



STATE AUDIT OFFICE OF GEORGIA

## REPORT

# ON THE GOVERNMENT'S REPORT ON THE ANNUAL EXECUTION OF 2023 STATE BUDGET

SHORT VERSION





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# THE KEY ECONOMIC AND FISCAL INDICATORS



	2019	2020	2021	2022	2023	
MACROECONOMIC INDICATORS						
Nominal GDP (mln GEL)	49,726	49,789	60,724	72,860	80,246	
Economic growth	5.4%	-6.3%	10.6%	11.0%	7.5%	
Average inflation rate	4.9%	5.2%	9.6%	11.9%	2.6%	
Foreign trade balance (mln GEL)	-5,720	-4,708	-5,856	-7,964	-9,501	
FDI (mln GEL)	1,352	595	1,253	2,098	1,595	
Remittances (mln US Dollar)	1,733	1,886	2,350	4,372	4,123	
CA deficit to GDP (%)	5.9%	12.4%	10.3%	4.5%	4.3%	
FISCAL INDICATORS						
Receipts (mln GEL)	13,252	18,042	18,378	20,529	22,680	
Expenditures (mln GEL)	13,470	16,175	19,808	20,163	22,350	
Change in cash balance (mln GEL)	-217	1,868	-1,430	366	330	
Tax revenues (mln GEL)	9,666	9,365	11,439	14,977	16,994	
Budget deficit to GDP (GFSM 2014)	2.6%	9.1%	6.3%	2.2%	2.2%	
Public debt stock (mln GEL)	20,623	30,835	31,216	29,655	32,481	
Government debt stock (mln GEL)	19,916	29,672	29,812	28,587	31,482	
Debt Rule Ratio	40.8%	60.4%	49.7%	39.3%	39.3%	

# 1. TENDENCIES OF THE STATE BUDGET EXECUTION



The state budget receipts and expenditures for the fiscal year 2023 were initially planned at 21.9 billion GEL and 21.8 billion GEL, respectively. After the amendment in the State Budget Law, the plan of the receipts was increased by 256.7 million GEL (1.2%) and expenditures – by 431.2 million GEL (2.0%).

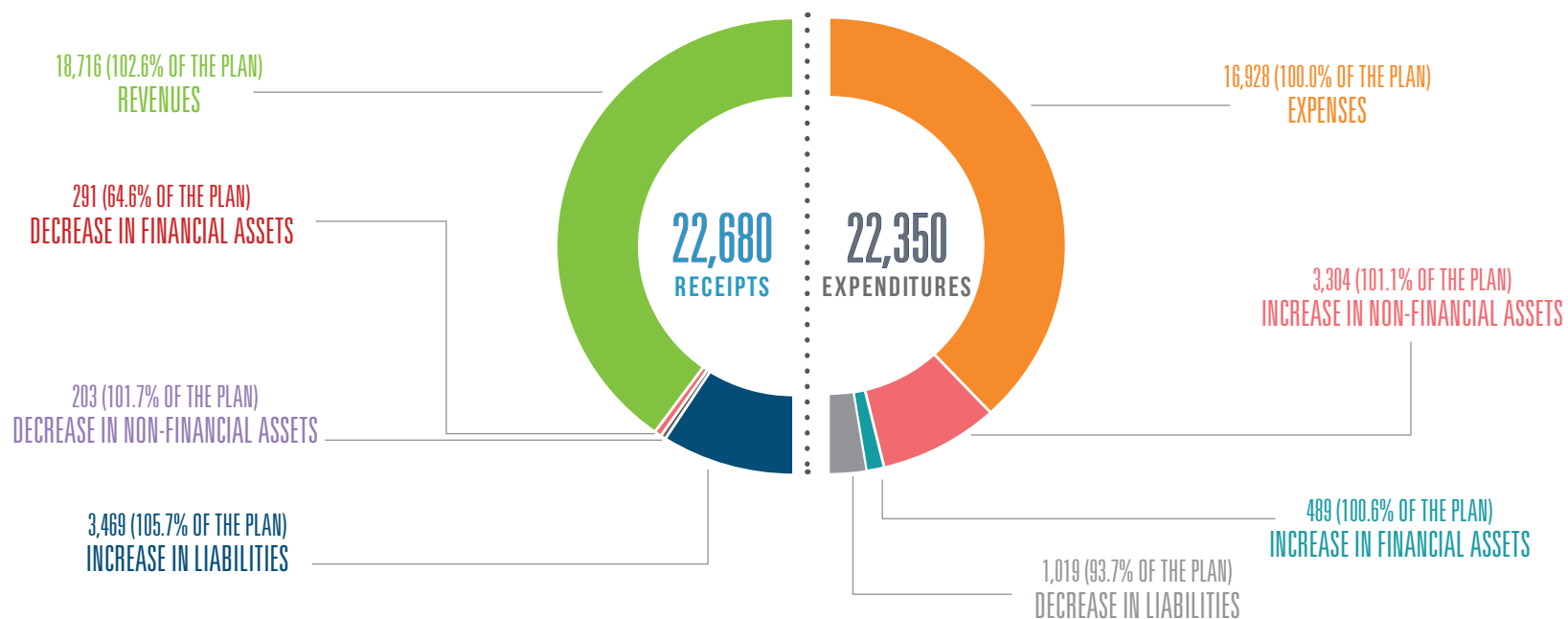
By the end of the fiscal year, actual receipts and expenditures amounted to 22.7 billion and 22.4 billion GEL, respectively. Therefore, the state budget cash balance increased from 1.2 billion GEL to 1.6 billion GEL.

**Table 1.** Execution of the State Budget components – 2023 (million GEL)

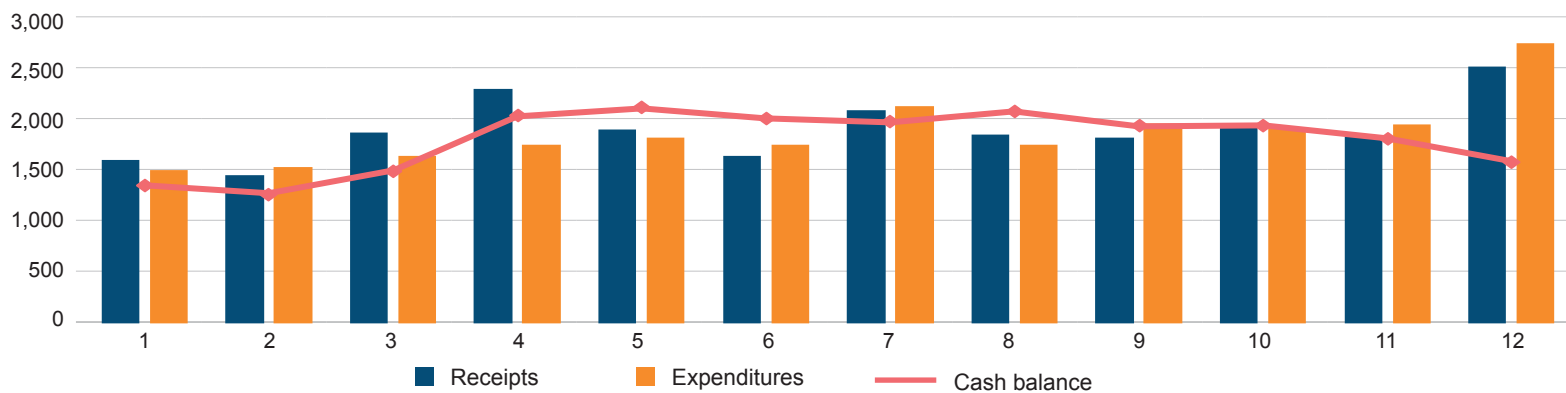
	BUDGET LAW Initial	BUDGET LAW Amendment	ACTUAL
Receipts	21,914	22,171	22,680
Expenditures	21,880	22,311	22,350
Change in balance	34	-140	330



**Figure 1.** Execution of the State Budget components – 2023 (million GEL)



**Figure 2.** Monthly dynamics of the state budget receipts, expenditures and cash balance – 2023 (million GEL)



## 2. ANALYSIS OF MACROECONOMIC FORECASTS AND FISCAL RISKS REALISATION

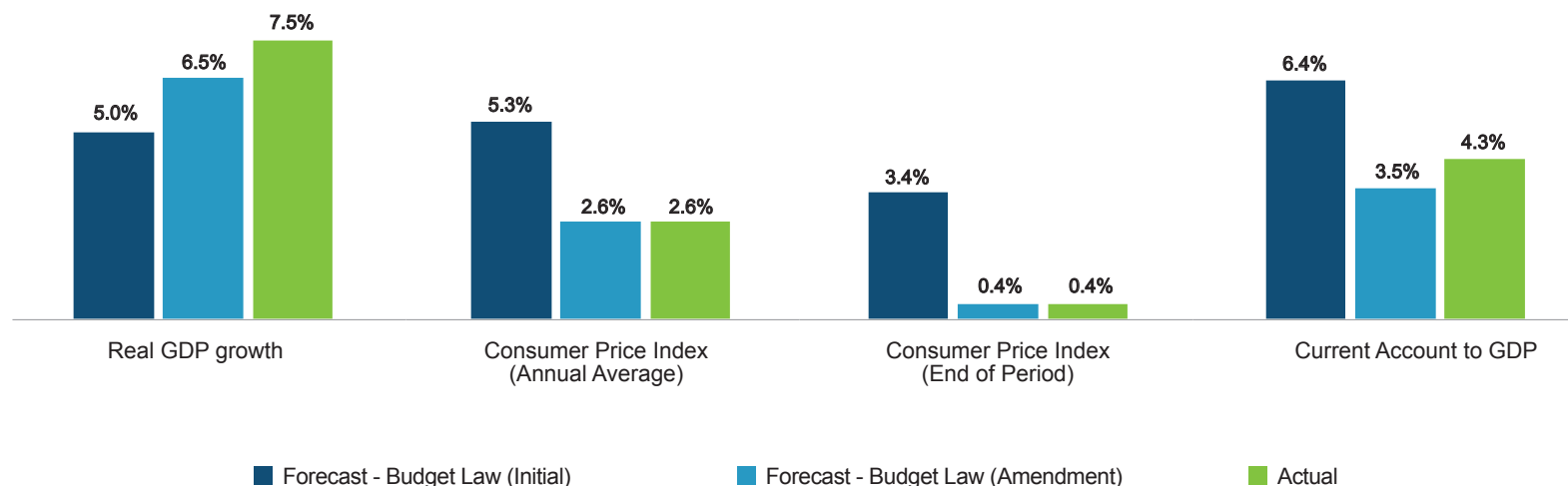


### 2.1 OVERVIEW OF THE MACROECONOMIC ENVIRONMENT

In 2023, real GDP growth was 7.5% and exceeded the MoF's forecast by 1 p.p. (6.5%). The main reasons behind the growth were the recovery of the tourism sector and significant increase in the remittances received from abroad.

Increase in the average consumer price index YoY was 2.6% and equaled to the forecasted figure reflected in the final version of the State Budget Law. However, it fell short of the forecast presented in the initial State Budget Law (5.3%) by 2.7 p.p.

**Figure 3.** Comparative analysis of the forecasted and actual figures of key macroeconomic indicators - 2023



## 2.2 OVERVIEW OF THE MACROECONOMIC AND FISCAL RISKS REALISATION

“Fiscal Risks Analysis” document, attached to the initial State Budget Law, was not updated when the the State Budget Law was amended. However, “Macroeconomic Scenario Analysis” document was adjusted, and the state budget parameters for

2023 were re-planned based on the six negative macroeconomic risks.

In contrast to the previous years, report on the annual execution of 2023 state budget also presents information about the status of the identified macroeconomic risks realization, the need of which has been emphasized by the State Audit Office (SAOG) in its previous reports.

**Table 2.** Actual and forecasted macroeconomic parameters based on the different scenarios - 2023 (million USD)

INDICATORS		BASIC	PESIMISTIC	OPTIMISTIC	ACTUAL
Real GDP growth		6.5%	3.7%	7.9%	7.5%
CPI	✓	0.4%	-0.8%	1.6%	0.4%
CA to GDP		-3.5%	-3.0%	✓ -4.0%	-4.4%
CA		-1,050	-862	✓ -1,223	-1,327
Export of goods		9,051	✓ 8,766	9,238	8,142
Import of goods		-15,259	✓ -14,430	-15,782	-14,254
Export of services	✓	6,887	6,494	7,112	6,890
Import of Services	✓	-3,593	-3,390	-3,765	-3,520
Budget deficit		3.0%	3.0%	✓ 2.7%	2.2%
Government debt / GDP		38.4%	✓ 40.0%	37.5%	39.3%



Presenting information about impact of risk factor realization on fiscal aggregates and corresponding fiscal policy responses remains a challenge and is important to be presented in state budget annual execution report.

Compliance analysis of the actual macroeconomic parameters versus the figures presented in the macroeconomic scenarios document, attached to the State Budget Law, indi-

cates that in 2023 economic tendencies developed in combination of all three scenarios.

The information presented in the “Fiscal Risk Analysis” document does not allow users analyze SOE’s risk indicators classified as the General Government (GG) and the Public Corporations (PC) sector separately.

1

State-owned enterprises are one of the main sources of fiscal risks due to their negative financial results in the recent years. According to the Fiscal Risk Analysis Document, attached to the 2024 State Budget Law, total net income of 117 SOEs in FY 2022 amounted to 1.0 billion GEL, which, similar to 2021, is mainly resulted from the appreciating national currency (net profit from only this source equals to 787 million GEL in 2022 and 515 million GEL in 2021). Excluding the impact of exchange rate fluctuations, over the past eight years consolidated financial result of the SOEs were positive only in 2019 and 2022. Without excluding this effect, profitability in this period was recorded only in 2021-2022 years.

2

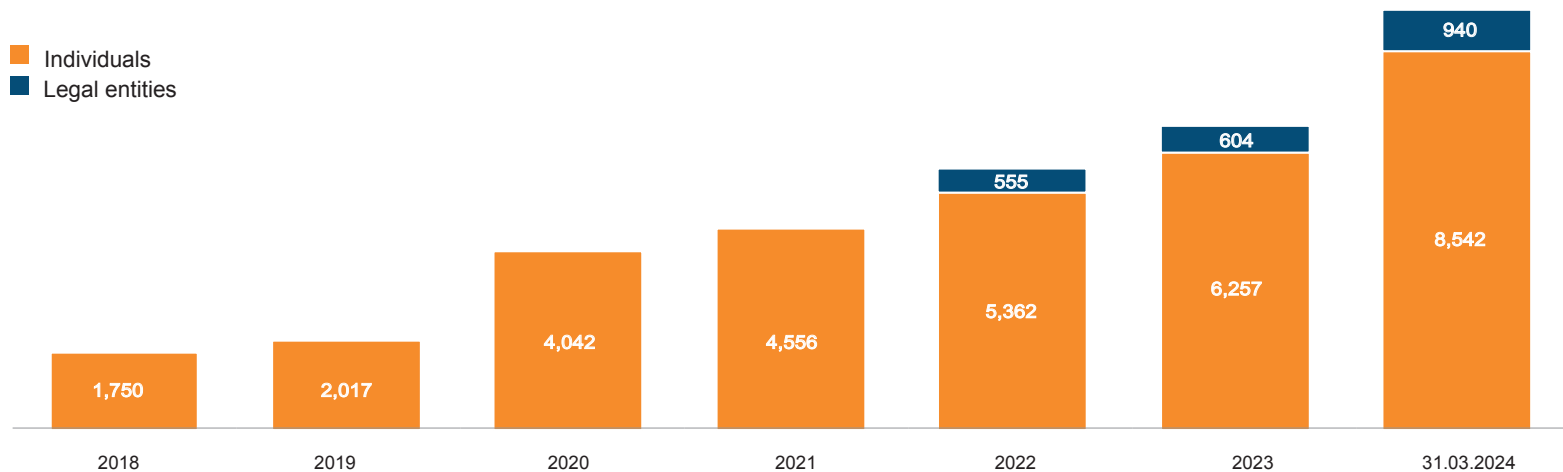
International arbitration disputes presents another source of fiscal risks. In 2023, 3 new disputes have arisen, resulting in the total potential disputes amounting to 3.6 billion USD from 10 ongoing international arbitration cases.

3

Deposit insurance system is one of the significant sources of fiscal risks. As of December 31, 2023, the total volume of deposits insured by the system amounted to 6.9 billion GEL, while the size of the insurance fund was 193 million GEL.



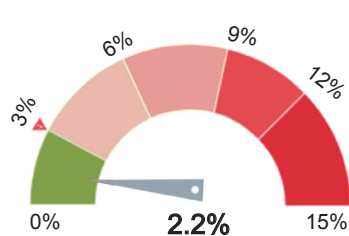
**Figure 4.** Volume of insured deposits (million GEL)



## 2.3 FISCAL RULES

### BUDGET BALANCE RULE

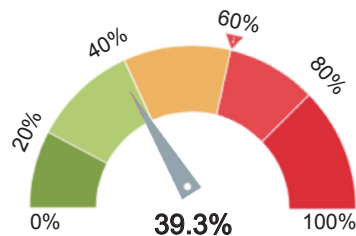
Budget deficit to GDP



▼ Limit set by the Organic Law

### DEBT RULE

Public debt to GDP



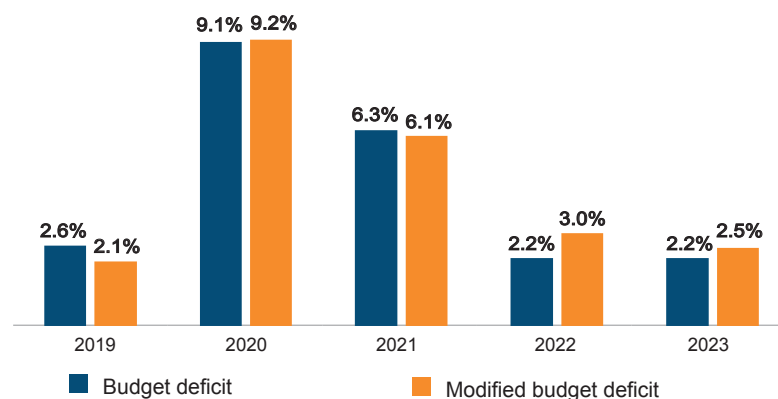
▼ Limit set by the Organic Law

### BUDGET BALANCE RULE (BUDGET DEFICIT)

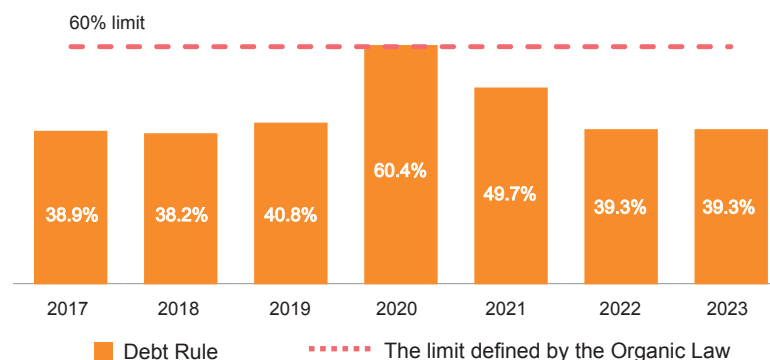
At the end of 2023, budget deficit amounted to 2.2% of GDP (1.8 billion GEL). Compared to the previous year, all parameters affecting deficit formation have increased. However, the growth in expenditures (expenses increased by 2.8 billion GEL (16%), change in non-financial assets by 627 million GEL (10%)) exceeded the increase in revenues (by 3.2 billion GEL (15%)).



**Figure 5.** Dynamics of budget deficit and modified budget deficit (defined under the ongoing IMF program) to GDP



**Figure 6.** Debt Rule indicator and its compliance with the 60% limit set by the Organic Law on Economic Freedom (%).



## DEBT RULE

According to the information presented in the annual report on the state budget execution, the Debt Rule indicator at the end of 2023 comprised 39.3%, which is under the 60% limit set by the Organic Law on “Economic Freedom”. Compared to the previous year, stock of government debt increased, however, this increase was fully offset by nominal GDP growth, and the debt rule indicator remained at the 2022 level.

It is worthy to mention that the government debt volume at the end of 2023 is accounted inaccurately. In particular, the government debt statistics include debt of budgetary organizations amounting to 81.8 million GEL, out of which 48.8 million GEL is the debt of SOEs classified as part of GG sector.<sup>1</sup> However, the SAOG identified additional 5 SOEs also classified as part of GG sector, which had financial and other types of liabilities totaling 39 million GEL by December 31, 2023.

<sup>1</sup> This debt represents the liability of JSC “Georgian Development Fund”, the legal successor of JSC “Partnership Fund of Georgia”, to JSC “Georgian Railway”.





## RECOMMENDATIONS

### TO THE MINISTRY OF FINANCE:

- It is important that in the "Fiscal Risk Analysis" document, fiscal risks arising from the SOEs classified as corporate sector and government sector to be analyzed separately. Additionally, the financial indicators and corresponding risks of enterprises assigned to the government sector should be analyzed in the context of their impact on the government debt and consolidated government budget deficit, also within the scope of the "Government Debt Sustainability Analysis" document.
- It is advisable that information about potential risks arising from the deposit insurance system operating in Georgia to be presented in the "Fiscal Risk Analysis" document attached to the State Budget Law.



### 3. STATE BUDGET REVENUES



In 2023 revenues received in the state budget comprised 18.7 billion GEL and exceeded the projected figure reflected in the final version of the State Budget Law by 477 million GEL (2.6%). All components of the revenues outturned corresponding forecasted values.

**Table 3.** State budget revenues - 2023 (million GEL)

	Actual	Execution with approved plan (%)	
		Budget Law Initial	Budget Law Amendment
Tax revenues	16,994	104.3%	101.7%
Grants	326	116.5%	116.5%
Other revenues	1,397	133.0%	111.7%
<b>Revenues</b>	<b>18,716</b>	<b>106.2%</b>	<b>102.6%</b>

The tax revenues amounted to 17.0 billion GEL and increased by 2 billion GEL (13.5%) compared to the previous FY. As in the previous years, VAT (40.0%) and personal income tax (32.8%) present the leading contributors to the tax revenues. Excise (13.4%), corporate earning (11.9%) and import taxes (0.9%) have relatively modest share in tax revenues.

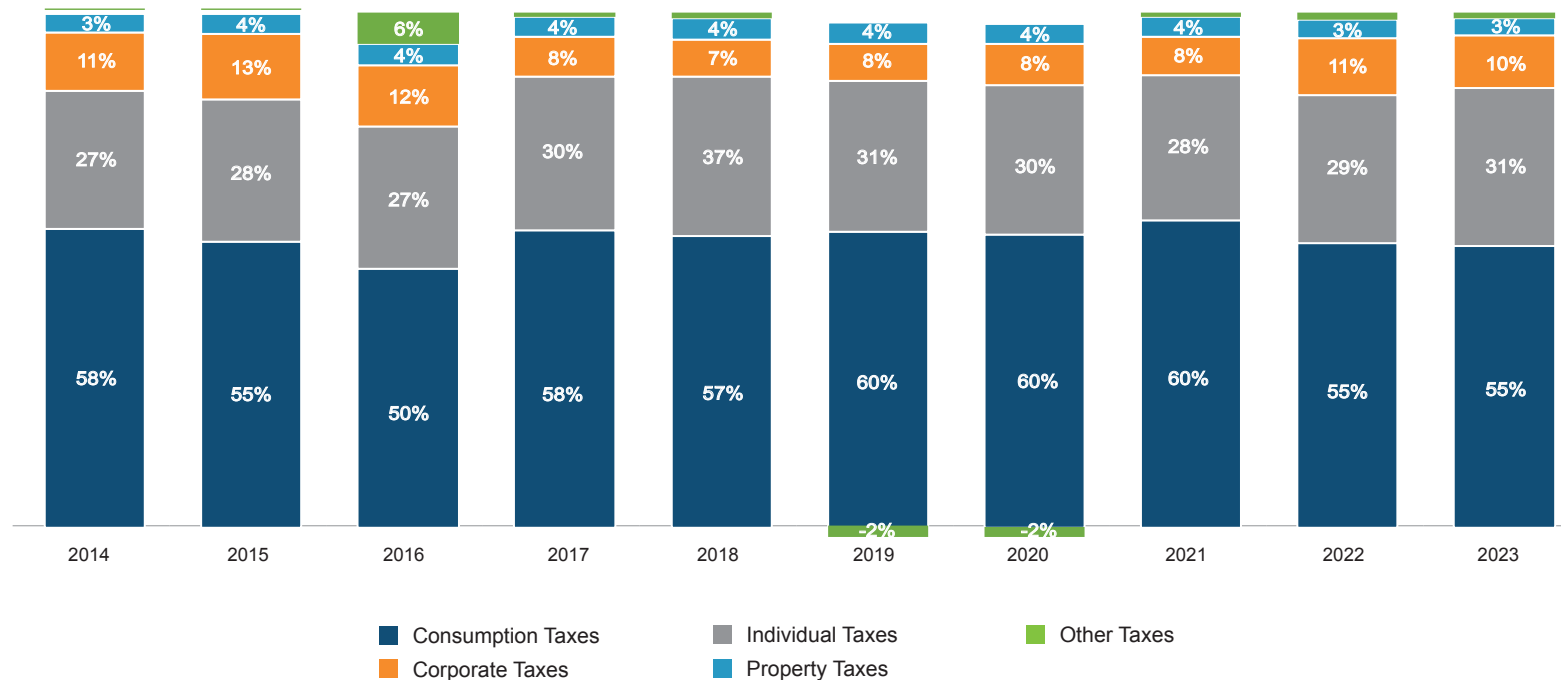
Since 2014 to the present, taxes on consumption of goods and services have held the largest share in the consolidated budget's tax revenues.<sup>2</sup> The next largest contributor is the personal income tax, share of which in total taxes are relatively stable. The share of the tax on corporate earnings was also stable until 2017, but sharply decreased from 2017 due to changes in the tax code.<sup>3</sup> The share of property tax is also stable, comprising approximately 4%.

<sup>2</sup> This includes VAT, excise, and import taxes.

<sup>3</sup> This change was due to the transition to the "Estonian model" of corporate income tax.



**Figure 7.** The structure of tax revenues in the consolidated budget.



The tax revenue structure in Georgia is slightly different from that of developed countries. Specifically, in the OECD countries, the largest contributor to the tax revenues is also taxes on goods and service consumption, which is around 43%. However, this is significantly lower than in Georgia. The share

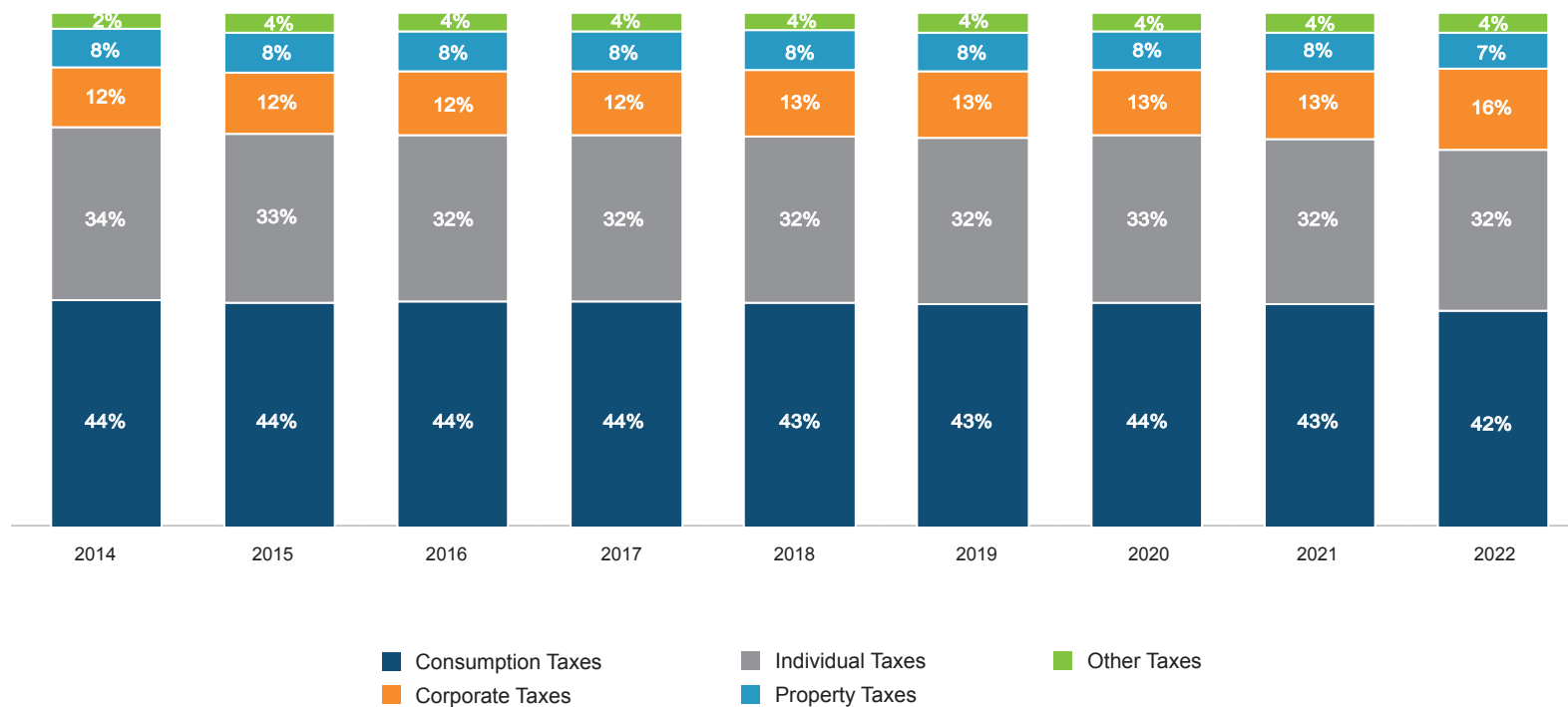
of personal income tax in 2014-2022 averaged 32% and slightly exceeds the corresponding figure in Georgia. In the OECD countries, property tax has a markedly higher share in tax revenues compared to Georgia, accounting for approximately 8% of total tax revenues.

<sup>4</sup> <https://data.oecd.org/tax/tax-revenue.htm#indicator-chart>

<sup>5</sup> Taxes on goods and services include value-added tax, import taxes, and excise taxes.



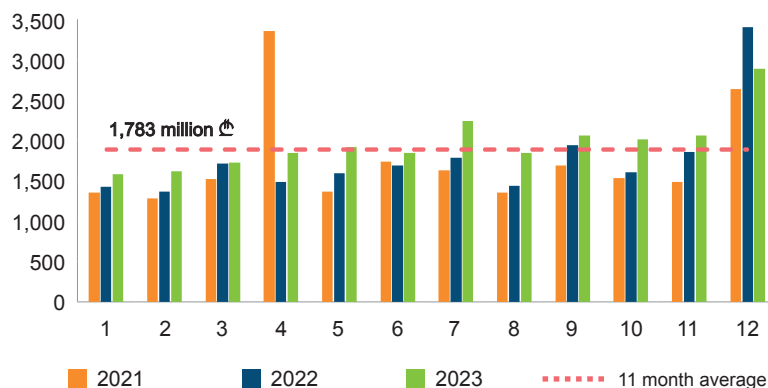
**Figure 8.** The structure of government tax revenues in the OECD countries.



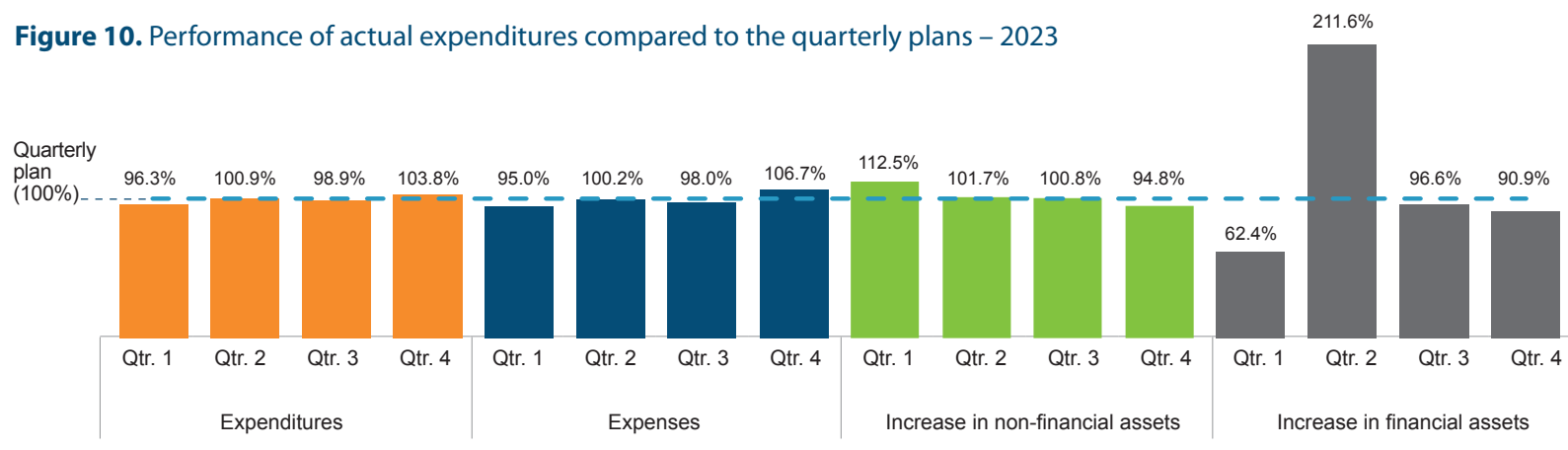
## 4. STATE BUDGET EXPENDITURES

Compared to the previous years, there is an improvement in the dynamics of expenditures throughout the year, however, there still is a room for improvement. In particular, in the last month of 2023 expenditures increased dramatically. Only in December, the amount spent reached 2.7 billion GEL and 12.2% of the entire expenditure. As a result, in December budget expenditures exceeded that of previous eleventh month's average figure by 53%.<sup>6</sup>

**Figure 9.** Monthly expenditures of the State Budget (million GEL)



**Figure 10.** Performance of actual expenditures compared to the quarterly plans – 2023



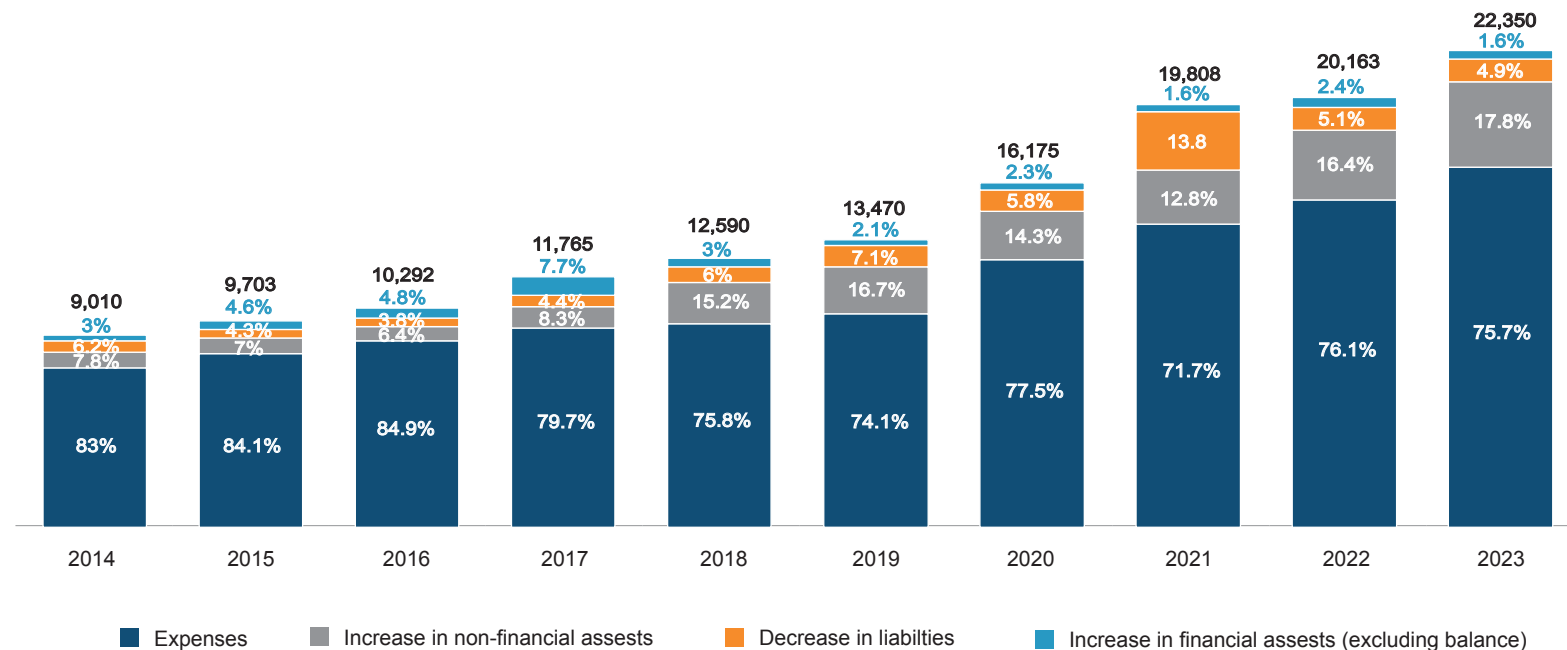
<sup>6</sup> The corresponding figures for 2021 and 2022 were 58.8% and 109.4%, respectively.



Over 2014-2023 period the amount of expenditures increased from 9 billion GEL to 22.4 billion GEL (by 148.1%) and average growth rate of expenditures equaled 10.8%. Similar to the previous years, the largest component expenditures is “expenses” (75.7%). It should be noted, that share of “expenses” in overall expenditure is decreasing

while share of “increase in non-financial assets” is increasing. In 2014 shares of “expenses” and “increase in non-financial assets” in total expenditures were 83.0% and 7.8% respectively, while they amounted to 75.7% and 17.8% in 2023.

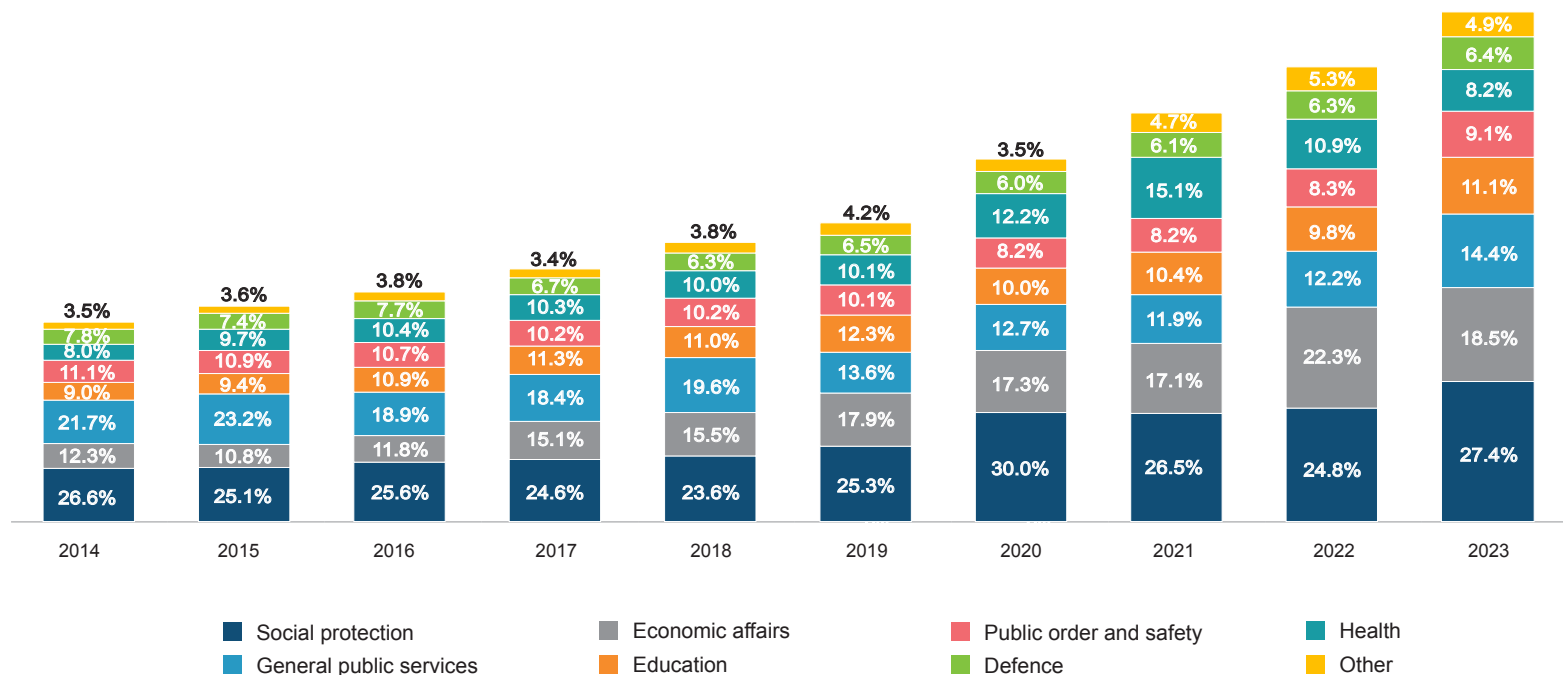
**Figure 11.** State Budget expenditures (million GEL) and its structure (%) - 2014-2023



According to the functional classification of operations in the state budget expenses and non-financial assets,<sup>7</sup> spendings across 10 main functional categories totaled 20.9 billion GEL in 2023. Similarly to the previous years, Social Protection

(27.4%), Economic Affairs (18.5%) and General Public Services (14.4%) took the largest amount of budgetary resources in 2023.

**Figure 12.** Functional classification of the state budget expenditures - 2014-2023



<sup>7</sup> According to the Government Finance Statistics Manual (GFSM 2014), the Classification of the Functions of Government (COFOG) for expenses and transactions on non-financial assets includes information about detailed expenditures for achieving governmental functions or socio-economic objectives.



## 4.1 MEDIUM-TERM BUDGET PLANNING

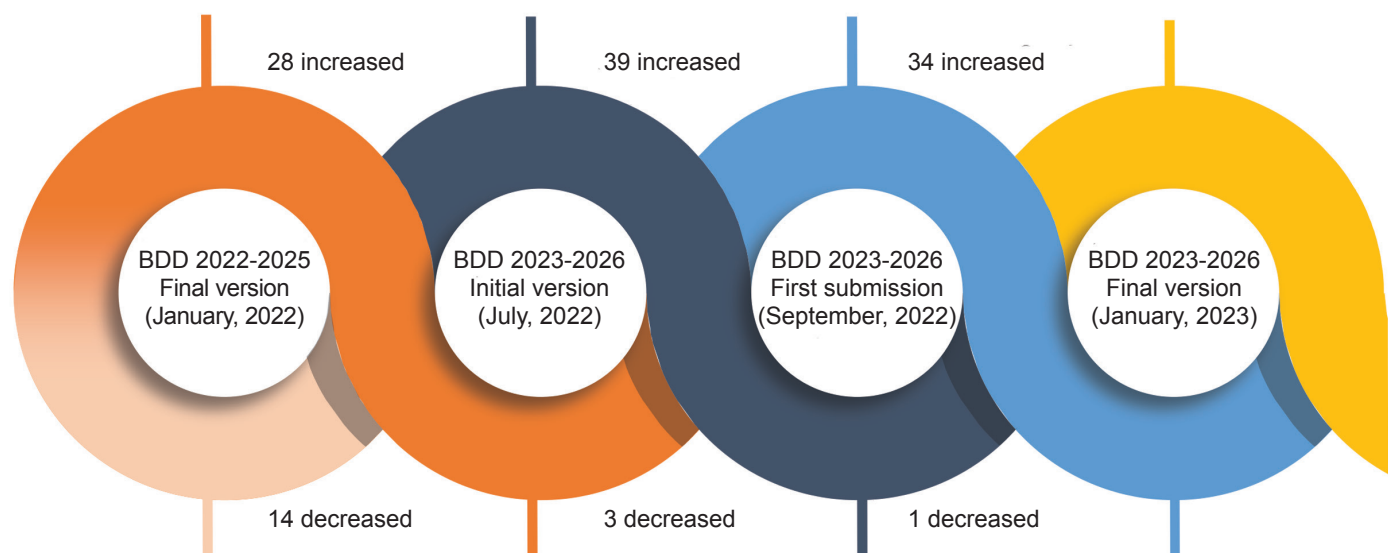
During the planning stage of expenditures for 2023, the ceiling of appropriations for individual spending agencies were changed significantly across different versions of BDD document prepared throughout 2022. Given the complexity of budget planning, it is expected to have differences in target amounts across various versions of the BDD. However, the volume and frequency of these mismatches requires further attention.

SAOG conducted comparative analysis of financial plans in the medium-term action plans and plans reflected in the budget

proposals for the programs of 7 line ministries. The analysis uncovered that the amount of appropriations in the budget proposals and in the medium-term action plans differ in 52 programs out of 77. Compared to medium-term action plans, appropriations are increased for 28 programs and decreased for 24 in budget proposals. Change is more than 10% in case of 22 programs.

As medium-term action plans have significant role in medium term budget planning, spending agencies should focus on quality improvement of those documents.

**Figure 13.** The number of spending agencies for which 2023 budget were changed in different versions of BDD

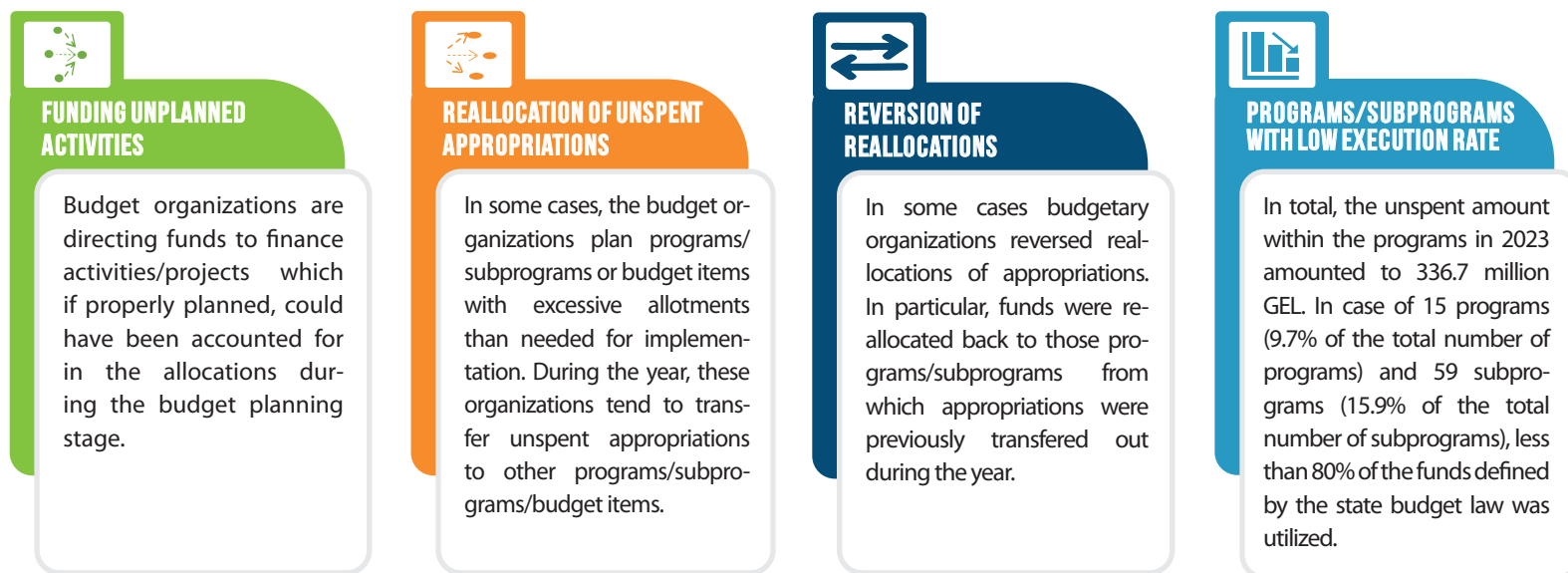


## 4.2 ADJUSTMENTS AND SPENDING OF APPROPRIATIONS

From 155 programs<sup>8</sup> defined in the 2023 State Budget Law, financial plans were adjusted for 103 programs<sup>9</sup> (66.5% of all programs) over the fiscal year. The sum of adjustment in terms of monetary units reached 522.3 million GEL.<sup>10</sup> In case

of 9 programs, adjustment exceeded 30% of the initial appropriations.

While analyzing budget execution of the spending agencies, SAOG identified the following systematic deficiencies regarding adjustment and usage of budgetary funds:



<sup>8</sup> From the state-wide expenditures only "Donor-Funded State-Wide Expenditures" (55 13) is included.

<sup>9</sup> These figures do not include adjustments resulting from the allocation of funds from reserve funds.

<sup>10</sup> In 2022, the corresponding figure was 363.9 million GEL.



## 4.3 EXPENDITURES OF GENERAL STATE IMPORTANCE

Actual execution of expenditures of general state importance amounted to 3.8 billion GEL (96.1% of the plan). From this angle, the following matters should be examined:

### REGIONAL DEVELOPMENT FUND - 497 MILLION GEL

The regional development fund is characterized by uneven utilization, such as 47% of total allocated resources being spent in the fourth quarter.

### GOVERNMENT RESERVE FUND - 95 MILLION GEL

From the government reserve fund, similar to previous years, there was funding for expenditures (amounting 27 million GEL) that are systematic in nature and, with proper planning, could have been accounted for at the budget planning stage.

**Figure 14.** Distribution of funds allocated from the government reserve fund in 2023 by purpose (million GEL)

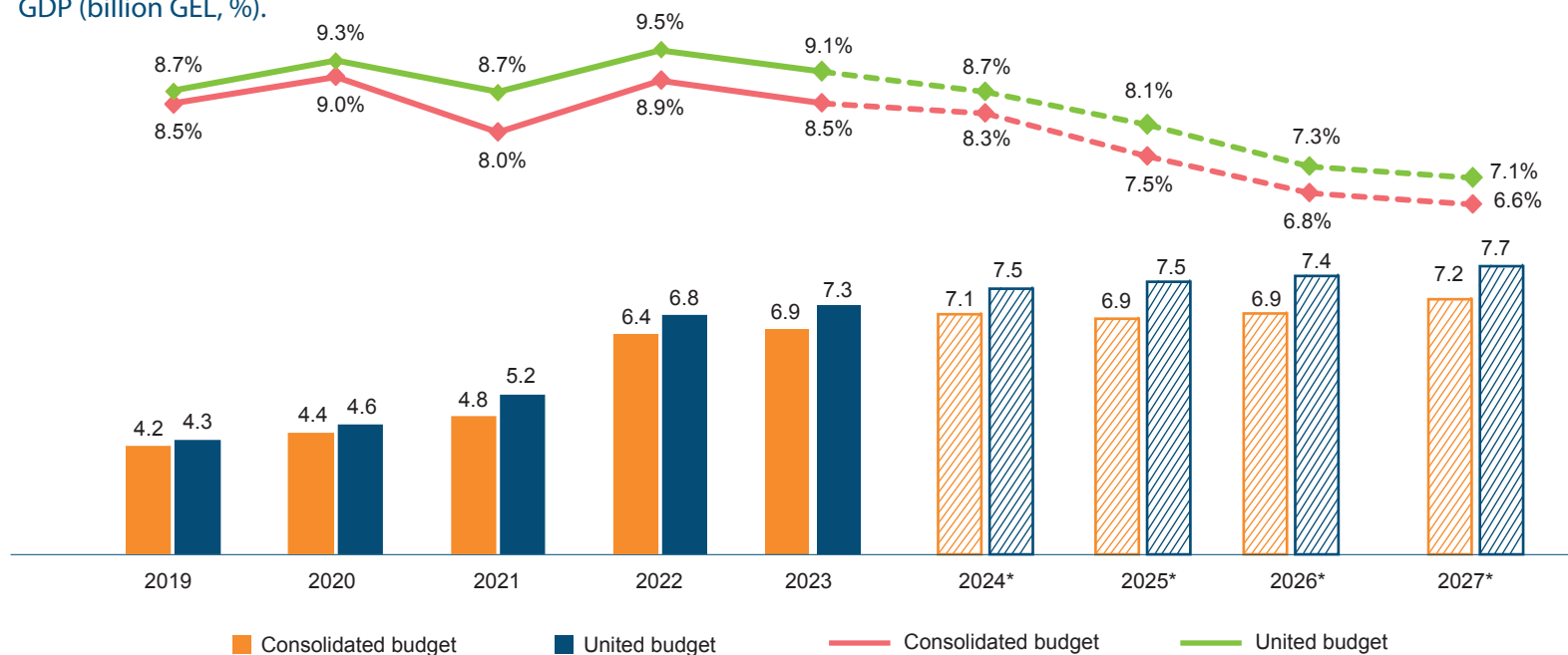


## 4.4 MANAGEMENT OF INVESTMENT PROJECTS

In 2023 capital expenditures of consolidated budget amounted to 6.9 billion GEL and 8.5% of GDP. According to the Budget Code of Georgia, consolidated budget doesn't

contain expenditures of LEPL/NNLE financed by their own revenues, from which 298 million GEL were spent on increasing financial and non-financial assets in 2023. In order to present a complete picture of capital expenditures, in addition to aggregated budget, indicators of united budget should be considered.

**Figure 15.** Dynamics of capital expenditures of consolidated and united budget in nominal terms and as a percentage of nominal GDP (billion GEL, %).



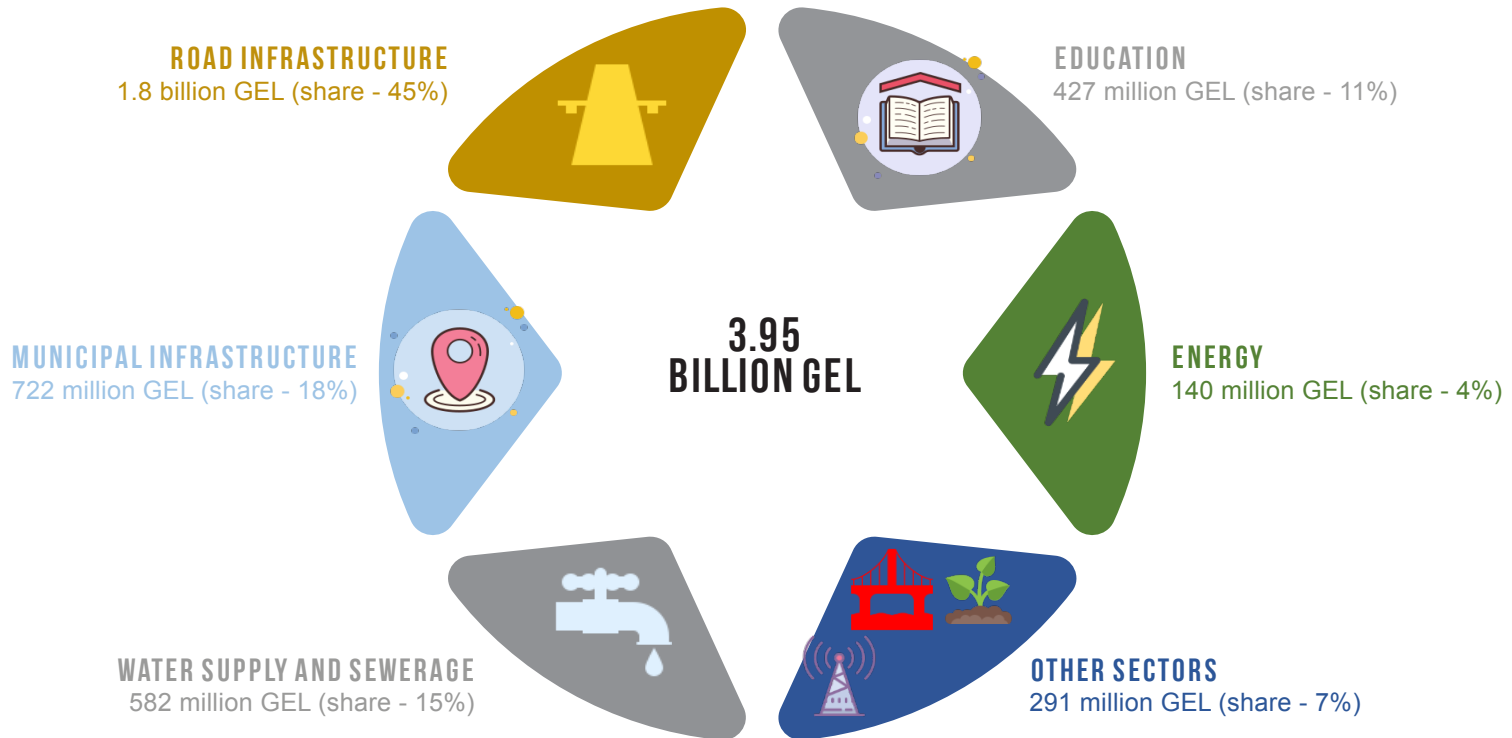
\* Forecast



In terms of current and capital expenditures, it's noteworthy that within the framework of the 2022 IMF program, the initial current expenditure limit for the consolidated budget for 2023 was set at 16.5 billion GEL and its actual amount exceeded this limit by 218 million GEL.

In 2023 actual financing of investment/capital projects equaled to 3.95 billion GEL (101% of the annual plan), which exceeds that of 2022 by 384 million GEL (11%). According to sectoral classification of investment projects, the largest components are road infrastructure (45%), municipal infrastructure development (18%) and water supply and sewerage (15%) projects.

**Figure 16.** Sectoral classification of investment projects, volume of each sector in nominal values (million GEL) and share in total investment projects (%) – 2023



## REGARDING TO THE MANAGEMENT OF THE INVESTMENT PROJECTS, THE FOLLOWING ISSUES SHOULD BE CONSIDERED:



### COMPLETENESS OF THE CAPITAL ANNEX

Within the state budget, projects are being implemented that qualitatively comply with the investment project criteria defined by the "Investment/Capital Project Management Methodology", but are not reflected in the "Capital Projects Annex".



### REPORTING

In 2023 financing of 30 capital projects where changed by the amendment of the state budget (43% of the total projects), total 138 million GEL. However, the "Capital Projects Annex" had not been updated accordingly, which represents a deficiency in terms of transparency and accountability.



### CHANGES IN THE PLANS

Deficiencies in the planning process of investment projects by implementing agencies often lead to large-scale changes in the project plans. In particular, in 2023 compared to 2021, the plans were increased by more than 50% for 23 projects and decreased for 6 projects, while compared to 2022, the plans were increased by more than 50% for 12 projects and decreased for 12 projects.



### UNSPENT PREDEFINED RESOURCES

Out of 99 projects presented in the 2023 state budget law, in 25 cases, less than 80% of the allocated funding was spent. Out of these projects, 10 projects were also characterized by low utilization in 2022. In the case of 7 projects, no resources were spent at all. Unspent funds are particularly critical for investment projects that are financed by external credit resources and involve paying a commitment fee on the undrawn portion of the loans.



### TIME OVERRUNS

According to the 2021 state budget law, 11 projects had to be completed by 2023. Due to the delays in the implementation process of these projects, in the 2022 state budget law the implementation of 5 projects were postponed to 2023 and their plans were set at 67 million GEL. The plans for remaining 6 projects remained zero. In the 2023 state budget law: a) funding was allocated for the aforementioned 6 projects, totaling 122 million GEL, b) out of the 5 projects, the plans for 4 were adjusted again, with total funding increasing to 111 million GEL.



## 4.5 LEGAL ENTITIES OF PUBLIC LAW/NON-PROFIT (NON-COMMERCIAL) LEGAL ENTITIES

The analysis of the consolidated balance of the LEPLs/NPLEs, presented in the annual execution of the state budget report, revealed the following deficiencies related to the completeness/accuracy of the reported information and planning of receipts/expenditures:

The consolidated balance sheet document of the state budget execution report does not provide information about the receipts/expenditures of individual LEPLs/N(N)LEs according to their sources of formation.

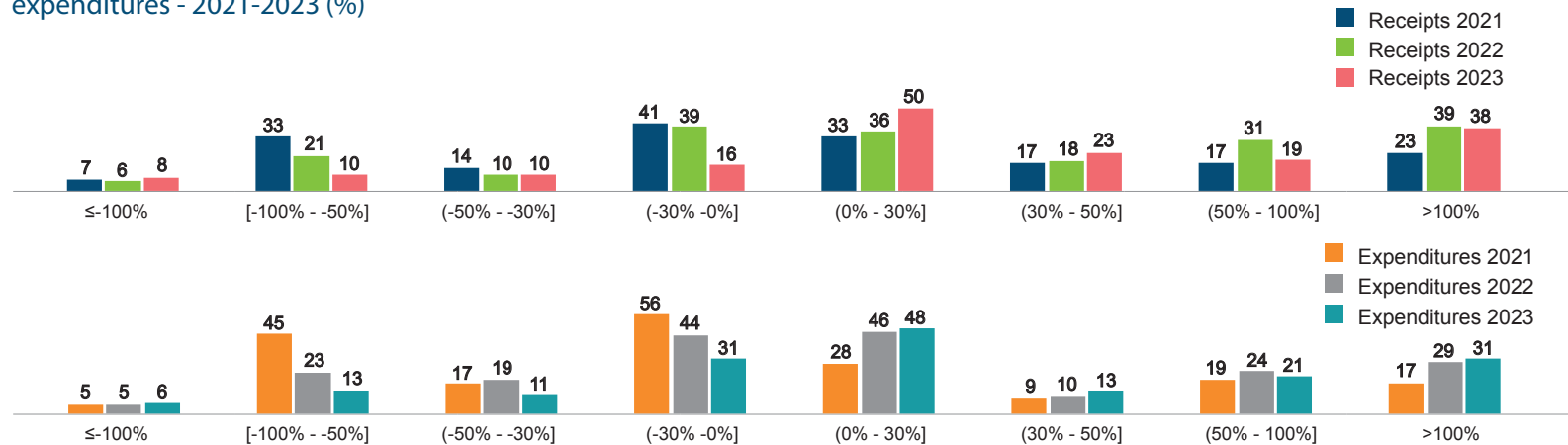
Both the own receipts and expenditures were planned as zero by 36 agencies. However, the actual receipts amounted 98 million GEL, while expenditures amounted to 25 million GEL. Out of these organizations, 18 entities planned their receipts and expenditures as zero in 2022 as well, but the actual amount of receipts equaled 19 million GEL, while expenditures equaled 23 million GEL.

Within the 234 examined agencies, a reduction in balance was planned as 215 million GEL in total. However, there was an increase in total balance by 344 million GEL. 13 organizations have a difference of more than 10 million GEL between planned and actual balances, among them, in case of 5 agencies, the difference exceeds 30 million GEL. It's worth to mention that in 2022 as well, the actual balance growth significantly exceeded the planned amount.

Given the frequency and scale of deviations between the planned and actual figures, in several cases characterized with the systemic nature, it is recommended for agencies to pay additional attention defining realistic plans at the planning stage of their own revenues and expenditures.

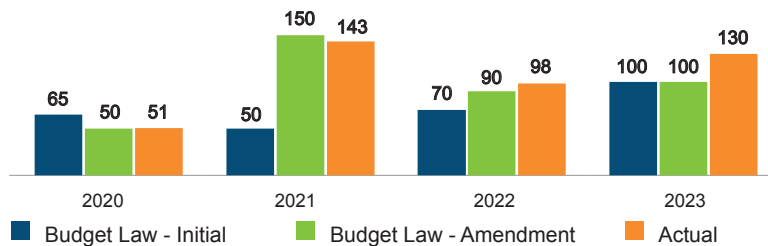


**Figure 17.** Distribution of LEPLs/NPLEs based on deviations between the actual and planned figures of their own revenues and expenditures - 2021-2023 (%)



In 2023, 130 million GEL was transferred to the state budget by 42 LEPLs/NPLEs as a grant,<sup>11</sup> which is 130% of the amount determined by budget law (100 million GEL).

**Figure 18.** Planned and actual amount of resources transferred to the state budget from the own revenues received by LEPLs/NPLEs (million GEL).

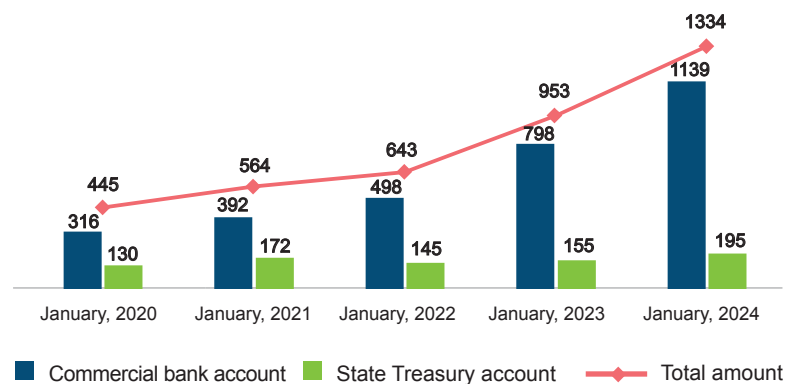


According to the information received from the State Treasury, at the end of 2023, the total balance of LEPLs/NPLEs increased by 381 million GEL compared to the previous year and amounted to 1.3 billion GEL, from which 195 million GEL is placed in the state treasury, and 1.1 billion GEL – in the commercial banks. In 2022-2023, the volume of balance doubled (from 643 million GEL to 1.3 billion GEL). In 2023, 71 agencies received 133 million GEL interest income from deposits placed in commercial banks (in 2022, 65 agencies received 83 million GEL).

<sup>11</sup> From 2017, Legal Entities of Public Law (LEPLs) whose annual revenue, excluding funding received from the budget, exceeds 1 million GEL, were required to direct at least 10% of their own income to the state budget.



**Figure 19.** Total balance of LEPLs/NPLEs placed in the commercial banks and the State Treasury (million GEL).



By the end of December 2023, out of 99 LEPLs/NPLEs examined by SAOG, 60 entities deposited 714 million GEL in total on commercial bank accounts. Among them, 427 million GEL was in on-call deposit and card accounts, while 287 million GEL (by 11 agencies) on term accounts – 100 million GEL

with a term of less than 2 years, 187 million GEL with a term of 2 years.

According to the existing legislature, LEPLs/NNLEs are eligible to open deposit accounts in the commercial banks without approval from the State Treasury. In addition, there are no restrictions on transferring funds between deposit accounts within the same bank. In some cases, interest earned on deposits by LEPLs/NNLEs is credited to the same or other deposit accounts, rather than to the Treasury Single Account.<sup>12</sup> In addition, the existing legislation doesn't directly oblige LEPLs/NNLEs to periodically report to the State Treasury about their financial resources in commercial banks.<sup>13</sup> Considering mentioned factors, existing legal framework is characterised with control weaknesses in monitoring and does not ensure comprehensive reporting of deposits and interest income.<sup>14</sup>

<sup>12</sup> Subparagraph «a» of Part 8 of Article 7 of the Budget Code of Georgia.

<sup>13</sup> According to existing practice, the State Treasury conducts periodic monitoring of these resources, but it is of an informal nature.

<sup>14</sup> The SAOG identified cases where the interest accrued by commercial banks on deposits of certain Legal Entities of Public Law (LEPLs) was deposited into a deposit account, which, as of December 31, 2023, was retained in the same account and, moreover, was not reflected in the State Treasury's data.





## RECOMMENDATIONS

### TO THE MINISTRY OF FINANCE:

- In the consolidated balance sheet document of Legal Entities of Public Law (LEPL) / Non-Profit (Non-Commercial) Legal Entities (N(N)LE) within the annual report on the state budget execution, it is advisable to present information on the revenues received and expenses incurred by individual LEPLs/N(N)LEs, categorized according to their sources of formation.
- It is advisable for the Ministry of Finance to develop a systematic approach that ensures the State Treasury possesses complete and accurate information about the financial resources of LEPLs/N(N)LEs placed in commercial banks.

## 4.6 PROGRAM BUDGETING

In Georgia the program-based budgeting was introduced in 2012, yet it remains as an annex to the state budget aw. An analysis by the SAOG has identified systemic shortcomings

that often make it difficult or even impossible, in some cases, to evaluate the effectiveness of a program during the reporting stage. 31% of 557 indicators determined within programs/subprograms framework, were characterized with deficiencies:



For several indicators developed within the programs, it is impossible to compare the results achieved in the current year with the targets, as these programs are not presented at the subprogram level. Additionally, there is no separation made between the targets for the current and subsequent years.

In some cases, a specific goal to be achieved within the program/subprogram is not defined, or the indicator does not meet the criteria specified in the program budgeting methodology. This complicates the assessment of the effectiveness of the program/subprogram at the reporting stage.

For some programs/subprograms, reporting on achieved results are not fully carried out, or the evaluation of results is not conducted in relation to the predetermined indicators.

In case of multiple programs/sub-programs, the achieved results are presented in a different format - inconsistent with the indicators determined at the planning stage, which makes it complicated to compare the planned and achieved results.

In case of certain programs/sub-programs, there is no explanation of the deviations between the planned and achieved results, or the given explanations are of a general nature and makes it challenging to determine the causes of the deviations.

It is important to consider the recommendation of the SAOG and formally approve an action plan for implementing program budgeting, which would outline specific activities to be carried

out within the framework of the reform, along with corresponding milestones and responsible agencies.



# 5. MANAGEMENT OF FINANCIAL ASSETS

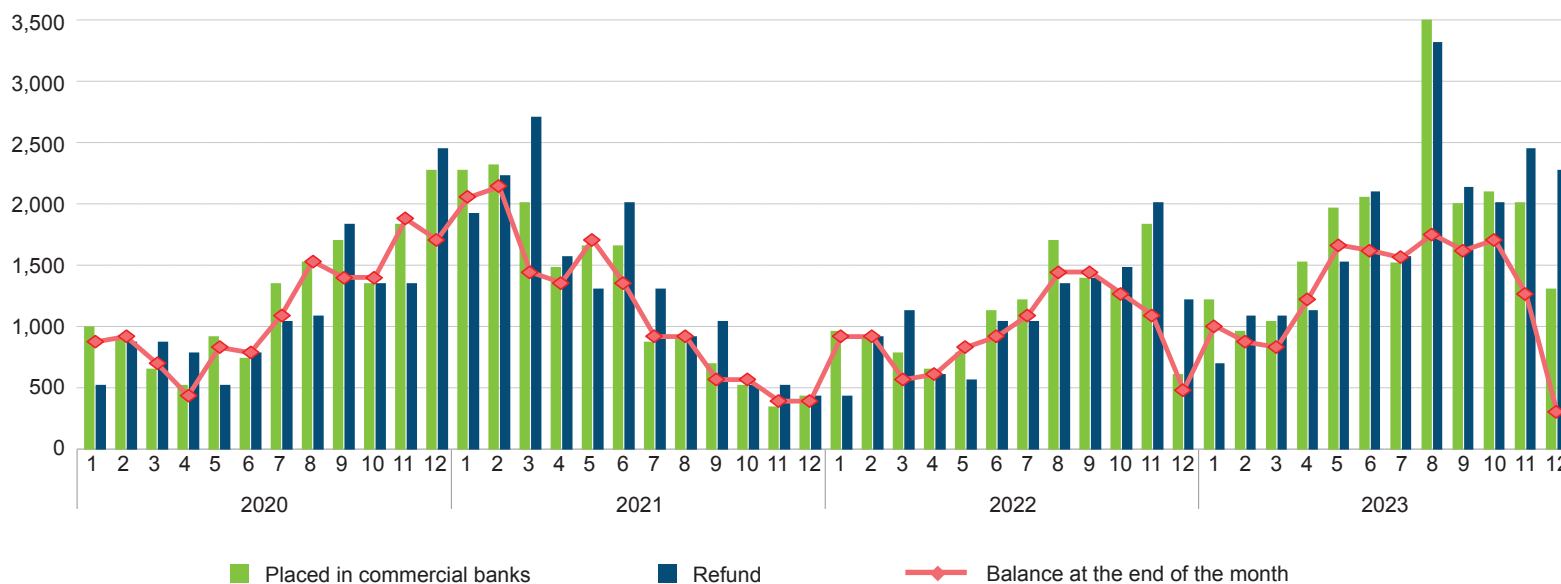


## 5.1 CURRENCY AND DEPOSITS

At the beginning of 2023, the state budget cash balance was 1.2 billion GEL, which increased to 1.6 billion GEL during the year. On the other hand, the amount of deposits placed in the com-

mercial banks by the MoF was decreased from 550 million GEL to 350 million GEL.

**Figure 20.** Amount of deposited balance at the end of each month in the commercial banks (million GEL)



## 5.2 LOANS

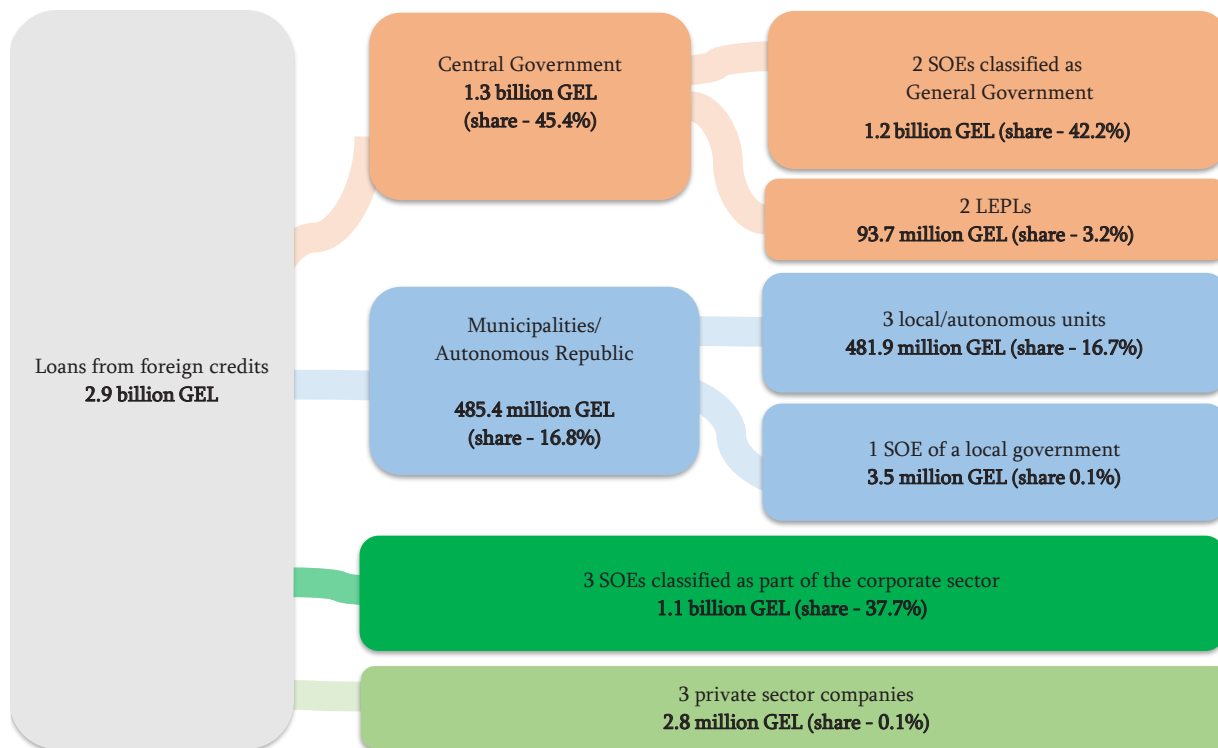
### 5.2.1 LOANS ISSUED FROM THE EXTERNAL CREDIT RESOURCES

In 2023 354.4 million GEL were on-lent for supporting implementation of various investment projects, (127 million GEL

(55.9%) more than in 2022). The major part of the on-lend funds (52%) were directed to the implementation of water supply related activities.

As of the end of 2023, the size of the portfolio of on-lendings was 2.9 billion GEL. The portfolio consists of 75 loans,<sup>15</sup> out of which 20 are restructured.

**Figure 21.** Structure of on-lend resources by beneficiaries - 2023 (million GEL, %)



<sup>15</sup> Loans for which the debtor had outstanding debt as of December 31, 2023.



While examining the management of on-lendings portfolio, SAOG identified deficiencies mainly related to the portfolio management:

As of December 31, 2023, the balance of restructured loans in the on-lending portfolio amounts to 435 million GEL, which is 15.1% of the total portfolio. Considering that in case of non-fulfillment and/or postponement of obligations under the sub-loan agreement, the servicing and repayment of obligations under the main loan agreement is carried out from the state budget, loan restructuring is a source of additional financial pressure on the budget.

An inconsistent approach is observed in the loan restructuring process. In some cases, based on the beneficiary's request, obligations may be postponed without registering it as a restructured loan and without imposing the corresponding penalty. In other cases, loans are restructured also without imposing penalties. This is caused by the absence of formal policies/procedures in the on-lending management process.

Similar to previous years, financial assets and operations on them include loans issued to beneficiaries (debtors) who regularly receive funding from the state budget to cover operating expenses and service the liabilities recorded on their balance sheets. This, in turn, indicates the limited solvency of these enterprises and the indirect participation of the state in the debt servicing process.

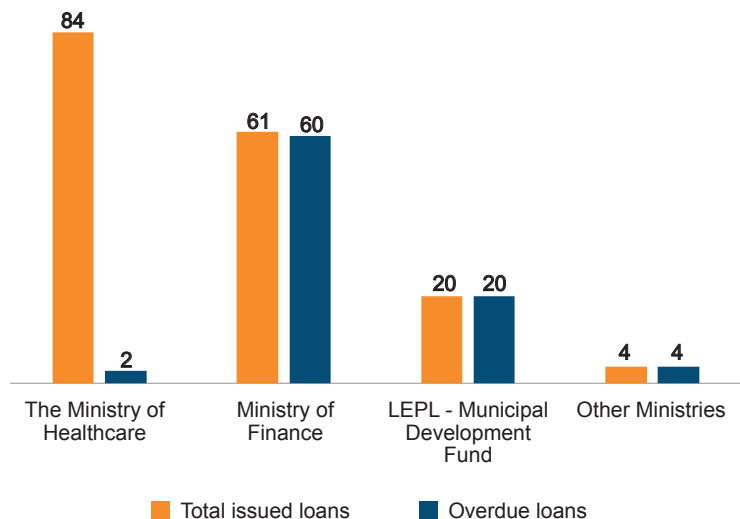
It is important to consider the recommendation of the State Audit Office and for the Ministry of Finance to develop an on-lending policy/policy document for resources mobilized from external credit sources, which will reflect the full cycle of the on-lending process and, accordingly, ensure the establishment of a transparent and uniform approach for each stage of this process.



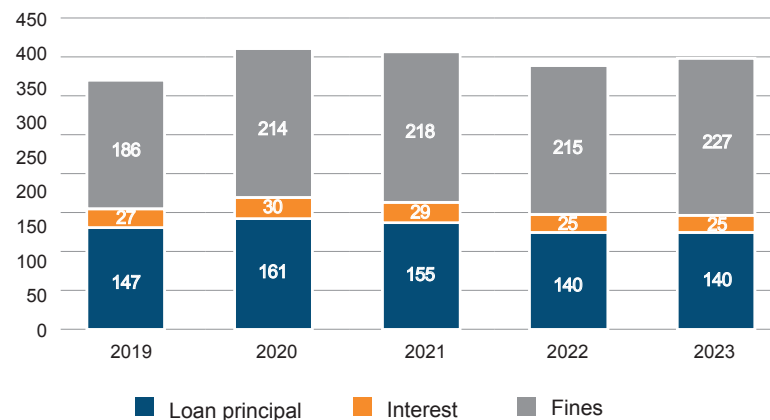
## 5.2.2 LOANS ISSUED FROM THE BUDGETARY RESOURCES

By the end of 2023 173.2 million GEL is lent from the budgetary resources. Total liabilities stemming from these loans are 391.7 million GEL. Out of 169 loans accounted in the portfolio, 82 have a grace period, 1 loan is serviced as planned and 86 are overdue. Total liability accrued on those 86 loans include fines (57.8%), overdue principal amount of the loans (35.7%), and overdue interest payments (6.4%).

**Figure 22.** The total number of loans issued from the budgetary resources reflected in the unified register and among them, the number of overdue loans, categorized by lending agencies - 2023



**Figure 23.** Types of arrears on overdue budgeting loans as of December 31, 2023 (million GEL).



In some cases, creditor agencies do not provide required information in accordance with the budget code's requirements, which cause material inaccuracies in the information reflected in the unified loan registry. Specifically, in December 2022, the Ministry of Economy and Sustainable Development issued a loan of 230 million GEL from budgetary resources to JSC "Georgian Oil and Gas Corporation", which is not recorded in the registry as of December 31, 2023.



## 5.3 SHARES AND OTHER EQUITY

Receipts accumulation from decrease in “shares and other equity” was not planned by the state budget law of 2023, however, the actually mobilized amount during the year totaled 1.6 million GEL. It is notable that out of this amount, 1.4 million GEL was received from sales of land and buildings, which according to the budget classification counts as “Decrease in Non-Financial Assets” operation. Therefore, it is incorrectly classified as “Decrease in Financial Assets”.

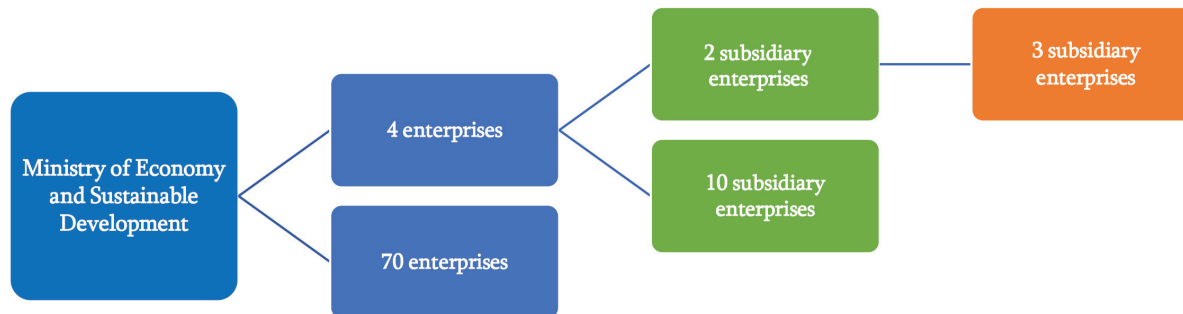
As for the increase in the “shares and other equity”, 1.5 million GEL was spent by the Ministry of Economy and Sustainable Development’s LEPL - Innovation and Technology Agency for capital injection in venture investment fund.

## 5.4 STATE-OWNED ENTERPRISES (SOEs) CLASSIFIED AS GOVERNMENT SECTOR

Within the framework of the state enterprise reform, 325 enterprises<sup>16</sup> were attributed to the government sector, of which 167 are under the central government control. These enterprises should gradually transfer their bank accounts to the Treasury’s Single Account.

The majority of enterprises attributed to the government sector (85 enterprises) are directly or indirectly under the subordination of the Ministry of Economy and Sustainable Development.

**Figure 24.** The number of SOEs belonging to the government sector under the Ministry of Economy and Sustainable Development and their subsidiary companies.



<sup>16</sup> Order N45 of the Minister of Finance of Georgia dated February 15, 2023 “On the Approval of the State Enterprise Sectorization Registry”.



16 SOEs are under subordination of JSC “Georgia Development Fund”.<sup>17</sup> The remaining enterprises belonging to the government sector are under 5 different ministries, autonomous republics, municipalities, and other governmental organizations.

Existing establishment of diversification of controlling agencies for enterprises belonging to the government sector may create certain challenges in the process of implementation of the planned reform, especially when the Ministry of Finance, being in charge of this reform, does not have direct control over them. It is important that the controlling agencies of SOEs, involved in the reform process, commit to the consistent, effective, and successful implementation of the reform.

In the annual report on 2023 state budget execution, information related to SOEs classified as part of central government is presented for only 60 of them out of 167. It should be noted, that 3<sup>18</sup> SOEs among those, which did not submit information to the Ministry of Finance (MoF), are classified as Entities of Public Interest.<sup>19</sup> While the number of reported enterprises has increased compared to 2022,<sup>20</sup> data completeness is still a significant challenge.

The quality and accuracy of data submitted to the Ministry of Finance by the SOEs requires additional attention. In 44 out of 60 enterprises, there are discrepancies between the data submitted and the information presented in the 2023 annual budget execution report. These inconsistencies stem from either errors found by the Ministry of Finance in the initial data or clarifications provided later by the SOEs themselves.

Therefore, existing control mechanisms cannot fully ensure the submission of accurate and complete information by the SOEs.

Given the scale of potential impact on fiscal parameters, it is vital to improve the completeness and accuracy of information submitted by SOEs to the MoF.

Among 60 enterprises reported in the annual report on the state budget execution, sum of their revenues amounted to 1.98 billion GEL, total expenditures – 2.11 billion GEL. 4 SOEs revenues accounted for 79% of total revenues (1.39 billion GEL), while their expenditure (1.46 billion GEL) equaled to 68% of total expenditures. Contribution of mentioned enterprises to the

<sup>17</sup> Legal successor of JSC “Partnership Fund”.

<sup>18</sup> JSC “Georgian Development Fund”; JSC “Borjomi Likani International”; JSC “Universal Medical Center”.

<sup>19</sup> A Public Interest Entity is defined by the Law of Georgia “On Accounting, Reporting and Auditing” and by the Decree №584 of the Government of Georgia dated November 29, 2019.

<sup>20</sup> In the 2022 state budget execution annual report, information was presented about 24 enterprises.



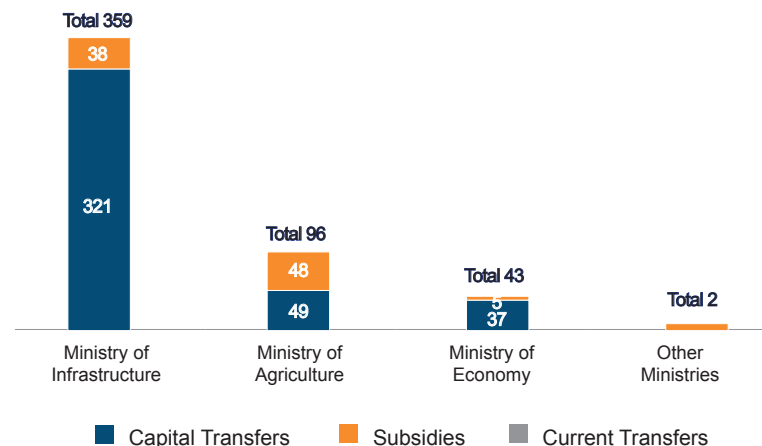
budget deficit is 232 million GEL. Individually, budget balances of 23 enterprises are positive, 3 – zero and 34 – negative. Organizations employ overall 11,991 people, with over 50% employed by 3 SOEs.

Several SOEs heavily rely on regular funding from the state budget, mostly for operational costs or/and covering liabilities. However, budget documentation doesn't provide information on the amount of funding enterprises receive from the state budget.<sup>21</sup>

Particularly, in 2023 enterprises under five ministries received total 522 million GEL from the state budget "Expenses". 407 million GEL was used for financing capital projects. The rest (64 million GEL) was used for subsidizing various activities, operational costs of companies or/and covering liabilities.<sup>22</sup>

In order to improve fiscal transparency, detailed information about funding received by SOEs (considering sectorization) from the state budget, including the purpose of funding, should be presented in the annual report on the state budget execution.

**Figure 25.** Funds transferred from the state budget to SOEs by controlling agencies - 2023 (million GEL)



<sup>21</sup> The information is partially presented in the "Fiscal Risk Analysis" document attached to the state budget law. Specifically, the document includes information about funding provided to state enterprises in the form of loans and subsidies, but does not include information about amounts disbursed as current and capital transfers from the "Other Expenses" item. Furthermore, the data presented in the document does not provide information about the intended purpose of the allocated funds.

<sup>22</sup> For example, funds were transferred to LLC "Georgian Amelioration" and LLC "Georgian Solid Waste Management Company" to cover operational costs. Funds were also transferred to LLC "United Water Supply Company of Georgia" to cover operational costs and liabilities.



## 6. PUBLIC AND GOVERNMENT DEBT

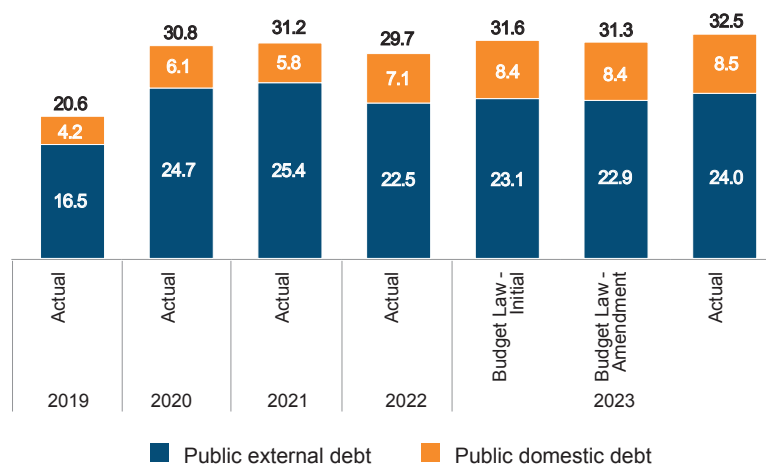
### 6.1 PUBLIC DEBT

The initial state budget law for 2023 established the maximum limit of the public debt<sup>23</sup> at 31.6 billion GEL. A subsequent amendment to the state budget law reduced this indicator to 31.3 billion GEL. As of December 31, 2023, the actual volume of public debt amounted to 32.5 billion GEL (40.5% of GDP), exceeding the maximum limit by 1.2 billion GEL. The public external debt surpassed the limit by 1.1 billion GEL, while the public domestic debt exceeded it by 106 million GEL.

According to the MoF, the excess in the public external debt is attributable to the exchange rate fluctuations between planned and actual measures, as well as higher-than-anticipated disbursements in investment projects. The public domestic debt's overrun of the maximum indicator results from the premium emission of securities due to declining interest rates.

The state budget law amendment occurred in October 2023, at which point both the expenditure dynamics of investment projects and the trends related to the treasury securities emission were largely known. Considering these factors, the surpassing of the state debt ceiling can be partially attributed to the planning deficiencies.

**Figure 26.** The threshold and actual indicators of the public debt as defined by the state budget law (billion GEL)



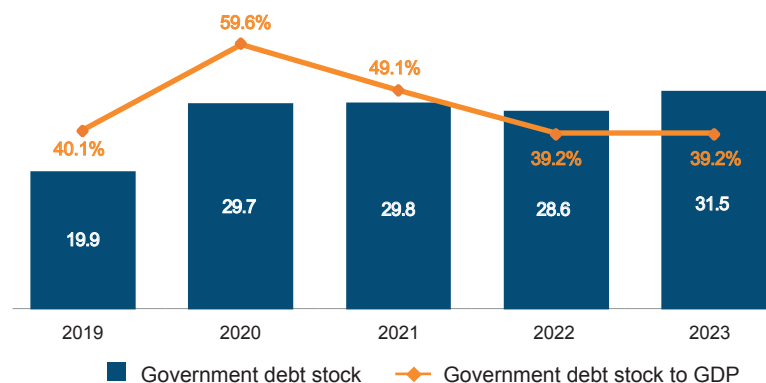
<sup>23</sup> State debt encompasses the debt of the general government sector and the National Bank.



## 6.2 GOVERNMENT DEBT

At the end of 2023, the government debt stock<sup>24</sup> amounted to 31.5 billion GEL, which increased by 2.9 billion GEL (10.1%) compared to the previous year. It is noteworthy that government debt volume constituted 39.2% of GDP, which is equivalent to that of 2022. The primary factor contributing to this outcome is increase in nominal GDP by 7.4 billion GEL (10.1%). The debt amount was affected by the depreciating of the national currency and the mobilization of new credit resources. In particular, as a result of the depreciation of the national currency, the debt stock increased by 381 million GEL, while the mobilization of new debts led to increase of 2.5 billion GEL (government's domestic debt - by 1.4 billion GEL; government's foreign debt - by 1.1 billion GEL).

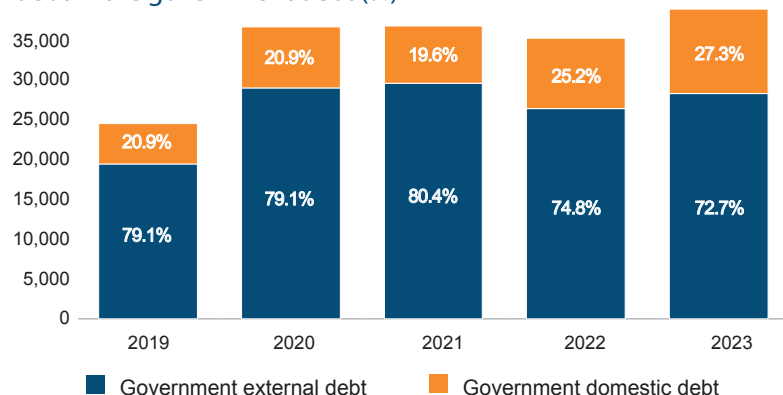
**Figure 27.** Government debt stock (at the end of the year) and its ratio to the GDP of the corresponding year (billion GEL; %)



The assessment of the government debt stock at the end of 2023 reflects an incomplete amount. Specifically, it does not include the debt of five SOEs attributed to the government sector, amounting to a total of 39 million GEL.

The share of the foreign debt in the government debt stands at 72.7% at the end of 2023, which is 2.2 p.p. less than the corresponding figure of 2022 (74.8%). Despite the reduction in the share of external debt, the sensitivity of government debt to the fluctuations in currency exchange rates is still a significant challenge. It is important to note that the Government Debt Management Strategy for 2024-2027 envisions a reduction of the aforementioned indicator to 63.1% by the year 2027.

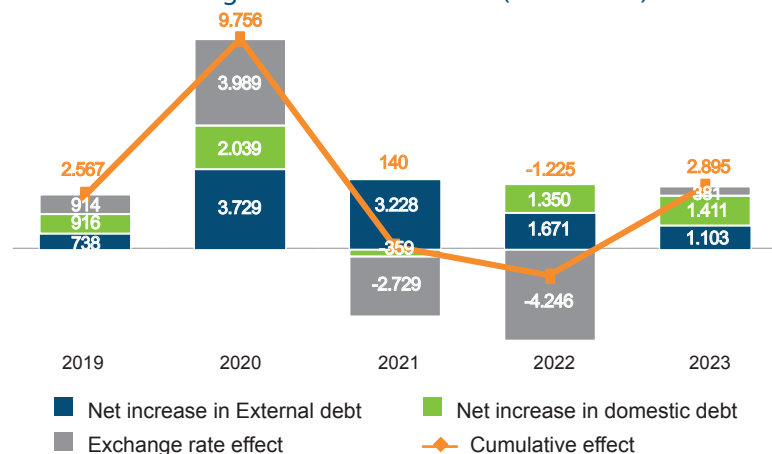
**Figure 28.** The share of the government's external and domestic debt in the government debt (%)



<sup>24</sup> For the purposes of the Organic Law of Georgia "On Economic Freedom", government debt includes the state debt as defined by the Law of Georgia "On the State Debt", excluding the National Bank's debt to the IMF, and additionally includes the loan obligations of municipalities, Legal Entities of Public Law (LEPLs), and state enterprises attributed to the government sector.



**Figure 29.** The effect of the GEL exchange rate and new borrowing on the increase in government debt stock (million GEL)



According to the Order No. 328 of the Minister of Finance dated September 26, 2022, the Government Debt Management Strategy, after approval by the government, should be placed/published on the website of the Ministry of Finance by December 31 of each year. It should be noted that over the past two years, the publication of the government-approved strategy has been carried out in violation of the deadlines set by this order as publications took place on the subsequent fiscal year. Moreover, as of May 20, 2024, the 2024-2027 strategy has not been approved by the government.

For better integration of the directions defined in the strategy into the budget process, it is advisable to update it before submitting the final version of the draft state budget law for the following year. It should be noted that the integration of the strategy into the budget process is also required by the DeMPA methodology developed by the World Bank.

It should be positively assessed that the Government Debt Management Strategy 2024-2027 takes into account the recommendation made by the SAOG. Particularly, as recommended, in the first pillar of the strategy, the target benchmarks are set considering the government debt defined in the Organic Law of Georgia on "Economic Freedom", instead of the government's net debt measure.

According to the strategy, its scope and objectives extend to the components of the debt rule indicator defined by the Organic Law of Georgia on "Economic Freedom" (government debt and obligations arising from PPP projects). However, obligations arising from PPP projects are reflected only in the review section of the existing debt portfolio, while they are not considered in the target indicators of the strategy.

In relation to the government debt management strategy, several issues are noteworthy:



Some activities planned under the strategy do not have deadlines and mid-term targets; also, certain activities/measures require the existence of formally written criteria. Defining criteria and setting deadlines is particularly critical for the activities whose targets are solely set by this strategy and are not regulated by other regulatory acts.

### 6.3 GOVERNMENT'S EXTERNAL DEBT

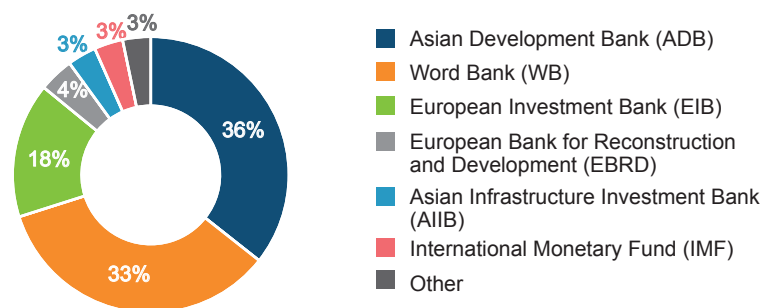
At the end of 2023 the volume of the government's external debt amounted to 22.9 billion GEL, which is 6.9% (1.5 billion GEL) more than the corresponding figure of the previous year. The largest part of the government's external debt portfolio - 17.2 billion GEL (constituting 75.2% of the total external debt portfolio) - consists of borrowings from the multilateral creditors.

Among the multilateral creditors, the Asian Development Bank (ADB) represents the largest lender (6.1 billion GEL, 35.7% of the total multilateral credit volume), followed by the World Bank (WB) (5.7 billion GEL, 33.1% of the total multilateral credit volume).

Bilateral credits also constitute a significant part of the government's external debt, accounting for 19.0% (4.3 billion GEL).

France, Germany, and Japan represent the largest bilateral donors. The cumulative indebtedness to these countries amounts to 4.2 billion GEL (96.2% of the bilateral creditors' share).

**Figure 30.** Components of the Government's external debt by creditors (billion GEL. %) - 2023

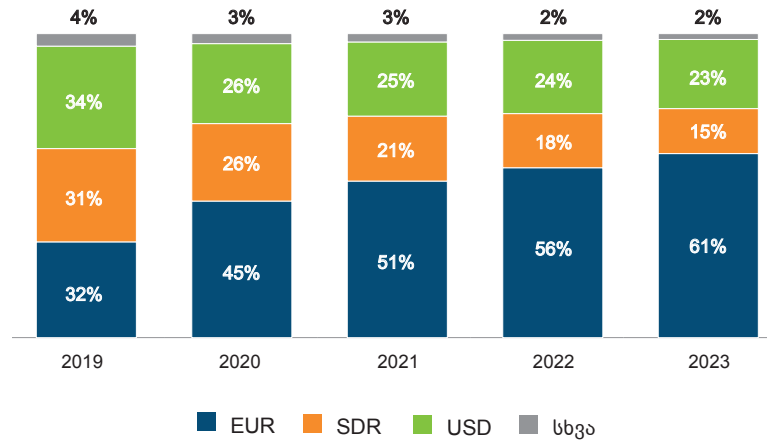


As of December 31, 2023 the Government's external debt portfolio consists of loans denominated in five different currencies.<sup>25</sup> It should be noted that the currency structure of foreign loans has changed significantly in the recent years. In particular, the share of liabilities denominated in USD and SDR decreased, while the share of liabilities in EUR almost doubled compared to 2019, reaching to 61%.

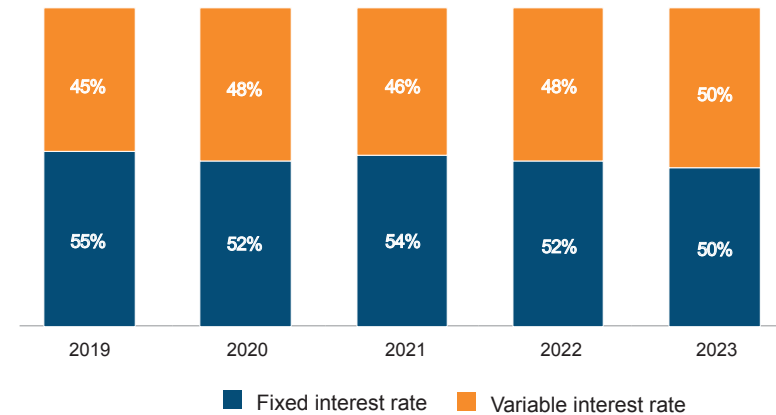
<sup>25</sup> United States Dollar, Euro, Special Drawing Rights (SDR), Japanese Yen, Kuwaiti Dinar.



**Figure 31.** Structure of government's external debt by currencies (%)



**Figure 32.** Government's external debt stock by interest rate types (%)



In recent years, the share of floating interest rate loans in the credit portfolio has an increasing tendency. Compared to 2019, the share of loans bearing floating interest rates increased by 5.1 p.p. and equaled to 50% at the end of 2023. It should be mentioned that according to the existing Government Debt Management Strategy (MTDS), the share of floating rate debt should not exceed 50% by 2025.

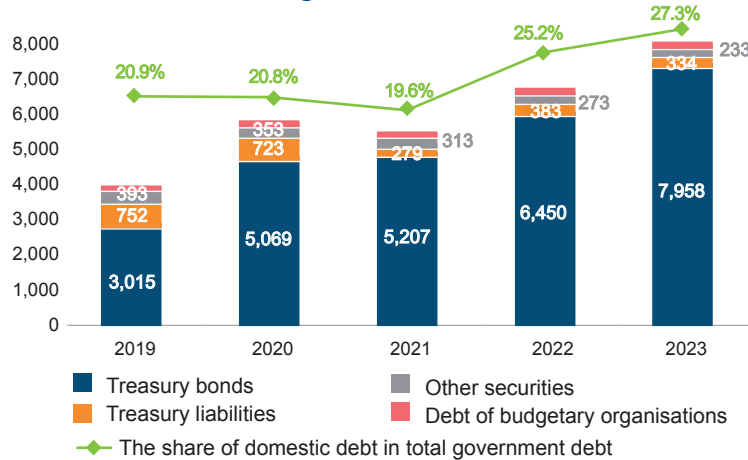
## 6.4 GOVERNMENT'S DOMESTIC DEBT

In 2023 the Government's domestic debt grew by 1.4 billion GEL compared to the previous year and equaled to 8.6 billion GEL. The growth was fully caused by the increase in the volume of treasury securities. The share of the domestic debt in the governments total debt increased by 2.1 p.p. compared to 2022 and equaled to 27.3%.

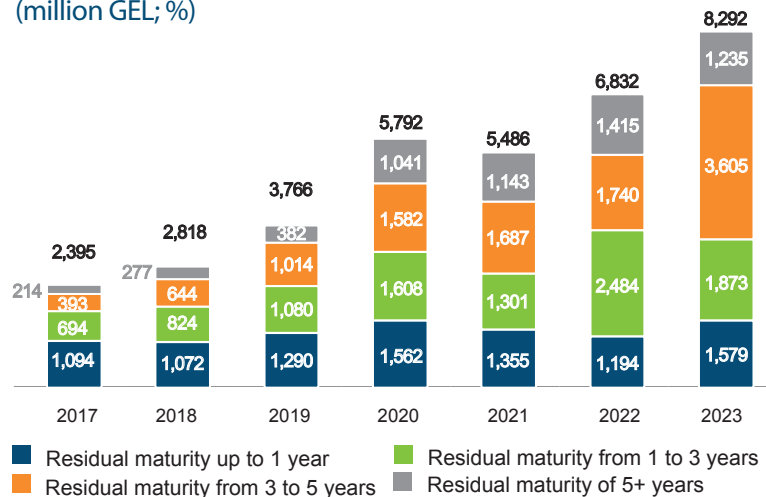
As of the end of 2023, treasury bonds with a residual maturity of 3-5 years has the largest share (43.5%) in the total treasury securities portfolio, which represents a significant increase compared to previous years.



**Figure 33.** The composition of the government's domestic debt and its share in the total government debt (million GEL, %)



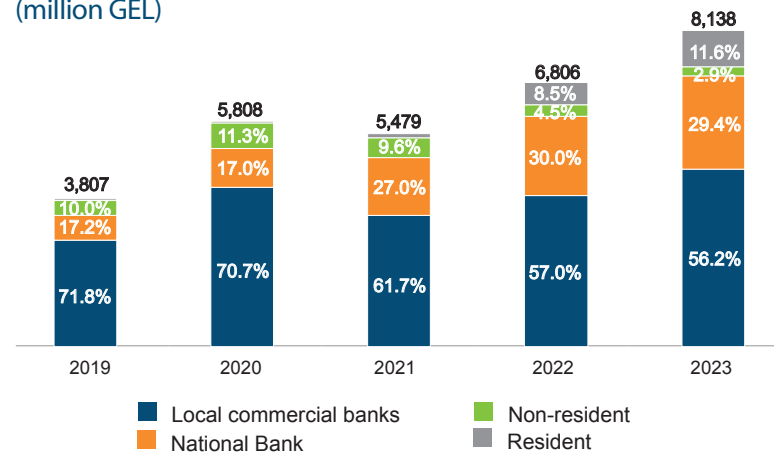
**Figure 34.** Treasury securities portfolio by residual maturity (million GEL; %)



In 2023, the government issued treasury securities with a nominal value of 2.9 billion GEL. Recent years have witnessed a significant increase in the issuance of long-term treasury bonds, while treasury bills issuances have decreased.<sup>26</sup> By the SAOG's assesment, to minimize refinancing risks, given the increasing share of domestic debt in government debt portfolio, it is advisable to gradually revise the minimum ATM threshold, declared in the MTDS for domestic debt upwards.

The holders of the treasury securities are mainly local commercial banks. However, it should be noted that over the last 5 years, the share of commercial banks has been characterized by a decreasing dynamics. The commercial banks owned 56.2% of the total securities at the end of 2023. In comparison to 2022, the share of other resident investors increased by 3.1 p.p., reaching 11.6%.

**Figure 35.** Distribution of the treasury securities by holders (million GEL)



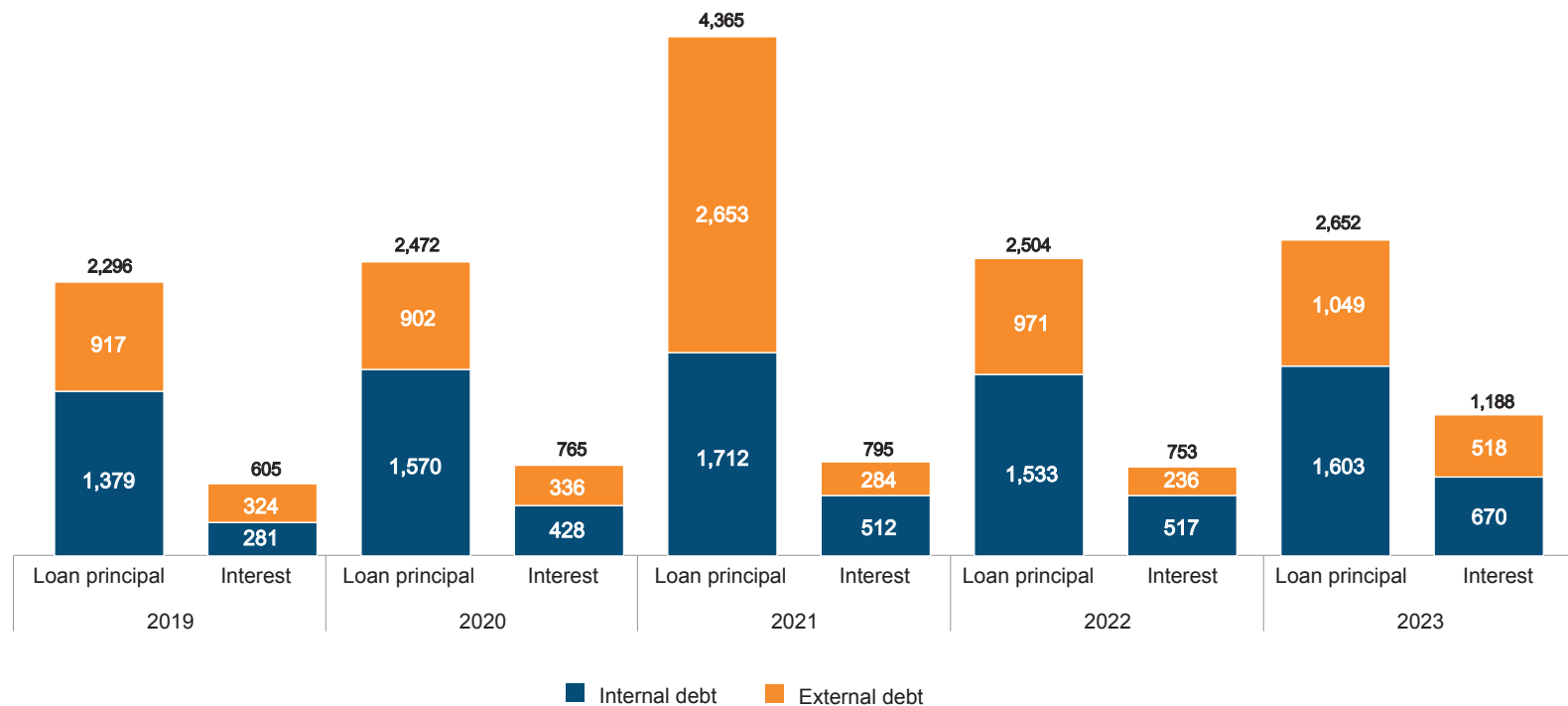
<sup>26</sup> In 2022, the issuance of long-term securities amounted to 2.3 billion GEL, while short-term securities totaled 535 million GEL; in 2021, short-term issuances amounted to 360 million GEL, while long-term issuances totaled 991 million GEL.



## 6.5 GOVERNMENT DEBT INTEREST AND REPAYMENT COSTS

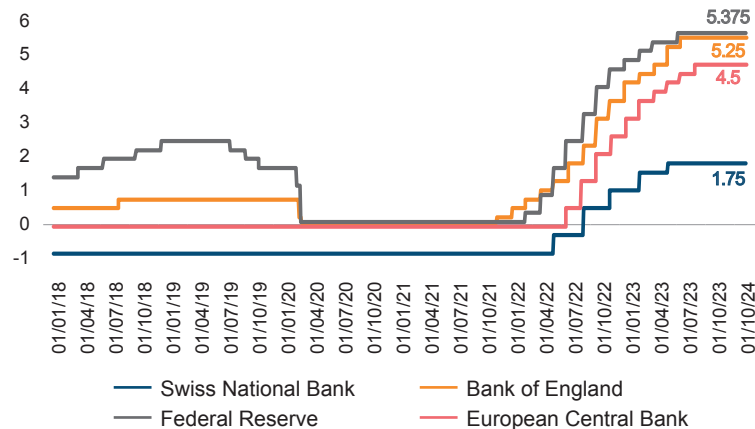
In 2023 3.8 billion GEL was spent on the government debt interest and repayment, which is 95.7% of the budget plan determined by the state budget law. The largest share (59.2%) of government debt servicing and repayment costs comes from domestic debt servicing and repayment expenses, which amounted to 2.3 billion GEL. The government directed the majority of this amount (70.5%) towards the repayment of principal.

**Figure 36.** Dynamics of the government debt service costs (million GEL)

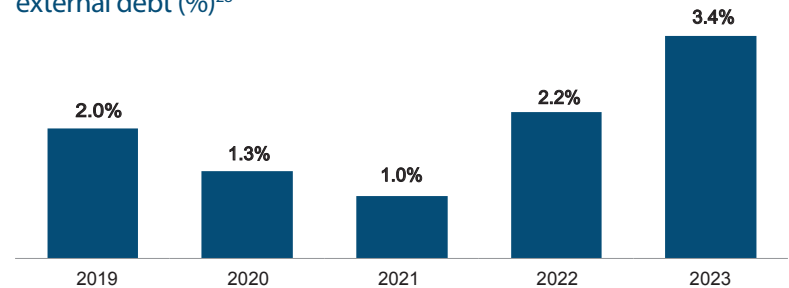


Since the beginning of 2022, amidst the tightening of global monetary policy, the weighted average interest rate on government external debt has increased dramatically, reaching 3.4% by the end of 2023. Considering that half of the external debt comprises floating interest rate bearing loans, the interest expenses on external debt have increased substantially compared to the previous years.

**Figure 37. Dynamics of Central Banks' Monetary Interest Rates<sup>27</sup> - 2018–2024 (% Q1)**



**Figure 38. Weighted average interest rate on government's external debt (%)<sup>28</sup>**



Conversely, resources mobilized from domestic sources are characterized by higher interest rates compared to those obtained from external sources. Consequently, the increasing share of domestic debt in the government debt portfolio significantly pushes interest costs upward.

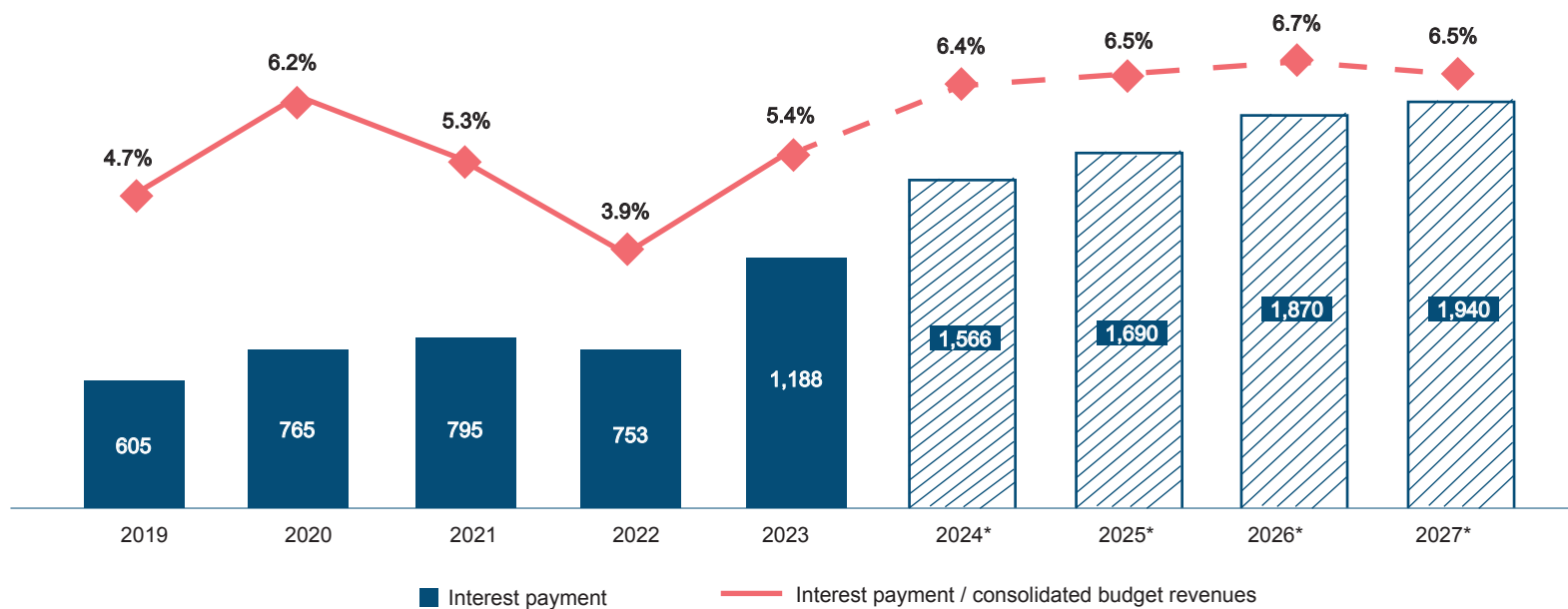
The simultaneous impact of the aforementioned two phenomena (tightening of global monetary policy and the increasing share of domestic debt) creates substantial fiscal pressure on the state budget.

<sup>27</sup> Source: Bank for International Settlements (BIS)

<sup>28</sup> It is worth noting that up to and including 2020, the debt portfolio included Eurobonds issued in 2011 with a coupon rate of 6.875%. In April 2021, these Eurobonds were refinanced with new Eurobonds carrying a 2.75% coupon rate. As a result, assuming global interest rates remained unchanged, the weighted average interest rate of the debt portfolio should have decreased in the following years.



**Figure 39.** Government debt service (interest) costs (million GEL) and its share in consolidated budget revenues (%)



\* Forecast

It is advisable to take into consideration the recommendation of the SAOG and incorporate indicator(s) for assessing debt service expenses in the government debt management strategy

document and the potential impact of the strategy's predefined target indicators on this/these indicator(s).



## 7. STATUS OF THE IMPLEMENTATION OF RECOMMENDATIONS ISSUED BY THE SAOG

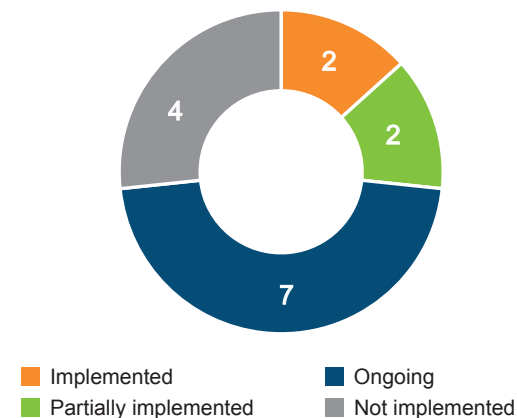


The annual report on the state budget execution of 2023 includes information on possibility of taking into account the remarks and recommendations presented in the SAOG's report on government's report on the state budget execution of 2022.

It is noteworthy that an action plan, as defined by the government decree, has not been prepared in response to the aforementioned recommendations.<sup>29</sup>

In response to the systemic deficiencies and shortcomings identified in the 2020-2022 budget executions, the SAOG issued 15 recommendations. Currently, 4 recommendations have been fully or partially implemented and 7 recommendations are ongoing.

**Figure 40.** Status of implementation of recommendations issued by the SAOG in the report on government's report on the state budget execution for 2020-2022



<sup>29</sup> For the purpose of strengthening reporting and accountability in the public financial management process, Decree No. 144 of the Government of Georgia was issued on March 30, 2015, according to which the Government of Georgia determines an action plan regarding the consideration of comments and recommendations expressed in the report prepared by the SAOG on the execution of the state budget.





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