 2008 armed conflict with the Russian Federation and the global economic crisis. The conflict displaced more than 200,000 people and demonstrated the fragility of the Caucasus region, adding to political risk perceptions, interrupting investment flows, and challenging the country's territorial integrity. Political relations with the Russian Federation remain strained but have been improving since 2013.¹ Despite these challenges, Georgia's gross domestic product (GDP) per capita rose from \$916 in 2003 to \$3,597 in 2013, as GDP growth averaged nearly 6%. Georgia is classified as a lower-middle-income economy.²

2. **Economic and institutional reforms.** Broad economic and institutional reforms since 2003 have transformed Georgia's business and economic environment. The government has streamlined business regulations, liberalized trade policies, simplified the tax system, reduced the size of the civil service, and privatized government assets. As a result, governance and the business environment have improved, and Georgia's ranking in several international indexes has risen.³ However, rankings may not capture performance across key dimensions. Challenges remain in access to finance, the availability of skilled workers,⁴ regulatory structures, and the framework for public–private partnerships (PPPs).⁵ These issues and the pattern of reforms have constrained growth in the more labor-intensive tradable sectors.

3. **Unemployment and poverty.** Georgia's strong growth during the past decade has not delivered commensurate declines in unemployment and poverty. Infrastructure gaps, agricultural stagnation, and an entrenched skills mismatch in the labor market have dampened the impact of growth on poverty reduction. The official unemployment rate rose from 11.5% in 2003 to 16.9% in 2009, before moderating to 14.6% in 2013. Labor shedding in the public sector exceeded job creation in the private sector. An estimated one-fifth of the labor force is underemployed. The percentage of the population living below the relative poverty line declined from 24.9% in 2004 to 21.4% in 2013.⁶ The percentage of the population living on less than \$2.00 a day at purchasing power parity decreased only marginally from 36.7% in 2003 to 35.6% in 2010, while the poverty headcount ratio at \$1.25 a day at purchasing power parity slightly increased from 17.7% to 18.0% over the same period. With persistent high unemployment, poverty reduction has mostly resulted from declining food prices in 2012 and increasing social transfers and remittance inflows.⁷ The Gini coefficient in 2013 remains high at 0.42, reflecting the concentration of income growth in urban areas and among the top 10% of income earners.⁸ Georgians living in small towns and engaging in smallholder agriculture have gained little.

¹ Georgia has unilaterally established visa-free entry for Russian citizens, which has led to an influx of visitors for both trade and tourism. The Russian Federation recently lifted an embargo on Georgia's agricultural exports.

² Georgia's gross national income per capita, based on the World Bank's Atlas method, was \$3,570 in 2013.

³ Georgia's ranking on the overall ease of doing business improved to eighth of 189 countries in the World Bank's Doing Business 2014 report from 112th of 145 countries in the 2005 report. However, rankings in key areas lag, including insolvency resolution and business exit, and judicial independence.

⁴ Technical and vocational skills are lacking, while the pool of workers with tertiary education is large.

⁵ This includes institutional mechanisms to ensure that PPPs optimize value-for-money for the government.

⁶ The relative poverty line is equal to 60% of median consumption.

⁷ Poverty Analysis (accessible from the list of linked documents in Appendix 2).

⁸ The National Statistics Office of Georgia estimates the Gini coefficient by consumption expenditures at 0.40 in 2013.

4. **Millennium Development Goals and gender equality.** Some progress has been made in reducing non-income poverty, with Georgia on track to meet most of its education and health Millennium Development Goal commitments. However, gender-related disparities need to be addressed, and challenges persist, including unequal access to assets and resources, availability of affordable childcare, skewed sex ratio at birth, and domestic violence. Access to education has not translated into increased employment and economic participation. The gender wage gap remains high with women earning 42% less than men.⁹ Women also are underrepresented in politics and decision making, holding only 11.3% of parliamentary seats.

B. Economic Assessment and Outlook

5. **Economic outlook.** Since 2003, Georgia has seen strong real GDP growth, rising real wages, a declining fiscal deficit, and improved competitiveness. Key areas contributing to the economy are services (led by trade, tourism, and transport); manufacturing (led by ferroalloys, nitric fertilizer, cement, and steel and scrap metal); construction; and mining. Despite slower growth in 2013 and increasing regional instability in 2014, the economic outlook is positive. The Asian Development Bank (ADB) forecasts an acceleration of real GDP growth to 5.5% in 2014 and in 2015. The potential drivers of this growth include tourism, manufacturing and agribusiness, and energy exports. Tourism is a fast-growing sector, accounting for an estimated 14% of total employment and 16% of GDP (direct and indirect) in 2013.¹⁰ Manufacturing, agribusiness, and energy exports will benefit from continued improvements in infrastructure, particularly roads and supply chain management, and better access to finance. Inflation is forecast to accelerate to 4.0% in 2014 and 5.0% in 2015, as faster economic growth, and higher pensions and transfer payments are expected to generate demand-side inflationary pressures.

6. **Vulnerabilities.** Georgia is vulnerable to exogenous shocks because of its heavy reliance on foreign direct investment and remittance inflows, low domestic savings, large current account deficit, and a high level of dollarization.¹¹ While foreign direct investment has declined from its 2007 peak of \$2 billion, it remains important for the economy at 5.8% of GDP in 2013. The persistent current account deficit reflects the high import content of public infrastructure investments that underpinned economic growth during 2003–2012, and the closing of the Russian market to Georgia’s agricultural exports in 2006. The current account deficit improved substantially in 2013, and further to 5.6% by mid-year 2014, reflecting in equal measure the structural improvement in agricultural exports and sustained growth in tourism, and a cyclical drop in imports due to lower economic growth and reduced public infrastructure investments. The International Monetary Fund (IMF) projects a decline in the current account deficit to 5% of GDP by 2019; however, this reduction is contingent on continued fiscal consolidation, a flexible exchange rate regime, and implementation of structural reforms to enhance competitiveness. Given Georgia’s economic vulnerabilities, the IMF approved in 2012 a two-year Stand-By Arrangement as a medium-term macroeconomic safety net. A new three-year Stand-By Arrangement was endorsed by the IMF’s Board in July 2014. This SDR100 million (about \$154 million) program aims to facilitate Georgia’s external adjustment, reduce key macroeconomic vulnerabilities, rebuild fiscal space, and support growth.

7. **Barriers to private sector development and inclusive growth.** Despite improvements in business climate survey rankings, constraints on private sector development and inclusive

⁹ National Statistics Office of Georgia. 2013. *Women and Men in Georgia*. Tbilisi. <http://www.geostat.ge>

¹⁰ World Travel and Tourism Council. 2014. *Travel & Tourism, Georgia: Economic Impact 2014*. London.

¹¹ Economic Analysis (accessible from the list of linked documents in Appendix 2). This vulnerability could pose further downside risks to the economic outlook in view of the current geopolitical risks.

economic growth remain.¹² They include gaps in transport, logistics, energy, and municipal infrastructure; insufficient regional economic cooperation; a shortage of skilled labor (particularly engineers and technicians); lack of business skills among micro, small, and medium-sized enterprises (MSMEs); and limited access to affordable bank financing. To realize its potential as a transit corridor and a regional trade and logistics hub, Georgia needs to complete improvements to the East–West Highway, which connects Black Sea ports to Azerbaijan. High transport and logistical costs also leave parts of Georgia economically isolated from national and regional markets. Despite notable progress in reducing corruption, concerns remain and the judicial system’s capacity to protect private property and contracts needs to be strengthened.¹³

C. Highlights of Previous ADB Country Strategy

8. **Previous country strategy and program.** Georgia joined ADB in 2007, and ADB approved an interim operational strategy (IOS), 2008–2009 in January 2008.¹⁴ The IOS focused on improving municipal service delivery, reducing road transport constraints, and upgrading energy infrastructure. During implementation, the scope of the IOS was widened to include support for the government’s fiscal response to the conflict with the Russian Federation and the global economic crisis. During 2007–2013, ADB approved a total of \$1.36 billion for 21 loans, including three nonsovereign loans totaling \$125 million and nine tranches under the three ongoing multitranche financing facilities (MFFs). Loans and MFF subprograms approved were on average 3–4 times larger than anticipated in the IOS because of larger project scopes and the availability of additional Asian Development Fund (ADF) and ordinary capital resources.

9. **Assessment of performance and lessons learned.** The final review of country operations covering ADB assistance during 2008–2012 concluded that the performance of the program had been satisfactory.¹⁵ ADB successfully established its presence in Georgia within a short period, becoming a leading source of infrastructure finance. The program was broadly in line with country needs, completed operations were successful, and ongoing operations are likely to achieve their goals. Implementation of the MFFs has, however, been adversely affected by delays, cost overruns, scope changes, and weak safeguard implementation capacity.¹⁶ Sustainability was identified as a concern given low rates of cost recovery and limited spending on infrastructure operation and maintenance (O&M). Key program strengths included (i) strong government ownership, (ii) government commitment to macroeconomic stability and private-sector-led growth, and (iii) ADB responsiveness to changes in the development setting. To improve development effectiveness, the review recommended (i) making growth more inclusive in the core sectors, including through dialogue on finance sector reforms; (ii) clearly identifying country- and sector-level results; (iii) improving infrastructure sustainability; (iv) enhancing the quality of government project preparation; (v) focusing more on capacity development, policy reform, and knowledge services; and (vi) forging stronger partnerships to leverage the impacts of ADB assistance.

10. **Independent validation.** ADB’s Independent Evaluation Department (IED) *Validation Report of the Final Review of Country Operations, 2008–2012* rated the IOS and the country

¹² Private Sector Assessment (accessible from the list of linked documents in Appendix 2). This vulnerability could pose further downside risks to the economic outlook in view of the current geopolitical risks.

¹³ Georgia was ranked 55th of 177 countries in Transparency International’s 2013 corruption perceptions index, compared with 133rd of 145 countries in the 2004 index.

¹⁴ ADB. 2008. *Georgia: Interim Operational Strategy, 2008–2009*. Manila.

¹⁵ Country Strategy Final Review (accessible from the list of linked documents in Appendix 2).

¹⁶ Portfolio performance reflects a low overall disbursement ratio due to start-up delays and frequent changes in scope.

program *successful*.¹⁷ IED rated all aspects of the program, except efficiency, *satisfactory* or better. IED rated the program *less than efficient*, citing low disbursements, cost overruns, frequent scope changes, weak monitoring and evaluation systems, and implementation delays due to protracted land acquisition and procurement. The lessons drawn by IED include the need for stronger focus on inclusive growth, more attention to policy reform, and more careful scrutiny of project designs and costs estimates. IED recommended increased support for energy planning for efficient hydropower development, and for wastewater treatment and sanitation. IED also advised assessing the problem of internally displaced persons (IDPs) and the extent to which their vulnerability might be addressed through the country program.

11. Responding to these recommendations, the country partnership strategy (CPS), 2014–2018 includes (i) sharper focus of infrastructure on inclusive growth (e.g., targeting secondary roads and smaller towns in lagging regions); (ii) policy-based lending and a larger technical assistance (TA) program targeting policy reforms and capacity development, including finance sector reform; and (iii) continued financing for wastewater treatment and sanitation infrastructure. As other development partners have sizeable grant assistance for energy policy and planning, ADB will continue to focus on nonsovereign lending for private sector hydropower, in line with government priorities.¹⁸ ADB assistance for urban services addresses the needs of IDPs as a part of project design. This complements the substantial grant and loan assistance for IDPs provided by other development partners.

II. THE COUNTRY STRATEGY

A. Government National Strategy

12. **National development objectives.** The government's Socio-economic Development Strategy of Georgia (Georgia 2020) targets inclusive economic growth by ensuring macroeconomic stability and effective public administration, improving private sector competitiveness, developing human capital, and increasing access to finance.¹⁹ Private sector competitiveness will be improved by developing infrastructure; maximizing transit potential; further improving the business environment; and supporting innovation, technology, and export growth and diversification. Human capital will be developed by improving general and vocational education; strengthening social protection; and providing quality, affordable health care. Private sector access to finance will be increased by promoting domestic savings, attracting more foreign investment, and developing the finance sector (especially capital markets and nonbank financial institutions). Local government reform will promote regional development and increase the role of local self-governing bodies.

13. **Intersection with ADB's Midterm Review of Strategy 2020.** Georgia 2020 and ADB's Midterm Review of Strategy 2020 both foster inclusive economic growth, while enhancing support for human resource development and social protection.²⁰ Both strategies promote sustainable infrastructure, private sector development, good governance, and innovation and knowledge solutions. Both strategies also emphasize the need to ensure the environmental sustainability of growth, including the integration of climate risk management into infrastructure planning. Georgia's vision to leverage its strategic location and develop as a transport corridor is also consistent with the midterm review's emphasis on regional integration.

¹⁷ Georgia: Validation Report of the Final Review of Country Operations, 2008–2012 (accessible from the list of linked documents in Appendix 2).

¹⁸ The World Bank is financing a strategic environmental assessment for hydropower development in 2014.

¹⁹ Government of Georgia. 2014. *Socio-economic Development Strategy of Georgia (Georgia 2020)*. Tbilisi.

²⁰ ADB. 2014. *Midterm Review of Strategy 2020: Meeting the Challenges of a Transforming Asia and Pacific*. Manila.

14. **ADB and other development partners.** Many development agencies operate in Georgia and comprehensively support the country's economic development.²¹ The World Bank finances infrastructure (roads, municipal infrastructure and services, and irrigation) and provides policy and project lending to develop human resources (health, education, and social protection) as well as business competitiveness and public financial management. The European Bank for Reconstruction and Development and the International Finance Corporation have supported a wide array of private sector investments, and together with German development cooperation through KfW, are assisting in energy and access to finance. The European Investment Bank and Japan have financed roads. Major grant financiers for energy, agriculture and rural development, education, and health and social protection include the European Union and the United States. The IMF supports macroeconomic stability through standby arrangements, advises on tax administration, and has assessed the implementation of anti-money-laundering policy. To achieve synergies and avoid duplication, ADB extensively consulted its development partners during the formulation of its CPS.

B. ADB Country Strategy

15. The CPS is based on ADB's Midterm Review of Strategy 2020 and fully aligns with Georgia 2020. It seeks to foster inclusive economic growth, while enhancing regional connectivity and ensuring environmentally sustainable growth. Its priority sectors (transport, water supply and sanitation, energy, public sector management, and finance) are within ADB's core areas of operations. Common drivers of change in Georgia 2020 and the CPS include private sector development, governance and capacity development, and knowledge solutions.

1. Strategic Agenda

16. **Inclusive economic growth.** The CPS primarily focuses on the first pillar (high and sustainable growth to create and expand economic opportunities) and the second pillar (broader access to economic opportunities) of inclusive economic growth. It addresses some of the main barriers to inclusive economic growth, including deficiencies of transport, energy, and basic urban infrastructure, and inadequate access of the private sector to finance. ADB will foster inclusive economic growth by helping to (i) improve internal and regional market connectivity; (ii) make essential drinking water, and sewerage and sanitation services more accessible and reliable, particularly in secondary cities, which are the potential hubs for agribusiness and tourism; (iii) improve the security and stability of power systems, especially for communities in lagging regions; (iv) strengthen public sector management; and (v) increase access to finance, particularly for MSMEs and customers outside Tbilisi. Infrastructure investments, combined with policy reform and capacity development support, will improve social conditions and economic opportunities in smaller towns and cities, stimulating investment, job creation, and incomes where these are needed the most. The CPS also supports the third pillar of inclusive growth (provision of adequate social protection to reduce poverty and vulnerabilities) through policy-based lending to improve domestic resource mobilization and help Georgia strengthen its fiscal management to sustain higher levels of social expenditure in the medium term.²² Support for

²¹ The development coordination matrix is in Table 5 of the Country and Portfolio Indicators (accessible from the list of linked documents in Appendix 2).

²² This third pillar is also supported through the World Bank's multiyear development policy lending for health, education, and social protection; and grant financing from the European Union, the United States, and other bilateral donors (for health, education, and vocational training). The Millennium Challenge Corporation provides a \$140 million grant for primary and secondary education, technical and vocational education and training, and university education (courses in science, math, and engineering). See Poverty Analysis and development coordination matrix in Table 5 of the Country and Portfolio Indicators (accessible from the list of linked documents in Appendix 2) for details.

capital markets and pension reform will also help Georgia develop a sustainable system of social protection by enhancing domestic savings generation and mobilizing long-term finance.

17. **Regional integration.** ADB will help Georgia realize its potential as a transit corridor and a regional trade and logistics hub through lending and knowledge work, including dialogue with official, technical, and civil society organizations and networks in the southern Caucasus.²³ The East–West Highway will reduce travel times and costs on the main regional trade route, while complementing ADB assistance for Armenia’s North–South Road Corridor. Support for multimodal transport policy and regional power trade will help Georgia integrate into regional and global markets. ADB will encourage private investment in value chains and logistics facilities to help improve trade competitiveness. ADB will bring neighboring countries together to discuss regional transport, power trade, and other economic issues. Knowledge-sharing initiatives to leverage Georgia’s experience in customs reform and trade facilitation will continue, particularly with the Central Asia Regional Economic Cooperation countries.

18. **Environmentally sustainable growth.** ADB will finance clean energy and energy efficiency projects, water supply and sanitation, and solid waste management. ADB-financed project planning and engineering designs will mainstream climate change adaptation and resilience, as well as disaster risk considerations. ADB will promote energy-efficient water systems and wastewater treatment, and sustainable municipal plans, and will encourage sustainable urban transport including low-carbon mobility and mass transport systems. Improvements in road networks and traffic management will help reduce vehicle damage and pollution. ADB will also help build government capacity in climate change mitigation and adaptation, particularly through regional TA and knowledge-sharing. This will include support for disaster-risk screening and cost-effective risk mitigation strategies during project design.

2. Priority Sectors

19. ADB will focus on sectors where it has comparative strengths and that require large and complex public investments, policy and institutional reforms, and capacity development. ADB will (i) support infrastructure using its ongoing MFFs and selected strategic projects, (ii) align policy reform and capacity development TA and loan components closely with strategic priorities, and (iii) integrate knowledge products with investment operations to draw lessons for scaling-up. By improving connectivity, power networks, and access to basic urban services in small towns, ADB assistance will complement government programs in agriculture and rural development. Advisory and capacity development support will be provided in finance, public sector management, governance, and safeguards to improve infrastructure service delivery. The TA program will enhance development impact by making ongoing infrastructure investments more sustainable and the growth they support more inclusive. The CPS supports regional cooperation and economic integration in transport, trade, and power exchange. It promotes PPPs to meet the government’s ambitious infrastructure and service-delivery targets.

20. **Transport.** The East–West Highway remains incomplete, and secondary and local roads are in poor condition. ADB will help integrate the East–West Highway with other transport modes, and support the formulation of a national transport policy for more efficient, accessible, and sustainable transport. Effective implementation of the ongoing East–West Highway MFF will foster trade and enhance regional connectivity.²⁴ ADB will help link this major road corridor to

²³ At the end of 2013, 56% of the active sovereign portfolio supported regional integration.

²⁴ ADB. 2009. *Report and Recommendation of the President to the Board of Directors: Proposed Multitranche Financing Facility to Georgia for the Road Corridor Investment Program*. Manila. Two tranches totaling \$258 million under the MFF finance the 34-kilometer Kobuleti bypass.

regional centers and lagging areas through selected secondary and local road improvements to help connect the poor to markets and make growth more inclusive.²⁵ ADB will assist in modernizing technical standards and specifications for roads; narrowing critical gaps in sector, technical, and project management skills; and improving road safety. TA will strengthen the enabling environment for PPPs, where critical for the operational and financial sustainability of infrastructure, such as in performance-based contracting and toll roads.

21. **Urban water, sanitation, and transport services.**²⁶ Rapid urbanization supports economic growth, but has put stress on basic service delivery and the environment. Problems include unreliable drinking water, insufficient sewerage, and little wastewater treatment. Public transport systems, including intercity connections and pedestrian facilities, need attention. ADB will build on existing MFF operations in urban transport and water supply and sanitation to promote livable cities that are competitive, socially inclusive, and environmentally sound.²⁷ This requires integrated urban planning and policy formulation, including city development plans and follow-on investment. ADB will address the basic infrastructure needs of small towns and secondary cities that are the economic links between rural areas and market centers. ADB will increase its focus on wastewater and solid waste management; continue to enhance the operational and managerial performance of water utilities; and maintain assistance for policy and regulatory reforms for sustainable and efficient urban services, including through PPPs.

22. **Energy.** ADB will continue to help Georgia improve its electricity transmission and distribution network, and to enhance energy efficiency through the rehabilitation of aging assets.²⁸ Private sector operations will promote low-carbon development by financing hydropower generation. Ongoing and future support for regional power transmission enhancement will boost power system reliability, enhance energy efficiency, and construct physical facilities for power exports, furthering progress toward regional cooperation and integration.²⁹ These initiatives will also promote climate change mitigation and adaptation. ADB will collaborate with its development partners to support regulatory policy and institutional reforms to ensure a sound regulatory and safeguards environment for private sector investment, including cross-border transmission connectivity and power trade.³⁰

23. **Public sector management.** Public sector management in Georgia has improved significantly, but it still has many weaknesses. Through policy-based lending, ADB will support public sector management reforms to increase domestic savings and improve the legal, regulatory, and institutional framework for private sector development. In particular, ADB will support the introduction of contributory pension schemes, establishment of an effective

²⁵ Some 38% of secondary roads and 54% of local roads are in poor or very poor condition, hindering market access.

²⁶ Urban transport is discussed under water and other urban infrastructure and services, although it is included under transport in the results frameworks.

²⁷ ADB. 2010. *Report and Recommendation of the President to the Board of Directors: Proposed Multitranche Financing Facility to Georgia for the Sustainable Urban Transport Investment Program*. Manila; ADB. 2011. *Report and Recommendation of the President to the Board of Directors: Proposed Multitranche Financing Facility to Georgia for the Urban Services Improvement Investment Program*. Manila.

²⁸ While the power transmission and distribution system has improved dramatically, much of it still depends on extremely old and potentially unreliable technology. The average age of existing hydropower plants is 37 years; the oldest plants have operated for 75 years, and will need replacing.

²⁹ ADB. 2012. *Report and Recommendation of the President to the Board of Directors: Proposed Loan to Georgia for Regional Power Transmission Enhancement Project*. Manila.

³⁰ World Bank support for a strategic environmental assessment in the hydropower sector should lay a sound environmental basis for further hydropower development.

competition agency, tax reforms, and improvement of the legal and regulatory framework for PPPs.³¹ ADB will help strengthen capital budgeting and public debt management.

24. **Finance.** ADB will support the government in improving access to finance for the private sector, including MSMEs in agribusiness, retail trade, small manufacturing, and tourism. Through policy-based lending and TA grants, ADB will help Georgia promote finance sector development. ADB will support a more favorable legal and regulatory framework for developing nonbank financial institutions, including pension funds. ADB will assist in developing government securities and corporate bond markets to promote capital market development, including local currency bond issuance. ADB private sector operations will continue ongoing support to commercial banks to expand lending to MSMEs, particularly in Georgia's regions.

3. Drivers of Change

25. **Private sector development and private sector operations.** ADB will promote private sector development by (i) addressing major infrastructure constraints and skills gaps through public and private service provision; (ii) improving the legal, regulatory, and institutional framework for doing business; (iii) increasing access of the private sector to finance; and (iv) enhancing the enabling environment for PPPs. Support will be provided for developing a framework and legislative and regulatory arrangements for PPPs. Following on from upstream support for PPP frameworks and government capacity development, ADB will explore opportunities to provide transaction advisory services on the design and development of PPP projects, including opportunities in transport and logistics infrastructure. To help improve financial markets, ADB will support the use of international financial reporting standards to improve the resilience and service outreach of financial institutions, enhance transparency and corporate governance, and encourage capital market development. Assistance for financial inclusion will promote financial literacy among consumers and entrepreneurs, and increase access to financial services in rural areas and among MSMEs.

26. As viable investments emerge, ADB will expand its private sector operations. ADB's Private Sector Operations Department will explore investment in hydropower generation, transport, logistics, and agribusiness. In addition, ADB will continue to support qualified commercial banks through loan and guarantee facilities for trade finance, and MSME and rural finance; and may explore opportunities to develop commercial bank capacity for project finance.

27. **Good governance and capacity development.** ADB will contribute to institutional reforms by enhancing implementation capacities, improving institutional frameworks, and strengthening governance systems. ADB will support sector reforms to (i) improve planning; (ii) enhance procurement, audit, reporting, and financial management capacity in implementing agencies; and (iii) strengthen the regulatory oversight (including anticorruption measures) of implementing agencies. Improvements in public sector financial management of infrastructure delivery will be supported through TA for (i) more transparent and efficient project management policies and procedures, including those related to safeguards; and (ii) improved financing and management of O&M, including greater cost recovery.

28. ADB is also preparing a country safeguards framework. ADB will identify gaps between national requirements and ADB's Safeguard Policy Statement (2009), and advise on compliance with the Safeguard Policy Statement. ADB and Georgia will jointly develop the

³¹ At present, PPPs are constrained by an inadequate legal and regulatory framework that does not boost investor confidence and hampers full private sector participation in economic growth.

country safeguards framework as a knowledge product to guide more effective and efficient safeguards design and project implementation.

29. **Gender equality.** Gender equality will be fostered through mainstreaming gender in relevant ADB projects. Broader gender impacts will be achieved by (i) promoting the use of sex-disaggregated data and gender analysis to inform project design, (ii) ensuring that women are encouraged to apply for positions created under ADB-supported projects, (iii) encouraging the consideration of women candidates on ADB-supported institutional bodies, and (iv) developing project communication strategies that consider women's concerns. Where possible, projects will include gender action plans with design features, targets, and indicators to promote women's participation and access to project benefits. Women's access to finance will be supported through policy-based lending and TA for financial inclusion.

30. **Knowledge solutions.** ADB will promote knowledge solutions by capturing, generating, and disseminating operationally relevant knowledge from the Georgia portfolio and from across ADB. Planned knowledge products include disseminating Georgia's experience in using geographic information systems to improve infrastructure asset management. ADB will also apply ADB-wide knowledge to design projects and reform programs. Lessons will be drawn from well-performing programs and disseminated through policy notes and public outreach efforts. In the finance sector, Southeast Asia's experience in bond market development will be shared and exchanges organized between professional organizations. ADB will also collaborate with the Academy of the Ministry of Finance, local universities, and research centers to foster wider knowledge sharing. Consistent with ADB's Midterm Review of Strategy 2020 and emphasis on a "One ADB" approach to knowledge management, ADB's Georgia Resident Mission will take the lead in preparing a country knowledge plan and a small-scale TA to support implementation.³²

III. STRATEGY IMPLEMENTATION

A. Indicative Resource Parameters

31. Financing for the CPS is estimated at \$1.0 billion.³³ A \$516.0 million assistance package is proposed for the country operations business plan (COBP), 2015–2017, comprising ordinary capital resources lending of \$383.5 million and ADF lending of \$132.5 million.³⁴ With \$183 million of proposed lending in 2014, the CPS pipeline for 2014–2017 totals \$699 million. Cofinancing will be pursued to increase the impact of ADB assistance. An annual average of about \$3.0 million in TA resources is proposed under the COBP, of which nearly 50% will be allocated to project preparation. These resources will be supplemented by regional TA and urban and water partnership funds. TA grants will target policy and institutional reform for inclusivity and sustainability, and improve the quality of infrastructure. Under the cost-sharing arrangements, ADB will finance up to 99% of total project costs on a portfolio-wide basis.

B. Program Overview

32. The COBP, 2015–2017 details the operational program.³⁵ In line with the CPS, sovereign operations will focus on five sectors: transport, water and other urban infrastructure

³² Efforts will be guided by the Midterm Review of Strategy 2020 (footnote 20) and ADB. 2013. *Knowledge Management Directions and Action Plan, 2013–2015*. Manila. A country knowledge plan is under preparation.

³³ This comprises public and private sector loans and credit enhancement products.

³⁴ ADB has approved Georgia's graduation from access to ADF resources with effect from 1 January 2017. The resources available for approval during 2015–2017 are \$482.5 million, comprising ordinary capital resources of \$350.0 million and ADF of \$132.5 million. The COBP assumes overprogramming of \$33.5 million.

³⁵ Country Operations Business Plan, 2015–2017 (accessible from the list of linked documents in Appendix 2).

and services, energy, public sector management, and finance. The bulk of public sector lending comprises tranches under ongoing MFFs in urban water and sanitation for small towns and secondary cities, and urban transport. Policy-based lending for public sector management and finance will support increasing the availability of domestic resources for effective public and private investment. The remaining loans during the COBP period will finance projects to upgrade power transmission networks and rehabilitate secondary roads. Both projects will broaden access to public infrastructure and improve connectivity.

IV. RESULTS MANAGEMENT

A. Monitoring

33. ADB and the government will use the CPS results framework to track progress toward achieving the targeted results.³⁶ The CPS results framework will be updated annually during preparation of the COBPs and portfolio reviews. These consultations will help ensure the country program is responsive to the government's implementation capacity and Georgia's evolving development needs.

B. Risks

34. **Macroeconomic management risks.** Georgia faces macroeconomic risks due to the economy's openness and its reliance on foreign capital inflows. These risks are exacerbated by regional factors, including continued tensions with the Russian Federation. Political reconciliation with the Russian Federation and restoration of close economic ties is likely to be a lengthy and difficult process, which will be made more challenging by regional instability and Georgia's aspiration for closer integration with the European Union. The large trade and current account deficits, and the low level of domestic savings, make Georgia vulnerable to sudden changes in exports, remittances, and foreign direct investment inflows, which could negatively impact growth and revenues. To help improve Georgia's external position, ADB will (i) conduct targeted advisory work to strengthen the finance sector; and (ii) support enhanced competitiveness and productivity by improving power, transport, and urban infrastructure.

35. **Project management risks.** A governance risk assessment has identified risks and mitigating measures at the country and sector levels.³⁷ Key risks include decentralization reforms that could challenge effective asset management and service delivery if not properly designed and executed. Insufficient attention to regulatory and policy reform could also hamper service delivery, while institutional and O&M funding gaps could reduce project sustainability. While infrastructure projects tend to be well-designed, implementation is hampered by weak procurement outcomes and construction supervision.³⁸ To mitigate these risks, ADB will provide TA for public sector management and dialogue with government on sector policy and regulatory reforms to sustain infrastructure investment. ADB will also provide regional TA to support government capacity for safeguards and procurement. Annual country portfolio and country programming reviews will monitor delivery on agreed actions to improve project implementation and outcomes. Steps will be taken to strengthen resident mission capacity to oversee programming and project administration, as well as its capacity for knowledge management.³⁹

³⁶ Country Partnership Strategy Results Framework (Appendix 1).

³⁷ Risk Assessment and Risk Management Plan (accessible from the list of linked documents in Appendix 2).

³⁸ The quality of consulting engineers and contractors has not been consistent across the portfolio, suggesting the need for more emphasis on quality of tenders.

³⁹ The COBP, 2015–2017 includes small-scale TA resources to assist the resident mission in operationalizing the country knowledge plan.

COUNTRY PARTNERSHIP STRATEGY RESULTS FRAMEWORK

Country Development Goals			
1. Robust and inclusive GDP growth, averaging 7% per annum from 2014 to 2018 2. Price stability with inflation averaging 5% per annum 3. Improved external balance with the current account deficit declining to 6% of GDP by 2018 4. Fiscal prudence with the budget deficit remaining below 3% of GDP 5. Unemployment rate reduced from 14.6% in 2013 to less than 13% in 2018 6. Decrease in the Gini coefficient by consumption expenditure from 0.43 in 2010 to less than 0.38 in 2018 7. Population living below 60% of median consumption reduced from 21.4% in 2013 to less than 20% in 2018			
Sectors Selected for ADB Support			
Government Sector Objectives	Sector Outcomes that ADB Contributes to and Indicators	ADB Areas of Intervention	ADB Indicative Resource Allocation in the Pipeline for 2014–2017 and Strategic Priorities
1. Transport (Core Area 1: Infrastructure, Core Area 2: Environment, and Core Area 3: Regional integration)			
Improve transport and logistical infrastructure and services	<p>Outcome: More people have access to efficient, reliable, safe, and sustainable transport system including in urban areas</p> <p>Indicator: Number of fatalities per 10,000 registered cars decreases to 4.7 in 2018 (2013 baseline: 5.5)</p> <p>At least 2.5 million people in Anaklia, Batumi, Rustavi, and Tbilisi use improved transport services (including public transport and road expansion) by 2018 (2012 baseline: 0)</p> <p>Urban population in Tbilisi riding public transport increases to at least 59% by 2018 (2011 baseline: 54%)</p> <p>Annual average daily traffic at kilometer 64 of the Senaki–Poti–Sarpi road section increased to 7,500 vehicles by 2018 (2013 baseline: 6,000)</p>	<p>Construction and rehabilitation of expressways, national, secondary, and urban roads</p> <p>Road and sector-wide transport policies and reform</p> <p>Road maintenance and road safety</p> <p>Public transport and urban transport planning and reforms</p>	<p>\$157 million or 22% of total CPS envelope of which:</p> <p>ESG: 100% GEM: 0% PSD: 0% RCI: 64%</p>
2. Water and other urban infrastructure and services (Core Area 1: Infrastructure and Core Area 2: Environment)			
Modern systems of water supply and waste management developed	<p>Outcome: More people have access to good quality, reliable, and continuous water supply and improved sanitation services</p> <p>Indicator: Percentage of urban population with access to piped water supply increases to at least 86% by 2018 (2013 baseline: 75%)</p> <p>Percentage of urban population with access to piped sewerage connection increases to at least 72% by 2018 (2013 baseline: 64%)</p> <p>Population with access to improved sanitation increases to at least 95% by 2018 (2012 baseline: 93.3%)</p>	<p>Drinking water and sanitation systems, and wastewater management</p> <p>Urban planning, tariff policies reform, and sector development</p>	<p>\$292 million or 42% of total CPS envelope of which:</p> <p>ESG: 100% GEM: 97% PSD: 0% RCI: 0%</p>

Government Sector Objectives	Sector Outcomes that ADB Contributes to and Indicators	ADB Areas of Intervention	ADB Indicative Resource Allocation in the Pipeline for 2014–2017 and Strategic Priorities
3. Energy (Core Area 1: Infrastructure and Core Area 3: Regional integration)			
Increased energy security and reliable and efficient power supply for all consumers	<p>Outcome: More people use improved domestic energy supply</p> <p>Outcome: Increased energy trade with neighboring countries</p> <p>Indicator: Electric power consumption per capita increases to 2.690 GWh by 2018 (2013 baseline: 2.158 GWh)</p> <p>Export of electricity increases to at least 17% of domestic generation by 2018 (2013 baseline: 4%)</p> <p>Annual carbon dioxide emissions decreases by at least 20 kilotons by 2018 (2010 baseline: 6,241 kilotons)</p>	<p>Power generation, electricity transmission, renewable energy, and energy efficiency</p> <p>Energy sector policy and regulation, and management improvement</p>	<p>\$50 million or 7% of CPS envelope of which:</p> <p>ESG: 100% GEM: 0% PSD: 0% RCI: 0%</p>
4. Public sector management (Core Area: Other areas of operations)			
Increased efficiency and effectiveness of public sector management	<p>Outcome: Increased fiscal consolidation and efficient utilization of public resources</p> <p>Indicator: Fiscal deficit reduced to 2.5% of GDP by 2018 (2012 baseline: 3.0%)</p> <p>Effectiveness in collection of tax payments increased to C as measured by PEFA PI-15 by 2018 (2012 baseline: D)</p> <p>Effectiveness of spending unit's internal audit increased to B as measured by PEFA PI-21 by 2018 (2012 baseline: C)</p>	<p>Improved management of debt, cash, and fiscal risk</p> <p>Improved public financial management</p> <p>Legal and regulatory framework for enhancing domestic savings and capital markets</p>	<p>\$100 million or 14% of CPS envelope of which:</p> <p>ESG: 0% GEM: 63% PSD: 100% RCI: 0%</p>
5. Finance (Core Area 4: Finance sector development)			
Increased access to finance for private sector	<p>Outcome: Nonbank finance sector provides increased levels of financial intermediation</p> <p>Outcome: Increased use of efficient and reliable financial services by MSMEs</p> <p>Indicator: Bank credit to GDP increases to at least 38% in 2018 (2012 baseline: 35%)</p> <p>Domestic savings as percent of GDP increases to at least 22.0% by 2018 (2013 baseline: 12.3%)</p> <p>Access to financing through local equity markets rank improves to at least 100 by 2018 (2013 baseline: 126)</p>	<p>Finance sector development, money and capital markets, insurance and contractual savings, and small and medium-sized enterprise finance</p>	<p>\$100 million or 14% of CPS envelope of which:</p> <p>ESG: 0% GEM: 63% PSD: 100% RCI: 0%</p>

ADB = Asian Development Bank; CPS = country partnership strategy; ESG = environmentally sustainable growth; GDP = gross domestic product; GEM = gender equity and mainstreaming; kWh = kilowatt-hour; MSME = micro, small, and medium-sized enterprises; PEFA = public expenditure and financial accountability; PI-15 = effectiveness in collection of tax payments; PI-21 = effectiveness of internal audit; PSD = private sector development and private sector operations; RCI = regional integration.

Sources: ADB, Government of Georgia, International Monetary Fund, and World Bank.

LIST OF LINKED DOCUMENTS

<http://www.adb.org/Documents/CPS/?id=GEO-2014>

1. Economic Analysis (Summary)
2. Poverty Analysis (Summary)
3. Gender Analysis (Summary)
4. Environment Assessment (Summary)
5. Private Sector Assessment (Summary)
6. Sector Assessment (Summary): Transport
7. Sector Assessment (Summary): Water and Other Urban Infrastructure and Services
8. Sector Assessment (Summary): Energy
9. Sector Assessment (Summary): Public Sector Management
10. Sector Assessment (Summary): Finance
11. Risk Assessment and Risk Management Plan (Summary)
12. Country and Portfolio Indicators
13. Country Performance Assessment Ratings
14. Country Cost-Sharing Arrangements and Eligible Expenditure Financing Parameters
15. Country Partnership Strategy Formulation
16. Country Strategy Final Review
17. Country Operations Business Plan, 2015–2017
18. Validation Report of the Final Review of Country Operations, 2008–2012

Supplementary Documents

19. Socio-economic Development Strategy of Georgia (Georgia 2020)
20. Georgia Transport Sector Assessment, Strategy and Road Map