Further macro-financial assistance to Georgia

2017/0242(COD) - 29/09/2017 - Legislative proposal

PURPOSE: to provide macro-financial assistance to Georgia.

PROPOSED ACT: Decision of the European Parliament and of the Council.

ROLE OF THE EUROPEAN PARLIAMENT: the European Parliament decides in accordance with the ordinary legislative procedure and on an equal footing with the Council.

BACKGROUND: relations between the European Union and Georgia continue to develop within the framework of the **European Neighbourhood Policy** (ENP) and the Eastern Partnership. The EU-Georgia Association 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.

Georgia continues to face a **weak external environment**, which, through reduced exports and remittances, has contributed to the relatively subdued GDP growth of 2.7% in 2016 (compared to 2.9% in 2015 and 4.6% in 2014). Georgia's fiscal deficit remains significant and its public debt-to-GDP ratio has increased. Georgia's balance of payments position remains vulnerable due to a very large current account deficit and high external debt.

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 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.

In view of Georgia's residual external financing needs, the **Georgian authorities requested complementary macro-financial assistance from the Union in June 2017**. The proposed new MFA operation is the third one after Georgia's military conflict with Russia in August 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 EU's macro-financial assistance is an exceptional emergency instrument aimed at addressing severe balance-of-payment difficulties in third countries.

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.

CONTENT: the proposed new MFA operation under consideration would amount to a maximum of **EUR 45 million.** It will help Georgia cover part of the external financing needs for the period of 2017-2020, which are estimated at USD 752 million. 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.

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**.

The Commission is considering releasing the assistance in two instalments.

Disbursements would be conditional on successful reviews under the IMF programme and on the effective drawing by Georgia on IMF funds. The Commission 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 and the World Bank.

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.

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.

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

The Commission should also regularly inform the Council and the Parliament about developments relating to the assistance and provide them with relevant documents.

BUDGETARY IMPLICATION: assistance shall be provided in the form of a loan and grants.

The loan part will be financed through a borrowing operation that the Commission will conduct on behalf of the EU.

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.