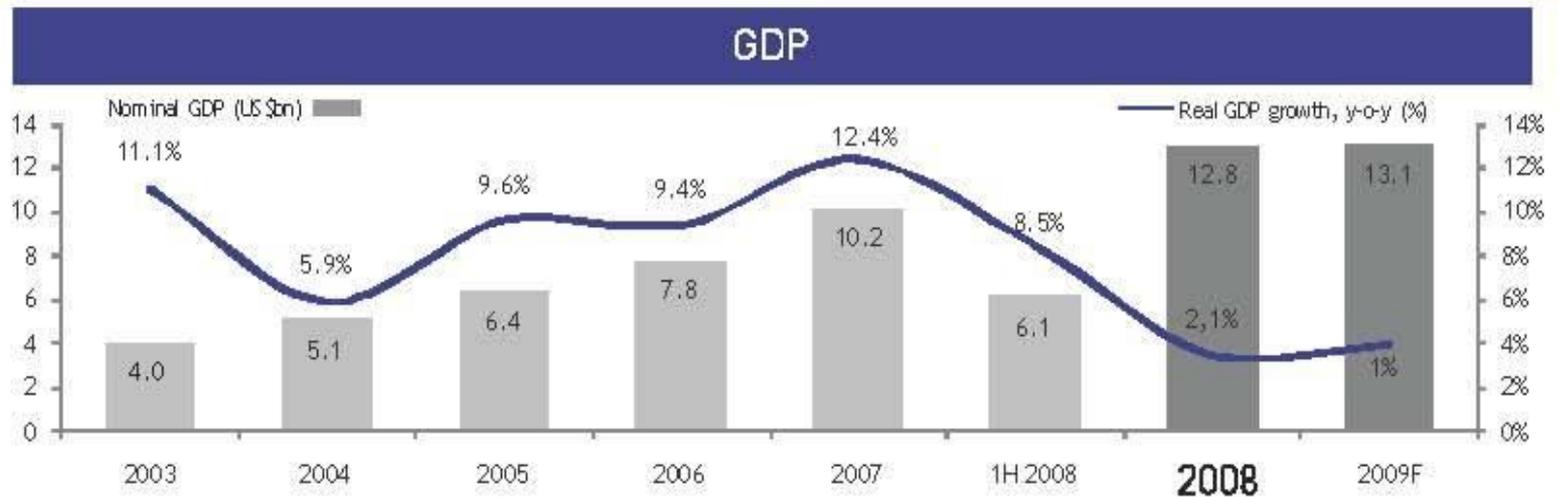


Impact of TwinCrises

Georgian Reform Agenda

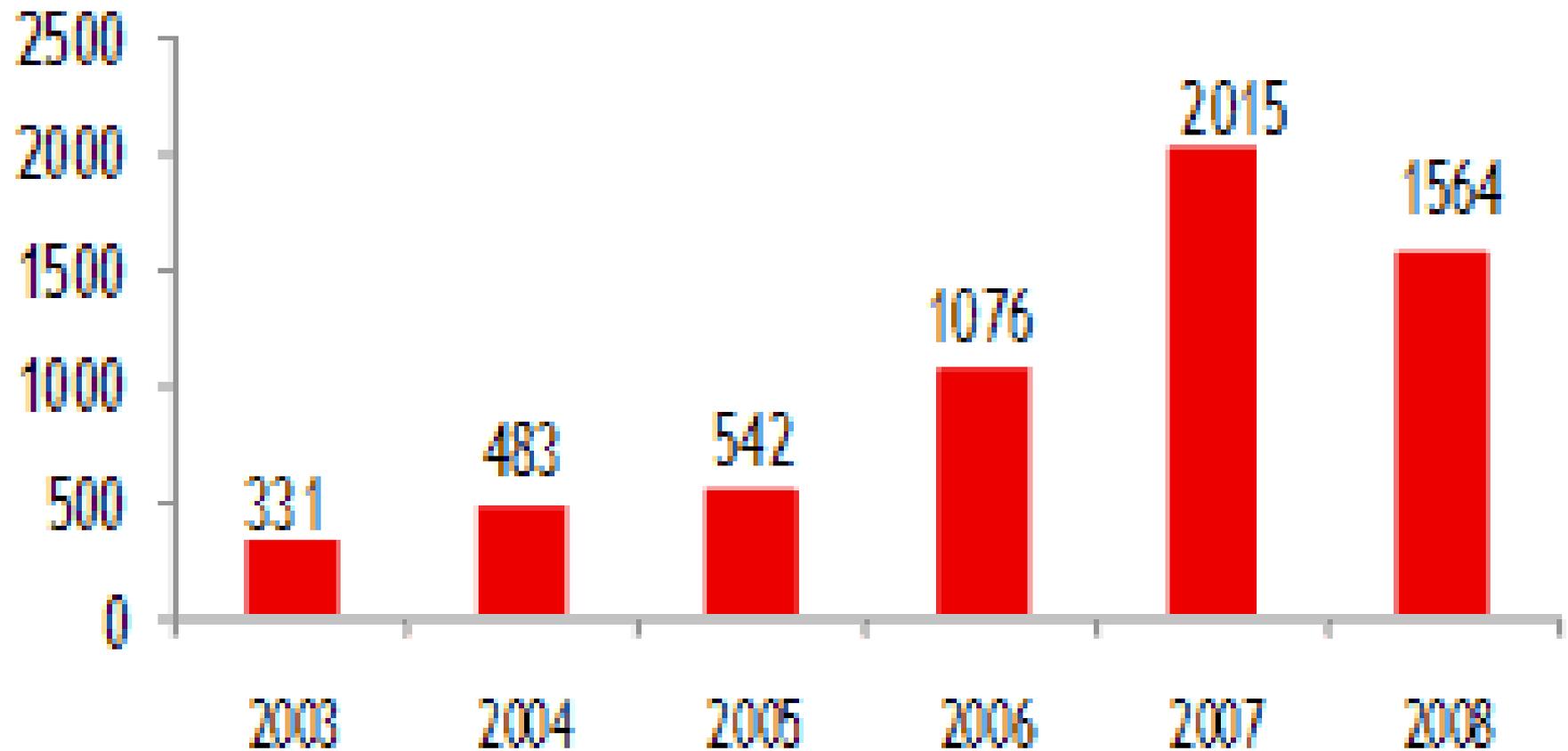
Dr. Dimitri Japaridze
Georgian Entrepreneurs Confederation

Stable Macroeconomic Environment



Source: Department of Statistics of Georgia, Ministry of Finance of Georgia, IMF forecast

Net FDI inflows

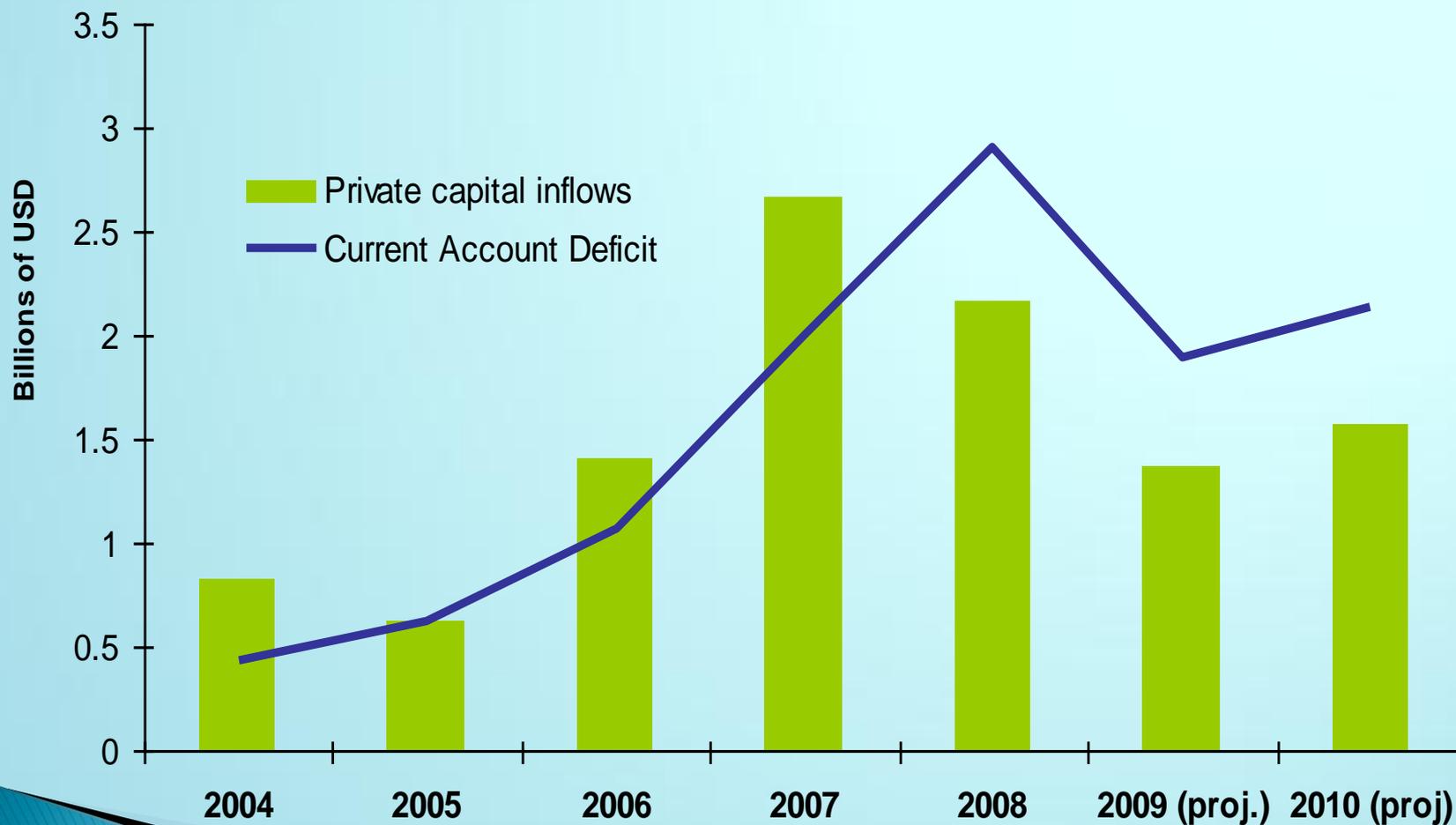


Source: Department of Statistics of Georgia

Impacts of financial and economic crises

- weakening of investor, lender and consumer confidence
- contraction of liquidity in the banking system
- contraction of foreign capital inflow
- stress on public finances
- damage to physical infrastructure
- the GDP growth plummeted to 2.1% by end-year

Georgia: The External Financing Shock



Sources: Statistics Department of Georgia and IMF Staff Estimates

Georgia's exposure to the international crisis

▶ **Channels of transmission of the international crisis:**

- Contraction of export markets
- Lower remittances
- Freeze of credit markets (debt rollover problem)
- Repatriation of hot money
- Falling commodity prices

▶ **Resilience factors:**

- large donor financial package
- track record of pro-growth structural reforms and sound macro-economic policies

Which policies have been implemented in response?

Due to “Twin Crises” in Georgia, it was necessary to address many issues in order to restore public confidence in financial market:

- Donor-financed fiscal stimulus to limit the economic slowdown
- Adjustment of the exchange rate through a devaluation of 17 percent in November 2008
- Introduction of foreign exchange auctions to allow for more flexibility
- Adjusting fiscal policy by allowing an increase in infrastructure and social spending
- boosting official reserves

IMF Approved a \$710 Stand-By Arrangement (Credit Line) in September, 2008

- ▶ **Duration:** 18 months
- ▶ **Objectives:**
 - Stabilize the economy, restore confidence and meet external payment obligations with least disruption
- ▶ **Policies:**
 - align public spending to available external resources
 - allow the exchange rate to adjust flexibly to market pressures and thus protect international reserves
 - maintain close vigilance over banks to pre-empt possible problems

National Bank of Georgia(NBG) Actions

- NBG reduced the required reserve ratio from 13% to 5%
- NBG used the lending of last resort facility, 3 commercial banks made use of this instrument for a total amount of GEL 38.1 million
- NBG launched a special loan facility, which was extended in September in the total amount of GEL 135.9 million with six-month maturity period
- NBG managed to provide the banking system with foreign exchange cash banknotes (the US dollar and the euro)
- NBG allowed commercial banks to repurchase securities before maturity date

The Banking Sector

- Commercial banks succeed in rollover measures of their external debt thanks to the early capital injection from the international financial institutions
- The immediate risks of a liquidity crunch were rapidly addressed through easing monetary conditions and selected regulatory forbearance
- Banks have managed to withstand the significant withdrawals of deposits, including in foreign exchange

Factors Impeding SME Business Development

1	Not protecting business interests by authorities	9	Markets are not protected against falsified goods
2	Underdeveloped financial markets and low liquidity of enterprise assets	10	Increased prices on goods and services
3	Bank credits are hardly available	11	Unnecessary involvement of governmental institutions and controlling agencies in business
4	High interests on bank credits	12	Low competitiveness of goods/services produced
5	Disorder in tax system	13	Other
6	High rate of taxes	14	There are no factors impeding business development
7	Corruption	15	Do not know
8	Internal markets are not protected against smuggling	16	Refusal to answer

Government strategy to support SME financing in time of crises and beyond

It is planned to make amendments in the tax code that would make tax environment friendlier:

- 20% Flat Personal Income tax decreasing to 15% by 2013
- 5% interest income and dividend tax rates decreasing to 0% by 2012

- Main focus is done on two areas featured in the SME financing practice: credit guarantee schemes and venture capital/equity funding.
- State program of “Cheap Credit” has allocated GEL 60 mln in 2007 and GEL 20 mln in 2008 for debt financing of SMEs involved in tourism, agriculture, etc.
- Guarantee schemes are introduced by international organisations (USAID, KFW, etc.)



- All abovementioned instruments are employed at the moment, however, the scale of use of the mentioned instruments are too far from sufficient level. Recent reports highlight, that Georgian SMEs still face significant constraints with respect to long-term banking finance.

The Challenges Ahead

- The external imbalances
 - Further declines in:
 - private capital inflows
 - exports
 - Remittances
-

However:

- The adaptability of policies and the improved planning capacity demonstrated in recent months
- solid track record of structural and market reforms
- Trade revenue, tax revenues, and other activity indicators have been showing improvements in the third and fourth quarter of 2009

THANK YOU