

# Comments from Central and Eastern European Bankwatch Network to the European Bank for Reconstruction and Development (EBRD) Country Strategy for Georgia

25 July, 2013

## Introduction

The following are comments from CEE Bankwatch Network to the European Bank for Reconstruction and Development Country Strategy for Georgia. We hope that this document will lead to changes to the strategy, in order to ensure that the Bank's expertise and funds will be used for the development of environmentally and socially friendly projects and programs in Georgia, support diversification of Georgia's economy.

The draft strategy prepared by Bank focused on some transition challenges in order to overcome existing shortcomings defines the strategic directions over the next three years.

## Political assessment and its relation to strategy

Georgia aspires to integrate with the EU and to finally become a member of the bloc, and it serves as a red line in all political negotiations. Georgia is part of the EU's European Neighborhood Policy, and there were successful finalization of negotiations between Georgia and the EU regarding the Associated Partnership Agreement, including DCFTA (Deep and Enhanced Trade Agreement).

The national parliamentary elections of 2012 have been assessed as an important test of democracy for the country – according to international observers, Georgia passed this test successfully.

While the elections were dubbed 'historic', there are still a great deal remains to be done in order to ensure the real development of democratic institutions, the rule of law and respect for all human rights, including social, economic and cultural rights.

Since Georgia's Rose revolution in 2003, the country has increased and deepened its political and economic relations with both the United States and the European Union. However, such developments have provided little in the



Striving for environmental and  
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way of improved human rights. Although there have been a number of positive steps taken, such as combatting petty corruption and undertaking reforms in the education and business sectors, Georgia has not made significant progress in strengthening representative institutions or introducing democratic procedures. In recent years Georgia has made significant progress in fighting petty corruption, ranking 64th among 183 countries in Transparency International's 2011 Corruption perception report. However, as reported in the European Commission's ENP progress report for 2011, persistent areas of concern include so-called elite corruption among high ranked officials, the lack of transparency in procurement and privatisation processes, weak accountability for reserve funds, violation of property rights and a lack of transparency in Georgian media: "More broadly, many Georgian analysts allege that much of Georgian business is still controlled by officials and politically connected figures – although in a much more discreet manner than in previous times ... Put simply, there is little public information about who owns large sections of Georgian business and media, and very little can be proved one way or the other"<sup>1</sup>. But both local observers and foreign commentaries, the U.S. State Department's Human Rights Report on Georgia for 2010, mention concerns about "elite corruption."<sup>2</sup>

Transparency International in 2012 creates the amazing evidence of elite corruption cases and governmental pressure on business. The Book "Who owned Georgia" - encompassing the period from 2003 until 2012, that evidences how major sectors of economy from the world of telecommunications to broadcasting, advertising, oil, pharmaceuticals and mining is connected with the companies registered offshore, by former members of the government and their relatives, how government supports those shareholding companies and creates artificial barriers and even criminal cases against those without any "elite" support <http://dfwatch.net/elite-corruption-and-government-pressure-on-business-in-georgia-10473>

The transitional challenges stressed by EBRD, includes: 1) Low levels of private investment in the economy; 2) Underutilized renewable energy sector potential; 3) Limited integration in regional and global production markets and value chains. These transitional challenges also find its roots in elite corruption and lack of transparency in decision making processes.

The new government that took office in October 2012 should be in a position to address all the problems associated with the legacy of the past, including Georgia's heavily impacted ordinary citizens and local business. The some positives steps including the changes of Labour Code in accordance with requirement of ILO and EU have been already passed, however, much more needs to be done in order to ensure from one side protection of Labour rights and from another, development of thoroughly sustainable business environment.

### **Georgia's development priorities and Donor coordination**

Government of Georgia with support of EU, in 2010-2012 prepares and adopts to Regional Development Strategy 2012-2017 and Agriculture Development Strategy 2012-2022. The Sectoral Budget Support has been allocated by EU to Georgia, in order to implement activities both in regional development, as well as in agricultural sector.

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<sup>1</sup> [http://carnegieendowment.org/files/georgias\\_choices.pdf](http://carnegieendowment.org/files/georgias_choices.pdf)

<sup>2</sup> "There were reports of selective application of the law--crimes supposedly involving government officials or supporters were slowly investigated and often remained pending, while crimes allegedly involving persons or organizations linked to the opposition were investigated quickly and prosecuted to the full extent of the law. This imbalance led to allegations of impunity for government officials." <http://www.state.gov/j/drl/rls/hrrpt/2010/eur/154425.htm>

The draft Single Support Framework document for 2014–2020 prepared by European Commission under the European Neighborhood Instrument, among number of priorities stressed the Agriculture and Regional Development, that aims to support strengthen the social and technical infrastructure and diversification of economic activity in the small towns and rural areas. It envisaged the EBRD’s involvement both to support the Agribusiness as well as regional development through its Municipal and Environmental Infrastructure Programme.

It should be stressed that EU through its new European Neighborhood policy and draft European Neighborhood Instrument, proposed by European Commission to EU Parliament<sup>3</sup> strives to ensure implementation of More for More and Less for Less principle. The draft of Common Rules regulation<sup>4</sup> proposes to increase the donor coordination through development of joint multiannual programing document, to ensure that MS and other donors (at least European multilateral and bilateral banks) are in same line with EU’s commitment.

Therefore, it is important that the EBRD admits the importance to target improvement of “productivity levels in sectors employing large shares of workers, especially agriculture, manufacturing and construction, and will increase its focus on SME development through access to finance and integration into a viable value chain. The Bank will support the new government’s objectives of improving the quality of life for the Georgian people by re-engaging in municipal projects where it can bring value-added through design, implementation and grant and TC support from donors”

However, the Banks operational response is very general and does not address specificity of Georgia. It is important that Bank clarifies what kind of transition is desirable in these sector’s, taking into account particularities of Georgia’s agricultural sector, problems related with land market and features of regional development. Specifically, it would be impossible to follow the standard (western) agribusiness models that are large extent environmentally unsustainable themselves. In addition, in Georgia, the preferences should be given to development of local food markets through ensuring the product diversity and local traceability, and minimise food transportation.

## **Energy Sector**

According to the EBRD’s draft strategy document the central strategic direction would be to “Complete the modernization of the energy sector”. The bank stressed that “the country’s integration in regional energy markets remains incomplete and the sector still suffers from significant distribution losses and seasonal supply patterns inherent to Georgia’s hydrology.” However, rather to address the identified problem, the Bank determines as number one priority “to attract FDI in large hydropower generation projects”.

Unfortunately, Bank does not analyse in depth the overall problems of Georgia’s power sector as well as its own experience in a field.

In general, Georgia’s has no strategic development plan for energy sector and since 2001 energy balance has not been prepared. Despite certain positive changes over the past years, the sustainability of energy system is still problematic in Georgia. Among the key problems we can distinguish the safety of supplies; integration of environmental standards both in the process of energy generation and consumption; also development of competitive systems with the purpose of supplying power to consumers at moderate prices. Today Georgia is completely dependent on imported organic fuel that

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<sup>3</sup> [http://ec.europa.eu/world/enp/docs/2011\\_prop\\_eu\\_neighbourhood\\_instrument\\_reg\\_en.pdf](http://ec.europa.eu/world/enp/docs/2011_prop_eu_neighbourhood_instrument_reg_en.pdf)

<sup>4</sup> [http://ec.europa.eu/world/enp/docs/2011\\_prop\\_com\\_ext\\_instruments\\_en.pdf](http://ec.europa.eu/world/enp/docs/2011_prop_com_ext_instruments_en.pdf)

increases the risk of economic and political dependence of the country, whereas the parameter of energy intensity exceeds the parameters of EU member states.

Without proper analyses to address the legacy of the past, Georgian Government works to position the country as a future regional renewable energy hub and develop number of the HPPs, including both highly controversial large dam cascades mainly in the mountainous areas of Georgia, including the Khudoni HPP (702MW, annual output 1.5 TWh) on Enguri, the Namakvani cascade (450 MW, annual output 1.6 TWh), Nenskra Cascade (438 MW, annual output 1.2 TWh), as well as divert ones such as Paravani (87 MW) and Dariali HPP (109 MW), as well as small HPPs all around the country with almost 1000 MW installed capacity.

However, the planned projects do not comply with the principles of sustainable development, and they may have serious negative impacts for the environment, drastically change the social and demographic situation in Georgia's mountainous regions and also lead to the destruction of cultural heritage. Simultaneously those newly developed HPPs will hardly address the problems of seasonal imbalance and excess of energy (Experts estimate the amount of excess energy to be approximately 700-800 GWh annually, or about ten per cent of total in-country electricity generation), as well as affordability of electricity prices and energy intensity.

### **Investment in Greenfields**

The draft strategy underlines that “the first Greenfield hydro power plant construction project in Georgia has excellent transition impact potential thanks to its positive demonstration effects of new products and expansion of renewable energy markets, as well as promoting private ownership in the sector.”

It's strange but strategy does not mention the name of the only EBRD funded Greenfield HPP project. Bank funded 87 MW Paravani HPP project appeared quite controversial, due to its negative environmental and social impacts, while project documentation does not have any ground for positive economic justification of the project.

Association Green alternative submitted complaint re: Paravani HPP in the EBRD's Project Compliance Mechanism (PCM) of the EBRD in February 2011.

Yet final report of PCM is not available, as EBRD Management team has not respond finding of PCM expert. However, according to letter of PCM officer, the preliminary find of PCM expert is that project is non-compliant with PR 1 “Environmental and Social appraisal and Management”, PR 6 “Biodiversity Conservation and Sustainable Management of living Natural Resources” and PR 10 “Information Disclosure and Stakeholder Engagement”<sup>5</sup>.

Therefore, the Bank's attempt to assess the project's transition impact as an Excellent, based only on criteria's as expansion of renewable energy markets, the promotion of private ownership, without taking into account the problems of non-compliance with own Environmental and Social Policy, as well as significant environmental and social impacts is more than alarming.

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<sup>5</sup> Email of the EBRD PCM officer Anoush Begoyan “I am writing to let you know that the PCM finalised the Compliance Review on Paravani HPP Project; Compliance Review Expert Mr Glen Armstrong made finding of non-compliance with PRs 1, 6 and 10 of the Environmental and Social Policy of EBRD”

## Energy Efficiency and EBRD

The Strategy stressed that “There is a substantial potential for energy efficiency (EE) improvements” and need “to improve and develop energy legislation and regulation as well as technical standards and operational procedures in the electricity sector”.

Georgia still has no formulated state vision or strategy in energy efficiency and development of renewable energy, despite commitments undertaken by Georgian Government towards EBRD<sup>6</sup> as well as to the EU<sup>7</sup>.

That approach should be changed and EBRD should stop lending to Georgia’s energy sector, until the government would not implement already undertaking commitments regarding energy efficiency. It should also include Energy Efficiency as transition challenges in the energy sector for next three years, namely, (1) Improving efficiency of the energy system by reducing losses in transmission and distribution and by extending geographic reach; and (2) Improving energy efficiency and cross-country energy trading by strengthening tariff setting methodology and eliminating cross-subsidies to reflect more closely the regional market price of energy;

The recent report Green Business Support Strategy for Georgian Private Sector Organizations<sup>8</sup> highlights the energy sector and the energy efficiency of buildings as sectors with high potential for green business in Georgia, as environmental effectiveness coincides with the economic variety.

Among the obstacles, the study identifies the following issues: (i) no separate government agency for promoting energy efficiency; (ii) lack of modern technologies in the private sector; (iii) a lack of awareness about economic benefits from energy efficiency and renewable energy projects at all levels: government (national, regional and local), private sector and general public; (iv) few tax and tariff incentives; (v) limited availability of domestic credit (also due to the low awareness of the local banking sector); (vi) limited outreach of existing programmes to the broader population. Therefore, if a proper legal and financial framework was in place, energy efficiency could become a leading sector for the development of a green economy in Georgia and for increasing green job opportunities.

**In current situation EBRD should assure and assist Ministry of Energy in development of proper energy strategy, energy balance and ensure adoption of the law on renewable and energy efficiency. It also can assist the ministry to set up institutional structures for facilitation sustainable energy development and addressing legacy of the past, including regulations for maintenance of existing HPP infrastructure.**

**Bank should continue to support the government of Georgia as well as private owners of HPPs and ensure rehabilitation of existing HPPs including cleaning up of reservoirs from sediments and development and implementation of a comprehensive energy efficiency development plan.**

**EBRD should avoid investments in Greenfield projects until required strategies are not developed and safeguard policies implementation capacity is not ensured.**

**In addition, Bank should develop the sustainability criteria’s for HPPs in order to ensure sustainability and value added of its own projects.**

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<sup>6</sup> Enguri rehabilitation project agreement between EBRD and Georgia;

<sup>7</sup> EU Georgia ENP Action Plan;

<sup>8</sup> gue, 14–16 September 2011. 15. See: [http://www.bec.ge/images/doc/green\\_per\\_cent20business\\_per\\_cent20strategy\\_per\\_cent20eng.pdf](http://www.bec.ge/images/doc/green_per_cent20business_per_cent20strategy_per_cent20eng.pdf)

## Energy efficiency

EBRD was promoting energy efficiency in Georgia through an energy credit line of 35 million euros. The credit line was designed to increase the competitiveness of Georgian businesses. The corporate loans involve free energy audits, offering new energy efficient technologies. Later, the credit line was expanded and loans became available for individuals, too<sup>9</sup>, via the 15 per cent of the grant component covered by BP. The following major banks are participating in this credit line: Bank of Georgia, TBC Bank, Bank Republic (Société General) and Cartu Bank.

The credit line has three main features: (i) local banks use the credit line to provide commercial loans, at their own risk; (ii) every credit line is supported by a comprehensive, donor-funded, technical assistance package that helps potential borrowers to prepare loan applications and train local bank loan officers to process sustainable energy investment opportunities. This assistance is provided free of charge by a project implementation team consisting of international and local experts; and (iii) often a performance-related incentive fee is paid to the participating banks and to the end-borrowers<sup>10</sup>.

The approach taken by EBRD in general is to mitigate the major financial barriers, such as the high risk, low return/long payback, lack of domestic sources, weak project development, appraisal and technical assessment capacity, lack of energy efficiency project developers and lack of the relevant expertise. Therefore, it is important that initiative continued and planned with wider participation with CSOs in order to really promote the EE in Georgia.

**We strongly believe that EBRD has to determine as priority transition challenges assisting to develop a more dedicated policy approach with regard to promoting energy efficiency, namely, developing general energy efficiency legislation including institutional setup for energy efficiency and developing expertise for the implementation of energy efficiency projects.**

### Annex.1 Bank's past experience in Georgia's Energy Sector

#### Black Sea transmission line project

One of the preconditions for becoming an exporting country to Turkey and South Eastern Europe, according to the Ministry of Energy and Natural Resources of Georgia, is the harmonisation of Georgia's energy system. Georgia plans to enter the South-East Europe electric power market by 2015-2017. In order to help achieve this, the government has initiated the construction of a number of high-voltage transmission lines from Georgia to Turkey. The Black Sea transmission line project is closely linked with building Greenfield HPPs in Georgia and to thus increase electricity export, as the new line will have a capacity of up to 1,000 MW, excessive for Georgia's current domestic demand, but "pertinent in the face of increasing investment". As the project aims not only stabilisation of the domestic grid, but also represents potential for further greenfield projects, in order to boost export capability to Turkey, Europe and Iran, and to ensure trade within the region, it was important to ensure to develop prior of the project Strategic Environmental Assessment (SEA) that all project sponsors failed to do. The SEA that would also address the issues such as how many large and small HPPs need to be developed, the types of HPPs and their impact on river ecosystems, an assessment of projected trade with neighboring

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<sup>9</sup> See: [www. Energocredit.ge](http://www.Energocredit.ge)

<sup>10</sup> Review of the implementation of the OSCE commitments in the field of energy efficiency, 9 September 2011, Promotion of common actions and cooperation in the OSCE area in the fields of development of sustainable energy and transport, concluding meeting, Prague, 14-16 September 2011, [www.unecp.org/.../trans/osce/osceunece/19th\\_OSCE\\_2011\\_Final.pdf](http://www.unecp.org/.../trans/osce/osceunece/19th_OSCE_2011_Final.pdf)

countries, the implication of the excess water issue in the summer period, and likely revenues for the state budget.

#### Other energy initiatives

EBRD draft strategy paper stressed that “the Bank has commissioned strategic environmental assessments of multiple hydropower developments on the Mktvari (Kura) River and on the Paravani River, which will be valuable for developers and regulatory authorities for future projects in these river basins”. Association Green Alternative, as well as local groups from the region has no information about the Strategic Environmental Assessment process, neither have access to that document. It should be stressed, that even bank prepared this document for its own use, that SEA is reaching its own purpose and significance if it prepared through participation of public, as it stressed by EU SEA directive and/or Aarhus Convention.

Continuation of hydropower stations’ rehabilitation process, including Enguri station in 2009-2010, deserves positive assessment. Besides works have started for rehabilitation of Vardnili HPP Cascade (EBRD, EIB, EU). This will provide the country with additional 245 megawatts and reduce hazard risks to the population living downstream the power plant in both, Zugdidi and Gali regions.