



*Delivering Progress*

# Implementing Structural Reforms

## The Experience of Georgia

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Vienna

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- General
- Challenges before reforming
- Economic Structure Overview
- Reforms
  - Fiscal Reforms- Tax Policy, Trade Policy, and Import Duties Administration
  - Business Enabling Environment (BEE) regulatory reform
  - Anti-Corruption reforms
- Current challenges, risks, and opportunities

# Georgia - Country overview

2015	
Area	69.7 km <sup>2</sup>
Population, million	3.7
Capital	Tbilisi (1.13 mln)
GDP, current US\$ billion	14
GDP per capita, current US\$	3754
GDP growth rate	2.6%
Exchange rate, end of the year	2.3949
Inflation, end of the year	4.90%
Poverty rate(\$2.5/day 2005PPP terms)	32.3
Poverty rate(\$5/day 2005PPP terms)	69.4
Gini Coefficient	40.1
Life Expectancy at birth, years	73.9



# Challenges of the Government of Georgia in 2003

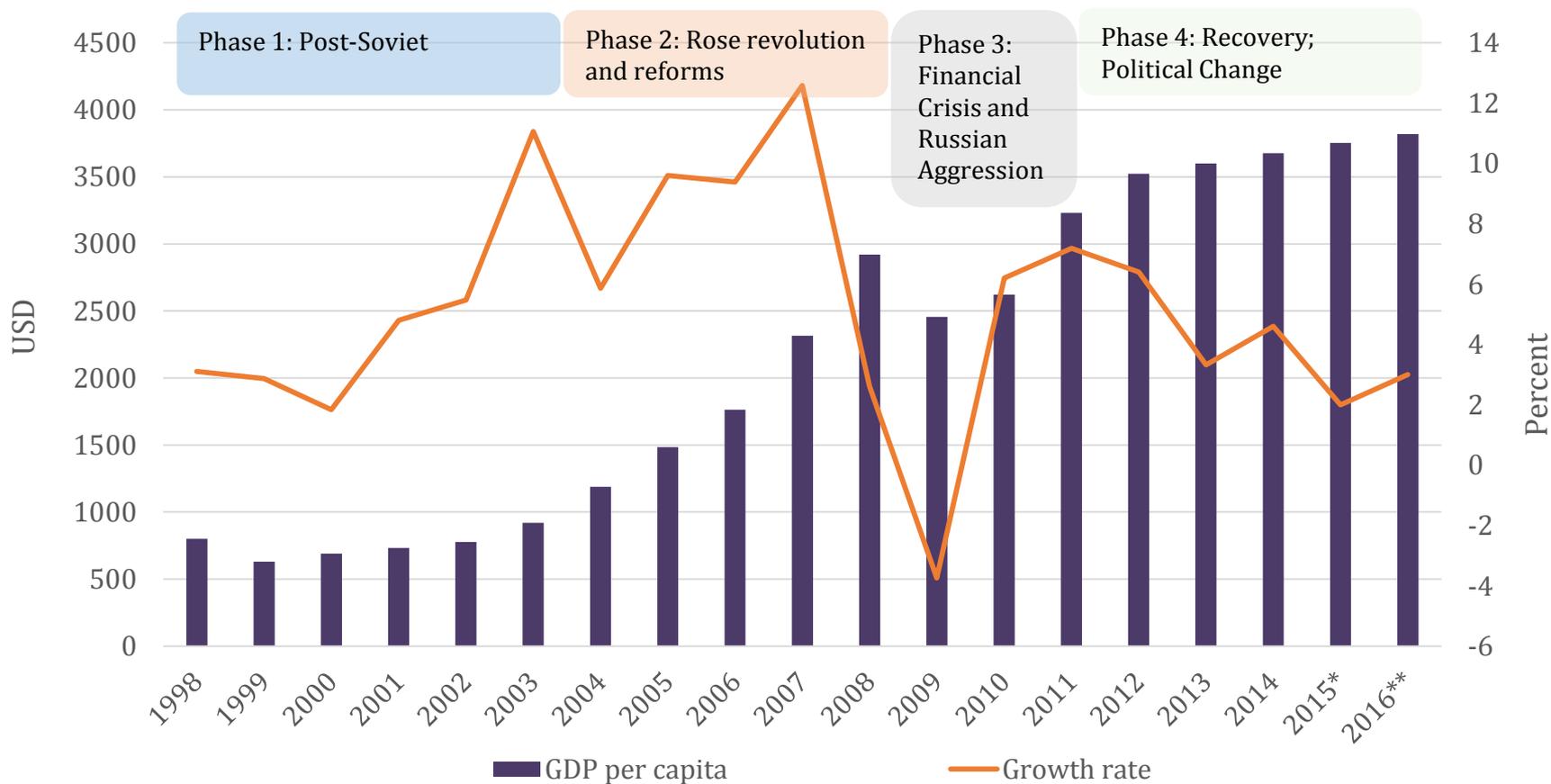
- State Default and Insolvency: Huge budget arrears, including in pensions, salaries, social spending, etc.
- Non efficient, non transparent budget and financial management system
- High level of corruption and corrupted system
- High number of government units and employees
- Not motivated, purely remunerated and badly managed government employees
- Duplicated functions between different government units
- Lack of transparency in the government and low level of public credibility
- High level of business regulation from government agencies
- Lack of communication and coordination

# Reforms in Georgia

- Property rights
- Liberal fiscal and trade regimes
- Improved budget policy
- Improved public services
- Structural Reforms
- Price liberalization
- Privatization
- Legal Framework
- Fighting corruption



# GDP per capita and real GDP growth



Source: National Statistics office of Georgia

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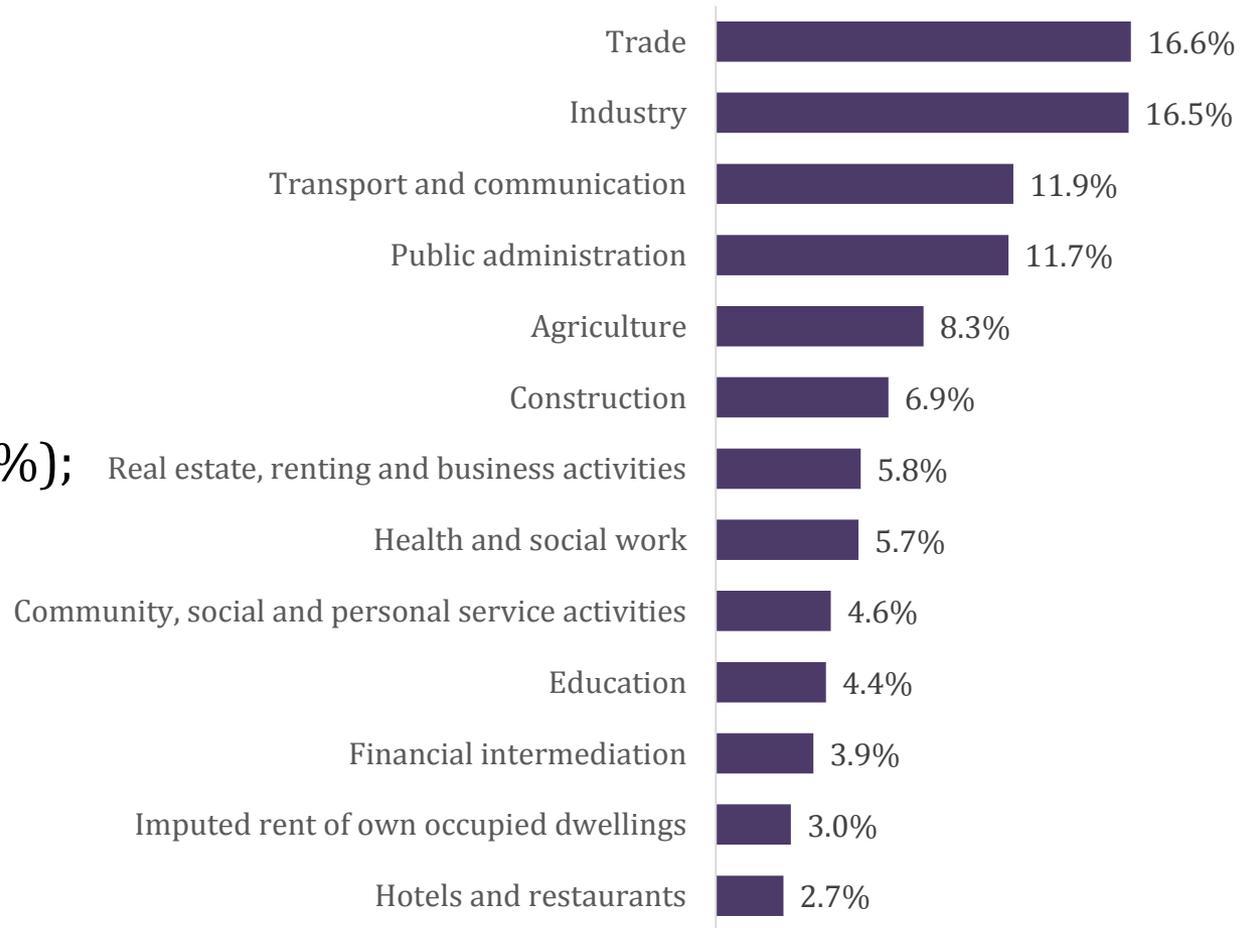
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# Structure of GDP (2015)

The main sectors, which contribute in GDP 2015 are:

- Trade (16.6%);
- Industry (16.5%);
- Transport & Communication (11.9%);
- Public Administration (11.7%);
- Agriculture (8.3%)



Source: National Statistics office of Georgia

# External Sector

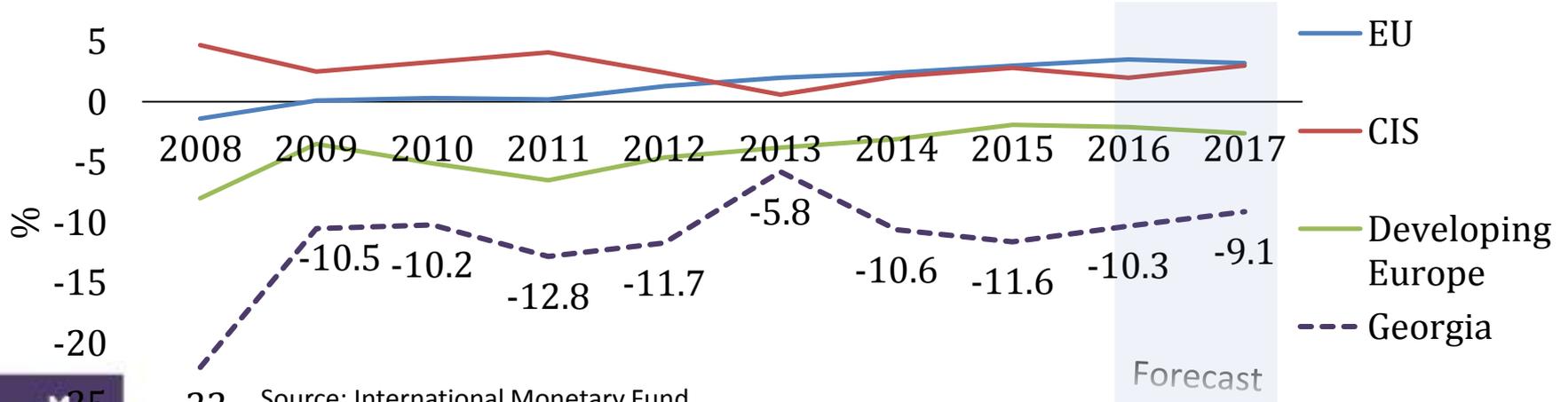
GEL/USD Real Exchange Rate



Exchange rate depreciated by 38.5% in 2014-2015

Source: National Bank of Georgia

Current Account, % GDP



Source: International Monetary Fund  
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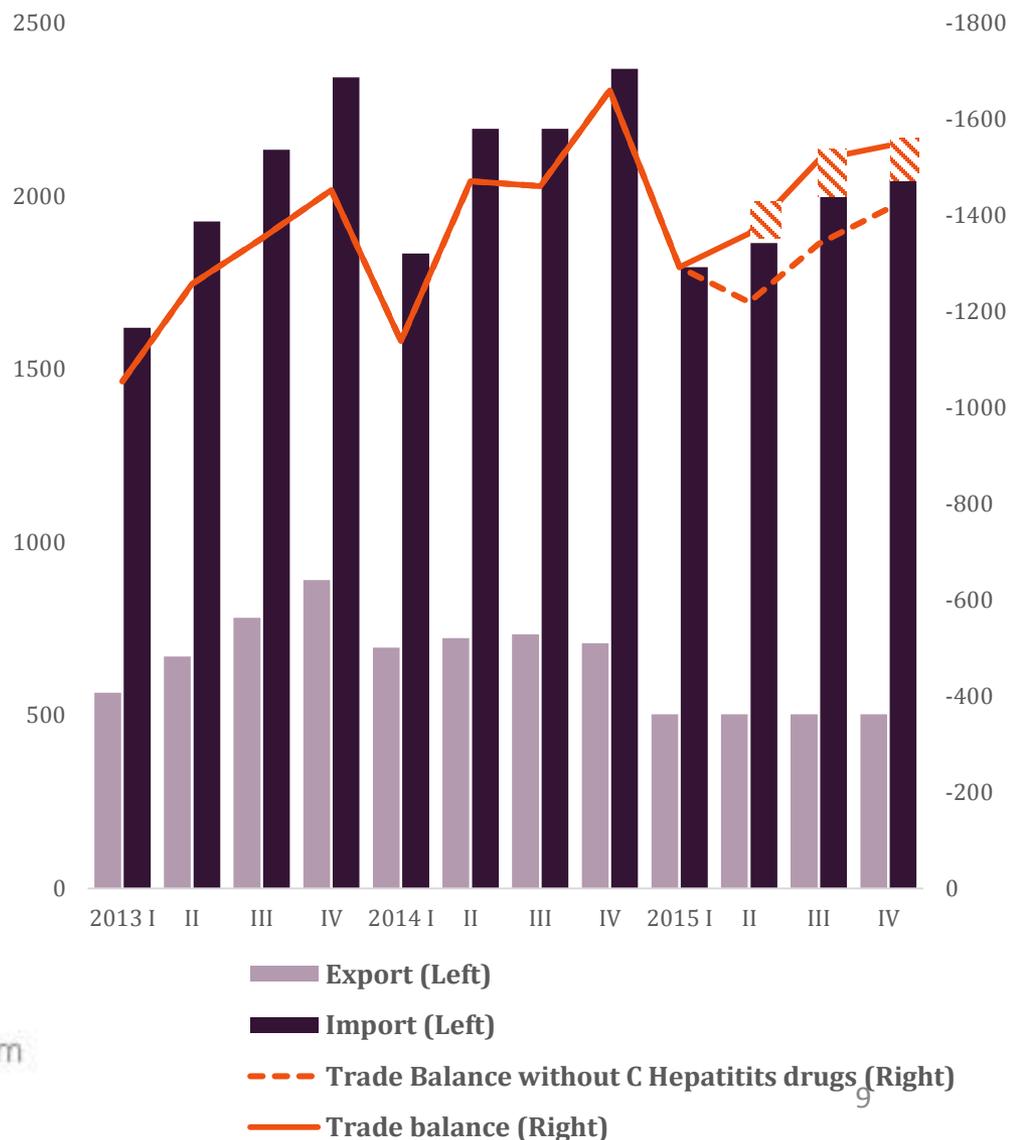
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# External Trade

- The value of export decreased (-22.9%) as well as decreased the value of import (-10.1%).
- Trade balance is negative (- \$5525 mln.USD).
- Top three trading partner countries by export are Azerbaijan (10.9%), Bulgaria (9.7%) and Turkey (8.5%).
- The highest share in export has copper ores (12.2%), Ferro-alloys (8.8%) and cars (8.1%)
- Top three trading partners by import in 2014 are Turkey (17.2%), Russia (8.0%) and China (7.6%)
- The major imported commodities are medicaments (9.6%), petroleum products (8.5%) and vehicles (6.1%).

Export, Import and Trade balance (mln \$), 2015



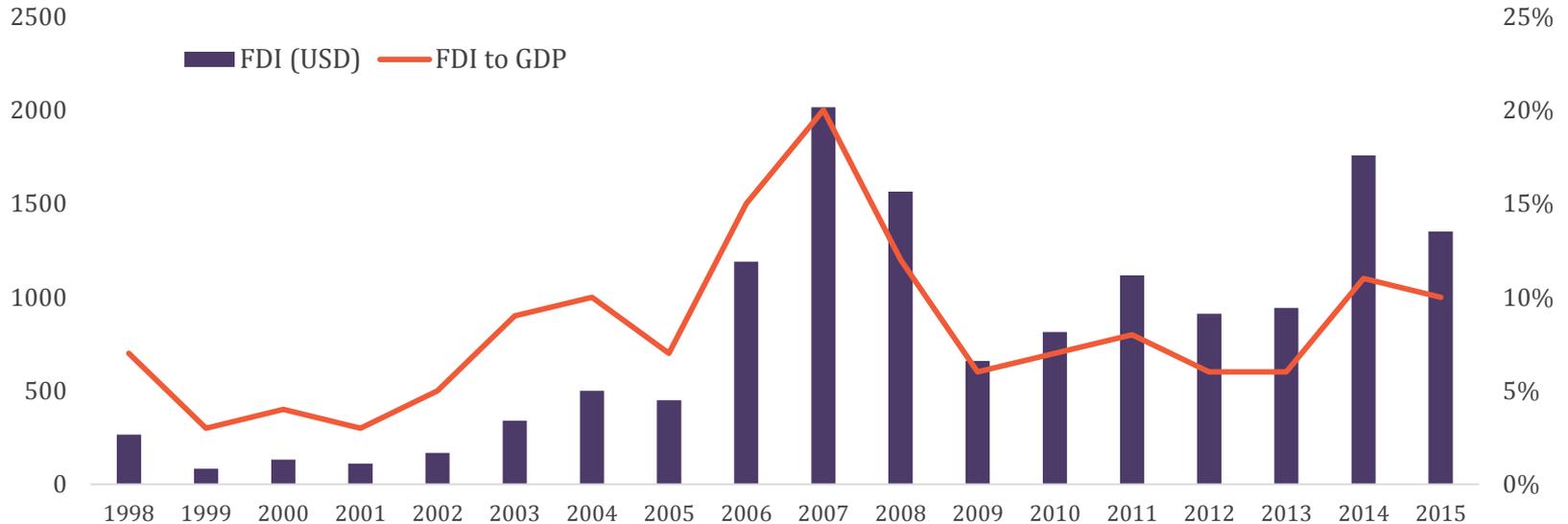
Source: National Statistics office of Georgia

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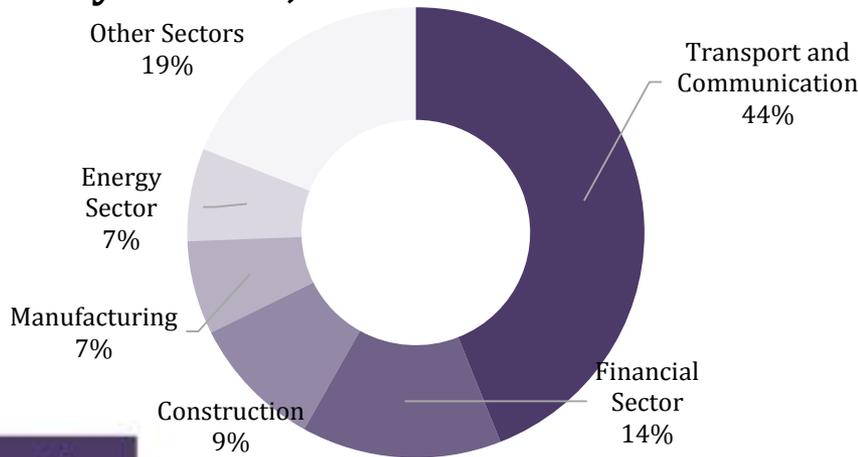
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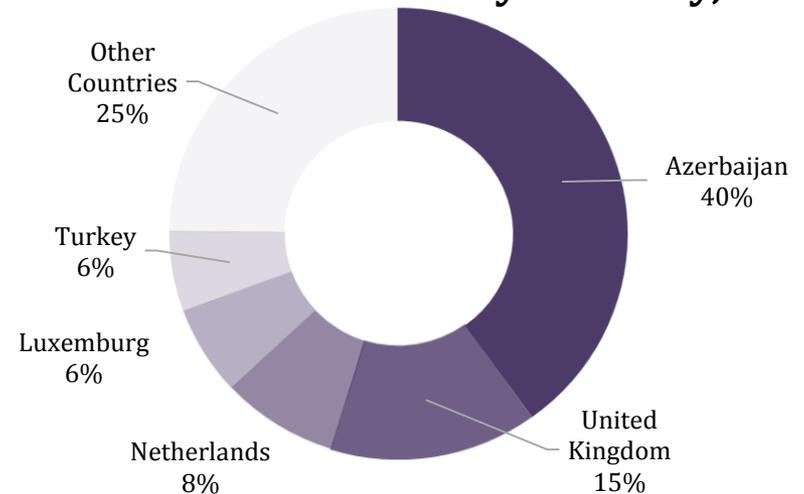
# Foreign Direct Investments



## FDI by sectors, 2015



## FDI by country, 2015



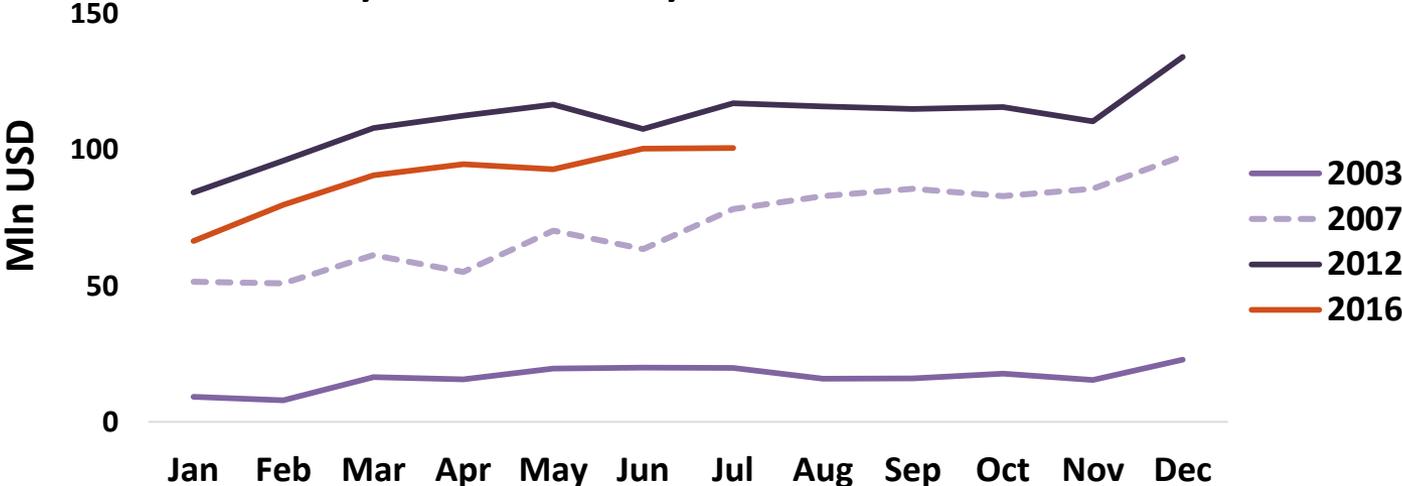
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Source: National Statistics office of Georgia

# External Sector cont.

The Dynamics of Money Transfers

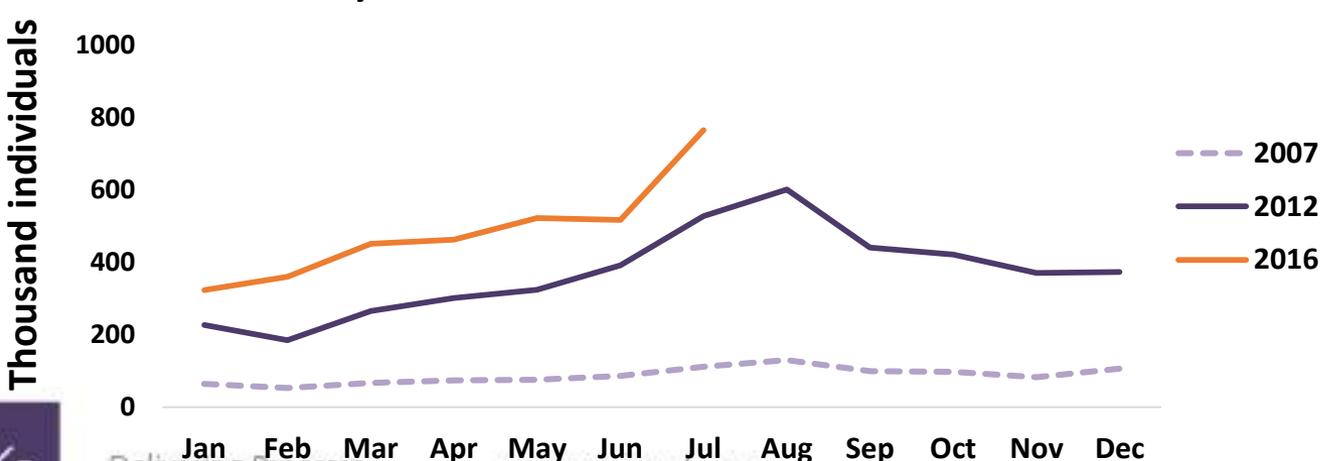


Top 5 transferor countries are:

- Russia
- Creek
- Italy
- USA
- Turkey

Source: National Bank of Georgia

The Dynamics of International Arrivals



Top 5 guest countries are:

- Armenia
- Azerbaijan
- Turkey
- Russia
- Ukraine

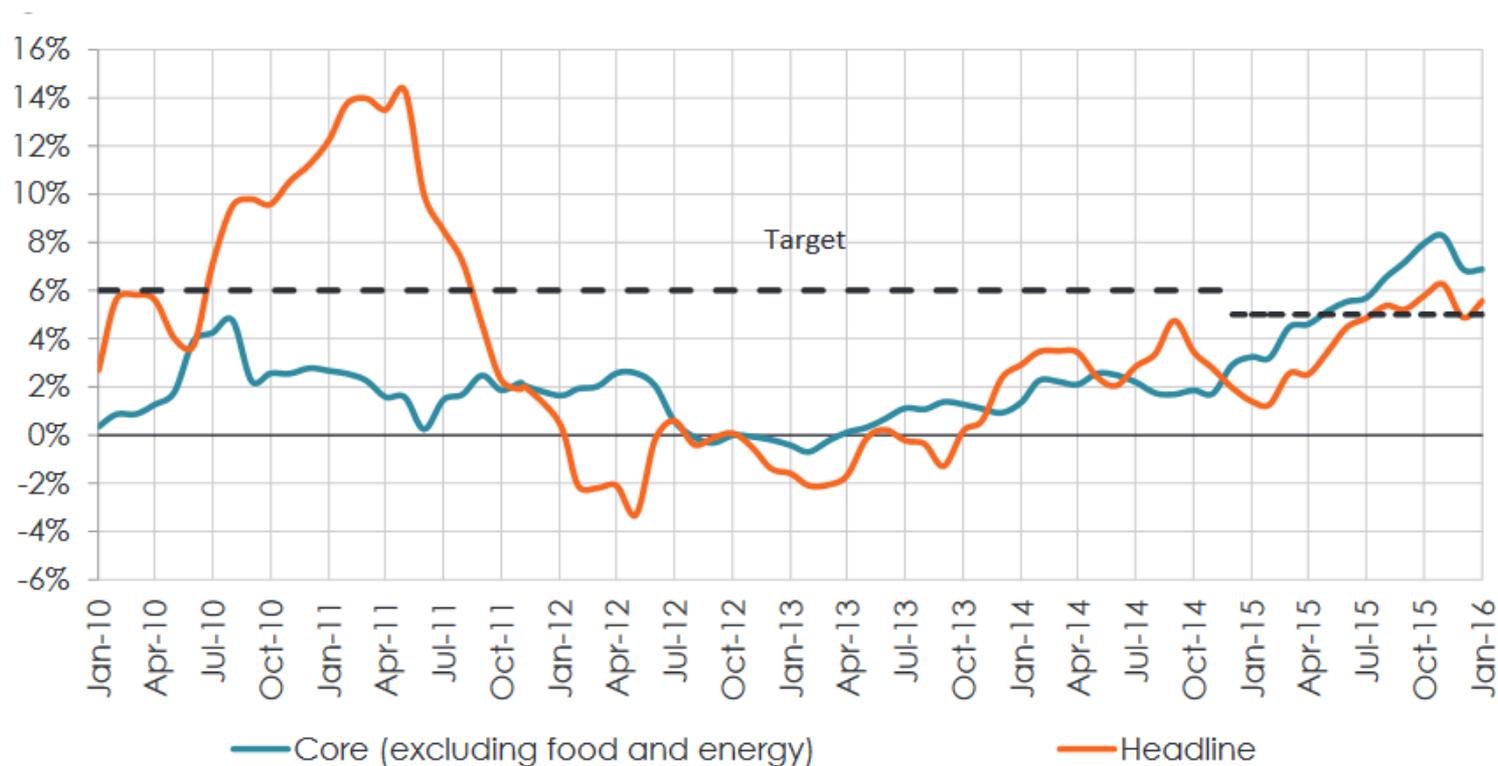
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Source: Georgian National Tourism Administration



# CPI and Core Inflation

- Import commodity price and exchange rate pressure on inflation



Source: National Bank of Georgia and Geostat

# Economic Activity Rate & Employment Statistics, 2015

- Labor force - 2 mln
- Unemployment in Georgia -12%

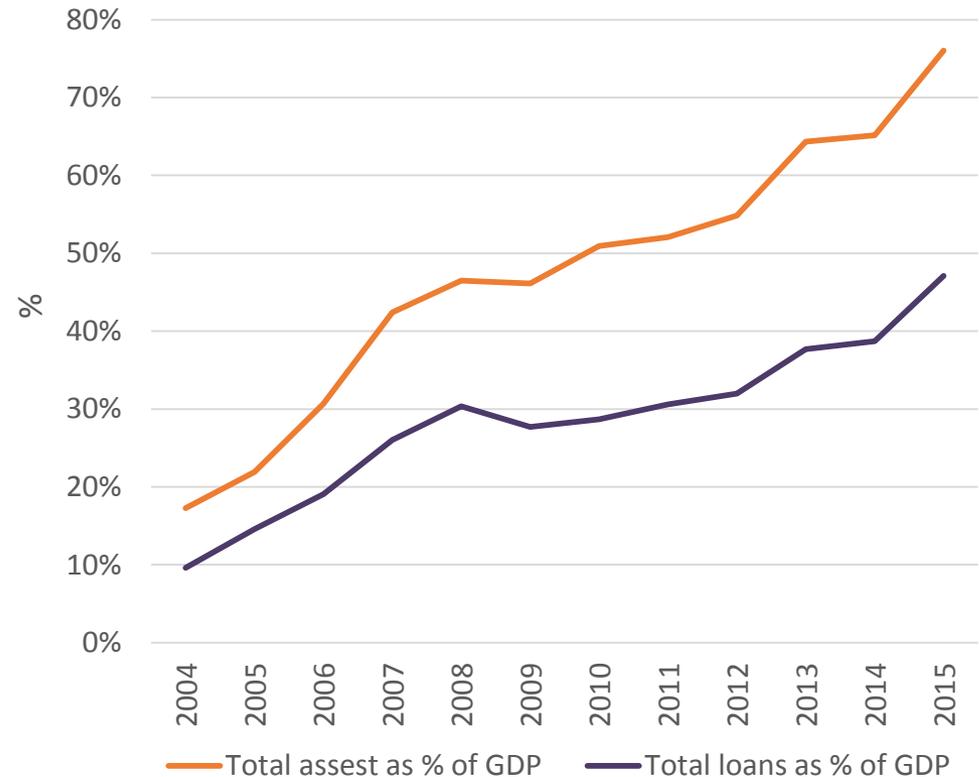
ILO definition: *6.5 working days in a year is counted as an employed (1 hour in a week);*

- 83% of self employed are peasants;
- 15% of hired employees are in public administration (in EU- 7%);
- According to survey (by Transparency International Georgia), 65% consider themselves unemployed (2016).
- Jobless growth!



# Financial Sector

- The banking sector is one of the most dynamic sectors of the economy;
- The financial sector is dominated by banks (more than 95% of assets);
- There are 19 commercial banks in Georgia;
- More than 80% of total banking sector capital is owned by international companies.

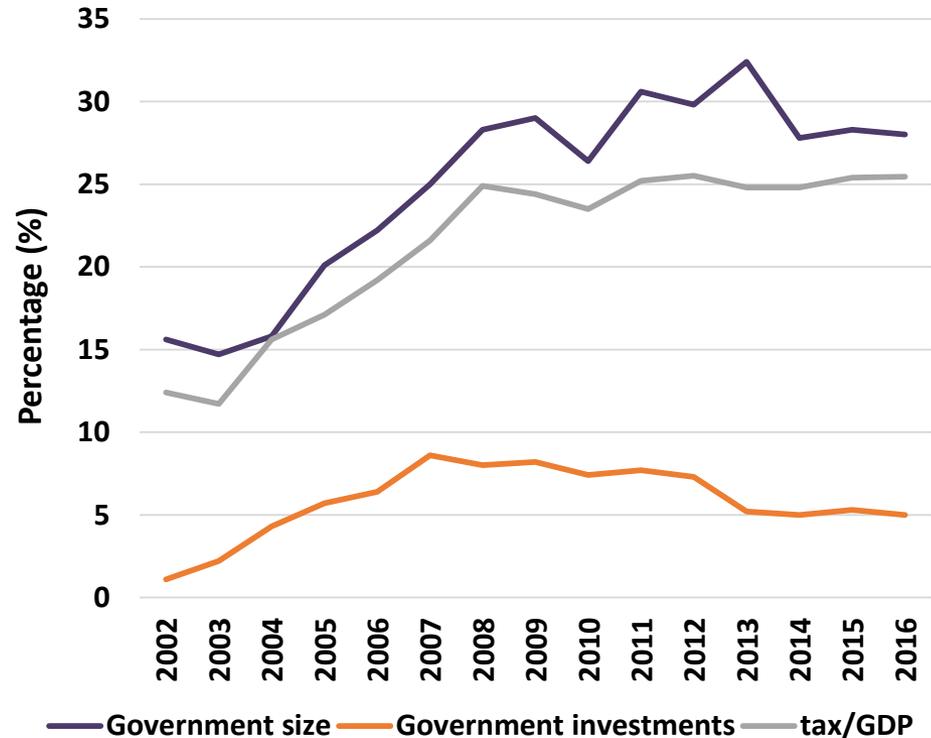


Source: National Statistics office of Georgia

# Budget/Fiscal Policy

- Based on stated policy, size of the government should not exceed 30% of GDP and is supposed to reduce to 25% for next years.
- Government Investment volume in government spending will be kept more then 5% of GDP (in a range of 6-8%)
- Introduction of the Medium Term Expenditure Framework (MTEF)
  - Better macroeconomic analysis
  - Allocation of the resources according to the priorities
  - Basic Data and Directions (BDD)
  - Defines the balance between current and capital expenditures in the medium term in order to ensure sustainable growth
  - Defines the size of government and allocations to government (25% range)

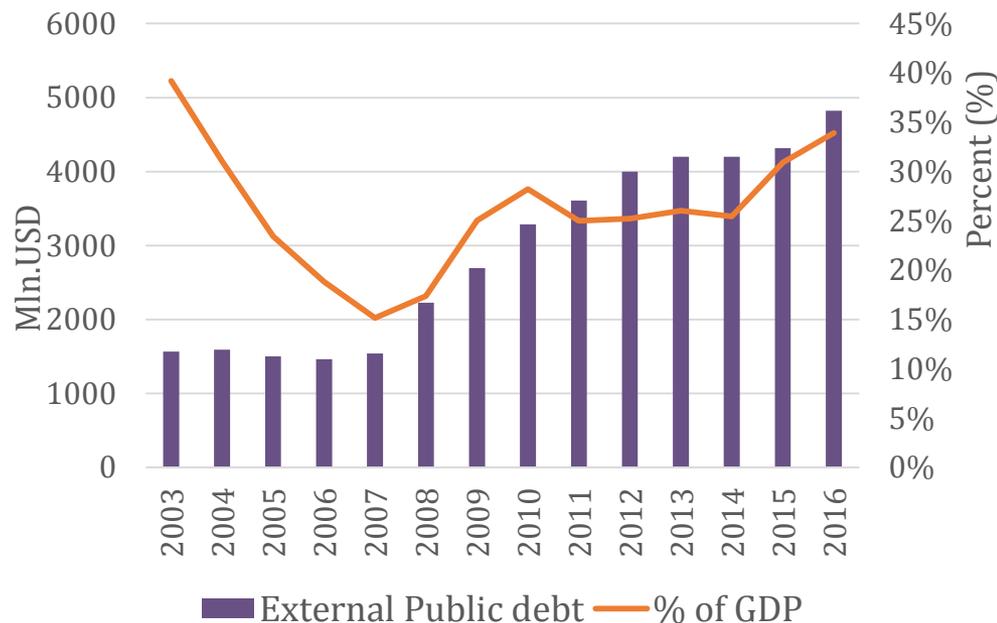
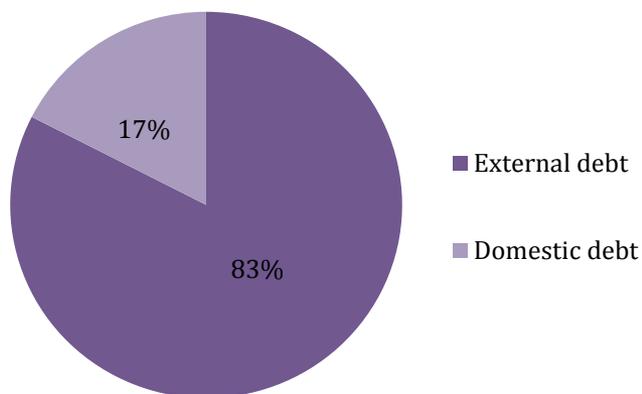
**Government size, government investment and tax burden**



Source: Ministry of Finance of Georgia

# External/Public Debt, 2015

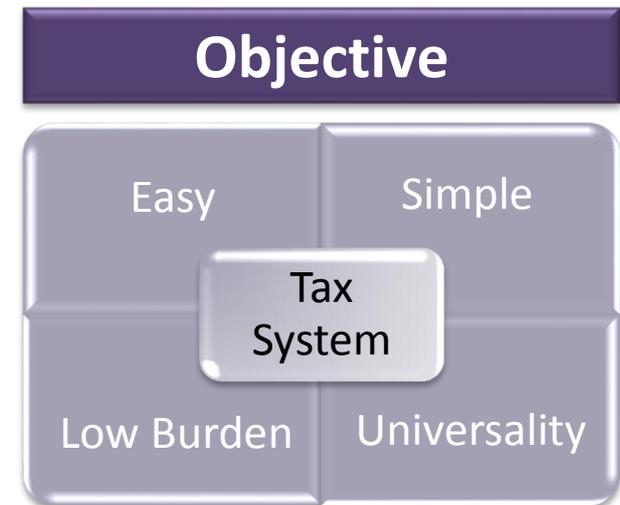
## Structure of public debt, 2015



- The coefficients of external debt as a % to GDP had decreasing pattern in 2003- 2007
- The coefficients of External Debt as a % to GDP increased in the period of 2008-2010
- In 2015, debt ratios to GDP increased to 33%
- External debt portfolio represents 83% of the total national debt

# Tax Reforms in Georgia

- Build Easy and Simple Tax System, with low rates
- Achieve trust of business to Government
- Easy and simple new tax code
- Law on tax type of amnesty
- Low tax rates - only six taxes at low rates (Income Tax, Profit Tax, VAT, Excise Tax, Customs Duty and Property Tax)
- Improving the Filling and Payment Procedures:
  - Easy Filling – e-filling
  - Easy procedures – e-procedures
- Improving the Control and Administration
- Corruption free
- Appeals Board – Under Ministry of Finance



# Tax Reforms in Georgia

Type of Tax	<2005	2002/2006	2007	2008	2009	2010-2016
Income Tax	Diff. 0%, 12%, 17%, 20%	12%	12%	25%	20%	20%
Social Tax, paid by employer	31%	20%	20%	-	-	-
Social Tax, paid by employee	2%	-	-	-	-	-
Profit Tax	20%	20%	20%	15%	15%	15%*
Dividends	10%	10%	10%	10%	5%	5%
Interests	10%	10%	10%	10%	7.5%	5%
VAT	20%	18%	18%	18%	18%	18%
Export	0%	0%	0%	0%	0%	0%
Excise	Differentiated**					
Property Tax for Enterprises, other than land	1%	1%	1%	1%	1%	1%
Customs Duties	Differentiated 0-30%, average weighted 7.6		Differentiated 0%, 5%, & 12%. Average Weighted 1.5***			

\* From profit tax to distributed profit tax- retained profit tax becomes 0% from 2017

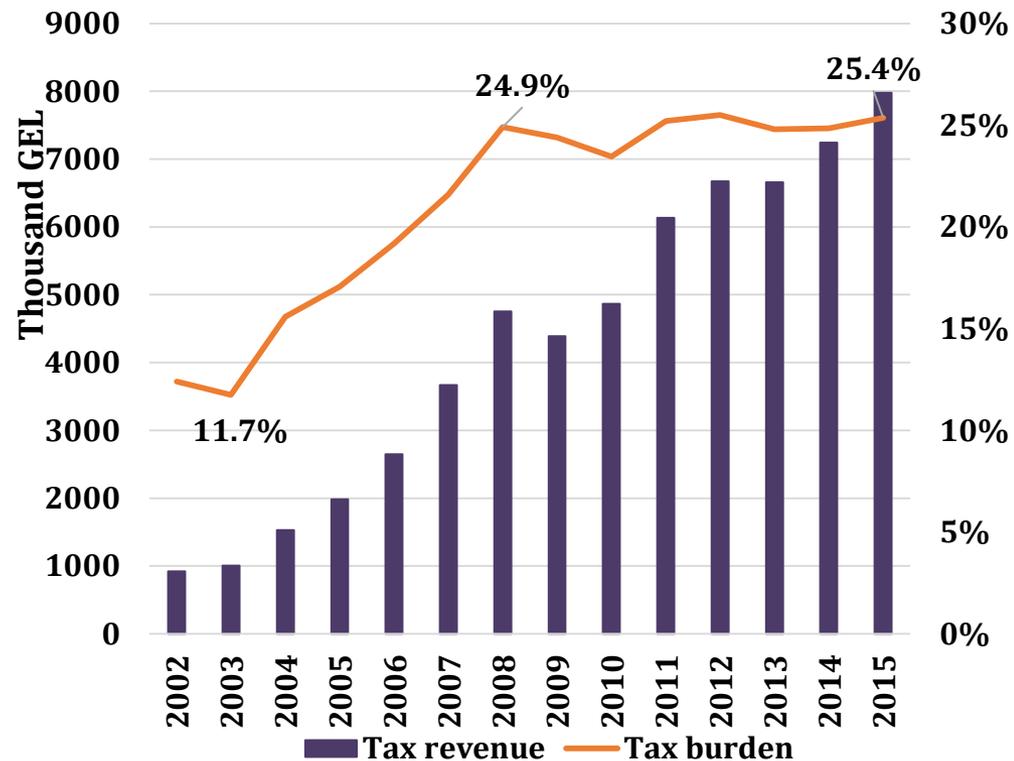
\*\* Excise tax for tobacco and alcohol has increased in January 2015

\*\*\* Imported capital goods VAT will be nullified from 2017

# Tax Reforms and Tax Revenues

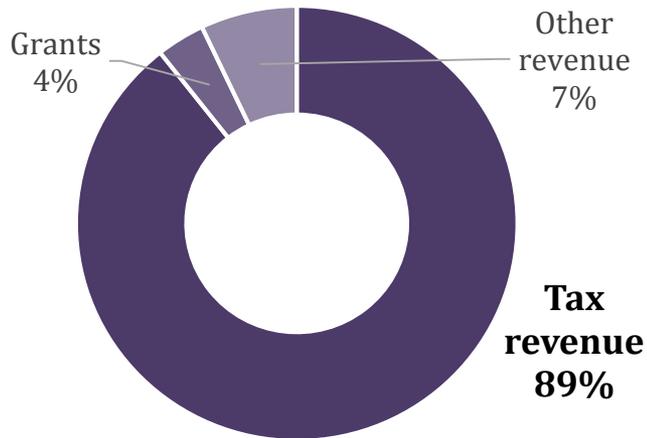
- The Reforms:
  - Only six taxes at low rates
  - Easy e-filing and e-procedures
  - Tax Appeal Board
- The Outcomes:
  - Corruption free environment
  - Significant improvement in tax control and administration since 2004
  - The ratio of tax revenues to GDP increased from 12% in 2003 to 25.4% in 2015;
  - Tax Revenue - the major source of revenue, 89% of total revenue (2015)
  - Informal Economy has been reduced from around 65 % to 10% of GDP

## Tax Revenues & Tax burden

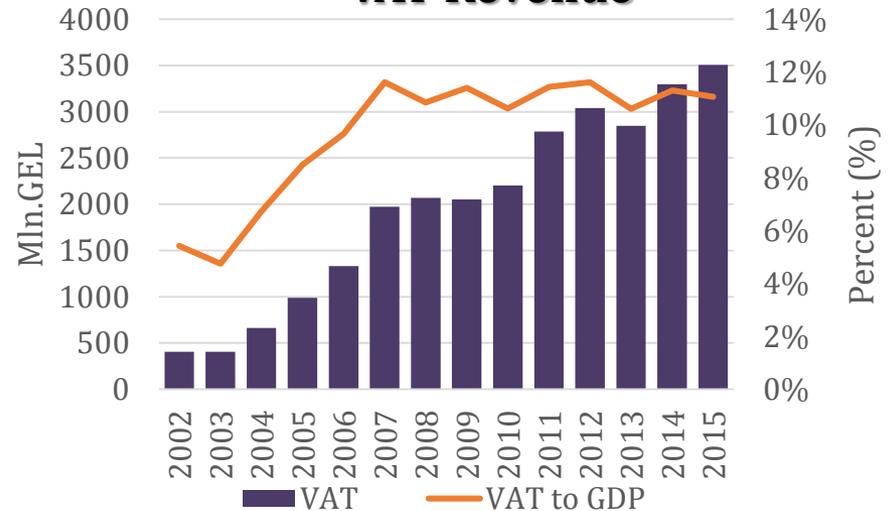


# Structure of Budget and Tax Revenues

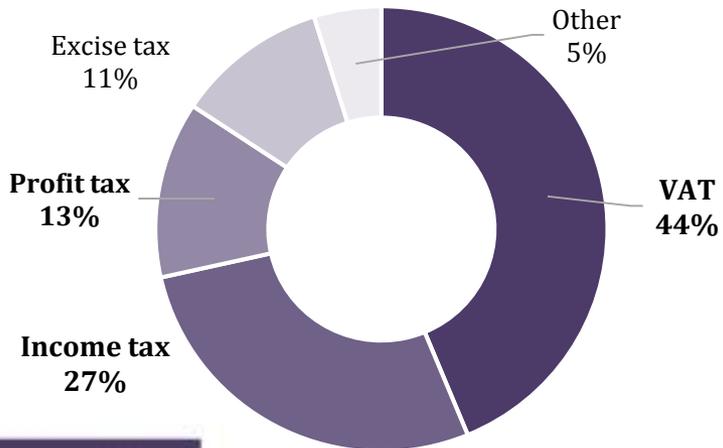
## Structure of the Budget, 2015



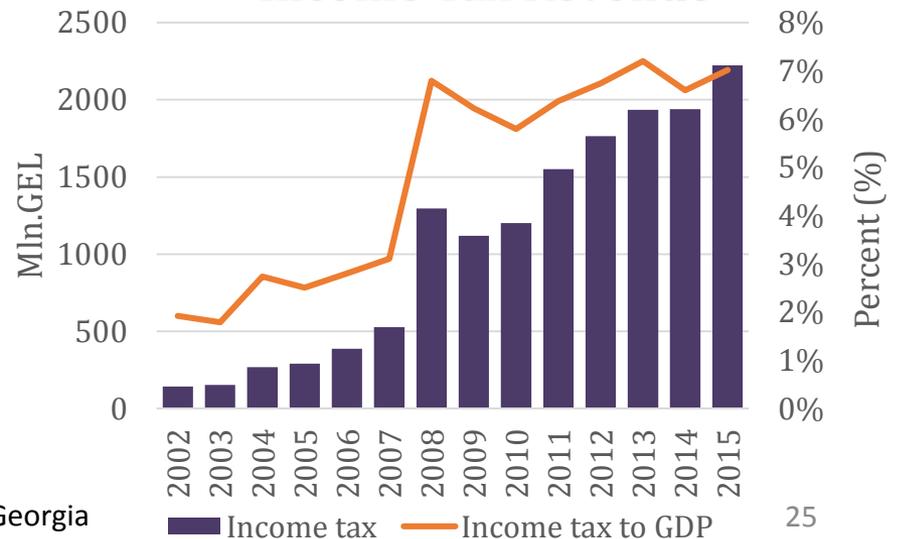
## VAT Revenue



## Structure of Tax Revenue, 2015



## Income Tax Revenue



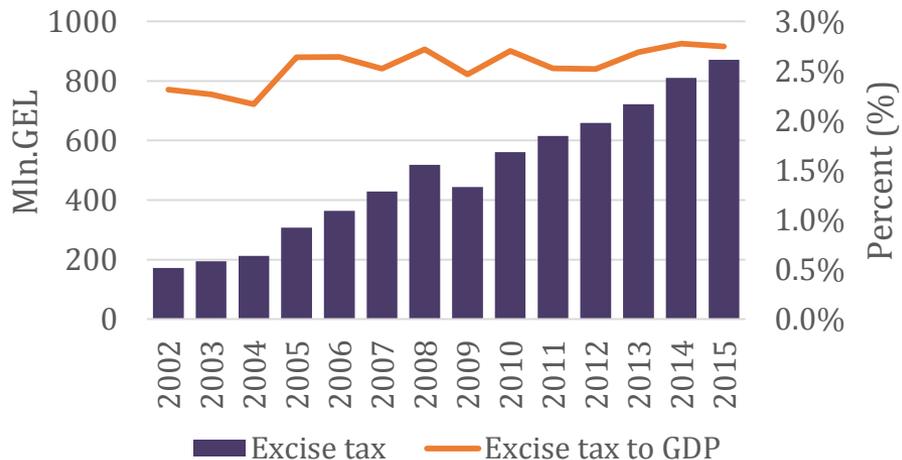
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Source: Ministry of Finance of Georgia

# Tax Revenues

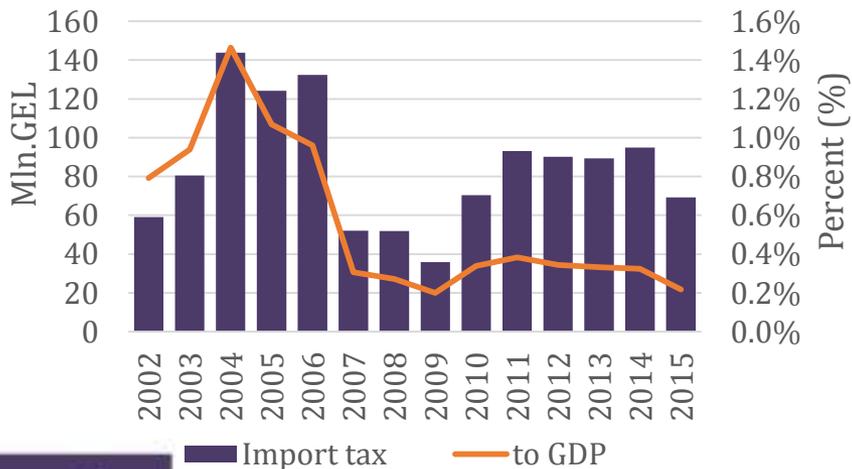
## Revenue from Excise Tax



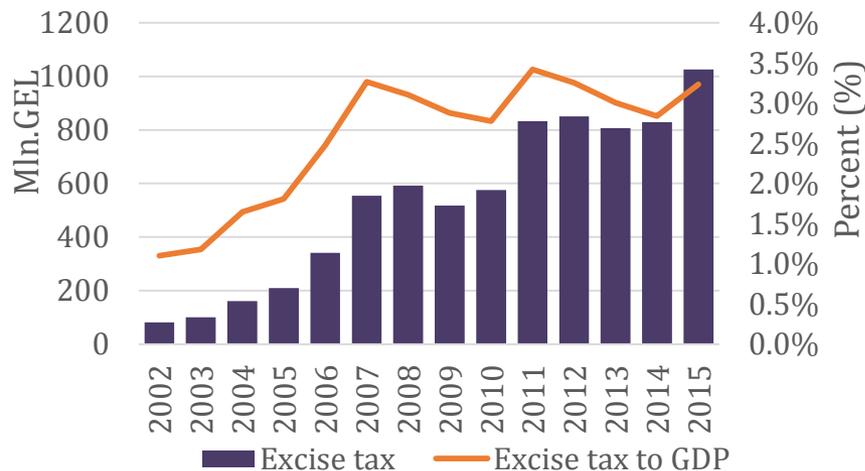
## Revenue from Profit Tax



## Revenue from Import Tax



## Revenue from Property Tax



# Customs & Trade Policy

## Challenges before reform:

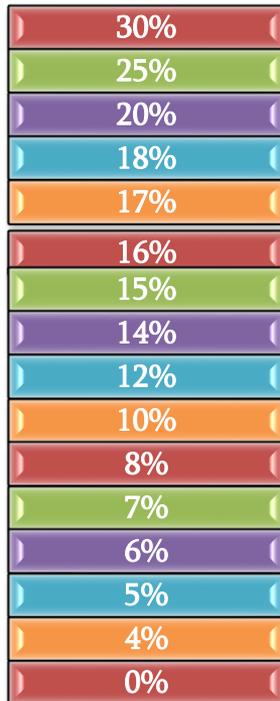
- Customs Code had a lot of ambiguous definitions
- Customs tariffs and procedures were scattered in many laws and sub-legislative acts
- Customs procedures were specified by more than 100 acts
- Customs offences were regulated according to the Code of Administrative Offences
- Customs legislation was not harmonized with international law

## Reforms:

- Improving the legal framework
- Simplify customs procedures
- Optimize customs duties
- Increase budget revenues
- Minimize corruption
- Preparation of the new and retraining of the old staff
- Attract additional transit
- Create a comfortable environment for tourists and importers

# New Duties

*Before 2007*



❖ One of the most liberal import duty systems in the world, with an average weighted import duty rate of 1.5%

❖ 90% of all imports have 0% duty

❖ Import duties on agricultural goods and construction materials

❖ Equal excise tax on imported and local goods

❖ No export and re-export duties

FTAs with : EU (DCFTA) 28 countries

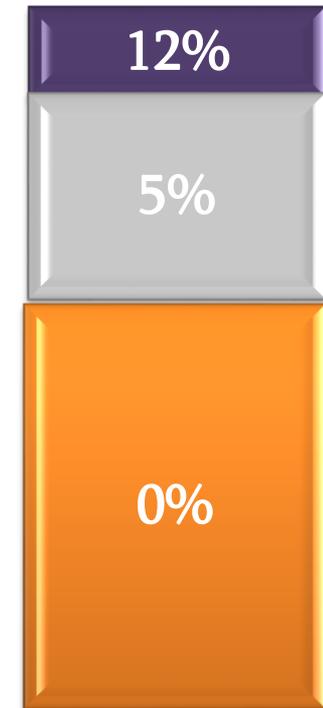
CIS - 8 countries

Turkey

GUAM (Georgia, Ukraine, Azerbaijan, Moldova)

Perspective to CHINA-Georgia FTA in 2016

*After 2007*



# Improving not only the Policy but ...

	DB 2006	DB 2007	DB 2008	DB 2009	DB 2010	DB 2015	gains
<b>Overall Rank</b>	<b>149</b>	<b>95</b>	<b>64</b>	<b>81</b>	<b>30</b>	<b>33</b>	<b>+116</b>
Documents to Export	9	8	8	8	4	4	-5
Time to Export	54	13	12	12	10	9	-45
Cost to Export	-	1370	1105	1380	1270	1355	-
Documents to Import	15	11	7	7	4	4	-11
Time to Import	52	15	14	14	13	10	-42
Cost to Import	-	1370	1105	1340	1250	1595	-

# For BEE 2003-2016

- eliminated the requirement for minimum capital, abolished the company seal and the company charter, made the use of notaries optional, and developed an online business registry
- the private credit bureau in Georgia now distributes full information,
- the corporate income tax rate was reduced and the social tax has been abolished.
- simplified process of obtaining confirmation from utilities, risk-based process of approval for building permits, and new time-limits for the occupancy certificate stage.
- implementing a central collateral registry with an electronic database accessible online
- streamlining the procedures for public auctions, introducing private enforcement officers and modernizing its dispute resolution system.
- streamlining the regulation of auction sales.
- broadening the range of assets that can be used as collateral
- simplifying the reporting for value added tax and introducing electronic filing and payment of taxes.
- allowing a security interest to extend to the products, proceeds and replacement of collateral, to secured transactions system
- creating customs clearance zones
- simplifying and speeding up the proceedings for commercial disputes
- establishing or tightening time limits for all insolvency-related procedures, including auctions
- implementing a new law on personal data protection
- Canceling the profit tax on retained profit (from 2017)

# Progress Displayed in DBI in Georgia

Starting Business takes 2 days and costs 3.5% of income per capita.

Dealing with Construction Permits takes 73.5 days and 14.9% of per capita income

Getting Electricity takes 71 days and costs 515% of per capita income

Registering Property takes 2 days and is free

Getting Credit is well-organized as there exists comprehensive database for creditworthiness

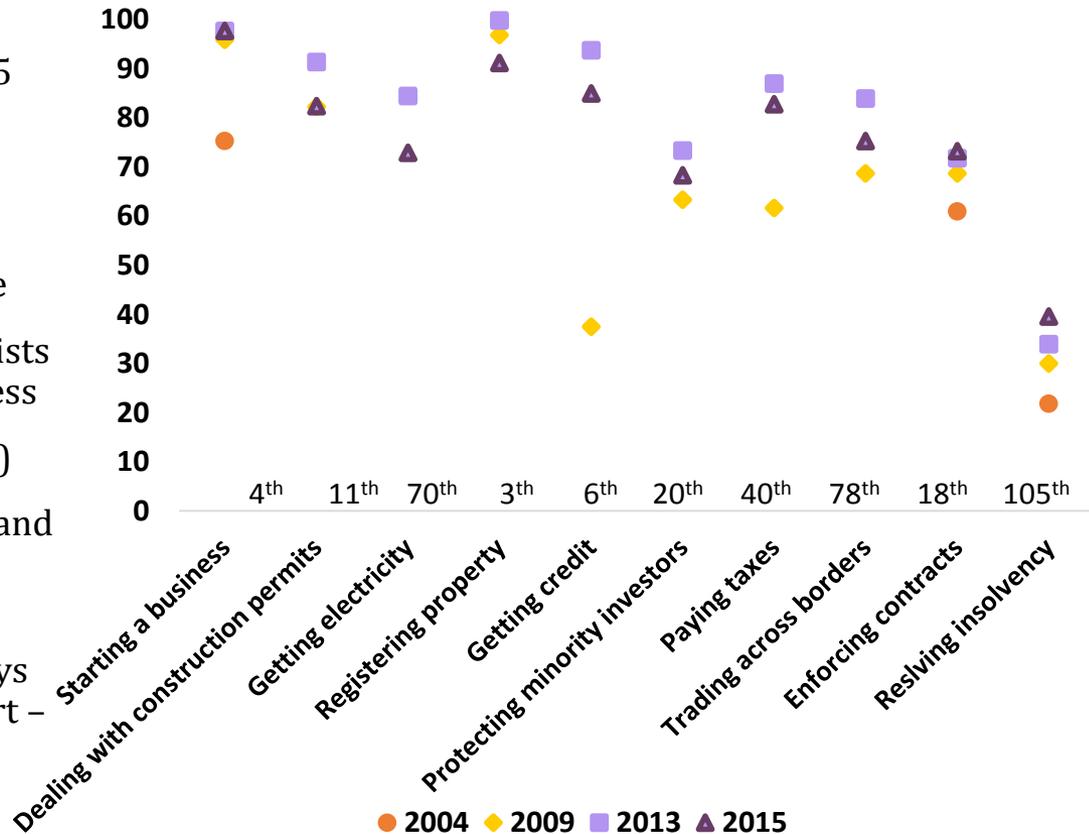
Protection of Investors is strong (7 out of 10)

Paying Taxes requires 5 payments per year and takes 16.4% of profit (*will be changed from 2017*)

Trading Across Borders to export takes 9 days and costs 1,355 USD per container, to import – 10 days and 1,595 USD.

Enforcing Contracts requires 29.9% of the claim and takes 285 days

Resolving Insolvency takes 2 years and costs 10% of the estate



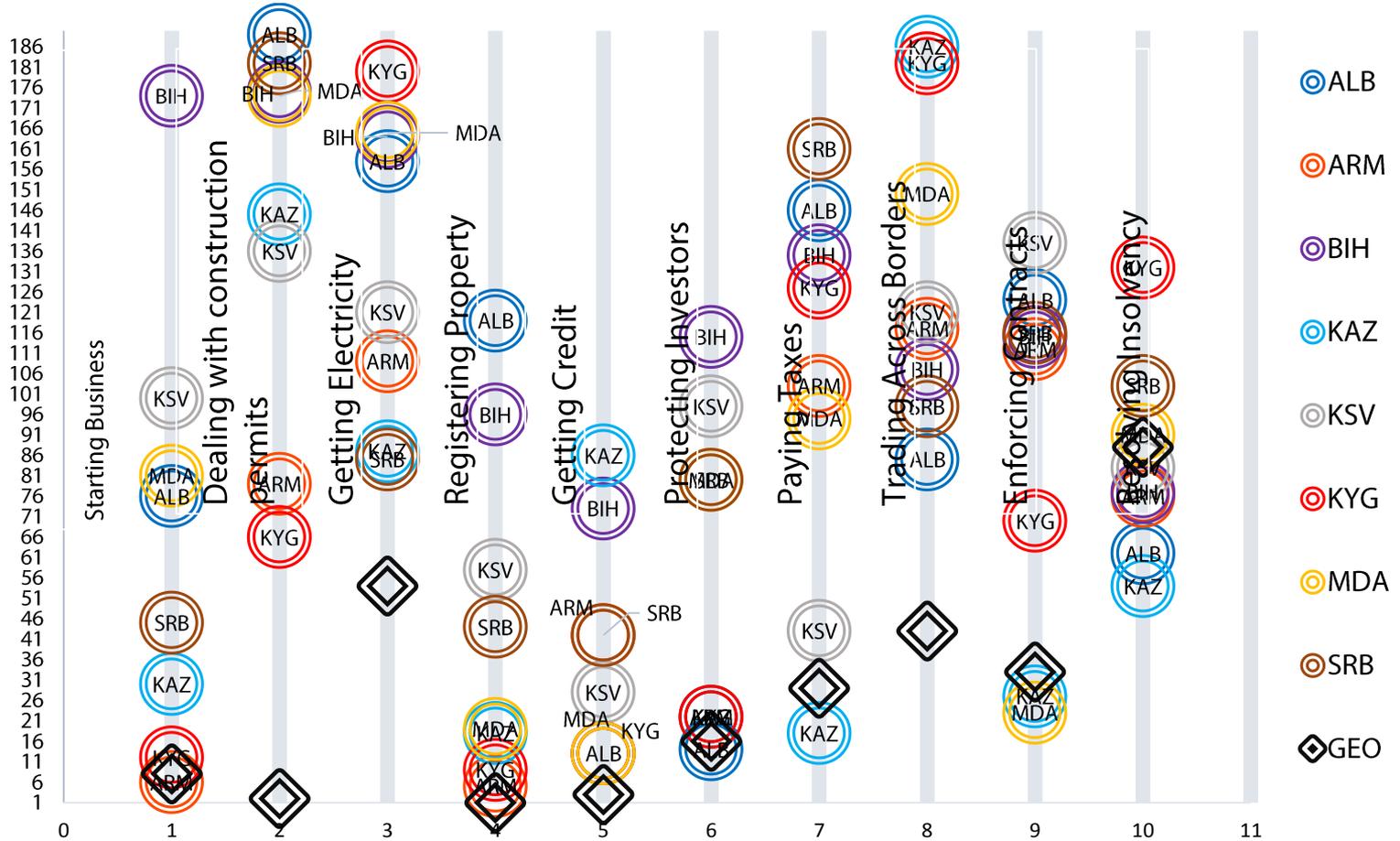
Source: The World Bank Doing Business Report



# Business Regulatory Reform and Economic Reforms

DB Rank 2016	GNI Per Capita (WB 2014)	Corruption Perception Index (2014)	WB Governance Indicators	
			Govt Effectiveness	Political Stability
1-25	\$38,799	22	89	77
26-50	\$23,381	55	73	61
51-75	\$15,802	71	59	46
76-100	\$11,739	90	50	56
101-125	\$8,179	87	45	44
126-150	\$2,560	116	29	36
151-189	\$2,672	137	14	22

# Gaps of Comparators



Source: The World Bank doing business report

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# Corruption-Free Environment

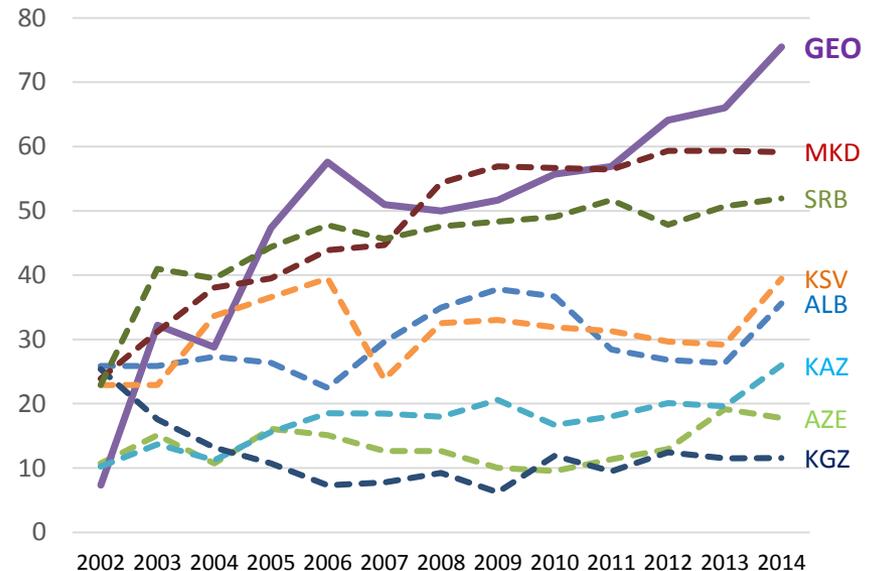
## Reform:

- ❖ Number one impediment to reforms - Bureaucracy
  - De-bureaucratization
  - Restructurization of each ministry
  - Staff reorganization
  - Separating policy elaboration and implementation
- ❖ The government has also pursued reforms to proactively release more public data online and has improved the responsiveness to Freedom of Information requests.

## Result:

- ❖ Georgia now satisfies the Millennium Challenge Corporation's indicator regarding "Control of Corruption" and scores above its peer group.
- ❖ The percentage of firms that identified corruption as a significant obstacle fell from 60% to 39% from 2002 to 2005.
- ❖ 52th place (out of 168 countries) in the ranking of Transparency International's Corruption Perception Index, 2015

CONTROL OF CORRUPTION PERCENTILE RANK (100=GOOD GOVERNANCE, 0=BAD GOVERNANCE)



Reflects perceptions of the extent to which public power is exercised for private gain, including both petty and grand forms of corruption, as well as "capture" of the state by elites and private interests.

Source: Worldwide Governance Indicators, 2013 Update, World Bank Database

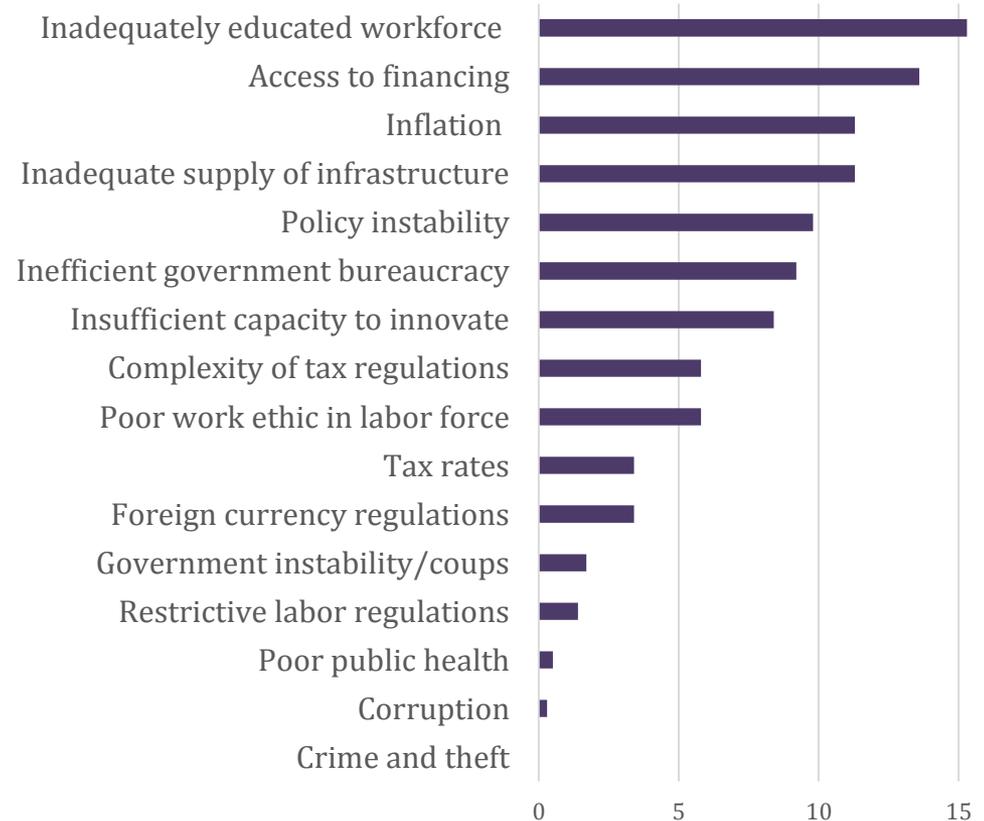
# Georgia in International Rankings

- BB-/BB-/BB – Standard and Poors, 2015
- 80th place (out of 142 countries) in the Legatum Prosperity Index, 2015
- 52th place (out of 177 countries) in the ranking of Transparency International's Corruption Perception Index, 2015
- 69th place (out of 144 countries) in the ranking in the Global Competitiveness Index of the World Economic Forum, 2014-2015
- 24th place (out of 189 countries) in the ranking of World Bank's ease of Doing Business, 2015
- 22st place (out of 178 countries) in the ranking of Heritage Foundation's Economic Freedom Index, 2015

# Current Challenges

- ❖ Property rights
- ❖ Rule of Law and Legal System
- ❖ Political Stability
- ❖ Unemployment
- ❖ Social Vulnerability
- ❖ High Trade Deficit
- ❖ Foreign Direct Investment
- ❖ External Debt

The most problematic factors for doing business



Note: From the list of factors above, respondents were asked to select the five most problematic for doing business in their country and to rank them between 1 (most problematic) and 5. The bars in the figure show the responses weighted according to their rankings.  
Source: Global Competitiveness Report 2015-16 (Executive Opinion Survey), World Economic Forum)

## Fiscal Risk

- Reluctant to budget adjustment
- Increasing in spending, especially in bureaucracy (manipulating by employment numbers)
- Fiscal sustainability. Elections and political pressure in 2016 will not allow reducing in deficit
- Consolidation of public finances : LEPL, SOEs, Partnership fund, etc.
- Quality and efficiency of spending: Investments, Social, Sectorial, etc.
- Transparency and accountability

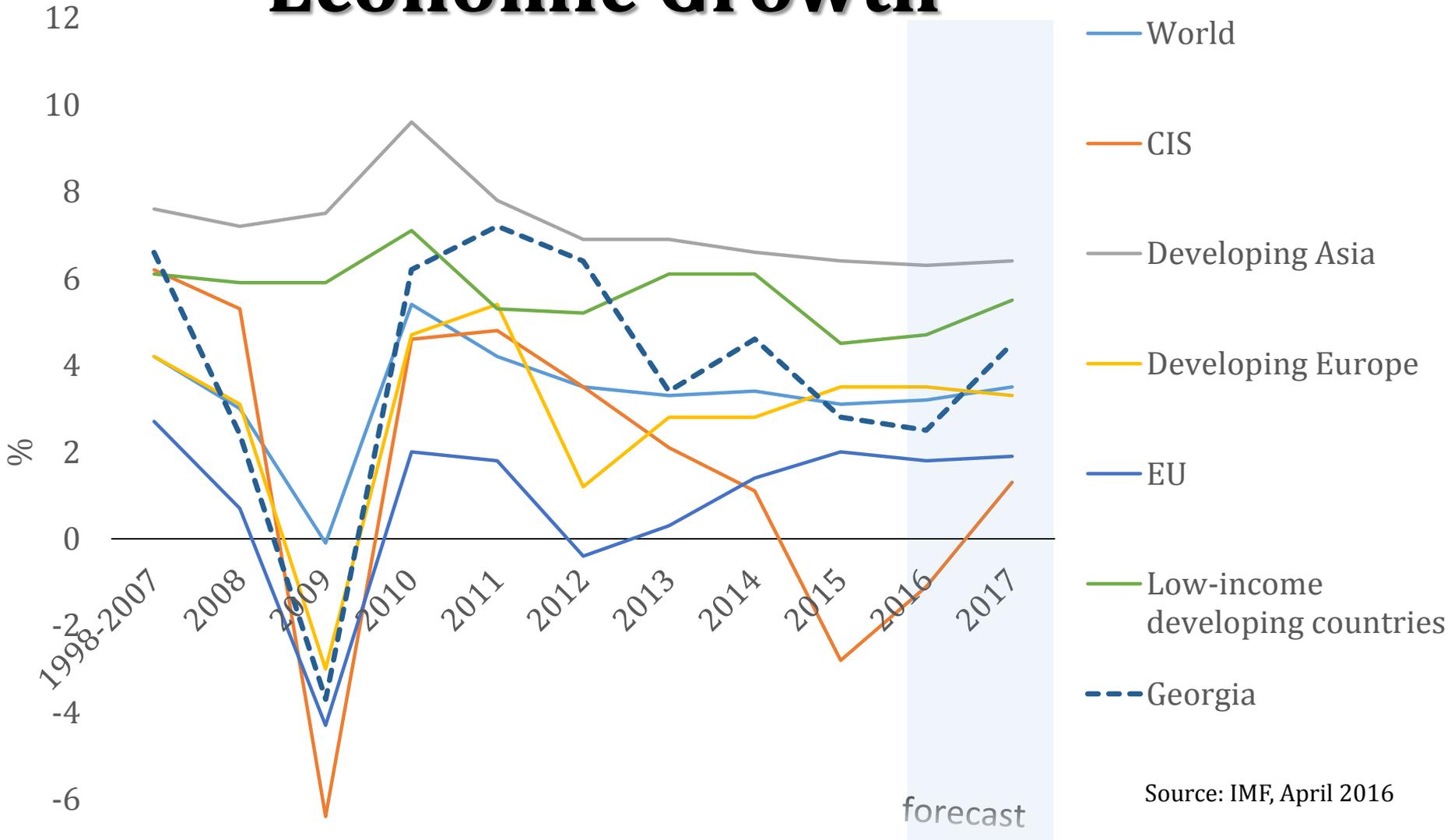
## Financial Risks

- Due to heavy dollarization, problem remains politically very vulnerable
- Exchange rate risk
- Pressure on currency regulations or exchange rate market restrictions

## Structural and Institutional Risks

- Subsidizing politically sensitive sectors (grapes, gas, electricity, transport, etc.), instead of price adjustment
- Business environment and overregulation (new initiatives from deferent levels of the government )
- New challenges from EU AA-DCFTA requirements
- Size of the public sector (# of hired employees)

# Economic Growth



Source: IMF, April 2016



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# Looking Ahead

- Facilitate GDP growth
- Further development of business enabling environment
- Increase capacity of public institutions
- Strengthen rule of law and legal system
- Scaling up the economy – further Integration (regional and global)
- Increasing competitiveness
- Increase FDI
- Reduce unemployment
- Maintain fiscal sustainability
- Improve the quality of education

## Progress in Countries with PMCG operations

Doing Business Indicators	Mongolia		Afghanistan		Kosovo		Kyrgyzstan	
	DB2012	16	DB2012	16	DB2012	16	DB2012	16
	86	56	160	177	117	66	70	67
<b>Starting a business</b>	97	36	30	34	168	47	17	35
<b>Dealing with Construction Permits</b>	119	25	162	185	171	136	62	20
<b>Getting Electricity</b>	171	134	104	156	124	124	181	160
<b>Registering Property</b>	26	44	172	184	73	32	17	6
<b>Getting Credit</b>	67	59	150	97	24	28	8	28
<b>Protecting Minority Investors</b>	29	8	183	189	174	57	13	36
<b>Paying Taxes</b>	57	91	63	89	46	67	162	138
<b>Trading Across Borders</b>	159	74	179	174	131	71	171	83
<b>Enforcing Contracts</b>	33	80	161	172	157	48	48	137
<b>Resolving Insolvency</b>	124	89	105	160	31	163	48	126

THANK YOU!