Dear President Kim,

The Government of Georgia takes this opportunity to express its profound appreciation to the World Bank for strong support to Georgia's economic reform strategy. We highly value our partnership within the scope of the Second Development Policy Operations contributing to the inclusiveness of growth and increased competitiveness of the private sector. To share the benefit from economic growth widely in society, the government that took office in 2016 initiated Four-Point Reform Plan aiming at structural reforms and economic efficiency. We are fully committed to continue pursuing economic policies consistent with macroeconomic fundamentals.

Since last quarter of 2014, we have to weather an economic slowdown caused by challenging external environment. Despite this, the economy showed resilience. Our macroeconomic policies are guided by our commitment to gearing our fiscal, monetary and exchange rate policies toward supporting macroeconomic stability and growth. The exchange rate was allowed to play its role as a buffer against external shocks. The National Bank of Georgia appropriately focused on bringing inflation toward its target while fiscal policy supported economic growth. Our social assistance programs have helped protect the most vulnerable. We are committed to fiscal consolidation program to reducing fiscal deficit to 2.8 percent of GDP in the medium term, thus ensuring funding for all public social obligations are sustained and growth supportive public investments are in place. We are committed to a flexible exchange rate to safeguard external sustainability, export competitiveness, and high growth prospects. Flexible management of the exchange rate contributed to the correction of real exchange rate misalignment and improvements in terms of trade. We expect current account deficit to adjust accordingly improving to the sustainable level in the medium term as exports rebounds going forward. The impressive progress Georgia demonstrated on implementation of DCFTA requirements opens new trade and investment opportunities as well. Georgia already has free trade agreement with Turkey, Russia and other CIS countries. In June 2016, Georgia signed Free trade Agreement with European Union (EFTA), which will come into force next year. In September, 2016 Georgia finalized FTA negotiations with China and simultaneously started negotiations on FTA with Hong-Kong, China.

We are also committed to persevering with our medium-term structural reform agenda consistent with National Socio-Economic Development Strategy (Georgia 2020). Government initiated the four-point plan which implies the following strategic directions:
• Education reform; supporting skills development through education reform targeted at bridging the gap between skills demand and supply.

• Infrastructure development to increase regional connectivity and utilize Georgia’s potential as a transit country and a tourism country; specially in core road infrastructure that consists of the East-West highway, two south-north corridors crossing the highway in Tbilisi and Kutaisi; and the road connecting the biggest sea port cities (Poti and Batumi).

• Governance reforms; including having the general public more actively participating in decision making and improving the provision of government’s services on the basis of the one-stop shop principle.

• Economic reforms to promote job creation by improving, among others, the business and investment environment.

Collaboration between Government of Georgia and IMF is very essential for the country. IMF shares and supports Georgian Government’s Economic Policy, which provides sustainable economic growth. IMF team reached a staff-level agreement with the Georgian authorities - a three-year Extended Fund Facility (EFF) in the amount of SDR 201.4 million (about $285 million) or 100 percent of Georgia’s quota. The agreement is subject to approval by the IMF’s Executive Board, which is expected to consider Georgia’s request in April.

It is very important, that the program is based on Government’s four point reform plan. IMF admitted Georgia’s economic and structural reforms, which main goal is the maintenance of macroeconomic stability and supporting the economic growth.

Government of Georgia is committed to implement the following important structural reforms:

• Pension reform;
• Public Finance reforms;
• Deposit Insurance System;
• Capital Market Development Reforms;
• Public Private Partnership system development;
• Insolvency legislative framework creation;
• Land Reform;
• Insurance System Reform;
• Etc.
Support from the World Bank is critical to the success of our ambitious reform agenda. The proposed second inclusive growth development policy operation is designed to back-up key elements of our policies and build upon the recent gains in poverty reduction.

Improving management of public finances is at the core of our efforts to achieve fiscal sustainability through efficient use of public money. Meeting country's infrastructure needs requires considerable improvements in management of public capital expenditure. Therefore we are adopting the measures to strengthen public investment management system in public sector. In particular, we developed a framework for systematic capital investment identification, preparation, appraisal and selection, both for the central and the local governments. This framework includes PIM guidelines as well as a manual. At the first stage we will implement this framework in one central government ministry and in five municipalities. All projects, financed by the state budget, co-financed by the donors and totally financed by the donors, which are worth GEL 5 million or more, will be assessed under the new framework.

In order to improve fiscal management we will continue strengthening our macro-fiscal analysis and forecasting capacity. We introduced the information annex on macroeconomic risks to the budget law 2015 to include estimates of upsides and downsides of macro variables affecting the fiscal stance. We extended macro-fiscal analysis for the budget law 2016 to include information in quasi-fiscal risks emanating from possible contingent liabilities of state owned enterprises. Detailed fiscal risk assessment of SOEs, including analysis of their financial indicators as well as the key factors driving the SOEs' aggregate and individual financial performance and position has been conducted and the major fiscal risks have been identified. As part of macro-financial analysis, the overview of SOEs has been attached as a separate annex to the 2017 budget law and will future be attached to each annual budget law. The 2017 Statement of Fiscal Risks represents impressive progress in the disclosure fiscal risks related to the energy sector. The statement highlights the nature of the commitments that have been provided by ESCO and the government, the circumstances under which these fiscal risks could materialize and the steps being taken to mitigate them. Comprehensive disclosure would itself be a risk mitigation measure, because transparency tends to affect behavior by making decision-makers and their advisers more cautious as well as more proactive in taking mitigating action. The descriptive analysis is based on financial database we collected from majority asset holder SOEs associated with the central and local governments, while administrative data on turnover and employment was available for all SOEs in the country through revenue service database. Going forward we will institutionalize and substantially improve data collection process as part of tasks of the Ministry of Economy and Sustainable Development. We will further strengthen analysis of the SOEs fiscal risks assessment, especially in energy sector, as part of annex to each annual budget law.
We are committed to improve public administration to enhance the capacity of public servants. Our objective is to establish a professional public sector, boost the satisfaction of civil servants, eliminate institutional source of inefficiencies, and optimize staff size and remuneration in line with the functions performed by each budgetary entity. In this regard our medium term objective is in line with the requirements of European Union and Association Agreement. The new framework law on civil service was adopted in October 2015 based on best international practices. It is expected to be enacted from July 1, 2017. Meanwhile we have an ambitious agenda to develop set of secondary regulations to ensure smooth implementation. We therefore busy to draft Law on remuneration and Law on Legal Entities of Public Law. Apart from those important documents are finalizing 11 legal acts as defined by the civil service law before its entrance into force. The reform process is fully coordinated with development partners, that include EU, NATO, USAID, WB and is subject to active public consultations.

Our objective is to provide adequate poverty alleviation to the neediest population of Georgia. We developed strong and well-targeted social safety nets including both targeted social assistance and the Universal Health Care Program. After almost 10 years from establishment the methodology of Targeted Social Assistance has been reassessed and revised to better determine eligibility in January 2015. In this new methodology we revised the formula to compute the eligibility score by updating its variables and their weights and we also introduced a differential system of scores and benefit amount. With this change we will improve the targeting accuracy of the TSA program by reducing inclusion and exclusion errors. The revised TSA methodology was pre-tested during January to May 2015. Results from pre-testing indicated that there were winners and losers under the revised methodology. The Ministry of Labor, Health and Social Affairs is still in the process of assessing the families and the full implementation of the program will be completed in 2017. Most of the newly eligible households were from the bottom and second decile of the welfare distribution curve and those with children. The losers were primarily single elderly households. For this reason we introduced mitigation measures to compensate the single elderly by modifying coefficients of the formula.

Due to high self-referrals there are still about 100 000 households remaining to be re-assessed with the new methodology. As for revision of the coefficient for single elderly, modification options will be proposed after re-assessment of all remaining households (that were assessed with previous methodology) is over - end July 2017 and based on the results of the evaluation of the impact that the proposed modifications will have.

Improving financial protection reducing the out-of-pocket burden of health care expenditures remains one of the biggest challenges for the health sector in Georgia. We introduced Universal Health Care (UHC) program in February 2013, which has led to a major expansion
in population entitlement to publicly financed health services and definitely positively reflected on OOP indicators. Results of Household Utilization and Expenditures Surveys (HUES) from 2010 to 2014 showed that OOP expenses per household declined by 23 percent following the introduction of the UHC program. Meanwhile out-of-pocket spending of households on medicines continues to be high. We decided to apply, first, the budgetary, resources to subsidize medicines for those chronic diseases that have high prevalence and which also pose significant risk for catastrophic health expenditures forcing household into poverty. These diseases included hepatitis C, thalassemia, breast cancer, juvenile arthritis, tuberculosis, etc. - As an example, hepatitis C afflicts nearly 15 percent of the population and a 12 week course of medication costs more than USD 84,000.

We are also committed to address the gaps in the quality of health services, particularly for obstetric and neonatal care before, during and after childbirth. This will be done by establishing effective functional links between different levels of perinatal services and ensuring adequate management of obstetric and neonatal diseases, complications and emergencies. We piloted this initiative in the 2 regions of Imereti and Racha-Lechkhumi-Kvemo Svaneti in 2015. In 2016 the program was expanded in Tbilisi and five additional regions, Samegrelo, Guria, Shida Kartli and Kvemo Kartli, Autonomous Republic of Adjara. Health professionals in these areas have been trained and referral mechanisms implemented to ensure that right patients receive right level of care at right time. Initial results have shown a positive effect in the handling of maternal and newborn complications. Result of the perinatal services regionalization program will give us a good sense of the impact on maternal mortality rates and newborn health complications.

We believe one of the most important resources for Georgia’s economic and social progress is human capital. Therefore, we are committed to further development of the education and science system of Georgia to improve quality, relevance, and accessibility to facilitate a long-term economic growth and social stability of the country and to harmonize it with the EU standards. As part of our reform agenda, we have introduced a comprehensive framework for the regulation of the teaching profession. In 2015, the Government has adopted a new Teacher Recruitment, Professional Development and Career Advancement Scheme. The scheme is targeted at increasing competitiveness of teaching profession and improving quality of teaching and learning in Georgia. The implementation of the new system is ongoing for 2016-2017 academic year. Current progress include multiple-stage increase of teacher salaries vis-à-vis the categories introduced by the new scheme, distribution of all general education teachers within the four different categories and introduction of more effective instruments to measure teacher effectiveness. We have adopted the credit accumulation manual for teachers that describes all steps and measures needed to acquire credits under the new scheme. The manual demonstrates the ways of credit accumulation and spells out the instruments of evaluation so as to equip teachers with all the necessary information related to professional development. As an effort to increase access and quality of preschool education, we have adopted the national
standards and curriculum for pre-school (school readiness) education in August 2015. All institutions which have pre-school students (age of 5 and 6 years) are required to use the new standards and curriculum in the educational year (2015-16). At the same time the Parliament of Georgia has adopted New Law on Early and Preschool Care and Education in 2016 and accordingly elaboration of educational standards and curriculum for all ages will be finalized soon.

Georgia's 2014 census took place after gap of 12 years and it has immense implication for policy making and accuracy of indicators that we set to monitor and evaluate outcomes of the reforms under Georgia 2020. The population census is implemented by Geostat and is governed by the Law on Statistics (2009). In 2016 we amended the law to specify census frequency as at least every 10 years.

From January 2017 we started implementation of two separate surveys: household income and expenditure surveys (HIES) and labor force survey (LFS), the latter with a doubled sample size and quarterly frequency of reporting. The sampling frame of both HIES and LFS has been updated, using the last census data. The design of the surveys has been updated as well, taking into account best international practices. This will enable the country to enhance the government’s monitoring of poverty trends and effects of social spending, and improve the quality of data used for national accounts and consumer prices.

We deeply appreciate the support of the World Bank in the implementation of the strategic actions outlined above. We are looking forward to our continued successful partnership with the World Bank, including cooperation in the context of the proposed Development Policy Operation.

Allow me, Mr. President, to take this opportunity and extend my regards and esteem.

Sincerely,

Giorgi Kvirikashvili

Mr. Jim Yong Kim
President of the World Bank
Washington, DC