

STRONGER ECONOMY

#eu4business



EU4Business

# Investing in SMEs in the Eastern Partnership

## Georgia

COUNTRY REPORT  
JUNE 2019

## 1. Recent economic developments in the country

The Georgian economy remains on the path of strong economic growth. Economic output expanded by 4.7 per cent in 2018, driven largely by growth in trade, real estate, transport and financial intermediation. The hospitality sector continued to boom, supporting overall economic performance; the share of tourism-related services in the whole economy increased from an average of 7.3 per cent in 2015-17 to 8.1 per cent in 2018.

However, output in the construction sector declined by 3.1 per cent, marking the first contraction in the sector since 2013. Supported by a growing network of free trade agreements, exports of goods increased by 22.6 per cent in 2018 and by 13.2 per cent in the first two months of 2019, both in nominal US dollar terms. In 2018, inflows of remittances increased by 13.1 per cent, amounting to 10.9 per cent of GDP and supporting household consumption. Combined with thriving tourism and rising exports of goods, this caused a narrowing of the current account deficit to 7.7 per cent of GDP in 2018.

At the same time, foreign investment into Georgia decreased by 34.9 per cent compared to 2017, hitting a five-year low at 7.3 per cent of GDP. This came on the back of completion of the South Caucasus Pipeline Expansion (SCPX – the gas pipeline connecting Azerbaijan and Turkey), the transfer of several enterprises to domestic ownership and debt repayments between connected companies.

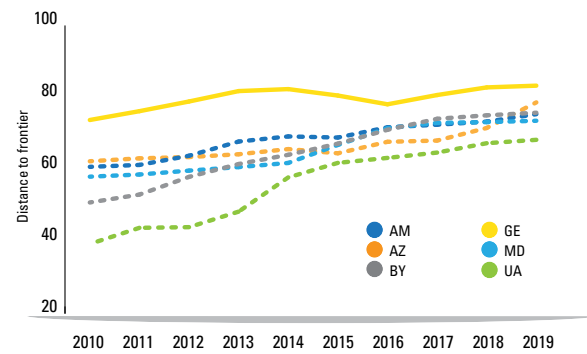
Despite the decline, FDI remained the main source of currency inflows, nearly offsetting the current account deficit. Balance of payments dynamics supported the currency, which, while subject to seasonal variations, remained resilient to negative developments in regional economies. High-frequency indicators point to economic growth of 4.1 per cent year-on-year in the first two months of 2019. The EBRD forecasts Georgia's real GDP to grow by 4.5 per cent in 2019 and by the same rate in 2020.

(<https://www.ebrd.com/where-we-are/georgia/overview.html>)

## 2. Business environment: Georgia and the EaP

The six Eastern Partner countries have been making steady progress in improving the business climate for SMEs. This overview of the Doing Business indicator of the World Bank shows how Georgia has improved over the years, gradually closing the gap with the best performing countries of the world ('distance to frontier'). Georgia has been the stellar performer, starting off very high at 75% of distance to frontier, and now standing at almost 85%.

Doing Business - Distance to frontier, EaP

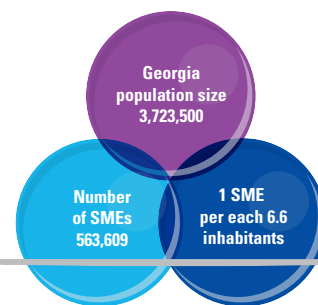


Source: Doing Business, World Bank, [www.doingbusiness.org](http://www.doingbusiness.org)<sup>1</sup>

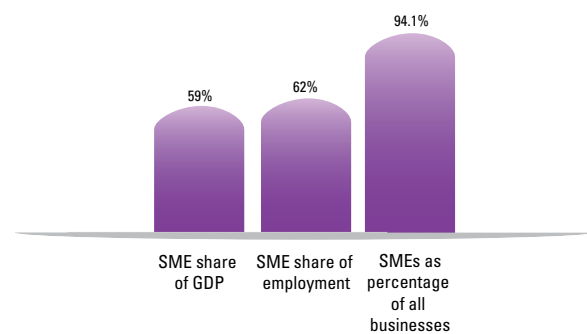
## 3. National SME performance

### a. Share of SMEs in the economy

Georgia has easily the highest number of SMEs per capita across the EaP, but not the highest share of employment generated by the SME sector. Likewise, their share in GDP comes to just over a half of the national economic output.



State of affairs of SMEs in 2017



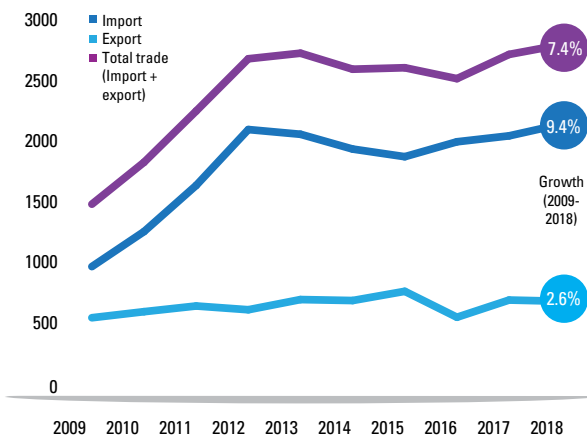
Source: OECD Eurasia Competitiveness Programme and Official Yearbook of the National Statistics Institute, 2018

<sup>1</sup> An economy's ease of doing business score is reflected on a scale from 0 to 100, where 0 represents the lowest and 100 represents the best performance. For example, an ease of doing business score of 75 in Doing Business 2018 means an economy was 25 percentage points away from the best regulatory performance constructed across all economies and across time.

## b. Trade with the EU

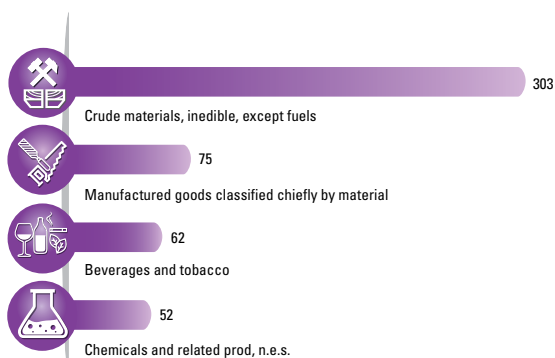
There has been a faster growth in imports from the EU than exports to it, although trade in both directions has been on the rise. Georgia currently imports EUR 2.1 billion and exports 653 million worth of goods and services from and to the EU respectively.

Trade figures (EUR million)

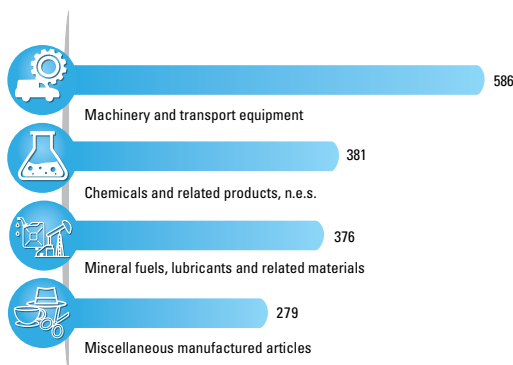


Below are the top products exported from Georgia to the EU and those imported the other way.

Top exported products in 2018 (EUR million)



Top imported products in 2018 (EUR million)



All trade data from DG trade

([https://webgate.ec.europa.eu/isdb\\_results/factsheets/country/](https://webgate.ec.europa.eu/isdb_results/factsheets/country/)).

## 4. SME legislation and institutional framework

In 2015, the Government of Georgia, with the support of the OECD, developed and adopted an SME Development Strategy for 2016-2020. The implementation of the 2018-2020 Action Plan is underway and the Ministry of Economy and Sustainable Development of Georgia relied on OECD assistance in assessing the status of the strategy's implementation, identifying outstanding issues for the SME sector, and establishing a results-based monitoring system.

### Key SME legislation in the country

- SME Development Strategy of Georgia 2016-2020, adopted in June 2016
- SME Development Strategy Action Plan 2018-2020, adopted in January 2018

### Name and date of establishment of the SME agency

Enterprise Georgia (Before 2017 - Enterprise Development Agency), February 2014

### Achievements in improving the SME climate

- The **institutional framework and operational environment** for SMEs has substantially improved, with, e.g. the adoption of a new SME definition, work on new insolvency regulation, the formalisation of platforms for public-private dialogue on business-related policies, and laying the groundwork for Regulatory Impact Assessments (RIA).
- 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.
- 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.
- 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 run by Enterprise Georgia with an aim to be expanded.
- Important steps have also been taken to facilitate **SME innovation and R&D activities**.

## EU4Business: From Policies to Action progress (OECD)

The OECD has a broad agenda of co-operation with the Government of Georgia, working primarily with the Ministry of Economy and Sustainable Development.

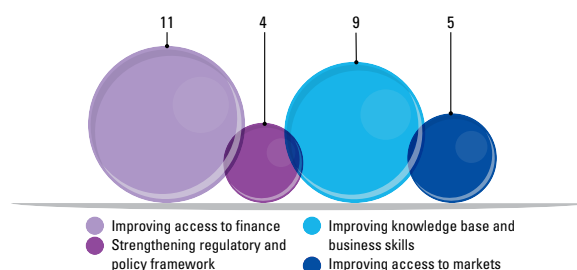
- At the **country level**, throughout 2018, the OECD supported the Government to set up a results-based monitoring system with three levels of monitoring: implementation, results and impact along each strategic direction of its SME strategy. In total, 22 quantitative indicators have been put forward with an indication of where data can be collected.
- The OECD summarised project findings in a policy paper, which provided a basis for discussion during the peer review of Georgia at the OECD Eurasia Competitiveness Roundtable 2018.
- In addition, the OECD is carrying out an Investment Policy Review (IPR) of Georgia to assist the Government in creating a favourable investment climate, improving the transparency of the investment regime and promoting responsible business conduct. The project was officially launched in February 2019, during a first Task Force meeting chaired by the Ministry of Economy. A draft report will be available by Q1 2020 and will be submitted for peer review at the OECD Investment Committee in Q2 2020.
- At the **regional level**, Georgia participates in the third round of the SBA Assessment, which will result in a regional benchmark to be published by March 2020. The new exercise is more ambitious than the previous editions, and relies on a new methodology that goes beyond the scope of SME policy to incorporate overall business environment conditions, including the topics of competition, business integrity and contract enforcement. An important milestone in this process took place in Tbilisi on 14 May 2019, consisting of a private sector focus group and a public-private reconciliation meeting to discuss preliminary findings and progress in SME policy since 2016. For this activity, the OECD works closely with the Private Sector Development Advisory Council to support the government in strengthening its public-private dialogue activities.

## 5. EU4Business portfolio for the country

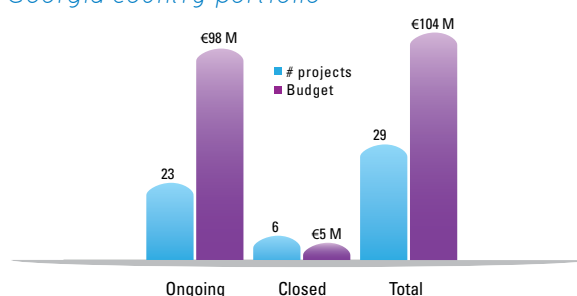
The total number of projects in Georgia is 29, of which the largest group focuses on improving access to finance. Out of the 29 projects, six have closed and the others are ongoing, with a total value of almost EUR 103.8 million.

### a. Impact to date

Projects by priority area - Georgia



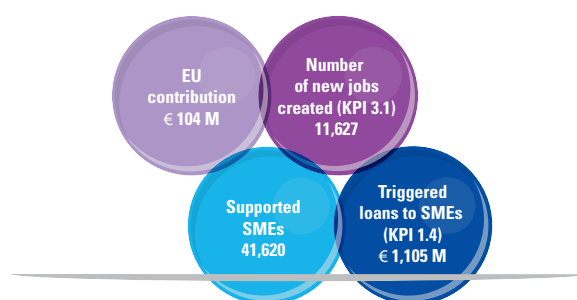
Georgia country portfolio



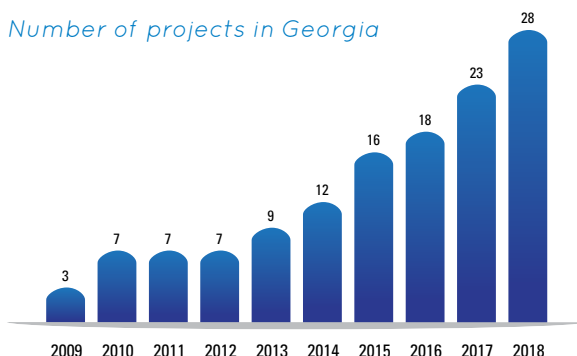
### b. Implementation progress - 10 years of EU4Business in the country

The funds invested by the European Union have triggered additional loans and financial assistance in the country, effectively increasing the assistance tenfold. This benefitted 41,620 SMEs and created an estimated 11,627 jobs, beyond the jobs that were sustained. The number of projects in the country, and with it the EU's assistance, has been on the steady rise over EU4Business's ten years of operation.

Implementation progress



Number of projects in Georgia



Source: EU4Business Secretariat project database

## 6. Stakeholder assessment

### a. Findings from the SMEs - Focus group assessment, Tbilisi, 11 April 2019

#### i. Key issues

Participants first reflected on the ease of accessing financial products, and remained critical of the intermediary banks/PFIs, suggesting they are not always as forthcoming with EU4Business products, sometimes pushing their own ones instead. When it comes to EU4Business loans, banks prefer dealing with larger companies, while technical assistance is more likely to be granted to the smaller ones. Still, it takes a long time to get a loan approved, the collateral requirements remain high, and the cashback component relatively low.

Georgian SMEs have little understanding of the overseas market needs necessary to make informed decisions, not only in organising potential exports but even procuring consulting services from those markets that could train them in certification, standards, logistics etc. Almost no information on the EU market is available, including from Georgian embassies abroad. To reach these countries, transportation costs often exceed manufacturing costs, because SMEs have very little knowledge of EU shipping, freight forwarding etc.

It is very difficult to get hold of the quality consultants who can provide the exact support that SMEs need. National experts are often missing, particularly for the areas that have developed recently, such as safety standards compatible with the EU. Even the national vocational education does not yet live up to the market expectations. For most of these issues,

SMEs need to look for technical assistance abroad, such as in Turkey. The GIZ-led cluster project was emphasised as nearly a turnkey solution for SMEs, where most issues can effectively be addressed. It is also an avenue for the same industry SMEs to connect with one another and increase mutual trust, working as a team. From there they discover complementarities and start collaborating, eventually preparing for fairs abroad and exports.

#### ii. SMEs' own needs assessment/priorities

SMEs find any peer-to-peer learning and awareness events very useful, including attendance of trade shows and fairs. These need to be organised more often, with perhaps some support for smaller firms to attend.

Regions outside Tbilisi remain disadvantaged and reaching out to them and disseminating information on available products' should happen in direct meetings with local entrepreneurs. This might involve or be conducted through PFIs.

The most critical areas requiring support are:

- access to finance to continue modernising production at higher standards
- certification support to become competitive abroad
- alternative sources of finance
- support to start-ups
- government needs to enforce anti-monopoly regulations and level the playing field
- improving quality and standards by providing tailored advice
- modernising local TVET institutions and producing qualified labour to suit market needs
- availability of management courses, particularly training for top and middle management

Finally, participants agreed that future programmes could benefit for a closer measuring of impact of the implemented projects, as it would be easier to actually attribute any increase in turnover, employment etc. to features of the projects.

### b. Views of the implementers - Georgia EU4Business Roundtable, Tbilisi, 12 April 2019

#### i. Key issues

With a strong presence of the IFIs, the roundtable discussion opened assessing the financial support. Participants concluded that given the still prevalent SME practice of maintaining different business records - actuals vs. officially declared - the transparency of business and accountability are the reasons why many SMEs cannot get loans from the banks. However, alternative sources of sources of finance, like angel investors and crowdfunding, are coming to life to support Georgian small enterprises and especially start-ups.

Participants agreed that SME competitiveness needs to be increased locally and internationally, for which quality and safety of products and services become ever more important. Not only is access to international markets a problem, but quite often SMEs face problems within the Georgian market too.

All parties agreed that knowledge is a key. Lack of knowledge, skills and entrepreneurial culture is the main problem among SMEs. Most SMEs find it difficult to navigate through the market triangle of SMEs-labour-education. While clusters add tremendous value, value chains are still weak and unattainable for smaller companies. Showcasing success stories in the regions has been of major benefit for entrepreneurs, who then demanded access to the quoted programmes. This communication was understandable to all, utilising simple messages driven by peers. More visibility, promotion and direct engagement with SMEs benefits everyone involved.

Despite very significant advances in smart regulation of the market, a number of regulatory issues still require attention for the benefit of local SMEs. Competition, procurement and business integrity remain underregulated.

## ii. Suggestions of the Roundtable going forward

In terms of facilitating access to finance, guarantees to support collateral requirements, specifically blending guarantees, and combining them with other tools are all seen as vital, while movable collateral should also be considered by banks/PFIs. Because Georgian SMEs are more labour intensive, the recommendation from the banks is to revise the eligibility of credit line programmes and the SME definition for loan purposes, as this would give the opportunity to more SMEs to benefit from programmes.

Supporting SMEs in trading with other countries, including the EU, has become critical at this stage of SME landscape development. This would require addressing the following issues:

- Purchasing new equipment or upgrade of existing material is not only a question of financial support, but also how to find the technical details of market trends in the EU.
- Support in negotiations, match making, linkage between new buyers and SMEs (this could also involve Georgian diaspora and embassies).
- Safety and security issues (e.g. food) need to be brought closer to SMEs, and their introduction facilitated by the regulators. This will often require one-on-one expert work with SMEs and on-the-job training.

- Awareness raising about the EU market and the DCFTA requirements is much needed, especially among less experienced and smaller firms. Working directly with EU experts is beneficial.
- Cluster work has made important strides and needs to intensify: existing clusters should consolidate, and new sectors should be identified (e.g. tourism and agribusiness). Linking Georgian high added value clusters to European SMEs is essential.
- Increase SME knowledge and literacy in accounting standards and legislation to comply with financial audit and accounting requirements, including EU regulations and how to apply what is needed.
- Knowledge sharing events with case studies from successful peers is an optimal means of training for other SMEs. Some of this might be achieved by strengthening BSOs for outreach and information sharing, particularly in the regions.
- TVET knowledge and skills will have to initially rely on bringing the appropriate expertise from the EU and then train the future local trainers. The government should elaborate on these plans in the new SME development strategy.

## c. Summary of recommendations for next planning cycle

Both SMEs and implementers agree that support is needed in the following areas:

- Safety, security, quality and certification issues top the needs agenda. This requires one-on-one expert work with SMEs and on-the-job training.
- Awareness raising about the EU market and the DCFTA requirements is much needed, ideally involving EU experts.
- Knowledge sharing events with case studies from successful peers is an optimal means of training for other SMEs.
- Greater awareness and know-how transfer might be achieved by strengthening BSOs for outreach and information sharing, particularly in the regions.
- Modernising local TVET institutions and producing qualified labour to suit market needs will close the existing skill gaps.





EU4Business

**Georgia:**  
Investing to serve the community



*“I’ve been able to pursue a dream of having my own business that enables me to support my family, and serve my friends in the local community.”*

**Inga Gelovani**  
Store Owner & Designer

DCFTA Initiative East

Thanks to the EIB’s investment facility under the EU4Business programme, Ms. Inga Gelovani was able to start a clothing business and to open a store in the centre of Tbilisi. The loans received under the programme allowed the designer to maintain the clothes shop in a productive manner and successfully improve her family’s livelihood, while serving the local community.



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**Georgia:**  
Georgian ICT Cluster –  
a new player in the field



*“Through the cluster, we can consolidate resources and compete with experienced international companies with joint forces.”*

**George Mzhavanadze**  
Executive Partner at Do So Management,  
member of the Georgian ICT Cluster  
management board

SME Development and DCFTA in Georgia

The Georgian ICT Cluster was established in December 2017 with the support of the EU-funded ‘SME Development and DCFTA in Georgia’ project. The cluster supports participation in public policy development for the ICT sector, dialogue with state agencies, and education - fostering the development of a professional workforce that will meet current industry demands and the challenge of internationalisation.

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