

SECTOR ASSESSMENT (SUMMARY): PUBLIC SECTOR MANAGEMENT¹

A. Sector Performance, Problems, and Opportunities

1. Public sector management has been improving owing to institutional reforms and capacity development undertaken by the government since 2004. Nonetheless, reforms are still needed to raise the efficiency of public resource utilization, reduce risks to macroeconomic stability, and stimulate economic growth and poverty reduction.

2. **Public financial management.** There have been significant improvements in recent years in public financial management (PFM). These include the introduction of a medium-term budget framework, program-based budgeting, a budget classification system based on the International Monetary Fund's *Government Finance Statistics Manual 2001*, and a rule-based system for fiscal transfers from the central government to local governments. In addition, a multi-currency Treasury single account, electronic budget management system (e-Budget), electronic treasury system (e-Treasury), and electronic government procurement system (Unified Electronic System of State Procurement) have been set up. The coverage of budget execution reports has been extended to include revenue and expenditure of legal entities of public law (LEPLs) under central government agencies.² The Debt Management and Financial Analysis System of the United Nations Conference on Trade and Development has been installed in the Ministry of Finance. The Law of Georgia on State Audit Office has been adopted and internal audit units have been established in line ministries. The State Audit Office of Georgia, which is the country's supreme audit institution, has introduced improved auditing standards and audit methodology. Legislative scrutiny of budget formulation has been strengthened. Accordingly, Georgia's score on most PFM performance indicators included in the World Bank's Public Expenditure and Financial Accountability assessment reports increased during 2008–2013.³

3. However, challenges remain, including weak public investment management, inadequate monitoring and analysis of government contingent liabilities, and weak capacity of the internal audit units of government agencies. Lack of assessment and monitoring of contingent liabilities exposes the government to various types of fiscal risks. Tax revenue redistribution and the resultant effect on intergovernmental transfers need fine-tuning for optimal results. Revenue and expenditure of LEPLs under local governments are not included in budget execution reports. Legislative scrutiny of external audit reports is generally weak.

4. **Macroeconomic management.** Macroeconomic management is generally sound. Despite large exogenous shocks, Georgia has maintained a reasonable degree of price stability since 2000, with inflation targeting adopted in 2009. The fiscal deficit narrowed from 9.2% of gross domestic product (GDP) in 2009 to 2.6% of GDP in 2013. Total public debt fell from 39.2% of GDP in 2010 to an estimated 33.9% of GDP in 2013, most of which is on concessional terms. Gross external debt (net of intercompany loans) rose from 44.3% of GDP in 2008 to 65.3% in 2013. The current account deficit exceeded 10% of GDP during 2005–2012, but narrowed to 5.9% of GDP in 2013.⁴

5. Nevertheless, the fiscal deficit in 2014 is still expected to be relatively large, given the low

¹ This summary is based on research done by Asian Development Bank staff and consultants.

² LEPLs are entities created under various government agencies to provide specific public services. They are allowed to charge fees for the services they provide and to retain the proceeds to finance their operations.

³ World Bank. 2013. *Georgia: Public Expenditure and Financial Accountability Assessment 2012*. Washington, DC.

⁴ International Monetary Fund Database. <http://www.imf.org/external/pubs/ft/weo/2014/01/weodata/weoseigr.aspx> (accessed 10 September 2014).

level of domestic savings, large current account deficit, and high level of external debt.⁵ The fiscal deficit is expected to widen in 2014 owing largely to a significant increase in social expenditure. To return to the path of fiscal consolidation, the government needs to keep social expenditure under control. To this end, it needs to introduce a contributory pension scheme to supplement the existing tax-financed universal pension system, and improve the coverage of the Targeted Social Assistance program. Furthermore, the National Bank of Georgia needs to improve its communication strategy and further strengthen its capacity for macroeconomic forecasting. More interagency coordination on public and external debt management is needed.

6. **Public administration.** Georgia has carried out major reforms of public administration since 2004. It drastically cut the number of government agencies and civil servants, and raised salaries of retained civil servants. As a result, public administration functions are more effective and efficient, though key regulatory bodies were adversely affected and the government is reintroducing some essential functions. Georgia's percentile rank on government effectiveness rose to nearly 70% in 2013 from 20% in 2002.⁶ Georgia has also made progress in introducing e-government. In particular, electronic identification, and a system for electronic filing of tax returns and tax appeals have been introduced. Nonetheless, Georgia can take further steps in developing e-government. The United Nations ranked Georgia 56th of 193 countries in its global E-Government Development Index in 2014.⁷

7. While amendments to the Constitution of Georgia in 2010 increased the independence of local governments, they lack capacity and financial resources needed to fulfill their responsibilities. Local development planning and expenditure management systems are largely absent. Civic engagement in local decision making is inadequate. Given that the central government makes decisions on most public investment projects, the needs of local communities may not be taken into account in project planning and implementation. Since 2012, the government has embarked on self-governance reform, beginning with adoption of a decentralization strategy in 2013, followed by parliamentary approval in February 2014 of the Local Self-Government Code. The code is an organic law of Georgia and a step forward for establishing an effective local governance system, including promotion of economic development. In consideration of the principles of decentralization, subsidization, and effective governance, and in compliance with the European Charter of Local Self-Government, the code establishes the proper legal basis for further development of local self-government in terms of territorial optimization of municipalities, functional strengthening of local self-government, and improvement of local public services. The new law clearly divides local competencies from central ones and it introduces higher standards in local self-government.

8. A concept approved by the Government of Georgia in 2014 will support an increase in the capabilities of municipalities. It stipulates the establishment of a flexible education network to promote development of human resources in local self-governing units. Municipalities will allocate 1% of their budget for capacity building of employees. A draft law of additional

⁵ Gross national savings declined from 22.9% of GDP in 2003 to 2.6% in 2009, before increasing to 19.4% of GDP in 2013 (footnote 4). Excluding net factor income and transfers from abroad, gross domestic savings is 12.3% of GDP in 2013. National Statistics Office of Georgia. <http://www.geostat.ge/> (accessed 4 November 2014).

⁶ The World Bank's Worldwide Governance Indicators measures the quality of public services, the quality of the civil service and the degree of its independence from political pressures, the quality of policy formulation and implementation, and the credibility of government commitment to such policies. The percentile rank on the Worldwide Governance Indicators is the proportion of countries that have a lower indicator score than the country concerned in the total number of countries for which the indicator is available. World Bank. Worldwide Governance Indicators. <http://info.worldbank.org/governance/wgi/index.aspx#reports> (accessed 18 October 2014).

⁷ United Nations. Public Administration Country Studies. E-Government Development Index. <http://unpan3.un.org/egovkb/en-us/Data-Center> (accessed 10 October 2014).

mechanisms on participation of citizens in local self-governance will be developed before 2015.

9. **Legal, regulatory, and institutional framework for doing business.** Since the mid-2000s, Georgia has significantly improved the legal, regulatory, and institutional framework for doing business. Its percentile rank on regulatory quality (which captures perceptions of the government's ability to formulate and implement sound policies and regulations that permit and promote private sector development) improved to 74% in 2013 from only 33% in 2005 (footnote 5). Its rank on the overall ease of doing business rose to eighth of 189 economies in the World Bank's *Doing Business 2014* report from 100th of 155 economies in the 2006 report.⁸

10. Weak protection and enforcement of property rights (including intellectual property rights), gaps in the legal and regulatory framework for public–private partnerships, weak mechanisms for resolution of commercial and tax disputes, difficulties in getting tax refunds, inadequate mechanism for resolving insolvency are challenges to Georgia's conducive business environment. In the *Global Competitiveness Report 2014–2015*, the World Economic Forum ranks Georgia low on the protection of property rights, efficiency of the legal framework in settling commercial disputes and challenging regulations, effectiveness of antimonopoly policy, and regulation of securities exchanges.⁹ In the *Doing Business 2014* report, Georgia is ranked relatively low (88th of 189 economies) on the ease of resolving insolvency (footnote 8).

11. **Judiciary.** One reason for the weak protection of property rights and the inefficiency of the system for settling commercial disputes in Georgia is the inefficiency in the judicial system and weak capacity of the courts. In the *Nations in Transit 2013* study, Freedom House ranked Georgia low on the judicial framework and independence.¹⁰ Similarly, the World Economic Forum ranked Georgia relatively low on judicial independence (footnote 9). The government recognizes this challenge and has taken steps to enhance judicial capacity and independence.

12. **Corruption.** Radical reform of public sector management and aggressive enforcement of anticorruption policies have largely eliminated petty corruption. Georgia's rank in the Transparency International's Corruption Perception Index 2013 rose to 55th of 177 countries from 79th of 180 countries in 2007.¹¹ Its percentile rank on control of corruption (which measures the extent to which public power is exercised for private gain as well as "capture" of the state by elites and private interests) improved to nearly 67% in 2013 from a low of 7% in 2002. Concerns about high-level corruption have remained; but the new government, which came to power in 2012, has made fighting high-level corruption a priority.

B. Government's Sector Strategy

13. The Socio-economic Development Strategy of Georgia (Georgia 2020),¹² which is the government's medium-term development strategy, identifies macroeconomic stability and effective public administration (defined broadly to include public financial management) as necessary conditions for inclusive economic growth. It calls for enhancement of government agencies' capacity for public policy management, strengthening of human resources management in the public sector, increased transparency of public policy management,

⁸ World Bank. 2013. *Doing Business 2014. Understanding Regulations for Small and Medium-Size Enterprises*. Washington DC.

⁹ World Economic Forum. 2014. *The Global Competitiveness Report 2014–2015: Full Data Edition*. Geneva.

¹⁰ The Freedom House. 2013. *Nations in Transit 2013: Authoritarian Aggression and the Pressures of Austerity*. Washington, DC.

¹¹ Transparency International. 2013. *Corruption Perceptions Index 2013*. Berlin.

¹² Government of Georgia. 2014. *Socio-economic Development Strategy of Georgia (Georgia 2020)*. Tbilisi.

development of e-government, greater efficiency of public financial management, and improved delivery of public services. To increase the efficiency and effectiveness of public expenditure, the government intends to improve the coverage and targeting of the Targeted Social Assistance program and strengthen public investment management. To increase domestic savings and improve access of the private sector to finance, the government plans to introduce contributory pension schemes and further reduce the fiscal deficit. With limited fiscal space, the government is developing public–private partnerships in infrastructure, and resolving issues on allocation of risk and managing government liabilities.

14. The government recognizes in Georgia 2020 that, despite the recent improvements, there are still serious deficiencies in the legal, regulatory, and institutional framework for doing business. To eliminate these deficiencies, the government intends to strengthen the protection of property rights, establish an efficient system for resolution of commercial disputes, streamline tax administration, and ensure greater transparency and stability of the tax legislation. In addition, the government plans to improve the investment legislation, the legal and institutional frameworks for competition and the development of capital markets, and the mechanisms for resolving insolvency and closing a business. The government attaches particular importance to increasing the independence of the judiciary and enhancing the capacity of courts to strengthen the protection of property rights, establishing an efficient system for resolution of commercial disputes, and creating a competitive business environment. In accordance with the European Union–Georgia Association Agreement and provisions for the Deep and Comprehensive Free Trade Area, the government plans to introduce best European practices in protecting intellectual property rights and promoting competition.

C. ADB Sector Experience and Assistance Program

15. Asian Development Bank (ADB) staff monitor and analyze developments in various areas of public sector management in Georgia, including macroeconomic management, public financial management, and public administration. This informs country economic work, such as the preparation of country chapters of Asian Development Outlook, and country performance assessments for performance-based allocation of ADB resources. Through the Municipal Services Development Project and the Municipal Services Development Project–Phase 2, ADB helped the Municipal Development Fund of Georgia and local governments enhance their capacity to implement public investment projects.¹³ By providing emergency assistance for post-conflict recovery, ADB helped the government mitigate adverse economic and social impacts of the 2008 armed conflict with the Russian Federation.¹⁴ ADB also conducted a country study on pensions and pension reform in 2011.¹⁵

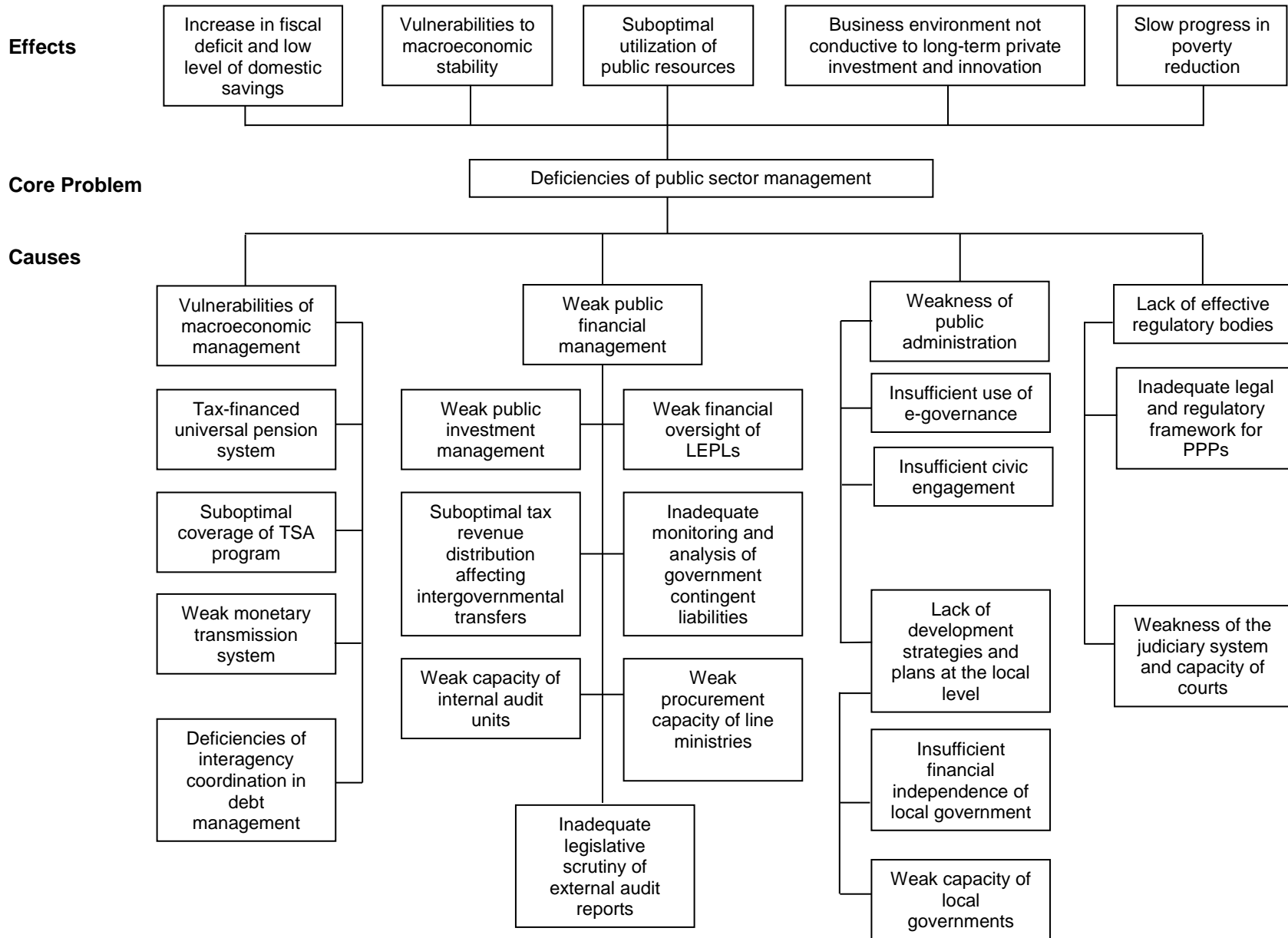
16. ADB is engaging with the government on a number of public sector management reforms that impact public and private resource mobilization and investment opportunities. Through programmatic policy-based lending, ADB will support the government in strengthening debt management and fiscal risk management, improving tax policy and administration efficiency, strengthening public expenditure management, enhancing domestic savings, and increasing private resource mobilization for investment. Technical assistance grants for policy advice and capacity development will also support the legal and institutional framework for a deeper capital market, savings, public–private partnerships, and debt management.

¹³ ADB. 2012. *Completion Report: Municipal Services Development Project in Georgia*. Manila; and ADB. 2013. *Completion Report: Municipal Services Development Project—Phase 2 in Georgia*. Manila.

¹⁴ ADB. 2010. *Completion Report: Emergency Assistance for Post-Conflict Recovery in Georgia*. Manila.

¹⁵ J. Gadbury and L. Schou-Zibell. 2011. Pensions and Pension Reform in Georgia. *ADB Central and West Asia Working Paper Series*. No. 1. Manila.

Problem Tree for Public Sector Management in Georgia



LEPLs = legal entities of public law, PPP = public-private partnership, TSA = targeted social assistance.

Sector Results Framework (Public Sector Management, 2014–2018)

Country Sector Outcomes		Country Sector Outputs		ADB Sector Operations	
Outcomes with ADB Contribution	Indicators with Targets and Baselines	Outputs with ADB Contribution	Indicators with Incremental Targets	Planned and Ongoing ADB Interventions	Main Outputs Expected from ADB Interventions
Increased fiscal consolidation and efficient utilization of public resources	<p>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>	Improved public sector management	<p>Government establishes a middle office function for upgraded debt management and risk analysis by 2016 (2013 baseline: none)</p> <p>Government adopts a medium-term public debt management framework by 2018 (2013 baseline: none)</p> <p>In phasing out the alternative audit program, the government increases the number of in-house auditors to at least 330 by 2016 (2013 baseline: 230)</p> <p>Government phases out the alternative audit program to improve revenue management by 2018</p> <p>Government design the structure of pension plan with defined contribution by 2015 (2013 baseline: none)</p> <p>Government launches an improved pension system with elements of mandatory contribution by 2018 (2013 baseline: none)</p>	<p>Planned key activity areas</p> <p>Improved management of debt, cash, and fiscal risk (25% of funds)</p> <p>Improved public financial management (35% of funds)</p> <p>Legal and regulatory framework for enhancing domestic savings and capital markets (40% of funds)</p> <p>Pipeline projects with estimated amounts</p> <p>Improving Domestic Resource Mobilization for Inclusive Growth Program, Subprograms 1, 2, and 3 (\$200 million)</p> <p>Development for Public–Private Partnerships (PATA, \$500,000)</p> <p>Development for Public–Private Partnerships 2 (PATA, \$500,000)</p> <p>Support for Operationalizing Country Knowledge Plan (S-PATA, \$100,000)</p> <p>Support for Knowledge Solutions (S-PATA, \$200,000)</p> <p>Ongoing projects with approved amounts</p> <p>Strengthening Domestic Resource Mobilization PATA (\$500,000)</p>	<p>Pipeline projects</p> <p>Debt management office upgraded and integrated with e-budget and e-treasury systems</p> <p>Tax administrative department established to improve tax collection efficiency</p> <p>Internal audit units created in high-spending ministries including education and infrastructure</p> <p>Regulations issued on mandatory occupational savings and voluntary savings</p> <p>Public–private partnership framework adopted to increase pipeline projects</p>

ADB = Asian Development Bank, GDP = gross domestic product, PATA = policy and advisory technical assistance, PEFA = public expenditure and financial accountability, S-PATA = small-scale policy and advisory technical assistance.
 Sources: ADB, Government of Georgia, and International Monetary Fund.