

Monitoring Georgia's SME Development Strategy 2016-2020



Policy Insights

**Monitoring Georgia's SME
Development Strategy
2016-2020**

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Acronyms and Abbreviations

AA	Association Agreement
APR	Annual progress report
CGS	Credit guarantee scheme
DACUM	Developing a Curriculum
DCFTA	Deep and Comprehensive Free Trade Area
EaP	Eastern Partnership
EBRD	European Bank for Reconstruction and Development
EC	European Commission
ECP	Eurasia Competitiveness Programme
EEN	Enterprise Europe Network
ETF	European Training Foundation
EU	European Union
FabLab	Fabrication laboratory
FDI	Foreign direct investment
GCCI	Georgian Chamber of Commerce and Industry
GDP	Gross domestic product
Geostat	National Statistics Office of Georgia
GoG	Government of Georgia
GIS	Geographic Information System
GITA	Georgia Innovation and Technology Agency
GIZ	Deutsche Gesellschaft für Internationale Zusammenarbeit
GVC	Global value chains
IFRS	International Financial Reporting Standards
INFE	OECD International Network on Financial Education
IP	Intellectual property
ISET-PI	International School of Economics at Tbilisi State University – Policy Institute

KPI	Key Performance Indicator
MIT	Massachusetts Institute of Technology
MoES	Ministry of Education and Science
MoESD	Ministry of Economy and Sustainable Development
MNE	Multinational enterprise
NBG	National Bank of Georgia
NCEQE	National Centre for Education Quality Enhancement
OECD	Organisation for Economic Co-operation and Development
PPC	Public-Private Consultation
PSDAC	Private Sector Development Advisory Council
R&D	Research and development
RIA	Regulatory impact assessment
SARAS	Service for Accounting, Reporting and Auditing Supervision
SBA	Small Business Act
SME	Small and medium-sized enterprise
TNA	Training needs analysis
UNDP	United Nations Development Programme
VET	Vocational education and training
WB	World Bank
WBL	Work-based learning
WEF	World Economic Forum

Executive Summary

In 2015, the Government of Georgia embarked on an ambitious effort to improve business environment conditions and tackle market failures that make it harder for entrepreneurs and managers of small and medium-sized companies to start, run and grow their businesses. The OECD supported these efforts, working with the Ministry of Economy and Sustainable Development to identify policy challenges and develop targeted measures to support Georgian SMEs.

These activities led to a peer review of Georgia at the OECD Eurasia Competitiveness Roundtable in November 2015 and to the subsequent adoption by the Government of Georgia's SME Development Strategy 2016-2020.

Part A of this report monitors the extent to which the 2015 OECD recommendations have translated into actual policy reforms, identifies outstanding gaps, proposes a way forward and most importantly suggests result-oriented Key Performance Indicators (KPIs) to help the government keep track of the impact of current and future SME policy reforms.

1. The **institutional framework and operational environment** for SMEs has substantially improved, with, e.g., the adoption of a new SME definition, the formalisation of platforms for public-private dialogue on business-related policies and laying the groundwork for Regulatory Impact Assessments (RIA). Building on these achievements, the introduction of SME-specific RIA tests could help the government better anticipate the potential impact of draft legislation on SMEs. Moreover, attention should also be drawn to carrying on the various activities aimed at improving business closure and insolvency procedures.
2. **Access to finance** for SMEs is now easier, thanks to changes in the legal framework allowing the provision of grants to commercial entities, an increase in the financial support offered by state agencies and the implementation of a multitude of financial education initiatives. However, a more co-ordinated approach to financial education could better address the specific needs of small and medium entrepreneurs, while also facilitating the adoption of international financial reporting standards. In addition, the creation of a full-fledged credit guarantee scheme and the development of alternative financing tools could reduce the burden of currently heavy collateral requirements on SMEs.
3. Georgia has made important progress in **developing skills and entrepreneurial culture**, especially regarding skills needs anticipation, the involvement of employers in setting education and training standards, and the introduction of mandatory entrepreneurship modules in vocational education and training curricula. The adoption of a strategic framework for women's entrepreneurship could help Georgia close the gender gap in entrepreneurship; but emphasis should be put on the implementation, monitoring and evaluation of the other various activities underway to effectively assess their impact.

4. **SME internationalisation** is being supported with a variety of export promotion activities, DCFTA information centres set up throughout the country, and a pilot FDI-SME linkages programme. Moving forward, the government could consider to further support cluster development, but also providing targeted financial support, such as export loans or export credit insurance instruments, to overcome financing barriers and risks encountered when engaging in international trade.
5. Important steps have also been taken to facilitate **SMEs' innovation and R&D activities**, by, e.g., allowing public universities and research centres to own spin-off companies and increasing financial support for innovation and expanding the statistical base on companies' use of ICT and innovation activities. The adoption of a more strategic approach towards SME innovation, including dedicated instruments to ensure better and more effective implementation of priority actions, would facilitate Georgia's shift towards a knowledge and innovation-based economy.

In response to a specific request from the government, Part B of this report presents an assessment of Georgia's current system for monitoring the implementation and impact of the SME Development Strategy 2016-2020, including an analysis of its targets. It also gives recommendations along three pillars – implementation, results and impact – to improve the current monitoring system:

1. **Implementation monitoring** of the SME strategy action plan could be improved by setting targets for quantitative indicators, which may be expressed in ranges to allow for deviations due to unpredictable events. More user-friendly tools for the annual progress report, such as heat-maps, would make it possible to enhance the communication value of the document for a wider audience.
2. **Results monitoring** would benefit from Key Performance Indicators for each strategic direction to clearly indicate the progress level of intended results. The annual progress report could therefore include a section reporting on these results, which will facilitate the revision and upgrading of the SME strategy for the next period.
3. **Impact monitoring** could be strengthened by adding a narrative section to the annual progress report, comparing current target values with past trends, reflecting changes in indicator values in the context of the overall economic cycle, and putting nominal values in perspective by reporting on changes in the overall price level.

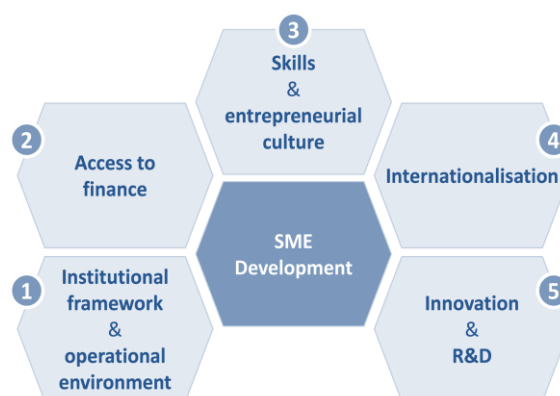
Introduction

OECD support for the SME sector in Georgia

In 2015, the Ministry of Economy and Sustainable Development (MoESD) embarked on an ambitious exercise to develop an overarching policy framework guiding government action to create a better business environment for SMEs and tackle the market failures that typically make it harder for small entrepreneurs to start, run and grow their businesses. With the support of the OECD as part of the EU4Business initiative, and inspired by international good practice, the Government of Georgia (GoG) engaged in a series of thematic workshops in consultation with the private sector to identify policy challenges and develop concrete measures for legislative and executive action to support small and medium enterprises (SMEs).

These steps led to the adoption of Georgia's SME Development Strategy 2016-2020, a multi-year government strategy with the stated objective of supporting the development and economic role of SMEs. The strategy identifies 33 priority actions to be taken in important areas for SME development, such as improving legislation, institutional frameworks, and the operational environment, as well as widening access to finance, developing entrepreneurial skills, broadening internationalisation, and supporting innovation activities (Fig.1).

Figure 1. Framework for SME Development in Georgia



Source: Public-Private working group for the SME Development Strategy 2016-2020

Following the adoption of the SME Development Strategy 2016-2020, the MoESD drafted the Action Plan 2016-2017 and started implementing SME policy reforms. The government recently approved a new Action Plan 2018-2020. It is thus an appropriate moment to assess the implementation status of the recommendations given in 2015.

This report assesses the extent to which OECD recommendations have translated into policy reforms, identifies outstanding gaps, proposes ways forward and most importantly suggests Key Performance Indicators to help the government monitor the impact of current and future SME policy reforms. The report also takes a critical look at the 2015

recommendations, reappraising the significance of those that have not been implemented by the government.

The assessment presented in this report is based on a number of sources, including: an initial fact-finding mission to Georgia in November 2017; an in-depth analysis of the annual progress reports on the SME Development Strategy Action Plan 2016-2017 prepared by the MoE; analysis of the inputs received from relevant line ministries and SME stakeholders on the OECD monitoring matrix based on the 2015 recommendations; two Working Group meetings held in 2018, with expert interventions on key performance indicators to better monitor the future Action Plan; and an analysis of official statistical sources.

Economic and policy developments since 2015

Economic growth in Georgia has been steady over the past years. Real GDP growth picked up in 2017, reaching 5%, after two consecutive years below 3%, led by the trade, construction and transport sectors in an improved external environment. Exports of goods expanded by 24% compared to 2016 on the back of stronger demand from Russia, Azerbaijan, Ukraine, China and the United States, while exports of services improved by 20%, mostly due to the tourism sector (WB, 2018). This positive trend continued in 2018 and economic growth in January-May amounted to 6.1%. Overall, since 2009, Georgia has experienced the strongest growth among countries in the European Union's "Eastern Partnership" (EaP)¹ and can be considered the most resilient economy in the EaP region.

Georgia is doing well in international rankings, having now entered the top ten in the World Bank's Doing Business 2019 report. Georgia's position improved by 18 positions since 2016 and now ranks 6th out of 190 countries. Georgia is in the world's top ten countries in the following four categories: starting a business (2nd), protecting minority investors (2nd), registering property (4th) and enforcing contracts (8th) and has not left the World Bank Top Improver classification since 2003, with a total number of 47 institutional and regulatory reforms carried out.

According to the Index of Economic Freedom 2018 (Heritage Foundation), Georgia ranks 16th out of 180 countries worldwide and 9th out of 44 countries in Europe, with a substantial improvement in property rights, judicial effectiveness and fiscal health. Fraser Institutes' Economic Freedom of the World 2018 puts Georgia in the list of top ten countries, ranking 7th out of 162. Moreover, Georgia has a free trade regime with one third of the world population, having in force free trade agreements with the Commonwealth of Independent States, Turkey, the European Union, the European Free Trade Association, China and Hong Kong.

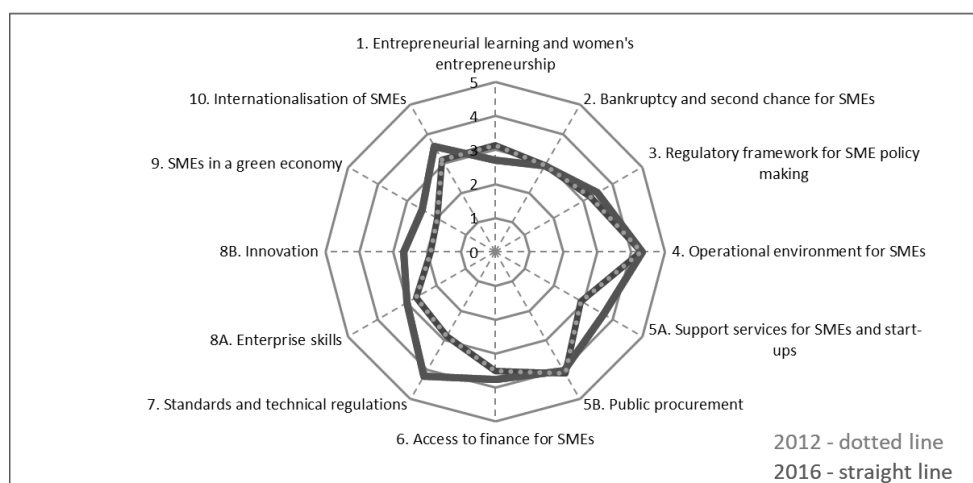
These considerable improvements are the result of Georgia's sustained and committed efforts to improve the business environment and increase investments over the past years. The government conducted a plethora of major reforms including simplifying the tax system, streamlining customs procedures, and combatting corruption, turning the country into an important destination for future investors.

¹ Armenia, Azerbaijan, Belarus, Georgia, Moldova and Ukraine.

The outlook is positive, as the EU-Georgia Deep and Comprehensive Free Trade Area (DCFTA) and Association Agreement (AA) are likely to further boost the country's economy, building on considerable efforts from Georgia to put in place a solid national awareness raising campaign to make the most out of these agreements.

SMEs have been a prominent item in the overall socio-economic reform agenda of the government. The OECD has supported this process by assessing Georgia's SME policies since 2012 in the framework of the Small Business Act Assessment in the EaP region (Fig. 2). In its latest edition published in 2016, the SME Policy Index for EaP countries highlighted the importance of establishing an institutional framework to carry out SME policies in Georgia. This included the design of guiding documents with a medium-term perspective, the SME Development Strategy and Action Plan, to help shape and implement the intended reforms.

Figure 2. SME Policy Index 2016: Small Business Act Assessment scores for Georgia

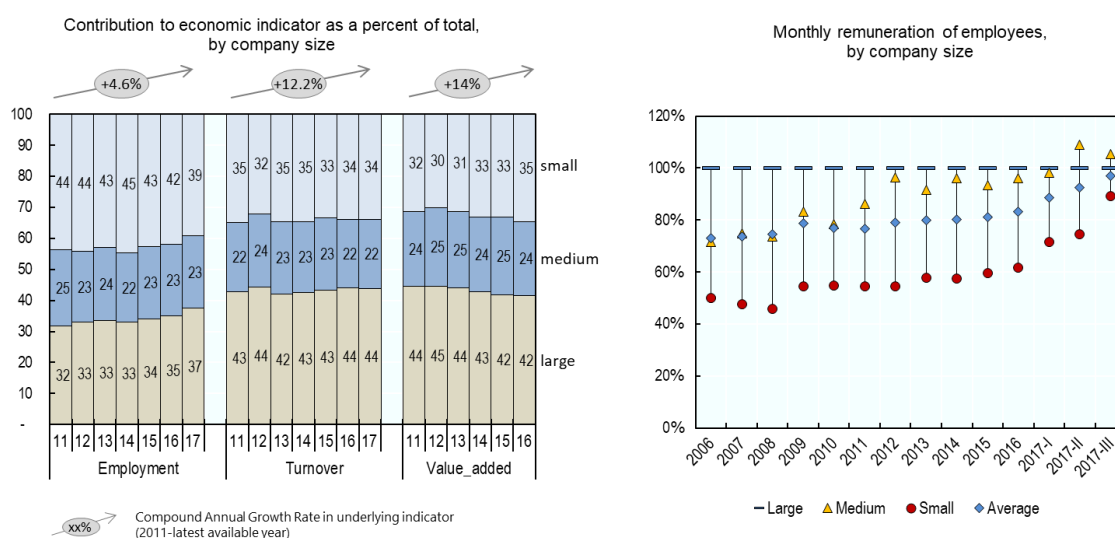


Source: OECD (2016a), SME Policy Index Eastern Partner Countries 2016

The SME sector in Georgia

Under the recently adopted new definitions and methodology, 99.7% of all firms in Georgia in 2017 were SMEs, accounting for 62% of total employment and 56% of total business sector turnover; in 2016, SMEs generated 59% of gross value added. SMEs' contribution to the economy is increasing in absolute terms, thanks to a steady growth in underlying indicators since 2011 (Figure 3). This trend is also accompanied by an increasing quality of jobs created, with remuneration in SMEs on a clear trajectory of catch-up with large firms.

Figure 3. The role of SMEs in Georgia's economy, 2011–2016/17



Note: A large enterprise is an enterprise in which the average annual number of employed exceeds 249 persons and/or volume of average annual turnover exceeds GEL 60 million. Medium-sized enterprises are all enterprises in which the average annual number of employed ranges from 50 to 249 persons and average annual turnover ranges between GEL 12 million to 60 million. Small-sized enterprises are enterprises in which the average annual number of employed does not exceed 50 persons and average annual turnover GEL 12 million.

Source: Geostat (2018a), “Business Statistics” (database)

As for the sectoral distribution, SMEs tend to be concentrated in low value-added sectors, such as trade (including repair of vehicles), manufacturing and construction, representing respectively 14.7%, 7.2%, and 10.4% of contribution to total value added in 2016. Geographically, almost half of all SMEs are located in the capital, while the rest are distributed mainly in the three larger regions of Georgia: Imereti (14%), Adjara (8.6%) and Samegrelo-Zemo Svaneti (8%) (Geostat, 2017).

Measurable targets² were set out in the SME Development Strategy to be achieved by 2020, namely:

growth in SME output by average 10% annually;

growth in the number of employees in SMEs by 15%; and

productivity growth (value added / number of persons employed) by 7%.

However, the lack of measurable and relevant key performance indicators beyond the three overall targets set out by the SME Development Strategy impedes the effective monitoring of implementation progress made along each strategic direction.

² Please refer to Part B for a detailed commentary on the targets of the SME strategy.

Main stakeholders in charge of SME policy implementation

Numerous stakeholders are involved in the implementation of SME policy reforms, with the most prominent roles being played by the entrepreneurship development agency *Enterprise Georgia* and the *Georgian Innovation and Technology Agency* (GITA), both of which fall under the authority of the Ministry of Economy and Sustainable Development.

The MoESD is in charge of setting the overall priorities and goals of SME policy, distributing roles and resources among stakeholders, and monitoring the implementation process.

Enterprise Georgia was established in February 2014 and is in charge of the implementation of SME support programmes. The main aim of Enterprise Georgia is to develop entrepreneurship by supporting the establishment of new enterprises, expanding existing ones and promoting entrepreneurial culture in the country. Based on three main pillars – business, investment and export – the agency focuses on increasing private-sector competitiveness, enhancing Georgia’s export potential and promoting foreign direct investment in Georgia. Its flagship programme offering support to SMEs is called *Produce in Georgia* (Box 2).

GITA was established in February 2014, with the goal of creating an innovation ecosystem within the country in order to support start-ups and R&D, especially in the ICT field. GITA focuses on the development of innovation infrastructure, such as technology parks, innovation centres and industrial laboratories, whilst also keeping an eye on the commercialisation and export potential of innovations and new technologies. Alongside plans to improve internet speed and access, including coverage in remote regions of Georgia, GITA aims to promote innovative business development with a particular focus on entering international markets. Beneficiaries of GITA, apart from receiving financial support, obtain assistance and trainings in a range of business areas.

Other stakeholders, such as relevant line ministries, the Georgian Chamber of Commerce, the National Bank of Georgia, various business associations, universities, research centres, the civil society and donors are involved in the implementation of SME policy reforms.

Part A – Monitoring of OECD 2015 Recommendations

Chapter 1: Improving the institutional framework and operational environment for SMEs

Findings of the 2018 assessment

Action 1: Create formal coordination mechanisms for SME policy among policy stakeholders

Since the implementation of the SME strategy began, the Georgian government has made significant efforts to improve co-ordination between relevant ministries, government agencies and private sector stakeholders. In 2016, the government established both a high-level Co-ordination Group and a Working Group to oversee the monitoring of the SME strategy. The former is headed by the Minister of Economy and Sustainable Development, overseeing the implementation progress, whereas the latter is led by the responsible Deputy Minister, in charge of collecting information from all relevant stakeholders and producing annual progress reports. Both entities include representatives of all implementing agencies, as well as business associations.

Co-ordination group and Working group meetings result in annual reports on implementation progress and Action Plan objectives and activities. The MoESD collects relevant information from the various stakeholders and prepares draft versions of the reports in December of each year. The drafts are available for comment throughout January and February, so that the implementing entities can respond before the MoESD finalises them.

In parallel, a Private Sector Development Advisory Council (PSDAC) was established in 2016. It operates under the supervision of the MoESD, with a Deputy Minister serving as Chair and a private sector representative serving as Deputy Chair. The bi-annual PSDAC meetings therefore formalise public-private consultations, raising awareness on ongoing and planned reforms, and providing the private sector, including SMEs and SME associations, with an opportunity to comment on entrepreneurship barriers and business-related legislation.

Additionally, the website matsne.gov.ge, established by the Legislative Herald under the Ministry of Justice, provides users with an access to all normative acts adopted by state agencies and enables public review of draft reforms. A dedicated web-portal with information about planned and implemented reforms under the DCFTA has also been created in 2017 by MoESD (dcfta.gov.ge), with, among other functions, the opportunity to comment on draft legislative acts uploaded on the portal.

Moreover, GoG recently introduced the concept of “Business Houses”, which would ensure the provision of over 800 government services to businesses through a “Single Window” principle by 2020. Services currently delivered by more than 60 public institutions will be centralised, both physically and digitally, to reduce time and resources spent by the businesses on various administrative procedures.

Action 2: Conduct regular SME-specific regulatory impact assessment

Regulatory impact assessment (RIA) initiatives have started in 2007, when the MoESD established an RIA Unit and began to promote the assessment process in Georgia. Throughout the years, the RIA Unit, together with line ministries, has participated in several trainings and seminars on required methodology and institutional set-up. Recently, the country has made important steps towards developing a full-fledged RIA system and procedures.

A national legislative RIA framework document has been prepared by the USAID project “Governing for Growth” in close co-operation with the private sector and academia and discussed in parliament, including recommendations on the institutional framework, criteria to identify regulations subject to RIA, the RIA methodology and capacity building needs of local institutions to effectively implement RIA. On its basis, the Government of Georgia elaborated a draft law aiming at making RIA legally binding. In addition to the above, RIA guidelines and manuals were elaborated, establishing the framework of the RIA methodology. Once the draft law adopted, a quality control unit will be created inside the government.

While the legislative framework awaits approval, pilot RIAs have been carried out for various draft laws such as the Law on Consumer Protection, the Law on Electricity Trading Mechanisms or the draft Environmental Assessment Code. It is also worth noting that in 2018, the MoESD has independently conducted an RIA on the Georgian Pension System Reform.

Regularly assessing potential impacts of new regulations on SMEs, including costs and benefits according to the EU “Think Small First” principle, remains a challenge. Ad-hoc SMEs tests have been carried out for selected laws, but at present, limited institutional capacity and financial resources at the centre of government and in relevant line ministries and agencies prevent a systematic approach to carry out full-fledged “SME-tests”. However, trainings and seminars for line ministries are planned in the near future to increase institutional capacity in this regard.

Action 3: Improve business closure and insolvency procedures

The government has been involved in a series of initiatives to support the improvement of business closure and insolvency procedures. A working group organised by the Ministry of Justice (MoJ), with the support of GIZ and participation of the Ministry of Finance and the Ministry of Economy and Sustainable Development as well as private practitioners, has assessed the existing legislation and identified areas for improvement.

Meanwhile, amendments to the Law on Insolvency Proceedings were adopted by parliament in May 2017. Alongside an in-depth study of international best practices, the working group has developed a new draft law, with the objective of further increasing the efficiency and transparency of insolvency proceedings by establishing flexible tools for rehabilitation as well as liquidation, increasing the role of courts in insolvency proceedings and granting creditors greater participation in important decisions (e.g. debtor’s reorganisation plans). Currently, an RIA of the draft law is being conducted. In addition, the MoJ has already started public discussions in order to collect feedback and comments on the draft law – in this regard, introducing a framework for efficient out-of-court insolvency settlements could also be considered.

Action 4: Streamline the SME definition across statistics and improve SME statistics collection and dissemination

Geostat, the National Statistics Office of Georgia, has recently revised the SME definition to comply with European Union standards and increase international comparability. The new Georgian definition comprises both the number of employees, as well as the total turnover of the company.³ Geostat has recalculated business statistics indicators according to the new definition since 1999 to allow for easy comparison and a smooth transition. Economic indicators with breakdown according to the old definition will be kept alongside the new one for another year.

The new definition enabled the government to obtain a more realistic idea of the weight of large companies in the Georgian economy. On the new definition, there are just 350 large companies, as compared to 4 000 on the old one. According to the previous definition, large companies in 2017 generated 82% of total turnover and 78% of value added. On new definition however, the share in total turnover is 44% and that of value added 42% (Geostat, 2018a).

Following the adoption of the SME strategy 2016-2020, Geostat has further made a substantial effort at improving SME statistics collection and dissemination. The Statistics Office performs quarterly surveys of 12 500 companies and annual surveys of 15 500. The surveys aim at collecting data on the number of employees, wages and geographical location of business entities, as well as business ownership disaggregated by gender. Additionally, since October 2018, Geostat started disseminated external trade data by size of enterprises.

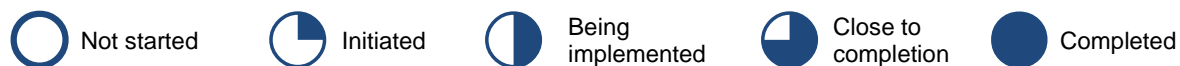
Furthermore, Geostat has developed a Geographic Information System (GIS) for the dissemination of business statistics, where, through an online tool, users can analyse comprehensive business statistics by region.

³ Old SME definition used by Geostat: Medium-sized enterprises employ up to 100 employees and have a turnover of up to GEL 1.5 million (~ EUR 500 000) annually. Small-sized enterprises employ up to 20 employees and have a turnover of up to GEL 500 000 (~EUR 170 000) annually.

New SME definition used by Geostat, according to EU standards: Medium-sized enterprises employ up to 250 employees and have a turnover of up to GEL 60 million (~EUR 20 million) annually. Small-sized enterprises employ up to 50 employees and have a turnover of up to GEL 12 million (~EUR 4 million) annually.

Overview of the monitoring assessment

Overall 2015 recommendation	Detailed 2015 recommendations	2018 monitoring assessment – progress status
Create formal coordination mechanisms for SME policy among policy stakeholders	<ul style="list-style-type: none"> • Maintain Working/Steering Group • Formalise PPC mechanisms, involve private sector 	
Conduct regular SME-specific regulatory impact assessment	<ul style="list-style-type: none"> • Introduce formal RIA mechanism/“SME test” • MoESD to pilot • Clear out obsolete laws 	
Improve business closure and insolvency procedures	<ul style="list-style-type: none"> • Ease liquidation and restructuring procedures • Strengthen creditor protection and participation 	
Improve SME statistics collection and dissemination	<ul style="list-style-type: none"> • Expand business statistics by sector and size class • Minimise effort for SMEs when providing data • Periodic analyses, published online 	
Streamline SME definition across statistics and policymaking	<ul style="list-style-type: none"> • Include micro-enterprises as a category • Align with EU’s SME definition 	



Suggested key performance indicators and way forward

To better monitor the progress made in improving the institutional environment for SMEs, the following proxy KPIs could be considered:

Table 1. KPIs to monitor the institutional environment for SMEs

KPI	Description/rationale	Source of data
Annual growth of investment by SMEs	An approach to assessing the impact of institutional improvements is through the observed behaviour of economic agents. Investment decisions by enterprises are sensitive to the level of perceived risk and uncertainty. Therefore, a predictable, transparent and simple institutional environment reduces one of the risks to investments. By this reasoning, the annual growth of investment by SMEs could be used as a proxy indicator for improvements in the overall institutional framework.	Geostat
Total early stage entrepreneurial activity Share of early stage entrepreneurs motivated by opportunity	Improved institutional environment can be expected to stimulate entrepreneurship based on business opportunities, rather than necessity due to lack of paid employment options. These indicators could therefore be used to measure the extent and quality of entrepreneurial activity. It should be noted, however, that the preparation of Global Entrepreneurship Monitor reports relies on local partner institutions and the collection of information for Georgia remains irregular (latest report available - 2016, no availability for 2015).	Global Entrepreneurship Monitor
Resolving insolvency indicator (distance to frontier)	The World Bank's <i>Doing Business</i> resolving insolvency indicator measures time, cost and outcome (recovery rate) of a typical insolvency procedure involving domestic companies. It will be important to not only look at the rank but also at the actual scores (distance to frontier), where the frontier represents the best performance observed on the indicator among participating countries.	World Bank Doing Business

Way forward

Introduce SME-specific regulatory impact assessment

Regulatory Impact Assessment remains an important area of future improvement for SME policy. In 2015, the OECD recommended the introduction of a formal RIA mechanism to measure the impact of new legislation on small and medium sized companies. While monitoring the implementation of the SME strategy, discussions between the Ministry of Economy and Sustainable Development and the OECD revealed that additional action is required in the sphere of RIA and its role in improving the institutional framework and operational environment for SMEs.

Building on the pilot RIAs that have been carried out for the above-mentioned draft laws, developing an SME-specific RIA test is an essential element of the policy making process and will enable the government to design specific tools to ensure that proposed legislation (new or amended) will not impact disproportionately SMEs.

Over the last years, OECD governments have made considerable efforts to use RIA in order to mitigate negative regulatory impact on small and medium sized enterprises. The

European Union's *Small Business Act for Europe* (European Commission, 2014) and its "Think Small First" principle recommend that policy-makers take into account the impact of legislation on small businesses through a dedicated "SME-test" (Box 1). Drawing on EU examples, Georgia could develop its unique SME test and designate a central entity to support its development and implementation.

Box 1. EU Guidelines for the SME test

Regulations may have a disproportionate effect on SMEs in terms of compliance costs. Therefore, the European Commission has set up the "SME test" as an integral part of the Better Regulation Guidelines, with four main steps aimed at better assessing/anticipating the impact of proposed legislation on SMEs.

Step 1: Identification of affected businesses

First, SMEs likely to be affected by new legislation should be identified. Governments should identify the characteristics of the affected businesses/sectors, and the potential impact on SMEs through subcontracting.

Step 2: Consultations that capture the SME angle

If SMEs are potentially affected, then the SME dimension should be a central element of the consultation strategy. In addition to an open public consultation, specific actions could be considered such as roundtable discussions, focus groups, and hearings with SME representatives.

Step 3: Measurement of the impact on SMEs

For each policy option, the distribution of costs and benefits with respect to business size should be analysed. Benefits may be offset by regulatory costs, some of which may be disproportionately felt by SMEs, such as compliance costs, administrative costs to provide additional information, possible impacts on barriers to entry, competition, market structure, and innovation activities.

Step 4: Assessment of alternative options and mitigating measures

The above-mentioned analysis may show that micro, small and/or medium-sized enterprises face a greater compliance burden than large companies. In that case, specific mitigating measures *may* be warranted for certain groups of SMEs, such as: temporary tax reductions or exemptions, direct financial aid to compensate costs incurred if compatible with existing legislation on competition or international trade, simplified reporting obligations, information campaigns or user guides, training and dedicated helpdesks, general simplification initiatives which can particularly benefit SMEs.

Source : European Commission (2017), The SME Test: Better Regulation Toolbox

Chapter 2: Enhance access to finance for Georgian SMEs

Findings of the 2018 assessment

Action 1: Amend the legal framework on public grants

The Law on Grants, which previously limited the scope for targeted financial assistance to SMEs and innovative start-ups, has been revised and amendments have been adopted in 2016. Following the revisions, state agencies such as Georgia's Innovation and Technology Agency or Enterprise Georgia's *Produce in Georgia* programme (Box 2) have been authorised to award public grants, exempted from relevant taxes, to private commercial entities.

Box 2. Enterprise Georgia's state programme *Produce in Georgia*

The state programme *Produce in Georgia* was launched in May 2014 as part of Georgia's strategy to support the development of the private sector, and SMEs in particular. The programme aims at facilitating the development of manufacturing industries, as well as the establishment of new enterprises and the growth of existing ones.

The programme is supervised by the Ministry of Economy and Sustainable Development of Georgia (implementing agencies: Enterprise Georgia, National Agency of State Property) and the Ministry of Agriculture of Georgia (implementing agency: Agriculture Projects Management Agency).

Under *Produce in Georgia*, Enterprise Georgia supports access to finance in form of co-financing of the interest rate on commercial loans during the first two years. A collateral guarantee of up to 50% of the loan is included in that financial support. The programme is implemented in cooperation with all major commercial banks and leasing companies in Georgia.

In 2015, within the framework of *Produce in Georgia*, the government introduced a sub-programme "Support to Micro and Small Businesses", which aims at developing enterprises with a blended approach combining financial assistance mechanisms (matching grants with a contribution by the beneficiary of at least 20%) with consulting services on business plan development and business administration in order to provide the beneficiaries with the necessary knowledge on modern business practices. The programme covers all regions of the country, except for the capital. Trained and selected project owners receive matching grants of up to GEL 5 000 (~ EUR 1660) (in case of cooperation of maximum 3 people – GEL 15 000 or EUR 5 000) from the government.

Enterprise Georgia received 42 000 applications in 2015-2017, of which 5 300 projects (GEL 38 650 000 or EUR 12 900 000) were selected to benefit from the grant scheme.

Overall, since its inception, *Produce in Georgia* mobilised private investment of around EUR 320 000 000 and contributed to the creation of more than 15 000 jobs.

Sources: Enterprise Georgia (2018), *Produce in Georgia*; OECD (2018a), *Financing SMEs and Entrepreneurs 2018: An OECD Scoreboard*

Action 2: Promote demand-side financial education programmes targeting SME entrepreneurs

A number of agencies involved in the implementation of the SME strategy have sought to provide tools to improve financial literacy among entrepreneurs. The work of the National Bank of Georgia (NBG) in this area, and in particular its recently created division for Financial Education within the Department of Consumer Protection, is particularly noteworthy.

In 2016, NBG elaborated and disseminated educational brochures for SMEs through its website and local banks. The initiative aimed at explaining a variety of financial concepts and tools relevant to running a business, focusing, among other things, on foreign exchange risk and different types of debt instruments. To expand the coverage and complement the lessons conveyed by the brochure, the NBG is currently working on

developing a broader guidebook and training module for micro and small enterprises⁴. These tools are focused on financial decision-making and interacting with financial institutions, with outreach activities in the regions, as well as additional financial education projects, targeting different segments of the population.

More broadly, the NBG has led the effort to measure financial literacy across the country. The Bank conducted a countrywide study on financial literacy and inclusion in 2016, based on the 2015 OECD/INFE toolkit for Measuring Financial Literacy and Financial Inclusion. The results of the study served as a baseline for the 2016 National Strategy on Financial Education, targeting SMEs as part of the broader population. The strategy is currently being implemented and aims, among other things, to introduce financial literacy in schools, through close collaboration with the Ministry of Education and Science. As a result of this close co-operation, a new national curriculum for secondary level (grades 7 to 9) including financial education topics has already been approved this year.

The Ministry of Finance, and especially the Service for Accounting, Reporting and Auditing Supervision (SARAS), is currently involved in designing and implementing the operational and legal framework for SMEs to produce financial statements in accordance with International Financial Reporting Standards for SMEs (IFRS for SMEs). This new system, with which SMEs must comply by end-2018, will allow them to submit financial statements through a simple online procedure, increasing the transparency and accountability of enterprises. To complement this effort, the Ministry of Finance, in co-operation with the World Bank, EBRD, Georgian Chamber of Commerce, accounting organisations, business and banking associations, is carrying out awareness raising campaigns since 2017 for accountants, CFO/CEOs and business owners throughout the country. Additionally, manuals for tutors and more than 20 training modules have been developed to help SMEs prepare financial reports in accordance with IFRS for SMEs.

Enterprise Georgia has also made significant efforts to improve the level of financial literacy among SMEs. Within the framework of the *Produce in Georgia* programme and its micro and small business support component (Box 2), the organisation provided training courses to around 14 500 beneficiaries throughout 2016-2017. The training included basic principles of financial literacy such as the preparation of business plans, business administration and accounting.

Action 3: Consider establishing a credit guarantee scheme as a risk-sharing mechanism

While credit conditions are generally improving (Box 3), high collateral requirements (up to 200% of loan value) and interest rates (at around 19% in local currency and 10% in foreign currency) still make it difficult for Georgian SMEs to borrow from banks. Due to information asymmetries between lenders and borrowers, land and real estate are the preferred forms of collateral demanded by banks, but SMEs are typically undercapitalised and innovative start-ups predominantly own mainly intangible assets.

⁴ The OECD/International Network on Financial Education (INFE) is developing a Core Competencies Framework on Financial Literacy for MSMEs, which could be used as an important source of inspiration for developing dedicated financial education initiatives for SME and entrepreneurs. (www.oecd.org/finance/financial-education/)

No full-fledged credit guarantee scheme currently exists in Georgia, but partial collateral guarantees are available under the state programme *Produce in Georgia*. Tailored to the specific stages of enterprise development and financial needs of the business, *Produce in Georgia* offers partial collateral guarantees of up to 50% of the loan amount (up to GEL 2 500 000 or EUR 850 000). Eligible loans are provided by twelve partner banks and must be in national currency since 2017.

In this regard, Georgia launched a new reform this year to improve SME access to finance, including plans to establish a credit guarantee scheme in close co-operation with international financial institutions (IFIs). The credit guarantee scheme intends to address specific market failures, which prevent credits from being issued to commercially viable businesses due to insufficient collateral. The mechanism is designed to support risk diversification, credit supply growth and reduction of interest rates, with a subsequent positive impact on economic growth.

Action 4: Improve alternative non-bank and equity financing for SMEs

Precise data on the availability and use of alternative finance instruments is lacking. However, initial evidence suggests that micro-finance is becoming an increasingly relevant source of alternative finance. As of 2017, there were 80 micro-finance organisations, with over 430 branches, registered in Georgia and supervised by the National Bank. Since 2010, lending by microfinance-organisations to SMEs has grown steadily. By end-2016, the total amount of loans to SMEs in the portfolio of microfinance organisations amounted to GEL 7.7 million (~EUR 2.6 million) compared to GEL 1.7 million (~EUR 570 000) in 2010. The main clients of microfinance institutions in Georgia are non-bankable micro and small enterprises (OECD, 2018a).

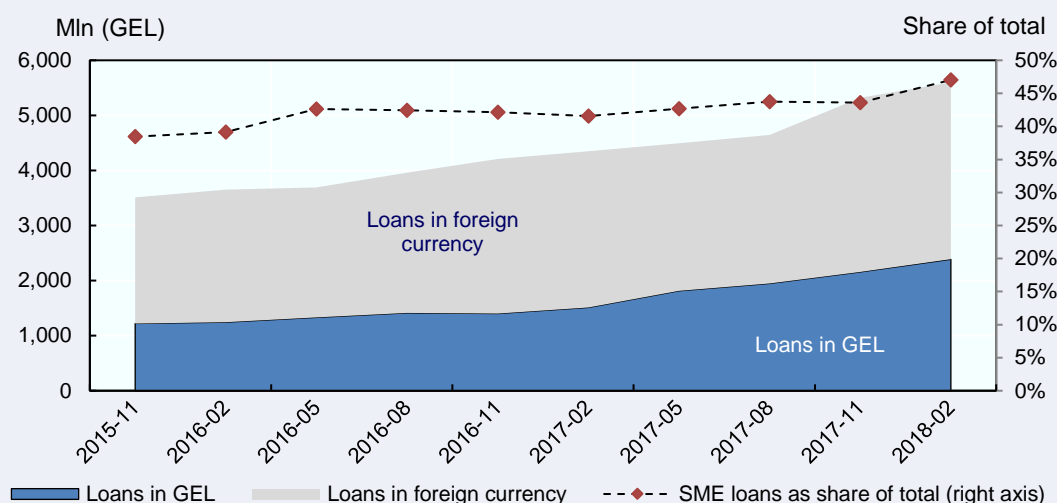
In 2017, GITA, in co-operation with Enterprise Georgia and the MoESD, conducted initial research and identified potential foreign venture capital funds to propose alternative finance mechanisms to selected start-ups. As a result, MoESD, in co-operation with IFIs, NBG and MoF, elaborated a draft law “on Investment Funds”, aiming at regulating the establishment, constitution and operation of collective investment schemes⁵, as well as the offer and marketing of such schemes in Georgia, in line with EU directives. In parallel, trainings on fundraising for start-ups are being held. In 2018, GITA became a member of the European Business Angels Network (EBAN), to support entrepreneurs in developing business models, refining pitching skills and facilitating linkages with potential investors.

⁵ An arrangement that enables a number of investors to pool their assets with a view to sharing the profits/income from the holding, management or disposal of the assets.

Box 3. Evolution of SME lending and interest rates

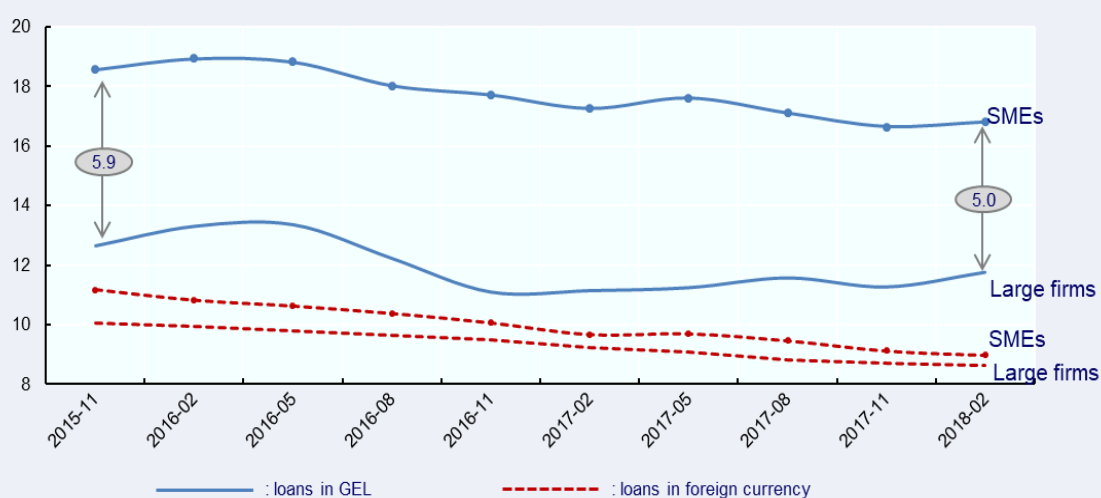
Bank lending to SMEs is increasing in both absolute terms and relative to large firms. This positive trend is more pronounced for loans denominated in GEL, which have almost doubled in nominal value since 2015, than for loans in foreign currencies (USD, EUR, GBP, RUB). As of February 2018, the stock of outstanding loans issued to SMEs made up 47% of total business loans, up from 38% two years earlier.

Figure 4. Loans to SMEs



Falling interest rates are to be considered at least partially responsible for the expansion of SME loans in the portfolios of banks. Most interestingly, the spread of interest rates on loans issued to SMEs vs. large firms is narrowing (i.e. credit conditions are improving), suggesting that the risk factor associated to SMEs is being reduced in the perception of banks.

Figure 5. Average interest rate on loans, %



Note: Loans issued in foreign currency are converted in GEL.
 Source: OECD analysis based on data from National Bank of Georgia

Overview of the monitoring assessment

Overall 2015 recommendation	Detailed 2015 recommendations	2018 monitoring assessment – progress report
Amend the legal framework on public grants	<ul style="list-style-type: none"> Amend laws on provision of public grants to make commercial entities eligible 	
Promote demand-side financial education programmes targeting small and medium entrepreneurs	<ul style="list-style-type: none"> Financial skills education initiatives Measure and monitor financial literacy of SMEs Include financial literacy in school curricula 	
Consider establishing a credit guarantee scheme as a risk-sharing mechanism	<ul style="list-style-type: none"> Introduce CGS with defined aims, target groups, coverage rate, fees, organizational structure and governance 	
Improve alternative non-bank and equity financing for SMEs	<ul style="list-style-type: none"> Strengthen venture capital environment Promote alternative forms of asset-based financing 	



Not started



Initiated



Being implemented



Close to completion



Completed

Suggested key performance indicators and way forward

Progress made on the improvement of access to finance for SMEs can be monitored with the help of the KPIs set out in Table 2. These KPIs should be monitored closely and with a critical eye: they should not be seen simply as individual targets for which policy-makers should “aim” but rather as a complex set of indicators that can together provide a picture of the evolution of SME access to finance.

Table 2. KPIs to monitor access to finance for SME

KPI	Description/rationale	Source of data
Annual growth rate of total loans to SMEs	Straightforward indicator providing a simple start to monitor SMEs access to bank financing; should not be seen as a target, as could be used to monitor potential bubbles (over-lending) as well as under-provision of credit.	National Bank of Georgia
Average interest rates for loans to SMEs	Useful to monitor credit conditions for SMEs, and relative risk perceived by banks when lending to SMEs vs. large firms	National Bank of Georgia
Interest rate spread (SMEs - large firms)	Useful to monitor the risk factor perceived by financial institutions when lending to businesses of different size class	National Bank of Georgia
Percentage of firms citing access to finance as one of the “most problematic factors for doing business”	A subjective indicator but one that still gives an indication of firms’ own perceptions of unmet needs; can provide important context for interpretation of other indicators.	WEF Global Competitiveness Report

Georgia also participates in the *OECD Scoreboard on Financing SMEs and Entrepreneurs*. This regular publication provides an extensive overview of indicators about the state of SME financing. While official data provided to the OECD by the Georgian authorities could be consulted independently, the Scoreboard allows for some degree of international comparison and could be considered by the MoESD as a useful resource to complement its monitoring effort.

Way forward

Adopt a co-ordinated approach to improving financial literacy for SMEs

Several scattered activities are being carried out to improve financial literacy for SMEs, including trainings within the framework of *Produce in Georgia* programmes and the dissemination of educational brochures for business owners and training modules for SMEs developed by the NBG. However, no strategic framework specifically targeting financial literacy of SMEs exists. A dedicated strategy for SME financial literacy, with an action plan including clearly defined roles, responsible implementing institutions, implementation timeframes, a monitoring system and attributed resources, could help Georgia adopt a more co-ordinated approach towards improving financial literacy of entrepreneurs.

As a first step, as a follow-up to the countrywide study conducted in 2016, the NBG could measure financial literacy levels of SME owners using the forthcoming OECD/INFE questionnaire⁶, specifically developed for small and medium entrepreneurs. Georgia could then take inspiration from the forthcoming *OECD/INFE Core Competencies Framework on Financial Literacy for MSMEs* to select or develop dedicated financial education initiatives.

Raising awareness of the benefits of IFRS could be considered one such initiative. Given the current reluctance of CEOs to report on their financial statements according to IFRS, the Georgian Associations of Banks and SME associations, in co-operation with SARAS and the NBG, could be mobilised to raise awareness among SMEs of the benefits of increased transparency in financial statements, not least in order to get easier access to credit.

Design a market-oriented full-fledged credit guarantee scheme as a risk-sharing mechanism

OECD (2015) recommended that the authorities consider the creation of a credit guarantee scheme (CGS) to support better SME access to credit. Although much has changed since then, continued large interest rate spreads and high collateral requirements would suggest that the case for such a scheme remains valid today. A CGS works as a risk-sharing mechanism between lenders (banks), borrowers (SMEs) and a guarantor (the state or a private entity). In exchange for a fee paid by the borrower, the guarantor provides banks with the guarantee that it would reimburse a pre-determined share of the outstanding loan in case of default by the borrower.

A CGS could create market-based incentives for banks to lend more to SMEs. By reducing the perceived risk, banks are expected to demand lower collateral and interest rates from SMEs. As a result, more credit is extended to borrowers than otherwise would be the case. Four key elements should be considered when designing a CGS for Georgia:

Objectives and eligibility: define the aims of the CGS and the target groups (i.e. SMEs with proven difficulties to access bank loans) to ensure financial and economic additionality, as well as the sustainability of the scheme.

Coverage rate: define the amount of risk shared with the bank (i.e. percentage of loan reimbursed in case of default) to encourage lending while limiting moral hazard.

Fees: define the fee charged to borrowers (e.g. a percentage of loan amount), which should both cover costs and ensure borrowers' participation in the scheme.

Type of CGS: set the organisational structure and governance of the scheme (i.e. public, private, or public-private with international support).

Develop alternative financing tools

The government has already taken steps to design an effective regulatory framework to stimulate the development of financial tools beyond traditional bank finance (e.g. Law of Georgia on Microfinance Organisations, Law on Collective Investment Undertakings,

⁶ To be published in 2019.

Law on Crowdfunding), but a much broader spectrum of alternative financial instruments exists (Fig.6).

Building on this, the government could promote SME awareness of the alternatives to bank lending, accompanied by training and financial education programmes to ensure the correct use of instruments according to the stage of any given firm's development, and investors (equity investment opportunities). Dedicated awareness-raising events, showcasing the most promising business ideas, could also help attract business angels and support the establishment of an angel investor community, leading to a possible legal framework on angel investment and incentives.

Another option, on the side of debt funding, would be to establish a regulatory framework for Peer-to-Peer (P2P) lending, a financing tool which is currently expanding in Georgia. P2P is the practice of lending money to individuals or businesses through online services that match lenders directly with borrowers. Since P2P companies offering these services operate entirely online, they can run with lower overhead and provide the service more cheaply than traditional financial institutions. As a result, lenders often earn higher returns compared to savings and investment products offered by banks, while borrowers can borrow money at lower interest rates, even after the P2P lending company has taken a fee for providing the match-making platform and credit checking the borrower.

Figure 6. Alternative external financing tools for SMEs and entrepreneurs

Low Risk/ Return	Low Risk/ Return	Medium Risk/ Return	High Risk/ Return
Asset-Based Finance	Alternative Debt	"Hybrid" Instruments	Equity Instruments
<ul style="list-style-type: none"> • Asset-based lending • Factoring • Purchase Order Finance • Warehouse Receipts • Leasing 	<ul style="list-style-type: none"> • Corporate Bonds • Securitised Debt • Covered Bonds • Private Placements • Crowdfunding (debt) 	<ul style="list-style-type: none"> • Subordinated Loans/Bonds • Silent Participations • Participating Loans • Profit Participation Rights • Convertible Bonds • Bonds with Warrants • Mezzanine Finance 	<ul style="list-style-type: none"> • Private Equity • Venture Capital • Business Angels • Specialised Platforms for Public Listing of SMEs • Crowdfunding (equity)

Source: OECD (2015), *New Approaches to SME and Entrepreneurship Financing: Broadening the range of instruments*

Chapter 3: Promote skills development and entrepreneurial culture

Findings of the 2018 assessment

Action 1: Develop a country-wide labour market and training needs analysis

The Ministry of Labour, Health and Social Affairs (MoLHSA) plays a central role in the effort to develop a country-wide labour market and training needs assessment. The first strategy on employment was thought out in 2013 and implemented in the subsequent couple of years. Within the framework of the strategy, since 2015, services such as career guidance, professional consultations and CV proofreading are being provided. The first labour market survey was carried out in 2015, involving 6 000 companies of different sizes, revealing the most demanded professions in the Georgian labour market.

Based on the findings of the survey, the Ministry of Labour, Health and Social affairs, in co-operation with the Ministry of Education and Science, designed training and re-training programmes for registered jobseekers. Implemented by the Social Service Agency of Georgia, training and re-training programmes were organised in both public and private Vocational Education and Training (VET) colleges throughout 2015-2017, with the aim of continuing until 2020. As a result, out of 2 130 beneficiaries of the programme in 2017, 400 jobseekers found employment by the end of 2017.

The training and re-training programme also offers a professional internship component, developed and implemented in collaboration with Georgian businesses. These two schemes will be closely monitored, updated and revised with help of regular surveys and consultations with the business community.

Additionally, the Ministry of Economy and Sustainable Development carried out an *Establishment Skills Survey* among 6 000 companies in 2017, to better meet the revealed demand of enterprises for human capital and increase the involvement of the private sector in education and professional trainings. A report based on survey results has recently been compiled and will be used to increase public awareness on the identified skills mismatches in the labour market and, at a later stage, inform (vocational education) training providers.

In 2016, MoLHSA established a comprehensive Labour Market Information System (LMIS) as an integrated and user-friendly public web portal, aimed at providing updated information on labour market trends, occupational profiles and career guidance for various stakeholders (students, jobseekers, research institutions, governmental bodies, the private sector etc.). Since 2017, the LMIS is administered by the Ministry of Economy and Sustainable Development, which took over the labour market analysis function from the MoLHSA.

In the area of Training Needs Analysis (TNA), Enterprise Georgia, in close co-operation with the European Training Foundation (ETF), has been playing an active role in setting up relevant mechanisms to assess SMEs' training needs in various sectors. A pilot project was launched in 2016 to assess the hospitality and paper/paper processing/printing and

publishing sectors. Enterprise Georgia has developed in-house skills to implement a TNA, including quantitative and qualitative employer surveys, with a participation of 132 companies. The results of the survey were disseminated at various events dedicated to the development of professional education.

Based on the results of the TNA, in 2018, a three-stage study on improvement of co-operation between the hospitality industry and educational institutions has been carried out with the support of ETF. The study revealed customer orientation, communication skills and knowledge of foreign languages and computer skills as main challenges in the hospitality sector, and developed recommendations to improve the abovementioned co-operation.

Action 2: Strengthen stakeholder participation in developing and implementing VET policies

Several initiatives have been put in place with the goal to strengthen stakeholders', participation in developing and implementing VET policies, with a particular attention paid to the private sector. In particular, dedicated councils on vocational education (National Vocational Education Council, chaired by the Minister of Education and Science of Georgia; Sectoral Councils; Supervisory Councils at college level) rely heavily on private sector and civil society representation, such as employers' associations and trade unions.

Since 2013, the above-mentioned sectoral councils, operating at the National Centre for Education Quality Enhancement (NCEQE), contributed to the validation of over 200 professional standards as well as to the preparation of framework documents to develop flexible modular VET programmes.

Additionally, the *Vocational Qualifications Development Programme*, carried out by the NCEQE, provides further possibility for the private sector to provide input for VET standard setting. The project follows the DACUM methodology⁷, which requires an equal participation of representatives of large, medium and small businesses. The aim of the programmes is to draw out vocational standards in accordance with employers' needs.

Finally, with the aim of further modernising VET to meet labour market needs, the MoES has worked out the concept of Work-Based Learning (WBL), with the support of UNDP and GIZ. Since 2016, up to 20 dual technical VET programmes have already been introduced in the agricultural, tourism, railway, transport and construction sectors, ensuring employers' participation in programme development, student selection and examination processes.

Action 3: Improve the quality and attractiveness of VET institutions

Improving the quality and attractiveness of VET institutions and increasing relevance of VET programmes for job-seekers is of central concern to the VET reform, carried out by the MoES in the framework of the VET Development Strategy 2013-2020. The State

⁷ DACUM: Developing a curriculum is a storyboarding process to capture the major duties and related tasks included in an occupation, as well as the necessary knowledge, skills, traits and tools the worker uses. (www.dacum.org)

Budget to implement the reform more than doubled from 2013 to 2016, increasing from GEL 13.3 million (~ EUR 4.5 million) to GEL 33.7 million (~ EUR 11.3 million) (GoG, 2017a).

Both the VET Development Strategy 2013-2020 and the 2016-2017 Action Plan for the SME strategy of Georgia highlight entrepreneurial learning as one of their priorities by including a compulsory entrepreneurship module in VET programmes to facilitate self-employment opportunities. This module is now mandatory in all VET programmes and includes capacity building of teaching staff with the support of various international partner organisations.

The reform of educational programmes also envisioned the transformation of subject-based curricula into modular teaching, aimed at developing particular competencies. This modularisation approach aims not only to promote the flexibility of VET options and thus improve its attractiveness, but also to make the education system more labour market oriented and flexible in terms of improving specific workforce skills. As of February 2018, up to 100 programmes have been re-designed and approved, and Georgia aims to shift all subject-based VET programmes to 'modular' by 2019.

The attractiveness of state VET colleges seems to be improving, with 11 170 enrolled students in 2016 (an increase of 10% compared to the previous year) and private institutions welcoming 4 469 students (ISET-PI, 2017). According to the 2015 tracer study conducted among 2 591 graduates of 2014, 30% of respondents started a job directly after graduation, 17% of respondents already had a paid job before graduating and the employment rate was at 56% within 3 months after graduation (GoG, 2015). The latest 2017 tracer study, conducted among 3 144 graduates of 2016, shows an employment rate of 56.2% reached within 3 months after graduation and 93% of the respondents were satisfied with their choice of VET institution.

Additionally, MoES launched a Vocational Skills Development Programme in 2017, with an aim to strengthen the collaboration between general schools and VET colleges for the provision of professional orientation services for graduate-level school students. After elaborating a joint project with the VET colleges according to their interest, school students take part in different VET skills development workshops at school with the support of schoolteachers.

Action 4: Facilitate SME access to non-formal training

Non-formal education is yet to be officially recognised in Georgia. In the last couple of years, the MoES, with the support of ETF, analysed the existing regulatory framework and developed a concept of recognition of non-formal learning. Since 2016, a pilot phase has been initiated in three sectors (IT, beekeeping and agricultural machinery mechanics).

As a next step, the government plans to develop a system of recognition of non-formal education. However, the financing of such a system, if opened up to all sectors, would be a major issue. The costs and benefits of recognition are yet to be determined. Ultimately, though, some recognition of non-formal education could support smoother transitions into lifelong learning.

Action 5: Promote entrepreneurship through formal educational institutions

In 2017, GoG adopted the Unified Strategy of Education and Science 2017-2021 and action plan in an effort to promote entrepreneurship and lifelong entrepreneurial learning. The action plan includes the introduction of entrepreneurial education at all education

levels, strengthened by the establishment of FabLabs in 14 colleges to support entrepreneurial innovations and the creation of start-ups. Several start-up projects have since been developed and implemented by VET students and graduates in these Fablabs. Under the umbrella of the MoES, an interagency working group has also been created with the purpose of implementing lifelong entrepreneurial learning in the education system.

Moreover, Enterprise Georgia created a university-private sector partnership platform in order to submit modification suggestions to educational programmes aimed at better meeting the requirements of companies operating in two pilot sectors, ICT and architecture & design.

Additionally, Entrepreneurial Clubs hosted by VET colleges in pilot regions aim to contribute to a smooth transition between education and the workplace. These clubs organised a series of events seeking to inspire young people by, for instance, inviting self-employed IT specialists to speak with and mentor students, encouraging them to create their own business ventures.

Action 6: Support women's entrepreneurship

The government has taken initial steps within the framework of the SME strategy to support women's entrepreneurship. The creation of a sub-council for women's entrepreneurship under the Private Sector Development Advisory Council in early 2018 lays the ground for establishing an institutional framework to support the promotion of women in business in Georgia and gradually close the gender gap in entrepreneurship. Moreover, the main implementing actors of the SME strategy have taken steps across several ongoing projects to support women-led businesses.







In 2016-2017, GITA was involved in the project "Strengthening Women's Entrepreneurship", including a visit of 200 women to the Technopark and an introduction to the possibilities and support offered to women entrepreneurs by GITA.

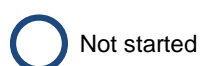
Enterprise Georgia introduced some preferential treatments for women in the selection process for the Micro and Small Business Support programme under *Produce in Georgia*: in case of limited resources, when two SME businesses, one led by a women and the other by men, apply for financial support and fulfil the same criteria, the women-led venture will be chosen over the men-led one. Women entrepreneurs amount to 40% of the programme's beneficiaries.

Geostat has recently begun publishing gender-disaggregated business statistics, including data on business ownership, wages and creation of new enterprises. In 2016, for instance, women represented 31% of new business owners, compared to 55% of men.⁸ This picture nearly mirrors the gender gap in the employment rate, which stood at 14 percentage points – women's employment rate represented 50.8% compared to 63.4% of men in the same year (Geostat, 2017).

⁸ 13% of respondents did not provide information about their gender.

Overview of the monitoring assessment

Overall 2015 recommendation	Detailed 2015 recommendations	2018 monitoring assessment – progress status
Develop countrywide labour market and training needs analysis	<ul style="list-style-type: none"> Perform regular countrywide labour market analyses Set up framework for training needs analysis 	
Strengthen stakeholder participation in developing and implementing VET policies	<ul style="list-style-type: none"> Involve employers in curricula design Set minimal standards for technical infrastructure of VET schools Strengthen SME participation and SME-VET cooperation 	
Improve the quality and attractiveness of VET institutions	<ul style="list-style-type: none"> Capacity building/training for teachers Involve professionals in VET teaching Career guidance/counselling in secondary schools Track graduates' career paths to evaluate VET system 	
Facilitate SME access to non-formal training	<ul style="list-style-type: none"> Set up stakeholder committee on SME training Consider financial support for lifelong learning/non-formal training 	
Promote entrepreneurship through formal educational institutions	<ul style="list-style-type: none"> Promote self-employment as a career option, include entrepreneurship in secondary school curricula Match entrepreneurial education with financial support for student-led ventures 	
Support women entrepreneurship	<ul style="list-style-type: none"> Base policies on gender-disaggregated business data and analysis. Set up gender-sensitive entrepreneurship training Establish a national commission on women's entrepreneurship 	



Not started



Initiated



Being implemented



Close to completion



Completed

Suggested key performance indicators and way forward

To better assess the progress made in developing skills and entrepreneurial culture in Georgia, the following KPIs could be considered:

Table 3. KPIs to monitor skills development and entrepreneurial culture

KPI	Description/rationale	Source of data
Indicators of student participation in VET	On the input side of the labour market, administrative data on VET could be used to measure the results in terms of the skills provided by the education system to SMEs as employers. Depending on the objectives, possible indicators could include number of students in VET compared to general secondary education/higher education, share of VET students in priority fields of study, or share of female VET students, employability of VET graduates.	VET students' database
Share of new enterprises established by women	This indicator would help monitor progress made to encourage female entrepreneurship.	Geostat
Share of respondents identifying "Inadequately educated workforce" as most problematic factor for doing business	Inadequately educated workforce is often ranked as one of the most problematic factors for doing business in Georgia, based on a survey of local enterprises. This survey is carried out annually and it would be of interest to observe the evolution of responses over time.	WEF Competitiveness Report

Way forward

Promote women's entrepreneurship

Considering the relatively low share of new enterprises created by women and their reduced willingness to take entrepreneurial risk in comparison to men⁹, more effort seems to be required to further develop targeted policies to seize the potential of women's entrepreneurship across the country.

The creation of a sub-council for women's entrepreneurship promotion within the Private Sector Development Advisory Council should be welcomed as an important step in this direction. However, the Government could go a step further and consider increasing the institutional reach of the sub-council by reporting on progress achieved and discussing priorities for the future with the Gender Equality Council of the Parliament of Georgia.

Furthermore, a separate Action Plan on promoting women's entrepreneurship could be designed, taking inspiration from recent OECD work, which specifies five main ways that

⁹ In 2014 (latest available data), only 26.7% of women thought they had sufficient capabilities and skills for starting a business, compared to 43.3% of men; in 2016, the female/male early-stage entrepreneurial activity ratio (% of women who are nascent entrepreneurs/owners of a new business, divided by the equivalent percentage for male counterparts) stood at 0.6 (Lezhava et al., 2014; GEM, 2016).

policy can address the gender gap in entrepreneurship (Box 4). While elaborating the action plan, it is important to keep in mind the institutional context affecting woman entrepreneurs in terms of motivations and resources. Removing barriers to women's entrepreneurship at the source, for instance by encouraging women to go into STEM (i.e. science, technology, engineering and mathematics) fields, should be considered a priority.

Overall, a multitude of activities is currently being carried out in order to promote skills development and entrepreneurial culture in Georgia. Therefore, before starting to consider a further set of policy actions, the government should focus on the implementation, monitoring and evaluation of the various activities underway and effectively assess their impact.

Box 4. How can policy support women entrepreneurs?

OECD Policy Brief on Women's Entrepreneurship

1. Improve the institutional conditions. Entrepreneurs are strongly influenced by role models and social context. It is therefore important to promote women entrepreneurs as role models and ensure that the education system does not discourage women from going into STEM fields. Another aspect is family and tax policies, which should seek to increase female labour market participation and female entrepreneurship.

2. Improve access to entrepreneurship skills programmes. Traditional policy action that supports the acquisition of entrepreneurship skills include training, coaching and mentoring programmes, and support in building entrepreneurial networks. Such programmes can be tailored to the specific barriers faced by women and delivered to women-only groups of beneficiaries.

3. Increase the use of loan guarantees. Most government policies to improve access to finance for women entrepreneurs focus on interventions that provide grants, loans, and microcredit. A growing trend is to improve access to bank financing through loan guarantees. Evaluations of women-specific loan guarantees in Canada suggest that they create more jobs than mainstream programmes, while programmes in European Union countries also tend to show positive impacts.

4. Help women realise the growth potential of their businesses. There is a growing emphasis in entrepreneurship policy to help women develop the skills needed to successfully launch and run businesses with high growth potential. One approach is to deliver tailored support through women-only business incubator and accelerator programmes. Experience in the US suggests that dedicated incubators can be more effective than mainstream ones, which rely on male-centric networks, fail to reach out to women's networks, select entrepreneurs through male-dominated selection panels, offer gender-insensitive programmes that do not address the needs of women.

5. Improve access to risk capital for women entrepreneurs. Both venture capital and angel investment markets are male-dominated and investments tend to be concentrated in male-dominated sectors. Experiments in the United States show that investors are 60% more likely to invest in male entrepreneurs, even when the content of investment pitches is the same, which suggests that women entrepreneurs pitching to investors can expect a lower chance of success because of their gender. Options for gender rebalancing include attracting more women investors and advisors as part of traditional venture capital and angel networks, and forming women's venture capital funds led by women and specifically directed at investment in women-owned enterprises. Support may be forthcoming from public policies that encourage the formation of women-focused venture capital investments – by, for example, offering matching funds for investment in women-owned or women-led start-ups, early-stage and expansion-stage ventures.

Sources: OECD Policy Brief on Women's Entrepreneurship (2016); 5 ways policy could close the gender gap in entrepreneurship (World Economic Forum; 2017)

Chapter 4: Support SMEs' internationalisation

Findings of the 2018 assessment

Action 1: Improve export promotion activities and export-related skills among SMEs

Since approval of the SME Development Strategy 2016-2020, Enterprise Georgia has identified a number of priority markets and (sub-) sectors with high export potential, based on consultations with the private sector, revealed competitiveness and increasing demand for Georgian products. The markets include China, USA, Japan, UAE, Saudi Arabia, Germany, France, Italy, Poland, Great Britain, Norway, Sweden, Latvia, Lithuania, Estonia, Denmark, Czech Republic, Hungary, Netherlands and Switzerland. The sectors considered having the highest export potential are food, beverages, light industry, ICT, business consulting, architecture and design.

Enterprise Georgia has further worked on developing new tools to support SME export promotion. Of particular interest is the export readiness test, which assesses the marketing abilities and competencies of the company to access foreign markets. With the help of such tool, the agency identified eight companies with high export potential and supported them in starting to export to the Baltic countries and Poland.

Additionally, Enterprise Georgia developed and launched export management courses, which to date have enabled up to 140 companies to strengthen their export skills and increase their readiness to access foreign markets. Beneficiaries of the agency can also participate in free-of-charge masterclasses on topics such as branding, PR, selling in Europe, project planning and implementation, IFRS and business management. Since April 2018, eleven masterclasses have been organised with the participation of more than 700 beneficiaries, with a rapidly increasing demand.

A significant effort has been made to help Georgian enterprises establish international trade relations. The involvement of Enterprise Georgia, GITA and the Georgian Chamber of Commerce and Industry (GCCCI) with the Enterprise Europe Network (EEN) has offered a number of opportunities to introduce Georgian SMEs to foreign markets. As a first step, two information days were held in 2017 to raise awareness of SMEs and start-ups on EEN possibilities, including information on technical requirements to export and business opportunities in Europe. Following that, new SMEs with high export potential were registered on the EEN platform and as a result, over 30 Georgian companies have received business offers from European companies, with three successful partnership agreements and five of them being in the negotiation process to start co-operation.

In parallel, Enterprise Georgia, in co-operation with GIZ, co-financed by the European Union and on behalf of the German Government, is active in supporting SMEs in sectors such as furniture, apparel, film/post-production and ICT, by implementing a cluster approach in order to meet the quality and quantity demands of international markets. Three of the abovementioned clusters, excluding apparel, are registered formally.

Moreover, the agency upgraded its *Tradewithgeorgia* website, offering comprehensive information on export-oriented Georgian companies to interested foreign buyers.

GCCI is another actor that has worked to introduce Georgian SMEs to foreign markets. The Chamber organised six business forums abroad as well as 14 forums and two fairs in Georgia throughout 2016 alone. Alongside the EU market, the Chamber is involved in the promotion of the “Belt and Road Initiative”, collaborating on several occasions with China. Examples of these bilateral projects include the custom warehouse in the city of Yiwu where Georgian goods are stored, the creation of 10 “Georgian Houses” in China and the soon to be opened Silk Road Information Centre in Georgia.

Action 2: Provide services to SMEs to adapt to DCFTA requirements

While the Government of Georgia is involved in the process of transposing EU regulations and standards, lack of knowledge about the standards and requirements needed to access the single market curbs the willingness of Georgian SMEs to export to the European Union. To improve this situation, and with co-financing from the European Union and on behalf of the German Government, GIZ has assisted GCCI in establishing DCFTA information centres in four Georgian regions, with the goal to raise awareness regarding the main provisions of the EU-Georgia Association Agreement and support SMEs in adapting to new legislative changes.

The DCFTA centres provide information on perspectives and requirements to export to the EU, including information on measures taken by the Georgian government to approximate European standards, good practices to access foreign markets and information on grant programmes available to exporting companies. The centres also carry out regular awareness raising campaigns and trainings, based on the needs of local entrepreneurs identified through face-to-face interviews and surveys. In addition to physical centres, MoESD and GIZ launched the web-portal dcfta.gov.ge, including a specific DCFTA for Business page, where interested stakeholders can find all abovementioned DCFTA related information.

Moreover, regular public-private roundtable discussions dedicated to the DCFTA implementation process are being conducted throughout the country. Carried out with the support of the EU-funded project “Facility for the Implementation of the Association Agreement”, the roundtables discuss challenges and opportunities of the DCFTA, with an ultimate aim to improve the competitiveness of SMEs on the EU internal market. To further involve the civil society in the implementation process of the agreement, MoESD established a DCFTA Advisory Group, which is proving to be a successful consultation platform to bring together GoG representatives with employers’ and business associations, trade unions and NGOs.

In addition, Enterprise Georgia and the MoESD are conducting DCFTA-related advisory services and trainings throughout the country. By end of 2017, more than one thousand SMEs participated in DCFTA-related discussions. Frequent trainings and seminars are also carried out in various governmental institutions, such as the Competition Agency, the Revenue Service and the Georgian National Agency for Standards and Metrology, building capacity of government staff on DCFTA requirements.

Action 3: Provide targeted financial support to exporting SMEs

The SME strategy Action Plan 2016-2017 did not include specific actions aimed at providing targeted financial support to exporting SMEs. However, Enterprise Georgia

provides some help, co-financing 70-80% of SMEs' costs of participation in trade fairs, international conferences and trade missions; additionally, a few major banks offer a narrow choice of trade finance instruments, including guarantees and letters of credit, but these are mostly taken up by larger firms.

Only 23% of SMEs directly exported in 2017, hampered as they were by difficult access to trade finance, which appears to be one of the most problematic factors for exporting, as reported by business executives (GeorgiaDCFTA, 2017; WEF, 2016). Limited availability and lack of awareness of trade finance instruments hinder further internationalisation of Georgian SMEs, an obstacle that could be removed by providing targeted financial solutions for exporting companies.

Action 4: Facilitate linkages between FDI and SMEs

In 2017, Enterprise Georgia, in co-operation with a UK-based consultancy, initiated a pilot project funded by the UK Department for International Development aimed at fostering linkages between multinational corporations (MNCs) operating in Georgia and local SMEs.

The project selected two sectors, hospitality and manufacturing, as most promising due to growth in both tourism and manufacturing and the high potential for creating and expanding linkages. The project is organised around three phases:





Assessment of demand-side companies in the chosen sectors, identifying MNCs already operating in Georgia, but also franchises (McDonalds, Wendy's, The Coffee Bean & Tea Leaf etc.). Information will be stored in a company database with details on location, business indicators and activities.

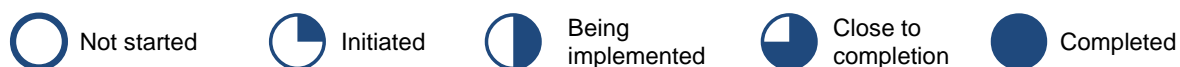
Pilot phase in the hospitality sector. The main goal will be to match SMEs with MNCs, especially targeting procurement managers, and based on a thorough business review of SMEs including an audit of skills and technology, and an initial training for SMEs to conduct business negotiations with MNEs.

Full transfer of methodology from the consultancy to Enterprise Georgia and roll-out plan to the same or other sectors.

The sustainable continuation of this project is a central focus of the SME strategy's Action Plan 2018-2020, with an aim to expand the linkage programme to other sectors in the future based on the results of the pilot project in the hospitality sector.

Overview of the monitoring assessment

Overall 2015 recommendation	Detailed 2015 recommendations	2018 monitoring assessment – progress status
Improve export promotion activities and export-related skills among SMEs	<ul style="list-style-type: none"> • Provide information on priority sectors and target markets for SMEs • Offer market research and trade information • Develop SMEs' export skills • Support SMEs to develop clusters with regional and industrial business partners 	
Provide services to SMEs to adapt to DCFTA requirements	<ul style="list-style-type: none"> • Provide information and training on technical regulations, standards and accreditation • Build capacity in government agencies 	
Provide targeted financial support to exporting SMEs	<ul style="list-style-type: none"> • Make suitable financial and insurance products available 	
Facilitate linkages between FDI and SMEs	<ul style="list-style-type: none"> • Establish FDI-SME linkage programmes • Match foreign investors with local SMEs 	



Suggested key performance indicators and way forward

A multitude of performance indicators could be used to track the progress of SME internationalisation in Georgia. Some data is already easily accessible through Geostat, others would require linking different data sources, but the KPIs below could be a start:

Table 4. KPIs to monitor SME internationalisation

KPI	Description/rationale	Source of data
Annual growth rate of SME exports	External merchandise trade data by size of enterprises is available on Geostat since October 2018, linking external trade data with data from the Georgian business register to characterise the volume of exports by size of enterprises.	Geostat
Share of exporting SMEs	This indicator could be used to monitor SME internationalisation by looking at the share of SMEs that receive at least some revenues from abroad by exporting their products or services. Several thresholds could be looked at to consider a company as an "exporting SME" i.e. revenues from abroad >0%, >= 50% of total.	Geostat
Share of exports to the EU and OECD countries in total exports	This could be a very useful indicator to measure improvement in product quality and compliance with international, and especially EU standards. To date, this data is not available with breakdown by enterprise size class (with detail of SMEs) yet, but the aggregate level taking all firm sizes into consideration could already offer an estimate of general improvement and compliance over time.	Geostat

Way forward

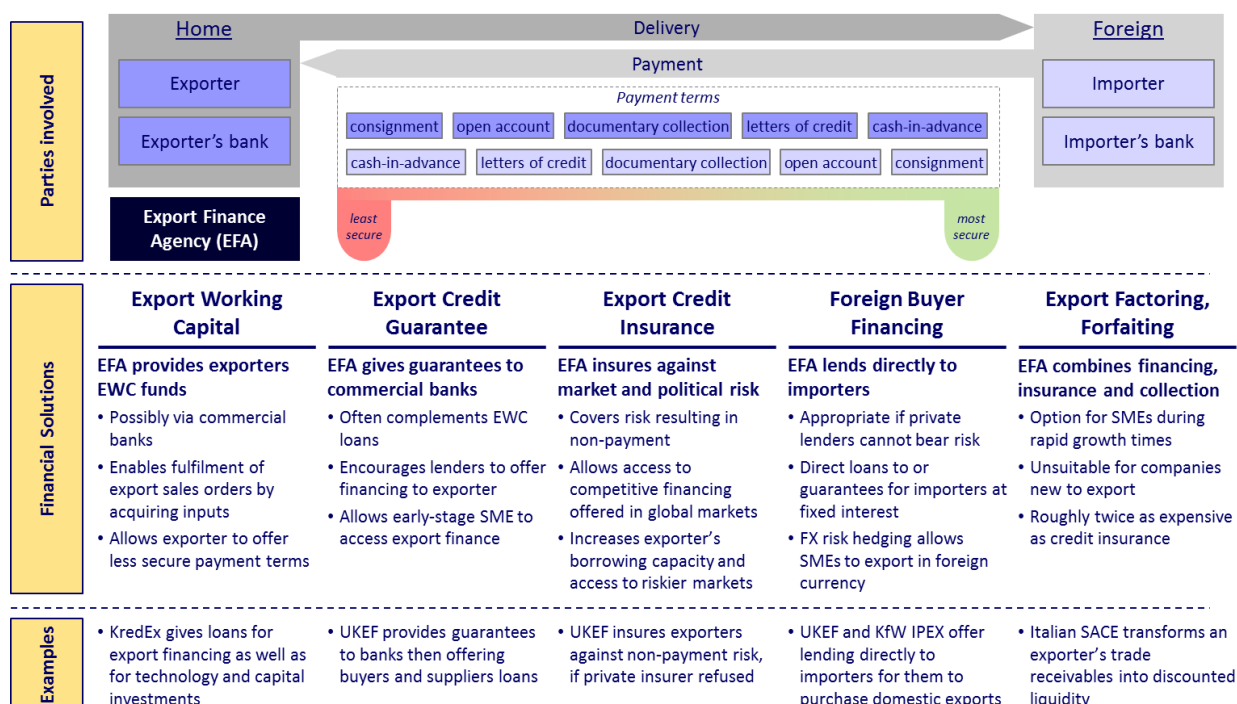
Consider providing targeted financial support to exporting SMEs

To further develop SME internationalisation, the government could consider providing additional targeted financial and insurance support to help SMEs overcome the financing barriers to exporting and the risks encountered, such as longer cash-flow cycles, physical distance from buyers and currency risk, when engaging in international trade.

As a first step, consultations among government, financial institutions and exporting SMEs should be held regularly, as well as surveys carried out, in order to identify specific barriers and needs for further internationalisation. Depending on the needs identified among Georgian SMEs, financial solutions could include export loans to finance additional working capital, export credit insurance to cover market and political risk, as well as export factoring to convert exporters' trade receivables in discounted liquidity (Figure 7).

Awareness raising campaigns promoting the availability of SME targeted trade finance instruments, as well as export-related finance and insurance skills trainings such as export risk management, should be considered an integral part of the proposed financial solution.

Figure 7. Trade finance solutions



Source: (OECD, 2016b).

Promote SME internationalisation through cluster development

To improve competitiveness of Georgian SMEs and to help them reach and succeed in the EU market, the GIZ SME DCFTA project currently supports more than 150 Georgian SMEs, benefitting more than 1000 employees by promoting the formation of clusters in four sectors: furniture/interiors, apparel, film production and ICT. Clusters can increase productivity, contribute to more rapid innovation and new business formation through co-operative research, sharing knowledge and infrastructure, and optimising costs in accessing inputs, marketing and distribution.

This initiative offers promising signs, with strong interest from government stakeholders and entrepreneurs. Three clusters have already been formally registered, with a management structure in place; five apparel companies are in negotiations with potential EU buyers and a first joint product of furniture producers and interior designers has been featured at international fairs (GIZ, 2018).

As a next step, a Georgian National Cluster Programme (GNCP), with dedicated government funding and an established management mechanism could support cluster development in additional sectors and increase the competitiveness of Georgian SMEs. In November 2018, the EU and the Government of Georgia agreed on next programme steps to further enhance economic and business development in Georgia, including the implementation of such a programme by 2021. A roadmap for the GNCP has already been developed by MoESD and key stakeholders, with the support of the GIZ SME DCFTA project.

Chapter 5: Facilitate SMEs' innovation and R&D

Findings of the 2018 assessment

Action 1: Amend the legal framework for innovation

In 2016, in order to create a supportive environment for innovation in the country, Georgia substantially amended the Law on Innovation, allowing public universities and research centres to own shares in spin-off companies and to commercialise their inventions and intellectual property rights generated through publicly-funded R&D. The Law provides for the creation of a comprehensive innovation infrastructure, including Technology Parks, business incubators and accelerators, an Innovation Centre delivering trainings on entrepreneurship and ICT skills, as well as FabLabs, to foster innovative activity throughout the country (GoG, 2016).

In addition, in 2017, the Parliament adopted amendments to the Law on Public Procurement, which introduced the principles of proportionality and equal treatment in a public tender process, thus removing obstacles to SME participation. In line with the principles of the Small Business Act for Europe, the law also includes the possibility of using e-procurement, which widens SMEs' access to information on procurement opportunities. The increased involvement of SMEs in public purchasing is likely to result in greater competition for public contracts, leading to better value for money for the procuring entities and more innovative approaches to contracting. The Law also specifies that preference should be given to performance and functional criteria when drawing up tender requirements, thus encouraging suppliers to deliver contracts in a more efficient and innovative way (GoG, 2018). However, more could be done to ensure innovation through public procurement.

As a complement to legislative improvements, Geostat and GITA have taken substantial steps to collect data on ICT use by households, individuals and enterprises, as well as on innovation activity in enterprises. The first surveys were conducted in 2016, resulting in three publications (on ICT access and use by households and individuals; ICT use by enterprises; and innovation activities in enterprises) and are to be replicated annually. As a next step, Geostat is considering breaking down the data on ICT usage by enterprise size.

Action 2: Foster collaboration between industry and academia

Collaboration between industry and academia has mainly been explored in the context of commercialisation of innovation and R&D projects. In 2015, the Massachusetts Institute of Technology (MIT) carried out a technology assessment of Georgian research institutes to understand their capabilities and explore their needs. The assessment aimed, among other things, at raising awareness of the institutes' research and administrative staff about new opportunities for co-operation with industry and motivating staff to commercialise in-house research. The assessment led to the selection of 13 out of 96 projects elaborated by the research institutes' staff, including recycling of waste materials, automobile fuel

cleaning, radiation safety devices and others, to be developed based on their commercial attractiveness.

Additionally, GITA has compiled a database of existing research institutes and research staff, which currently includes 70 scientists/representatives of research institutes. On this basis, GITA is planning to analyse the scientific potential of Georgia with a view to form innovation clusters in IT, e-commerce, biotech and plastics in light of a future commercialisation of business ideas. GITA could also further leverage the Enterprise Europe Network (EEN) to contribute to technology transfer in the country: by providing international business expertise with local knowledge on innovation and technology transfer, the EEN also aims to identify potential international research partners and supports the information exchange on innovative processes and tools in various sectors.

Overall, the innovation support infrastructure could be further developed: the scarcity of business incubators, accelerators and technology transfer offices, especially outside Tbilisi, does not allow for effective diffusion of innovations across the country. A first step has been made by GITA, which developed an action plan to establish a National Technological Transmission Office, with the aim to commercialise Georgian innovative products and support their export to foreign markets. This will be achieved by fostering innovation through research collaboration between academia and industry, evaluating the commercial potential of an innovation, and licensing of new technologies and inventions to selected industry partners. With donor support, the implementation is to begin in 2019.

Action 3: Consider providing financial support to SMEs for innovative activities

GITA is the main institution tasked with providing financial support for innovation in Georgia. Throughout 2016-2017, three schemes have been developed to this purpose: the Micro Grants, the Start-up Georgia and the Matching Grants programmes.




The Micro Grants Programme, launched by GITA in 2016, offers up to GEL 5 000 (~ EUR 1670) to support entrepreneurs with funds for developing prototypes within the GITA infrastructure, participating in fairs and innovation competitions. Since the inception of the programme, GITA received 350 applications, with grants distributed to more than 200 applicants. The Start-up Georgia Programme has a total budget of GEL 35 million (~ EUR 11.7 million), with GEL 11 million (~ EUR 3.7 million) disbursed in 2016 for the first round of the project. This programme issues grants of up to GEL 100 000 (~ EUR 33 000) to develop a business model and go-to-market strategies for their products. In the framework of the World Bank GENIE (Georgian National Innovation EcoSystem) project, GITA announced the launch of the Matching Grants Programme in 2018, with the objective to stimulate innovation and create innovative enterprises through product/service, process and technology development, adoption and commercialisation. This year, GITA already financed 17 start-ups with up to GEL 100 000, including a 10% co-financing component.

GITA complements its financial support with training, coaching, mentoring and consulting services for all programme beneficiaries. A specialised training on developing innovative business skills has recently been created and is being delivered throughout the country. Trainings on coding, robotics, intellectual property, digital marketing and export-oriented ICT skills are also regularly carried out on the premises of various innovation centres in Georgia's regions, registering currently over 1000 beneficiaries.

Lastly, GITA has contributed to the drafting of a new Law on Crowdfunding as an alternative way for businesses to collect financial resources for innovative ventures. The draft law is currently under revision by the NBG.

In 2016, Georgia has also joined Horizon 2020, EU's framework programme for research and innovation, which provides funding for developing scientific and innovation capacity of all programme partners, including research institutes, universities, individual researchers and SMEs. To date, the EU contributed EUR 2.5 million and counts 27 participants, with an objective to expand activities in the coming years.

Overview of the monitoring assessment

Overall 2015 recommendation	Detailed 2015 recommendations	2018 monitoring assessment – progress status
Amend the legal framework for innovation	<ul style="list-style-type: none"> Facilitate commercialisation of university-based research and innovation among SMEs Foster local competition Design policies to enforce IP rights for SMEs Assess opportunities to stimulate R&D and innovation among SMEs through demand-side policies 	
Foster collaboration between industry and academia	<ul style="list-style-type: none"> Increase awareness of research capacities among SMEs Establish joint research initiatives between SMEs and public research institutes Promote commercialisation of public R&D efforts 	
Consider providing financial support to SMEs for innovative activities	<ul style="list-style-type: none"> Design targeted financial instruments to support innovation Financial support for start-ups Use synergies with other instruments 	



Not started



Initiated



Being implemented



Close to completion



Completed

Suggested key performance indicators and way forward

Building on Geostat's dedicated survey of ICT and innovation activities, the indicators below could be used to track progress of SME's innovation efforts in Georgia:

Table 5. KPIs to monitor SMEs innovation and R&D

KPI	Description/rationale	Source of data
Share of SMEs introducing product innovations	Companies' introduction of a new or significant improved good or service is a very informative indicator of innovation activities. Data is currently presented at aggregate level, but information about number of employees is collected during the survey, allowing for breakdown of results by enterprise size class in the future.	Geostat
ICT usage for commercial purposes by SMEs (share of SMEs using e-invoicing, e-procurement, e-sales)	Indicators about business-related ICT use by SMEs could be built using the information collected in the annual dedicated Geostat survey.	Geostat

Way forward

Establish a strategic framework and improve instruments to foster SME innovation

Amendments to the legal framework and a large spectrum of activities, including providing financial support to innovative firms, have been carried out over the last three years by GITA and other stakeholders, to support business innovation throughout the country. A more co-ordinated approach could be achieved by designing a comprehensive medium-term strategic framework on innovation, with a focus on the SME sector.

One of the priorities to be reflected in the future innovation strategy is the development of the overall innovation infrastructure, especially outside Tbilisi and in rural areas, which is currently lagging. A special focus should be put on establishing a Technology Transfer Office (TTO), crucial for the movement of know-how, skills and technical knowledge from research institutions and universities to companies, thus bridging the gap between research and innovation and contributing to generate economic value.

As a go-to office dedicated to fostering and diffusing innovations, the TTO could take up various specific roles, ranging from simply establishing relationships with firms, through providing assistance in areas related to e.g. intellectual property, to facilitating the formation of university-connected companies using public research organisations' technologies. (OECD, 2011)

Moreover, on the basis of the amended Law on Public Procurement, and to ensure SME innovation potential through this process, Georgia could consider leveraging the six principles based on the OECD Recommendation of the Council on Public Procurement (Box 5), which would further align Georgia to international good practice (the principles on e-procurement and legal access for SMEs to public bids are already reflected in the current law).

In addition to the financial support currently in place, expenditure-based R&D tax incentives specifically for young companies could be introduced. Targeting young companies could help them challenge incumbent businesses and generate

disproportionately more jobs. Moreover, compared to other direct subsidies, support programmes or grants, R&D tax incentives allow firms to decide about the nature of their innovative activities. However, a close monitoring and evaluation of tax incentives should be ensured, demonstrating the effectiveness of such incentives and assessing the potential distortions of competition between incumbents and new entrants to the market.

Box 5. Six OECD principles on Public procurement for innovation

According to the OECD Recommendation of the Council on Public Procurement, the six following principles are particularly important and could be leveraged specifically to support procurement for innovation.

- 1) Access.** Access for all, and in particular SMEs, is essential to conducting procurement for innovation. Often, rather than established companies, creative newcomers are the source of innovative solutions. The OECD recommends that countries ensure that companies of all sizes can participate in bids. This is essential for countries wishing to encourage innovation, because red tape presents barriers particularly for small companies that might supply an innovative solution.
- 2) Participation.** It is of crucial importance to maintain open channels of dialogue, both with potential suppliers as well as with the beneficiaries of innovation, and allow for the participation of all relevant stakeholders. This principle advocates for transparent and regular dialogues, which can be leveraged for innovation generation.
- 3) Capacity.** Procurement for innovation requires specialised knowledge of public procurement staff, including an understanding of technical specifications to make informed strategic decisions and conduct a relevant and appropriate market analysis. Regular training, knowledge exchange with research institutions and a reward system for picking innovative solutions should be put in place to further encourage innovation.
- 4) Evaluation.** Ex-post evaluation is an important part of the process, as it will analyse if the innovative solution yielded better results than a more traditional solution. The OECD therefore recommends evaluating public procurement processes and systems, with a view to measuring effectiveness of innovative approaches. In addition, reliable information and data should be collected to guide future procurement decisions.
- 5) Risk management.** It is crucial to have an accurate understanding of the risks associated with a new solution (in contrast to the traditional solution), and take appropriate steps to mitigate risk. A sound risk management could include a higher risk tolerance in procurement for innovation cases, clear and open reporting structures to allow and early response to risks that materialise and guidelines on how to deal with “risky situations” in connection with innovations.
- 6) E-procurement.** The support of public procurement through electronic means represents a major breakthrough in recent years and an innovation in many countries, which can have benefits for innovation as well. E-procurement increases access and therefore competition amongst bidding enterprises by simplifying procedures. Innovative companies often have less capacity to participate in public procurement processes and e-procurement can be a lever to encourage their participation.

Source: Public Procurement for Innovation: Good practices and strategies (OECD, 2017)

ANNEX A – Overview of suggested monitoring KPIs

Table 6. Suggested result-oriented KPIs to monitor Georgia’s SME Development Strategy

KPI	Unit of measure	2015	2016	2017	Source of data
Institutional environment for SMEs					
Annual growth of investment by SMEs	%	-9.3	21.8	-	Geostat
Total early stage entrepreneurial activity	%	8.6	-	-	Global Entrepreneurship Monitor
Share of early stage entrepreneurs motivated by opportunity	%	-	48.9	-	Global Entrepreneurship Monitor
Resolving insolvency indicator (distance to frontier)	index	36.48	40.24	40.02	World Bank Doing Business
Access to finance for SME					
Annual growth rate of loans to SMEs	%	-	20	26	National Bank of Georgia
Average interest rates for loans to SMEs	%	13.7	12.6	12.2	National Bank of Georgia
Interest rate spread (SMEs - large firms)	percentage points	3.1	2.9	3.0	National Bank of Georgia
Percentage of firms citing access to finance as one of the “most problematic factors for doing business”	%	13.6	13.2	12.0	WEF Global Competitiveness Report
Skills development and entrepreneurial culture					
Number of VET students	number	-	-	-	VET students’ tracer study by MoES ¹⁰
Employment rate of VET graduates (1 year after graduation)	%	-	-	-	VET students’ tracer study by MoES ¹⁰
Share of new enterprises established by women	%	32	32	-	Geostat
“Inadequately educated workforce” as most problematic factor to do business	rank	1	1	1	WEF Global Competitiveness Report
SME internationalisation					
Annual growth rate of SME exports	%	-	-1	-16	Geostat
Share of exporting SMEs	%	-57	-61	-55	Geostat
Share of exports to the EU in total exports	%	29	27	24	Geostat
Share of exports to OECD countries in total exports	%	35	35	30	Geostat
SME innovation and R&D					
Share of SMEs introducing product innovation	%	-	-	-	Geostat ¹¹
Share of SMEs using e-invoicing	%	-	-	-	Geostat ¹¹
Share of SMEs using e-procurement	%	-	-	-	Geostat ¹¹
Share of SMEs using e-sales	%	-	-	-	Geostat ¹¹

Note: growth rates are calculated using published nominal values of underlying economic variables.

¹⁰ The study is not publicly available, but information could be requested by MoESD to MoES.

¹¹ Geostat gathers information about innovation activities and company use of ICTs through a dedicated survey. Since the number of employees is collected as part of the survey, data by enterprise size class should be available upon request by MoESD to Geostat.

Part B - Assessment of the SME Strategy's Monitoring System and Targets

In response to a request from the government, the following section presents an assessment of Georgia's current system for monitoring the implementation and impact of the SME Development Strategy 2016-2020, including an analysis of its targets.

Assessment of the current monitoring system

Implementation monitoring

The Action Plan for the implementation of the SME strategy includes clear and relevant output indicators for each planned action. Many of these indicators are quantitative but target values are not set. The Annual Progress Report (APR) uses these indicators, complemented by a concise narrative account of actions taken, to assess progress with implementation. Costing of planned actions is partial and there is no reporting on actual costs of implementation.

Results monitoring

No result indicators have been developed for the SME strategy. The APR is focused on implementation of the Action Plan – that is, on whether the relevant institutions have accomplished their tasks, while the results (in terms of improvements in SME performance achieved through the implementation of the Strategy/Action Plan) are not considered.

Impact monitoring

The Strategy sets three targets (growth of SME output, employment and productivity). These targets are relevant and related to what the strategy aims to achieve. Therefore, they may be considered as indicators of the overall impact of the strategy. The APR reports the current values of the indicators. However, it is important to keep in mind that these targets could be achieved as a result of other factors, which are not necessarily linked to the fulfilment of the SME strategy objectives.

The description of indicators is not entirely clear and there are some methodological issues related to their calculation. There is no explanation how the targets were set and no analysis of past trends in these indicators. The baseline for indicators is 2013, which is unusual for a strategy that was approved in 2016. These issues are explored further below.

Data availability

The definition of SMEs was changed in 2017 to increase international statistical comparability and the data were recalculated back to 2006. Statistical data about the business sector in Georgia are regularly compiled by Geostat and the National Bank of Georgia. Business demographics statistics with breakdown by enterprise size class are a useful analytical source and readily accessible through the Geostat website. Breakdowns of interest rate and loan statistics by size of enterprises can be obtained from the National Bank of Georgia upon request. Since 2016, a survey on innovation activities and ICT usage in enterprises is also performed and results reported, but breakdowns by the size of enterprise are not published. Data on exports by enterprise size are available on Geostat since October 2018.

Statistical data on SME performance are based on enterprise surveys. Their accuracy will further improve in the future, because all enterprises are now legally obliged to report their annual balance sheets to the Service for Accounting, Reporting and Auditing Supervision (SARAS). Obligatory reporting will be gradually implemented over the next two years, and availability of financial statements data from the entire population of

enterprises will allow Geostat to compare this administrative source with survey data and significantly improve the reliability of business and economic statistics.

In addition, financial statements data will be an important source for analytical and research purposes and could be used for estimating effects of grants to SMEs using a micro-econometric approach.

Institutional arrangements

The implementation of the SME strategy is monitored by the High Level Coordination Group (headed by the Minister of MoESD) and a working group (headed by the Deputy Minister). The APR is prepared by the Department of Economic Policy of the MoESD based on reports received from implementing institutions. Implementation reports are discussed with stakeholders, primarily within the Private Sector Advisory Council of MoESD. An independent external assessment of progress with the strategy and the SME sector development in general was produced in January 2018 by ISET-PI.

Overall, the monitoring and reporting framework, coordinated by the MoESD, is well designed. The implementation reports are produced annually and not semi-annually as was foreseen in the Strategy.

Recommendations for improvement

Implementation monitoring

Monitoring of implementation of the action plan would improve if targets were set for quantitative indicators. Without targets, it is very hard to assess whether the level of implementation was satisfactory (“as expected”). The targets may be expressed in ranges, to allow for deviations due to unpredictable events (for example “10-20 trainings on DFCTA requirements held” or “at least 200 beneficiaries supported with measures to stimulate exports”).

The APR is already clear and well organised, but its communication value could be further enhanced by using some user-friendly presentational tools, such as the overview “heat-map” table suggested by the OECD Economic Reform Programme Monitoring Tool (OECD, 2018b).

Results monitoring

Result indicators should be developed for each strategic direction. These indicators should aim to show whether the expected results were achieved, such as increased annual growth rate of loans to SMEs or increased share of exports to the EU in total exports. Suggestions for result indicators for each strategic direction are proposed throughout this report at the end of each chapter. These are by no means exhaustive or prescriptive, and are intended to stimulate the search for most appropriate indicators by MoESD and implementing institutions.

It is recommended that the 2019 APR include a section reporting on the results (effects) of the SME strategy. This may be a pilot report, to be enhanced in 2020, the last year of the current Strategy. Reporting on results will facilitate revision and upgrading of the Strategy for the next period.

Impact monitoring

The clarity of presentation of the indicators and targets needs to be improved. Reporting on targets in the APR would greatly benefit from adding a narrative section that would compare the current values with past trends, put the changes in indicator values in the context of the overall economic cycle, and put nominal values in perspective by reporting on changes in the overall price level.

Institutional arrangements

Presentation of implementation reports to stakeholders is a good way to increase awareness of the actions taken to develop the SME sector and their results, and to receive valuable feedback and proposals for improvement of specific policy actions. Efforts could be made to assure that a wider and more diverse range of stakeholders participate in this dialogue, through e.g. online platforms, public-private roundtable discussions, including researchers, specialized journalists, and stakeholders at local level.

Analysis of targets

The table below presents the targets *as defined in the SME strategy*, and the latest available values as reported in the APR for 2017.

Table 7. SME Development Strategy's targets

Indicator	Target value (by 2020)	Current value
Growth of SMEs output	10% (annual average)	14.8% (average 2014-16)
Growth of number of employees in SMEs	15%	20.5% (in 2016)
Productivity growth	7%	19.6% (in 2016)

Note: Indicators as defined in the Strategy document approved by GoG (2013 as baseline)

Source: OECD (2016b), SME Development Strategy of Georgia 2016-2020

Definition of indicators

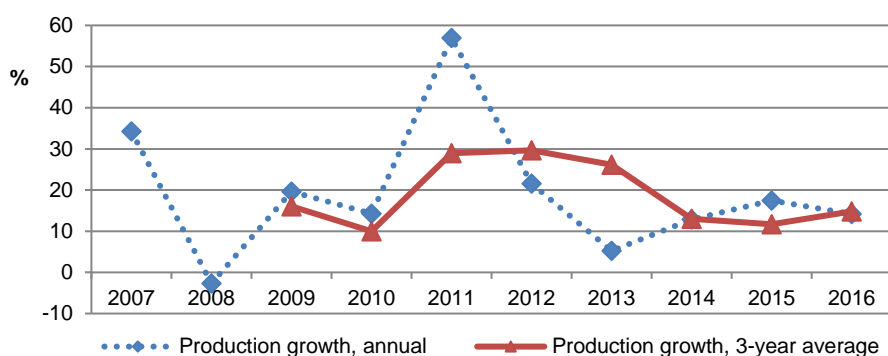
The definitions of indicators could be improved by providing explicit information on how values are calculated. Using data from Geostat on SME performance, the replication of calculations shows that the exact definitions of the indicators would be as follows:

- Average annual growth of production value of SMEs over the last three years
- Increase in the number of persons employed in SMEs since 2013
- Increase in productivity (value added per person employed) in SMEs since 2013

Setting ambitious and realistic targets

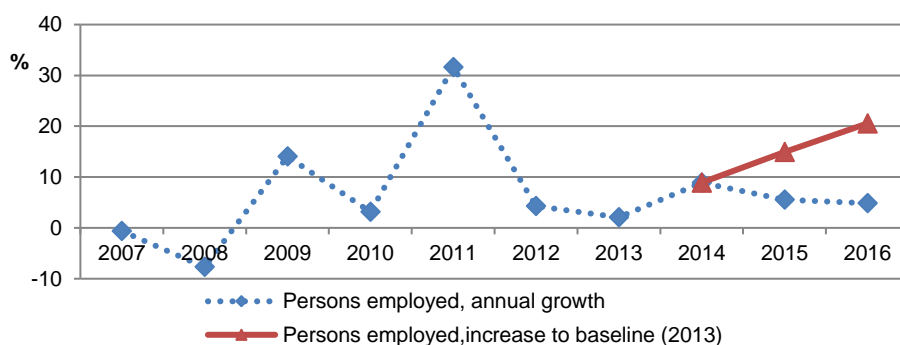
As evident from the values reported in the APR, the targets were already achieved in the first year of strategy implementation. This raises the question of whether the targets are sufficiently ambitious, or, on the other hand, whether further improvements in indicators are likely in the coming years.

The SME strategy does not provide information on how the targets were set, nor does it show an analysis of past trends of indicator values. To appreciate this, the charts below present the evolution over time (since 2007) for the underlying variables and values of indicators as defined above.

Figure 8. Production value in the SME sector

Source: OECD analysis based on data from Geostat

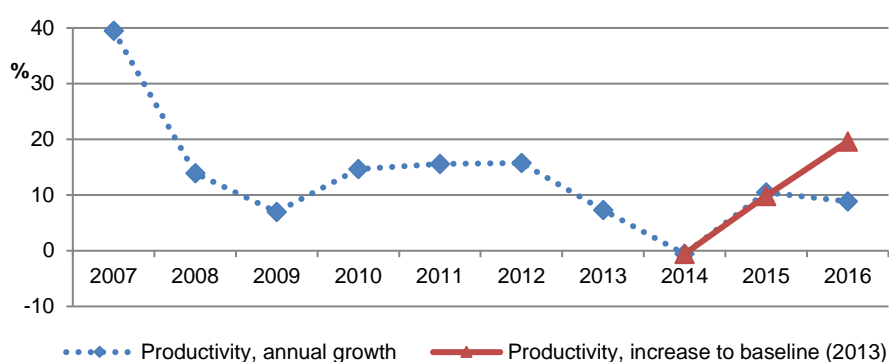
The value of the indicator (continuous red line) has been above the target over the entire period since 2007. This strongly suggests that a higher target could be set. However, based on quarterly data by Geostat for 2017, it is estimated that the growth of production value in 2017 was only 9.0%. This decrease may be due to cyclical factors, or to economic factors that work against sustainability of very high growth rates. If the latter is the case, then the target to keep the growth above 10% may be sufficiently ambitious.

Figure 9. Persons employed in the SME sector

Source: OECD analysis based on data from Geostat

The value of the indicator (continuous red line) is already above the target of 15%. The average annual growth rate of persons employed since 2012 was 5%; if this trend is sustained, the value of the indicator in 2020 will reach 46%. However, based on quarterly data by Geostat for 2017, it is estimated that the number of employed declined by 9.5% in 2017, reducing the value of the indicator to 9.1%. If this decrease is partly due to structural factors (i.e. it is not purely cyclical), then a target value between 20 and 25% may be sufficiently ambitious.

Figure 10. Productivity in the SME sector



Source: OECD analysis based on data from Geostat

The value of the indicator (continuous red line) is already above the target of 7%. It may be expected that, due to decline in employment, it has further increased in 2017. This strongly suggests that a more ambitious target for productivity could be set.

Overall, the charts above suggest that the targets could have been set at a higher level if the Strategy is expected to improve on past trends. It is therefore suggested to include a more substantive section on the targets in the next APR, comparing their current values with past trends and discussing how much the current performance is due to underlying cyclical and structural factors, and what was the likely contribution of the Strategy to improvements.

Instead of changing the targets, the baseline for calculation of indicators could be changed from 2013 to 2015, the last year before the approval of the Strategy.

Methodological issues

Production value or value added as an indicator of SME “output”?

Development strategies usually aim at increasing value added and not the production value. This is so because it is the value added that creates wealth and economic growth (growth of GDP is the sum of increases of value added in all economic sector, not the sum of increases in production). It is also generally considered that growth of value added reflects technological improvements, innovation and export competitiveness.

There is usually some discrepancy between the two indicators. For example, while the average annual growth of production value of Georgian SMEs in 2014-16 was 14.8%, the average growth of value added in the same period was 13.0%.

Nevertheless, focusing on production rather than value added may be justified in situations where a large share of SMEs is inactive or very small (micro) and operating in low value added sectors. For this reason, and to preserve the stability of the monitoring framework, it is not suggested to change the indicator at this point, but rather to consider using value added as the target for the next SME strategy after 2020. Nevertheless, it would be informative if the APR reported on developments in value added in addition to the value of production.

Persons employed or employees as an indicator of employment in SMEs?

Geostat provides two indicators for employment in the business sector. Employees are persons working for the enterprise on any kind of contract or agreement. In addition to this, the “persons employed” include also employed shareholders and employed family members.

It may be expected that the category of “employed” will be more sensitive to the economic cycle and the situation in the market for the enterprise’s goods and service. For example, while the increase in the number of persons employed by Georgian SMEs from 2013 to 2016 was 20.5%, the increase of the number of employees was only 13.5%. Similarly, the decline of the number of employed in 2017, as calculated from the quarterly data, was greater than the decline of the number of employees (9.5 and 7.1%, respectively).

There is no *a priori* reason to prefer one indicator over the other, but it has to be clear what is reported. The APR for 2017 speaks of “growth of the number of employees” but the figure reported is actually the figure for “growth of persons employed”. This should be more clearly reported in the future. Comparison between the two indicators (employees and persons employed) could also be informative.

Productivity indicator

Productivity of the business sector is usually measured as value added per employee. The APR calculation of productivity is indeed based on the value added, divided by the number of persons employed, which is consistent with the employment indicator.

Nominal or real values?

The targets for the production value and productivity (value added per person employed) are expressed and monitored in nominal values, that is, without adjustments for inflation.

Consumer prices in Georgia have increased by 9.5% from 2013 to 2016,¹² which suggests that real improvements in production and productivity of SMEs were considerably lower than suggested by nominal values of indicators (Geostat, 2018b). However, the choice of the most appropriate price index for deflating the indicators is a difficult methodological issue. It is therefore suggested to keep reporting on nominal values (and targets) but to put them in perspective by also providing information on overall price movements.

Summary

Target indicators are relevant and related to what the strategy aims to achieve. It is suggested to describe them more clearly, so that the method of their calculation becomes transparent. Target values set for 2020 do not seem very ambitious compared to past trends.

It is not recommended to amend the targets for the ongoing Strategy in order to preserve the stability of the monitoring framework. At the same time, reporting on targets in the APR would greatly benefit from adding a narrative section comparing current values with

¹² Based on the average annual consumer price index increase reported by Geostat.

past trends, put the changes in indicator values in the context of the overall economic cycle, and put nominal values in perspective against changes in the overall price level.

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MONITORING GEORGIA'S SME DEVELOPMENT STRATEGY 2016-2020

In 2015, the Government of Georgia embarked on an ambitious effort to improve the business environment and tackle market failures that make it harder for entrepreneurs and managers of small- and medium-sized companies to start, run and grow their businesses. The OECD supported these efforts, working with the Ministry of Economy and Sustainable Development to identify policy challenges and develop targeted measures to support Georgian SMEs. As a result of this work, the Government of Georgia was invited to a peer review under the auspices of the OECD Eurasia Competitiveness Roundtable in Paris in November 2015 which led to the subsequent adoption of Georgia's SME Development Strategy 2016-2020.

The first part of this Policy Insights monitors the extent to which the 2015 OECD recommendations have translated into actual policy reforms, identifies outstanding gaps, proposes a way forward and, most importantly, suggests result-oriented key performance indicators to assist the government in keeping track of the impact of current and future SME policy reforms. The second part presents an assessment of Georgia's current system for monitoring the implementation and impact of the SME Development Strategy 2016-2020, including an analysis of its targets. It also provides recommendations along three dimensions – implementation, results and impact – on how to further enhance the current monitoring system.

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