PROJECT INFORMATION DOCUMENT (PID)
APPRaisal STAGE
Report No.: PIDA250

<table>
<thead>
<tr>
<th>Project Name</th>
<th>Regional Development Project (P126033)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Region</td>
<td>EUROPE AND CENTRAL ASIA</td>
</tr>
<tr>
<td>Country</td>
<td>Georgia</td>
</tr>
<tr>
<td>Sector(s)</td>
<td>General water, sanitation and flood protection sector (60%), Urban Transport (30%), Sub-national government administration (8%), Vocational training (2%)</td>
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<tr>
<td>Lending Instrument</td>
<td>Specific Investment Loan</td>
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<td>Project ID</td>
<td>P126033</td>
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<td>Borrower(s)</td>
<td>Ministry of Finance</td>
</tr>
<tr>
<td>Implementing Agency</td>
<td>Georgia Municipal Development Fund</td>
</tr>
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<td>Environmental Category</td>
<td>F-Financial Intermediary Assessment</td>
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<tr>
<td>Date PID Prepared</td>
<td>08-Feb-2012</td>
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<td>Estimated Date of Appraisal Completion</td>
<td>08-Feb-2012</td>
</tr>
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<td>20-Mar-2012</td>
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<td>Decision</td>
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I. Project Context

Country Context
Following four years of rapid growth, backed by far-reaching reforms and strong FDI inflows, Georgia experienced a sharp economic downturn resulting from the August 2008 conflict and the global financial crisis. The authorities responded to the downturn with a countercyclical fiscal stimulus coupled with a marked reallocation of public expenditures toward social and infrastructure investments. As economic recovery takes hold, driven by higher exports and private investment, the authorities are winding down the stimulus and implementing fiscal adjustment to safeguard sustainability. Although economic recovery is underway, with growth estimated at 6.8 percent last year, there is significant uncertainty regarding the pace of economic growth in the future given global uncertainties and economy-wide structural issues, such as endemically low national savings rate and low productivity of the tradable sectors. The authorities are addressing macro-economic vulnerabilities through well designed fiscal, monetary and debt management policies. They are also engaged in negotiating a Deep and Comprehensive Free Trade Agreement that is expected to contribute not only to an enhanced market access for Georgian goods but also to the upgrading in tradeable industries.

Georgia is home to one of the world most competitive horizontal business environments - ranked 16th overall out of 183 countries according to the Doing Business Report, IFC 2012. In particular, Georgia ranks well in terms of business start-up, tax processes, investor protection, access to credit, enforcement of contracts, registering a property (among the top in the World), and dealing with construction permits.

The Government refocused efforts in the past six years by launching several initiatives to attract private investors in selected regions (Tbilisi, Adjara and Imereti) in various sectors. Georgia, however, has not yet fully tapped its potential to promote sustainable tourism in promising regions, such as Kakheti, or transform the rural economy through investment in agriculture supply chains for both export and import substitution.

In the framework of the CPS-PR for the period of FY12-FY13 presented to the Board in April 2011, the Government has asked the Bank to support regional development in Georgia by applying a programmatic approach. The proposed program of interventions will emphasize support to key pillars and drivers of economic growth in selected regions. This proposed initial Project will focus on support for the tourism sector and enabling the environment for the private sector to invest in Kakheti Region. Follow up interventions will likely focus on other economic sectors in Kakheti and/or replicate experience in another region.

II. Sectoral and Institutional Context
Georgia Regional Development Strategy: The Government of Georgia approved in June 25, 2010 (Government resolution no. 172), the State Strategy on Regional Development of Georgia for 2010-2017, prepared by the Ministry of Regional Development and Infrastructure (MRDI). The main objective of the strategy is to create a favorable environment for regional socio-economic development and improve living standards. These objectives will be attained through balanced socio-economic development, increased competitiveness and increased socio-economic equalization among the regions. The Government has been investing in Tbilisi as the growth pole of Georgia, as well as in Adjara and Kutaisi/Imereti (west of Georgia) as growth centers. To better utilize the tourism and agriculture potential of in Kakheti (east of Georgia) and to reduce internal socio-economic disparities, the Governments intends to invest in this region to enable it become a growth center.

In 2010, the UNDP assisted the Administration of the Governor of the Kakheti Region and the Kakheti Regional Development Agency in preparing a participatory Regional Development Strategy for Kakheti (2010-2014). The strategy concluded that tourism and agriculture offer significant development potential and proposed a priority action plan. Building on this program, the task team completed a supply chain analysis for tourism and agriculture. A rigorous economic analysis, drawing on the 2009 World Development Report, Reshaping Economic Geography, was also conducted to assess the institutional quality, infrastructural adequacy/connectivity, and proposed targeted interventions to foster growth in tourism. These analyses have informed the design of the project.

Kakheti is the largest region of Georgia with approximately 11,300 km². It consists of eight municipalities/Local Self-Governments (LSGs) and has a population of about 404,000, about 9% of the Georgia population, making it the fourth largest region. Due to its mountainous terrain, Kakheti is sparsely populated at 35 persons/km² in gross density compared to 75 persons/km² for Georgia. Most of the population lives in the two valleys of Alazani and Signagi. The region is sparsely urbanized, with about 21% of population living in cites.

Kakheti has always been at the heart of Georgia’s ancient culture, history and economy. Records from residents during the Stone Age have been documented. Kakheti was a key juncture on the Great Silk Road. It is home to unique cultural heritage assess. This includes the Nekresi Church Remnants (4th century AD), the Davit Gareji Caved Monastery (6th century AD), the Old Shuamta Basilica (5-6th century AD), the NinoTsminda Citadel (7th century AD), the Alaverdi Cathedral (11th century AD), the Bede Monastery (9-11th century AD), and the Gremi Archange Monastery Complex (16th century AD) among others. The ancient city of Telavi is the cultural and economic capital of Kakheti where early records of the city are cited by the Greek scholar Ptolemy (II century AD). Signangi and Kvareli are renowned for its unique architecture, Kakheti, also known as the cradle of vine and wine, has vineyards that cover the scenic Alazani and Signagi valleys. Local food processing plants are also found in Telavi, Signagi, Kvareli, and Akhmeta.

Kakheti is also home to three magnificently protected areas: Tusheti in the north, Lagodeki in the center, and Vashlovani in the south. Tusheti has preserved its unique cultural heritage, traditions and ceremonies over the years. It is renowned for its lush landscape and the historical villages of Dartlo and Omalo, which are distinguished by their vernacular architectural where residents have maintained their cultural endowments and pattern of life.

In contrast to other regions of Georgia, Kakheti has not undergone any significant transformation of its economy. Economic density in Kakheti is about GEL74,000/km², compared to GEL 409,000/km² in Adjara and GEL 52 million/ km² in Tbilisi. Agriculture, though declining in terms of contribution to GDP and employment, still represents a large part of the economy and remains less productive than elsewhere. Services, especially tourism, generate about 60 percent of the value added in Kakheti, while public administration is still playing a dominant role. The service sector, particularly hotels and restaurants, have taken on a more visible role.

The economic analysis of this Project has provided an overarching framework within which policy thinking regarding future development of Kakheti can be organized. This includes an analysis of the growth/employment impact of the proposed investments with sectoral breakdowns. The findings from the tourism value-chain analysis reveals huge tourism development potential, yet key challenges identified include:

- the vast majority of overnight visitors to Georgia are from low spending markets coming for business or to visit friends and relatives (VFR);
- the need for urban regeneration and the improvement in the quality of municipal infrastructure in key cultural centers (Telavi, Kvareli, and Dartlo);
- the low quality of municipal infrastructure (water, sanitation, access roads and solid waste disposal);
- limited hotel capacity;
- seasonality, particularly in the winter months;
- the lack of destination management organization and promotion activities;
- the lack of investor information, communication and cooperation among key investors to achieve a competitive edge; and
- inadequate service skills and foreign languages proficiency.

The proposed tourism strategy envisages developing Kakheti as a high quality geotourism destination throughout the year. It seeks to attract both domestic and international tourists, building on its cultural heritage and biodiversity, and shifting towards higher-spending visitors. The strategy details an integrated approach, using the concept of geotourism and applying a comprehensive urban regeneration effort at key centers of attraction (Telavi, Kvareli and Dartlo). The goal is to attract private investments, promote public-private partnerships, revitalize local business activity, define a full-fledged regional tourism circuit, and foster two leisure travel clusters along the following concepts:

- Cultural heritage/culinary tourism cluster: This cluster details landscape circuits to visit monuments, monasteries, museums and for visitors to experience the living culture of the Region (music, art, dance, culinary cuisine, mud SPA). It is designed to attract an older demographic (45-65 years of age) with higher levels of disposable income, education, and time for leisure travel than currently exists in Kakheti. Activities to be undertaken include branding, marketing, and event planning with improved facilities and services.
- Ecotourism/Adventure cluster: This cluster will highlight the pristine and protected landscape and target younger (25-45 years of age) though lower-spending visitors. Activities to be undertaken include circuit development, marketing, and training for both soft (hiking, birding, trekking, skiing, kayaking) and hard (mountaineering, paragliding, heli-skiing) adventure experiences.

Implementing this tourism vision through the proposed clusters will require a multi-faceted intervention: a minimum of infrastructure improvements to attract private sector investments; urban regeneration and conservation activities in key cultural centers (Telavi, Kvareli, and Dartlo); redevelopment of culture heritage sites to improve visitor experience; improved connectivity; improved planning and organization (e.g. destination management organization and office); institutional strengthening and capacity building; association/cluster development; geotourism mapping; tour circuit development; improved visitor services, signage and interpretation; and marketing activities. The proposed Project int ends to contribute to these activities.
III. Project Development Objectives
The Project Development Objective is to improve infrastructure services and institutional capacity related to the tourism economy in the tourism and heritage circuits of the Kakheti region.

IV. Project Description

Component Name
- Infrastructure Investment
- Institutional Development

V. Financing (in USD Million)

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<th>For Loans/Credits/Others</th>
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<td>International Bank for Reconstruction and Development</td>
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<td>Total</td>
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VI. Implementation

Building on the successful experience of the Regional & Municipal Infrastructure Development Project (RMIDP), this Project is a repeater in the sense of implementation arrangements, procurement, safeguards, financial management and disbursement arrangements. The Municipal Development Fund (MDF) will be responsible for all aspects project implementation. The MDF has grown up to become a solid non-bank financial intermediary (FI) that plays a very substantial role in funding and implementing regional and municipal infrastructure development. Due to the multi-sectoral nature of this Project, a Working Group has been established which involves all agencies concerned—namely, MDF, Georgia National Tourism Administration (GNTA), Agency for Culture Heritage Preservation of Georgia (ACHP), Culture Heritage Fund (CHF), Protected Areas Agency (PAA), United Water Company (UWC), Kakheti Governor Office, Ministry of Finance and Ministry of Regional Development & Infrastructure. The Working Group worked very well in the course of Project preparation.

All agencies in the Working Groups and LSGs in Kakheti have been actively involved with MDF in Project preparation activities, and will be involved in various aspects of bid evaluation and supervision. The detailed responsibility for each activity is as follows:
- Urban regeneration in Telavi and Kvareli: CHF, UWC and MDF.
- Revitalization in Dartlo heritage village and upgrading and management in 13 cultural heritage sites: ACHP, UWC and MDF.
- Screening of proposed private sector investments: The Working Group with MDF acting as a Secretariat. All proposed investments will be endorsed by the Supervisory Board.
- TA activities, i.e. Destination management, promotion, geotourism routes, tourism portal, skilled workforce development and capacity building: GNTA and MDF.
- Performance monitoring & evaluation activities: MDF.
- Procurement, safeguards, financial management, disbursement, supervision of all Project activities: MDF.

Governance structure of MDF: For the purpose of ensuring proper coordination and execution of the Project, the Government shall maintain the Supervisory Board of the MDF, chaired by the Prime Minister of Georgia, and comprising Minister of Finance, Minister of Economy and Sustainable Development, Minister of Regional Development, Minister of Justice, the Governor of Kakheti, Parliamentarians and NGOs. The functions of Board include, inter alia: (a) overall supervision of the implementation of the Project; (b) inter-agency coordination to achieve the Project objectives; and (c) review and approval of the annual work programs, budgets and reports for the operation of the MDF. The Supervisory Board met several times in the course of Project preparation and endorsed Project design, cost and procurement plan.

The Project incorporates recommendations on a Strategic Environmental, Cultural Heritage and Social Assessment (SECHSA), which analyzes the direct impact of proposed sub-projects as well as cumulative and induced impacts of tourism development in Kakheti. The SECHSA guides the preparation of sub-project-specific Environmental Assessments and/or Environmental Management Plans (EMPs). A Resettlement Policy Framework (RPF) has also been prepared to set out the principles of compensation in case that the Project implementation may have an impact of the property or user rights of affected people. It will govern preparation of Resettlement Action Plans (RAPs), if required. The MDF will carry overall responsibility of Project implementation, in compliance with the national legislation and the Bank safeguard policies. The Working Group members will continue to be directly involved in the implementation and supervision of the Project.

VII. Safeguard Policies (including public consultation)

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<th>Safeguard Policies Triggered by the Project</th>
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<td>Safety of Dams OP/BP 4.37</td>
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Projects on International Waterways OP/BP 7.50
Projects in Disputed Areas OP/BP 7.60

VIII. Contact point

World Bank
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