PROJECT INFORMATION DOCUMENT (PID)
APPRAISAL STAGE

Report No.: PIDA21023

Project Name	Third Regional Development Project (P150696)
Region	EUROPE AND CENTRAL ASIA
Country	Georgia
Sector(s)	General water, sanitation and flood protection sector (35%), Sub-national government administration (20%), Rural and Inter-Urban Roa ds and Highways (35%), SME Finance (10%)
Theme(s)	City-wide Infrastructure and Service Delivery (35%), Cultural Heritage (20%), Urban Economic Development (25%), Infrastructure servi ces for private sector development (10%), Micro, Small and Medium Enterprise support (10%)
Lending Instrument	Investment Project Financing
Project ID	P150696
Borrower(s)	Georgia
Implementing Agency	Georgia Municipal Development Fund
Environmental Category	B-Partial Assessment
Date PID Prepared/Updated	18-Feb-2015
Date PID Approved/Disclosed	18-Feb-2015
Estimated Date of Appraisal Completion	19-Feb-2015
Estimated Date of Board Approval	24-Mar-2015
Decision	

I. Project Context

Country Context

With a population of 4.5 million people growth in Georgia averaged nearly 6 percent p.a. during 2004-2013. While Georgia remains one of the very few countries in Europe and Central Asia (ECA) that have not yet caught up to their 1990 real GDP level, it has benefited from a noteworthy push on structural reforms and liberalization starting in 2004. Improvements in the business environment, infrastructure quality, public finance, and reduced trade barriers stimulated investments. GDP per capita increased from $920 in 2003 to $3,597 in 2013 although it is still among the lowest in ECA.Georgia did not experience the structural transformation associated with pushing resources and productivity growth towards the export sectors. While it achieved global recognition as a top performer on the Doing Business rankings (and ranked 8th out of 183 countries in the 2013 Doing Business Report), productivity gains were concentrated mainly in non-tradables, which is where FDI flowed largely to. Growth stemmed mainly from capital inflows before the twin crises of 2008 and from high public capital spending after. Growth was fueled by high foreign direct investment before the global economic crisis of 2008, a period of easy finance world-wide. This led to booming consumption, imports, and investment and allowed Georgia to incur a large current account deficit – reaching 20 percent in 2007 before moderating to a still high 11-12 percent range over 2011-2012. The twin shocks in 2008 of the global economic crisis and the conflict with Russia interrupted capital inflows and private investment and growth plummeted – in 2009 GDP contracted by 3.8 percent. The Government was quick to implement a fiscal stimulus to support recovery, including a large public investment package and increased social transfers. These efforts paid off and growth quickly rebounded, averaging more than 5 percent during 2010-2013. Despite growth, unemployment stayed high and it remains the most significant public policy challenge. Georgia's robust growth performance was accompanied by high unemployment, which remained in the 12-13 percent range even during the pre-crisis boom. Unemployment peaked to 17 percent in 2010 and then fell to 15 percent in 2012. Georgia was able to create significant new employment but this has been insufficient to bring about overall net job creation. Reducing poverty and promoting shared prosperity remain a challenge in Georgia. Poverty and extreme poverty, measured using absolute poverty lines anchored on the national relative poverty and extreme poverty lines, are high in Georgia compared to other countries in the region. In 2012, 14.8 percent and 3.7 percent of the population lived in poverty and extreme poverty respectively. Consumption growth among the bottom 40 percent of the population, the World Bank's indicator of shared prosperity, was also lower than for the population as a whole for the period 2006-2010. This was reversed in 2010-2012 mainly due to the benefits of the fiscal stimulus rolled out in the period after the global economic crisis that increased social transfers and finally brought about an improved shared prosperity of the bottom 40 percent.At the aggregate level, the Government aims to address two priorities— increasing employment and narrowing the current account deficit. These are to be achieved by promoting private investments in sectors such as tourism, energy and logistics, and by continuing public investment in infrastructure, regional development, agriculture and education. These efforts are seen as key catalysts for accelerating job creation. Consequently, Georgian authorities continue to support private sector to lead economic growth and job creation efforts.

Sectoral and institutional Context

Inequality in Georgia is spatially reflected in regional and urban/rural disparities. Unemployment in 2012 was largely urban at 26.2 percent, while rural unemployment was at 7 percent. However, 64 percent of the poor live in rural areas, despite the fact that rural areas comprise less than 50 percent of Georgia's total population. Regional disparities in service delivery are also very visible in water and sanitation. Today, only Tbilisi provides piped water to almost all households while in most of the remaining regions, piped water is available to no more than 30 percent of households. In Tbilisi, over 90 percent of households have bathrooms, while in economically weak rural regions, the number drops to only 3 to 4 households out of 10. Consequently, the Government identified addressing regional disparity, poverty and unemployment as key priorities for intervention in its new national development strategy " Socioeconomic Development Strategy of Georgia: 2020." The financing of regional development programs, decentralization and investment in municipal infrastructure and services, are emerging as key tools in this regard as articulated in the Strategy on Regional Development. The objective of this strategy is to address regional disparities, focusing on developing the potential sources of economic growth in each region. The development of the tourism sector (often focused on cultural heritage and nature) emerges as a source of economic growth both nationally and also in key regions and cities. International tourist arrivals have grown rapidly (more than 5 million visitors in 2013, representing a 66 percent increase since 2011). Tourism and travel sector is becoming a key generator of jobs, accounting for 14.2 percent of total employment in 2013 and 16 percent of GDP (directly and indirectly), with a forecast to continue growing by 4.8 percent per annum. The sector currently also provides nearly 20 percent of export earnings. In line with this strategic direction, the Government invested about US$400 million between 2005-2013 for revitalization of municipal infrastructure and restoration of old buildings (most of which have a cultural heritage value) in the cities of Tbilisi, Signagi, Mtskheta, Batumi and Kutaisi. Nonetheless, the Government recognized that restoring buildings and municipal infrastructure was not sufficient to trigger and sustain local economic transformation. Thus, an integrated and demand-driven approach to regional development was seen as critical to spurring growth in targeted cities and regions.The Government has, therefore, launched a Regional Development Program with support of the World Bank, to attract private investors, especially in tourism and agribusiness in targeted regions. The Regional Development Project (RDP - P126033, US$ 60 million), focusing on Kakheti region, was approved by the Board on March 20, 2012. The RDP was followed in November 2012 by the Second Regional Development Project (RDPII - P130421, US$ 30 million), which focused on Imereti. Both projects are under implementation, and achieving remarkable results. These include, in Kakheti, an increase in the number of hotel beds in the targeted areas from 1,610 to 2,511 (exceeding the project's targets of 1,932); an increase in the number of SME points of sales (tickets, souvenirs shops, restaurants, hotels, guest-houses and family houses) from 248 at baseline to 282 (expected to exceed the 323 target by end of 2014); an increase in the hours of water supply from 8h per day to 24h, and at least 80 new business start-ups. House owners have already transformed part of their properties into a productive or service asset (hand-crafts workshop, souvenir shop, café, restaurant or a guest-house).The Government requested the Bank to support a Third Regional Development Project (RDPIII) with US$60 million. The proposed Project will focus on Samtskhe-Javakheti, a lagging region in the south, and Mtskheta-Mtianeti, an economically growing region close to the capital.

II. Proposed Development Objectives

The Project Development Objective is to improve infrastructure services and institutional capacity to support increased contribution of tourism in the local economy of the Samtskhe-Javakheti and Mtskheta-Mtianeti regions.

III. Project Description

Component Name

Infrastructure Investment

Comments (optional)

Component 1.1: Urban Regeneration and Circuit Development. This component will finance: urban regeneration of old towns and villages, including restoration of building facades and roofs, public spaces, museums, roads and water, and enhancement of cultural and natural heritage sites, including access and presentation.

Component 1.2: Provision of Public Infrastructure to Attract Private Investments. To encourage private sector investments in the region, this component will support a selected number of private sector entities in Project areas that demonstrate interest and capacity to invest in tourism or agribusiness through investing in complementary public infrastructure that is necessary to ensure the viability of their investments.

Component Name

Institutional Development

Comments (optional)

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Support institutional capacity and performance of the Georgia National Tourism Administration (GNTA), National Agency for Culture Heritage Preservation of Georgia (NACHP), National Museum, Project Implementing Entity (Municipal Development Fund of Georgia, MDF), and other local and regional entities in order for them to carry out the following activities: setting up of destination management office in each of the two regions; marketing and promotion; preparation of sustainable site management plans for cultural heritage sites; training for skilled workforce development; cultural heritage advisory service to the NACHP; business start-up/expansion advisory service to tourism SMEs; performance monitoring & evaluation; and preparation of studies and construction supervision.

IV. Financing *(in USD Million)*

Total Project Cost:	75.00	Total Bank Financing:	60.00
Financing Gap:	0.00		

For Loans/Credits/Others	Amount
Borrower	15.00
International Bank for Reconstruction and Development	60.00
Total	75.00

V. Implementation

The Project will be implemented by the Municipal Development Fund (MDF) and builds on its successful project management of other Bank financed operations. The MDF will be responsible for all project implementation, procurement, safeguards, financial management and disbursements. Established by Presidential Decree # 294 on June 7, 1997, it has since developed into a solid non-bank financial intermediary (FI) that plays a central role in funding and developing regional and municipal infrastructure. Funds have been provided by the Government of Georgia, several international financial institutions and donors and its own revenue. Its solid implementation capacity and performance are reflected by the growing interest from the Government and donors to channel their grants and credits through MDF to municipalities.

VI. Safeguard Policies (including public consultation)

Safeguard Policies Triggered by the Project	Yes	No
Environmental Assessment OP/BP 4.01	✗	
Natural Habitats OP/BP 4.04	✗	
Forests OP/BP 4.36		✗
Pest Management OP 4.09		✗
Physical Cultural Resources OP/BP 4.11	✗	
Indigenous Peoples OP/BP 4.10		✗
Involuntary Resettlement OP/BP 4.12	✗	
Safety of Dams OP/BP 4.37		✗
Projects on International Waterways OP/BP 7.50	✗	
Projects in Disputed Areas OP/BP 7.60		✗

Comments (optional)

VII. Contact point

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