Macro-financial assistance to Georgia

2009/0147(CNS) - 16/10/2009 - Legislative proposal

PURPOSE: to provide macro-financial assistance to Georgia in the form of grant instalments for a total amount of EUR 46 million.

PROPOSED ACT: Council Decision.

BACKGROUND: Georgia's macro-economic performance was very strong until August 2008. Its real growth figures were above 9% in 2005 and 2006 and 12% in 2007. In the first half of 2008 the annual growth rate remained robust at 8.6%. Yet, the military conflict with Russia that erupted in August 2008 dented the strong growth performance of the previous years. The global financial crisis that has been developing since late 2008 further aggravated Georgia's economic situation. The IMF Board approved in mid-September 2008 an 18-month stand-by arrangement (SBA) for USD 750 million (which constitutes exceptional access at 300 percent of Georgia's quota). At the time of the preparation of the programme, the IMF estimated that Georgia's external financing needs for the period 2008-2010 not covered by the resources expected from the IMF would be about USD 650 million, including USD 450 million for 2009-2010.

Based on this estimated external financing gap, the Commission pledged macro-financial assistance of EUR 46 million. MFA from the EU would cover about 13% of the residual financing needs in 2009-2010.

IMPACT ASSESSMENT: macro-financial assistance is linked to the beneficiary country's economic programme supported by the IMF and covers part of Georgia's immediate external financing needs. The disbursements are tied to the use of IMF resources and therefore have a direct link to the implementation by the beneficiary of the agreed macroeconomic and structural policies and its pace of economic recovery. Project finance and/or technical assistance would not be suitable to address these macroeconomic objectives. When allocated to the budget deficit financing, as proposed in the case of Georgia, the grant disbursements increase the envelope which the government can use to finance fiscal measures during the economic downturn. Unlike the ENPI budget support operations, the macro-financial assistance is exceptional in nature and the timeframe for the assistance is limited to Georgia's stand-by arrangement with the IMF.

CONTENT: the Community shall make available to Georgia **macro-financial assistance in the form of grant instalments in a total amount of EUR 46 million**. The assistance will contribute to covering Georgia's residual external financing needs in 2009-2010 as identified by the IMF. The proposed macro-financial assistance is intended to run in parallel to the stand-by arrangement with the IMF approved in September 2008. This assistance, intended to be allocated to the financing of the deficit of the state budget, is part of a comprehensive Community package of up to EUR 500 million put in place in support of Georgia's recovery in the aftermath of the August 2008 armed conflict with Russia. It contributes also to helping Georgia address the consequences of the global economic and financial crisis.

The assistance, along with the bulk of the donor support to Georgia (with the notable exception of IMF funds) is planned to be channelled to the budget given that the financial constraints faced by the Georgian public finances appear at present as particularly severe.

The assistance will be disbursed in **two instalments in 2009-2010**. It will be managed by the Commission. Specific provisions on the prevention of fraud and other irregularities, consistent with the

Financial Regulation, will be taken into account. The first tranche is scheduled for late 2009, the second tranche is planned will be disbursed in early 2010. The macro-financial assistance could be frontloaded if warranted by the evolution of the economic situation in Georgia.

The conditions attached to the disbursement of the grant instalments will include the successful implementation of the IMF SBA and the fulfilment of specific conditions in a number of key policy areas that the European Commission and the government of Georgia will agree upon. The Commission intends to focus on a limited number of areas of particular importance for macro-financial stability, in particular public finances – thus following up on the previous EU macro-financial assistance to Georgia – and financial sector reforms. The conditions will be consistent with the priorities of the EU-Georgia ENP Action Plan.

BUDGETARY IMPLICATIONS: the assistance would be financed from commitment appropriations in 2009 under budget line 01 03 02 (Macroeconomic assistance), with payments taking place in 2009 and 2010.