

# **Mid Term Evaluation**

*Georgia's SME Development Strategy 2016-2020*

*Prepared by: Economic Policy Department of the Ministry for Economy and Sustainable Development of Georgia with support of OECD*

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# Contents

- Introduction .....3**
- Executive summary .....4**
- Acronyms and Abbreviations.....6**
- Methodology.....8**
- Background and main trends during AP implementation..... 10**
  - Introduction .....10*
  - Economic and policy developments since 2015.....11*
  - The SME sector in Georgia.....12*
  - Main stakeholders in charge of SME policy implementation .....13*
- Evaluation of implementation of main directions of SME development Strategy of Georgia ..... 14**
  - The First Strategic Direction: Further improvement of legislative, institutional framework and operational environment for SMEs .....14
  - Strategic Direction 2: Enhance access to finance for Georgian SMEs.....19
  - Strategic Direction 3: Promote skills development and entrepreneurial culture .....25
  - Strategic Direction 4: Support SMEs’ internationalisation.....31
  - Strategic Direction 5: Facilitate SMEs’ innovation and R&D .....36
- Action plan achievements ..... 40**
  - Implementation of Actions.....42
- Main Recommendations .....45**
- References..... 48**

## Introduction

In 2015, the Government of Georgia (GoG) embarked on an ambitious journey to improve business environment conditions and tackle market failures that make it harder for entrepreneurs and managers of small and medium-sized companies to start, run and grow their business. With the support of the OECD, the Ministry of Economy and Sustainable Development (MOESD) of Georgia engaged in a series of thematic public-private workshops to identify policy challenges and develop targeted measures to support Georgian SMEs. These activities led to a peer review of Georgia at the OECD Eurasia Competitiveness Roundtable in November 2015, and to the subsequent adoption by the Government of Georgia's SME Development Strategy 2016-2020.

The Strategy is based on the main principals of Small Business Act (SBA) for Europe, covering important areas such as improving SMEs' operational environment, access to finance, enhancement of skills, facilitation of internationalization and innovation activities.

Following adoption of the SME's Development Strategy (2016-2020) and relevant Action Plan, for the purpose of monitoring and evaluation of its implementation a high level Coordination Group (headed by the Minister) and the relevant Working Group (headed by Deputy Minister) was established by the Order of the Minister of Economy and Sustainable Development (Order N1-1/372 of the Minister of Economy and Sustainable Development of Georgia, 11.07.2016). Apart this, Economic Policy Department of MOESD has been tasked with the coordination and secretary activities of the abovementioned Groups, as well as implement analysis and evaluation of the SME Development Strategy and action plan.

Herewith, OECD with its staff and relevant international expert provided further support to MOESD in terms of monitoring and evaluation of SME Development Strategy implementation within the frame of the European Union co-funded project as part of the EU4Business initiative.

Aftermath of the work that was conducted with combined method (joint efforts of the Economic Policy Department with support of the OECD) in terms of evaluation of the SME Development Strategy's AP is summed up in this Report.

**Table 1: Main elements of the Mid-term evaluation Action plan for implementation of the SME Development Strategy 2016-2020.**

Purpose of the evaluation	Mid term covering period 2016-2017, with idea to evaluate implementation of SME Development Strategy AP, identifying outstanding issues for SME sector and identify the factors of success and failure as well as provide proper recommendations for the top management of MOESD in order to enhance SME development in Georgia
Methodological approach	Quantitative and qualitative
Time	Ex-post, mid-term evaluation
Who is doing	Internal (Economic Policy Department) with external consultancy support
Outcomes	An evaluation with idea to shape the future activities for further development of SME

## Executive summary

This report assesses the extent to which main directions and targets of SME Development Strategy's AP for 2016-2017 have translated into policy reforms, identifies outstanding gaps, proposes the ways forward and recommendations in order to enhance further development of SME sector in Georgia.

As a result of the evaluation that was carried out by Economic Policy Department of MOESD with support of OECD in general the following conclusions and recommendations have been elaborated:

- The main aim of this Strategy, which is based on “Think Small First” principle, is the enhancement of SME sector competitiveness, which will create solid base for inclusive and sustainable economic growth. Strategy sets targets (Growth SMEs output by average 10% annually by 2020; Growth of number of employees in SMEs by 15% by 2020; Productivity growth by 7% by 2020.) to be achieved by 2020. Targets of effective implementation of SME Development Strategy are as follows (baseline – 2013):

Targets<sup>1</sup> of SME development strategy **have been successfully fulfilled**. In particular:

- ✚ Average annual Growth SMEs output is 14.4% in 2014-2017;
  - ✚ Growth of number of employees in SMEs is by 27.4% in 2017;
  - ✚ Productivity growth is by 11.1% in 2017.
- The **institutional framework and operational environment** for SMEs has substantially improved, with, e.g., the adoption of a new SME definition, the formalisation of platforms for public-private dialogue on business-related policies and laying the groundwork for Regulatory Impact Assessments (RIA). Building on these achievements, the **introduction of SME-specific RIA tests** could help better anticipate the potential impact of draft legislation on SMEs.
- **Access to finance for SMEs** is now easier, thanks to changes in the legal framework allowing the provision of grants to commercial entities, an increase in the financial support offered by state agencies and the implementation of a multitude of financial education initiatives. However, a more co-ordinated approach to financial education could better address the specific needs of small and medium entrepreneurs, while also facilitating the adoption of international financial reporting standards. In addition, the **creation of a full-fledged credit guarantee scheme** and the **development of alternative financing tools** could reduce the burden of currently heavy collateral requirements on SMEs.
- Georgia has made important progress in developing **skills and entrepreneurial culture**, especially regarding skills needs anticipation, the involvement of employers in setting education and training standards, and the introduction of mandatory entrepreneurship modules in vocational education and training curricula. Separate Action Plan on promoting women's entrepreneurship could be designed. To proceed conduction of labour market

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<sup>1</sup> Target indicators calculated according to new definition of SME that is stipulated by new methodology of GEOSTAT. Namely, a large enterprise is an enterprise in which the average annual number of employed exceeds 249 persons and/or volume of average annual turnover exceeds GEL 60 million. Medium-sized enterprises are all enterprises in which the average annual number of employed ranges from 50 to 249 persons and average annual turnover ranges between GEL 12 million to 60 million. Small-sized enterprises are enterprises in which the average annual number of employed does not exceed 50 persons and average annual turnover GEL 12 million.

surveys, inter alia, **labour market surveys of priority economic sectors** in order to create relevant statistical data series for anticipation and creation basis for evidence based policy.

- **Cluster development** as well as providing **targeted financial support** could be considered for further support of **SME internationalisation**;
- Important steps have also been taken to facilitate **SMEs' innovation and R&D activities**, by, e.g., allowing public universities and research centers to own spin-off companies and increasing financial support for innovation and expanding the statistical base on companies' use of ICT and innovation activities. The **adoption of a more strategic approach towards SME innovation**, including dedicated instruments to ensure better and more effective implementation of priority actions, would facilitate Georgia's shift towards a knowledge and innovation-based economy.

## Acronyms and Abbreviations

AA	Association Agreement
APR	Annual progress report
CGS	Credit guarantee scheme
DACUM	Developing a Curriculum
DCFTA	Deep and Comprehensive Free Trade Area
EaP	Eastern Partnership
EBRD	European Bank for Reconstruction and Development
EC	European Commission
ECP	Eurasia Competitiveness Programme
EEN	Enterprise Europe Network
ETF	European Training Foundation
EU	European Union
FabLab	Fabrication laboratory
FDI	Foreign direct investment
GCCI	Georgian Chamber of Commerce and Industry
GDP	Gross domestic product
Geostat	National Statistics Office of Georgia
GoG	Government of Georgia
GIS	Geographic Information System
GITA	Georgia Innovation and Technology Agency
GIZ	Deutsche Gesellschaft für Internationale Zusammenarbeit
GVC	Global value chains
IFRS	International Financial Reporting Standards
INFE	OECD International Network on Financial Education
IP	Intellectual property
MIT	Massachusetts Institute of Technology
MoES	Ministry of Education and Science
MoESD	Ministry of Economy and Sustainable Development
MNE	Multinational enterprise
NBG	National Bank of Georgia
NCEQE	National Centre for Education Quality Enhancement

OECD	Organisation for Economic Co-operation and Development
PPC	Public-Private Consultation
PSDAC	Private Sector Development Advisory Council
R&D	Research and development
RIA	Regulatory impact assessment
SARAS	Service for Accounting, Reporting and Auditing Supervision
SBA	Small Business Act
SME	Small and medium-sized enterprise
SD	Strategic Direction
TNA	Training needs analysis
UNDP	United Nations Development Programme
VET	Vocational education and training
WB	World Bank
WBL	Work-based learning

## Methodology

The evaluation aims to assess the mid-term implementation of Action plan for the period 2016-2017 of SME Development Strategy of Georgia 2016-2020.

The report was made in line with Approved Methodology for Common Policy Monitoring, Reporting and Evaluation Systems as well as the Policy Planning Manual, which have been developed by the Administration of the Government of Georgia and adopted by Government Resolution<sup>2</sup>.

As for the method of implementation and applied methodology for evaluation report, it should be stressed that combined method was applied for the evaluation. It was conducted by civil servants of MOESD - by the staff of the Economic Policy department of MOESD with support of the OECD and International expert. All structural units of the department took active part in the evaluation process. This approach is recognised as good practice in the Georgian guidelines. Applied methodology comprises:

- Desk review:
  - ✓ An in-depth analysis of the annual progress reports on the SME Development Strategy Action Plan (years 2016 and 2017);
  - ✓ Ministry's Annual Reports (years 2016 and 2017);
  - ✓ Annual Reports of LEPL "Enterprise Georgia" and LEPL "Georgian Innovation and Technology Agency";
  - ✓ External reports about Georgia's SME Development prepared by donors, NGOs, or research institutions;
- Interviews with representatives of all relevant Ministry's departments as well as discussions with all relevant entities directly responsible for Action plan implementation.

Due to the mid-term character of the evaluation 3 parameters (**Relevance, Effectiveness, Implementation**) of evaluation was determined out of 6 (**Relevance, Effectiveness, Efficiency, Implementation, Impact, Sustainability**). In order to perform evaluation in accordance with approved Common Policy Monitoring, Reporting and Evaluation Systems as well as the Policy Planning Manual, which have been adopted by the Government of Georgia, the following steps were determined:

**Step 1:** Formulating evaluation questions;

**Step 2:** planning evaluation;

**Step 3:** Data collection and analysis methods;

**Step 4:** Writing Report

**Step 5:** Implementing evaluation Findings

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<sup>2</sup> Policy Planning Manual has been developed by the Administration of the Government of Georgia (Resolution of GoG №628; 30.12.2016). The Handbook presents the system and phases of policy planning, types of documents and their hierarchy, and the systems of monitoring, evaluation and reporting.

## Evaluation process

<p><b>Formulating evaluation questions:</b> WHAT we want to know?</p>	<p>The main evaluation questions are:</p> <ul style="list-style-type: none"> <li>• Does the strategy respond to the needs of the beneficiaries and set goals?</li> <li>• To which extent implementation of targets of the strategy and main directions are achieved in 2016-2017?</li> <li>• What are the lessons learnt from the Action Plan implementation?</li> <li>• How situation can be improved?</li> <li>• What are quality of implementation process and structures?</li> </ul>
<p><b>Planning Evaluation:</b> WHAT resources do we have? HOW will we evaluate? WHO should undertake it?</p>	<p>Resources:</p> <ul style="list-style-type: none"> <li>• Economic Policy Department of MOESD;</li> <li>• External consultant (within the support of OECD)</li> </ul> <p>Methodology:</p> <ul style="list-style-type: none"> <li>• By Approved Methodology for Monitoring and Evaluation of the Implementation of the Strategy and Action developed by the Administration of the Government of Georgia</li> <li>• Policy Planning Manual</li> <li>• Good international evaluation practice</li> </ul>
<p><b>Data collection &amp; analysis methods:</b> WHAT data do we need? HOW do we collect? HOW do we analyze data?</p>	<p>All relevant Agencies and entities presented their progress regarding achievements in their field of responsibility, in particular regarding Action Plan implementation.</p> <p>Georgia in comparison with other EaP countries has significantly improved data access and quality, as well as Statistical data that are in full compliance with EUROSTAT.</p>
<p><b>Writing Report:</b> WHAT is the format? WHO needs it? HOW do we communicate?</p>	<p>Writing Report:</p> <ul style="list-style-type: none"> <li>• Draft Report was prepared by the Economic Policy Department of MOESD</li> </ul> <p>Main beneficiary of the Report:</p> <ul style="list-style-type: none"> <li>• MOESD to make adjustment in the policy creation process and actions</li> </ul> <p>Communications:</p> <ul style="list-style-type: none"> <li>• Presentation of the MOESD senior management</li> <li>• Presentation with relevant stakeholders from Government, MOESD, donors and beneficiaries</li> <li>• Making Report publicly available</li> </ul>
<p><b>Implementing evaluation Findings:</b> WHAT and WHEN should be implemented? HOW do we monitor progress?</p>	<p>Regular reporting on the Acton Plan implementation for the Administration of the Government of Georgia</p> <p>Findings should be used for Improvement of the policy creation, implementation and control in order to enhance further development of SME sector in Georgia</p>

## Background and main trends during AP implementation

### *Introduction*

In 2016, Government of Georgia adopted Georgia's SME Development Strategy 2016- 2020 and relevant Action Plan with the stated objective of supporting the development and economic role of SMEs. The strategy identifies 5 essential directions and relevant priority actions to be taken in important areas for SME development, such as improving legislation, institutional frameworks, and the operational environment, as well as widening access to finance, developing entrepreneurial skills, broadening internationalization, and supporting innovation activities (Fig.1).

**Figure 1. Framework for SME Development in Georgia**



Following the adoption of the SME Development Strategy 2016-2020, the MoESD drafted the Action Plan 2016-2017 and started implementing SME policy reforms. At the end of 2017, in accordance with findings of 2016-2017 AP's monitoring of implementation, the government approved an Action Plan for the next 3 year (2018-2020) as well.

All Strategic directions are crucial to be addressed to provide promotion of the development of the small and medium businesses, facilitate their growth and competitiveness, which is vital for employment growth and creating new employment opportunities, also for strengthening SMEs position on local and international markets.

### *Economic and policy developments since 2015*

Economic growth in Georgia has been steady over the past years. Real GDP growth picked up in 2017, reaching 5%, after two consecutive years below 3%, led by the trade, construction and transport sectors in an improved external environment. Exports of goods expanded by 24% compared to 2016 on the back of stronger demand from Russia, Azerbaijan, Ukraine, China and the United States, while exports of services improved by 20%, mostly due to the tourism sector (WB, 2018). Overall, since 2009, Georgia has experienced the strongest growth among countries in the European Union's "Eastern Partnership" (EaP)<sup>3</sup> and can be considered the most resilient economy in the EaP region.

Georgia is doing well in international rankings, having now entered the top ten in the World Bank's Doing Business report. Georgia's position improved by 18 positions since 2016 and now ranks 6<sup>th</sup> out of 190 countries. Georgia is in the world's top ten countries in the following four categories: starting a business (2<sup>nd</sup>), protecting minority investors (2<sup>nd</sup>), registering property (4<sup>th</sup>) and enforcing contracts (8<sup>th</sup>) and has not left the World Bank Top Improver classification since 2003, with a total number of 47 institutional and regulatory reforms carried out.

According to the Index of Economic Freedom 2018 (Heritage Foundation), Georgia ranks 16<sup>th</sup> out of 180 countries worldwide and 9<sup>th</sup> out of 44 countries in Europe, with a substantial improvement in property rights, judicial effectiveness and fiscal health. Fraser Institutes' Economic Freedom of the World 2018 puts Georgia in the list of top ten countries, ranking 7<sup>th</sup> out of 162. Moreover, Georgia has a free trade regime with one third of the world population, having in force free trade agreements with the Commonwealth of Independent States, Turkey, the European Union, the European Free Trade Association, China and Hong Kong.

These considerable improvements are the result of Georgia's sustained and committed efforts to improve the business environment and increase investments over the past years. The government conducted a plethora of major reforms including simplifying the tax system, streamlining customs procedures, and combatting corruption, turning the country into an important destination for future investors.

The outlook is positive, as the EU-Georgia Deep and Comprehensive Free Trade Area (DCFTA) and Association Agreement (AA) are likely to further boost the country's economy, building on considerable efforts from Georgia to put in place a solid national awareness raising campaign to make the most out of these agreements.

SMEs have been a prominent item in the overall socio-economic reform agenda of the government. The OECD has supported this process by assessing Georgia's SME policies since 2012 in the framework of the Small Business Act Assessment in the EaP region. In its latest edition published in 2016 - "SME Policy Index in Eastern Partner Countries 2016" Georgia is a top reformer country amongst EaP Countries and has made significant improvements to its institutional framework for SME policy. According to this evaluation based on the 10 principles of the Small Business Act (SBA), Georgia received the highest scores amongst the Eastern Partnership countries in 7 out of 12 dimensions (these 7 dimensions are: Small and medium Business Environment, Public Procurement, Access to finance for SMEs, Entrepreneurial Learning & Women Entrepreneurship, Entrepreneurial skills, SME in Green Economy and SME

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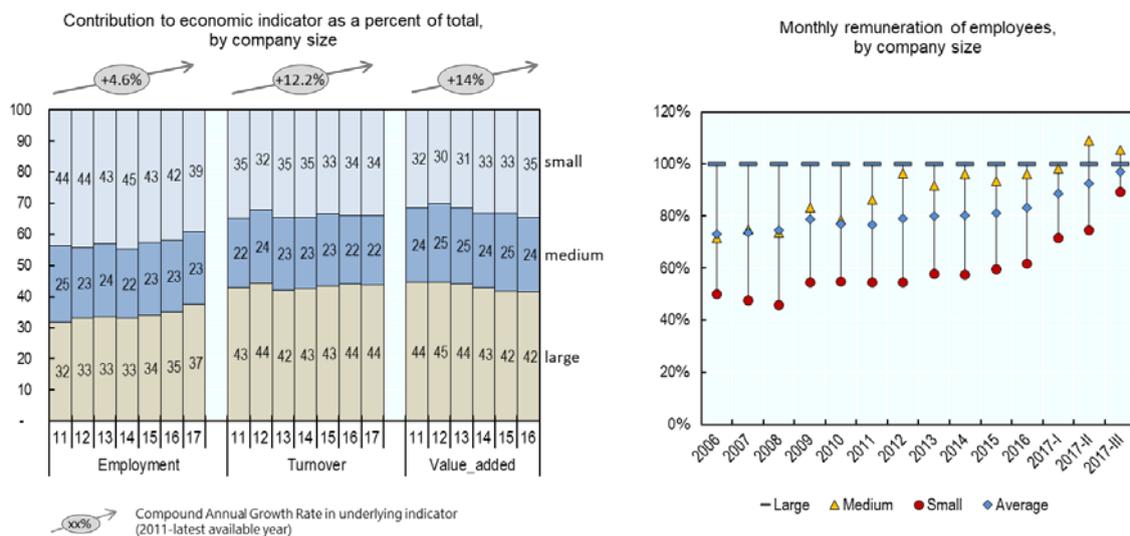
<sup>3</sup> Armenia, Azerbaijan, Belarus, Georgia, Moldova and Ukraine.

internationalization).

### *The SME sector in Georgia*

Under the recently adopted new definitions and methodology<sup>4</sup>, 99.7% of all firms in Georgia in 2017 were SMEs, accounting for 62% of total employment and 56% of total business sector turnover; in 2016, SMEs generated 59% of gross value added. SMEs' contribution to the economy is increasing in absolute terms, thanks to a steady growth in underlying indicators since 2011 (Figure 2). This trend is also accompanied by an increasing quality of jobs created, with remuneration in SMEs on a clear trajectory of catch-up with large firms.

**Figure 2. The role of SMEs in Georgia's economy, 2011–2016/17**



Source: Geostat (2018a), "Business Statistics" (database)

As for the sectoral distribution, SMEs tend to be concentrated in low value-added sectors, such as trade (including repair of vehicles), manufacturing and construction, representing respectively 14.7%, 7.2%, and 10.4% of contribution to total value added in 2016. Geographically, almost half of all SMEs are located in the capital, while the rest are distributed mainly in the three larger regions of Georgia: Imereti (14%), Adjara (8.6%) and Samegrelo-Zemo Svaneti (8%) (Geostat, 2017).

Measurable targets were set out in the SME Development Strategy to be achieved by 2020, namely:

- Growth in SME output by average 10% annually;
- Growth in the number of employees in SMEs by 15%; and
- Productivity growth (value added / number of persons employed) by 7%.

<sup>4</sup> New definition of SME that is stipulated by new methodology of GEOSTAT. Namely, a large enterprise is an enterprise in which the average annual number of employed exceeds 249 persons and/or volume of average annual turnover exceeds GEL 60 million. Medium-sized enterprises are all enterprises in which the average annual number of employed ranges from 50 to 249 persons and average annual turnover ranges between GEL 12 million to 60 million. Small-sized enterprises are enterprises in which the average annual number of employed does not exceed 50 persons and average annual turnover GEL 12 million.

### ***Main stakeholders in charge of SME policy implementation***

Numerous stakeholders are involved in the implementation of SME policy reforms, with the most prominent roles being played by the entrepreneurship development agency *Enterprise Georgia* and the *Georgian Innovation and Technology Agency* (GITA), both of which fall under the authority of the Ministry of Economy and Sustainable Development.

The MoESD is in charge of setting the overall priorities and goals of SME policy, distributing roles and resources among stakeholders, and monitoring the implementation process.

Enterprise Georgia was established in February 2014 and is in charge of the implementation of SME support programmes. The main aim of Enterprise Georgia is to develop entrepreneurship by supporting the establishment of new enterprises, expanding existing ones and promoting entrepreneurial culture in the country. Based on three main pillars – Business, investment and export – the agency focuses on increasing private-sector competitiveness, enhancing Georgia’s export potential and promoting foreign direct investment in Georgia. Its flagship programme offering support to SMEs is called *Produce in Georgia* (Box 1).

GITA was established in February 2014, with the goal of creating an innovation eco-system within the country in order to support start-ups and R&D, especially in the ICT field. GITA focuses on the development of innovation infrastructure, such as technology parks, innovation centres and industrial laboratories, whilst also keeping an eye on the commercialisation and export potential of innovations and new technologies. Alongside plans to improve internet speed and access, including coverage in remote regions of Georgia, GITA aims to promote innovative business development with a particular focus on entering international markets. Beneficiaries of GITA, apart from receiving financial support, obtain assistance and trainings in a range of business areas.

Other stakeholders, such as relevant line ministries, the Georgian Chamber of Commerce, the National Bank of Georgia, various business associations, universities, research centres, the civil society and donors are involved in the implementation of SME policy reforms.

## Evaluation of implementation of main directions of SME development Strategy of Georgia

### **The First Strategic Direction: Further improvement of legislative, institutional framework and operational environment for SMEs**

#### **Improvement of procedures for closing business and insolvency**

**Relevance** – Existing insolvency proceedings/closing business is one of the obstacle for SME’s. Simplification of it is issue of great importance, as it will support companies to move from inefficient into efficient businesses, increase recovery rate, which is comparatively low in Georgia, according to Doing Business evaluation. Improvement of procedures for closing business and insolvency is valid and actual for further improvement of legislative, institutional framework and operational environment for SMEs. As a result, it complies with set goals and Government priorities.

**Effectiveness** - The government has been involved in a series of initiatives to support the improvement of business closure and insolvency procedures. A working group organized by the Ministry of Justice (MoJ), with the support of GIZ and participation of the Ministry of Finance and the Ministry of Economy and Sustainable Development as well as private practitioners, has assessed the existing legislation and identified areas for improvement.

Meanwhile, amendments to the Law on Insolvency Proceedings were adopted by parliament in May 2017. Alongside an in-depth study of international best practices, the working group has developed a new draft law, with the objective of further increasing the efficiency and transparency of insolvency proceedings by establishing flexible tools for rehabilitation as well as liquidation, increasing the role of courts in insolvency proceedings and granting creditors greater participation in important decisions (e.g. debtor’s reorganisation plans). RIA of the draft law is conducted. In addition, the MoJ has already started public discussions in order to collect feedback and comments on the draft law – in this regard, introducing a framework for efficient out-of-court insolvency settlements could also be considered.

**Implementation** - “Performance indicators” corresponding to the Improvement of procedures for closing business and insolvency were performed in 2016 - 2017. In particular, the amendments were made by the Government of Georgia to the law of Georgia on “Resolving insolvency proceedings”; The draft law of Georgia on Insolvency Proceedings was developed;

#### **“Updating the definition of small and medium size enterprises” and “Improving Business Statistics”**

**Relevance** - Introduction of a new SME definition with consideration of current level of economic development of Georgian companies, as well as to align it with the International and European criteria will support the collection of more accurate statistics on enterprises and enable the design of targeted SME support efficient policies and activities. Besides, improved SME statistics will lead to the collection of more detailed information on enterprises that will enable policy-makers to better analyse SME performance and design effective policies and measures for fostering SME development. Thus, these measures are actual and in compliance with public needs as well as with Government priorities;

**Effectiveness** - Geostat, the National Statistics Office of Georgia, has recently revised the SME definition to comply with European Union standards and increase international comparability. The new Georgian definition comprises both the number of employees, as well as the total turnover of the company.<sup>3</sup> Geostat has recalculated business statistics indicators according to the new definition since 1999 to allow for easy comparison and a smooth transition. Economic indicators with breakdown according to the old definition will be kept alongside the new one for another year.

The new definition<sup>5</sup> enabled the government to obtain a more realistic idea of the weight of large companies in the Georgian economy. On the new definition, there are just 350 large companies, as compared to 4 000 on the old one. According to the previous definition, large companies in 2017 generated 82% of total turnover and 78% of value added. On new definition however, the share in total turnover is 44% and that of value added 42% (Geostat, 2018a). Herewith, according to GEOSTAT' data, in 2016 output of SME amounted to 58.4% and 59.2% in 2017, while number of employees in 2016-2017 constituted 67.0%. Value added of SME amounted to 58.4% and 61.6%, respectively, in 2016 and 2017.

Following the adoption of the SME strategy 2016-2020, Geostat has further made a substantial effort at improving SME statistics collection and dissemination. The Statistics Office performs quarterly surveys of 12 500 companies and annual surveys of 15 500. The surveys aim at collecting data on the number of employees, wages and geographical location of business entities, as well as business ownership disaggregated by gender.

Furthermore, Geostat has developed a Geographic Information System (GIS) for the dissemination of business statistics, where, through an online tool, users can analyze comprehensive business statistics by region.

**Implementation** - "Performance indicators" corresponding to Updating the definition of small and medium size enterprises and Improving Business Statistics were fully performed in 2016 - 2017. In particular, the definition of small and medium sized enterprises was elaborated, Consultations with stakeholders were conducted; The recommendations for expanding the scope of business statistics have been developed; The existing scope and methodology of business statistics have been expanded and Published statistical data.

### "Strengthen SME support institutions"

**Relevance** - Strong SME support institutions will greatly contribute to the development of the SME sector and support the enhancement of their competitiveness. Thus, this is the measure which plays important role for further Development of SME and respectively is in compliance with set goals, beneficiaries needs and GoG priorities;

**Effectiveness** - Entrepreneurship Development Agency (Enterprise Georgia) actively works on analysis and implementation of success cases of other similar organizations from around the world.

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<sup>5</sup> Old SME definition used by Geostat: Medium-sized enterprises employ up to 100 employees and have a turnover of up to GEL 1.5 million (≈ EUR 500 000) annually. Small-sized enterprises employ up to 20 employees and have a turnover of up to GEL 500 000 (≈ EUR 170 000) annually.

New SME definition used by Geostat, according to EU standards: Medium-sized enterprises employ up to 250 employees and have a turnover of up to GEL 60 million (≈ EUR 20 million) annually. Small-sized enterprises employ up to 50 employees and have a turnover of up to GEL 12 million (≈ EUR 4 million) annually.

With this aim, EDA visited western European and eastern Asian organizations orientated on entrepreneurship development. In addition to this In order to Strengthen of SME support institutions analysis of SME supporting institutions were held and SME needs were analyzed. Besides analysis of international experience and best practices were conducted.

One of the most important EDA's everyday activities is SME needs assessment. For this reason, thematic meetings are held with representatives from different economic sectors. Their challenges are identified and they are offered with respective support. Capacity building trainings are constantly organized for EDA and its capacity are growing constantly.

In 2016 number of international MoUs were signed, with the aim to initiate or deepen partnership between Georgian Innovation and Technology Agency (GITA) and international organizations supporting startup and innovation ecosystem. GITA studied the best practice of the start-up and SME support institutions of the following countries: USA, China, Germany, Estonia, Israel, UK, South Korea and Netherlands. The knowledge gained as a result, GITA has applied in its activities. GITA studied business incubation and acceleration management in the US and with the gained experience, for the first time, GITA had coordinated business incubator and accelerator project in 5 Universities.

The MOU was signed in October 2016 for establishing IAC Georgia, with Tallinn Technology University (TTU) Mektory technological park for promoting the joint R&D and startup activities. In the framework of MoU, it is planned to open Georgian startup and cultural room at Mektory, Estonia.

GITA's representatives held a visit in London with the aim to study 1. Crowdfunding platforms and its regulation; 2. Technology Transfer Center model; 3. Financing and management mechanisms for innovation; 4. Catapult system. All experience gained during the visit enhanced GITA's capacity.

**Implementation** - "Performance indicators" corresponding to Strengthening of SME support institutions were performed in 2016 – 2017. In particular, Needs analysis were identified with the aim of improving the functioning of SME's supporting institutes; Projects of relevant Normative Acts were elaborated and submitted to GoG (Based on reorganization of LEPL "Entrepreneurship Development Agency" LEPL "Enterprise Georgia" is created); SME needs based services were introduced; Meetings were arranged with SME support institutions; Unified front office of SME's state supportive programs under the umbrella of LEPL "Enterprise Georgia" were created.

### "Strengthen Public-Private Dialogue"

**Relevance** - The introduction of an institutional platform for PPD is one of great importance as it will help the government to develop effective policies for SMEs and eliminate obstacles to SMEs growth and development. Effective PPD will support building trust between the government and private sector, possibility to analyse problems jointly and identify policies and institutional reforms that will contribute to a more conducive environment for private sector development. Regular and structured dialogue with private sector will create the basis for creation more predictable environment and ensure that private sector perspectives are taken into account. Thus this is the measure that is really actual and in compliance with SME's needs, set goals and GoG priorities;

**Effectiveness** - Private Sector Development Advisory Council (PSDAC) was established in 2016. It operates under the supervision of the MoESD, with a Deputy Minister serving as Chair and a private sector representative serving as Deputy Chair. The bi-annual PSDAC meetings therefore formalise public-private consultations, raising awareness on ongoing and planned reforms, and providing the private sector, including SMEs and SME associations, with an opportunity to comment on entrepreneurship barriers and business- related legislation.

Additionally, the website [matsne.gov.ge](http://matsne.gov.ge), established by the Legislative Herald under the Ministry of Justice, provides users with an access to all normative acts adopted by state agencies and enables public review of draft reforms. A dedicated web-portal with information about planned and implemented reforms under the DCFTA has also been created in 2017 by MoESD ([dcfta.gov.ge](http://dcfta.gov.ge)), with, among other functions, the opportunity to comment on draft legislative acts uploaded on the portal.

As a result, private sector increased awareness in terms of ongoing and planned reforms. Besides, GoG became more aware of problems of SME's from the side of business.

**Implementation** - “Performance indicators” corresponding to Strengthening of Public-Private Dialogue were performed in 2016 – 2017. In particular, Private Sector Development Advisory Council was established with the aim of deepening cooperation between public and private sector; Regular meetings of the PSDAC are held.

### “Establishment of RIA system for priority economic legislation”

**Relevance** – In order to avoid imposing disproportionate burden on SMEs, as well as lead to elimination of existing regulations which are burdensome for SMEs, establishment of a RIA is issue of great importance. As facilitation of business environment inter alia in terms of legislation is one of the main priority of GoG and respectively, of economic policy, establishment of a RIA is in full compliance of it.

**Effectiveness** - Regulatory impact assessment (RIA) initiatives have started in 2007, when the MoESD established an RIA Unit and began to promote the assessment process in Georgia. Throughout the years, the RIA Unit, together with line ministries, has participated in several trainings and seminars on required methodology and institutional set-up. Recently, the country has made important steps towards developing a full-fledged RIA system and procedures.

A national legislative RIA framework document has been prepared by the USAID project “Governing for Growth” in close co-operation with the private sector and academia and discussed in parliament, including recommendations on the institutional framework, criteria to identify regulations subject to RIA, the RIA methodology and capacity building needs of local institutions to effectively implement RIA. On its basis, the Government of Georgia elaborated a draft law aiming at making RIA legally binding. In addition to the above, RIA guidelines and manuals were elaborated, establishing the framework of the RIA methodology. Once the draft law adopted, a quality control unit will be created inside the government.

Besides the fact that the legislative framework was not adopted, pilot RIAs have been carried out for various draft laws such as the Draft Law on Consumer Protection, the draft on Environmental Assessment Code and the draft Criminal Procedure Code. It should be noted that, RIA on the Law on Consumer Protection caused implementing changes in the mentioned draft law and it became more effective. Besides, based on RIA elaborated new draft law met the EU Directives requirements. The same results caused RIA on the draft on Environmental Assessment Code and on the draft Criminal Procedure Code.

Regularly assessing potential impacts of new regulations on SMEs, including costs and benefits according to the EU “Think Small First” principle, remains a challenge. Ad-hoc SMEs tests have been carried out for selected laws, but at present, limited institutional capacity and financial resources at the centre of government and in relevant line ministries and agencies prevent a systematic approach to carry out full-fledged “SME-tests”. However, trainings and seminars for line ministries were conducted to increase institutional capacity in this regard.

**Implementation** - “Performance indicators” corresponding to the establishment of RIA system for

priority economic legislation, were performed in 2016 – 2017. In particular, RIA institutional mechanism and legislative framework document were elaborated.

## *Way forward*

### **Introduce SME-specific regulatory impact assessment**

1. Regulatory Impact Assessment remains an important area of future improvement for SME policy. In 2015, the OECD recommended the introduction of a formal RIA mechanism to measure the impact of new legislation on small and medium sized companies. While monitoring the implementation of the SME strategy, discussions between the Ministry of Economy and Sustainable Development and the OECD revealed that additional action is required in the sphere of RIA and its role in improving the institutional framework and operational environment for SMEs.
2. While the legislative framework awaits approval, pilot RIAs have been carried out for various draft laws such as the Law on Consumer Protection, the Law on Electricity Trading Mechanisms or the draft Environmental Assessment Code.
3. Regularly assessing potential impacts of new regulations on SMEs, including costs and benefits according to the EU “Think Small First” principle, remains a challenge. Ad-hoc SMEs tests have been carried out for selected laws, but at present, limited institutional capacity and financial resources at the centre of government and in relevant line ministries and agencies prevent a systematic approach to carry out full-fledged “SME-tests”. However, trainings and seminars for line ministries are planned in the near future to increase institutional capacity in this regard.
4. Building on the pilot RIAs that have been carried out for the above-mentioned draft laws, developing an SME-specific RIA test is an essential element of the policy making process and will enable the government to design specific tools to ensure that proposed legislation (new or amended) will not impact disproportionately SMEs.
5. The European Union’s *Small Business Act for Europe* (European Commission, 2014) and its “Think Small First” principle recommend that policy-makers take into account the impact of legislation on small businesses through a dedicated “SME-test”. Drawing on EU examples, Georgia could develop its unique SME test and designate a central entity to support its development and implementation.

## **Strategic Direction 2: Enhance access to finance for Georgian SMEs**

### **Amend the legal framework on public grants**

**Relevance** – Grant financing is one of the priority direction in order to improve SMEs access to finance. Respectively, improved legislative framework for this purposes will support the attraction of finances for R&D and innovative growth by SMEs and in general SME's Development. Respectively, the measure is actual and comply with the goal.

**Effectiveness** - The Law on Grants, which previously limited the scope for targeted financial assistance to SMEs and innovative start-ups, has been revised and amendments have been adopted in 2016. Following the revisions, state agencies such as Georgia's Innovation and Technology Agency or Enterprise Georgia's Produce in Georgia programme (Box 1) have been authorized to award public grants, exempted from relevant taxes, to private commercial entities.

**Implementation** - "Performance indicator" corresponding to the Amendment the legal framework on public grants, were performed. In particular, amendments were made to the state program "Produce Georgia" with the aim of further improving access to finance.

#### **Box 1**

##### **Enterprise Georgia's state programme *Produce in Georgia***

The state programme *Produce in Georgia* was launched in May 2014 as part of Georgia's strategy to support the development of the private sector, and SMEs in particular. The programme aims at facilitating the development of manufacturing industries, as well as the establishment of new enterprises and the growth of existing ones.

The programme is supervised by the Ministry of Economy and Sustainable Development of Georgia (implementing agencies: Enterprise Georgia, National Agency of State Property) and the Ministry of Agriculture of Georgia (implementing agency: Agriculture Projects Management Agency).

Under *Produce in Georgia*, Enterprise Georgia supports access to finance in form of co- financing of the interest rate on commercial loans during the first two years. A collateral guarantee of up to 50% of the loan is included in that financial support. The programme is implemented in cooperation with all major commercial banks and leasing companies in Georgia.

In 2015, within the framework of *Produce in Georgia*, the government introduced a sub-programme "Support to Micro and Small Businesses", which aims at developing enterprises with a blended approach combining financial assistance mechanisms (matching grants with a contribution by the beneficiary of at least 20%) with consulting services on business plan development and business administration in order to provide the beneficiaries with the necessary knowledge on modern business practices. The programme covers all regions of the country, except for the capital. Trained and selected project owners receive matching grants of up to GEL 5 000 (~ EUR 1660) (in case of cooperation of maximum 3 people – GEL 15 000 or EUR 5 000) from the government.

Enterprise Georgia received 42 000 applications in 2015-2017, of which 5 300 projects (GEL 38 650 000 or EUR 12 900 000) were selected to benefit from the grant scheme.

Overall, since its inception, *Produce in Georgia* mobilized private investment of around EUR 320 000 000 and contributed to the creation of more than 15 000 jobs.

*Sources: Enterprise Georgia's report, Produce in Georgia; OECD (2018a), Financing SMEs and Entrepreneurs 2018: An OECD Scoreboard*

## Promote demand-side financial education programmes targeting SME entrepreneurs

**Relevance** – The improvement of financial literacy will facilitate to raise the awareness about existing requirements on financial market, financial products and liabilities. This will support companies to make efficient financial decisions for further growth and development. Promote demand-side financial education programmes targeting SME entrepreneurs is an issue of great importance and actual as well as in compliance with goal.

**Effectiveness** - A number of agencies involved in the implementation of the SME strategy have sought to provide tools to improve financial literacy among entrepreneurs. The work of the National Bank of Georgia (NBG) in this area, and in particular its recently created division for Financial Education within the Department of Consumer Protection, is particularly noteworthy.

In 2016, NBG elaborated and disseminated educational brochures for SMEs through its website and local banks. The initiative aimed at explaining a variety of financial concepts and tools relevant to running a business, focusing, among other things, on foreign exchange risk and different types of debt instruments. To expand the coverage and complement the lessons conveyed by the brochure, the NBG is currently working on developing a broader guidebook and training module for micro and small enterprises<sup>6</sup>. These tools are focused on financial decision-making and interacting with financial institutions, with outreach activities in the regions, as well as additional financial education projects, targeting different segments of the population.

More broadly, the NBG has led the effort to measure financial literacy across the country. The Bank conducted a countrywide study on financial literacy and inclusion in 2016, based on the 2015 OECD/INFE toolkit for Measuring Financial Literacy and Financial Inclusion. The results of the study served as a baseline for the 2016 National Strategy on Financial Education, targeting SMEs as part of the broader population. The strategy aims, among other things, to introduce financial literacy in schools, through close collaboration with the Ministry of Education and Science.

The Ministry of Finance, and especially the Service for Accounting, Reporting and Auditing Supervision (SARAS), is currently involved in designing and implementing the operational and legal framework for SMEs to produce financial statements in accordance with International Financial Reporting Standards for SMEs (IFRS for SMEs). This new system, will allow them to submit financial statements through a simple online procedure, increasing the transparency and accountability of enterprises. To complement this effort, the Ministry of Finance, in co-operation with the World Bank, EBRD, Georgian Chamber of Commerce, accounting organizations, business and banking associations, is carrying out awareness raising campaigns for accountants, CFO/CEOs and business owners throughout the country. Additionally, manuals for tutors and more than 20 training modules have been developed to help SMEs prepare financial reports in accordance with IFRS for SMEs.

Enterprise Georgia has also made significant efforts to improve the level of financial literacy among SMEs. Within the framework of the *Produce in Georgia* programme and its micro and small business support component (Box 1), the organisation provided training courses to around 14 500 beneficiaries throughout 2016-2017. The training included basic principles of financial literacy such as the preparation of business plans, business administration and accounting.

**Implementation** - “Performance indicators” corresponding to the promoting demand-side financial education programmes targeting SME entrepreneurs, were performed fully. In particular, needs of SMEs in financial literacy were identified and trainings were conducted for them; Awareness Training modules of IFRS for SME was prepared and trainings was conducted for SME;

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<sup>6</sup> The OECD/International Network on Financial Education (INFE) is developing a Core Competencies Framework on Financial Literacy for MSMEs, which could be used as an important source of inspiration for developing dedicated financial education initiatives for SME and entrepreneurs. ([www.oecd.org/finance/financial-education/](http://www.oecd.org/finance/financial-education/))

### **Increase knowledge on fund raising among SMEs and support to SMEs to increase access to finance**

**Relevance** – Raising the levels of SMEs’ knowledge and capacity in fund raising is essential for SME development and growth, as their knowledge about attraction of additional financial resources is limited. Thus, Support to SMEs to increase knowledge on fund raising and as a result, to increase their access to finance is one of the priorities of Georgia’s economic policy. This is the measure, which is quite actual for further development of SME and respectively in compliance with goal and needs of beneficiaries.

**Effectiveness** - In 2016-2017, information meetings in fundraising issues were held for businessmen and the participants of 19 teams of Business Incubator **were trained on fundraising topics.**

In 2017 the roundtables/discussions were held between the parties for the identification of obstacles to financing small and medium enterprises to reduce them in the future. **In 2016-2017, 5 roundtables/discussions were held to identify obstacles to financing small and medium enterprises.**

While credit conditions are generally improving (Box 2), high collateral requirements (up to 200% of loan value) and interest rates (at around 19% in local currency and 10% in foreign currency) still make it difficult for Georgian SMEs to borrow from banks. Due to information asymmetries between lenders and borrowers, land and real estate are the preferred forms of collateral demanded by banks, but SMEs are typically undercapitalized and innovative start-ups predominantly own mainly intangible assets.

Partial collateral guarantees are available under the state programme *Produce in Georgia*. Tailored to the specific stages of enterprise development and financial needs of the business, *Produce in Georgia* offers partial collateral guarantees of up to 50% of the loan amount (up to GEL 2 500 000 or EUR 850 000). Eligible loans are provided by 12 partner banks and must be in national currency since 2017.

A credit guarantee scheme in close co-operation with international financial institutions (IFIs) should be the future steps in order to increase accesses to finance for SME’s. The credit guarantee scheme intends to address specific market failures, which prevent credits from being issued to commercially viable businesses due to insufficient collateral. The mechanism is designed to support risk diversification, credit supply growth and reduction of interest rates, with a subsequent positive impact on economic growth.

**Implementation** - “Performance indicators” corresponding to the raising the levels of SMEs’ knowledge and capacity in fund raising, were performed fully. In particular, Using alternative sources of financing (alternative funds, IFI funds, donors programmes) for SMEs were assessed as well as information meetings, *inter alia*, individual meetings, were held for entrepreneurs in fundraising Issues.

### **Improve alternative non-bank and equity financing for SMEs**

**Relevance** – Attraction of SME-oriented private equity funds in Georgia will support improvement of SMEs’ access to alternative sources of finance, company growth, development and competitiveness increase and attraction of venture capital funds will support the start-up development. Respectively, issue of the improvement alternative non-bank and equity financing for SMEs is actual and in compliance with goal.

**Effectiveness** - Precise data on the availability and use of alternative finance instruments is lacking.

However, initial evidence suggests that micro-finance is becoming an increasingly relevant source of alternative finance. As of 2017, there were 80 micro-finance organisations, with over 430 branches, registered in Georgia and supervised by the National Bank. Since 2010, lending by microfinance-organisations to SMEs has grown steadily. By end-2016, the total amount of loans to SMEs in the portfolio of microfinance organisations amounted to GEL 7.7 million ( $\approx$ EUR 2.6 million) compared to GEL 1.7 million ( $\approx$ EUR 570 000) in 2010. The main clients of microfinance institutions in Georgia are non-bankable micro and small enterprises (OECD, 2018a).

In 2017, GITA, in co-operation with Enterprise Georgia and the MoESD, conducted initial research and identified potential foreign venture capital funds to propose alternative finance mechanisms to selected start-ups. As a result, MoESD, in co-operation with IFIs, NBG and MoF, elaborated a draft law “on Investment Funds”, aiming at regulating the establishment, constitution and operation of collective investment schemes<sup>7</sup>, as well as the offer and marketing of such schemes in Georgia, in line with EU directives. In parallel, trainings on fundraising for start-ups are being held.

“Enterprise Georgia” regularly monitors the relevance of the existing financial policy/tools to the private sector needs. Since 2014, Enterprise Georgia has amended/updated portfolio of its financial tools. Furthermore, number of new directions has been added to the initial program’s design, which has been reflected on defined interest rates and also on increasing of partial collateral guarantees from 30% up to 50%. Besides, 2 new directions has been added to the program (hotel industry incentive and film industry incentive program) Implemented changes in financial tools were carried out based on communication with private sector.

With the aim to further improve access to finance within the State Program “Produce in Georgia”, Enterprise Georgia constantly monitors and evaluates the efficiency of existing tools of access to finance, based on which relevant recommendations for improvement of instruments of access to finance will be elaborated.

**Implementation** - “Performance indicators” corresponding to the improvement of alternative non-bank and equity financing for SMEs, were performed fully. In particular, 2 Venture Fund was identified for alternative funding for start-ups; 10 start-ups with investment potential were identified; Round tables/discussions were held to identify the obstacles to financing small and medium enterprises.

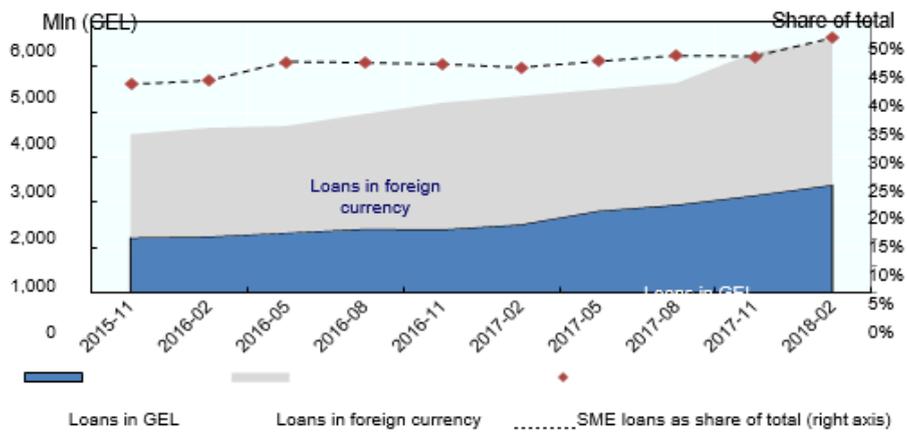
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<sup>7</sup> An arrangement that enables a number of investors to pool their assets with a view to sharing the profits/income from the holding, management or disposal of the assets.

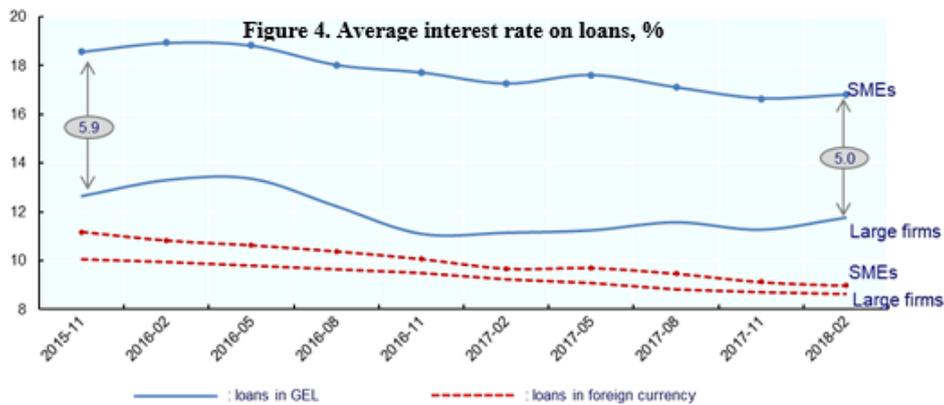
**Box 2. Evolution of SME lending and interest rates**

Bank lending to SMEs is increasing in both absolute terms and relative to large firms. This positive trend is more pronounced for loans denominated in GEL, which have almost doubled in nominal value since 2015, than for loans in foreign currencies (USD, EUR, GBP, RUB). As of February 2018, the stock of outstanding loans issued to SMEs made up 47% of total business loans, up from 38% two years earlier.

**Figure 3. Loans to SMEs**



Falling interest rates are to be considered at least partially responsible for the expansion of SME loans in the portfolios of banks. Most interestingly, the spread of interest rates on loans issued to SMEs vs. large firms is narrowing (i.e. credit conditions are improving), suggesting that the risk factor associated to SMEs is being reduced in the perception of banks.



Note: Loans issued in foreign currency is converted in GEL.  
 Source: analysis based on data from National Bank of Georgia

## *Way forward*

Adopt a co-ordinated approach to improving financial literacy for SMEs.

Several scattered activities are being carried out to improve financial literacy for SMEs, including trainings within the framework of *Produce in Georgia* programmes and the dissemination of educational brochures for business owners and training modules for SMEs developed by the NBG. However, no strategic framework specifically targeting financial literacy of SMEs exists. A dedicated strategy for SME financial literacy, with an action plan including clearly defined roles, responsible implementing institutions, implementation timeframes, a monitoring system and attributed resources, could help Georgia adopt a more co-ordinated approach towards improving financial literacy of entrepreneurs.

As a first step, as a follow-up to the countrywide study conducted in 2016, the NBG could measure financial literacy levels of SME owners using the forthcoming OECD/INFE questionnaire, specifically developed for small and medium entrepreneurs. Georgia could

then take inspiration from the forthcoming *OECD/INFE Core Competencies Framework on Financial Literacy for MSMEs* to select or develop dedicated financial education initiatives.

Raising awareness of the benefits of IFRS could be considered one such initiative. Given the current reluctance of CEOs to report about their financial statements according to IFRS, the Georgian Associations of Banks and SME associations, in co-operation with SARAS and the NBG, could be mobilised to raise awareness among SMEs of the benefits of increased transparency in financial statements, not least in order to get easier access to credit.

Although much has changed since then, continued large interest rate spreads and high collateral requirements would suggest that the case for a credit guarantee scheme (CGS) remains valid today. A CGS works as a risk-sharing mechanism between lenders (banks), borrowers (SMEs) and a guarantor (the state or a private entity). In exchange for a fee paid by the borrower, the guarantor provides banks with the guarantee that it would reimburse a pre-determined share of the outstanding loan in case of default by the borrower.

A CGS could create market-based incentives for banks to lend more to SMEs. By reducing the perceived risk, banks are expected to demand lower collateral and interest rates from SMEs. As a result, more credit is extended to borrowers than otherwise would be the case. Four key elements should be considered when designing a CGS for Georgia:

- ✓ Objectives and eligibility: define the aims of the CGS and the target groups (i.e. SMEs with proven difficulties to access bank loans) to ensure financial and economic additionality, as well as the sustainability of the scheme.
- ✓ Coverage rate: define the amount of risk shared with the bank (i.e. percentage of loan reimbursed in case of default) to encourage lending while limiting moral hazard.
- ✓ Fees: define the fee charged to borrowers (e.g. a percentage of loan amount), which should both cover costs and ensure borrowers' participation in the scheme.
- ✓ Type of CGS: set the organisational structure and governance of the scheme (i.e. public, private, or public-private with international support).

Develop alternative financing tools: Government could promote SME awareness of the alternatives to bank lending, accompanied by training and financial education programmes to ensure the correct use of instruments according to the stage of any given firm's development, and investors (equity investment opportunities). Dedicated awareness-raising events, showcasing the most promising business ideas, could also help attract business angels and support the establishment of an angel investor community, leading to a possible legal framework on angel investment and incentives.

### **Strategic Direction 3: Promote skills development and entrepreneurial culture**

#### **Develop a country-wide labour market and training needs analysis**

**Relevance** - Georgia faces relatively high level of unemployment, despite the decrease of this indicator recently. Job mismatch on the labour market negatively influences employment tendency. In order to reduce existing misbalance between labour market supply and demand, the issue of development of a country-wide labour market and training needs analysis plays important role. Elaboration of training programmes related to matching labour market demand should be based on Survey of labour market needs for SMEs. Thus, development of a country-wide labour market and training needs analysis is really actual and comply with goals.

**Effectiveness** - The Ministry of Labour, Health and Social Affairs (MoLHSA) plays a central role in the effort to develop a country-wide labour market and training needs assessment. The first strategy on employment was thought out in 2013 and implemented in the subsequent couple of years. Within the framework of the strategy, since 2015, services such as career guidance, professional consultations and CV proofreading are being provided. The first labour market survey was carried out in 2015, involving 6 000 companies of different sizes, revealing the most demanded professions in the Georgian labour market.

Based on the findings of the survey, the Ministry of Labour, Health and Social affairs, in co-operation with the Ministry of Education and Science, designed training and re-training programmes for registered jobseekers. Implemented by the Social Service Agency of Georgia, training and re-training programmes were organised in both public and private Vocational Education and Training (VET) colleges throughout 2015-2017, with the aim of continuing until 2020. As a result, out of 2 130 beneficiaries of the programme in 2017, 551 jobseekers found employment by the end of 2017. Comparing to 2016, we have positive picture as in 2016, 1804 beneficiaries were trained and 534 of them were employed after it.

The training and re-training programme also offers a professional internship component, developed and implemented in collaboration with Georgian businesses. These two schemes will be closely monitored, updated and revised with help of regular surveys and consultations with the business community.

In 2016, MoLHSA established a comprehensive Labour Market Information System (LMIS) as an integrated and user-friendly public web portal, aimed at providing updated information on labour market trends, occupational profiles and career guidance for various stakeholders (students, jobseekers, research institutions, governmental bodies, the private sector etc.). Since 2017, the LMIS is administrated by the Ministry of Economy and Sustainable Development, which took over the labour market analysis function from the MoLHSA.

In the area of Training Needs Analysis (TNA), Enterprise Georgia, in close co-operation with the European Training Foundation (ETF), has been playing an active role in setting up relevant mechanisms to assess SMEs' training needs in various sectors. A pilot project was launched in 2016 to assess the hospitality and paper/paper processing/printing and publishing sectors. Enterprise Georgia has developed in-house skills to implement a TNA, including quantitative and qualitative employer surveys, with a participation of 132 companies. The results of the survey were disseminated at various events dedicated to the development of professional education.

**Implementation** - “Performance indicators” corresponding to development of a country-wide labour market and training needs analysis, were performed fully. In particular, Qualitative research of labor market was conducted and the report was prepared; Job seekers gain benefits from the retraining program; Employers were involved in the teaching process; Employees were retrained through retraining and internship, including vulnerable groups; Individual and group consultations were held at Municipal level.

### **Strengthen stakeholder participation in developing and implementing VET policies**

**Relevance** – Partnership between the VET and private sector at the macro, mezzo and micro/institutional level is an issue of high importance as it implies the involvement of the private sector in the process of VET policy formation as well as at the stage of formation and development of VET qualifications and cooperation with and the direct engagement of educational institutions. To support the process with encouraging work-based learning and continuous improvements of training content, infrastructure and methodology is crucial as well. All these are actual and valid for human capital development and respectively are in compliance with goals.

**Effectiveness** - Several initiatives have been put in place with the goal to strengthen stakeholders’, participation in developing and implementing VET policies, with a particular attention paid to the private sector. In particular, dedicated councils on vocational education (National Vocational Education Council, chaired by the Minister of Education and Science of Georgia; Sectoral Councils; Supervisory Councils at college level) rely heavily on private sector and civil society representation, such as employers’ associations and trade unions.

Since 2013, the above-mentioned sectoral councils, operating at the National Centre for Education Quality Enhancement (NCEQE), contributed to the validation of over 200 professional standards as well as to the preparation of framework documents to develop flexible modular VET programmes.

Additionally, the *Vocational Qualifications Development Programme*, carried out by the NCEQE, provides further possibility for the private sector to provide input for VET standard setting. The project follows the DACUM methodology<sup>8</sup>, which requires an equal participation of representatives of large, medium and small businesses. The aim of the programmes is to draw out vocational standards in accordance with employers’ needs.

Finally, with the aim of further modernising VET to meet labour market needs, the MoES has worked out the concept of Work-Based Learning (WBL), with the support of UNDP and GIZ. Since 2016, up to 20 dual technical VET programmes have already been introduced in the agricultural, tourism, railway, transport and construction sectors, ensuring employers’ participation in programme development, student selection and examination processes.

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<sup>8</sup> *DACUM: Developing a curriculum is a storyboarding process to capture the major duties and related tasks included in an occupation, as well as the necessary knowledge, skills, traits and tools the worker uses. (www.dacum.org)*

**Implementation** – “Performance indicators” corresponding to Strengthening stakeholder participation in developing and implementing VET policies were performed fully. In particular, SMEs were involved in Vocational Education Council and thematic groups; Professional standards were developed with the participation of entrepreneurs; Programs were implemented through work-based teaching principle; Trainings were held for teachers and employers related to the work-based teaching.

#### **Improve the quality and attractiveness of VET institutions**

**Relevance** – Improving the quality and attractiveness of VET institutions and increasing relevance of VET programmes for job-seekers is of central concern to the VET reform, carried out by the MoES in the framework of the VET Development Strategy 2013-2020. This is measure that is in full compliance with the goal.

**Effectiveness** - The State Budget to implement the reform of VET system more than doubled from 2013 to 2016, increasing from GEL 13.3 million ( $\approx$  EUR 4.5 million) to GEL 33.7 million ( $\approx$  EUR 11.3 million) (GoG, 2017a).

Both the VET Development Strategy 2013-2020 and the 2016-2017 Action Plan for the SME strategy of Georgia highlight entrepreneurial learning as one of their priorities by including a compulsory entrepreneurship module in VET programmes to facilitate self-employment opportunities. This module is now mandatory in all VET programmes and includes capacity building of teaching staff with the support of various international partner organisations.

The reform of educational programmes also envisioned the transformation of subject-based curricula into modular teaching, aimed at developing particular competencies. This modularisation approach aims not only to promote the flexibility of VET options and thus improve its attractiveness, but also to make the education system more labour market oriented and flexible in terms of improving specific workforce skills.

The attractiveness of state VET colleges seems to be improving, with 11 170 enrolled students in 2016 (an increase of 10% compared to the previous year) and private institutions welcoming 4 469 students (ISET-PI, 2017). According to the 2015 tracer study conducted among 2 591 graduates of 2014, 30% of respondents started a job directly after graduation, 17% of respondents already had a paid job before graduating and the employment rate was at 56% within 3 months after graduation (GoG, 2015). The latest 2017 tracer study, conducted among 3 144 graduates of 2016, shows an employment rate of 56.2% reached within 3 months after graduation and 93% of the respondents were satisfied with their choice of VET institution.

Additionally, MoES launched a Vocational Skills Development Programme in 2017, with an aim to strengthen the collaboration between general schools and VET colleges for the provision of professional orientation services for graduate-level school students. After elaborating a joint project with the VET colleges according to their interest, school students take part in different VET skills development workshops at school with the support of schoolteachers.

**Implementation** – “Performance indicators” corresponding to Improving the quality and attractiveness of VET institutions were performed. In particular, entrepreneurship module in VET programmes were included as compulsory; Attractiveness of state VET colleges improved evidenced by tracer study.

### **Facilitate SME access to non-formal training**

**Relevance** – In order to promote employability and lifelong competitiveness of the workforce in Georgia, streamlined cooperation between stakeholders is important. It is important for the improvement of recognition and trust in the non-formal education and training. Proceeding from this for institutionalization of recognition of non-formal learning, elaboration of rules and mechanisms is an issue of great importance and is in full compliance with set goals.

**Effectiveness** - Non-formal education is yet to be officially recognised in Georgia. In the last couple of years, the MoES, with the support of ETF, analysed the existing regulatory framework and developed a concept of recognition of non-formal learning. Since 2016, a pilot phase has been initiated in three sectors (IT, beekeeping and agricultural machinery mechanics).

As a next step, the government plans to develop a system of recognition of non-formal education. However, the financing of such a system, if opened up to all sectors, would be a major issue. The costs and benefits of recognition are yet to be determined. Ultimately, though, some recognition of non-formal education could support smoother transitions into lifelong learning.

**Implementation** – “Performance indicators” corresponding to facilitation SME access to non-formal training were performed. In particular, draft Methodology of recognition of informal education were elaborated and draft amendments were made to the rule of recognition of informal vocational education.

### **Promote entrepreneurship through formal educational institutions**

**Relevance** – Promotion of a modern entrepreneurial culture and improvement of business skills is crucial for SMEs growth and enhancement of competitiveness. To develop and implement training programs by SME support institutions in cooperation with educational institutions is significant issue. Respectively, measures regarding promoting entrepreneurship through formal educational institutions are relevant.

**Effectiveness** - In 2017, GoG adopted the Unified Strategy of Education and Science 2017-2021 and action plan in an effort to promote entrepreneurship and lifelong entrepreneurial learning. The action plan includes the introduction of entrepreneurial education at all education levels, strengthened by the establishment of FabLabs in 14 colleges to support entrepreneurial innovations and the creation of start-ups. Several start-up projects have since been developed and implemented by VET students and graduates in these Fablabs. Under the umbrella of the MoES, an interagency working group has also been created with the purpose of implementing lifelong entrepreneurial learning in the education system.

Moreover, Enterprise Georgia created a university-private sector partnership platform in order to submit modification suggestions to educational programmes aimed at better meeting the requirements of companies operating in two pilot sectors, ICT and architecture & design.

Additionally, Entrepreneurial Clubs hosted by VET colleges in pilot regions aim to contribute to a smooth transition between education and the workplace. These clubs organised a series of events seeking to inspire young people by, for instance, inviting self-employed IT specialists to speak with and mentor students, encouraging them to create their own business ventures.

**Implementation** – “Performance indicators” corresponding to promoting entrepreneurship through formal educational institutions were performed. In particular, a university-private sector partnership platform was created; Introduction of entrepreneurial education at all education levels, strengthened by the establishment of FabLabs.

#### **Support women’s entrepreneurship**

**Relevance** – To promote inclusive growth, it is important to reinforce female entrepreneurship. Women are less active in entrepreneurial activities rather than men so it is important to develop specific mechanisms to stimulate deeper involvement of women in entrepreneurial and economic activities. Taking into account all the mentioned Support women’s entrepreneurship is an issue that is in full compliance with set goals.

**Effectiveness** - The government has taken initial steps within the framework of the SME strategy to support women’s entrepreneurship. The creation of a sub-council for women’s entrepreneurship under the Private Sector Development Advisory Council lays the ground for establishing an institutional framework to support the promotion of women in business in Georgia and gradually close the gender gap in entrepreneurship. Moreover, the main implementing actors of the SME strategy have taken steps across several ongoing projects to support women-led businesses.

In 2016-2017, GITA was involved in the project “Strengthening Women’s Entrepreneurship”, including a visit of 200 women to the Technopark and an introduction to the possibilities and support offered to women entrepreneurs by GITA.

Enterprise Georgia introduced some preferential treatments for women in the selection process for the Micro and Small Business Support programme under *Produce in Georgia*: in case of limited resources, when two SME businesses, one led by a women and the other by men, apply for financial support and fulfil the same criteria, the women-led venture will be chosen over the men-led one. Women entrepreneurs amount to 40% of the programme’s beneficiaries in 2016-2017.

**Implementation** – “Performance indicators” corresponding to the Support of women’s entrepreneurship were performed. In particular, Gap assessments and needs analyses of women’s involvement in businesses were conducted; Development of mechanisms for promotion of women entrepreneurship were elaborated and Support to female participation in SMEs support state programs was implemented; As a result of these activities, women’s involvement in businesses increased.

### *Way forward*

To proceed with the conduction of labour market surveys, inter alia, labour market surveys of priority economic sectors in order to create relevant statistical data series for anticipation and creation basis for evidence based policy.

Considering the relatively low share of new enterprises created by women and their reduced willingness to take entrepreneurial risk in comparison to men, more effort seems to be required to further develop targeted policies to seize the potential of women's entrepreneurship across the country.

Government could go a step further and consider increasing the institutional reach of the sub-council for women's entrepreneurship promotion by reporting on progress achieved and discussing priorities for the future with the Gender Equality Council of the Parliament of Georgia.

Separate Action Plan on promoting women's entrepreneurship could be designed.

## **Strategic Direction 4: Support SMEs' internationalisation**

### **✚ Improve export promotion activities and export-related skills amongst SMEs**

**Relevance** – Promotion of export and export-related skills amongst SMEs have the utmost importance for enhancement of competitiveness of SMEs. Thus, it is crucial issue and in full compliance with set goals.

**Effectiveness** - Since approval of the SME Development Strategy 2016-2020, Enterprise Georgia has identified a number of priority markets and (sub-) sectors with high export potential, based on consultations with the private sector, revealed competitiveness and increasing demand for Georgian products. The markets include China, USA, Japan, UAE, Saudi Arabia, Germany, France, Italy, Poland, Great Britain, Norway, Sweden, Latvia, Lithuania, Estonia, Denmark, Czech Republic, Hungary, Netherlands and Switzerland. The sectors considered having the highest export potential are food, beverages, light industry, ICT, business consulting, architecture and design.

Enterprise Georgia has further worked on developing new tools to support SME export promotion. Of particular interest is the export readiness test, which assesses the marketing abilities and competencies of the company to access foreign markets. With the help of such tool, the agency identified eight companies with high export potential and supported them in starting to export to the Baltic countries and Poland.

Additionally, Enterprise Georgia developed and launched export management courses, which to date have enabled up to 140 companies to strengthen their export skills and increase their readiness to access foreign markets. Beneficiaries of the agency can also participate in free-of-charge masterclasses on various topics such as branding, PR, how to sell in Europe, project planning and implementation, IFRS and business management.

A significant effort has been made to help Georgian enterprises establish international trade relations. The involvement of Enterprise Georgia, GITA and the Georgian Chamber of Commerce and Industry (GCCCI) with the Enterprise Europe Network (EEN) has offered a number of opportunities to introduce Georgian SMEs to foreign markets. As a first step, two information days were held in 2017 to raise awareness of SMEs and start-ups on EEN possibilities, including information on technical requirements to export and business opportunities in Europe. Following that, new SMEs with high export potential were registered on the EEN platform and as a result, over 30 Georgian companies have received business offers from European companies, with three successful partnership agreements and five of them being in the negotiation process to start co-operation.

In parallel, Enterprise Georgia, in co-operation with GIZ, is active in supporting SMEs in pilot sectors such as furniture, apparel and film post-production, to develop a cluster approach in order to meet the quality and quantity demands of international markets. Moreover, the agency upgraded its *Tradewithgeorgia* website, offering comprehensive information on export-oriented Georgian companies to interested foreign buyers.

GCCI is another actor that has worked to introduce Georgian SMEs to foreign markets. The Chamber organised six business forums abroad as well as 14 forums and two fairs in Georgia throughout 2016 alone. Alongside the EU market, the Chamber is involved in the promotion of the “Belt and Road Initiative”, collaborating on several occasions with China. Examples of

these bilateral projects include the custom warehouse in the city of Yiwu where Georgian goods are stored, the creation of 10 “Georgian Houses” in China and the soon to be opened Silk Road Information Centre in Georgia.

As a result, there is positive trends in terms of export. In particular, according to GEOSTAT, in 2016 export amounted to 2,113 mln USD and it increased by 29% and reached 2,735 mln USD in 2017.

**Implementation** – “Performance indicators” corresponding to the improvement of promotion of export and export-related skills amongst SMEs were performed. In particular, activities in terms of improvement of promotion export and export-related skills amongst SMEs, including conducting of sector specific analysis of SMEs export potential, identifying SMEs with export potential by sectors, Elaborating and implementing of supportive instruments (e.g. technical financial).

#### **Provide services to SMEs to adapt to DCFTA requirements**

**Relevance** –To raise awareness on DCFTA requirements and assist the adaptation of businesses to those requirements, it is crucial to be able to maximise the benefits that DCFTA potentially offers to Georgian producers. This is an issue which is also underlined in Georgia 2020: one of the main tasks of the GoG is to support Georgian businesses to enhance competitiveness and to generate products and services, which will be competitive not only on the local market, but also, on the EU and international markets. At the same time, it must be considered, that some regulations covers European markets as well as Georgian markets, which enhance importance of strengthening of companies’ capabilities to meet DCFTA requirements. Conformation to DCFTA requirements for now, is a challenge especially for SMEs, as far as, it requires knowledge of demands of export markets, as well as, additional financial resources for proper development of this requirement. Measures regarding to Provide services to SMEs to adapt to DCFTA requirements are in full compliance with set goals.

**Effectiveness** - While the Government of Georgia is involved in the process of transposing EU regulations and standards, lack of knowledge about the standards and requirements needed to access the single market curbs the willingness of Georgian SMEs to export to the European Union. To improve this situation, DCFTA information centres have been established by GCCI in close co-operation with GIZ in six Georgian regions, with the goal to raise awareness regarding the main provisions of the EU-Georgia Association Agreement and support SMEs in adapting to new legislative changes.

The DCFTA centres provide information on perspectives and requirements to export to the EU, including information on measures taken by the Georgian government to approximate European standards, good practices to access foreign markets and information on grant programmes available to exporting companies. The centres also carry out regular awareness raising campaigns and trainings, based on the needs of local entrepreneurs identified through face-to-face interviews and surveys. In addition to physical centres, MoESD and GIZ launched the web-portal [dcfta.gov.ge](http://dcfta.gov.ge), including a specific DCFTA for Business page, where interested stakeholders can find all abovementioned DCFTA related information. The web-portal was

launched in June of 2017. Statistics shows high increase of visitors to this web-portal. In particular, in 2017 the total number of visitors was 4,873 visitors, and in 2018 amounted to 20,239 visitors.

Moreover, regular public-private roundtable discussions dedicated to the DCFTA implementation process are being conducted throughout the country. Carried out with the support of the EU-funded project “Facility for the Implementation of the Association Agreement”, the roundtables discuss challenges and opportunities of the DCFTA, with an ultimate aim to improve the competitiveness of SMEs on the EU internal market. To further involve the civil society in the implementation process of the agreement, MoESD established a DCFTA Advisory Group, which is proving to be a successful consultation platform to bring together GoG representatives with employers’ and business associations, trade unions and NGOs.

In addition, Enterprise Georgia and the MoESD are conducting DCFTA-related advisory services and trainings throughout the country. By end of 2017, more than one thousand SMEs participated in DCFTA-related discussions. Frequent trainings and seminars are also carried out in various governmental institutions, such as the Competition Agency, the Revenue Service and the Georgian National Agency for Standards and Metrology, building capacity of government staff on DCFTA requirements.

**Implementation** – “Performance indicators” corresponding to the providing services to SMEs to adapt to DCFTA requirements were performed. In particular, Consulting Centres on DCFTA issues were established; The relevant measures have been undertaken to raise awareness about DCFTA’s perspectives and requirements; 305 beneficiaries were supported for adaptation with DCFTA requirements and 108 beneficiaries have been supported for stimulating export of small and medium enterprises only in 2017. The profiles of Georgian companies was registered on EEN platform;

#### **Facilitate linkages between FDI and SMEs**

**Relevance** – Establishment of FDI-SMEs linkages will facilitate inclusion of Georgian SMEs in supply chains and encourage growth and development. Thus, elaboration efficient mechanisms and supportive instruments in order to enable SMEs to meet demand and/or other requirements of investors or large companies, is an issue of great importance. Herewith it is actual and comply with set goals.

**Effectiveness** – Activities aiming to promote the connection of local small and medium sized enterprises with multinational companies operating in Georgia were started. In particular, bilateral meetings between Georgian and foreign businessmen were held. In total, the Investment Agency organised eleven business forums in 2016 and one - in 2017, where about 60 companies were involved. The number of foreign potential investor companies were identified who were consulted about the partnership of local small and medium-sized companies and their potential for the supply of goods/services. In particular, in 2017 LEPL “Enterprise Georgia” was involved in contacting up to ten Georgian business representatives with potential investors in the various sectors - production, real estate, export of services, and in most cases negotiations were successful. In addition, dozens of foreign companies and potential investors were informed about Georgian companies in order to contact them.

In 2017, Enterprise Georgia, in co-operation with a UK-based consultancy, initiated a pilot project funded by the UK Department for International Development aimed at fostering linkages between multinational corporations (MNCs) operating in Georgia and local SMEs.

The project selected two sectors, hospitality and manufacturing, as most promising due to growth in both tourism and manufacturing and the high potential for creating and expanding linkages. The project is organized around three phases:

- Assessment of demand-side companies in the chosen sectors, identifying MNCs already operating in Georgia, but also franchises (McDonalds, Wendy's, The Coffee Bean & Tea Leaf etc.). Information will be stored in a company database with details on location, business indicators and activities.
- Pilot phase in the hospitality sector. The main goal will be to match SMEs with MNCs, especially targeting procurement managers, and based on a thorough business review of SMEs including an audit of skills and technology, and an initial training for SMEs to conduct business negotiations with MNEs.
- Full transfer of methodology from the consultancy to Enterprise Georgia and roll-out plan to the same or other sectors.

The sustainable continuation of this project is a central focus of the SME strategy's Action Plan 2018-2020, with an aim to expand the linkage programme to other sectors in the future based on the results of the pilot project in the hospitality sector.

**Implementation** – “Performance indicators” corresponding to the facilitation of linkages between FDI and SMEs were performed. In particular, bilateral meetings between Georgian and foreign businessmen were held; Potential foreign investor companies were identified, who have been consulted with local small and medium companies about partnership and their potential for the supply of goods and services.

### *Way Forward*

Consider providing targeted financial support to exporting SMEs

To further develop SME internationalization, the government could consider providing additional targeted financial and insurance support to help SMEs overcome the financing barriers to exporting and the risks encountered, such as longer cash-flow cycles, physical distance from buyers and currency risk, when engaging in international trade.

As a first step, consultations among government, financial institutions and exporting SMEs should be regularly held, as well as surveys carried out, in order to identify specific barriers and needs for further internationalization. Depending on the needs identified among Georgian SMEs, financial solutions could include export loans to finance additional working capital, export credit insurance to cover market and political risk, as well as export factoring to convert exporters' trade receivables in discounted liquidity.

Awareness raising campaigns promoting the availability of SME targeted trade finance instruments, as well as export-related finance and insurance skills trainings such as export risk management, should be considered an integral part of the proposed financial solution.

### Promote SME internationalisation through cluster development

To improve competitiveness of Georgian SMEs and to help them reach and succeed in the EU market, the GIZ SME DCFTA GE project currently supports more than 150 Georgian SMEs, benefitting more than 1000 employees by promoting the formation of clusters in four sectors: furniture/interiors, apparel, film production and ICT. Clusters can increase productivity, contribute to more rapid innovation and new business formation through co-operative research, sharing knowledge and infrastructure, and optimising costs in accessing inputs, marketing and distribution.

This initiative offers promising signs, with strong interest from government stakeholders and entrepreneurs. Two clusters have already been formally registered, with a management structure in place; five apparel companies are in negotiations with potential EU buyers and a first joint product of furniture producers and interior designers has been featured at international fairs (GIZ, 2018).

Following an evaluation of the effectiveness of the clustering scheme, additional sectors for cluster development could be explored, responding to the needs of the Georgian government and meeting market demand from regional neighbours and EU countries. Sustainability of the GIZ clustering methodology should also be ensured through continuous involvement of government stakeholders and co-operation with local partners throughout the process.

## **Strategic Direction 5: Facilitate SMEs' innovation and R&D**

### **Amend the legal framework for innovation**

**Relevance** – Supporting the development of innovation and R&D is crucial for competitiveness and productivity. To create a supportive environment for innovation is crucial to amend the legal framework and it comply with set goals.

**Effectiveness** – In 2016, in order to create a supportive environment for innovation in the country, Georgia substantially amended the Law on Innovation, allowing public universities and research centres to own shares in spin-off companies and to commercialise their inventions and intellectual property rights generated through publicly-funded R&D. The Law provides for the creation of a comprehensive innovation infrastructure, including Technology Parks, business incubators and accelerators, an Innovation Centre delivering trainings on entrepreneurship and ICT skills, as well as FabLabs, to foster innovative activity throughout the country (GoG, 2016).

In addition, in 2017, the Parliament adopted amendments to the Law on Public Procurement, which introduced the principles of proportionality and equal treatment in a public tender process, thus removing obstacles to SME participation. In line with the principles of the Small Business Act for Europe, the law also includes the possibility of using e-procurement, which widens SMEs' access to information on procurement opportunities. The increased involvement of SMEs in public purchasing is likely to result in greater competition for public contracts, leading to better value for money for the procuring entities and more innovative approaches to contracting. The Law also specifies that preference should be given to performance and functional criteria when drawing up tender requirements, thus encouraging suppliers to deliver contracts in a more efficient and innovative way. However, more could be done to ensure innovation through public procurement.

As a complement to legislative improvements, Geostat and GITA have taken substantial steps to collect data on ICT use by households, individuals and enterprises, as well as on innovation activity in enterprises. The first surveys were conducted in 2016, resulting in three publications (on ICT access and use by households and individuals; ICT use by enterprises; and innovation activities in enterprises) and are to be replicated annually. As a next step, Geostat is considering breaking down the data on ICT usage by enterprise size.

**Implementation** – “Performance indicators” corresponding to the amendment of the legal framework for innovation were performed. In particular, amended the Law on Innovation in terms of creation a supportive environment for innovation.

### **Foster collaboration between industry and academia**

**Relevance** – Facilitation of research-industry linkages is issue of high importance, as it will supportive to for commercialization of innovations and R&D. This measure is actual and in compliance with set goals.

**Effectiveness** – Collaboration between industry and academia has mainly been explored in the context of commercialisation of innovation and R&D projects. In 2015, the Massachusetts

Institute of Technology (MIT) carried out a technology assessment of Georgian research institutes to understand their capabilities and explore their needs. The assessment aimed, among other things, at raising awareness of the institutes' research and administrative staff about new opportunities for co-operation with industry and motivating staff to commercialise in-house research. The assessment led to the selection of 13 out of 96 projects elaborated by the research institutes' staff, including recycling of waste materials, automobile fuel cleaning, radiation safety devices and others, to be developed based on their commercial attractiveness.

Additionally, GITA has compiled a database of existing research institutes and research staff, which currently includes 70 scientists/representatives of research institutes. On this basis, GITA is planning to analyse the scientific potential of Georgia with a view to form innovation clusters in IT, e-commerce, biotech and plastics in light of a future commercialisation of business ideas. GITA could also further leverage the Enterprise Europe Network (EEN) to contribute to technology transfer in the country: by providing international business expertise with local knowledge on innovation and technology transfer, the EEN also aims to identify potential international research partners and supports the information exchange on innovative processes and tools in various sectors.

Overall, the innovation support infrastructure could be further developed: the scarcity of business incubators, accelerators and technology transfer offices, especially outside Tbilisi, does not allow for effective diffusion of innovations across the country. A first step has been made by GITA, which developed an action plan to establish a National Technological Transmission Office, with the aim to commercialize Georgian innovative products and support their export to foreign markets. This will be achieved by fostering innovation through research collaboration between academia and industry, evaluating the commercial potential of an innovation, and licensing of new technologies and inventions to selected industry partners. With donor support, the implementation is to begin in 2019.

**Implementation** – “Performance indicators” corresponding to the Fostering collaboration between industry and academia were performed. In particular, Situational analysis has been carried out related to research; The survey was conducted throughout the country to identify R & D's ability and potential of human resources; The cluster mapping is drawn up based on the assessment of existing potential; Mechanisms for promoting communication between R & D and production are developed; The very first draft of concept of the National Technological Transfer Office (NTTO) was developed.

#### **Consider providing financial support to SMEs for innovative activities**

**Relevance** – Innovation remains a risky business and therefore, there is low level of access to finance for it. As a result of it, measures to consider providing financial support to SMEs for innovative activities is always actual and in compliance with set goals.

**Effectiveness** – GITA is the main institution tasked with providing financial support for innovation in Georgia. Throughout 2016-2017, three schemes have been developed to this purpose: the Micro Grants, the Start-up Georgia and the Matching Grants programmes.

The Micro Grants Programme, launched by GITA in 2016, offers up to GEL 5 000 (≈ EUR 1670) to support entrepreneurs with funds for developing prototypes within the GITA

infrastructure, participating in fairs and innovation competitions. Since the inception of the programme, GITA received 350 applications, with grants distributed to more than 200 applicants. The Start-up Georgia Programme has a total budget of GEL 35 million ( $\approx$  EUR 11.7 million), with GEL 11 million ( $\approx$  EUR 3.7 million) disbursed in 2016 for the first round of the project. This programme issues grants of up to GEL 100 000 ( $\approx$  EUR 33 000) to develop a business model and go-to-market strategies for their products.

GITA complements its financial support with training, coaching, mentoring and consulting services for all programme beneficiaries. A specialised training on developing innovative business skills has recently been created and is being delivered throughout the country. Trainings on coding, robotics, intellectual property, digital marketing and export-oriented ICT skills are also regularly carried out on the premises of various innovation centres in Georgia's regions, registering currently over 1000 beneficiaries.

Lastly, GITA has contributed to the drafting of a new Law on Crowdfunding as an alternative way for businesses to collect financial resources for innovative ventures. The draft law is currently under revision by the NBG.

In 2016, Georgia has also joined Horizon 2020, EU's framework programme for research and innovation, which provides funding for developing scientific and innovation capacity of all programme partners, including research institutes, universities, individual researchers and SMEs. To date, the EU contributed EUR 2.5 million and counts 27 participants, with an objective to expand activities in the coming years.

**Implementation** – “Performance indicators” corresponding to the providing financial support to SMEs for innovative activities were performed. In particular, Call of proposals for grant projects were made; Pitching sessions of short listed candidates among granting council were held; winning projects were financed.

### *Way forward*

Establish a strategic framework and improve instruments to foster SME innovation;

Amendments to the legal framework and a large spectrum of activities, including providing financial support to innovative firms, have been carried out over the last three years by GITA and other stakeholders, to support business innovation throughout the country. A more co-ordinated approach could be achieved by designing a comprehensive medium-term strategic framework on innovation, with a focus on the SME sector.

One of the priorities to be reflected in the future innovation strategy is the development of the overall innovation infrastructure, especially outside Tbilisi and in rural areas, which is currently lagging. A special focus should be put on establishing a Technology Transfer Office (TTO), crucial for the movement of know-how, skills and technical knowledge from research institutions and universities to companies, thus bridging the gap between research and innovation and contributing to generate economic value.

As a go-to office dedicated to fostering and diffusing innovations, the TTO could take up various specific roles, ranging from simply establishing relationships with firms, through providing assistance in areas related to e.g. intellectual property, to facilitating the formation of university-connected companies using public research organisations' technologies. (OECD, 2011)

In addition to the financial support currently in place, expenditure-based R&D tax incentives specifically for young companies could be introduced. Targeting young companies could help them challenge incumbent businesses and generate disproportionately more jobs. Moreover, compared to other direct subsidies, support programmes or grants, R&D tax incentives allow firms to decide about the nature of their innovative activities. However, a close monitoring and evaluation of tax incentives should be ensured, demonstrating the effectiveness of such incentives and assessing the potential distortions of competition between incumbents and new entrants to the market.

## Action plan achievements

Highest majority of actions are planned to be implemented during all period of implementation for action plan of SME Development Strategy. This is obvious and logical because planned actions in order to improve legislative, institutional framework and operational environment for SMEs, as well as improve of access to finances, SME skills development and promotion of entrepreneurial culture, export promotion and SMEs internationalization, to facilitate Innovations and R&D in SMEs are main priorities and basic functions of the Ministry and doesn't have beginning nor the end. From other side there are small number of the actions which is planned to be finished in one or two years of Action Plan implementation and majority of those actions are one-term activities.

The MoESD is in charge of setting the overall priorities and goals of SME policy, distributing roles and resources among stakeholders, and coordination, monitoring and evaluation of the implementation process.

Numerous stakeholders are involved in the implementation of SME policy reforms, with the most prominent roles being played by the entrepreneurship development agency Enterprise Georgia and the Georgian Innovation and Technology Agency (GITA), both of which fall under the authority of the Ministry of Economy and Sustainable Development.

Other stakeholders, such as relevant line ministries, the Georgian Chamber of Commerce, the National Bank of Georgia, various business associations, universities, research centres, the civil society and donors are involved in the implementation of SME policy reforms.

Key principles and the best practices of EU countries in terms of SME business Policy are stipulated in SME Development Strategy of Georgia 2016-2020 and Related Action Plan.

**Table: Status of compliance with Criteria of Evaluation**

<p><b>Relevance / Topicality</b> <i>compliance of strategy goals and objectives with public needs and Government priorities;</i></p>	<p>Government of Georgia has prioritized SME development as it is considered as main source of private sector growth, jobs creation and innovation. SMEs, having enormous potential in employment generation and job creation, as well as in fostering economic growth, is considered as a backbone of each country's economy. A strong and well-developed SME sector significantly contributes to export, innovation, and creation of modern entrepreneurial culture, playing at the same time a significant role in achieving prosperity in the country;</p> <p>All actions defined in the AP are relevant and in full compliance with public needs because they linked with creation of better environment for SME operation, access to finance, improvement</p>
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	<p>entrepreneurial learning and culture, promotion of export, Development of innovation and R&amp;D.</p> <p>Strategy targets - <i>Growth SMEs output by average 10% annually by 2020; Growth of number of employees in SMEs by 15% by 2020; Productivity growth by 7% by 2020</i> – are well designed and their achievement will ensure enhancement of wellbeing of society.</p>
<p><b>Effectiveness</b></p> <p><i>compliance of the achieved results of the strategy to the planned results, as well as to the needs of direct and indirect beneficiaries;</i></p>	<ul style="list-style-type: none"> <li>– Activities of Ministry and other implementing institutions of AP were fully in line with Strategy and Government priorities.</li> <li>– Official statistics shows the progress of SME Sector in terms of number of established SME's and employed by them, production value, productivity by SME's and etc.</li> </ul>
<p><b>Implementation</b></p> <p><i>quality of implementation process and structures;</i></p>	<ul style="list-style-type: none"> <li>– Target indicators of Strategy as well as priority measures and activities of AP are implemented according to the timeframe and all implemented institutions are ready to ensure quality control during implementation process.</li> </ul>

## Implementation of Actions

SME Development Strategy covers period until 2020 and the program is still ongoing. Some of activities are constant and some of them, could be characterized as one-off actions. The table below shows successful implementation all the activities in detail, which were envisaged by AP:

*Table: Progress status for implementation of SME Development Strategy AP 2016-2017*

N	Priority Actions	Activities	Progress Status
<b>Strategic Direction 1: Further improvement of legislative, institutional framework and operational environment for SMEs</b>			
1.1.	<b>Improvement of closing business procedures</b>	3 Actions	<i>Completed</i>
1.2.	<b>Revision of SMEs definition and improvement of SMEs statistics</b>	4 Actions	<i>Completed</i>
1.3.	<b>Improvement Enterprise Statistics</b>	3 Actions	<i>Completed</i>
1.4.	<b>Strengthening of the SME supporting institutions</b>	6 Actions	<i>Completed</i>
1.5.	<b>Public Private Partnership</b>	2 Actions	<i>Completed</i>
1.6.	<b>Establishment of RIA system</b>	4 Actions	<i>Completed</i>
<b>Strategic Direction 2: Improvement of Access To Finance</b>			
2.1	<b>Improvement of financial literacy</b>	5 Actions	<i>Completed</i>
2.2	<b>Support SMEs for implementation of IFR for SMEs in financial accounting</b>	3 Actions	<i>Completed</i>
2.3.	<b>Increase knowledge on fund raising among SMEs</b>	2 Actions	<i>Completed</i>
2.4.	<b>Attraction of SMEs oriented private equity funds and venture capital funds for start-up financing in Georgia</b>	2 Actions	<i>Completed</i>
2.5.	<b>Support to SMEs to increase access to finance through micro financial organizations (MFIs)</b>	3 Actions	<i>Completed</i>

2.6.	<b>Improvement of SMEs' financing through grants</b>	2 Actions	<i>Completed</i>
<b>Strategic Direction 3: SME skills development and promotion of entrepreneurial culture</b>			
3.1.	<b>Identification of labour market needs for SMEs and development of relevant employment programmes</b>	3 Actions	<i>Completed</i>
3.2.	<b>Training Needs Assessment (TNA) for SME sector in Georgia</b>	5 Actions	<i>Completed</i>
3.3.	<b>Establishment of Life Long Entrepreneurial Learning (LLEL) at all levels of the education system</b>	5 Actions	<i>Completed</i>
3.4.	<b>Development of SMEs oriented VET system</b>	7 Actions	<i>Completed</i>
3.5.	<b>Facilitation of access to non-formal training for SMEs</b>	2 Actions	<i>Completed</i>
3.6.	<b>Provision of Technical Assistance (TA) for SME sector</b>	4 Actions	<i>Completed</i>
3.7.	<b>Development of educational component on the web-site of Enterprise Georgia</b>	1 Actions	<i>Completed</i>
3.8.	<b>Expand portfolio of Services by Business Service Center for SMEs</b>	2 Actions	<i>Completed</i>
3.9.	<b>Encouragement of female entrepreneurship</b>	3 Actions	<i>Completed</i>
3.10	<b>Promotion of green practices among SMEs</b>	3 Actions	<i>Completed</i>
<b>Strategic Direction 4: Export Promotion &amp; SME Internationalization</b>			
4.1.	<b>Raising awareness on perspectives offered by DCFTA and DCFTA requirements</b>	4 Actions	<i>Completed</i>
4.2.	<b>Support businesses in adaptation to DCFTA requirements</b>	5 Actions	<i>Completed</i>
4.3.	<b>Support SMEs in export promotion</b>	9 Actions	<i>Completed</i>
4.4.	<b>Support SMEs to establish partnerships with foreign companies</b>	2 Actions	<i>Completed</i>

4.5.	<b>Promotion of Responsible Business Conduct among SMEs</b>	4 Actions	<i>Completed</i>
4.6.	<b>Support to the establishment of FDI-SMEs linkages (inclusion in local value chains)</b>	3 Actions	<i>Completed</i>
<i>Strategic Direction 5: Facilitation of innovation and R&amp;D in SMEs</i>			
5.1.	<b>Stimulation of innovation among SMEs</b>	6 Actions	<i>Completed</i>
5.2.	<b>Elaboration effective plan of financing of innovations and R&amp;D</b>	3 Actions	<i>Completed</i>
5.3.	<b>Support to commercialization of innovations and R&amp;D</b>	5 Actions	<i>Completed</i>
5.4.	<b>Improvement ICT Skills among businesses</b>	3 Actions	<i>Completed</i>
5.5.	<b>Providing Infrastructure for innovation (FabLabs; iLabs; TechPark BroadBand for All; Computerization)</b>	6 Actions	<i>Completed</i>

To sum up of this table, should be said, that amongst 124 activities all are completed and respectively all relevant Priority actions are fulfilled.

Herewith, according to Geostat, all targets of SME development strategy (*According to strategy targets are as follows: Growth SMEs output by average 10% annually by 2020; Growth of number of employees in SMEs by 15% by 2020; Productivity growth by 7% by 2020*)) **have been successfully fulfilled**. In particular:

- ✓ Average annual Growth SMEs output is 14.8% in 2014-2016;
- ✓ Growth of number of employees in SMEs is by 20.5% in 2016;
- ✓ Productivity growth is by 19.6% in 2016.

## Main Recommendations

### *General Recommendation for all SD*

- SME Development Strategy and relevant Action Plan should be more precise in terms of budgetary issues regarding needs of donors' support as well as state financing;
- The action Plan should include information on possible risks related to implementation of priority measures envisaged under the strategic directions;

### *Recommendations for each SD separately*

#### **SD1:**

Regulatory Impact Assessment remains an important area of future improvement for SME policy. While monitoring and evaluating the implementation of the SME strategy, the evaluation revealed that additional action is required in the sphere of RIA and its role in improving the institutional framework and operational environment for SMEs.

Developing an SME-specific RIA test is an essential element of the policy making process and will enable the government to design specific tools to ensure that proposed legislation (new or amended) will not impact disproportionately SMEs.

Government will have to make considerable efforts to use RIA SME Test in order to mitigate negative regulatory impact on small and medium sized enterprises. Drawing on EU examples, Georgia should develop its unique SME test and designate a central entity to support its development and implementation.

#### **SD 2:**

A dedicated strategy for SME financial literacy, with an action plan including clearly defined roles, responsible implementing institutions, implementation timeframes, a monitoring system and attributed resources, could help Georgia adopt a more co-ordinated approach towards improving financial literacy of entrepreneurs.

To develop dedicated financial education initiatives remains as issue of high importance. Raising awareness of the benefits of IFRS could be considered one such initiative. Georgian Associations of Banks and SME associations, in co-operation with SARAS and the NBG, could be mobilized to raise awareness among SMEs of the benefits of increased transparency in financial statements, not least in order to get easier access to credit.

To set up a Credit Guarantee Scheme (CGS) remains as issue of great importance as CGS could create market-based incentives for banks to lend more to SMEs. A CGS works as a risk-sharing mechanism between lenders (banks), borrowers (SMEs) and a guarantor (the state or a private entity). By reducing the perceived risk, banks are

expected to demand lower collateral and interest rates from SMEs. As a result, more credit is extended to borrowers than otherwise would be the case.

Government could promote SME awareness of the alternatives to bank lending, accompanied by training and financial education programmes to ensure the correct use of instruments according to the stage of any given firm's development, and investors (equity investment opportunities). Dedicated awareness-raising events, showcasing the most promising business ideas, could also help attract business angels and support the establishment of an angel investor community, leading to a possible legal framework on angel investment and incentives.

### **SD 3:**

To proceed conduction of Labour market surveys, inter alia, labour market surveys of priority economic sectors in order to create relevant statistical data series for anticipation and creation basis for evidence based policy.

Considering the relatively low share of new enterprises created by women and their reduced willingness to take entrepreneurial risk in comparison to men, more effort seems to be required to further develop targeted policies to seize the potential of women's entrepreneurship across the country.

Government could go a step further and consider increasing the institutional reach of the sub-council for women's entrepreneurship promotion by reporting on progress achieved and discussing priorities for the future with the Gender Equality Council of the Parliament of Georgia.

Separate Action Plan on promoting women's entrepreneurship could be designed.

### **SD 4:**

Consider providing targeted financial support to exporting SMEs;

To further develop SME internationalization, the government could consider providing additional targeted financial and insurance support to help SMEs overcome the financing barriers to exporting and the risks encountered, such as longer cash-flow cycles, physical distance from buyers and currency risk, when engaging in international trade.

As a first step, consultations among government, financial institutions and exporting SMEs should be regularly held, as well as surveys carried out, in order to identify specific barriers and needs for further internationalization. Depending on the needs identified among Georgian SMEs, financial solutions could include export loans to finance additional working capital, export credit insurance to cover market and political risk, as well as export factoring to convert exporters' trade receivables in discounted liquidity .

Awareness raising campaigns promoting the availability of SME targeted trade finance instruments, as well as export-related finance and insurance skills trainings such as export risk management, should be considered an integral part of the proposed financial solution.

Clusters can be considered as tool for improvement of competitiveness of Georgian SMEs and support them reach and succeed in the EU market. Clusters can increase productivity, contribute to more rapid innovation and new business formation through co-operative research, sharing knowledge and infrastructure, and optimizing costs in accessing inputs, marketing and distribution.

Following an evaluation of the effectiveness of the clustering scheme, relevant sectors for cluster development could be explored, responding to the needs of the Georgian government and meeting market demand from regional neighbors and EU countries.

#### **SD 5:**

Establish a strategic framework and improve instruments to foster SME innovation

A more co-ordinated approach could be achieved by designing a comprehensive medium-term strategic framework on innovation, with a focus on the SME sector.

One of the priorities to be reflected in the future innovation strategy is the development of the overall innovation infrastructure, especially outside Tbilisi and in rural areas, which is currently lagging. A special focus should be put on establishing a Technology Transfer Office (TTO), crucial for the movement of know-how, skills and technical knowledge from research institutions and universities to companies, thus bridging the gap between research and innovation and contributing to generate economic value.

Expenditure-based R&D tax incentives specifically for young companies could be introduced. Targeting young companies could help them challenge incumbent businesses and generate disproportionately more jobs. Moreover, compared to other direct subsidies, support programmes or grants, R&D tax incentives allow firms to decide about the nature of their innovative activities.

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