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Proposal for a

**DECISION OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL**

**providing further macro-financial assistance to Georgia**

{SWD(2017) 321 final}

## EXPLANATORY MEMORANDUM

### 1. CONTEXT OF THE PROPOSAL

#### • Reasons for and objectives of the proposal

Georgia continues to face a weak external environment, which, through reduced exports and remittances, has contributed to relatively subdued GDP growth of 2.7% in 2016 (compared to 2.9% in 2015 and 4.6% in 2014). GDP growth is projected to increase gradually to 3.5% in 2017, supported by consumption and investment. Regional and global growth is also expected to pick up in 2017, but will remain subject to downside risks of geopolitical instability, protectionism and volatility in the financial markets.

Georgia's fiscal deficit remains significant (4.1% of GDP in both 2016 and, as expected by the International Monetary Fund (IMF), in 2017). The public debt-to-GDP ratio has increased from 35.6% in 2014 to 44.6% in 2016, mainly due to the fact that around 80% of public debt is denominated in foreign currency, and the national currency (the Georgian lari, GEL) depreciated sharply during that period. Moreover, Georgia's balance of payments position remains vulnerable due to a very large current account deficit (12.4% of GDP in 2016) and high external debt (111.8% of GDP in 2016). Georgia's foreign exchange reserves have been broadly stable in absolute terms since 2011, totalling USD 2.8 billion at end-2016, but reserve needs have been increasing according to the composite IMF metric. Therefore, reserves are currently below the level estimated by the IMF to be adequate. Georgia also continues to adapt to the requirements of the Deep and Comprehensive Free Trade Area (DCFTA) with the EU, which, along with opportunities, also entail adjustment costs.

In this context, on 12 April 2017 Georgia and the IMF agreed a three-year (2017-2020) extended arrangement under the Extended Fund Facility (EFF). The EFF represents 100% of Georgia's quota in the Fund (SDR 210.4 million, or about USD 285 million). The aim of the EFF programme is to support an economic reform programme which will help Georgia reduce economic vulnerabilities, and promote higher and more inclusive economic growth.

The government of Georgia also requested Macro-Financial Assistance (MFA) from the EU on 16 June 2017. In light of this request and the economic situation in the country, the Commission is submitting to the European Parliament and the Council a proposal for MFA to Georgia, based on Article 212 (2) of the TFEU. The proposal is for an amount of up to EUR 45 million, of which EUR 35 million are in the form of loans and EUR 10 million in the form of grants.

The proposed new MFA operation is the third one after Georgia's military conflict with Russia in August 2008. In October 2008, the EU pledged two MFA operations of EUR 46 million each at the International Donors' Conference in Brussels. The first of those operations (EUR 46 million, fully in the form of grants) was implemented in 2009-2010 and the second (again EUR 46 million, half in grants and half loans) in 2015-2017. The last tranche of the 2015-2017 MFA operation was disbursed in May 2017.

The proposed new MFA will help Georgia cover part of the external financing needs for the period of 2017-2020, which are estimated at USD 752 million (EUR 671 million).<sup>1</sup> The operation will reduce the economy's short-term balance of payments and fiscal vulnerabilities. It will be designed and implemented in coordination with the adjustment and reform programmes Georgia has agreed with the IMF and the World Bank, as well as with the reforms agreed in the context of the EU's budget support operations and the DCFTA.

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<sup>1</sup> All conversions in this document are based on a EUR/USD exchange rate of 1.12.

As further elaborated in the Commission Staff Working Document accompanying this proposal, the Commission considers, based also on the assessment of the political situation made by the European External Action Service (EEAS), that the political and economic pre-conditions for the proposed MFA operation are satisfied.

- **General context**

The macroeconomic outlook for Georgia remains vulnerable. The ongoing fiscal consolidation could weaken domestic demand and lower economic growth in Georgia. In addition, the Georgian economy faces broader risks due to an uncertain regional and global economic outlook, external imbalances (notably, a large and still increasing current account deficit and significant external debt) as well international reserves that are below the adequate level.

The economic slowdown in the region and the fact that the currencies of major trading partners have depreciated sharply since late 2014 have weighed on Georgia's exports and remittances. This contributed to a deceleration of economic growth to 2.7% in 2016, from 2.9% in 2015 and 4.6% in 2014. Georgia's *GDP growth* in 2016 was mainly driven by investment, while private consumption remained subdued, reflecting the reduction in disposable income induced by the increase in the domestic-currency value of households' repayment obligations on US dollar-denominated loans in a context of sharp depreciation of the lari. GDP growth is projected to increase gradually, to 3.5% in 2017, supported by consumption and investment, and to 5.0% in 2020 (the end of the recently-agreed arrangement with the IMF).

The *exchange rate* (USD/GEL period-average) moved from 1.77 in 2014 to 2.27 in 2016, meaning around 22% depreciation of the Georgian lari. The effects of this volatility are amplified by the still high dollarisation of the Georgian economy, where 70% of deposits and 65% of loans were denominated in US dollars in 2016.

Although the *unemployment rate* in Georgia (11.8% at end-2016) has been on a downward trend since 2009 (16.9%), it remains an important challenge. While employment opportunities have been created in new growth sectors, especially in tourism and other services, high unemployment persists due to challenges associated with skills mismatch and large regional disparities. Georgia also lacks an unemployment benefit scheme.

In terms of the external sector, Georgia's *current account deficit* further deteriorated in 2016 to 12.4% of GDP (from 12.0% of GDP in 2015 and 10.6% in 2014) and, as noted, remains a major source of vulnerability. The current account deficit widened in 2014-2016, despite the slowdown in economic growth, as the weakness of exports more than compensated for the weak domestic demand for imports, resulting in a larger trade in goods deficit. The current account deficit is expected to worsen further to 12.9% in 2017, before decreasing modestly to 11% in 2020, according to IMF programme projections. The very large current account deficit is mainly driven by the trade in goods deficit which is only partly offset by the trade in services surplus and income and transfers from abroad, including remittances.

Although the current account deficit has mainly been financed by inflows of *foreign direct investment*, the latter is expected to decrease slightly from 11% of GDP in 2016 to 10.3% of GDP in 2017 and remain at a similar level until 2020. Moreover, debt-creating financial inflows have also contributed to the financing of the current account deficit. Hence, Georgia's *external debt*, which hovered around 80% of GDP in 2008-2014, has increased significantly in the following years, to 111.8% of GDP at end-2016. The external debt is projected to increase further, to 120.2% in 2020. As most foreign debt is denominated in US dollar, the lari depreciation has played an important role in this increase.

The National Bank of Georgia (NBG) has generally refrained from large interventions in the foreign exchange market and allowed the lari to depreciate. This has allowed *gross*

*international reserves* to remain stable overall, totalling USD 2.7 billion at end-February 2017 (about 3 months of next year's imports). The recently-agreed IMF programme targets a 54% increase in reserves, from USD 2.8 billion at end-2016 to USD 4.2 billion in 2020 (about 4 months of import cover).

The period-average *inflation* (consumer price index, CPI) decelerated to 2.1% in 2016, compared to 4.0% in 2015. CPI is projected to increase to 5.7% in 2017, in line with the increase of excise duties which entered into force in January 2017, but should decrease to 3.0% in 2018 and remain at a similar level in 2019 and 2020.

Following a long period of fiscal consolidation since 2009, the *fiscal deficit* of the general government started to widen in 2015 (3.8% of GDP), partly as a result of an increase in social spending aimed at addressing the country's high levels of poverty and inequality, but also reflecting the negative impact of the economic slowdown on tax revenues. The budgetary position further deteriorated in 2016, with the government deficit estimated by the IMF at 4.1% of GDP, as a result of both weaker-than-expected revenues and spending increases ahead of the October parliamentary elections (mainly in defence, public transport, infrastructure and healthcare). The fiscal deficit (which was projected to increase further, to around 6% of GDP this year, before the new IMF programme was agreed) is now forecast to remain at the same level (4.1%) in 2017 and to decrease gradually afterwards, reaching 3.1% in 2020. *Public debt* also increased to an estimated 44.6% of GDP in 2016 (from 35.6% in 2014) and is expected to rise further, peaking at around 47% in 2019, before decreasing gradually afterwards.

The fiscal strategy of the Georgian authorities is based on further consolidation. Notably, the Georgian authorities plan to reduce current spending (a reduction in the wage bill and administrative expenses, efficiency gains in healthcare spending, and new spending controls on local governments), whilst increasing capital spending, mainly in infrastructure, and introducing a second (funded) pillar of the pension system. On the revenue side, the Georgian authorities have increased taxes (notably, excise duties on tobacco products, vehicles and fuel) to compensate for revenue losses due to the corporate income tax reform that entered into force in January 2017 and are ready to take additional measures if needed.

The fiscal consolidation is complemented by the structural reform agenda which focuses on improving business environment, education and public administration as well as investing in infrastructure. Additional measures include fiscal reforms (notably, improving the management of risks stemming from public-private partnerships and state-owned enterprises), strengthening of the financial sector (for instance, introducing a deposit guarantee scheme and improving regulatory, supervisory and resolution frameworks for banks), as well as the ongoing adaptation to the requirements of the DCFTA.

The IMF's projections of March 2017 point towards significant *external financing needs* for the period of 2017-2020, with the total external financing gap estimated at USD 752 million (USD 256 million in 2017, USD 222 million in 2018, USD 183 million in 2019 and USD 91 million in 2020). This financing gap can broadly be attributed to three factors: a relatively large current account deficit, the need to increase foreign exchange reserves, and significant expected debt amortisation requirements.

The proposed MFA operation of EUR 45 million (around USD 50 million), in addition to EUR 23 million (around USD 26 million) disbursed under the previous MFA operation in May 2017, would cover 10% of the total estimated financing gap and 33% of the residual financing gap (after deducting net IMF financing and the expected disbursement of World Bank policy-based loans).

Other key contributions to covering the residual financing gap include budget support grants from the French development agency, AFD (of USD 62 million in 2017), and the Asian Development Bank (expected to amount to USD 100 million in 2018-2019).

- **Existing provisions in the area of the proposal**

Decision No 778/2013/EU providing previous macro-financial assistance to Georgia in the amount of EUR 46 million (half in grants and half in loans) was adopted by the European Parliament and the Council on 12 August 2013.<sup>2</sup> The assistance was fully implemented in 2015-2017, with the last disbursement in in May 2017.

- **Consistency with the other policies and objectives of the Union policies**

The EU and Georgia have developed close political and economic relations over the years, leading to the conclusion of the Association Agreement, including the DCFTA, which was signed in 2014 and entered into force in July 2016. This Association Agreement, which has replaced the previous Partnership and Cooperation Agreement, will allow for political association and economic integration of Georgia with the EU. The EU Single Support Framework (SSF) identifies the priority sectors of cooperation with Georgia, funded by the European Neighbourhood Instrument (ENI). The SSF for 2017-2020 is currently being finalised.

Georgia's economic ties with the EU are already well developed. In 2016, the EU was the main trading partner of Georgia, with a 32.6% share of trade, well ahead of other main trading partners (Turkey and Russia, with, respectively, 17.2% and 8.1% shares of trade). The EU is also Georgia's main investment partner and donor.

Countries that are covered by the ENP are eligible for MFA. The EU MFA will complement the grants mobilised under the ENI and other EU programmes and in particular the conditionality envisaged under the budget support packages being implemented by the EU. By supporting the adoption, by the Georgian authorities, of an appropriate framework for macroeconomic policy and structural reforms, the EU's MFA will enhance the added value and effectiveness of the EU's overall financial interventions, including through other financial instruments.

Georgia has consolidated its democracy and the rule of law, as well as further reinforced respect for human rights. The latest parliamentary elections in October 2016 were competitive and well-administered. Regarding the judiciary, Georgia's reforms have promoted judicial independence, professionalism and accountability.

In view of the above, the political preconditions for granting MFA to Georgia, including the aspect of political and economic closeness to the EU, may be considered to be satisfied. A detailed assessment of the satisfaction of the political criteria for MFA, produced by the EEAS, is annexed to the Commission Staff Working Document accompanying the proposal.

## **2. LEGAL BASIS, SUBSIDIARITY AND PROPORTIONALITY**

- **Summary of the proposed action**

The MFA operation under consideration would amount to a maximum of EUR 45 million. The Commission proposes to provide the amount of the assistance in the form of medium-term loans of up to EUR 35 million and grants of up to EUR 10 million. Given the proposed size of the

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<sup>2</sup> Decision No 778/2013/EU of the European Parliament and of the Council of 12 August 2013 providing further macro-financial assistance to Georgia (OJ L 218, 14.8.2013, p. 15).

operation, the Commission is considering releasing the assistance in two instalments.<sup>3</sup> The first tranche would indicatively be composed of a loan element of EUR 15 million and a grant element of EUR 5 million, and the second tranche of a loan element of 20 million and a grant element of EUR 5 million.

The assistance will be managed by the Commission. Specific provisions on the prevention of fraud and other irregularities, consistent with the Financial Regulation, are applicable.

Disbursements under the proposed MFA operation would be conditional on successful reviews under the IMF programme and on the effective drawing by Georgia on IMF funds. In addition, the Commission – on behalf of the EU – and the Georgian authorities would agree on a specific set of structural reform measures, to be defined in a Memorandum of Understanding. These reform measures would support the authorities' reform agenda and complement the programmes agreed with the IMF, the World Bank and other donors, as well as the policy programmes associated with the EU's budget support operations. They would be consistent with the main economic reform priorities agreed between the EU and Georgia in the context of the Association Agreement, including the DCFTA and the Association Agenda.

The decision to disburse around 22% of the proposed assistance in grants (EUR 10 million out of a total of EUR 45 million) and the rest in loans is justified by Georgia's level of economic and social development (as measured by the country's per-capita income, with Georgia being classified by the World Bank as a lower middle-income country, and the incidence of poverty), as well as by its relatively high indebtedness. Whilst Georgia is no longer eligible for concessional financing from either the IMF or the World Bank, its graduation from this concessional financing is relatively recent. Nevertheless, this graduation argues in favour of prioritising the loan element.

- **Legal basis**

The legal basis for this proposal is Article 212 (2) TFEU.

- **Subsidiarity (for non-exclusive competence)**

The subsidiarity principle is respected as the objectives of restoring short-term macroeconomic stability in Georgia cannot be sufficiently achieved by the Member States alone and can be better achieved by the European Union. The main reasons are the budgetary constraints faced at the national level and the need for strong donor coordination in order to maximise the scale and effectiveness of the assistance.

- **Proportionality**

The proposal complies with the proportionality principle: it confines itself to the minimum required in order to achieve the objectives of short-term macroeconomic stability and does not go beyond what is necessary for that purpose.

As identified by the Commission based on the estimates of the IMF in the context of the Extended Fund Facility programme, the amount of the proposed new MFA, in addition to the last disbursement under the previous MFA operation in May 2017, corresponds to 10% of the total estimated financing gap for the period 2017-2020 and 33% of the residual financing gap (i.e. excluding the IMF's net contributions and expected disbursements of World Bank policy-

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<sup>3</sup> Depending on the pace of the legislative process and, thereafter, the implementation of the MFA operation, the disbursement of the proposed assistance may take place in 2018 or be split between 2018 and 2019.

based loans). This is consistent with standard practices on burden-sharing for MFA operations, taking into account the assistance pledged to Georgia by other bilateral and multilateral donors.

- **Choice of the instrument**

Project finance or technical assistance would not be suitable or sufficient to address these macroeconomic objectives. The key value added of the MFA in comparison to other EU instruments would be to alleviate the external financial constraint and to help create a stable macroeconomic framework, including by promoting a sustainable balance of payments and budgetary situation, and an appropriate framework for structural reforms. By helping to put in place an appropriate overall policy framework, MFA can increase the effectiveness of the actions financed in Georgia under other, more narrowly-focused EU financial instruments.

### **3. RESULTS OF EX-POST EVALUATIONS, STAKEHOLDER CONSULTATIONS AND IMPACT ASSESSMENTS**

- **Consultation of interested parties**

MFA is provided as an integral part of the international support for the economic stabilisation of Georgia. In the preparation of this proposal for MFA, the Commission services have consulted with the IMF and the World Bank, which have already put in place sizeable financing programs and are preparing new ones. The Commission has also been in regular contact with the Georgian authorities.

- **Collection and use of expertise**

In line with the requirements of the Financial Regulation, the European Commission services have carried out an Operational Assessment of the financial and administrative circuits of Georgia in order to ascertain that the procedures in place for the management of programme assistance, including MFA, provide adequate guarantees. The preliminary findings from a mission conducted by a consultancy company for the purposes of this Operational Assessment were received in September 2017. They indicate that the current status of the administrative and financial circuits of Georgia is adequate for managing a new MFA operation although some weaknesses remain. The draft final report on this Operational Assessment is expected to be received in November 2017. Developments in that area will continue to be closely monitored also through the regular progress reports on public finance management (PFM) reforms produced by the EU Delegation in Tbilisi.

- **Impact Assessment**

The EU's macro-financial assistance is an exceptional emergency instrument aimed at addressing severe balance-of-payment difficulties in third countries. Therefore, this MFA proposal is exempted from the requirement to carry out an Impact Assessment in accordance with the Commission's Better Regulation Guidelines (SWD(2015) 111 final).

More generally, the Commission's MFA proposals build on lessons learned from ex-post evaluations carried out on past operations in the EU's neighbourhood. The new MFA and the economic adjustment and reform programme attached to it will help alleviate Georgia's short-term financing needs while supporting policy measures aimed at strengthening medium-term balance of payments and fiscal sustainability and raising sustainable growth, thus complementing the programme agreed with the IMF. These policy conditions should address some of the weaknesses shown over the years by the Georgian economy and economic governance system. Possible areas of conditionality could, in principle, include reforms aimed

at reinforcing social safety nets, PFM, strengthening the investment climate and supporting the implementation of the DCFTA.

#### **4. BUDGETARY IMPLICATIONS**

The planned assistance will be provided in the form of loans and grants. The loan part will be financed through a borrowing operation that the Commission will conduct on behalf of the EU. The budgetary impact of the loan assistance will correspond to the provisioning of the EU's Guarantee Fund for external actions, at a rate of 9% of the amounts disbursed, from budget line 01 03 06 ("Provisioning of the Guarantee Fund"). Assuming that the two loan disbursements (of EUR 15 million for the first tranche and EUR 20 million for the second tranche) will be made in 2018, the provisioning will take place in the 2020 budget, in accordance with the rules governing the Guarantee Fund mechanism, for an amount of EUR 3.15 million.

The grant element of the assistance (EUR 10 million in total, i.e. EUR 5 million for each of the two tranches) will be financed from commitment appropriations of the 2018 budget, under the budget line 01 03 02 (Macro-financial assistance), with payments also taking place in 2018.<sup>4</sup>

Based on current projections on the utilisation of the budget lines 01 03 02 and 01 03 06, the Commission assesses that the budgetary impact of the proposed MFA operation for Georgia can be accommodated.

#### **5. OTHER ELEMENTS**

- **Review/revision/sunset clause**

The proposal includes a sunset clause. The proposed MFA would be made available for two and a half years, starting from the first day after the entry into force of the Memorandum of Understanding.

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<sup>4</sup> As already indicated, depending on the pace of the legislative process and, thereafter, the implementation of the MFA operation, the disbursement of the proposed assistance may take place in 2018 or be split between 2018 and 2019.



Proposal for a

**DECISION OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL**

**providing further macro-financial assistance to Georgia**

THE EUROPEAN PARLIAMENT AND THE COUNCIL OF THE EUROPEAN UNION,

Having regard to the Treaty on the Functioning of the European Union, and in particular Article 212 (2) thereof,

Having regard to the proposal from the European Commission,<sup>5</sup>

After transmission of the draft legislative act to the national parliaments,

Acting in accordance with the ordinary legislative procedure,<sup>6</sup>

Whereas:

- (1) Relations between the European Union (“the Union”) and Georgia continue to develop within the framework of the European Neighbourhood Policy (ENP) and the Eastern Partnership. Georgia joined the EU’s Eastern Partnership in 2009, which was followed by the negotiation of an EU-Georgia Association Agreement. This agreement, which includes the gradual introduction of a Deep and Comprehensive Free Trade Area (DCFTA), was signed in June 2014 and entered into force on 1 July 2016.
- (2) Georgia continues to face a weak external environment, which, through reduced exports and remittances, has contributed to the relatively subdued GDP growth in 2016. Whilst regional and global growth is expected to pick up in 2017, it will remain subject to downside risks.
- (3) Georgia’s fiscal deficit remains significant, and its public debt-to-GDP ratio is increasing. Georgia’s balance of payments position also remains vulnerable due to a very large current account deficit and high external debt. Georgia’s foreign exchange reserves have been stable in absolute terms, but – in the face of rising reserve needs – they have fallen below the level estimated by the International Monetary Fund (IMF) as adequate. Georgia also continues to adapt to the requirements of the DCFTA with the Union.
- (4) In this context, the Georgian authorities and the IMF agreed, in April 2017, on a three-year (2017-2020) Extended Fund Facility (EFF) arrangement in the amount of USD 285.3 million. The arrangement was approved by the IMF Executive Board on 12 April 2017. The aim of the EFF arrangement is to support an economic reform programme which will help Georgia reduce economic vulnerabilities, and promote higher and more inclusive economic growth.
- (5) In view of Georgia’s residual external financing needs, the Georgian authorities requested complementary macro-financial assistance from the Union in June 2017.

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<sup>5</sup> OJ C [...], [...], p. [...].

<sup>6</sup> Position of the European Parliament of ... and Decision of the Council of ... .

- (6) Since the military conflict with Russia in August 2008, Georgia benefitted from two MFA operations pledged by the Union at the International Donors' Conference in Brussels in October 2008. The first of those operations (EUR 46 million, fully in the form of grants) was implemented in 2009-2010 and the second (again EUR 46 million, half in grants and half loans) in 2015-2017. The Union has also made available EUR 610-746 million to Georgia under the European Neighbourhood Instrument (ENI) for the period 2014-2020, including budgetary support and technical assistance. In addition, Georgia benefits from the Neighbourhood Investment Facility (NIF) which contributed around EUR 86 million to projects in Georgia during the period of 2008-2017.
- (7) Given that Georgia is a country covered by the ENP, it should be considered to be eligible to receive macro-financial assistance from the Union.
- (8) The Union's macro-financial assistance should be an exceptional financial instrument of untied and undesignated balance-of-payments support, which aims at addressing the beneficiary's immediate external financing needs and should underpin the implementation of a policy programme containing strong immediate adjustment and structural reform measures designed to improve the balance-of-payments position in the short term.
- (9) Given that there is still a significant residual external financing gap in Georgia's balance of payments over and above the resources provided by IMF and other multilateral institutions, the Union macro-financial assistance to be provided to Georgia is, under the current exceptional circumstances, considered to be an appropriate response to Georgia's request for support to the economic stabilisation, in conjunction with the IMF programme. The Union's macro-financial assistance would support the economic stabilisation and the structural reform agenda of Georgia, supplementing resources made available under the IMF's financial arrangement.
- (10) The Union's macro-financial assistance should aim to support the restoration of a sustainable external financing situation for Georgia thereby supporting its economic and social development.
- (11) The determination of the amount of the Union's macro-financial assistance is based on a complete quantitative assessment of Georgia's residual external financing needs, and takes into account its capacity to finance itself with its own resources, in particular the international reserves at its disposal. The Union's macro-financial assistance should complement the programmes and resources provided by the IMF and the World Bank. The determination of the amount of the assistance also takes into account expected financial contributions from bilateral and multilateral donors and the need to ensure fair burden sharing between the Union and other donors, as well as the pre-existing deployment of the Union's other external financing instruments in Georgia and the added value of the overall Union involvement.
- (12) Taking into consideration Georgia's residual external financing needs, the level of its economic and social development, as measured by per capita income and the incidence of poverty, as well as its level of indebtedness, a part of the assistance should be provided in the form of grants.
- (13) The Commission should ensure that the Union's macro-financial assistance is legally and substantially in line with the key principles, objectives and measures taken within the different areas of external action and other relevant Union policies.
- (14) The Union's macro-financial assistance should support the Union's external policy towards Georgia. Commission services and the European External Action Service

should work closely together throughout the macro-financial assistance operation in order to coordinate, and to ensure the consistency of, Union external policy.

- (15) The Union's macro-financial assistance should support Georgia's commitment to values shared with the Union, including democracy, the rule of law, good governance, respect for human rights, sustainable development and poverty reduction, as well as its commitment to the principles of open, rules-based and fair trade.
- (16) A pre-condition for granting the Union's macro-financial assistance should be that Georgia respects effective democratic mechanisms – including a multi-party parliamentary system – and the rule of law, and guarantees respect for human rights. In addition, the specific objectives of the Union's macro-financial assistance should strengthen the efficiency, transparency and accountability of the public finance management systems in Georgia, and promote structural reforms aimed at supporting sustainable and inclusive growth, employment creation and fiscal consolidation. Both the fulfilment of the preconditions and the achievement of those objectives should be regularly monitored by the Commission and the European External Action Service.
- (17) In order to ensure that the Union's financial interests linked to the Union's macro-financial assistance are protected efficiently, Georgia should take appropriate measures relating to the prevention of, and fight against, fraud, corruption and any other irregularities linked to the assistance. In addition, provision should be made for the Commission to carry out checks and for the Court of Auditors to carry out audits.
- (18) Release of the Union's macro-financial assistance is without prejudice to the powers of the European Parliament and the Council (as budgetary authority).
- (19) The amounts of macro-financial assistance provided in the form of grants and the amounts of the provision required for macro-financial assistance in the form of loans should be consistent with the budgetary appropriations provided for in the multiannual financial framework.
- (20) The Union's macro-financial assistance should be managed by the Commission. In order to ensure that the European Parliament and the Council are able to follow the implementation of this Decision, the Commission should regularly inform them of developments relating to the assistance and provide them with relevant documents.
- (21) In order to ensure uniform conditions for the implementation of this Decision, implementing powers should be conferred on the Commission. Those powers should be exercised in accordance with Regulation (EU) No 182/2011 of the European Parliament and of the Council.<sup>7</sup>
- (22) The Union's macro-financial assistance should be subject to economic policy conditions, to be laid down in a Memorandum of Understanding. In order to ensure uniform conditions of implementation and for reasons of efficiency, the Commission should be empowered to negotiate such conditions with the Georgian authorities under the supervision of the committee of representatives of the Member States in accordance with Regulation (EU) No 182/2011. Under that Regulation, the advisory procedure should, as a general rule, apply in all cases other than as provided for in that Regulation. Considering the potentially important impact of assistance of more than EUR 90 million, it is appropriate that the examination procedure be used for operations above that

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<sup>7</sup> Regulation (EU) No 182/2011 of the European Parliament and of the Council of 16 February 2011 laying down the rules and general principles concerning mechanisms for control by Member States of the Commission's exercise of implementing powers (OJ L 55, 28.2.2011, p. 13).

threshold. Considering the amount of the Union's macro-financial assistance to Georgia, the advisory procedure should apply to the adoption of the Memorandum of Understanding, and to any reduction, suspension or cancellation of the assistance.

HAVE ADOPTED THIS DECISION:

#### *Article 1*

1. The Union shall make macro-financial assistance of a maximum amount of EUR 45 million available to Georgia ("the Union's macro-financial assistance"), with a view to supporting Georgia's economic stabilisation and a substantive reform agenda. Of that maximum amount, up to EUR 35 million shall be provided in the form of loans and up to EUR 10 million in the form of grants. The release of the Union's macro-financial assistance is subject to the approval of the Union budget for the relevant year by the European Parliament and the Council. The assistance shall contribute to covering Georgia's balance of payments needs as identified in the IMF programme.

2. In order to finance the loan component of the Union's macro-financial assistance, the Commission shall be empowered on behalf of the Union to borrow the necessary funds on the capital markets or from financial institutions and to on-lend them to Georgia. The loans shall have a maximum average maturity of 15 years.

3. The release of the Union's macro-financial assistance shall be managed by the Commission in a manner consistent with the agreements or understandings reached between the International Monetary Fund (IMF) and Georgia, and with the key principles and objectives of economic reforms set out in the EU- Georgia Association Agreement, including the DCFTA, agreed under the European Neighbourhood Policy (ENP).

The Commission shall regularly inform the European Parliament and the Council of developments regarding the Union's macro-financial assistance, including disbursements thereof, and shall provide those institutions with the relevant documents in due time.

4. The Union's macro-financial assistance shall be made available for a period of two and a half years, starting from the first day after the entry into force of the Memorandum of Understanding referred to in Article 3(1).

5. Where the financing needs of Georgia decrease fundamentally during the period of the disbursement of the Union's macro-financial assistance compared to the initial projections, the Commission, acting in accordance with the advisory procedure referred to in Article 7(2), shall reduce the amount of the assistance or suspend or cancel it.

#### *Article 2*

1. A pre-condition for granting the Union's macro-financial assistance shall be that Georgia respects effective democratic mechanisms – including a multi-party parliamentary system – and the rule of law, and guarantees respect for human rights.

2. The Commission and the European External Action Service shall monitor the fulfilment of this pre-condition throughout the life-cycle of the Union's macro-financial assistance.

3. Paragraphs 1 and 2 of this Article shall be applied in accordance with Council Decision 2010/427/EU<sup>8</sup>.

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<sup>8</sup> Council Decision 2010/427/EU of 26 July 2010 establishing the organisation and functioning of the European External Action Service (OJ L 201, 3.8.2010, p. 30).

### *Article 3*

1. The Commission, in accordance with the advisory procedure referred to in Article 7(2), shall agree with the Georgian authorities on clearly defined economic policy and financial conditions, focusing on structural reforms and sound public finances, to which the Union's macro-financial assistance is to be subject, to be laid down in a Memorandum of Understanding ("the Memorandum of Understanding") which shall include a timeframe for the fulfilment of those conditions. The economic policy and financial conditions set out in the Memorandum of Understanding shall be consistent with the agreements or understandings referred to in Article 1(3), including the macroeconomic adjustment and structural reform programmes implemented by Georgia with the support of the IMF.
2. The conditions referred to in paragraph 1 shall aim, in particular, at enhancing the efficiency, transparency and accountability of the public finance management systems in Georgia, including for the use of the Union's macro-financial assistance. Progress in mutual market opening, the development of rules-based and fair trade, and other priorities in the context of the Union's external policy shall also be duly taken into account when designing the policy measures. Progress in attaining those objectives shall be regularly monitored by the Commission.
3. The detailed financial terms of the Union's macro-financial assistance shall be laid down in a Loan Agreement and a Grant Agreement to be concluded between the Commission and the Georgian authorities.
4. The Commission shall verify, at regular intervals, that the conditions referred to in Article 4(3) continue to be met, including whether the economic policies of Georgia are in accordance with the objectives of the Union's macro-financial assistance. In so doing, the Commission shall coordinate closely with the IMF and the World Bank, and, where necessary, with the European Parliament and the Council.

### *Article 4*

1. Subject to the conditions in paragraph 3, the Union's macro-financial assistance shall be made available by the Commission in instalments, each of which shall consist of a loan and a grant element. The size of each instalment shall be laid down in the Memorandum of Understanding referred to in Article 3.
2. The amounts of the Union's macro-financial assistance provided in the form of loans shall be provisioned, where required, in accordance with Council Regulation (EC, Euratom) No 480/2009.<sup>9</sup>
3. The Commission shall decide on the release of the second instalment subject to the fulfilment of all of the following conditions:
  - (a) the pre-condition set out in Article 2;
  - (b) a continuous satisfactory track record of implementing a policy programme that contains strong adjustment and structural reform measures supported by a non-precautionary IMF credit arrangement; and
  - (c) the satisfactory implementation of the economic policy and financial conditions agreed in the Memorandum of Understanding.

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<sup>9</sup> Council Regulation (EC, Euratom) No 480/2009 of 25 May 2009 establishing a Guarantee Fund for external actions (OJ L 145, 10.6.2009, p. 10).

The release of the second instalment shall not, in principle, take place earlier than three months after the release of the first instalment.

4. Where the conditions in paragraph 3 are not met, the Commission shall temporarily suspend or cancel the disbursement of the Union's macro-financial assistance. In such cases, it shall inform the European Parliament and the Council of the reasons for that suspension or cancellation.

5. The Union's macro-financial assistance shall be disbursed to the National Bank of Georgia. Subject to the provisions to be agreed in the Memorandum of Understanding, including a confirmation of residual budgetary financing needs, the Union funds may be transferred to the Georgian Ministry of Finance as the final beneficiary.

#### *Article 5*

1. The borrowing and lending operations related to the loan component of the Union's macro-financial assistance shall be carried out in euro using the same value date and shall not involve the Union in the transformation of maturities, or expose it to any exchange or interest rate risk, or to any other commercial risk.

2. Where the circumstances permit, and if Georgia so requests, the Commission may take the steps necessary to ensure that an early repayment clause is included in the loan terms and conditions and that it is matched by a corresponding clause in the terms and conditions of the borrowing operations.

3. Where circumstances permit an improvement of the interest rate of the loan and if Georgia so requests, the Commission may decide to refinance all or part of its initial borrowings or may restructure the corresponding financial conditions. Refinancing or restructuring operations shall be carried out in accordance with paragraphs 1 and 4 and shall not have the effect of extending the maturity of the borrowings concerned or of increasing the amount of capital outstanding at the date of the refinancing or restructuring.

4. All costs incurred by the Union which relate to the borrowing and lending operations under this Decision shall be borne by Georgia.

5. The Commission shall inform the European Parliament and the Council of developments in the operations referred to in paragraphs 2 and 3.

#### *Article 6*

1. The Union's macro-financial assistance shall be implemented in accordance with Regulation (EU, Euratom) No 966/2012 of the European Parliament and of the Council<sup>10</sup> and Commission Delegated Regulation (EU) No 1268/2012.<sup>11</sup>

2. The implementation of the Union's macro-financial assistance shall be under direct management.

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<sup>10</sup> Regulation (EU, Euratom) No 966/2012 of the European Parliament and of the Council of 25 October 2012 on the financial rules applicable to the general budget of the Union and repealing Council Regulation (EC, Euratom) No 1605/2002 (*OJ L 298, 26.10.2012, p. 1*).

<sup>11</sup> Commission Delegated Regulation (EU) No 1268/2012 of 29 October 2012 on the rules of application of Regulation (EU, Euratom) No 966/2012 on the financial rules applicable to the general budget of the Union (*OJ L 362, 31.12.2012, p. 1*).

3. The Loan Agreement and the Grant Agreement to be agreed with the Georgian authorities shall contain provisions:

- (d) ensuring that Georgia regularly checks that financing provided from the budget of the Union has been properly used, takes appropriate measures to prevent irregularities and fraud, and, if necessary, takes legal action to recover any funds provided under this Decision that have been misappropriated;
- (e) ensuring the protection of the Union's financial interests, in particular providing for specific measures in relation to the prevention of, and fight against, fraud, corruption and any other irregularities affecting the Union's macro-financial assistance, in accordance with Council Regulation (EC, Euratom) No 2988/95<sup>12</sup>, Council Regulation (EC, Euratom) No 2185/96<sup>13</sup> and Regulation (EU, Euratom) No 883/2013 of the European Parliament and of the Council<sup>14</sup>;
- (f) expressly authorising the Commission, including the European Anti-Fraud Office, or its representatives to carry out checks, including on-the-spot checks and inspections;
- (g) expressly authorising the Commission and the Court of Auditors to perform audits during and after the availability period of the Union's macro-financial assistance, including document audits and on-the-spot audits, such as operational assessments;
- (h) ensuring that the Union is entitled to early repayment of the loan and/or to full repayment of the grant where it has been established that, in relation to the management of the Union's macro-financial assistance, Georgia has engaged in any act of fraud or corruption or any other illegal activity detrimental to the financial interests of the Union.

4. Before the implementation of the Union's macro-financial assistance, the Commission shall assess, by means of an operational assessment, the soundness of Georgia's financial arrangements, the administrative procedures, and the internal and external control mechanisms which are relevant to the assistance.

#### *Article 7*

1. The Commission shall be assisted by a committee. That committee shall be a committee within the meaning of Regulation (EU) No 182/2011.

2. Where reference is made to this paragraph, Article 4 of Regulation (EU) No 182/2011 shall apply.

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<sup>12</sup> Council Regulation (EC, Euratom) No 2988/95 of 18 December 1995 on the protection of the European Communities financial interests (OJ L 312, 23.12.1995, p. 1).

<sup>13</sup> Council Regulation (EC, Euratom) No 2185/96 of 11 November 1996 concerning on-the-spot checks and inspections carried out by the Commission to protect the Communities' financial interests against fraud and other irregularities (OJ L 292, 15.11.1996, p. 2).

<sup>14</sup> Regulation (EU, Euratom) No 883/2013 of the European Parliament and of the Council of 11 September 2013 concerning investigations conducted by the European Anti-Fraud Office (OLAF) and repealing Regulation (EC) No 1073/1999 of the European Parliament and of the Council and Council Regulation (Euratom) No 1074/1999 (OJ L 248, 18.9.2013, p. 1).

### *Article 8*

1. By 30 June of each year, the Commission shall submit to the European Parliament and to the Council a report on the implementation of this Decision in the preceding year, including an evaluation of that implementation. The report shall:

- (i) examine the progress made in implementing the Union's macro-financial assistance;
- (j) assess the economic situation and prospects of Georgia, as well as progress made in implementing the policy measures referred to in Article 3(1);
- (k) indicate the connection between the economic policy conditions laid down in the Memorandum of Understanding, Georgia's on-going economic and fiscal performance and the Commission's decisions to release the instalments of the Union's macro-financial assistance.

2. Not later than two years after the expiry of the availability period referred to in Article 1(4), the Commission shall submit to the European Parliament and to the Council an ex-post evaluation report, assessing the results and efficiency of the completed Union's macro-financial assistance and the extent to which it has contributed to the aims of the assistance.

### *Article 9*

This Decision shall enter into force on the third day following that of its publication in the *Official Journal of the European Union*.

Done at Brussels,

*For the European Parliament*  
*The President*

*For the Council*  
*The President*



## LEGISLATIVE FINANCIAL STATEMENT

### **1. FRAMEWORK OF THE PROPOSAL/INITIATIVE**

- 1.1. Title of the proposal/initiative
- 1.2. Policy area(s) concerned in the ABM/ABB structure
- 1.3. Nature of the proposal/initiative
- 1.4. Objective(s)
- 1.5. Grounds for the proposal/initiative
- 1.6. Duration and financial impact
- 1.7. Management mode(s) planned

### **2. MANAGEMENT MEASURES**

- 2.1. Monitoring and reporting rules
- 2.2. Management and control system
- 2.3. Measures to prevent fraud and irregularities

### **3. ESTIMATED FINANCIAL IMPACT OF THE PROPOSAL/INITIATIVE**

- 3.1. Heading(s) of the multiannual financial framework and expenditure budget line(s) affected
- 3.2. Estimated impact on expenditure
  - 3.2.1. *Summary of estimated impact on expenditure*
  - 3.2.2. *Estimated impact on operational appropriations*
  - 3.2.3. *Estimated impact on appropriations of an administrative nature*
  - 3.2.4. *Compatibility with the current multiannual financial framework*
  - 3.2.5. *Third-party contributions*
- 3.3. Estimated impact on revenue

## LEGISLATIVE FINANCIAL STATEMENT

### 1. FRAMEWORK OF THE PROPOSAL/INITIATIVE

#### 1.1. Title of the proposal/initiative

Proposal for a Decision of the European Parliament and of the Council providing Macro-financial assistance to Georgia

#### 1.2. Policy area(s) concerned in the ABM/ABB structure<sup>15</sup>

Policy area: Title 01 – Economic and Financial Affairs

Activity: 03 – International economic and financial affairs

#### 1.3. Nature of the proposal/initiative

X The proposal/initiative relates to **a new action**

#### 1.4. Objectives

##### 1.4.1. *The Commission's multiannual strategic objective(s) targeted by the proposal/initiative*

“A new boost for jobs, growth and investment: promoting prosperity beyond the EU”

The DG ECFIN related activities pertain to:

- (a) Supporting macro-financial stability and promoting growth-enhancing reforms outside the EU, including through regular economic dialogues with key partners and by providing macro-financial assistance; and
- (b) Supporting the enlargement process, the implementation of the EU Neighbourhood Policy and EU priorities in other third countries by conducting economic analysis and providing policy assessments and advice.

##### 1.4.2. *Specific objective(s) and ABM/ABB activity(ies) concerned*

Specific objective: “Promoting prosperity beyond the EU”

ABM/ABB activity(ies) concerned:

- (a) Supporting macro-financial stability and promoting growth-enhancing reforms outside the EU, including regular economic dialogues with key partners and by providing macro-financial assistance; and
- (b) Supporting the enlargement process, the implementation of the EU Neighbourhood Policy and EU priorities in other third countries by conducting economic analysis and providing policy assessments and advice.

##### 1.4.3. *Expected result(s) and impact*

The proposed assistance consists of an EU loan of up to EUR 35 million and a grant of up to EUR 10 million to Georgia, with a view to contributing to a more sustainable balance of payments situation. The assistance, to be disbursed in two instalments, should help the country overcome the difficult economic and balance of payments situation it is experiencing. It will also promote structural reforms aimed at raising sustainable economic growth, reducing macroeconomic vulnerabilities and improving public finance management.

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<sup>15</sup> ABM: Activity-Based Management – ABB: Activity-Based Budgeting.

#### *1.4.4. Indicators of results and impact*

The authorities will be required to report on a set of indicators to the Commission services on a regular basis and provide a comprehensive report on the compliance with the agreed policy conditions ahead of the disbursement of all instalments of the assistance.

The Commission services will continue to monitor public finance management, following the operational assessment of the financial circuits and administrative procedures in Georgia that has been carried out in preparation of this operation. The EU Delegation in Tbilisi will also provide regular reporting on issues relevant for the monitoring of the assistance. The Commission services will remain in close contact with the IMF and the World Bank to benefit from their insights from their on-going activities in Georgia.

An annual report to the Council and European Parliament is foreseen in the proposed legislative decision, comprising an assessment of the implementation of this operation. An independent ex-post evaluation of the assistance will be carried out within two years after the expiry of the availability period.

### **1.5. Grounds for the proposal/initiative**

#### *1.5.1. Requirement(s) to be met in the short or long term*

The disbursement of the assistance will be conditional upon a satisfactory track record in the implementation of the economic programme between Georgia and the IMF, which was approved by the IMF Executive Board on 12 April 2017. In addition, the Commission shall agree with the Georgian authorities on specific policy conditions, listed in a Memorandum of Understanding, to be satisfactorily met before the second instalment is released by the Commission.

#### *1.5.2. Added value of EU involvement*

The proposed MFA will help Georgia overcome the consequences of a weak external environment which, through reduced exports and remittances, has contributed to relatively subdued GDP growth in 2016, as well as reduce the vulnerability of the country's balance-of-payments position and cope with the adaptation to the requirements of the DCFTA. In doing so, the proposed MFA will contribute to promoting macroeconomic stability and structural reforms in the country. By complementing the resources made available by the international financial institutions, other EU instruments and other donors, it will contribute to the overall effectiveness of the package of financial support provided by the international donor community.

The proposed programme will also strengthen the government's reform commitment and its aspiration towards closer relations with the EU. This result will be achieved, inter alia, through appropriate conditionality for the disbursement of the assistance. In a larger context, the programme will signal to the other countries in the region that the EU continues to support countries embarking on a clear path towards political reforms in times of economic difficulties.

#### *1.5.3. Lessons learned from similar experiences in the past*

Since 2004, more than fifteen ex-post evaluations have been carried out on macro-financial assistance operations. These evaluations conclude that MFA operations contribute, albeit sometimes modestly and indirectly, to the improvement of external sustainability and macroeconomic stability and to the achievement of structural reforms in the recipient country. In most cases, MFA operations have had a positive effect on the balance of

payments of the beneficiary country and helped to relax their budgetary constraints. They have also led to a somewhat higher economic growth.

#### 1.5.4. *Compatibility and possible synergy with other appropriate instruments*

The EU is the biggest donor to Georgia. The EU's assistance committed for Georgia under the European Neighbourhood Partnership Instrument (ENPI) for the period 2007-2013 totalled EUR 452 million. For the period 2014-2020, under the European Neighbourhood Instrument (ENI), the EU's assistance to Georgia may range between a minimum allocation of EUR 610 million and a maximum allocation of EUR 746 million. These funds are complemented by financing from other EU instruments, such as the Neighbourhood Investment Facility (NIF). In addition to bilateral cooperation programmes, Georgia benefits from various regional programmes mainly in the area of transport, energy and environment. Georgia also participates in the initiatives open to all Neighbourhood countries such as Erasmus+, TAIEX and SIGMA. In addition to the ENI, Georgia is eligible for funding under the EU thematic instruments and programmes: the European Instrument for Democracy and Human Rights (EIDHR), the Instrument contributing to Stability and Peace (IcSP), as well as the programmes on Civil Society Organisations and Local Authorities, Human Development and Migration & Asylum. The European Investment Bank has also provided loans in the amount of EUR 1 267 million since 2010.

The key value added of the MFA in comparison to other EU instruments would be to help create a stable macroeconomic framework, including by promoting a sustainable balance of payments and budgetary situation, and an appropriate framework for structural reforms. MFA does not provide regular financial support for the long-term economic and social development of the recipient countries. It is to be discontinued as soon as the country's external financial situation has been brought back onto a sustainable path. Afterwards, regular EU cooperation assistance instruments are meant to take over.

MFA is also meant to be complementary to interventions by the international financial institutions, in particular the adjustment and reform programme supported by the IMF's EFF and the Development Policy Loans of the World Bank.

#### 1.6. **Duration and financial impact**

X Proposal/initiative of **limited duration**

X Proposal/initiative in effect for two and a half years from the entry into force of the Memorandum of Understanding, as stated in Article (1.4) of the Decision

X The financial impact is expected to occur from 2017 to 2020

#### 1.7. **Management mode(s) envisaged<sup>16</sup>**

X **Direct management** by the Commission

### 2. **MANAGEMENT MEASURES**

#### 2.1. **Monitoring and reporting rules**

This assistance is of macroeconomic nature and its design is consistent with the IMF-supported economic programme. The monitoring of the action by the Commission services will take place on the basis of progress in the implementation of the IMF programme and

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<sup>16</sup> Details of management modes and references to the Financial Regulation may be found on Europa: [http://ec.europa.eu/budget/explained/management/managt\\_who/who\\_en.cfm](http://ec.europa.eu/budget/explained/management/managt_who/who_en.cfm)

specific reform measures to be agreed with the Georgian authorities in a Memorandum of Understanding (see also point 1.4.4).

## **2.2. Management and control system**

### *2.2.1. Risk(s) identified*

There are fiduciary, policy and political risks related to the proposed MFA operation.

There is a risk that the macro-financial assistance could be used in a fraudulent way. As MFA is not designated to specific expenses by Georgia, this risk is related to factors such as the general quality of management systems in the central bank and the ministry of finance and the appropriateness of internal and external audit capabilities.

A second risk stems from the possibility that Georgia will fail to service the financial liabilities towards the EU stemming from the proposed MFA loans (default or credit risk), which could be caused, for example, by a significant additional deterioration of the balance of payments and fiscal position of the country.

Another key risk to the operation stems from the regional geopolitical situation, in particular due to Georgia's still difficult relations with Russia and the breakaway regions of Abkhazia and South Ossetia. A worsening of this regional geopolitical situation could have a negative impact on Georgia's macroeconomic stability, affecting the IMF programme performance and the disbursement and/or repayment of the proposed MFA.

Finally, the Georgian economy faces other broader risks due to an uncertain regional and global economic outlook. Regional and global growth is expected to pick up in 2017, but will remain subdued and subject to downside risks of protectionism, volatile financial markets and potential further appreciation of the US dollar. If these risks materialise, they could result in lower economic growth in Georgia which, coupled with persistently high inequality and a relatively limited social safety net, could weigh on the budget and reduce domestic support for structural reforms.

### *2.2.2. Control method(s) envisaged*

The macro-financial assistance will be liable to verification, control and auditing procedures under the responsibility of the Commission, including the European Antifraud Office (OLAF), and by the European Court of Auditors.

### *2.2.3. Costs and benefits of controls and probable non-compliance rate*

The basic costs for the Commission related to the methods of verification and control are described in Table 3.2.1. In addition, there are costs for the European Court of Auditors and of possible interventions of OLAF. The Operational Assessment of financial and administrative circuits of Georgia, to be concluded by the Commission services – with the support of external consultants – in 2017, helps to assess risks of misuse of the funds and, as a collateral benefit, provides useful information on the necessary reforms in the area of public finance management, which can then be reflected in the policy conditionality of the operation. Regarding the probable non-compliance rate, the risk of non-compliance (in the form of non-repayment of the loan or misuse of the funds) is judged to be low, based on the experience with the MFA instrument since its creation.

## **2.3. Measures to prevent fraud and irregularities**

To mitigate the risks of fraudulent use several measures will be taken:

First, the Loan Agreement and the Grant Agreement will comprise a set of provisions on inspection, fraud prevention, audits, and recovery of funds in case of fraud or corruption. Also, the assistance will be paid to a specific account of the National Bank of Georgia.

Moreover, the Commission services, with the support of external consultants, are currently finalising a draft Operational Assessment on the reliability of Georgia’s financial circuits and administrative procedures that are relevant to this type of assistance. The consultants’ preliminary findings (as received in September 2017) conclude that the current status of the administrative and financial circuits of Georgia is adequate for managing a new MFA operation although some weaknesses remain.

Finally, the assistance will be liable to verification, control and auditing procedures under the responsibility of the Commission, including the European Antifraud Office (OLAF) and the European Court of Auditors.

### 3. ESTIMATED FINANCIAL IMPACT OF THE PROPOSAL/INITIATIVE

#### 3.1. Heading(s) of the multiannual financial framework and expenditure budget line(s) affected

- Existing budget lines

01 03 02: Macro-financial assistance

01 03 06 – Provisioning of the Guarantee Fund

In order of multiannual financial framework headings and budget lines.

Heading of multiannual financial framework	Budget line	Type of expenditure	Contribution			
	Number [Description.....]	Diff./non-diff. <sup>(17)</sup>	from EFTA countries <sup>18</sup>	from candidate countries <sup>19</sup>	from third countries	within the meaning of Article 18(1)(aa) of the Financial Regulation
4	01 03 02 Macro-financial assistance	Diff.	NO	NO	NO	NO
4	01 03 06 Provisioning of the Guarantee Fund	Non-diff.	NO	NO	NO	NO

The Guarantee Fund for external actions has to be provisioned according to the Fund Regulation,<sup>20</sup> using the appropriations under budget line 01 03 06 (“Provisioning of the Guarantee Fund”), at a rate of 9% of the total outstanding liabilities. The provisioning

<sup>17</sup> Diff. = Differentiated appropriations / Non-Diff. = Non-differentiated appropriations.

<sup>18</sup> EFTA: European Free Trade Association.

<sup>19</sup> Candidate countries and, where applicable, potential candidate countries from the Western Balkans.

<sup>20</sup> Council Regulation (EC, EURATOM) No 480/2009 of 25 May 2009 establishing a Guarantee Fund for external actions, OJ L 145, 10.6.2009, p. 10.

amount is calculated at the beginning of the year “n” as the difference between the target amount and the Fund’s net assets at the end of the year “n-1”. This provisioning amount is entered in year “n” into the “n+1” draft budget and effectively paid in one transaction at the beginning of the year “n+1” from the budget line “Provisioning of the Guarantee Fund” (budget line 01 03 06). As a result, 9% (i.e. a maximum of EUR 3.15 million) of the effectively disbursed amount will be considered in the target amount at the end of the year “n-1” for the calculation of the provisioning of the Fund.

New budget lines requested: not applicable.

### 3.2. Estimated impact on expenditure

#### 3.2.1. Summary of estimated impact on expenditure

#### Heading of multiannual financial framework:

4

EUR million (to three decimal places)

DG: ECFIN			Year 2017 <sup>21</sup>	Year 2018	Year 2019	Year 2020	Year 2021	TOTAL
• Operational appropriations								
Budget line 01 03 02 Macro-financial assistance	Commitments	(1)		10				10
	Payments	(2)		10				10
Budget line 01 03 06 Provisioning of the Guarantee Fund	Commitments	(1a)				3.15		3.15
	Payments	(2a)				3.15		3.15
Operational assessment and ex-post evaluation								
Budget line 01 03 02 Macro-financial assistance	Commitments	(3)	0.07			0.15		0.22
	Payments	(3a)	0.07				0.15	0.22
<b>TOTAL appropriations for DG ECFIN</b>	Commitments	(4) =1+1a +3	0.07	10		3.3		13.37
	Payments	(5) =2+2a +3	0.07	10		3.15	0.15	13.37

<b>TOTAL appropriations under HEADING 4 of the multiannual financial framework</b>	Commitments	=4	0.07	10		3.3		13.37
	Payments	=5	0.07	10		3.15	0.15	13.37

<sup>21</sup> Year in which implementation of the proposal/initiative starts.

**If more than one heading is affected by the proposal / initiative:**

EUR million (to three decimal places)

<b>Heading of multiannual financial framework:</b>		<b>5</b>		<b>‘Administrative expenditure’</b>			
		<b>Year 2017</b>	<b>Year 2018</b>	<b>Year 2019</b>	<b>Year 2020</b>	<b>Year 2021</b>	<b>TOTAL</b>
DG: ECFIN							
• Human resources		0.041	0.058	0.006	0.010	0.010	<b>0.125</b>
• Other administrative expenditure		0.010	0.020				<b>0.030</b>
<b>TOTAL DG ECFIN</b>	Appropriations	0.051	0.078	0.006	0.010	0.010	<b>0.155</b>
<b>TOTAL appropriations for HEADING 5 of the multiannual financial framework</b>	(Total commitments = Total payments)	0.051	0.078	0.006	0.010	0.010	0.155

EUR million (to three decimal places)

		<b>Year 2017</b>	<b>Year 2018</b>	<b>Year 2019</b>	<b>Year 2020</b>	<b>Year 2021</b>	<b>TOTAL</b>
<b>TOTAL appropriations under HEADINGS 1 to 5 of the multiannual financial framework</b>	Commitments	0.121	10.078	0.006	3.310	0.010	<b>13.525</b>
	Payments	0.121	10.078	0.006	3.16	0.16	<b>13.525</b>



3.2.2. *Estimated impact on operational appropriations*

- The proposal/initiative does not require the use of operational appropriations
- The proposal/initiative requires the use of operational appropriations, as explained below:

Commitment appropriations in EUR million (to three decimal places)

Indicate objectives and outputs		Year 2017		Year 2018		Year 2019		Year 2020		Year 2021		TOTAL	
		Type <sup>22</sup>	Number	Cost	Number	Cost	Number	Cost	Number	Cost	Number	Cost	Total number
SPECIFIC OBJECTIVE NO 1 <sup>23</sup>													
- Output 1	Grant disbursements			2	10							2	10
- Output 2	Provisioning of the Guarantee Fund							1	3.15			1	3.15
- Output 3	Operational assessment	1	0.07										0.07
- Output 4	Ex-post evaluation							1	0.15			1	0.15
Subtotal for specific objective No 1				2	10			2	3.3			5	13.37
<b>TOTAL COST</b>				2	10			2	3.3			5	13.37

<sup>22</sup> Outputs are products and services to be supplied (e.g.: number of student exchanges financed, number of km of roads built, etc.).

<sup>23</sup> As described in point 1.4.2. ‘Specific objective(s)...’

### 3.2.3. Estimated impact on appropriations of an administrative nature

#### 3.2.3.1. Summary

- The proposal/initiative does not require the use of appropriations of an administrative nature
- The proposal/initiative requires the use of appropriations of an administrative nature, as explained below:

EUR million (to three decimal places)

	Year 2017	Year 2018 <sup>24</sup>	Year 2019	Year 2020	Year 2021	TOTAL
<b>HEADING 5 of the multiannual financial framework</b>						
Human resources	0.041	0.058	0.006	0.010	0.010	<b>0.125</b>
Other administrative expenditure	0.010	0.020				<b>0.030</b>
<b>Subtotal HEADING 5 of the multiannual financial framework</b>	<b>0.051</b>	<b>0.078</b>	<b>0.006</b>	<b>0.010</b>	<b>0.010</b>	<b>0.155</b>
<b>Outside HEADING 5<sup>25</sup> of the multiannual financial framework</b>						
Human resources						
Other expenditure of an administrative nature						
<b>Subtotal outside HEADING 5 of the multiannual financial framework</b>						
<b>TOTAL</b>	<b>0.051</b>	<b>0.078</b>	<b>0.006</b>	<b>0.010</b>	<b>0.010</b>	<b>0.155</b>

The administrative appropriations required will be met by the appropriations of the DG which are already assigned to management of the action and/or which have been redeployed within the DG, together if necessary with any additional allocation which may be granted to the managing DG under the annual allocation procedure and in the light of budgetary constraints.

<sup>24</sup> Year in which implementation of the proposal/initiative starts.

<sup>25</sup> Technical and/or administrative assistance and expenditure in support of the implementation of EU programmes and/or actions (former 'BA' lines), indirect research, direct research.

### 3.2.3.2. Estimated requirements of human resources

- The proposal/initiative does not require the use of human resources.
- The proposal/initiative requires the use of human resources, as explained below:

*Estimate to be expressed in full time equivalent units*

	Year 2017	Year 2018	Year 2019	Year 2020	Year 2021		
<b>• Establishment plan posts (officials and temporary agents)</b>							
01 01 01 01 (Headquarters and Commission's Representation Offices)	0.30	0.42	0.04	0.07	0.07		
XX 01 01 02 (Delegations)							
XX 01 05 01 (Indirect research)							
10 01 05 01 (Direct research)							
<b>• External personnel (in Full Time Equivalent unit: FTE)<sup>26</sup></b>							
XX 01 02 01 (CA, INT, SNE from the "global envelope")							
XX 01 02 02 (CA, INT, JED, LA and SNE in the delegations)							
<b>XX 01 04 yy<sup>27</sup></b>	- at Headquarters						
	- in delegations						
<b>XX 01 05 02 (CA, SNE, INT - Indirect research)</b>							
10 01 05 02 (CA, SNE, INT - Direct research)							
Other budget lines (specify)							
<b>TOTAL</b>	<b>0.30</b>	<b>0.42</b>	<b>0.04</b>	<b>0.07</b>	<b>0.07</b>		

**XX** is the policy area or budget title concerned.

The human resources required will be met by staff from the DG who are already assigned to management of the action and/or have been redeployed within the DG, together if necessary with any additional allocation which may be granted to the managing DG under the annual allocation procedure and in the light of budgetary constraints.

Cost of the staff needed is estimated on the basis of 30% of the annual expenditure for an AD5-AD12 grade official.

Description of tasks to be carried out:

Officials and temporary staff	<p>HoU: Supervise and manage the operation, negotiate the Memorandum of Understanding, lead missions and assess progress with conditionality compliance.</p> <p>Desk: Prepare the Memorandum of Understanding, liaise with the authorities and the IFIs, liaise with external experts for the operational assessment and ex-post evaluation, conduct review missions, prepare Commission staff reports and Commission procedures related to the management of the assistance.</p>
External staff	N/A

<sup>26</sup> CA= Contract Agent; LA = Local Agent; SNE = Seconded National Expert; INT = agency staff ('Intérimaire'); JED= 'Jeune Expert en Délégation' (Young Experts in Delegations).

<sup>27</sup> Sub-ceiling for external staff covered by operational appropriations (former 'BA' lines).

3.2.4. *Compatibility with the current multiannual financial framework*

- X Proposal/initiative is compatible the current multiannual financial framework.

3.2.5. *Third-party contributions*

- X The proposal/initiative does not provide for co-financing by third parties.

**3.3. Estimated impact on revenue**

- X Proposal/initiative has no financial impact on revenue.

**COM (2017) 559**

**Information Note**

**1. Proposal**

On a proposal for decision of the European Parliament and of the Council, providing further macro-financial assistance to Georgia

**2. Date of Commission document**

29.9.2017

**3. Number of Commission document**

COM (2017) 559 final

**4. Number of Council document:**

2017/0242 (COD)

**5. Dealt with in Brussels by**

[EFC/EWG and ECOFIN]

**6. Department with primary responsibility**

Department of Finance

**7. Other Departments involved**

None

**8. Background to, Short summary and aim of the proposal**

*MFA proposal details*

- The government of Georgia requested Macro-Financial Assistance (MFA) from the EU in June 2017. In light of this request and the economic situation in Georgia, the Commission has submitted a proposal to the European Parliament and the Council for MFA to Georgia, based on Article 212 of the TFEU.
- The proposed new MFA will help Georgia cover part of its external financing needs for the period of 2017-2020 which are estimated at US\$752 million (€671 million).<sup>28</sup>

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<sup>28</sup> Conversions in this document are based on a EUR/USD exchange rate of 1.12.

### *Macroeconomic outlook & rationale for MFA proposal*

- Georgia continues to face a weak external environment, which, through reduced exports and remittances, has contributed to the relatively subdued GDP growth.
- Georgia has also been impacted by a depreciation in the currencies of its main trading partners. The effects of this exchange rate volatility are amplified by high dollarisation in the Georgian economy.
- Georgia's macroeconomic outlook remains vulnerable. Ongoing fiscal consolidation may weaken domestic demand and lower economic growth. In addition, the Georgian economy faces broader risks due to an uncertain regional and global economic outlook, external imbalances, and potential further appreciation of the US dollar.
- The proposed new MFA would support economic stabilisation and the structural reform agenda of Georgia, supplementing resources made available from the IMF. It will reduce the economy's short-term balance of payments and fiscal vulnerabilities.
- Georgia meets the criteria for receiving MFA grants, notably due to its level of economic and social development (as measured by the country's per-capita income and incidence of poverty) and its relatively high indebtedness.

### *Previous MFA & link to other programmes*

- The proposed new MFA operation is the third one after Georgia's military conflict with Russia in August 2008. The last tranche of the 2015-2017 MFA operation was disbursed in May 2017.
- It will be designed and implemented in coordination with the adjustment and reform programmes Georgia has agreed with the IMF and the World Bank, along with the reforms agreed in the context of the EU's budget support operations and the DCFTA (Deep and Comprehensive Free Trade Area) agreement.

### *Disbursements*

- The Commission is submitting a proposal to the European Parliament and the Council for an amount of up to €45 million, of which €35 million would be in the form of loans and €10 million in the form of grants.
- The first tranche would indicatively be composed of a loan element of €15 million and a grant element of €5 million, and the second tranche of a loan element of €20 million and a grant element of €5 million.

## **9. Legal basis of the proposal**

The legal basis for this proposal is Article 212 (2) TFEU.

## **10. Voting Method**

The Council, acting by a qualified majority (QMV) on a proposal from the Commission, shall decide on any change to be made to the programme.

## **11. Role of the European Parliament**

Codecision procedure (COD) (Ordinary legislative procedure). In order to ensure that the European Parliament and the Council are able to follow the implementation of this Decision, the Commission should regularly inform them of developments relating to the assistance and provide them with relevant documents.

## **12. Category of proposal**

Macro-Financial Assistance from the EU.

## **13. Implications for Ireland & Ireland's Initial View**

No major implication for Ireland. Ireland approves the proposal by the Commission to provide further macro-financial assistance to Georgia.

## **14. Impact on the public**

N/A

## **15. Have any consultations with Stakeholders taken place or are there any plans to do so?**

MFA is provided as an integral part of the international support for the economic stabilisation of Georgia. In the preparation of this proposal for MFA, the Commission services have consulted with the IMF and the World Bank, which have already put in place sizeable financing programs and are preparing new ones. The Commission has also been in regular contact with the Georgian authorities.

## **16. Are there any subsidiarity issues for Ireland?**

No. The subsidiarity principle is respected as the objectives of restoring short-term macroeconomic stability in Georgia cannot be sufficiently achieved by the Member States alone and can be better achieved by the European Union. The main reasons are the budgetary constraints faced at the national level and the need for strong donor coordination in order to maximise the scale and effectiveness of the assistance.

## **17. Anticipated negotiating period**

N/A

## **18. Proposed implementation date**

The proposal includes a sunset clause. The proposed MFA would be made available for two and a half years, starting from the first day after the entry into force of the Memorandum of Understanding.

The MFA operation under consideration would amount to a maximum of €45 million, consisting of loans of up to €35 million and grants of up to €10 million. Given the proposed size of the MFA, the Commission is considering releasing the assistance in two instalments. The first tranche would indicatively be composed of a loan element of €15 million and a grant element of €5 million, and the second tranche of a loan element of €20 million and a grant element of €5 million.

## **19. Consequences for national legislation**

N/A

## **20. Method of Transposition into Irish law**

N/A

## **21. Anticipated Transposition date**

N/A

## **22. Consequences for the EU budget in Euros annually**

The planned assistance will be provided in the form of loans and grants. The loan part will be financed through a borrowing operation that the Commission will conduct on behalf of the EU. The budgetary impact of the loan assistance will correspond to the provisioning of the EU's Guarantee Fund for external actions, at a rate of 9 per cent of the amounts disbursed, from budget line 01 03 06 ("Provisioning of the Guarantee Fund").

Assuming that the two loan disbursements (of €15 million for the first tranche and €20 million for the second tranche) will be made in 2018, the provisioning will take place in the 2020 budget, in accordance with the rules governing the Guarantee Fund mechanism, for an amount of €3.15 million.

The grant element of the assistance (€10 million in total, i.e. €5 million for each of the two tranches) will be financed from commitment appropriations of the 2018 budget, under the budget line 01 03 02 (Macro-financial assistance), with payments also taking place in 2018.<sup>29</sup>

Based on current projections on the utilisation of the budget lines 01 03 02 and 01 03 06, the Commission assesses that the budgetary impact of the proposed MFA operation for Georgia can be accommodated.

## **23. Contact name, telephone number and e-mail address of official in Department with primary responsibility**

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**Date 17 October 2017**

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<sup>29</sup> Depending on the pace of the legislative process and, thereafter, the implementation of the MFA operation, the disbursement of the proposed assistance may take place in 2018 or be split between 2018 and 2019.