Indebted Georgia on Borrowed Time?

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Government confident it can ride out period of rising debt and low economic performance, but other economists question how sustainable this is.

Economists say Georgia is increasingly at risk from its mounting foreign debt, which could reach critical levels if the government does not curb its appetite for borrowing.

Latest finance ministry figures indicate that the government’s external debt stood at 3.4 billion US dollars at the end of May. That is nearly 19 per cent more than it was at the same point last year, and a whopping 28 per cent higher than at the start of 2009.

As of the end of 2009, the ratio of foreign public debt to gross domestic product, GDP, an important measure of a country’s economic health had surpassed 31 per cent at the end of 2009, compared with 21 per cent the previous year.

While the government continues to accrue loans to pay for a host of projects nationwide, analysts say the economy is growing too slowly to bring in the kind of tax revenues that would allow the state to meet its repayment obligations comfortably.

“In the last three years, foreign debt has grown noticeably, and the trend continues,” said David Narmania, head of the Economic Issues Research Centre in Tbilisi. “By European standards, a critical debt-to-GDP ratio for a country with an economy like Georgia’s would be 50 to 60 per cent. Georgia has not yet reached that point, but it is steadily heading towards it.”

Repayments weigh heavily on the national budget, and are projected to increase exponentially from 95 million dollars this year to 275 million in 2012. According to Narmania, repayments will be especially burdensome in 2013 when a sum of 772 million will be due.

“The state will probably be unable to make such a payment out of its own resources alone, and it will therefore have to borrow more,” Narmania said.

Government officials play down concerns about the state’s creditworthiness.

Deputy finance minister Dmitri Gvindadze says that while the ratio of external public debt to GDP is predicted to grow to 37 per cent this year, “it will start to fall in 2011 and will be just 28 or 29 per cent in 2013 and 2014. That’s not a bad indicator if you consider that the figure is higher than 100 per cent in many other countries, including European Union members,”

Gvindadze said the reason the government was going further into debt was the 2008 war with Russia, after which international lenders made funds available to help rebuild the country.

However, a respected Georgian economist, Demur Giorkhelidze, said that as it understated the scale of the problem, the government was omitting to mention the underlying weakness of the economy.

“If the country’s foreign debt is growing, then its economic potential needs to be growing too, but that isn’t happening,” Giorkhelidze said. “Yes, there are countries where the debt-to-GDP ratio is over 100 per cent yet they still remain creditworthy. But it all depends on how strong a country’s economy is. Georgia’s economy isn’t up to it.”

Giorkhelidze said current growth projections of five or six per cent for this year were over-optimistic, and at best, GDP would probably rise by no more than two or three per cent year on year.

“With a background of negative external factors – above all I mean the global economic crisis and its consequences – Georgia’s government needs to act very carefully because it is a country that is dependant on support from allies, which have been hard hit by the crisis,” he said.

Giorgi Khukhashvili, chairman of the Centre for Public Projects, said the government needed to change its economic policies if it wanted to stay afloat in the longer term.

He called for wide-ranging reforms to create a more liberal business climate free from political interference so as to ensure continued growth. At the moment, he said, “the authorities act as managers rather than partners for businesses. The problem stems from bad legislation and poor administration.”

“The country is not yet on the brink of default; external debt isn’t critical,” Khukhashvili said. “But that isn’t the only issue here. It’s also about the capacity of the economy to service the debt, and it isn’t fit enough.

At the moment we are in a stable phase of development because of donor aid. But the aid will dry up, and what will we fill the gap with then?”

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Location: Georgia
Topic: Economy