REINVENTING GEORGIAN WINE BY 'THINKING OUTSIDE THE QVEVRI'

WHITHER THE LARI? GEORGIAN BANKS, BUSINESSES TAKE A LOOK AT 2022

WHAT CAN BE DONE ABOUT GEORGIA'S DEBT PROBLEM

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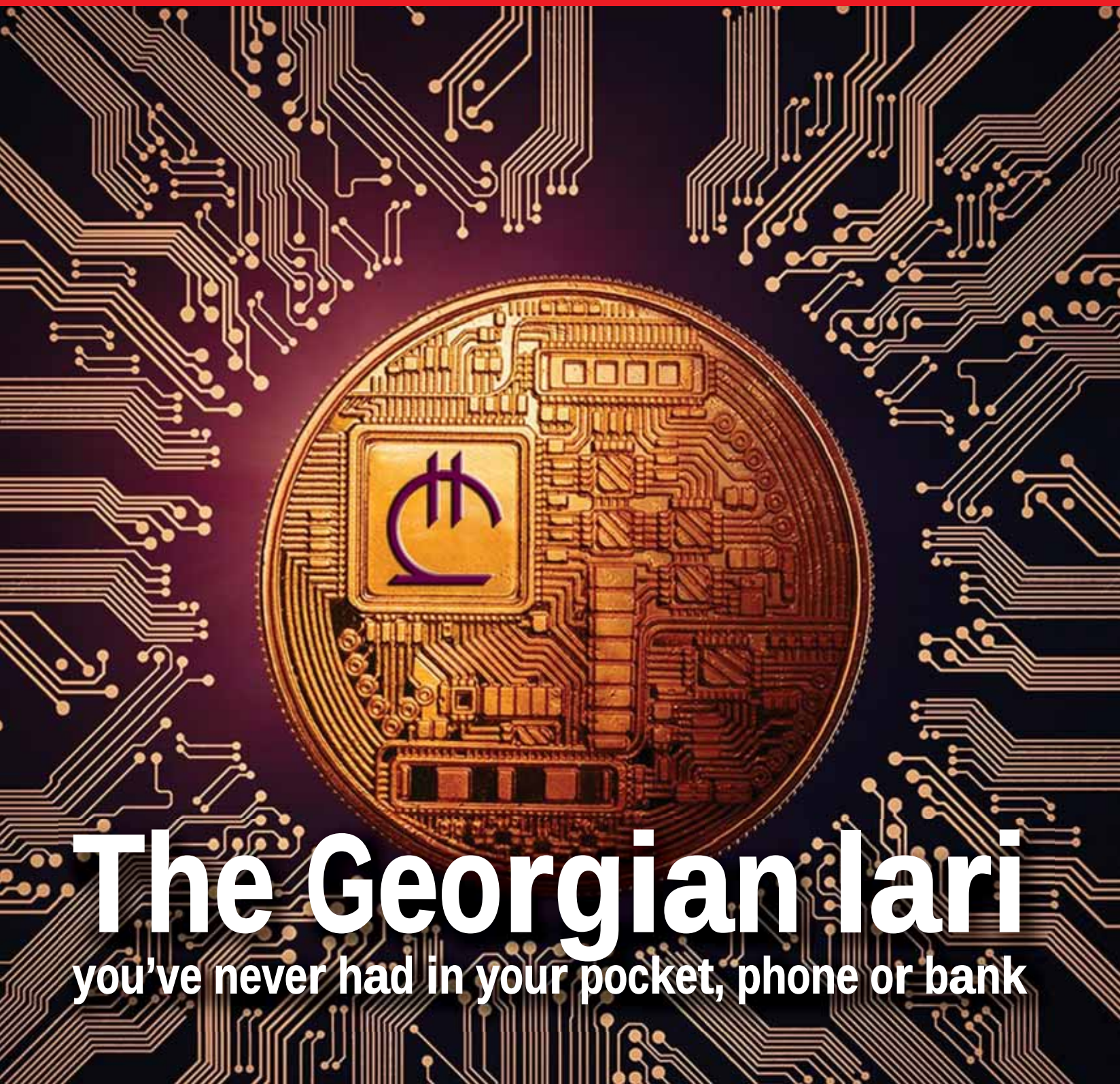

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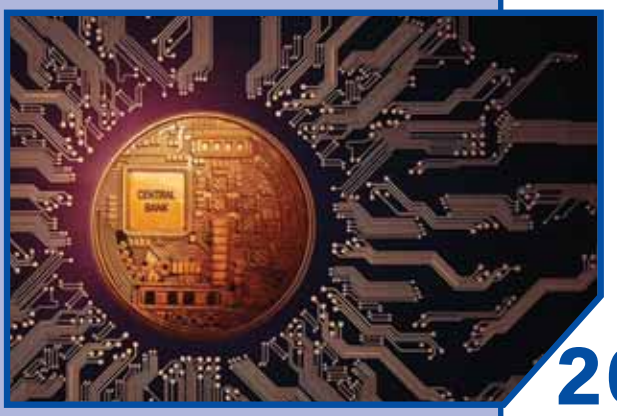
CONTENT

14



26

38

41

6. Investment news

10. Reinventing Georgian wine by 'thinking outside the *qvevri*'

12. Galt & Taggart: Georgian wine industry entering a new era

14. Saperavi to the rescue – why it pays to have thick skin in the era of climate change

18. Small donations and big changes: USAID supports crowdfunding to boost civic initiatives

20. What can be done about Georgia's household debt problem

24. ISET-PI: is there an end in sight to food price inflation?

26. The new kind of Georgian lari you've never had in your pocket, phone or bank

30. BLC: protecting your investment under Georgia's network of international investment treaties

32. TBC Capital's monthly tourism watch: sector continues to grow but remains vulnerable

34. Whither the lari? Georgian banks, businesses take a look at 2022

38. A *kovidsalami* to the new Georgian – how COVID-19 has changed the language forever

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ADB: GEORGIAN ECONOMY TO GROW 8.5% IN 2021, 6.5% IN 2002

The Georgian economy is expected to grow 8.5% in 2021 driven by an expansion in agriculture, industry, and services as well as the gradual lifting of restrictions imposed due to the COVID-19 pandemic, the Asian Development Bank (ADB) said in its annual economic publication the Asian Development Outlook 2021 Update.

In addition, the bank predicts the Georgian economy to grow a further 6.5% in 2022.

The ABD also notes that the country's strong rebound from more than a 6% contraction last year to growth of 12.7% in the first half of 2021 following significant government support to firms and households as well as sizable assistance from development partners.

GEORGIAN WINE EXPORTS UP NEARLY 20%

Georgia exported 65 million bottles of wine to 59 countries in January-August 2021, which is an increase of 19% compared to the same period of 2020, says the Georgian National Wine Agency. Wine exports generated $145 million in revenue, which were up 13% YoY.

This news comes after Prime Minister Garibashvili announced in August that the government intends to help boost wine exports to $1 billion in the next 10 years.

Garibashvili also noted that the government has allocated 100 million GEL to subsidize the grape harvest in 2021 and help about 25,000 wine growers and producers avoid negative impacts of the COVID-19 pandemic.

The Georgian government announced in September that it had approved a new state program to co-finance marketing campaigns of wine companies in new export markets.

The program, which will exclude marketing for Russia and CIS countries, will be implemented by the National Wine Agency and have a budget of 3 million GEL.

GEORGIAN NATIONAL BANK INCREASES REFINANCING RATE TO 10%

The National Bank of Georgia (NBG) announced after the August meeting of its Monetary Policy Committee that it planned to increase the refinancing rate by 0.5 percentage points to 10%.

Georgia's annual inflation came out unexpectedly high in comparison with last year and amounted to 11.9% in July, the NBG stated.

The NBG reported that various factors contributed to high inflation, such as sharply increased prices of food and oil in international markets as well as significantly increased international shipping costs, which affects the prices of imported goods.

"The short-term inflation forecast has increased considerably compared to the previous forecasts, and it is expected that inflation in 2021 on average will be higher than 9%," the statement of the NBG reads.

NGO Society and Banks stated that 140,100 loans tied to floating interest rates remain active as of July 1, 2021, which means that the prices of these loans may grow as well because of the increased refinancing rate.

GEORGIAN ECONOMY GROWS 10.3% IN AUGUST, 12% IN THE FIRST EIGHT MONTHS OF 2021

The estimated real GDP growth rate in August 2021 amounted to 10.3% YoY and 12% YoY in January-August of 2021, shows preliminary data from Geostat.

Last month, the following industries of the economy posted growth compared to the same period of the previous year: manufacturing; financial and insurance activities; trade; electricity, gas, steam and air conditioning; hotels and restaurants; transportation and storage; arts, entertainment and recreation. A decline was registered in construction, mining and quarrying.

Georgian Prime Minister Irakli Garibashvili said that the economic growth data of Georgia 'is unprecedented in the region' and it became possible to achieve high economic growth thanks to state programmes such as Preferential Agro-Credit, Produce in Georgia, and Plant the Future. He said that starting in 2022, the government will implement larger programs and will invest 2.5 billion GEL ($803.9 million) in the development of local production while 7 billion GEL ($2.25 billion) will be invested in agriculture.

MONEY TRANSFERS TO GEORGIA UP AN AVERAGE 10.8% IN JULY AND AUGUST

Georgia received $413.3 million from abroad in July and August 2021, which is 10.8% more than the amount received in the same period of 2020, the National Bank of Georgia reports. The largest remittance senders were Russia ($77.8 million), Italy ($66.9 million) and the United States ($50.1 million).

REVENUE FROM INTERNATIONAL TOURISM UP 45.6% IN JANUARY-AUGUST

Georgia received $703.9 million from international tourism in January-August 2021, which is 45.6% more compared to the same period last year.

In August alone, Georgia received $198.8 million, which is an increase of 1,243% compared to 2020 and a decrease of 51.8% compared to the pre-pandemic year of 2019. Georgia hosted 266,544 visitors in August 2021, which is a 510% increase compared to the same month of 2020; however, it is still 75% less than August 2019.

The top ten countries that tourists came from were: Russia, Turkey, Ukraine, Georgia (non-residents), Armenia, Saudi Arabia, Belarus, Kazakhstan, Azerbaijan, and Poland.

TBILISI INTERNATIONAL AIRPORT RANKED AMONG THE BEST AIRPORTS IN EASTERN EUROPE

Tbilisi International Airport has been named one of the best airports in Eastern Europe for the eighth time in a row by Skytrax World Airport Awards 2021. Ten airports were named the best airports in Eastern Europe in 2021, in which Tbilisi International Airport took sixth place.

The survey evaluates customer satisfaction across 39 key performance indicators for airport service and product," said the sole operator of the Tbilisi and Batumi airports, TAV Georgia. Tbilisi International Airport won the Golden ▸▸

Brand in the category of Public Transport and Service in 2011 and the Routes Airport Marketing Award in 2013.

FRASER INSTITUTE REPORT: GEORGIA 5TH IN WORLD IN TERMS ECONOMIC FREEDOM

Georgia has taken 5th place among 165 countries in the world in the economic freedom annual report published by the Fraser Institute. Last year Georgia took 8th place among 162 countries in the same report. The report measures economic freedom based on regulation, freedom to trade internationally, size of government, property rights, government spending, and taxation.

Fraser's report notes that "people living in countries with high levels of economic freedom enjoy greater prosperity, more political and civil liberties, and longer lives."

ANNUAL INFLATION AT 12.8% IN AUGUST, BREAKING 10-YEAR RECORD HIGH

The annual inflation rate in August amounted to 12.8%, Geostat data shows. With regard to the annual core inflation, prices increased by 6.7%, while annual core inflation without tobacco amounted to 6.8%.

The annual inflation rate was mainly influenced by price changes for the following groups: food and non-alcoholic beverages (+16.2%); transport (+22.5%); housing, water, electricity, gas and other fuels (+11.6%); and health (+10.9%).

TURKEY, RUSSIA, CHINA – TOP TRADE PARTNERS IN JANUARY-AUGUST 2021

Turkey ($1.28 billion), Russia ($1.01 billion) and China ($941.3 million) were Georgia's top trading partners in total external trade turnover in January-August 2021, according to preliminary data from the National Statistics Office of Georgia.

In the reporting period, Georgia's top trading partners by exports were China ($421.8 million), Russia ($377.1 million) and Azerbaijan ($347 million), while top trading partners by imports were Turkey ($1.07 billion), Russia ($634.8 million) and China ($519.5 million).

The top three exports were copper ores and concentrates ($ 517.9 million), motor cars ($293.4 million), and ferro-alloys ($265.5 million). The top three imports were motor cars ($547.6 million), petroleum and petroleum oils ($492.1 million), and copper ores and concentrates ($ 445.9 million).

Overall, Georgia's external trade turnover amounted to $8.68 billion in January to August 2021, which is 22.3% higher compared to the same period of the last year.The value of exports increased 26% and totaled $2.61 billion, while imports also increased 20.7%, amounting to $6.07 billion.

UNEMPLOYMENT UP 3.8% IN Q2 OF 2021

The unemployment rate in Georgia has increased 3.8% in the second quarter of 2021 compared to the same period of last year, amounting to 22.1 per cent, the National Statistics Office of Georgia reports. In the reporting period, the economically active population came to 51.4% of the working age population (aged 15 and older).The economic activity rate has increased by 1.1%, while the employment rate decreased by 1.0%.

Georgian Economy Minister Natia Turnava says the increased unemployment rate in the second quarter of 2021 is related to coronavirus restrictions imposed in the same period of last year.

People who lost their jobs last year were represented in statistics in the following period. This circumstance largely explains the increase in unemployment in the second quarter of this year," Turnava stated.

EU SIMPLIFIES EXPORT PROCEDURES FOR GEORGIAN HAZELNUTS

The EU is simplifying the export procedures for Georgian hazelnuts as a result of an increased confidence in the quality of Georgian hazelnuts and an effective policy of state control, announced the National Food Agency of Georgia.

Specifically, the standing committee on plants, animals, food and feed of the EU Commission's Directorate-General

for Health and Food Safety has decided to reduce the frequency of inspection of Georgian hazelnuts exported to the EU.

The agency reports that the decision of the committee was based on the measures taken by Georgia in 2020 to comply with the requirements of the European Union and avoid aflatoxin contamination.

The decision was made on July 9 and came into force on July 29.

Georgia exported 18,000 tonnes of hazelnuts abroad in 2020, which is a 34% increase compared to 2019, says the Ministry of Agriculture of Georgia. To the EU alone, Georgia exported 12,900 tonnes of hazelnuts last year, 59% higher than 2019.

Statistics show that 44% of agri-food exports from Georgia to the EU come from hazelnuts, followed by wine (15%) and mineral waters (15%).

NEW ROADS CONNECT GEORGIA'S CAPITAL AND REGIONS

Progress on the Rikoti Pass highway, a mountain pass which divides Georgia into its eastern and western parts, is moving steadily forward with the opening of two lanes of a four-lane section in late September.

A total of 51.6 km of roads are planned to be built on the Rikoti Pass, which will include 96 bridges and 53 tunnels. So far, eight tunnels have already been carved.

Minister of Infrastructure Irakli Karseladze says that 80% of the Rikoti Pass project is in the active construction phase. About 2.6 billion GEL ($836 million) will be spent on the construction of all roads on the Rikoti Pass.

On September 28, a 51 kilometer road connecting the two Georgian regions of Zemo Imereti and Racha also opened, shortening the distance between

the two regions by 80 km and reducing travelling time by 1.5 hours.

Georgian Prime Minister Irakli Garibashvili said that thanks to the new road, it will now be possible to travel from Tbilisi to Racha in about three hours. "This is a very comfortable road for our citizens, the population of Racha, the population of Upper Imereti and our tourists and vacationers," Garibashvili said. Construction of the new road was financed from the budget and cost around 111 million GEL ($35.7 million).

AVERAGE SALARY INCREASES BY 15.5% IN Q2 2021

The average monthly nominal earnings in Georgia increased by 15.5% (+177.9 GEL) in the second quarter of 2021 compared to the same quarter of the previous year and amounted to 1,328 GEL ($428), reports the National Statistics Office of Georgia.

Georgian Economy Minister Natia Turnava said that following the recovery of the economy, the salaries of employees in a number of sectors have improved.

The highest increase in monthly earnings were observed in the following fields: financial and insurance activities (+15.4% YoY); information and communication (+12.4% YoY); construction (+23.7% YoY); and professional, scientific and technical activities (+7.4% YoY).

FINANCE MINISTER PRESENTS 10-YEAR DEVELOPMENT PLAN

Georgian Finance Minister Lasha Khutsishvili presented his ministry's 10-year development strategy in August, which aims to tackle poverty and unemployment as well as increase overall economic well-being in Georgia.

The proposed macroeconomic stability plan and reforms aim to ensure high economic growth. They include: reducing foreign debt to 45% by 2026 and below 40% by 2030; reducing the current account deficit by 4%; decreasing the share of foreign currency in total debt by 65%; improving the tax dispute resolution system; and implementing capital market reforms.

The finance minister also announced reforms to state-owned enterprises, including the introduction of a corporate governance standard; commerciality; competition promotion in the field; correctly formed rationality of state participation in enterprises; and the need for a corporate purpose application document.

He also noted that in terms of budget transparency, Georgia is among the six countries in the world with a fully transparent budget index.

Reinventing Georgian wine by 'thinking outside the *qvevri*'

Source: Chateau Mukhrani

AS GEORGIAN WINES CONTINUE TO FIND FAME AND FANS ABROAD, THE COMPETITION BETWEEN THEM IS STIFFENING. PRODUCERS ARE NOW LOOKING FOR INNOVATIVE APPROACHES TO DIFFERENTIATE THEIR WINES FROM TOP COMPETITORS. WINE BLOGGER AND TOUR ORGANIZER DARIA KHOLODILINA GIVES HER TAKE ON THE MANY EXCITING INVENTIONS IN THE WORLD OF GEORGIAN WINE.

DARIA KHOLODILINA

Being a wine aficionado in Georgia has never been so exciting. A walk through the Tbilisi districts of Vera or Sololaki provides a testament to the number of new brands and bars that are thriving despite the pandemic. A recent Galt and Taggart report is equally optimistic in its assessment, expecting the industry's revenue to double in the next five years to $350 million.

Much of this is happening on the back of external markets that are welcoming newcomers who can deliver quality, unique wine experiences. However, Georgian winemakers are running into competition – with themselves. In an effort to differentiate their products, winemakers are getting creative and innovating in qvevri production methods.

SKINS AND STEMS VYING FOR A PLACE UNDER THE SUN

Though wine has been a part of Georgia's material culture for 8,000 years and the country is affectionately known as the 'cradle of wine', it is only in recent years that wine has acquired the culture of consumption found in the more classic wine countries, including tastings and increased attention to flavors and properties.

This recent change in the focus of local wine culture has been accompanied by increasingly sophisticated qvevri winemaking process, a trend that started with a dozen vintners back in 2007-2008 and has regained its popularity to the extent that larger producers like Teliani Valley have jumped in to get a piece of the action. It has also led to the emergence of new maranis [Geo. wine cellars]. The National Wine Agency says they have been growing since 2017 at a rate of around 50 new maranis a year.

> Qvevris are an ancient Georgian wine making vessel, generally egg-shaped and made of terra-cotta clay. It is typically buried in the ground for natural temperature control.

The uniqueness of qvevri wines has not gone unnoticed by markets thirsty for new tastes. However, importers, tour organizers and eager oenophiles venturing into the country's wine-growing regions often end up hearing much of the same story when it comes to the qvevri and its place in the long history of Georgian wine. This author likes to joke that bingo card terms compiled from one marani would win every time at al-

most any other. The words 'tradition', 'qvevri', 'ancestors', 'skins and stems' and 'gaumarjos' are powerful, but lose marketing appeal when overused.

While a healthy respect for ancient traditions is to be appreciated, producers should remember a niche importer may taste 10 or 20 equally good samples made through the same process of skins and stems left in the qvevri for six months before being bottled immediately. With similarly high levels of tannins, exotic flavours of black tea, camomile, baked quince and apricot pie, as well as a narrative of the family's winemaking roots, retailers have difficulty selling the same stories repeatedly. It is becoming increasingly clear to market insiders that in order for Georgian wines to compete in these new competitive markets, they need to diversify their products and think outside the qvevri.

Many new ideas have arrived with people who have seen something beyond the existing paradigm and are eager to implement it in Georgia. For instance, Frenchmen Vincent Jullien and Guillaume Gouerou at Lapati Wines (2012-2013) and Bastien Warskotte of Ori Marani (2017) have contributed to the development of a natural sparkling wine culture and brought the term pét-nat into the Georgian wine vernacular.

Pét-nat (pétillant naturel, or natural sparkling) is a wine that finishes its primary fermentation in the bottle and gets its bubbles from the carbon dioxide that is released as a byproduct of fermentation and pressurization. It has been a trendy drink internationally for quite some time, but the hype in Georgia mostly started with the help of these French winemakers.

Both cellars have added a Georgian twist to the global trend by making their base wine in a qvevri. Usually, the traditional sparkling wine would be conceived in stainless steel or wood, but here we see an innovative French-Georgian fusion technique.

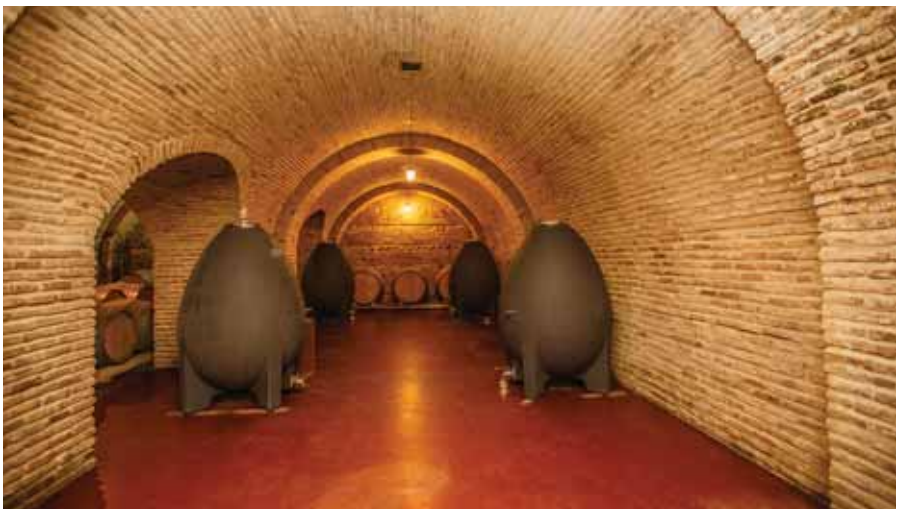
Another fresh and unorthodox practice of qvevri wine making is installing the vessels 'naked' in the cellar. Instead of resting them on the floor as has been done for centuries, winemakers are experimenting by keeping the qvevri on metal feet that keep it balanced. Barbale, Chateau Mukhrani and Igavi Wines have all implemented the new technique recently. Papari Valley, a winery famous for its underground qvevri terraces, has also set up some terracotta giants outside of the ground.

It's too early to tell if there is a dramatic difference between "airy" and "earthy" qvevris. The main goal of this novel technique is to increase micro-oxidation for certain types of wines, a change of style that also leads to a slightly different final product. One recent example is Shavkapito from Barbale. In a recent cellar tasting, this author noticed a distinguishably milder taste and aromas that opened up faster from the qvevri that had rested outside the ground compared to its traditional peer.

Source: Chateau Mukhrani

When talking about the variety of vessels, it's impossible not to mention Chateau Mukhrani. A visit there, in the company of assistant winemaker Vano Tsertsvadze, showed some truly exciting innovations: the winery is actively experimenting with a traditional trio of "stainless steel vats, barriques, and qvevris under the ground," but also with qvevris on feet, bigger barrels, and concrete eggs. As Tsertsvadze explained, the winemakers there are researching the influence of vessels on different wines, playing with blending and seeking the perfect synthesis of various techniques.

Practices like these inspire those who want to start or upgrade their winery to stand out and establish niche products on the export market. With 50 new maranis emerging annually, the market is sure to see even more interesting innovations in the years to come.



Source: Chateau Mukhrani

Daria Kholodilina is a WSET-certified Georgian wine enthusiast, wine tours curator at Trails and Wines (www.trailsandwines.com) and a supporter of small organic wineries. She shares her wine adventures on Instagram at the handle @darikomogzauri.

GALT & TAGGART
RESEARCH

Georgian wine industry entering a new era

AS GEORGIA ENTERS THE PEAK OF ANOTHER FRUITFUL GRAPE HARVEST, THE WINE INDUSTRY IS IMPLEMENTING NEW MEASURES AIMED AT IMPROVING BOTH THE QUANTITY AND QUALITY OF ITS PRODUCTS. G&T TAKES A LOOK AT RECENT DEVELOPMENTS IN THE GEORGIAN WINE BUSINESS AND EXAMINES HOW THE SECTOR MIGHT JUST DOUBLE ITS PROFITS IN FIVE YEARS.

The Georgian wine industry is at long last entering a new era, G&T writes in its recent report on the country's wine and spirit sector.

Global trends in wine consumption are guiding the Georgian market to evolve in ways industry experts have long been calling for: away from quantity and towards quality. This is because wine consumers are drinking less but better, Wine Intelligence data for 2007-2019 shows, and they are searching for low-alcohol and 'organic alternatives.' Consumers are willing to spend more per bottle as well, and attention to labelling and design have become particularly important factors in affluent markets such as the UK, US, Canada, Australia and Japan.

'Not missing a drop', G&T's report notes; the Georgian wine industry is keeping up with these trends.

To do so, Georgian companies are increasing their capital investments into product quality and improving product mix, experimenting with unique Georgian grape varieties and mixing Georgian with French and other international varieties to discover unique flavors.

Further quality stabilization will be supported by a trend of increased investments in vineyards by large wine companies, allowing for more uniform production and quality assurance, a problem that has otherwise plagued the industry for years. Kakhetian Traditional Winemaking, by far the largest private sector winemaking company by market share, is itself planning to invest nearly $52 million into its own vineyards, adding c. 3,458 hectares of vineyards to its base by 2024.

On the back of these developments, grape yield per hectare is also expected to grow, for which there is plenty of room: G&T estimates overall current yield at 5.3 tonnes per hectares, which is nearly two times lower than the 2019 world average. G&T attributes the low yield to the fact that the majority of vineyards are owned by households which employ technologically unsophisticated production methods, though it notes that Georgia's larger wineries enjoy a yield similar to global levels.

While market forces have certainly been a factor in convincing farmers to alter their production models towards quality over quantity, the National Wine Agency has also done its part: mandatory quality controls on wine destined for exports and tightened export procedures have also done much to raise the overall perception of Georgian wine abroad.

Indeed, some industry shake up is expected this rtveli [harvest season] after the NWA released new regulations stipulating grape sugar content be no lower than 18% to be eligible for use in winemaking; otherwise, grapes will be classified as suitable for the production of spirits only.

G&T Senior Analyst Tatia Mamrikishvili says that while the new regulations may cause some discomfort amongst a portion of producers, the brokerage believes the move is 'a step in the right direction, moving the price of quality grapes upwards, and incentivizing farmers to shift towards the quality over quantity paradigm.'

Numerous awards and impressive victories at international wine competitions in recent years have also helped cement Georgian wine as a brand of quality: Georgian wines took 13 gold and 1 silver medal at the 8th Sakura international competition held in Japan in 2021, while they were awarded with gold and silver medals at the International Rosé Championship held in Poland in 2020.

Wine marketing efforts have borne fruit in new target export markets as well. Since 2013, the NWA has been investing heavily to popularize Georgian wine in new strategic markets, including the US, UK, China, Poland, Japan, Germany and others. Georgian wine companies participated in more than 20 international exhibitions and 242 wine tasting events in 2019-2020.

EXPORTS

While domestic consumption more than halved during the pandemic due to the fall off in tourism, exports came to the rescue and buoyed the sector significantly to prevent serious damage.

"Wine in general is a commodity more resilient to wider price shifts", G&T's Mamrikishvili notes, citing figures that global wine exports were down just 1.7% in volume and 6.7% in YoY value in 2020.

"Local wine and spirit exports were down just 1.5% in 2020, which is a low contraction for the year. Demand from target markets such as the US, UK and the Baltic states was up, while traditional markets stayed comparably stable," Mamrikishvili adds. Wine exporters are entering new markets, the report notes, but dependency on Russia and other post-Soviet countries remains significant. Exposure to new export markets (the US, UK, China, Japan, Germany, Poland and the Baltic states) has increased in recent years, accounting for 21.5% of total exports in 1H21 in value terms, up from 10.9% in 2013. However, Russia still absorbed around 58% of Georgia's total wine exports in 2017-2020. This is a result of developed trading networks and benefits from the widespread popularity of Georgian wine in Russia, which removes additional marketing costs.

Considering the painful effects of the Russian 2006 embargo and the unpredictability of this market, G&T writes that diversification to other markets should remain a number one priority for Georgian wine companies in the medium to long term.

Overall, the brokerage's expectations on exports are positive, supported by growing investments in vineyards, government support for the sector, healthy demand from export markets and free trade agreements with the EU and China. This is good news, considering exports remain the main driver for sector revenue growth, with 82.4% of total turnover coming on average from export markets between 2012-2020.

G&T also anticipates the average

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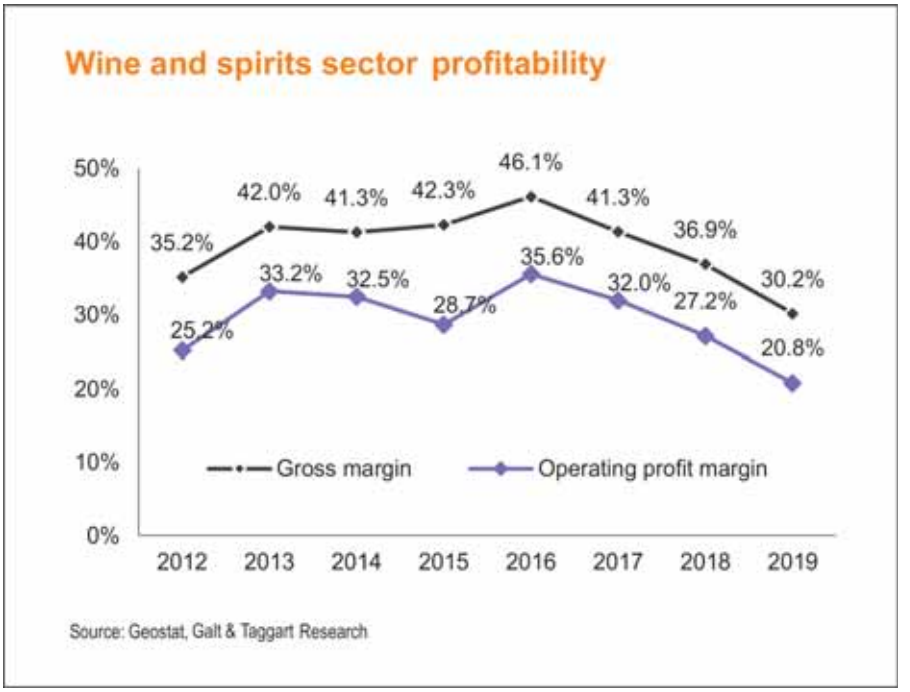
export price to increase, along with a gradual transition towards new export markets in the medium term. Considering this, G&T says wine exports are expected to almost double in the next five years to around US $350 million by 2025.

Notably, the average export price for Georgian wine is 26% higher in new target export markets (the US, UK, China, Japan, Germany etc.) than in Russia and other CIS states. Since 2013, in cooperation with the private sector, the NWA has been investing heavily to popularize Georgian wine in new strategic markets, including the US, UK, China, Poland, Japan, Germany and others. As a result, Georgian wine exports were up at a CAGR of 22% to $13.3 million to China, 19.5% to $11.3 million to Poland, 28.9% to $4.2 million to the USA, 20.9% to $2.6 million to Germany, and 26.7% to $1.3 million to the UK, from 2013-2020.



The sector has shown resilience to the COVID-19 crisis, with turnover down by just 2.1% YoY to GEL 1.1 billion in 2020 thanks to strong external demand, making up for the domestic market more than halving in 2020. G&T expects a full recovery in line with the restoration of tourism sometime in 2022.

Despite the drop in tourism, the wine and spirits business continues to be one of the most profitable sectors in Georgia, posting 30.2% gross profit and 20.8% operating profit margins in 2020, 1.4 and 1.7 times above the business sector averages, respectively.

Notably, the top 10 companies have outperformed sector performance, with weighted gross profit and EBITDA margins averaging 41.2% and 24.9%, respectively, over 2017-2020. The sector remains fragmented, but the share of large companies is increasing. Out of 625 companies operating in the sector, only seven are large, 37 medium and 581 small, with small and medium companies generating c. 59% of total revenue in 2020. However, the share of large companies increased to c. 41% of total turnover in 2020, up from 12% in 2015. G&T sees further consolidation potential which will improve the sector's financial performance.

NEXT DROPS

Wine companies should be more ambitious to grab a greater market share in new target export markets, G&T writes in its report.

Despite some success, Georgia still accounts for less than 1% of total wine imports in new target markets (excluding Poland, where Georgia holds 3%). One of the main obstacles behind low exports are high costs associated with marketing and product shelving as well as companies' fear of investment failure.

Notably, a new state co-financing program seeks to address these concerns with support for expenses associated with marketing in new target markets.

Mamrikishvili says this is indeed the way to help the country's wine industry along: "Subsidizing the sector through the direct or indirect purchase of grapes from farmers has served as a disincentive to improve quality and product. The new scheme will be more beneficial in the long-term development of the industry and will help popularize Georgian wine on new markets."

Saperavi to the rescue – why it pays to have thick skin in the era of climate change

CLIMATE CHANGE IS POSING A CHALLENGE TO VINTNERS AROUND THE GLOBE, WHO ARE EXPERIMENTING WITH THE HARDINESS OF GEORGIAN GRAPE VARIETIES TO RESPOND TO RISING TEMPERATURES AND INCREASED SUN EXPOSURE.

SALLY WHITE

There's one thing that unites us with grapes: we're both extremely prone to sunburn. Earlier just one of the many issues faced by grape farmers, climate change is now making this vulnerability a major concern in vineyards from Europe to Australia and North America. Excess sun can cause sugar content in grapes to spike and thus raise potential alcohol content when vinified.

International interest in Georgia's two main grape varieties, Rkatsiteli and Saperavi, has thus peaked in recent years. Both have developed tough skins as a result of their thousands of years of development and hard history, and they both seem relatively unfazed by the sun. They have good track records, too, on disease resistance and in the drier and less predictable weather cycles that are upsetting grape chemistry amidst climate change.

Trial growing of both Georgian varieties to test their all-round climate-change resilience – not just to the sun – is ongoing in France, Italy, Australia and the US (although a few vineyards in the two latter countries had previously discovered Saperavi's capacity to make high quality wine). Right now, though, what growers and winemakers are seeking globally are hardy varieties to help them adapt their vineyards and enable them to stay in business despite extreme weather. These new weather patterns encompass record temperatures, destructive unexpected frosts, hail storms and high winds.

And Georgia's vine pool seems to have still more to offer. While these two leading varieties grow well in the wide diversity of conditions seen across Georgia's climate zones, there is also a long list of other Georgian vines that have adapted successfully to conditions prevailing in specific locales, as detailed in the Italian-funded report Georgian Grapevine Cultivars: Ancient Biodiversity for Future Viticulture. These range, for example, from Tsolikouri in Svaneti and Imereti, to Takveri in South Kartli and Chkhaveri in Guria. Nearly 40 Georgian grape cultivars are currently recommended for wine production, but further studies are in progress to enable more to be recognised as invaluable sources of biodiversity.

Two European research programmes, GrapeGen06 and COST Action FA1003, in collaboration with a strong and active network of European-Georgian scientists, have worked on genetically characterising and preserving Georgian genetic resources of wine.

"All the outcomes about the genetic characterisation" of Georgian vines showed "uniqueness and originality of this germplasm when compared to the European and Central Asian germplasm," say Georgian Cultivars' authors. And the varieties from different regions of Georgia were not only different but maintained their originality when grown elsewhere. Since diversity is a

"major source of crop improvement and adaptation of changing environmental conditions," the report states, Georgia's vines provide an excellent "foundation for any breeding programme."

Wine companies (and oenophiles) have been reading with horror the growing pile of gloomy reports on what lies ahead as temperatures mount (France had its earliest harvest in 500 years in 2020 and Australia the hottest summer on record).

Newspaper headlines around the world have, over recent months, picked on the nub of the potential crisis: "Global heating may lead to wine shortage - rise of 2°C would cause 56% loss of vineyard land, while 4°C would wipe out 85%," "Wine regions face dramatic shrink with climate change," "Climate change threatens world wine supply," and "Goodbye Cabernet Sauvignon: How climate change will end wine as we know it."

Vitis vinifera – the common grape does best where the average temperature sits between 13°C and 21°C, but growers have been pushing the species to its limits for millennia with excellent results. Quality wines have emerged from such disparate places as North Africa, the Swiss alpine slopes, and even wet, cool England.

"The wine grape is the most valuable crop on the planet. It's also remarkably prodigious. There are at least 6,000 varieties of Vitis vinifera, with previously undocumented cultivars (varieties produced by selective breeding) being identified all the time. But despite this, only a dozen or so – mainly French – grapes make up 80% of wine on the global market, and many are simply not fit to withstand warmer, drier climates. Varieties such as Merlot, Chardonnay, Pinot and Cabernet dominate vineyards from Napa to New Zealand, despite the climatic differences and the cultivars' French ancestry. But these grapes were never meant to be grown everywhere," comments US science and technology magazine Wired.

While scientists have been drawing attention to these looming problems for some time, it is only in the last couple of years that crises in the vineyards have driven growers en masse to wake up to their warnings. Work published as far back as 2000 by Professor Hans Reiner Schultz, a viticulture scientist at Germany's Geisenheim University with experience advising winegrowers across four continents, had contradicted the formerly prevailing belief that a hotter, drier climate always makes better wine. He pointed out that "elevated levels of ultraviolet B rays are transforming grape composition" and "upsetting the metabolites responsible for giving grapes their flavour."

In the French wine region of Bordeaux, which makes $4 billion in annual wine sales, hotter and longer summers were at first welcomed with vintage after vintage producing fabulous wines. "But then 2017 happened. A freak late-April frost devastated the crop, and production in Bordeaux crashed by 295 million bottles," describes Wired. This destroyed 40% of the crop, with the worst hit variety being the sensitive Merlot.

Most widely read of all the vine and climate change-related research papers has been one published in the online journal Nature Climate Change from Dr. Elizabeth Wolkovich, an ecologist at the University of British Columbia, who wrote a report with colleagues as far back as ten years ago to describe how climate change posed serious challenges for wine growers. Recent record high temperatures across the world, plus the soaring incidence of fires in vineyard regions, are now bringing this issue into focus. As she notes in the paper: "With continued warming, it may be hard to continue growing grapes in some regions."

She continued: "Wine producers' increasing reliance on a few major varieties translates into a global market that is investing in an increasingly limited portfolio at exactly the time when a large diversity of varieties is most needed. This narrow focus means a narrower range of critical traits related to climate, which in turn reduces the flexibility of most vineyards to adapt to climate change."

Through research on European vineyards, she and her colleagues found that harvest time there was now coming two to three weeks earlier than during the 1980s. Every stage of the vine growth cycle has been shifting, from budburst to ripening, opening vineyards to vulner- ▸▸

abilities like frost and drought. These conditions trickle down into taste, aroma, alcohol content and general wine quality.

That paper re-opened a debate that has been growing in the wine world for the past decade, expanding on the idea that a great redrawing of wine maps was needed. Wolkovich says attention should be paid to the many regional varieties that have been pushed into obscurity by global wine trends. Yet, while diversification is seen as the only long-term solution, even this "will save only 42% if temperatures rise as much as four degrees," according to Ignacio Morales-Castilla at Spain's University of Alcala.

One vineyard exploring new vine varieties and possible diversification, sited at the University of Bordeaux's Science Institute of Vine and Wine Bordeaux Sciences Agro project, VitApt, has over 50 different vines in its vineyard. The professor in charge, Cornelis van Leeuwen, told Wired: "We are just going back to the common sense that people have used for ages, and in many cases have forgotten as growers jumped on the Cabernet-Pinot-Merlot-Chardonnay bandwagon." Common sense, he said, was understanding the differences between later and earlier ripening varieties. The ones found in their trials to be most at risk from warmer, drier climates were early ripening ones, including the top European favourites of Pinot Noir, Chardonnay and Sauvignon Blanc.

Now that each season seems to bring weather that used to cause once-in-a-generation disasters, science and new tech are being called on to help care for vines and to maintain the necessary acid and sugar balance of the grapes. While diversification is constantly referred to as a solution, in tightly regulated countries such as France, bringing in non-traditional foreign or even local grape varieties is frowned upon (particularly by France's Institut National de l'Origine de la Qualite), so there is pressure to change the rules. There is also the problem of introducing consumers to new grape varieties.

Researchers in Wolkovich's team foresee late ripening varieties such as Syrah, Grenache and Mourvedre becoming more widespread in Europe and the Pacific Northwest. Most of the classics in Napa Valley and Sonoma, including Cabernet Sauvignon, Pinot and Merlot, would be all right with a two degree rise in temperature, they believed, but in South Africa they would be lost. Vineyards in hot countries such as Italy and Spain would suffer the most. While growers may move vines to higher or north-facing locations to avoid the worst of the sun, the problem is then the colder night-time temperatures and a high location brings with it different levels of precipitation.

Wolkovich acknowledged that a growers' life will be far from easy: "For regions where our results suggest that cultivar diversity may be most critical, growers must choose to actively shift varieties—which requires overcoming legal and cultural hurdles. Currently, traditional practices, alongside regulations at local, regional, and higher levels, limit how much and where growers can shift varieties easily. This, coupled with other considerations, such as the temporal and related financial cost of replanting or regrafting a vineyard, may lead many growers to prefer alternative options that keep a particular variety tied to a region. For example, local management practices to reduce microclimatic temperatures or adjust the pace of development (e.g., shade cloth, reduced leaf area to fruit weight ratio, or longer-cycle rootstocks) may help some growers but generally work best for lower amounts of warming, especially compared to changing varieties."

Among those seeing Saperavi vines as a solution is one major vineyard in Italy, where the climate is becoming more tropical. Castello Banfi in Tuscany told UK magazine Drinks Business that Saperavi was part of its search for grapes that are "resistant to botrytis, thick skinned and lower flowering," which "makes them more durable and able to thrive in Tuscany without being sprayed with artificial chemicals and can weather the region's intensifying heat and sunlight over the next few decades." Trials are being carried out and once the grapes ripen, they are vinified in small batches so the end result can be assessed by researchers.

Various reasons have been put forward for the resilience of Georgian vines, and their relative mildew, fungus, disease and climate resistance compared to commonly planted European varieties. The Italian-Georgian team that researched Georgian Grapevine Cultivars: Ancient Biodiversity for Future Viticulture. (This was funded by the University of Milan and the National Wine Agency of Georgia as part of ongoing research to help Georgian farmers and build the status of Georgian wines.) credit the long history of development: in the South Caucasus it was 8,000 years ago that humans "started with the conscious or unconscious selection of desirable phenotypical traits." There have also been the benefits of bi-directional gene flow between wild and cultivated vines, "a relatively recent event occurring over the last few hundred years [that] led to the birth of so-called anthropic crosses, with the aim of satisfying specific requirements." It has helped, too, that research in Soviet times focused on developing Saperavi and Rkatsiteli for vineyards across all of Georgia's climate zones.

The report states that Georgia's

"geographical features strongly characterize the climate of its 12 wine-growing regions with "profoundly different conditions ranging from hot continental summer to warm summer continental." There is "high variability in the plant phenology among Georgian cultivars, both in sprouting date and in the ripening period…" with a large degree of adaptability: "a delayed budburst perhaps representing an avoidance mechanism against spring frosts." Usefully, the Georgian varieties have been found "not to change their characteristics when grown internationally."

In Europe more work is being carried out to help solve some of the wine growers' problems, and recently €3.4 billion was allocated by the EU from its environment budget to help build software models to show the impact of climate change globally at vineyard level. The New Zealand-based project director, Herve Quenol, told the trade magazine Wine Business International that data on how climate change was affecting vines was being combined with regional climate change studies. Their aim is to build software models to enable vintners to make informed choices on what to plant and how to manage their vineyards.

In Australia's Queensland wine-growing region, Sirromet Wines' chief winemaker and viticulture director, Mike Hayes, is among those who have been introducing Saperavi as the country struggles with months of droughts. "Many regions are now dabbling in emerging varieties for climate change and we will see a huge increase in their plantings," he told the Sydney Morning Herald.

"If we don't become new farmers, we will perish. The industry has to change. It's quite a controversial issue, but deep down, most in the industry know it's accurate."

As Wired comments: "The wine industry has faced crises before, and it has adapted." It is this history, more than anything else, that gives scientists such as Van Leeuwen "reason for hope."

In the 19th century, he points out, "the Phylloxera aphid, that feeds on the roots and leaves of most kinds of Vitis vinifera grapes, devastated much of the European, and particularly French, wine industry. The sector eventually rebounded, but only after a global network of botanists and growers joined forces to counter the threat." The multi-national trials with Georgian vines are striving to repeat history.

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Small donations, big changes: USAID supports crowdfunding to boost civic initiatives

USAID/GEORGIA

Want to organize a rock climbing club as an after school activity for orphaned children? Or build a playground for local kids? As part of its emphasis on spurring civic action in Georgia's communities, the United States Agency for International Development (USAID) is partnering with Orbeliani Meti to help local movements raise the money they need to make big changes. By matching 50% of the funds raised through private donations, USAID is putting resources into the projects that matter most to the Georgian people.

Rock climbing has been a crucial part of Lazare Komakhidze's life since childhood. Lazare grew up in Dzegvi, a small village in Mtskheta Municipality. He recalls his childhood as being relatively aimless. That is, until someone came from outside the village to establish a rock climbing club. Lazare joined the club and developed a hobby and a purpose for the first time.

Fast forward a few years, and Lazare is now a professional climber. He is also devoted to giving back to the community. The son of a social worker employed at the local orphanage, he grew up with a keen understanding of the lack of opportunity that many children face. "These children are forgotten by society," says Lazare. "They have nothing."

He set up a rock climbing club in the village of Nigozi, where most of the members are orphaned. Finding money to build a climbing wall was not easy. Then, he found out about Orbeliani Meti, an online crowdfunding platform where the money raised by local contributors is matched by international donors, including USAID.

"We felt that everybody should be able to take action, to do something good, whatever they feel is important for their community," says Ketevan Khachidze, program director at Orbeliani. The organization has operated since 2014, helping people get the funding they need to turn good ideas into positive action. Orbeliani has set out to "revolutionize" aid by changing how people obtain the resources to improve their communities. They launched their crowdfunding platform, Orbeliani Meti, in July 2020.

HOW USAID AND ORBELIANI SUPPORT CIVIC INITIATIVES

The platform follows a simple model: anyone who wants to make their community thrive can submit an idea. Once they are listed on the platform, it's up to them to raise the funds they need.

USAID, through its flagship civil society capacity building program, is also doing its part, matching 50% of the funding raised by selected projects. USAID has already supported nearly 20 projects this way, with activities ranging from equipping a media center at a public school in Gori to planting trees to improve air quality in Rustavi.

The extra funding from international donor organizations has made a big difference, and not only in material terms. According to Khachidze, project initiators receive extra motivation when they know that donors like USAID are taking an interest in their initiatives.

Once a project is registered on the platform, Orbeliani staff provide the initiators with training on fundraising, outreach, and media relations. The goal is to help them attract private donations, while gaining the skills needed to implement successful civic projects in the future.

CROWDFUNDING PROVIDES A MODEL FOR COMMUNITY ENGAGEMENT

High in the mountains of Adjara, in the village of Pachkha in Khulo Municipality, Asmat Bolkvadze and her team of volunteers are working tirelessly to support the local community. They have led a number of projects, including collecting donations to deliver supplies to people most at risk during the COVID-19 pandemic. Their most ambitious, and successful, project to date may have been raising funds for a new playground with the support of Orbeliani and USAID. Asmat is especially proud of this initiative not only because it resulted in a new playground, but because so many members of the community helped make it possible.

"It's been incredibly rewarding to see that everyone cares, and everyone who chipped in a little bit of money, also started really caring about the project," says Asmat. Not only did people donate money, but many more members of the community joined her civic movement. In Asmat's view, the project helped make the community stronger and more resilient.

Academic research has identified this as something that sets crowdfunding apart from other means of financing public projects: "An element differentiating crowdfunding from traditional finance is the possibility for building a relationship with a large number of people," finds a study by Melina Moleskisl and Ines Alegre. The authors mention that crowdfunding "can help to generate awareness of the cause, more favourable word of mouth advertising, and even trust."

When implemented effectively, these campaigns can also point the government toward issues that matter to local citizens. Because crowdfunding is by definition a "democratic" undertaking - citizens are putting their money toward the issues that matter to them - the public sector has an interest in supporting those same projects.

In the case of Lazare's rock climbing club, Georgia's Ministry of Sport and Youth Affairs pitched in roughly GEL 10,000 for the project after staff members learned about it through the media. "The additional funds were not only extremely important in speeding up the project, but it also felt as a confirmation that what we're doing is important," said Lazare.

What can be done about Georgia's household debt problem

DESPITE THE FACT THAT MORE THAN HALF OF GEORGIA'S POPULATION REPORTS BEING INDEBTED, SOCIAL STIGMA HAS STIFLED A PUBLIC DISCUSSION OF HOW TO ADDRESS THE ISSUE. RECENT EFFORTS BY THE NBG TO REGULATE HOUSEHOLD DEBT ARE A GOOD START, BUT THE COUNTRY STILL HAS A LONG WAY TO GO.

MACKENZIE BALDINGER

As COVID-19 decimated the tourism industry in 2020 and pushed the unemployment rate to almost 20%, another less talked about pandemic wreaked havoc on Georgian households – debt. In an effort to ease the burden on those affected, major banks agreed to a brief moratorium on loan payments at the beginning of the crisis. However, accruing interest and exorbitant monthly payments highlighted the vulnerability of many Georgians in relation to their personal debt.

According to the National Bank of Georgia, in 2018 there were 5.6 million active loans and 2.1 million borrowers in a country of approximately 3 million adults. Data from the National Democratic Institute indicates that over 50% of Georgian households are currently indebted – many of them with multiple loans.

Household debt by itself is not problematic; on the contrary, it has fueled the country's economic growth and allows consumers to purchase large items like houses and cars. However, the rate at which consumer debt is increasing, coupled with low financial literacy and little regulation, has created a burden on the population that is no longer tenable.

Many forms of consumer credit, like mortgages and student loans, first became widely available in Georgia in 2007. From 2007 to 2008, the volume of loans issued increased by 97.5%, signaling the Georgian public's high demand for credit. Since their introduction, the volume of personal loans taken by Georgians have continued to increase significantly, multiplying 7.5 times in the last decade.

In 2007, the household debt to GDP ratio was just under 6%. By 2020, that figure had risen to 41.9%. While a rising household debt to GDP ratio in a developing economy is par for the course, Georgia's level of debt is rising faster than its GDP is growing.

This trend is especially concerning considering the effect consumer debt has on a country's long term growth. Research done by the IMF shows that a drastic increase in household debt can decrease a country's economic growth in the long run. It can also cause higher unemployment and increase the probability of a banking crisis.

In addition to alarm about the rate at which debt is growing in Georgia is the

concern about how much of a burden it is becoming on the population. UNICEF reports that 17% of all households note 'crushing debt' as the main problem they face, and a recent survey done by the National Democratic Institute shows that 30% of Georgians rank paying off debts among their highest household expenses. Furthermore, in 2017, the National Bank of Georgia estimated that approximately 700,000 Georgians were behind on their loan payments.

DE-REGULATION AND SOCIAL STIGMA

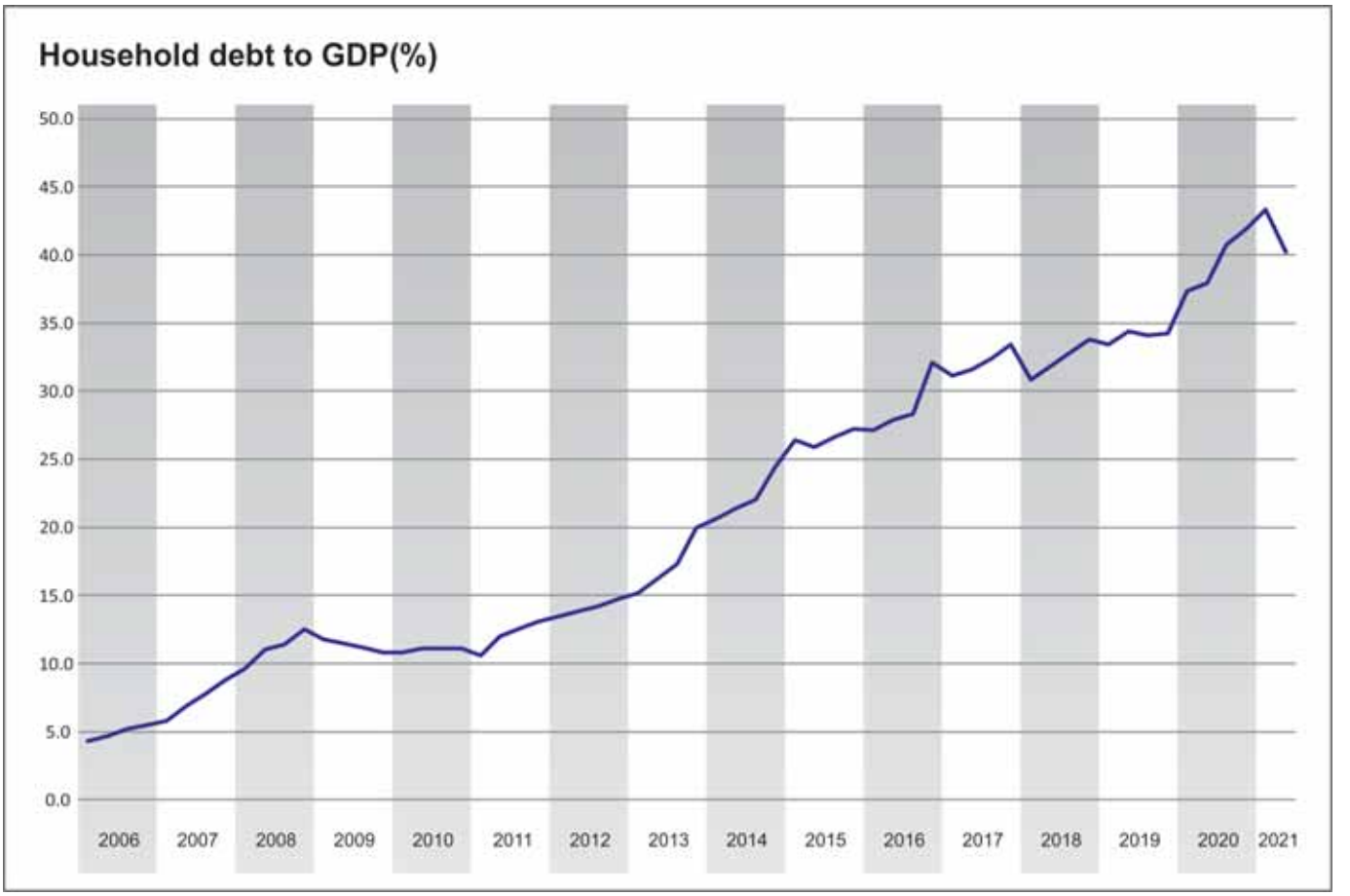
Georgia's current debt crisis can be traced back to regulatory changes instituted after the Rose Revolution of 2003. From the country's independence in 1990 until 2007, legislation and court precedent limited interest rates on loans to 'reasonably correspond' with the rates provided by the National Bank. Generally, these rates ranged between 2.4 and 3% monthly.

In 2007, the United National Movement government instituted a massive campaign of de-regulation; the resulting changes to the civil code instituted a principle of 'contractual freedom,' meaning that any interest rate that the lender and borrower agreed upon could be charged. Interest rates well over 100% became common practice in the following years. Economic instability, easy access to loans, and low levels of financial literacy meant that many continued to borrow despite the fact that they could not afford the monthly payments.

The burden of debt and inability of many to repay loans has been further complicated by the stigma around the topic. Eva Fernández-Martín, who led the People in Need project 'Tackling Indebtedness in Georgia through Czech Innovations,' notes that social stigma surrounding debt is "minimizing the public conversation in Georgia, which makes it harder to grasp the real impact of debt."

NEW LIMITS ON LOANS

In an effort to decrease the vulnerability of the financial sector, the National Bank of Georgia introduced new regulations in 2018 to limit the availability of credit. These regulations included newly required income and credit checks as well as the introduction of a national registry of loans. The NBG also capped the effective interest rate for banks at 50% and instituted payment-to-income (PTI) and loan-to-value (LTV) requirements to limit the amount of credit borrowers could access relative to their income and assets. One key aspect of the new regulation was a constraint ▸▸

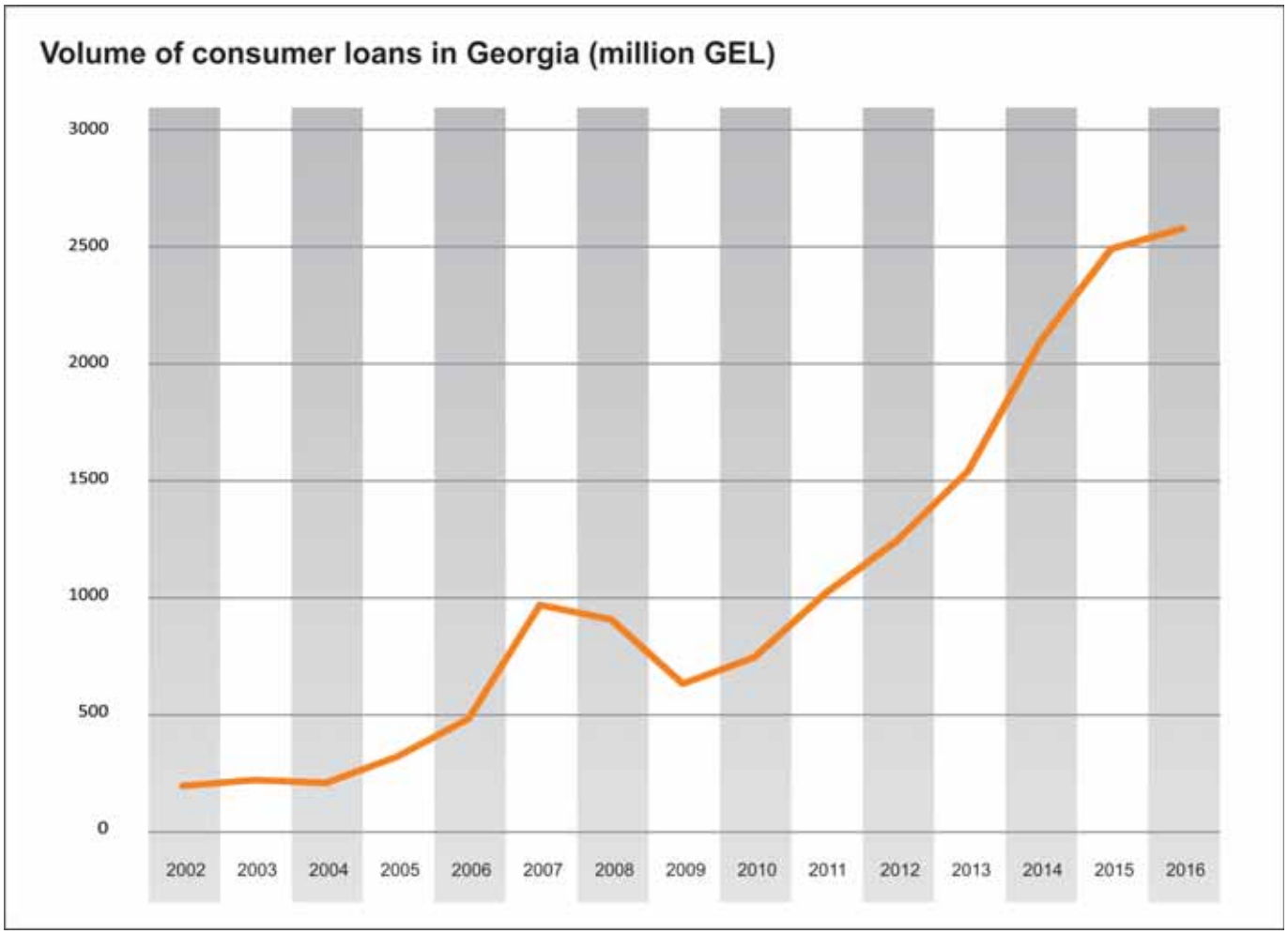


on the ability of lenders to offer foreign currency loans, a practice that had become commonplace and left borrowers exposed to the exchange rate volatility of the Georgian lari.

This effort to increase the 'larization' of loans seemed to be a positive step in combating the crisis in Georgia. However, the National Bank of Georgia cautioned in a 2019 report that introducing credit limits only decreased the supply of loans available and did little to satiate the continued high demand for credit among the population. In fact, critics expressed concern that a deficiency of formal credit for many borrowers of excessive debt, who are characterized by a willingness to "accept credit with any conditions," could lead to a return to more informal types of shadow borrowing.

REGULATE OR EDUCATE? NEXT STEPS IN GEORGIA'S FIGHT AGAINST DEBT

As analysts at the NBG have noted, Georgia's debt problem requires more than just a restriction of access to credit. For many Georgians, debt has become a way of surviving everyday life. Ac-



cording to Mikheil Svanidze, an analyst who has looked into the issue of household debt in Georgia, education alone is also not enough to remedy this issue: "it is a bit patronizing to tell someone that cannot afford to pay for their food or medicine that understanding their loan better is the key to solving their problem."

Instead, Svanidze recommends a combination of both education and regulation, noting that "regulation is the most important part of solving this crisis." Svanidze's recent study on consumer debt in Georgia provided a list of recommendations, including the introduction of a financial ombudsman to "defend the interests of the debtors...with legal and financial advice," as well as personal bankruptcy laws and a consumer protection law, none of which the country currently has.

In the past, low levels of political will towards debt regulation have prevented draft legislation from passing; however, Georgia's association agreement obliges the country to "approximate its consumer legislation" with EU law. Svanidze's study notes that "While many regulations in the draft law [initiated by previous parliaments] are already in the NBG regulatory system, an overarching legal framework would help cement the structure of protection and reduce the information deficit for customers."

For the growing number of Georgians who are already trapped in a crushing debt cycle, Svanidze suggests parliament should cooperate "with interest groups and experts to continue its work on insolvency that started in 2017." Georgia did pass comprehensive insolvency reform for businesses in 2020; however, no such relief exists yet for individuals.

People in Need, with the support of UNDP and the Czech Ministry of Foreign Affairs, has also worked to raise awareness on the issue and provide financial tools to citizens. The organization released a debt advisory guide this year and provided training to local action groups in various regions of the country. Fernández-Martín, the project's manager, notes that "in order to combat indebtedness, it is essential to enhance consumer protection rights and ensure borrowers have the knowledge and resources to protect their rights."

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ISET-PI: is there an end in sight to food price inflation?

SALOME DEISADZE AND
ELENE SETURIDZE FOR ISET-PI

In the past year and a half since the pandemic began, we've all become familiar with phrases such as "supply chain disruption," "turbulence and volatility in international markets," and "in these unprecedented times," often used to preface news about pandemic-related food price increases across the globe.

Georgia has not been isolated from the trend, and consumers have seen drastic food price inflation. Food producers and suppliers in Georgia have struggled with disruptions in transportation and shortages in the labor force, both of which have caused food prices to rise.

Now, eighteen months into the pandemic, food prices in Georgia are far from stabilizing. Is there an end in sight to inflation?

A SNAPSHOT OF INFLATION FROM THE BEGINNING OF THE PANDEMIC

Since February 2020, when the first case of COVID-19 was recorded in Georgia, YoY monthly prices for food and non-alcoholic beverages have increased on average by 9.3%.

Annual prices increased for almost every major food commodity in 2020, as did the share of expenditure on food in total household consumption expenditure, from 43% in 2019 to 47.4% in 2020, according to GeoStat.

In August 2021, prices for food and non-alcoholic beverages, as measured by the Food Price Index (FPI), drastically increased by 16.2% compared to August 2020, hitting its highest rate since July 2011.

GeoStat's analysis shows that prices increased for all sub-categories of food and non-alcoholic beverages in August 2021: oils and fats (+43.9%); vegetables (+42.2%); milk, cheese and eggs (+17.3%); sugar, jam, honey, chocolate and confectionery (+16.9%); bread and cereals (+13%); fish (+11.9%); mineral waters, soft drinks, fruit and vegetable juices (+11.5%); meat (+8.3%); coffee, tea and cocoa (+6.8%); fruit and grapes (+5.4%).

WHAT'S DRIVING UP PRICES?

Georgia is a net importer of food commodities and the share of imported food in the consumption basket is high – around 80% of the food products consumed in Georgia.

In 2020, the self-sufficiency ratio for wheat was 15%, for meat 49%, for vegetables 63%, and for poultry 34%, according to GeoStat. High dependency on food imports makes food prices in Georgia more vulnerable to fluctuations in the exchange rate and international prices.

Dynamics of the exchange rate: the main driver of food price increases in the last couple of years was the depreciation of the Georgian lari against the US dollar.

In 2020, the Georgian lari depreciated against the US dollar by 10.3% from 2.82 to 3.11 GEL/USD compared to 2019. The depreciation of the Georgian lari put upward pressure on prices of imported food products and inputs, including chemicals and fertilizers, fuel, and milk powder.

Figure 2 shows the dynamics of the food price index and the monthly average US dollar to Georgian lari exchange rate.It is evident that the exchange rate is strongly setting the pace for food price inflation.

Trends in the international markets: Given Georgia's high dependency on food imports, global agricultural commodity markets have a great impact on domestic prices of food products.

The Food and Agriculture Organization (FAO) food price index shows that global food prices have been on the rise throughout 2020 and 2021, reflecting increased import demand in anticipation of a tightening in export availability from main exporter countries due to declined production (e.g., cereal, vegetable oil, sugar, meat, dairy).

Though trends on the international markets generally need time to be transmitted to local markets, due to certain circumstances the upward trend of hikes in food prices were transmitted faster than usual onto local prices. For instance, price increases and export restrictions due to

Figure 1: Annual Food Price Inflation (January 2010-August 2021) Source: GeoStat, 2021

expectations of unfavorable weather conditions and reduced production on the Russian market, which serves as Georgia's main import partner of wheat and sunflower oil, have contributed to the spike in Georgian prices for these particular products.

Even though 2020 was a good year for Georgian agriculture in terms of harvest yield, these positive trends in production were not enough to balance the effects of the exchange rate and COVID-19-related trade restrictions on food prices.

The political and economic situations related to the parliamentary elections in October 2020 in Georgia, as well as a slow vaccination rate, have increased uncertainty in the country and hit expectations as well, further increasing pressure on the exchange rate and thus on prices.

WILL PRICES COME BACK DOWN?

To examine upcoming trends for food prices in Georgia, let's review some of the key factors that affect local prices and form expectations for the upcoming months.

As already mentioned, trends on international markets need time to be transmitted to local markets.

With this in mind, as the FAO food price index has continued to increase on a YoY monthly basis from the beginning of 2021, local food prices may mimic the trend and continue to rise. However, the lengths of transmission differ by commodity.

For example, research done by ISET-PI's team suggests that a price change on the international market for wheat generally takes about seven months to be reflected in local prices. Therefore, while one can still expect an increase in international prices, the transmission period should allow the government of Georgia to adjust to those changes and plan its interventions accordingly.

The National Bank of Georgia's (NBG) interventions may put downward pressure on inflation including food prices in the medium-term.

To steer the country's inflation rate back to a short-term target of 6%, as set by the NBG, the central bank has further tightened the refinancing rate over the spring and summer. In August 2020 the refinancing rate was at 8%. It was first increased in March 2021 by 0.5 percentage points, then by 1 percentage point in April; a final increase took place in August, when the rate was raised from 9.5 to 10%. This is the highest value of the indicator seen in the last ten years. As the change in refinancing rate requires some time (approximately six months) to have an impact, prices are expected to go down in the next months.

Elevated fuel and oil prices may further contribute to inflationary pressure. Recent increases in fuel oil prices may increase transportation costs and therefore affect food prices.

Since February 2021, annual prices in the category of transport have increased by 15% on average each month, hitting the highest rate of 22.5% in August 2021. Fuel prices not only increase the costs of transporting food from farm to table, but it also affects farming as well: oil byproducts are a significant component of fertilizers. The recent hike in oil prices will also be edging up food prices in Georgia.

Despite the stabilization of the Georgian lari exchange rate, the average GEL/USD exchange rate is still higher than before the pandemic. In June 2021, the Georgian lari started to appreciate relative to the USD, from the average GEL/USD exchange rate of 3.38 in May 2021 to 3.16 in June 2021. However, the average GEL/USD exchange rate is still higher (3.11 in August 2021) than it was before the pandemic (2.85 in February 2020). The exchange rate is still negatively affecting the prices of imported food commodities.

In addition to these factors, the elections of local self-governments are around the corner, which is usually linked to high government spending. An expansionary fiscal policy might create inflationary expectations in a country. Finally, according to the NBG forecast, the level of inflation should peak in the third quarter of 2021 and go slightly down by the fourth quarter, but it will remain around 10%. Inflationary expectations may also affect food prices. In addition, harvest yield and agricultural production will influence local food prices.

It looks like households are in for an extended rough patch as prices will continue to grow across key food commodities in the upcoming months. Poorer households, in particular, may have an even more difficult time as the holiday season approaches and prices rise. This could cause further strain on household budgets, which are already largely allocated for food purchases.

Some relief may be provided by subsidized farm inputs (fertilizers, pesticides, diesel, animal feed, etc.) to reduce the costs of production for farmers. Farming season in Georgia is already over, but this option is still valid for farmers with greenhouses and animal production. Furthermore, additional state support programs could mitigate disruptions and delays in food supply chains and logistics to avoid a further increase in food prices. A longer-term policy should consider not only an increase in domestic production of key food commodities but also a diversification of import markets to ensure low volatility in food supply and prices.

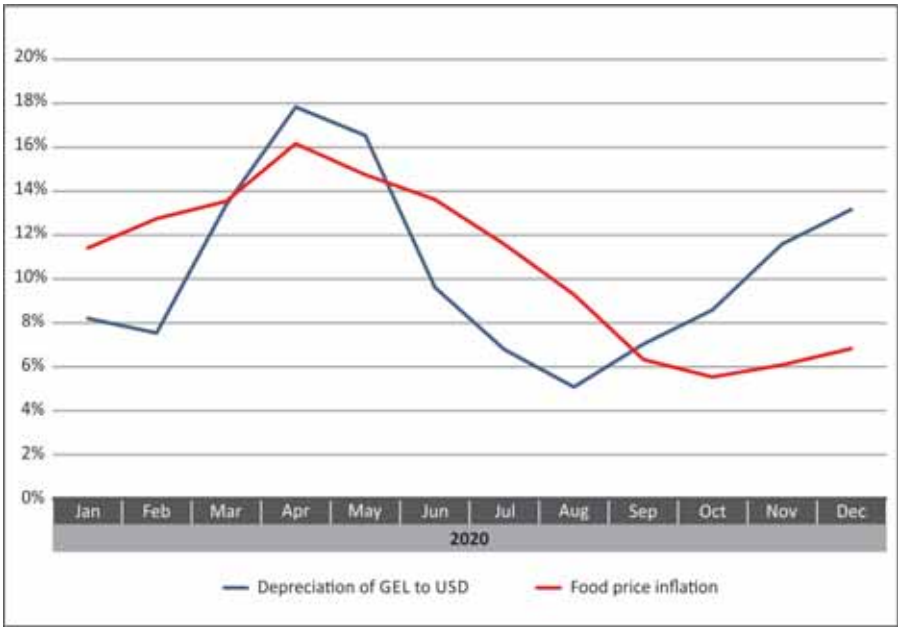

Figure 2: Dynamics of FPI and USD to GEL monthly average exchange rate

The new kind of Georgian lari you've never had in your bank, phone or pocket

ANI MEZVRISHVILI

If your leisurely beachside reading this summer included news from the riveting world of central banking, you might very justifiably think the death of cash is nigh. Central banks around the world are diving down the blockchain-crypto rabbithole to catch up with the industry after years of nay-saying, tacitly admitting the future of money may just be on the blockchain.

China, the Bahamas and Sweden have already begun piloting central bank digital currencies (CBDC), while US Fed Chair Jay Powell announced over the summer that a digital dollar is 'a top priority' for the bank. The EU has also started formal research into a digital euro, and 80% of central banks worldwide are engaged in CBDC research, according to a recent survey by the Bank of International Settlements. Georgia even preceded the flurry of announcements with its own news in May that the National Bank of Georgia is working on a 'digital lari.'

The reaction to the news has been tepid, with the media and public alike unsure of what to make of the endeavour. Afterall, you might say, 'I've had digital lari since I've had online banking…'

WHAT IS DIGITAL CURRENCY?

Well, not exactly. Central banks currently only offer one direct form of money available to the general public – physical cash.

The money accessible in a mobile banking app is a type of private money secured by the commercial bank where it is kept. Central banks support and acknowledge this commercial bank money, which is why you can easily turn it into cash with a simple ATM withdrawal.

However, CBDCs represent a new type of money, directly linked between the central bank and the public that can be used for digital payments – essentially, a digital form of cash.

Like its paper colleague, the digital lari will be be a fiat currency, issued only by the National Bank of Georgia. Unlike cryptocurrencies, the value of which is often supported by proof of stake or proof of work concepts, a digital GEL will be controlled solely by the NBG, and offered at a 1:1 rate with its cash counterpart.

The National Bank of Georgia is still deciding on the exact structure of the digital currency, but it is strongly considering the use of blockchain technology, given its security and flexibility in programming.

GAINS FOR CONSUMERS AND THE STATE

One of the primary purposes of introducing a CBDC is to create a quicker, more flexible and cashless settlement tool.

For everyday users, this will allow for the instant transfer of funds through a secure, national bank-backed platform, which may lower costs for consumers and businesses alike: cashless payments currently go through an intermediary, in most cases a bank, which takes a service commission. Be it paying for utilities, fines, or sulguni at the market, all cashless transactions have a commission. Georgian Fintech Association Chair David Kikvidze claims transfers in digital lari could save the economy "about 600-700 million GEL per year in service commissions. [And this extra amount freed up in public expenditure] could have a considerable effect on the consumer market," Kikvidze says.

For an emerging market like Georgia's, digital currency could promote financial inclusion and serve the 'underbanked,' or those living in areas where accessing commercial bank services is difficult. A currency linked directly to the central bank could ease the process through which social programs are distributed, lowering costs for the government and alleviating the burden some pensioners face when collecting their money at a brick and mortar bank. Adopting a digital lari could also make sending remittances easier, which accounted for 13.3% of Georgia's GDP in 2020.

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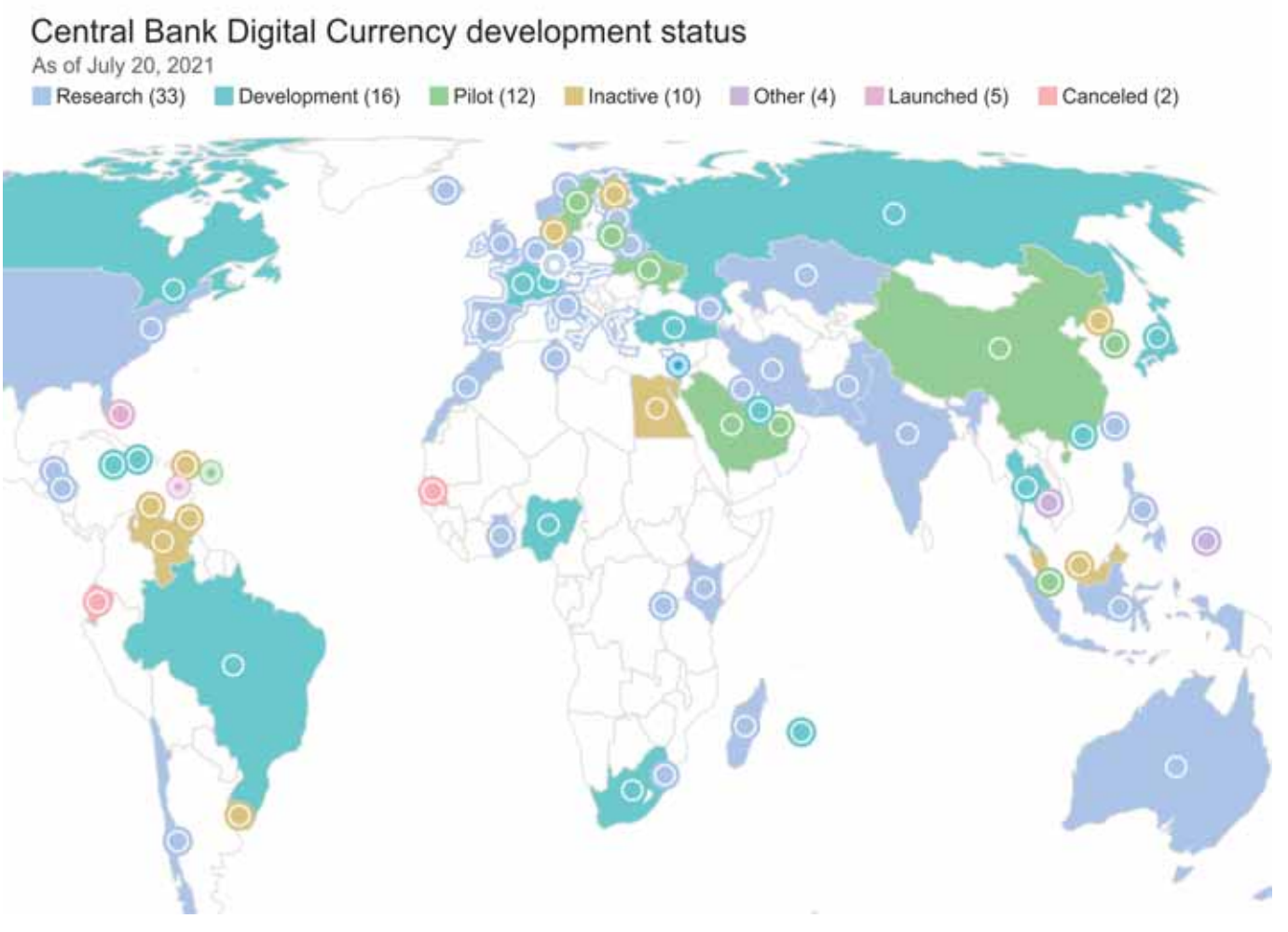
The NBG has even more to gain. Local currency loss of market transaction share through displacement by cryptocurrencies is one major concern that has central banks pursuing CDBCs. Rector at the Neuron Academy for Artificial Intelligence and researcher Levan Bodzashvili told Investor.ge that the NBG's decision to pursue a CBDC is especially understandable given the country's somewhat trying experience with runaway crypto-mining in the mid-2010s and the fact that its breakaway, Russian-occupied region of Abkhazia has now effectively become a playground for cryptomagnates.

"Cryptocurrency has decentralized financial resources in a number of states. A state's financial power is concentrated in its national bank which establishes the rules of the game, and the quick development of cryptocurrency could result in a state losing influence in this sphere. In order to stop this process somehow and wrest back the reins of financial control, central banks are looking at issuing digital currencies," Bodzashvili explains.

Prodding consumers to pay more often with electronic means and by ensuring that cashless transactions remain within the realm of a centralized system could further clamp down on the shadow economy, the share of which in the total economy may be higher than 50%, an IMF Working Paper in 2018 estimated. For the NBG, the cost of not implementing a CBDC could even prove detrimental to its monetary policy. The advent of easy-to-use digital euros and dollars with no Georgian equivalent could lead to a 'digital dollarization,' wherein the population would favor the use of digital foreign currencies and the central bank's control would slip.

Head of the NBG's Financial and Supervisory Technologies Development deparment Otar Gorgodze says that this fear of being eclipsed by competing digital currencies has been a large motivating factor for many central banks. Touching on Facebook's announcement in 2019 that it intended to develop its own blockchain-based payment system, he notes "That's probably why there



was a big outcry when Libra [Ed. now Diem] was announced. It was suddenly recognized that it will be more global than any of the central banks' currencies. And if it's better and more efficient, then that would be it."

BUT WHAT ABOUT THE BANKS?

One stakeholder that has expressed its take on CBDCs with less than fervent enthusiasm is the banking sector, which stands to lose market share as the traditional transaction intermediary.

President of the Banking Association of Georgia Alexandre Dzneladze says that in discussing the supposed benefits to be brought into the economy by a CBDC, "it is important for everyone's interests in the process to be protected." Dzneladze further told Investor.ge that it 'would not be reasonable' to fully replace bank transactions with digital lari, as this would inflict losses on commercial banks.

"We see a risk of certain commercial operations generally performed by the population with the help of banks going over to the digital lari, which is why it is important for us to know what preconditioned the adoption of a digital lari, as well as to talk about and review the details of what awaits commercial banks if it becomes possible to conduct financial transactions by bypassing them," Dzneladze told Investor.ge.

In response, the National Bank says that their goal is not to weaken banks: they see digital lari not as a competitor to electronic bank transactions but as a more modern alternative to cash. While the NBG's Gorgodze notes that their CBDC does hope to lighten some of the financial burden that small businesses face with commission fees, he is also insistent that this new form of currency will not be possible without the assistance of the private sector and commercial banks:

"The digital lari will not replace banking services or the need for an intermediary. Besides, the digital lari can become a new possibility for banks and financial companies to offer new products to consumers. The private sector will be able to provide onboarding services to the system, wallets, license providers, maybe even a payment service provider. The CBDC will simply be a core infrastructure open for financial firms to innovate and build new financial solutions for its customers. We have decided to go with a private-public partnership model for this endeavor as much as possible."

Another issue that has worried banks has been that of savings, and whether consumers will be tempted to keep their money in the NBG's digital account as opposed to in commercial banks.

"For this, we will have a direct limit on wallets, how much you can hold in them. In Europe, they're considering limiting it to around 50,000 euros. Here, we will consider an amount that the average Georgian needs for transactions... the digital lari won't be for saving," says Gorgodze.

Yet others ask the question: to what extent will the National Bank of Georgia and other state agencies have access to information about consumer transactions?

As concerns day-to-day transactions, Gorgodze says, "We're thinking about a setup that is very much like banks. In this network, which is operated by the central bank or somebody they trust, there is no personal information tied to transactions themselves. You're not visible on this network, only your bank knows that this is your account and you're transacting."

In other cases concerning financial crimes such as money laundering, or in cases where transactions may be tied to terrorism, Gorgodze says that the state will have to go through a legal process to receive access to detailed information.

The National Bank of Georgia has invited financial institutions as well as technological and fintech companies to participate in the development of the digital currency, hoping to eliminate regulatory, financial, and technological problems through joint cooperation.

The USAID Economic Security Program has been offering technical assistance to the NBG, advising on functionalities of CBDCs and helping to build solid linkages with major fintech players who can provide valuable inputs for the development of the CBDC project.

Program lead George Darchia explains that "our role is to provide technical advice and explain to major players like fintech, financial institutions, e-commerce and other vendors what the digital lari is, to make sure they understand it and [can] make a decision as to whether they want to utilize it or not."

In addition to clarifying the national bank's intentions, Darchia's team will serve in an advisory role for both the NBG and "private sector representatives who at the second stage will be even more involved in the consultative process to define what are the best functionalities and most appropriate shapes of CBDC for Georgia."

Through active communication and consultation with major market players, Darchia is confident that the process will be inclusive enough to reflect views of the private sector actors significantly.

The exact date of the launch of the digital lari remains under wraps, and the NBG has yet to release a time window on the project. However speculation has it that potential pilot projects may be seen as early as summer 2022. Cash won't be dead by then – you'll probably still be using it at your next beachside vacation to pay for lounge chairs – but it may already be on the way out.

HOW TO PROTECT YOUR INVESTMENT UNDER GEORGIA'S GROWING NETWORK OF INTERNATIONAL INVESTMENT TREATIES

International arbitration between states and private investors has been receiving increased attention from both the popular and business media. Perhaps the most illustrious example of an investment dispute was the arbitration between Russia and Yukos energy company of the embattled oligarch, Mikhail Khodorkovsky, which ended in 2014 with a ruling requiring Russia to pay over 50 billion US dollars in compensation. Other famous example is compensations awarded to Ukrainian business-owners who suffered losses due to Russia's annexation of Crimea.

These international cases arose from bilateral and multilateral investment treaties between states, which provide an option for investors to bring their disputes with the states before international arbitration. Investment treaties originated in the post-WW2 period as part of the Bretton Woods international economic system and have since played an important role in facilitating the cross-border flow of capital. There are presently more than 3,000 such treaties in force worldwide.

Few investors and local entrepreneurs know that Georgia also offers the possibility of defending their investments under the international investment treaty regime. In an attempt to foster its investment climate, Georgia has concluded almost 40 such bilateral and multilateral investment treaties. The ever-growing network of these treaties protects investors from potentially unfair interference by the state in private business activities.

That being so, not all investment treaties are created equal. A careful consideration and selection of the applicable treaty regime is required to allow investors to protect themselves from different categories of interference by administrative, judicial, tax and investigative bodies, as well as from unfair and confiscatory legislative and regulatory measures.

What are the advantages of investment treaty protection?

By far the most important guarantee of protection that investment treaties envisage for investors is the right to submit disputes with the state before a neutral international arbitration, instead of in domestic courts. Depending on the terms of the applicable treaty, investors can potentially bring their dispute with the state before the World Bank's International Centre for Settlement of Investment Disputes (ICSID) in Washington D.C., the International Chamber of Commerce (ICC) in Paris, or an ad hoc tribunal of the Permanent Court of Arbitration (PCA) in The Hague.

A major advantage of international arbitration is that it provides for the possibility of obtaining an effective compensatory award for damages. Such awards are enforceable against the assets of the state not only on the territory of that state, but virtually everywhere in the world[1]. Statistics show that respondents frequently comply with arbitration awards voluntarily due to the effective enforcement mechanisms in place. Non-compliance with arbitration awards may result in the deterioration of the state's credit ratings by the World Bank and International Monetary Fund – another factor that incentivizes states to comply with arbitral awards on a voluntary basis.

If an investor does not take advantage of the offer to defend its investment under the international investment treaty regime, it is left with the alternative to resolve its disputes with the state before local courts. For instance, the Law of Georgia on Support of Investment Activities (1996) allowed a foreign investor to bring an investment claim against Georgia in ICSID. However, this option was eliminated after the amendments to the law in 2009, leaving such disputes to the jurisdiction of Georgian courts. While Georgia has carried out a series of judicial reforms, significant challenges remain. There are demonstrable disadvantages to resolving complex business disputes before domestic courts compared to international arbitration. In particular:

- The likelihood of success in disputes against state bodies is low before domestic courts, especially in administrative, regulatory, tax and criminal disputes. In contrast, international arbitration provides a neutral and balanced forum, where private investors have a fair chance to prevail or achieve favorable settlement terms.
- Domestic courts often lack sufficient technical and international law competence and resources to entertain sophisticated economic disputes. In turn, international arbitrators are neutral and specialized in international disputes.
- Even where the investor prevails, domestic courts almost never provide for full compensation for the investor's losses. Domestic remedies often include nothing more than a declaration of invalidity of the disputed administrative act. If at all granted, compensation is usually limited to sunk-costs, often without interest. In turn, in international arbitration, the standard of

[1] *Convention on the Recognition and Enforcement of Foreign Arbitral Awards (New York, 1958) has 166 contracting states, while the ICSID Convention has 163 contracting states.*

compensation is full reparation, which fully restores the investor's financial position. The compensation often includes future cash flows (properly discounted) and interest.

Investment treaty protection is also advantageous outside the context of dispute resolution. It increases the investor's bargaining power in negotiations with state bodies and companies, and minimizes the possibility of improper treatment by regulatory authorities. Having access to an effective international dispute resolution mechanism provides a leverage that prevents such disputes from arising in the first place. Engaging in international arbitration with investors sheds a bad light on the investment climate and compels the state to mobilize considerable resources for arbitration costs which the state may prefer to avoid by offering reasonable settlement terms to the investor.

Who can benefit from investment treaty protection?

Investment treaties are primarily designed to protect enterprises that have ongoing business activities or are presently making their investments on the territory of the contracting states. As a rule, investment treaties protect investments is a wide array of economic sectors. This includes energy, mining, agriculture, tourism and hospitality, tech and telecommunications, construction, commodity trading and export-import, distribution, transportation, utilities, media, advertisement, medical services, insurance, banking and finance, as well as entertainment and gambling.

The network of Georgia's investment treaties provides an effective tool of protection not only for foreign investors in Georgia, but also for Georgian entrepreneurs investing abroad or at home. Indeed, some of Georgia's investment treaties provide protection for domestic investors who invest in their own country with a specifically designed corporate structure. However, not all treaties provide for the possibility of protecting such U-turn investments. Domestic investors that would like to come under international protection require a careful consideration of the treaty and arbitral practice and meticulous planning of the corporate structure.

On the other hand, being a foreign investor does not automatically guarantee effective protection under investment treaties. For instance, Russian investors in Georgia do not come under international treaty protection unless they adopt specific treaty planning practices.

Similarly, having a tax efficient corporate structure that involves so-called offshore jurisdictions does not necessarily provide investment treaty protection. For example, enterprises that have participation from British Virgin Islands, Cyprus and the Isle of Man – all relatively popular jurisdictions on the Georgian market – do not automatically fall under Georgia's investment treaties. Enterprises that have such tax optimization structures in place require specialist legal advice ensuring careful planning for treaty protection.

How to plan for investment treaty protection?

The level of protection and the availability of international arbitration to different industries varies depending on the terms of each specific treaty, treaty practice and arbitral case law. For instance, energy companies have a wide range of available options of favorable investment treaty regimes. In turn, commodity-trading, pharmaceutical and gambling enterprises need a more carefully tailored structure in order to enjoy full protection.

To come under such protection, investors must take carefully tailored steps for treaty planning. This entails structuring capital inflow through a well-designed shareholding structure and jurisdictions that enjoy the most favorable treatment under the existing investment treaty regime. The planning must consider not only the obvious terms of the applicable treaties, but also numerous jurisdictional and substantive pitfalls that may emerge from the treaty practice of the contracting states and the vast arbitral case law related to multiple aspects of relevant treaty terms. Most importantly, steps should be taken as a precautionary measure before an actual dispute with the state materializes. After the state takes adverse measures, it is too late as investors are no longer allowed to apply for international protection.

The complexity of the process and the lack of the specialist expertise on the Georgian legal market often prevent local companies from taking advantage of this opportunity. International investment arbitration is a niche sector, in which even well-known international law firms have often limited expertise. Lévy Kaufmann-Kohler (LKK) is a Geneva based boutique law firm which is a market leader in international investment and commercial arbitration. BLC Law Office has recently joined their efforts with LKK's lawyers in advising local and foreign clients on investment treaty planning in Georgia.

Overall, investment treaties can provide a powerful security for a variety of legal risks for international and domestic investors. At the same time, these are complex legal instruments that contain multiple procedural and substantive provisions that require specialist legal knowledge. Investors that take calculated steps have a chance to secure their position under a favorable international regime which enhances protection from the state's adverse interferences and, above all, allows them to submit their disputes to a neutral international arbitration.

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TBC CAPITAL

TBC CAPITAL'S MONTHLY TOURISM WATCH:

SECTOR CONTINUES TO GROW BUT REMAINS VULNERABLE

www.tbccapital.ge

As the second summer of the pandemic draws to a close, TBC Capital's recent tourism monthly watch report shows the sector has seen a strong rebound compared to 2020, with visitor growth up more than 500% in August. Despite these promising signs of recovery, numbers remain far below 2019 levels, indicating that the sector still has a long way to go.

Strong MoM growth in June and July indicated that the sector may see less seasonality in 2021 as delayed demand flattened what is usually a peak of tourism in August and sharp decline from September. However, due to the fourth wave of COVID-19 in August, revenue and visitor numbers slumped, underscoring the sector's continued vulnerability to the epidemiological situation in the country.

RECOVERY FORECASTS

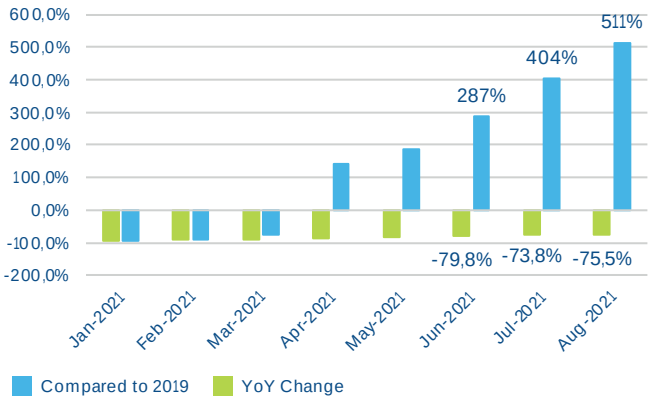
While the industry has seen exceptional YoY growth from 2020, it is still lagging considerably behind pre-pandemic levels. Georgian Minister of Economy Natia Turnava estimated back in May that tourism revenue would recover by up to 50% of 2019 levels by the end of 2021. Recently, however, she revised that statement down and indicated that recovery of around 25 to 30% is expected this year.

TBC's Head of Research Irina Kvakhadze stresses how vital the country's epidemiological situation will be to the sector's recovery: "While June and July saw impressive growth, the August data is slightly disappointing and largely a result of the fourth wave of COVID-19." TBC's forecasts estimate that tourism revenue could recover 37.5% of 2019 levels by the end of 2021. Moreover, she notes that "forecasts for 2022 recovery are as high as 80% of 2019 levels - but again, this is largely dependent on the COVID-19 situation and the vaccination rate."

ORIGIN AND NUMBER OF VISITORS

Georgia's visitor numbers grew YoY by 511% in August, reflecting substantial growth since the summer of 2020. However, visitor numbers still registered 75.5% lower than 2019 levels.

Haltered recovery to 2019 level in August

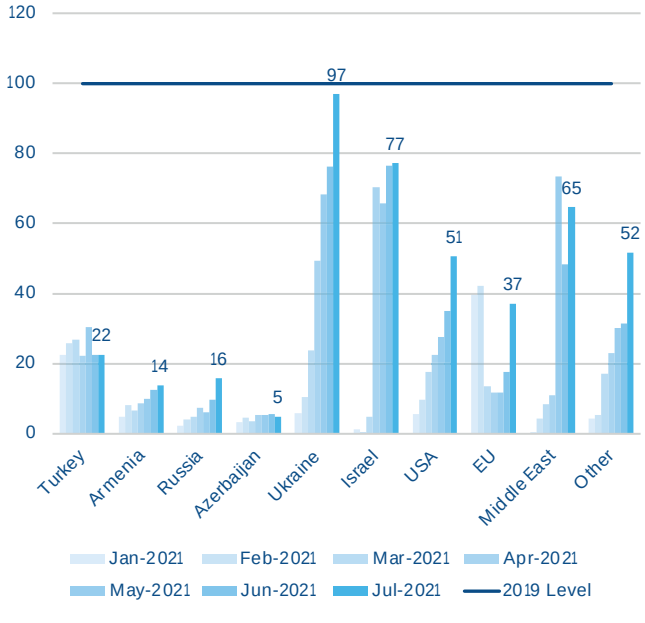


Source: GNTA

In July, the share of travelers to Georgia who came from neighboring countries was 38%, down from 72% in 2019. This substantial decrease in visits from neighboring countries can be attributed in part to Georgia's closed land borders, which reopened for the first time since the pandemic began in June. In August, this figure grew to 41%, and the share of tourists coming from neighboring Russia and Turkey increased. The largest share of visitors in August originated from Russia, Turkey, Ukraine and Armenia.

Notably, in the first seven months of 2021, a strong recovery was seen in the number of travelers coming from Ukraine, Israel, the Middle East, the US, and the UK. COVID-19 safety in origin and destination countries has a strong impact on travel decisions, so it is unsurprising that travel originating from countries with higher vaccination rates has seen higher recovery.

Recovery of international visitor trips to 2019 levels (%)



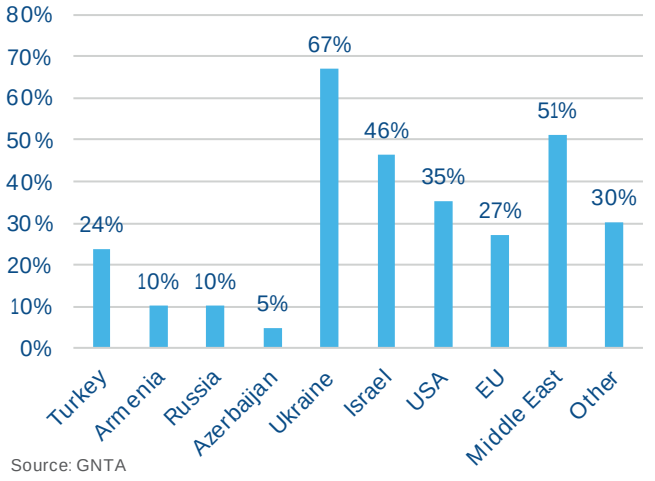
Source: GNTA

TOURISM REVENUE

In July, tourism revenue amounted to 52% of 2019 levels. While August was expected to register even higher growth, revenue decreased to 48%. Tourism revenue has notably recovered at a faster rate than the number of travelers. This indicates that the spending habits of tourists are changing. In July, the average spending per visitor was 98% higher than in the same month of 2019.

As TBC Capital's head of research, Irina Kvakhadze notes, "this could be due to delayed demand. Because of the risks and costs associated with international travel currently, many tourists are taking extended trips, which is increasing their spending." Other factors, like accidental savers, people eager to change locations after lockdown, and the rise of 'work from home' positions could all be impacting the length of time visitors are staying.

Recovery of international visitor trips to 2019 levels (%)



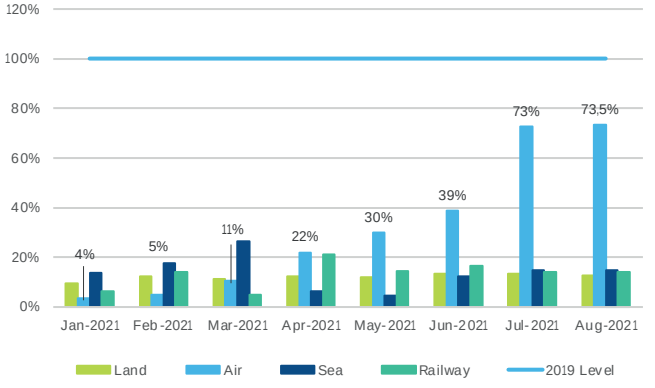
Source: GNTA

AIR TRAVEL

In the summer of 2021, air travel replaced land crossings as the number one method of arrival to Georgia. In July of 2019, land border crossings accounted for 76% of arrivals. In July of 2021, air travel surged in popularity, accounting for 60% of all arrivals. This is most likely due to additional restrictions and closures of Georgian land borders that only opened on June 1.

Despite the opening of the borders in June, land arrivals saw slow recovery in July, amounting to only 13% of 2019 levels. Air travel, on the other hand, recuperated to 73% of 2019 levels in July and 73.5% in August.

International Visitor Trips by Borders (% change relative to 2019)

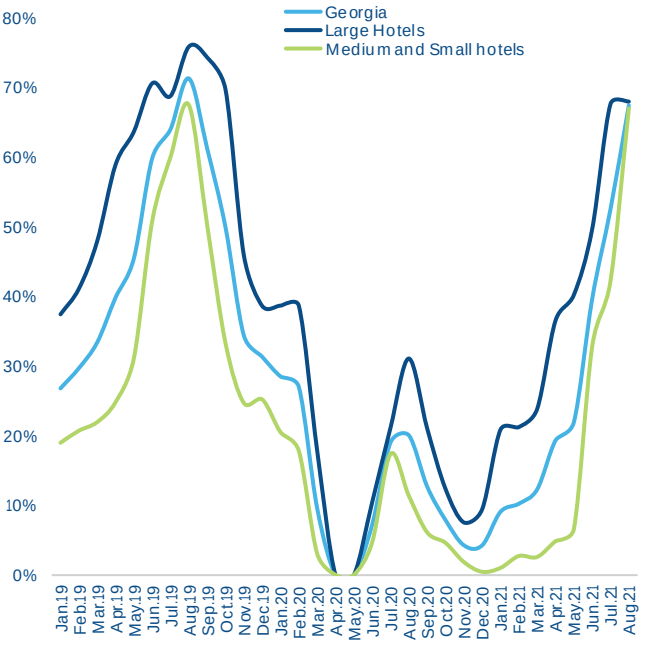


Source: GNTA

THE HOTEL INDUSTRY

The hotel industry has seen impressive growth this summer, which could be a result of increased safety measures and higher levels of domestic travel. Hotel occupancy rates averaged 40% in June, 53% in July, and 67% in August.

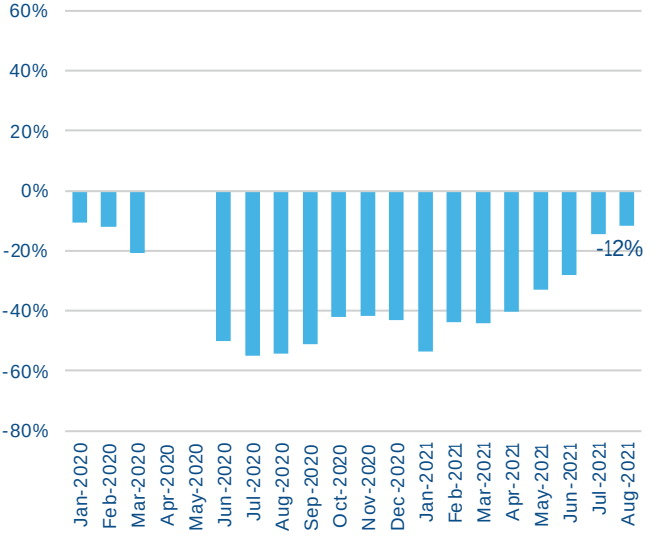
Average Hotel Occupancy



Source: TBC Capital survey;
* Large hotels: more than 80 rooms, small and medium hotels: less than 80 rooms

Average daily rates (ADR) have also seen a steady recovery since March of this year. According to a survey done by TBC Capital, ADRs in July were only 14% behind 2019 levels. In August, ADRs were only 12% below pre-pandemic prices.

Average Daily Rate (change relative to 2019)



Source: TBC Capital survey

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Whither the lari?

Georgian banks, businesses take a look at 2022

THE LARI'S VALUE AGAINST THE DOLLAR HAS BOUNCED TURBULENTLY IN THE LAST YEAR, PLUMMETING TO 3.44 GEL/USD IN MAY AND REACHING A HIGH OF 3.06 IN AUGUST. ANALYSTS EXPRESS CAUTIOUS OPTIMISM FOR A MORE STABLE LARI AS THEY LOOK TOWARDS 2022.

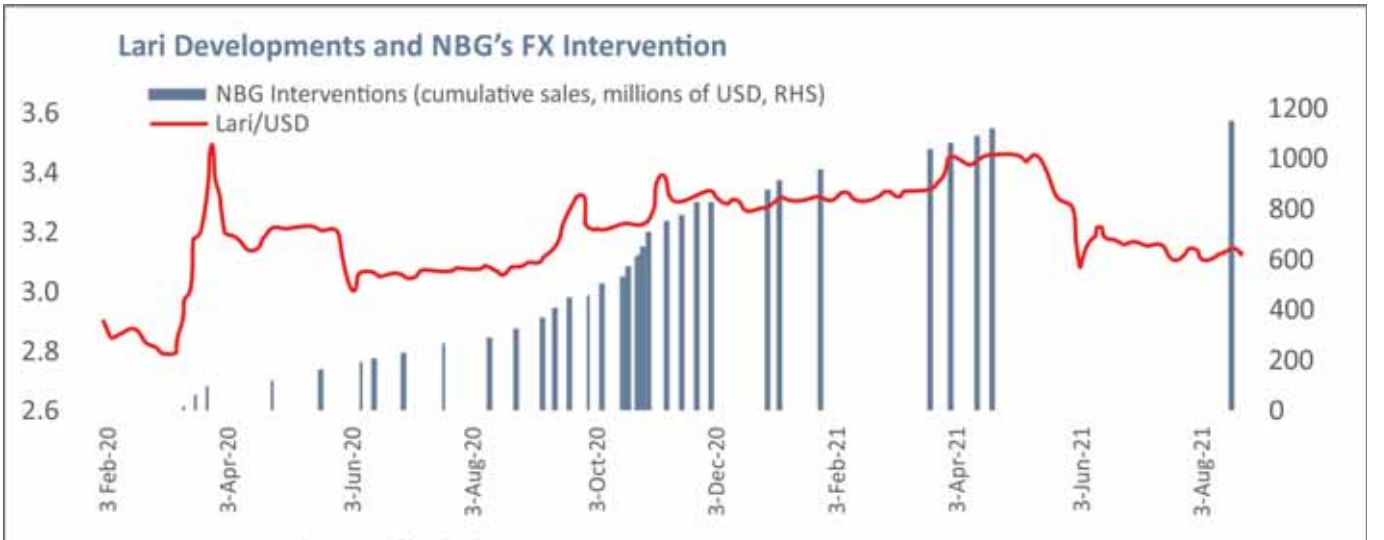
SALLY WHITE

The volatility of the lari has been a major hindrance for much of Georgia's business community this summer, according to a Q3 survey carried out by the Business Association of Georgia (BAG). The BAG Business Climate Index, which examines the views of member corporations and businesses for the next six months, found that among the three-quarters who were experiencing problems, 78% of its major manufacturing members and 68% of the total membership were concerned about lari volatility.

While the economic and capital flow fundamentals would seem to indicate currency stability into 2022, many businesses, having been burnt in the past, are reluctant to believe that the lari can break out from its years-long trend of depreciation against the dollar. This is indicated by the fact that 55% of BAG's members now expect the lari to depreciate, up from 49% in Q2. This is distressing for the population since so many identify the dollar-lari rate as the key barometer for the country's economic health.

CAUTIOUS OPTIMISM

Yet as tourism recovers, there is more optimism among professional watchers of the economy and currency, including BAG, investment bankers Galt & Taggart and TBC Capital, and international rating agency Fitch as well as the National Bank of Georgia (NBG) itself. One indicator that the volatility causing Georgian businesses so much concern may have come to an end (for now, at least) is that international data group Trading Economics



Source: NBG, Haver, and IMF staff calculations.
Note: NBG sales in 2020 amounted to USD 873 Million. Total sales in 2020 and 2021 were USD 1,146 million.

now carries a forecast of around 3.2 GEL to the dollar until July 2022 – not much changed from current levels.

Many of the factors that were pulling down the lari have reversed, and the economy has "rebounded at a speed exceeding even the most optimistic scenarios," as TBC Capital's chief economist Otar Nadaraia described. TBC Capital's range suggestions for the months ahead are 3 to 3.3 GEL against the dollar, and 3.69 to 3.86 GEL against the increasingly important euro. More attention should be paid to the euro, believes TBC's chief economist, as its rate has been less volatile against the lari than the dollar. The EU is also the source of 40% of the money sent home this summer by Georgians abroad as well as 23% of trade in 2020 (making it Georgia's top trade partner). EU tourist inflows are rising rapidly as well.

At Galt & Taggart, Head of Research Eva Bochorishvili says "We do not expect sharp volatility in the FX market in 2H21, with the GEL ranging from 3.1 to 3.2 against the dollar in this period." She added: "We see GEL appreciation potential in 2022 amid an expected full recovery in tourism, and we assume tourism will recover to 36% of its 2019 level in 2021." Further stability is expected from a reduced budget deficit and continued improvement in the economy.

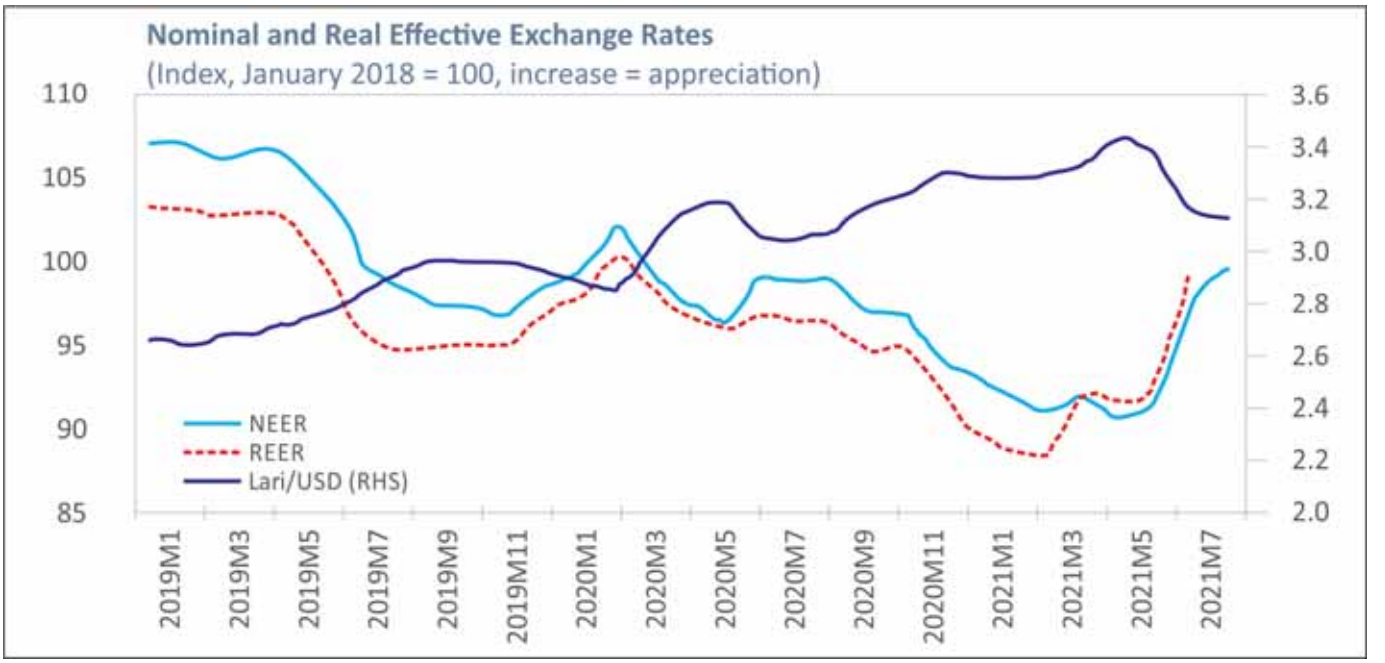
However, history gives reminders that it is essential to be aware of what could bring another lari reversal. "Risks which may delay GEL appreciation are possible new variants of COVID-19, a vaccination slowdown, political instability, and turbulence in regional and global financial markets as well as tightening in financial conditions," she adds.

At BAG, too, there is optimism about an end to lari volatility – for the rest of this year, at least. Economist Natia Bantsuri points to numerous factors backing the currency: the effect of the money flowing into Georgia from tourists and trade, and the sizable economic and fiscal stimuli brought in to counter the impact of COVID-19. The mortgage subsidy program is expected to create demand for the lari, and government spending is typically higher in Q4. She also notes that for financial market investors (foreign as well as domestic), the lari's relatively high interest rates, at around 11% or higher on some deposits, make it attractive to the yield-hungry, given that international rates are frequently, as in the US, below 1%.

However, she too voices the proviso that "risk factors are always in place," among which must be counted the vulnerability of small and very open economies such as Georgia's, whose shallow financial markets offer little protection for their floating exchange rates. Events that could bring renewed pressure on the lari include concern about management of the pandemic and new waves as well as delays in economic recovery. But, she notes: "The policy response to these changes is no less important."

POSSIBLE SCENARIOS

A range of currency scenarios – baseline, upside and adverse – have been published by the NBG. Its prime preoccupation is the control of inflation, with a current target of 3% (rather far from the current, pandemic driven, 12.8% in August), and it steers its monetary policy ▸▸



and interest rates towards achieving that goal.

"The NBG has intervened in the foreign exchange market extensively in order to alleviate excessive volatility of the exchange rate and supplied FX (foreign currency) liquidity (around $916m) to the market. However, the aim of FX interventions never was to set the exchange rate at any particular level," it states.

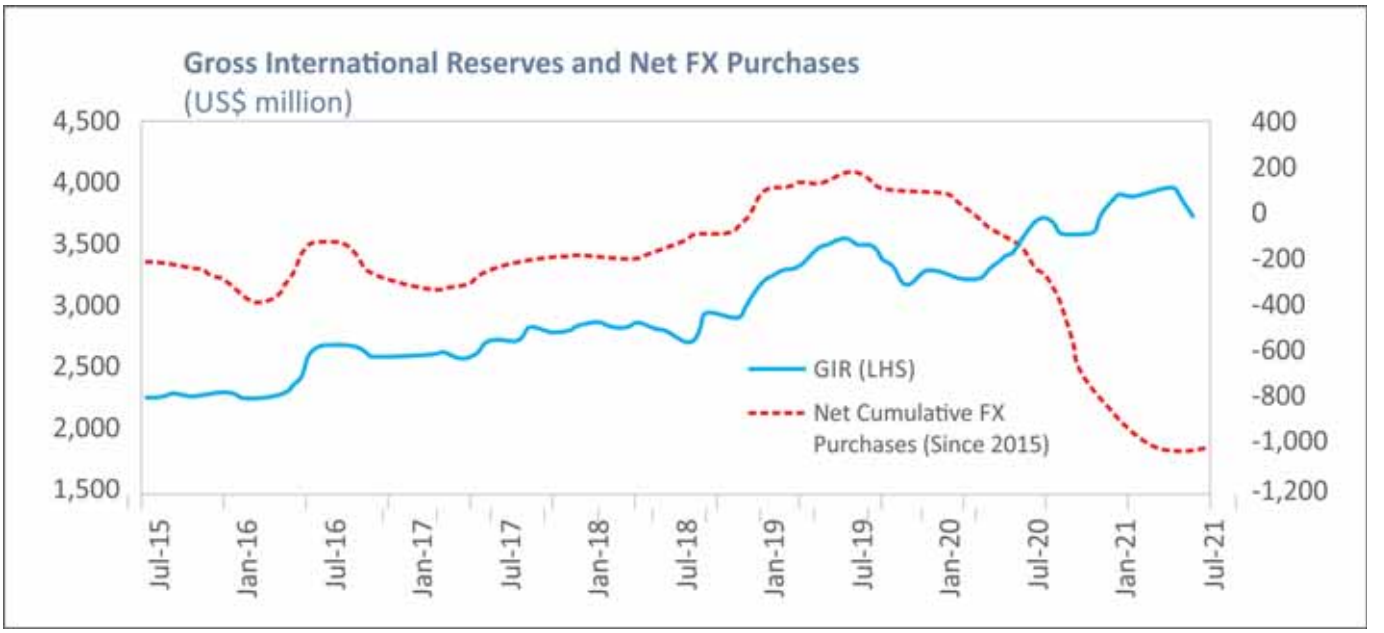
The intended purpose of the lari support operation (considering 2021's spending, it amounted to $1.12 billion) was to counter the inflationary effect when it was dumped heavily as a result of the 83% drop in receipts from pandemic-hit tourism, shrinking trade and industrial activity, and recent decline (50%) in major cross-border foreign direct investment. Nevertheless, its "monetary policy rate" (the key interest rate), which was recently increased to 10%, is vitally important for Georgian and foreign borrowers and savers (and it is not shy of raising it, as the bankers comment). Thus, the NBG influences the currency via both this interest rate and its direct market actions, making it one of the important players in currency flows and lari exchange rates.

The NBG aims to send clear signals, publishing guidance that relatively high interest rates (compared to other frontier markets) will continue for some time yet. Last month, after raising its monetary policy rate when inflation ratcheted up to 12.8%, the NBG stated that "in the baseline scenario, inflation will remain above the target this year, which is largely due to sharply higher commodity prices in the international market." It added that because of the risks, "monetary policy will remain relatively tight for a relatively long time. The pace of exit from the tightened monetary policy regime will depend on the reduction of inflation expectations." However, under the assumption that inflation will fall next year, current market expectations among commercial banks are that interest rates will also be heading down, with expectations ranging from cuts of 1.5 to 2% off the existing 10% by the end of 2022.

Another action taken by the NBG that has helped support the lari includes incentives for the banks to promote de-dollarization of deposits, which has eased demand for dollars, notes Galt & Taggart. Additionally, while its major auctions attract headlines, the NBG has also smoothed the thinly populated lari market with smaller auctions to prevent disruption by corporate trade-linked buying and selling.

In its base-line scenario for the lari (which has real GDP growth at 8.5% for this year and 4% for 2022 based on rising domestic consumption), the NBG's August Macroeconomic Forecast Scenarios concurs with the banking economists in its prediction of exchange rate stability. It foresees that inflation will start to decline next year, allowing interest rates to fall, and that economic growth and returning tourists are already reducing the burden of the large foreign debts noted by Fitch. "Consequently, the vulnerability of the domestic economy to external shocks will decrease, and the sovereign risk premium will remain at its current low level."

In its other possible scenarios, a positive outlook shows an immediate strong global post-pandemic rebound that would spur increased investment and trade demand. In that case, Georgia could see "GEL gains in value against the US dollar by 3% in the rest of 2021 and by another 3% in 2022." However,



if the global pandemic is not contained and restrictive measures last into late 2022, delaying international economic recovery, the NBG's worst case scenario outlines a picture in which risks to Georgia could bring the lari down 10% this year and 5% next, although 2023 could see this depreciation reversed.

Of course, as the economists observe, Georgia remains vulnerable to potential "shocks" from a worsening pandemic, soaring commodity prices, elections, and the economies and troubles of neighbors. However, encouragement for international observers is coming from a look at the sums that indicate currency flows are building up in the lari's favor and backing is coming from good international opinion of the NBG's financial risk management. This includes international rating agency Fitch, even though it notes the concerning bills Georgia faces for its mountain of foreign financing. Currently, net foreign debt is 77.5% of GDP compared to international peers' average of 18.7%.

Fitch has upgraded its outlook for Georgia, a vital score since its opinion dictates the price the country pays for international market funds. It points to the positives of money coming in from "growth in remittances, goods exports and a gradual return of tourists." And Georgia's friends have stepped in to help. Fitch added in its August review that the country's higher financing needs were accommodated by "strong support from official creditors" with international donors meeting "nearly all of the government's external financial needs." The report notes that their confidence was engendered by "a credible policy framework."

Other positive financial indicators highlighted by Fitch include the fact that the money available to the NBG to manage the lari has risen, helped by donors and the national bank's increasing use of sophisticated strategies to steer currency flows. The country's foreign currency reserves now stand at $4.1 billion. It also notes that the gap between money coming into the country and that going out is expected to drop from 12.4% of GDP last year to 6.8% this year. It is expected to narrow further to 3.3% by 2023. This is on the back of money inflows from tourism's recovery, sustained donor funding, and level foreign direct investment.

Increasingly sophisticated strategies are also being suggested to companies by their bankers, including deploying currencies of the neighbouring countries with which they are familiar to fully hedge the risks arising from lari volatility. TBC notes that Georgia has shown a propensity to save in dollars but borrow in lari. Certainly, borrowers with a lari income stream should have debt in the same currency, says Otar Nadaraia. However, especially for longer-term debt, high lari interest rates are an issue, and USD or EUR loans with lower rates are therefore preferable. He suggests a strategy of multi-currency borrowing, using a basket of currencies, could be a better solution for achieving a balance between the opportunities and risks: the choice reflecting the countries with which a company is trading, the availability of attractive credit costs, and assessment of the relative risks.

He suggests that the Russian rouble or Turkish lira could be incorporated in a basket, together with the euro. This basket "bears a much lower rate and at the same time largely mirrors the lari, especially over longer periods."

He adds it is noteworthy that the GEL exchange rate (as well as rates of other major currencies in the region) appears to be more stable against the EUR than against USD, especially over relatively longer periods. Therefore, "the euro should have more weight (in a basket) as compared with what would be implied from the Euro-area share in Georgia's trade in goods and services and remittance inflows." He notes that: "This idea could be also interesting for investments in high yield GEL instruments for those with EUR or USD income streams."

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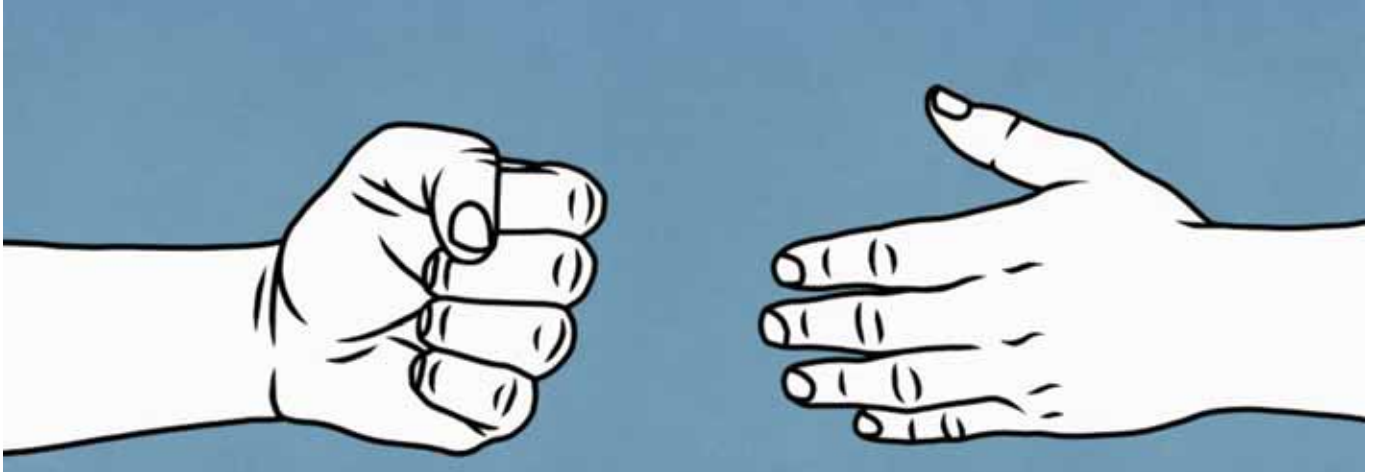


A *kovidsalami* to the new Georgian – how COVID-19 has changed the language forever

THOMAS WIER

Something very unusual happened at that unofficial bastion of the English language, the Oxford English Dictionary, in late 2020.

The editorial staff in charge of writing their annual report decided that the events of that year were so unusual in their effects on how people talk and describe the developments that were unfolding that they could not choose any one single 'Word of the Year' to encapsulate its myriad events. From 'R-0' to 'community transmission' to 'self-isolating' and 'doom-scrolling', words evolved or increased in frequency to describe new realities. They noted that the word 'coronavirus' itself became more frequent in their corpus databases than that ancient word, 'time.'

What happened to English is part of a broader trend around the world as speakers of all languages have been forced to adapt to changing environments and newly articulated realities. Here in Georgia, the effects of the pandemic produced an uneasy seesaw effect as early strict lockdowns imposed by Georgia's health authorities relented in the summer of 2020 to tentative broader reopening, only to be followed by renewed strict measures in the fall following October's parliamentary elections. Some of these figures, such as Health Minister Ekaterine Tikaridze or Center for Disease Control head Amiran Gamkrelidze, rose to iconic status, as their weekly or even daily pronouncements were followed by an anxious population. They found themselves having to explain, in Georgian, words, phrases and sentiments that were new even in the languages from which they were translating: lok'dauni anu sruli čak'et'va 'lockdown or in other words a complete closing', sp'aik'cila 'spike protein' or the esoterically statistical mosaxvevis gabrt'q'eleba 'flattening the curve.'

And it was not just in press-conference halls that the narrative changed. Some words already existed in the language, but received new prominence: k'arantini (quarantine), uk'ontakt'o (contactless), acra (shot, jab), gadamgebi (contagious), mosaxleobis imunit'et'i (herd immunity), and of course p'irbade (facemask). Many words like lockdown were either wholly new loans into Georgian or generally unrecognized by the wider population: k'last'eri (cluster), k'ont'akt't'reisingi (contact-tracing), sup'er-sp'rederi (super-spreader) and ant'ivakseri (anti-vaxxer) required a certain level of discernment or insider-knowledge to decode for Georgians who were not up to date with the latest jargon and cultural trends. In some cases, pre-existing words changed meaning: in 2019, a vent'ilat'ori referred primarily to a fan to cool down with, but one year later it came to have a more somber medical meaning. And some words mixed and matched foreign concepts with indigenous resources: tvitizolacia 'self-isolation,' ep'idsit'uacia 'epidemic situation,' ep'idvitareba 'epidemic development' and sac'olpondi 'bed capacity.'

Then there were words that did not describe the pandemic itself so much as people's reactions to it and the new social conditions it brought. Government regulatory agencies debated whether citizens needed k'ovidp'asp'ort'ebi (COVID-passports), and who precisely counted as aucilebeli mušebi (essential workers), not to mention musings about how big the generation of k'oronialebi ('Coronials,' Corona-babies) would be. People were asked to dist'ancia daicavit 'maintain distance;' notably, the phrase does not use the older Georgian word for distance, mandzili, probably reflecting its origins as a translation from Western languages. People also forsook handshakes and began greeting each other with fist or elbow bumps as a kind of k'ovidsalami (COVID-greeting). Almost everyone was forced to resort at least sometimes to online meetings through the Zoom application, with its associated confusion over who gets to talk (Daimiute! 'Mute yourself!') and was subject, as it unfortunately sometimes was, to zumbombingi (Zoombombing). Many welcomed the

introduction of vaccines, any vaccines, as a kind of deus ex machina heralding a return to normality. These eagerly sat at their computer console, waiting for a seat in the Georgian Health Ministry's vaccination program to open up. Afterwards they sometimes flaunted their new status as vakcinosani, literally 'clothed in the protection of a vaccine,' an allusion to the great medieval Georgian epic poem, the Vepxist'q'aosani (The Knight in the Tiger Skin). Others, probably the majority, were not so sure: they had their doubts about vaccines in general, or just the Russian or Chinese vaccines. Some people hedged their bets: they got their first shot of one brand (usually Sinopharm or Sinovac which were first available), but then gadacra-ed (literally 'transjabbed') a different one for their second. Such was the dislocation in people's lives that people began to speak of 2019 as a new k'oronik'oni 'Corona-era', an allusion to the era names of medieval kings and emperors.

As in the West, this wave of neologisms reflects the way in which Georgians experiencing the pandemic have internalized its presence in their lives and begun to integrate it into their larger hopes and fears about the state of the world. The visible role in public life of the Georgian Orthodox Church (of which 83% of Georgians are members) has witnessed varying levels of controversy in recent years, and since the start of the pandemic this has only been accentuated by the unwillingness of some clerics to emphatically support vaccination and public health measures endorsed by the government. The sight of priests driving through the streets in acts of mass-blessing with holy water, or encouraging parishioners to believe that drinking holy wine from a common communion spoon will protect them from the spread of the virus, elicited quiet skepticism from some quarters, while from others derisive calls of k'ovzidiot'ebi (from k'ovzi 'spoon' and idiot'i 'idiot', a play on the western neologism covidiot).

The pandemic has also provided fodder for all kinds of misinformation about the pandemic and accompanying conspiratorial thinking about its origins and propagation. According to Dustin Gilbreath, deputy director of the Caucasus Research Resource Center (CRRC) in Tbilisi, Georgia has one of the highest vaccine-hesitancy rates in the world: in a survey done on 30 March 2021, 57% of respondents said they would not want to receive a vaccine if it were available now.1,2 A year earlier, around 42% of the Georgian population believed the virus was created in a lab,3 a figure which has probably not dropped much since. It is easy to encounter wilder conspiracies in Georgian-language media: that the biblical Book of Revelation says vaccines are the mark of the Beast;4 that retractable vaccine syringes are being used to inject nanochips to control people;5 that apparent COVID-19 victims are still alive and being held in Australia;6 and that vaccines are actually šxamkcini, literally 'poison-vaccines.'

Though it is hard to take these claims with any level of seriousness, they are having an undoubted effect on how people talk about the pandemic: dğes Ast'razenek'ati davičip'e 'Today I got chipped with Astrazeneca', former State Minister for Reconciliation Paata Zakareishvili is reported to have said. This is because languages evolve and change to reflect not the world as it really is, but rather the world as their speakers perceive it.

Will any of these changes have a lasting effect on the language? This is impossible to know. In every era of change, new generations adopt or reject the phraseology of times past based on who is now using it, how often, and why. Language is a kind of self-organizing system that tracks the patterns of human social networks that we all live in and interpret our world with. It is effectively a kind of communicative currency, the value of which changes depending on who uses it and why. When properties of those social networks change, language usually changes too. But if past epidemics are any guide to the future, even truly great changes in society may take years or decades to become apparent. When the bubonic plague ravaged medieval England in the years 1347-1352 and killed half the population, international trade came almost to a standstill, and it had an immediate effect on the French-speaking aristocracy and barristers, who became too thin on the ground. Within ten years, the language of the colonial occupiers, French, ended up being replaced by the indigenous language English in the courts of law. It also helped lead to a rebirth of English as a literary medium and reinforced the dialect of London as a new standard form of language: Geoffrey Chaucer, William Langland, and John Wycliffe all flourished in its immediate aftermath. But the real change did not come for generations more when systematic changes to English pronunciation known as the Great Vowel Shift started spreading through the population. Thus Middle English began its transition to Modern English.

Whether and how that earlier pandemic was related to the seismic change in language is controversial and unclear. What is clear is that it was changing the world in which speakers talked about and conceived their relationships to each other. It was changing, in the most literal sense, who was talking to whom. And that much is true in today's Georgia during the COVID-19 pandemic as it was in ages past.

AMCHAM

CONTENT

42 Meeting with Georgian Speaker of Parliament on improving parliament-business community engagement

41 AMCHAM HOLDS LUNCHEON WITH ACTING ASSISTANT SECRETARY PHILIP REEKER

42 AMCHAM MEMBERS MEET WITH GEORGIAN INFORMATION INTEGRITY PROGRAM TEAM

43 NEW MEMBERS

44 MEMBER DIRECTORY

48 BOARD OF DIRECTORS

AMCHAM MEETS WITH GEORGIAN PARLIAMENTARY SPEAKER KAKHABER KUTCHAVA

Georgian Parliamentary Speaker Kakhaber Kutchava held a meeting with AmCham First Vice President Irakli Baidashvili, Vice President Michael Cowgill, Executive Director George Welton and Legal and Public Policy Director Lina Jikia on June 8. The parties discussed how to improve cooperation between the Parliament and businesses.

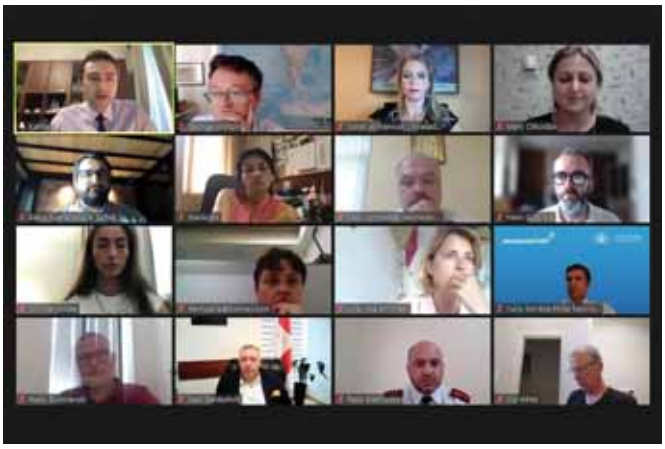
LUNCH WITH ACTING ASSISTANT SECRETARY PHILIP REEKER

AmCham hosted a lunch with Acting Assistant Secretary Philip Reeker, at the end of his week-long Caucasus tour on June 11. The meeting included Ambassador Reeker and US-Ambassador Kelly Degnan as well as First Vice President of AmCham Irakli Baidashvili and high-level business guests.

AMCHAM MEMBERS MEET WITH GEORGIAN INFORMATION INTEGRITY PROGRAM TEAM

AmCham Georgia hosted The USAID-funded Georgian Information Integrity Program team represented by Chief of Party Mikheil Benidze, Deputy Chief of Party William Dunbar and Research Manager Nina Khatisashvili on July 1. The speakers presented the results of their first wave of nationwide public opinion polling regarding the impact of Russian and Georgian disinformation on the Georgian population.

MEETING WITH GEORGIAN SPEAKER OF PARLIAMENT ON IMPROVING PARLIAMENT-BUSINESS COMMUNITY ENGAGEMENT



AmCham Georgia hosted the Speaker of the Parliament of Georgia Mr. Kakhaber Kutchava at an online meeting with members on July 7. Kutchava discussed how engagement between parliament and businesses could be improved. The presentation was followed by a dynamic Q+A.

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