Research

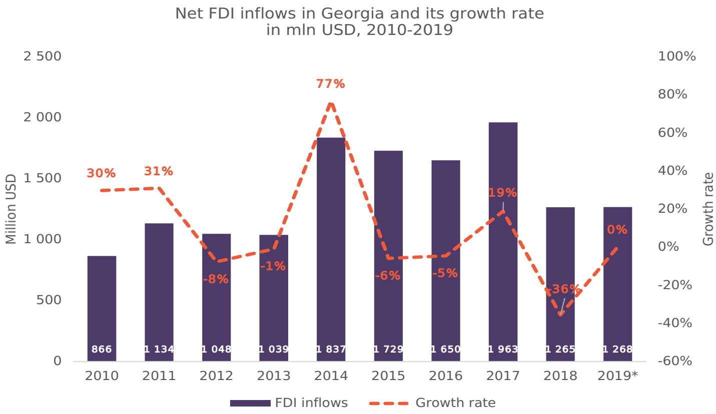
# Foreign Direct Investments in Georgia

## Economic Outlook and Indicators

Issue #119/ 24.06.2020

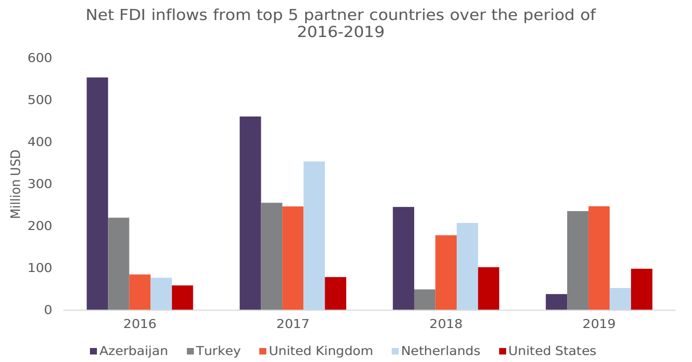
- Due to the COVID-19 pandemic, global FDI is expected to fall by 30-40% in 2020 (UNCTAD), while the decrease in Georgia is forecast at 19% (IMF)
- Net FDI inflows have been decreasing in Georgia since 2017, based on both, yearly and Q1 data.
- Net FDI inflows in Georgia experience volatility over time, due to large one-off investment projects.
- Georgia has been leading among EaP countries in terms of the share of FDI in GDP in 2017 and 2018.
- Net FDI inflows decreased by 41.7% in Q1 of 2020, compared to Q1 in 2019, mainly due to COVID-19 pandemic

The COVID-19 pandemic and the subsequent Great Lockdown has affected investment flows all over the globe, especially in emerging markets. As of April 9, portfolio outflows from developing countries amounted $100 billion, which is 3 times higher than the corresponding figure during the Great Recession in 2008[1]. Deteriorating investor confidence will alter the global Foreign Direct Investment (FDI) flows as well. United Nations Conference on Trade and Development (UNCTAD) estimates global FDI flows to shrink by 30-40%% in 2020[2], reaching the lowest level of the past two decades. As for Georgia, International Monetary Fund (IMF) forecasts a 19% decrease in FDI flows in Georgia[3]. In order to assess the impact of the crisis on the FDI flows in Georgia in the future, it is crucial to have a snapshot of pre-crisis situation.




Over the past decade, Net FDI inflows[4] in Georgia experienced growth compared to the previous year in only 4 years out of 10. These years were 2010 (30% growth), 2011 (31% growth), 2014 (77% growth) and 2017 (19% growth)[5].

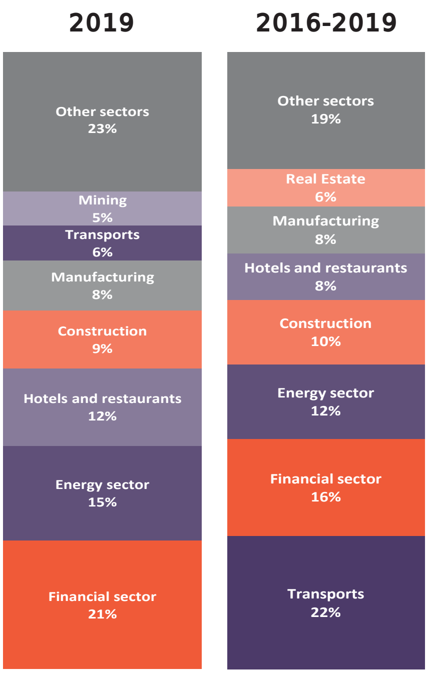
The relatively higher figures between 2014 and 2017 can be explained by large investments in Tbilisi-Supsa pipeline (by BP) and in Baku-Tbilisi-Kars railway project. Thus, Georgian Net FDI inflows remain relatively sensitive to large individual projects.




The above-mentioned volatility of FDI is even more evident when it is decomposed in terms of partner countries. The period of 2016-2019 saw significant tendencies in Net FDI Inflows from biggest partners of Georgia during these years.

Azerbaijan was the biggest partner in 2016 out of 5 countries, but the amount of FDI inflows to Georgia decreased drastically (-93%) in 2019 compared to 2016. It was mainly due to the completion of Baku-Tbilisi-Kars railway project in 2017.

Net FDI inflows from Turkey have experienced a fall by 81% in 2018, which was mainly due to acquisition of Geocell by Silknet.




Net FDI inflows from Netherlands recorded the highest growth of 358% in 2017. Moreover, in 2017 Net FDI Inflow from the United Kingdom increased by 190% compared to 2016, while FDI Inflows from the United States recorded a growth by 34%.

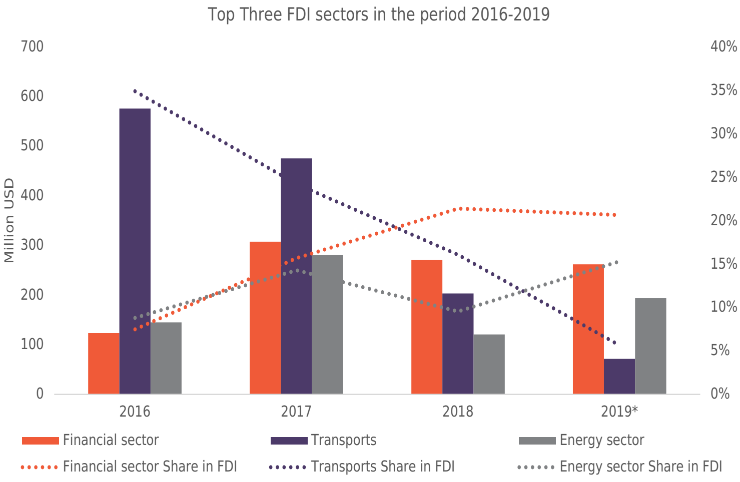
The decomposition of Net FDI inflows by sectors revealed that the ranking and composition of the sectors in terms of largest Net FDI Inflows is slightly different when aggregate numbers of the period 2016-2019 are compared to the figures of 2019.

The analysis of Net FDI inflows by sectors over the period of 2016-2019 shows that the most FDI over this period was directed to the transports (21.6%), followed by financial sector (15.7%) and energy sector (12%).

In 2019, the financial sector was leading in terms of share in Net FDI inflows (20.6%), followed by energy sector (15.3%) and hotel and restaurants sector (12.4%).

The comparison of Net FDI inflows in 2019 to the average Net FDI inflows of the three year period of 2016-2018 reveals that the highest growing major sector in 2019 was hotels and restaurants (55% growth), followed by communications (42% growth) and mining (26% growth).

The sector which declined the most in 2019, compared to the average of 2016-2018, was real estate (124% decline), followed by transports (83% decline) and construction (32% decline).




The analysis of top three sectors of Net FDI inflows during the period of 2016-2019 again underlines the volatility of FDI flows in Georgia.

The analysis reveals a strong downward sloping trend for transports sector, with its share in total Net FDI inflows decreasing from 34.9% in 2016 to 5.6% in 2019.

Conversely, there has been a strong upward sloping trend for financial sector over the period, as its share in total Net FDI inflows nearly tripled from 7.5% in 2016 to 20.6% in 2019.

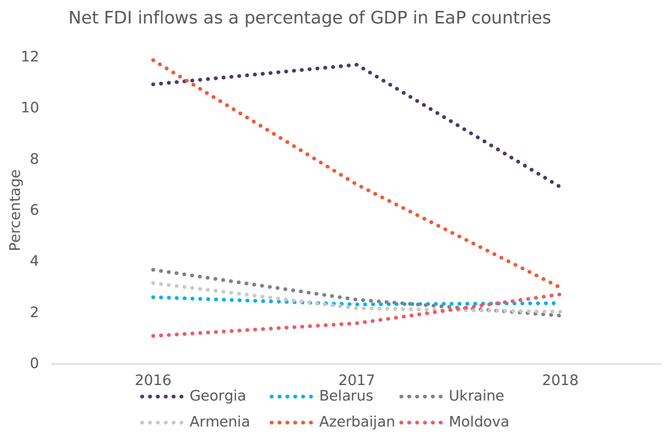
As for the energy sector, it has also shown an upward-sloping trend over the period, however, it was less pronounced than that of financial sector. Its share in total Net FDI inflows nearly doubled from 8.8% in 2016 to 15.3% in 2019.

It is worth noting that, based on World Bank database, Georgia is characterized with the highest figures of Net FDI inflows as a percentage of GDP amongst EaP countries since 2016. Georgia reached its peak of 11.7% in 2017, but decreased to 6.9% in 2018.

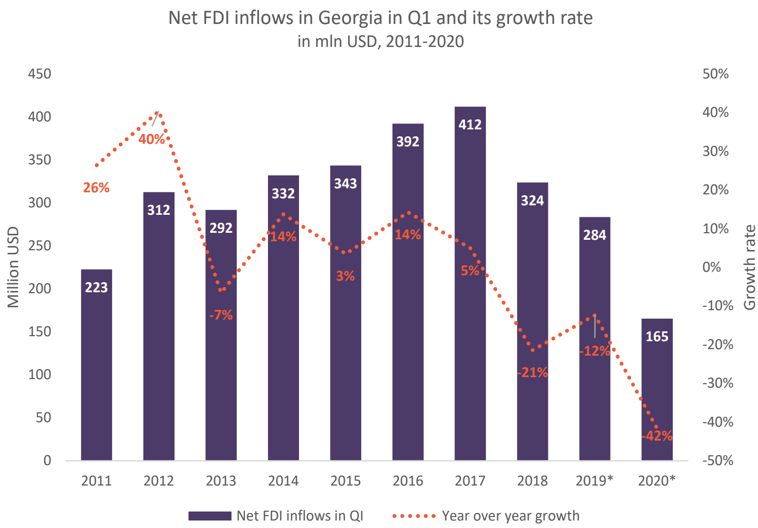
Azerbaijan had the highest share of Net FDI inflows in GDP of 11.9% in 2016, but it decreased significantly to 3% in 2018.

Moldova experienced an increase of share of Net FDI inflows in GDP from 1% in 2016 to 2.7% in 2018.

Armenia's share gradually decreased from 3.2% in 2016 to 2% in 2018, while Ukraine followed the similar pattern and its share decreased from 3.7% to 1.9%.




Net FDI inflows in Belarus were not characterised with significant fluctuations and its share in GDP slightly decreased from 2.6% in 2016 to 2.4% in 2018.




Net FDI Inflows in Georgia decreased by 41.7% in Q1 of 2020, compared to Q1 in 2019, while compared to its peak in Q1 of 2017, Net FDI inflows decreased by 59.8% in Q1 of 2020.

The average growth rate of Net FDI inflows in Q1 over past decade amounted 2.1%. The growth rate has been negative and expressed in double figures since 2018.

A vast majority (81.6%) of Net FDI inflows in Q1 were reinvestments of earnings, while only 13.7% were equity investments.

As the main consequences of the crisis will be realised in Q2, even gloomier figures of Net FDI inflows are expected. Thus, a strong rebound is needed in Q3, a quarter which on average accounts for the most Net FDI inflows (31%), in order to end the year with the estimates of IMF (-19%).

The significance of FDI flows for the development of the country is indisputable. When the crisis ends, investors will be looking to direct their funds to lucrative investment options, thus, it is of paramount importance that Georgia positions itself as an attractive market.

[1]https://www.imf.org/en/News/Articles/2020/04/07/sp040920-SMs2020-Curtain-Raiser
[2]https://unctad.org/en/PublicationsLibrary/wir2020_en.pdf
[3]https://static1.squarespace.com/static/5548d1b5e4b0680763eeeb53/t/5ecc04bd29db2e1e76cf1635/1590428863594/GEO__AGBC+Annual+Conference_May+2020.pdf
[4]Net FDI inflows are the value of inward direct investment made by non-resident investors in the reporting economy, including reinvested earnings and intra-company loans, net of repatriation of capital and repayment of loans (UN definition).
[5]The data source on which the subsequent analysis and graphs are based on is National Statistics Office of Georgia, unless stated otherwise.

| Basic Economic Indicators | 2016 | 2017 | 2018 | 2019 | 2020 Q1 |
|---|---|---|---|---|---|
| Nominal GDP (mln USD) | 15 141.7 | 16 248.5 | 17 596.6 | 17 736.6* | 3 780.3* |
| GDP per Capita (USD) | 4 062.1 | 4 358.5 | 4 722.0 | 4 763.5* | 1 017.1* |
| GDP Real Growth (%) | 2.9% | 4.8% | 4.8% | 5.1%* | 2.2%* |
| Inflation | 2.1% | 6.0% | 2.6% | 4.9% | - |
| FDI (mln USD) | 1 650.3 | 1 962.6 | 1 265.2 | 1 267.7* | 165.4* |
| Unemployment Rate (%) | 14.0% | 13.9% | 12.7% | 11.6% | 11.9% |
| External Debt (mln USD) | 4 516 | 5 177 | 5 434 | 5 741 | 5 689 |
| Poverty Rate (relative) | 21.0% | 22.3% | 20.5% | 20.1% | - |

*preliminary data