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Annex 1: Action Fiche Georgia

1. Identification

Title/Number	Support to Regional Development Reform in Georgia CRIS: ENPI/2010/21077		
Total cost	€19 million		
Aid method / Method of implementation	Sector Policy Support Programme (SPSP): - Sector budget support (centralised direct management) €17 million - Project mode (centralised direct management) €2 million		
DAC-code	15112	Sector	Decentralisation and support to sub national government

2. Rationale and country context

2.1. Country context and rationale for SPSP

2.1.1. *Economic and social situation and poverty analysis*

Georgia is a small transition economy with a population of about 4.5 million people and a gross national income (GNI) per capita of US\$ 2,470. Between 2004 and 2008, Georgia has benefited from a high rate of economic growth achieved through rapid implementation of economic liberalisation. Sound fiscal and monetary policies supported by structural reforms to unleash the supply-side dynamics positively impacted economic growth in larger Georgian cities, e.g. Batumi and Tbilisi. The August 2008 conflict and the following global economic downturn have altered the dynamic. Foreign investment and trade will be lower in the short-term which will affect GDP growth. Current projections¹ are for GDP to contract by about 4.5% - 5% in 2009, before growth resumes at about 2% in 2010.

Poverty remains high in the country (about 27.8%). The situation worsened after the August 2008 conflict, with 30,000 new Internally Displaced Persons (IDPs) left unemployed. Rural poverty rates are higher than urban poverty rates, and the incidence of extreme poverty in rural areas is almost twice that in urban areas. While rural areas largely depend on agriculture to generate revenues, the farming sector in Georgia is still based on archaic production methods with low productivity rates. Agriculture output only accounts for 11%² of the GDP but employs almost 60% of the population.

2.1.2. *National development policy*

The Government's poverty reduction strategy document "Georgia without Poverty", was approved on 31 January 2008. While this strategy still provides the main directions of the Government's reform programme, the pace of reforms was adjusted to the

¹ World Bank, International Monetary Fund figures

² Ministry of Economic Development of Georgia, Department of Statistics, Quarterly Bulletin 2009.I.

impact of the 2008 double shocks to the economy, the August conflict and the global economic crisis.

The Government prepares an annual strategy document titled *Basic Data and Directions*, which outlines the medium-term reform programme and its objectives, provides the medium-term macroeconomic framework, including the fiscal resource envelope and fiscal allocations, and includes descriptions of the individual sectoral strategies. The *Basic Data and Directions 2010-13* has been prepared and submitted to Parliament as of May 2009.

The proposed programme is in line with the EU's policy in Georgia, as expressed in the European Neighbourhood Policy Action Plan (ENP AP) which foresees under Priority Area 1, to "finalise and implement a strategy and programme for local government reform". The National Indicative Programme 2007-2010 includes among its sub-priorities "rural and regional development". The proposed programme will also contribute to the fulfilment of objective 3.5 of the Eastern Partnership "Supporting economic and social development – Memoranda of understanding on regional development". Proposed activities are within the scope of the European Neighbourhood and Partnership Instrument (ENPI) Regulation EC n. 1638/2006 of 24 October 2006, article 2.2(f), which foresees support measures "pursuing regional and local development efforts, in both rural and urban areas, in order to reduce imbalances and improve regional and local development capacities".

2.2. Sector context: policies and challenges

Poverty reduction and economic development policies for rural areas are high on the Government's agenda. Consequently, several national programmes were launched, namely the "Cheap Credit Programme", and the "100 agro-processing programme". A new agriculture strategy, presented in December 2008, includes, among its priorities, the development of rural areas through the establishment of an enabling environment for agricultural development, including extension services, import substitution and agro-processing.

Reducing regional disparities within Georgia is recognised as a key objective by the Government of Georgia (Government's programme "Georgia without Poverty 2008-2012" and Basic Directions and Data 2010-2013).

The Ministry of Regional Development and Infrastructure (MoRD&I) has committed itself to drafting and implementing a regional development strategy, and to setting up and conducting a broad donor coordination mechanism. In December 2008, a Task Force for Regional Development was set up with the support of the EC and other donors. In February 2009, the State Ministry for Regional Development became a full-fledged Ministry, adding infrastructure to its scope of competence. The Minister is also first vice-Prime Minister. On the 6th of June 2009, a Diagnostic Report on Regional Development in Georgia was made public. Based on this document, a strategy is being drafted by the Government of Georgia and should be approved during the first quarter of 2010. An action plan is expected for the summer 2010.

Local Self Governments in Georgia were significantly reformed by the 2005 organic law, which was implemented only in late 2006. While it introduces a series of territorial

and administrative changes to the benefit of local authorities' increased efficiency³, the decentralization process still faces serious challenges. Local authorities have limited administrative capacity and financial resources to be able to effectively plan and implement programmes and budgets conducive to economic development. A National Strategy for Local Self Government Reform is currently being prepared, that should improve the current situation in terms of functions distribution and decision making mechanisms⁴.

2.3. Eligibility for budget support

After several years of strong economic growth, albeit with increasingly high inflationary pressures, Georgia's economic prospects were severely affected in August 2008 by the conflict with Russia, and by the subsequent loss of business confidence. In spite of substantial support from the donor community, Georgia experienced negative growth through the second half of 2008 and in 2009.

The latest forecasts for 2009 predict a fall in GDP from 4% to 5.5%. Cuts in capital inflows and remittances caused a fall in imports and narrowed the payments deficit, easing foreign currency demand and inflation. Reduction in capital inflows also impacted negatively on budgetary revenue, however, the IMF's latest Review Mission concluded: "Georgia's strong record of reform and good performance under the Stand by Agreement give confidence about the authorities' ability to steer the economy through a difficult adjustment period". Despite risks to mid-term sustainability of growth the general condition of macroeconomic stability is satisfied, having the Government of Georgia operational programmes ongoing with IMF and other IFIs, including the World Bank and the Asian Development Bank.

The latest assessment of the status of Public Finance Management (PFM) reforms was updated by the EU Delegation in Tbilisi in November 2009, followed by the last review mission to assess compliance with conditions of the SPSP for PFM under the 2007 Annual Action Programme. Both the review mission and the Delegation report on PFM positively assessed the status of sector policy reforms in PFM. Therefore, the general condition on satisfactory PFM is satisfied.

Also a PFM reform programme (phase II) is currently being discussed (part of this AAP) and will run from 2010 to 2012. It shall entail provisions regarding the strengthening of the Chamber of Control of Georgia, responsible for auditing all public spending including those of the local self governments, and the State Procurement Agency.

2.4. Lessons learnt

Since 2005, the EU Delegation has been engaged with several Georgian institutions and donor organizations, (DFID, GTZ, USAID, UNDP/Sida, OSCE and the Council of Europe) in local/regional development activities.

Support was provided to rural development programmes, in four selected regions (Samtskhe Javakheti, Kvemo Kartli and Samagrelo/Upper Svanetia, later Rach-

³ LSG units were merged together so that the amount was reduced from 900 to 69.

⁴ See *Comments on the Draft National Strategy for the Local Self-Government Reform in Georgia (2009-2012)*, Council of Europe, DGDPA/DDI, 20 July 2009.

Lechkhumi), which aimed at reducing poverty and generating incomes for the rural population based on a deeper dialogue with local authorities and to further strengthen capacities in design and implementation of economic development plans.

These projects resulted in a number of municipal and regional socio-economic development plans (Samtshkhe Javakheti, Kvemo Kartli and Samagrelu/Uper Svanetia and Kakheti) based on regional/local strengths and peculiarities.

All projects have also successfully worked as a facilitator to provide agriculture extension services and support to farmer groups/co-operatives and establishing Rural Service Centres as independent organizations providing training and consultation, inputs and machinery to farmers. In addition the projects assisted in the establishment and consolidation of farmer co-operatives, which operate according to market economy principles.

Other keys for successes of the projects were the collaboration of local government with surrounding communities, as well as having an integrated approach, along the production chain. Local government became involved in the process and drew the communities into their planning process.

2.5. Complementary actions

The European Commission will support the Task Force for Regional Development until the adoption of the Strategy, while USAID shall take over to accompany the finalisation of the Action Plan.

In the first half of 2010, a service contract (under ENPI AAP 2009) will be launched in order to strengthen monitoring and evaluation mechanisms in the area of regional development. The European Commission is also preparing a Budget Support Programme in favour of IDPs, which focuses mainly on housing, local infrastructure and socio-economic integration (ENPI AAP 2009).

DFID GTZ, Sida, USAID and the Council of Europe were or are implementing similar projects to the TACIS Pilot Project for Poverty reduction in other regions. USAID is preparing a local infrastructure programme. As far as decentralization is concerned, the UNDP is assisting the preparation of the National Strategy for the Local Self Government Reform, together with the Council of Europe.

2.6. Donor coordination

Since 2005, the EU Delegation has co-ordinated with other donors (DFID, GTZ, USAID, UNDP/SIDA, OSCE and the Council of Europe) and with the Government of Georgia in the area of regional development. Since July 2009, the MoRD&I has convened two donor coordination meetings and has improved coordination mechanisms, with the setting up of a dedicated web site, including amongst others, a detailed list of donor funded projects.

3. Description

3.1. Objectives

The proposed programme aims at narrowing social and regional disparities in Georgia. The specific objective of the programme is to contribute to the implementation of the Strategy for Regional Development of Georgia. The expected results of the programme are as follows:

- Streamlining of institutional, legislative and territorial arrangements ensuring the long-term sustainability of a regional development policy in Georgia, including the adoption of municipal development plans.
- Contribution to creating the basis for a sustainable human resource management framework and a training/re-training mechanism for civil servants in charge of local/regional management at all territorial levels.
- Improving financing mechanisms legislation and regulations with a view to foster fiscal decentralization and reduce local self government dependency from the central level and building budgeting capacities at local level.
- Improving statistical instruments, data collection mechanisms (including gender disaggregated data) necessary for planning, monitoring and evaluating development at all territorial levels. Increased public access to and visibility of statistical data on regional development.
- Contribution to the implementation of a funding mechanism for innovative economic development projects designed at regional level.

3.2. Risks and assumptions

Risks:

Political instability, weak institutional capacity; high staff turnover and continuous restructuring of the public administration may hamper the effectiveness of the programme.

Assumptions:

The National Strategy on Regional Development is approved by the Government of Georgia; local elections to be held in May 2010 are deemed legitimate and democratic; progress is made with regards to progressively suppressing the structural causes for high turn over among local and regional level civil servants; transparent management of funding by local self government units and fostering of fiscal decentralization; continuous commitment of local self government and local stakeholders to participate in the programme.

The programme and related technical assistance will contribute to set up appropriate human resource measures, namely a comprehensive human resource management framework, qualification requirements for local self government/regional deconcentrated ministries branches, training needs assessments and curriculums.

3.3. Stakeholders

The Ministry of Regional Development and Infrastructure, as well as deconcentrated administration at regional level ("Governors' offices") and local self government will directly benefit from the programme.

Local self government will have better access, on a competitive basis, to local development funds, to implement activities included in the competitiveness promotion mechanism.

The local population will engage with the local authorities, together with foreign and local investors, as well as business associations (among which the banking sector).

Synergies, if not joint implementation of projects, will be sought with other donors. In particular, attention will be given to those donors that will continue support to the Government of Georgia in this area: GTZ, Sida, USAID.

3.4. Crosscutting Issues

Coherence with the cross-cutting issues can be characterised as follows:

- *Good governance and human rights:* While promoting better dialogue between different level of the state administration, local self government and civil society, the programme will promote good governance principles (particularly ownership, equity, transparency and anti-corruption) and democracy, especially at the local level.
- *Gender balance:* The programme will contribute to promote gender balance in several ways, and ensure that in areas such as training, women's participation is adequately considered.
- *Environment:* The competitiveness promotion and capacity building components of the programme will take into consideration the environmental sustainability of projects.

4. Implementation issues

4.1. Method of implementation

Direct centralised management.

4.2. Procurement and grant award procedures

All contracts implementing the action must be awarded and implemented in accordance with the procedures and standard documents laid down and published by the Commission for the implementation of external operations, in force at the time of the launch of the procedure in question.

Participation in the award of contracts for the present action shall be open to all natural and legal persons covered by the ENPI Regulation. Further extensions of this participation to other natural or legal persons by the concerned authorising officer shall be subject to the conditions provided for in article 21(7) of the ENPI Regulation.

4.3. Budget and calendar

The programme has a budget of €19 million, out of which €17 million will be used for budget support and €2 million for technical assistance (TA).

The €17 million component of budget support will be disbursed through 3 instalments. The first fixed tranche instalment of €5 million will be payable at the signature of the Financing Agreement to the Georgian State budget, subject to pre-conditions (e.g. with regard to sector management). The balance of €12 million will be paid in 2 equal instalments against successful achievement of policy conditions to be further identified in areas such as those listed under section 3.2.

A TA provision is included in the programme to finance (a) evaluation, audit, and visibility actions (approx. €0.2 million), (b) independent expertise to assess the fulfilment by the Government of Georgia of the conditions for disbursements (approx. €0.5 million), (c) capacity building to the recipient institutions (approx. €1.0 million)

(d) any other activities to promote participative sector management (approx. €0.3 million).

The operational duration of the programme should indicatively be a maximum of 60 months as from signature of the Financing Agreement.

4.4. Performance monitoring and criteria for disbursement

A Technical assistance project (€2.0 million, under ENPI AAP 2009) will contribute to the setting up of a Monitoring and Evaluation framework for the Regional Development Policy of Georgia. The project will aim to achieve the following results: a) designing a Regional Development Monitoring and Evaluation Policy, b) setting up a Regional Development Monitoring Agency and c) strengthening of existing training and coaching mechanisms for civil servants in charge of regional policy. The project is expected to start its activities in September 2010 and will be designed and implemented according to the Backbone Strategy on Reforming Technical Cooperation and the guidelines on "Making Technical Cooperation more effective".

The disbursement of budget support tranches will be subject to general and specific conditions, which will be laid down in the Financing Agreement implementing this programme.

The standard general eligibility conditions will apply for the disbursement of all tranches. The specific conditions will be based on agreed key areas of the Regional Development Strategy and action plan of the Government of Georgia, linked to results listed under §3.2 above and according to policy priorities as established in the EU-Georgia Action Plan.

In line with good practice, performance measurement will be made through a limited number of performance indicators per variable tranches in order to facilitate the assessment of progress in the sector and avoid over-burdening the reform process.

4.5. Evaluation and audit

Evaluation of the programme as well as external audits may be carried out if so decided by the European Commission. In such a case, they may be entrusted to independent consultants.

4.6. Communication and visibility

Communication and visibility will be organised in close cooperation with the Ministry of Regional Development and Infrastructure and in accordance with the orientations of the Manual on Visibility of External Actions (e.g., press release at the signature of the Financing Agreement, visibility for reports and studies, etc).