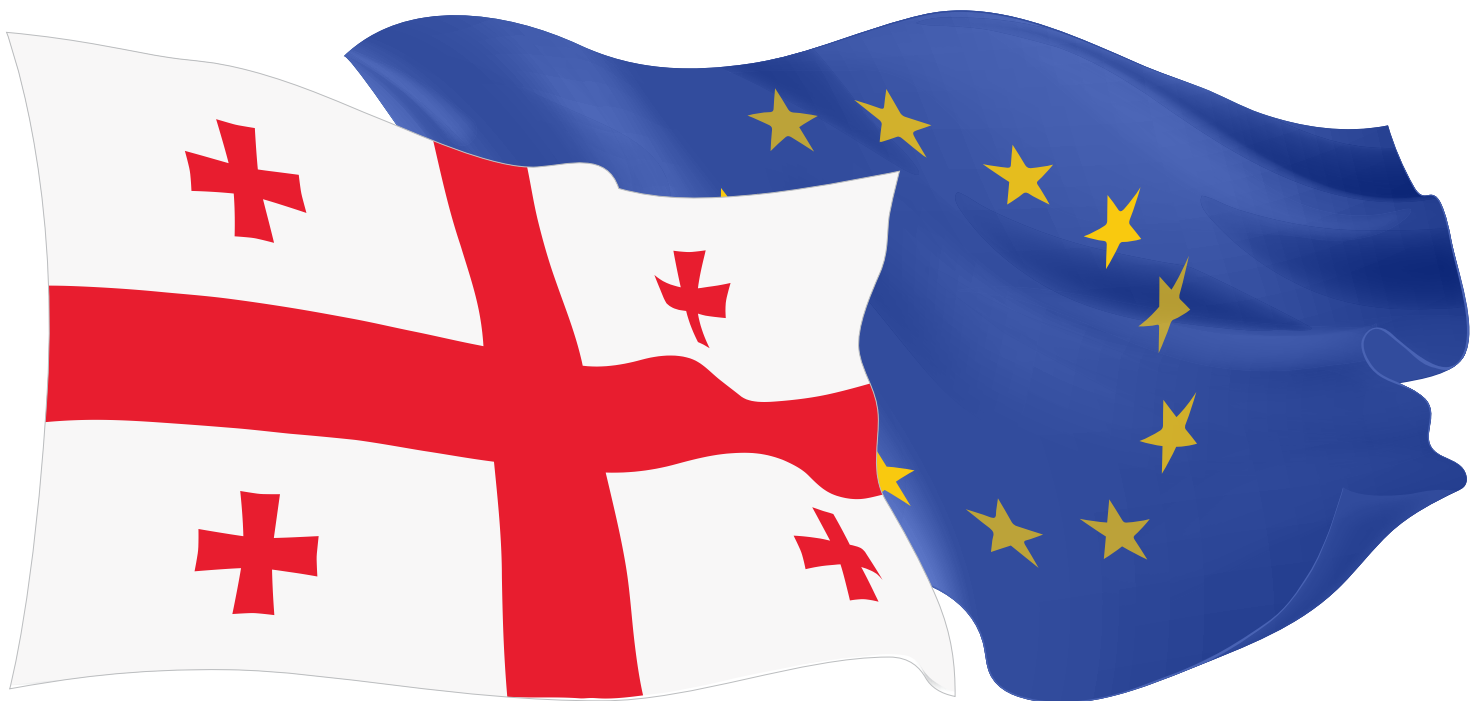




საქართველოს ეროვნული ბანკი  
National Bank of Georgia

# ANNUAL REPORT

## 2023





საქართველოს ეროვნული ბანკი  
National Bank of Georgia

# ANNUAL REPORT

## 2023



# TABLE OF CONTENTS

Abbreviations	7		
Introduction	10		
<b>01</b>			
<b>MACROECONOMIC ENVIRONMENT</b>	18		
1.1 Global Economy	19	4.8 Liquidity Risk	100
1.2 External Sector and Balance of Payments	22	4.8.1 Liquid Asset Structure	100
1.3 Economic Growth	35	4.8.2 Liability Structure	102
1.4 Change in Consumer Prices	37	4.8.3 Retail Funding	103
		4.8.4 Wholesale Funding	105
		4.9 Macroprudential Risks	106
		4.10 Operational Risk	108
		4.10.1 Operational risk in georgia's banking sector	109
		4.11 Cyber Risk	112
		4.11.1 Regulatory Actions Addressing Cyber Risks	113
		4.12 Development of Financial and Supervisory Technologies	114
		4.12.1 Promoting Financial Innovations	114
		4.12.2 Model Risk	118
		4.12.3 Credit information bureau/platform	119
		4.12.4 Open Banking/Finance	121
		4.13 Data Processing and Supervisory Technologies	122
		<b>05</b>	
	43	<b>CONSUMER RIGHTS PROTECTION</b>	124
	44	5.1 Improving the legislative framework	125
	53	5.1.1 Regulation on Consumer Rights	125
	53	5.1.2 The Consumer Rights Law	126
	54	<b>06</b>	
	54	<b>FINANCIAL EDUCATION</b>	132
	55		
	55	<b>07</b>	
	59	<b>NON-BANK SUPERVISION</b>	147
	59	7.1 Regulation of non-banking sector and regulatory framework	148
	60	7.2 Microfinance Organizaations	148
		7.2.1 Lending Entities	156
		7.2.2 Currency Exchange Bureaus	158
		7.2.3 Credit Unions	159
		<b>08</b>	
		<b>SECURITIES MARKET</b>	160
	62	8.1 Activities implemented to develop the securities market and measures taken to enhance the transparency of the market	161
	65	8.2 Securities Market Indicators	163
	69	8.3 Overview of Market Players	166
	71	8.4 Investment Activities of the Pension Agency	170
	72	8.5 Overview of Activities of Investment Funds	172
		<b>03</b>	
		<b>FINANCIAL STABILITY POLICY</b>	
		3.1 Development of Financial Stability Framework	
		3.2 Recovery and Resolution Framework	
		3.3 Interagency Financial Stability Committee	
		3.4 Liquidation of Financial Institutions	
		<b>04</b>	
		<b>BANKING SUPERVISION</b>	
		4.1 Development of Supervisory Framework	
		4.2 Corporate Governance and Group Structure Risk	
		4.3 Capital Adequacy	
		4.4 Financial Reporting and Transparency	
		4.5 Credit Risk	
		4.6 Market Risk	
		4.6.1 Interest Rate Risk	
		4.7 Profitability Risk	

## 09

### LAUNDERING INSPECTION AND SUPERVISION

173

## 10

### PAYMENT SYSTEMS OVERSIGHT

178

10.1 Legislative Framework

179

10.2 Transactions in the RTGS System

181

10.3 Electronic Means of Payment

186

10.4 Card Instruments Market

188

10.5 Payment Service Providers

193

## 11

### SUPERVISION OF PAYMENT SERVICE PROVIDERS AND REGISTRATION OF VIRTUAL ASSET SERVICE PROVIDERS

195

## 12

### DEVELOPMENT OF INFORMATION TECHNOLOGIES

201

## 13

### ORGANIZATION OF CASH AND EMISSION ACTIVITIES

207

## 14

### INTERNAL AUDIT AND CENTRALIZED RISK MANAGEMENT

218

14.1 Internal Audit

219

14.2 Non-financial Risk Management

220

14.3 Business Continuity Management

221

## 15

### PUBLIC RELATIONS AND INTERNATIONAL COOPERATION

222

## 16

### HUMAN RESOURCE MANAGEMENT AND DEVELOPMENT

228

## 17

### DEVELOPMENT OF LEGAL FRAMEWORK

231

## 18

### STATISTICAL ACTIVITIES

266

## 19

### FINANCIAL STATEMENTS

272

### BOXES

BOX 1. SHARE OF PROFIT AND WAGES IN INFLATION

41

BOX 2. CREATING MONEY IN THE ECONOMY: GEORGIA'S CASE

50

BOX 3 THE PURPOSE OF CREATING A NEW FINANCIAL INSTITUTION,  
THE MICROBANK, AND ITS ACTIVITIES

75

BOX 4. SUPPLEMENTARY SUPERVISION OF REGULATED ENTITIES  
IN THE FINANCIAL CONGLOMERATE

77

BOX 5. UPDATED FRAMEWORK MANAGEMENT OF CONFLICT  
OF INTEREST

80

BOX 6. PRIVACY ENHANCEMENT TECHNOLOGIES (PET)

117

BOX 7. GENERATIVE AI

118

### DIAGRAMS

Diagram N 1.1 Real GDP Growth in the World

19

Diagram N 1.2 CPI inflation in the world

21

Diagram N 1.3 Real GDP Growth in Georgia and weighted average  
growth of trading partner countries

22

Diagram N 1.4 The ratio of Current Account Components to GDP

23

Diagram N 1.5 Annual Change in Export and Import of Goods

24

Diagram N 1.6 Exports structure by country 2023

25

Diagram N 1.7 Top Ten Export Commodities

26

Diagram N 1.8 Import Structure by Country in 2023

27

Diagram N 1.9 Top Ten Import Commodities

28

Diagram N 1.10 Revenues from International Travel

29

Diagram N 1.11 Number of International Visitors to Georgia by Country

29

Diagram N 1.12 Revenues from export of goods and services to GDP

30

Diagram N 1.13 Personal Remittances

30

Diagram N 1.14 Instant Money Transfers by Country

31

Diagram N 1.15 Financing the current account deficit (in % of GDP)

32

Diagram N 1.16 Assessment of international reserve adequacy  
(ARA metric) according to the IMF methodology

33

Diagram N 1.17 Indices of real and nominal effective exchange  
rates (Dec. 2015=100)

34

Diagram N 1.18 Real GDP Growth by Expenditures

37

Diagram N 1.19 Investments to GDP

37

Diagram N 1.20 Headline and Core (excluding food, energy  
and tobacco) Inflations

38

Diagram N 1.21 Contribution of major components to inflation

39

Diagram N 1.22 Imported, mixed and domestic inflation

39

Diagram N 1.23 Annual change in CPI and GDP Deflator

41

Diagram N 1.24 Decomposition of GDP Deflator Change

42

Diagram N 2.1 Monetary Policy Rate

46

Diagram N 2.2 Interest Rate Spread and Lending Activity  
(annual growth rate of loans by currencies)

46

Diagram N 2.3 Factors affecting annual change in refinancing loans

48

Diagram N 2.4 Interbank Money Market

48

Diagram N 2.5 Banking Sector Dollarization (excluding the exchange rate effect)	49	Diagram N 4.41 Distribution of total loss of the banking system for 2023 by categories of events	111
Diagram N 2.6	51	Diagram N 4.42 Number and volume of current loans (2023)	119
Diagram N 2.7 Dynamics of Certificates of Deposit Portfolio 2018-202	56	Diagram N 4.43 Unique number of current borrowers (2023)	119
Diagram N 2.8 Dynamics of Treasury Bills and Treasury Bonds Portfolio 2018-2023	57	Diagram N 4.44 Number of customer claims (2023)	120
Diagram N 2.9 Treasury Bills and treasury bonds portfolio dynamics by ownership 2018-2023	57	Diagram N 4.45 Number of cashed international remittances (2023)	120
Diagram N 2.10 Official International Reserves 1997-2023 (million USD)	61	Diagram N 4.46 The number of unique persons cashing the remittances (2023)	121
Diagram N 3.1 Comparison of Loan and Nominal GDP growth rates	65	Diagram N 5.1 Distribution of Claims at Commercial Banks By Product	128
Diagram N 3.2 Concentration of System-maker banks in the banking market (As of December 31, 2023)	70	Diagram N 5.2 Distribution of Claims at Commercial Banks By Nature	129
Diagram N 3.3 Progress of Liquidation of Financial Institutions in 2023	73	Diagram N 5.3 Distribution of Claims at Commercial Banks By Status	129
Diagram N 4.1 Capital Adequacy Ratios under Basel III	82	Diagram N 5.4 Distribution of Claims at Microfinance Organizations By Product	130
Diagram N 4.2 Pillar 2 aggregate requirements for commercial banks as of 31 December, 2023	84	Diagram N 5.5 Distribution of Claims at Microfinance Organizations By Nature	130
Diagram N 4.3 Change in total loan portfolio compared to the previous year	85	Diagram N 5.6 Distribution of Claims at Microfinance Organizations By Status	130
Diagram N 4.4 Monthly weighted average interest rates on loans per segment	86	Diagram N 7.1 Number of microfinance organizations and branches	149
Diagram N 4.5 Average weighted interest rates on loans for the corporate segment	87	Diagram N 7.2 Number of staff at microfinance organizations	149
Diagram N 4.6 Weighted average interest rates on loans for the MSME segments	87	Diagram N 7.3 Regional distribution of the branches and borrowers of microfinance organizations	149
Diagram N 4.7 weighted average interest rates on loans for the retail segment	88	Diagram N 7.4 Number of microfinance organizations and borrower	150
Diagram N 4.8 Share of economically vulnerable sectors in the total loan portfolio	89	Diagram N 7.5 Volume of loan portfolio of microfinance organizations	150
Diagram N 4.9 Segment balances by currency at the end of 2023 (except interbank loans)	90	Diagram N 7.6 Loan Portfolio Structure	151
Diagram N 4.10 Composition of the retail portfolio by currencies	91	Diagram N 7.7 Cost of the weighted average interest rates and funds in the portfolio	151
Diagram N 4.11 Quality of Retail Portfolio and Cost of Risk by products	92	Diagram N 7.8 Loan Portfolio Quality	152
Diagram N 4.12 Change in cost of risk (Dec-2022 - Dec-2021)	93	Diagram N 7.9 Dollarization of the loan portfolio	152
Diagram N 4.13 Loan Portfolio by Quality Indicators (except interbank loans)	93	Diagram N 7.10 Source of Funding	152
Diagram N 4.14 Share of restructured loans by currencies in total loan	93	Diagram N 7.11 Borrowings Structure	153
Diagram N 4.15 Share of non-performing loans by currencies in the business loans	94	Diagram N 7.12 Borrowings from individuals and the number of individual creditors	153
Diagram N 4.16 Share of non-performing loans by currencies in the mortgage loans	94	Diagram N 7.13 Funds of non-residents	154
Diagram N 4.17 Loan Loss Reserves to Total Portfolio	95	Diagram N 7.14 Regulatory Capital	154
Diagram N 4.17 Loan Loss Reserves to Total Portfolio	95	Diagram N 7.15 Structure of Regulatory Capital	155
Diagram N 4.19 Loan Write-offs and Recoveries	96	Diagram N 7.16 Capital structure by residency	155
Diagram N 4.20 Problem Assets	96	Diagram N 7.17 Dynamics of net and operating income	156
Diagram N 4.21 Repossessed assets	97	Diagram N 7.18 Regional distribution of structural units of lending entities	156
Diagram N 4.22 Balance sheet and consolidated open currency positions to regulatory capital	98	Diagram N 7.19 Lending entities and the number of borrowers	157
Diagram N 4.23 Change in EVE to Tier1 Capital	99	Diagram N 7.20 Dynamics of total assets and net loans	157
Diagram N 4.24 Return on Equity and Assets	99	Diagram N 7.21 Source of funding for lending entities	158
Diagram N 4.25 costs to income and assets ratio	100	Diagram N 7.22 number and branches of currency exchange bureaus	158
Diagram N 4.26 Level of Liquid Assets	100	Diagram N 7.23 Regional distribution of structural units of currency exchange bureaus	159
Diagram N 4.27 Dynamics of LCR Ratio (10 day floating average)	101	Diagram N 8.1 Balances of NGO Bonds at the end of the period (2014-2023)	163
Diagram N 4.28 Net Stable Funding Ratio	101	Diagram N 8.2 Balances of Corporate Bonds by International Credit Ratings (2014-2023)	164
Diagram N 4.29 Liquidity Gap – Assets to Liabilities ratio	102	Diagram N 8.3 Industry distribution of balances of corporate bonds (2022)	164
Diagram N 4.30 Volume and structure of liquid assets	102	Diagram N 8.4 Balances of Treasury Securities by Maturities (2010-2023)	165
Diagram N 4.31 Liability Structure	103	Diagram N 8.5 Secondary Market Activity for debt securities issued in Georgia (2015-2023)	165
Diagram N 4.32 Annual Growth of Non-bank Deposits	103	Diagram N 8.6 Distribution of Treasury securities by ownership (2014-2023)	166
Diagram N 4.33 Share of non-resident depositors	104	Diagram N 8.7 Total value of securities of clients registered in securities accounts of brokerage companies (GEL)	167
Diagram N 4.34 Share of non-resident depositors (Dec 2023)	104	Diagram N 8.8 Distribution of securities of clients registered in securities accounts of brokerage companies (securities issued in foreign countries and Georgia)	167
Diagram N 4.35 non-resident deposits by countries (Dec 2023)	105	Diagram N 8.9 Key Trade Indicators (transactions offered at trading session and recorded in stock exchange) 2012-2023	168
Diagram N 4.36 Total loans to non-bank deposits ratio by currencies	105	Diagram N 8.10 Number of transactions recorded on trading session and stock exchange by years (2012-2023)	168
Diagram N 4.37 Dynamics of Dollarization of Deposits (fixed exchange rate)	107	Diagram N 8.11 Securities deposited with the Central Depository by years (2012-2023)	169
Diagram N 4.38 Total losses for banking sector in 2023	110	Diagram N 8.12 Funds deposited at the Central Depository by years (2012-2023)	169
Diagram N 4.39 total losses for the last five years (2019-2023)	110		
Diagram N 4.40 Dynamics of the operating loss indicator in 2023 (total loss to total income)	111		



# ABBREVIATIONS

<b>API</b> (Application Programming Interface)	<b>GFIN</b> (Global Financial Innovation Network)
<b>ARA</b> (Assessing Reserve Adequacy)	<b>GGF</b> (Green for Growth Fund)
<b>BCBS</b> (Basel Committee on Banking Supervision)	<b>GRAPE</b> (General Risk Assessment Program)
<b>BI</b> (Business Intelligence)	<b>GSSS</b> (Georgian Securities Settlement System)
<b>BIA</b> (Business Impact Analysis)	<b>HR</b> (Human Resource)
<b>BIS</b> (Bank for International Settlements )	<b>HRMS</b> (Human Resource Management System)
<b>BISIP</b> (BIS Investment Pool)	<b>IFC</b> (International Finance Corporation)
<b>BMatch</b> - Bloomberg foreign exchange trading platform	<b>IFRS</b> (International Financial Reporting Standards)
<b>BSCEE</b> (Banking Supervisors from Central and Eastern Europe)	<b>IFT</b> (Inflation Forecast Targeting)
<b>CAREC</b> (Central Asia Regional Economic Cooperation)	<b>IIA</b> (Institute of Internal Auditors)
<b>CBDC</b> (Central Bank Digital Currency)	<b>IMF</b> (International Monetary Funds)
<b>CICR</b> (Currency Induced Credit Risk)	<b>IOSCO</b> (Technical Committee of the International Organization of Securities Commissions) –
<b>CIF</b> (Cost, Insurance and Freight)	<b>IPPF</b> (International Professional Practice Framework) –
<b>CPMI</b> (Committee on Payments and Market Infrastructures)	<b>ISO</b> (International Organization for Standardization)
<b>CRA</b> (Credit Risk Adjustment buffer)	<b>IT</b> (Information Technology)
<b>CRD IV</b> (Capital Requirement Directive)	<b>LCR</b> (Liquidity Coverage Ratio)
<b>CRR</b> (Capital Requirements Regulation)	<b>LTV</b> (Loan to Value)
<b>CSP</b> (Customer Security Programme)	<b>NGFS</b> (Network for Greening the Financial System)
<b>CYFI</b> (Child and Youth Finance International)	<b>NII</b> (Net Interest Income)
<b>DDos</b> (Distributed Denial-of-service attack)	<b>NPL</b> (Non-Performing Loan)
<b>DeFi</b> (Decentralized Finance)	<b>NSFR</b> (Net Stable Funding Ratio)
<b>DPM</b> (Data Point Model)	<b>OECD</b> (Organizaton for Economic Co-operaton and Development)
<b>EAD</b> (Exposure At Default)	<b>OECD/INFE</b> (Organizaton for Economic Co-operaton and Development/International Network on Financial Education)
<b>EBA</b> (European Banking Authority)	<b>PTI</b> (Payment to income ratio)
<b>EBITDA</b> (Earnings Before Interest, Taxes, Depreciation and Amortization)	<b>ROA</b> (Return on Assets)
<b>EBRD</b> (European Bank for Reconstruction and Development)	<b>ROE</b> (Return on Equity)
<b>ECB</b> (European Central Bank)	<b>ROSC</b> (Report on the Observance of Standards and Codes)
<b>EFSE DF</b> (Development Facility of the European Fund for Southeast Europe)	<b>RTGS</b> (Real Time Gross Settlement)
<b>ESG</b> (Environmental, Social, and Governance)	<b>RTP</b> (Request to Pay)
<b>ETL</b> (Extract, Transform, Load) - General procedure for importing data from different sources (MS SQL, MS Excel, etc.), converting and saving in the required format	<b>SBA</b> (Stand-by Arrangement) an IMF support program
<b>EVE</b> (Economic Value of Equity)	<b>SBFN</b> (Sustainable Banking and Finance Network)
<b>FAO</b> (Food and Agriculture Organization)	<b>SDR</b> (Special Drawing Rights)
<b>FATF</b> (Financial Action Task Force)	<b>SECO</b> (State Secretariat for Economic Affairs)
<b>FEA Georgia</b> (Financial Education Association of Georgia)	<b>SEPA</b> (Single Euro Payment Area)
<b>FinEdu</b> - The first Georgian educational web portal for financial education - <a href="http://www.finedu.gov.ge">www.finedu.gov.ge</a> („FinEdu“)	<b>SMEDA</b> (Small and Medium Enterprise Development Authority)
<b>FINREP</b> - (Financial Reporting) (An European regulation which applies to credit institutions)	<b>SWIFT</b> (Society for Worldwide Interbank Financial Telecommunication)
<b>FOB</b> (Free on Board)	<b>TIBR</b> (Tbilisi Interbank Rate)
<b>FRD</b> (Fraud Data)	<b>TMS</b> (Taxonomy Management System)
<b>FSAP</b> (Financial Sector Assessment Program) –	<b>UNCTAD</b> (United Nations Conference on Trade and Development)
<b>FSI</b> (Financial Stability Indicators)	<b>USAID</b> (United States Agency for International Development)
<b>GAN</b> (General Adversarial Networks)	<b>XBRL</b> (Extensible Business Reporting Language)
<b>GET</b> (German Economic Team)	





# INTRODUCTION

The 2023 annual report of the National Bank of Georgia (NBG) has been prepared in accordance with Articles 60 and 61 of the Organic Law on the National Bank of Georgia. This report includes a comprehensive review of audited financial statements and monetary, foreign exchange and regulatory policies.

According to the Organic Law of Georgia on the National Bank of Georgia, the primary objective of the National Bank of Georgia is to ensure price stability. Additionally, the National Bank of Georgia is responsible to maintain the stability and transparency of the financial system and to promote sustainable economic growth of the country so as not to jeopardize its core objectives. Price stability implies having a level of inflation in the medium term that is optimal for high and sustainable economic growth. Focusing on the medium-term is important as inflation may deviate from the target rate due to shocks. However, through the policies implemented by the NBG, and in the absence of additional shocks, inflation is expected to return to the target in the medium term, thus achieving price stability.

To ensure price stability, the National Bank of Georgia implements monetary policy under an inflation targeting regime, globally considered to be the most effective model. This regime implies announcing an inflation target in advance and implementing policies in a manner so that inflation comes close to the target level in the medium term. This regime ensures that inflation stays close to its target rate over the medium term while allowing temporary deviations in response to exogenous shocks to minimize overall macroeconomic fluctuations.

Monetary policy primarily influences demand, so central banks mainly respond to demand shocks. As responding to supply shocks (such as increases in excise

taxes, global commodity prices, and international transportation costs) is associated with significant costs for the economy and can lead to fluctuations in economic growth and, in the long term, a reduction in employment. An exception is made when a supply shock is significant or prolonged enough to affect inflation expectations.

This approach ensures price stability and the lowest long-term interest rates compared to other alternatives. As monetary policy instruments and their transmission mechanisms develop, public expenditure to maintain price stability decreases. Therefore, the National Bank of Georgia is persistently improving its monetary policy instruments and enhancing the efficiency of the monetary policy transmission mechanism.

The key instrument of the National Bank of Georgia's monetary policy is the monetary policy rate, which is adjusted based on the inflation forecast. If inflation forecast exceeds the target level, the National Bank of Georgia tightens monetary policy. Conversely, if the inflation forecast is below the target level, the National Bank of Georgia loosens monetary policy.

At the current stage of Georgia's economic development, the long-term inflation target rate has been set at 3% since 2018. The National Bank of Georgia (NBG) first adopted the inflation targeting regime in 2009. Since then (2009 – 2022), the average annual inflation rate in Georgia has been 4.5%. Prior to adopting this regime, inflation averaged 6.6% during 2000-2008. When inflation targeting was initially introduced, the inflation target was set at 6%, but it was gradually reduced to 3% by 2018.

In 2023, inflationary pressures were alleviated. Starting from early 2023, inflation began to decline and remained below the 3% target after March,

averaging 2.6% during the year. Core inflation, which excludes volatile prices of food, energy and cigarettes, averaged 3.8%. The decline in inflation early in the year was due to the diminishing impact of external shocks. Later in the year, internal economic factors contributed to the decrease, supported by a timely and sufficiently tightened monetary policy that reduced inflationary expectations. Additionally, the inflation of domestically produced products and services significantly decreased.

Considering the inflation trends and forecasts, the NBG began a gradual withdrawal from its strict monetary policy. At the beginning of the year, the monetary policy rate was maintained at 11%. From May onwards, the NBG started to reduce the rate incrementally. Although inflation began to decrease early in 2023, primarily due to the neutralization of exogenous factors, significant inflationary pressure from local factors persisted and reflected in the relatively high core and domestic inflation. High inflationary risks remained due to the acute geopolitical situation and global uncertainty, posing potential price increase risks for certain imported products.

Given these circumstances, the NBG adopted a cautious approach, gradually easing its strict monetary policy. This strategy helped to normalize inflationary expectations and further reduced inflation. Along with headline inflation, the domestic, core and service inflation decreased throughout the year. By December 2023, the monetary policy rate was decreased by 1.5 percentage points from its peak, to 9.5%.

According to preliminary data, Georgia's real Gross Domestic Product (GDP) increased by 7.5 percent in 2023 compared to the previous year. The investments were the main drivers of this growth, contributing 5.4 percentage points (pp) to the overall 7.5 percent increase. This surge in investments was partly due to a significant rise in capital expenditures from the budget and business loans. Consumption also contributed positively to economic growth, with a 3.1 pp. However, the impact of foreign demand on economic growth

was relatively weak. This was due to the diminishing effect of migration and a decrease in foreign demand for export of goods.

Throughout the year, the growth rate of external inflows normalized, largely due to the fading of the one-time migration effect, as it was expected. In 2022, the number of long-term visitors from Russia, Belarus, and Ukraine had increased significantly due to the ongoing war. However, in 2023, the growth rate of citizens from these countries slowed down. Despite the fading of the migration effect, in light of increased visitors from EU and Türkiye, revenues from international travel increased. Nonetheless, due to the weakening of the base effect and the one-time effect of migration, instant money transfers declined annually. Additionally, external demand for domestically produced export goods was weak, affected by reduced competitiveness due to an appreciated exchange rate and slower economic growth in trading partner countries. This was partially offset by an increasing trend in the re-export of cars, though this growth also slowed down towards the end of the year. The weakening of external inflows was largely balanced by the import of goods. Namely, the decrease in prices of oil products and other commodity groups on the global market reduced the costs of imported goods. As a result, the current account deficit of the balance of payments amounted to 4.3 percent of GDP, the lowest historical level for Georgia. With historically low current account deficits, the real effective exchange rate appreciated by 2.1 percent and the nominal effective exchange rate by 14.8 percent in 2023, significantly contributing to the reduction in inflation.

In 2023, the gross international reserves of the National Bank of Georgia increased by USD 108.1 million compared to the previous year, reaching a historically high amount of USD 5.01 billion as of December 31, 2023. A high level of reserves ensures the country's macroeconomic stability and positively impacts its creditworthiness. Foreign exchange interventions and funds raised by the government from international

organizations (including program grants and loans) contributed to the growth of reserves. In 2023, the National Bank's net purchases in the foreign exchange market (both through foreign exchange auctions and the BMatch platform) amounted to USD 1.28 billion. However, foreign debt servicing and other government foreign exchange expenses impacted international reserves. Additionally, the decrease in balances on the reserve accounts of commercial banks, due to both the easing of reserve requirements and the decrease in dollarization of deposits, also affected reserves.

Promoting financial stability, as a prerequisite for sustainable economic growth, is one of the most important tasks of the National Bank of Georgia (NBG). To ensure financial stability, the NBG implements macroprudential policy and financial sector supervision. By identifying, evaluating, and monitoring systemic risks, the NBG develops response policies to mitigate these risks, thus enhancing the stability of the financial system.

The main instrument of the NBG's macroprudential policy is the capital countercyclical buffer. Its purpose is to limit excessive lending to the economy that leads to increased systemic risks. In March 2023, the Financial Stability Committee set the neutral (base) rate of the countercyclical buffer at 1%, implying that the buffer rate will be 1 percent under normal conditions. However, given the globally tightened financial conditions, the countercyclical buffer will be built up gradually.

The NBG is actively working to reduce structural risks caused by the high level of financial dollarization. Despite significant reductions in dollarization due to measures taken by the NBG, dollarization and related risks remain significant challenges for the financial sector. To mitigate these risks, the NBG has imposed additional requirements on regulated financial institutions. Starting January 1, 2024, the limit on unhedged foreign currency loans will increase to 300,000 GEL, and from May 1, 2024, it will increase

to 400,000 GEL. The NBG will continue to gradually increase this limit in the future, taking into account the macroeconomic environment and risks.

Alongside easing monetary policy, the NBG has also eased conditions for issuing consumer loans. Given that the growth rate of unsecured consumer loans in 2023 decreased compared to 2022 and that credit activity remains at a sustainable level, the Financial Stability Committee decided that from November 1, 2023, the maximum term limit for these loans will increase from 3 years to 4 years.

In May 2023, to promote financial stability, the NBG established the minimum requirement for own funds and eligible liabilities (MREL) for systemic banks. This recommendation was issued in 2021 within the framework of the joint financial sector assessment program (FSAP) conducted by the International Monetary Fund (IMF) and the World Bank in Georgia, and it is based on the practices envisaged by the European Bank Recovery and Resolution Directive (BRRD). The MREL requirement aims to create a balance sheet structure in advance that allows banks to maintain stability through recapitalization during stressed situations.

These measures reflect the NBG's ongoing efforts to enhance financial stability and support sustainable economic growth by addressing both immediate and structural risks within the financial system.

The financial system of Georgia maintained stability in 2023, continuing to provide uninterrupted credit to the economy. Banks demonstrated sound capital and liquidity ratios, and the quality of assets improved compared to the previous year. As of December 2023, the annual growth of loans, excluding the effect of the exchange rate, reached 17.2%, primarily driven by the growth of business loans. The ratio of loans to gross domestic product (GDP) gradually approached the long-term trend, significantly reducing the negative gap seen at the beginning of the previous year. This

reflects the normalization of high economic growth and sustainable credit activity.

In 2023, the NBG actively implemented measures outlined in the Sustainable Finance Roadmap. The NBG published its third report on sustainable finance, providing an overview of current trends, policies, and future plans in this area in Georgia.

As part of sustainable finance efforts, the NBG developed Environmental, Social, and Governance (ESG) Guidelines in 2023. Additionally, in collaboration with the International Finance Corporation (IFC), the NBG completed the development of an ESG Scorecard for commercial banks. This scorecard assesses the ESG practices and approaches of commercial banks using a risk scorecard methodology based on various ESG indicators.

In accordance with the Corporate Governance Code (CG Code), banks disclosed ESG information using the NBG template for the third time in 2023. The ESG disclosures for 2021-2023 by financial institutions are published on the NBG website, providing valuable information for investors and other stakeholders.

From 2023, commercial banks in Georgia can designate a loan as green, social, and/or sustainable only if it meets the technical criteria defined in the Taxonomy. Banks are required to make monthly statements of green loans using the format specified by the taxonomy regulation. Additionally, in their Pillar 3 annual reports, banks must disclose information related to green, social, and sustainable loans in accordance with the taxonomy regulation.

In 2023, the NBG developed a methodology and tool for calculating and reporting financed emissions for Georgia's financial sector. This project, implemented in cooperation with the German Sparkassenstiftung for International Cooperation, is detailed in a report available on the NBG website. Moreover, the NBG published a research paper titled which analyzes the

links between biodiversity loss and financial stability.

Since 2021, the NBG has been working on implementing the framework for the recovery and resolution of commercial banks (the resolution framework). Active work continued throughout 2023, with close cooperation from the International Monetary Fund (IMF) and the World Bank. The World Bank team conducted the second part of the resolution simulation mission, testing the processes related to the implementation of the resolution. This simulation assessed preparedness for financial crises and provided practical recommendations.

In 2023, each participant of the banking sector has prepared recovery plans, which include measures to be implemented by the commercial bank to improve the financial situation, restore and maintain critical functions in the event of significant financial difficulties and/or disruption of critical functions. The National Bank of Georgia examined the documents and, considering the regulatory rule and international good practice, provided the appropriate feedback. Commercial banks will update recovery plans, and the National Bank of Georgia will evaluate them annually, and the evaluation document will be integrated into the overall risk management framework of banks.

In 2023, according to the planned schedule and to discuss thematic issues, the meeting of the resolution committee created within the framework of the resolution was held. In the course of 2023, the need for resolution in the banking sector or its early warning signs were not revealed, and the grounds for the implementation of recovery measures were not observed.

In 2023, the National Bank of Georgia (NBG) continued its established practice and issued another supervisory strategy document for 2023-2025. This document outlines the priorities of the supervisory strategy for 2023-2025 and the planned activities for their implementation. Additionally, it includes a summary

report on the implementation of the strategy for 2020-2022, providing an overview of the achievements and challenges faced during that period.

Compared to previous years, the National Bank of Georgia (NBG) conducted the work on the supervisory strategy for 2023-2025 with even greater involvement of the private and civil sectors. Opinions and recommendations from interested parties were solicited through a publicly published questionnaire<sup>1</sup>, followed by the publication of the initial supervisory strategy document for consultation<sup>2</sup>. This inclusive approach resulted in the determination of supervisory priorities, which take into account the NBG's activities for 2023-2025. The priorities of the 2023-2025 supervisory strategy include:

- Improvement of the financial sector risk management framework and proactive response to the results;
- Promotion of competition in the financial sector;
- Encouraging financial innovation and development of supervisory technologies;
- Approximation to international standards;
- Strengthening the supervisory function of the NBG and increasing transparency.

In 2023, the Parliament of Georgia adopted the Law of Georgia "On the Activities of Microbanks" and related bills to create a medium-sized, stable business model and a new financial institution with a high reputation in the financial sector, to promote lending to entrepreneurial and agricultural activities, and to increase competition and reduce interest margins on credit products. The adoption of the legislative package led to the microbank being added to the list of supervised entities of the National Bank of Georgia. Early in the year, the National Bank of Georgia worked

particularly actively on the development of subordinate legal acts and their approval within the relevant terms. The NBG actively cooperated with the private and public sectors and transparently managed the work process, including using the format of public consultations. As a result, a regulatory framework for microbanks was developed, within the framework of which a number of important issues, including licensing requirements, the suitability of administrators and the conditions for acquiring a significant share (including eligibility criteria), were based on the existing regulation for commercial banks and aligned with European and international standards.

In line with the Association Agreement between Georgia, the European Union, and the European Atomic Energy Community, Georgia has taken steps to align its laws with EU legislation. Specifically, to align with the European Parliament and Council Directive 2002/87/EC of December 16, 2002, the National Bank of Georgia, in cooperation with the State Insurance Supervision Service of Georgia (a legal entity of public law), has prepared the draft Law of Georgia "On Additional Supervision of Regulated Enterprises Included in the Financial Conglomerate," along with related draft laws. The draft law aims to ensure comprehensive supervision of financial conglomerates, improving regulatory oversight and stability within the financial sector. The National Bank of Georgia shared and discussed the draft law with the banking association and the banking sector to gather feedback and ensure a collaborative approach to the new regulations.

The said legislative package was adopted by the Parliament of Georgia in three readings. As a result, the NBG was granted the right to exercise additional supervision over the regulated entities included in the financial conglomerate.

1. The National Bank of Georgia publishes a questionnaire to ensure the involvement of the sector in the process of developing a new supervisory strategy document ([nbg.gov.ge](http://nbg.gov.ge))

2. The National Bank of Georgia publishes the initial draft of the Supervisory Strategy document for 2023-2025 years for public review ([nbg.gov.ge](http://nbg.gov.ge))

The National Bank of Georgia, in cooperation with the relevant counterpart agency, continues to determine the need for the development of legal acts based on the said law and the activities related to their development within the relevant period.

In 2023, within the framework of the mandate, in the process of developing legislative and subordinate legal acts, the NBG approved the guidelines for holding public consultations with the sector and interested parties.

The NBG has long implemented the practice of public consultations with the sector and stakeholders in the process of developing legal acts, however, the development of the manual will help to formalize the process and bring it closer to the best international practices, resulting in even higher degree of transparency on the part of the NBG in the process of policy development and implementation. The guidelines detail the process and timelines for conducting consultations.

In 2023, the NBG continued to bring the capital adequacy standards closer to the EU regulations. In particular, in accordance with the changes made in the said regulations, the commercial bank is obliged to deduct the foreseeable dividend from the undistributed profit to be included in the common equity tier 1 capital. In addition to the criteria for classification as additional primary and secondary capital instruments, a new requirement was added. The instrument contract must now include conditions for writing off or converting the obligations of the commercial bank for the purpose of recapitalization. Furthermore, the legislation governing the instrument agreement should allow for the use of resolution instruments to write off or convert the obligations of the commercial bank for recapitalization purposes in case of the bank's resolution.

In October 2023, the National Bank of Georgia (NBG) implemented significant changes to the regulations on conflict of interest management, aiming to align with international standards and enhance control

and management standards by commercial banks. These changes require banks to adjust their policies and procedures within 6 months to comply with the new requirements, with certain provisions becoming effective immediately upon the order's enactment.

The amendments focused on these areas:

- Definition of Related Party: The definition of a related party was revised, requiring entities to be identified on the list of related persons. In some cases, banks were given a 12-month grace period to update their existing list of related persons. Additionally, ownership of a significant share in a bank was established as a criterion for recognition as a related party.
- Collateral Requirements: The regulations now include general requirements related to collateral, specifying the types of collateral permissible for creating a risk position with related parties. The assessment of compliance of such collateral with the regulation/documentation is also addressed.

One of the most important projects in terms of convergence with international standards was the transition of commercial banks' supervisory reports to International Financial Reporting Standards (IFRS), as outlined in the 2020-2022 supervisory strategy. With the adoption of IFRS, the public and supervisory reporting of the banking sector in Georgia has become more aligned with the practices of Europe and other developed countries. Consequently, from January 1, 2023, commercial banks have been complying with supervisory regulations based on IFRS numbers and approaches.

By December 31, 2023, the total loan portfolio of the banking system reached 52.9 billion GEL, marking an annual growth of 16.6 percent when excluding the effect of the exchange rate (using the exchange rate at the end of 2022). The composition of the loan portfolio (excluding interbank loans) has seen slight changes in terms of segments; specifically, the share of the corporate segment has increased over the year,

while the shares of the retail and small and medium enterprise segments in the total portfolio have decreased.

The loan portfolio is sectorally diversified. Notably, at the end of December 2023, the total share of economically vulnerable sectors (real estate development, real estate management, hotels and tourism, restaurants and catering establishments, car dealers) in the portfolio amounted to 17.7 percent, which is 1.1 percentage points higher than the same figure in December of the previous year.

Regarding the quality of the retail loan portfolio, the share of non-performing loans in the total retail products portfolio has decreased, largely due to the improvement in the quality of consumer and mortgage loans. Additionally, the volume of the retail products portfolio has increased more compared to the previous year. The percentage share of expected credit losses in the portfolio for all retail products, except overdrafts, has reduced, reflecting the effect of portfolio write-offs and growth.

During 2023, the exchange rate of GEL appreciated against the main currencies, while banks continued their activities with stable currency positions. The currency position limit is 20 percent of the regulatory capital. At the end of the year, the cumulative foreign exchange position is long and is within 1.9 percent of regulatory capital. From 2023, the currency position is presented in accordance with International Financial Accounting Standards. Dollarization in the banking system of Georgia is still high, as a result, the currency risk factor remains important for Georgian banks. The National Bank of Georgia continues its supervisory work in the direction of improving foreign exchange risk management. In terms of the decomposition of profits in 2023, several important factors affecting the profitability of the banking system should be noted. During the year, net interest income increased against the background of increased credit activity. Also,

operational efficiency of banks has increased.

During 2023, the volume of liquid assets in relation to total assets has slightly decreased, although banks operate with adequate liquidity buffers. Liquid assets reach 21 percent of total assets and 33.4 percent of non-bank deposits. The liquidity coverage ratio (LCR) remained at a high level. The Net Stable Funding Ratio (NSFR) also remained high. The minimum requirement is 100 percent, although banks operate with adequate buffers, and as of the end of the year, the ratio reaches 126 percent.

The National Bank of Georgia actively works with commercial banks to assess and improve operational and cyber risk management processes. Commercial banks continue to be checked for their compliance with the operational risk management framework of the NBG. Among these, a lot of attention is paid to commercial banks' business continuity in various scenarios, which also includes outsourcing processes (including cloud services).

In 2023, the team of the operational risks department of NBG actively worked on digital banks and microbanks as the new supervisory entity. The Operational Risks Department developed regulations related to operational risk management, which were also published on the website of the National Bank of Georgia. The Operational Risk Division continues to oversee the implementation of the operational risk management framework for digital and micro banks. The regulation on operational risk management by commercial banks was amended and published, where the requirements for outsourcing were specified. NBG attaches great importance to data quality and accuracy risk in the banking sector. In this regard, the operational risk loss accounting and reporting guidelines were published and entered into force. Also, the principles of effective risk data aggregation and risk reporting are under development.

The National Bank of Georgia pays great attention to raising awareness of operational risks in the Georgian banking sector, expanding operational risk management and developing supervisory principles. Also, sharing of recommendations on implementation of operational risk management practices and evaluation is carried out in this direction, as part of the efforts to promote digitization of non-banking financial institutions, startups and companies providing financial technologies.

During 2023, the National Bank of Georgia conducted an audit of the cyber security practices of commercial banks. As a result, key areas for improvement included the formalization of policy procedures ensuring cyber and information security, improvement of risk management practices, especially from the point of view of third-party risk management, ongoing attention to awareness raising and empowering of human resources employed in information and cyber security with appropriate competencies.

Periodic audits and penetration testing of information systems are important for financial sector cyber and information security. The National Bank of Georgia attaches great importance to conducting appropriate field tests/audits and quality control; for this purpose, in 2022 the "Guidelines for the Audit of Information Systems and Cyber Security Management Framework in Commercial Banks" was approved.

The National Bank of Georgia monitors the current events in the banking sector so that, in case of identifying cyber-attacks, information is provided to the banking sector immediately. The production of quarterly reports on cyber incidents allows to demonstrate the dynamics of cyber incident trends.

The most significant incident of 2023 was identified as the third-party cyber incident. In addition, within the framework of 2023, as well as in 2022, in the banking sector mainly the so-called Phishing and Distributed Denial of Service (DDoS) attacks were recorded.

It should be noted that the National Bank of Georgia closely monitors the technological innovations in the financial sector, which, in turn, are related to cyber and information security challenges. The increase in the use of cloud outsourcing services led to the development and approval of requirements for the use of cloud outsourcing services by financial organizations.

Measures were planned and implemented in accordance with the supervisory framework of the fight against money laundering and financing of terrorism of the National Bank of Georgia, as part of the 2023 risk-based supervisory strategy, which were based on the process of identifying and assessing the risks of each financial institution remotely. The supervisory measures implemented during 2023 included both complex and thematic, special and control-type on-site inspections.

In 2023, the actions taken towards the implementation of the supervisory framework for virtual asset service providers included the development of legal acts and the evaluation of registration applications submitted by interested parties. Actions taken in the direction of compliance with international sanctions regimes are particularly noteworthy. In order to share relevant experience, the Department of Money Laundering Inspection and Supervision, during the year, closely cooperated with various international organizations and agencies.



# MACROECONOMIC ENVIRONMENT

01

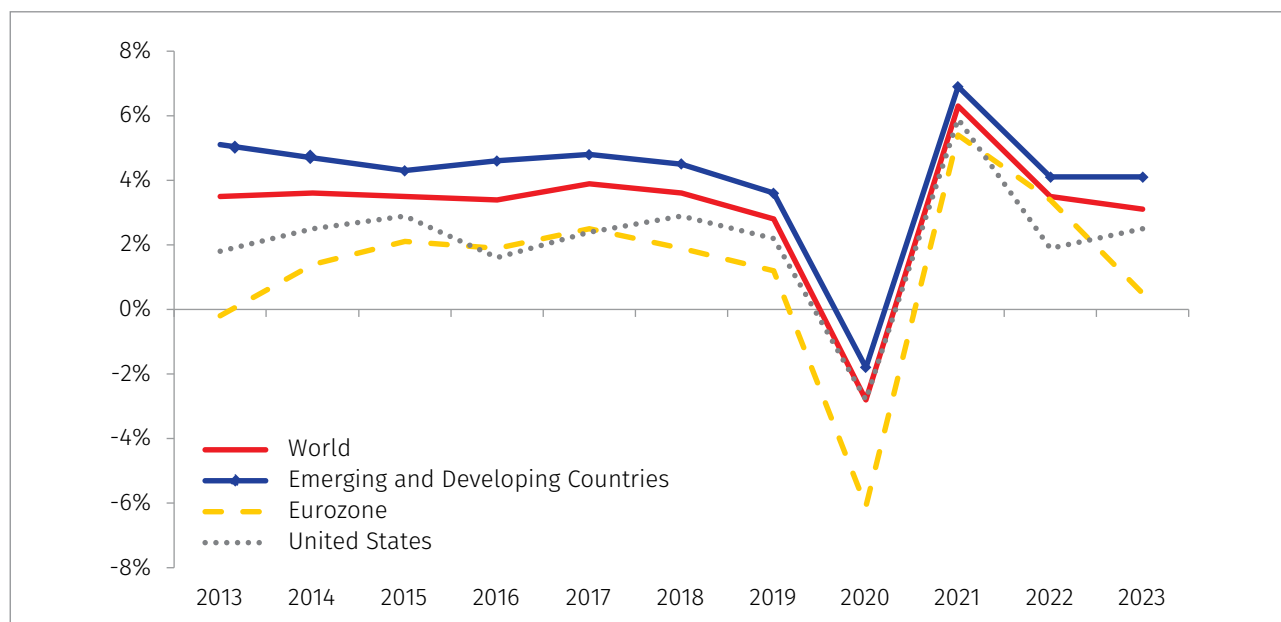
## 1.1. GLOBAL ECONOMY



Amid the challenges caused by the COVID-19 pandemic, as well as the ongoing military conflicts in Ukraine and the Middle East, the world economy recovered only at a moderate pace in 2023. The main reasons for this moderate recovery include the high-inflationary environment present in both developed and developing economies, along with increased expectations of inflation and the subsequent tightening of monetary policy. However, due to the influence

of the tightened financial environment, inflationary pressure gradually decreased during the year. According to the January 2024 estimate of the International Monetary Fund (IMF)<sup>3</sup>, the average inflation in 2023 was 6.8 percent globally. It is noteworthy that the index of international prices of food products, on average, decreased by 13.8<sup>4</sup> percent compared to the previous year, and the average price of one barrel of Brent oil decreased by 15.8 percent, to 82.6<sup>5</sup> US dollars. As for global economic growth, it amounted to 3.1 percent in 2023.

Diagram N 1.1 Real GDP Growth in the World



Source: IMF

In the Eurozone and the United Kingdom, consumer and business sentiment remained at an improved level in the first half of 2023. This was due to the restoration of supply chains, the reduction of prices of energy carriers, including oil, and, overall, the decreasing dynamics of inflation. However, in the second half of the year, due to the influence of the monetary policy

tightened by the European Central Bank (ECB) and the Bank of England, the economic growth somewhat slowed down. In Germany, consumer and business sentiments have worsened alongside high inflation and a tightening financial environment. Both consumption and investment volume decreased. The foreign sector also deteriorated. According to IMF estimates<sup>6</sup>, the

3. International Monetary Fund. 2024. The World Economic Outlook Update: Moderating Inflation and Steady Growth Open Path to Soft Landing. Washington, D.C., January. (further: WEO January update, 2024).

4. UN Food and Agriculture Organization (FAO).

5. Bloomberg

6. WEO January update, 2024.

real economy in Germany will decrease by 0.5 percent in 2023. Economic activity was also low in Italy, amid reduced investment and high public debt. Also, high inflation and a tightening financial environment created additional pressure on activity. As a result, Italy's real economy grew by only 0.7<sup>7</sup> percent in 2023. Economic activity was also low in France, where private consumption and consumer spending declined alongside high inflation and a tightening financial environment. Finally, according to IMF estimates<sup>8</sup>, France's real economy will grow by 0.8 percent in 2023. Compared to other European countries, a high rate of economic activity has been recorded in Spain, which is linked to strong foreign demand as a result of increased activity in the tourism sector. Domestic demand was also strong and, ultimately, Spain's real economy grew by 2.4 percent<sup>9</sup>, in 2023, although the annual rate of inflation remained high throughout 2023. Activity was also high in Greece, driven by increased investment and a stable labor market. According to IMF estimates<sup>10</sup>, Greece's real economic growth in 2023 was 2.5 percent. The annual inflation of the Eurozone countries in 2023 averaged 5.5 percent. In response to increased inflationary expectations, the European Central Bank had to raise the monetary policy rate to 4.5 percent during the year.

In the first half of 2023, the pace of economic activity improved in the US. Consumer sentiment and retail

sales improved. This was facilitated by the dynamics of reducing consumer prices. The employment rate also increased. Improvements continued in the second half of the year, albeit at a slower pace, largely influenced by the tight financial environment. Inflation declined during the year, but remained above target, and the US Federal Reserve tightened monetary policy in response to rising inflation expectations. Ultimately, according to the IMF's January<sup>11</sup> estimates, real economic growth in the US in 2023 was 2.5 percent, and annual inflation averaged 4.1 percent.

In 2023, economic activity improved slightly in emerging and developing economies. This is related to the globally high inflationary environment and, as a result, the tightened financial environment. The pace of improvement in economic activity in Türkiye has slowed amid deteriorating consumer sentiment and the business environment. In particular, retail sales, consumer spending and the manufacturing index declined. In the second half of the year, with the additional devaluation of the lira, the inflationary pressure increased even more. Against this background, the Central Bank of the Republic of Türkiye has sharply tightened the monetary policy. According to IMF estimates<sup>12</sup>, Türkiye's real economy will grow by 4 percent in 2023. As for inflation, it will average 53.4 percent in 2023.

---

7. WEO January update, 2024.

8. WEO January update, 2024.

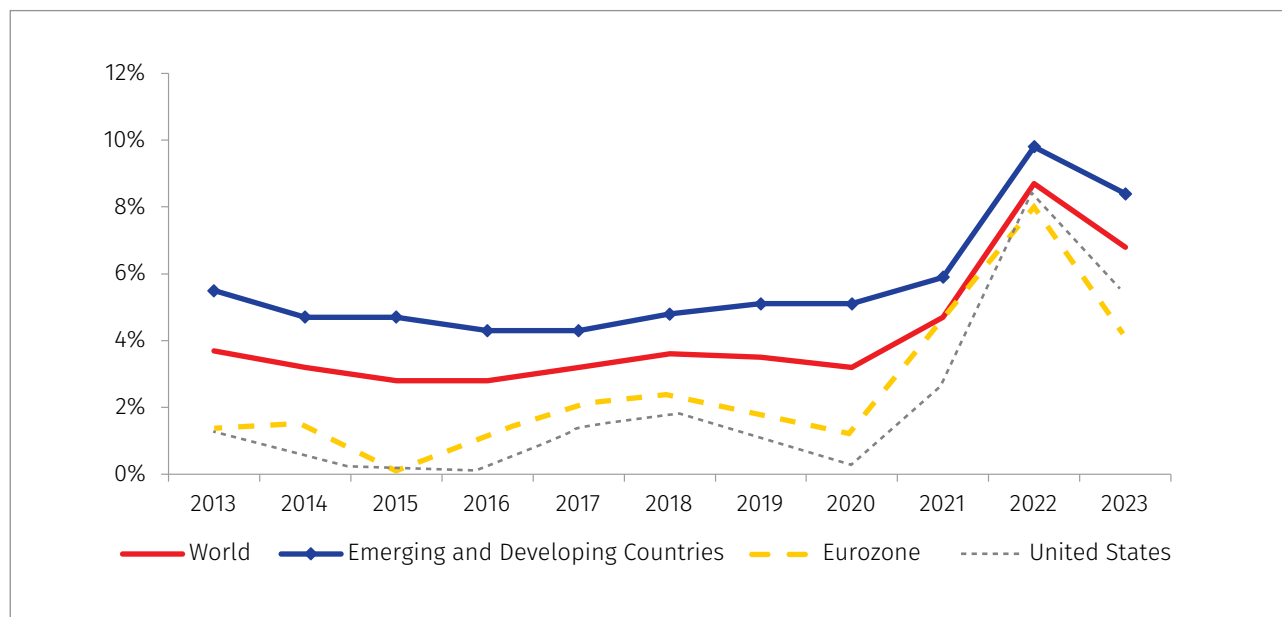
9. WEO January update, 2024.

10. International Monetary Fund. 2023. The World Economic Outlook: Navigating Global Divergences. Washington, D.C., October. (further: WEO, October 2023).

11. WEO January update, 2024.

12. WEO, October 2023.

Diagram N 1.2 CPI inflation in the world



Source: IMF

In 2023, higher-than-expected economic activity was recorded in Russia. However, on the whole, against the background of the sanctions imposed by the West, both the business environment and the volume of investments and the foreign sector continue to deteriorate. Amid labor shortages, unemployment was at historic lows, which in turn put upward pressure on wages. From the second half of the year, this was accompanied by the devaluation of the Russian ruble, which was reflected in the increase in inflation. In response to increased inflationary expectations, the Central Bank of Russia increased the monetary policy rate several times. According to IMF estimates<sup>13</sup>, after a 2.1 percent decline in 2022, real economic growth in Russia was 3 percent in 2023, and the inflation rate averaged 5.9 percent.

The war waged by Russia has a heavy impact on Ukraine both socially and economically. Many critical infrastructure facilities have been destroyed, reducing

the potential of the economy. According to the IMF<sup>14</sup>, after a 29.1 percent decline in 2022, Ukraine's real economic growth was 2 percent in 2023, and the average inflation rate was 13.4 percent. It should be emphasized that, parallel to the war, the civilized part of the world, including Georgia, supports Ukraine.

2023 was marked by high economic activity in Armenia. Similar to Georgia, this was mainly due to the effect of high migration of Russian citizens, against the background of which the business environment and service sector improved. At the same time, inflation decreased rapidly during the year, urging the Central Bank of Armenia to begin withdrawing from the stance of tightening monetary policy. According to IMF<sup>15</sup> estimates, Armenia's economic growth in 2023 was 7 percent, and inflation was 2 percent on average.

As for Azerbaijan, economic activity in Azerbaijan improved in 2023, which was mainly due to the

13. WEO January update, 2024.

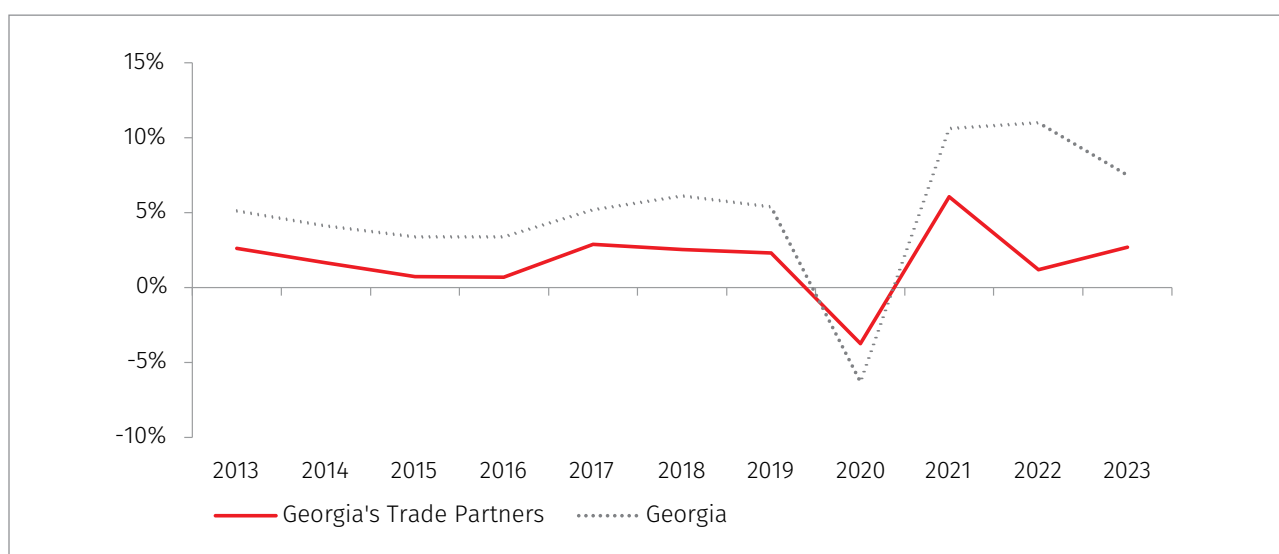
14. WEO, October 2023.

15. WEO, October 2023.

increase in industrial production in the non-oil sector. However, the end of the conflict in Nagorno-Karabakh had a positive impact on consumer and business sentiment. From the second half of the year, against the background of the tightened monetary policy, the inflation rate decreased. According to IMF<sup>16</sup> estimates, in 2023, the real GDP of Azerbaijan increased by 2.5 percent, and the annual inflation averaged 8.9 percent.

Ultimately, the economy of Georgia's trade partner countries grew by an average of 2.7 percent in 2023, while in 2022, an average growth of 1.2 percent was recorded. As for Georgia, real GDP in 2023, according to preliminary data, increased by 7.5 percent, which is a rather high indicator after the 11 percent growth in 2022 (see diagram 1.3). Inflation averaged 2.6 percent in 2023.

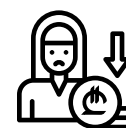
Diagram N 1.3 Real GDP Growth in Georgia and Weighted Average Growth of Trading Partner Countries



Source: IMF, NBG calculations

As mentioned above, the central banks of Georgia's trade partner countries, tightened the monetary policy during 2023 in response to high inflationary pressure and inflation expectations. In particular, the US Federal Reserve increased the federal funds rate to 5.25-5.5 percent, and the European Central Bank increased the main refinancing rate to 4.5 percent. As for the central banks of the Republic of Türkiye and Russia, they increased the monetary policy rate to 42.5 and 16 percent, respectively.

## 1.2. EXTERNAL SECTOR AND BALANCE OF PAYMENTS



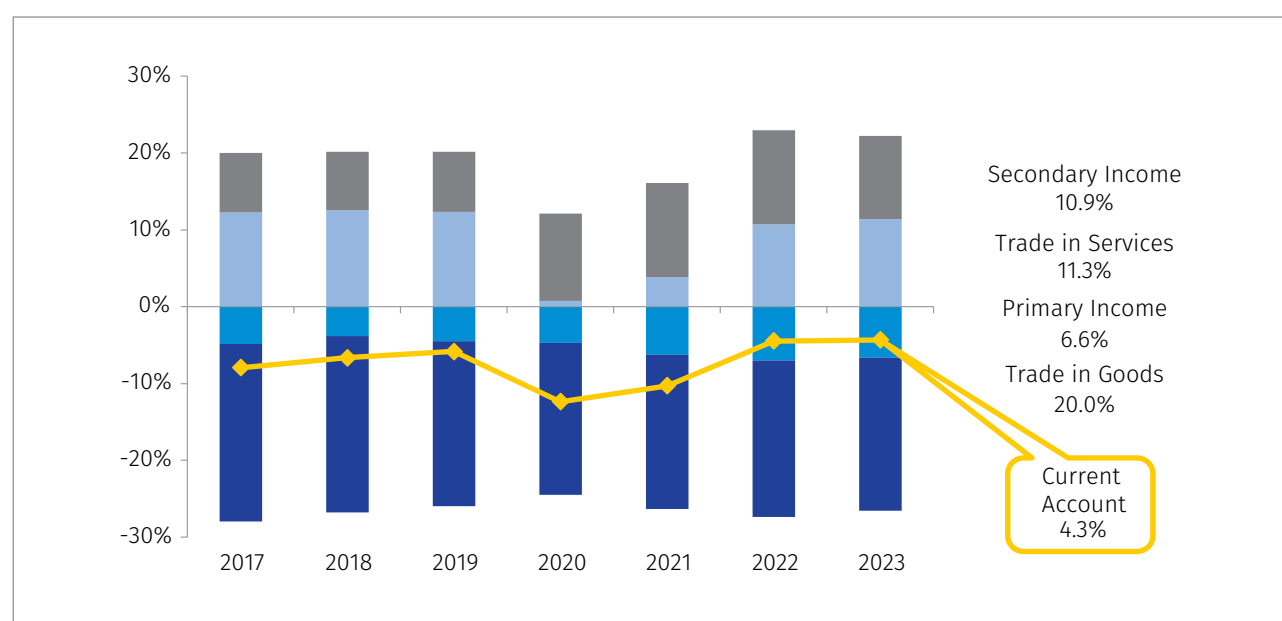
In 2023, external demand made a negative annual contribution to the economic growth. During 2023, the growth rate of external inflows gradually normalized, which was largely due to the fading of the one-time effect of migration, as expected. Due to the ongoing war, the number of long-term visitors from Russia,

Belarus and Ukraine increased significantly in 2022, and in 2023, as expected, some of the citizens from these countries left the country. Despite the exhaustion of the one-time effect of migration, revenues from international travel continued to increase in 2023, on the back of growth in visitors from the EU and Türkiye. However, partially due to the weakening of the base effect and the one-off effect of migration, instant money transfers declined annually. In addition, foreign demand for domestic exports of goods was weak, which was driven by reduced competitiveness due to the strengthened exchange rate and the slowdown in economic growth of trading partner countries. To some extent, this was balanced by the increasing trend of re-export of motor cars. However, at the end of the year, the growth rate of re-export of cars also slowed down. A certain slowdown of external inflows was largely balanced by the low growth rate of imports of goods. On the one hand, this was caused by the decrease in the prices of oil products and other commodity groups at the international market, due total value of imported goods decreased. As a result, the current

account balance amounted to 4.3 percent of GDP, which is historically the lowest indicator for Georgia (see diagram N 1.4).

The 2023 current account deficit increased by USD 206 million to USD 1,326 million compared to the previous year and amounted to 4.3 percent of GDP. Trade deficit decreased to 20.0 percent of GDP in 2023. Against the background of the growth of revenues from international travel (annual growth of 17.3 percent, as well as growth of 26.2 percent compared to 2019), the surplus of trade in services increased substantially and contributed significantly to the improvement of the current account balance. In 2023, the current account balance was negatively affected by the deficit of primary income account<sup>17</sup>, which is mainly caused by the increase in net investment income on assets of non-residents in Georgia. It should be noted that, as in previous years, both the volume of dividends issued and reinvested income is high, which increases the deficit of the current account.

Diagram N 1.4 The ratio of Current Account Components to GDP



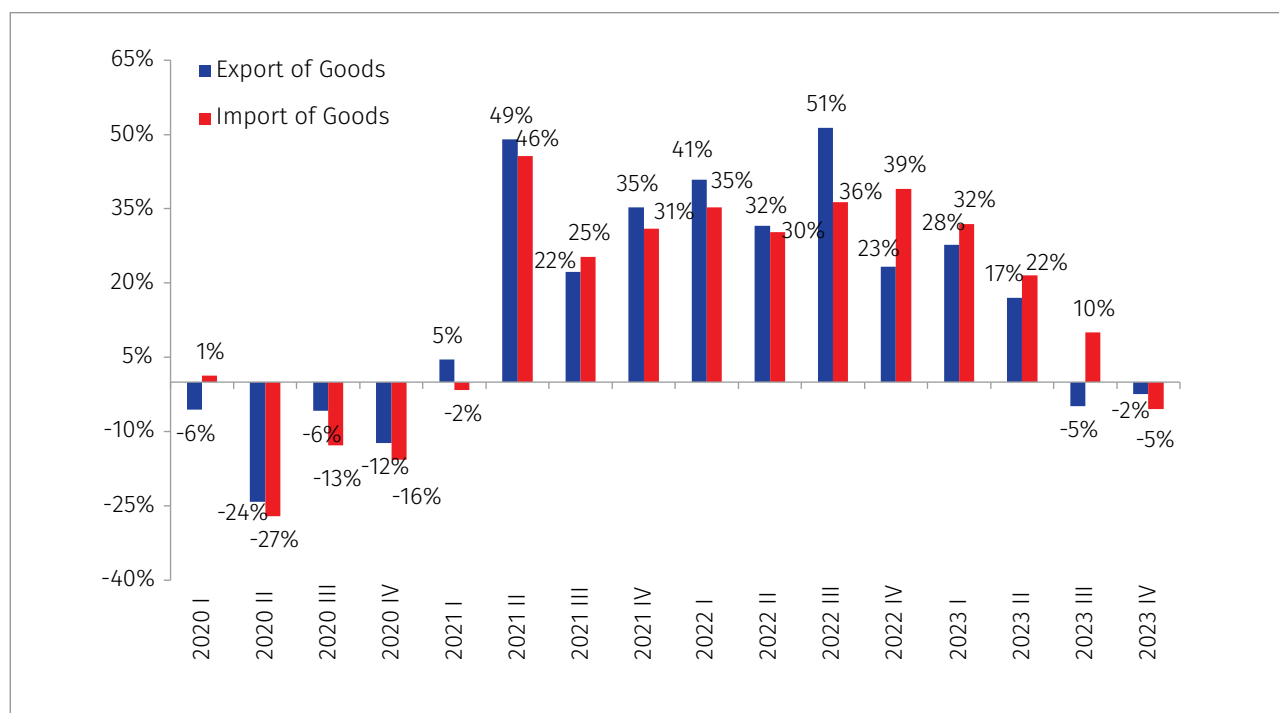
Source: NBG

17. Primary income is a current account item that records resident and non-resident income related to production processes and property (e.g. salaries, investment income, etc.).

The trade balance of goods is still the highest negative component of the current account balance. In 2023, the volume of goods trade deficit increased by 19 percent compared to the previous year, however, against the background of high economic growth, it amounted to 20.0 percent of GDP, which was 0.5 percentage points less than the previous year. A further widening of the trade deficit was decelerated by a moderate increase in imports. In particular, in 2023, despite the strong economic activity, the import of goods increased by 12.4 percent. As a result, compared to the previous year, the deepening of the trade deficit had a negative impact on the current account balance (see diagram 1.5).

In 2023, the registered exports of goods increased by 9.1 percent. At the beginning of the year, the exports of goods grew at a fast pace, which was largely due to the increase in re-exports, especially the re-export of cars. However, from the second half of the year, amid the decrease in foreign demand for cars, the export growth rate slowed down and decreased year-on-year at the end of the year. The decline in exports, in addition to the base effect, was associated with a slowdown in economic activity in the region as well as in other countries. On the one hand, exports to EU countries decreased annually, but on the other hand, they increased to Central Asian countries, mostly due to the acceleration of re-export of motor cars.

Diagram N 1.5 Annual Change in Export and Import of Goods<sup>18</sup>



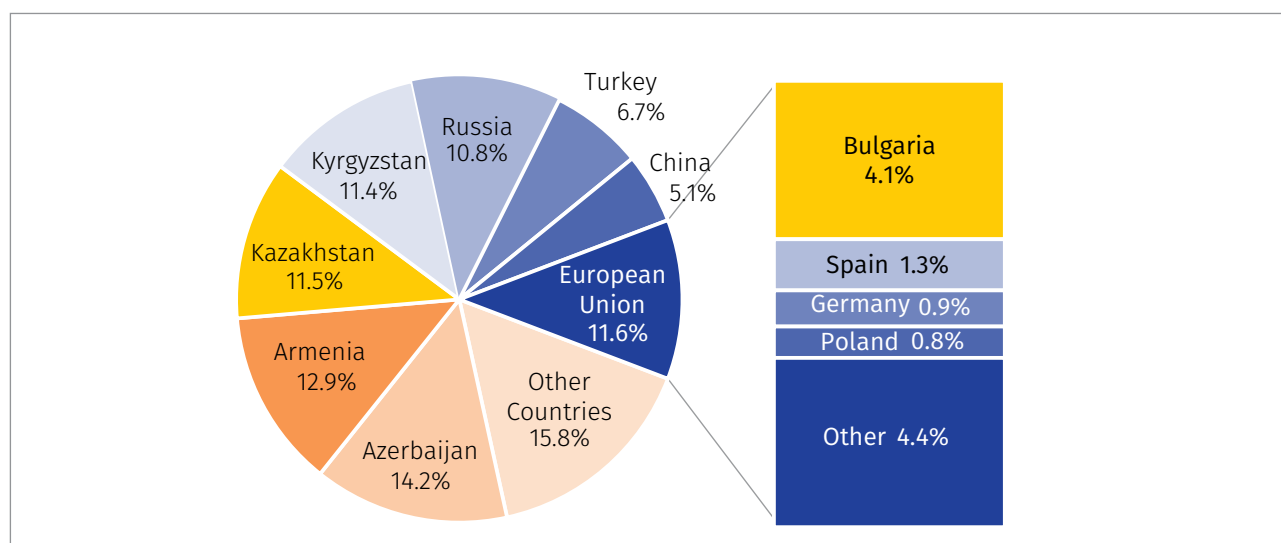
Source: NBG

18. Exports of goods in the balance of payments (BOP). The external trade data provided by GeoStat and the data on exports/imports by the BOP are different concepts that rely on different methodological frameworks. Foreign trade statistics are based on the principle of crossing a border, whereas the main principle of trade of goods in the BOP is a change of ownership between residents and nonresidents. Moreover, in the external trade statistics, exports are presented in FOB price, while imports are presented in CIF price. In contrast, export/import of goods are presented in FOB prices in the BOP.

In 2023, exports of goods from Georgia to Central Asian countries, especially Kyrgyzstan (7.4 times more) and Kazakhstan (3.0 times more), increased. The increase in exports to neighboring countries was mainly due to the increase in exports to Armenia (by 34.7 percent) and Azerbaijan (by 28.2 percent). Among the countries of the European Union, Spain (by 56.3 percent) and Greece (by 213.9 percent) stood out in terms of export growth, while in Bulgaria (-41.0 percent) it decreased significantly, mainly due to the decrease in the re-export of copper ores and concentrates. From the rest of the countries, the decreased sales in China (-57.8 percent) and the USA (-63.4 percent) made a high negative contribution to the change in revenues from exports of goods.

According to the data of 2023, foreign trade in the direction of Central Asian countries has significantly increased, which, like the previous year, was mainly caused by the re-export of motor cars. From the rest of the countries, Iraq (100.6 percent increase) and the United Arab Emirates (72.8 percent increase) were distinguished by their increased contribution to total exports. Sales of live bovine and non-bovine animals accounted for 95 percent of Iraq's exports, while re-exports of motor cars and copper ores and concentrates accounted for the majority of exports to the United Arab Emirates. It should be noted that the export of mineral and chemical fertilizers to Morocco has increased significantly. Compared to the previous year, the export of goods became less diversified by country.

Diagram N 1.6 Exports structure by country 2023



Source: GeoStat

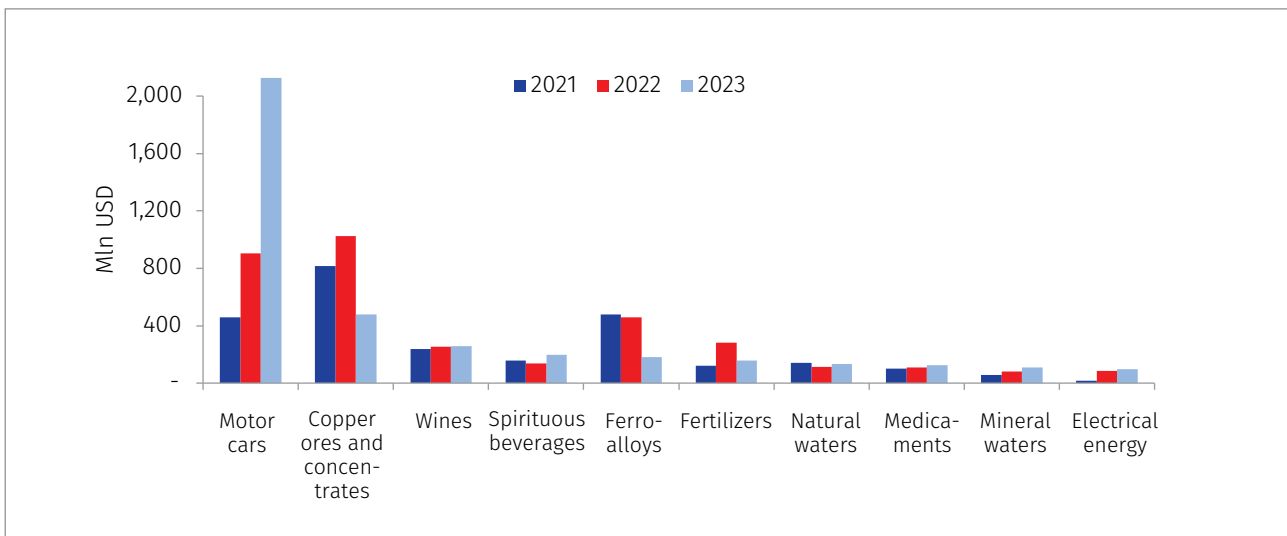
In 2023, the re-export of motor cars had a significant share in the export of goods, which increased by 134.8 percent compared to the previous year and amounted to 34.9 percent of the total export. At the same time, the re-export of copper ores and concentrates had a high share, which decreased by 53.2 percent annually. It is worth noting that in 2023, the globally reduced prices for raw materials made a certain contribution to the decrease in the amount received from the export

of copper ores and concentrates. Finally, exports of domestically produced goods declined significantly year-on-year, reflecting reduced demand in neighboring countries. Exports of mineral and chemical fertilizers, various fruits, clothes and nuts also decreased from the leading export groups. In addition, ferroalloys exports decreased the most due to the decrease in prices in the international market and the resulting decrease in supply. In contrast, several domestically produced

goods such as electricity, mineral and natural waters and live bovine animals, their exports continued to grow and volumes increased by 13.2, 23.7 and 54.5 percent, respectively. At the same time, sales of spiritual beverages, wines and unprocessed gold were still at a high level. Overall, in 2023, registered exports of goods increased by 9.1 percent, while domestic

exports of goods decreased by 24.4 percent. It should also be noted that in 2023, in total, the price indices for export goods decreased, and in real terms, the export of goods from Georgia increased by approximately 2 percent. It is also noteworthy that exports of goods have become much less diversified by commodity.

Diagram N 1.7 Top Ten Export Commodities



Source: GeoStat

In 2023, the imports of registered goods increased by 14.9 percent. A regional analysis of imports shows that in 2023, imports from both the EU (by 24.0 percent) and the category of other countries (by 11.0 percent) increased. The USA (6.9 pp), Japan (2.2 pp) and Germany (2.1 pp) had a high contribution to the growth of imports, which was connected to a sharp increase in the import of motor cars from these countries. The increase in imports from Italy (0.6 pp) and the Netherlands (0.6 pp) also contributed to the growth of total imports from EU countries. On the contrary, due to the ongoing war in Ukraine, imports from this country have decreased significantly, mostly due to the decrease in purchases of cigarettes and medicaments. The decrease in imports from Armenia and Chile was caused by the decrease

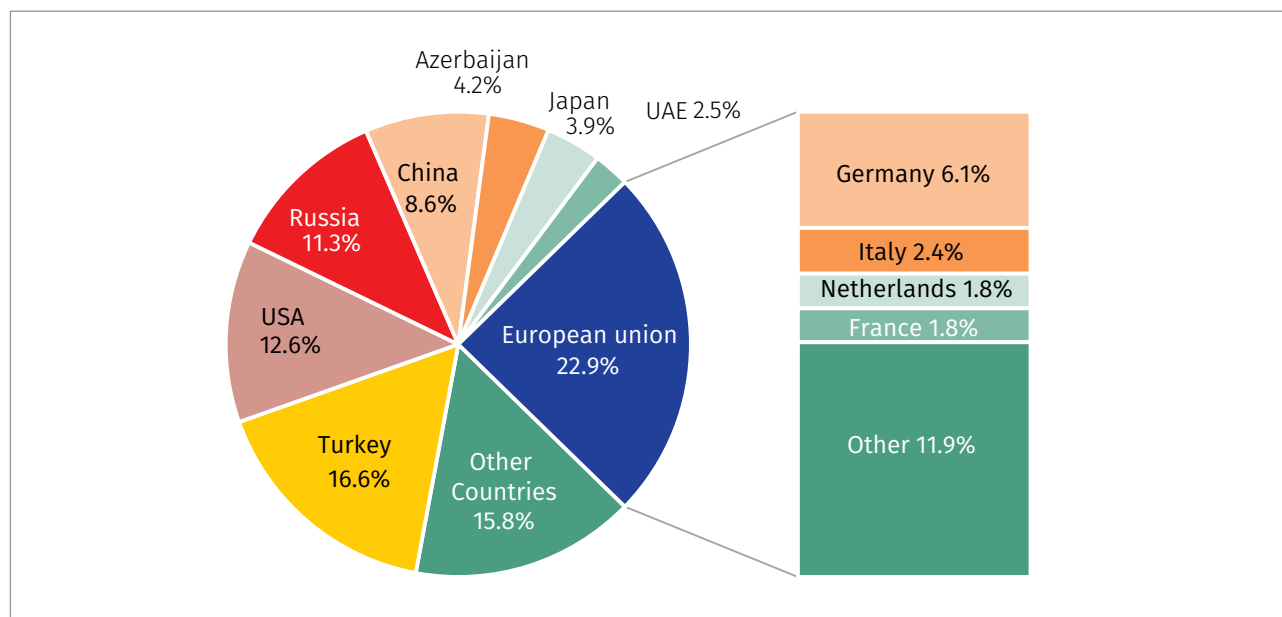
in copper ores and concentrates, and the decrease in the import of petroleum and petroleum products from Russia and Turkmenistan.

As in previous years, among the importing countries, after the European Union, Türkiye was the leading country in the region, from which imports increased by 8.3 percent annually in 2023, which was caused by the increase in purchases of medicaments, washing and cleaning products, and other aircraft vehicles. Imports from China increased by 18.0 percent due to a sharp increase in imports of data processing machines and their units, as well as motor cars for transport of goods, while imports from the United Arab Emirates increased due to increased purchases of telephone

sets and articles for table and parlour games. Imports from the United Kingdom were boosted by purchases of construction machinery and mixtures of beverage

additives. It is significant that imports have become much less diversified by country. (see diagram N 1.8).

Diagram N 1.8 Import Structure by Country in 2023

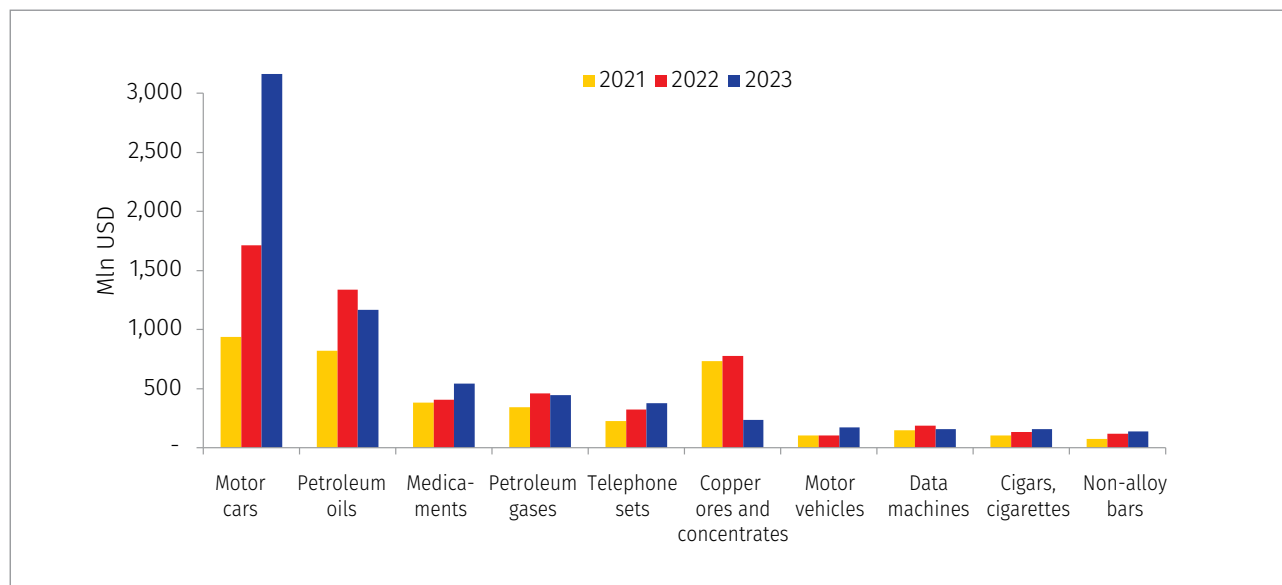


Source: GeoStat

In 2023, consumer goods made the largest contribution to the increase in the imports of goods, which is connected with the growing aggregate demand and the high level of re-exports. The increase in the import of consumer goods was mainly caused by the re-export of motor cars, which increased by about 2 times annually and contributed 10.7 pp to the growth of the total import. In addition, the import of petroleum and petroleum products (7.6 percent of total imports) decreased, which was partly a reflection of the reduced price of oil on international markets. In particular, during the year 2023, the expenditures on the import of petroleum and petroleum products decreased by 12.6 percent, of which

the effect of price reduction is 19.2 pp, while the import of petroleum products increased by 6.6 percent in real terms. A sharp decrease in the import of intermediate consumption goods was caused by a decrease in the import of copper for re-export, as well as precious metal ores and concentrates. At the same time, imports of ferrous metal structures, cement and immune products were still high. Among the groups of investment goods, the groups of motor vehicles for the transport of goods, tractors, large construction vehicles and motor vehicles for the transport of ten or more persons were distinguished by the increased contribution to the growth of imports (see diagram N 1.9).

Diagram N 1.9 Top Ten Import Commodities



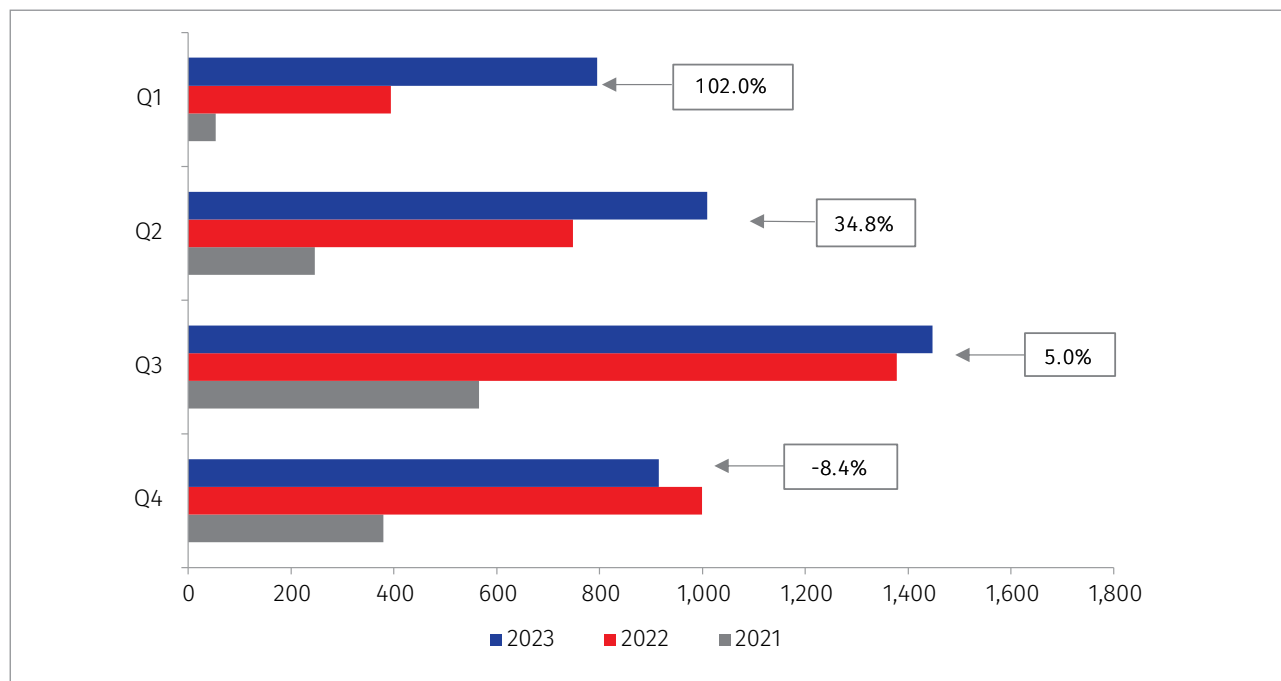
Source: GeoStat

It should be noted that the slow growth rate in imports of goods in 2023 was also contributed by the decrease in the prices of several imported goods expressed in US dollars. The import price index gradually decreased during the year, and therefore the import of goods increased more in real terms. In 2023, imports became less diversified by commodity, largely due to an increased share of imports of motor cars and a decreased share of copper ores and concentrates.

In 2023, the significantly increased surplus of trade in services had a positive effect on the current account balance. In particular, the ratio of service trade surplus to GDP was 11.3 percent, which is 0.6 percentage points higher than the same indicator of the previous year. In absolute terms, the positive balance of trade in services in 2023, compared to the previous year, was USD 788 million more and amounted to USD 3,462 million. As in previous years, revenue from international travel

is one of the most important components of the services trade surplus. The end of the Covid-19 pandemic and the easing of global restrictions have, as expected, had a positive impact on exports of services, especially tourism and related business activities. In addition, migration flows, which started in Georgia during the ongoing war due to Russia's invasion of Ukraine, have slowed down, although the expenses of foreigners in the local market for services, especially for accommodation and food, were still at a high level. As a result, revenues received from international travelers, which are the main part of service exports, amounted to USD 4,125 million in 2023, which is by 17.3 percent higher than the previous year (see diagram N 1.10). At the same time, the expenses of Georgian citizens traveling abroad have increased. Finally, the foreign trips of resident travelers amounted to 2.8 million, which was 31.6 percent more than the previous year.

Diagram N 1.10 Revenues from International Travel

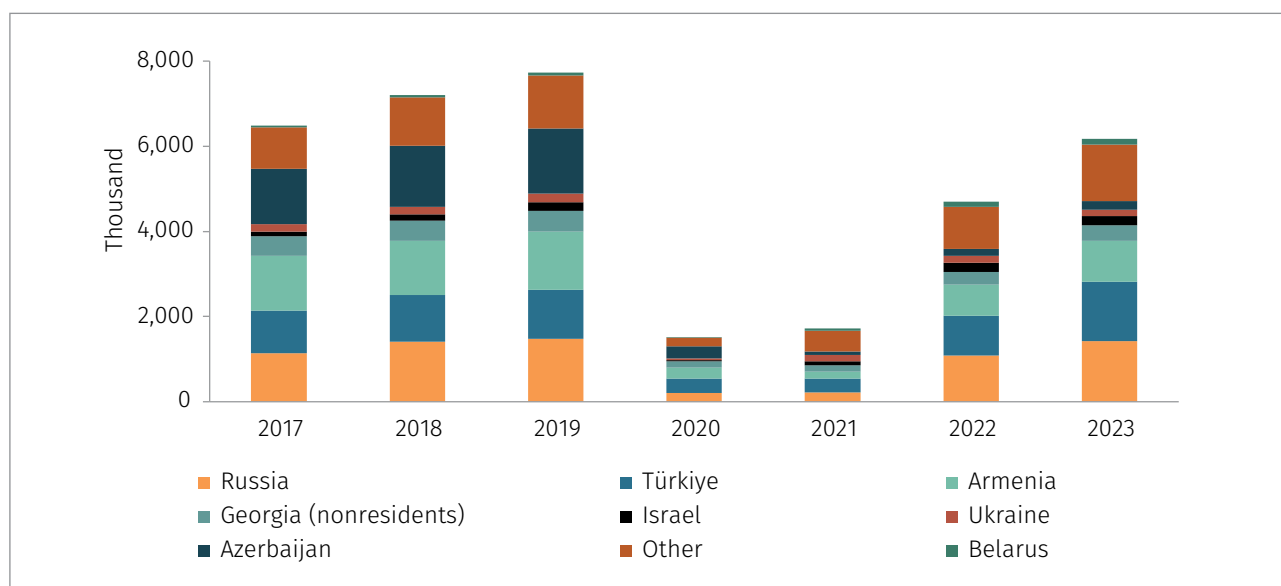


Source: National Bank of Georgia

Despite the recovery of global tourism and the slow-down in migration flows in 2023, the number of international visitor arrivals increased by 31.2 percent annually, although compared to the pre-pandemic level, it is still lower (-20.1 percent). Traditionally, neighboring countries were distinguished by high contribution

to the increase of visitors: Türkiye (10.0 pp), Russia (7.0 pp) and Armenia (4.7 pp). Poland and Germany stood out in terms of the increase of visitors from EU countries. It should be noted that in 2023, the diversification of visitors by country has increased significantly.

Diagram N 1.11 Number of International Visitors to Georgia by Country

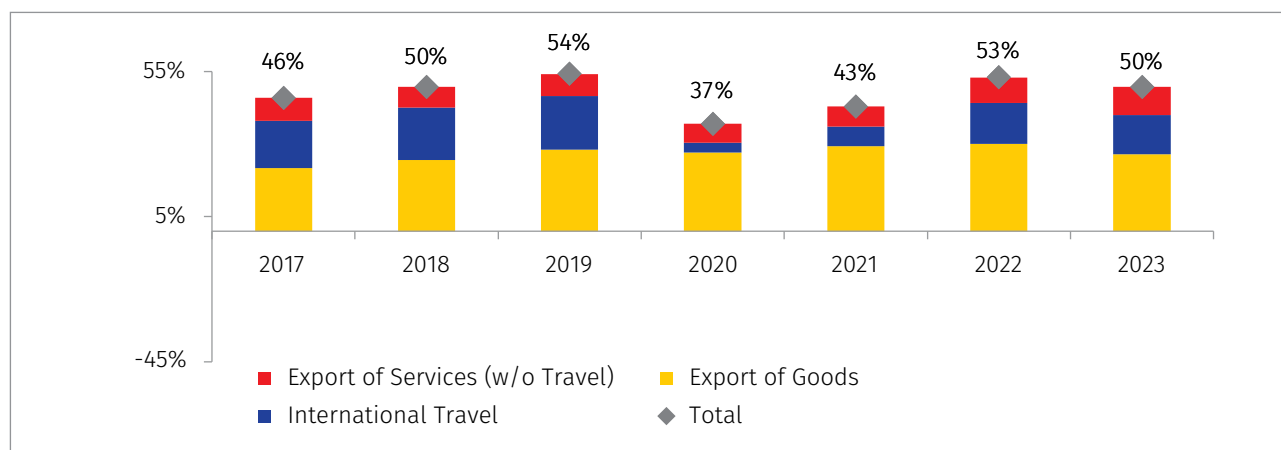


Source: Ministry of Internal Affairs of Georgia

In 2023, similar to the increase in revenues from international travel, the amount received from other types of service exports (including sea and border transport shipments) increased significantly. It is also worth not-

ing the increase in the export of services in the field of computer and information services (see diagram N 1.12). Overall, high revenues from service exports had a positive impact on the current account balance in 2023.

Diagram N 1.12 Revenues from export of goods and services to GDP

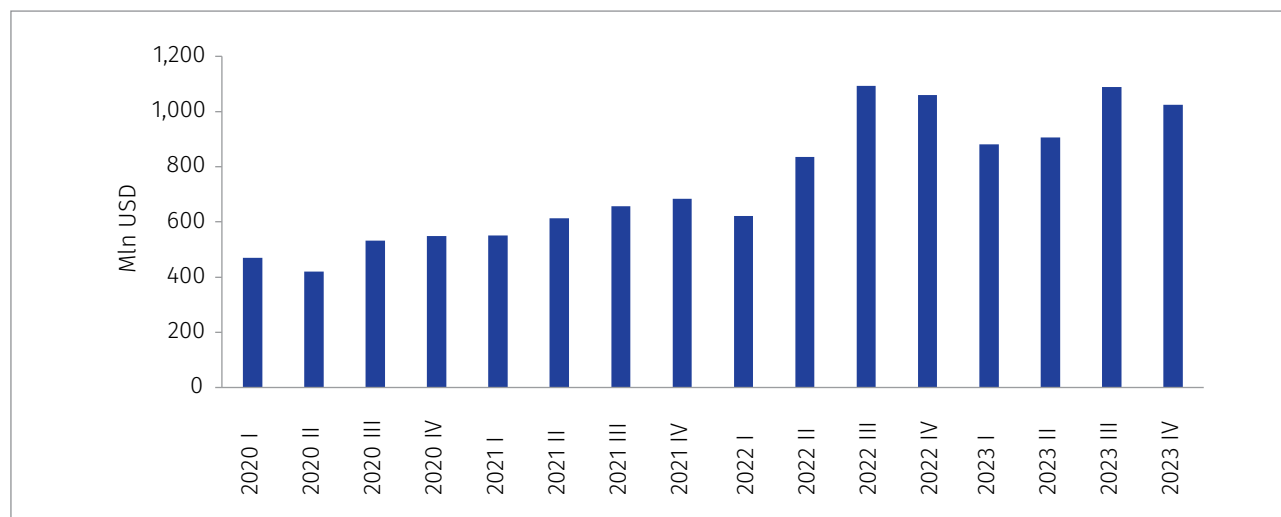


Source: NBG

The primary income account deficit in 2023, compared to the previous year, widened by USD 278 million and amounted to USD 2,026 million. The main reason for the high deficit of the primary income account remains the negative balance of investment income, which increased by USD 329 million in 2023 and amounted to USD 2.8 billion. The high level of the investment income deficit is due to the increase in the interest income of other investments and the income account in the part of foreign direct investments - both distributed dividends paid and reinvested earnings. As for the

balance of compensation of employees, in 2023 this component increased by USD 72 million and amounted to USD 743 million. According to the IMF's methodology, part of the citizens of a foreign country (migrants) who planned to stay in the country for more than 1 year, were registered as residents, and their expenses were no longer included in the revenues from international travel. However, this change increased the balance of compensation of employees and therefore had a positive effect on the primary income surplus.

Diagram N 1.13 Personal Remittances

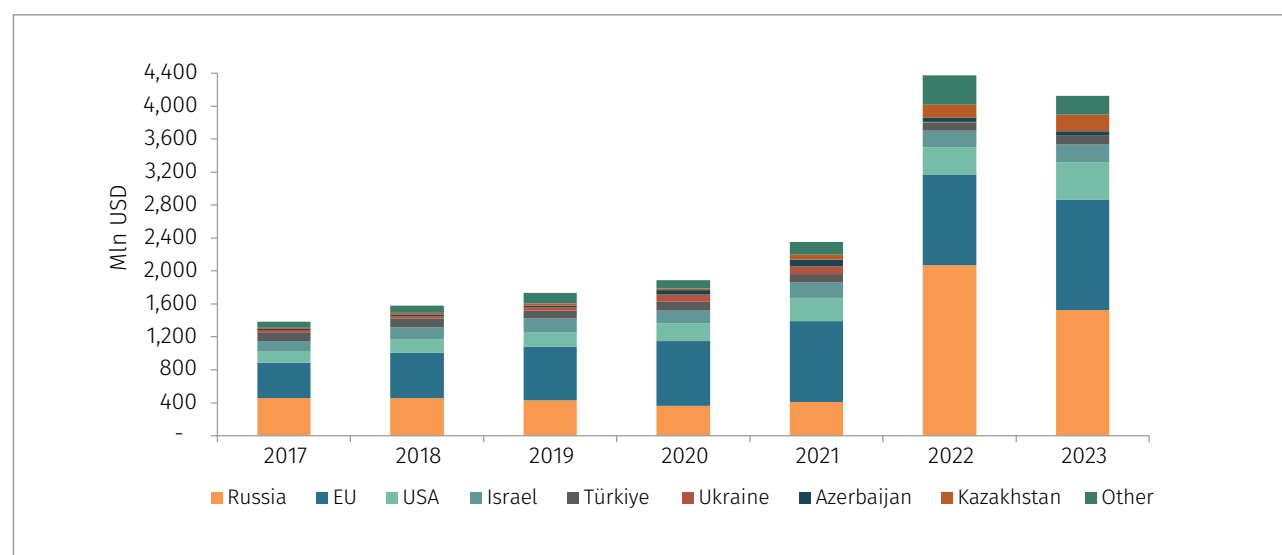


Source: NBG

Secondary income in 2023<sup>19</sup>, largely due to higher remittances from abroad, grew moderately (9.1 percent). Personal remittances, which is usually the largest part of secondary income, grew by 8.1 percent annually (see diagram N 1.14). It should be noted that throughout the year, especially from the second half of the year, instant money transfers decreased annually, which is largely related to the base effect and the slowdown of migration flows. During 2023, the increased transfers from the USA (3.0 pp), Italy (2.0 pp) and Germany (1.5 pp) made a high positive contribution to the change in total transfers (see diagram N 1.14). Prior

to the Ukraine's war with Russia, remittances to the region were increasingly coming from the European Union, with Russia's contribution declining. However, this trend reversed in 2022, with a significant surge in remittances from Russia. However, in 2023, inflows from Russia again declined by 26.2 percent annually, although still the highest share of total remittances. Instant money transfers from EU countries increased by 21.0 percent, mainly due to the increase in transfers from Germany, Greece and Italy. In addition, transfers from Israel and Kazakhstan made a significant contribution to the volume of total instant money transfers.

Diagram N 1.14 Instant Money Transfers by Country



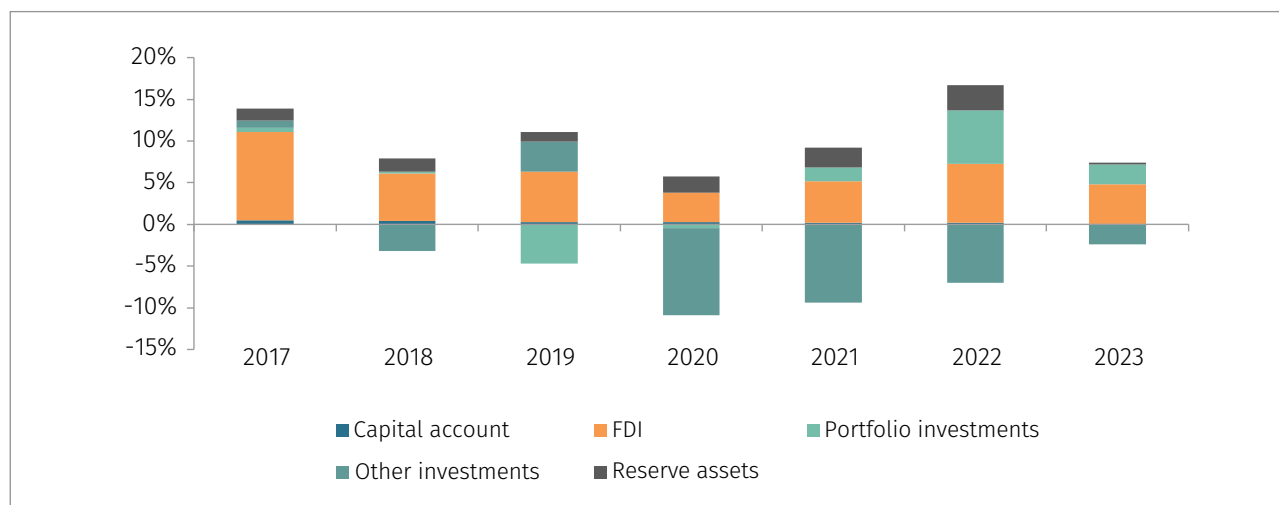
Source: NBG

In 2023, as in previous years, net FDI remained a major source of financing of the current account deficit (see Diagram No. 1.15). FDI inflow in Georgia amounted to 1.6 billion US dollars, that is 24 percent less than the previous year. The decrease in foreign direct investment is mostly related to the decrease in debt obligations, although the increase in equity investments continued.

The largest part of foreign direct investments was directed to finance, manufacturing and real estate sectors. Compared to the previous year, investments mostly increased in manufacturing, finance and transport sectors, and decreased in real estate and energy sectors.

19. Secondary income is part of the current account balance of payments that shows current transfers (excluding capital transfers) between residents and non-residents (personal transfers, budgetary transfers and grants in the framework of international cooperation, social contributions and benefits, etc.).

Diagram N 1.15 Financing the current account deficit (in % of GDP)



Source: NBG

In 2023, the flow of net portfolio investments amounted to USD 713 million, the largest part of which comes from the non-banking private sector. The increase in assets of residents amounted to USD 328 million, which was mostly directed in the equity capital in the private sector. In 2023, the holding of securities by non-residents in the non-banking sector decreased annually, while residents continued to purchase bonds issued by international financial companies in GEL. At the same time, in other sectors, the residents repaid part of the bonds issued in previous years by taking new loans.

In 2023, the contribution of other investments in financing the current account deficit decreased compared to the previous year. In terms of inflows, the main part of the increase in liabilities comes from loans raised in both the government and private (non-banking) sectors. Long-term loans received by the government sector totaled USD 447 million. In addition, against the backdrop of high economic activity, large amounts of money have been accumulated by non-residents in the form of cash and deposits in the banking sector. At the same time, commercial banks increased their cash and deposits in foreign banks annually.

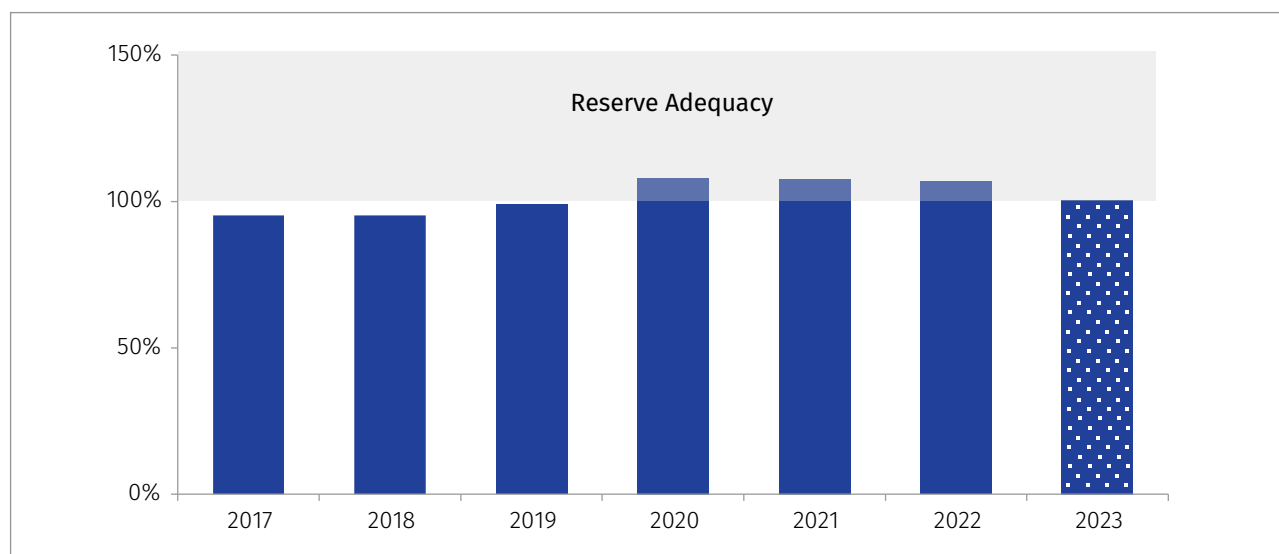
In 2023, gross international reserves increased by USD 108 million and amounted to USD 5.01 billion. Foreign exchange interventions and funds raised by the gov-

ernment from other international organizations (including program grants and loans) contributed to an increase in international reserves. Finally, in 2023, the NBG's net purchases in the foreign exchange market (both through foreign exchange auctions and through the BMatch platform) amounted to USD 1.28 billion. On contrary, foreign debt servicing and other foreign exchange expenses of the government had a deceleration impact on international reserves accumulation. At the same time, deposit dollarization decreased significantly this year. As reserve requirement norm for foreign currency depends on the level of deposit dollarization, lower level of dollarization induced the reserve requirement norm to go down and commercial banks required holding of amount in FX corresponding account decreased accordingly. In addition, the upper limit of the reserve norm on short-term foreign currency liabilities has been reduced from 25 percent to 20 percent from December 2023, further reducing foreign exchange reserves.

At the end of 2023, Assessment of Reserve Adequacy (ARA) metric by IMF methodology<sup>20</sup> stood around 100.4%, which is within the adequacy range (from 100 to 150 percent) necessary to insure against external and liquidity shocks. By the end of 2023, the ratio of reserves to months of imports (forecasted imports of 2024) was around 4 months.

20. For details, visit <https://www.imf.org/external/np/spr/ara/>

Diagram N 1.16 Assessment of international reserve adequacy (ARA metric) according to the IMF methodology



Source: NBG

Table N 1.1 Balance of Payments 2018-2023 (million USD)<sup>21</sup>

	2018	2019	2020	2021	2022	2023
<b>Current Account</b>	<b>-1,192</b>	<b>-1,034</b>	<b>-1,984</b>	<b>-1,943</b>	<b>-1,120</b>	<b>-1,326</b>
goods	-4,116	-3,792	-3,165	-3,790	-5,100	-6,093
Export	4,407	4,946	4,347	5,539	7,536	8,111
Import	-8,522	-8,737	-7,512	-9,329	-12,636	-14,204
Services	2,244	2,176	124	725	2,674	3,462
Credit	4,490	4,600	1,580	2,547	5,703	7,050
o/w: Revenues from Travel	3,222	3,269	542	1,245	3,517	4,125
Debit	2,246	2,425	1,456	1,822	3,029	3,588
Primary Income (Net)	-684	-793	-752	-1,181	-1,748	-2,026
o/w: Investment Income	-1,381	-1,600	-1,241	-1,644	-2,419	-2,769
o/w: Compensation of Employees	697	807	488	463	671	743
Secondary Income (Net)	1,364	1,375	1,810	2,304	3,053	3,330
o/w: General Government	173	133	256	200	183	199
o/w: Financial corporations, nonfinancial corporations, households, and NPISHs	1,190	1,242	1,553	2,104	2,870	3,131
<b>Capital Account</b>	<b>76</b>	<b>47</b>	<b>41</b>	<b>38</b>	<b>41</b>	<b>37</b>
<b>Financial Account</b>	<b>-1,252</b>	<b>-1,069</b>	<b>-2,039</b>	<b>-1,937</b>	<b>-1,169</b>	<b>-1,248</b>
Direct investment (Net)	-1,010	-1,073	-572	-931	-1,766	-1,306
o/w: Direct Investments in Georgia	1,304	1,384	556	1,278	2,131	1,778
Portfolio investment (Net)	48	-829	-75	311	1,608	735

21. 6th edition of balance of payments statistics manual.

(continue)

Financial Derivatives (other than reserves) and employee stock options: net	1	-4	-27	-1	-3	48
Other Investments (Net)	-569	634	-1,670	-1,769	-1,772	-773
o/w: General Government	-351	-346	-1,445	-1,333	-505	-418
o/w: Others	-218	980	-225	-436	-1,267	-355
Reserve Assets	278	202	305	453	765	47
<b>Net Errors and Omissions</b>	<b>-136</b>	<b>-82</b>	<b>-97</b>	<b>-33</b>	<b>-90</b>	<b>41</b>

**Important Coefficients**

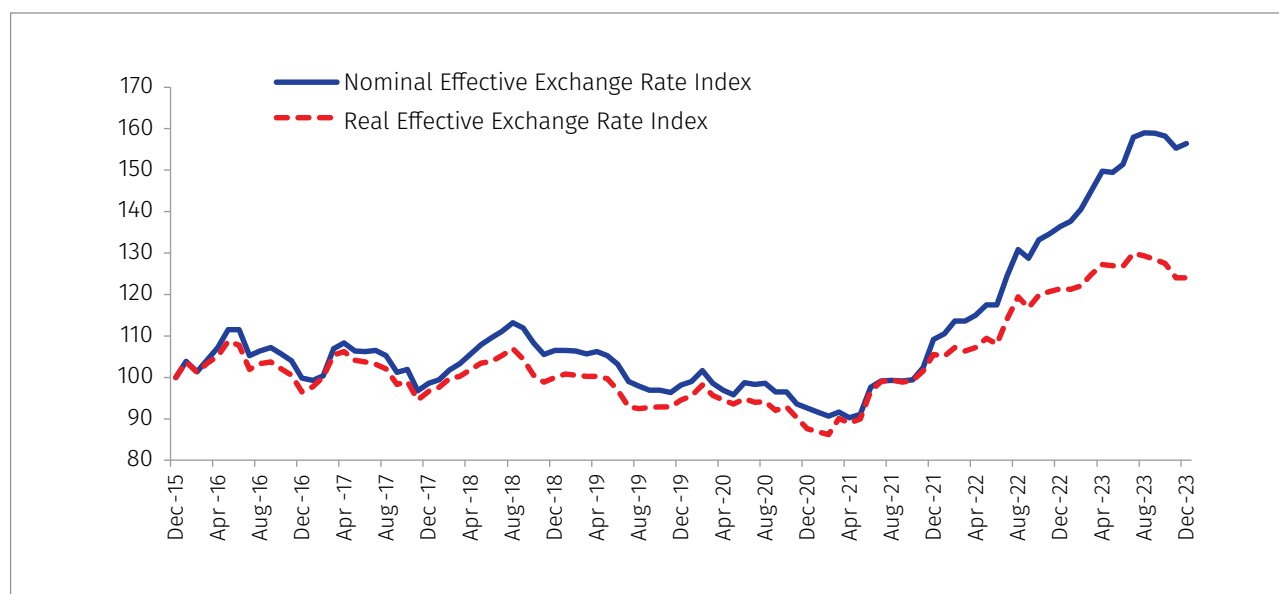
Reserve Assets in Months of Imports of the Next Year (Months)	3.5	3.5	5.1	5.0	4.2	4.0
Export / Import (G&S)	-83%	-86%	-66%	-73%	-85%	-85%
CAB/GDP	-6.8%	-5.9%	-12.4%	-10.3%	-4.5%	-4.3%
FDI/GDP	7.5%	7.7%	3.7%	6.6%	8.4%	5.2%
Revenues from Travel/GDP	18.0%	18.5%	3.4%	6.6%	14.1%	13.5%
Personal Transfers/GDP	9.8%	10.6%	12.3%	13.3%	14.4%	12.8%

Source: NBG

Against the background of high external inflows and a moderate widening of the current account deficit, both the real and the nominal exchange rate continued to appreciate from the beginning of the year, although it slightly depreciated in the second half of the year (see diagram N 1.2.14). In particular, in 2023, the real effective exchange rate appreciated by 2.1 percent, and

the nominal effective exchange rate appreciated by 14.8 percent, which, other things being equal, implies a decrease in foreign competitiveness. In 2023, the currencies of Russia, Armenia and China made a high contribution to appreciating the real effective exchange rate (see Table N 1.2).

Diagram N 1.17 Indices of real and nominal effective exchange rates (Dec. 2015=100)



Source: NBG

Table N 1.2 Annual changes in effective exchange rates in 2023

	Nominal effective exchange rate change, %	Real effective exchange rate change, %	Contribution in real effective exchange rate
<b>Effective Exchange Rate</b>	<b>14.8</b>	<b>2.1</b>	<b>2.1</b>
Eurozone	-3.1	-5.4	-0.9
Türkiye	56.0	-4.9	-0.9
Ukraine	0.6	-3.9	-0.1
Armenia	2.4	3.5	0.3
USA	0.1	-2.8	-0.2
Russia	38.9	29.8	5.1
Azerbaijan	0.3	-1.4	-0.1
China	2.3	3.1	0.4
Bulgaria	-3.1	-7.0	-0.3
Poland	-10.2	-15.3	-0.3

Source: NBG

### 1.3. ECONOMIC GROWTH



According to preliminary data, the real Gross Domestic Product of Georgia in 2023 increased by 7.5 percent compared to the previous year. The main contribution to economic growth, 6.3 pp, was made by service industries. The factors contributing to the solid growth of the service sector are strong domestic demand, the tourism industry and a significant number of migrants

in the country. In total, the growth contribution of trade, transport, hotels and restaurants, information and communication, arts, entertainment and recreation to the overall growth during the year was 4.2 pp.

The construction made the largest contribution to economic growth from industrial sectors (17.2% growth, 1.2 pp growth contribution), where both private and infrastructure constructions were active. (Table 1.3).

Table N 1.3 GDP by Economic activities

	Real growth					Contribution to growth (pp)				
	2023Q1	2023Q2	2023Q3	2023Q4	2023	2023Q1	2023Q2	2023Q3	2023Q4	2023
Agriculture, forestry and fish farming	-0.7%	-9.5%	6.4%	-8.1%	-2.8%	-0.1	-0.8	0.5	-0.4	-0.2
Mining industry	-19.1%	-9.8%	8.5%	5.5%	-4.0%	-0.3	-0.1	0.1	0.0	0.0
Manufacturing industry	15.4%	-0.7%	1.5%	0.1%	3.3%	1.5	-0.1	0.1	0.0	0.3
Supply of electricity, gas, steam and air conditioning	7.2%	-7.0%	-2.2%	-10.6%	-3.2%	0.2	-0.2	-0.1	-0.3	-0.1
Water supply; Sewerage, waste management and pollution control	-21.2%	-16.3%	-2.6%	-5.0%	-11.3%	-0.2	-0.1	0.0	0.0	-0.1
construction	22.3%	33.9%	18.2%	4.1%	17.2%	1.3	2.1	1.3	0.3	1.2
Wholesale and retail trade; Repair of cars and motorcycles	21.4%	18.0%	9.3%	9.4%	13.6%	2.5	2.3	1.1	1.3	1.8
Transport and warehousing	9.5%	3.1%	21.3%	17.7%	13.3%	0.5	0.2	1.2	1.0	0.7

(continue)

Accommodation and catering	18.2%	-2.5%	4.8%	2.2%	4.6%	0.5	-0.1	0.2	0.1	0.2
Information and communication	54.2%	32.1%	9.6%	25.9%	27.4%	1.9	1.3	0.4	1.2	1.2
Finance and insurance	10.2%	-0.6%	15.4%	4.0%	7.1%	0.5	0.0	0.6	0.1	0.3
Real estate	-23.7%	-5.0%	9.7%	9.9%	-2.5%	-2.1	-0.4	0.8	0.8	-0.2
Professional, scientific and technical work	3.0%	16.1%	28.1%	27.3%	19.1%	0.0	0.2	0.5	0.5	0.3
Administrative and support services	21.2%	34.2%	23.5%	26.9%	26.4%	0.2	0.3	0.2	0.2	0.2
State governance and defense; Mandatory social security	9.6%	13.6%	14.2%	16.8%	13.7%	0.6	0.7	0.7	0.9	0.8
Education	8.8%	18.7%	17.3%	30.4%	18.9%	0.4	0.8	0.6	1.1	0.7
Health and social services activities	-27.6%	-14.9%	-12.1%	-4.5%	-15.4%	-1.3	-0.5	-0.4	-0.1	-0.5
Art, entertainment and recreation	12.5%	4.7%	5.0%	8.6%	7.6%	0.5	0.2	0.2	0.3	0.3
Other services	27.2%	17.0%	-1.5%	8.2%	11.0%	0.2	0.1	0.0	0.1	0.1
Activities of households as employers; Production of undifferentiated goods and services by households for their own consumption	32.9%	37.4%	-15.6%	-16.2%	5.2%	0.0	0.0	0.0	0.0	0.0
(+) Taxes on products	10.7%	19.0%	-6.4%	-1.0%	3.8%	1.3	2.4	-0.9	-0.2	0.5
(-) Subsidies on products	-2.8%	12.1%	11.6%	10.2%	8.8%	0.0	-0.1	0.0	0.0	0.0
<b>GDP</b>	<b>8.2%</b>	<b>8.1%</b>	<b>7.0%</b>	<b>6.9%</b>	<b>7.5%</b>	<b>8.2</b>	<b>8.1</b>	<b>7.0</b>	<b>6.9</b>	<b>7.5</b>
Of these:										
Agriculture	-0.7%	-9.5%	6.4%	-8.1%	-2.8%	-0.1	-0.8	0.5	-0.4	-0.2
Industries	12.4%	7.4%	6.8%	0.6%	6.2%	2.6	1.5	1.4	0.1	1.3
Services	8.3%	10.8%	7.5%	10.1%	8.8%	5.7	7.4	5.1	7.2	6.3

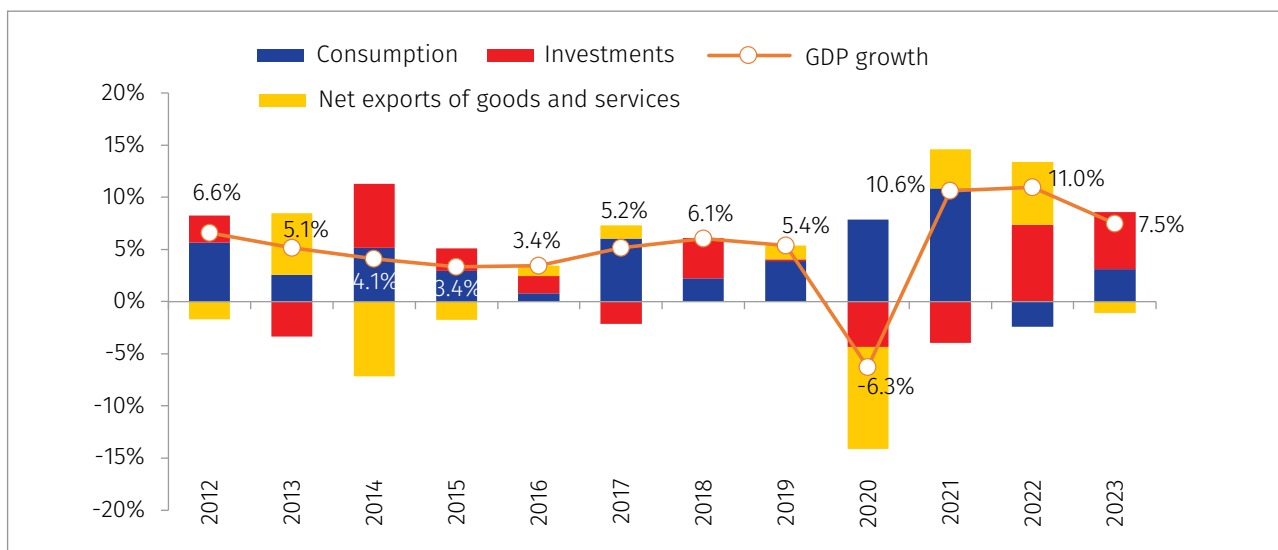
Source: GeoStat and NBG calculations

## DEMAND

The investments were the main driver of real GDP growth in 2023. In particular, the investments contributed 5.4 pp to the 7.5 percent economic growth. The increase in investments was partly caused by a significant increase in capital expenditures from the budget and business loans. A relatively small positive contribution to economic growth was made by consumption, the contribution of which was 3.1 pp. The impact of foreign demand on economic

growth was relatively weak, which is related to the exhaustion of the effect of migration on the one hand and the weakening of foreign demand for exports of goods on the other. In 2022, as a result of migration, service exports increased by real 87.9%. Because of this, the main driver of economic growth was net exports. In 2023, due to the base effect, the growth of service exports sharply decreased to 4.1 percent, and the contribution of net exports to economic growth became negative 1.1 pp. (diagram N 1.18)

Diagram N 1.18 Real GDP Growth by Expenditures

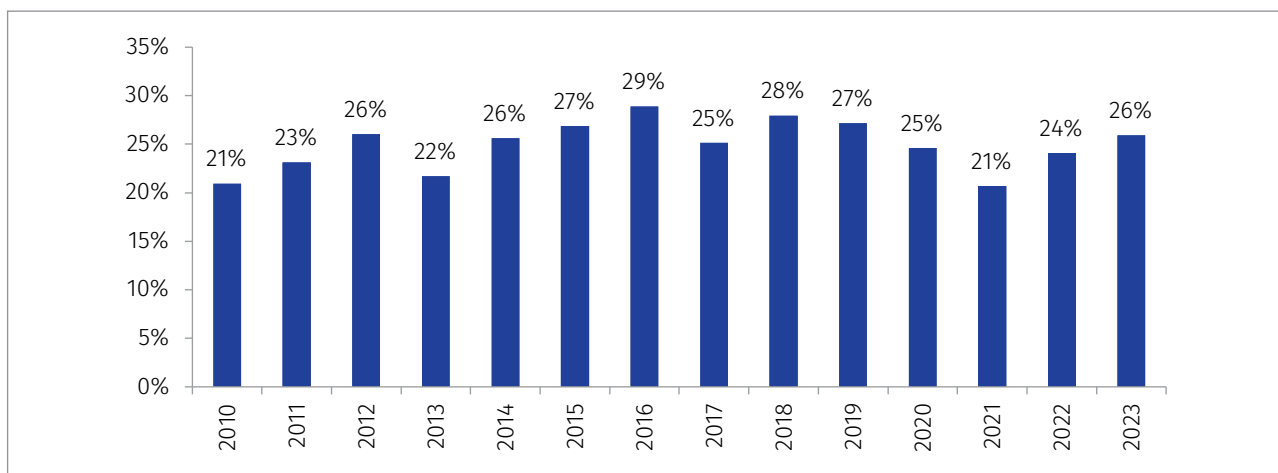


Source: GeoStat and NBG calculations

Against the background of the leading role of investments in economic growth, the contribution of investments in expenditures also increased and made 26

percent of GDP, which increases the total production potential of the Georgian economy (see diagram N 1.19).

Diagram N 1.19 Investments to GDP



Source: GeoStat

## 1.4. CHANGE IN CONSUMER PRICES

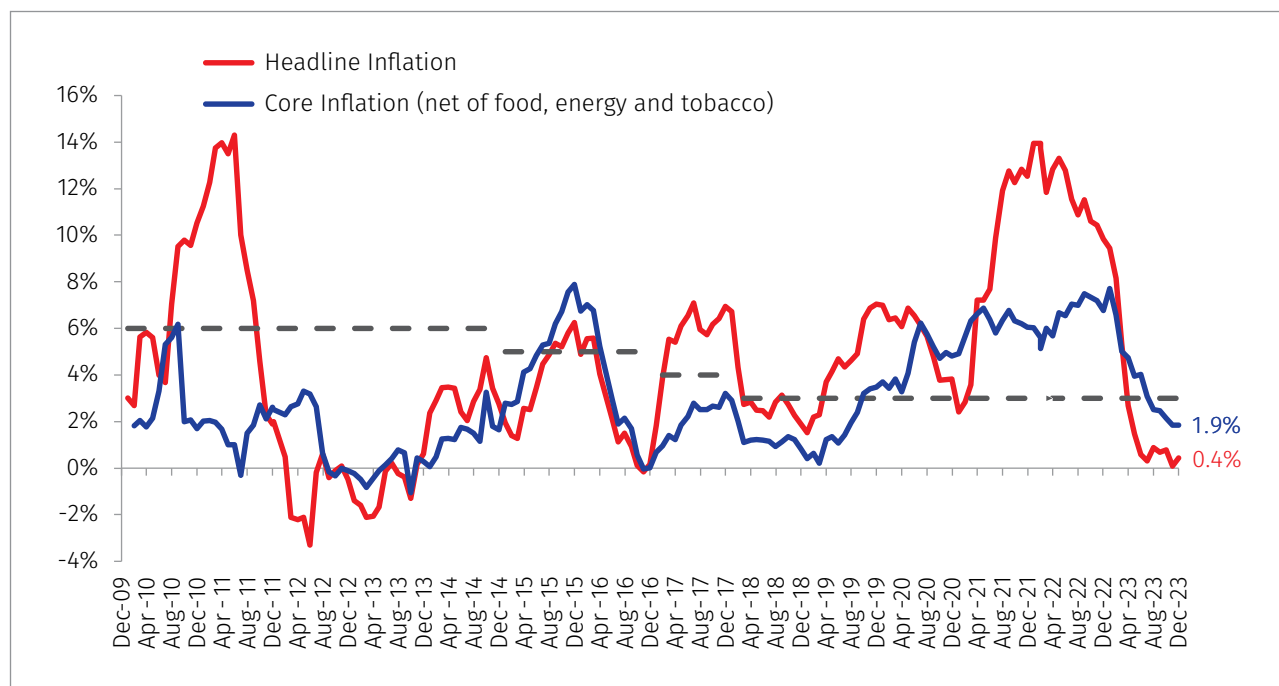


locally produced products as a result of tight monetary policy, and on the other hand, by the gradual easing of external shocks.

Inflation started to decrease from the beginning of 2023 and remained below the target of 3 percent after March (Diagram N 1.20). The decrease in inflation was driven, on the one hand, by the decrease in inflation of

Inflation averaged 2.6 percent in 2023, and core inflation, which excludes the highly volatile prices of food, energy carriers and cigarettes from the consumer basket, averaged 3.8 percent.

Diagram N 1.20 Headline and Core (excluding food, energy and tobacco) Inflations



Source: GeoStat

Food prices on international markets during 2023<sup>22</sup> mainly showed a declining trend, which, together with the strong position of the GEL exchange rate, reduced the prices of food products in the local market. At the beginning of the year, high inflation was caused mainly by the annual increase in food prices. From the average inflation of 7.6% in the first quarter, 4.3 percentage points came from food. During the year, both indicators gradually decreased. In December, when inflation decreased to 0.4 percent, the contribution of food made a negative 1.0 pp.

The contribution of fuel to inflation was largely negative, which was driven by reducing oil prices and exhaustion of the base effect. However, in the second half of the year, fuel prices began to rise and stabilized only in December. Due to this, in the second half of the year, the negative contribution of fuel to inflation gradually dissipated, and in December it already be-

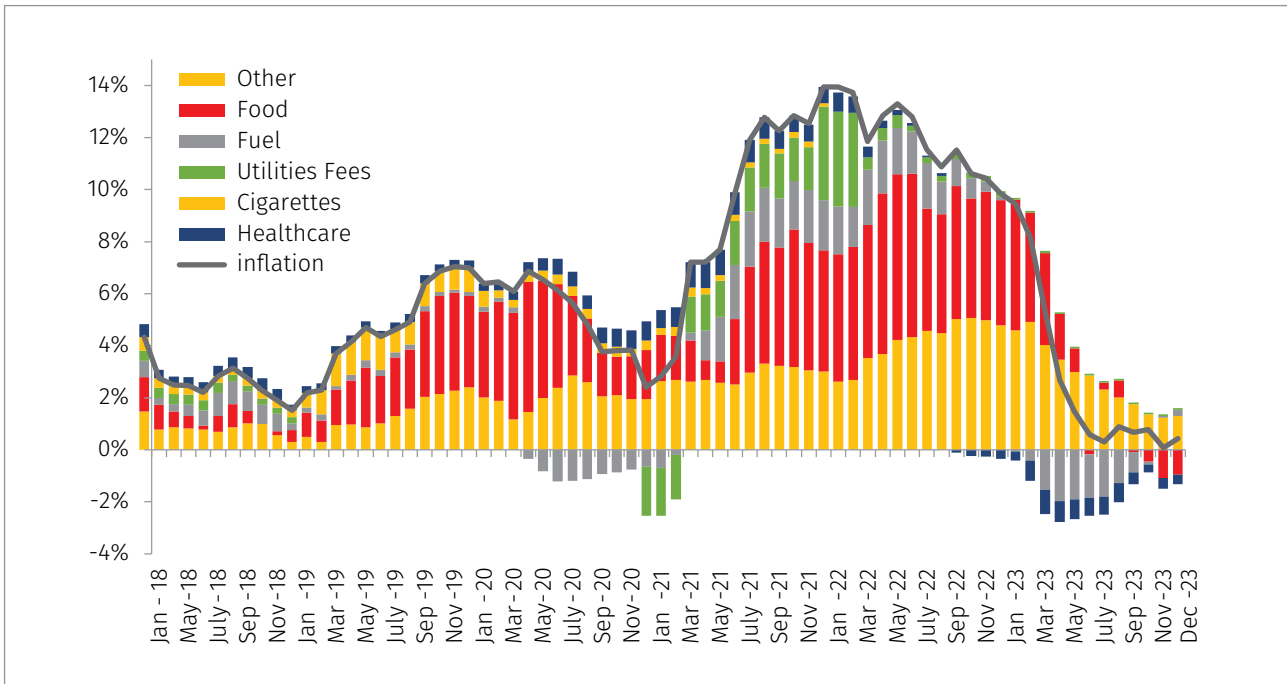
came positive 0.3 pp.

The negative contribution of the healthcare group products is attributable to the price reduction of widely used medicines that are part of the consumer basket. Over the past year, annual price increases were most noticeable on other products. The largest part of this came from services (diagram N 1.21).

Georgia has seen a rise in foreign residents due to two main factors. First, tourism has rebounded strongly after the pandemic, attracting many visitors. Second, the war in Ukraine has prompted some people to relocate to Georgia. This fact, along with strong domestic demand, increased prices for services. It should be noted that the service inflation gradually decreased during the year along with the exhaustion of the base effect. It decreased from 13.4 percent in January to 6.6 percent in December, averaging 9.4 percent (Table N 1.4).

22. Food and Agriculture Organization of the United Nations International Food Index <https://www.fao.org/worldfoodsituation/foodpricesindex/en/>

Diagram N 1.21 Contribution of major components to inflation



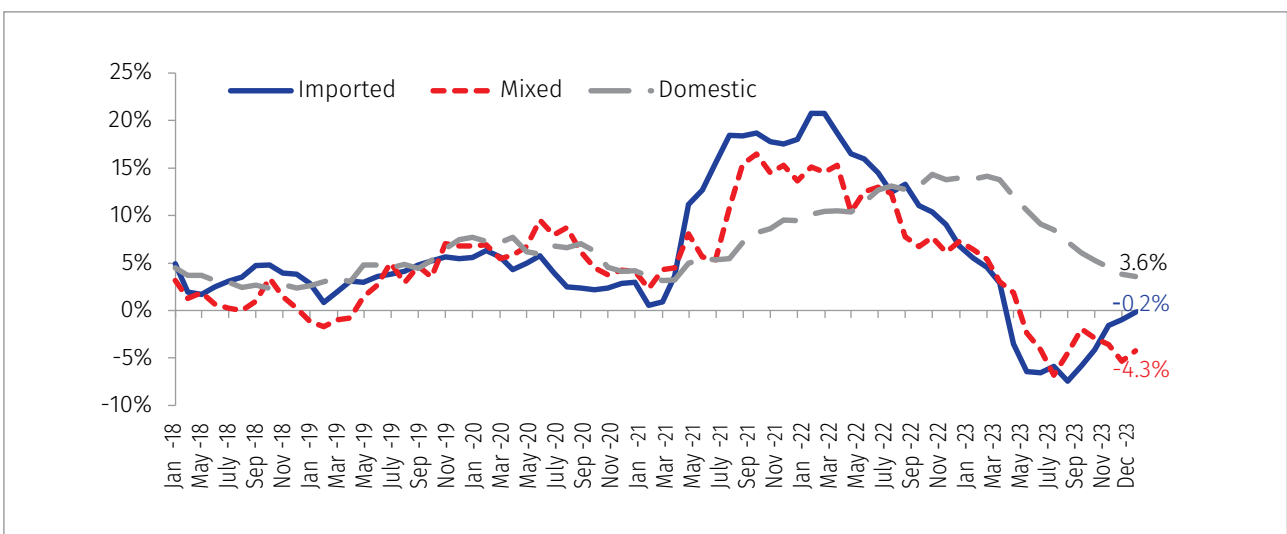
Source: GeoStat and NBG calculations

During the year, imported, mixed and domestic inflation differed significantly from each other. The prices of imported and mixed goods were deflationary after the first quarter of the year due to the strong position of the exchange rate of lari and the stable and in some cases decreasing trend of the prices of goods and transportation in the world. High inflation of domestic

products was caused by the service sector.

Together with the exhaustion of service inflation, domestic inflation gradually decreased. In the second half of the year, deflation of imported goods had a downward trend, mainly due to the increase in fuel prices. (diagram N 1.22).

Diagram N 1.22 Imported, mixed and domestic inflation



Source: GeoStat

Table N 1.4 Inflation indicators by groups of products, their weight in the consumer basket and impact on inflation

	2023 year weights	Dec23/Dec22		2023 average/2022 average	
		inflation	contribution	inflation	contribution
<b>Total</b>	100.0%	0.4%	0.4%	2.6%	2.6%
Food and Non-Alcoholic Beverages	33.7%	-2.7%	-0.9%	3.7%	1.2%
Food	30.9%	-3.1%	-1.0%	3.5%	1.0%
Bread and Bakery	6.1%	-8.0%	-0.5%	1.1%	0.1%
Meat and Meat Products	7.0%	5.6%	0.4%	7.7%	0.5%
Fish Products	0.5%	-0.1%	0.0%	7.8%	0.0%
Milk, Cheese, and Eggs	6.9%	-3.3%	-0.2%	5.2%	0.3%
Oil and Fats	2.6%	-19.2%	-0.5%	-16.2%	-0.5%
Fruits, grapes	1.6%	17.3%	0.3%	1.7%	0.0%
Vegetables, Melons, Potatoes and other Tubers	3.4%	-9.8%	-0.3%	12.1%	0.4%
Sugar, Jams, Honey, Syrups, Chocolate, Pastry	2.2%	-3.1%	-0.1%	1.7%	0.0%
Other Food Products	0.7%	-1.8%	0.0%	0.5%	0.0%
Non-alcoholic beverages	2.9%	2.4%	0.1%	6.1%	0.2%
<b>Alcoholic Beverages, Tobacco</b>	6.9%	3.4%	0.2%	6.4%	0.4%
<b>Clothing and Footwear</b>	4.0%	0.1%	0.0%	0.1%	0.0%
Housing, Water, Electricity, Gas and other Fuels	9.0%	2.3%	0.2%	6.5%	0.6%
Furnishings, household equipment and maintenance	5.2%	-3.3%	-0.2%	2.5%	0.1%
Healthcare	9.4%	-3.8%	-0.4%	-6.1%	-0.6%
Transport	12.3%	5.1%	0.6%	-4.7%	-0.6%
Communication	3.6%	-2.3%	-0.1%	-2.8%	-0.1%
Recreation and Culture	3.1%	-1.6%	-0.1%	0.2%	0.0%
Education	4.4%	3.6%	0.2%	5.8%	0.3%
Hotels, Cafes and Restaurants	3.1%	6.4%	0.2%	9.7%	0.3%
<b>Miscellaneous Goods and Services</b>	5.3%	10.1%	0.5%	12.1%	0.6%
<i>Consumer goods</i>	63.6%	-1.4%	-0.9%	0.6%	0.4%
<i>Average consumer goods</i>	7.1%	-1.6%	-0.1%	0.8%	0.1%
<i>Durable goods</i>	4.9%	-3.6%	-0.2%	-7.8%	-0.4%
<i>Service</i>	24.4%	6.6%	1.6%	9.4%	2.2%

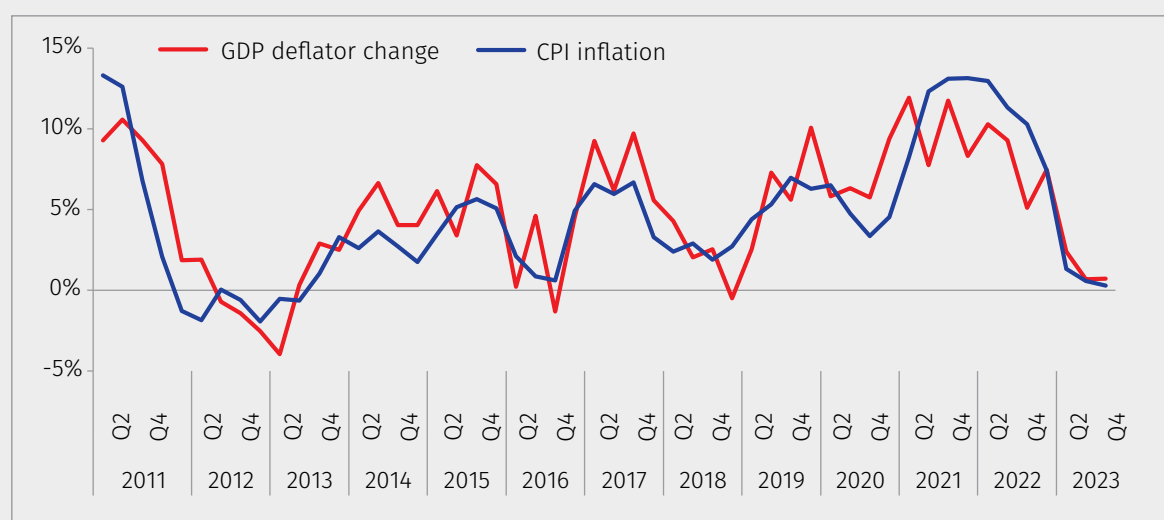
Source:GeoStat

## BOX 1 SHARE OF PROFIT AND WAGES IN INFLATION

The global economy has faced a one-two punch: pandemic supply chain disruptions and the war in Ukraine. These events have created pressure for hyperinflation, a rapid and excessive rise in prices. While inflation has peaked and started to ease in some countries, it remains a major concern worldwide.

To effectively combat inflation, policymakers are increasingly focused on how company profits and wages interact<sup>23</sup>. This analysis is rooted in the concept of Gross Domestic Product (GDP) deflator<sup>24</sup>, which tracks price changes of a nation's goods and services. Importantly, there's a strong link between GDP deflator inflation and Consumer Price Index (CPI) inflation, the measure most people are familiar with when discussing rising prices (see diagram 1.23).

Diagram N 1.23 Annual change in CPI and GDP Deflator



Source: GeoStat

In general, due to the increase in aggregate demand, along with the increase in the price level, the incomes of the companies operating in the market also increase. However, then, under inflationary pressures, employees also have an incentive to demand higher wages, which leads to an increase in their wages. At this time, the situation can develop in one of the following two directions:

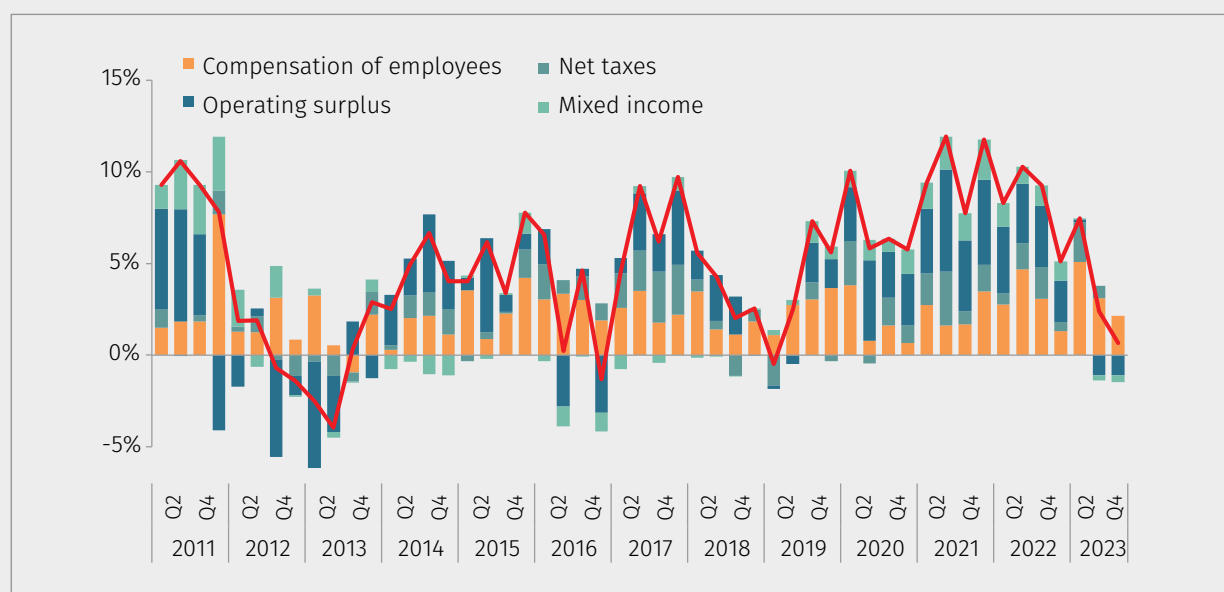
- 1) As the nominal cost per unit of labor increases for companies due to higher wages, they also raise prices in order to keep the initially increased profit margin at a higher level. That's the wage-price spiral. In such a scenario, we get the following picture: Finally, high inflation is simultaneously fueled by rapidly growing nominal profit of the companies and fast growing nominal wages.
- 2) Companies meet the demand for wage growth at the expense of slowing down their profit growth. In the case of such a scenario, we get the picture that inflation, which was initially caused by the increase in the profits of companies, will decrease again, even though the increase in wages will be high in the transition period.

23. For example, Philip Lane, the member of the board of the European Central Bank (ECB), notes in one of the interviews, that the profit rates of companies are unusually high. ([source](#)); his colleague Fabio Panetta highlights the potential threats of the profit-price spiral ([source](#)).

24. The Gross Domestic Product is the sum of the incomes of the entities involved in economic processes (company profits, employee compensation, net taxes, mixed income) and its analysis allows us to directly assess the impact of each of these factors on the inflation dynamics of the GDP deflator.

The analysis presented in this section paints a picture of the most likely scenario for Georgia, based on recent data. The decomposition of the GDP deflator indicates that the significant rise in Georgia's overall price level during the pandemic was indeed linked to an increase in company profits (as shown in diagram 1.24). At the onset of the pandemic, restrictions and disruptions in supply chains led to shortages of certain products, prompting producers to raise prices. Subsequently, the lifting of these restrictions was accompanied by a surge in pent-up demand. With supply chains still under strain, this increased demand provided producers with an additional incentive to raise prices, and thereby profits, even further. The influx of migration following the Russia-Ukraine war had a similar impact on demand. Collectively, these factors explain why suppliers have increased their prices, which in turn has boosted their profits.

Diagram N 1.24 Decomposition of GDP Deflator Change



Source: GeoStat and NBG calculations

It's worth noting that, in the wake of increased profits for companies amidst rising prices and heightened inflationary pressure, employees began to demand higher wages. The state of the labor market, particularly its density, also played a significant role in this dynamic<sup>25</sup>. Consequently, to retain or attract qualified personnel, companies were compelled to increase employee remuneration. However, the primary question is: which of the two aforementioned approaches have companies adopted to address the upward pressure on wages? As Diagram 1.24 illustrates, recently, companies have met the upward pressure on wages by reducing their profit growth rates. This suggests that, most likely, the conditions for a wage-price spiral to develop in Georgia are not present. Nevertheless, the National Bank of Georgia maintains a cautious policy and withdraws from the strict monetary policy only at a slow pace in order to minimize the risk of a high-inflationary environment.

25. Labor market tightness refers to a situation where companies find it difficult to find labor because there is a shortage of free staff with appropriate qualifications on the market.



## 2.1. MONETARY POLICY



Fostering price stability is the primary goal of the National Bank of Georgia<sup>26</sup>. Price stability implies a level of inflation over the medium term that is optimal for high and sustainable economic growth in the long term.

The monetary policy of the NBG relies on inflation-targeting framework. Under the inflation targeting regime, the target rate of inflation, i.e. the level of optimal inflation for the country, is set in advance. Then the monetary policy will be conducted in a way that for the medium-term there will always be an expectation of inflation returning to its target rate, including from the private sector. While the regime ensures that inflation is close to its target rate in the medium term, it also allows inflation to temporarily deviate from the target level in response to exogenous shocks<sup>27</sup> to minimize overall macroeconomic fluctuations. That is why, professional circles often refer to inflation targeting as flexible inflation targeting<sup>28</sup>. Complete elimination of short-term one-off factors affecting inflation cannot and should not be the goal of monetary policy, because such policy would result in excessively high macroeconomic volatility, making it difficult to achieve price stability in the medium term. Monetary policy is a tool to influence demand. Thus central banks mainly respond to demand shocks, because responding to supply shocks (for example, increase in excise duty, global commodity prices, and international transportation costs) is costly to the economy, leads to fluctuations in economic growth and decreases employ-

ment in the long run. Exception is when supply shock is prolonged and affects inflation expectations. It is important to note, that as Bernanke & Blinder (1992) and Bernanke & Gertler (1995) studies show, it takes some time to transfer monetary policy changes to the economy<sup>29</sup>.

Under the inflation targeting regime, the monetary policy rate (refinancing rate) is the NBG's main monetary policy tool to achieve inflation target. The monetary policy rate changes according to the inflation forecast. The decision to change the monetary policy rate is made following the analysis of the macroeconomic environment, study of the current situation in the financial markets, forecast of the inflation dynamics, evaluation of macroeconomic risks affecting inflation and inflation expectations. If the forecast inflation rate is higher than targeted, the National Bank of Georgia will tighten its monetary policy, and conversely, if the inflation forecast is below the target, the National Bank of Georgia will loosen the monetary policy. This tactic safeguards price stability and the lowest long-term interest rates compared to other alternatives. With the development of monetary policy instruments and its transmission mechanism, public spending is also reduced to ensure price stability. That is why the National Bank of Georgia is persistently improving the monetary policy instruments and increasing the efficiency of the monetary policy transmission mechanism.

The NBG implements the monetary policy in accordance with the Main Directions<sup>30</sup> of the Monetary and Exchange Rate Policy developed by it and approved by

26. Paragraph 1 Article 3 of the Organic Law on the National Bank of Georgia.

27. The term exogenous shocks implies external changes independent from the monetary policy.

28. "Under the flexible IFT framework, strong exogenous macroeconomic shocks did lead to significant deviations of inflation from the target, and of economic activity from potential. But monetary policy instruments were systematically adjusted to bring inflation back to target over time." - Clinton, Hlédik, Holub, Laxton, & Wang (2017) „Czech Magic: Implementing Inflation-Forecast Targeting at the CNB”, IMF Working Paper, pp. 30

29. Bernanke & Blinder (1992) „The Federal Funds Rate and the Channels of Monetary Transmission”, American Economic Review; vol. 82, issue 4, 901-21.

Bernanke & Gertler (1995) „Inside the Black Box: The Credit Channel of Monetary Policy Transmission”, the Journal of Economic Perspectives, Vol. 9, No. 4 (Autumn, 1995), pp. 27-48.

30. Resolution of the Parliament of Georgia on Main Directions of Georgia's Monetary and Exchange Rate Policies for 2023-2025, paragraph 1.

the Parliament of Georgia, according to which the inflation target has been set at 3% since 2018. Relatively high inflation is characteristic of transition economy countries, compared to developed economies, which is due to a faster rate of productivity growth in these countries<sup>31</sup> compared to developed countries. (Balassa, 1964; Samuelson, 1964).

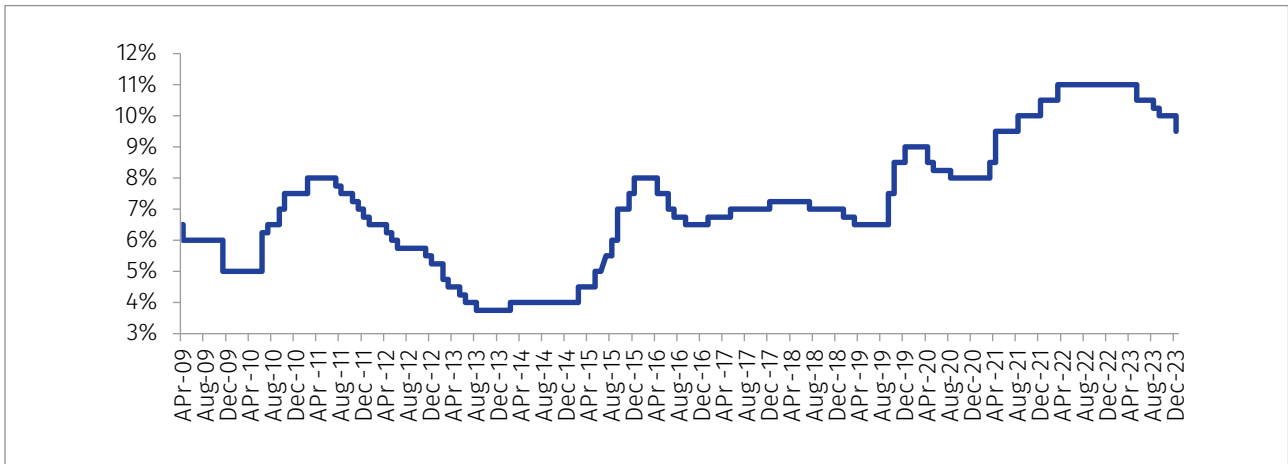
In 2023, inflationary pressures were alleviated. From the beginning of the year, inflation started to decline and remained below the target of 3% after March. The initial decrease in inflation was primarily attributable to the gradual dissipation of external shocks. In the post-pandemic period, the supply-demand imbalance in the international commodity market was rectified, and international food prices began to decrease. Concurrently, supply chains gradually recovered, and logistics disruptions were relatively reduced. Consequently, starting in 2022, the cost of global transportation gradually decreased, with this trend persisting into 2023. As a small open economy, Georgia is susceptible to global events, and the changes in international prices were also reflected in the local market. This was accompanied by a strengthening of real and nominal effective exchange rates in the first half of the year. Thus, the decrease in inflation at the beginning of the year was primarily driven by the reduction in the prices of imported products. From the second half of the year, the decline in inflation was primarily due to internal economic factors. In particular, as a result of timely and sufficiently tightened monetary policy, inflationary expectations exhibited a decreasing trend. Additionally, from the second half of the year, the inflation of locally produced products and services decreased significantly. The opening of the Turkish medicine market

also contributed to the reduction of inflation in 2023. In summary, the main factors for the elimination of inflationary pressures in 2023 were the neutralization of foreign influences and the normalization of the prices of locally produced products and services, achieved through a strict monetary policy.

In 2023, based on the inflationary trends and the inflationary forecast, the National Bank of Georgia began a gradual exit from tight monetary policy stance. At the beginning of the year, the Monetary Policy Committee (MPC) maintained the monetary policy rate at 11%. Since May, the monetary policy rate was cautiously reduced by at a slow pace. Neutralization of exogenous factors impact on inflation led to inflation deceleration from the beginning of 2023. Nevertheless, inflationary pressures stemming from domestic factors remained significant, as evidenced by the relatively high inflation of core and domestically produced products. Additionally, inflationary risks remained at a high level. Against the backdrop of the current acute geopolitical situation, global uncertainty was high, which meant that the risks of price increases for certain groups of imported products persisted. Along with external risks, local economic trends were also noteworthy. These factors led to the National Bank of Georgia's cautious approach and its gradual exit from a strict position in small increments. The policy implemented by the National Bank of Georgia contributed to the normalization of inflationary expectations and the overall reduction of inflation. As a result, domestically produced products, services, and core inflation decreased at a relatively slow pace during the year. In December 2023, the monetary policy rate, compared to the peak of the previous year, decreased by 1.5 percentage points (pp) and amounted to 9.5% (see diagram N 2.1).

31. Balassa, B. (1964), "The Purchasing Power Parity Doctrine: A Reappraisal", *Journal of Political Economy*, 72, 584-96.  
Samuelson, P (1964), "Theoretical Notes on Trade Problems", *Review of Economics and Statistics*, 23, 1-60.

Diagram N 2.1 Monetary Policy Rate

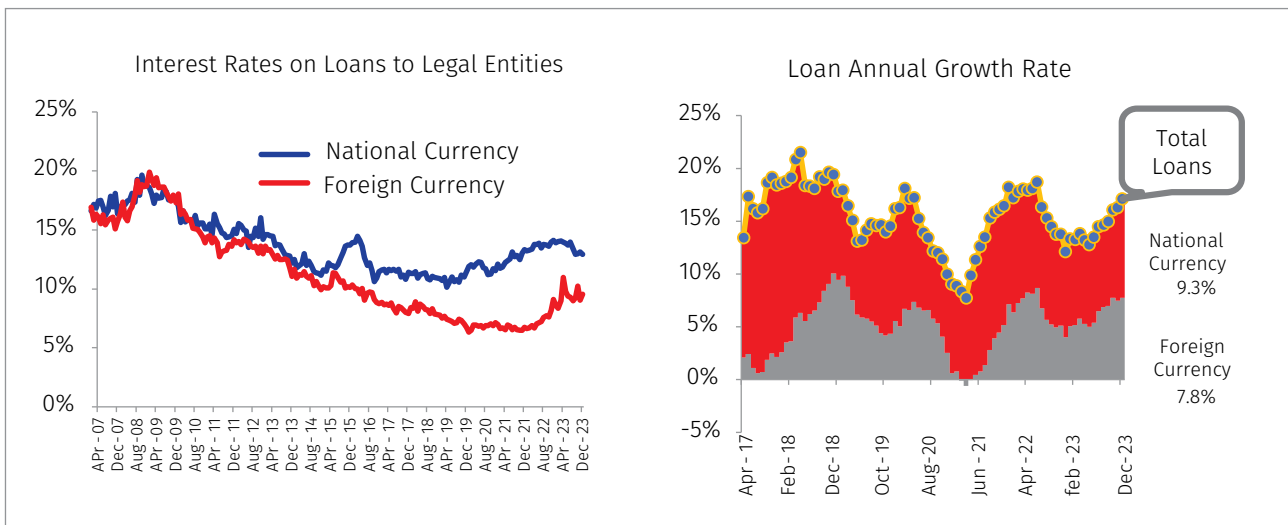


Source: NBG

Credit channel is a major transmission channel of monetary policy. Under loose monetary policy stance, market interest rates are low, which increases the lendin-

ing incentives and thus stimulates aggregate demand. In line with gradual exit from tight monetary policy in 2023, credit activity has accelerated.

Diagram N 2.2 Interest Rate Spread and Lending Activity (annual growth rate of loans by currencies)



Source: NBG

In August 2022, the maximum maturity of consumer loans was reduced from 4 to 3 years. The aim of this measure was to impose additional limitations on lending and mitigate the high-inflationary environment. As inflation significantly decreased in the second half of 2023 and fell short of the target rate, the NBG increased the maximum maturity of consumer loans to 4

years from November 1, 2023. This change, on the one hand, promotes and improves access to finance for the population, and on the other hand, renews the growth of consumer loans. Indeed, in December, compared to October 2023, the growth rate of consumer loans increased by 0.5 percentage points (pp), which has a loosening effect.

Due to the prolonged high inflationary environment Federal Reserve System and the European Central Bank maintained tight monetary policy. To mitigate the impact of globally tightened financial conditions on the local economy, the countercyclical capital buffer was accumulated gradually, while the upper limit of the minimum reserve requirements for funds attracted in foreign currency will be reduced from 25 percent to 20 percent. This will provide the local market with additional liquidity in foreign currency and more flexibility for buffer accumulation, which will somewhat mitigate the impact of globally tightened financial conditions on the financial sector, and as a result, improve access to finance. By reducing the minimum reserve requirement, the NBG can influence the rate of loans in the country. When the reserve requirement decreases, it becomes cheaper for the bank to attract deposits, which, in turn, is reflected in the reduction of the loan rate. As a result, foreign currency loans become cheaper for the borrower. Therefore, the reduced minimum foreign currency reserve requirement encouraged foreign currency lending in the local market.

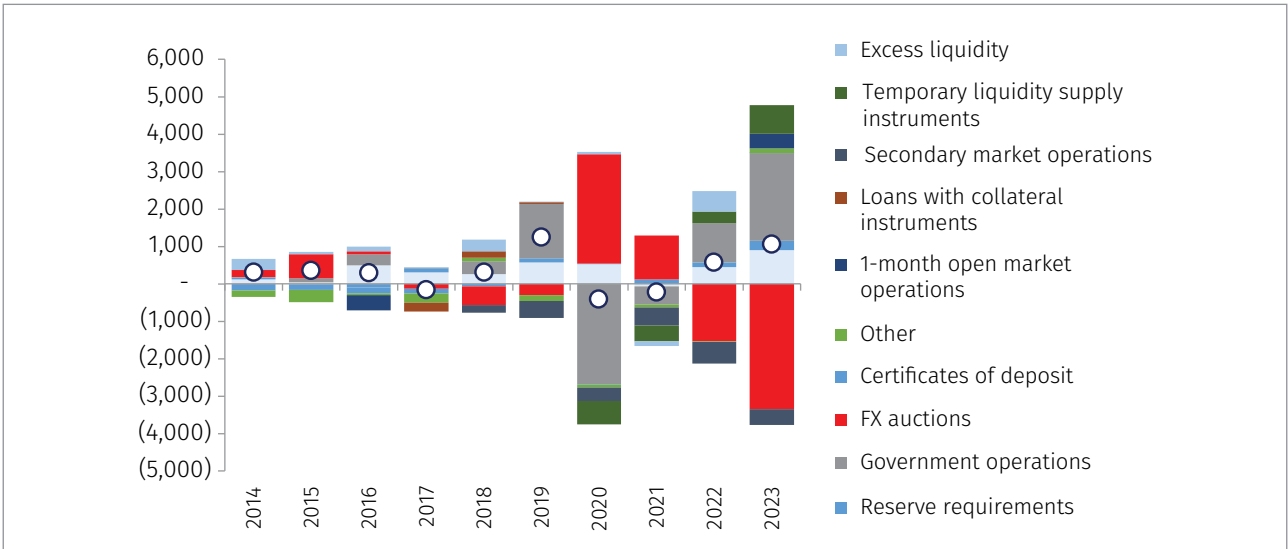
Under inflation targeting, the operational objective of the NBG is to manage short-term interest rates to safeguard price stability. For the effectiveness of monetary policy, it is important that the change in the policy rate is reflected in the interbank interest rate and, ultimately, affects the real economy. Short-term interest rates, in turn, are managed using the liquidity management framework.

The liquidity management framework of the National Bank of Georgia includes both liquidity supply and liquidity absorbing instruments. These are open market operations (refinancing loans and certificates of deposit), minimum reserve requirements, and stand-by instruments. During the year, the NBG continued to issue 3-month certificates of deposit, the purpose of which is to form the short-term yield curve. As a result, with these operations, the NBG kept the balance of deposit certificates at a minimum level, within 60-80 million GEL.

In 2023, banks actively used refinancing loans to manage liquidity and balance fluctuations arising from other sources of liquidity supply. Compared to 2022, the volume of refinancing loans increased at the end of 2023. Several factors influenced the volume of refinancing loans during the year (see diagram N 2.3).

On the one hand, against the background of strong economic growth, the demand for cash increased. At the same time, increased incomes also had a positive effect on the volume of deposits, which, in turn, was reflected in the increase in reserve requirements and, accordingly, in the increased demand for refinancing loans. Fiscal consolidation also had a significant impact - due to the reduction of government spending, the financial system lost part of the liquidity, to balance the demand for refinancing loans increased. The temporary suspension of the one-month open market instrument had a similar effect. At the same time, the use of temporary liquidity supply instruments launched during the pandemic gradually decreased, which greatly increased the demand for refinancing loans. In particular, the use of currency swap operations ended, and the volume of loans issued by the instrument supporting the liquidity of small and medium-sized businesses also decreased during the year. At the end of 2023, the additional instruments to provide liquidity, launched during the economic crisis caused by Covid-19, ended. In the first half of the year, against the background of the strengthening of the exchange rate, the National Bank of Georgia purchased a substantial amount of foreign currency through foreign exchange auctions and the rule-based interventions (BMatch); as a result, GEL resources were supplied to the market with this instrument, which sharply reduced the demand for refinancing loans. The supply of liquidity through foreign exchange interventions, in the first stage, is balanced by a reduced level of refinancing loans. Accordingly, due to the low level of demand for liquidity, the NBG temporarily suspended the use of the one-month open market operations in May 2023, and the secondary market purchases in August. Ultimately, the reduction in the supply of liquidity through these channels increased the demand on refinancing loans.

Diagram N.2.3 Factors affecting annual change in refinancing loans

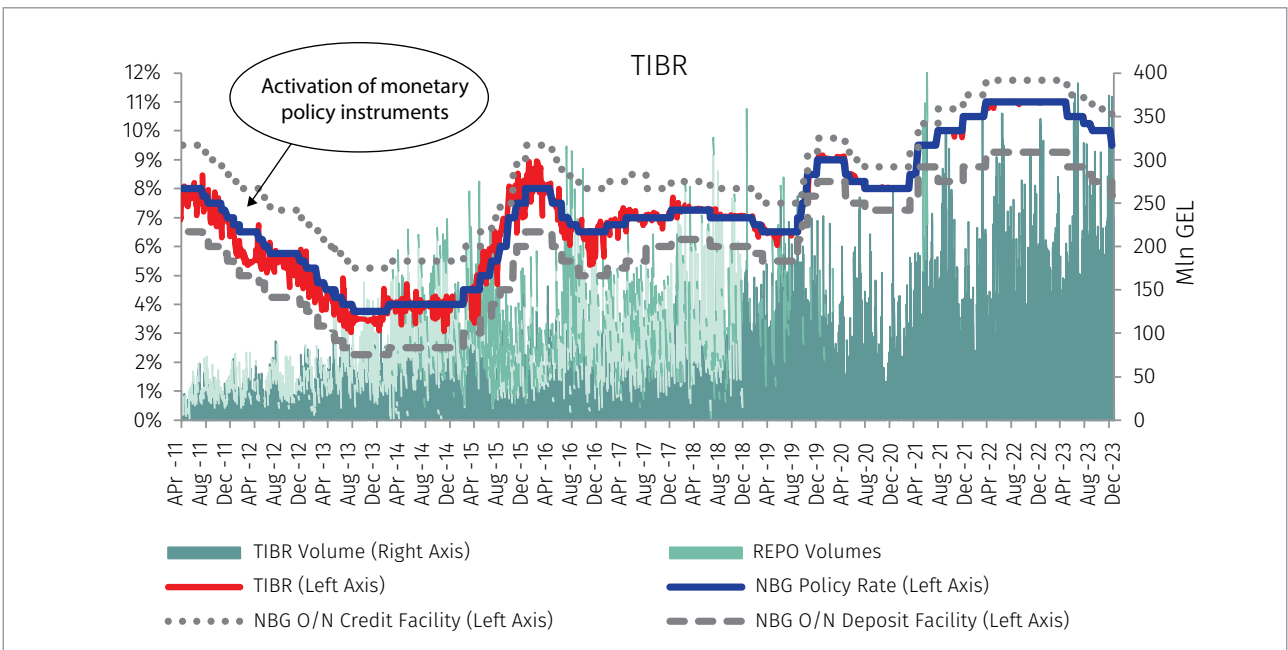


Source: NBG

Through the instruments described above, the NBG provided as much short-term liquidity to the financial sector as needed. As a result, as can be seen in diagram N2.4, interest rates in the interbank money market remained close to the policy rate, which is the best indicator to determine that the NBG provided the financial system with the appropriate amount of liquidity. If the system is supplied with less than the needed liquidity, then the interbank interest rate in-

creases relative to the policy rate and, conversely, goes down in case of excess liquidity. This would increase the interest rate volatility and reduce the effectiveness of monetary policy. The availability of sufficient resources of GEL for the banking system and, at the same time, effective management is important for encouraging GEL lending and promoting de-dollarization, which, in turn, reduces risks to financial stability.

Diagram N.2.4 Interbank Money Market



Source: NBG

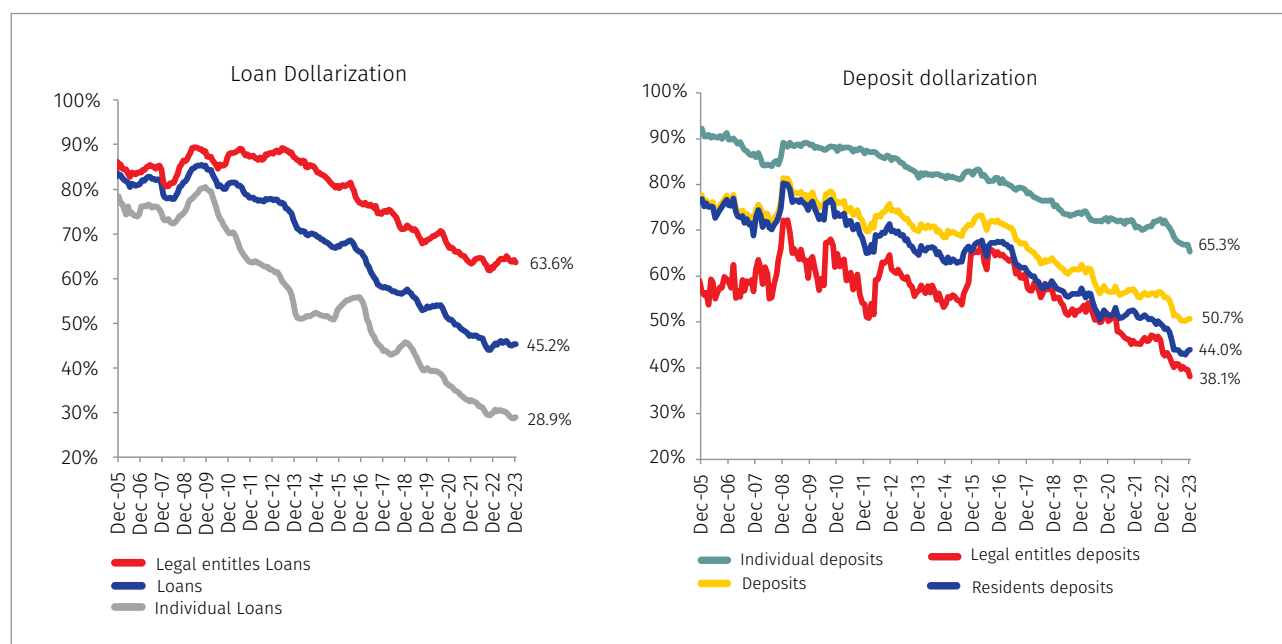
Promoting larization is a long-term goal for the National Bank of Georgia. Dollarization is an important challenges that becomes especially relevant with the increase in GEL interest rates, as a larger spread between GEL and foreign currency interest rates is reflected in higher foreign currency lending. High dollarization limits the effectiveness of monetary policy and contains risks to financial stability. Encouraging larization is a prerequisite for reducing macro-financial risks and increasing resilience to external vulnerabilities. Therefore, NBG prioritizes growth of larization and implements reforms to support it.

Larization continued actively in 2023. From the second half of 2023, the trend of loans' dollarization has slowed down and its level of dollarization slightly increased to mitigate the risks caused by the dollarization of loans, in 2023 the NBG imposed an additional requirement on regulated financial institutions. Unhedged foreign currency loan limit has been increased to 300,000 GEL from January 1, 2024. Foreign-currency denominated loans mostly variable-rate loans are accompanied by interest and exchange rate risks. The latter is particularly noteworthy, given the high share of unhedged foreign currency borrowers and the in-

creased volatility of regional exchange rates. It was the neutralization of such risks that became the reason for imposing additional requirements.

To evaluate in more detail the steps taken towards dedollarization, it is interesting to discuss the dynamics of dollarization of loans and deposits. Dollarization of loans amounted to 45.2 percent in December 2023, which is 0.4 pp higher than in the same period of 2022. As for the dollarization of deposits, in 2022, as a result of significantly increased migration flows due to the Russia-Ukraine war, the deposits of non-residents increased significantly. Most of these deposits were denominated in foreign currency. A similar trend continued in the first half of 2023, despite the fact that the dollarization of deposits decreased significantly. During 2023, the dollarization of total deposits, excluding exchange rate effect, decreased by 5.2 pp and equaled 50.7 percent. Despite the growing foreign currency deposits of non-residents, the dollarization of residents and individuals decreased by 5.2 pp and 6.2 pp, respectively, and amounted to 43.9 and 65.3 percent, which indicates an improvement in the level of dollarization of deposits.

Diagram N 2.5 Banking Sector Dollarization (excluding the exchange rate effect)



Source: NBG

## BOX 2. CREATING MONEY IN THE ECONOMY: GEORGIA'S CASE

Questions such as how money is created in the modern economy, who are the participants in this process, and where is the role of the central bank, often gain relevance. However, it is also often the case that only one factor of money creation is observed, which, of course, can easily lead to erroneous conclusions. For example, one such conclusion is that there is necessarily a positive relationship between the growth rate of broad money supply (M2) and inflation. In one of the previous monetary policy reports, we have already discussed this issue, where, based on the relevant data, it was clearly shown that there is no positive correlation between the change in the money supply and inflation after 2010. At this point one may wonder why there is no apparent correlation between these two variables when simple logic tells us that there should be. To answer this question, it is important to understand what the reason is for the increase in the money supply - an increase in the money supply or an increase in the demand for money. To see this, it is important to understand who and by what operations the money supply is created. This is exactly what we describe (the decomposition of the change in the money supply according to the sources of its supply) in this section.

All sources of creation/supply of money supply will ultimately be reflected in the balance sheet of depository corporations. Depository corporations are financial institutions that issue broad money liabilities. According to the international methodology, this sector is divided into two parts: the central bank, which issues M0 (cash outside banks) from the aggregates of the money supply, and other deposit corporations, which issue deposits included in broad money (in the case of M2 broad money, we are talking about deposits of GEL only, that is  $(M2 - M0)$ ). Other deposit corporations in the monetary landscape of Georgia are represented by commercial banks. Obviously, this decomposition of the money supply comes from accounting equality, not cause-and-effect theory, but that is the advantage of this decomposition of the money supply, that it is in itself true.

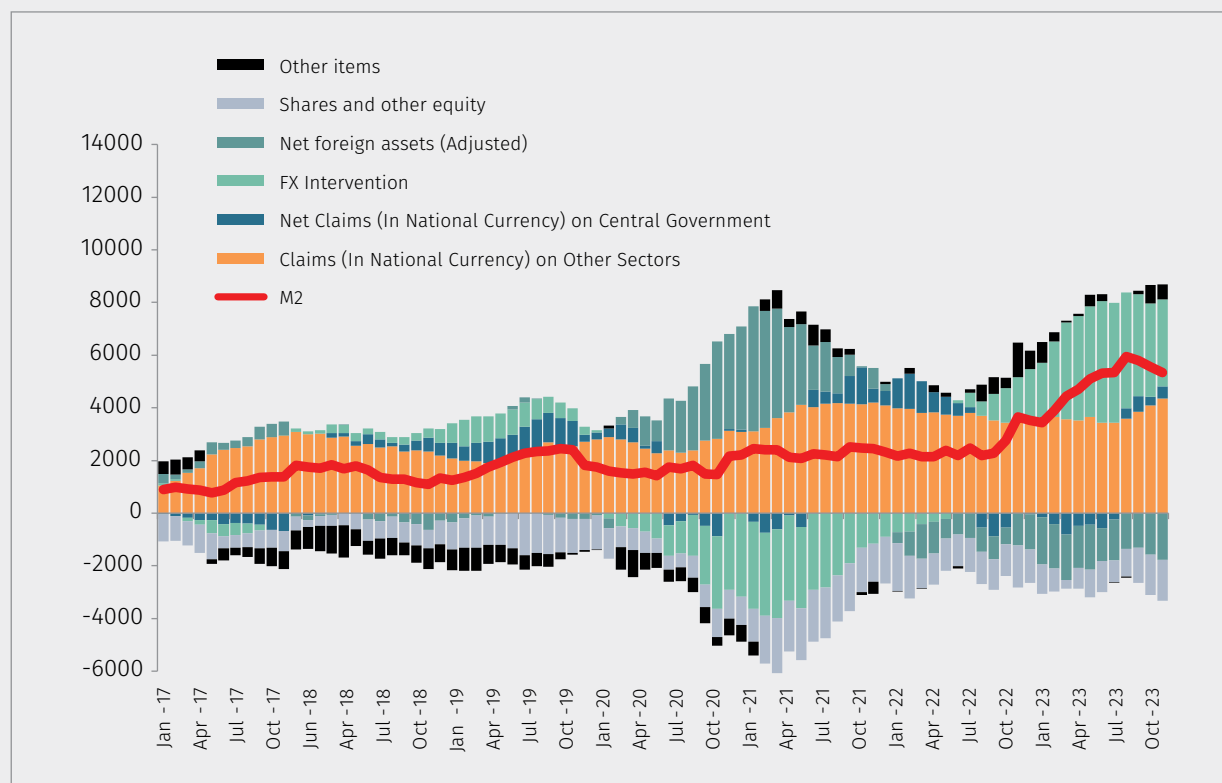
Therefore, to see what components determine the change in the money supply M2, we need to look at the aggregated balance sheets of the central bank and other depository corporations. The goal is to regroup the balances in such a way that on the left side of the balance sheet we have M0 (in the case of the central bank) and  $M2 - M0$  (in the case of the aggregated balance sheet of commercial banks), and all other items are on the right side. After making appropriate combinations/groupings of the balance sheet items, which makes the interpretation easier, we get the following 5 main items, which back the money supply M2:

- 1. Net foreign assets (with appropriate adjustments)** - This item represents net foreign assets on the balance sheet of the central bank less foreign currency liabilities to the central government and foreign currency liabilities to other depository corporations (such as required reserves, as well as amounts in foreign currency correspondent accounts of commercial banks). It shows the sources (transactions) of the money supply that change M2 and affect adjusted net foreign assets. One of these operations is the the central bank intervention in the foreign exchange market. For example, the purchase of foreign currency by the central bank increases M2, and the sale - on the contrary, decreases it. In addition, the same item reflects the government's transactions in foreign currencies, which ultimately change the money supply. For instance, it can be the government taking a foreign debt and then using this amount to purchase goods or services from the resident in national currency, or even transfer this amount to the resident as a transfer. Conversely, paying off the foreign debt with taxes collected by the government from residents will reduce M2. Therefore, the main source of the money supply described in this

item is central bank foreign exchange interventions and government budget deficits that are financed by foreign debt.

2. **Net claims to the central government in national currency** - this article represents the difference between the national currency claims and liabilities of depository corporations (central and commercial banks) to the central government. This reflects the operations of the national currency of the government, which replaces M2, for example, when the government takes a debt in national currency and then this amount gets into the accounts of residents. Accordingly, the source of the money supply described in this article is primarily the government budget deficit, financed by domestic debt.
3. **Claims against other sectors in national currency** - this item mainly includes loans issued by commercial banks to the national economy in national currency. Both in terms of content and statistics, this item is the main determinant of money supply, and it is commercial banks that create the largest part of money in the economy.
4. **Shares and other capital** - this item includes capital change operations. An increase in the capital of depository corporations reduces the money supply, since at this time other obligations of the central or commercial bank decrease, which implies a decrease in the share of deposits (which is the main part of M2), and a decrease in capital, on the contrary, increases M2. Consequently, capital growth requirements in the banking sector reduce money supply growth.
5. **Other items** - all other items that are not included in the above 4 items, such as net errors and omissions and other items left out in the rearrangement. As a rule, the combination of these articles is not a quantitatively important factor.

Diagram N 2.6



Source: NBG

Diagram 2.6 shows the annual change in the above 5 items from January 2017 to December 2023, which is summed up to the annual change in the money supply M2. Accordingly, they explain at the actual level the factors driving the change in the money supply. As expected, and which is fully compatible with the modern description of money creation (the so-called credit theory of money creation), the most important component in the change in the money supply throughout the period is the demand for other sectors in the national currency, i.e. the loans issued by commercial banks to the resident economy in the national currency. The next most visible component throughout the period is stocks and other capital, which also makes sense since, as we said above, changes in capital directly affect M2. While the growth of loans increased the money supply, the growth of capital, on the contrary, decreased it.

As can be seen from the results, the most interesting are the years 2020-2023. From the change in adjusted net foreign assets described above, we have extracted net central bank interventions (US dollar purchases minus US dollar sales) and this is shown in light green. As we can see, throughout 2020 and half of 2021, the central bank's sale of dollars in the foreign exchange market made a rather large negative contribution to the change in the money supply (restrained the growth of the money supply), although it was balanced by the government's foreign currency operations, which largely financed the budget deficit (which, on the contrary, accelerated the growth of the money supply). As for the second half of 2021 onwards, these two effects acted oppositely, the central bank's foreign exchange interventions (net purchase of dollars) had a positive effect on the change in M2, while other operations affecting the change in adjusted net foreign assets, on the contrary, reduced the growth of the money supply.

By isolating these main drivers of money supply growth (loans, budget deficits and central bank interventions) on a quantitative level, it is possible to get some idea of where money supply growth is coming from - demand or supply. For instance, while high credit growth and high budget deficits can usually be seen as money supply, central bank foreign exchange interventions are usually a reflection of money demand. For example, when confidence in GEL deposits increases and the demand for GEL increases, at this time we see a decrease in inflation and an appreciation of the GEL exchange rate. The purchase of US dollars by the central bank through foreign exchange interventions is done precisely in the conditions of appreciation of the exchange rate. As a result, it turns out that, as a rule, with foreign exchange interventions, the money supply increases when the demand for money also increases. At such a time, we can easily have a situation where the growth of the money supply has accelerated, just as inflation has decreased and the exchange rate has stabilized, as happened in 2023. Obviously, there may be an example in the opposite as well. Such examples in both directions largely eliminate the positive correlation between money supply and inflation.

## 2.2. MONETARY POLICY INSTRUMENTS



The implementation of Monetary Policy Committee (MPC) decisions (tightening, easing, or keeping monetary policy unchanged) is done through monetary operations. The objective of monetary operations is to keep interbank interest rates stable and close to the policy rate determined by the Monetary Policy Committee of the NBG. The NBG's operational framework consists of the following monetary instruments: refinancing loans, the one-month open market instrument, open market operations with government securities, overnight loans, overnight deposits, certificates of deposit, and minimum reserve requirements.

The interbank deposit/loan market is a money market where banks trade in short-term liquidity. This market is of great interest to the National Bank of Georgia, as it plays a crucial role in the functioning of the monetary policy transmission mechanism. The NBG influences interest rates by monetary policy decisions and monetary policy instruments.

The Tbilisi Interbank Interest Rate (TIBR) index of the money market is the overnight interest rate benchmark. It is based on actual transactions on the interbank money market, which also increases the credibility of the index. The reliability of the index is enhanced by the involvement of the NBG in the process of collecting information and calculating the index. For the use of medium and long-term instruments in the market as a benchmark (especially in GEL variable rate instruments) on March 14, 2019, the National Bank of Georgia started publishing TIBR term rates that are based on the overnight TIBR index and represent a more effective way to manage interest rate risks. In a market economy, the interest rates on financial instruments (coupons, interest) are of different maturities (month, quarter, 6 months, year). Management of financial

risks arising from exchange rate volatility requires appropriate maturity insurance mechanisms and appropriate maturity indices for pricing. Such indices, in turn, rely on a transparent methodology and market players trust these as an independent source.

The methodology for calculating the TIBR index and TIBR term rates that includes procedures for calculating and publishing indices, was developed in close cooperation with players of money markets and with the help of the EBRD. This methodology also provides procedures for data control and methodology review. The TIBR indices are published daily (at 9 a.m.) on the official website of the National Bank of Georgia.

In 2023, the volume of transactions performed in national currency on the interbank market was 22.3 percent larger compared to the previous year's same rate and amounted to GEL 4 6.85 billion. As the monetary policy rate of the National Bank of Georgia changed, so did the interbank interest rates in 2023, moving close to the monetary policy interest rate. As part of the decisions of the Monetary Policy Committee and based on the short-term liquidity forecast in the banking system, the National Bank of Georgia set the weekly volumes of refinancing loans and those for one-month open market instruments. The NBG managed these processes in such a way that the average interest rate stated at the auction was kept close to the monetary policy rate.

### 2.2.1. REFINANCING LOANS

The National Bank of Georgia used the refinancing loan instrument on a weekly basis through 2023 to ensure short-term liquidity in the banking system. The refinancing instrument provides adequate liquidity to the banking system. Representing a reliable and low-risk source of short-term liquidity, refinancing loans have positively affected the development of the money market and overall financial stability. The GEL liquidity risks in the money market and fluctuations in market interest rates are declining, which is evident from the

dynamics of TIBR interest rates over the last decade. As the National Bank of Georgia is the sole provider of short-term liquidity in lari on the market, the NBG has the capacity to achieve its desired interest rate on the interbank market with the help of the refinancing loan instrument. The interest rate for refinancing loans offered on auctions are based on the NBG's monetary policy rate.

In 2023, the collateral base of monetary operations encompassed certificates of deposits of the National Bank of Georgia, Georgian government securities, lari-denominated securities issued by international financial intuitions and lari-denominated securities issued by legal entities, and loan assets of commercial banks. To qualify for certain operations, the NBG defined appropriate criteria for each type of collateral (e.g. minimum level, residual maturity, currency, etc). Commercial banks used all types of collateral in their operations with the National Bank of Georgia in 2023.

### 2.2.2. ONE-MONTH OPEN MARKET INSTRUMENT

Similar to other monetary instruments, the one-month instrument functions to manage short-term interest rates in the interbank market, which is in line with best international practice and the recommendations of the International Monetary Fund's Technical Assistance Mission. The liquidity forecasting group evaluates the short-term liquidity deficit in the banking system on a weekly and monthly basis, and then, an auction is announced, based on this, on the specific volume of the one-month open market instrument to be offered. The minimum interest rate on this instrument at auction equals the monetary policy rate. The assets same as for the refinancing loans are used as collateral. During 2023, the National Bank of Georgia absorbed surplus foreign currency in the foreign exchange market and provided the market with the corresponding amount of GEL liquidity. Due to this, the money market needed temporary liquidity from the National Bank of Georgia

in a smaller volume. Hence, from May 2023, the National Bank of Georgia stopped using the one-month open market instrument and mainly used the refinancing loan instrument for temporary liquidity needs.

### 2.2.3. OVERNIGHT LOANS AND OVERNIGHT DEPOSITS

The National Bank of Georgia continued to use the interest rate corridor in the interbank market in 2023 to support the development of the money market, reduce the volatility of interbank interest rates and increase the activity of the money market. The latter facilitated the interbank market to maintain a stable interest rate. The interest rate corridor was defined as an equal deviation from the monetary policy rate to form the upper and lower bounds of interest rates. The upper bound of the interest rate was used for overnight (O/N) loans of the National Bank of Georgia, and the lower interest rate bound was used for O/N deposits of the National Bank of Georgia. In 2023, the interest rate corridor was 2.5pp – the monetary policy rate plus/minus 0.75pp. That was to maintain the advantage of interbank deposits compared to overnight deposits of the National Bank of Georgia. The use of an interest rate corridor reduces the excessive volatility of interest rates in the interbank market and, in turn, helps bring the interbank interest rate closer to the monetary policy rate.

Overnight loans of the National Bank of Georgia represent the fastest source of liquidity for the banking sector, albeit being offered at a higher price in comparison with the market rate. The collateral base accepted for overnight loans was the same as that for refinancing loans.

Commercial banks can use the O/N deposit instrument to place excess GEL liquidity on correspondent accounts on the National Bank of Georgia's overnight deposits at the end of the day. Such deposits are returned to

the commercial banks' correspondent accounts at the beginning of the next business day. This instrument plays an important role in stabilizing interest rates in the interbank market.

#### 2.2.4. ADDITIONAL LIQUIDITY SUPPLY INSTRUMENTS

In the context of the pandemic, the National Bank of Georgia launched temporary liquidity instruments: currency swaps, standby swaps, and liquidity supply instruments for small and medium-sized businesses, to minimize potential liquidity risks to the financial sector in 2020.

##### **Standby Swap Instrument**

The National Bank of Georgia introduced and launched a standby swap instrument as an additional liquidity support instrument, and also the one to insure against liquidity risks, for the banking sector in May, 2020, allowing commercial banks to receive additional lari liquidity at any day at a penalty interest rate. None of the commercial banks used this instrument in 2023, due to its higher interest rate.

##### **Liquidity Instrument to Support SME**

In June 2020, the National Bank of Georgia launched an additional liquidity instrument to reduce the negative impact of the pandemic on the economy and to support small and medium-sized businesses. The one-month liquidity instrument designed to support small and medium-sized businesses offered the possibility of monthly renewals and was used by six commercial banks in 2023. Based on the need for

liquidity, the volume of the instrument changed over the months and its maximum number was GEL 314.1 million early in the year, while its minimum number was GEL 21.7 million at the end of the year. Supply of liquidity through this mechanism gradually reduced in 2023. This mechanism of liquidity management was operational until the end of 2023.

#### 2.2.5. SECURITIES

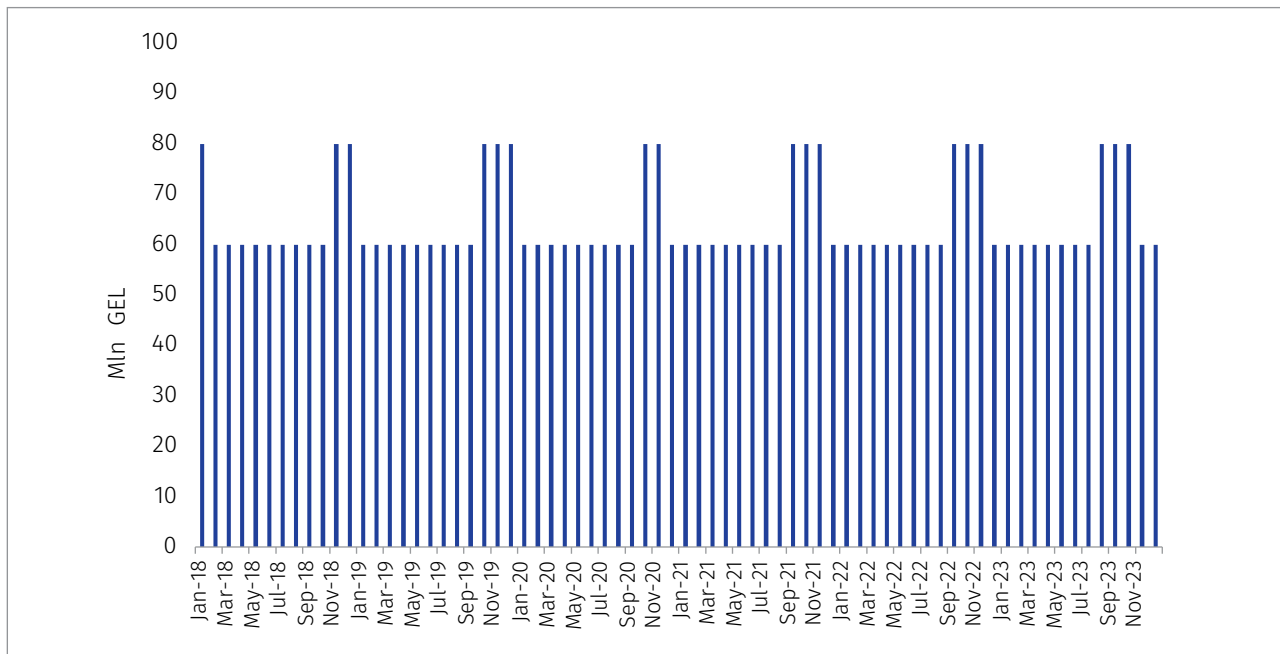
The National Bank of Georgia issued 3-month certificates of deposit, and the Government of Georgia issued treasury securities of 6-month, 1, 3, 5, 7 and 10-year residual maturities in 2023. These securities were in high demand by commercial banks and helped to establish a stable yield curve. This curve provides important information about interest rates at different maturities and the expectations of financial market players.

##### **Certificates of Deposit**

The National Bank of Georgia issued 3-month certificates of deposit, used by the banking sector as an attractive and effective short-term liquidity management tool in 2023.

Out of 13 auctions announced in 2023, commercial banks purchased the full amount of certificates of deposit offered at all auctions. In total, certificates of deposit with a nominal value of GEL 260 million were placed and same were repaid. As of December 31, 2022, GEL 60 million worth certificates of deposit in circulation were held by 4 commercial banks.

Diagram N 2.7 Dynamics of Certificates of Deposit Portfolio 2018-2023



Source: NBG

**Government Bonds**

As of December 31, 2023, the National Bank of Georgia held government bonds with a nominal value of GEL 152 million, which were not used for open market operations during the year.

**Treasury Bills and Treasury Bonds**

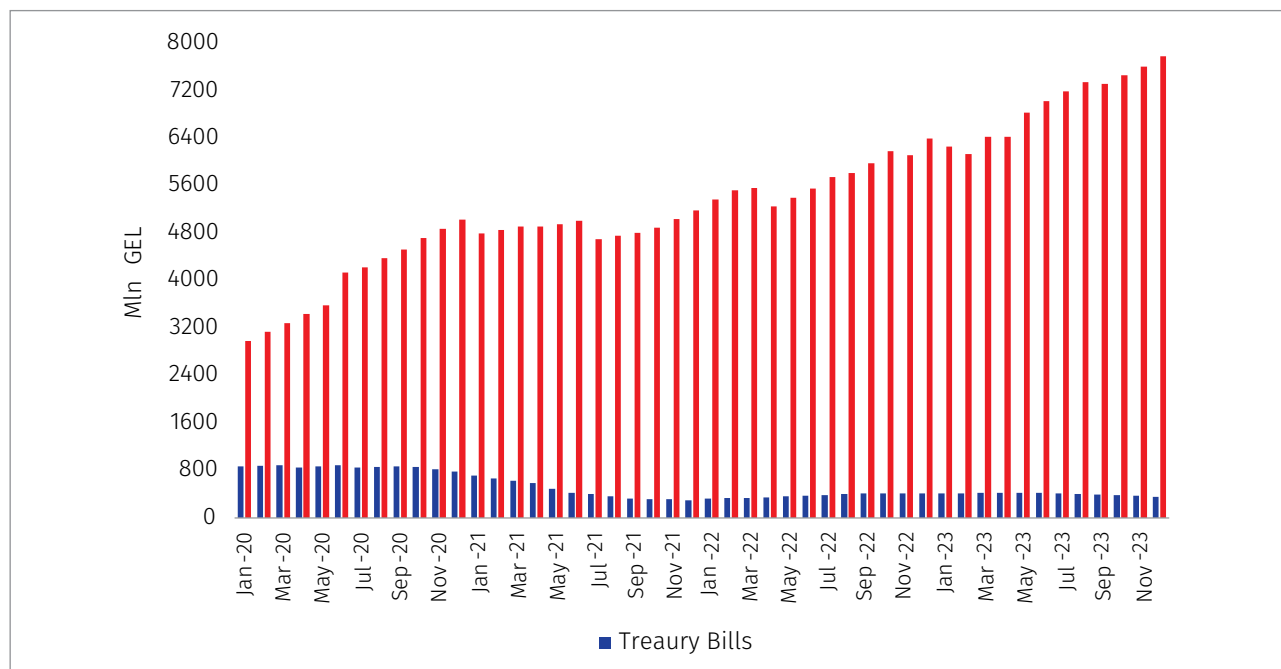
To further develop the GEL money market, it was crucial that the Ministry of Finance of Georgia increased the emission of government securities. In 2023, the Ministry of Finance issued 6-month and 1-year residual maturity discount securities – treasury bills, and 3-, 5-, 7 and 10-year residual maturity coupon securities – the treasury bonds. These securities were denominated in the national currency in dematerialized form. The nominal value of a security is GEL 1,000. The placement of treasury bills and bonds are executed through a multiple price auction conducted by the NBG via the Bloomberg trading platform. All commercial

banks licensed by the National Bank of Georgia can participate directly in an auction and any legal entities or individuals may also participate using a commercial bank as an agent.

In 2023, 66 auctions of treasury bills and notes were conducted, and GEL 2.9 billion worth of securities were offered. As of 31 December 2023, 14 commercial banks, the NBG and non-banking investors held GEL 8.1 billion worth of securities in circulation. Non-banking investors held treasury securities worth GEL 1175.0 million.

The volume of government securities in circulation in the market is still small compared to the size of the economy. In order to increase market liquidity, the Government of Georgia has issued 2-, 5- and 10-year benchmark bonds since 2018. This has led to an increase in the issuance of treasury securities, which contributes to the reduction of foreign exchange risk.

Diagram N.2.8 Dynamics of Treasury Bills and Treasury Bonds Portfolio 2018-2023

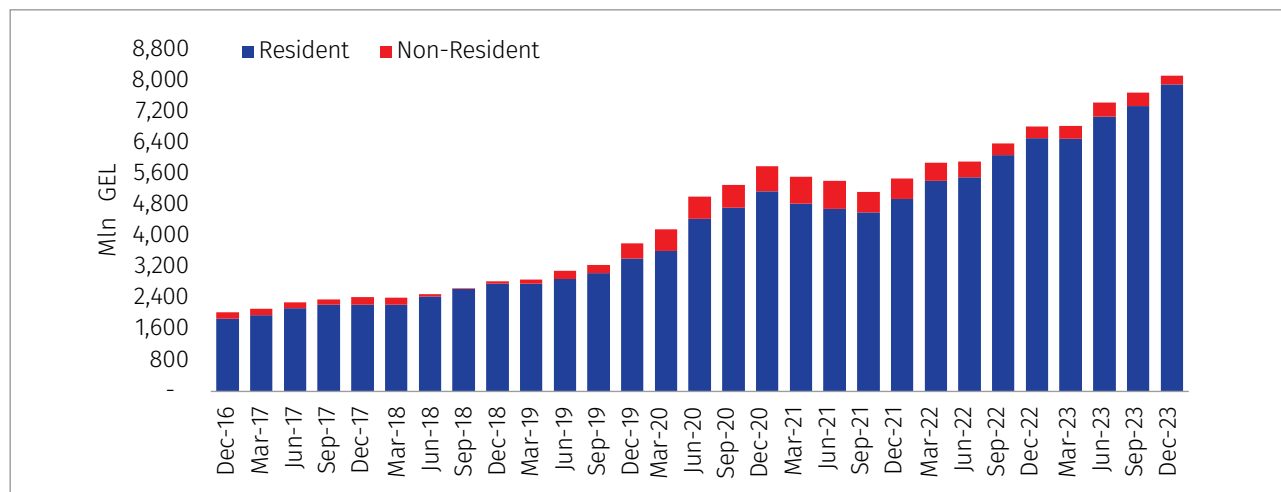


Source: NBG

Treasury securities are mainly owned by residents. The portfolio of securities owned by residents amounted to GEL 7,904 million as of December 31, 2023. The portfolio

of treasury securities owned by non-residents amounted to GEL 234 million as of December 31, 2023.

Diagram N.2.9 Treasury Bills and treasury bonds portfolio dynamics by ownership 2018-2023



Source: NBG

To provide incentives for the secondary securities market, the National Bank of Georgia continued to foster the full functioning of the Georgian Securities Settlement System (GSSS) and various integrated systems in accordance with the current requirements, by its own material and intellectual investments. The interbank repo market, based on the repo

master agreement, was established in line with best international practice and initiated by the National Bank of Georgia in close cooperation with the Georgian banking community. A repo transaction is the sale of securities with a subsequent obligation to sell back the same or equivalent securities under pre-agreed terms. Banks used the Bloomberg trading platform

and the Georgian Securities Settlement System (GSSS) to conduct repo transactions. Using these systems, in 2023 a total of 33 repo transactions were made between commercial banks worth GEL 3,175.5 million.

The National Bank of Georgia closely cooperates with Bloomberg to support the development of the financial market. Over the past decade, the Bloomberg platform has been dynamically used by both the National Bank of Georgia and local market players. The interbank market embarked on the new E-Bond platform in 2023, with the active participation of the National Bank of Georgia and commercial banks. Notably, Georgia is the first country where this new Bloomberg platform was introduced. The Bloomberg E-Bond technology solution allows local market players to trade repo transactions using modern technologies. The E-Bond platform provides the market with all necessary instruments, price quotations, and analytical data for concluding repo transactions. The platform is integrated through a secure interface with the local GSSS (Georgian Securities and Settlement System), providing fast and secure settlement of transactions concluded. The infrastructure and experience in the securities market provide a good basis for the further activation of the secondary securities market, which should lead to an increase in the liquidity of the securities market.

### **A pilot program for the primary dealer system for the development of the securities market**

Development of the Treasury securities market is a strategic focus of the development of the Georgian financial market and government debt management. In recent years, the volume of the securities market has been gradually increasing. The benchmark bonds were first issued in 2018, with volumes gradually increasing.

To take the securities market development to the next level, to expand the investor base and activate the secondary market, the National Bank of Georgia and the Ministry of Finance of Georgia considered it expedient to establish a primary dealer institute tested in international practice. The institute of primary dealer can act as an important mediator in

the securities market, between the Ministry of Finance of Georgia as the issuer of treasury securities, and investors. The well-developed government securities market will in turn help the advancement of the capital market. Primary dealers will take care of the diversification of the investor base and the increase of the liquidity of the secondary market by regular price updates and provision of appropriate trade and settlement infrastructure.

The National Bank of Georgia and the Ministry of Finance of Georgia, with the technical assistance of the International Monetary Fund and the World Bank, spent a great deal of time in recent years preparing a pilot program for primary dealers. A jointly prepared memorandum of understanding was discussed with market players. Finally, six commercial banks operating in Georgia expressed readiness to participate in the pilot program of the primary dealer, and memoranda of understanding were signed with them. The pilot program launched in November 2020 and its validity period was set at 1-1.5 years initially. The progress of the pilot program is assessed on a regular basis. As it develops further, the results of the pilot program will be summarized and future development plans will be outlined. During 2023, four commercial banks continued to participate in the pilot program of primary dealers.

### **NBG Operations in the Secondary Market**

The National Bank of Georgia works on improvement and development of monetary instruments and the liquidity management framework on an ongoing basis. Buying and selling securities through open market operations is one of the central banks' monetary policy instruments that serves the task of managing liquidity.

In 2023 the NBG continued purchasing securities under open market operations in the secondary market. The goal of these operations was to effectively manage the liquidity of the national currency, along with promoting the development of the securities market. In August 2023, due to the low level of demand for liquidity, NBG temporarily stopped buying securities in the secondary market.

The National Bank of Georgia held 8 auctions during 2022 in which it purchased treasury securities with GEL 480 million of nominal value. Of this, the securities portfolio held by the National Bank of Georgia as of December 31, 2023, amounted to GEL 2,388.6 million, considering the balances of securities repaid in 2023 and acquired in previous years. At the end of 2022, the volume of this portfolio was GEL 2,043.8 million.

## 2.2.6. MINIMUM RESERVE REQUIREMENTS

By employing the minimum reserve requirements instrument the National Bank of Georgia creates a precondition for the effective use of other monetary instruments. Minimum reserve requirements for funds raised in GEL have not changed recently. These did change in late 2021 for foreign currency attracted funds, staying in the range of 10-25% before December 2023, becoming 10-20% in December 2023 subject to the level of dollarization at each commercial bank. The higher the dollarization of deposits at a commercial bank, the more the reserve requirements are for this bank. In terms of residual maturities, funds borrowed in national currency with a maturity of more than 1 year and in foreign currency with a maturity of more than 2 years are exempt from reserve requirements.

Minimum reserves placed in the national currency by commercial banks at the National Bank of Georgia during 2023 were subject to the monetary policy rate<sup>32</sup> (active at that period) accrued on them by the National Bank of Georgia, 0 (zero) percent for foreign currency.

## 2.2.7. DEVELOPMENT OF THE SECURITIES SETTLEMENT SYSTEM IN GEORGIA

The Securities Settlement System has been operating at the National Bank of Georgia since 2010. This modern, high-tech, fast and secure electronic system ensured safe and transparent securities transactions for Government and NBG-issued securities.

Launched on 3 December 2018 and successfully

operating throughout 2023, the Georgian Securities Settlement System (GSSS) provides both local and international financial market members with high-quality services. This system can settle the whole spectrum of both public and private securities. Transactions with securities have become faster, cheaper, more convenient and fully protected. This project is a clear example of successful cooperation between the National Bank of Georgia and the private financial sector. The innovative GSSS system includes modern attitudes such as effective liquidity management mechanisms, partial settlement capacity, netting of reverse transactions, automatized pledging and intraday liquidity provision mechanisms. All local commercial banks, as well as some brokerage companies are connected to the GSSS. The system is integrated with the stock exchange and Bloomberg trading platforms and automates the entire trading and settlement cycle. Thus, it only takes a few minutes from the time of a transaction to its settlement. With the introduction of the new system, available procedures and payment procedures, which were based on the principles recognized in international best practice, were renewed. Investors' security holdings will now be more securely protected, making it easier and more convenient to convert them into cash (through sales, pledge or repo operations) if needed. This will undoubtedly increase the attractiveness of the Georgian capital market for Georgian and foreign investors.

The updated GSSS allows the integration of the Georgian Central Securities Depository in the system, to provide services to all members of the Georgian securities market, and to register and settle all types of securities in this system in Georgia (including bonds and shares issued by private companies). Private securities issuance, repayment, buying and selling, repo, coupon and dividend payment operations registered in this system are fully automated, as well as their pledging to the National Bank of Georgia or professional market members.

32. See details at: <https://www.nbg.gov.ge/index.php?m=558>

The updated GSSS system is expected to make the Georgian financial markets attractive for foreign financial institutions and investors, while helping local securities market infrastructure to become more reliable and up-to-date.

## 2.3. EXCHANGE RATE POLICY AND INTERNATIONAL RESERVES MANAGEMENT



### Exchange Rate Policy

Georgia is a small, open economy with floating exchange rate regime. Under Floating exchange rate regime the exchange rate is formed on the basis of market supply and demand and macroeconomic fundamental factors. The floating exchange rate is optimal for Georgia. With inflation targeting and free capital mobility, it is necessary to have a floating exchange rate regime. On the one hand, free capital mobility helps productivity growth which ultimately leads to high long-term economic growth. On the other hand, independent monetary policy is essential so that the monetary policy stance be in line with the business cycles of the Georgian economy, so that the response of the monetary policy is in accordance with the economic cycles of Georgia. An independent monetary policy is optimal because Georgia's economic cycles do not match those of other developed countries, including the United States. Independent monetary policy reduces the economic fluctuations caused by business cycles. As a result, inflation and employment are more stable, which is a prerequisite for long-term economic growth and social welfare.

During 2023, in order to reduce sharp fluctuations in the exchange rate and maintain gross international reserves at an adequate level, the National Bank of Georgia intervened in the foreign exchange market through foreign exchange auctions and the BMatch platform. During the reporting period, the National Bank of Georgia actively used the BMatch platform that was implemented in 2020. Interventions of the National Bank of Georgia on the BMatch platform are

based on rules and are carried out within the limits of predetermined amounts and conditions. During 2023, the NBG mainly purchased FX through BMatch platform, and the net purchase amounted to 1,445.5 million USD. Through foreign exchange auctions, during 2023, the National Bank of Georgia sold 166.8 million US dollars. Thus, in the reporting year, the net purchases of the NBG 1,278.7 million US dollars.

The nominal exchange rate of GEL appreciated significantly for the reporting period. In 2023, the nominal effective exchange rate of the lari appreciated by 14.8 percent per year, and the real effective exchange rate went up by 2.1 percent per year.

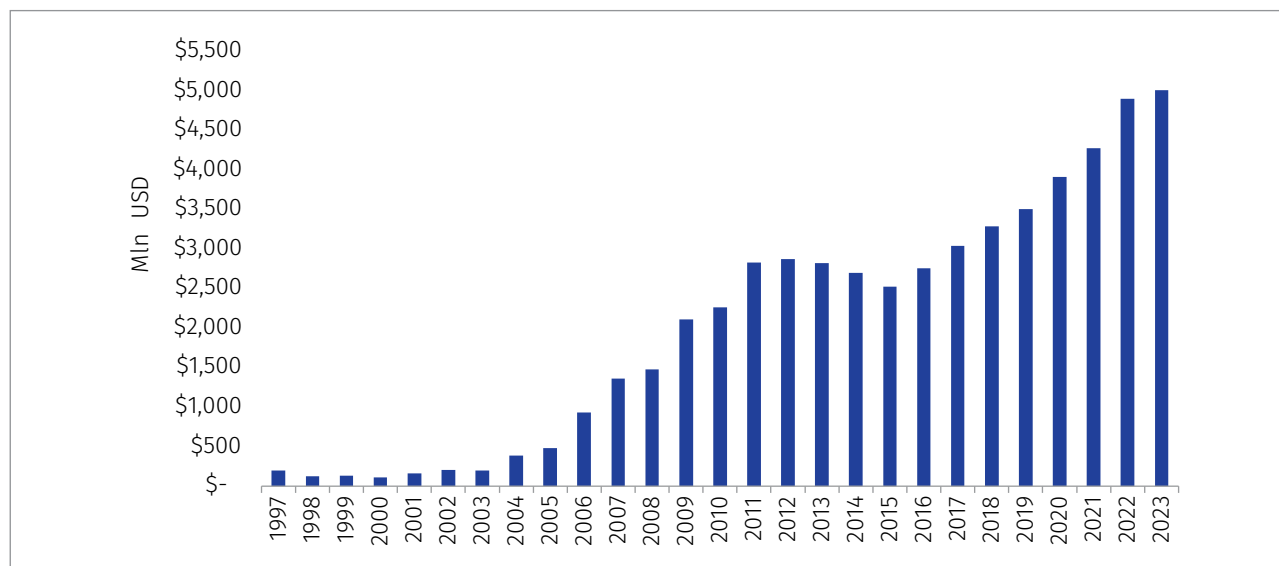
### International Reserves Management

The volume of international reserves of the National Bank of Georgia increased by USD 108.1 million in 2023, compared to the previous year and as of December 31, 2023 amounted to USD 5.01 billion.

The factors that affected the volume of the NBG's international reserves during 2023 traditionally were: the foreign exchange auctions of the NBG, servicing of government debt and FX expenses, credits and grants from international institutions, change of balance on reserve accounts. NBG was a net purchaser in the FX market during 2023: net foreign exchange purchases of the NBG in 2023 through foreign exchange auctions and Bloomberg's Bmatch platform amounted to USD 1.28 billion. The amount of grants and loans received from international financial institutions and donor states in foreign currency to the National Bank of Georgia accounts to finance various programs and projects was about USD 468.5 million.

In the reporting year, the reduction of international currency reserves led to a decrease in the balances on the reserve accounts of commercial banks. The dollarization of deposits in 2023 was significantly decreasing. Due to the fact that compliance with mandatory reserve norms depends on the dollarization of deposits, the amount of money to be kept by banks as minimum mandatory reserves decreased, leading

Diagram N 2.10 Official International Reserves 1997-2023 (million USD)



Source: NBG

to a decrease in balances on reserve accounts and reducing international currency reserves. In addition, from December 2023, the upper limit of the reserve norm on short-term foreign currency liabilities was reduced from 25 percent to 20 percent, which further reduced foreign exchange reserves. Following from both of these factors, the reserves of the National Bank of Georgia decreased by 573 million USD in 2023. At the same time, the service of the state foreign debt and foreign exchange expenses amounted to approximately 1,354.1 million US dollars.

During 2023, the investment policy of the National Bank of Georgia was still conservative and focused on reducing credit risks. International reserves of the National Bank of Georgia were placed in state treasury obligations of the USA, Eurozone countries, Canada, state agencies of the same countries and supranational financial institutions with high liquidity and international banking institutions with high credit rating. During 2023, the revenues received from the management of international reserves of the National Bank of Georgia amounted to 391.6 million GEL. The dynamics of the yield of reserves during 2023 was

determined by the increase in interest rates on a global scale.

In 2023, the National Bank of Georgia continued to cooperate with the World Bank within the framework of the Sovereign Investment Partnership Program. The NBG became a member of this program in 2009 and provides technical support for the further development of the field of international reserves management at the NBG, creation of relevant infrastructure and accumulation of knowledge, and also includes the sharing of experience of the World Bank in the fields of portfolio and risk management, settlement, accounting, legal and information technology.

In 2023, the cooperation between the National Bank of Georgia and the Bank for International Settlements (BIS) continued, in whose investment program the National Bank of Georgia joined the BIS Investment Pool (BISIP) at the end of 2014. The program involves the management of funds of various central banks and international financial institutions united in one portfolio. The BISIP program also includes assistance and experience sharing in the field of reserve management.



# FINANCIAL STABILITY POLICY

03

Promoting financial stability as a precondition for sustainable economic growth is one of the fundamental goals of the National Bank of Georgia. As defined by the Organic Law on the National Bank of Georgia, the NBG is mandated to maintain financial stability in the country as long as that objective does not come into conflict with its main mandate of maintaining price stability. Financial stability is the state under which the financial system can provide crucial services to market players in both good and stressed times.

The NBG conducts macroprudential policy and financial sector supervision with the goal of maintaining financial stability. The NBG identifies, evaluates and monitors systemic risks and implements corresponding policies to prevent or mitigate those risks, thereby enhancing the resilience of the financial system. The Financial Stability Committee (FSC) of the NBG, which is chaired by the Governor, coordinates macroprudential policy within the NBG's mandate. The FSC identifies and analyses systemic risks and ways to mitigate them, makes recommendations on the use of macroprudential measures and coordinates actions that promote financial stability.

The countercyclical capital buffer is used as one of the main macroprudential policy instruments. Its goal is to limit excessive credit growth that leads to the build-up of systemic risks. The countercyclicality of the buffer serves the main purpose of macroprudential policy, which is to reduce systemic risks. In the event of negative shocks, the countercyclical capital buffer should help the financial system avoid a significant deterioration of lending to the economy and thus help prevent a further worsening of conditions in the financial sector and the economy as a whole. In March 2023, under updated framework for setting the countercyclical capital buffer<sup>33</sup>, the Financial Stability Committee decided to set the cycle-neutral (base)

rate of the countercyclical capital buffer at 1%, which implies that the buffer rate would be 1 percent in normal periods. Initially, banks were given a 12-month period to meet this requirement, however, by the decision of the Financial Stability Committee, against the background of globally tightened financial stance, the countercyclical capital buffer will be accumulated gradually, and banks will be required to accumulate a cycle-neutral countercyclical capital buffer according to the following schedule: 0.25 percent by March 15, 2024, 0.5 percent by March 15, 2025, 0.75 percent by March 15, 2026, 1 percent by March 15, 2027. Cyclical demand against the backdrop of excessive growth of loans can be determined in accordance with the increase of cyclical risks. The analysis of the latter depends on factors such as the Credit-to-GDP ratio and its deviation from its long-term trend, lending conditions, various indicators of the cyclical position of the financial sector, the characteristics of the domestic and foreign macro-financial environment, etc.

In addition to the countercyclical capital buffer, the National Bank of Georgia uses other capital buffers consistent with Basel III standards. Macroprudential instruments also include the payment-to-income and loan-to-value ratios, sectoral risk weights and other instruments.

The NBG actively continues to work on reducing the structural risks caused by the high level of financial dollarization. Against the background of measures taken by the NBG, dollarization has significantly decreased, although dollarization and related risks remain one of the main challenges for the financial sector. Foreign currency-denominated, mostly variable-rate loans, are accompanied by interest and exchange rate risks. The latter is particularly noteworthy given the high share of unhedged foreign currency borrowers and the increased volatility of regional currencies'

33. [nbg.gov.ge/fm/ფინანსური\\_სტაბილურობა/კომიტეტის\\_გადაწყვეტილებები/eng/fsc-pressrelease-q4-eng.pdf?v=3hj3u](https://nbg.gov.ge/fm/ფინანსური_სტაბილურობა/კომიტეტის_გადაწყვეტილებები/eng/fsc-pressrelease-q4-eng.pdf?v=3hj3u)

exchange rates. In order to mitigate the risks caused by dollarization, the NBG imposed additional requirements on regulated financial institutions. From January 1, 2024, the limit on unhedged foreign currency loans has increased to 300,000 GEL. In order for the reduction of structural risks to continue irreversibly in the future, NBG, in agreement with the banks, will gradually increase the limit, considering the current macroeconomic environment and risks.

By the decision of the NBG, along with easing the monetary policy, the conditions for issuing consumer loans were also eased. Taking into account that the growth rate of unsecured consumer loans in 2023 has decreased compared to 2022, and credit activity remains at a sustainable level, by the decision of the Financial Stability Committee, from November 1, 2023, the maximum term limit for this type of loans will increase from 3 years to 4 years again.

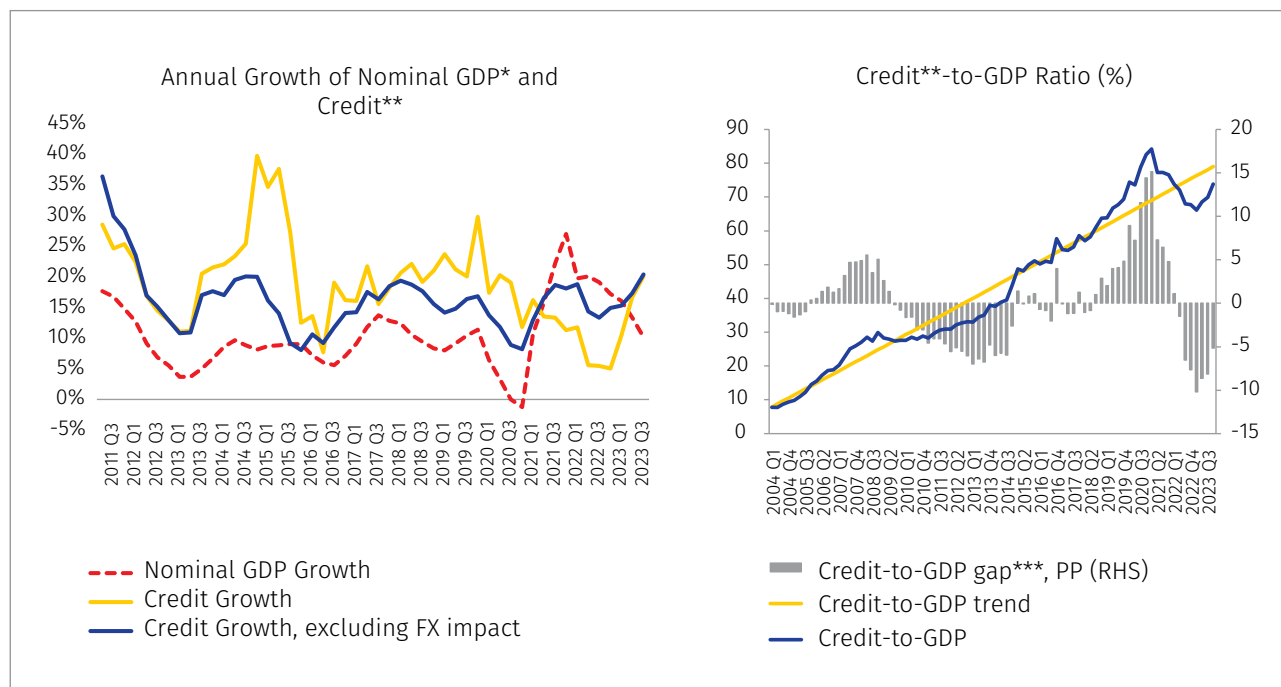
In recent years, the real estate market has seen an upward trend in prices, which was due to increased demand on the one hand, and increased construction costs on the other hand. After the start of hostilities by Russia in Ukraine, as a result of increased migration to the country, the demand for real estate increased, which was especially reflected in the increase in the rent price, although this effect weakened from the second half of 2023. As of April 2023, the price of rent in the real estate market exceeded its long-term trend by about 30%, which is why the NBG recommended to

financial institutions to consider this dynamic when assessing the stability of income from rent.

In May 2023, in order to promote financial stability, the NBG established the Minimum Requirement for Own Funds and Eligible Liabilities (MREL) for systemic banks. The recommendation to establish the said regulation was issued in 2021 within the framework of the joint financial sector assessment program conducted by the International Monetary Fund and the World Bank in Georgia, and it is based on the common practice envisaged by the framework of the European Bank Recovery and Resolution Directive (BRRD). The purpose of the MREL requirement is to create such a structure of the balance sheet in advance by the banks, which will contribute to the stability of the bank through recapitalization in a stressed situation.

The Georgian financial system maintains stability and continues smooth lending to the economy. As of 2023, banks have sound capital and liquidity ratios. Compared to last year, the quality of assets has also improved. In December 2023, the annual credit growth, excluding the exchange rate effect, amounted to 17.2%, which is largely due to the growth of business loans. According to the data of the fourth quarter of 2023, the credit-to-GDP ratio is gradually approaching the long-term trend. Compared to the beginning of last year, the negative gap in the credit-to-GDP ratio has been significantly reduced, reflecting the normalization of high economic growth and sustained credit activity.

Diagram N 3.1 Comparison of Loan and Nominal GDP growth rates



\*Loans include the loans issued by banks and microfinance institutions, as well as bonds issued locally by companies.

\*\* Gap of loans to GDP ratio is the difference between the ratio of loans to GDP to its long-term trend. An HP filter is used to evaluate the trend according to the Basel recommendation.

Source: National Bank of Georgia, GeoStat

### 3.1. DEVELOPMENT OF FINANCIAL STABILITY FRAMEWORK



The development of the financial stability framework is part of the NBG’s mandate to provide financial stability, which is one of the key factors determining a country’s economic development. The importance of financial stability and macroprudential policy has increased all over the world in recent years. In 2023, increased financial risks amid heightened global inflation and tighter financial conditions have reaffirmed the importance of financial stability. A sound and efficient framework for financial stability will ensure a smooth supply of financial resources, even during periods of economic downturn, and will make a significant contribution to the rapid recovery of the economy. Regular comprehensive and in-depth

analysis of financial stability are required according to best international practice. Financial stability analysis does not only encompass an evaluation of risks in the banking system, but also focuses on external factors, which have been a source of significant risk in recent years. Financial stability also assesses the domestic macro-financial environment, including households, companies, and non-banking institutions.

The NBG continues to develop a financial stability policy framework in accordance with best international practice of other central banks. As this requires developing adequate analytical capacity, the first step in this direction was focused on developing complex, Georgia-specific financial stability indicators. These indicators are used to make cyclical macroprudential policy decisions. Next, the NBG published the macroprudential policy strategy<sup>34</sup>. This strategy reflects the basic principles of the NBG’s macroprudential policy

34. visit: <https://www.nbg.gov.ge/index.php?m=738>

and aims to improve the decision-making process, communication and accountability to the public. In addition, the National Bank of Georgia is permanently working on the development of analytical instruments. They are based on international experience as well as country-specific characteristics. A research paper prepared by the Financial Stability Department in 2020<sup>35</sup> is important in this regard, as it offers analytical tools to ensure timely detection of systemic risks and thus establish a credible macroprudential policy guide.

Macro-financial modeling is another important part of the financial stability analysis framework. The NBG is working on the development of a macro-financial model that aims to assess the risks to financial and macroeconomic stability; constructing and analyzing macro-financial scenarios; and conducting macroeconomic stress tests. These are the foundation stones of appropriate macroprudential policy design. The development of the financial system and its accompanying challenges are expanding the scope of application of the macro-financial model and creating growing demands on it. Thus, the development and advancement of the macro-financial model is an ongoing process, in which cooperation with partner international institutions is crucial.

Increasing transparency and improving communications is one of the most important aspects of the financial stability framework. The NBG is constantly updating the financial stability section of its website in order to increase public awareness about financial stability policy. The website outlines the core tasks of the Financial Stability Committee (FSC) and describes the available macroprudential policy tools; it also provides a calendar of committee meetings, reports on committee statements and decisions, issues related to IFRS 9<sup>36</sup> and information regarding the sustainable finance framework.

The NBG supports the efficient implementation of new financial accounting standards (IFRS 9) by financial institutions. The NBG regularly publishes macroeconomic and financial forecasts and risk scenarios along with quantitative assessments<sup>37</sup> of macroeconomic trends to aid the transparent, consistent and efficient implementation of IFRS 9, and ensure comparability across the reports. The estimates provided within these scenarios can be used for calculating expected credit losses. The macroeconomic forecast scenarios for IFRS 9 are based on the macro-financial model and incorporate additional analysis and expert judgment. The scenarios provided are countercyclical by nature, which helps mitigate the potential impact of financial cycles. Given the high uncertainty caused by Russia's invasion of Ukraine in 2023, the NBG released two updates to the forecast scenarios, thus allowing financial companies to reflect macroeconomic forecast information in their loan loss reserve estimates in a timely manner.

A sustainable financial system is essential for financial stability. This revolves around the management of social and environmental risks and is one of the main factors contributing to sustainable development. The NBG became a member of the Sustainable Banking and Finance Network (SBFN) in September 2017. Since then, it has been intensively working on developing a framework for sustainable finance.

In 2023, the NBG remained committed to implementing actions under Sustainable Finance Roadmap<sup>38</sup>. The Sustainable Finance Roadmap (hereinafter, the Roadmap) for Georgia includes all the possible measures planned by the NBG until the end of 2023. In 2024, the NBG will develop a new Roadmap, which will combine the action plan and measures to be implemented for the next few years. The main objective of the Roadmap is to create a reliable, predictable

35. "Evaluation of the credit gap as a guideline for macroprudential policy in Georgia" refer to: [bit.ly/36me1EE](https://bit.ly/36me1EE)

36. IFRS (IFRS 9).

37. visit: <https://www.nbg.gov.ge/index.php?m=694>

38. Refer to: <https://nbg.gov.ge/en/page/sustainable-finance-roadmap>

and stable regulatory framework that will prepare the market for the transition to sustainable finance.

In accordance with the requirement established by the Corporate Governance Code (CG Code), in 2023, banks disclosed ESG information using the NBG template for the third time. Templates completed by financial institutions in 2021-2023 are published on the website<sup>39</sup> of the NBG. Banks will make similar reports annually, which in turn will help provide information on ESG issues to investors and other stakeholders.

In 2023, the NBG published the third report on sustainable finance. This is annual edition has been published on the website<sup>40</sup> of the NBG since 2021. It presents an overview of current trends, policies and plans regarding sustainable finance in Georgia. The steps taken by the NBG are analyzed, the current and planned projects in the near future are described, and the information submitted by commercial banks in the ESG forms is summarized. The report also presents trends in the issuance of green and sustainable bonds in Georgia and the related dynamics of the capital market in general.

Development of Sustainable Finance Taxonomy<sup>41</sup> is one of the crucial phases in the development of sustainable finance, a step specified in the Sustainable Finance Roadmap. The lack of common definitions and classification systems in this regard is recognized as one of the major challenges in the development of sustainable finance. To address this challenge, the NBG approved a sustainable finance taxonomy<sup>42</sup> and the regulation<sup>43</sup> on loan classification and reporting according to the taxonomy (hereinafter, the Taxonomy Regulation) in 2022.

The Taxonomy Regulation formally defines green, social and sustainable loans and imposes reporting requirements on commercial banks for loans that comply with the taxonomy. The regulation states that, from 2023, a commercial bank can call a loan green, social and/or sustainable only if it meets the technical criteria defined in the Sustainable Finance Taxonomy. Also, banks are obliged to make monthly statements of green loans in the monthly reporting form determined by the taxonomy regulation. Also, disclosure of information on green/social/sustainable loans in the ESG reporting and disclosure form<sup>44</sup> in the Pillar 3 Annual Report must be done in accordance with the Taxonomy Regulation. This is expected to ensure the availability of comparable and consistent data on green loans in Georgia and to facilitate the development of the sustainable finance market.

In 2023, the NBG has developed a methodology and tool for calculating and reporting financed emissions for the financial sector of Georgia. This project was implemented in cooperation with the German Sparkassenstiftung for International Cooperation. A description of the methodology and detailed results are presented in the report, which is available on the website<sup>45</sup> of the NBG. The methodology is used for different classes of assets, including any important asset for banks, such as the portfolio of business loans. The capital provided to the companies in the form of a loan from the bank is used to finance both business processes and greenhouse gas emissions generated by the company. The Financed Emissions Tool allows a financial institution to analyze its loan portfolio, determine the share of the financed emissions included in it, and identify risks and opportunities related to climate change, which will help it to improve

39. Refer to: <https://nbg.gov.ge/financial-stability/esg-reporting-and-disclosure>

40. Refer to: <https://nbg.gov.ge/en/page/sustainable-finance-in-georgia>

41. The Sustainable Finance Taxonomy is a document that identifies and classifies activities and economic activities that have positive environmental and/or social impact.

42. Refer to: <https://nbg.gov.ge/en/page/sustainable-finance-taxonomy>

43. Refer to: <https://nbg.gov.ge/legal-acts/acts>

44. Refer to: <https://nbg.gov.ge/financial-stability/esg-reporting-and-disclosure>

45. See: <https://nbg.gov.ge/en/page/financed-emissions>

business processes and make strategic decisions in environmental management.

In cooperation with the IFC, the NBG completed work on the development of the ESG Scorecard<sup>46</sup> for commercial banks. ESG Scorecard assesses ESG practices and approaches of commercial banks using the ESG risk scorecard methodology and is based on various ESG indicators. The purpose of this evaluation system is to develop a comparable, consistent and transparent system for evaluating the implementation of ESG principles in banks, to identify underlying weaknesses and challenges, and to develop response policies to address them. The ESG Scorecard will be used as a progress measurement tool to assess the steps taken by financial institutions towards sustainable finance.

In 2023, the NBG published a research paper entitled Biodiversity-related Financial Risks – why it matters and how can we measure them? Case study of Georgia.<sup>47</sup> The research paper aims to analyze the links between biodiversity loss and financial stability. The paper discusses the financial risks related to the loss of biodiversity and presents a quantitative assessment of the dependence and impact of the financial system on ecosystem services on the example of Georgia.

Within the framework of sustainable finance in 2023, the National Bank of Georgia developed ESG Guidelines<sup>48</sup>. The ESG Guidelines for Commercial Banks sets out the principles and standards that banks should follow in order to: (i) properly assess and manage ESG risks, (ii) promote the development of a responsible banking sector by developing sustainable financial products, and (iii) ensure compliance with ESG-related regulatory policies. By recognizing and analyzing these risks and opportunities, Georgia's financial institutions can contribute to shaping the green and inclusive growth agenda and also ensure their own long-term financial stability and sustainability. The ESG Guidelines are

based on the best international standards and also incorporate the practices currently used by local financial institutions.

Early in 2023, the conference *Green Finance for Sustainable Economy* was organized by the National Bank Georgia, the European Bank for Reconstruction and Development (EBRD) and the International Chamber of Commerce (ICC). The event aimed to raise awareness about the importance of green financing in the process of sustainable development of the country and transition to a low-emission economy. Also, discussion was held on the sustainable finance taxonomy developed by the NBG and the expected effects of the relevant regulation. The participants of the event spoke extensively about the main risks, challenges and opportunities that may arise in the private sector and the banking system in the process of climate change mitigation and transition to a green economy.

The NBG with the financial support of the European Investment Bank (EIB) and the involvement of international experts continued to develop the climate scenario analysis and stress-testing framework. The NBG relies on NGFS climate scenarios to develop climate scenarios for Georgia. The framework also includes the analysis of the vulnerabilities of commercial banks under different scenarios. The results of the bank vulnerability analysis will be used in the climate stress test, planned for 2024.

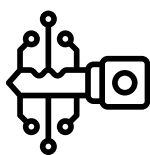
As part of the implementation of the Sustainable Finance Roadmap and corresponding Action Plan, the NBG is working on the regulation of Green/Social/Sustainable/Sustainability-related (GSS+) bonds. The framework and related regulation define the conditions for granting, maintaining and canceling the status of GSS+ bonds, as well as the reporting requirements. It is planned to adopt the framework in 2024.

46. See: <https://nbg.gov.ge/en/page/sustainable-finance-in-georgia>

47. See: <https://nbg.gov.ge/en/media/news/a-new-paper-on-biodiversity-related-financial-risks>

48. See: <https://nbg.gov.ge/en/page/esg-guidelines>

## 3.2. RECOVERY AND RESOLUTION FRAMEWORK



In 2021, the National Bank of Georgia started working on the implementation of the Commercial Bank Recovery and Resolution Framework (hereinafter referred to as the Resolution Framework).

Intensive work continued during 2023, as the NBG closely cooperated with the International Monetary Fund and the World Bank. The World Bank team, as part of the mission, conducted the second part of the simulation, testing implementation of the resolution. The World Bank team, conducted the simulation exercise with the involvement of the NBG, the Deposit Insurance Agency and the Ministry of Finance. The simulation tested preparedness for the financial crisis and gave practical recommendations.

Each member of the banking sector generated a recovery plan in 2023. The plans describe measures to be implemented by the commercial banks to improve the financial state, restore and maintain critical functions in the event of significant financial distress and/or disruption of critical functions. The National Bank of Georgia examined each bank's recovery plan and provided appropriate feedback in consideration of the regulatory procedure and international good practices.

An important element of a commercial bank's recovery plan is the self-assessment of critical functions and, in case of these are terminated, the assessment of timely replaceability by other market players, considering the impact on counterparties and the real economy.

The following functions are deemed critical for the system:

- Taking deposits;
- Lending;
- Payment services, cash services, clearing, settlement services, savings services;

- Security market services;
- Wholesale finance.

The requirements for the above plan (recovery plan) are regulated by the relevant procedure of the resolution framework. The document focuses on: marking indicators for recovery purposes and calibrating their boundaries, determining remedial measures, testing the extent of financial damage and effectiveness of remedial measure(s) by using stress scenarios that are relevant for the bank, and doing preparatory work. The document also focuses on the management of governance issues, with the aim of early detection of deteriorating financial condition and further organizational management.

*Mandatory categories of recovery plan indicators are:*

- capital;
- liquidity;
- profitability;
- asset quality.

The commercial banks take care of updating recovery plans and the NBG, on its part, evaluates them on an annual basis. The assessment document is integrated into the overall risk management framework of the banks.

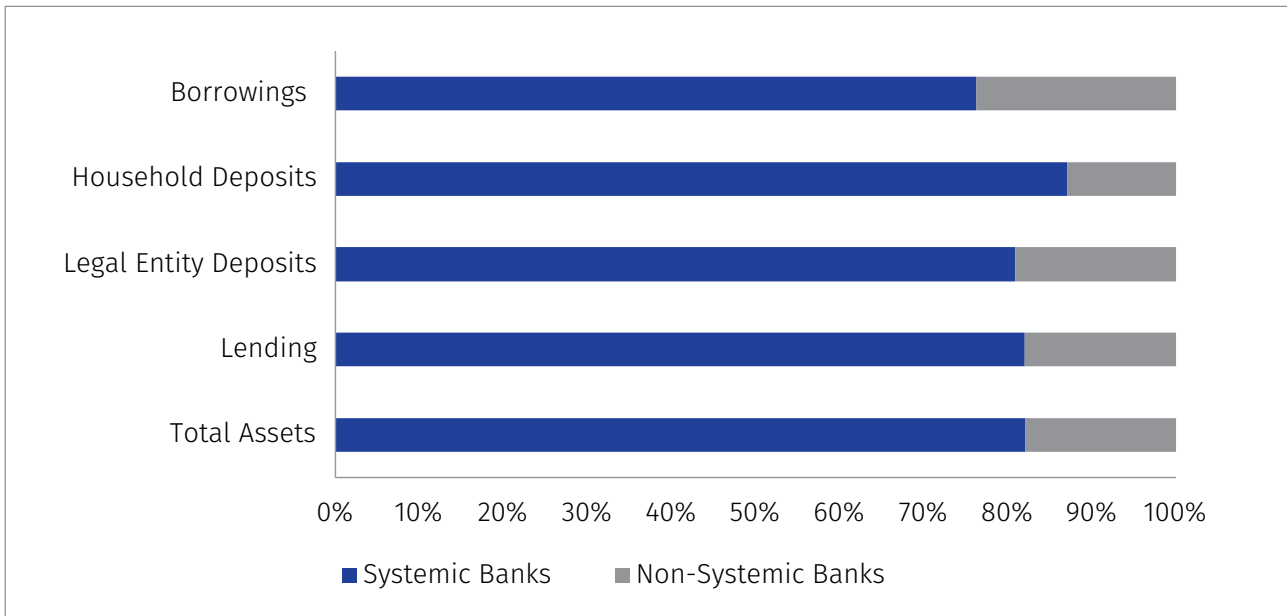
The resolution mechanism, presented with appropriate resolution tools, is an opportunity to recover a bank in a severe financial crisis. It is used when remedial measures are unlikely to be implemented within a reasonable time, and, to avoid a significant negative impact on the stability of the financial sector, it is advisable to maintain the functioning (critical functions) of the financial institution while restricting the use of taxpayers' funds.

The resolution authority of the National Bank of Georgia includes the individual or combined use of the following resolution instruments without the consent and prior notice of the shareholders and/or creditors:

- Merger of a commercial bank;
- The sale of shares, assets and/or liabilities of a commercial bank;

- The transfer of shares, assets and/or liabilities of a commercial bank to a temporary bank;
- Recapitalization of a commercial bank by issuing new shares;
- Recapitalization of a commercial bank by a write-off of liabilities, or bail-in

Diagram N 3.2 Concentration of System-maker banks in the banking market (As of December 31, 2023)



Source: NBG

The peculiarities of the banking sector and the high concentration of systemically important (system-maker) banks indicate the criticality of their economic functions and the need for resolution plans. The NBG revised and updated resolution plans for systemically important banks. Upon the IMF recommendation, a resolution plan was developed also for a relatively large, non-system bank. Their key elements are assessing resolvability and determining the preferred resolution strategy, that would include the following aspects: plan triggers, qualitative and quantitative analyses of instruments, key phases of the resolution, core processes and others. The international practice suggests that the expansion of the resolvability and operational organization of the instruments is under development and is still a topical issue, even in advanced countries. Important work was done to operationalize the resolution framework: upon the IMF recommendations, the NBG started work on resolution instruments, the so-called playbooks. The NBG will be working on these issues next year as well.

The meeting of the resolution committee was held in 2023 to discuss current issues. No need for resolution in the banking sector or its early warning signs were identified in the course of 2023, and no grounds for implementing recovery measures were observed.

In 2021, within the framework of the joint Financial Sector Assessment Program (FSAP) conducted by the International Monetary Fund and the World Bank in Georgia, recommendations were made that the National Bank of Georgia should establish the Minimum Requirement for Own Funds and Eligible Liabilities (MREL) for by the existing resolution framework for commercial banks with systemic importance. It is a percentage derived from the ratio of eligible liabilities and own funds to regulatory capital and total liabilities.

In addition, from December 2023, it became mandatory for commercial banks to consider the contractual condition of using the resolution instruments of writing off the bank's liabilities or bailing in for the

purpose of recapitalization in the agreements of such equity instruments, which are fully or partially regulated by foreign legislation. A similar requirement in the agreements containing such obligations, which are subject to the *Regulation on writing off or bailing-in the liabilities of a commercial bank in resolution for the purpose of recapitalization*, approved by the decree of the Governor of the National Bank of Georgia No. 241/04 dated December 29, 2020, will be applied to commercial banks from April 1, 2024. The consideration of the condition defined by the said requirement in the contract does not affect the creditor hierarchy provided by the legislation.

The regulation is based on the common practice provided by the framework of the European Bank Recovery and Resolution Directive (BRRD). The purpose of the requirement is to create a balance sheet structure in advance by systemic banks for crisis situations, which will allow the NBG, within its mandate, to effectively recapitalize the bank in resolution mode by writing off liabilities or bailing-in.

Minimum Requirement of Own Funds and Eligible Liabilities (MREL) rate for systemic commercial banks is determined in accordance with the following amounts and terms:

- 10 % from January 1, 2024;
- 15% from December 31, 2025;
- 20% From December 31, 2027;

Starting from 2024, systemic banks are obliged to submit monthly MREL reports to the National Bank of Georgia.

Also, in December 2023, the Parliament of Georgia approved legislative amendments related to the resolution fund, according to which commercial banks were determined to make preliminary contributions to the resolution fund (ex-ante fund) in order to reach the target set by law:

- Target benchmark of the fund: 3% of insured deposits;

- Contributions: banks should start making contributions from 2025;
- The period required to reach the target: 8 years (it can be changed if the amount in the fund is used or the deposit insurance limit is increased);
- Methodology of contributions: in proportion to the share of assets of commercial banks in the system, considering the individual risk profile.

The ex-ante fund is administered by the National Bank of Georgia, which, according to the law, has the right to transfer the fund to the Deposit Insurance Agency for administration. In the resolution fund, in addition to advance contributions by commercial banks, funds necessary accumulating of financial funds allocated within the framework of temporary state financing (the so-called ex-post fund) and utilized in a targeted way. After the end of the resolution regime and in case of financial support of the process by the Ministry of Finance, the state funds utilized through the resolution fund will be reimbursed by the operating commercial banks, under the established conditions and proportionality as determined by the National Bank of Georgia.

### 3.3. INTERAGENCY FINANCIAL STABILITY COMMITTEE



The Interagency Financial Stability Committee - a new cooperation platform was set up in 2020, within the framework of the powers granted by the legislation of Georgia and in compliance with the principle of independence, missioned to promote the stable functioning of the financial system, to ensure the regular exchange of information, the development of financial crisis management mechanisms and effective coordination. The committee is represented by the Minister of Finance, the NBG Governor, the head of the Deposit Insurance Agency and the head of the State Insurance Supervision Service. The interagency committee is chaired by the Minister of Finance of Georgia, and the NBG performs secretarial functions.

The committee holds a meeting at least once a year or at the request of the NBG. The core task of the committee is to develop mechanisms for managing crisis situations and financial crises to promote the stable functioning of the financial system.

In 2023, the annual meeting of the Interagency Financial Stability Committee was held. The committee was chaired by the Minister of Finance and the leaders of the NBG, the Deposit Insurance Agency and the State Insurance Supervision Service participated. The discussion at the session concerned the key elements and aspects of the resolution framework, the interaction of the National Bank of Georgia with the banking sector and the need to invigorate cooperation between agencies. In addition, the committee members shared information on the status of the recommendations issued by the FSAP and the IMF technical mission and emphasized that all the main recommendations have already been implemented, and the remaining part is actively being worked on. It was explained that systemically important commercial banks have been set the minimum requirement for own funds and eligible liabilities (MREL).

### 3.4. LIQUIDATION OF FINANCIAL INSTITUTIONS



There were 17 commercial banks operating in Georgia as of December 31, 2023, along with 34 microfinance institutions, 1 credit union and 31 providers of payment services.

There were no cases of bank liquidation initiated in 2023 and the last liquidation in the banking sector was completed in 2019.

During and after the liquidation of the supervised entities, the National Bank of Georgia registers the

funds unclaimed from the creditors in a special account, administers them and, upon disclosure of the holder, ensures the return of these funds to them. The National Bank of Georgia also manages the assets discovered after the liquidation of a commercial bank (there were such occurrences in the early years after the liquidation was completed). The proceeds are normally distributed among the remaining creditors of the liquidated bank, in the appropriate order<sup>49</sup>. In 2023, two newly discovered assets of liquidated commercial banks were being disposed of. In one of these, the funds partially recovered and distributed to creditors, had been paid in previous years. Disposal of such assets will continue into 2024. In carrying out its liquidation functions, the National Bank of Georgia is guided by the applicable laws and decrees in relation to the following supervisory entities. In the implementation of liquidation functions in relation to the below-mentioned supervisory entities, the National Bank of Georgia is guided by relevant laws and orders.

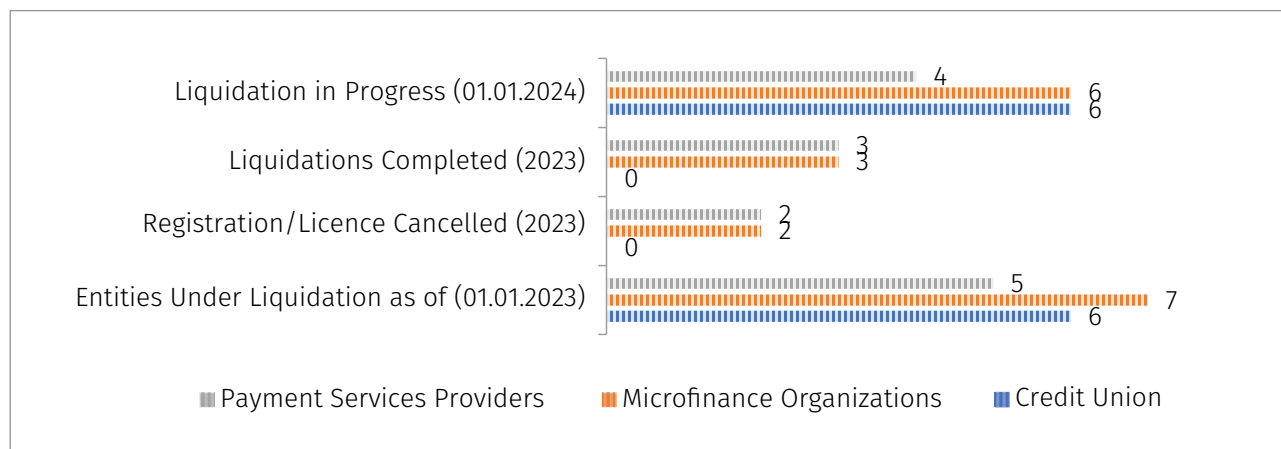
In addition, according to Article 48, Paragraph 16 of the Organic Law of Georgia On the National Bank of Georgia, the supervisory authority of the National Bank of Georgia was expanded - when the entity subject to supervision does not have the funds to cover liquidation costs, the National Bank of Georgia became authorized to allocate funds to cover the costs to smoothly run the liquidation process in the entity subject to supervision.

Based on this, in 2023, appropriate changes were made in the by-laws. This process will continue actively in 2024 as well.

In addition to the existing legal acts, the National Bank of Georgia will develop procedures and other technical documents of internal control, which helps to improve governance issues during liquidation and makes the processes more organized and standardized.

49. Recovery of the asset, which was the asset of the commercial bank before the issuance of the individual administrative-legal act on the completion of the liquidation, it will automatically be considered as the asset of the liquidated commercial bank and the National Bank of Georgia acquires the right to dispose of it (the Law of Georgia on the Activities of Commercial Banks Article 3712 paragraph 15).

Diagram N 3.3 Progress of Liquidation of Financial Institutions in 2023



Source: NBG

With the co-authorship of the National Bank Georgia, a package of legislative changes was developed in 2020-2023, which will be submitted to the Parliament for approval. Legislative changes are planned in the Organic Law of Georgia "On the National Bank of Georgia", "On Microfinance Organizations", "On the Payment System and Payment Services" and in several other legal acts. The task of legislative changes is to expand the authority of the NBG for both liquidation and insolvency/bankruptcy of microfinance organizations and payment service providers, as well as the introduction and operation of the regime of temporary administration of microfinance organizations. The mentioned changes give the NBG the sole authority

to declare the microfinance organization and payment service provider insolvent and/or bankrupt, which will contribute to the timely and effective management of the process of meeting the demands of the creditors of the microfinance organizations and payment service providers. The NBG will appoint the liquidator of the said supervisory entities, as well as the temporary administrator of the microfinance organization, and they will be accountable to the NBG. As the bill is passed, the supervisory framework of the NBG will be strengthened in regulation and supervision of microfinance organizations and payment service providers.



# BANKING SUPERVISION

04

## 4.1 DEVELOPMENT OF SUPERVISORY FRAMEWORK



In 2023, the Parliament of Georgia adopted the Law of Georgia "On the Activities of Microbanks" and related bills to create a medium-sized, stable business model and a new financial institution with a high reputation in the financial sector, to promote lending to entrepreneurial and agricultural activities, to increase competition and reduce interest margins on credit products. As a result, a microbank was added to the list of supervised entities of the National Bank of Georgia.

Early in the year, the National Bank of Georgia worked particularly actively on the development of by-laws

and their approval within the relevant terms, actively cooperating with the private and public sector and transparently managing the work process, including through the format of public consultations. As a result, a regulatory framework for microbanks was developed, within which important issues, including licensing requirements, conditions for the suitability of administrators and the acquisition of a significant share, including eligibility, fit and proper criteria, were based on the existing regulation for commercial banks and accordingly replicated European and international standards.

Entities seeking a microbank license have already applied to the NBG with license applications, and the NBG is actively working on relevant matters stipulated by the legislation.

### BOX 3 THE PURPOSE OF CREATING A NEW FINANCIAL INSTITUTION, THE MICROBANK, AND ITS ACTIVITIES:

The non-banking sector in Georgia is diverse, encompassing both small-sized, single-product-oriented organizations and large organizations with a broad profile. Their financing structures also vary. Notably, large organizations that have access to resources from foreign financial institutions act as financiers for entrepreneurs and agricultural sectors, aligning with classic microfinance activities. Given this context, it is crucial that different business models, despite having the same status, be subject to distinct regulatory and supervisory regimes.

This situation has highlighted the need to improve the supervisory framework for non-banking institutions. In response, the International Monetary Fund developed relevant [recommendations](#). Consequently, the National Bank of Georgia decided to establish a supervisory framework for a new financial institution, the microbank.

In form of microbank, new financial institution format was created, which is designed to operate in sectors where commercial banks have relatively low interest due to high operating costs. The mandate of the microbank, as defined by law, is primarily to lend to the entrepreneurial and agricultural sectors, thereby increasing financial inclusion, especially in the regions.

Compared to a microfinance organization, a microbank will significantly reduce costs and increase access to resources in both local (including monetary instruments) and international markets. This, in turn, will contribute to cheaper credit products and, consequently, increased competition in the market.

The business model of the microbank is based on lending to individuals who receive income from entrepreneurial activities, including agricultural ventures. Specifically, at least 70 percent of the microbank's credit

portfolio must consist of business loans and/or loans where the repayment source is income from business activities.

According to the Law of Georgia "On the Activities of Microbanks", banking activities allowed for a microbank are:

- Issuance of loans, guarantees, letters of credit and leasing, factoring operations, within the established limit;
- Attracting interest-bearing and interest-free demand and term deposits within the limit established by the Law of Georgia on the Deposit Insurance System, as well as above the limit, servicing current accounts in compliance with the liquidity requirements determined by the National Bank of Georgia.
- Opening and servicing of correspondent accounts;
- Implementation of cash and non-cash settlement operations and provision of cash-collection services;
- Issuing payment cards and organizing their circulation;
- Providing payment services, operating the payment system, performing the functions of a settlement agent;
- Providing interest-free banking services;
- Placement of derivatives, buying and selling of securities with own funds, except for the case where the said activity requires a brokerage license;
- Buying and selling foreign currency with own and clients' funds;
- Storage of valuables;
- Leasing of property only for the implementation of activities provided within the scope of permitted activities;
- Providing other services related to each permitted activity;
- In accordance with the Organic Law of Georgia "On the National Bank of Georgia," providing virtual asset services for the benefit of another person, including the mutual exchange of a convertible virtual asset (including through a self-service kiosk) in national or foreign currency for another virtual asset or financial instrument, transfer and/or storage of a convertible virtual asset or the tool necessary for its use, which allows control of the virtual asset, and the support activities necessary for the provision of this service.
- Raising returnable funds, including from individuals (including individual entrepreneurs), in accordance with the law.

Microbanks may only lend in the national currency.

If the total assets of the microbank exceed 2 percent of the total assets of the banking sector, the National Bank of Georgia is authorized to require the microbank to submit a plan to return to this limit or to define additional and/or different supervisory requirements.

Within the framework of the Association Agreement between Georgia and the European Union, the European Atomic Energy Community, and their member states, and in order to align Georgian law with European Union law, particularly Directive 2002/87/EC of the European Parliament and the Council of December 16, 2002, the National Bank of Georgia, in cooperation with the Insurance State Supervision Service of Georgia (a legal entity of public law), prepared the draft Law of Georgia "On Supplementary Supervision of Regulated Entities in Financial Conglomerate" along with related draft laws. These drafts were shared and discussed by the

National Bank with the Banking Association and the banking sector. The legislative package was adopted by the Parliament of Georgia in three readings, granting the National Bank the authority to exercise additional supervision over regulated entities in the financial conglomerate.

The National Bank of Georgia, in cooperation with the relevant counterpart agency, continues to determine the need for the development of by-laws and the activities related to their development within the relevant period.

#### BOX 4. SUPPLEMENTARY SUPERVISION OF REGULATED ENTITIES IN THE FINANCIAL CONGLOMERATE

In accordance with the Law of Georgia "On Supplementary Supervision of Regulated Enterprises in the Financial Conglomerate," the National Bank of Georgia and the Insurance State Supervision Service of Georgia have been granted new powers. Specifically, they have the right to exercise additional supervision over regulated entities included in the financial conglomerate, taking into account their respective mandates. This authority will be exercised in parallel with sectoral supervision.

##### What is a financial conglomerate?

- **A group or subgroup is headed by a regulated entity and all of the following conditions are met:**
  - The enterprise at the head of the group/subgroup is the parent enterprise of the enterprise in the financial sector or an enterprise connected with any enterprise in the financial sector by joint management, or when more than half of the members of the governing bodies of the enterprises are the same persons during the financial year until the date of preparation of consolidated statements.
  - At least one enterprise in the group/subgroup is a commercial bank or an enterprise in the brokerage sector, and at least one is an enterprise in the insurance sector.
  - The consolidated or aggregated activities of group/subgroup enterprises are considered significant in case of enterprises in the insurance, as well as in banking or brokerage sectors.
- **A group or subgroup is headed by an unregulated entity and all of the following conditions are met:**
  - The main activity of the group/subgroup is in the financial sector.
  - At least one enterprise in the group/subgroup is a commercial bank or an enterprise in the brokerage sector, and at least one is an enterprise in the insurance sector.
  - The consolidated or aggregated activities of group/subgroup enterprises are considered significant in case of entities in the insurance, as well as in banking or brokerage sectors.

##### Criteria for recognizing a group/subgroup as a financial conglomerate

Activity in the financial sector is considered the main activity of the group/subgroup if the sum of the total assets of the enterprises included in the financial sector of the group exceeds 40% of the total assets of the group.

A consolidated or aggregated activity carried out by each sector within the financial sector is considered significant if:

- The sum of the assets of the enterprises included in the insurance sector and the banking and brokerage sectors exceeds 10% of the total assets of the enterprises included in the total financial sectors of the group.
- The capital adequacy/solvency margin requirement of the enterprises included in the insurance sector and the banking and brokerage sectors exceeds 10% of the capital adequacy/solvency margin requirement of the enterprises included in the financial sectors of the group.

The activity of enterprises included in the financial sector is considered significant also in case if the total assets of the smallest financial sector of the group exceed the equivalent of 6 billion euros in GEL.

In order to implement additional supervision of the financial conglomerate effectively, a supervisory authority responsible for coordination and implementation of additional supervision (the coordinator) is determined from among the supervisory authorities. The joint decision of the supervisory authorities on the appointment of the coordinator should be published on the official websites of the supervisory authorities. Additionally:

- If there is a regulated enterprise at the head of the financial conglomerate, the supervisory body that issued a permit/license for the activity of the relevant enterprise or registered the said enterprise is appointed as the coordinator.
- If there is no regulated enterprise at the head of the financial conglomerate, the law determines the procedure for selecting the coordinator.

Regulated entities included in the financial conglomerate, independently of the sectoral supervision rules, are subject to supplementary supervision in terms of risk concentration, intragroup transactions, and capital adequacy/solvency margin. These enterprises are also obliged to have adequate risk management processes and an adequate internal control mechanism at the level of the financial conglomerate, including reasonable and effective administrative and reporting procedures. Supervisory authorities also assess potential/existing risks arising from unregulated entities within the financial conglomerate and their impact on the risk profile of the financial conglomerate.

It should be noted that at this stage, no group of entities in Georgia meets the criteria of a financial conglomerate.

In 2023, the National Bank of Georgia continued its established practice and issued a supervisory strategy [document](#) for 2023-2025. This document reflects the priorities of the supervisory strategy for 2023-2025, the activities planned for their implementation, and the summary report on the implementation of the strategy for 2020-2022.

Compared to previous years, the National Bank of Georgia (NBG) conducted the work on the supervisory strategy for 2023-2025 with even greater involvement of the private and civil sectors. Opinions and recommendations from interested parties were solicited through a publicly published questionnaire<sup>50</sup>, followed by the publication of the initial supervisory

50. The National Bank of Georgia publishes a questionnaire to ensure the involvement of the sector in the process of developing a new supervisory strategy document (nbg.gov.ge)

strategy document for consultation<sup>51</sup>. This inclusive approach resulted in the determination of supervisory priorities, which will be taken into account by the NBG in its activities during 2023-2025. The priorities of the 2023-2025 supervisory strategy include:

- Improvement of the financial sector risk management framework and proactive response to the outcomes.
- Promotion of competition in the financial sector.
- Promotion of financial innovation and development of supervisory technologies.
- Approximation to international standards.
- Strengthening the supervisory function of the NBG and increasing transparency.

According to observations of the National Bank of Georgia and feedback received from external parties, the strategy document contributes to the effective planning of the NBG's activities, clear formulation of future vision for employees, increased predictability for sector on forthcoming events and availability of information on supervisory priorities and plans for investors, international financial institutions, rating agencies, the citizens, and other interested parties. Practice has shown that the supervisory strategy has become a rather important reference document for representatives of the financial sector.

As in previous years, the supervisory strategy document shall be updated annually. Update shall include a report on the implementation of the action plan for achieving supervisory priorities and the activities defined within this plan. It also allows for possible changes to the deadlines provided for in the action plan, if necessary. Supervisory priorities will remain unchanged as part of the annual reviews.

In 2023, the NBG continued its practice of promoting transparency and public involvement by holding public consultations. Several drafts of changes and

regulations related to supervision were published on the NBG's website, allowing the general public to share comments and recommendations. In 2023, the NBG enhanced this practice, by formalizing the process and moving closer to best international practices. Specifically, the NBG approved the *"Guidelines for policy development and implementation on important issues subject to the regulation of the National Bank of Georgia,"* significant part of which is a process for public consultations/consultations with the sector. The NBG also developed and approved the *"Handbook for holding consultations with the sector and public consultations with interested parties,"* detailing the process and timelines for conducting consultations. This makes the process of consultations/public consultations even more transparent, especially for documents that lead to material changes in existing policy or have significant impact on the relevant sector and society.

Additionally, in 2023, the NBG actively continued to work on recommendations received from the International Monetary Fund and the World Bank as part of the Financial Sector Assessment Program (FSAP), for developing and improving the supervisory framework of the NBG, as well as worked for aligning it with European and best international standards.

## 4.2 CORPORATE GOVERNANCE AND GROUP STRUCTURE RISK



During 2023, the NBG actively monitored the implementation of the Corporate Governance Code in commercial banks, focusing on the functions and duties of the Supervisory Board, the number of independent members, and the composition of the board committees. The compliance of remuneration policies with the updated requirements of the Code was also assessed through consultations with commercial banks. One requirement of the Corporate Governance

51. The National Bank of Georgia publishes the initial draft of the Supervisory Strategy document for 2023-2025 years for public review (nbg.gov.ge)

Code is the evaluation of the Bank's Supervisory Board's activities, which includes self-evaluation and periodic evaluation by an external evaluator. The National Bank of Georgia also reviewed the assessments and the internal audit function to ensure its independence and proper functioning. These assessments is considered within the General Risk Assessment Program (GRAPE).

To improve gender diversity in the Supervisory Board and Directorate of Commercial Banks, the Corporate Governance Code of Commercial Banks was amended on August 24, 2022, increasing the demand for gender diversity. Banks were required to have a share of the opposite gender in the supervisory boards of at least 33% by June 1, 2023, and at least 40% by June 1, 2025. The verification/monitoring of banks' compliance with this obligation was ongoing in 2023. The demand for gender diversification first appeared in the Corporate Governance Code in 2018, requiring at least 20% of the Supervisory Board to be composed of representatives of different genders. As of December 2023, the share of female representatives in the boards exceeded the established requirement, reaching 35%.

In December 2023, to monitor and ensure the independence of the members of the Supervisory Board, the Corporate Governance Code defined the authority of the NBG to request or inspect the suitability of independent members at any time if

there is a reasonable suspicion of non-compliance. The National Bank of Georgia could request the bank to terminate Membership Status of Supervisory Board Independence, if non-compliance was established.

The assessment of corporate governance and group structure of commercial banks is part of the general risk assessment program. It includes assessing the ownership structure, risks related to investments and transactions within banking group members, and evaluating the risks of the banks' investments and investment activities. The NBG actively monitors developments in the parent countries of international banking groups in Georgia and evaluates significant shareholders.

In October 2023, the NBG made significant changes to the regulation on the management of conflict of interest to align with international standards and improve control and management standards by commercial banks. Banks were given six months to bring their policies/procedures into compliance with the requirements of the decree, and certain requirements became effective immediately after the decree came into effect (see box 5). Transactions with related parties and compliance with the regulation's requirements are part of the corporate governance and group structure risk assessment of commercial banks.

### BOX 5. UPDATED FRAMEWORK MANAGEMENT OF CONFLICT OF INTEREST

Work on improving management of conflict of interest standards in the National Bank of Georgia started in 2021 with the goal of introducing control and management standards by commercial banks to avoid conflicts of interest. The changes made in the regulation are based on international practices (IAS 24, London listing Rules) and aim to address deficiencies identified in the financial sector of Georgia and mitigate risks in this area.

The changes touched on various issues of the statute. Significant changes were made to the definition of a related party, including the requirement to be identified on the list of related persons and, in some cases, related persons should have been retained in the list even after leaving a bank for next 12 months. The 12-month retention principle in the list of related persons applies to persons who leave the Bank after the implementation of this decree. Additionally, ownership of a significant share of the bank was determined as a criterion for recognition as a related party.

General requirements related to collateral were also outlined in the regulation, defining a list of permissible collateral for creating a risk position with related parties and specifying the assessment/documentation of the compliance of the said collateral with the regulation's requirements. The changes also include an analysis of compliance with the arm's length principle, clarifications on prohibited transactions, and exceptions to the requirements set forth in the regulation.

During the work process, the NBG actively communicated with commercial banks regarding draft changes. Banks were informed about the changes at the beginning of 2022, and in June 2023, the draft changes to the conflict of interest management regulation were published for consultation. The changes entered into force on October 31, 2023. Due to the fact that the changes to be implemented by the banks and to be introduced in the internal policy are quite voluminous, according to the decree, commercial banks have been given a six-month period to bring the policies/procedures into compliance with the requirements of this decree. Commercial banks were instructed to comply with certain requirements from the moment the decree came into force.

In 2023, two digital banks, JSC Hash Bank and JSC Pave Bank Georgia, received banking licenses. JSC Hash Bank aims to provide banking services mainly through electronic channels, targeting both traditional and technology-driven markets transitioning to a digital strategy. JSC Pave Bank Georgia aims to combine financial products and connect them with digital assets and account programmability, serving technologically advanced companies. Both banks will operate in test mode for 7 months after receiving the banking license, with limited rights to carry out banking activities in the real environment. Authorization to carry out banking activities in real mode will be granted gradually based on the fulfillment of license requirements and approval from the National Bank of Georgia.

In November 2022, JSC "Paysera Bank Georgia" received a banking license. The bank's business model is based on integration with the financial system of the European Union and offering innovative digital products to customers. Initially working in test mode, the bank was allowed to carry out banking activities in a real environment in 2023, operating within the framework of a conditional banking activity license and continuing to fulfill requirements set by the NBG. As of December 31, 2023, there are 17 commercial

banks operating in the banking sector of Georgia. The participation of non-resident owners in the assets of banks, according to final ownership, is 88 percent, and 87.7 percent in equity.

In line with international best practices, important changes were made in the *"Regulation on the fit and proper requirements for commercial bank administrators"* and the *"Regulation on the acquisition of a significant share of commercial banks"* on October 31, 2022, based on the NBG decree. Commercial banks, their administrators, and persons holding a significant share are required to comply with the updated eligibility criteria defined by the regulations and submit relevant information/documentation to the NBG by August 1, 2023. The National Bank of Georgia provided consultations to commercial banks regarding these provisions and monitored their fulfillment in 2023.

The National Bank of Georgia continues to work on the consolidated supervision framework. Since the end of 2017, the NBG has been mandated to carry out supervision at the level of the banking group (consolidated supervision) following legislative changes in the Organic Law of Georgia "On the National Bank of Georgia".

## 4.3 CAPITAL ADEQUACY



By the end of 2023, the banking system of Georgia continued to maintain an adequate level of capital within the Basel III capital adequacy framework, considering the supervisory measures related to COVID-19.

The Financial Stability Committee of the National Bank of Georgia decided to update the framework for establishing a countercyclical capital buffer in November 2022 considering the recommendations of the Basel Committee on Banking Supervision (BCBS)<sup>52</sup>. This implied the establishment of a neutral positive

countercyclical buffer to accumulate capital buffers for stressful periods.

In accordance with the updated framework, by the decision of the Financial Stability Committee in November 2023, banks are obliged to meet the countercyclical capital buffer rate of 0.25% by March 15, 2024, 0.5% by March 15, 2025, 0.75% by March 15, 2026, and 1% by March 15, 2027.

In January 2023, the regulation on establishing a systemic buffer for systemically important commercial banks was updated, setting the points for systemically importance and relevant weights. In accordance with the new regulation, the systemic buffer was set at the following rates for three banks:

Commercial Bank	Systemic buffer rate
Bank of Georgia JSC	2.5%
TBC Bank JSC	2.5%
Liberty Bank JSC	1%

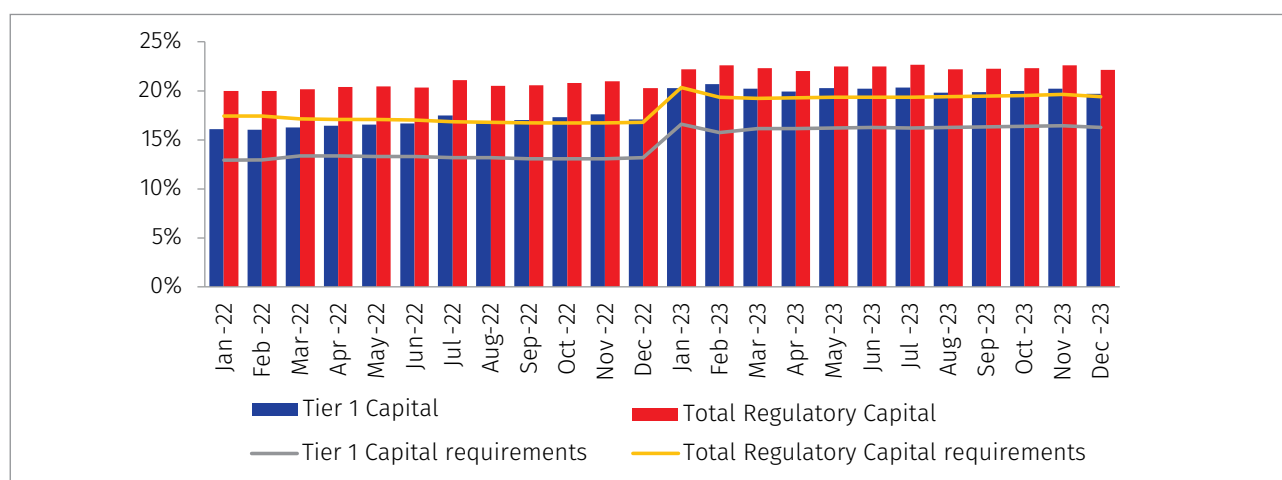
In addition, if the bank's market share in deposits exceeds 40 percent, the systemic buffer will increase to 3 percent. In case of increasing the buffer to 3 percent, banks will have 12 months to comply with it.

As of December 31, 2023, based on International Financial Accounting Standards (IFRS), the Tier 1 capital

ratio is 19.7 percent, and total regulatory capital ratio is 22.14 percent, which is 3.47 and 2.74 pp higher than the total capital adequacy requirements, respectively.

As of December 31, 2023, the leverage ratio<sup>53</sup> is also high, equal to 15.19 percent and exceeding the requirement by 10.19 pp.

Diagram N 4.1 Capital Adequacy Ratios under Basel III



(The data for 2022 are given on the basis of local accounting, and the data for 2023 - in accordance with the IFRS).

Source: NBG

52. Buffer usability and cyclicity in the Basel framework, October, 2022 - <https://www.bis.org/bcbs/publ/d542.pdf>

53. Capital to assets ratio.

The Pillar 2 framework defines the capital buffer requirement for credit portfolio concentration risk (both nominal and sectoral concentration risks), unhedged currency induced credit risk buffer (CICR), credit risk adjustment buffer (CRA), net stress test buffer calculated based on supervisory stress tests, and the procedure for determining the net GRAPE buffer established by the National Bank of Georgia under the general risk assessment program.

It is important that the capital buffers imposed under

Pillar 2 (except credit risk adjustment and stress test buffers) are required to be complied with by commercial banks with the same proportion of regulatory capital elements as required by the minimum requirements (CET1 capital - 4.5 percent, Tier 1 capital - 6 percent and total regulatory capital - 8 percent). Accordingly, 56 percent of the capital required under Pillar 2 must be observed by CET1 capital elements and 75 per cent by Tier1 capital elements. Commercial banks were given appropriate deadlines to comply with these requirements (Table N 4.1).

Table N 4.1 Concentration and net GRAPE buffer phase-in dates before COVID-19 related supervisory actions

<b>Concentration (nominal and setoral) and net GRAPE buffers</b>	<b>31/03/2021</b>	<b>31/03/2022</b>	<b>31/03/2023 and onward</b>
CET1 Capital	30%	45%	56%
Tier 1 Capital	40%	60%	75%
Total Regulatory Capital	100%	100%	100%

The buffers released at the beginning of the COVID 19 crisis began to restore on January 1, 2022. Banks were given a deadline of January 1, 2023 to restore the CICR buffer, and January 1, 2024 to meet the capital conservation buffer requirement. As of December 31, 2023, only three banks used the COVID-19 capital release. In addition, during 2023, banks were actively raising capital instruments, both in the form of Tier 2 capital and Additional Tier 1 capital instruments. Additional Tier 1 instruments were issued by two banks.

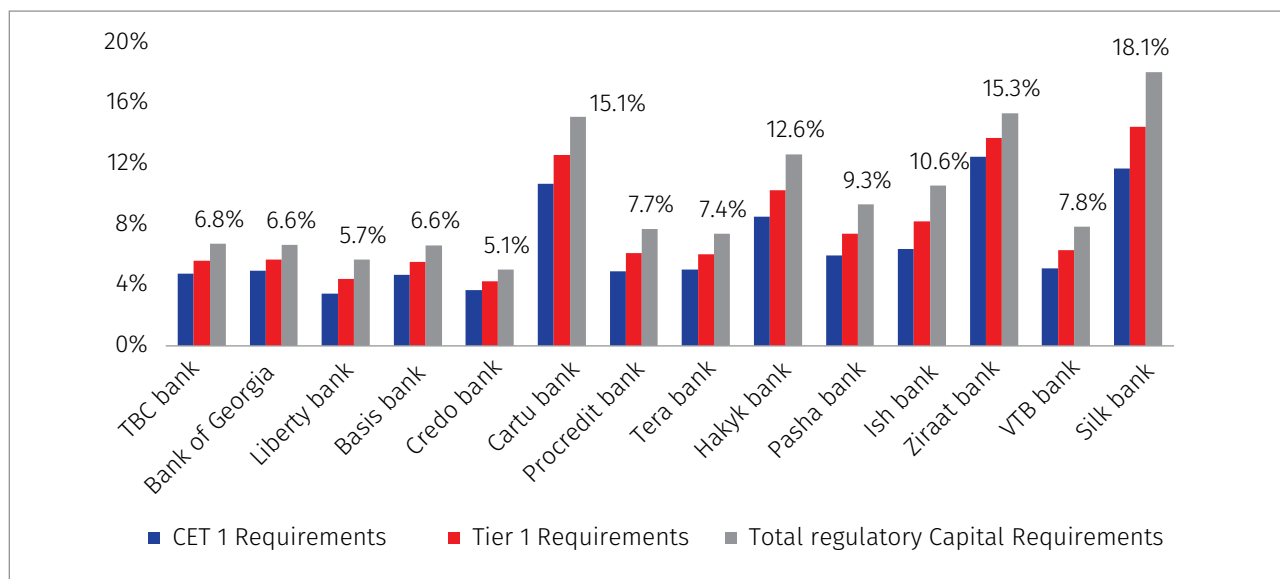
Despite considerable decline, dollarization remains one of the main challenges for the financial sector. To address it, a new methodology for calculating the CICR buffer was approved in March 2022, becoming mandatory in March 2023. With this change, whenever dollarization is 40 percent or less, the risk weight will be equal to 40 percent (instead of 75), and every one pp increase in bank's dollarization will increase

the additional risk weight by 3 pp, up to a maximum of 100 percent. As of end-2023, the transition to the new methodology reduced the regulatory capital requirement at the system level by 0.35% pp.

In 2023, commercial banks conducted a supervisory stress test on the instructions of the National Bank of Georgia. Following the review of the results, it is planned to establish a stress test buffer in the framework of Pillar 2 in 2024.

Net GRAPE buffer, launched In 2018, is set as part of the continuous risk-based supervision cycle and assesses the risks of commercial banks. GRAPE is used to assess the risk profile of each commercial bank. In August 2022, NBG updated the net GRAPE buffers once again, and then the individual GRAPE buffers was determined in the range of 1.3-9.3 percent of risk-weighted assets.

Diagram N 4.2 Pillar 2 aggregate requirements for commercial banks as of 31 December, 2023



Source: NBG

NBG continued to align the capital adequacy standards with the EU regulations in 2023. In accordance with the changes made in the regulations, commercial banks are now obliged to deduct the foreseeable dividend from the undistributed profit to be included from CET 1 capital. Additionally, for an instrument to qualify as additional Tier 1 and Tier 2 capital, the instrument contract must include conditions for writing off or bailing-in the liabilities of the commercial bank for the purpose of recapitalization. The legislation governing the instrument contract should also provide for the possibility of using the resolution instrument to write off or bail-in the liabilities of the commercial bank for recapitalization in case of resolution.

Since January 1, 2023, the banking system has successfully transitioned to International Financial Reporting Standards (IFRS). This transition led to a decrease in surplus on total regulatory capital in the banking system, with an increase in surplus on CET1 capital and Tier 1 capital. Consequently, commercial banks have been actively attracting and extending Tier 2 capital instruments during 2023.

## 4.4 FINANCIAL REPORTING AND TRANSPARENCY



The transition of commercial banks' supervisory reports to International Financial Reporting Standards (IFRS) was part of the 2020-2022 Supervisory Strategy. By switching to IFRS, the public and supervisory reporting of the banking sector got closer to the practices of Europe and other developed countries. As a result of the transition to IFRS, commercial banks shall comply with supervisory norms with IFRS-based numbers and methodologies. Respective changes in the regulatory framework entered into force on January 1, 2023.

In addition, parallel reporting was maintained in the first half of 2023, which involved the submission of reporting forms with both local (GAAP) and IFRS requirements. During this process, significant efforts were made by the banks and the quality of reporting was improved. Accordingly, NBG made a decision to end parallel reporting.

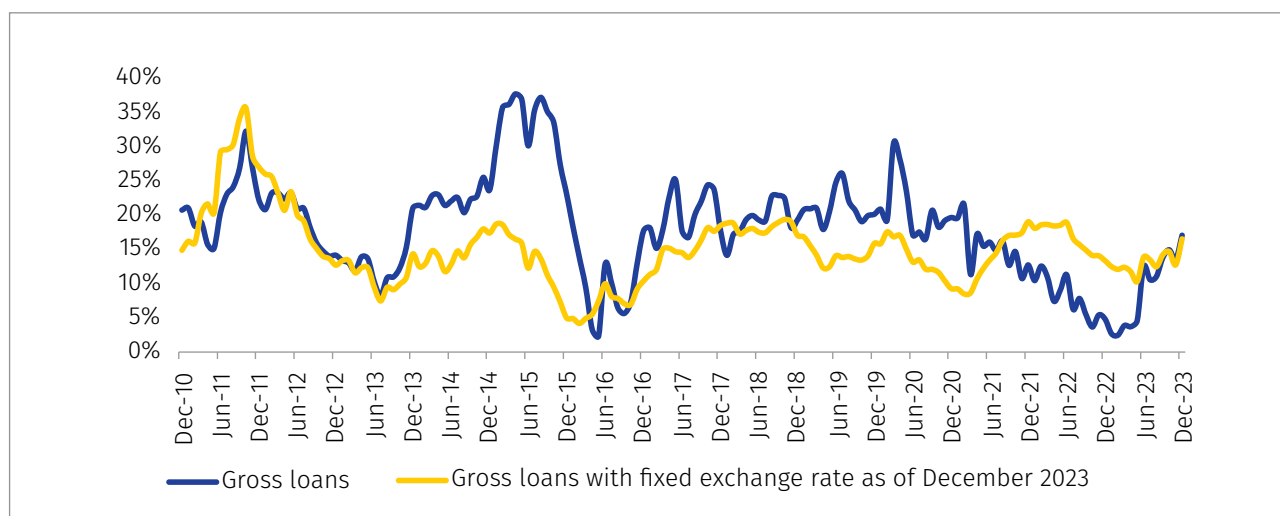


## 4.5 CREDIT RISK

In December 2023, an amendment was made to the *Regulation on disclosure of information by commercial banks within the framework of Pillar 3* with the aim of increasing transparency and confidence about the risks faced by commercial banks and the adequacy of regulatory capital, in the light of the transition to IFRS. Under the amendment, the frequency of the information disclosure about the banks' financial condition by the National Bank of Georgia was determined. In particular, NBG will publish balance sheet data, profit and loss information, main banking indicators, and consolidated statistical information about the financial condition of the banks every month. This information will be disclosed within thirty calendar days from the end of the reporting month, in accordance with the form established by the NBG.

By December 31, 2023, the total credit portfolio of the banking system reached 52.9 billion GEL, and its annual growth, without the effect of the exchange rate (at the exchange rate at the end of 2023), was 16.5 percent, while the portfolio without interbank loans reached 52.8 billion GEL and without the effect of the exchange rate (2023 at the current exchange rate at the end of the year) increased by 17.6%<sup>54</sup>.

Diagram N 4.3 Change in total loan portfolio compared to the previous year



Source: NBG

In 2023, a resegmentation occurred, specifically separating the micro segment into its own category. This resulted in 80% of the micro segment portfolio coming from the corporate and small and medium segments, and 20% from the retail segment. Over the year, the composition of the credit portfolio (excluding interbank loans) shifted slightly in terms of segments. The share of the corporate segment increased, while

the share of the retail and small and medium segments in the total portfolio decreased. Additionally, the volume of securities purchased by commercial banks from various corporate clients increased. Considering this effect, the corporate segment's portfolio grew by 24.7%, and the total loan portfolio (excluding interbank loans) grew by 18.2%.

54. The data of 2023 in the mentioned subsection does not include the information of VTB Bank.

Table N 4.2 Composition of the loan portfolio (excluding interbank loans) by segment, without exchange rate effect, the exchange rate as of the end of 2023

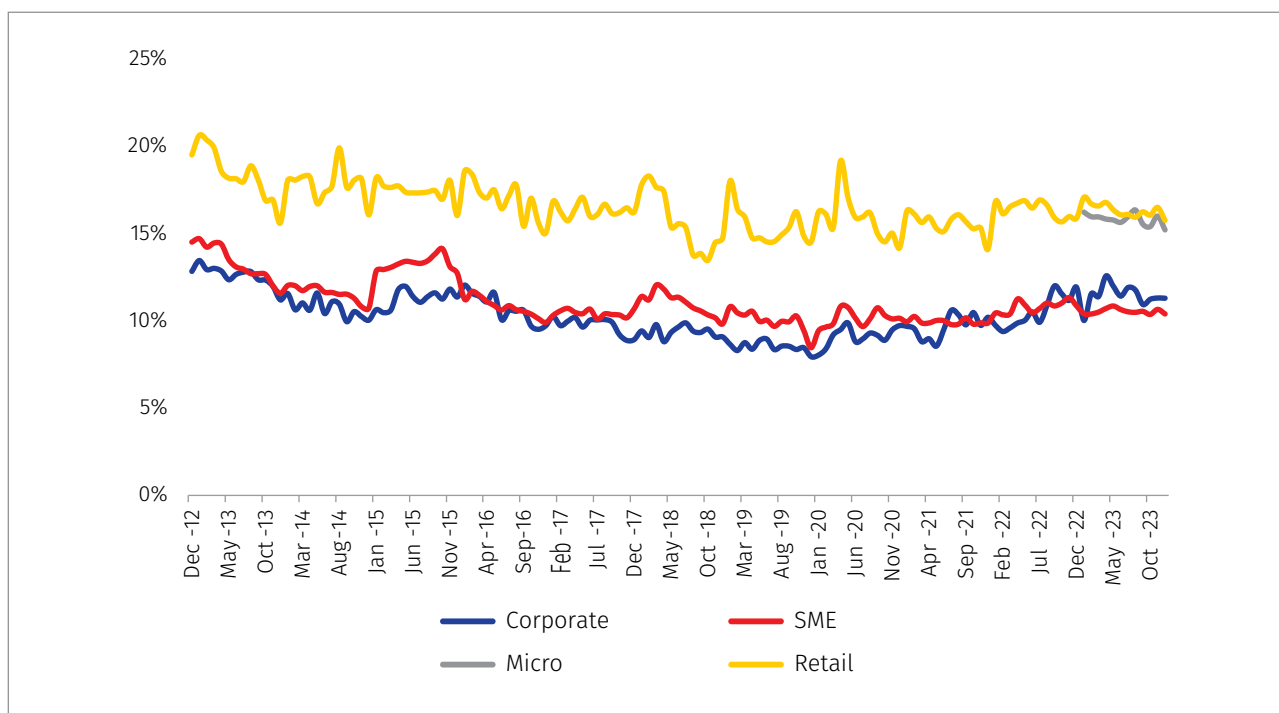
	Dec-22		Dec-23		Change at fixed rate %	Change at fixed rate and without reclassification effect %
	Million GEL	share %	Million GEL	share %		
Corporate	14,026	31%	17,772	34%	26.7%	22.8%
SME	7,897	18%	8,848	17%	12.0%	18.1%
Micro	6,209	14%	7,138	14%	15.0%	16.2%
Retail	16,801	37%	19,072	36%	13.5%	13.5%
Total:	44,932	100%	52,830	100%	17.6%	17.6%

Source: NBG

In 2023, foreign currency loans were issued at a higher rate than in 2022, driven by the increase in the Secured Overnight Financing Rate (SOFR) during the year. Conversely, interest rates on loans in the national currency decreased compared to the previous year, due to the gradual reduction of the National Bank of

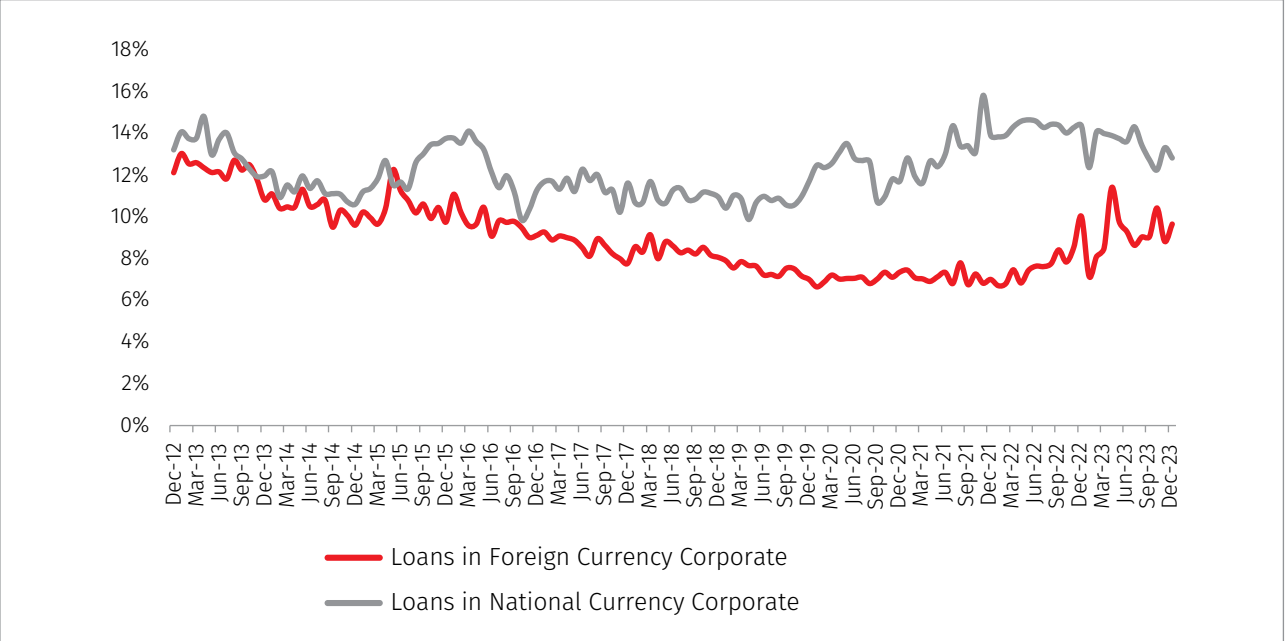
Georgia's refinancing rate. These changes primarily impacted the corporate segment, which has a high share of foreign currency loans, resulting in a slight increase in the weighted average rate for the segment as a whole compared to the previous year.

Diagram N 4.4 Monthly weighted average interest rates on loans per segment



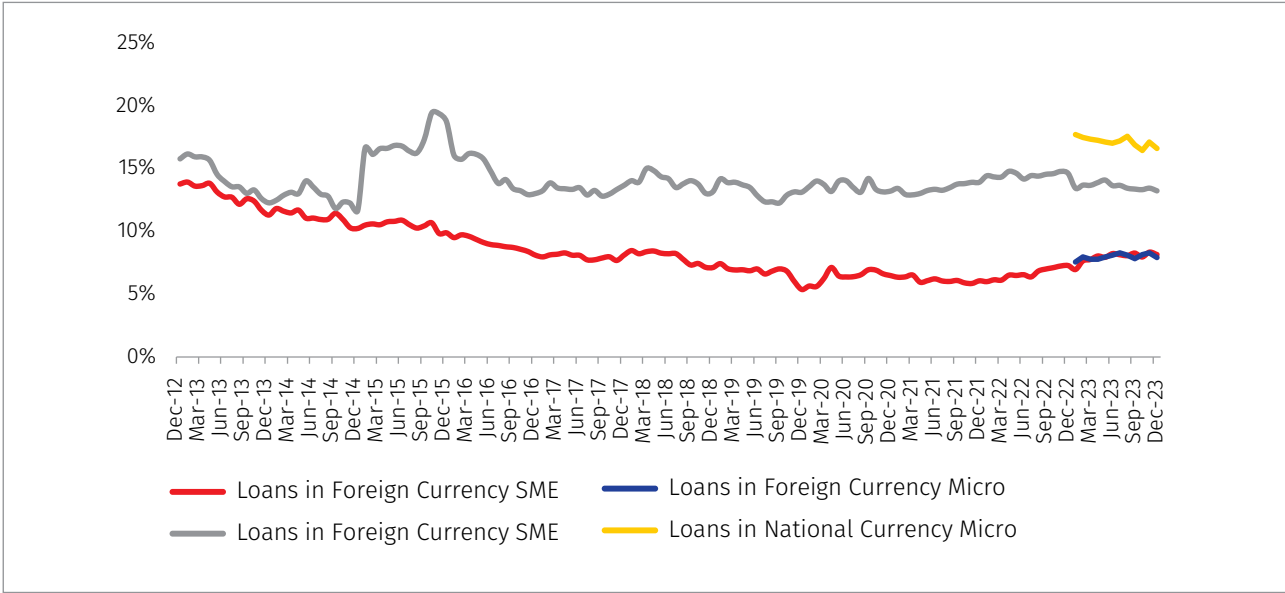
Source: NBG

Diagram N 4.5 Average weighted interest rates on loans for the corporate segment



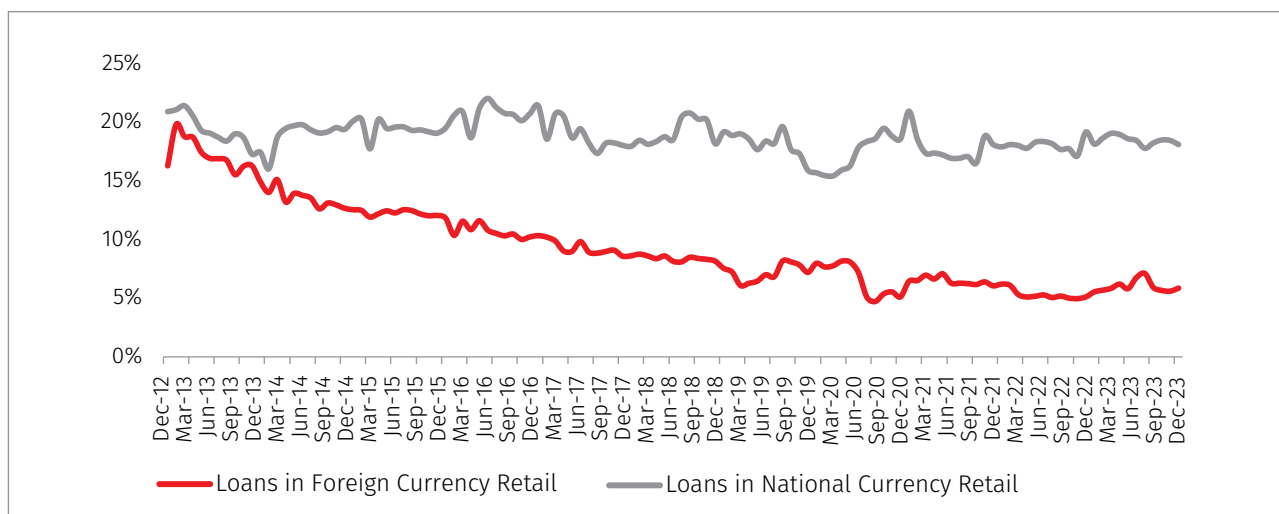
Source: NBG

Diagram N 4.6 Weighted average interest rates on loans for the MSME segments



Source: NBG

Diagram N 4.7 weighted average interest rates on loans for the retail segment



Source: NBG

The loan portfolio is diversified in sectors. At the end of December, 2023, the total share of economically vulnerable sectors (real estate development, real estate management, hotels and tourism, restaurants

and catering, car dealers) in the portfolio was at 17.7 percent, 1.1 pp more than in the same period of the previous year.

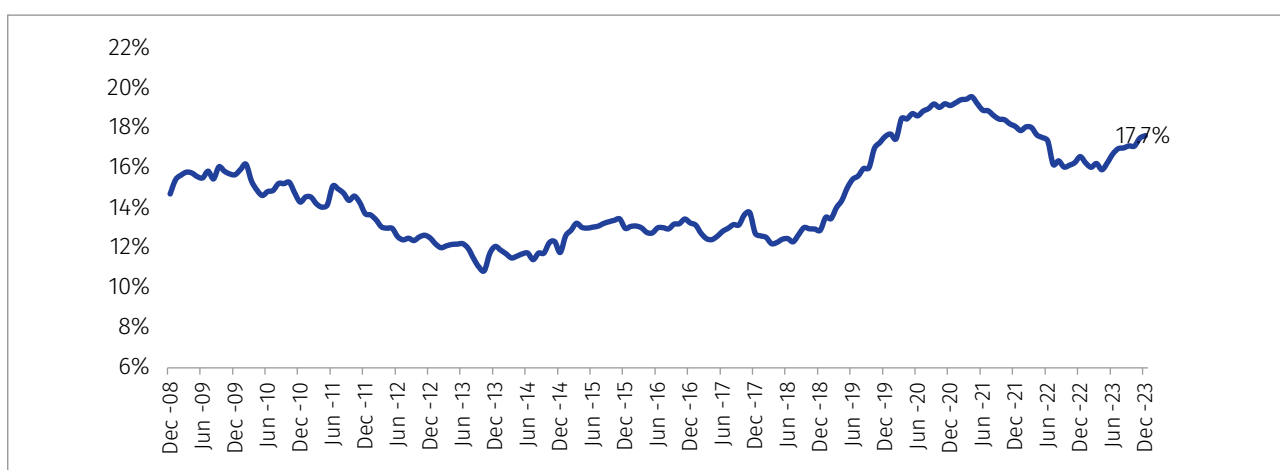
Table N 4.3 Sectoral Distribution of the Loan Portfolio

Sector except interbank loans (million GEL)	Share in total portfolio	Financial instrument principal	Amortized cost of financial instrument	Expected credit loss	Expected credit loss %
Government organizations	0.2%	94	94	1	0.7%
Financial institutions	1.2%	625	630	4	0.6%
Wholesale pawn shop	0.4%	231	232	1	0.6%
Real estate development	4.9%	2,596	2,623	38	1.4%
Real estate management	5.5%	2,892	2,935	25	0.9%
Construction companies (not developers)	1.7%	912	929	29	3.1%
procurement, production and trade in construction materials	3.5%	1,853	1,868	22	1.2%
Trade in consumer goods	3.5%	1,835	1,847	16	0.9%
production of consumer goods	2.9%	1,548	1,565	52	3.3%
Production and trade of durable consumer goods	1.0%	512	515	5	0.9%
Production and trade of footwear, clothing and textiles	1.0%	539	545	5	1.0%
trade (other)	3.8%	2,012	2,034	39	1.9%
manufacturing (other)	1.6%	866	875	16	1.8%
Hotels and tourism	5.5%	2,882	2,920	42	1.4%
Restaurants, bars, cafes and fast food establishments	1.4%	729	737	9	1.2%
Heavy industry	1.4%	750	765	13	1.6%
Petrol stations and petrol importers	0.7%	367	369	6	1.6%
energy	4.0%	2,108	2,139	7	0.3%

Car dealers	0.4%	230	232	1	0.6%
Healthcare	2.2%	1,152	1,161	16	1.4%
pharmaceuticals	0.3%	164	165	1	0.5%
telecommunications	0.4%	222	234	17	7.1%
Services	5.3%	2,787	2,812	48	1.7%
Agriculture	5.6%	2,974	3,061	81	2.6%
other	0.4%	204	212	6	2.7%
<b>Retail products</b>	<b>41.2%</b>	<b>21,747</b>	<b>22,033</b>	<b>484</b>	<b>2.2%</b>
Transportation loans	0.4%	185	188	4	2.3%
Consumer loans	18.0%	9,505	9,563	345	3.6%
Pay Day Loans	0.0%	1	1	.2	26.9%
Instant installment	0.8%	432	430	13	3.1%
overdrafts	0.1%	70	73	15	20.0%
Credit cards	0.9%	452	462	29	6.2%
Mortgages – purchase of complete real estate	15.8%	8,327	8,494	64	0.8%
mortgage – construction, purchase of real estate under construction	3.0%	1,578	1,607	6	0.4%
mortgage – for repairs of real estate	1.7%	874	889	5	0.6%
Retail pawn shop loans	0.6%	317	322	2	0.7%
Student loans	0.0%	6	6	.1	1.7%
<b>Loan portfolio</b>	<b>100.0%</b>	<b>52,830</b>	<b>53,533</b>	<b>981</b>	<b>1.8%</b>

Source: NBG

Diagram N 4.8 Share of economically vulnerable sectors in the total loan portfolio



Source: NBG

The year 2023 saw a higher growth of retail products compared to 2022. An increase was observed in all products except pay day loans. However, given the fixed exchange rate, the increase in mortgage and

consumer lending was the main driver of growth in retail products, although the latter grew more than mortgages.

Table N 4.4 Growth in retail products (excluding the exchange rate effect, at the exchange rate active as of end-2023)

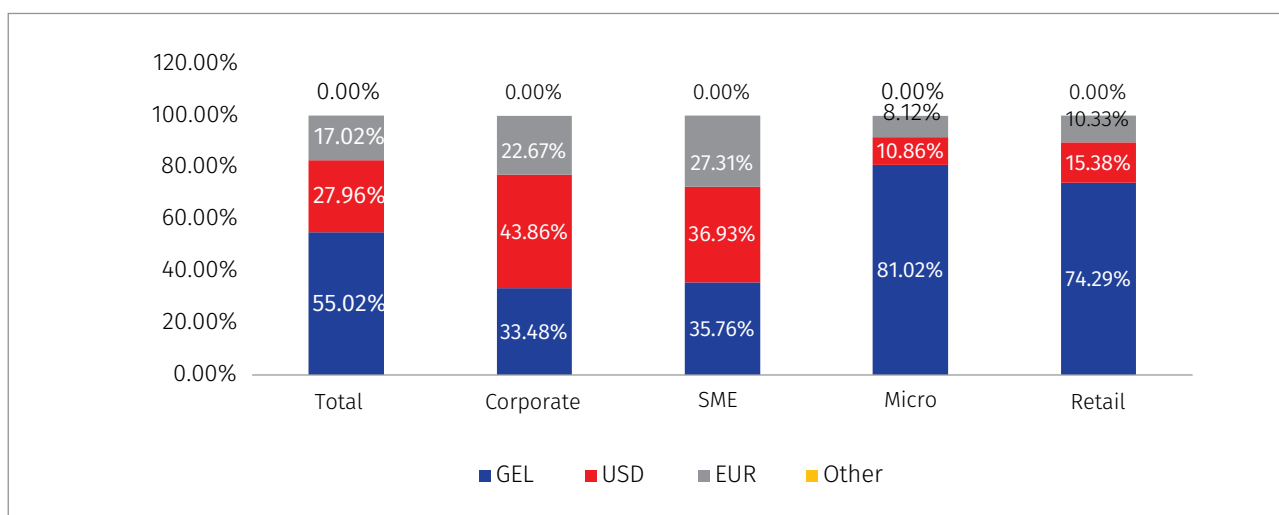
Product	Dec-22		Dec-23		Change % at fixed rate	Change million GEL	change, % at fixed rate and reclassification
	Million GEL	share, %	Million GEL	share, %			
Retail products	18,465	100%	21,747	100%	17.8%	3,282	17.8%
Transport loans	146	0.8%	185	0.9%	27.0%	39	27.0%
Consumer loans	7,438	40.3%	9,505	43.7%	27.8%	2,067	27.8%
Pay Day Loans	4	0.0%	1	0.0%	-81.4%	-3	-81.4%
Instant installment	378	2.0%	432	2.0%	14.1%	53	14.1%
Overdrafts	51	0.3%	70	0.3%	36.3%	19	36.3%
Credit cards	429	2.3%	452	2.1%	5.4%	23	5.4%
mortgage – purchase of complete real estate	7,511	40.7%	8,327	38.3%	10.9%	815	10.9%
mortgage – construction, purchase of real estate under construction	1,387	7.5%	1,578	7.3%	13.8%	191	13.8%
mortgage – real estate for renovation	806	4.4%	874	4.0%	8.4%	67	8.4%
Retail pawn shop loans	310	1.7%	317	1.5%	2.4%	7	2.4%
Student loans	3	0.0%	6	0.0%	87.2%	3	87.2%

Source: NBG

The structure of the retail product portfolio has changed slightly compared to the previous year, echoed in the higher share of consumer loans and lower share

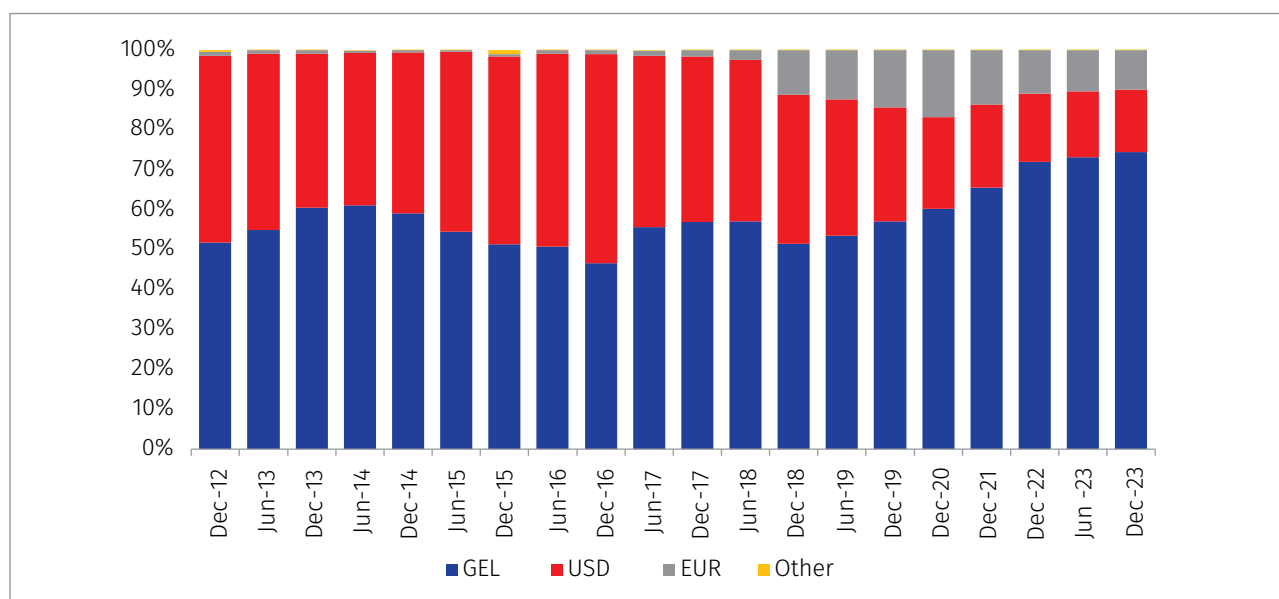
of mortgage loans (purchase of complete real estate). The decrease in the share of mortgage loans is mainly due to the higher growth rate of consumer loans.

Diagram N 4.9 Segment balances by currency at the end of 2023 (except interbank loans)



Source: NBG

Diagram N 4.10 Composition of the retail portfolio by currencies



Source: NBG

At the end of 2023, compared to December 2022, the indicators of non-performing loans and expected credit losses on the portfolio have improved significantly, which is caused both by the improvement of the portfolio quality and by the banks' transition

to the classification/provision of loans using the IFRS methodology, however, as a counterweight to this, an additional requirement for capital in the form of a CRA buffer has been established for banks.

Table N 4.5 Classification of loan portfolio by quality

Category (except interbank loans)	Principal, million GEL	amortized cost, million GEL	share	Expected credit loss %
Credit risk stage 1	48,637	49,159	92.1%	0.5%
Credit risk stage 2	2,824	2,901	5.3%	6.1%
<i>Non-performing loans</i>	1,369	1,473	2.6%	37.9%
Credit risk stage 3	1,255	1,356	2.4%	38.9%
POCI	114	117	0.2%	26.1%
<b>Total:</b>	<b>52,830</b>	<b>53,533</b>	<b>100.0%</b>	<b>1.8%</b>

Source: NBG

Table N 4.6 Portfolio Quality by Segments

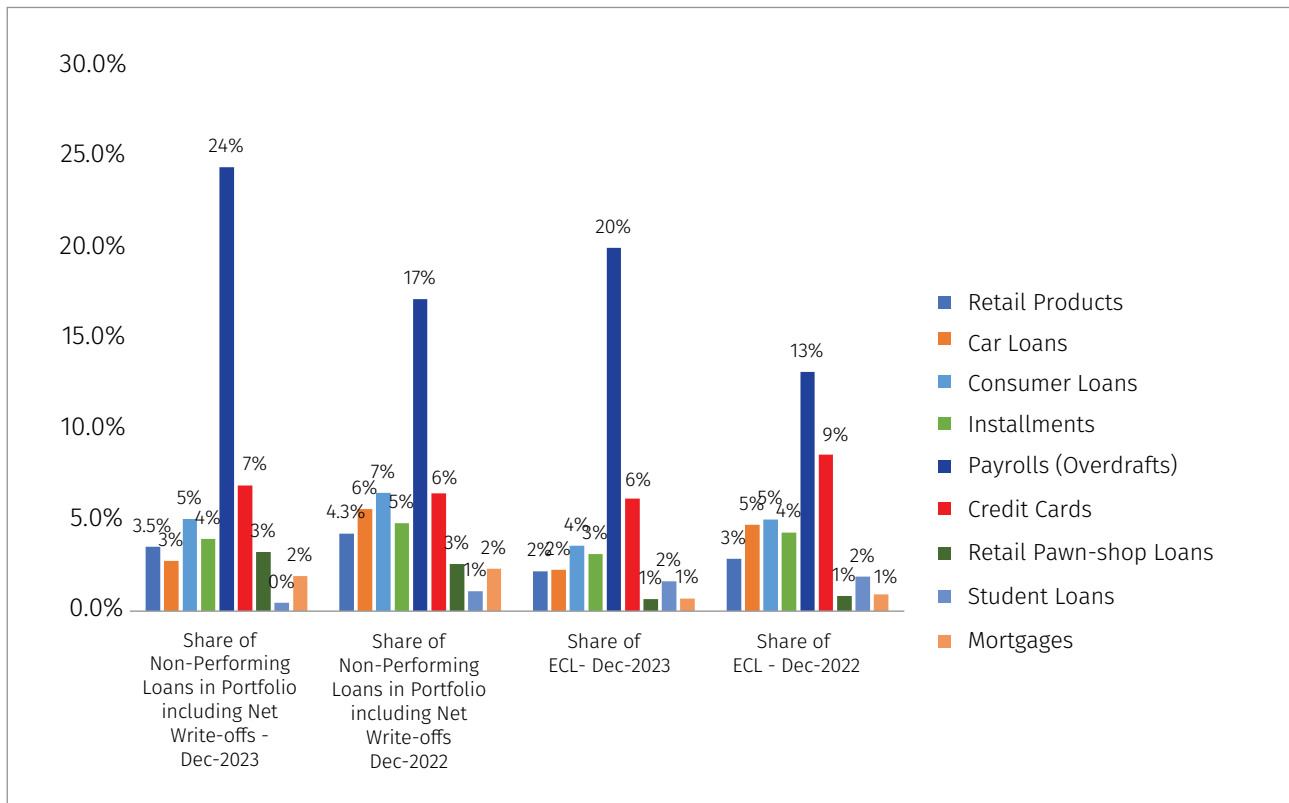
segment	Non-performing loans	Expected credit loss %
Corporate	1.84%	1.14%
Small and medium	4.45%	1.77%
Micro	2.47%	2.55%
Retail	2.48%	2.24%

Source: NBG

Regarding the quality of the retail credit portfolio, the share of non-performing loans in the total retail products portfolio has decreased, largely due to the improvement in the quality of consumer and mortgage loans. Additionally, the volume of the retail products portfolio has increased more compared to the previous year. The percentage share of expected credit losses in the portfolio for all retail products, except overdrafts, has reduced, considering the effects of portfolio write-offs and growth.

Compared to 2021, the cost of risk increased for the retail product portfolio in 2022. However, the cost of risk for auto loans, credit cards, home improvement loans, and mortgages decreased compared to the previous year. For consumer loans, instant installments, and overdrafts, the increase in the cost of risk was caused by the higher write-off rates of loans for these products.

Diagram N 4.11 Quality of Retail Portfolio and Cost of Risk by products

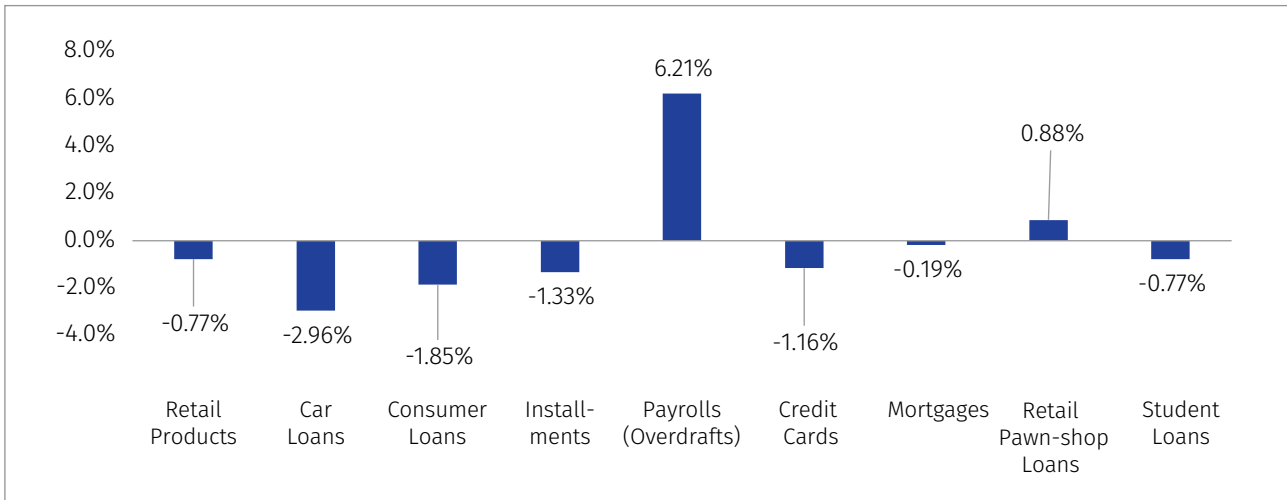


Source: NBG

The cost of risk for the retail product portfolio decreased in 2023, compared to 2022, although the

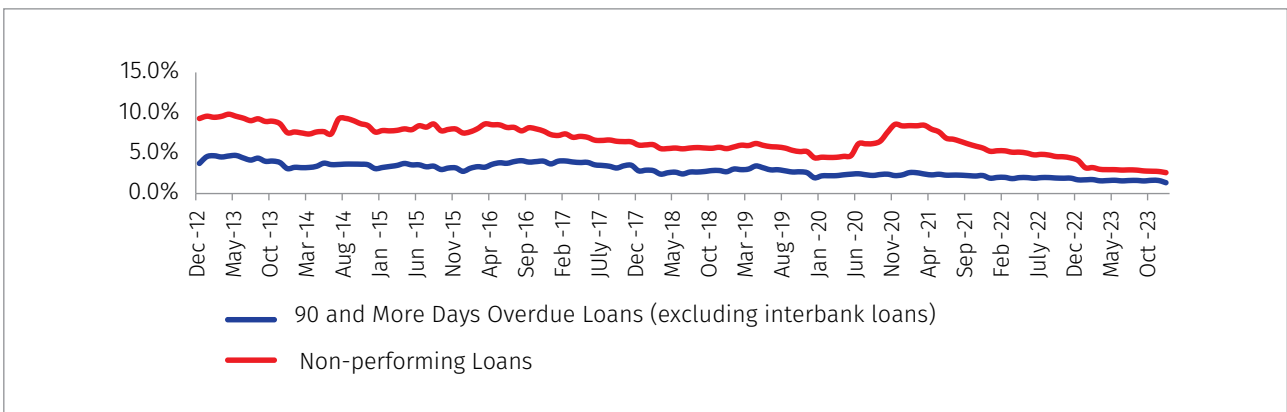
cost of risk for car overdrafts and retail pawn shop loans increased compared to previous years.

Diagram N 4.12 Change in cost of risk (Dec-2022 - Dec-2021)



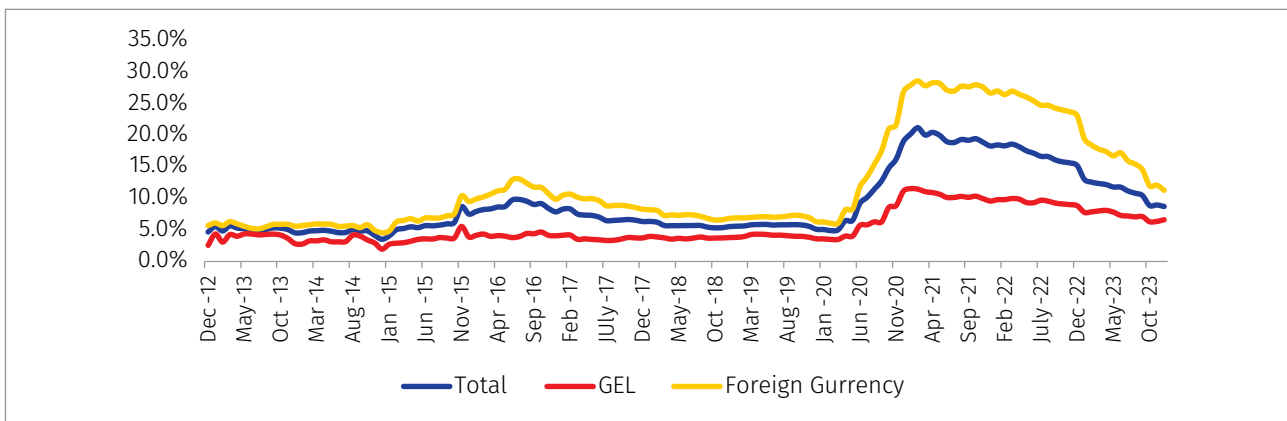
Source: NBG

Diagram N 4.13 Loan Portfolio by Quality Indicators (except interbank loans)



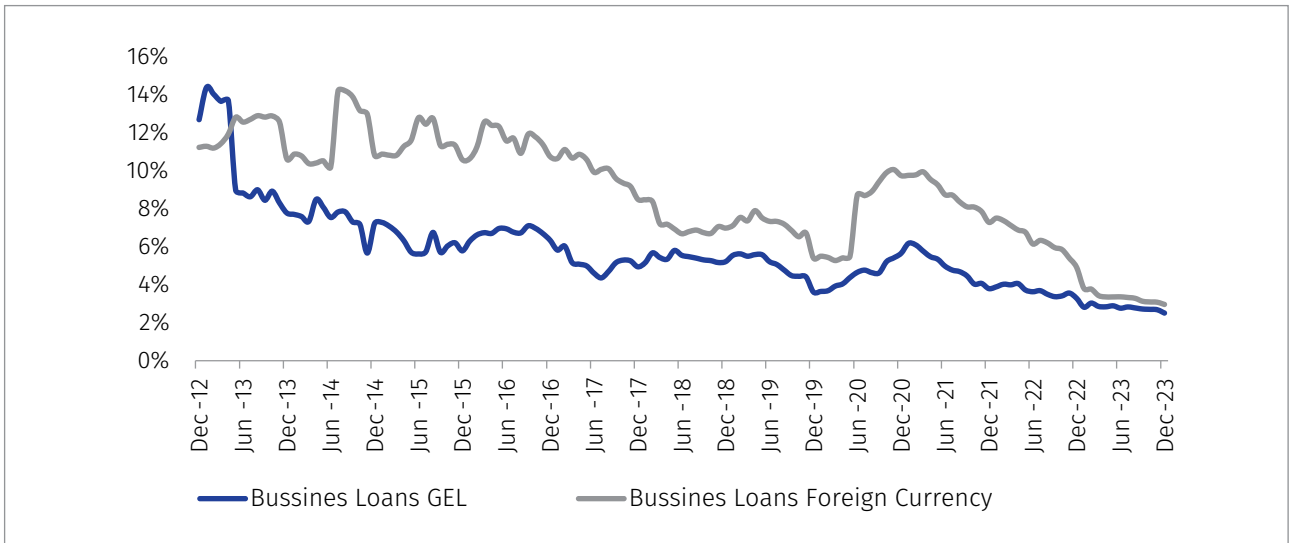
Source: NBG

Diagram N 4.14 Share of restructured loans by currencies in total loan portfolio



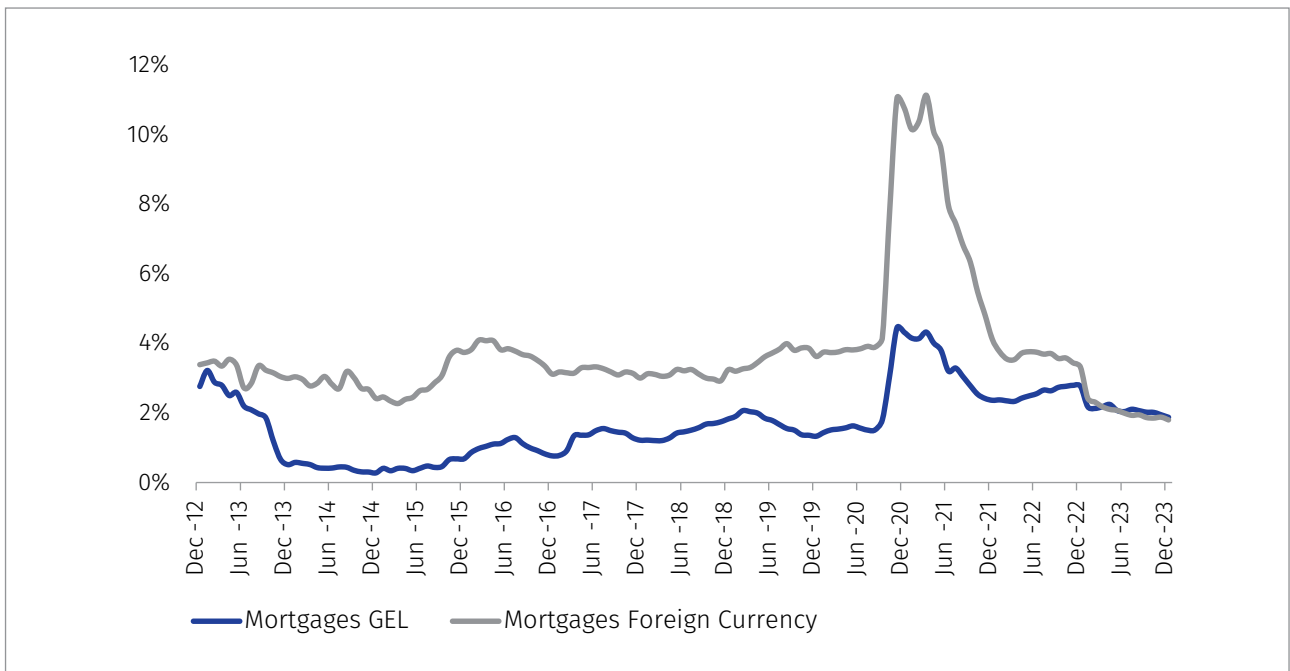
Source: NBG

Diagram N 4.15 Share of non-performing loans by currencies in the business loans



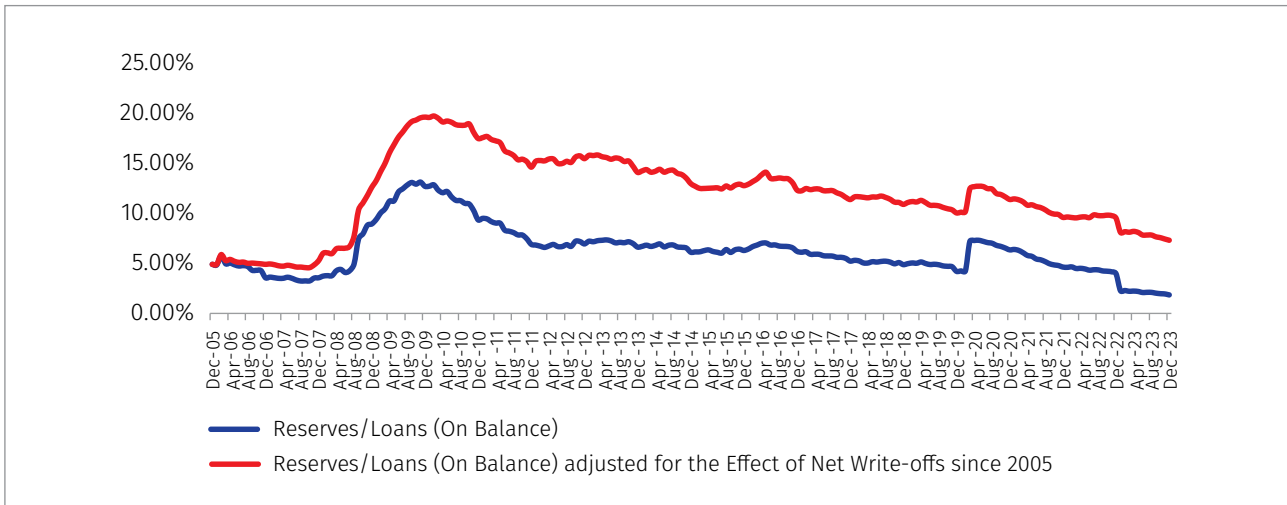
Source: NBG

Diagram N 4.16 Share of non-performing loans by currencies in the mortgage loans



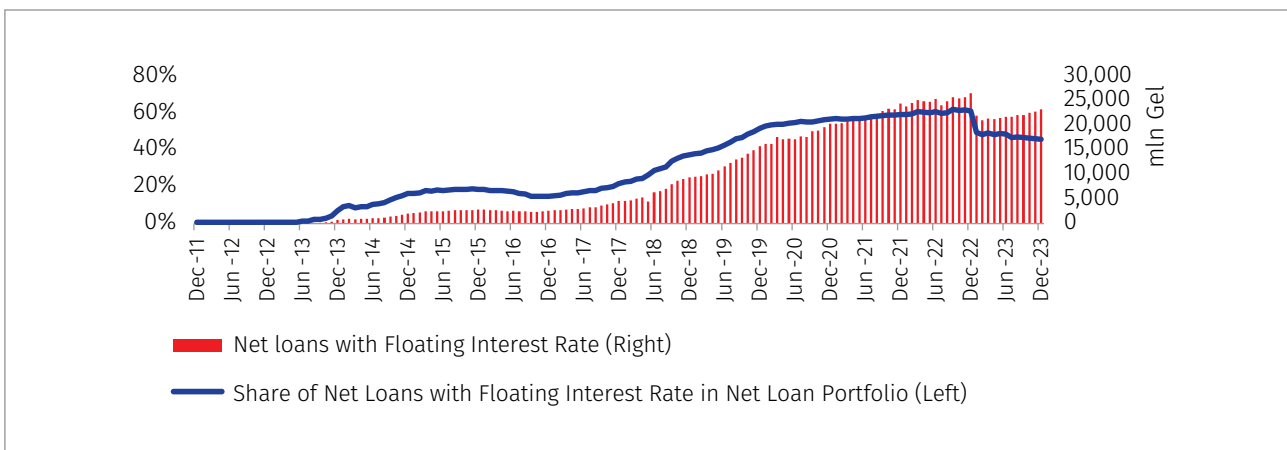
Source: NBG

Diagram N 4.17 Loan Loss Reserves to Total Portfolio<sup>55</sup>



Source: NBG

Diagram N 4.18 and share of net floating interest rate loans in the net loans



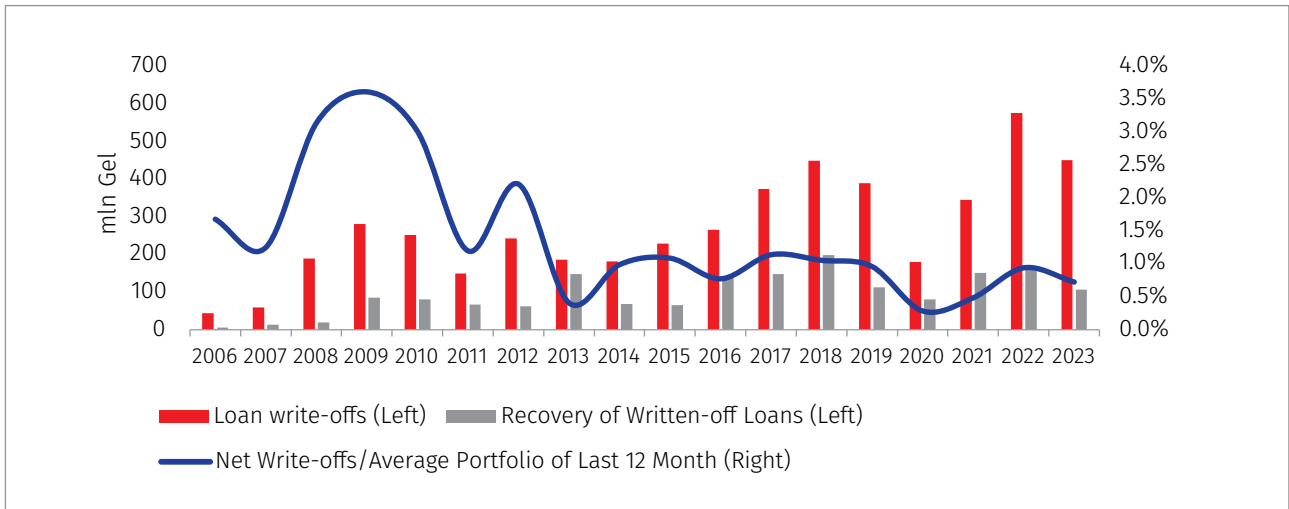
Source: NBG

The volume of net written-off loans in 2023 decreased by 15.3 percent compared to the same period in 2022. A large share of net written-off loans comes from the retail segment, like in the previous year. A decrease is

recorded in both written-off assets and recoveries of written-off assets, although the latter shows a faster decrease than the write-offs of assets.

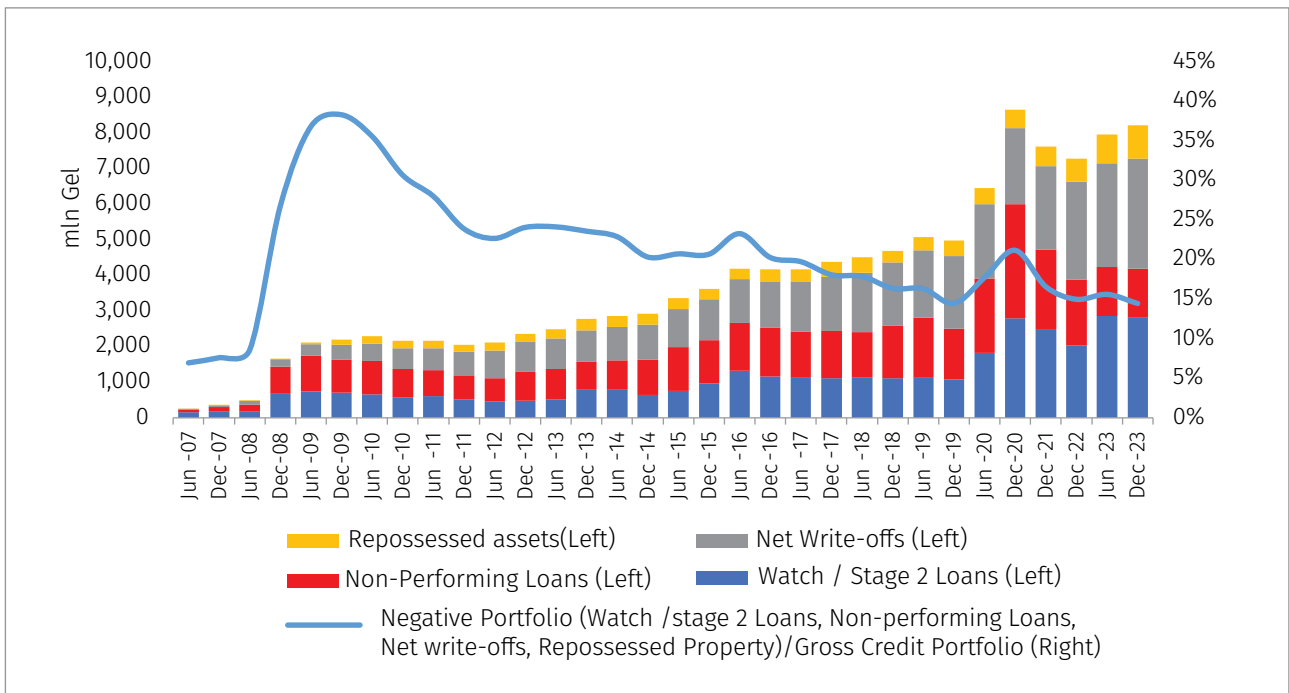
55. Includes general reserve

Diagram N 4.19 Loan Write-offs and Recoveries



Source: NBG

Diagram N 4.20 Problem Assets

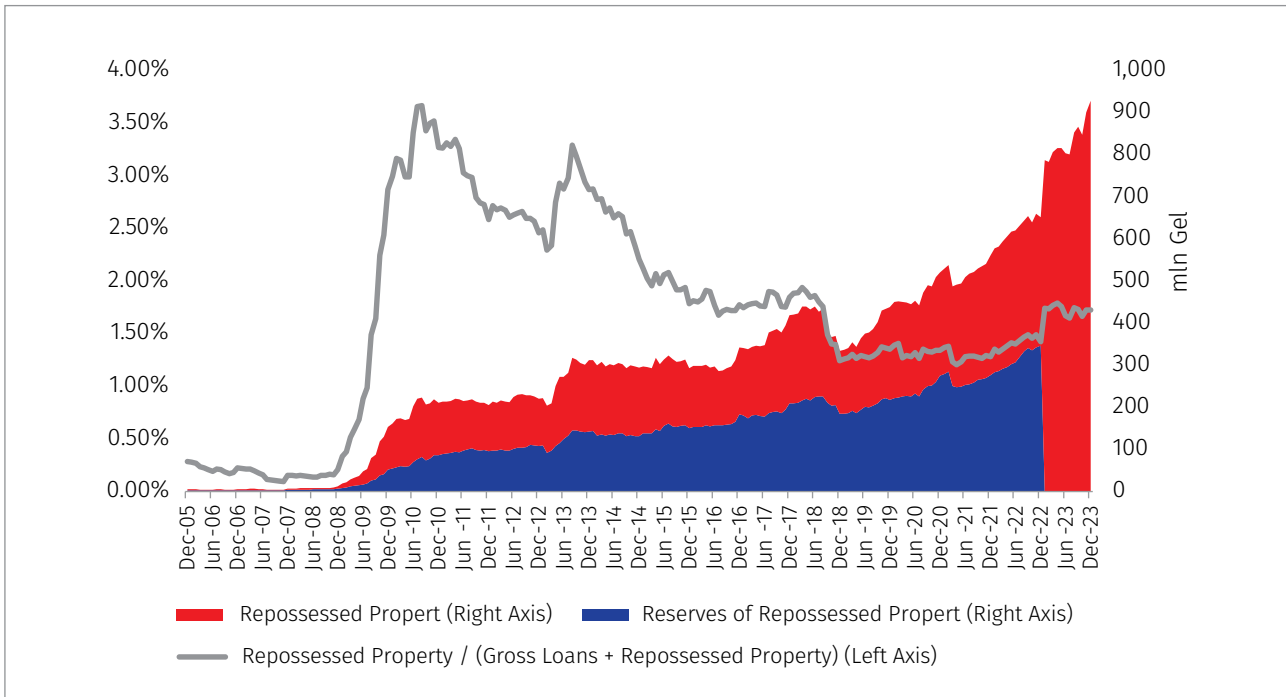


Source: NBG

In 2023, compared to 2022, the volume and share of repossessed property in total investments (repossessed property added to loans) slightly increased. This was caused by the recovery of owned property written off in the previous period according to the IFRS methodol-

ogy. It should be noted that under IFRS, there is no expected credit loss on owned property. However, similar to loans, an additional capital requirement in the form of a CRA buffer was established for banks as a counterbalance to this.

Diagram N 4.21 Repossessed assets



Source: NBG

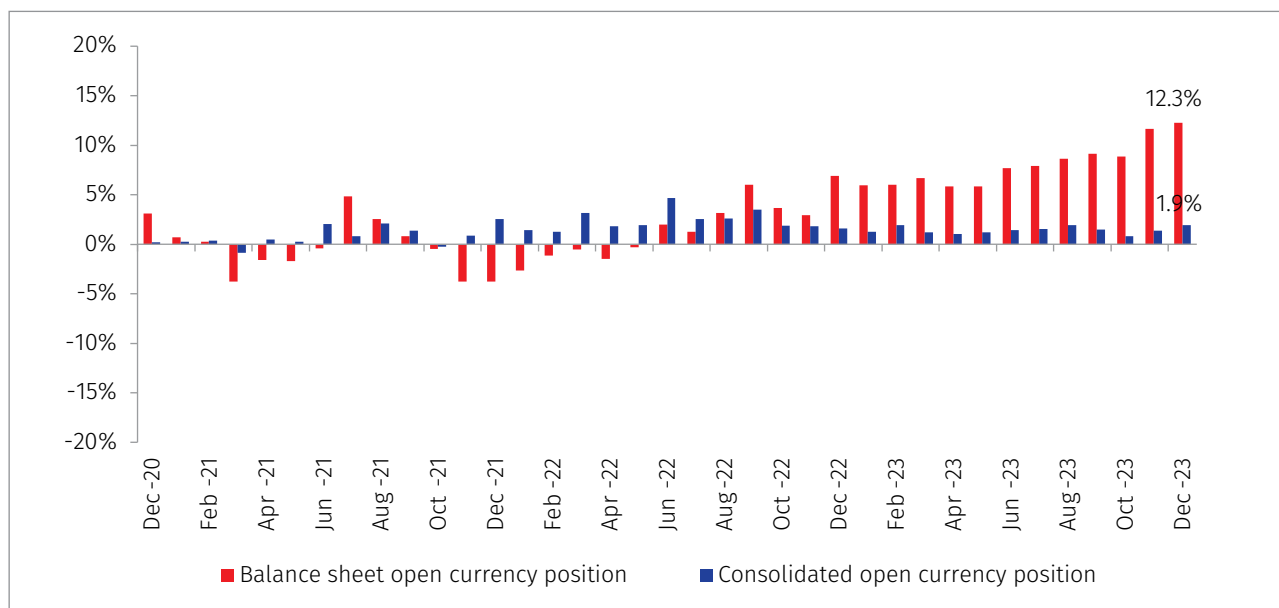
## 4.6 MARKET RISK



Exchange rate of GEL against US dollar appreciated during 2023, and depreciated against Euro, while banks proceeded with stable currency positions. The aggregate currency position was within 1.9 percent at the end of the year.

The share of foreign currency assets and liabilities in the Georgian banking system is still high, so, currency risk factor remains important for Georgian banks. The National Bank of Georgia continues its supervisory work striving to improve current methodology of foreign exchange risk management, including the improvement of reflecting the reserve of foreign currency assets in the open currency position. Starting from July 2023, the foreign currency position is presented in accordance with IFRS, where the reserves for the possible loss of the foreign currency assets are fully deducted.

Diagram N 4.22 Balance sheet and consolidated open currency positions to regulatory capital



Source: NBG, from July 2023, the corresponding data of IFRS accounting is provided

#### 4.6.1 INTEREST RATE RISK

In 2023, the refinancing rate reduced by 1.5 pp. There was a significant increase in the international rates of the US dollar and the euro. Similar fluctuation of interest rates reaffirms the importance of interest rate risk in banks and the need for its regular monitoring and adequate assessment.

Banks operating in Georgia hold almost no securities for trading. However, banks that have a trading book<sup>56</sup> are required to develop appropriate procedures and report to the National Bank of Georgia. If the monitoring identifies the possibility of significant portfolio growth, a trade book risk management regulation will apply.

At present, the regulation and tactics for interest rate risk for the banking book are applied to the aggregate balance. The Regulation on the Management of Interest Rate Risk for the Banking Book (IRRBB) is meant to identify, assess, and manage interest rate arising on banking book, and by imposing related requirements,

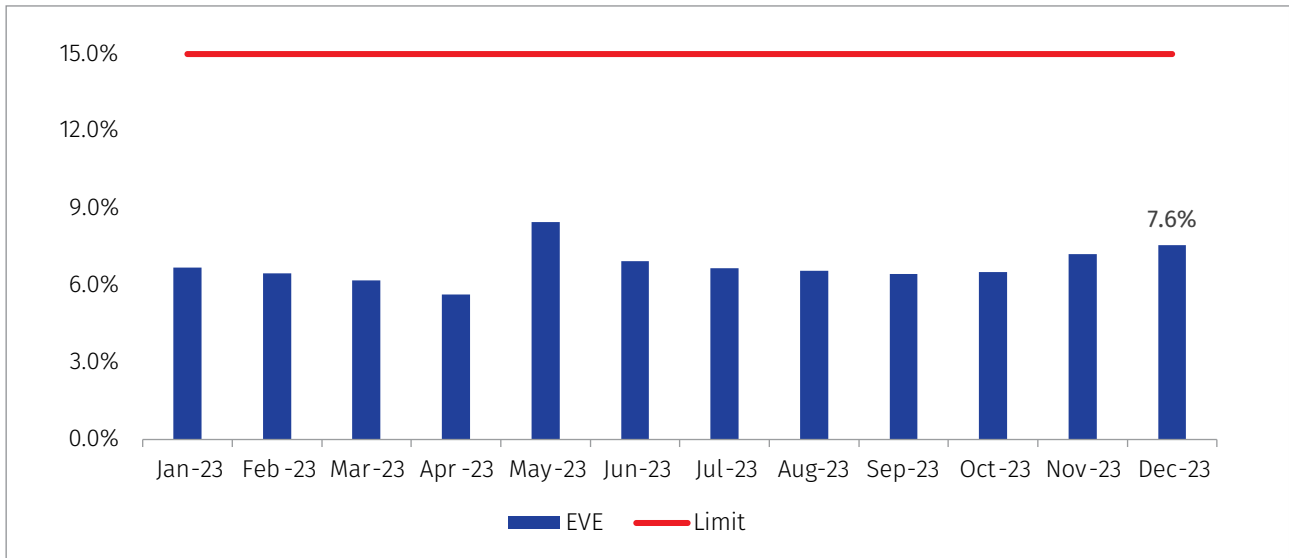
to promote the stability and sound functioning of commercial banks and the financial sector. Interest rate risk reflects the Bank's sensitivity to changes in interest rates. It refers to the current or future risk to the bank's capital and income that arises from changes in interest rates and affects banking book positions. Changes in interest rates change the net present value and residual maturities of future cash flows, changing the respective assets, liabilities, off-balance sheet items and their economic value (EVE). Changes in interest rates also affect the bank's net interest income (NII) being a result of changes in income and expenses that are sensitive to interest rate risk. This risk management has a significant impact on the bank's profitability and capital.

As of December 2023, based on the current interest rate risk approach, the ratio of changes in system economic value (EVE) and net interest income (NII) to Tier 1 capital is 7.6% and 3.4%, respectively. The figures for 2023 remain well below the maximum regulatory limit.

56. The trading book includes financial instruments that a commercial bank owns:

- for selling in the short term;
- due to the expected change in the price, with the expectation of the profit obtained by revaluation;
- to generate revenues using it through arbitration;
- for insuring the risk positions of the instruments purchased for the purposes of subsections "a"- "c".

Diagram N 4.23 Change in EVE to Tier1 Capital



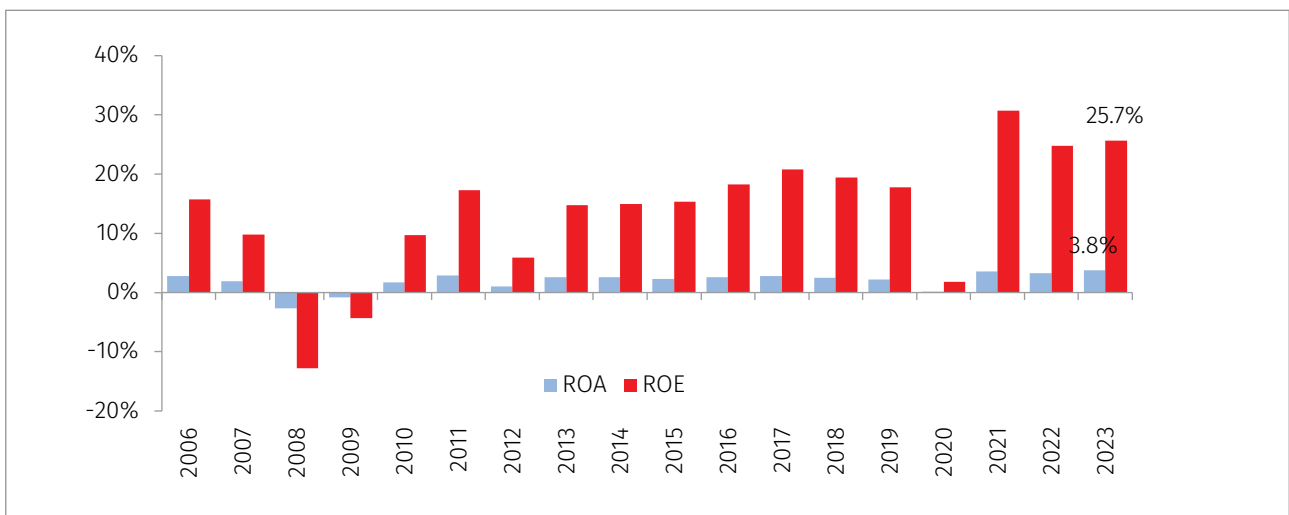
Source: NBG, from July 2023, the corresponding data of IFRS accounting is provided.

## 4.7 PROFITABILITY RISK

In 2023, the return on average assets and equity<sup>57</sup> amounted to 3.8% and 25.7%, respectively. These results incorporate the relevant indicators from NBG ac-

counting for January-June 2023 and IFRS accounting for July-December. According to the NBG census in 2022, the corresponding indicators were 3.2% and 24.7%. This year, the banking system's indicators continue to demonstrate stability, meeting the acceptable return on capital levels for shareholders.

Diagram N 4.24 Return on Equity and Assets



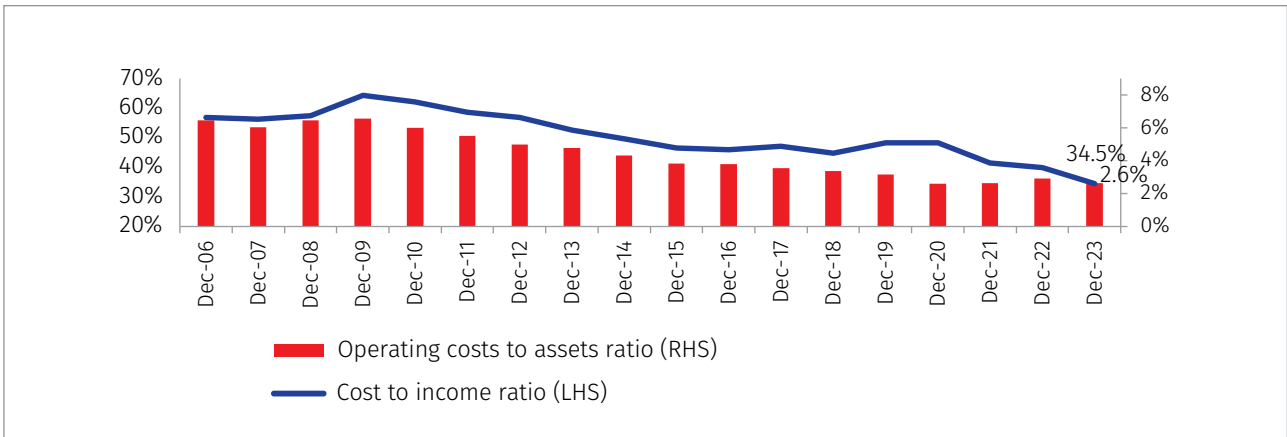
Source: NBG, from July 2023, the corresponding data of IFRS accounting is provided.

57. ROE is net profit relative to the average share capital of the year, and ROA - net profit relative to the average assets of the year. In these calculations, NBG's net income is calculated as the sum of net interest income and net non-interest income less the amount of allowance for possible losses on loans and other financial assets, after allowance for contingencies and taxes. IFRS net income is calculated as the sum of net interest income (expense) and net non-interest income (expense) less expected losses and impairments, after income taxes.

In 2023, several important factors affected the profitability of the banking system. Net interest income increased by 23% amid increased credit activity during the year. Despite an 18% increase in non-interest

expenses, the cost-to-income ratio decreased from 39.9% to 34.5%. Additionally, the cost-to-assets ratio decreased from 2.9% to 2.6%, reflecting the effect of the transition to IFRS accounting.

Diagram N 4.25 costs to income and assets ratio



Source: NBG, IFRS December data are provided for 2023

The National Bank of Georgia continues to review the profitability forecasts of banks, analyze the business models and strategies of individual institutions, and assess the mitigating factors relevant to risks. Considerable attention is paid to scale effect, market niche and/or other competitive advantage and projected credit loss factors. Development and improvement of pricing models for bank products is closely monitored.

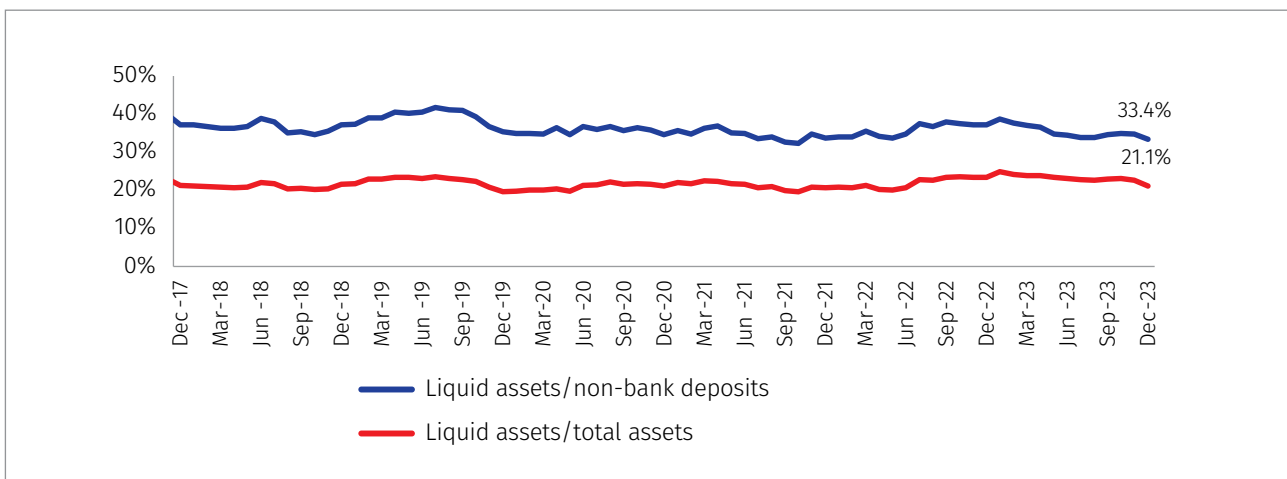
## 4.8 LIQUIDITY RISK



### 4.8.1 LIQUID ASSET STRUCTURE

The volume of liquid assets slightly decreased in 2023. As a result, liquid assets account for 21 percent of total assets, enough to cover up to 33.4 percent of non-bank deposits.

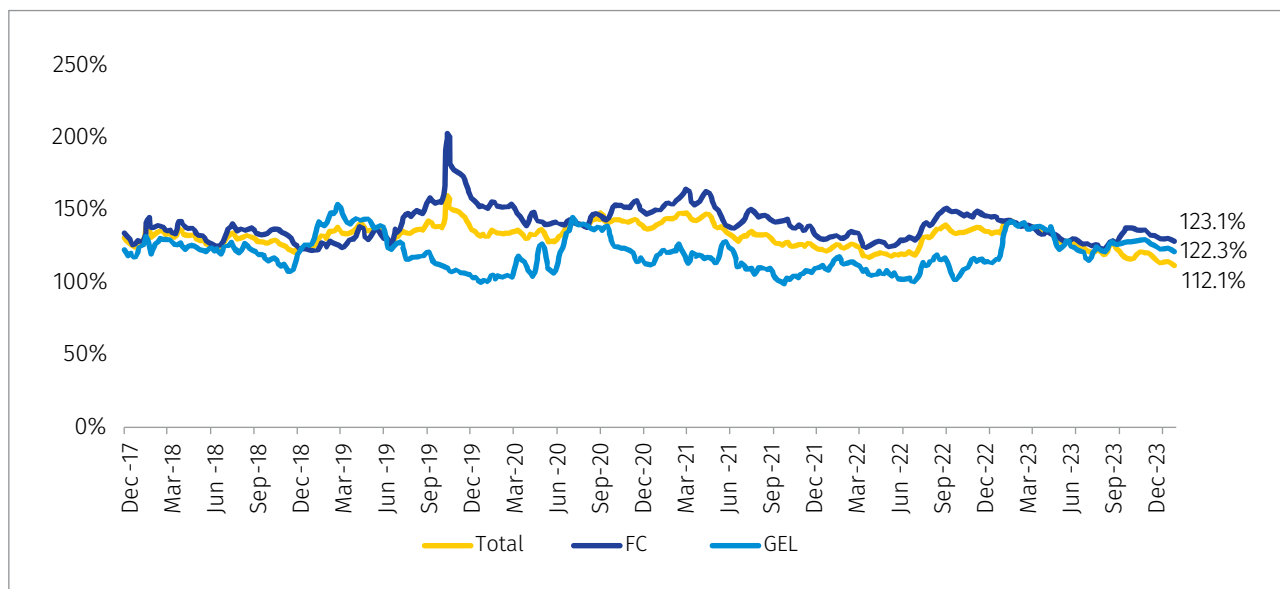
Diagram N 4.26 Level of Liquid Assets



Source: NBG

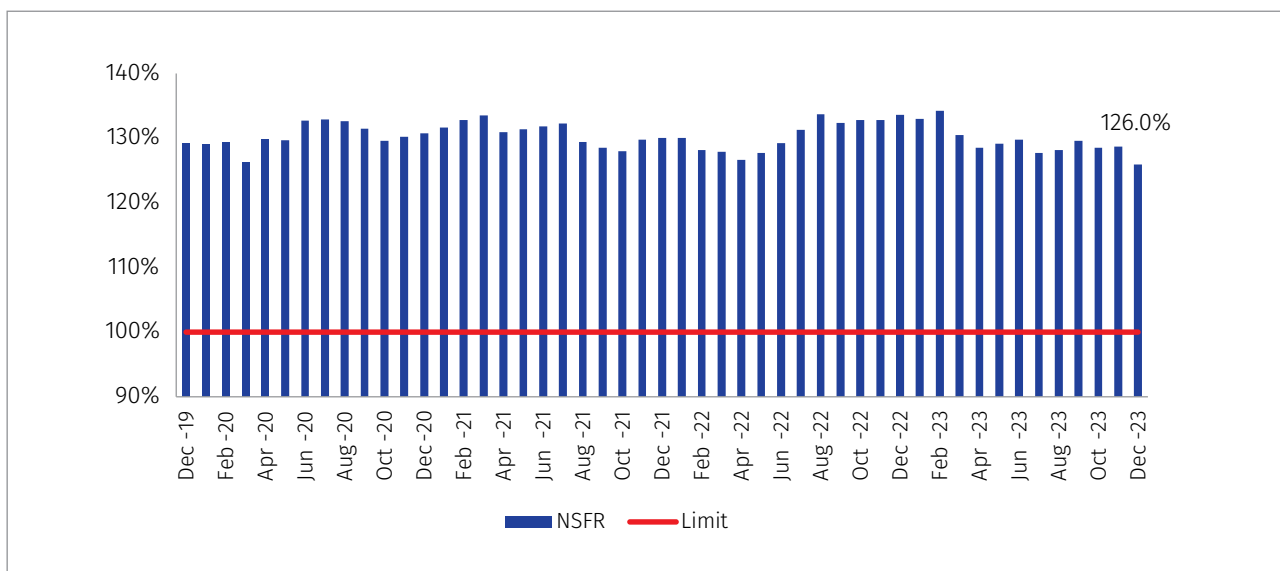
The liquidity coverage ratio (LCR) for 2023 remained at a high level. The Net Stable Funding Ratio (NSFR) also remained high and stood at 126 percent at the end of the year.

Diagram N 4.27 Dynamics of LCR Ratio (10 day floating average)



Source: NBG

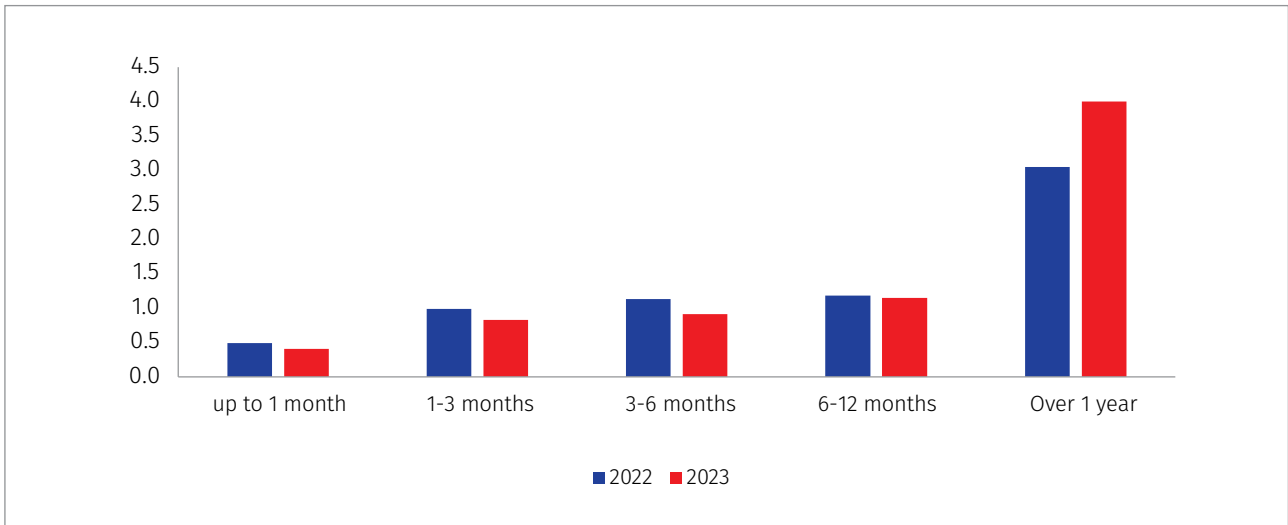
Diagram N 4.28 Net Stable Funding Ratio\*



Source: NBG

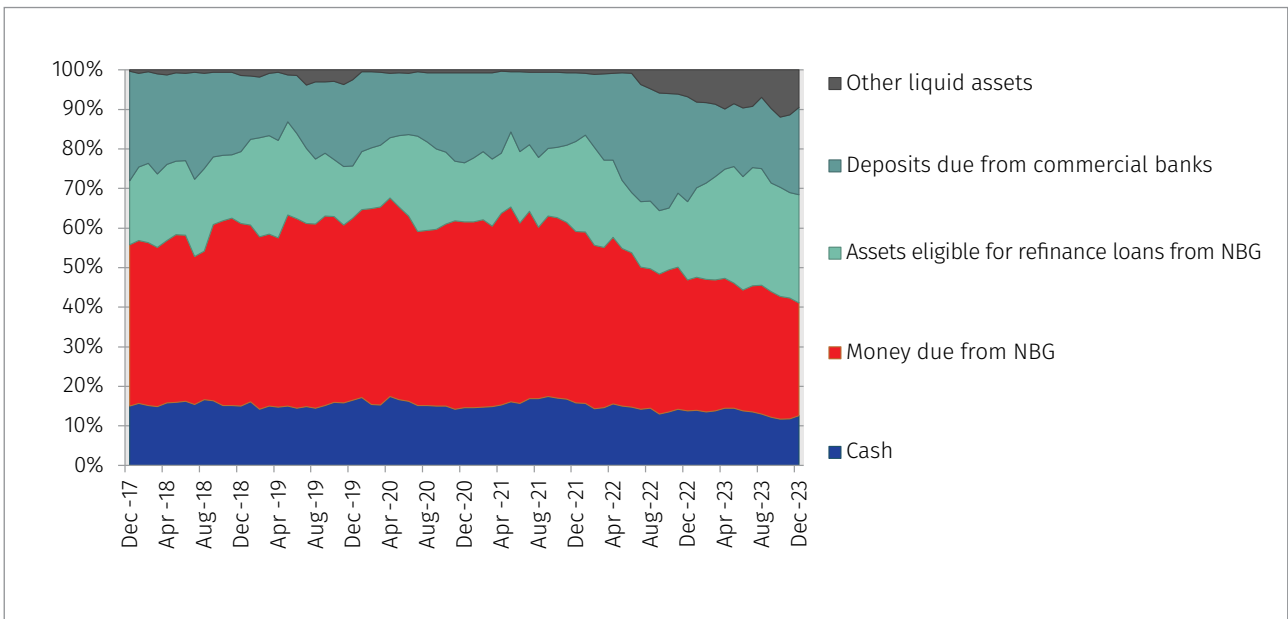
In 2023, the liquid asset gap structure remained stable for both up to 1 year and more than 1 year time baskets.

Diagram N 4.29 Liquidity Gap – Assets to Liabilities ratio



Source: NBG

Diagram N 4.30 Volume and structure of liquid assets



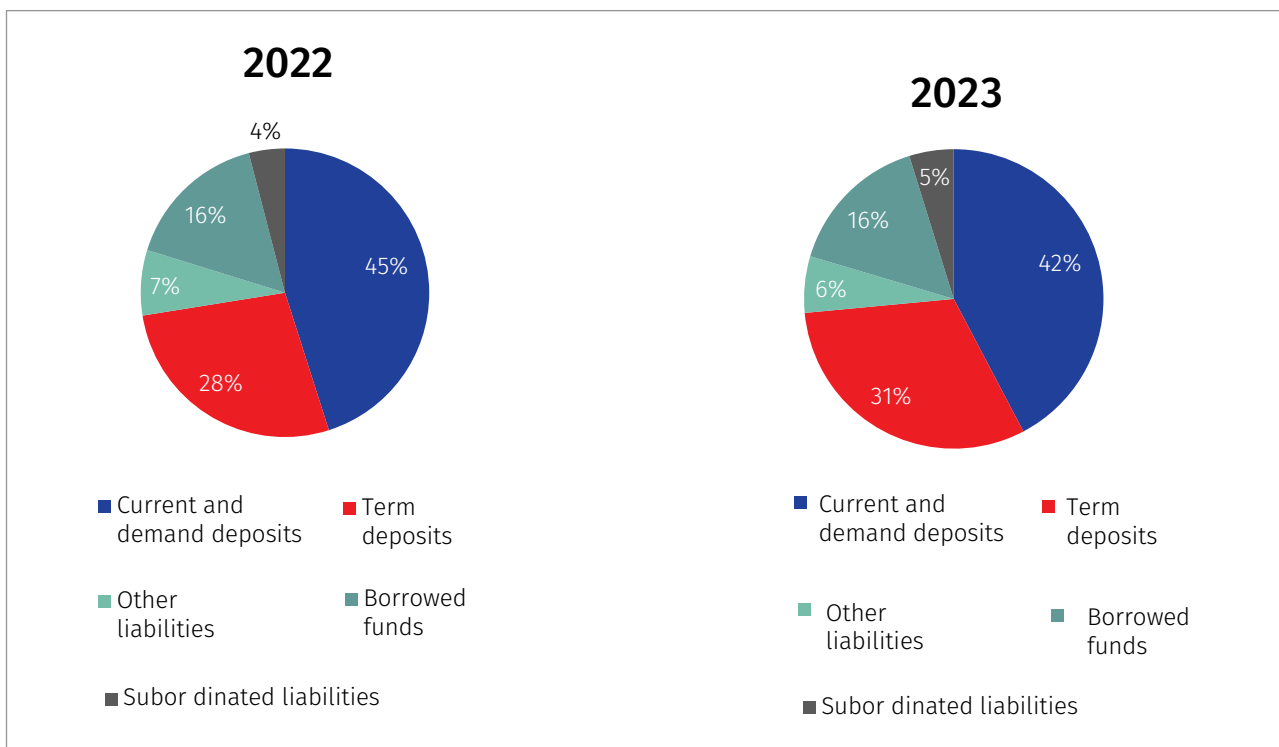
Source:NBG

### 4.8.2 LIABILITY STRUCTURE

The liability structure remains stable. Compared to the previous year, the share of current and demand accounts has slightly increased. The share of borrow-

ings is unchanged and the share of term deposits is slightly reduced. At the same time, banks maintain a fairly comfortable level of liquid assets equivalent to the risks of the liability structure.

Diagram N 4.31 Liability Structure

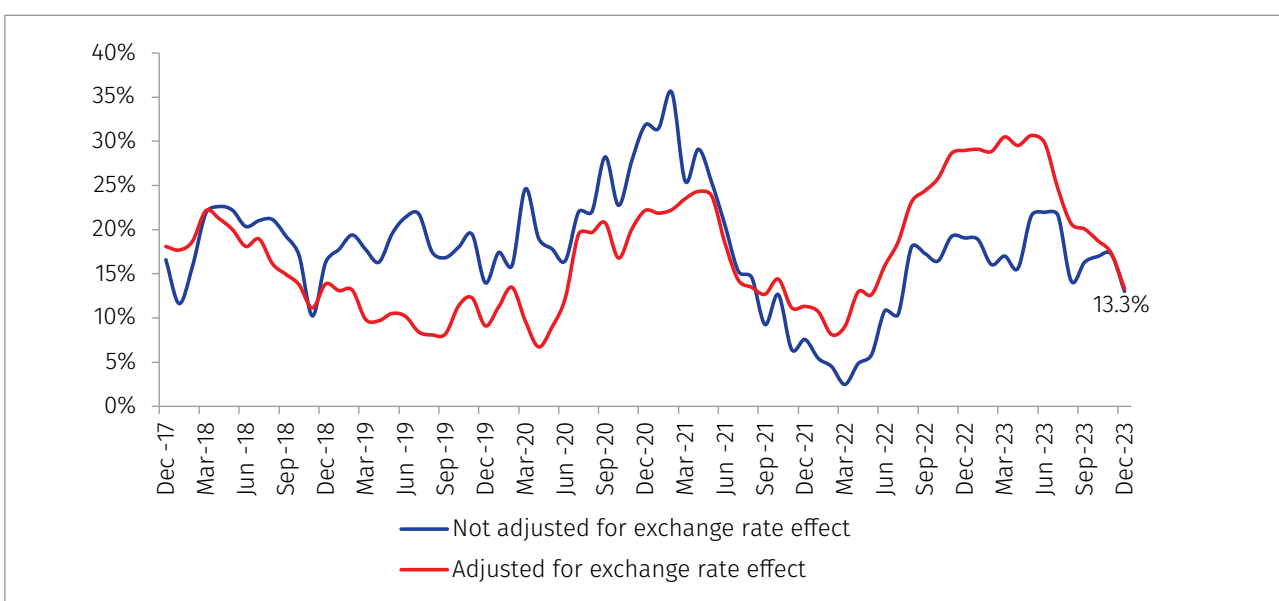


### 4.8.3 RETAIL FUNDING

During 2023, non-bank deposits increased by GEL 5.8 billion (13 pp, 13.3 pp net of the effect of the exchange rate) and amounted to GEL 50 billion by December. By depositor structure, the growth of deposits of individu-

als and legal entities was 15.1 percent and 13.3 percent, respectively (15.5 and 13.5 percent, respectively, net of effect of the exchange rate). During 2023, the deposit larization increased and reached 49.6 percent by the end of December.

Diagram N 4.32 Annual Growth of Non-bank Deposits

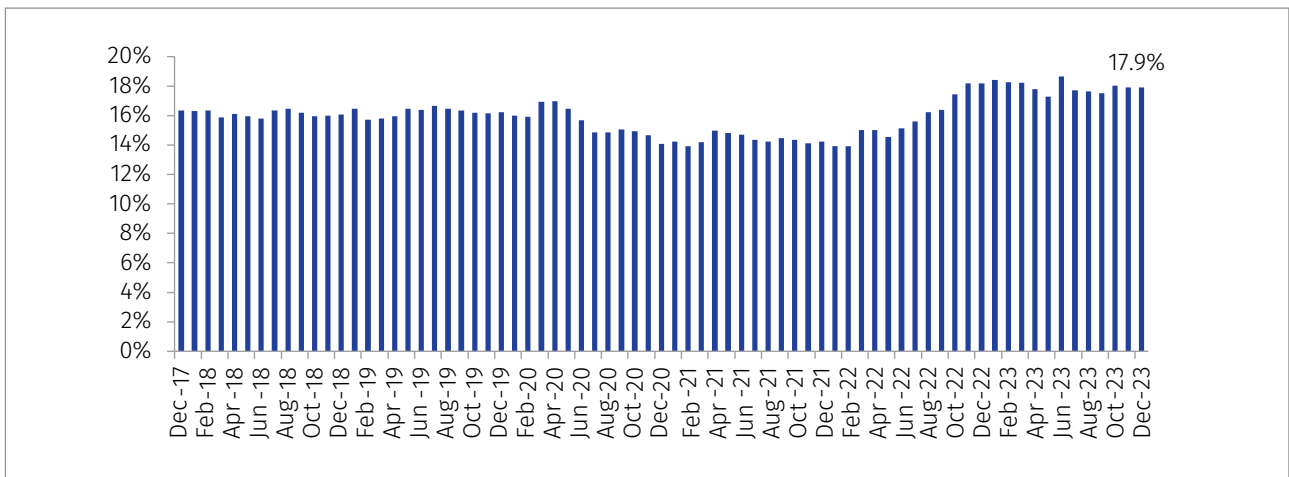


Source: NBG

The share of deposits of non-resident customers in total non-bank deposits decreased by 0.3 pp during 2023 and reached 17.9 percent by the end of December. By origin, the share of Russian residents in the total deposits of non-residents has increased to 38 percent, although in total these deposits are still diversified, both by countries and types of deposits, and that is

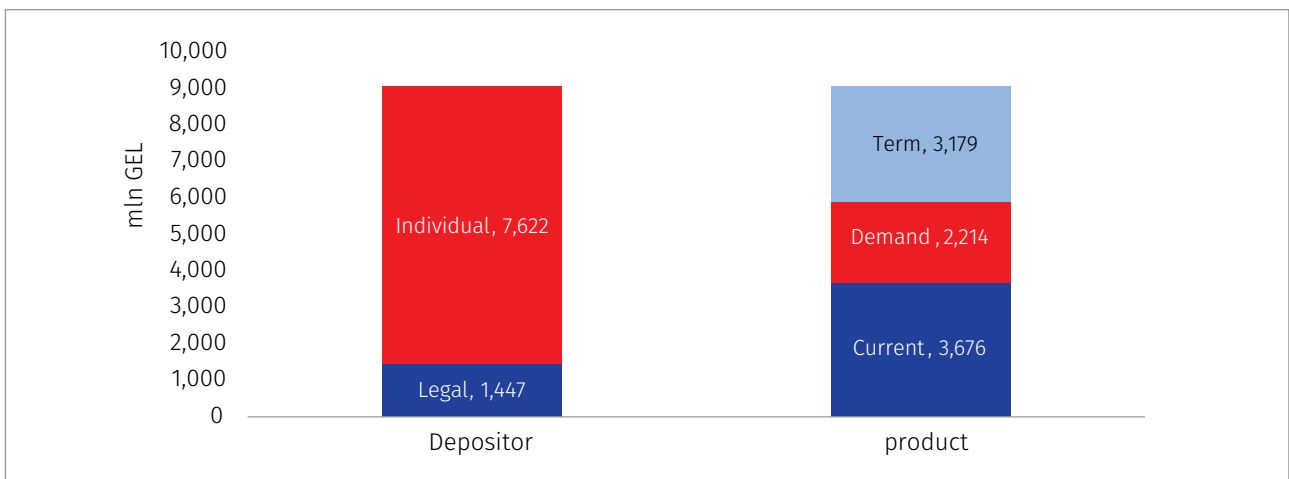
a positive factor in terms of riskiness. In order to prevent excessive dependence on this type of funding, the National Bank of Georgia maintains an additional liquidity requirement for deposits raised from non-residents<sup>58</sup>. The need for additional liquidity in banks with a high share of non-resident deposits reduces the incentive to attract this type of deposit portfolio.

Diagram N 4.33 Share of non-resident depositors



Source: NBG

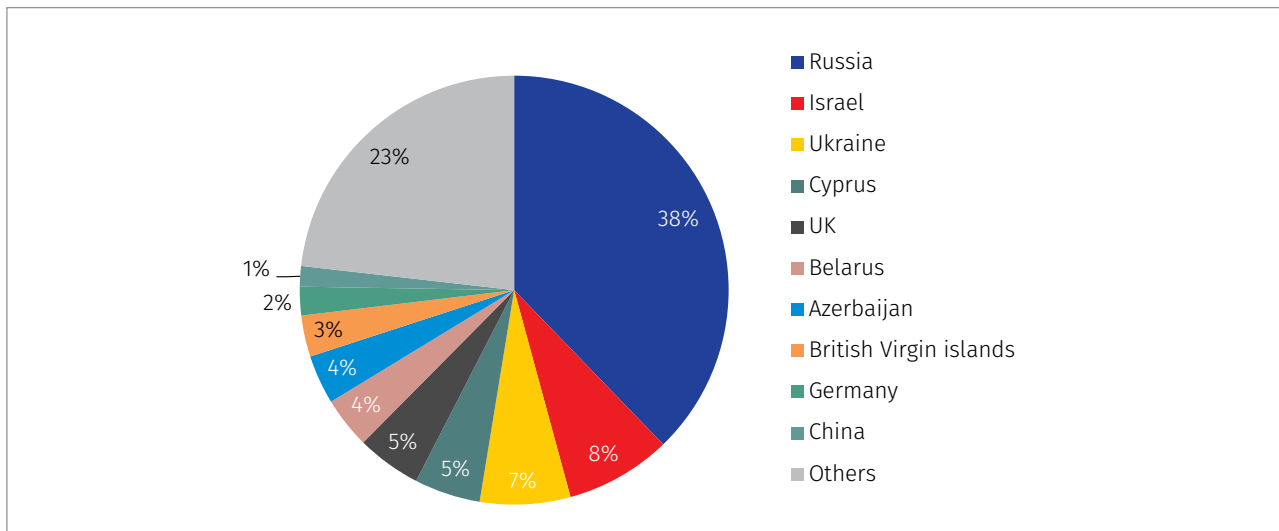
Diagram N 4.34 Share of non-resident depositors (Dec 2023)



Source: NBG

58. For the purpose of calculating the liquidity coverage ratio and the net stable funding ratio, non-resident deposits are subject to higher liquidity requirements than those of residents.

Diagram N 4.35 non-resident deposits by countries (Dec 2023)



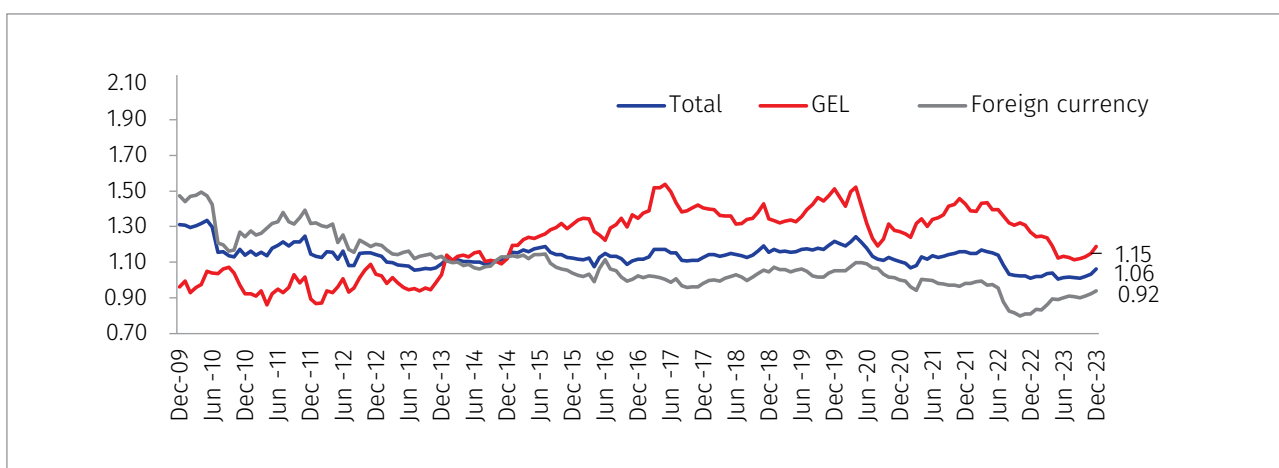
Source: NBG

#### 4.8.4 WHOLESAL FUNDING

The loan-to-deposit ratios during 2023 were overall stable. The ratio increased in foreign currency and decreased in GEL, which is caused by the fact that during the year the growth of deposits in GEL exceeded the growth of loans, and the growth of loans in foreign currency significantly exceeded the growth of deposits.

It is worth noting that the same ratio calculated for loans and deposits in GEL still exceeds the index calculated for loans and deposits in foreign currency, which, to some extent, is caused by the high growth rate of loans in GEL due to currency risks and larization measures.

Diagram N 4.36 Total loans to non-bank deposits ratio by currencies



Source: NBG

Amounts received from external sources of wholesale financing are quite diversified both in terms of the type of lenders and residual maturities. The residual maturity of more than 45 percent of the mentioned financing exceeds 2 years, which reduces the risks of system funding.

The 63.1 percent of wholesale funding comes from international financial institutions, 8.2 percent from parent/affiliated companies, and 28.7 percent from other private institutions. A high share of international financial institutions and a long-term repayment schedule can be considered low risk. For the purposes of managing funding risk, the NBG regularly monitors covenants.<sup>59</sup>

Table N 4.7 External sources of wholesale funding and their repayment schedule as of December 2023

month	<1	1-3	3-6	6-12	12-24	24-36	36-60	>60	ჯამი
sum	5.9%	5.0%	11.6%	12.9%	18.5%	10.5%	22.0%	13.7%	100.0%
International Financial Institutions	1.8%	4.0%	1.8%	7.1%	13.5%	6.8%	16.6%	11.5%	63.1%
Parent/affiliate financial institutions	0.9%	0.0%	0.7%	0.8%	1.0%	2.2%	2.2%	0.4%	8.2%
Other private funding	3.3%	0.9%	9.0%	4.9%	4.1%	1.4%	3.2%	1.8%	28.7%

Source: NBG

## 4.9 MACROPRUDENTIAL RISKS



The National Bank of Georgia continues to monitor systemic risk indicators that may have a material impact on the banking sector. Information about these risks is also provided in different chapters of this report. The main challenge in this regard last year was again to assess the risks to the stability of the financial sector arising from the uncertainty in the region and to develop and implement appropriate macroprudential and supervisory policies.

The National Bank of Georgia performs macroprudential supervision in the following main areas: increased debt burden for non-hedged borrowers due to foreign currency loans; overindebtedness of the vulnerable part of the population; fierce competition in business and mortgage lending amid imperfect pricing mod-

els; cyber risks and scams across the system; potential growth of non-regulated financial intermediation based on financial technologies; threats in the region, etc. During 2023-2024, several important decisions were made for mitigating these risks:

- According to the decision of the Financial Stability Committee, the countercyclical buffer accumulation schedule was changed: commercial banks will have to accumulate a countercyclical buffer according to the following schedule: 0.25 percent by March 15, 2024, 0.5 percent by March 15, 2025, 0.75 percent by March 15, 2026, 1 percent by March 15, 2027.
- According to the decision of the Financial Stability Committee, the maximum term of consumer loans was increased from three to four years.
- The National Bank of Georgia has set an additional requirement for regulated financial institutions to grant new foreign currency loans to individuals

59. limitations set under loan agreements.



The National Bank of Georgia maintains a prudential approach to credit risk caused by currency mismatches. More specifically, the requirement of additional capital applies to foreign currency loans issued to non-hedged borrowers, while in the case of individuals, there are more conservative additional credit standards imposed. To support the larization of liabilities, the NBG uses more preferential requirements for liquidity and minimum reserves on the national currency.

## 4.10 OPERATIONAL RISK



Operational risk is the risk of loss arising from faulty or inefficient internal processes, people, systems, or events. Beyond these factors, the Russia-Ukraine war remains a significant concern this year, having a large-scale impact on the world and heightening operational risks within the financial sector. One of the primary risks in operational risk management is business continuity risk, along with cyber risk and the modern challenges related to cybersecurity management. The National Bank of Georgia is actively working with commercial banks on business continuity management principles and appropriate planning. Additionally, the National Bank of Georgia focuses on various critical components of business continuity management, including infrastructure soundness and business continuity plan testing. It is important for banks to continuously ensure business continuity by various scenarios, which also includes outsourcing (including cloud services).

It is equally important for the financial sector and banking systems to focus on their recovery plans. The NBG continues to monitor the testing of commercial banks' business continuity plan, with particular emphasis on the continuity of employees and smooth operation of critical processes. The operational risks function of the NBG is involved in the assessment of the recovery plan of commercial banks. In 2023, NBG continued to evaluate the operational and cyber risk management frameworks of commercial banks in a hybrid mode.

To monitor the commercial banks evaluated last year, NBG continuously assessed the current statuses of the supervisory requirements issued to them.

NBG actively worked on digital banks and new supervisory entities, such as microbanks. The Operational Risk Department developed regulations related to operational risk management, which were published on the National Bank of Georgia's website. NBG continues to oversee the implementation of the operational risk management framework with digital and microbanks.

As remote services and digitization processes expand in the financial sector, introducing and constantly improving control mechanisms for fraud and technological risks is essential. Over the past year, operational risk supervision has been actively involved in studying and assessing operational and cyber risks related to open banking, digital banking, remote identification of individuals, and electronic signature processes in the banking sector.

A significant number of commercial banks have begun to implement electronic signature processes. Currently, two electronic signature options are offered: 1. Qualified electronic signature, and 2. Advanced electronic signature. The electronic signature is a novelty for banks at this stage and has become a contributing factor for remote services. Its implementation is a step forward for financial organizations, although the risks accompanying the electronic signature process must be considered. Therefore, this process needs to be studied in practice.

The National Bank of Georgia pays great attention to raising awareness of operational risks in the financial sector of Georgia, expanding operational risk management and developing supervisory principles. Banks were advised to do awareness raising for both bank employees and customers. Furthermore, as part of promoting digitization among various non-banking financial institutions, startups, and financial technology

providers, NBG actively shares recommendations on the implementation of operational risk management practices and conducts evaluations.

The National Bank of Georgia, in collaboration with commercial banks, continues to ensure that banks have appropriate and flexible control mechanisms in place. This includes developing and implementing enhanced fraud monitoring tools and information systems, such as behavior-oriented analytical management systems. One of the key priorities for the National Bank of Georgia is the development of processes for detecting and preventing various types of fraud related to payment cards and digital channels.

To provide timely information and prevent major operational events, including the systemic spread of cyber risk, an information sharing and analysis center has been introduced. This center is actively used as a closed communication platform with the commercial banks of Georgia.

In 2023, expanding operational risk forecasting tools remained a priority. In this context, operational risk stress tests are being studied and researched, which provide the opportunity to determine the expected impact of events on an organization's capital and financial condition and to mitigate these effects in negative scenarios. Consequently, recording and refining historical data on potential or real operational risk losses, performing cause-effect analysis of operational risk events, and assessing systemic impacts have become increasingly important.

The National Bank of Georgia emphasizes the importance of data quality and accuracy in the banking sector. In line with this, operational risk loss accounting

and reporting guidelines were published and put into effect. Additionally, principles for effective risk data aggregation and risk reporting are being developed.

The NBG continuously assesses the accuracy, integrity, and quality of financial data within the banking sector. As part of data quality management, the focus is on ensuring smooth business processes related to financial reporting, enhancing analytical tools, increasing the level of automation in reporting processes, and reducing the complexity of related information systems.

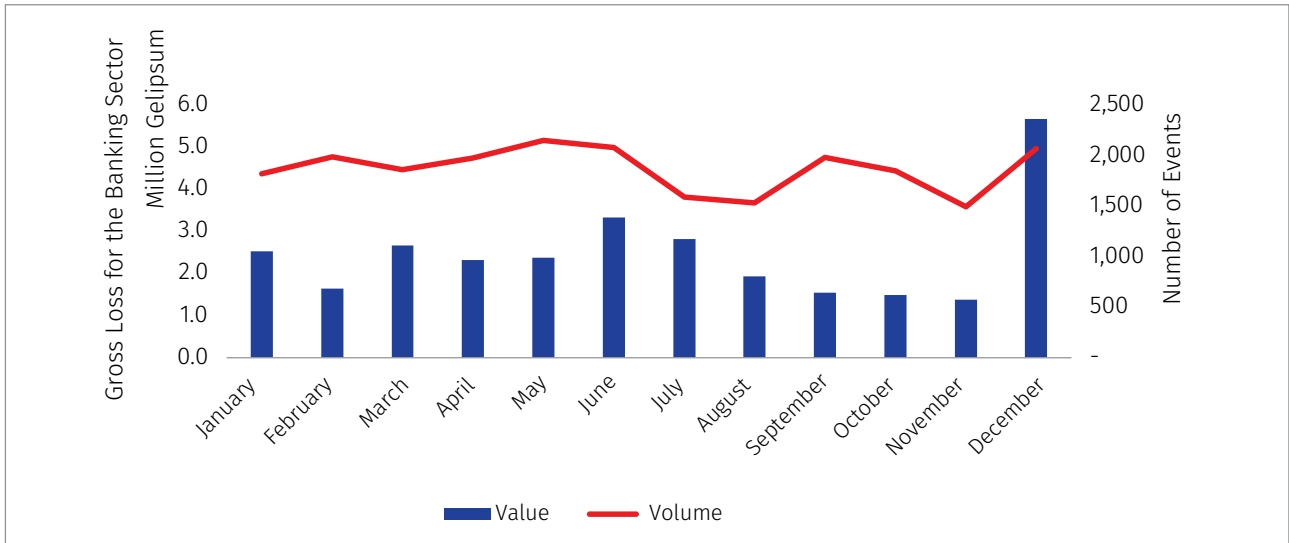
#### 4.10.1 OPERATIONAL RISK IN GEORGIA'S BANKING SECTOR

The local banking system offers relatively low complexity in its banking products and services. However, there is a noticeable trend towards increased reliance on information systems, which consequently elevates the operational risk within the financial sector. Like in 2022, 2023 saw a significant quantitative growth in digital services. This growth aligns with the future strategies for digitizing the financial sector.

In 2023, the total operational losses of commercial banks of Georgia amounted to 29.7 million GEL, which was 32% less than the total losses in 2022. The gross losses relate to the initial amount of the operational event prior to any reimbursement of operational losses.

In 2023, there were 22,408 operational loss events, which is 10 percent less than in 2022. It should be noted that under the operational risk reporting of the National Bank of Georgia, the commercial bank is obliged to record all operational loss events, the total loss of which is equal to or greater than 10 GEL. Diagram N 4.38 shows the dynamics of total operational losses in 2023.

Diagram N 4.38 Total losses for banking sector in 2023

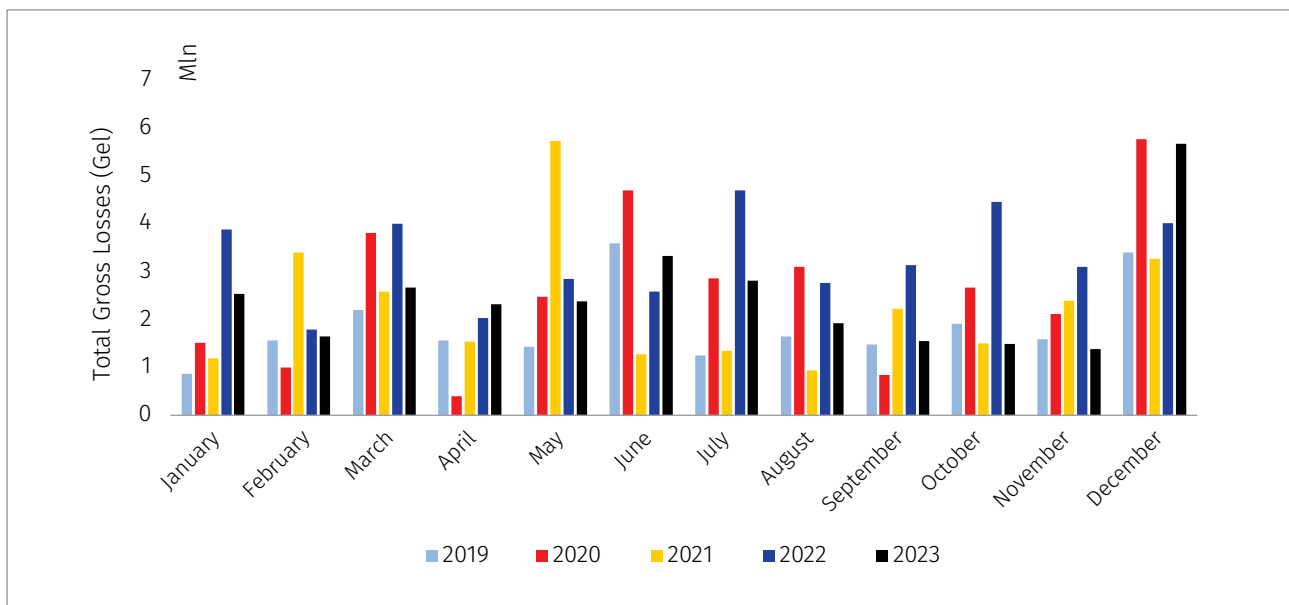


Source: NBG

Diagram No. 4.39 shows the dynamics of total operational loss over the last five years (2019-2023). Historically, December records more operational events than

other times of the year, which is largely related to the end of the reporting year.

Diagram N 4.39 Total operational losses for the last five years (2019-2023)

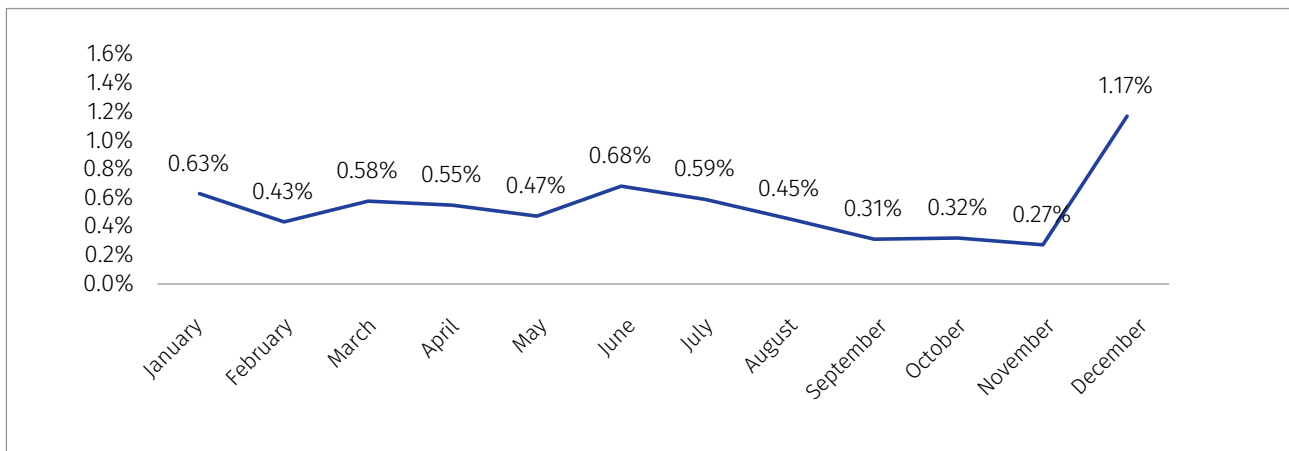


Source: NBG

Operational risk loss indicator is one of the best measures to determine the operational risk of the financial system. This indicator is calculated by the ratio of the total operational loss of the financial system to the total income. In 2023, the ratio of total annual gross

losses to gross income calculated under Basel II was 0.54 percent. Diagram No. 4.40 shows the dynamics of the operational loss indicator of the Georgian banking sector by months.

Diagram N 4.40 Dynamics of the operational loss indicator in 2023 (total loss to total income)



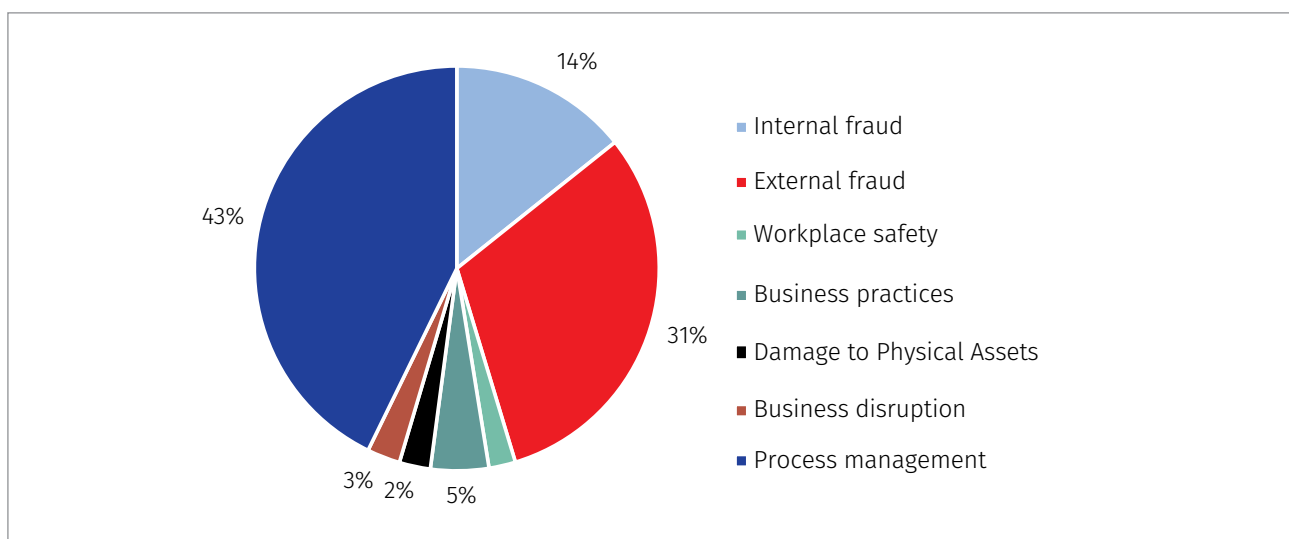
Source: NBG

In 2023, as in 2022, operational losses were mainly recorded in the retail banking services and, to some extent, commercial banking services. The retail banking business line, along with direct retail banking, also includes operational losses related to payment cards.

Looking at operational losses by event categories, one would observe that the category of process manage-

ment recorded the largest share of losses in terms of amount (43 percent of total losses), while external fraud was the second largest category (31 percent share). The proportional increase in external fraud compared to the previous year is due to one major event of external fraud. The structure of operational losses in 2023 is shown in Diagram No. 4.41.

Diagram N 4.41 Distribution of total loss of the banking system for 2023 by categories of events



Source: NBG

## 4.11 CYBER RISK



The relevance of cybersecurity as a type of operational risk is increasing in the wake of digital transformation and reliability concerns. International financial institutions continue to identify cyber risk as the biggest threat to the financial sector. Notably, the 2023 report by the International Monetary Fund, which addresses the protection of financial stability amidst high inflation and geopolitical risks, mentions that non-traditional risks, such as cyber risks, are increasing due to geopolitical tensions, thereby threatening financial stability.

In 2023, one of the most important issues in Georgia's financial sector was the proper management of risks originating from third parties. The Cyber Risk Supervision Team of the NBG issued extraordinary supervisory instructions and warnings, aiming to require commercial banks to take additional measures and ensure the cyber and information security of third parties. In addition, the NBG's Cyber Risk Oversight Team conducted one of the most important third-party audits of the financial sector's cyber and information security practices. As remote service channels are evolving, ensuring and maintaining cyber security at an appropriate level is still one of the most important challenges for the financial sector. The National Bank of Georgia continuously observes the current events in the banking sector and monitors cyber risk, to be able to respond to cyber attacks, when identified, in a timely manner, eliminate and analyze them and make sure to immediately notify the entire banking sector.

Supervisory requirements of cyber security were introduced in the banking sector in 2019. Based on these, the National Bank of Georgia provides monitoring and supervision of the implementation, maintenance and continuous improvement of the cyber security management framework in the banking sector.

During 2023, the Cyber-Risk Supervision Division performed cyclical assessments of commercial banks to

determine compliance with the above framework. Assessments were mostly conducted remotely, with actual visits only to check data warehouses. A number of findings and shortcomings were identified and mandatory requirements and recommendations were developed.

Considering the current challenges and context, the main areas for improvement included formalizing cyber and information security policies and procedures, improving risk management practices, including managing cyber and information security risks from third parties, the effectiveness of the processes and technological solutions implemented for the purpose of information protection, constant attention to raising awareness and empowering of human resources employed in information and cyber security with appropriate competencies. It is also important to have effective business continuity and vigilance plans in place in the event of a potentially large-scale cyber incident.

In addition to the above supervisory requirements, commercial banks are additionally required to conduct audits of information systems and penetration testing of said systems, which serves to eliminate weaknesses and reduce cyber risks. Accordingly, the National Bank of Georgia gives special importance to conducting appropriate field tests/audits and quality control.

Availability of effective processes and mechanisms for managing cyber incidents is one of the important components of cyber security oversight. The Cyber-Risk Supervision Division continues to analyze the mandatory reports on cyber incidents from commercial banks and produce quarterly reports, which allows the dynamics of cyber incidents trends to be seen both for an individual bank and for all banks.

The banking sector was a target for the so-called Denial of Service (DDos) attacks through 2023, similar to the previous year: these involve hackers stealing users' confidential and sensitive information and then using it for their own purposes (phishing) or after some time interrupting the services of commercial banks (DDos

attacks). The National Bank of Georgia, together with commercial banks, has been intensively working to improve appropriate control mechanisms to prevent similar incidents.

Having up-to-date information about cyber threats and sharing it among stakeholders is a recognized important practice that serves to effectively manage cyber risk. The NBG used a portal to share information on cyber threats in 2023, to inform commercial banks. The platform provides an opportunity for members to share timely, accurate and actionable cyber threat information. Sharing cyber threat information on the platform helps platform members gain knowledge of current trends, anticipated threats, and past experiences that can be used for prevention of cyber risks.

Cyber security awareness raising campaigns for the financial sector and consumers were implemented in 2023. The financial sector continued to participate in the international campaign organized by the National Bank of Georgia. Cyber Security Awareness Month was organized for the second time in Georgia in 2023. Events were organized by the NBG and commercial banks, including competitions, conferences, educational videos and others, supporting awareness of cyber security among the citizens.

The Georgian legislation on information security was updated in 2021, and entered into force in 2022. The NBG's cyber risk supervision team, in the process of authorization of companies performing information security audits and penetration testing for systemic banks, fulfilled the obligation assumed under the law.

#### 4.11.1 REGULATORY ACTIONS ADDRESSING CYBER RISKS

The National Bank of Georgia developed the Guide for the Audit of Information Systems and Cyber Security Management Framework in Commercial Banks, with the goal of developing the supervision function and

regulatory instruments. This document ensures the effectiveness and quality of the assessment of information systems and cybersecurity frameworks.

The NBG pays particular attention to the quality of audit findings and the subsequent correction of deficiencies identified in these findings by supervisory entities. Consequently, monitoring post-audit measures by the NBG is used as an additional supervisory tool in practice.

In recent years, the financial sector, especially banking institutions, have been using cloud outsourcing services. From August 1, 2023, the decree of the Acting Governor of NBG "On the use of cloud outsourcing services by financial organizations" came into force. The NBG prepared the cloud outsourcing service guideline and shared with stakeholders. The guideline contains the preventive requirements. When fulfilled in a timely manner, these support the the supervisory entities in managing the challenges/risks related to the cloud environment. The guideline imposes a number of requirements on financial institutions related to the preliminary evaluation of cloud outsourcing service providers, as well as the assessment of critical and/or important functions, assessment of cyber and information security risks, the acquisition of appropriate industry credentials, the realization of audit and supervision rights, monitoring and exit strategy.

In 2023, the decree of the Acting Governor of the National Bank of Georgia on "Approving the Cybersecurity Management Framework of Microbanks" was issued, with the "Guidelines for the Audit of Information Systems and Cybersecurity Management Framework in Microbanks" as an appendix. Based on the decree, a plan-schedule for ensuring cyber and information security requirements was developed for the entity wishing to be licensed as a microbank. The Cyber Risk Oversight Team actively communicates with the applicant entities.

Adequately ensuring cyber and information security requirements for licensing as a digital bank is still a pressing issue. In 2023, a package of key requirements was developed by the NBG's cyber risk supervision team, the status of which is being actively monitored by a designated team.

The year 2023, like the previous one, was marked by the introduction of new products and services in the financial sector, which are increasingly reliant on information systems. Consequently, the Cyber Risk Supervision Team continued to play a crucial role in the study and proper evaluation of these new products.

The National Bank of Georgia has established a procedure for the registration, cancellation of registration, and regulation of the Credit Information Bureau within the National Bank of Georgia. Among other requirements, these rules set specific information systems standards for the bureau and the platform. In 2023, the Cyber Risk Oversight Team issued numerous recommendations to organizations seeking platform registration, focusing on regulating information security policies and procedures and ensuring the security of information systems. Special attention was given to professionally conducted audits and penetration tests, with their reports being utilized for further improvements.

Given the growing importance of cyber security, the National Bank of Georgia emphasizes the need for cyber security specialists with strong competencies and proper career development support. Throughout 2023, the Cyber Risk Supervision Team participated in various industry seminars and trainings. Notably, team members hold internationally recognized industry certifications, underscoring their expertise and commitment to maintaining high standards in cyber risk management.

## 4.12 DEVELOPMENT OF FINANCIAL AND SUPERVISORY TECHNOLOGIES

### 4.12.1 PROMOTING FINANCIAL INNOVATIONS

The speed of innovation in the financial sector is increasing, which brings new opportunities as well as new risks. The financial sector remains the most regulated economic sector in the world, and its regulation continues to grow. As a result, the modern supervisory framework is quite technical and complex, especially for new financial startups. It is thus an important challenge for financial sector regulators to encourage innovators with Fintech ideas whilst at the same time supporting the transformation of these ideas into sustainable financial models. In response, the NBG is paving the way to the availability of basic Fintech infrastructure by developing various supervisory tactics.

#### **Financial Innovations Office** <sup>[1]</sup>

The Financial Innovations Office is the bridge between the NBG and the financial innovator community. The mission of the Innovation Office is to facilitate responsible innovation in the financial sector and to assist fintech organizations/startups in learning about the National Bank of Georgia's regulatory approach.

During 2023, the Financial Innovations Office facilitated numerous important meetings with individuals presenting innovative ideas. With the support of the Innovations Office, the first digital bank license was issued in 2022, making Paysera Bank Georgia the first digital bank. Several other license applications were received, and in 2023, two more licenses were issued to Hash Bank and Pave Bank Georgia. There remains one application under consideration, indicating that the active work on licensing digital banks will continue into 2024. Regarding innovations in the financial sector, the Inno-

[1] Information on the Financial Innovations Office is available in section of the NBG website <https://nbg.gov.ge/en/page/supervision>

vations Office maintained close contact with USAID, the German Economic Team (GET), BaFin, GFin, and other organizations throughout the year. This collaboration was aimed at staying abreast of new developments and supervisory approaches, ensuring that the National Bank of Georgia remains at the forefront of financial innovation and regulatory best practices.

### Regulatory Sandbox

The Regulatory Sandbox is an important tool for promoting financial innovation that allows for real-time testing of innovative products and services. In 2023, the innovative remote identification service of one entity was tested in the real environment of the regulatory sandbox. Also, at the end of the year, 3 new projects were submitted to the regulatory sandbox for review: "Issuance of loans secured by crypto-currencies"; "Implementation of online currency exchange"; "Credit Information Bureau - Platform".

In 2023, the evaluation of fintech business models developed worldwide was undertaken, leading to the identification of several promising fintech business models with significant additional benefits for end users, based on the so-called mapping framework. To promote the development of these innovative business models, two "targeted sandboxes" were announced: one for "implementation of online currency exchange" and another for "implementation of escrow services by non-banking institutions."

The targeted sandbox for online currency exchange was announced in June 2023. By the end of the year, the NBG had already received one application, with several companies' projects in the preliminary discussion stage. Interest in the escrow service is high, and applications will be accepted starting January 2024, coinciding with the announcement of the targeted sandbox for this service.

### Digital GEL

The the central bank digital currency (CBDC) of is quite relevant for the majority of central banks at the cur-

rent stage. The characteristics and technological aspects of digital currencies differ by country depending on the purpose. The National Bank of Georgia publicly announced its interest in digital currency in April 2021 and invited fintech companies to cooperate. In 2022, the NBG continued to communicate with technological companies that expressed their desire to join the digital GEL project. The digital GEL project is still under consideration. The *Central Bank Digital Currency and Decentralized Finance Conference*, a joint event of the Innovations Office and USAID, was held in Tbilisi On May 4-5, 2022. Top technology companies were in attendance. The technological requirements that the digital GEL technology should meet in the pilot mode were specified after the conference. The characteristics of the digital GEL pilot mode were specified and the launch of the pilot mode in 2023 was planned.

In 2023, the National Bank of Georgia initiated a pilot project with Ripple, a technology company, to explore four trial use cases over the next year and a half. These cases include:

1. Payroll management
2. Tokenization of collectible coins
3. Real estate purchases through smart contracts
4. Tokenization of capital market financial instruments

The project is divided into two phases. The first phase involves developing the project implementation plan, defining the necessary technology and design components, and identifying and attracting potential stakeholders. Key performance indicators (KPI) and intermediate evaluation criteria will be established to assess the project's progress and results.

Additionally, the National Bank of Georgia started collaborating with the BIS Innovation Hub (BISIH) on the digital GEL initiative. The NBG participated in the mBridge and Aurum projects led by the Hong Kong Innovation Center of Basel, gaining valuable insights into Distributed Ledger Technology (DLT) and Central Bank Digital Currencies (CBDCs).

The mBridge project focuses on cross-country payments using a DLT platform, enabling different central banks to issue and transact digital currencies. The Aurum project explores retail digital currencies (CBDCs) and builds technology prototypes for intermediate CBDC and CBDC-backed stablecoin architectures.

Through these collaborations, the NBG benefits from the digital currency experiences of other countries and tests its own CBDC technology. It also gains access to the resources and expertise offered by the BIS Innovation Hub.

In 2023, the National Bank of Georgia signed a bilateral memorandum with the ECB and the Digital Euro Association to share knowledge on digital currencies, work on innovative projects, and implement joint educational programs to raise awareness about digital currencies in public.

The National Bank of Georgia received an international award for the digital GEL project, recognizing it as the CBDC initiative of the year.

### Smart Contracts

Along with the development of blockchain technologies and digital communication systems, interest in smart contracts has surged. Smart contracts, regarded as highly effective tools of digital technology, offer significant benefits to businesses and consumers by leveraging the advancements in digital technologies.

The debate on smart contracts gained prominence with the advent of blockchain and cryptocurrency. Blockchain and smart contracts are recognized methods of data storage, provided they comply with existing legal rules and regulations. Blockchain-based smart contracts are agreements between two parties stored in a blockchain database, often functioning as self-enforcing code.

Due to the growing importance and necessity of understanding smart contracts, the National Bank of Georgia, in collaboration with USAID, began researching smart contracts in 2023. The research focuses on identifying

the legal challenges and limitations present in the Civil Code or other legal acts, and on exploring global best practices. This research aims to develop a comprehensive understanding of the challenges associated with smart contracts in sectors such as banking, insurance, and real estate.

Moreover, the concept of smart contracts is a cornerstone of the digital GEL ecosystem initiated by the National Bank of Georgia. The ability to utilize these contracts is crucial for various fintech companies to offer innovative products to customers.

Local and international experts, in cooperation with the National Bank of Georgia and supported by USAID, are actively engaged in conducting this research to explore and address the challenges and opportunities presented by smart contracts.

### Credit Registry

The National Bank of Georgia continued collecting credit registry data in test mode in 2023. Also, in order to complete the information and bring it into compliance with IFRS reporting, the credit registry form was updated, the process of verifying the accuracy of the received data was actively underway, and parallel reporting using the data of the credit register started. Developed in consultation with the World Bank Working Group, the Credit Registry is a database that allows the collection of comprehensive information on credit risk. The data filed to the NBG on a monthly basis include the following data sets:

- Loan liability details
- Loan liability collateral data
- Information on refinanced loans
- Information on investments
- Information on rejected loan applications
- Information on loan files closed during the reporting month.

In 2024, it is planned to eliminate errors related to data accuracy, for which methods of comparing credit registry data with data from various reports submitted by commercial banks to the NBG, as well as data from stress tests will be used.

## BOX 6. PRIVACY ENHANCEMENT TECHNOLOGIES (PET)

In recent years, many financial services in Georgia have been created as a result of companies collecting and processing customer data. The use of data has become an important motivation for business development in various areas, including payments and settlements. Along with the growing demand for data usage, the development of privacy enhancement technologies (PET) is necessary. PET is a set of technologies designed to protect the privacy of personal information by providing secure and anonymous ways to access and transmit information. It includes many technologies that differ in features, complexity, computing resource requirements, and more. Among them, the most widespread techniques are: Differential Privacy; Homomorphic Encryption; Federated Learning; Zero-knowledge Proofs.

Privacy-enhancing technologies and their use in payments and financial services may have a significant impact on central bank digital currency research, according to research conducted by central banks in various countries. According to the World Economic Forum report<sup>60</sup>, PET, using new forms of data sharing, can play a major role in opening up new value chains in the financial industry and become an important factor in the process of creating new innovative financial products/services. These technologies may be used in areas such as: AML/CFT, CBDC, Open Banking/Finance, etc.

In March 2023, an OECD study<sup>61</sup> was published that reviews current regulatory and policy approaches to PET, with the aim of helping regulators and policy makers better understand how these technologies can be properly used to protect data privacy and improve overall governance.

The National Bank of Georgia constantly researches new financial technologies and tries to raise awareness in the financial sector by communicating with them frequently about trends and innovations in this field. For this purpose, the National Bank of Georgia has been actively researching international practice in privacy improvement technologies for the past year. In 2023, a meeting was held with representatives of the financial sector, where the results of the research, the essence of this technology, various mechanisms, examples of use today and future prospects were presented. The Financial and Supervisory Technology Department plans to make such meetings regular and proactively present research results to representatives of the financial sector, who will further use and implement privacy-enhancing technologies, which will ultimately improve the stability and efficiency of the payment and settlement system.

Despite its obvious advantages, artificial intelligence also comes with challenges. Among them, the so-called hallucinations when an artificial intelligence model offers contrived, unrealistic and illogical information. Research shows that incorrect or non-existent information generated by artificial intelligence is considered one of the biggest global risks in 2024 (2nd place)<sup>62</sup>. By 2024, Generative AI is expected to further develop and increase the share of automation in industries. The focus will continue to be on the validity and relevance of the content created.

The National Bank of Georgia is actively exploring the possibilities of Generative AI and its use in its activities, both in the direction of developing LLM and other machine learning models.

60. The Next Generation of Data-Sharing in Financial Services: Using PET to Unlock New Value

61. OECD emerging privacy enhancing technologies

62. WEF's Global Risk Report 2024

## BOX 7. GENERATIVE AI

Generative AI is a type of artificial intelligence that can create new content, such as ideas, texts, and images. These AI models have become particularly intriguing and popular among the public. In the financial sector, generative AI is used to introduce automation processes, which are partially or entirely governed by AI models. However, the financial sector's stringent regulations pose many barriers and obstacles, particularly concerning security and privacy risks. The use of AI also involves considerations of robustness and regulatory compliance.

Many leading countries are developing legal frameworks for artificial intelligence. In 2021, the European Union developed, and in 2023 the European Parliament adopted, a legal framework for AI.

AI is also significant in banking supervision. The latest AI models, such as ChatGPT, Gemini, and Claude, have enabled banks to effectively utilize these resources in their operations. This approach benefits both banks and customers by reducing costs and enhancing customer service through automation. Central banks frequently employ AI and machine learning models. Recently, Large Language Models (LLMs) have been increasingly used. Some central banks use these models for social media analysis to investigate and measure public trust in their monetary policy.

### 4.12.2 MODEL RISK

The use of different statistical models for business decision making has become a common practice in the financial sector. Such models are widely used in lending, financial accounting, and risk management. There has been especially large growth in the use of mathematical/statistical models in the area of retail and MSME lending. Recently, models based on machine learning and artificial intelligence algorithms have started to be used more frequently. Although these increase the efficiency of models, they can complicate understanding results, doing analysis and assessing risks.

Current trends in the sector prompted the necessity to develop a framework for the ethical use of the model. To address this issue, the regulation sets out the ethical aspects of model development, implementation and application, and ways to mitigate possible unethical use of the model. This change is implemented for the benefit of customers: there is a risk that a model built without ethical principles may unfairly classify a

certain group of consumers and restrict their rights. The second change concerns the expansion of the risk-based approach: the new amendment offers a methodology for ranking/grouping models by risk. The third change is about the entities using the model ensure the transparency and interpretability of the model by employing the statistical method. This change will restrict model users from using 'black boxes' and shifting responsibility for model results to the model creators.

Models for accounting for expected credit losses in financial institutions following the introduction of the IFRS 9 standard are being introduced at the NBG. Based on their complexity and the impact on the bank's financial position, these models are high risk carriers. In 2023, the analysis of the models and methodologies was started, and feedback has already been made with several banks. In 2024, the analysis of the models will continue and as much as possible, the flaws that can cause the risk of the model will be identified.

### 4.12.3 CREDIT INFORMATION BUREAU/PLATFORM

The NBG has been regulating and supervising the work of the Credit Information Bureau (the Bureau) since 2018. Over the years, the functioning of the Bureau, as well as the entities having a contractual relationship with it, have been supervised. As of December 2023,

there were 250 lending entities and 19 organizations involved on a non-mandatory basis in the contractual relationship with the Credit Information Bureau. The indicator naturally varies depending on the years, and that is affected by the process of periodic registration and cancellation of lending entities.

Diagram N 4.42 Number and volume of current loans (2023)

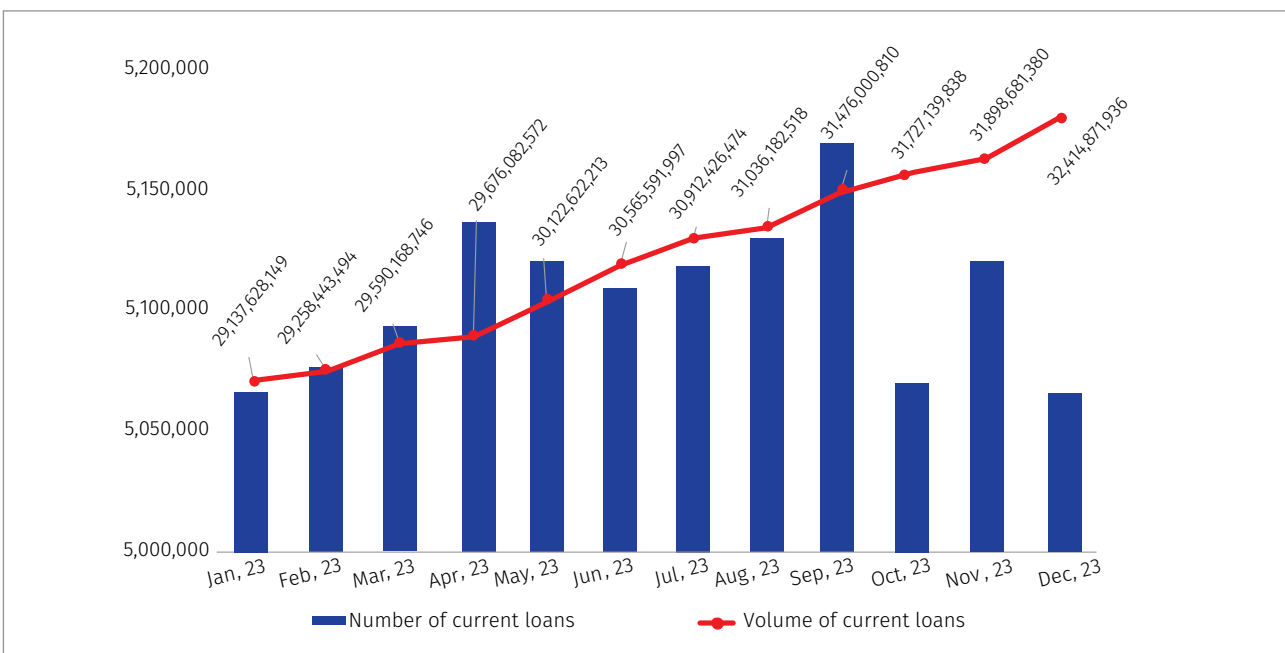
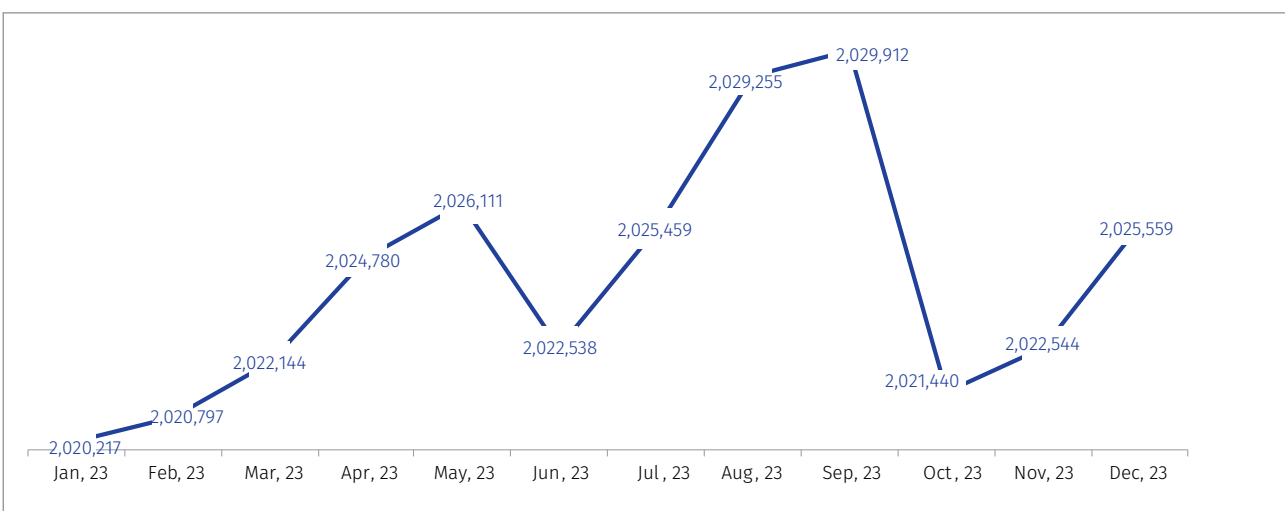


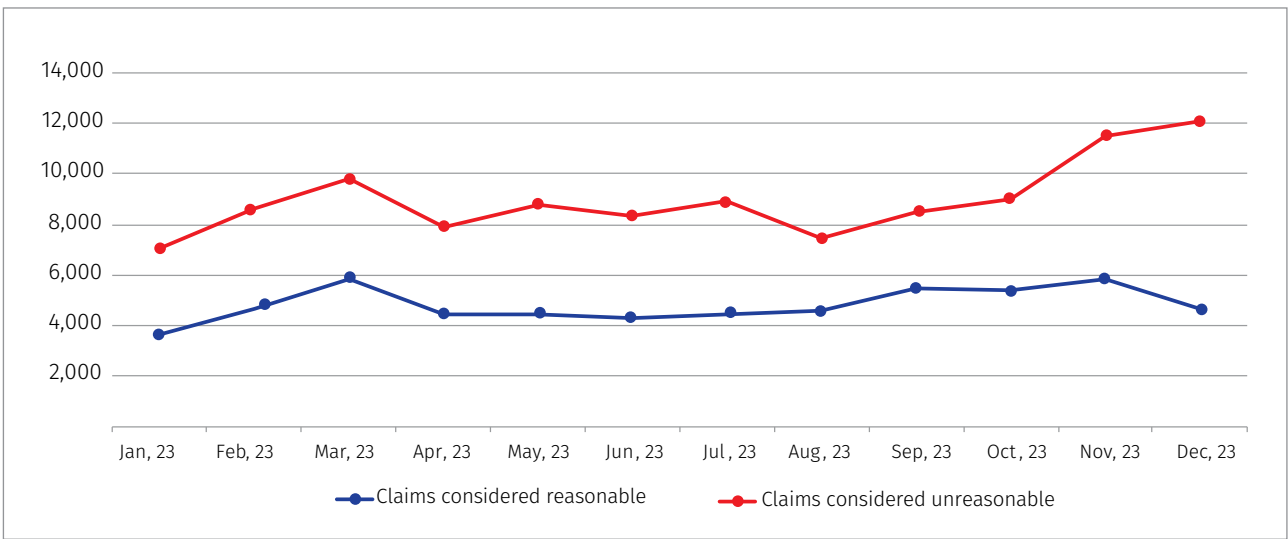
Diagram N 4.43 Unique number of current borrowers (2023)



Protection of consumer rights is very important for the National Bank of Georgia. In order to correctly and fairly reflect their data in the credit information database, the claims registered by them are studied

and appropriately responded to. The number of claims recorded during 2023 by months is presented in the diagram below.

Diagram N 4.44 Number of customer claims (2023)



It is crucial that, during the supervision process, any needs or issues identified through practical experience in the sector are addressed to improve its overall functioning. This may involve revising and amending existing regulations to better suit the current requirements and demands of the industry. In order to promote the development of financial and supervisory technologies, in 2022, with the change in the rules developed for the supervision of the credit information bureau, the National Bank of Georgia allowed the registration of the credit information bureau platform

with different/simplified requirements. By the end of 2023, two platforms have been registered, and several applications are in the pre-review stage.

In addition, following the changes made in the regulations, in 2023, the NBG expanded the database of the Credit Information Bureau with data on the income received from international remittances to simplify the process of obtaining loans for the recipients of remittances, and lending to financial institutions.

Diagram N 4.45 Number of cashed international remittances (2023)

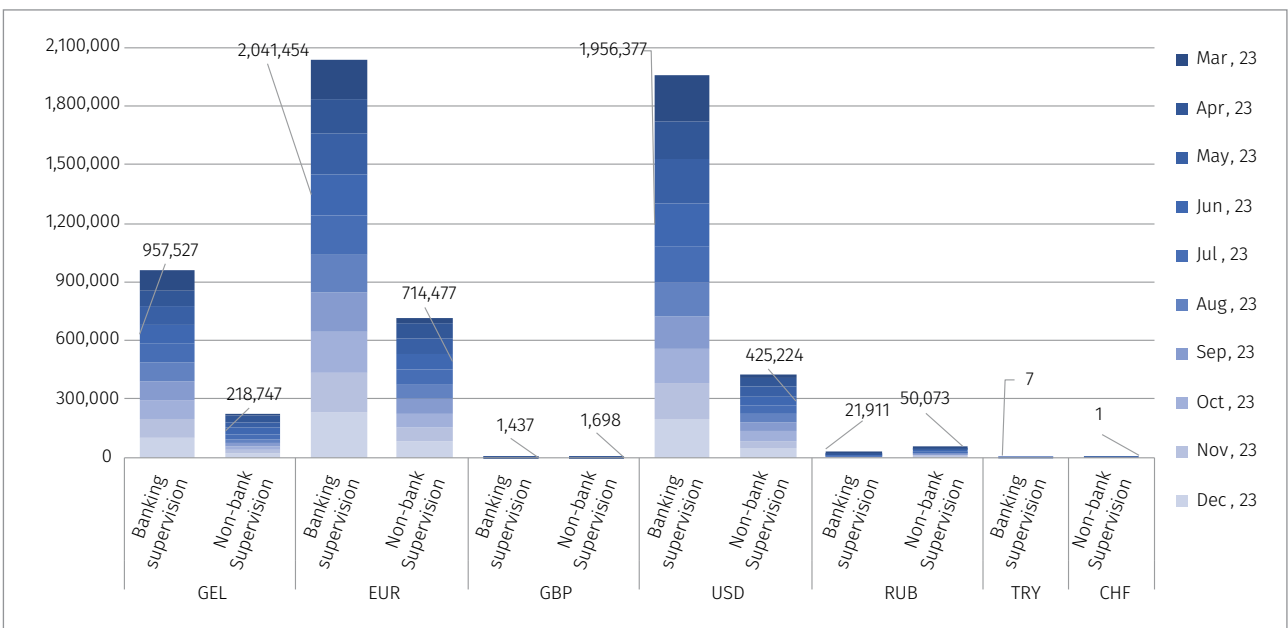
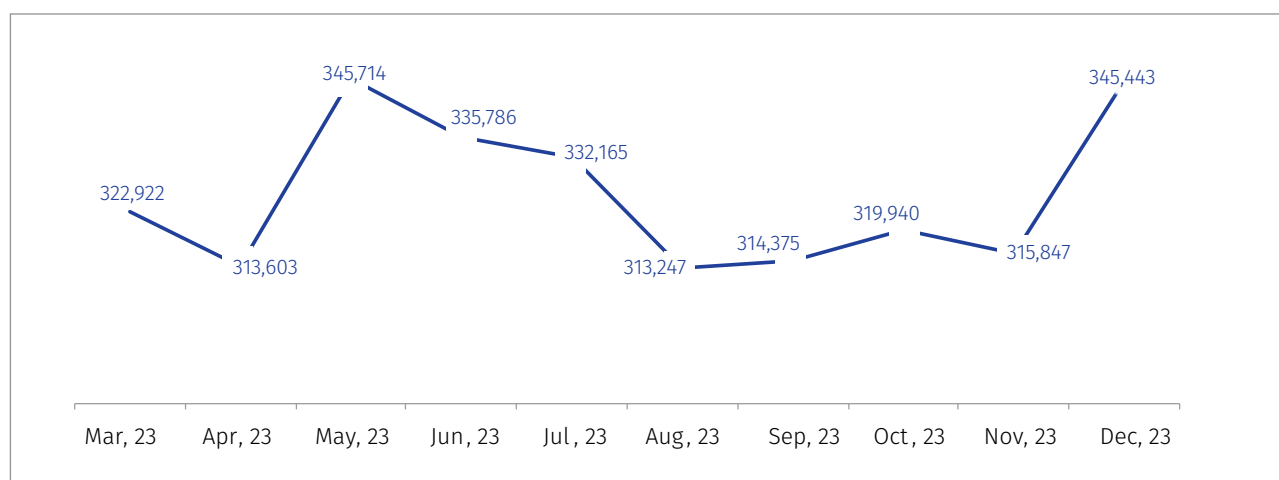


Diagram N 4.46 The number of unique persons cashing the remittances (2023)



In reference to the provided diagrams, it is noted that the total number of unique individuals who withdrew remittances from March to December 2023 was 1,256,713.

Furthermore, based on the needs and issues identified during the process of monitoring and supervising the compliance of lending entities with the established rules, the NBG issued a total of 9 written warnings to the credit information bureau, 51 written references to entities regulated by the NBG, and 11 monetary fines in 2023.

#### 4.12.4 OPEN BANKING/FINANCE

In 2023, significant efforts were made towards expanding Open Banking services in Georgia and enabling fintech companies to participate in the Open Banking ecosystem. To facilitate this, several new regulations were introduced and enacted, including *the regulation on inclusion in Open Banking* that were approved by the Governor of the National Bank of Georgia on May 3, 2023, under decree No. 80/04.

In addition, numerous meetings were held throughout the year with the supervisory entities of the National Bank of Georgia, as well as fintech companies, to exchange information about the potential of Open Banking and its future development.

Open Banking is a system that allows for the immediate exchange of financial information between different organizations using electronic technologies, with the user's consent and permission.

The National Bank of Georgia began work on the Open Banking project in 2019. In early 2020, the Open Banking Committee was established within the framework of the Georgian Bankers' Association, with the aim of developing a common standard for the introduction of Open Banking in Georgia and promoting the project's further development. Open Banking services were launched in Georgia on March 31, 2021.

In 2022, the available Open Banking services were expanded to include the exchange of information on standard products and account information for legal entities. In 2023, additional API services were introduced, such as the transfer initiation service for individuals and legal entities, remote identification service using Open Banking, and bulk payments service.

In 2024, it is planned to add the following API services: a service for sharing information on deposits and loans, support for advanced forms of payment initiation, and a *request to pay service*.

In July 2023, the NBG, in collaboration with the International Finance Corporation (IFC), launched the Open Banking Technical Sandbox project. The primary objective of the project was to foster the growth of Open Banking and enhance its utility for users. Additionally, the project aimed to provide a platform for start-up and fintech companies, interested in the field of financial technologies, to test Open Banking API services.

The participants of the Technical Sandbox comprised of representatives from both the financial and other sectors, as well as Georgian and overseas start-up companies. The participants were given the opportunity to explore the capabilities of two pre-selected Open Banking APIs in a test environment and utilize them to create innovative and attractive financial products for customers.

A comprehensive report of the project's final results and recommendations for the next steps are expected to be received from the IFC in March 2024. This will enable the NBG to gain insights into the future prospects of Open Banking/Finance development and determine the necessary measures to be taken to promote the growth of financial technologies.

The next phase in the evolution of Open Banking is the transition to Open Finance, which involves a much broader exchange of information. In 2024, along with commercial banks, other representatives of the financial sector and licensed fintech companies are planned to be integrated into the system. Furthermore, consultations with representatives from other sectors have been initiated to explore the possibility of their inclusion in Open Finance. This is expected to contribute to the increased availability and diversity of financial services for consumers.

## 4.13 DATA PROCESSING AND SUPERVISORY TECHNOLOGIES



The National Bank of Georgia continues using the International Standard XBRL (Extensible Business Reporting Language) information system in efforts to improve the exchange of supervisory reports and data quality. Its two important components are: a reporting portal and Taxonomy Management System (TMS). The project enjoys cooperation with the top British company Corefiling.

While transitioning to XBRL standard, banks can submit the required supervisory reports, both in conventional and XBRL format. The validity of the reports submitted in XBRL format is checked by the appropriate taxonomy. With the help of the portal, banks can view the validation results before sending the data to the NBG, which significantly improves data quality, reduces the likelihood of error, and conforms to established best supervisory practices. After the data is validated, the information provided is recorded in the database and is made available for stakeholders.

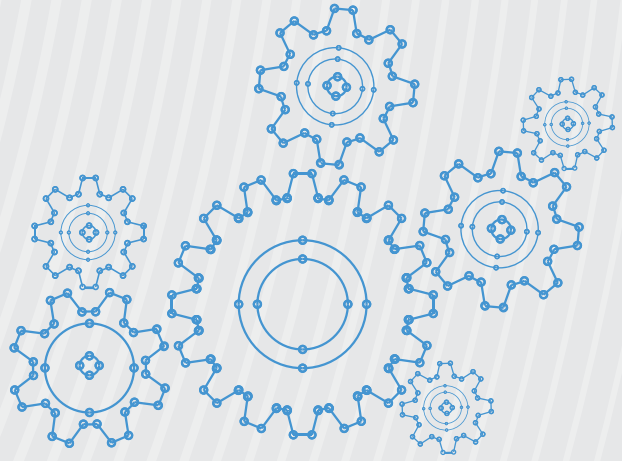
In 2023, support for the process of fully converting supervisory reports to IFRS continued. Using the supervisory portal, all mandatory supervisory reports are received from commercial banks, both in traditional and XBRL standard, including the individual FinRep financial statements established by the EBA in the EU. As part of the project to transition to the XBRL standard in 2023, work on relevant XBRL taxonomies for supervisory reports continued.

In 2023, the NBG developed the so-called taxonomy of green loan financing reporting. Climate and

environmental change and social issues represent an important challenge for the economy and financial sector, therefore it is necessary to monitor and observe the above-mentioned data.

For data exchange, a system supporting the XBRL format is used, and for data processing and visualization, the NBG uses the system developed by the department and the leading Business Intelligence system Tableau. Using available supervisory technologies, 2023 continued to process data, create analytical dashboards for supervisory purposes, and share information with stakeholders. In addition, a credit bureau and credit registry data processing system was created, and, with the help of visualization, relevant analytical information boards were prepared.

Also, work continued to improve the availability of analytical dashboards and information, which implies placing data visualizations on the website of the NBG. In 2023, NBG actively shared knowledge both within the NBG and with partners. Another annual Eurofiling conference was held in Frankfurt, Germany, attended by NBG representatives and presented on green financial technology strategy issues. Several key issues were highlighted at the conference, on which leading European countries are actively working. The processing of granular data, the development of financial technologies and the issues of environmental protection are important challenges among them. In response to these and other challenges, the NBG actively continues to develop supervisory technologies.



# CONSUMER RIGHTS PROTECTION

05

## 5.1. IMPROVING THE LEGISLATIVE FRAMEWORK



### 5.1.1. REGULATION ON CONSUMER RIGHTS

The study and analysis of the best international practices as well as the challenges in the sector continued in 2023, to improve the customer-friendly environment. As a result, the National Bank of Georgia made certain changes in 2023 in the *Regulation on the Protection of Consumers' Rights in the Provision of Services by Financial Organizations*" (the regulation) approved by decree #32/04 of March 9, 2021:

- In 2022, the National Bank of Georgia started working on the development of new transparency requirements for financial organizations, which were approved and implemented in 2023. The change requires financial organizations, when offering combined financial products to consumers, to provide a transparent indication of the price of a separate financial product and provide proper information to consumers. The changes ensure transparency of the prices of the products included in the package when financial products are combined in one package, to promote the most informed decision-making by consumers and to encourage competition in the market. With this change, customers were given the opportunity to compare financial products of one or different financial organizations, to help them make an informed decisions.

The National Bank of Georgia actively cooperated with the experts of the World Bank while working on the amendments. The draft was published on the website of the NBG to receive opinions, comments and recommendations from interested parties.

- Also, the regulation forbids to offer/advertise such credit product/service to the customers by the financial organization, the source of payment

of which is related to social assistance/pension. The purpose of the said change is to limit the offering/advertising of high-risk credit products/services by financial organizations, without the explicit consent of the user, for the socially vulnerable segment, to protect them from making uninformed decisions.

In addition to the above, in 2023, the National Bank of Georgia continued to work on other changes to the regulation, including, in order to comply with the requirements of the Association Agreement between Georgia and the European Union. Based on this, the National Bank of Georgia has published a draft of amendments to the regulation, which is based on the requirements of the EU Directive on the one hand and, at the same time, responds to the challenges in the sector. It includes:

- Clarification of various concepts and terms. In particular, the concepts of "credit intermediary", "total amount of credit" and "deposit" were clarified; The definition of the term "Internet/Mobile Bank" was added;
- Obligation of financial organizations, when offering a financial product, to inform the customer verbally of the important terms of the agreement before the delivery of the financial product, except for the case when the product is offered by means of remote communication that excludes possibility of verbal communication and the said information is delivered to the user in another way (including remote communication means);
- The right to refuse the contract, according to which the financial organization is obliged to cancel the contract within 14 days after the signing of the unsecured loan agreement and loan agreement secured by movable property, upon the customer's request and refund of the corresponding amount. The draft decree also includes exceptions, in which case the right to refuse does not apply;
- Mandatory information to be indicated in the

header of the contract, including the existence and non-existence of the right to refuse the contract; Also, taking into account the requirements of the regulation approved by the decree No. 44/04 of the Governor of the National Bank of Georgia dated March 13, 2020, *on the approval of the regulation on lending to individuals*, information on the right to unconditional extension of the credit term.

The draft changes was published on the website of the National Bank of Georgia for public consultation. Also, to discuss the project, meetings were held with representatives of the financial sector. It is planned to approve and implement the changes in 2024.

### 5.1.2. THE CONSUMER RIGHTS LAW

In March 2022, the Law of Georgia on Protection of Consumer Rights (hereinafter - "the Law") was passed, the main requirements came into effect on June 1, 2022, and some requirements - on November 1 of the same year.

The National Bank of Georgia ensures the execution of mentioned law in the financial sector, including the monitoring of compliance by financial institutions with the requirements defined by the above law, within the framework of the powers defined by the relevant legislation. Based on the above, in 2023, appropriate changes were prepared in the regulation on determining, imposing and enforcing monetary fines for commercial banks, micro-banks, microfinance organizations and loan lending entities operating in Georgia, by which the amount of appropriate monetary fines was determined for non-fulfillment of the requirements established by the above-mentioned law. The changes came into effect in January 2024.

#### Market Conduct Supervision

The National Bank of Georgia is committed to protecting consumer rights and works in various areas to achieve this goal. These efforts include responding to consumer inquiries, improving the

existing regulatory framework, and monitoring its implementation by financial institutions. To proactively identify and mitigate potential risks to consumers and investors, (based on the international best practices and experience, as well as the recommendations of the World Bank technical assistance project), the NBG has decided to study and monitor the market behavior of financial sector representatives, credit information bureaus, and loan lending entities, and to implement a risk-based supervision function.

The market conduct supervision involves the observation and monitoring of various indicators to detect and prevent potential risks to consumer rights. This approach also includes studying and analyzing the market practices of financial institutions that may not be covered by the current legal framework, and developing recommendations and guidelines based on the results. The regulatory framework will also be refined as necessary. The approach aims to direct more supervisory resources towards systemically important and potentially risky financial institutions in the area of consumer rights protection.

In 2023, the National Bank of Georgia conducted two thematic reviews to study the existing market practices and evaluate compliance with current requirements in the area of consumer rights protection. These reviews focused on the process of offering and selling financial products through remote channels, as well as the consumer complaints' handling.

#### Remote and on-site inspection of consumer rights protection standards in the financial sector

Following the observation of the challenges in the market the NBG continued remote inspections of entities under its supervision in 2023, to monitor the protection of financial sector consumer rights. In 2023, in addition to standard inspections, two thematic reviews were conducted in the scope of market conduct supervision: within the scope of thematic reviews,

the National Bank of Georgia remotely inspected a total of 16 (sixteen) financial organizations, of which 5 (five) are commercial banks, 6 (six) microfinance organizations and 5 (five) loan lending entities. In addition, several financial organizations participated in both thematic reviews. Based on the inconsistencies identified in relation to the current legislation, appropriate recommendations were developed for financial organizations, and in some cases, appropriate supervisory measures were taken.

The issues raised in the complaints laid by the customers in the National Bank of Georgia, as well as those mentioned in the complaint reports provided by financial organizations were studied remotely, and a number of supervisory actions were taken in response to the identified violations of the requirements of the legal framework. Written instructions were sent to 5 (five) commercial banks, 4 (four) microfinance organizations and 18 (eighteen) loan lending entities; In total, 4 (four) commercial banks were fined 93,000 (ninety-three thousand) GEL, 1 (one) microfinance organization 2,000 (two thousand) GEL, and 11 (eleven) loan lending entities - 21,000 (twenty-one thousand) GEL.

## Customer Appeals

In 2023, a total of 8,478 customer appeals were recorded in the Consumer Rights Protection Department of the National Bank of Georgia, about 13% more than the previous year.

As in previous years, the majority of customers contacted the bank by phone: 6,132 contacts (72.32 percent) were recorded through that channel, a slight decrease compared to the previous year, the reason being the preference of other channels. More specifically, 1,098 applications (12.95 percent) were made by e-mail, 752 (8.87 percent) applications in writing, 151 applications (1.78 percent) through social networks, and 345 customers (4.06 percent) visited National Bank of Georgia in person.

In terms of content, the majority of appeals in 2023, similar to the previous year, were related to

administration and services. However, the specific topics of these appeals have changed. Instead of appeals related to general issues or loan/credit restructuring requests, in 2023, appeals related to the terms of the agreement and interest payments were also prevalent. In terms of products, the most frequent appeals were related to pension loans, consumer loans, mortgage loans, and problematic loans.

## Credit Information Bureau

The National Bank of Georgia has been analyzing consumer claims recorded in the Credit Information Bureau since 2019, in accordance with the Regulation on providing information to the Credit Information Bureau in the territory of Georgia, recording and making available information in the Credit Information Bureau database, approved by the Governor of the National Bank of Georgia on August 27, 2018.

In 2023, a total of 166,068 claims were recorded in the Credit Information Bureau. Of these, in 13,402 cases consumers were identified and claims responded to, while feedback to unidentified users could not be implemented, although the issues were studied by the bureau.

The most frequent claims were related to the following issues: updating information on the repaid loan liability, updating information on the reduced principal of the loan amount, updating the information about the payment of the current overdue amount on the loan.

Examination of these claims revealed that most of them were related to the fast delivery of information to the Bureau, which is provided by financial organizations. Additionally, there were deficiencies related to the transfer of information by financial organizations, as well as the reflection of the said information in the database of the Credit Information Bureau. In some cases, customers requested the transfer of the information to and/or reflection of this information in the database of the Credit Information Bureau in such terms that the relevant regulatory framework does not provide.

### Claims laid in Financial Organizations

The National Bank of Georgia publishes monthly reports on customer complaints recorded by financial organizations, in accordance with the Regulation on the Protection of Consumers' Rights in the Provision of Services by Financial Organizations.

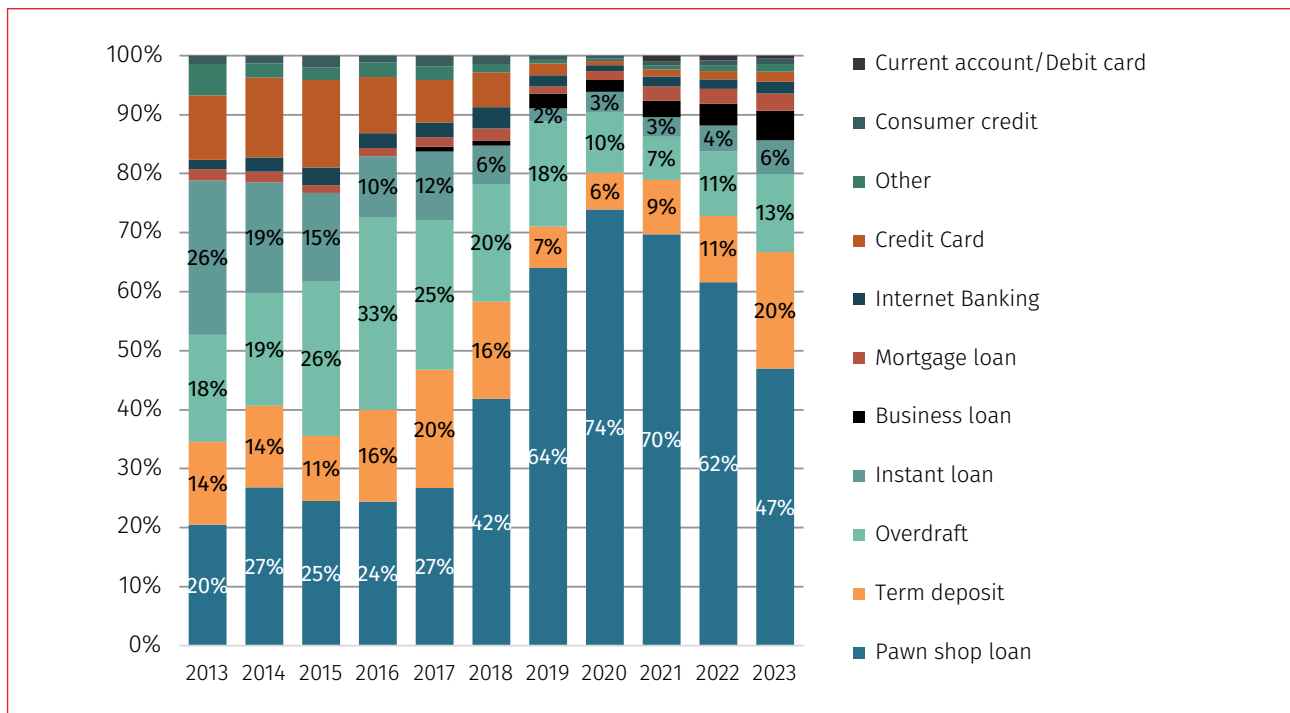
In 2023, a total of 22,794 claims were recorded in commercial banks, which represents a decrease of 1.9% compared to the previous year. The number of claims has been increasing since 2012, mainly due to increased awareness of the complaint handling mechanism and the impact of the COVID-19 pandemic

in 2020-2021. Hence, the reduction in the number of claims in 2022 and 2023 is attributed to the reduction of pandemic-related challenges.

In terms of the nature of complaints, issues related to transactions, administration/service, and contractual terms continue to be the most predominant. In terms of product types, the most frequent claims were related to current accounts/debit cards, consumer loans, and credit cards.

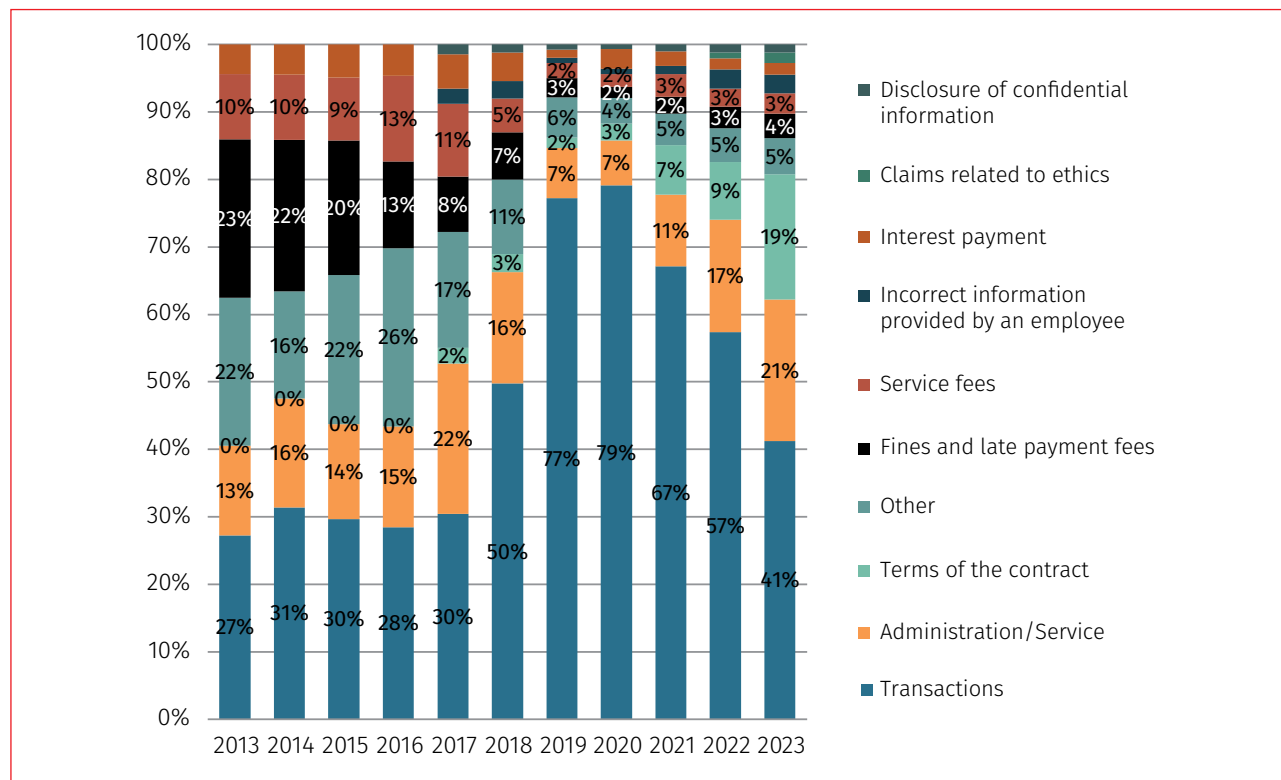
It's worth mentioning that despite the slight decrease in the total number of claims, the share of valid claims has increased by 8%.

Diagram N 5.1 Distribution of Claims at Commercial Banks By Product



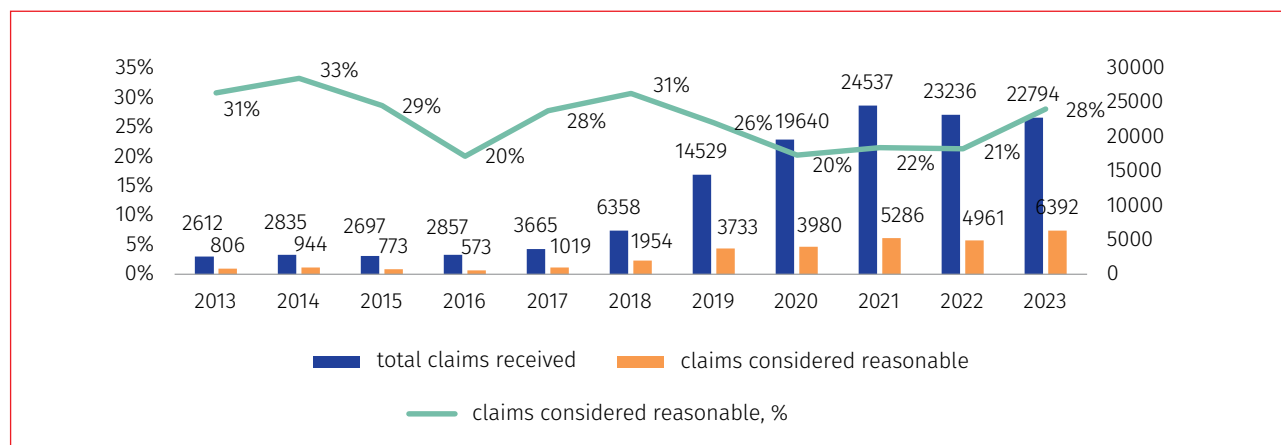
Source: NBG

Diagram N 5.2 Distribution of Claims at Commercial Banks By Nature



Source: NBG

Diagram N 5.3 Distribution of Claims at Commercial Banks By Status



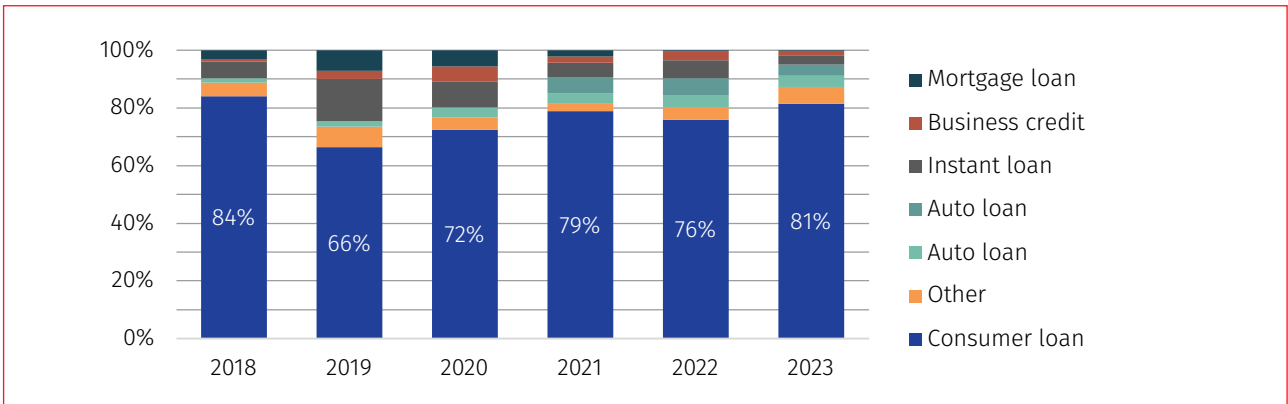
Source: NBG

In 2023, a total of 1,229 claims were registered in microfinance organizations, which is about 20% more than the previous year. The reason is a technical error detected in one of the organizations, which has now been eliminated.

In terms of the content, in 2023, approximately 67% of

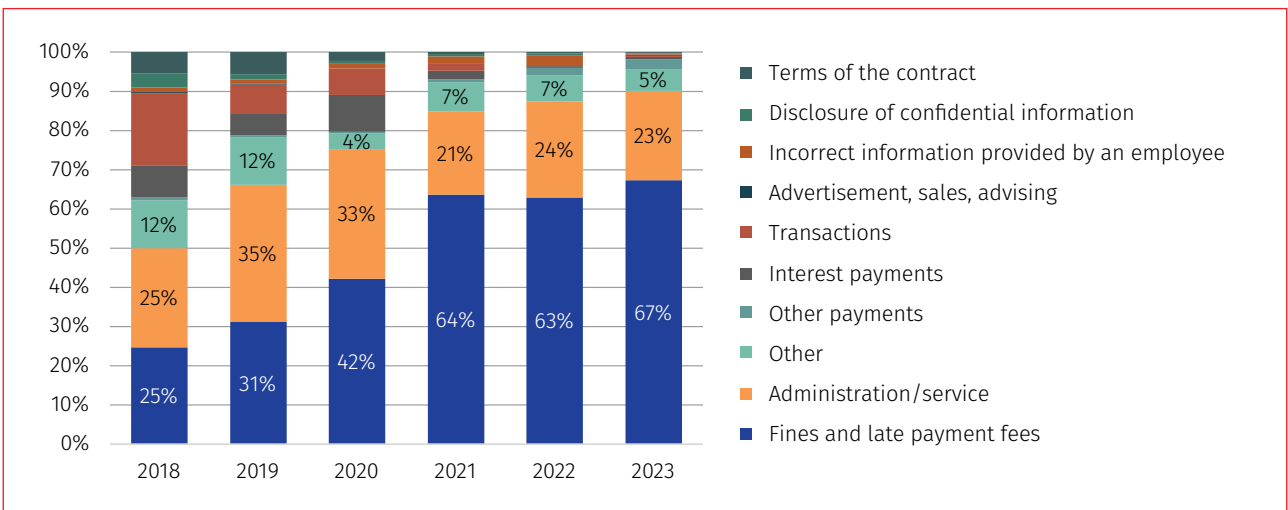
the complaints recorded in microfinance organizations relate to fines and late payment fees, and 23% are about administration and services. As for the claims by products, in 2023 like the previous year, the claims about consumer, auto and pawn loans prevailed. At the same time, the share of valid claims has increased by about 7%, due to the same technical error mentioned above.

Diagram N 5.4 Distribution of Claims at Microfinance Organizations By Product



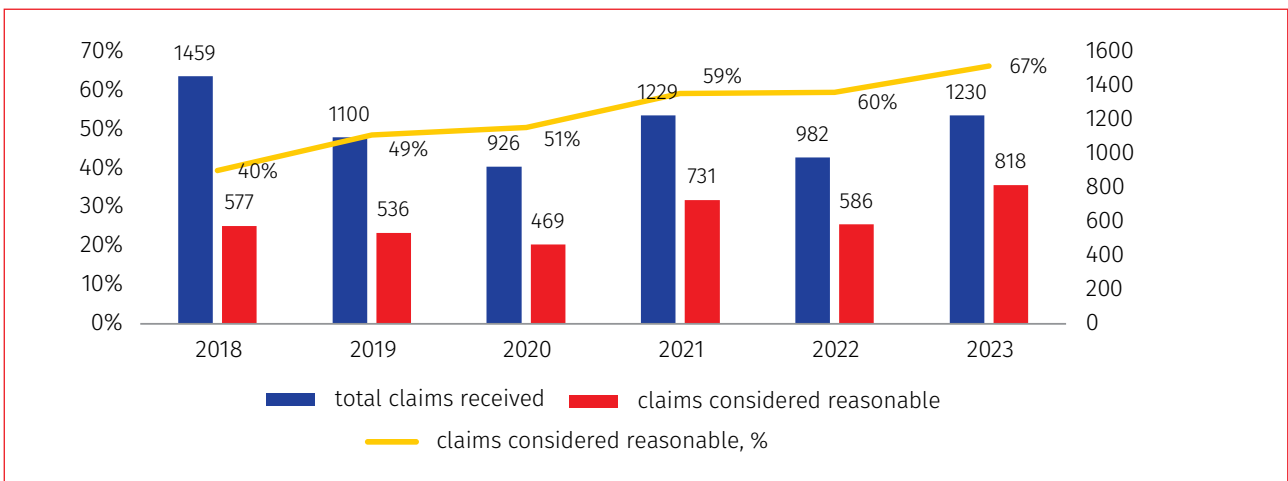
Source: NBG

Diagram N 5.5 Distribution of Claims at Microfinance Organizations By Nature



Source: NBG

Diagram N 5.6 Distribution of Claims at Microfinance Organizations By Status



Source: NBG

Since 2022, the National Bank of Georgia has been publishing statistics on the claims recorded by consumers in loan lending entities on its website. In 2023, a total of 1,928 claims were registered among loan lending entities, which is approximately 45% less than the previous year. The decrease in the number of claims is due to the regularization of the recording of claims by the lending entities - in 2022, there were frequent cases of duplicate registration of claims.

Similar to the previous year, in 2023, the majority of claims by nature were related to administration/ services and other charges. According to the product type, the most frequent claims in 2023 were recorded on consumer and pawn loans. Despite the decrease in the number of claims, the share of the number of valid claims has increased by approximately 27%.



# FINANCIAL EDUCATION

006

## Financial Education

Following the structural changes in September 2023, the Financial Education Division was separated from the Consumer Rights Protection Department, expanded and formed as the Financial Education and Strategic Development Department.

## NATIONAL STRATEGY FOR FINANCIAL EDUCATION OF GEORGIA 2023

On January 24, 2023, coinciding with International Day of Education, the National Bank of Georgia (NBG) proudly announced the approval of a revised National Financial Education Strategy<sup>63</sup> (the Strategy).

This updated Strategy outlines key priorities, objectives, and a practical framework for promoting collaboration among stakeholders. This improved approach ensures:

- **Increased Accessibility:** Expanded access to financial education for all target groups.
- **Tailored Programs:** Development and implementation of activities specifically designed to meet the needs of diverse populations.
- **Long-Term Sustainability:** A commitment to ensuring the ongoing success of financial education initiatives.

The previous Strategy, adopted in 2016, relied heavily on international best practices. The new document leverages Georgia's own experiences and insights, enabling a more targeted response to local challenges in financial education. Prior to finalization, the Strategy was published on the NBG website for public discussion. The final version incorporates valuable feedback received from partners, stakeholders, and international experts.

## National Financial Education Strategy Management Committee and Working Group

At the beginning of the year, the National Bank of Georgia held a workshop for stakeholders within the framework of the new National Financial Education Strategy, summarizing the activities of the past year and presenting the 2023 working projects. The summary of one year's activities clearly showcased the achieved results and new opportunities for future development. The projects of 2023 enjoyed engagement of the following agencies and organizations: Ministry of Education and Science, Revenue Service, State Insurance Supervision Service, Deposit Insurance Agency, Pension Agency, Youth Agency, Society and Banks, Junior Achievement Georgia, Aflatoun International, Deutsche Sparkassenstiftung für internationale Kooperation (DSIK), European Fund for Southeast Europe (EFSE), Civil Education Teachers Forum, Small and Medium Entrepreneurship Development Association (SMEDA), Bank of Georgia, TBC Bank, Basisbank, Liberty Bank, Credo Bank, Pasha Bank, Microfinance Organization MBC, Microfinance Organization Swiss Capital, Microfinance Organization Crystal, Ilia State University, Caucasus International University. At the meeting, representatives of the educational, public, civil, media and commercial sectors agreed on the development and future engagement of the 2024 Action Plan with the National Bank of Georgia.

## FINANCIAL EDUCATION PLATFORM WWW.FINEDU.GOV.GE

The financial education platform [www.finedu.gov.ge](http://www.finedu.gov.ge) (Finedu), launched by the National Bank of Georgia in September 2020 and its social networks channels (Facebook, Instagram, LinkedIn, YouTube, now also including TikTok platform), have been one of the effective tools for the dissemination of financial education throughout Georgia.

63. [https://finedu.gov.ge/storage/files/doc/%E1%83%A1%E1%83%A2%E1%83%A0%E1%83%90%E1%83%A2%E1%83%94%E1%83%92%E1%83%98%E1%83%90%202023\\_%E1%83%A5%E1%83%90%E1%83%A0%E1%83%97%E1%83%A3%E1%83%9A%E1%83%98.pdf](https://finedu.gov.ge/storage/files/doc/%E1%83%A1%E1%83%A2%E1%83%A0%E1%83%90%E1%83%A2%E1%83%94%E1%83%92%E1%83%98%E1%83%90%202023_%E1%83%A5%E1%83%90%E1%83%A0%E1%83%97%E1%83%A3%E1%83%9A%E1%83%98.pdf)

The website was refreshed and replenished with new, diverse educational materials. During 2023, there were 267,876 unique users of Finedu, and we're reaching 1,028,728 users through social networks, including Facebook. This year, Finedu also started posting educational videos on the TikTok channel. The number of followers on Instagram and LinkedIn pages was 3,257.

### **Awareness Raising Activities**

The National Bank of Georgia has traditionally marked important dates related to financial literacy in 2023, including: World Consumer Rights Day (March 15), Global Money Week, Innovation Camp, International Youth Day (August 12), Cybersecurity Awareness Month, World Savings Day (October 31), and Insurance Day in Georgia. For the first time, a literary contest was held dedicated to the World Book and Copyright Day, April 23.

### **World Consumer Rights Week**

Since 1983, March 15th has been recognized globally as World Consumer Rights Day. This day aims to empower consumers by raising awareness of their rights across various sectors. In Georgia, the National Bank of Georgia (NBG) has led initiatives to mark this day for three consecutive years, using the consistent slogan "Know Your Rights - Stay Protected!"

This year, the NBG together with four additional regulatory agencies: National Competition Agency, Communications Commission, National Energy and Water Supply Regulatory Commission and State Insurance Supervision Service took a significant step by expanding the celebration into Georgia's first Consumer Rights Week, held from March 13th to 17th.

Throughout the week, these agencies:

- Reviewed sectoral reforms
- Discussed ongoing challenges
- Explored best practices in consumer protection
- Held meetings with consumers, students, and the business sector

Additionally, an informative social media campaign was launched on Finedu's channels, featuring thematic news posts and video clips.

### **Global Money Week**

Global Money Week is held annually in over 170 countries to raise financial, economic, and entrepreneurial awareness among children and young people. In March 2023, Finedu, the educational platform of the National Bank of Georgia, organized several important activities for Global Money Week in Georgia, involving representatives from the financial sector. Georgia joined the International Week for the ninth time, focusing on diverse topics such as sustainable development, ecology, and public care. The theme of the week was "Plan Your Money, Plant Your Future".

Several projects were implemented to mark the occasion:

"Invite Finedu to Class" - Representatives of the National Bank of Georgia and partner organizations, acting as Finedu Ambassadors, gave open lessons to students from grades III-IX in both Tbilisi and regional schools. The Ambassadors discussed the history of money, the functions of the National Bank of Georgia, the importance of saving, sustainable development, and environmental issues. Some students attended these lessons online. The event reached about 4,000 students in approximately 125 classes.

The purpose of the poster and slogan contest "Plan Your Money, Create Your Future" was to raise public awareness about financial literacy, environmental issues, and sustainable development. The contest was supported by the Bank of Georgia, TBC Bank, Basisbank, Credo Bank, Micro Business Capital, Crystal, the Pension Agency, Ilia State University, Caucasus International University, and Aflatoun International. Out of about 170 entries, the jury, following the competition's conditions and criteria, selected and awarded 20 finalists.

The video contest "My Money" started on March 11 and was implemented with the involvement and support of the Pension Agency, Bank of Georgia, MFO Micro Business Capital, Ilia State University, and Caucasus International University. The contest aimed to engage schoolchildren in financial matters and encourage discussion about the history, functions, and importance of money. A total of 35 videos were received - they were uploaded to Finedu's Facebook page as a comments of the Contest post and five winners were revealed.

### **Insurance Day**

Through the initiative of the NBG and the State Insurance Supervision Service of Georgia, and with the support of the Association of Insurance Companies of Georgia and the involvement of the insurance sector, May 2 has been designated as Insurance Day in Georgia starting from 2022. The idea for Insurance Day arose during discussions on projects to be implemented under the National Strategy for Financial Education, with the goal of raising public awareness about insurance.

As part of the information campaign dedicated to Insurance Day, the financial education platform provided a variety of engaging educational materials about insurance to consumers on the Finedu website and social networks. These materials included articles, crosswords, posters, and other informative content.

On May 2 in Tbilisi, a significant event was held to celebrate Insurance Day with the involvement of the insurance sector. At the event, the Vice Governor of the National Bank of Georgia emphasized the importance of raising awareness and financial education among the citizens about insurance.

### **Innovation Camp on Financial Education**

Organized through the initiative of the National Bank of Georgia and Junior Achievement Georgia, an Innovation Camp event on the topic of financial education was held in Kutaisi at Akaki Tsereteli State University. This event was in cooperation with the

Ministry of Education and Science of Georgia, Caucasus International University, and the Bankers' Association, with financial support from the Bank of Georgia, TBC Bank, BasisBank, and Credo Bank.

Innovation Camp is a 12-hour idea-generating event where young people come together to tackle a specific challenge, develop effective solutions, and present their results to a jury. The event has a 12-year history as part of the USAID project "Supporting Entrepreneurial Education in Europe and Eurasia." With the involvement of the National Bank of Georgia, the event has focused on financial education challenges for the sixth time.

In 2023, about 100 young people aged 15-18 participated in the event, working with situational tasks under the guidance of invited banking and finance experts. The National Bank of Georgia presented on the need for financial education and its importance. This year, participants spent the day developing ideas to enhance the financial literacy of immigrants and their families and to engage them in entrepreneurship.

The jury selected the #4 team, named Human Intelligence, as additional favorites, a distinction also recognized by Caucasus International University and the National Bank of Georgia. All participants received certificates recognized in 123 countries, and the winning teams received symbolic gifts.

### **World Savings Day**

In 2023, the National Bank of Georgia celebrated World Savings Day for the twelfth time with the involvement of the financial sector. The aim of the initiative was to encourage savings among the population, especially children and young people, and to raise awareness of the benefits of savings.

The World Savings Day information campaign began on October 31 and ran throughout November. The campaign was organized by the National Bank of Georgia and the educational platform Finedu, with support from partner organizations such as Basisbank, TBC Bank, Credo

Bank, Bank of Georgia, Microfinance Organization MBC, the Pension Agency, Junior Achievement Georgia, and Caucasus International University. The participation of school teachers as Finedu Ambassadors gave the campaign an exceptional scale.

The initiative included a variety of activities for schools, from the "Invite Finedu to Class" project to traditional open lessons for students from grades III-IX on the importance of saving. Events took place across Georgia, reaching up to 8,000 students in 350 classes across 45 cities and villages of Georgia. Participating schools received a wide variety of commemorative educational materials and certificates.

### Cybersecurity Awareness Month

The development of technology has enabled the quick and efficient delivery of financial services. However, this also comes with an increase in cybercrime risks. New cyberattacks and fraud schemes emerge every year, posing significant challenges for identification and prevention, even in developed countries. This is why raising public awareness about cyber and financial security issues is given high priority in the National Strategy for Financial Education.

The International Cybersecurity Awareness Campaign has been celebrated globally since October 2004. Last year, through the initiative of the National Bank of Georgia, the financial sector joined the campaign for the third time. The campaign's slogan, "Think Before You Open", focused on activities related to social engineering and defense against cybercriminals. New educational materials were developed and shared on Finedu's social channels, including informative videos.

Participating in the campaign were the Banking Association of Georgia, Bank of Georgia, TBC Bank, Basisbank, Liberty Bank, Credo Bank, Procredit Bank, Rebank, and Microfinance Organization MBC. Finedu's

Facebook channel facilitated direct engagement and educational media broadcasts.

## FINANCIAL EDUCATION PLATFORM FINEDU'S FACEBOOK CHANNEL LIVE ENGAGEMENTS AND EDUCATIONAL MEDIA BROADCASTS

### Facebook Live Series - Finosophical Diaries

One of the successful initiatives in 2023 was the extension of the *Finosophical Diaries* series on Finedu's Facebook page. The series aimed to present financial issues in an interesting way and promote sensible financial attitudes among the general public. Throughout 2023, there were 21 sessions of The *Finosophical Diaries*, where invited speakers presented financial topics in an original and engaging manner. These sessions were open to everyone, allowing viewers to ask questions in the comments and receive live responses from the speakers without pre-registration. Recordings of the sessions are available on the financial literacy portal<sup>64</sup>, and its YouTube channel<sup>65</sup>, in addition to the Facebook page.

### Facebook Live broadcast series - Expert on Finedu

In 2023, the Facebook project "Expert on Finedu" was successfully reintroduced after being scrapped in 2021. The project aims to provide objective and competent coverage of important financial issues. The speakers' discussions typically focus on topics directly or indirectly related to finance and financial decision-making. Throughout the year, seven sessions of the "Expert on Finedu" project were held. Invited speakers discussed timely topics, answered questions from listeners, and engaged in discussions related to the theme of each session.

The recordings can be viewed on both the financial literacy portal<sup>66</sup> and its YouTube<sup>67</sup> channel, in addition to the Facebook page.

64. <https://finedu.gov.ge/ge/video-galerea-2/finosofiuri-dghiurebi-1>

65. [https://www.youtube.com/watch?v=ySAglFW6yI4&list=PLhi\\_8\\_nnsD1NHDTf\\_DKNkdp6M5D-wHkbp](https://www.youtube.com/watch?v=ySAglFW6yI4&list=PLhi_8_nnsD1NHDTf_DKNkdp6M5D-wHkbp)

66. <https://www.finedu.gov.ge/ge/video-galerea-2/eksperti-fineduze-1>

67. [https://www.youtube.com/playlist?list=PLhi\\_8\\_nnsD1M0Ie0-CiiZW\\_BgBpNFfxj2](https://www.youtube.com/playlist?list=PLhi_8_nnsD1M0Ie0-CiiZW_BgBpNFfxj2)

### **Facebook Live broadcast Series - "Business Conversations"**

In 2023, the Finedu Facebook project "Conversations on Business" continued, featuring invited speakers discussing topics related to entrepreneurs' financial decisions. The sessions primarily focused on issues related to business continuity. The format allowed anyone to join the session, ask questions in the comments, and receive live responses from the speaker without needing to pre-register. Throughout the year, 20 sessions of the "Conversations on Business" project were held. Recordings of these sessions are available on both the financial literacy portal<sup>68</sup>, and its YouTube<sup>69</sup> channel, in addition to the Facebook page.

### **FINANCIAL LITERACY CREATIVE CONTESTS**

In 2023, the National Bank of Georgia announced periodic competitions through the social channels of Finedu to increase interest in financial literacy among the population. The year was marked by a variety of contests aimed at engaging people in financial education.

#### **Literary Competition "Financial Education in Literature"**

The National Bank of Georgia and Finedu partnered to celebrate World Book and Copyright Day on April 23rd. To promote financial literacy, they launched the "Financial Education in Literature" contest. The competition challenged participants to creatively showcase the importance of financial knowledge. Partner organizations from banking, education, and publishing supported the initiative. These included Bank of Georgia, TBC Bank, Credo Bank, Micro Business Capital, Crystal, Caucasus International University, Ilia State University, Bakur Sulakauri Publishing House, Diogenes Publishing House, Artanuji Publishing House,

Intellect Publishing House and SME Development Association.

A distinguished jury, composed of writer Dato Turashvili, general director of the National Library of the Parliament of Georgia and writer Giorgi Kekelidze and editor of the publishing house "Artanuji" Zviad Kvaratskhelia, was selected by the organizers. The National Bank of Georgia hosted discussions between the jury and interested individuals, where they explored life's challenges and the role of literature in financial education.

The "Financial Education as an Artist" competition challenged participants to write short stories that explored themes of financial literacy. The motto "Write, Give, Win!" captured the essence – creating, sharing, and being rewarded for financial knowledge.

Open to all Georgian citizens, the contest entries were judged on two key criteria. First, the jury assessed how effectively the story addressed financial literacy concepts. Second, they evaluated the creative/literary merit and how well the story resonated with everyday readers.

The "Financial Education in Literature" contest received response, with 87 short stories and 95 entries from schools. The jury selected 14 finalists and awarded Ramaz Abashidze Public School in Chaisubani village (Khoni municipality) as the winning school.

A celebratory event at the National Library on September 9th honored the competition's achievements. All 14 finalists received diplomas and gifts, with the top three receiving additional prizes. This event also marked the 3rd anniversary of Finedu, showcasing its accomplishments.

68. <https://www.finedu.gov.ge/ge/video-galerea-2/eksperti-fineduze-1>

69. [https://www.youtube.com/playlist?list=PLhi\\_8\\_nnsD1M0le0-CiiZW\\_BgBpNFfxj2](https://www.youtube.com/playlist?list=PLhi_8_nnsD1M0le0-CiiZW_BgBpNFfxj2)

The competition embraced the spirit of giftng. As part of the contest, there was also the idea of replenishing the library of one of the schools in Georgia with books. By the jury's decision, the library of the Ramaz Abashidze Public School in the village of Chaisubani, Khoni Municipality, was selected to receive the books as a gift. In 2020, the school's building and, consequently, the library were completely destroyed in a fire.

Inspired by the 87 entries, Finedu with supporting from partners purchased and donated 87 books to rebuild library of the School. Representatives from Finedu visited the school on October 18th, presenting the books, conducting a financial literacy lesson for students, and providing additional educational materials.

### **International Youth Day Photo Contest**

The celebration of the International Youth Day on August 12 was initiated by the United Nations in 1999. It highlights the special role of young people in overcoming global challenges. Finedu, the financial education platform, celebrated International Youth Day in 2023 with its third time. This year a photo contest "Catch the Financial Shot" was announced. Partnering with various organizations, the contest aimed to:

- Engage young people: Disseminate financial literacy topics through an exciting and creative medium.
- Raise awareness: Increase young adults' understanding of financial issues.
- Promote responsible behavior: Encourage informed financial decision-making.

On August 21, an informational meeting was held with the NBG jury member, photographer Giorgi Shermazanashvili. The speaker discussed the art of photography and its purpose, as well as technical and practical aspects. The meeting was held in Q&A format.

The contest culminated in a final event on September 17th at the Youth Agency's office. A jury selected 20 finalists from nearly 100 submissions. The finalists

presented their works, showcasing their financial messages through photography.

Beyond the top three main winners, there were revealed winners in additional categories:

- Most Memorable Youth Shot
- Best Financial Humor
- Customer's Favorite

Winners received certificates, commemorative gifts, and cash prizes, while finalists were awarded special certificates and gifts. Notably, interns from the NBG's Financial Education Division played a key role in this youth-focused initiative.

The National Bank of Georgia, Finedu, Basisbank, Credo Bank, Micro Business Capital, Pasha Bank, Bank of Georgia, the Youth Agency, and Caucasus International University all contributed to the contest's success.

### **Financial Education Projects for the Younger Generation**

The National Strategy for Financial Education prioritizes the young generation. Throughout 2023, a number of educational and awareness-raising activities were implemented to empower young people with financial knowledge.

### **Educational Lecture at the National Bank of Georgia**

On April 28, the National Bank of Georgia hosted students of the Conrad Adenauer Foundation Academy of Political Education. At the meeting, the head of the Consumer Rights Protection and Financial Education Department discussed the importance of consumer rights protection with students and the role of the National Bank of Georgia in this regard.

Students learned about consumer rights, the financial sector oversight framework, and gained insights into how to respond to consumer concerns. They heard about the National Strategy for Financial Education,

the educational portal Finedu and projects targeted to the younger generation and students.

### **Finedu Inspires Young Minds at Career Forum**

On June 1st, the National Bank of Georgia hosted a Student Internship and Career Development Forum. This initiative aimed to connect students with potential career paths within the NBG.

Representatives from various departments showcased the Bank's diverse activities and functions, outlining internship and career development opportunities. Undergraduate and graduate students gained valuable insights into:

- Specifics of different NBG departments
- Current challenges and future prospects within the organization
- Answers to their career-related questions

Many students expressed interest in internship opportunities with the Finedu team. Three students were selected to intern within the NBG's Financial Education Department in 2023.

These interns played a vital role in planning and implementing student-focused projects throughout the year. Notably, they headed the "Catch a Financial Shot" photo contest held on Youth Day. This successful initiative was entirely conceived and driven by the interns' creativity.

### **Financial Literacy at Shaori Youth Camp: Empowering Young Minds**

As part of their ongoing collaboration with the Georgian Youth Agency, the National Bank of Georgia participated in the Shaori Youth Camp held during July and August. This camp, supported by the Ministry of Culture, Sports and Youth, fosters social integration, informal education, and national/European values among young people.

Financial literacy was a key component of the Camp's program. Over a five-week period, NBG employees

conducted informational meetings and training sessions for approximately 500 participants.

These interactive sessions covered a range of topics relevant to young adults:

- Introduction to the National Bank's activities
- Understanding insurance and banking products
- Consumer rights and avoiding financial fraud
- Financial management essentials: saving, budgeting, and overcoming challenges

Engaging discussions promoted the importance of responsible financial decision-making, equipping young people with practical knowledge for their future.

### **Training for Students of Akaki Tsereteli State University**

On October 25th, the National Bank of Georgia's Financial Education Department offered a training session titled "Guide for Financial Independence of Students" at Akaki Tsereteli State University in Kutaisi.

This training aimed to equip students living in the region with the tools and knowledge they need to achieve financial independence and build confidence in managing their finances.

The session focused on two key areas:

- Financial planning for early careers: Students gained insights into navigating their financial journey as they enter the workforce.
- Budgeting and saving strategies: The training offered practical tools and techniques to build healthy financial habits.

In addition to the theoretical content, the session included interactive activities and practical assignments. This fostered a sense of community, allowing students to connect with peers and build valuable networks.

Upon completion of the training, participants received certificates and educational materials developed

by the National Bank, equipping them with ongoing financial literacy resources.

### **Financial Education Projects for School Teachers and Students**

Students, as one of the most important segments of the younger generation, are one of the priority target segments of the national financial education strategy, and teachers and their support and empowerment focus on accessing them. The year 2023 was marked by a wide variety of educational activities aimed at students and teachers.

#### **Training for the School Banking Project**

The National Bank of Georgia's *School Banking* project continued to expand its reach in 2023. This initiative incorporates the Child and Youth Finance International (CYFI) program, developed by Aflatoun International and adapted for Georgia by the National Bank of Georgia.

The CYFI program consists of 15 interactive lessons designed to enhance the financial literacy of 7th-9th graders. These lessons cover crucial topics in clear and engaging language:

- Saving and budgeting
- Banking products and services
- Responsible borrowing
- Consumer rights and responsibilities
- Financial security

To effectively deliver the CYFI program, the National Bank conducted two teacher training sessions in 2023. Open to all teachers in Georgia, these sessions were held on May 27-28 and September 13-14. Approximately 40 teachers from Tbilisi and various regions participated.

The training covered all topics included in the "*School Banking*" handbook and emphasized engaging teaching methods. This equips teachers with the knowledge

and skills necessary to integrate financial literacy education into their classrooms.

Upon completion of the training, participants received training materials and certificates. This initiative empowers teachers to be catalysts for financial literacy among young students, promoting responsible financial habits for the future.

#### **Developing a Teachers' Auxiliary Guide for "Citizenship" Module**

In 2023, the National Bank of Georgia collaborated with the German Sparkassenstiftung Foundation, the Forum of Teachers of Civic Education, the State Insurance Supervision Service, and the Revenue Service to create a valuable resource for teachers: a supplementary guide on financial and economic literacy for the "Citizenship" subject.

This auxiliary textbook specifically targets 9th-grade "Citizenship" teachers. It aims to:

- Enhance Teacher Knowledge: Provide educators with a comprehensive understanding of financial literacy topics.
- Promote Active Learning: Encourage engaging lesson delivery through practical activities, group work, and games.
- Motivate Students: Foster student interest by connecting financial literacy concepts to real-world applications.

The guide incorporates both theoretical and practical components, offering a well-rounded approach to financial education. The electronic version of this valuable resource is now available for free on the Finedu platform, empowering teachers across Georgia to integrate financial literacy into their classrooms.

#### **Training for Teachers of school subject of "Citizenship"**

The National Bank of Georgia, in partnership with the financial education platform Finedu, has led a

training initiative for 9th-grade "Citizenship" teachers in Georgian public schools. This ongoing program aims to equip teachers with the knowledge and tools to effectively deliver financial literacy education as part of the National Curriculum.

Offered free of charge, the training program caters to all interested "Citizenship" teachers through a combination of in-person and online formats. The training module is built on supportive learning materials designed for both teachers and their students.

The two-day training program focuses on essential financial and economic topics aligned with the 9th-grade curriculum:

- Career choices and employment
- State budget and taxes
- Financial institutions and services
- Insurance
- Consumer rights and responsibilities

Beyond theoretical knowledge, the program incorporates practical activities, fostering effective lesson delivery and helping students grasp financial concepts within a real-world context. Upon completion, participants receive training materials and certificates. Throughout 2023, close to 100 teachers from public and private schools across Georgia participated in these trainings.

Since the integration of financial literacy into the national curriculum, the National Bank has consistently provided these training sessions, reaching over 700 "Citizenship" teachers by the end of 2023.<sup>70</sup>

### **Financial Education in Schools: A Competition for Teachers**

On June 12, 2023, the National Bank of Georgia, in collaboration with Finedu (<https://www.finedu.gov.ge/>), launched the "Financial Education in Schools"

contest for teachers. This initiative, supported by the Ministry of Education and Science of Georgia, along with State Insurance Supervision Service of Georgia, Civil Education Teachers Forum, Bank of Georgia, TBC Bank, Basisbank, Liberty Bank, Credo Bank, PSP Insurance and Insurance Group of Georgia, aimed to:

- **Boost Teacher Engagement:** Increase teacher interest in financial literacy education.
- **Promote Knowledge Sharing:** Encourage teachers to share knowledge and best practices.
- **Develop Engaging Materials:** Help teachers create effective tools for delivering financial literacy lessons as mandated by the National Curriculum.

Teachers were challenged to develop creative learning methods and activities to teach financial literacy concepts in the classroom. The competition deadline for submissions was October 15th, with finalists notified by January 24th, International Education Day. Partner organizations awarded a total of 11 cash prizes, with the top three winners receiving GEL 2,000 each.

Two informational meetings were held for teachers on June 27th and October 2nd. Representatives from the National Bank and the Ministry of Education provided competition details, evaluation criteria, and answered teacher inquiries.

The competition attracted 65 teachers from public and private schools across Georgia. A jury selected 20 finalists who presented their work during the final event held on January 24th. Based on additional evaluation criteria, the jury awarded five special prizes, two runner-up positions, and three top prizes.

### **Open Financial Education Classes for Schoolchildren**

Throughout 2023, the National Bank of Georgia (NBG) remained committed to promoting financial

70. <https://finedu.gov.ge/storage/files/doc/Financial%20Education%20in%20Schools.pdf>

literacy among young people. This initiative involved collaborating with the educational platform Finedu to conduct open lessons for interested Georgian schools' and financial education clubs' students.

Representatives from NBG's financial education department, along with other employees, led these interactive sessions. Students gained valuable knowledge on various financial topics, including the financial system, financial security, saving, budgeting, and inflation. Additionally, engaging activities helped participants understand how these concepts apply to their everyday lives.

In 2023, these open lessons reached a total of 492 students across 19 schools in Georgia.

### Financial Literacy Projects for Women

Women were identified as one of the target groups by the National Strategy for Financial Education. During 2023, numerous trainings and meetings were held throughout Georgia to strengthen women's economic empowerment.

### Financial Empowerment for Women Living Near the Occupation Line

On June 27th, the National Bank of Georgia hosted a special informational meeting for women living near the occupation line. This session focused on personal finance management and access to financial resources, empowering them to build a secure future.

Representatives from the National Bank's Financial Education Unit led the meeting, providing valuable insights into:

- Personal finance management: Participants gained knowledge on managing their finances effectively, overcoming challenges specific to their situation.
- Budgeting and saving: The session covered strategies for creating and maintaining a budget, as well

as effective saving habits.

- Access to finance: Information was provided on available financial resources and opportunities to secure funding.

A representative from USAID's Strong Village Project also presented information about the *entrepreneurship grant program*. This broadened the participants' understanding of resources available to support their goals.

### Take Charge of Your Finances: A Women's Financial Independence Course

Empowering Women Through Financial Literacy "A Guide for the Financial Independence of Women" training course, was a collaborative effort by the National Bank of Georgia, Finedu, and the German Sparkasse Foundation. Held across four Georgian cities (Tbilisi, Telavi, Kutaisi, and Gori) during the last quarter of 2023, this program aimed to equip women with the tools and knowledge to achieve financial independence and self-confidence.

The course utilized a blend of mini-lectures and practical activities, ensuring a dynamic and engaging learning experience.

Key Topics included:

- Financial planning for women entering the workforce
- Effective budgeting and saving strategies

The program fostered a supportive environment, allowing participants to network, build connections, and gain potential support systems.

Upon completion of the course, participants received certificates acknowledging their commitment to financial literacy. This training course empowers women to take control of their financial future. By gaining valuable financial knowledge and skills,

participants can build a secure foundation for personal and professional success.

### **Financial Education Projects for Immigrants**

Based on the renewed National Strategy for Financial Education, immigrants and their family members were identified, among other vulnerable groups, as one of the targeted segments.

### **Training for Immigrants and Their Families**

On November 21st, Finedu offered a training session titled "How to Manage Income earned abroad Effectively." This workshop aimed to equip immigrants and their families with practical advice and strategies for managing their finances. Supported by Bank of Georgia and Caucasus International University, the training covered a wide range of topics:

- Personal budgeting and savings: Building financial stability through sound budgeting and saving habits.
- Revenue management: Learning to effectively manage income generated through emigration.
- Financial independence: Exploring strategies to achieve financial self-sufficiency.
- Investment opportunities: Understanding investment options and managing risk.
- Financial literacy: Identifying and avoiding unreliable financial products and services.
- Banking tools and remittances: Utilizing banking products and services for efficient money transfers.

By addressing these crucial areas, the training aimed to empower immigrants and their families to make informed financial decisions.

### **Facebook Live "About Immigrants, For Immigrants"**

Finedu hosted a Facebook Live panel discussion titled "About Immigrants, For Immigrants" on December 18th in recognition of International Migrants Day.

Prior to the event, Finedu collaborated with immigrants to identify relevant and challenging topics for discussion. The live session featured four speakers who addressed these pre-selected issues.

Open to all viewers without registration, the event fostered high audience engagement. Immigrants and their families submitted questions anonymously through live comments.

### **Financial Education Projects for MSMEs MSMEs Training**

MSMEs are a key focus area in the financial education strategy. Previously, educational activities were limited to online discussions on Facebook. To address this gap, a new 2-day, in-person training course was launched in 2023.

Held in Zugdidi on December 22nd-23rd, the training targeted entrepreneurs and aspiring business owners. Participants from Samegrelo and Imereti regions, representing various sectors like manufacturing, trade, services, and agriculture, attended the program. The German Savings Banks Foundation Sparkassenstiftung also played a role in this initiative. The two-day training program combined theory and practical exercises to equip micro and small entrepreneurs with essential knowledge. Participants learned about:

- Business financing sources
- Financial products offered by financial institutions
- The importance of business loans
- Financial accounting and analysis
- Consumer rights protection

This comprehensive training empowered MSMEs representatives to make informed financial decisions for their businesses. Training participants were given supportive training material and certificates.

### **Financial Education Exhibition**

On October 6-7, for the first time this year, through the initiative of the National Bank of Georgia, the financial

sector of Georgia joined the International Exhibition of Education in Expo Georgia. The purpose was to raise awareness of financial literacy among the citizens. At the event, the National Bank of Georgia was represented by financial education platform Finedu. The exhibition had attendance of the Bankers' Association and five commercial banks - Bank of Georgia, TBC Bank, Liberty Bank, Credo Bank and Pasha Bank/Rebank.

Guests of the exhibition had the opportunity to learn about Finedu's activities and educational materials, participate in various cognitive and interactive activities, test their financial knowledge, and win prizes.

### **Development of Video Resources**

For easy and concise delivery of financial literacy topics, video resources are an important educational material. For this purpose, Finedu has developed a number of video footage during 2023.

### **Educational Animated Videos**

In 2023, TikTok was added to the social media platform for the purpose of developing Finedu in 2023, specifically for this purpose. Short animated videos on various issues related to financial literacy have been created, as well as informational links supporting information campaigns, such as on cybersecurity and savings.

### **Educational Videos with Teachers**

In order to support the teachers of the subject "Citizenship", 7 video lessons were prepared by the end of 2023, which includes the financial education issues envisaged in the National Curriculum. The mentioned video lessons are led by the teachers actively involved in the Finedu projects.

### **Local and International Cooperation**

The National Bank of Georgia cooperates with various organizations for the dissemination of financial education issues. More than 20 organizations are united with the National Bank of Georgia in the

Financial Education Committee established within the framework of the National Strategy for Financial Education. In addition to cooperation within the framework of the Committee, the National Bank of Georgia always responds to the initiatives of various organizations on the dissemination of financial education among the citizens.

### **Memorandum of Cooperation between the National Bank of Georgia and Ilia State University**

On February 27, the Governor of the National Bank of Georgia and the Chancellor of Ilia State University signed a memorandum of cooperation.

The document signed between the National Bank of Georgia and Ilia State University aims to enhance mutual cooperation in increasing access to financial education and raising awareness among the young generation.

### **International Cooperation**

The collaboration between the OECD (Organization for Economic Co-operation and Development) and the Netherlands' Ministry of Finance on a 5-year technical assistance project through the OECD/INFE (International Network on Financial Education) was extended in 2023.

The project unites 10 countries of the region (Bosnia and Herzegovina, Bulgaria, Moldova, Montenegro, Romania, Georgia, Armenia, Ukraine, the Republic of North Macedonia, Croatia) and aims to promote financial literacy in the region.

Within the framework of this project, an international conference and several workshops were held in the same year, in which the National Bank of Georgia was also represented.

### **International Workshop on Teacher Trainings**

On October 20, the National Bank of Georgia participated in an international workshop on teacher

trainings. The first part of the workshop was dedicated to sharing experiences between countries in the region. The participants of the meeting shared their experiences in developing and implementing teacher financial literacy trainings and discussed key findings and existing challenges. The representative of the National Bank of Georgia spoke to the participants of the meeting about the experience of the National Bank of Georgia in implementing financial education in schools, teacher training program and teacher trainings within the framework of the “School-Banking” project.

The second part of the meeting was dedicated to sharing best practices by OECD/INFE member states. Invited experts informed the attendees about innovative approaches and key factors necessary to implement successful and effective trainings of teachers.

### **Opening Meeting of the New International Financial Education Project**

The Hague hosted the opening meeting of a new five-year financial education project by the OECD/INFE, co-funded by the Netherlands and OECD. Representatives from 50 countries, including Georgia, participated in the event.

The meeting focused on evaluating progress, identifying challenges, and exploring innovative approaches to financial literacy. A particular focus was on initiatives tailored to youth and vulnerable groups.

At the panel “Financial Education and Financial Literacy: New Challenges and Strategic Priorities”, NBG’s Executive Director shared their accomplishments and experiences in financial education. They also presented the updated National Strategy for Financial Education in 2023, which addresses current challenges in a targeted way.

High-ranking attendees included Queen Máxima of the Netherlands and government officials. The event was also attended by employees of the National Bank

of Georgia and the Ministry of Education and Science together with 50 representatives of different countries.

### **National Bank of Georgia at an International Conference Organized by Aflatoun International**

On November 9, 2023, more than 300 representatives from 80 countries gathered to discuss the challenges and opportunities of children's financial literacy at an international conference in Utrecht, Netherlands, organized by Aflatoun International. During the conference, panel discussions were held in which representatives of central banks, educational institutions and non-governmental organizations shared their experience on teaching financial literacy issues to school-aged children.

At the panel discussion of the Central Banks, the Head of the Financial Education and Strategic Development Department of the National Bank of Georgia discussed the Bank’s experience, implemented projects and future plans and highlighted the importance of compulsory training in general educational schools on financial education issues.

A poster by the National Bank of Georgia’s Financial Education Platform Finedu won the poster contest “Social and Financial Empowerment of Children”, dedicated to financial education held at the international conference.

### **Strategic Development - Educational Space of the National Bank of Georgia**

Recognizing that financial literacy is essential for a country's economic soundness and citizen well-being, the National Bank of Georgia prioritizes financial education for its citizens. To achieve this, they established a Division of Strategic Development and Projects within their reformed department. This division focuses on creating an educational space.

This educational space aims to share the NBG's intellectual capital and experience, both internally and

externally. Target audiences include public institutions, the financial sector, and international organizations.

Due to growing interest in the NBG's expertise from regional and European central banks, a centralized educational space is being developed by the Department of Financial Education and Strategic Development. This platform will offer continuous learning opportunities through online, in-person, and hybrid training programs.

Covering topics like macroeconomics, payment systems, and financial stability, the platform caters to both internal and external audiences. It aims to share the NBG's knowledge and best practices through lectures and training programs.

To ensure the platform's effectiveness, extensive consultations were conducted throughout the year. This included market research, internal resource evaluation, and discussions with local and international organizations.

Within 2 months after its creation, the department presented the initiative/concept to create an educational space to a number of local and international partners and potential donor organizations, including the International Monetary Fund (IMF), IMF Regional Capacity Development Center for the Caucasus, Central Asia, and Mongolia (CCAMTAC), Joint Vienna Institute

(JVI), Gerzense Training Center, The House of Training Training (ATTF Luxembourg) Training Centers of Swiss, and Polish Central Banks. Meetings with educational academies and associations were also held in Georgia.

### **E-learning for Capital Market Participants**

The Educational Space of the National Bank of Georgia focuses on encouraging representatives of financial institutions by providing them with access to training programs. The National Bank of Georgia, with support from the European Bank for Reconstruction and Development, is offering a new e-learning program to representatives of the Georgian capital market. This program, hosted on the platform <https://www.capitalmarketselearning.com/resources>, aims to enhance their knowledge and skills.

Thirty participants from brokerage and asset management companies will gain insights into various capital market aspects. The program, developed by Intuition, a leading international company, covers key concepts, investment strategies, financial markets, risk management, and more.

A program presentation was held on December 19th, led by Natia Turnava, Acting Governor of the National Bank of Georgia. This initiative is expected to significantly contribute to the development of Georgia's capital market.



# NON-BANK SUPERVISION

07

## 7.1. REGULATION OF NON-BANKING SECTOR AND REGULATORY FRAMEWORK



As of December 31, 2023, the non-bank financial sector consists of 34 microfinance organizations, 169 lending entities, 510 currency exchange offices, and one credit union. The total assets of the non-banking financial sector amount to 2.6 billion GEL, which is 3% of the

financial sector. Microfinance organizations hold the largest share of assets, at 2 billion GEL.

While the non-banking sector is not large, it plays a role in providing financial services to businesses and residents in Georgia's regions. Organizations in this sector operate in up to 1,500 locations and employ up to 7,000 people. The size of the sector's user base increases its responsibility in the process of providing services.

	Microfinance organization	Lending entity	Currency exchange office	Total
Number of branches	398	330	728	1,456
Number of staff	4,474	2,452	1,846	6,926
Number of borrowers	524,626	592,882		1,063,626

Recent improvements in the regulatory framework of the non-bank financial sector have led to an increase in its credibility and reputation, resulting in increased funding from non-resident institutional lenders. The sector has successfully overcome the negative effects of the past years and maintains adequate capital and liquidity ratios, a stable growth rate, and profitability.

Amendments to the Law of Georgia "On Microfinance Organizations" came into force in 2023, mainly due to the implementation of microbank legislation. As a result of these changes, microfinance organizations can be transformed into microbanks or commercial banks without undergoing a liquidation process. Certain practices were also regulated, and lending entities were permitted to operate only as limited liability companies or joint-stock companies. Additionally,

lending entities were granted the right to perform currency exchange operations without the need for additional registration as a currency exchange office.

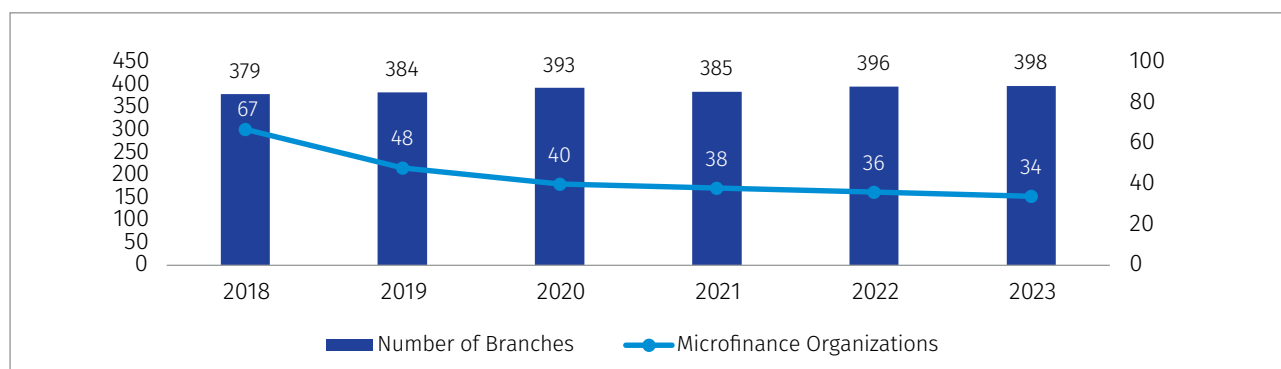
To ensure compliance with current legislation and the accuracy of reporting data, remote supervision of non-banking institutions was conducted in parallel with an active inspection process throughout 2023.

## 7.2. MICROFINANCE ORGANIZATIONS



In 2023, the registration of two microfinance organizations was revoked, however, due to their insignificant market share, this fact did not have a negative impact on the growth rate of the total assets of the sector.

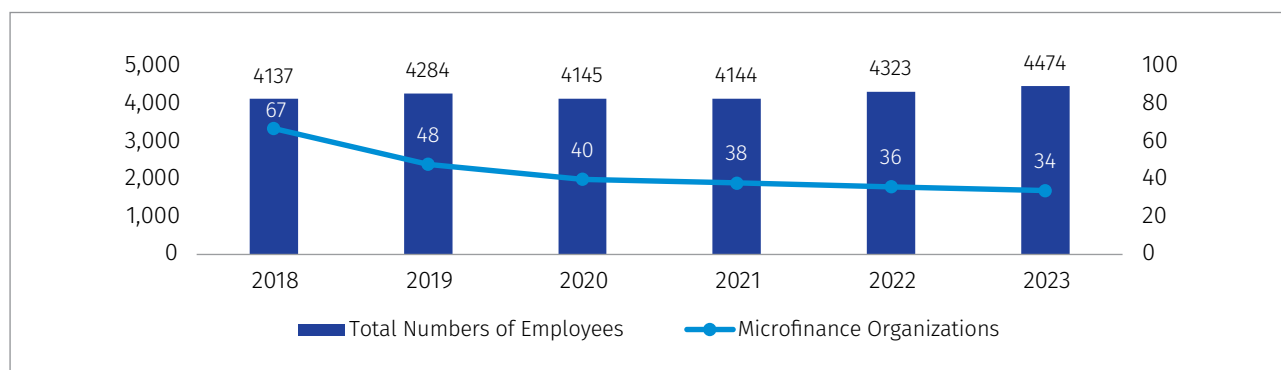
Diagram N 7.1 Number of microfinance organizations and branches



Source: NBG

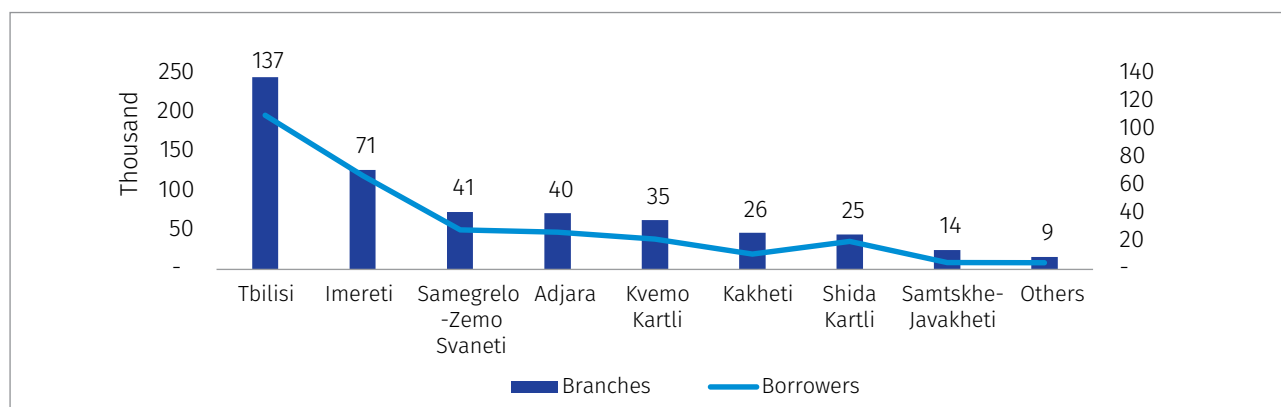
During the year, there was an increase in the number of branches and employees of operating microfinance organizations.

Diagram N 7.2 Number of staff at microfinance organizations



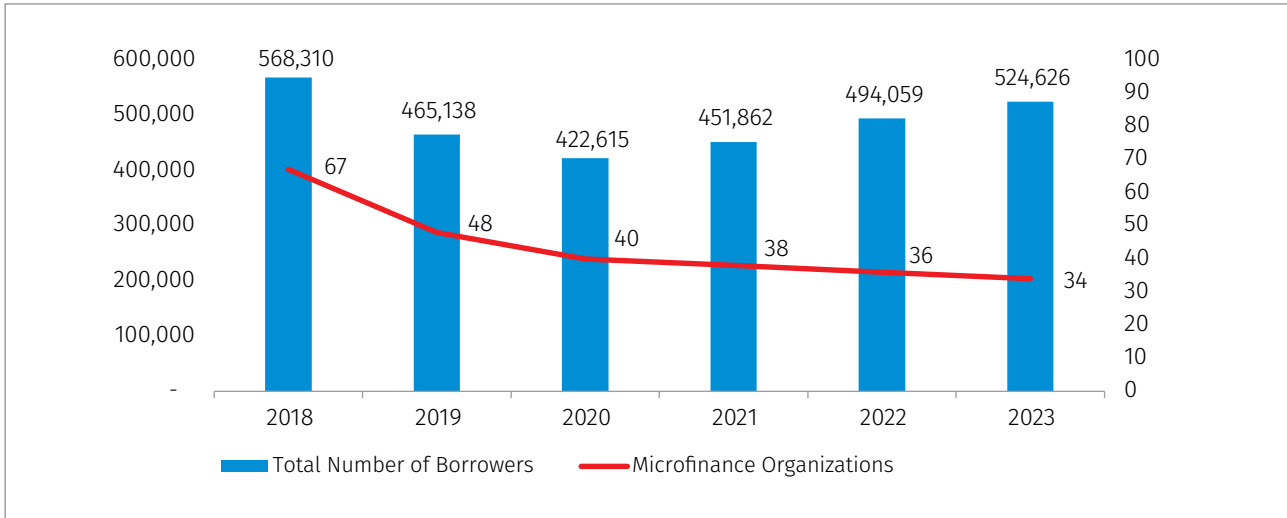
Source: NBG

Diagram N 7.3 Regional distribution of the branches and borrowers of microfinance organizations



Source: NBG

Diagram N 7.4 Number of microfinance organizations and borrowers

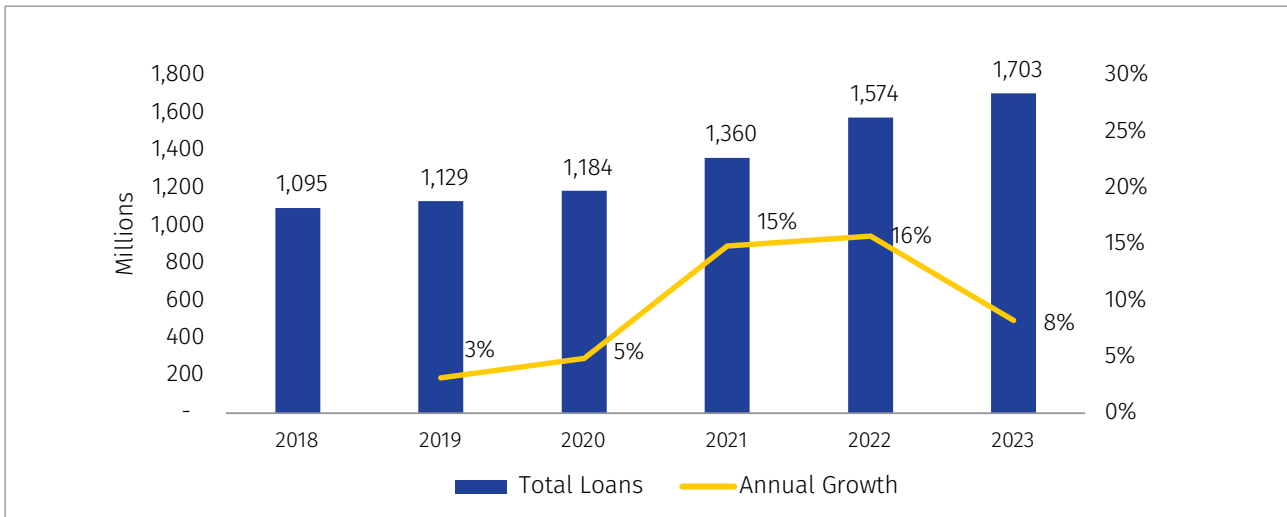


Source: NBG

During the year, parallel to the growing trend of the number of borrowers, the loan portfolio also main-

tained its growth trend (annual growth rate of 8 per-cent) and amounted to 1.7 billion GEL.

Diagram N 7.5 Volume of loan portfolio of microfinance organizations

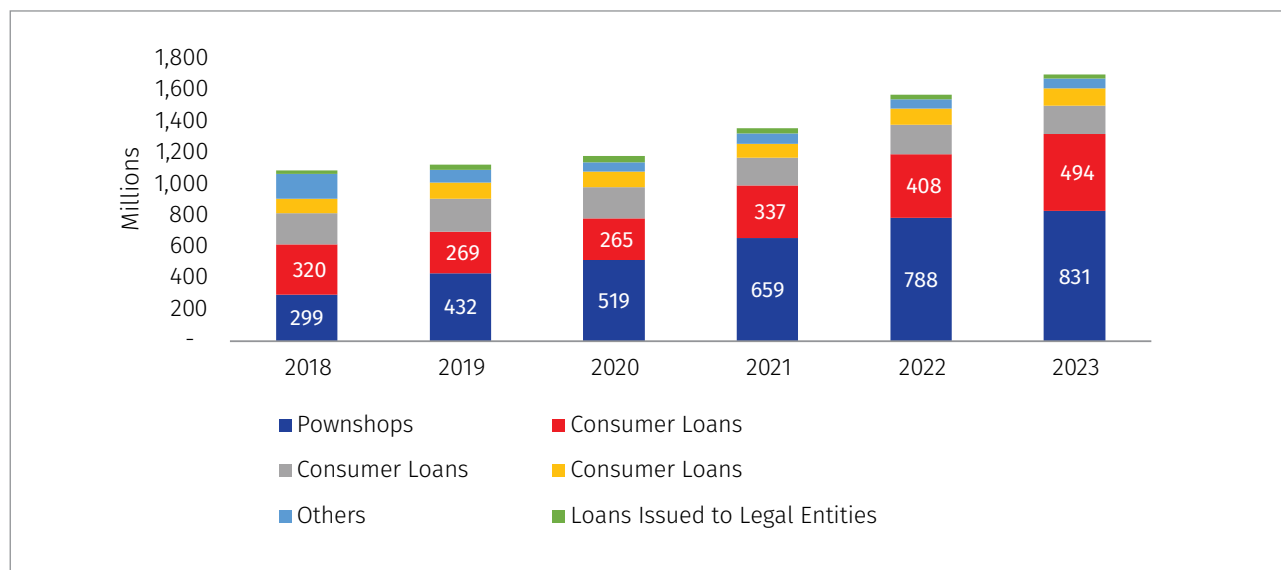


Source: NBG

Importantly, the growth rate of the loan portfolio is twice as low as the previous year, which is due to the pawnshop portfolio. The growth rate of that portfolio peaked in 2022, which is somewhat related to the post-pandemic effects.

The main direction of lending in the microfinance sector is consumer loans issued to individuals (pawnshop, consumer loans, etc.) and constitutes 81 percent of the sector's total loan portfolio, amounting to 1.4 billion GEL. The remaining 19 percent comes from loans given to agriculture, trade-service sector and legal entities, amounting to 317 million GEL.

Diagram N 7.6 Loan Portfolio Structure



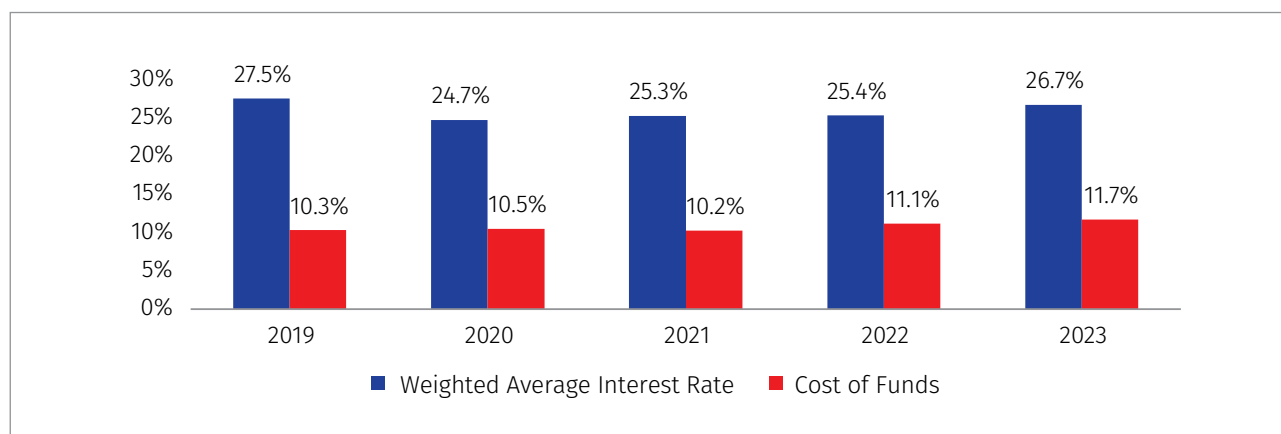
Source: NBG

The growth rate of total assets of the sector was mainly due to the growth of consumer loans: out of the 130 million GEL annual growth of the credit portfolio, 86 million GEL comes from consumer loans and 43 million GEL from pawn loans. During the year, a decrease of 8 million GEL was observed in the trade-service sector

and loans granted to legal entities.

The increase in the value of the funds of the microfinance sector was partly due to the increased interest rate on the funds raised from the resident commercial banks.

Diagram N 7.7 Cost of the weighted average interest rates and funds in the portfolio

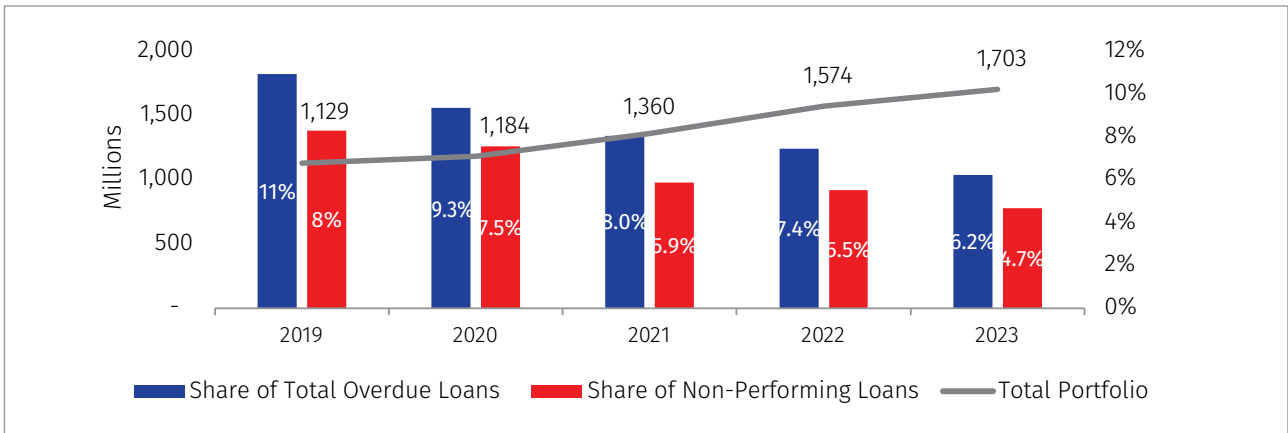


Source: NBG

In terms of improving the quality of the loan portfolio, the positive trend continues in 2023 as well: compared to last year's indicators, the share of non-performing loans in the total portfolio decreased by 0.8 pp, and

the share of overdue portfolio decreased by 1.2 pp. The issuance of new loans also influenced the above to some extent.

Diagram N 7.8 Loan Portfolio Quality

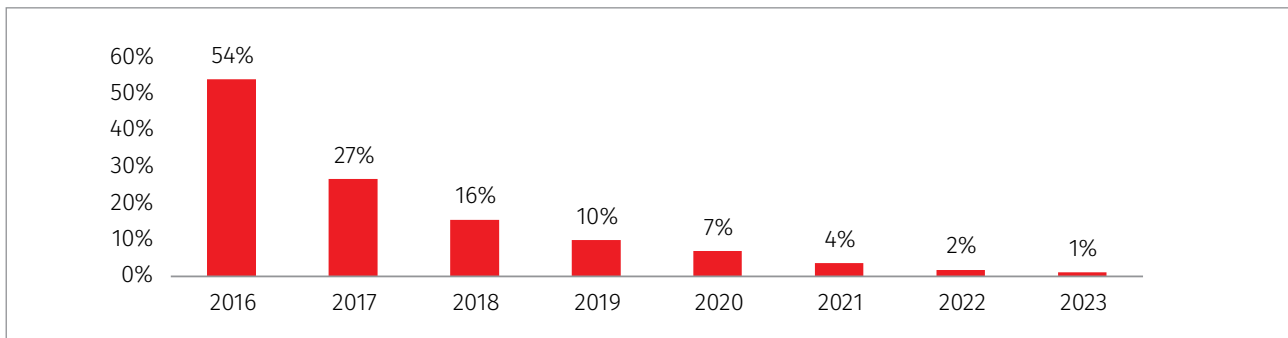


Source: NBG

In light of the changes made in Article 625 of the Civil Code of Georgia regarding the prohibition of issuing loans in foreign currency up to 200 thousand GEL to an

individual, the trend of dollarization of the loan portfolio is maintained.

Diagram N 7.9 Dollarization of the loan portfolio

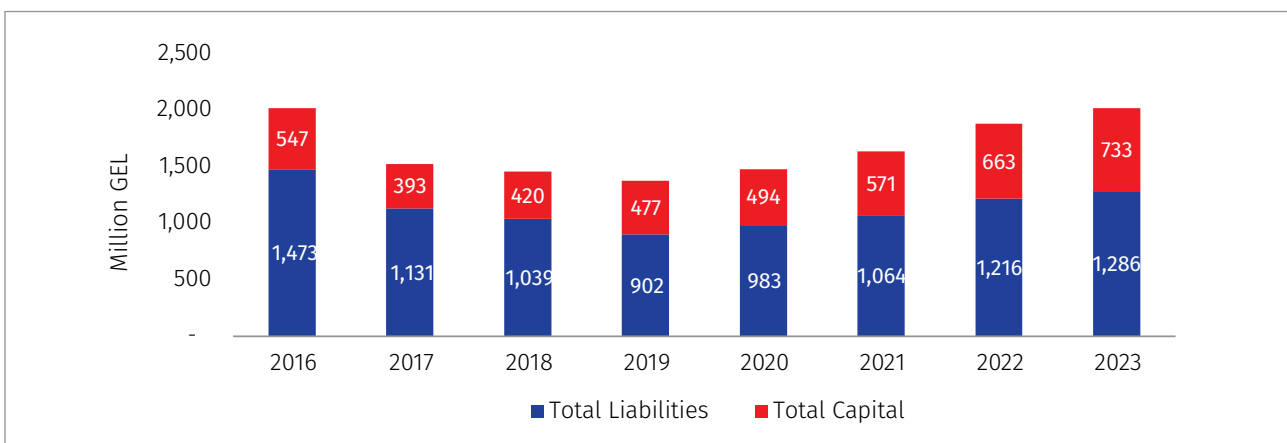


Source: NBG

Despite the 11% increase in the volume of capital, its share in the funding structure is similar to previous

years and is set at 36%. Liabilities increased by 7 percent during the year, amounting to 80 million GEL.

Diagram N 7.10 Source of Funding

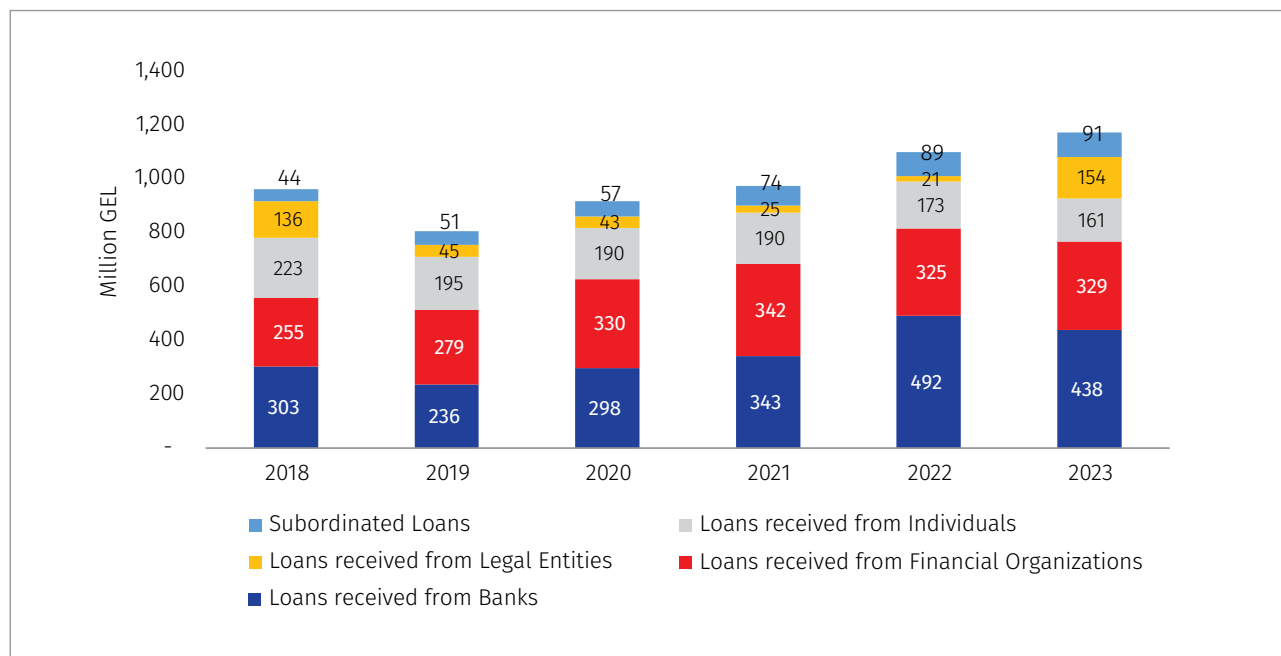


Source: NBG

Borrowings increased by 73 million GEL in 2023. The 66 million GEL decrease in loans received from banks

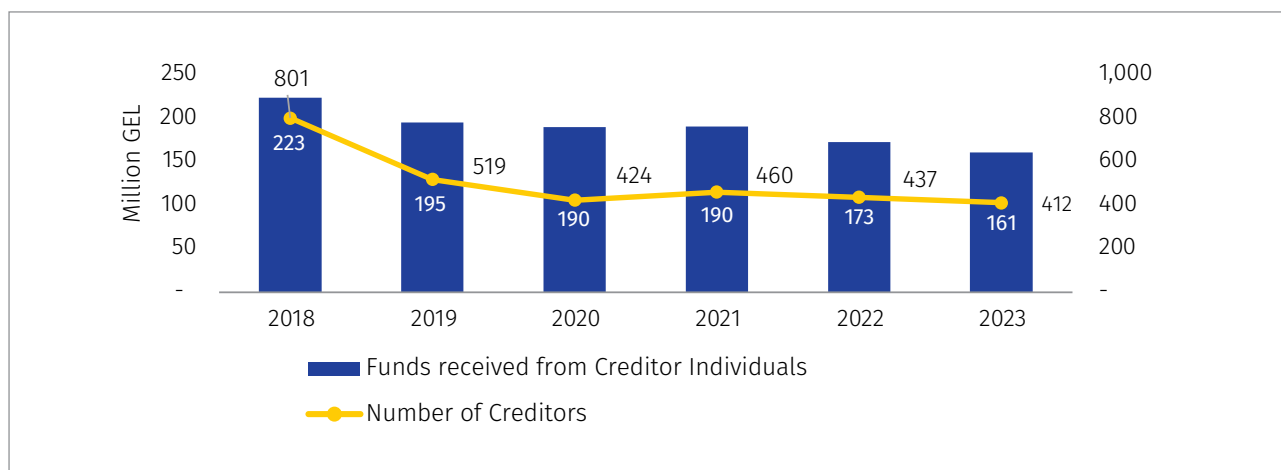
and individuals was mostly covered by the increase in loans received from legal entities.

Diagram N 7.11 Borrowings Structure



Source: NBG

Diagram N 7.12 Borrowings from individuals and the number of individual creditors

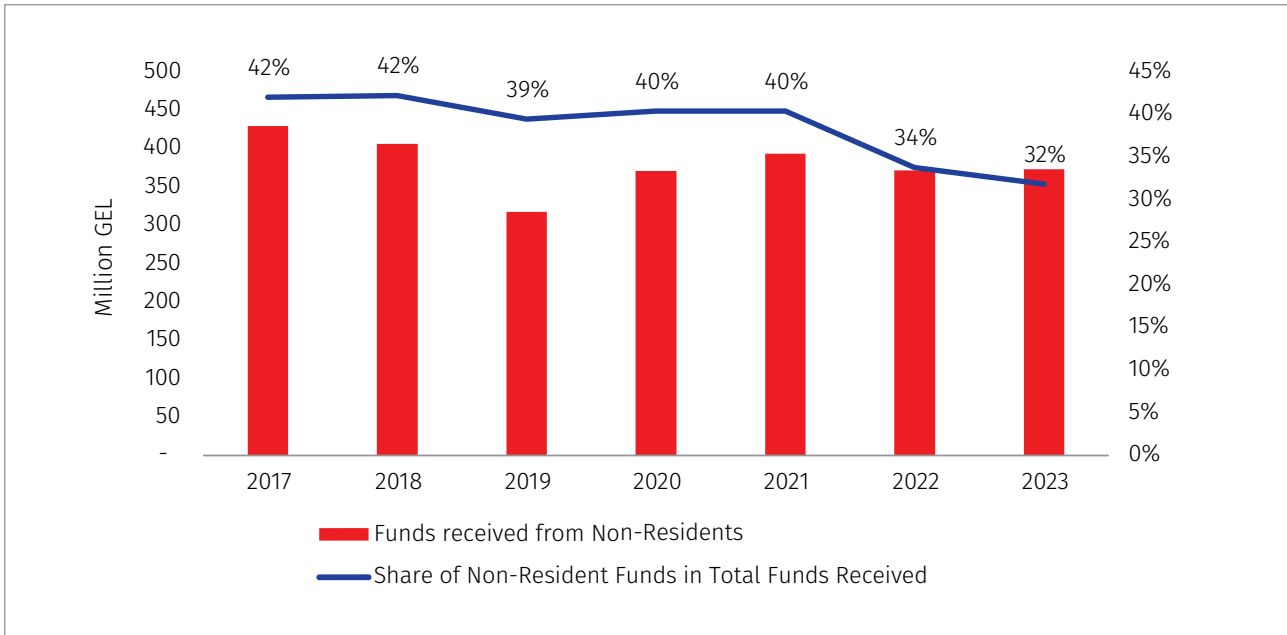


Source: NBG

Although the share of borrowed funds from non-resident persons in borrowings continues to decrease like

the previous year, going down by 2 pp, although it increased by 2 million GEL.

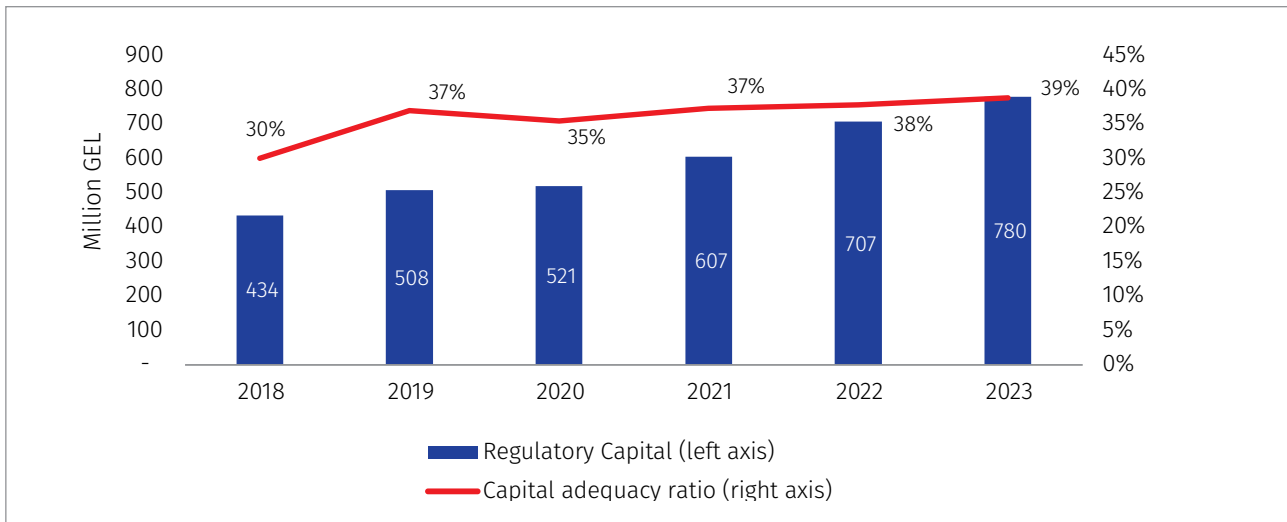
Diagram N 7.13 Funds of non-residents



Source: NBG

As in previous years, the capital adequacy of the sector is still at a high level.

Diagram N 7.14 Regulatory Capital

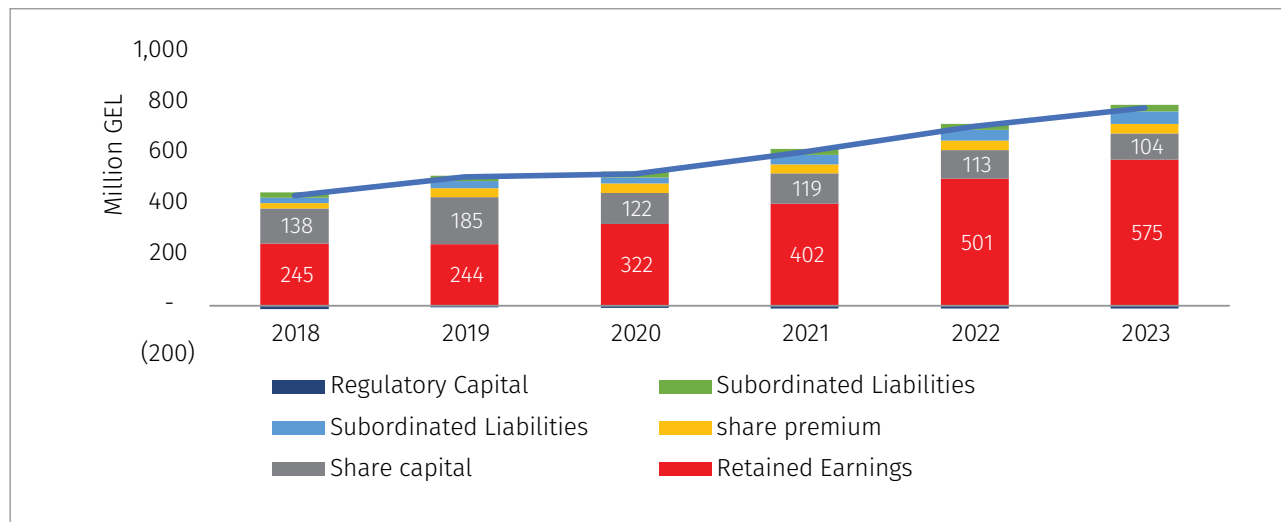


Source: NBG

A 10 percent increase in regulatory capital, amounting to 73 million GEL, was mainly due to the increase in retained earnings. The reduction of the authorized

capital is related to the microfinance organizations liquidated during the year.

Diagram N 7.15 Structure of Regulatory Capital

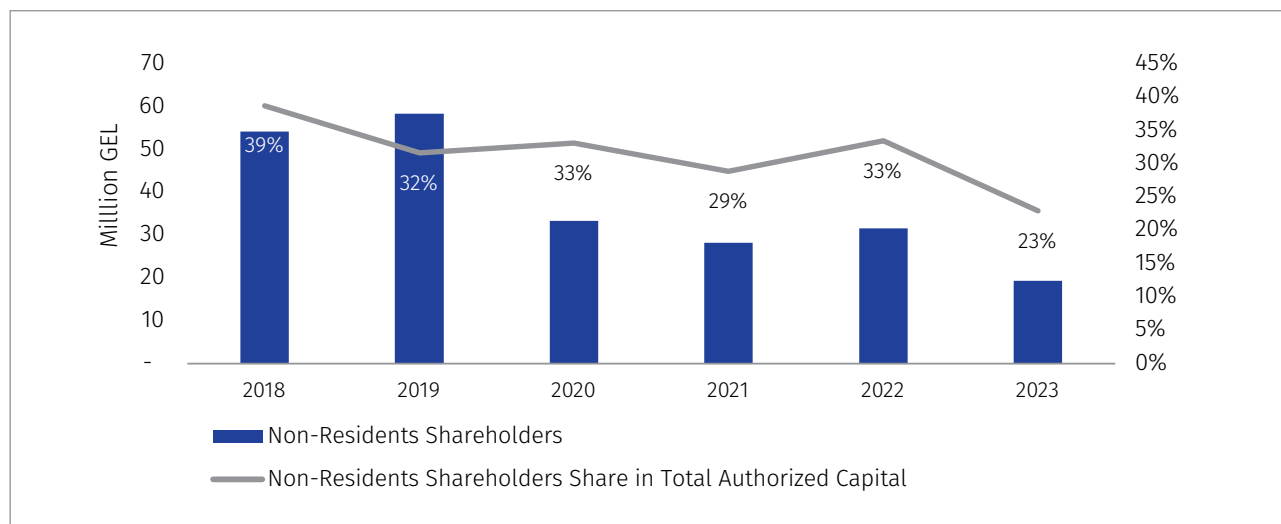


Source: NBG

Decrease in the share of non-resident shareholders in the authorized capital from 33 percent to 23 percent

was mainly the effect of a microfinance organization who went into liquidation.

Diagram N 7.16 Capital structure by residency

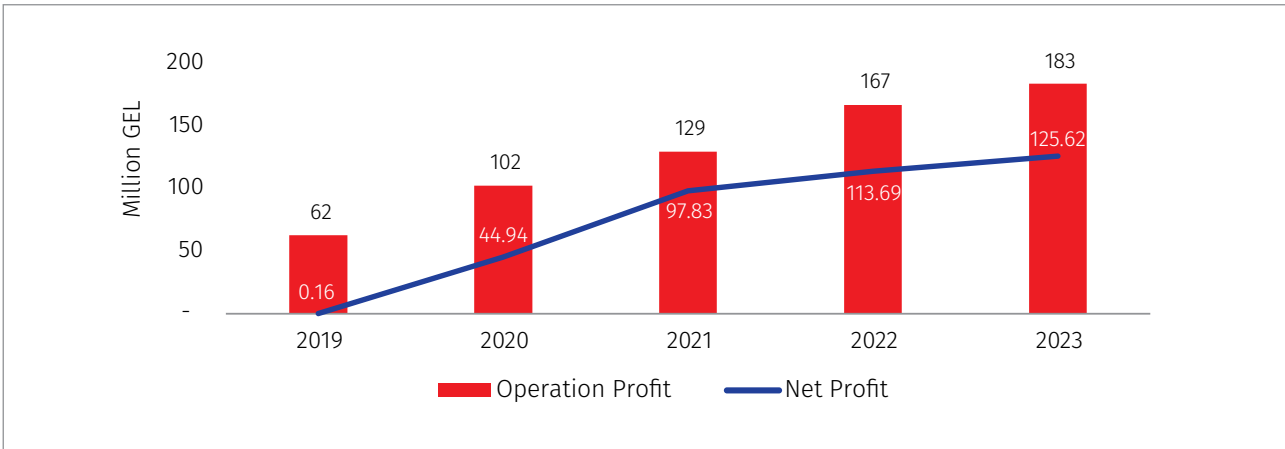


Source: NBG

Majority of microfinance organizations ended 2023 with a profit, and despite the liquidation of two micro-

finance organizations, the sector showed higher profitability during the year than the previous year.

Diagram N 7.17 Dynamics of net and operating income



Source: NBG

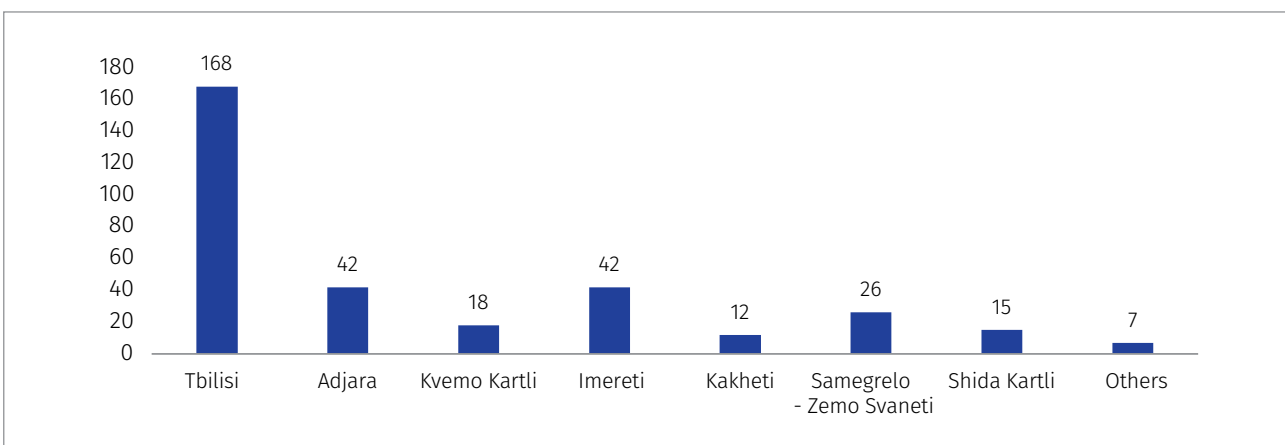
The dynamics of operating profit growth is consistent with the growth of the loan portfolio, having increased by 10% compared to the previous year.

The sector's return on equity stood at 18%, similar to last year's figure, while return on assets increased from 6% to 7%.

### 7.2.1. LENDING ENTITIES

During 2023, 21 new lending entities were registered and 21 branch activity permits were issued. The registration of 28 lending entities was revoked, and the branch activity permit was terminated for 16. Accordingly, as of December 31, the number of registered lending entities amounted to 169, which, together with branches, are located in 330 locations throughout the country.

Diagram N 7.18 Regional distribution of structural units of lending entities

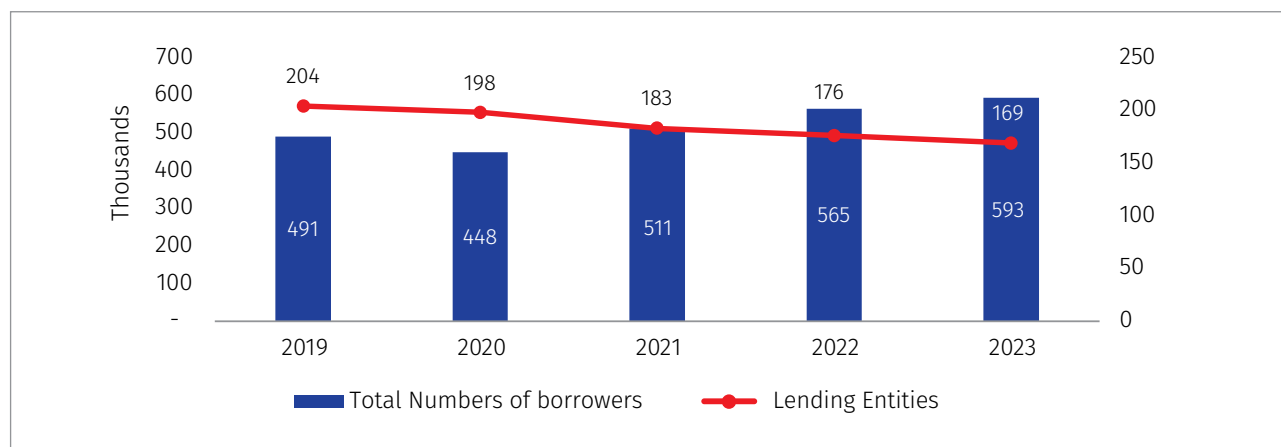


Source: NBG

It is important to note that more than half of the total number of borrowers in the non-banking sector come from lending entities and are mainly represented by individuals, since this sector is mostly focuses on gran-

ular/small-scale consumer and pawn products. Lending organizations also work on recovering problematic consumer loans.

Diagram N 7.19 Lending entities and the number of borrowers

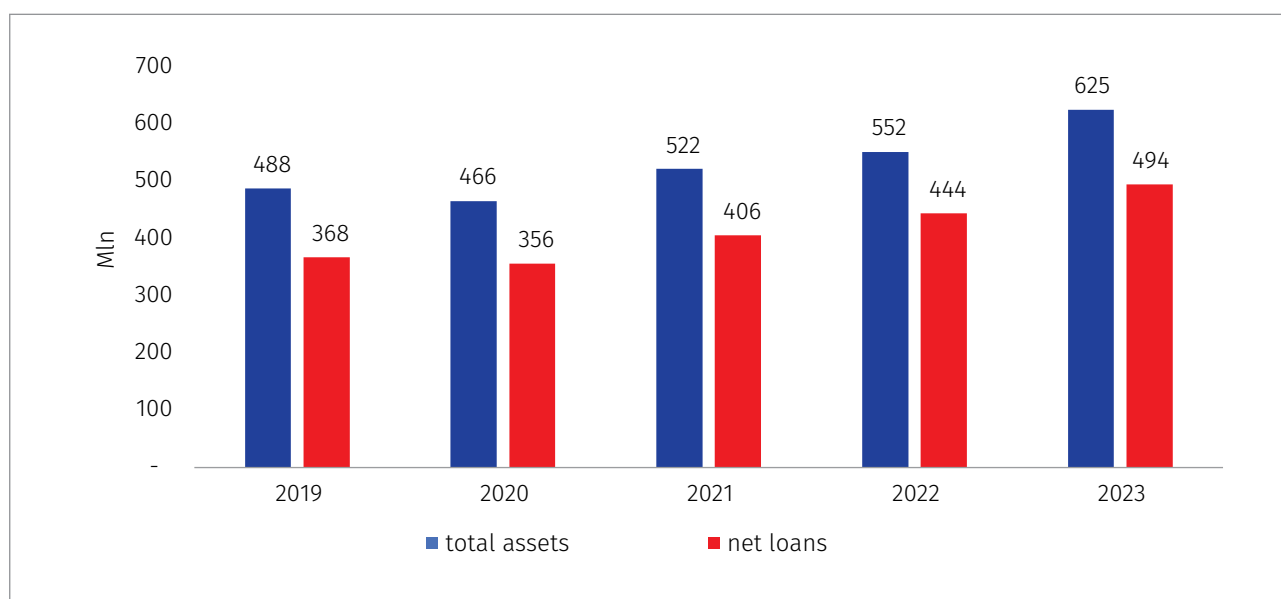


Source: NBG

The reduction in the number of lending entities by 7 units did not affect the volume of total assets and net loans of this sector. Rather, the growth of total assets

was 13 percent, and the growth of net loans was 11 percent during the year.

Diagram N 7.20 Dynamics of total assets and net loans

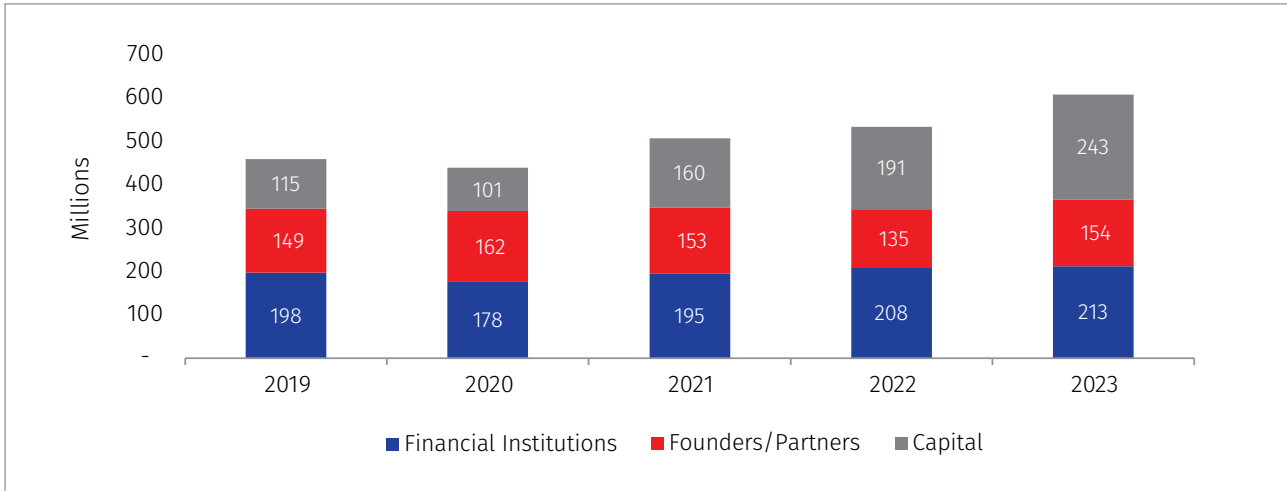


Source: NBG

Funds received from partners and financial institutions constitute the main source of financing of the sector of lending entities. However, it should be noted that

a positive trend of capital growth has been observed over the last year.

Diagram N 7.21 Source of funding for lending entities



Source: NBG

As of December 31, 2023, return on equity and assets amounted to 27 and 4 percent, respectively.

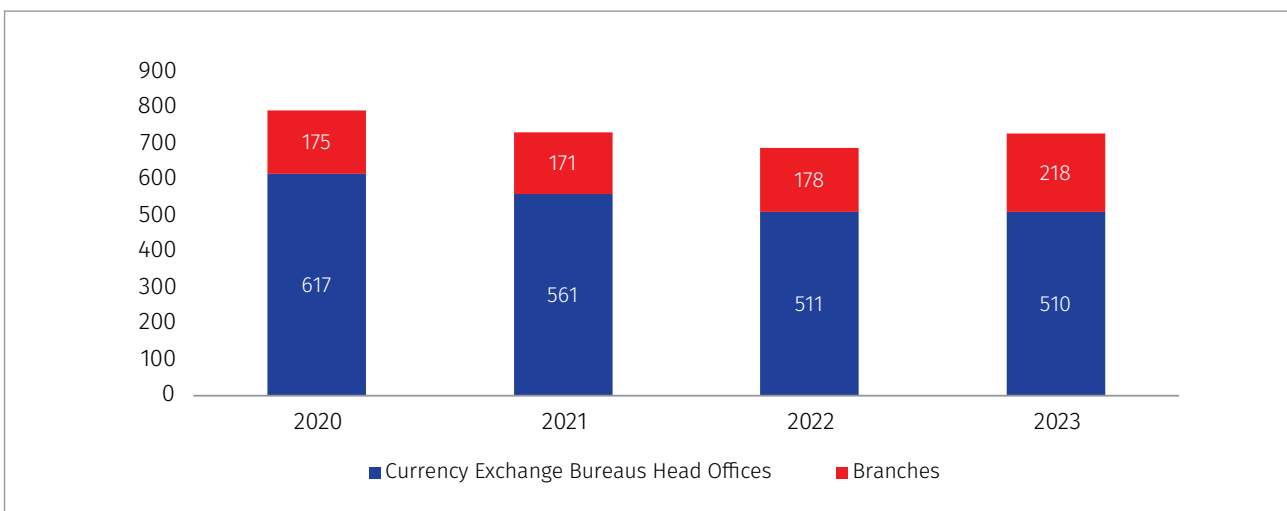
### 7.2.2. CURRENCY EXCHANGE BUREAUS

During 2023, 64 new currency exchange bureaus were registered and 69 branch activity permits were issued. The registration of 65 currency exchange bureaus was cancelled, and the branch activity permit was terminated for 29. The registration of 52 of the canceled currency exchange bureaus was canceled

based on their own application, the majority of which were in Tbilisi. The registration of the remaining units was canceled due to non-compliance with the requirements established by the law.

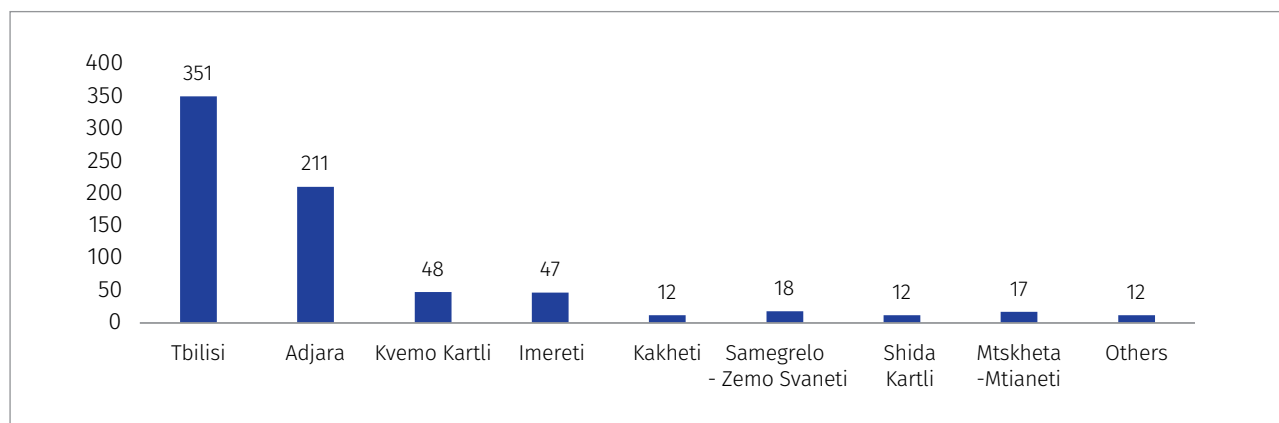
As of December 31, the number of registered currency exchange offices amounted to 510, which, together with branches, are located in 728 locations throughout the country.

Diagram N 7.22 number and branches of currency exchange bureaus



Source: NBG

Diagram N 7.23 Regional distribution of structural units of currency exchange bureaus



Source: NBG

In 2023, 321 units of currency exchange bureaus (headquarters/branches) were inspected on site in 4 regions of Georgia in order to determine compliance with the requirements established by the *Regulation on Registering and Regulating Currency Exchange Bureaus*, approved under decree of the Governor of the National Bank of Georgia No. 37/04 of February 28, 2018. Of the inspected currency exchange offices and branches, 68 units fully complied with the established requirements, 78 units were sent a written warning, 161 units were fined in the total amount of 856,000 GEL, and 14 units could not be fully inspected for various reasons.

### 7.2.3. CREDIT UNIONS

The legislative amendments of 2017 set the limit for the number of members in a credit union, and defined the principles of their operation. It meant bringing together the individuals residing in the administrative unit of the same self-governing community and uniting them on a common ground. These changes served to eliminate the unsound practices established in the sector, the practices being that the credit unions had used the funds attracted as deposits from the members for the lending activities that were inappropriate the purposes of the cooperative.

As of December 31, 2023, only one credit union with assets of GEL 0.5 million continued to operate in the market.



# SECURITIES MARKET

08

## 8.1. ACTIVITIES IMPLEMENTED TO DEVELOP THE SECURITIES MARKET AND MEASURES TAKEN TO ENHANCE THE TRANSPARENCY OF THE MARKET



The NBG undertook significant efforts to develop the securities market and implement supervisory measures to promote transparency.

The year 2023 was important in terms of the development of the regulatory framework for structured financial products. With the participation of the NBG, the Law of Georgia “On Securitization” was approved by the Parliament of Georgia, and the NBG issued the *Regulation “On Covered Bonds”*.

In 2023, the NBG, in cooperation with the international rating agency Moody's and the European Bank for Reconstruction and Development (EBRD), hosted an event dedicated to covered bonds, to provide financial sector participants with information on the dynamics of the covered bond market, credit rating approaches and instrument pricing, along with consideration of other practical aspects relevant to issuers and investors. It is noteworthy that such an event was held in Georgia for the first time. The participants had the opportunity to receive important information about the covered bond market from representatives of Moody's, the European Covered Bond Council (ECBC) and the EBRD. The experts shared their extensive experience from Eastern Europe and international markets with the representatives of the financial sector of Georgia.

The efforts made by the NBG in introduction of covered bonds were highlighted in the influential international publication of ECBC, in which current issues of the covered bond market are discussed. The publication positively reviewed the law on covered bonds adopted by the Parliament of Georgia in 2022, as well as the regulation on covered bonds approved by the NBG in

2023 based on it. It is emphasized in the publication that the regulatory framework of covered bonds operating in Georgia is in full compliance with the requirements of the EU legislation. In 2023, the NBG was invited to the Working Group of European Supervisors of Covered Bonds organized by the Association of German Covered Bond-Issuing Commercial Banks (Verband deutscher Pfandbriefbanken - vdp).

In 2023, the NBG continued to promote the development of the investment funds market. With the support of the NBG, the first regional venture investment summit - Central Eurasia Venture Summit was held in Georgia to promote the development of venture capital investment funds in Georgia and the countries of the region. In the panel discussion held within the summit, the participants had an in-depth discussion of the opportunities and challenges that the startup ecosystem and venture capital funds are facing in the countries of the region today. More than 20 regional venture funds from Turkey, Czech Republic, Kazakhstan, Uzbekistan, Great Britain, Armenia and other countries participated in the summit. The summit was also attended by heads of regional innovation agencies, representatives of organizations focused on the development of the startup ecosystem, as well as independent investors and startups.

The steps taken by the country, including the NBG, to improve the regulatory framework of securities in recent years were positively assessed by the European Commission in the report<sup>71</sup> published in 2023 regarding Georgia's application to join the European Union. The report indicates that the *corporate governance code of public securities issuers* developed by the NBG reflects the recommendations of the European Commission and the principles of the Organization for Economic Cooperation and Development (OECD). The report also mentions that the framework for the prevention of insider trading and market manipulation, as well as the legislation regulating collective investment schemes (investment funds) in Georgia is in line with the requirements of the European Union.

71. Analytical Report following the Communication from the Commission to the European Parliament, the European Council and the Council, Commission Opinion on Georgia's application for membership of the European Union (Brussels, 1.2.2023 SWD(2023) 31).

In 2023, the National Bank of Georgia continued to protect the rights of investors in the securities market within its mandate. In order to ensure transparency in the market, supervisory measures were taken against 24 issuers for non-submission or submission with

violations of annual reports in 2023 (of those, 9 were fined), and for non-submission or submission with violations of semi-annual reports in 2023 - against 7 issuers (6 of them were fined).

## THE LAW ON HOLDING DEMATERIALIZED SECURITIES

In December 2023, the Parliament of Georgia approved the Law of Georgia "On Holding Dematerialized Securities" along with related amendments to the Law "On Securities Market" and several other legislative acts. The legislative package was prepared with the participation of experts from the National Bank of Georgia and the International Monetary Fund. The Ministry of Economy and Sustainable Development was also actively involved in the process, and consultations were conducted with relevant representatives of the local financial sector.

The new law defines the legal status of dematerialized securities and addresses the legal aspects of their issuance, custody, disposal, payment of coupons and dividends, and redemption. The law also establishes the roles, obligations, and rights of issuers, central depositories, custodians, and other financial intermediaries throughout these stages.

With this legislative act, Georgia's securities market becomes more compatible with EU standards and best international practices. The adoption of the new law will also simplify the process of issuing securities in Georgia and better protect investors' interests.

## LAW OF SECURITIZATION

In December 2023, the Parliament of Georgia approved the law on securitization and related legislative amendments. The law regulates the conversion of long-term cash assets (future receivables from customers) into liquid assets by business entities through the issuance of securities. The new legal framework substantially reduces the risks associated with securitization and provides transaction transparency for investors.

The goal of the reform is to increase the availability of financing in the country for both the financial and non-financial sectors. The new law will allow business entities to convert stable flows of future receivables into current liquid assets and expand their activities based on that.

The law was developed under the authorship of the National Bank of Georgia and the Ministry of Economy and Sustainable Development, and is based on the best European practices. In particular, the law incorporates approaches from jurisdictions with a developed securitization market, such as Luxembourg, as well as the principles and main provisions of the securitization regulation in force in the European Union. The Asian Development Bank, the European Bank for Reconstruction and Development, and the United States Agency for International Development provided active support in the process of developing the law.

## 8.2. SECURITIES MARKET INDICATORS



As in previous years, the local securities market continued to grow in 2023. The development of a number of legislative/regulatory reforms and the introduction of new products will help maintain this dynamic and develop the capital market.

### Bonds Market

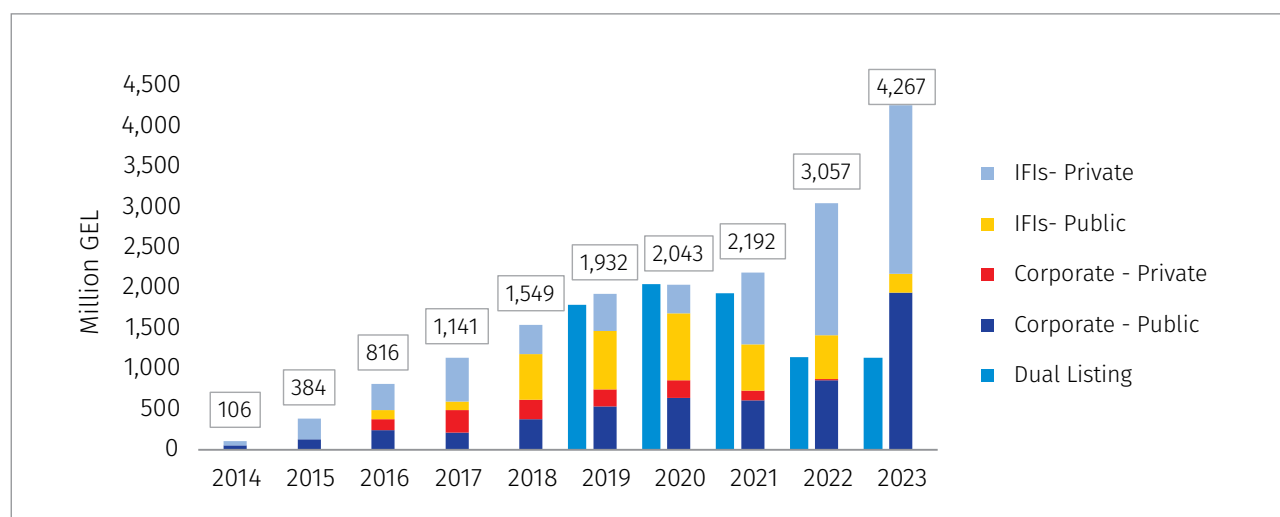
The year 2023 saw a growing trend in the bond market. This market segment grew by 39.6<sup>72</sup> percent and was 5.32<sup>73</sup> percent of GDP in size. Of the bonds issued, 54.4% were GEL denominated bonds by international financial institutions. Notably, quotes from international financial institutions increased by 6.4%, while the corporate bond segment went up by 121.9%.

The upward trend continued in the bond market in

2023. Compared to the previous year, this segment of the market increased by 39.6 percent, and its size was 5.32 percent of the gross domestic product. 54.4 percent of the issued bonds were those denominated in GEL issued by international financial institutions. The market of bonds issued by international financial institutions grew by 6.4 percent, and the segment of corporate bonds grew by 121.9 percent. Hence, at the end of 2023, the size of the corporate bond market amounted to 1.947 billion<sup>74</sup> GEL. The average growth rate of the public corporate bond market in the last 5 years reached 38.7 percent.

In 2023, 7 local environmental and social corporate bonds were issued on the capital market (three green, one gender, and three related to sustainability), the total value of which amounted to 537.4 million GEL. In 2023, 21 public corporate bonds (2022: 8) and 4 private bonds of international financial institutions were issued on the local market (2022: 7) (see diagram No. 8.1).

Diagram N 8.1 Outstanding Non-Government Bonds at the end of the period (2014-2023)



Source: NBG, Georgian Stock Exchange, Bloomberg, Other public sources

72. The data includes public corporate bonds issued in the local market, private corporate bonds known to the National Bank of Georgia, and public and private bonds issued by international financial institutions (IFIs) in the local market. The data does not include non-governmental debt securities and certificates of deposit dually listed on the Georgian Stock Exchange.

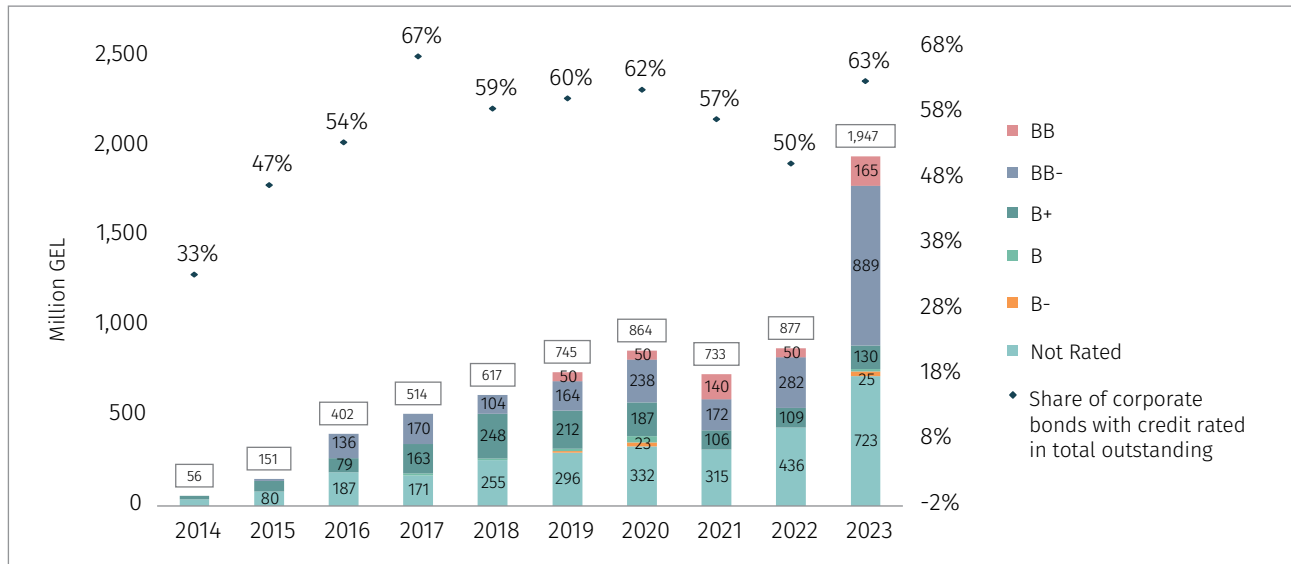
73. The expected value of the gross domestic product in 2023 is taken based on the preliminary data of the gross domestic product of 2023 published by the National Statistical Service of Georgia.

74. The data includes only public corporate bonds issued in the local market. The data does not include dually listed non-governmental debt securities and certificates of deposit on the Georgian Stock Exchange.

Of the corporate bonds issued in 2023, 72.8% were rated by international rating agencies, which is significantly higher than the 36.7% indicator (by value) of 2022. As for the balances at the end of 2023, 63% of

corporate bonds were rated (2022 : 50%). In 2023, 13.5% of market-rated corporate bond balances were rated BB (2022: 11.3% interest), and 86.11% were rated BB/BB (2022: 75.2% interest).

Diagram N 8.2 Outstandings Corporate Bonds by International Credit Ratings (2014-2023)<sup>75</sup>

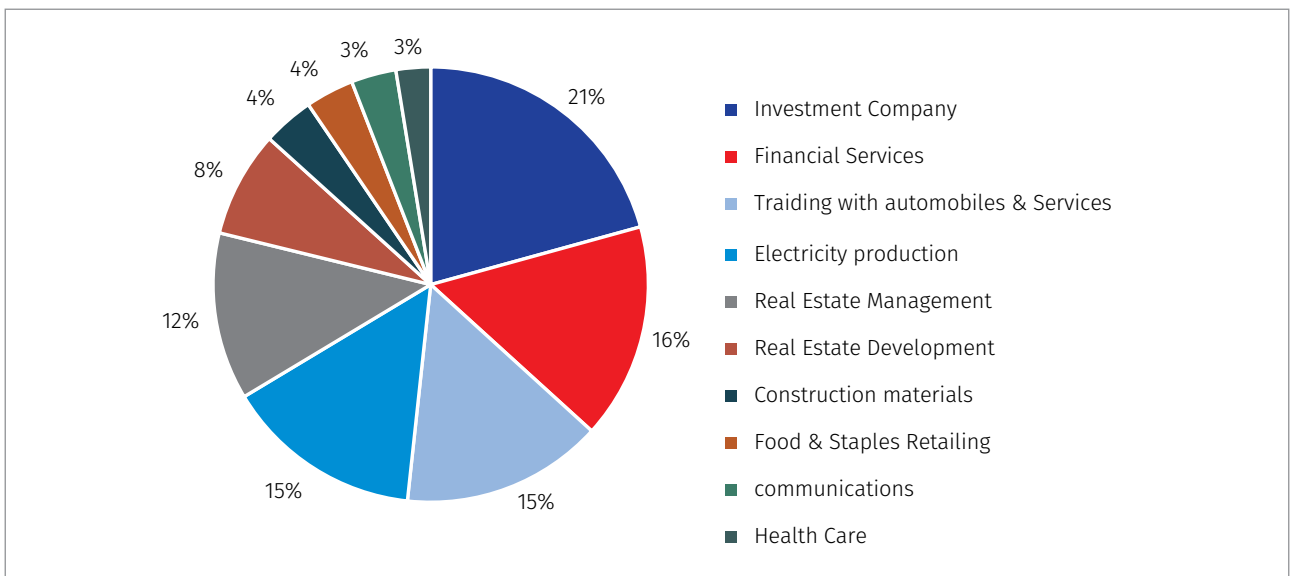


Source: NBG

In 2023, the corporate bond market was diversified by industry and included issuers from 10 industries. In terms of corporate bond balances, investment companies held the largest share of the market at 21% (power generation held the largest share at 26% in 2022), with

the next three largest sectors - financial services, automotive trade and services, and power generation - collectively accounting for bonds. represented 46% of the market.

Diagram N 8.3 Industry distribution of outstandings corporate bonds (2022)

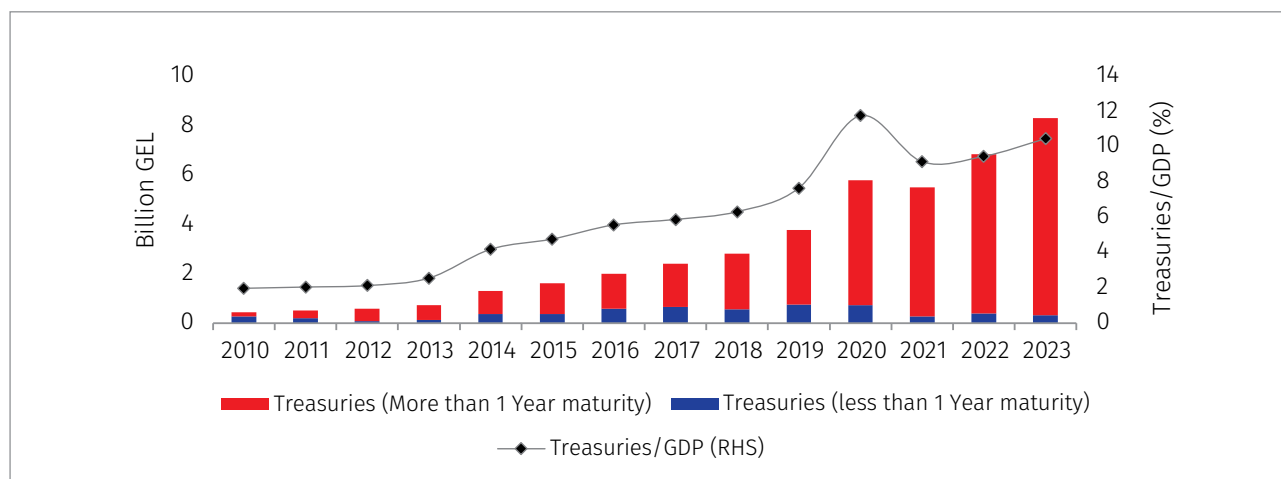


Source: NBG

75. For bonds that do not have their own rating, the long-term credit rating of the corporation (issuer) is assigned, taking into account the currency of the bond issue.

After a 24.5 percent increase in 2022, the Treasury bond market ended 2023 with a 21.4 percent increase, and the balance was 10.3 percent of GDP. (see diagram No. 8.4)

Diagram N 8.4 Outstandings Treasury Securities by Maturities (2010-2023)

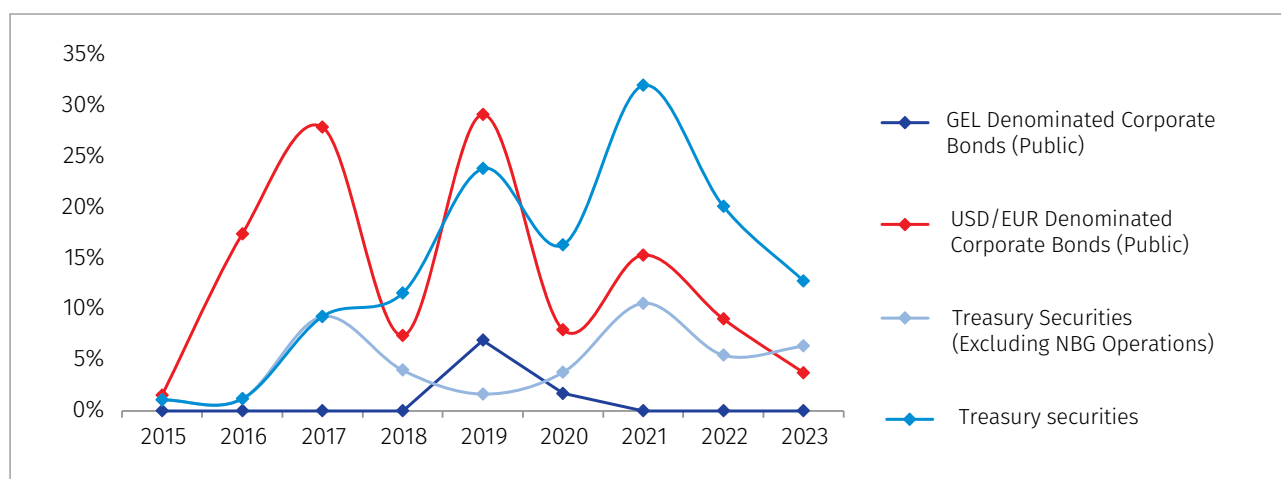


source: Ministry of Finance of Georgia, GeoStat

In 2023, the indicator<sup>76</sup> of local market liquidity varies for different segments of the bond market. For bonds denominated in foreign currency in the corporate securities market, this indicator is 4%. As for Treasury se-

curities, the liquidity rate was 13%, including the NBG operations, and without it - 6%. Liquidity in the GEL corporate bond market is still 0%.

Diagram N 8.5 Secondary Market Activity for debt securities issued in Georgia<sup>77</sup> (2015-2023)

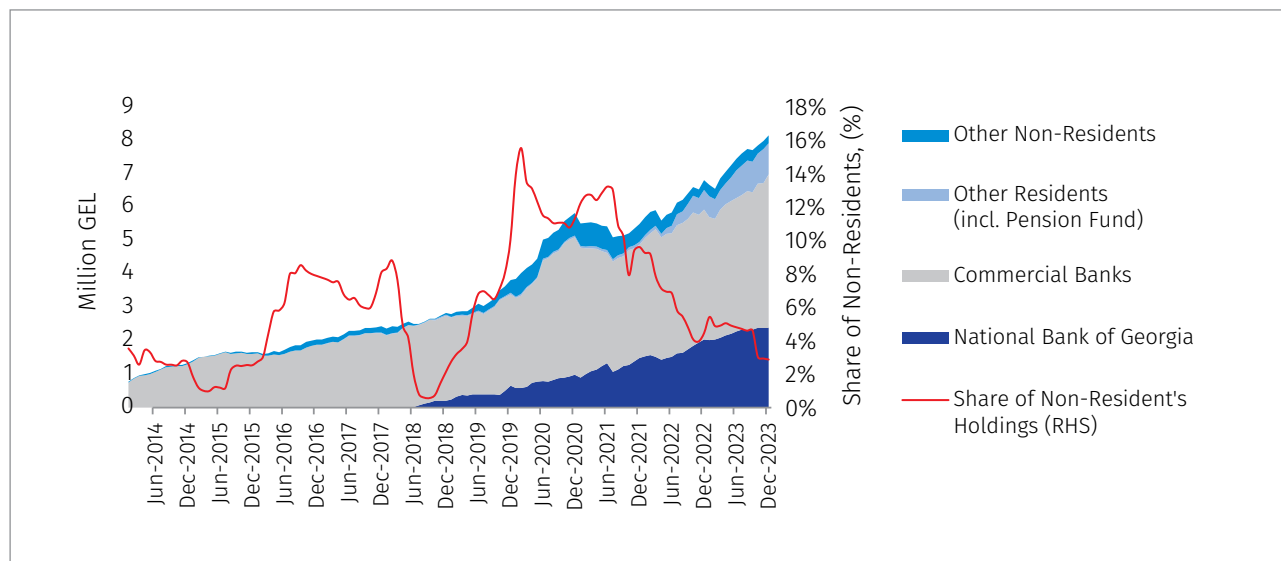


source: NBG, Georgian Stock Exchange

76. The data is calculated by the ratio of the value of transactions performed in the secondary market during the year to the average annual balance of bonds.

77. The graph shows the secondary market activity during the year by comparing the volume of secondary market transactions with the average annual balances of securities.

Diagram N 8.6 Distribution of Treasury securities by ownership (2014-2023)



Source: NBG; Ministry of Finance

### 8.3. OVERVIEW OF MARKET PLAYERS



By the end of 2023, there were 2 stock exchanges, 1 central securities depository, 9 brokerages and 3 independent securities registrars operating in the Georgian securities market. Three out of nine brokerages were not members of the stock exchange.

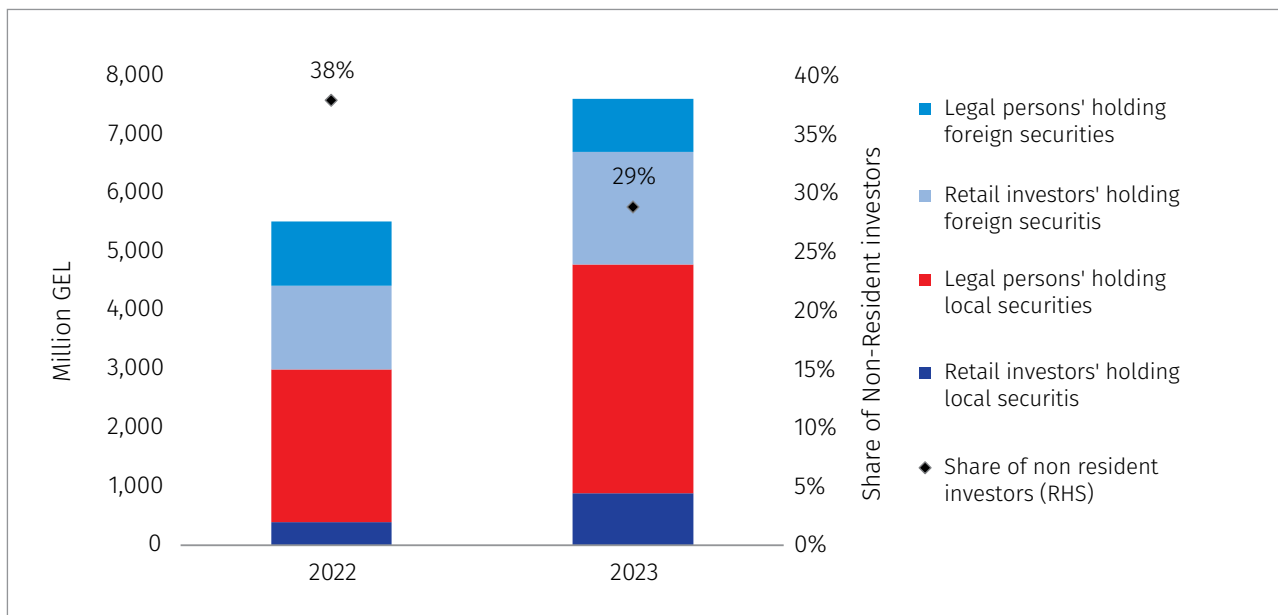
#### Brokerages

As of December 31, 2023, total volume of assets of brokerage companies (excluding the money and securities of clients in nominal ownership) amounted to 35 million GEL.

At the end of 2023, the total value of securities listed in the securities accounts of clients of brokerage companies amounted to 7.6 billion GEL, an increase of 38% compared to 2022 (without accounting for the effect of the exchange rate). This increase is mostly related to local securities accounts. Notably, accounts of non-resident investors represent 29% of the clients' securities balance.

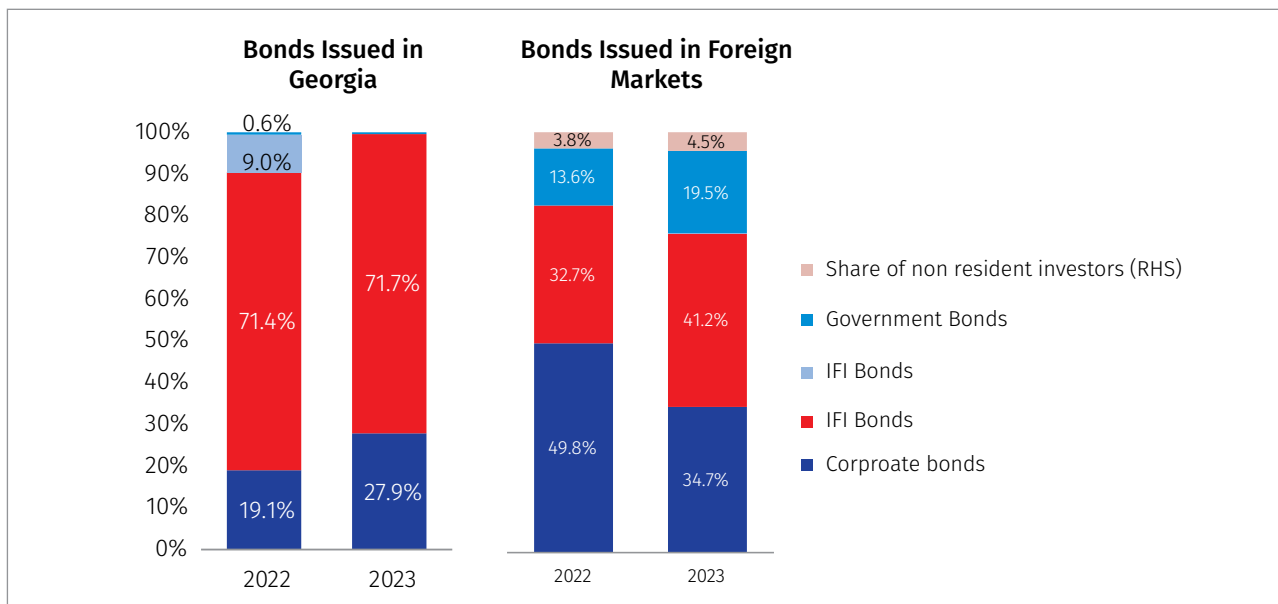
As of December 2023, the total number of clients receiving brokerage services from brokerage companies and banks was 67,844, with the majority (96%) being resident individuals. Compared to the end of 2022, the number of clients of brokerage companies increased by 160%. Additionally, 93% of the client securities balance and 98% of the number of clients are concentrated in the two largest brokerage companies.

Diagram N 8.7 Total value of securities in brokerage companies' client accounts (GEL)



Source: NBG, monthly reports of brokerages

Diagram N 8.8 Distribution of securities in brokerage companies' client accounts (securities issued in foreign countries and Georgia)



Source: monthly reports of brokerages and commercial banks

### Stock Exchange

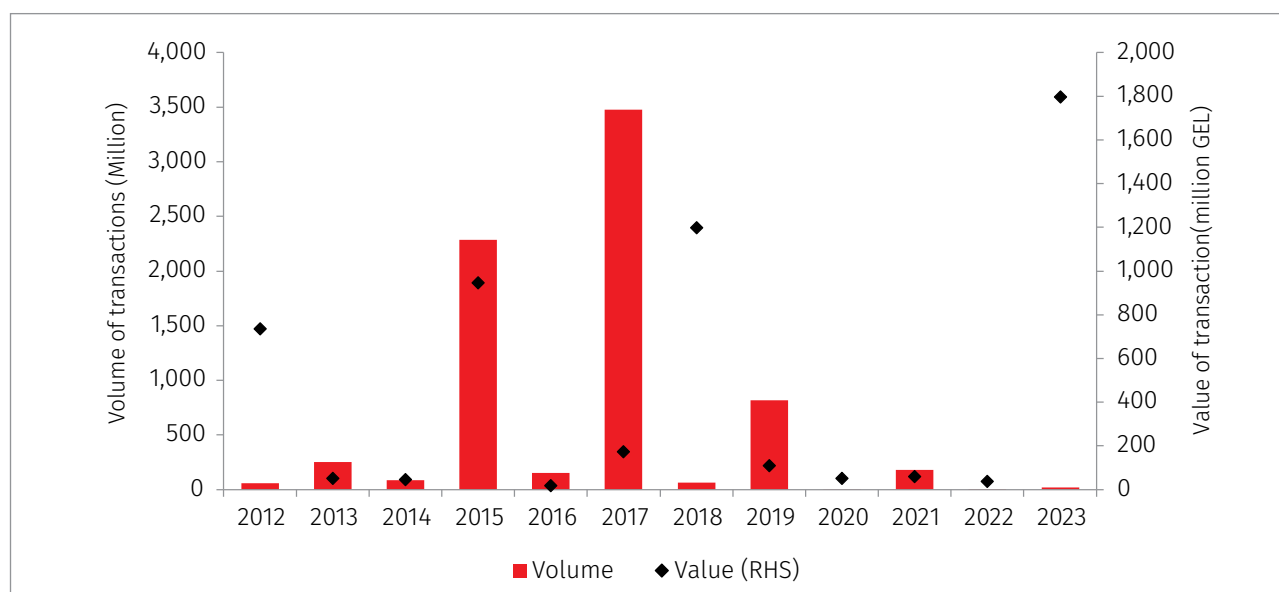
As of December 31, 2023, securities of 28 issuers were admitted to the trading system of the Georgian Stock Exchange. The total value of transactions recorded in trading sessions and the stock exchange during the reporting period amounted to GEL 1.8 billion (19.3 million

units of securities). Of this, a total of GEL 0.2 million thousand was traded at the stock exchange trading session, while the value of the stock traded was GEL 1.8 billion. The increased transaction value in 2023 is largely due to the non-exchange transaction concluded with shares of Bank of Georgia, which amounted to 1.7 billion GEL.

Table N 8.1 Aggregate information based on the rates recorded in the trading sessions and on the exchange (2022-2023)

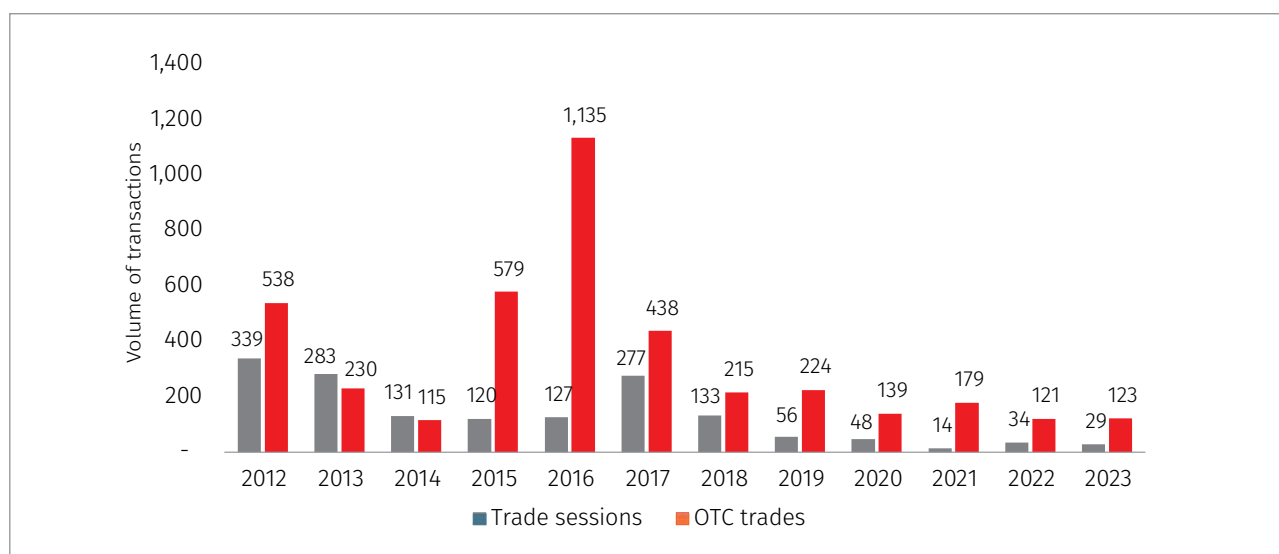
year	Number of deals		Number of securities		Value of securities (GEL)	
	2023	2022	2023	2022	2023	2022
Stock exchange	29	34	3,804,161	1,256,350	162,430	7,395,948
recorded	123	121	15,525,632	700,824	1,795,211,906	30,366,907
<b>Total</b>	<b>152</b>	<b>155</b>	<b>19,329,793</b>	<b>1,957,174</b>	<b>1,795,374,336</b>	<b>59,049,951</b>

Diagram N 8.9 Key Trade Indicators (transactions offered at trading session and recorded in stock exchange) 2012-2023.



Source: Annual Report of the Georgian Stock Exchange

Diagram N 8.10 Number of transactions recorded on trading session and OTC by years (2012–2023)



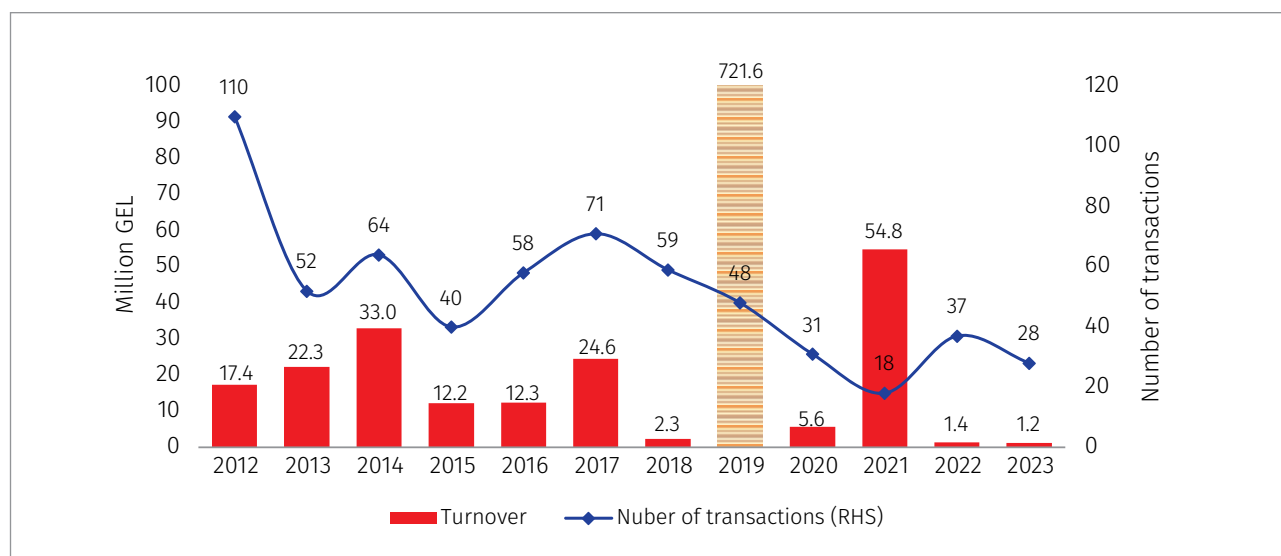
Source: Annual Report of the Georgian Stock Exchange

### Central Depository

In 2023, the Central Depository had 1.2 million securities and GEL 4.7 million deposited in it. Of this, 60 percent of cash deposit transactions and 80 percent of the total amount were made with the participation of Bank of Georgia JSC. The number of transactions on securities

deposited with the Central Depository decreased by 24 percent compared to the same period last year, while the number went down by 250 thousand units of securities. A total of 33 new accounts were opened with the Central Depository throughout 2023.

Diagram N 8.11 Securities deposited with the Central Depository by years (2012-2023)

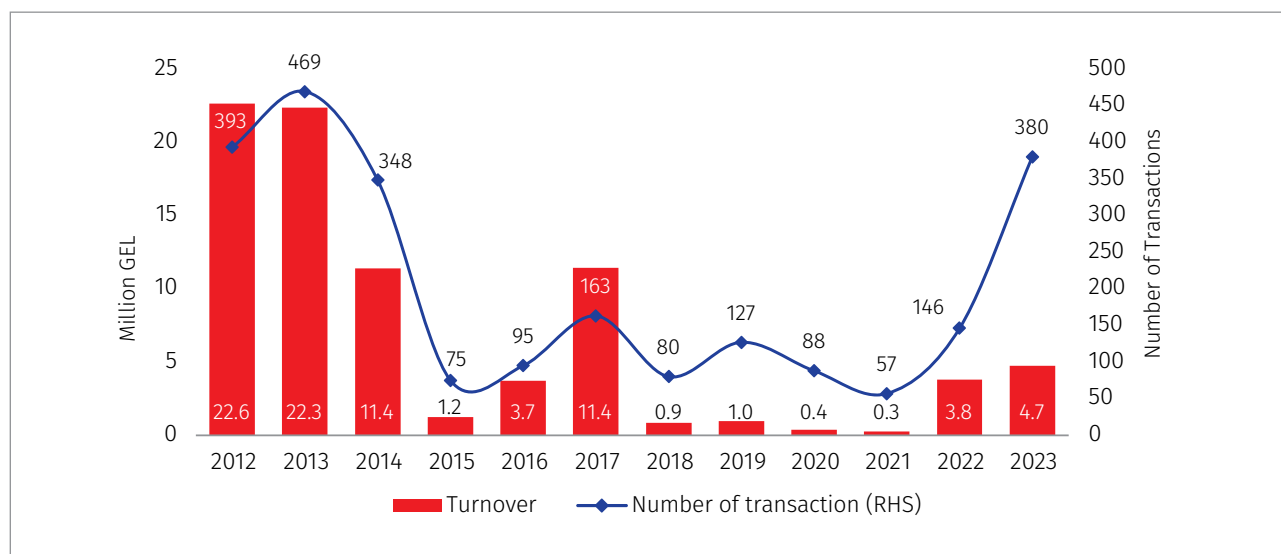


Source: Annual Report of the Georgian Securities Central Depository

In the reporting year, the cash turnover in the central depository increased by 935 thousand GEL. As for the

number of cash transactions, this indicator is 160% higher than the previous year's indicator.

Diagram N 8.12 Funds deposited at the Central Depository by years (2012-2023)



Source: Annual Report of the Georgian Securities Central Depository

## 8.4. INVESTMENT ACTIVITIES OF THE PENSION AGENCY



### Reallocation of Investment Portfolios

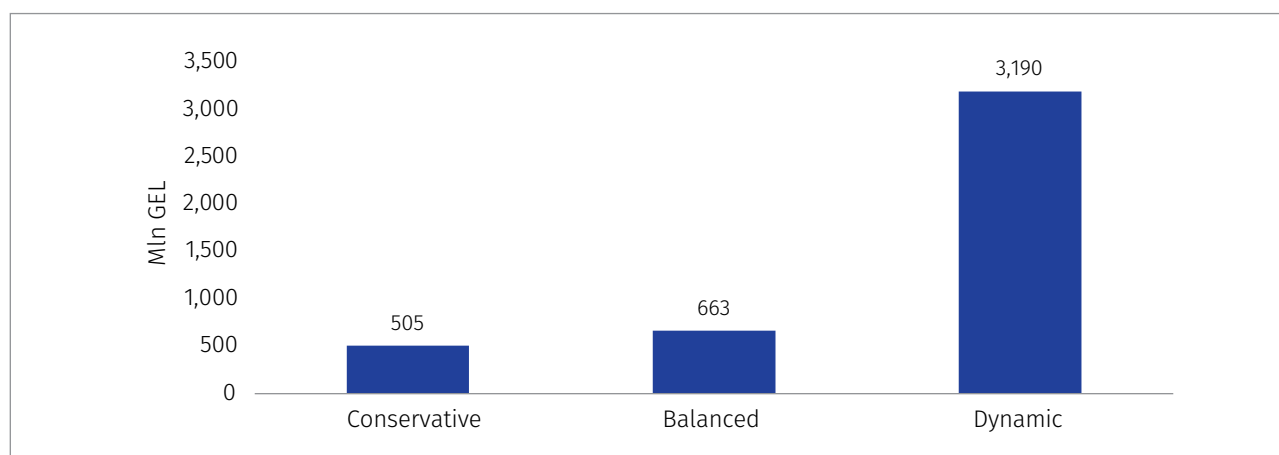
According to the Law of Georgia on Cumulative Pension, only the less risky portfolio was active during the first five years. On August 7, 2023, in accordance with the Law of Georgia on Cumulative Pension, the reallocation of accumulated pension assets was carried out into three investment portfolios with different risk levels and expected returns: low risk (conservative), medium risk (balanced), and high risk (dynamic). According to the law, existing participants were allocated to the respective portfolios based on their age. Participants who wished to change their portfolio were given one month to do so. Those who did not select a preferred portfolio during this month (until September 7)

automatically remained in the portfolios distributed according to age:

- Pension assets of participants under 40 were allocated to a dynamic (high-risk) investment portfolio.
- Pension assets of participants aged 40 to 50 were allocated to a balanced (medium-risk) investment portfolio.
- Pension assets of participants aged 50 or older were allocated to a conservative (low-risk) investment portfolio.

Since most of the participants in the pension scheme are under 40 years old, data at the end of the year shows that approximately 71% of the participants were in the dynamic portfolio, 16% were in the balanced portfolio, and 13% were in the conservative portfolio. As for the distribution of total pension assets, as of December 31, 2023, 3,190 million GEL was in the dynamic portfolio, 663 million GEL was in the balanced portfolio, and 505 million GEL was in the conservative portfolio.

Diagram N 8.13 Distribution of Pension Assets by Portfolios, December 31, 2023



Source: Pension Agency

### Investment Activities

In 2023, the Pension Agency developed a benchmark portfolio<sup>78</sup> for all three investment portfolios in terms of strategic asset allocation and began to converge the investment portfolios to the benchmark.

In accordance with the investment policy document, the investment board also decided that the foreign shares included in the benchmark portfolio will be purchased in the following indices weighted with equal weights:

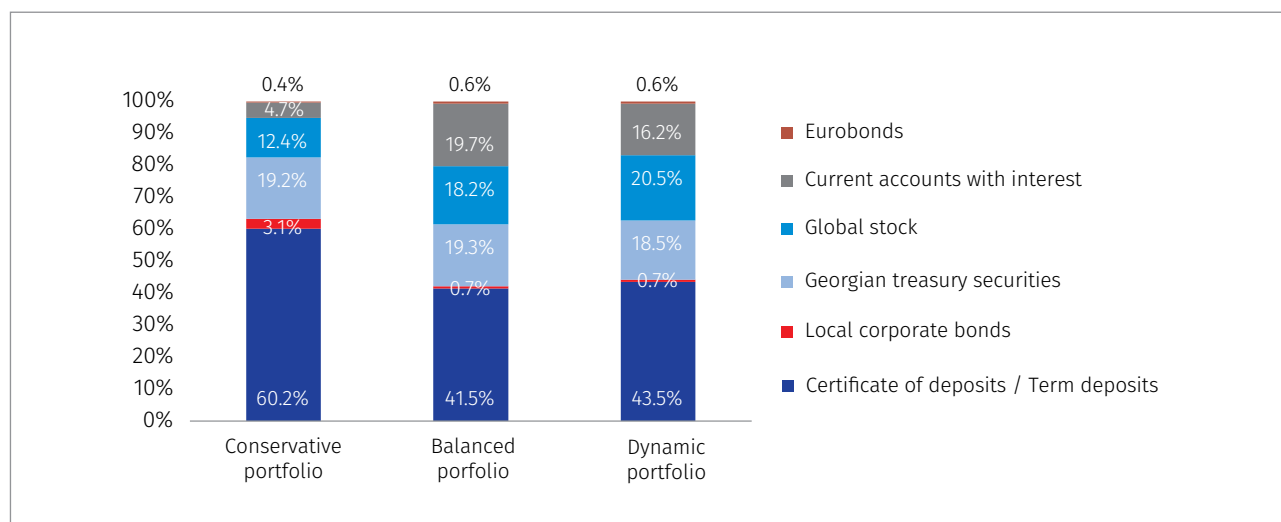
78. The conservative portfolio benchmark consists of three classes of assets: Georgian treasury bonds (20 percent), deposits/certificates of deposit in GEL (60 percent) and foreign stocks (20 percent). The benchmark weights of the balanced portfolio are distributed as follows: Georgian treasury bonds (20 percent), deposits/certificates of deposit in GEL (45 percent) and foreign shares (35 percent). and dynamic as follows: Georgian treasury bonds (20 percent), deposits/certificates of deposit in GEL (25 percent) and foreign shares (55 percent).

- Vanguard FTSE Pacific ETF (code VPL)
- Vanguard FTSE Europe ETF (code VGK)
- SPDR S&P500 ETF (code SPY)
- iShares MSCI Emerging Markets ETF (code EEM)

As of December 31, 2023, the share of global shares in total pension assets was 19.2%. 43.4% of the Pension Agency's stock portfolio was invested in North America,

18.5% in the developed Asia region, and 17.6% in Europe. Regarding asset allocation directly in the portfolios, as of December 31, 2023, 4.7% of the conservative portfolio was placed in current yield? interest? accounts, 19.2% in local treasury bonds, 12.4% in global stocks, 0.4% in Eurobonds, 3.1% in local corporate bonds, 60.2% was placed in local certificates of deposit and term deposits.

Diagram N 8.14 Distribution of Pension Asset Portfolios, 31 December, 2023



Source: Pension Agency

As for the balanced portfolio, the distribution was as follows: 19.7% of the portfolio was placed on current yield accounts, 19.3% in local Treasury bonds, 18.2% in global shares, 0.6% in Eurobonds, 0.7% in local corporate bonds, and 41.5% local certificates of deposit and term deposits.

The dynamic investment portfolio had the following distribution: 16.2% of the portfolio was placed in interest-bearing accounts, 18.5% in local Treasury bonds, 20.5% in global shares, 0.6% in Eurobonds, 0.7% in local corporate bonds, and 43.5% in local certificates of deposit and term deposits.

As of December 31, 2023, the volume of the Pension Fund amounted to 4.4 billion GEL, of which the net total assets were 856.7 million GEL. Net return on the Pension Fund since the launch (January 1, 2019) through December 2023 amounted to 58.2%, and real return (inflation adjusted) for the same period amounted

to 14.8%. As for individual portfolios, the structures looked like this:

- Conservative portfolio: the annualized real returns of the said portfolio since inception (January 1, 2019) to the end of 2023 were 2.74%.
- Balanced portfolio: the actual returns of the said portfolio since inception (August 7, 2023) to the end of 2023 were 3.26%.
- Dynamic portfolio: the real return on the portfolio since inception (August 7, 2023) until the end of 2023 was 3.40%.

### Updates in Legislative Framework

In 2023, significant changes were made to the Law of Georgia On Accumulated Pension. These changes mainly affected investment limits/restrictions, regulatory norms for private asset management companies, the role of the chief investment risk officer, the terms and mechanisms for allocating participants

to investment portfolios based on age, and other related issues. Specifically:

- The pension fund now has the opportunity to invest in alternative investment instruments like real estate investment funds and private equity funds in the balanced and dynamic portfolio. Additionally, the pension fund can participate in a loan co-financed by international financial institutions.
- The law now distinguishes between investment and non-investment risk management, with their respective rights and duties. Investment risk, which includes any risk related to investment activity, is now under the full supervision of the Investment Council. Non-investment risk management, however, remains the responsibility of the Supervisory Board.
- From January 1, 2025, all participants will have the option to choose a private asset manager to manage their savings. The supervisory approaches and principles for these private asset managers will be similar to those of the Pensions Agency.
- Participants who have not chosen their preferred investment portfolio will be automatically moved to the conservative portfolio from January 2024, regardless of their age group. New contributions from January 1, 2028, will be allocated to age-appropriate portfolios unless the participant decides to change the portfolio. The savings will remain in the existing portfolios until January 1, 2028.
- The Investment Council is now authorized to select and sign an agreement with only one specialized depository. The NBG may also provide specialized depository services if obtaining them otherwise is impossible or would require unreasonable effort or expense.

## 8.5. OVERVIEW OF ACTIVITIES OF INVESTMENT FUNDS



In 2020, the investment funds' regulatory framework was entirely revised and aligned with EU directives, contributing to the increasing interest in this sector. Both the NBG and the private sector have been actively promoting awareness in recent years.

In 2023, seven private investment funds were registered, including Globally Diversified Bond Fund JSC, Cash Plus Capital JSC, the joint investment fund Euro Secured Loan Portfolio, Baobab Capital JSC, the joint investment fund Forsyth Development Fund, the Joint Investment Fund Alpha Plus US Dollar Treasury Bond Fund, and Starbridge LLC.

As for asset management companies, three were registered in 2023: Alpha Plus Asset Management LLC, Stargate LLC, and Capital Craft JSC. Additionally, one asset management company, BOG Asset Management LLC, was licensed. In total, there are now 13 investment funds and eight asset management companies operating in Georgia.

As of December 31, 2023, the total volume of investment funds is 128 million GEL.

An amendment was made in 2023 to the Regulation on activity of a specialized depository approved by the Decree No. 168/04 of the Governor of the National Bank of Georgia, September 22, 2020. This amendment grants those entities (Bank of Georgia JSC, TBC Bank JSC) that had obtained specialized depository authorization based on the Regulation on Specialized Depository for Accumulative Pension Scheme, approved under the Decree of the Governor of the National Bank of Georgia November 30, 2018 №259/04 had the right to provide specialized depository services for investment funds as well.

Furthermore, in 2023, Khalik Bank of Georgia JSC received approval to conduct activities as a specialized depository of the authorized investment fund. At present, there are three participants in the market offering specialized depository services.



# MONEY LAUNDERING INSPECTION AND SUPERVISION

09

In line with the “Supervisory Framework for Combating Money Laundering and Terrorism Financing” of the National Bank of Georgia, the Bank planned and executed measures within the 2023 risk-based supervisory strategy. These measures were primarily based on the off-site identification and assessment of risks, both - for the sectoral and for each individual financial institution.

To identify and assess risks remotely, the NBG received and processed money laundering and terrorism financing risk supervision reports from entities subject to AML/CFT (Anti-Money Laundering/Combating the Financing of Terrorism) supervision, listed in the diagram (Table N9.1) twice, during 2023.

Table N 9.1 Off-site supervision 2023

Financial sector	number
Commercial bank	13
Microfinance organization	34
Payment service provider	31
Brokerage company	8
Currency exchange bureau	510
Securities registrar	3
Credit union	1
Lending entity	171

It is noteworthy that in 2023, in order to conduct off-site evaluation of the commercial banks' internal control systems compliance with the legislation on the prevention of money laundering and terrorism financing, as well as the requirements of the NBG and international best practices, compliance control system supervision questionnaires of commercial banks were requested, and a corresponding analysis was conducted.

The supervisory measures implemented during 2023 encompassed complex and thematic, special and follow up on-site inspections. In line with the identified sectoral threats and risks, the on-site inspections were focused on the following topics:

For commercial banks:

- Adequacy of the process of classifying clients (including those identified/verified through remote channels) according to risk, reassessing the risk, and implementing preventive measures corresponding to the risk;
- Process of identification and verification of beneficial owners of clients with complex ownership structures; The bank's knowledge of clients related to offshore and high-risk jurisdictions by

governance and ownership structure, as well as transactions and parties involved in such areas;

- Compliance with international sanctions regimes (related to the Russian Federation, Belarus, Iran);
- Effectiveness of the process of detecting the origin of cash;
- Process of detecting suspicious/unusual transactions, including the effectiveness of the process for detecting the use of shell companies/transit companies, measures taken in terms of the implementation of UN resolutions (TF/Proliferation), the adequacy of software, the bank's knowledge of transactions carried out by charitable and non-commercial (non-commercial) legal entities;
- Effectiveness of the risk management process related to virtual assets.

For payment service providers:

- Compliance with international sanctions regimes (related to the Russian Federation, Belarus);
- Adequacy of the process of classifying clients according to their risk, reassessing the risk, and implementing preventive measures corresponding to the risk;
- The process of identifying suspicious/unusual

transactions (including measures taken in terms of the implementation of UN resolutions (TF/Pro-liferation), software adequacy);

- Effectiveness of the risk management process related to virtual assets;

For brokerage companies:

- Compliance with international sanctions regimes (related to the Russian Federation, Belarus);
- Adequacy of the process of classification of clients according to risk, risk reassessment, and preventive measures corresponding to risk;
- Process of identification and verification of beneficial owners of clients with complex ownership structures;
- Brokerage company's knowledge of intermediaries and the adequacy of the process of monitoring transactions carried out through them;
- The process of identifying suspicious/unusual transactions (including measures taken in terms of the implementation of UN resolutions (TF/Pro-liferation), software adequacy);
- Effectiveness of the process of determining the origin of cash;
- Checking the accuracy of reporting.

For microfinance organizations:

- Compliance with international sanctions regimes (related to the Russian Federation, Belarus);
- Adequacy of customer risk classification, risk reassessment, and risk-based due diligence measures;
- Organization's knowledge of international transactions (including those related to offshore and

high-risk jurisdictions);

- Assessment of the process of compliance with US, EU, UK sanctions; for this purpose, the study of transactions performed by fast money transfer systems and the assessment of the adequacy of the organization's knowledge and measures taken;
- The process of identifying suspicious/unusual transactions (including measures taken in terms of the implementation of UN resolutions (TF/Pro-liferation), software adequacy);
- Effectiveness of the process of detecting the origin of cash;

During 2023, 54 representatives of the financial sector were inspected to determine their compliance with the Georgian legislation on the prevention of money laundering and financing of terrorism. In order to ensure the elimination of the deficiencies identified during inspections, the Money Laundering Inspection and Supervision Department of the National Bank of Georgia carried out distance type – follow up inspections. It is important to note that in 2023, special attention was paid to compliance with international sanctions and the study of transactions made through the remittance system. For this purpose, the effectiveness of the process of compliance with international sanctions regimes (related to the Russian Federation, Belarus, and the Islamic Republic of Iran) was studied in commercial banks and payment service providers.

The total amount of fines imposed for violations of the Georgian legislation on the prevention of money laundering and financing of terrorism was 1,195,800 GEL.

Table N 9.2 Fines in 2023

Financial Sector	Amount of Fine in GEL
Commercial bank	257 800
Microfinance organization	129 600
Payment service provider	100 000
Lending entity	55 000
Brokerage company	58 000
Currency exchange bureau	595 400

Source: NBG

In addition to monetary fines imposed based on the on-site inspections, corrective measures were actively applied to representatives of the financial sector through 2023. A number of recommendations

were issued in 2023 based on the results of on-site inspections to immediately eliminate identified weaknesses and increase the level of compliance of financial sector representatives.

Table N 9.3 Number of recommendations, 2023

<b>Financial Sector</b>	<b>Number of recommendations</b>
Commercial bank	39
Microfinance organization	73
Payment service provider	15
Lending entity	18
Brokerage company	117
Currency exchange bureau	167

Source: NBG

In 2023, significant steps were taken towards implementing the supervisory framework for virtual asset service providers. These actions included the development of legal acts and the AML/CFT assessment of registration applications submitted by interested parties. Considering international practices, including studies and recommendations published by influential international agencies, the experience shared by various regulators and experts, as well as feedback received from the private sector, the following legal acts were developed and approved:

- The rule for the Virtual Asset Service Provider's (VASP's) registration at the National Bank of Georgia, registration cancellation, and regulation Regulation on the information accompanying the transfer of a virtual asset (the so-called Travel Rule).

The actions taken by the National Bank of Georgia in 2023 in terms of compliance with the international sanctions regimes are particularly noteworthy. In order to share experience, the Money Laundering Inspection and Supervision Department has been closely cooperating with various international organizations and agencies.

During 2023, the following documents were developed:

- *Screening rule of the Society for World Interbank Financial Telecommunications (SWIFT) message*, to ensure compliance with sanctions regimes and establish a unified approach to the screening of SWIFT messages;
- *Regulation for execution of sanctions regimes by obliged entities subject to supervision of the National Bank of Georgia*, laying down responsibilities of obliged entities to comply with sanctions regimes and, in this context, to develop and implement effective internal control mechanisms;
- *Guideline on the execution of payment operations consequent to trade restrictions provided by sanctions regimes*. The document specifies the requirements for the examination of operations related to import, export and re-export of goods, submission of additional documentation, as well as other measures to be taken in order to comply with trade restrictions.

In order to ensure compliance with the anti-money laundering and anti-terrorist financing legislation, the "Rule on Completing and Submitting Money Laundering and Terrorism Financing Risk Supervision Report of Commercial Banks" was updated in 2023. In addition, the "Rule on Completing and Submitting Money Laundering and Terrorism Financing Risk Supervision Reports of Microbanks" was developed.

“The Money Laundering and Terrorism Financing Risk Assessment Report of Georgia” was approved in 2023. The report not only assessed the money laundering and terrorism financing risks of the sector under the supervision of the National Bank of Georgia, but also covered the risk assessment of new services and delivery channels as well as the virtual asset services sector.

To improve the perception of risks by financial institutions within their organization and to plan measures to mitigate these risks, the Money Laundering Inspection and Supervision Department evaluated the organizational and group-wide risk assessment documents of commercial banks. It is noteworthy that commercial banks were instructed to update the organizational and group-wide risk assessment document in terms of compliance with international sanctions regimes.

During 2023, as in previous years, the Money Laundering Inspection and Supervision Department was involved in reviewing products developed and presented by financial institutions individually.

The National Bank of Georgia makes special emphasis on the implementation of preventive supervisory measures, which ensures consistent informing of representatives of the financial sector about supervisory expectations and raising their level of compliance. For this purpose, the representatives of the financial sector were actively trained, during the year, to familiarize them with methodical guidelines and supervisory documents and to effectively implement them in practice, as well as to successfully manage current challenges. The training modules and the number attendees according to the sectors are presented in the Table:

Table N 9.4 Training Modules, 2023

Training Modules	Microfinance organization	Payment service provider	Currency exchange bureau	Lending entity	Brokerage company	Registrar	Investment fund/Asset management company
Compliance control system	41	28	56	29	8	5	4
Risk assessment and preventive measures	41	28	56	29	8	5	4
Compliance with international sanctions	41	28	56	29	8	5	4
Review of the Money Laundering and Terrorism Financing Risk Assessment Document	41	28	56	29	8	5	4

Communication with representatives of the financial sector was intensive in 2023, in addition to thematic training. Meetings were actively held to share information and familiarize them with supervisory expectations. Notably, active communication was carried out to ensure compliance with international sanctions. In this regard, trainings, as well as group and individual work meetings, were held with sector

representatives in different formats. Furthermore, it is important to mention that representatives of the financial sector received feedback on a daily basis, during the year, regarding the issues relevant to them and the effective implementation of legislative requirements and methodological guidelines in practice.



# PAYMENT SYSTEMS OVERSIGHT

10

Safeguarding the efficient and reliable operation of payment systems is crucial in the face of financial innovation and the rapid development of digital technologies. To achieve this, central banks must strengthen their oversight of payment systems, refine the legal framework, and implement standards that improve risk management, particularly systemic risks, within financial market infrastructures, including payment systems. In 2023, the National Bank of Georgia took several measures to achieve this goal. One significant step was the adoption of the Regulation on Oversight of the Payment System and Payment System Operators, which introduced the Principles of the Financial Market Infrastructure (PFMI) of the Committee on Payment and Settlement Systems and the International Organization of Securities Commissions (CPSS-IOSCO). The regulation was developed based on the recommendations of the Financial Sector Assessment Program (FSAP) of Georgia, implemented by the International Monetary Fund (IMF) and the World Bank, and is in line with the principles of financial market infrastructures of CPSS-IOSCO and the European Central Bank's payment systems oversight requirements (Regulation (EU) No 795/2014 for systemically important payment systems ECB/2014/28).

Another important aspect of strengthening oversight is improving the monitoring of the payment market, specifically the collection and analysis of information. In 2023, the National Bank of Georgia continued to work on improving data quality. Additional work was carried out in the unified information system of the National Bank of Georgia - NBGStat, to detail and improve the quality of data, including the market data of card instruments according to the types of trade/service facilities, which allows for the improvement of the analysis of the retail payments market.

The promotion of cashless payments is closely linked to users' trust in payment and settlement systems, an important component of which is the protection

of the rights of payment service users. In accordance with the requirements of the Directive (EU) 2015/2366 on payment services of the European Parliament and the Council (PSD2), an independent dispute resolution commission started its activities in Georgia from December 1, 2023. This allows users to apply directly to a specialized commission focused on the field of payment services, which will consider the user's complaint free of charge within a much shorter time frame, instead of going to court. The National Bank of Georgia ensured that all legal, organizational, and technical issues were settled in order to start the activity of the commission within the time limits defined by the legislation. Additionally, a specialized unit was created within the Payment Systems Department - the support division for the dispute review commission - to provide support to the commission in the review of disputes and other multifaceted issues related to its proper functioning.

In 2023, work also began on a project to create a unified portal for payment service providers' fees, which would increase the transparency of the payment market and enable consumers to make more informed decisions. Research and fintech companies will also have the opportunity to access the information in an automated way, allowing them to provide analytical and other information to users in a variety of ways.

## 10.1. LEGISLATIVE FRAMEWORK



The National Bank of Georgia continued its efforts to align the legal framework on payment systems and services with international standards in 2023 and to modify and improve it based on the needs identified in practice.

To ensure the reliable, efficient, and effective functioning of payment systems as a financial market infrastructure, and to improve risk management in payment systems, the NBG adopted two regulations in

2023: *the Regulation on determining the subcategories of an important system and assigning the status of an important system to the payment system* (referred to as the regulation on assigning the status of an important system) and the *Regulation on supervision (oversight) of the payment system and payment system operators* (referred to as the Oversight regulation). These regulations are based on the principles of financial market infrastructures of CPSS-IOSCO, as well as the requirements of the European Central Bank's oversight of payment systems.

Payment systems, under the regulation, were divided into three categories based on the status of important systems: a) systemically important; b) exceptionally important; and c) other payment systems. The defining criteria for each category of important systems were established, along with the process of granting and canceling status for them, and issues of production of the registry of systemically important and exceptionally important payment systems and their operators. The guidelines for requirements that are systemically important, exceptionally important, and relevant for other payment systems have been specified by the Oversight Regulation. A part of the regulations established by the said regulatory document came into effect from January 1, 2024, a part will enter into force from June 1, 2024, and the remaining part from January 1, 2026. The self-assessment of compliance with the requirements of the Oversight Regulation by the representatives of the sector is carried out using the assessment methodology based on the principles of financial market infrastructure developed by CPSS-IOSCO.

The Oversight Regulation, among other things, defined minimum standards for the management of legal, credit, liquidity, operational, investment, and general business risks. The requirements for the governance structure of the payment system and the settlement of the payment system, as well as the rules and procedures for the default of the participant of the payment system,

have been established. Certain requirements were set for system operators to determine the conditions of access and participation in the system. In addition to the above, the obligation of the system operator to have processes in place, according to which it will be able to identify and incorporate market requirements to ensure the efficient and effective functioning of the payment system, has emerged.

The effect of the *regulation on granting the status of a significant system* and the Oversight Regulation applies to cash payment systems in Georgia and their operators, including payment systems operated by the National Bank of Georgia.

Public discussions with the representatives of the sector were actively being held in the process of working on the said regulation.

### **Amendments to the Regulation on Information Accompanying Transfers**

In accordance with the duties defined by the organic law on the National Bank of Georgia and the requirements for dynamic alignment with EU regulations as per the Association Agreement with the European Union, significant changes were made to the regulations. These changes aligned the regulations with the updated European Regulation (Regulation (EU) 2023/1113 of the European Parliament and of the Council of 31 May 2023 on information accompanying transfers of funds and certain crypto-assets and amending Directive (EU) 2015/849). The amendments addressed issues related to the transfer of virtual assets and specified additional information that must accompany the transfer of funds. Notably, the Legal Entity Identifier (LEI) was defined as a required piece of accompanying information. Terminological changes were made accordingly. Furthermore, the amendments established obligations for payment service providers and virtual asset service providers to store consent information and maintain internal policies, procedures, and appropriate control mechanisms.

## Transparency of Fees Related to Payment Services

In 2023, efforts continued to introduce transparency principles for the effective functioning of the payment market, particularly through the development of a unified portal for payment service providers' fees. Minor adjustments were made to the draft regarding the information to be published on the NBG's website. The Terms of Reference for the project implementation was developed, and a company was selected to execute the task. This initiative aims to allow users to easily compare product/service rates, calculate costs using online calculators, and promptly receive information from commercial banks about current and historical currency exchange rates. This will facilitate user access to banking services, enhance decision-making, and promote competition. Work also progressed on the draft *Regulation on the Availability of Service Fees Related to Payment Accounts*, based on the Payment Account Directive (Directive 2014/92/EU). This regulation is expected to be adopted in 2024, following the creation of the unified portal for payment service providers' fees.

## Dispute Resolution Commission

In September 2022, the Parliament of Georgia adopted a package of draft laws developed by the National Bank of Georgia, which included extensive changes to the Organic Law On the National Bank of Georgia and the Law of Georgia On the Payment System and Payment Services. This legislation fulfilled Georgia's obligation under the Association Agreement with the European Union to align with PSD2.

In accordance with the timelines set by these legislative amendments, a Commission for reviewing disputes with the National Bank of Georgia was established in August 2023. The Commission consists of five members, with no more than two members being employees of the National Bank of Georgia and at least three members being independent individuals. The commission members, including the chairman, are appointed by the Board of the National Bank of Georgia for a term of five years.

The Dispute Review Commission considers disputes between payment service users and payment service providers related to rights and obligations arising from the Organic Law On the National Bank of Georgia, the Law of Georgia On the Payment System and Payment Services, and the subordinate normative acts adopted under these laws. The review of complaints is free of charge, and the Commission operates based on principles of competition, fairness, transparency, objectivity, impartiality, and equality of the parties. The legislation allows up to 90 calendar days for dispute consideration. Depending on the complexity and specifics of the complaint, as well as the course of the dispute and the issues to be investigated, this period can be extended by no more than 30 calendar days. The Commission's decisions are binding and can be appealed in court.

The independent Dispute resolution Commission is expected to enhance user trust in electronic payments, allowing payment service users to effectively protect their rights. Additionally, it ensures that the review process is conducted in a shorter time frame and without charge.

## 10.2. TRANSACTIONS IN THE RTGS SYSTEM

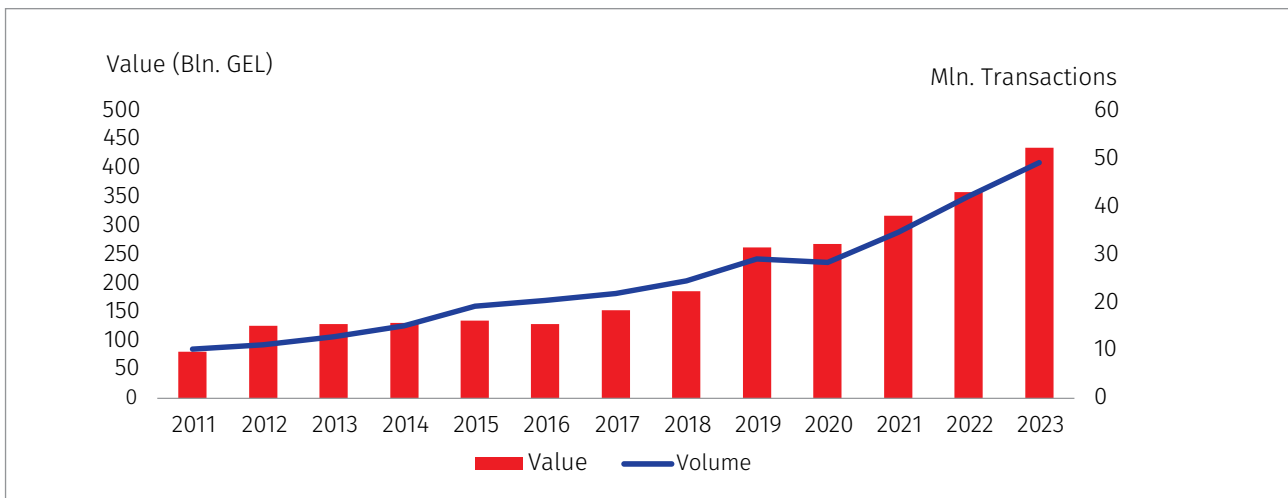


The NBG's Real-Time Gross Settlement System (RTGS) is the key mechanism for interbank payment in national currency. In 2023, similar to previous years, ensured high quality of uninterrupted services. System availability exceeded 99.8 percent for members, which is important considering the role of the RTGS system as a settlement agent for other systems (GSSS and card systems). As of December, 2023, its members were: 15 commercial banks licensed in Georgia, the National Bank of Georgia and the Treasury Service of the Ministry of Finance. Both large interbank payments and retail payments of members' customers are processed through the RTGS system. The RTGS system also ensures the settlement of transactions processed in the Georgian Securities Settlement Systems (GSSS) and

international card systems. Due to its importance, the RTGS system has a business continuity plan developed in accordance with the best international practices, and it is regularly tested using the pre-defined scenarios. At least once every three years, the National Bank of Georgia performs self-assessment of the RTGS system based on the principles of financial market infrastructures (the most recent self-assessment was done in 2021 within the scope of the Financial Sector Assessment Program (FSAP), the joint mission of the

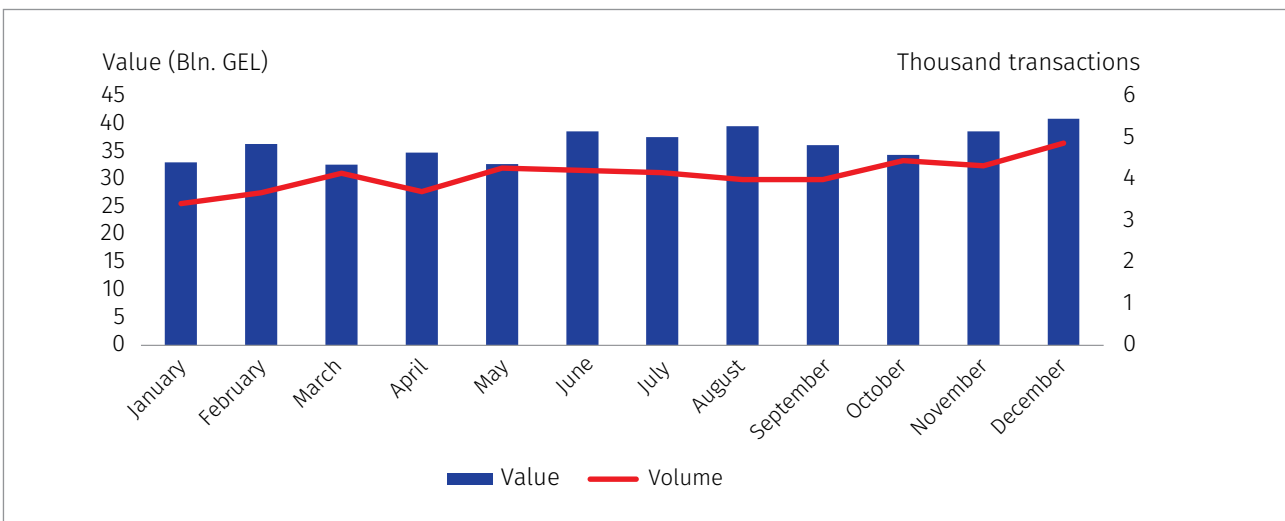
World Bank and the International Monetary Fund.<sup>79</sup>). In 2023, 49.2 million payment operations were carried out through the RTGS system, amounting to 435.7 billion GEL, which is 16.7 percent more quantitatively and 21.5 percent more than the figures of the previous year. It is noteworthy that the number of payments between commercial banks increased by 18.8 percent, and the amount by 12.6 percent. See the diagram No.10.1 below for the dynamics of monetary and quantitative indicators of payments made through the RTGS system.

Diagram N 10.1 Transfers through the RTGS (2011-2023)



Source: NBG

Diagram N 10.2 Transfers through the RTGS (2023)



Source: NBG

79. <https://www.imf.org/en/Publications/CR/Issues/2021/09/17/Georgia-Financial-System-Stability-Assessment-465911>

Diagram N 10.3 Amount of RTGS Transactions by months and years (2018-2023)

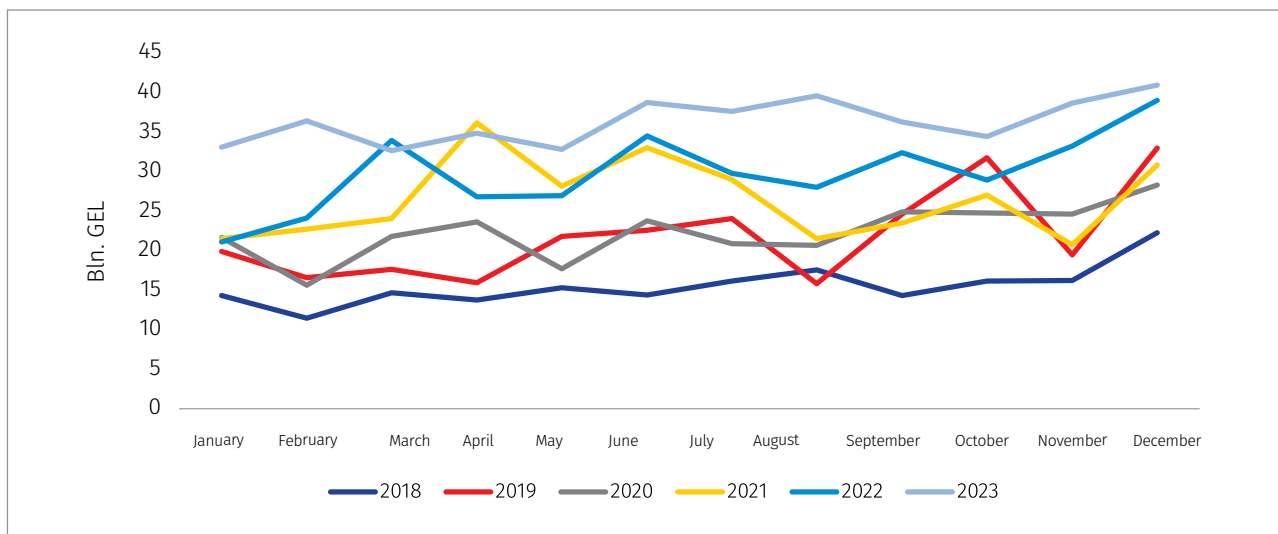


Diagram N 10.4 Number of RTGS Transactions by months and years (2018-2023)

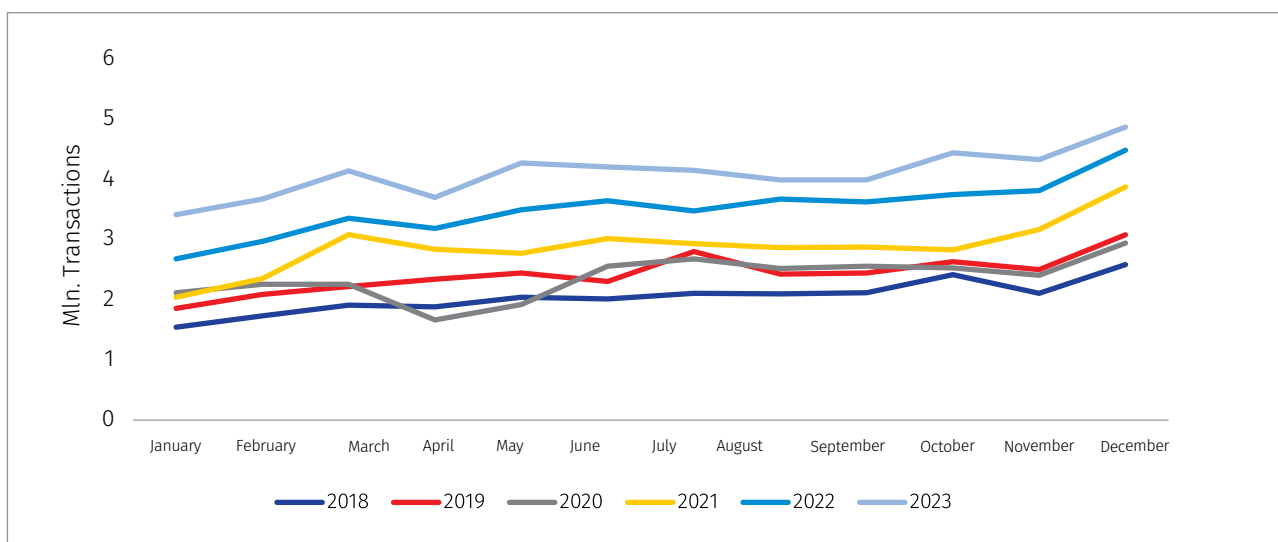


Diagram N 10.5 Amount of RTGS Transactions by members (2011-2023)

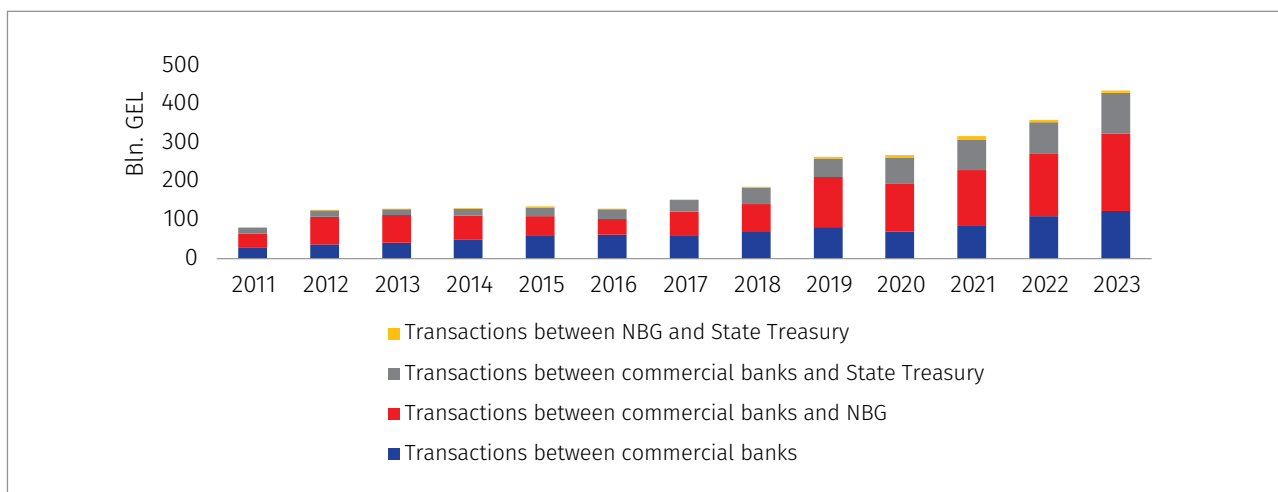
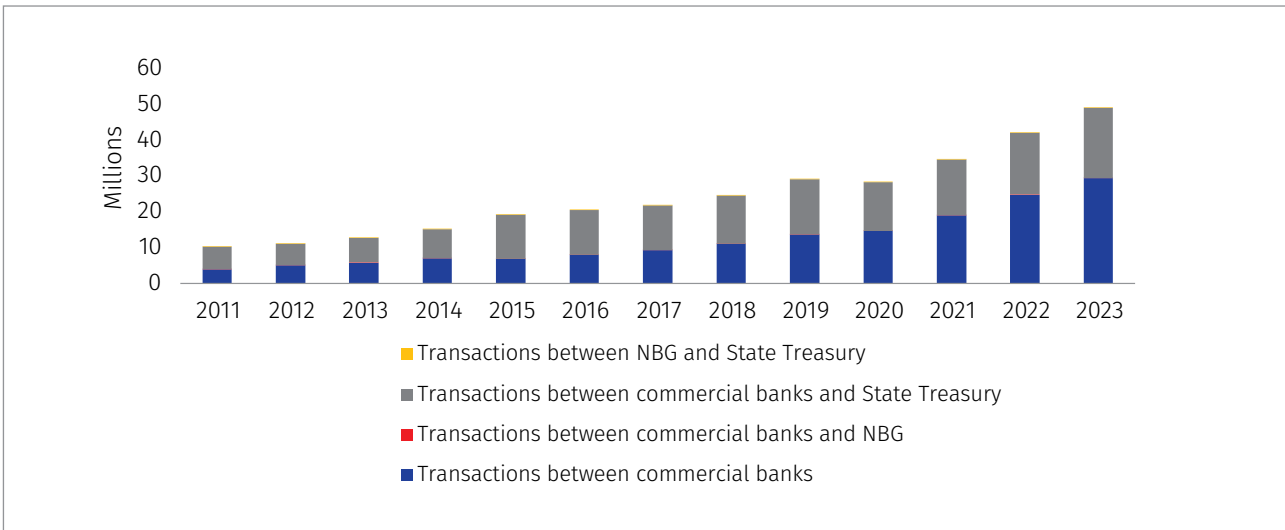


Diagram N 10.6 Number of RTGS Transactions by members (2011-2023)

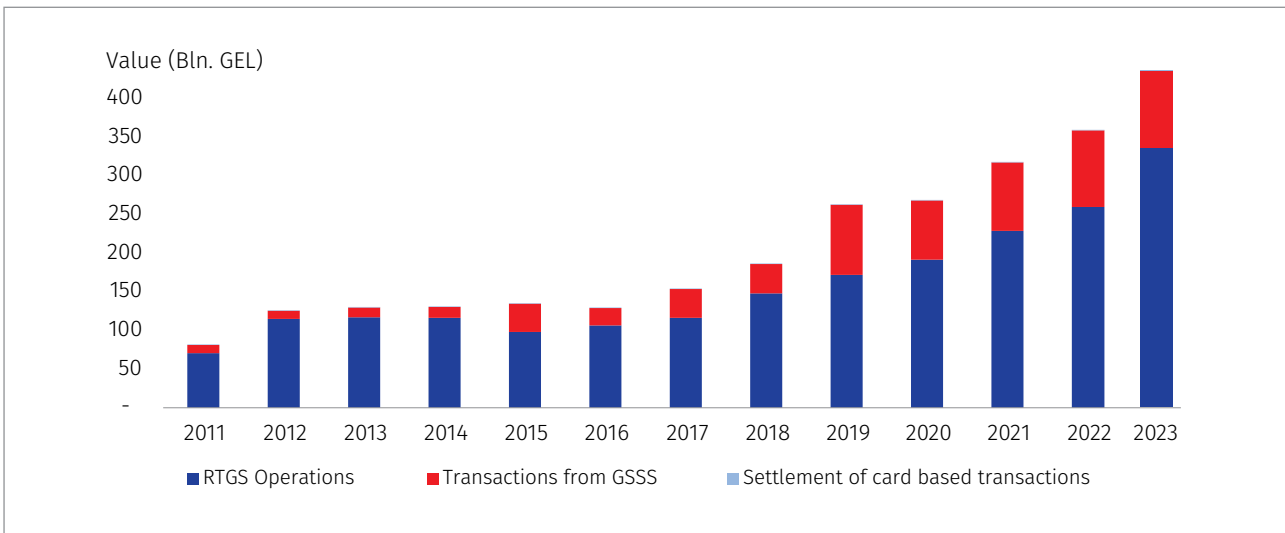


Source: NBG

As in previous years, the role of the RTGS system as a settlement mechanism for other systems is important. In 2023, the amount of final settlement operations of

other systems increased by 7.7 percent, and its share in total operations performed by the RTGS system amounted to 24.7 percent (see diagram N 10.7).

Diagram N 10.7 Amount of RTGS Transactions by settlement (2011-2023)

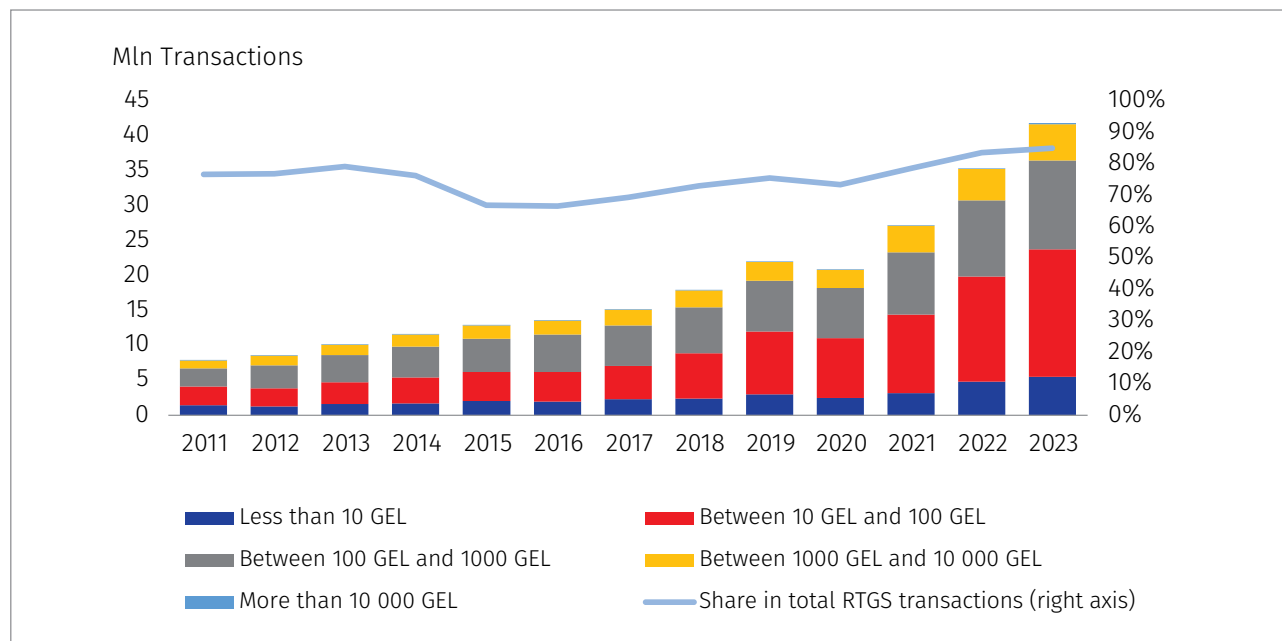


Source: NBG

RTGS system plays an important role not only in terms of large amount (wholesale) but also retail payments. In 2023, the share of commercial banks' customer payments in total RTGS payments was 29.1 percent in terms of money and 85 percent in terms of quantity. The

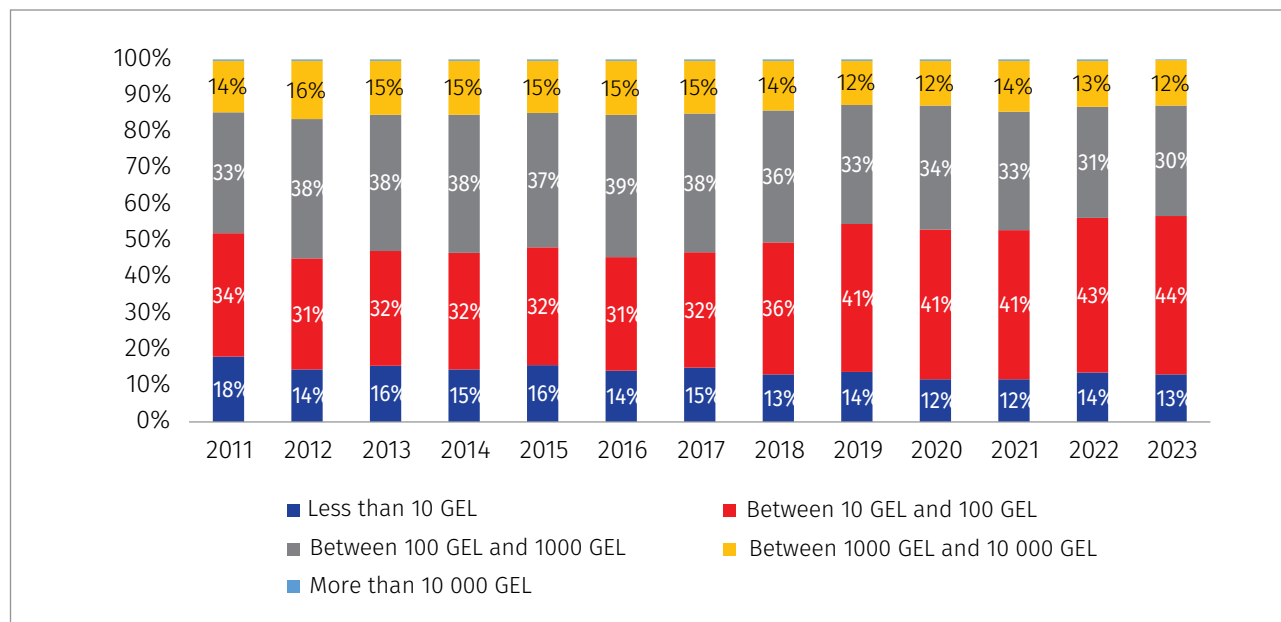
largest share (44 percent) of the number of retail payments comes from payments from 10 to 100 GEL, and then (30 percent) from payments from 100 to 1000 GEL (see diagram N 10.8 and diagram N 10.9).

Diagram N 10.8 Number of payments by bank clients by amount limits



Source: NBG

Diagram N 10.9 Distribution of payments by bank clients by amounts



Source: NBG

### 10.3. ELECTRONIC MEANS OF PAYMENT



The development of technologies in the modern world enables the introduction of innovations and the creation of new payment products that are better adapted to the needs of modern users, thereby contributing to the development of cashless electronic payments.

Over the past eight years, mobile banking has been the fastest-growing payment channel, with an average annual growth rate of approximately 128 percent in the number of payments. Not surprisingly, it quickly established itself as the most commonly used payment method in Georgia after card instruments. By 2020, the number of payments made using mobile banking surpassed those made through internet banking, which had previously been second only to card instruments in terms of the number of payments made. Additionally, the volume of payments made through mobile banking has shown rapid growth, with an average annual growth rate of about 102 percent over the last eight years. In 2022, for the first time, the volume of payments made through mobile banking exceeded those made via card instruments, although it was still below the volume of payments made through internet banking. It should be noted that in 2023, payments made through mobile banking surpassed those made through non-remote channels (branches and service centers) in terms of monetary value. Traditionally, the largest number of non-cash payments are made through internet banking, which significantly exceeds the volume of payments made by other means.

In 2023, compared to the previous year, the number of payments made using mobile banking increased by 120 percent, accounting for 27 percent of total non-cash payments, which is 9 percentage points higher

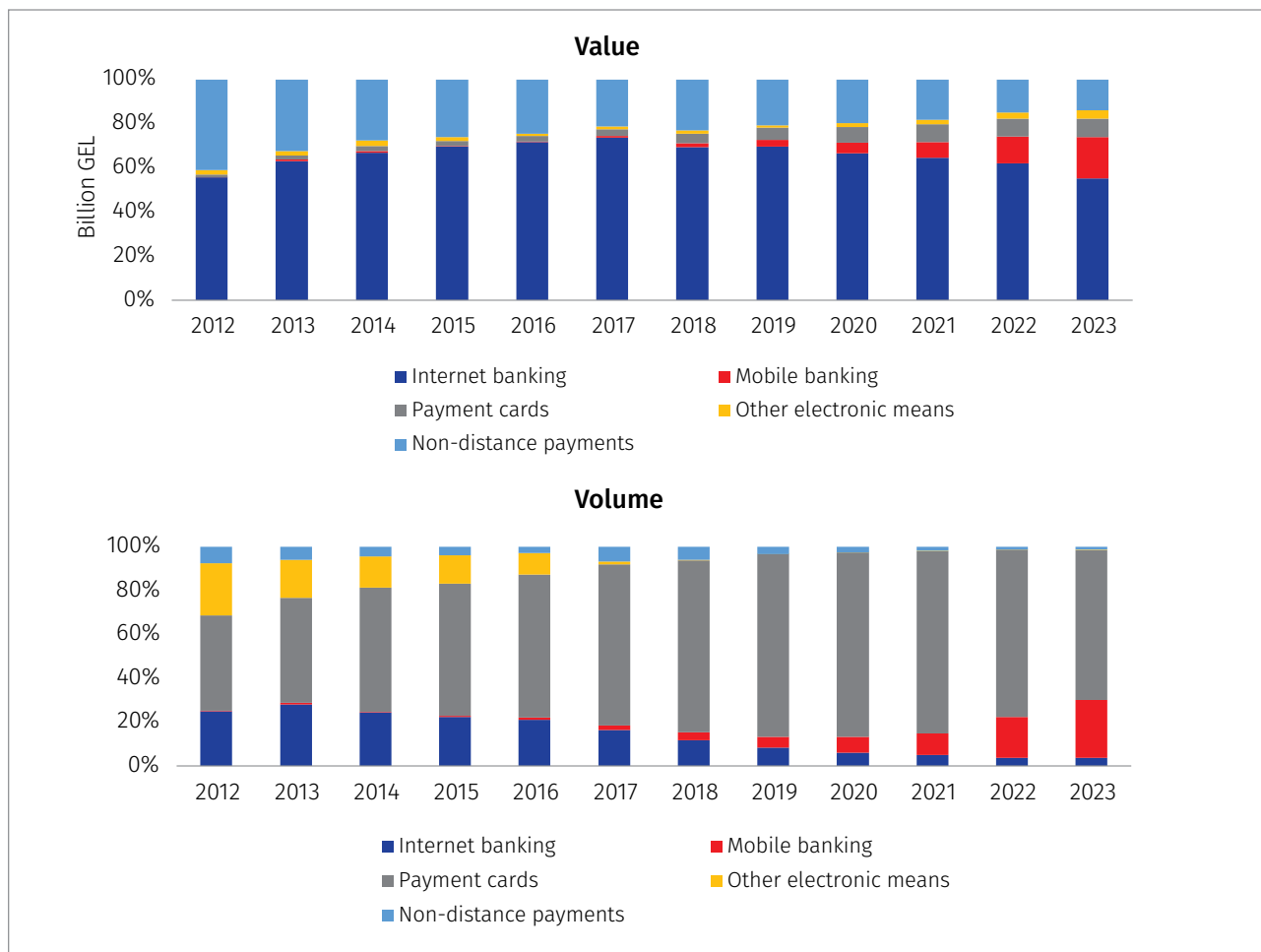
than in 2022. Quantitatively, the most frequently used electronic payment method remains the card instrument. In 2023, the number of payments made through cards increased by 36.6 percent, making up 68 percent of total non-cash payments. The number of payments made through internet banking also increased by 46 percent, comprising 4 percent of the total number of non-cash payments.

In monetary terms, payments made through mobile banking in 2023 increased by 104 percent compared to the previous year, accounting for 19 percent of total non-cash payments, which is 7 percentage points higher than the previous year. The increase in the share of mobile bank payments was almost entirely at the expense of internet bank payments. Despite this trend, internet banking remains the largest payment channel in terms of monetary value. In 2023, the volume of credit payment orders initiated through internet banking increased by 17.8 percent, accounting for 55 percent of total non-cash payments, which is 7 percentage points less than the previous year, primarily due to the rapid growth of mobile payments. The share of the volume of payments made by card instruments increased insignificantly, by half a percentage point compared to 2022, reaching 9.6 percent of total non-cash payments. Additionally, 3.7 percent of total non-cash payments were made using other electronic means.

As for payments initiated by physical means (in branches, service centers), it is worth noting that their share has been steadily decreasing over the last decade. In 2012, their share was 41 percent of the total payments, but by 2023, it had decreased to 14 percent of the total non-cash payments, which is 1 percentage point less than in 2022.

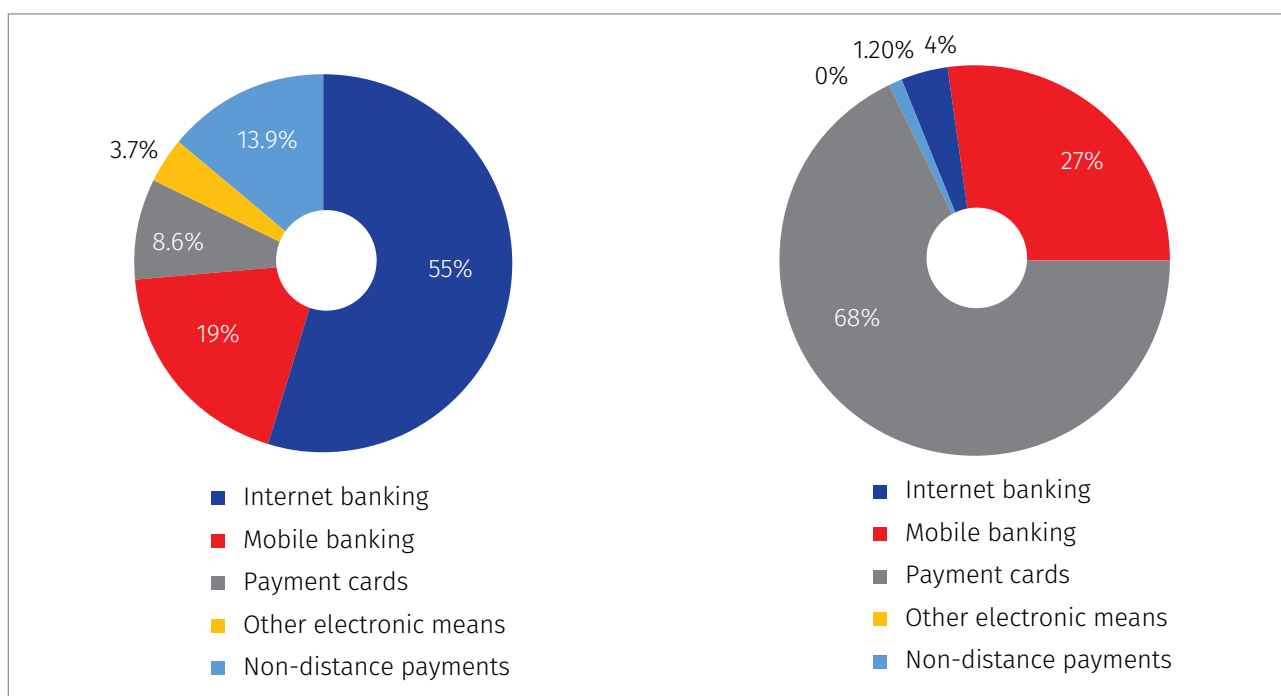
Statistical data of non-cash payments, in terms of means of their initiation, are shown in Diagram N10.10 and Diagram N10.11.

Diagram N 10.10 Use of cashless payment initiation means in 2012-2023



Source: NBG

Diagram N 10.11 Distribution of cashless payments by means of initiating payment orders (2023)

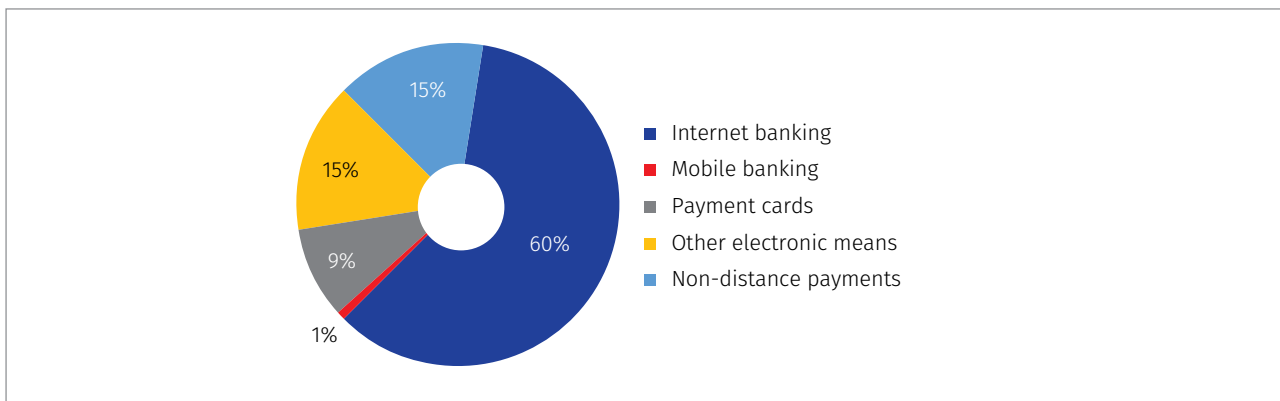


Source: NBG

In 2023, significant efforts were made to enhance the process of receiving the information on payments made by commercial banks. Notably, the statistics on bank payments were expanded to include data on payments made abroad, categorized by the country of the receiving bank. This detailed breakdown allows for a more in-depth analysis of cash flows. According to the 2023 data, payments made abroad, like local payments, are predominantly conducted through internet banking, accounting for 60 percent of the total amount of payments made abroad. The second and

third most common methods are non-remote/bank-initiated payments with a 15 percent share, and card transactions with a 9 percent share. Payments made via mobile banking abroad are minimal, constituting only 1 percent of the total amount (see diagram N10.12). Regarding the quantitative indicators of payments made abroad, card payments are the clear leader, making up 98 percent of the total number of payments. Internet banking payments account for 1.4 percent, and non-remote/bank-initiated payments represent 0.6 percent of the total.

Diagram N 10.12 Distribution of the amount of non-cash payments abroad according to the means of their initiation (2023)



## 10.4. CARD INSTRUMENTS MARKET

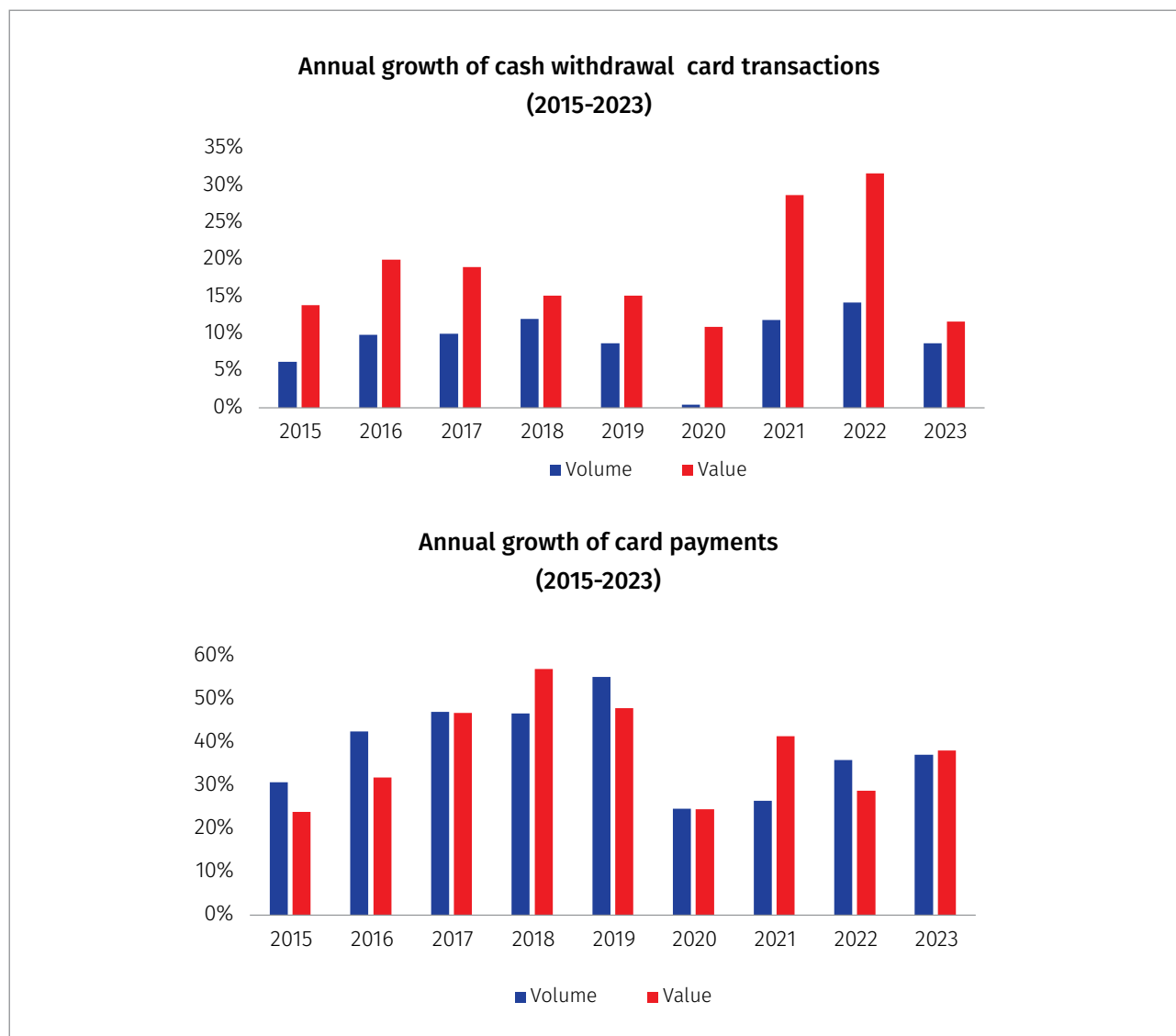


In 2023, following the development of innovative services in the payment market, the introduction and improvement of mobile applications by commercial banks (including Google Pay and Apple Pay) continued actively. This progress led to a significant increase in card operations performed via these applications. Specifically, compared to 2022, the number of operations performed with mobile applications increased by 53 percent, and the monetary value of these operations grew by 33 percent. The annual growth rate of cash withdrawal operations with card instruments experienced a sharp decrease, dropping

from 31.6 percent in 2022 to 11.6 percent in 2023. Conversely, the annual growth rate of cashless card payment transactions in 2023 was 37.8 percent, which is 10 percentage points higher than the corresponding rate in 2022. A similar trend is observed in terms of the number of operations performed with card instruments. In 2023, the increase in the number of cash withdrawal operations compared to the previous year was 8.7 percent, which is 5.4 percentage points lower than the similar figure for 2022. On the other hand, the growth rate of non-cash payments by card increased by 3.3 percentage points, reaching 36.9 percent.

Diagram N10.13 depicts the annual growth of quantitative and monetary indicators of card operations from 2015 to 2023:

Diagram N 10.13 Annual Growth of Card Operations, in amount and number

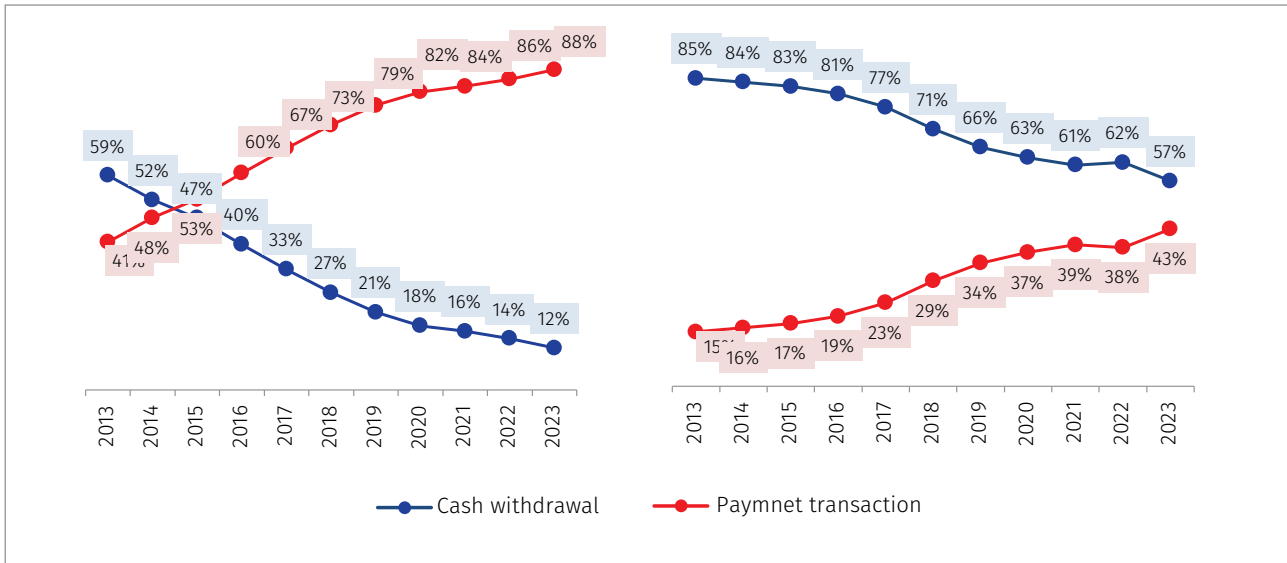


Source: NBG

The above dynamics of cash withdrawals and non-cash payments carried out by the card instruments had a positive effect on the growth of the share of non-cash payments, which in 2021-2022 was noticeably slower compared to the dynamics of previous years.

More specifically, the share of non-cash payment transactions in the total amount of card transactions increased by 5 percentage points and amounted to 43 percent (Diagram N10.14).

Diagram N 10.14 Dynamics of the share of cash withdrawals and non-cash payments made by card instrument in 2013-2023

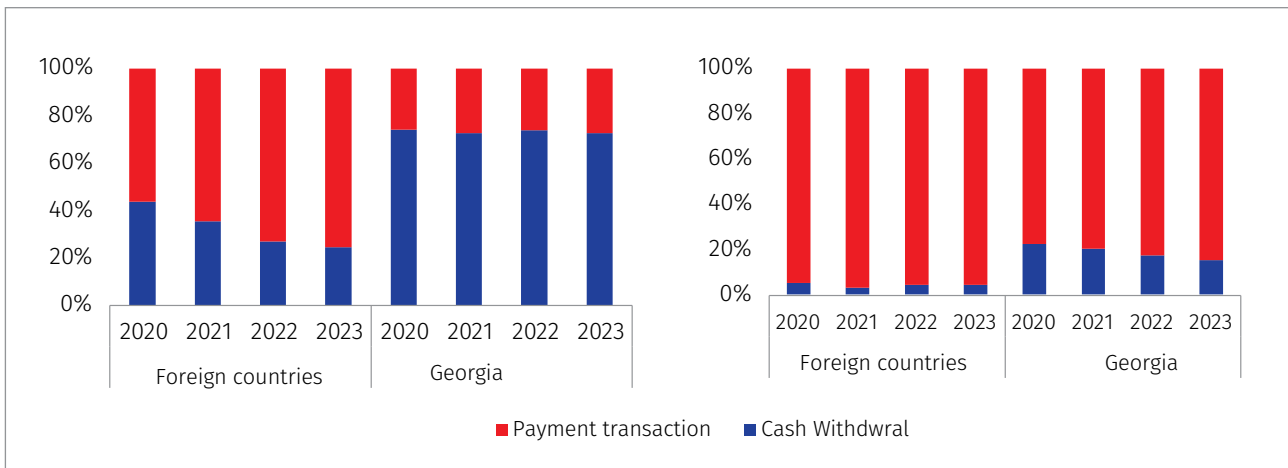


Source: NBG

In 2023, a total of 894 million operations amounting to 72.3 billion GEL were performed with card instruments issued in Georgia. Of these, 92 percent of the operations and 90 percent of the total amount were conducted within the country, which is slightly different from the similar indicators of the previous year. Notably, the share of non-cash payments (both in terms of number and amount) for operations carried out abroad is significantly higher compared to those

conducted within Georgia. Specifically, the share of cash withdrawal operations abroad is 10.8 percent by amount and 1.3 percent by number, whereas in Georgia, the shares are 61.6 percent by amount and 12.5 percent by number. Additionally, the trend of increasing the share of operations with physical POS terminals is nearly equally evident for both domestic and international transactions (Diagram No.10.15).

Diagram N 10.15 Dynamics of the share of cash withdrawals carried out by card instruments and payments by POS terminals abroad and in Georgia in 2020-2023

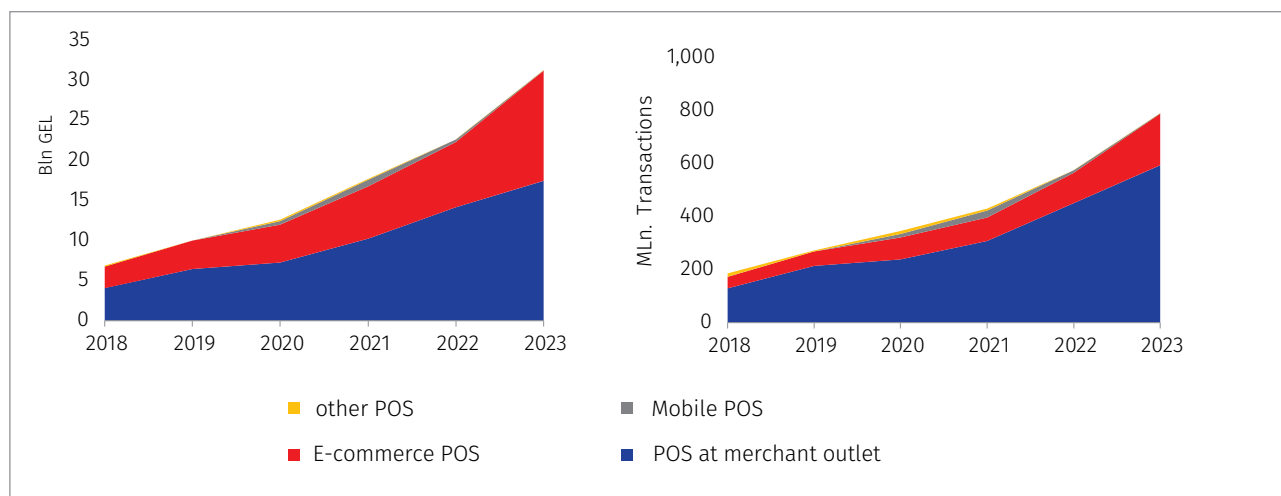


Source: NBG

In 2023, e-commerce transactions accounted for 25 percent of the number and 44 percent of the amount of non-cash payment transactions carried out in Georgia and abroad. These figures represent an increase of 5 and 8 percentage points, respectively, compared to the indicators of 2022. Additionally, 30 percent of the amount and 26 percent of the number of payments made via e-commerce terminals were from operations

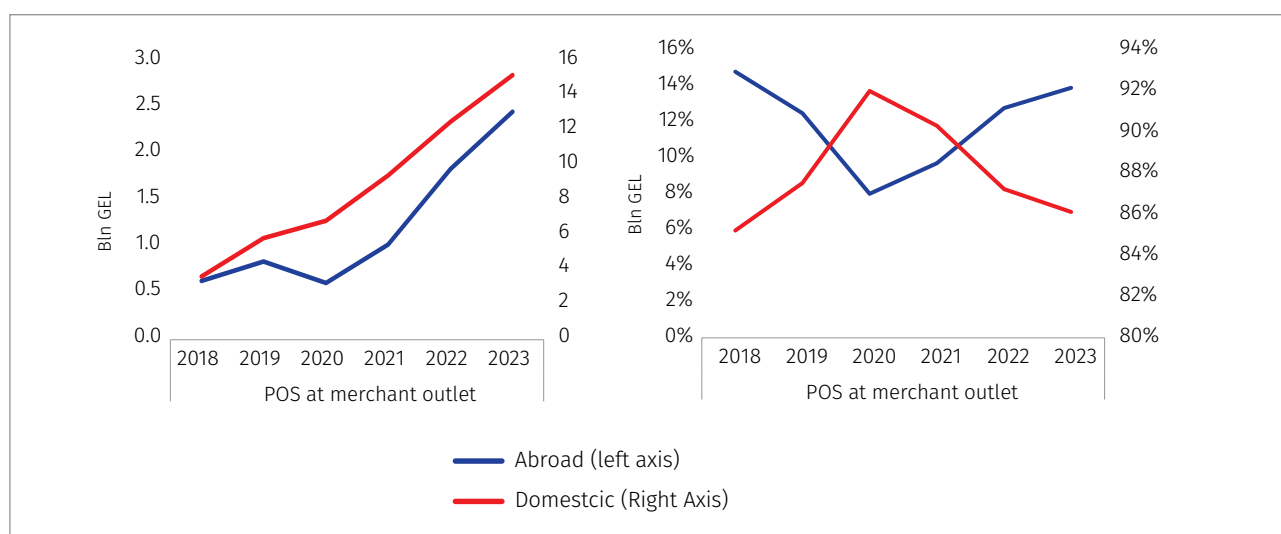
performed abroad. In contrast, for payment POS terminals, only 14 percent of the amount and 3.5 percent of the number of operations were from transactions conducted abroad (Diagrams N10.16-10.17 show the dynamics of non-cash payment operations). It is worth noting that the share of Georgian card payments made at foreign payment POS terminals in 2022-2023 has returned to pre-pandemic levels (see diagram N10.17).

Diagram N 10.16 Dynamics of non-cash payment transactions performed with cards issued in Georgia 2018-2023



Source: NBG

Diagram N 10.17 Restoring the dynamics of payments made with Georgian cards at POS terminals abroad after the pandemic

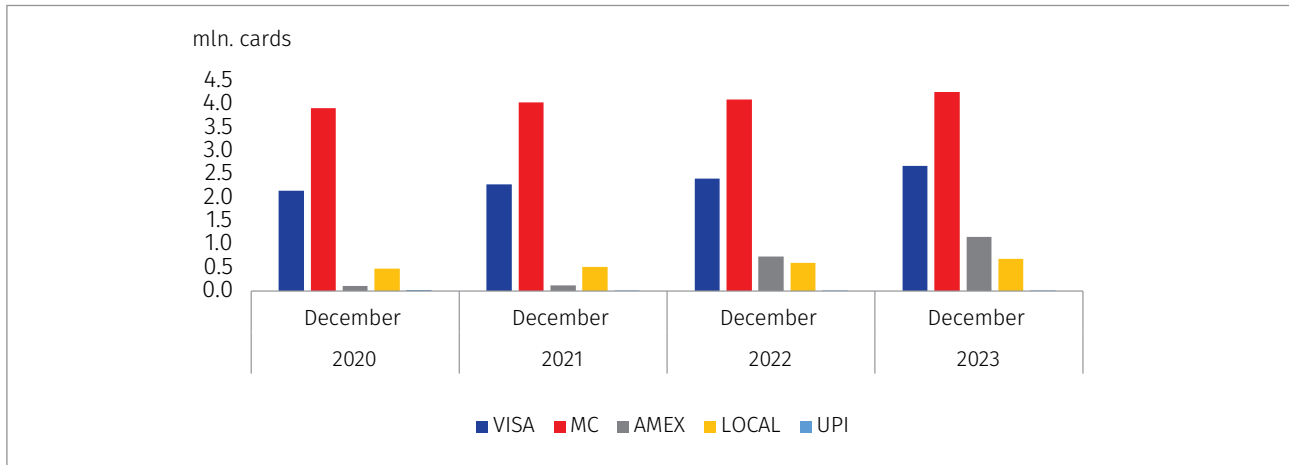


Source: NBG

As of December 31, 2023, commercial banks in Georgia had issued a total of 8.8 million debit and credit payment cards, which is a 13 percent increase from the corresponding indicator of 2022. Of the issued cards, 87 percent are chip cards<sup>80</sup>, and 6 percent are credit

cards. The number of payment cards issued per capita is 2.4. Cards of international card schemes make up the largest share of cards issued in Georgia, accounting for 93 percent of all issued cards. The dynamics of payment cards issued by year according to card schemes is shown in diagram No.10.18:

Diagram N 10.18 Number of cards issued by commercial banks according to card schemes

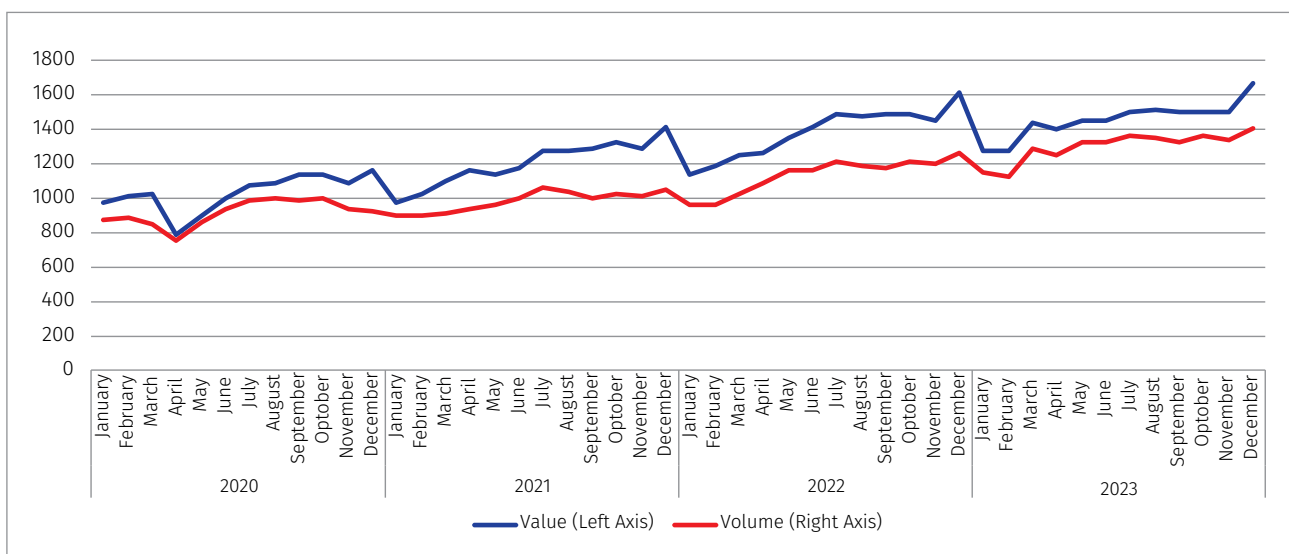


Source: NBG

During 2023, the monthly average number of active cards<sup>81</sup> was 4.1 million, which is 49.3 percent of the monthly average number of issued cards and slightly (by 0.5 percentage points) exceeds the similar indicator of 2022. In 2023, the average number of operations performed per month with one active card was 18, and

the amount was 1.5 thousand GEL, which is 2 operations and approximately 100 GEL more than the corresponding indicators of the previous year. Diagram No. 10.19 shows the dynamics of the number and amount of payments made per month on average with active cards.

Diagram N 10.19 Average number and amount of payments made per month with an active card



Source: NBG

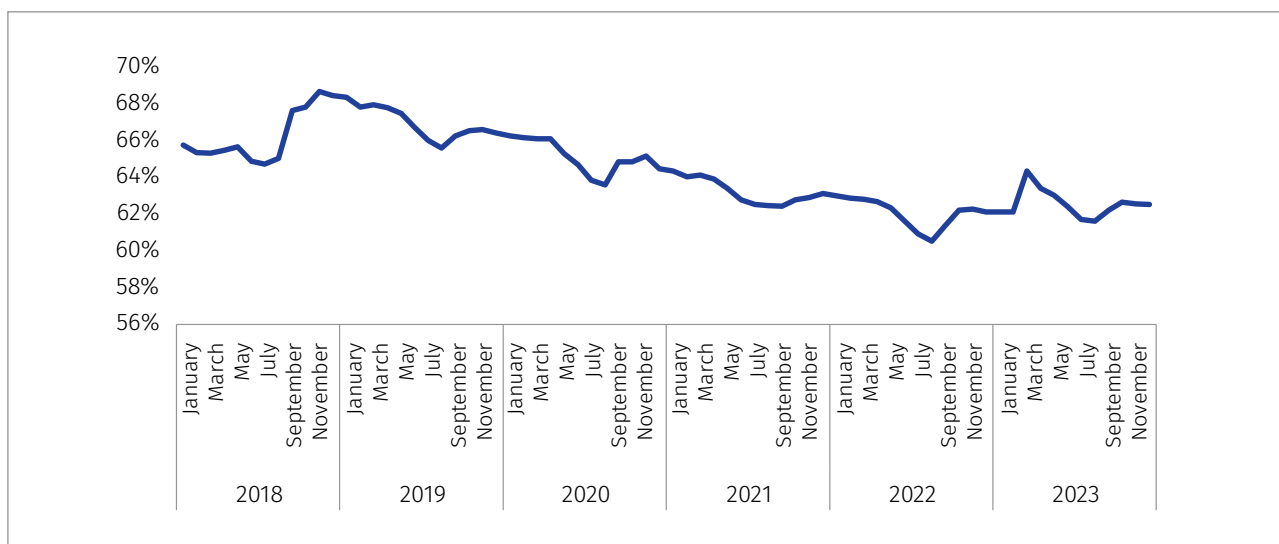
80. Chipless (no magnetic strip) cards are special purpose and social cards, the use of which is significantly less for payments.

81. Active card - an issued payment card that performed at least one transaction during the reporting period.

As of December 2023, there were approximately 106,000 payment POS terminals in Georgia, which is 25 percent more than in the corresponding period of the previous year. 63 percent of POS payment terminals are located

in the capital. Despite this concentration, the past 5 years has seen a tendency to decrease the share of payment POS terminals located in Tbilisi.

Diagram N 10.20 Share of the number of payment POS terminals located in Tbilisi in total payment POS terminals (2019-2023)



Source: NBG

In 2023, a total of 828.8 million operations were performed with card devices located in Georgia, amounting to 70.6 billion GEL. These figures are 29% higher in terms of the number of operations and 19% higher in terms of the amount compared to the corresponding indicators of 2022. In 2023, 97 percent of the number of operations and 95 percent of the amount were performed with Georgian card instruments, and the rest are operations performed with foreign card instruments. 87 percent of the number of card transactions performed (38 percent of the amount) are non-cash payment transactions.

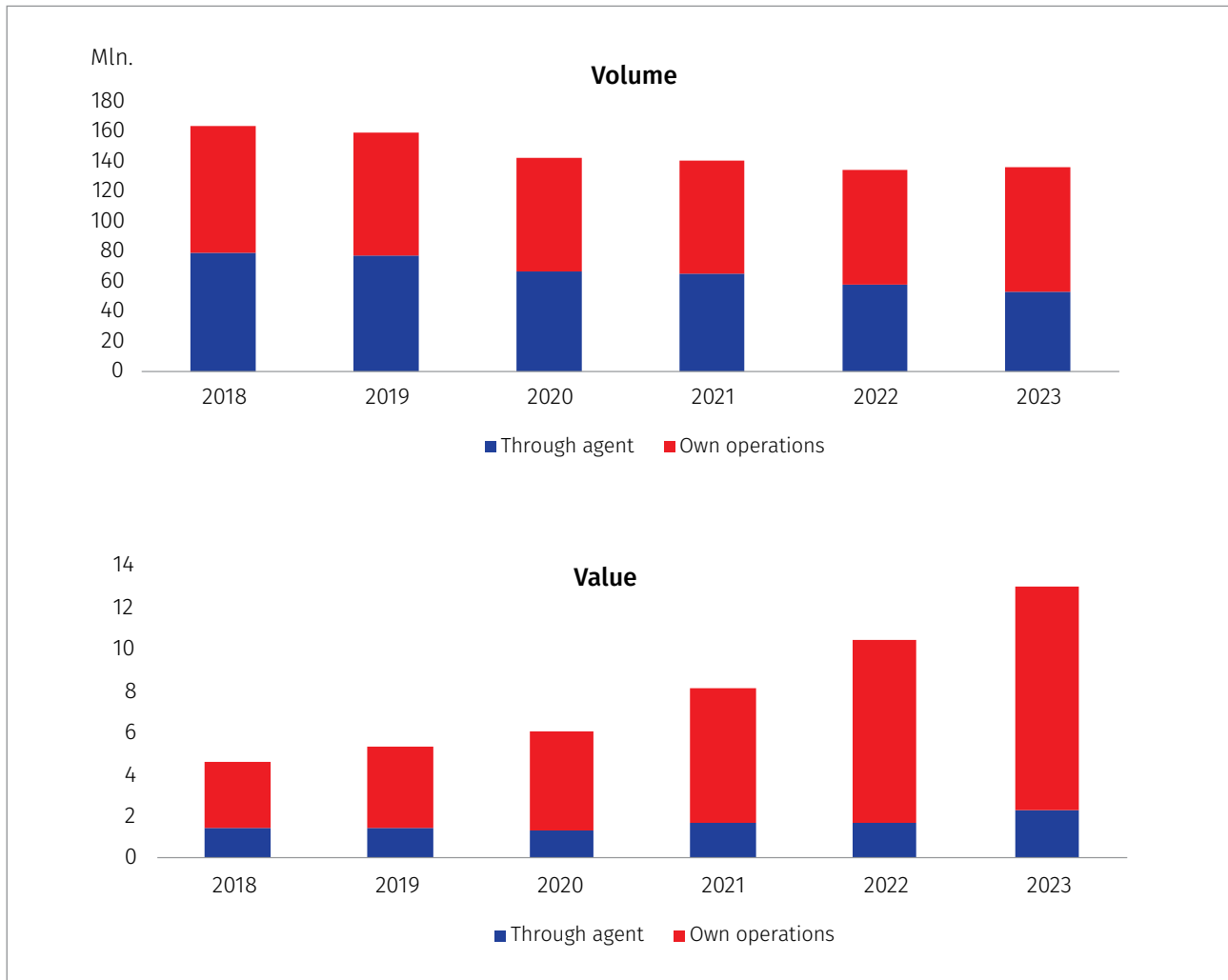
## 10.5. PAYMENT SERVICE PROVIDERS



### Provider Payments (except transactions with electronic money)

In 2023, payment service providers carried out 137.6 million operations with a total volume of 13.1 billion GEL. Compared to 2022, the number of payments increased by 2%, while the amount increased by 25%. The dynamics of provider payments, excluding electronic money, are shown in Diagram No.10.21. Self-service kiosks have traditionally been used to make payments, enabling users to initiate electronic payments with cash. In 2023, 89% of the total number of payments and 95% of the total amount were made through kiosks, which is 5 and 0.2 percentage points less than the similar indicators of 2022, respectively.

Diagram N 10.21 Payments made by payment service providers (except electronic money)

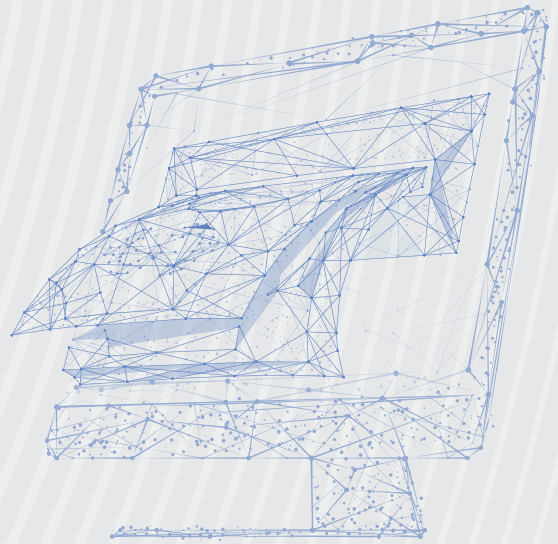


Source: NBG

### Payments with Electronic Money

In the electronic money payments market of 2023, prepaid transport cards have traditionally held a special position. The average amount of a single payment made using these cards is 0.44 GEL, which is significantly different from payments made with other forms of electronic money. Notably, transport cards are widely used for paying for city public transport, which

is why the number of payments made through them is considerably higher than the number of payments made with other electronic money, accounting for 94 percent of the total number of electronic money payments and 11.6 percent of the total amount. In 2023, electronic money providers (excluding transport payments) facilitated 12 million payments totaling 386.2 million GEL.



# SUPERVISION OF PAYMENT SERVICE PROVIDERS AND REGISTRATION OF VIRTUAL ASSET SERVICE PROVIDERS

11

On September 9, 2022, the Parliament of Georgia approved a package of legislative amendments to the Law of Georgia *On Payment System and Payment Service* to align it more closely with the European Directive, specifically the Payment Service Directive 2 (PSD2). These amendments, among other matters, included the introduction of two new payment services: account information and payment initiation services. Furthermore, it introduced the registration and regulation of new types of payment service providers at the National Bank of Georgia, which providing above mentioned payment services. The legislative package also established a regulatory framework for virtual assets and virtual asset service providers within Georgia, which goal was to oversee the registration, registration cancellation, and AML/CFT (Anti-Money Laundering and Countering the Financing of Terrorism) measures for virtual asset service providers. During the development of this regulatory framework, guidelines from the Financial Action Task Force (FATF) and recommendations from international partner organizations were incorporated. Consequently, amendments were made to several laws of Georgia, including: the Organic Law of Georgia *On the National Bank of Georgia*, the laws: *on Facilitating the Prevention of Money Laundering and Terrorism Financing*, *on Commercial Banks' Activities*, *on Microfinance Organizations*, *On Securities Market*, and *On Registration Fees*. Additionally, on March 10, 2023, when the Parliament of Georgia approved the Law of Georgia on the Activities of Microbanks, certain virtual asset services were defined as permissible activities for microbanks, along with banks, microfinance organizations, and brokerage companies. Detailed information on these legislative changes related to virtual assets can be found on the official website of the National Bank of Georgia at [www.nbg.gov.ge](http://www.nbg.gov.ge), under the following tab: Supervision → AML/CFT Supervision → Virtual Asset Service Providers (VASPs). With the amendments to the Organic Law of Georgia On the National Bank of Georgia, the National Bank of Georgia was tasked to develop legal acts, including the rule for the registration, registration cancellation, and regulation of virtual asset service providers by July 1, 2023, and the rules for determining information

accompanying the transfer of virtual assets by January 1, 2024. Additionally, amendments to the Law of Georgia *On Payment System and Payment Services* instructed the National Bank of Georgia to update and develop relevant legal acts, specifically the Rule of Registration and Regulation of Payment Service Providers and the Regulation on Capital Adequacy Requirements of Payment Service Providers by May 1, 2023, to further align with Euro-directives.

In the National Bank of Georgia, the following structural units were defined as responsible for the development of bylaws: the Supervision Division of Payment Service Providers and the Payment Systems Oversight Division of the Payment Systems Department and the Legal Department. Money Laundering Inspection and Supervision Department also was defined as the structural unit responsible for the development of by-laws related to virtual assets.

In March 2023, the responsibility for the registration of virtual asset service providers was added to the duties of Payment Service Providers Supervision Division. In November 2023, the Division of Payment Service Providers Supervision and Virtual Asset Service Providers Registration was separated from the Payment Systems Department and transformed into a department that combines two divisions: the Supervision and Registration Division and the Regulation and Support Division.

The main task of the newly created department is to register and supervise payment service providers, including important payment service providers, as well as account information service and/or payment initiation service providers. Additionally, the department is responsible for the registration of virtual asset service providers and the evaluation of schematic descriptions of their services, including the representatives of the financial sector who are authorized to implement virtual asset services by the activity regulatory legislation. Within the scope of its competence, the department is also responsible for the development of prudential supervision of payment service providers and the normative base and standards of virtual asset service providers.

## Legal Acts Developed

On May 1, 2023, the updated version of the **Rule on Registration and Regulation of Payment Service Providers** was approved by Decree No. 77/04 of the Governor of the National Bank of Georgia. The need for the change was due to the amendments made to the Law of Georgia *On Payment System and Payment Service* on September 9, 2022, as well as the need to strengthen the supervision of the activities of providers operating in the payment market and to address the challenges identified in practice during market regulation.

When changing the regulation, local practice and the following guideline of the European Banking Authority (EBA) were incorporated: Guidelines on the information to be provided for the authorization of payment institutions and e-money institutions and for the registration of account information service providers under Article 5(5) of Directive (EU) 2015/2366. In the new edition of the document, two new payment services, account information and payment initiation services (so-called open banking services) provider registration issues were added. The regulation also established criteria for determining a important payment service provider, new criteria for the suitability of the administrator, and requirements for persons with significant influence, significant share (direct/indirect) holders, and beneficial owners. The adjustments to the requirements related to internal policies and risk management were also made. The regulation clarified records including business plan, head office requirements, and schematic descriptions. Additionally, new terms and appendices were added to the regulation. The regulation defined the terms and form of publication of the list of payment services agreed with the National Bank of Georgia by payment service providers. According to the new edition, by June 1, 2023 the payment service providers were instructed to present to the National Bank of Georgia the list of payment services which they had been providing in accordance with the service schemes presented within the notification. In September 2023 (within the time frame determined by the legislative amendments), the National Bank of Georgia published the list of payment service providers indicating the payment service/

services permitted for the respective provider.

From 2024 (after the entry into force of capital adequacy requirements for providers and no later than April 15, 2024) important payment service providers are indicated separately in the said list.

By the decree of the Governor of the National Bank of Georgia No.79/04 of May 1, 2023, the **Regulation on capital adequacy requirements of payment service providers** was approved. The development of the regulation was prompted by the amendments made to the Law of Georgia *On Payment System and Payment Service* on September 9, 2022, within the framework of convergence with the Euro-Directive, PSD2, and its purpose was to facilitate financial stability of important payment service providers in Georgia, including electronic money important provider, also payment initiation service providers (authorized payment institutions and e-money institutions according to PSD2), effective functioning and reduction of risks arising from business activities. The regulation details the methods for calculating supervisory capital, as well as the criteria that capital instruments must meet in order for a provider to be eligible for Tier 1 or Tier 2 capital and to meet minimum supervisory or supervisory capital requirements. January 1, 2024 was set as the effective date of the regulation.

The decree of the Governor of the National Bank of Georgia No. 94/04 of June 13, 2023 approved the **Regulation on Registration, Registration Cancellation and Regulation of Virtual Asset Service Providers at the National Bank of Georgia**, which came into effect on July 1, 2023. The regulation applies to the virtual asset service providers and the representatives of the financial sector, who have been granted the authority to provide the virtual asset service by the pertinent legislation. The regulation provides for the registration requirements of the virtual asset service providers, the eligibility criteria of the administrators and the significant stake holders, both direct/indirect and beneficial owners; AML/CFT requirements for head office, branches, self-service kiosk, electronic system and other obligations.

It is worth to note, that prior to completion of development of the *Regulation on registration, registration cancellation and regulation of the virtual asset service providers in the National Bank of Georgia*, on May 31, 2023, the comprehensive regulation of the virtual assets European market was published the Regulation (EU) 2023/1114 Markets in Crypto Assets Regulation, and amending Regulations (EU) No 1093/2010 and (EU) No 1095/2010 and Directives 2013/36/EU and (EU) 2019/1937, which is a mandatory regulation for the EU member countries from December 30, 2024. According to that regulation, European financial sector regulatory bodies - European Securities and Markets Authority (ESMA) and European Banking Authority (EBA) were instructed to issue corresponding guidelines and technical standards. The National Bank of Georgia continues to monitor the process of implementing Euro-regulations, guidelines and technical standards in the European territory and, along with Georgia's acquisition of candidate status, plans to cooperate with European financial sector regulators in order to improve the legal framework of virtual assets in the territory of Georgia in the future.

In 2023, work was underway on updating the decree of the Governor of the National Bank of Georgia No. 253/04 of November 30, 2018 on the *Approval of the Regulation on Information Accompanying the Transfers* in relation to virtual asset service providers and those representatives of the financial sector who are authorized by law to provide virtual asset services. The title of the document was also changed to **Regulation**

**on the information accompanying the transfer of funds and the transfer of virtual assets.** The main purpose of these changes is to promote transparency and traceability of virtual asset transfer transactions and ensure compliance with the requirements of the Financial Action Task Force (FATF) recommendations related to virtual assets. While working on the draft, the regulation of the European Parliament and the following European Council of 31 May 2023 was considered: Regulation (EU) 2023/1113 of the European Parliament and of the Council of 31 May 2023 on information accompanying transfers of funds and certain crypto-assets and amending Directive (EU) 2015/849. Given the complexity of the changes and the scope of the requirements, as well as the significant technological solution to be implemented, the virtual asset providers were allowed to ensure compliance with the requirements of the decree until December 31, 2027.

### Payment Service Providers

By the end of 2023, the number of payment service providers registered with the National Bank of Georgia was 31. During the year, 3 entities were registered with the NBG and the status of payment service provider was granted to them. The registration of 2 payment service providers in the NBG was canceled and the process of liquidation began, the liquidation of 3 providers was completed during the year. Changes related to registration/registration cancellation of payment service providers during 2023 are given in the Table N 11.1:

Table N 11.1 Indicators related to the registration of payment service providers during 2023

Change	Number of Providers
Number of providers at the beginning of 2023	30
Registered	3
Registration was canceled and liquidation started	2
Number of providers at the end of 2023	31
Providers in liquidation process	5
Liquidation of the provider completed	3

During 2023, the largest number of providers (17) provided acquiring services and electronic money activities, while no entities provided payment initiation

and/or account information services. The number of providers according to the payment services provided is shown in the Table N 11.2:

Table N 11.2 The number of providers according to the payment services performed

N	Payment Service	Number of providers, providing the corresponding payment service
1	Execution of payment transactions through a payment card or other electronic device, with the funds of the payment service user	10
2	Issuing payment instruments, including electronic money instruments	10
3	Acquiring of payment transactions	17
4	Money remittance	16
5	Issuing of electronic money, execution of payment transactions by electronic money, with mobile phone, internet or other electronic device	17

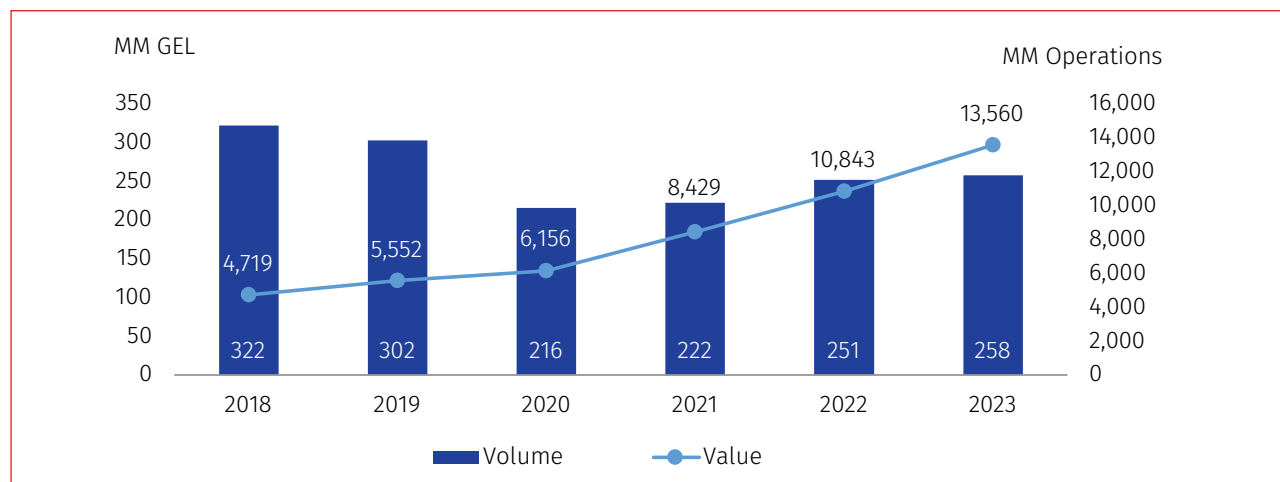
According to changes made in the *Rule on Regulation on Registration and Regulation of Payment Service Providers*, payment service providers already registered with the NBG are required to submit additional documents and information. These obligations were fully met by the providers during the year. Additionally, greater clarity regarding the permitted payment services was provided in the decrees on registration. Consequently, a list of payment service providers, along with the specific payment services allowed for each provider, was published on the official website of the National Bank of Georgia. This list is available under the tab: Payment Systems → Payment Service Providers → Payment Services, at [www.nbg.gov.ge](http://www.nbg.gov.ge).

In 2023, significant changes were made to automatize and systematize the statistical reporting forms of

payment service providers. From March 1, 2023, payment service providers began submitting periodic reports to the NBG through the remote supervision portal, in accordance with the *Regulation on Using the NBFi Remote Supervision Portal* approved by Decree No. 14/04 of the Governor of the National Bank of Georgia, dated January 25, 2023.

During 2023, 257.6 million payment transactions amounting to 13.6 billion GEL were carried out by registered payment service providers. Compared to the previous year, 2022, the number of transactions increased by 3%, and the total amount by 25%. The dynamics of payment transactions performed by payment service providers registered with the NBG over the years are shown in the Diagram N 11.1.

Diagram N 11.1 Payment operations carried out by payment service providers by year



Source: NBG

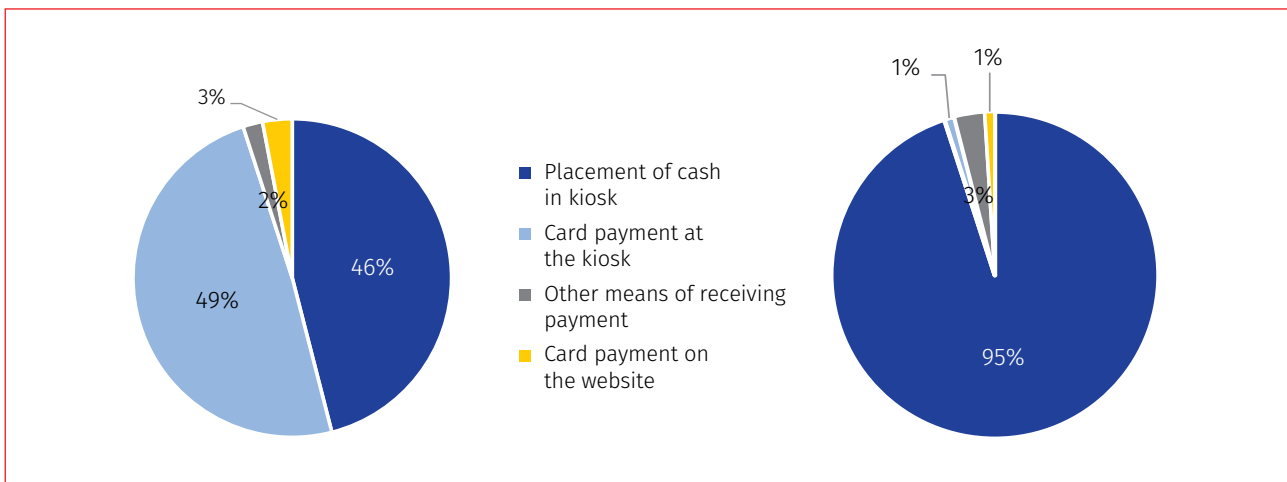
In 2023, 47% of the total number of transactions and 3% of the amount is electronic money payments<sup>82</sup>. 94% of the number of electronic money payments and 21% of the amount were made with prepaid cards (the largest share of which comes from transport cards), the rest of the transactions were made from the provider's website (0.18% of the number and 19% of the amount), with a mobile application (0.28% of the number and 7% of the amount), from the recipient's website (0.1% of the number and 17% of the amount) and other means/ channels (5% of the number and 36% of the amount).

The number of operations performed with self-service kiosks during 2023, compared to 2022, decreased by 2% and the amount increased by 26%. In total, the number

of operations performed by the kiosk during the last year amounted to 122.7 million operations, amounting to 12.5 billion GEL. As of the end of December 2023, the total number of kiosks in the country amounted to 14,544 units, 11% more than the number of kiosks of the previous year.

In terms of means of payment initiation in 2023, the number of card transactions carried out by kiosks (49%) and cash placement operations in kiosks (46%) were the highest. In terms of amount, the 95% were the operations of cash placement in-kiosks. The distribution of the operations performed by means of payment initiation is given in the Diagram 11.2:

Diagram N 11.2 Information on the distribution of operations performed by means of payment initiation



Source: NBG

### Virtual Asset Service Providers

From the second half of 2023, the National Bank of Georgia began accepting and reviewing registration applications of virtual asset service providers operating in the Georgian market. Throughout the year, a total of 32 registration applications were submitted to the NBG. The National Bank of Georgia has completed the

administrative proceedings for one application and has registered one entity as a virtual asset service provider. Due to the complexity of the applications, the decision-making process for the remaining applications is expected to be completed in 2024, in accordance with the deadlines defined by the legislation.

82. Electronic money operations include only electronic money payments and do not include electronic money issuance and redemption operations.



# DEVELOPMENT OF INFORMATION TECHNOLOGIES

12

In 2023, Infrastructure Management Division of the Information Technologies Department introduced modern accurate time synchronization system, that provides high accuracy time service from satellites.

The introduction of the new system has enabled the National Bank of Georgia to provide accurate time delivery services for critical applications, servers, and network devices. This change ensures service delivery independently, without third-party involvement, thereby improving security.

In 2023, the stability of the optical connection between data processing centers was significantly enhanced. Modern optical modules were used to completely update the connection architecture, resulting in improved data replication and throughput between active data storage systems.

Additionally, critical infrastructure systems, such as internet and mail filtering systems, data storage, archiving storage devices, hyperconvergent infrastructure, and other critical components that ensure continuous IT service delivery, were updated to the latest manufacturer-recommended versions.

Similar to the previous year, various changes were made in the application management and cybersecurity departments to comply with SWIFT's Customer Security Program (CSP) requirements. These changes ensured full system security protection and high resilience.

In 2023, employees of the infrastructure management department underwent official manufacturer training and received relevant certifications in the management and administration of modern network security access systems.

Cybersecurity remains a priority for the Information Technology Department of the National Bank of Georgia. Throughout 2023, multiple vulnerability scans of the bank's infrastructure components were conducted to identify and address weaknesses. In addition to vulnerability scanning, the bank's

information technology systems underwent "Gray Box" penetration testing to detect weaknesses and assess potential risks.

During 2023, the cybersecurity department actively continued normalizing, aggregating, and correlating security events through the implemented information security incident monitoring and management system. This effort improved the quality of information security event processing and automated the detection and response to information security incidents.

Year by year, the monitoring and logging system for privileged user access implemented at the bank continues to expand. Privileged access to the bank's critical infrastructure is allowed and monitored through this system.

The National Bank of Georgia annually conducts a self-assessment process to ensure compliance with the Customer Security Program framework established by the World Interbank Financial Telecommunications Society (SWIFT). In 2023, to meet the framework's requirements and successfully complete the self-assessment process, the Cyber Security, Application Management, and Infrastructure Management sections of the Information Technology Department carried out numerous activities.

In today's digital world, the human factor is the most significant risk. Cyber incidents often result from inadequate knowledge and lack of awareness. Therefore, raising employees' cybersecurity awareness is a priority for the National Bank of Georgia. In 2023, the Cyber Security Department conducted mandatory cybersecurity awareness training for the entire bank. Additionally, to assess employees' cyber awareness and response time to incidents, phishing simulations were performed.

The previous year was also productive for the professional development of the cybersecurity department's employees. They attended various online conferences and seminars, including the

notable EU4DIGITAL Cyber Security Capacity Building Workshop. In 2023, the Data Management and Software Department undertook several significant projects to improve the functionality of the bank's electronic systems and participated in the implementation of new projects, including:

- Updating the National Bank of Georgia's unified statistical information system (NBGSTAT):
- Expanding the PCS family of payment card statistics. Updates to the NBGSTAT real environment were completed, specifically transferring the extended PCS data family from the test to the production environment.
- Introducing a new MTD data family in a test environment for daily remittance data recording for banks. This change was successfully tested by the Data Management and Software Division of the Information Technology Department, the Monetary Statistics Division of the Macroeconomics and Statistics Department, and financial institutions. The task involved updating the database and the structure of certain tables, with functional changes made to nearly all modules.
- Adding a new role to the pass access program, which can be enabled by the administrator. This allows the admitting person to grant a special status to guests.
- Integrating data collected in the turnstile program into the Human Resources Management and Development Department's database. This integration enables the department to monitor and control employee attendance and process the received data effectively.
- GeoGold software was updated, changes were made to the code, formulas and ratios were modified. The logic for calculating the price of a 1,000 gram gold bar and the functionality of forwarding to the TGX system were added to the software.
- Operating systems and software of the critical system databases at the National Bank of Georgia were completely updated in 2023. This upgrade improved support and compatibility with modern

technologies, as well as system performance and stability. The security level and compatibility with other systems, along with the necessary modern technologies for safe and secure communication, were enhanced. Additionally, the level of systems administration was improved.

In 2023, the Applications Administration Department made several changes to various business applications:

- The Wallstreet reserve management system was fully updated and migrated to a new environment.
- SWIFT MX standards were implemented and integrated with Transguard in the B6 of the main banking system in ALTA.
- The SWIFT system was updated multiple times throughout the year, improving the standard of message exchange security.
- The Automated Human Resource Management System (HRMS) was updated to enhance the security of confidential information.
- A unified system for the management and planning of production resources (ERP) was introduced and maintained, enabling the automation of key processes across various structural units of the bank.

In 2023, two significant documents developed by the service department were approved: the *Procedure on the Management of Customer Accounting Records* and the *Procedure on the Management of Information Technology Incidents*.

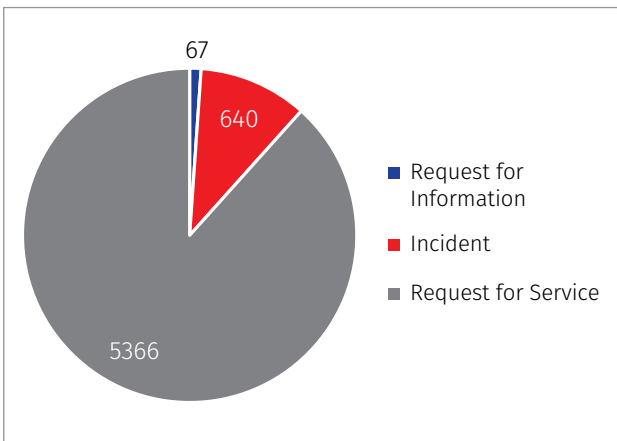
The procedure for managing customer accounting records fully defines the process of creating and managing accounting records of bank employees, as well as the process of unifying customers into functional and legal groups.

Incident management is organized as a comprehensive process that includes incident reporting, registration, response, resolution, closure, updating the relevant knowledge base, and analysis and reporting of results. Based on this, the information technology incident

management process was updated and described in the information technology incident management procedure. This procedure aims to establish mandatory rules for reducing the potential negative impact of incidents.

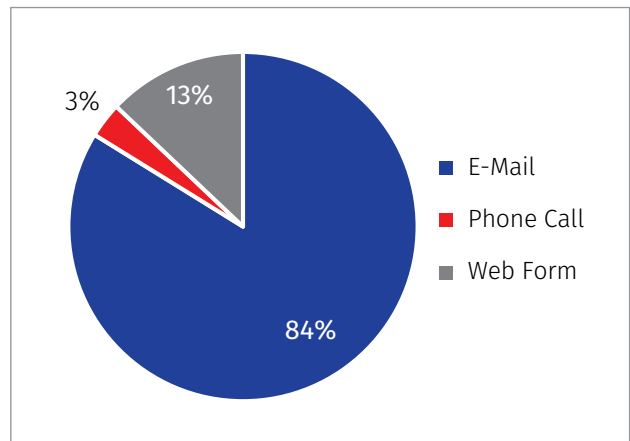
In 2023, a total of 6,073 incidents/requests were registered on the service desk portal. Bank employees demonstrated a high level of responsiveness to service-type requests. The most popular method of reporting a request was by sending a message to the service desk email address.

Diagram N 12.1 Types and number of requests



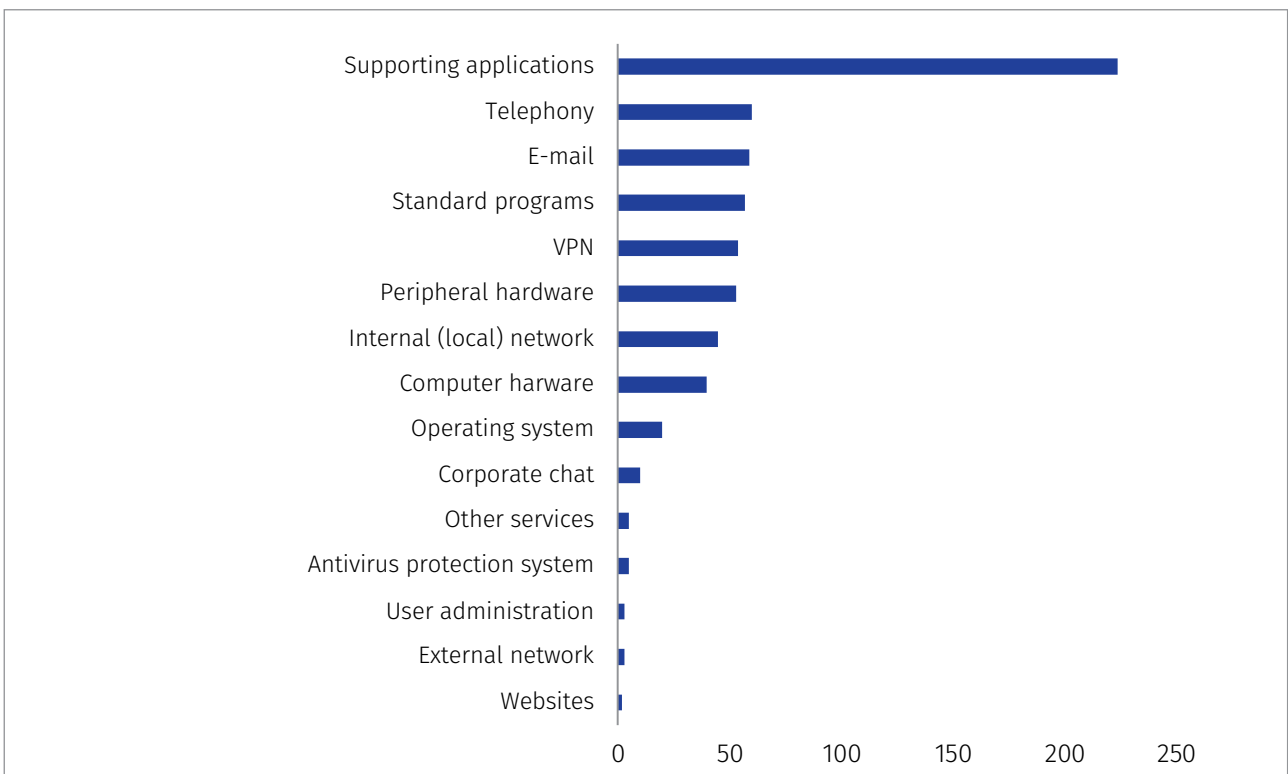
Source: NBG

Diagram N 12.2 Number and sources of registration



Source: NBG

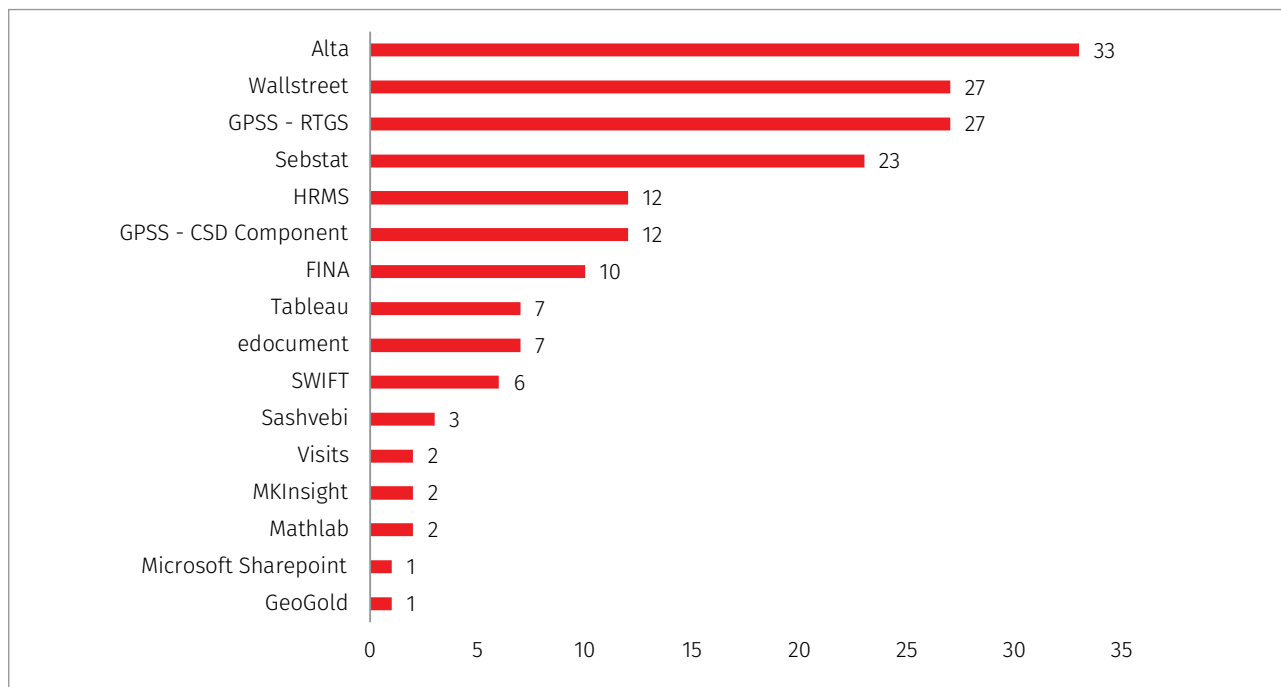
Diagram N 12.3 Most incidents were about the following services:



Source: NBG

Much as 48% of the incidents were made through different business apps.

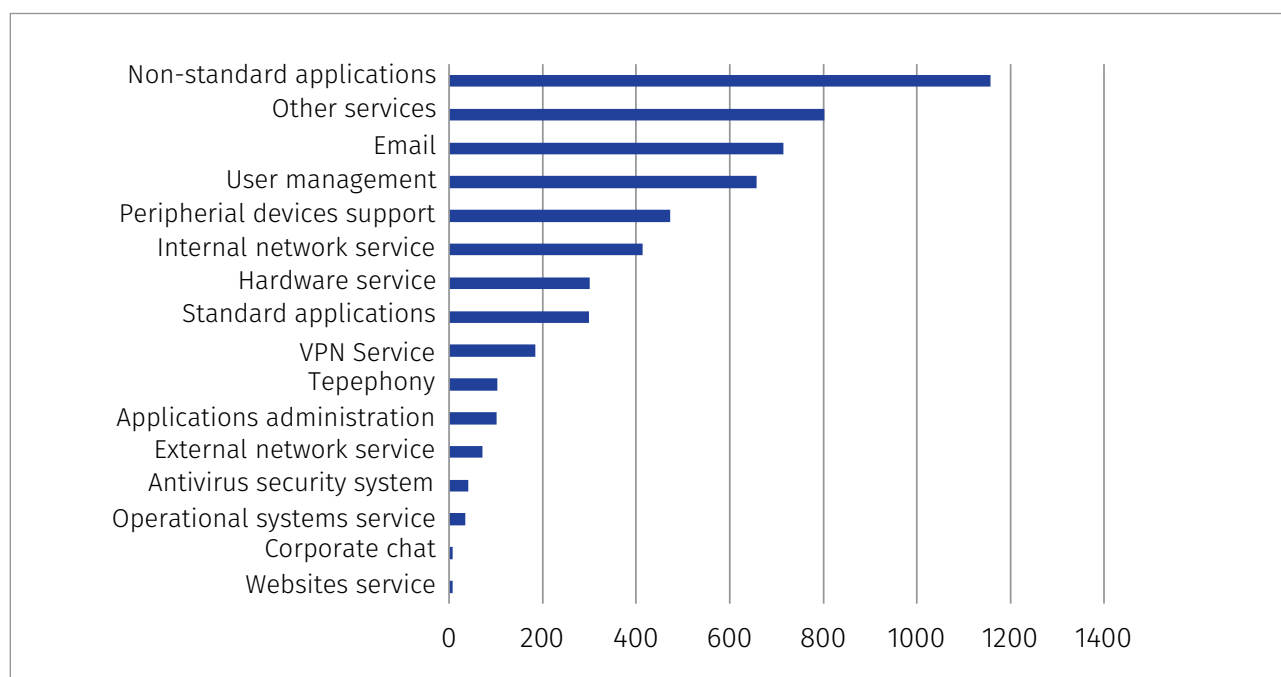
Diagram N 12.4 Incidents through different business apps



Source: NBG

Much as 78 percent of incidents were resolved within the specified timeframe, while 22 percent required more time to resolve, largely due to communication with a third party.

Diagram N 12.5 Most requested IT services according to the annual report of the service desk



Source: NBG

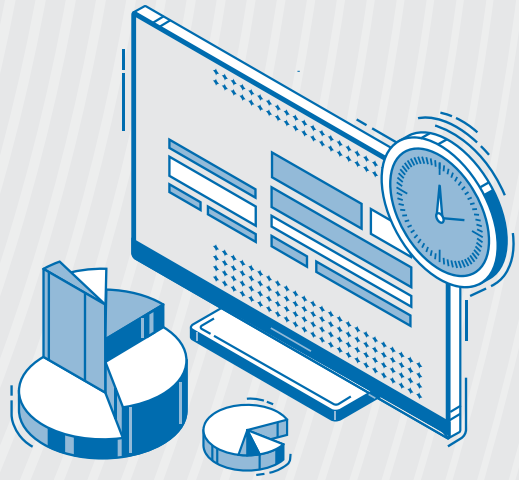
Table N 12.1 The figures for the distribution of incidents and requests between the divisions of the Information Technology Department

<b>IT Department</b>	<b>Information request</b>	<b>incident</b>	<b>Service request</b>
Services Division	27	450	3200
Apps Administration Division	34	97	816
Infrastructure Management Division	3	50	506
Cyber Security Division	3	15	599
Data Management Division	0	28	245

Source: NBG

The year 2023, like previous years, was fruitful in terms of professional growth for employees, as well as the renewal and improvement of information technology processes. The information technology mission of the

National Bank of Georgia remains unchanged: to create, manage, and develop secure, high-quality IT services and infrastructure focused on business requirements and customer needs.



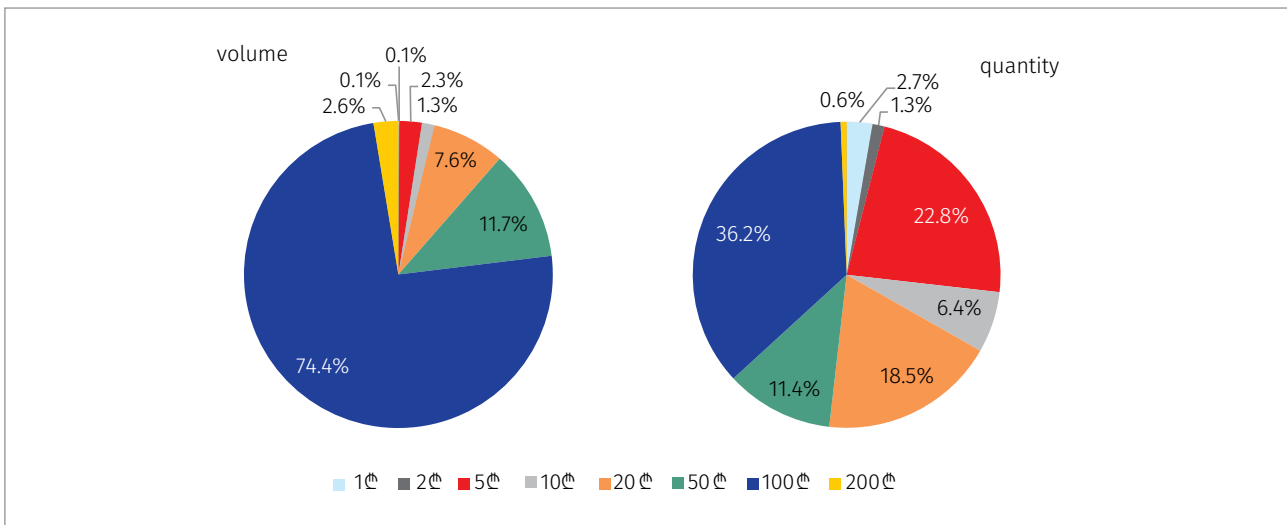
# ORGANIZATION OF CASH AND EMISSION ACTIVITIES

13

Provision of the national economy with cash, regulation of cash circulation, fostering favorable conditions for the circulation of national currency, quality management of national currency in circulation, promotion of the fight against counterfeit money, and promotion of the national currency are important functions of the NBG.

As of December 31, 2023, the cash in circulation amounted to GEL 5,934.1 million. Among them, the banknotes were GEL 5,748.9 million, and the coins were GEL 185.2 million (as of December 31, 2023, the share of banknotes in circulation by individual denominations is shown by amount and quantity on Diagram No. 13.1)

Diagram N 13.1 Share of banknotes in circulation by denominations\*



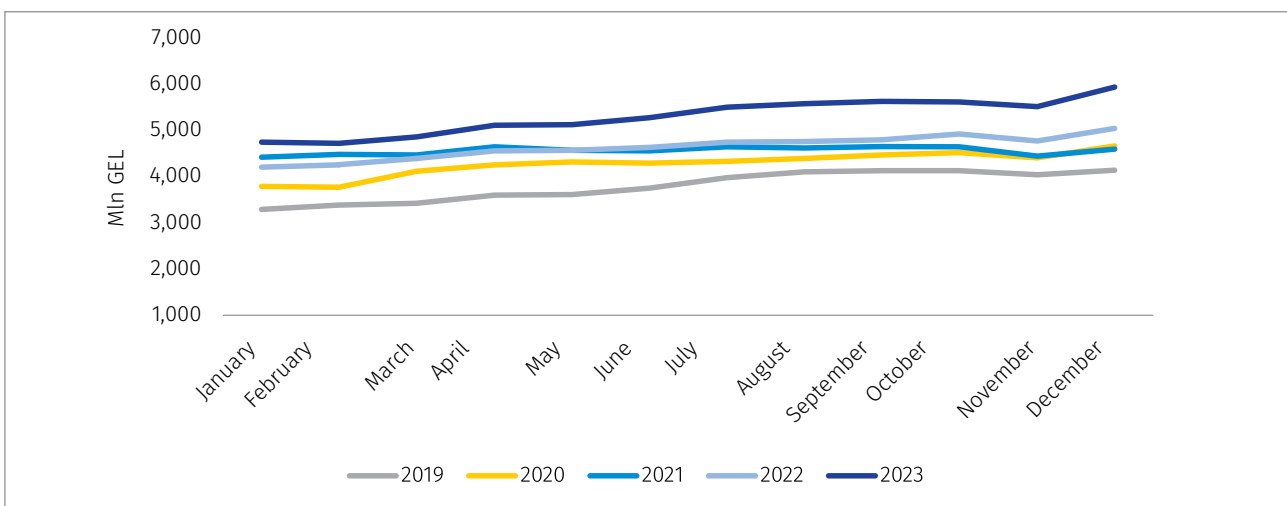
\*Including the 1- and 2-lari banknotes in circulation, which ceased to be manufactured after coins of the same denomination were placed in circulation..

Source: NBG

During the reporting period, the volume of cash in circulation increased by GEL 893.6 million, or 17.7 percent compared to the beginning of the year (The dynamics

of the national currency - GEL circulation in 2019-2023 is shown in Diagram 13.2).

Diagram N 13.2 2 Cash in Circulation (2019-2023)

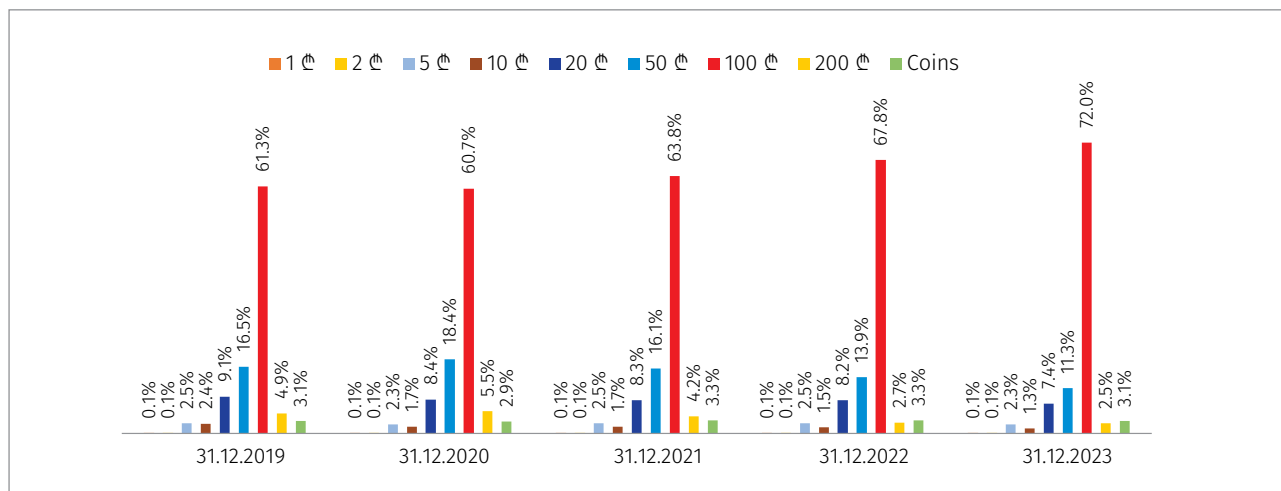


Source: NBG

The amount of banknotes in circulation increased by GEL 875.2 million during 2023, and its share in the total amount of money in circulation was 96.9 percent. The

amount of coins in circulation increased significantly (by 11 %) YoY with the share in the total circulation being 3.1 percent (see Diagram No.13.3).

Diagram N 13.3 Share of banknotes of individual denominations and coins in circulation (2019-2023)\*



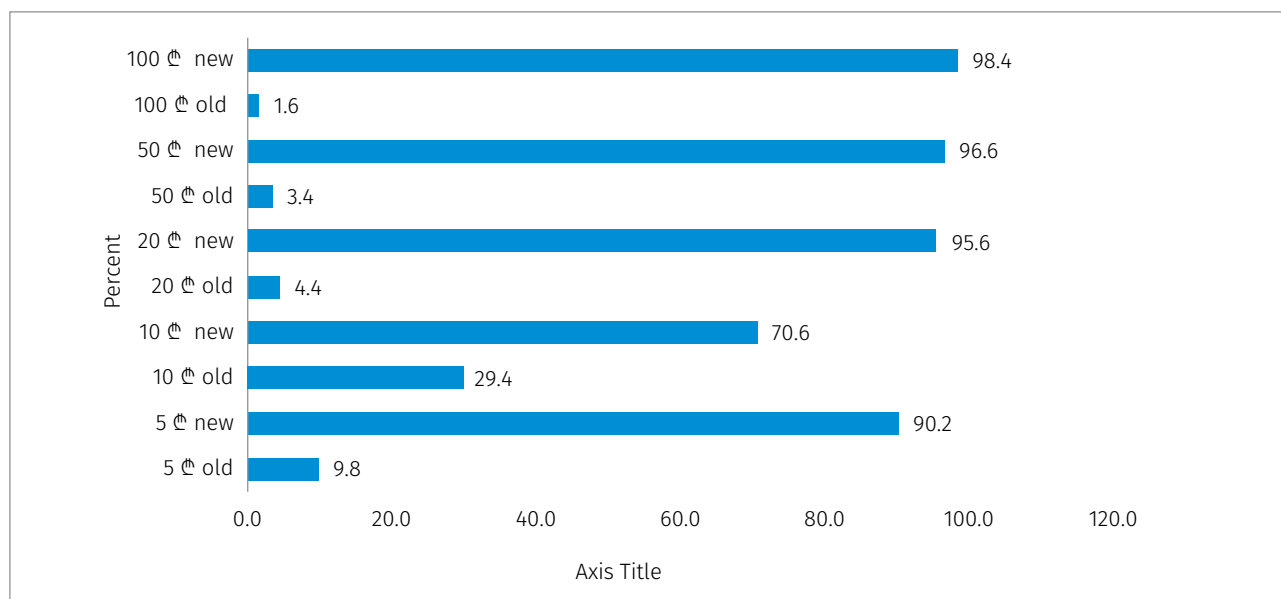
\* Including the 1- and 2-lari banknotes in circulation, which ceased to be manufactured after coins of the same denomination were placed in circulation.

Source: NBG

Upgrading the circulation by withdrawing banknotes issued before 2016 and replacing them by 5-, 10-, 20-, 50-, and 100-lari banknotes of the new issue was ongoing in the reporting period. At the end of the reporting period, the renewed 5-lari banknote accounted for

90.2 % of the total banknote in circulation, the 10-lari banknote accounted for 70.6%, the 20-lari banknote for 95.6%, the 50-lari banknote for 96.6 %, the 100-lari banknote for 98.4 % (Diagram No. 13.4).

Diagram N 13.4 10-, 20-, 50- and 100-lari denomination banknotes in circulation, according to modifications (percentage).



Source: NBG

By the end of the reporting period, the share of the number of banknotes of the old modification (before 2016) in relation to the new modification banknotes of the same denominations in circulation is only 6.2 percent.

The total amount of GEL 1 and 2 coins in circulation increased by 12.2 percent and amounted to GEL 126.2 million at the end of the year. The rate of withdrawal of 1 and 2 GEL banknotes from circulation is insignificant, because after the establishment of coins of this denomination in circulation, the number of banknotes in circulation is significantly reduced.

The amount of tetri coins in circulation increased by 8.7 percent.

To ensure the smooth provision of cash to the country's economy and to replenish the reserve stocks of the National Bank, the following actions were implemented during the reporting period:

- Procedures for selecting a partner for the production of banknotes for circulation were established. An appropriate contract was signed with the selected enterprise, and relevant work with the manufacturer was carried out for the purpose of producing banknotes. Currently, the process of preparing and agreeing on printed samples is underway.
- The process of control inspection of 5 tetri, 1 and 2 GEL coins received in previous years and settlement with their manufacturers has been completed.
- The process of control inspection of 5 tetri, 1 GEL, and 2 GEL coins received in previous years and settlement with their manufacturers has been completed.
- Procedures for selecting a partner for the production of one-denomination coins for circulation were carried out. An appropriate contract was signed with the selected enterprise, and relevant work was conducted with the manufacturer for coin production. At this stage, the manufacturing process is completed, and the

first batch of coins will be delivered in the near future.

- Additionally, partner selection procedures for the production of three-denomination coins for circulation were conducted, and two partner enterprises were selected. The process of signing agreements with these enterprises is currently underway and will be completed soon.

During the reporting period, the production of 1/10, 1/4, 1, 5, and 10-ounce gold coins for investment purposes at the State Mint of Baden-Württemberg was completed, and their full supply was achieved. To promote the national currency and the country, the National Bank of Georgia continued issuing collectible coins during the reporting period (for more information, see below - "Collectible Coins"). In 2023, compared to the previous year, the amount of cash national currency received by the National Bank of Georgia increased to 8,579.6 million GEL, which is 2 percent higher than the 2022 figure. For GEL banknotes, 68.3 percent of total revenues were processed directly at the Cash Center, while 31.7 percent were handled through the external warehouses of the Cash Center. For coins, 53.6 percent of total revenues were processed directly in the Cash Center, with 46.4 percent processed through external storages.

Banknotes issued before 2016 make up 3.3 percent of the GEL banknotes introduced by commercial banks, indicating a significant reduction of these older banknotes in circulation. Among the imported GEL banknotes, 50 and 100 GEL denominations account for 81.4 percent of the monetary share, representing 23.6 and 57.8 percent, respectively.

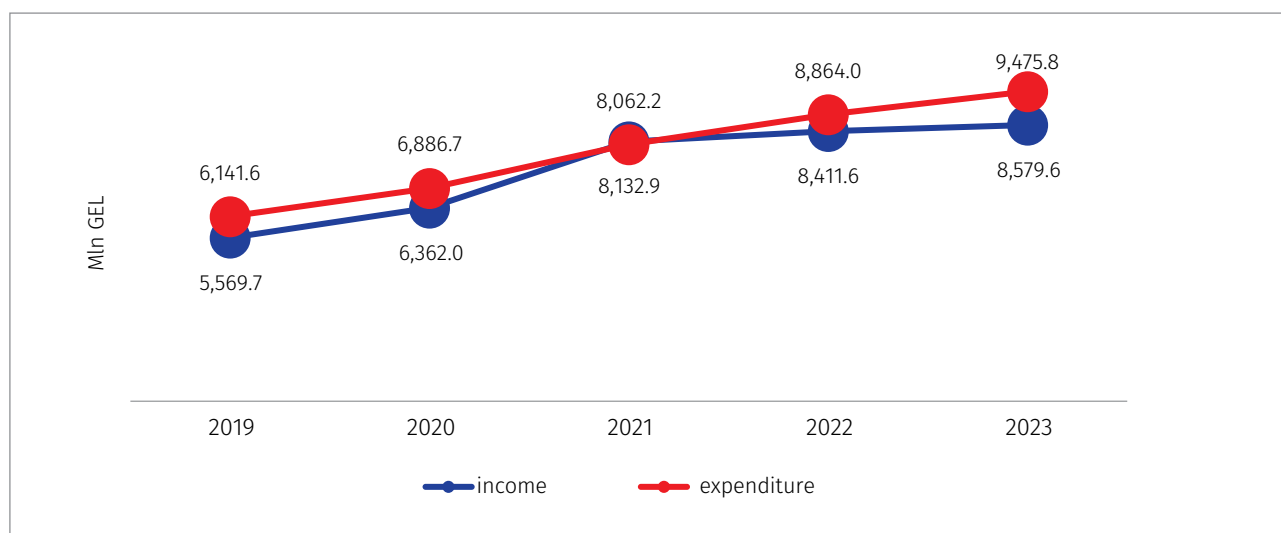
During the reporting year, foreign currency banknotes amounting to 101.9 million US dollars and 50.7 million euros were also received from commercial banks.

In the same period, the funds issued by the National Bank of Georgia amounted to 9,475.8 million GEL, which is 6.9 percent higher than the same indicator of 2022. The outgoing amount of national currency exceeded the

incoming amount by 896.2 million GEL, or 10.3 percent. Banknotes comprised 98 percent of the total money issued. Throughout the year, 50 and 100 GEL banknotes were in high demand among the GEL denominations,

accounting for 82.7 percent of the total amount of GEL banknotes issued to commercial banks. Banknotes of 10 GEL denomination were less in demand.

Diagram N 13.5 Banknotes/Coins in and out of the Cash Center in 2019-2023



Source: NBG

During the reporting year, in response to requests from commercial banks, foreign currency amounting to 10 million US dollars was issued. Additionally, 60.9 million US dollars and 65.4 million euros were sent abroad to be reflected in the respective bank accounts.

In 2023, various technical devices were purchased to ensure the smooth operation of cash-issuing activities. Specifically, 10 pieces of PF-9007 counterfeit money detectors and 7 pieces of MUSASHI COM BBF 2 banknote wrapping devices were acquired. Moreover, complex equipment for laboratory testing of cash, "Docucenter FOSTER+FREEMAN VSC 8000/HS," was selected and purchased, and employee training for its installation and operation was conducted.

The department, with the participation of relevant specialists, organized a study-monitoring of the processing and sorting processes of GEL banknotes and coins in commercial banks. This study also

evaluated the capabilities of the technical facilities for processing GEL banknotes and coins, involving the participation of the department's specialists.

To ensure the production of circulation and collectible GEL banknotes and coins of appropriate quality:

- Samples of silver and gold coins of 20 tetri denomination and the 5 GEL collector coins dedicated to King Pharnavaz I and King Bagrat III, received from the Polish Mint Mennica Polska, were studied and approved.
- The 5 GEL silver and gold coins of 20 tetri denomination, collector coins dedicated to King Pharnavaz I and King Bagrat III made by the Polish Mint Mennica Polska, as well as the 5 GEL coins dedicated to King Giorgi the Brilliant made by the Lithuanian Mint, underwent quality control. This process ensured the quality of the silver and gold coins of the 5 GEL denomination.

To ensure the optimal circulation of the national currency throughout the country, control the quality of GEL banknotes and coins in circulation, and implement appropriate monitoring mechanisms in the channels of circulation, the department worked intensively on developing regulations on processing and recirculating cash, as well as other relevant regulations.

In addition, in accordance with the decision of the NBG Board, the department continued to work towards the decentralization of the cash management model. To this end, we researched international experiences of cash management, organized meetings with representatives of the central banks of Austria, Turkey, and Israel, and hosted a representative from the Bundesbank. During this visit, the cash management policy and future plans of the NBG were discussed. The Bundesbank representative shared their approaches to strategic

issues of cash management and introduced the NBG to best practices of decentralized models integrated by central banks around the world.

Based on the conducted research, the department prepared a short- and medium-term action plan, which included a list of tasks for the step-by-step transition to a decentralized model of cash management. This plan was presented to the NBG Board.

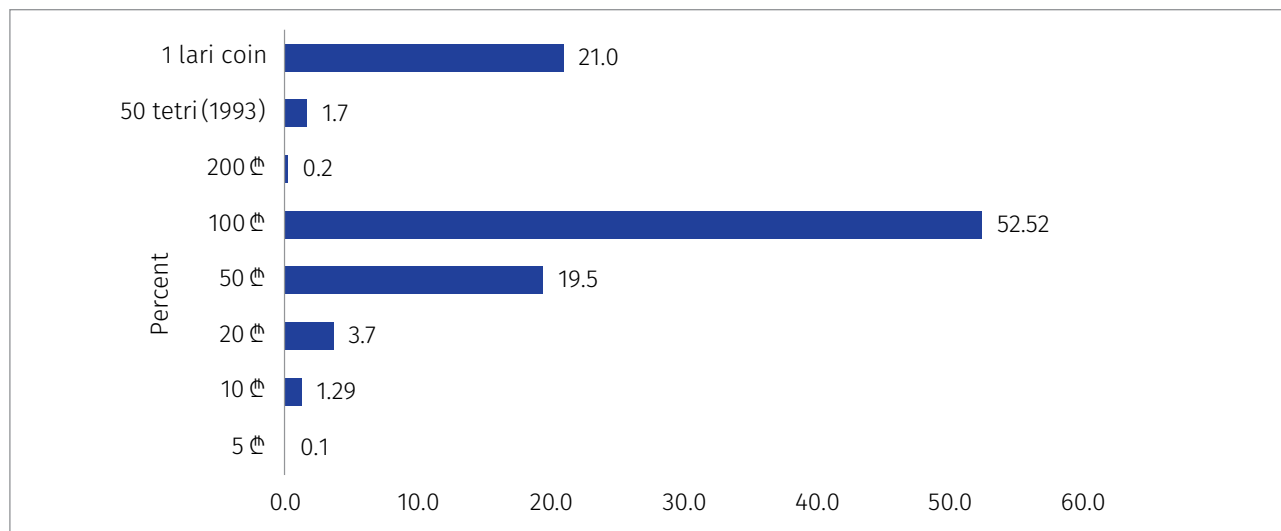
Over the past year, the examination of currency continued. Specifically, 6,350 pieces of suspicious money sent from cash center cash desks, commercial banks, currency exchange offices, microfinance organizations, law enforcement agencies, and brought in by individuals were examined. The results are shown in the table below.

Table N 13.1 results of expert examination of suspicious cash in 2023

	<b>suspicious</b>	<b>counterfeit</b>	<b>Genuine</b>	<b>unfit</b>
GEL banknotes	3430	1258	1263	909
GEL coins	410	370	40	-
USD	2171	1781	390	-
EUR	289	113	176	-
Other foreign currency	50	40	10	-
<b>Total</b>	<b>6350</b>	<b>3562</b>	<b>1879</b>	<b>909</b>

Source: NBG

Diagram N 13.6 Counterfeit GEL banknotes and coins found in 2023 (percentage)

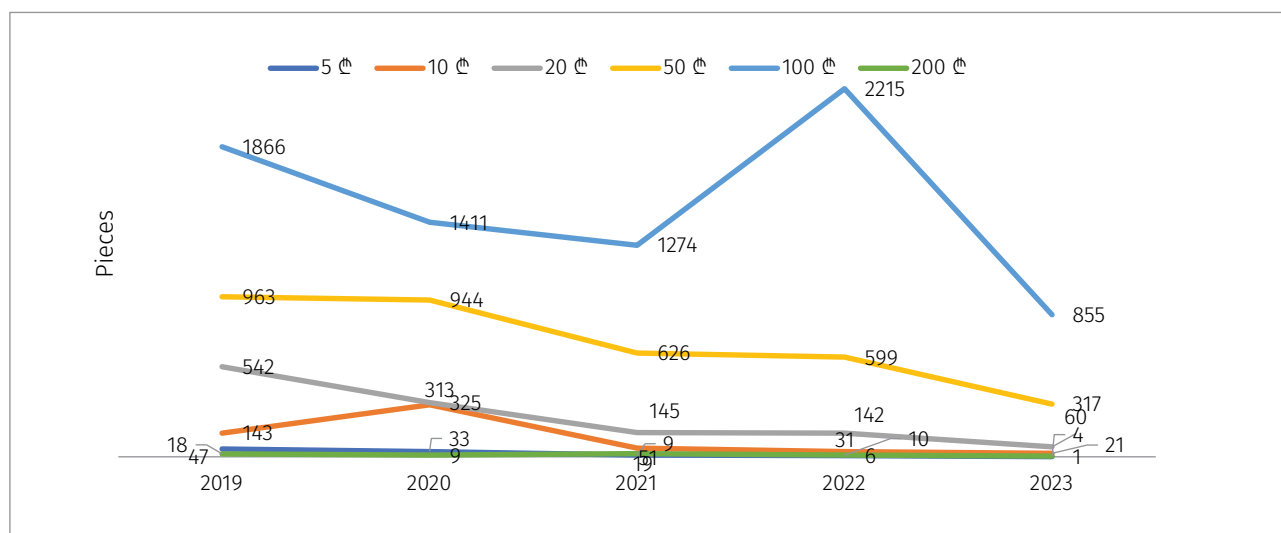


Source: NBG

The number of counterfeit GEL banknotes detected in 2023 decreased by 58.1 percent compared to the previous period (2022), and the number of counterfeit EUR banknotes decreased by 27.6 percent. Other counterfeit foreign currency went down by 62.6

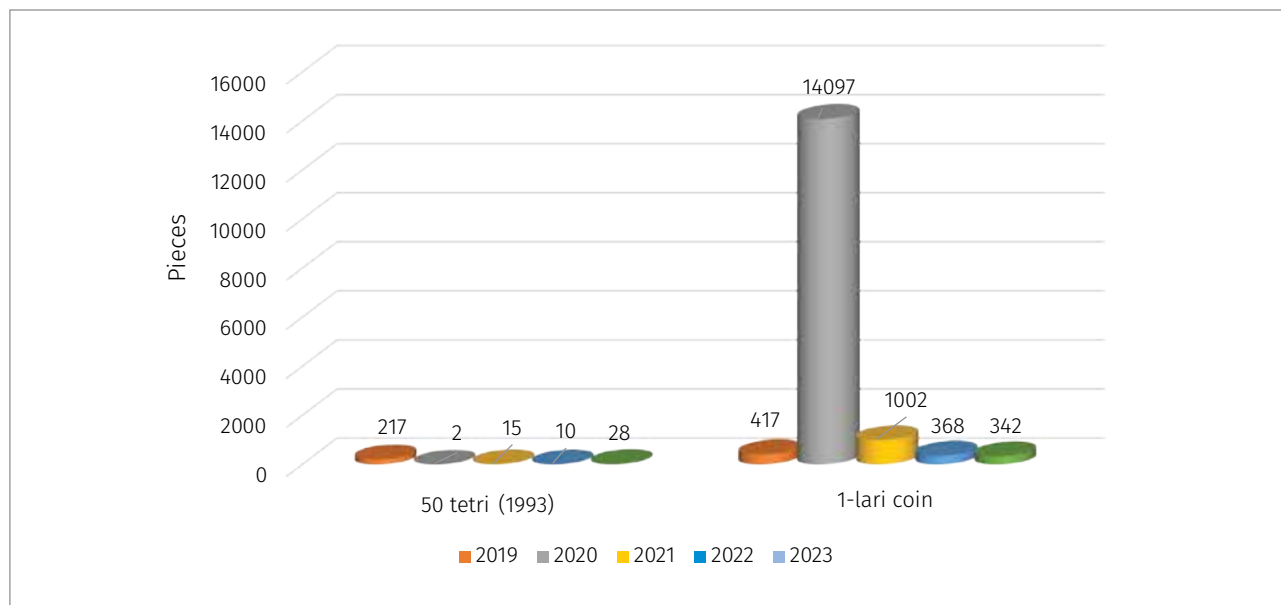
percent, counterfeit dollar notes increased by 9.9%. The number of counterfeit GEL coins has decreased by 2.1% compared to 2022. The number of counterfeit GEL banknotes and coins identified in the period 2019-2023 is shown in Diagram No.13.7 and No.13.8.

Diagram N 13.7 Number of Counterfeit GEL Coins Found in 2019-2023



Source: NBG

Diagram N 13.8 Counterfeit GEL coins found in 2019-2023



Source: NBG

Training was given to 210 interested persons in order to teach security mechanisms of cash, to determine the suitability of GEL banknotes and coins, and to raise the qualification of working with cash. Also, the illustrative materials of the security features of US dollar and euro banknotes necessary for teaching were prepared.

During the reporting period, both collection and numismatic valuables were sold.

In particular, during 2023, 10.8 million GEL worth (37.2 thousand units) of collectible, numismatic and other sales products were sold, including:

- 3.2 million GEL products were purchased with cash;
- 4.4 million GEL products through plastic cards;

- 3.2 thousand GEL products through the internet store;
- 12.9 thousand GEL products with advance payment;
- 8.1 thousand GEL products with after payment.

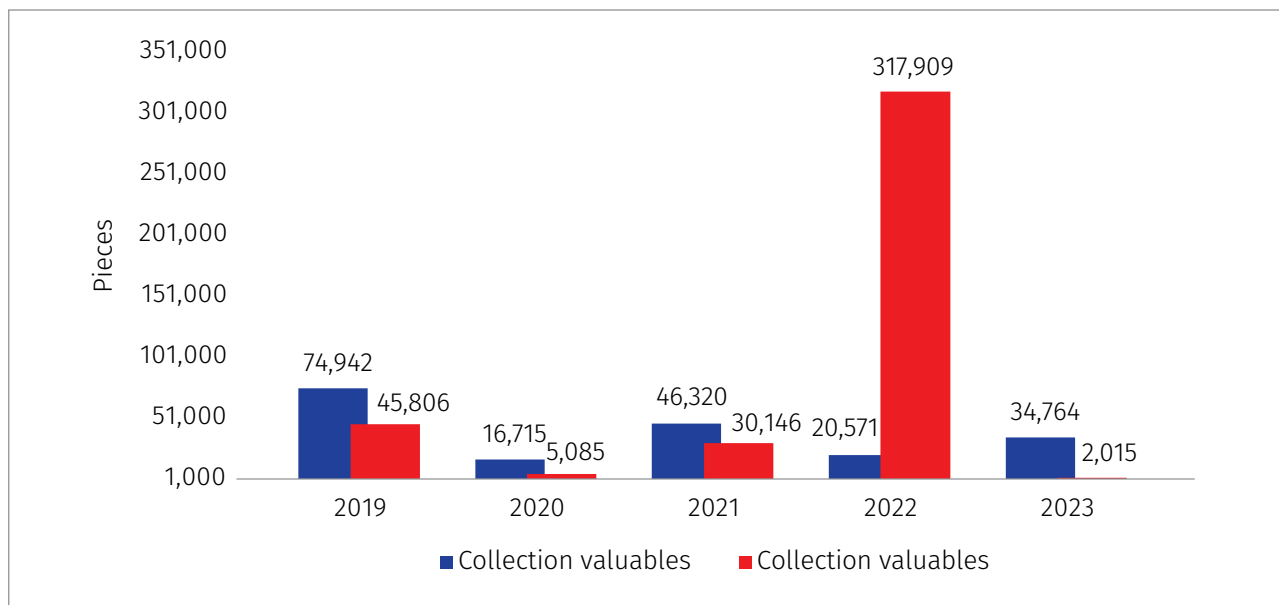
Compared to the previous year, 2022, the income from the sale of collectible coins has increased by 3.8 times, while the income from the sale of numismatic values has decreased by 37.3 times.

DIAGRAM? shows the dynamics of the sold collection value in 2019-2023.

Error! Reference source not found.9.

During the reporting period, 350 pieces of gold bars were sold, including 349 pieces of 20 gram bars and 1 piece of a one kilo bar.

Diagram N 13.9 Valuables sold in 2019-2023 (pieces)



Source: NBG

The NBG Money Museum offered educational courses to the public to familiarize them with the history of Georgian money and the development of the National Bank of Georgia as the central bank and its main activities. During the reporting period, the museum welcomed 4098 visitors, comprising 3963 locals and 135 foreigners.

In 2023, the Money Museum conducted 110 educational tours, which included an overview of Georgian numismatics and direct viewing of exhibits. These tours were attended by 1723 students and 132 teachers.

As part of the events celebrating the International Day of Museums and the Week of the Restoration of Georgia's Independence in May 2023, the Money Museum hosted an exhibition titled *The History of Georgian Money Production (1919-1921)*. Furthermore, on November 8, 2023, a temporary exhibition was held in honor of Banker's Day. The public had the opportunity to get to know the Treasury bills and cash from the period 1919-1921, as well as Georgian banking and financial stocks and documents.

### Improvement of the legislative framework:

In the reporting period, notable progress was made in improving and refining the legislative framework. The National Bank of Georgia, in its efforts to enhance the valuable sales process and ensure its transparency, approved a new *Regulation on Sales of GEL Banknotes/Coins, Gold Bars and Numismatic Valuables*. This regulation was enacted through Resolution No.10 of the Board of the National Bank of Georgia, dated November 30, 2023.

The new regulation includes several changes and improvements compared to the current one. Notably, the method of calculating the sales price of gold bars has been revised. Considering that gold bars are also an investment product, it was deemed appropriate to determine their sale price in a manner similar to the investment coins of the National Bank of Georgia. The price is now fixed once a day, based on the price of 1 ounce of gold in US dollars on the website of the London Precious Metals Market Association at 15:00 London time the previous afternoon. The officially effective exchange rate of the US dollar against the GEL, as determined by the National Bank of Georgia, is then applied.

### Collector Coins

The National Bank of Georgia, in order to promote the national currency and the country, continued to work on the issue of money tokens for collection purposes during the reporting period.

During the reporting period, the following collector coins were issued:

#### Vakhtang Gorgasali (from the series "Kings of Georgia")

During the reporting period, the collection and sale of the full amount of collectible silver coins on the theme of King Vakhtang Gorgasali (from the series "Kings of Georgia") was completed.

#### Giorgi the Brilliant (from the series "Kings of Georgia")

In 2023, the production of 1200 pieces of gold and 6500 pieces of silver coins for collection purposes on the theme of King George the Brilliant (from the series "Kings of Georgia") was completed at the Lithuanian Mint. In the reporting period, their full amount was produced, released and sold.



Designed by: Shmagi Burduli

The main composition of the obverse of the coin features the image of King George the Brilliant. He is holding a scale in one hand, symbolizing the legal reform carried out by him (this detail is gilded on the silver coin). In his other hand, he holds a scroll inscribed with the text "Establishing the monument." The coin also bears the inscription "George the Brilliant" and the years of his reign, "1299 - 1346."

The main composition of the reverse of the coin showcases the image of the crown of George the Brilliant. Its design incorporates details of the royal crown of the Bagratians and miniatures from the Georgian manuscript of the 15th-century psalm. The coin features the inscriptions: "5 GEL", "2023", "Georgia" and among these details, the ornament on the king's robes from the obverse is depicted.

#### Bagrat III and Pharnavaz I (from the series "Kings of Georgia")

In 2023, the production of 4,500 pieces of silver and 700 pieces of gold coins for collection purposes on the themes of King Bagrat the Third and Pharnavaz the First was completed at the Polish Mint. The full amount of these coins was supplied, released, and sold.

#### Bagrat III Coin:



Designed by: Mariam Chachanidze and Shorena Chachanidze

The main composition of the obverse of the coin is the figure of King Bagrat III with a model of the church in his hands, the image of which is cherished in the temple of Bedi. In the left part, there is a depiction of Bedia chalice, which King Bagrat III and his mother, Queen Gurandukht, donated to Bedia temple built by them (the detail is gilded on the silver coin). Georgian fabric samples of the 11th century are used on the king's clothes. It also features precious stones with studs. The obverse also features the inscription "Bagrat III" and the years of his reign - "975 - 1014".

The main composition of the reverse of the coin is the image of the crown of Bagrat III from the fresco of Bedia temple. The year "2023" is depicted on the reverse, and the circular inscriptions: "5 Lari", „საქართველო“, "GEORGIA", and the ornaments of Bedia Cathedral are depicted in between.

### Pharnavaz I coin:



*Designed by: Mariam Rusishvili (obverse), Giorgi (Genadi) Gegelia (reverse).*

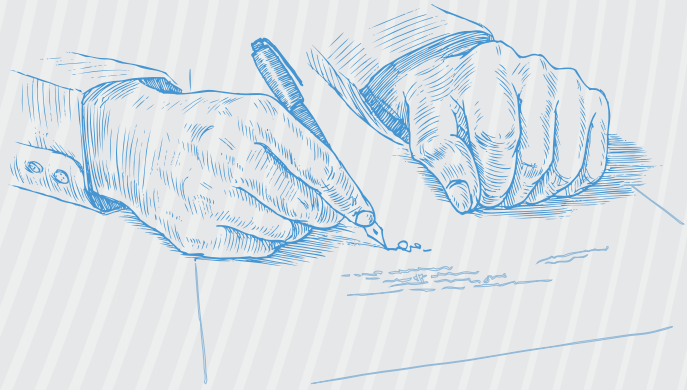
The main composition of the obverse of the coin is the image of King Pharnavaz the First with a scroll (this detail is gilded on the silver coin) in his hand and a capital-letter inscription denoting the king's name, from the bas-relief created by the sculptor Jemal Tushurashvili. The obverse also features the inscription "Pharnavaz I", the era of his reign - " IV-III centuries B.C. " and an excerpt from "The Life of Kartli" about Pharnavaz I: "He created the Georgian writing system", and the fragments of Georgian manuscript ornament are depicted among these.

The main composition of the reverse of the coin is the crown designed with the image of the alphabet of Pharnavaz the First. The denomination "5 GEL" is printed on the reverse, and the circular inscriptions: „საქართველო“, "GEORGIA", "2023".

### Celebrating 30 Anniversary of GEL

During the reporting period, preparations for the release of collectible coins and banknotes for the 30th anniversary of the Lari began in 2025. These included:

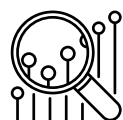
- Preparatory work commenced for the release of gold, silver and copper-nickel coins of 5 GEL denomination. For this purpose, an open competition was announced, sketches were selected, and partner selection procedures were carried out for the production of coins. Currently, selecting and approving a partner enterprise is underway.
- Preparatory works commenced for the release of a 50 GEL banknote for collection. An open competition was announced for the selection of design sketches.



# INTERNAL AUDIT AND CENTRALIZED RISK MANAGEMENT

14

## 14.1. INTERNAL AUDIT



During the reporting period, the Internal Audit Service conducted its activities in line with the 2023 assurance services plan, developed based on the risk-based audit planning methodology. Additionally, a detailed annual audit plan for the information security management system was prepared, and the scope of consulting services was defined. A long-term, indicative three-year plan for the Internal Audit Service was also developed. Adopting a modern risk-based internal audit approach, the updated assessment of the organization's risk maturity allowed for the following internal audit strategy: "To provide assurance on the effectiveness of the risk management process and response controls, advise on risk management improvements, and use operational management's risk assessments in audit planning." Consequently, the Internal Audit Service's assurance plan primarily drew from the organization's risk register. When prioritizing audit items, factors such as the risk rating of the item, the timing of the last audit, the results of prior audits, and the audit cycle were all considered.

Following a dynamic planning approach, the annual work plan was reviewed at six-month intervals during the reporting period. In addition, periodic reviews, accounting for structural changes within the organization, led to updates in the list of audit items, with relevant adjustments made to the audit universe. As a result, 27 audits and reviews were conducted as part of the assurance services during the reporting period. Under its advisory mandate, the Internal Audit Service also provided consultancy, following established practices, to the management of various structural units of the NBG, focusing on specific issues and procedural document drafts. Moreover, between September and December, the Internal Audit Service assessed compliance with the SWIFT Customer Security Controls Framework v2023, reviewing both mandatory and recommended controls within the SWIFT Customer Security Program.

Another key focus of the Internal Audit Service during the reporting period was monitoring the implementation of audit recommendations. Follow-up audits were conducted three times to verify the status of recommendations across different structural divisions of the NBG. This process was facilitated through the recommendations module of the audit and risk management software.

In 2023, a control audit was conducted to assess the NBG information security management system's compliance with the ISO 27001 standard, with the Internal Audit Service actively participating in the process.

As part of established practices, the Internal Audit Service maintained proper communication with representatives of the external audit firm during the audit of the National Bank of Georgia's financial statements. Furthermore, during the reporting period, the Internal Audit Service, upon request, provided updates on the implementation status of recommendations outlined in the Safeguards Assessment Mission (2022) report by the International Monetary Fund.

In October 2023, under the technical cooperation between the internal audit services of the National Bank of Georgia and the Central Bank of the Netherlands, an international seminar titled "Internal Audit in the Context of Governance" was organized by the NBG. The event aimed to foster discussions among experts and professionals from various countries on current internal audit topics, promote knowledge sharing, and strengthen communication among peers. Key speakers included experts from the Central Bank of the Netherlands. The seminar featured sessions on critical topics such as governance and its role, risk management and organizational culture, IT governance, auditing governance processes, and environmental, social, and governance (ESG) issues.

Participants included internal auditors from 12 central banks belonging to the Belgium-Netherlands constituency of the International Monetary Fund and the World Bank, as well as several Eastern

European and Central Asian countries. In support of the development of the internal audit profession in Georgia, representatives from the internal audit services of Georgian commercial banks and ministries were also invited. Employees of the NBG's Internal Audit Service played an active role in organizing the event and engaging in the seminar discussions.

Additionally, the Internal Audit Service participated in several collaborative meetings with other central banks during the reporting period. This included a study visit from the Central Bank of Uzbekistan, where NBG auditors shared their internal audit practices and experience. They also held a working meeting with representatives from the Central Bank of Armenia's Internal Audit Service, focusing on the implementation and practical use of the three-lines model in internal audit. Furthermore, during a visit from the Central Bank of the Netherlands, the Internal Audit Service presented its approach to conducting information technology audits to the Dutch colleagues.

In 2023, the Internal Audit Service joined the Central Bank Data Analytics Working Group (CBDAWG), which includes internal auditors from the central banks of Canada, Switzerland, the Netherlands, Morocco, Germany, and France. During the Group's October working meeting, participants discussed current challenges and achievements in data analysis, as well as the potential for introducing artificial intelligence (AI) and machine learning (ML) into central banking operations.

Alongside its main activities, the Internal Audit Service continued working towards its strategic goals during the reporting period. This included developing procedural documents for internal use, as well as focusing on the professional development and qualification of its employees.

Drawing on its accumulated experience and analyzing practices used by other central banks, the Internal Audit Service implemented a structural change in 2023. This change was guided by the strategic goals of the National Bank of Georgia and the modern challenges facing the internal audit profession. The restructuring

aimed to strengthen the information technology audit function, enhance financial and operational audit capabilities, and concentrate resources needed to carry out special, high-priority tasks assigned by the Governor of the National Bank of Georgia.

## 14.2.

### NON-FINANCIAL RISK MANAGEMENT



The National Bank of Georgia (NBG) has implemented a centralized risk management framework that provides a unified and consistent approach to identifying, analyzing, evaluating, defining treatments, monitoring, and reporting on non-financial risks, including operational and reputational risks. The framework is based on the requirements of both the Committee of Sponsoring Organizations of the Treadway Commission's Enterprise Risk Management (COSO ERM) and the International Organization for Standardization's ISO 31000 standards.

To ensure the efficiency of the risk management process, NBG uses a three-line model of risk management. This model includes the distribution of functions and responsibilities between the different branches of the Bank and their interdependence. The first line is the structural units (risk owners), the second line is the Centralized Risk Management Department, and the third line is the Internal Audit Office.

In accordance with the Risk Management Framework, in 2023, the Centralized Risk Management Department continued to identify the risks associated with the Bank's processes, define likelihood and impact of risks, control mechanisms, taking into account changes in external and internal events, and constantly update the Bank's risk register. For conducting the risk assessment process, the Bank uses the Risk and Control Self-Assessment (RCSA) method in relation to each of the Bank's function.

In accordance with NBG's model risk management framework, a model register has been created. This register describes the parameters associated with each model, their assessment, and the level of risk.

The process of documenting models in a standardized format, identifying non-financial risks and reflecting these risks in the register continued in 2023.

Another operational risk management tool, the incident management system, was used during the reporting period. The purpose of the system is to identify, record, analyze, identify weaknesses, and find ways to improve incidents related to business processes in order to reduce their recurrence.

In order to properly manage the processes of NBG, formalize these processes, and maintain corporate memory, NBG develops internal procedures. This year, the process of updating existing internal procedures and developing new procedures has been actively pursued. This, in turn, is an effective mechanism for creating and maintaining a supportive and adequate internal control environment for a centralized risk management framework.

The centralized risk management framework includes the determination of an acceptable level of non-financial risks (risk appetite). The acceptable level of risk is determined annually by the Board of NBG. Overall, NBG has a conservative approach to non-financial risks and has established an acceptable level in a low-risk area. In order to comply with and maintain an acceptable level, NBG allocates adequate resources and ensures of the continuous improvement of the Bank's internal control environment.

To strengthen the risk culture of the National Bank of Georgia (NBG), trainings on risk and incident management, relevant rules, procedures and the usage of Bank's system were held for various stakeholder groups of employees in 2023.

## 14.3. BUSINESS CONTINUITY MANAGEMENT



As an organization representing the country's critical infrastructure, the NBG attaches particular importance to the continuity of its services. The Bank constantly plans, implements, and monitors various types of activities that contribute to the continuous delivery of its critical services and increase the Bank's resilience in general. In 2023, work continued to test the readiness of human, technological, and logistical resources and to carry out relevant tests and practical exercises.

The Business Impact Analysis (BIA) process continued through the reporting period. BIA is the process of determining the resources required for the Bank's critical services processes. It makes it possible to identify all the technical, human, and logistical resources required for the provision of critical services, to identify the third parties involved in the delivery of critical services, to assess the potential risks that could lead to the interruption or disruption of the provision of services, as well as to determine the minimum time that the business can tolerate for the interruption of the service and the time frame that is mandatory for the technical recovery of this service.

In 2023, trainings were held to raise employee awareness and improve crisis management coordination.



**PUBLIC RELATIONS AND  
INTERNATIONAL COOPERATION**

**15**

## PUBLIC RELATIONS

Effective communication with the public is an important strategic tool for the National Bank of Georgia. The main purpose of the Communication Policy is to ensure transparency, clarity, and consistency in the communication of the National Bank of Georgia. This policy determines the reliability of the communication of the National Bank of Georgia and the proper preparation of the communication strategy.

In 2023, communication activities became even more diverse. The National Bank of Georgia implemented a structural change to improve its communication framework, where the Governor's Office was separated from the Department of Public Relations and International Cooperation and formed into two structural units: The Departments of Strategic Communications and International Cooperation.

During the planning of communication activities in 2023, a special emphasis was placed on making the processes taking place in the economy, the expected results, the tasks of the National Bank of Georgia, and its policies available and understandable to the public. Based on this, in 2023, the NBG team held numerous meetings with representatives of different sectors to further explain the decisions and steps that were implemented within the mandate. In addition, monetary policy communication activities became even more diverse, and the public had the opportunity to inform about the decisions and events of the National Bank of Georgia on a continuous basis using the NBG's digital channels.

To ensure maximum transparency, the National Bank of Georgia promptly disseminated press releases, statistical data, held periodic meetings with representatives of print and electronic media, and prepared short video clips where the Governor of the National Bank of Georgia focused on important aspects of the published report. A video recording of the presentation of the NBG's monetary policy report and brief, informative videos on financial stability and

monetary policy reports were regularly published on the official website and social network of the NBG.

Transparency is one of the priorities of the NBG, and for this purpose, the NBG prepares periodicals and thematic publications. Monthly published publications include Monthly Review, Macroeconomic Review, and Monthly Balances, as well as analytical reports such as Financial Sector Indicators and Current Macroeconomic Indicators. Each quarter, the NBG publishes a Monetary Policy Report. Statistical data and press releases of the Monetary Policy Committee were promptly published, and the Annual Report (2022) was issued. Electronic versions of the publications are available on the Bank's official website - <https://nbg.gov.ge/publications>.

The National Bank of Georgia's website is visited daily by a number of users, including representatives of the financial sector, academic circles, media, industry experts, analysts, numismatists, students, and others. Information is regularly communicated not only within the country but also outside the country to international partners, investors, and representatives of international financial institutions. By 2023, the number of visitors to the NBG's official website had doubled to 1.2 million (1.2m), an increase of 94.5% compared to the same period last year. The growing visitor statistics serve as the best illustration of increased customer interest.

In early 2023, a summary report on the 7-year tenure of Governor Koba Gvenetadze, Chairman of the Board of the National Bank of Georgia, was prepared for the public. The report focused on the reforms, activities, and challenges implemented over 7 years and how adequate the NBG's response was to the challenges posed.

Protecting the rights and interests of users of the financial sector is one of the main goals of the National Bank of Georgia. Throughout the year, the NBG provided information and warned consumers about possible financial scams spread on the Internet

through TV media and digital media channels. In order to promote the establishment of an environment more tailored to consumers and to introduce a high standard of protection for their rights, the NBG prohibited the advertising of pension-secured loans without the individual consent of pensioners.

In 2023, within the framework of the International Consumer Rights Week, the Vice-Governors of the National Bank of Georgia talked more about the consistent steps that the NBG has taken in recent years towards the protection of consumer rights of the financial sector. The consumer rights day has been celebrated in countries around the world since 1983, and its purpose is to raise awareness of their rights among consumers in different fields. Within the framework of the week, representatives of the Consumer Rights Protection Department of the National Bank of Georgia held workshops in the regions to raise awareness about their rights in small and medium-sized entrepreneurs; a video contest was announced, in which any interested person could participate, and the goal of the competition was to increase consumer rights awareness in the society.

The National Bank of Georgia continues to actively promote the development of financial technologies. In 2023, within the framework of the world's largest financial and technological industry - Singapore Fintech Festival, Natia Turnava, Acting Governor of the National Bank of Georgia, participated in a meeting of leading women and introduced the achievements of the financial technology industry of Georgia to the audience. She noted in her speech that "Georgia has all the prerequisites to become a regional hub of fintech in the middle corridor." The National Bank of Georgia continuously conducts informational and educational meetings with the involvement of international partners and experts in order to raise awareness in financial technologies, which is part of the process of Fintech Foundation Program Flex - the educational platform for financial technologies.

In order to effectively fulfill the supervisory mandate and strategic priorities during 2023, the National Bank of Georgia cooperated with supervised entities, Banking Association, external auditors, public institutions, media outlets, supervisors of other countries, and international organizations.

Enhancing public financial education is one of the priorities of the NBG. In 2023, at the initiative of the National Bank of Georgia, a new financial education strategy was developed, which will be a key reference document for any party interested in the dissemination of financial education. The strategy will prioritize directions and objectives and facilitate cooperation between stakeholders in a more practical format and increase access to financial education for all target groups. The National Bank of Georgia will participate in the new 5-year financial education project of the International Network on Financial Education (OECD/INFE). The new technical support project unites Georgia and 9 countries of South-Eastern Europe (Bulgaria, Romania, Moldova, Ukraine, Montenegro, North Macedonia, Croatia, Armenia, Bosnia, and Herzegovina) and aims to promote financial literacy in the region.

Within the framework of the project Financial and Economic Education for a Better Future, the employees of the National Bank of Georgia held public lectures at Tbilisi universities and discussed topical economic topics with students. In terms of financial literacy, the central bank of the country, in partnership with stakeholders, has been implementing a number of projects and events in recent years, such as Global Money Week, Saving Day activities, etc. In addition, in 2023, through the initiative of the NBG, Georgia's financial sector joined the International Education Exhibition.

In 2023, the National Bank of Georgia continued to prioritize effective communication and public education. Videos of employees discussing topical issues related to inflation/monetary policy, financial

stability, consumer rights protection, sustainable finance, and cybersecurity were published on social media.

To honor the contributions of outstanding employees in the banking sector, the National Bank of Georgia has awarded employees with more than 35 years of experience on Banker's Professional Day, held every November 8th at the National Library of the Parliament of Georgia. For the first time this year, employees of commercial banks were also awarded.

In response to increased demand for gold amidst increased inflation and geopolitical risks, the NBG started issuing and selling gold certificates and bars. To provide the public with comprehensive information about gold as a means of accumulation and diversification, television broadcasts were aired, and news articles, videos, blogs, posts, and quizzes were published on social media channels.

Throughout the year, the profiles of NBG employees were published on social media, highlighting their education, professional experience, and successful projects. 2023 was a historic year for our country. The dream of generations came true as the country received the status of a candidate EU member state. In this regard, the NBG was involved in a general communication campaign, which involved the lighting of various buildings in the colors of the EU flag throughout the country. Lighting the building of the NBG Cash Center in the colors of the EU flag received universal acclaim. The European Commission shared the photo of the illuminated building of the Cash Center on the social pages, and the photo was seen and liked by millions of people around the world. In order to mark the dates of historical and state significance, informative and interesting posts were regularly published - the history of Georgian money, Nobel Prize laureates in economics, and others.

In late 2023, following a change in the sanctions regime rule, three vice governors resigned, creating a

significant crisis for the National Bank of Georgia. To overcome the crisis, the NBG communicated openly, transparently, and directly with financial circles and the citizens. The communication strategy included the publication of detailed statements, press conferences, television programs, and the use of online platforms and social media. Meetings were also actively held with relevant audiences. The proactive and large-scale open communication approach proved effective, as the Bank was able to neutralize the most critical phase of the crisis within two weeks, and a survey by the International Republican Institute (IRI) showed that 39% of the general public positively assessed the activities of the National Bank of Georgia.

## INTERNATIONAL COOPERATION

International relations is one of the priorities of the National Bank of Georgia. During the year, representatives of the National Bank of Georgia participated in various high-level international conferences and forums. Koba Gvenetadze participated in the annual forum of Euromoney Central and Eastern Europe, and Archil Mestvirishvili, the Acting Governor of the National Bank of Georgia, participated in the annual spring high-level meetings of the International Monetary Fund and the World Bank in Washington. Papuna Lezhava, Vice Governor of the National Bank of Georgia, participated in the annual banking forum organized by The Financial and ProCredit Bank of Georgia, supported by the National Bank of Georgia and Bankers' Association. As part of the Forum on the Future of Banking, participants discussed issues related to digital technologies, cybersecurity enhancement, and consumer protection of the financial sector.

NBG became a member of the BSCEE group in 2013 and has been actively involved in the work process ever since. The BSCEE Group unites 25 organizations from 24 Eastern and Central European countries and its aim is to promote close cooperation between the banking supervisory bodies of the countries in the Group.

In 2023, the National Bank of Georgia was invited to the 35th BSCEE Group Conference in Sarajevo, Bosnia-Herzegovina. The employees of the NBG participated in a panel discussion on Challenges and Sustainability of Banks' Business Models, Assessing their Impact on the Banking System.

Natia Turnava, Acting Governor of the National Bank of Georgia, and Vice Governor Papuna Lezhava, participated in the conference Geopolitical Landscape Change - Economic Implications in Central, Eastern and Southeastern Europe organized by the European Central Bank in Frankfurt. The conference aimed to discuss the economic and financial issues in the region. Representatives of EU member states and those of central banks of countries with potential candidate status, were attending the conference for the first time this year. During the conference, Natia Turnava discussed the challenges facing the world. She focused on consistent steps of the National Bank of Georgia to ensure the stability of the financial system and sustainability of the country's financial sector. During the visit, Natia Turnava and Papuna Lezhava held workshops with representatives of the European Central Bank. Acting Governor of the NBG emphasized the importance of Georgia's accession to the Single Payment Area (SEPA).

Throughout the year the members of the management of the National Bank of Georgia held meetings with high-ranking representatives of partner countries. Acting Governor of the National Bank of Georgia, First Vice Governor, Natia Turnava, Vice-Governors Archil Mestvirishvili, Papuna Lezhava and Nikoloz Gagua met with David O'Sullivan, the EU Sanctions Envoy, James O'Brien, the Head of the Office of Sanctions Coordination in the Biden administration, and Kumar Iyer, the Director General for Economics, Science and Technology at the UK Foreign Office, along with other members of the sanctions delegation. The meeting focused on the implementation of financial sanctions imposed by the United States, the United Kingdom, the European Union and other countries on Russia for its

aggressive hostilities in Ukraine. The representatives of the NBG focused on the consistent steps that are in full compliance with the sanctions. International organizations positively evaluated the activities of the National Bank of Georgia in this direction. According to the U.S. State Department's Georgia Investment Environment Report, the National Bank of Georgia and Georgian financial institutions are acting in full compliance with the sanctions imposed on the Russian Federation by the United States and other countries. Compliance with international financial sanctions is systematically monitored during the on-site inspection of financial institutions.

Natia Turnava, Acting Governor of the NBG, held meetings with diplomatic corps representatives in 2023. She hosted U.S. Ambassador Kelly Degnan and USAID mission chief John Pennell at the NBG headquarters. The parties discussed the economic trends, macroeconomic policies for Georgia and also focused on the projects implemented within the framework of cooperation with USAID.

Supervisory priorities for credit risks and non-performing loans and their impact on Eastern Europe and the Caucasus region - a seminar was held at the Head Office of the NBG. The aim of the Joint Workshop of the NBG and the European Bank for Reconstruction and Development (EBRD) was to create a unified platform for sharing knowledge and experience. The event was opened by the Acting Governor of the National Bank of Georgia, Natia Turnava and the first Vice President of the EBRD, Jürgen Rigterink. Representatives of the National Bank of Georgia and Central Banks of Armenia, Ukraine and Moldova attended the seminar. The EBRD's first Vice President and Head of Customer Service Group, Jürgen Rigterink, and the EBRD's Managing Director for Eastern Europe and the Caucasus, Matteo Patrone, were on a working trip to the Caucasus. During the meeting with Natia Turnava, the conversation focused on the economic situation of the region and the current challenges. The Acting Governor introduced the positive trends in the

Georgian capital market to the guests and the steps taken by the NBG in this direction. It was noted that the reforms of the National Bank of Georgia contribute to the development of the capital market.

The measures taken by the National Bank of Georgia were positively evaluated by various international organizations and state agencies of different countries. International rating agency S&P Global Ratings has published a review of the risk assessment of the banking sector. The document summarizes the overall trends in the banking sector of individual countries, strengths and weaknesses, key challenges and macroeconomic risks. According to the report, Georgia's overall risk assessment improved and the country moved from Group 8 to Group 7, which is one of the highest assessments in the region compared to other countries. The banking system is assessed as stable, declining dollarization. S&P analysts expect that despite geopolitical tensions, the prospects for economic growth are favorable and the quality of assets will remain stable. The influential rating agency notes that banks in Georgia, unlike other countries in the region, face fewer risks. As a result of the policy implemented by the National Bank of Georgia, dollarization in loans decreased to 44% and in deposits to 51%, although this figure is still the highest in the region. The report discusses banking regulations, which, in the agency's estimates, contributed to the resilience of banks to stress. In the past years, the National Bank of Georgia has successfully responded to the growing risks arising from the changing macroeconomic environment.

In a new report published on the investment environment of Georgia by the US State Department, the activities of the NBG were positively assessed. The report provides a detailed overview of Georgia's

investment environment, the country's economic situation and monetary and fiscal policy. The Investment Environment Report highlights that the National Bank of Georgia and Georgian financial institutions fully act in compliance with the financial sanctions imposed by the United States, the European Union and the United Kingdom against the Russian Federation. The document assesses the measures taken by the National Bank of Georgia, which is confirmed by a number of international organizations and rating companies: "The International Monetary Fund, credit rating agencies and other international organizations positively assess the macroeconomic framework of the National Bank of Georgia and the inflation targeting regime. In June 2021, international publication Central Banking awarded NBG with the Transparency Award. This recognition highlighted the improvement of the communication on monetary policy, financial stability, consumer protection and financial education. In addition, the supervisory policy of the National Bank of Georgia is discussed in the report, as a result of which the financial sector and the banking system successfully cope with global challenges.

NBG received another award from the leading international publication Central Banking - the "CBDC Initiative". The National Bank of Georgia constantly cares about the development of the financial market, promotes the creation of basic infrastructure for fintech activities, and is focused on finding the optimal balance between innovation and risk. NBG has been actively working on CBDC since 2020. A number of studies have been conducted on the concept of the central bank's digital currency and decentralized finance. As a result of sharing international experience, the National Bank of Georgia decided to initiate a pilot digital currency project.



# HUMAN RESOURCE MANAGEMENT AND DEVELOPMENT

16

## STAFF STATISTICS

At the end of 2023, the National Bank of Georgia employed 601 individuals, of which 443 were civil servants. 54.4 percent of the total number of employees were women, and 45.6 percent were men. The average age of employees was 40 years.

In order to increase organizational efficiency and effectively fulfill the Bank's strategic goals, several structural changes were made at the National Bank of Georgia in 2023, including:

- The addition of a fifth Supervision Division to the Banking Supervision Department
- The splitting of the Small and Medium and Corporate Credit Risk Division of the Specialized Risk Department into two divisions: The Small and Medium Credit Risk Division and the Corporate Credit Risk Division
- The addition of a Competition Division to the Legal Department
- The addition of a Dispute Resolution Commission Support Unit (Office) to the Department of Payment Systems
- The establishment, on the basis of the above-mentioned department, of the Department for Supervision of Payment Service Providers and Registration of Virtual Asset Service Providers, consisting of Supervision and Registration and Regulation and Support Divisions;
- The abolition of one division in the Securities Market Supervision Department and the addition of two divisions: The Division of Securities Market Regulatory Policy and Supervisory Methodology and the Division of Securities Market Development and Research
- The addition of a Special Audit Unit to the Internal Audit Office
- The separation of the Governor's Office from the Department of Public Relations and International Cooperation and the creation of two new departments: the Department of International Relations,

which includes the Department of International Cooperation and the Protocol Unit, and the Department of Strategic Communication, which includes the Brand Development, Digital Media, and Media Relations divisions.

- The separation from the Department of Consumer Rights Protection and Financial Education of the Division of Financial Education and the addition of the Department of Financial Education and Strategic Development to the structure of the National Bank of Georgia, consisting of: Division of Financial Education and the Division of Strategic Development and Projects
- The addition of 1 Unit to the Consumer Protection Department, which consists of the Consumer Response Unit and the Market Behavior Supervision Unit.

Furthermore, in 2023, an independent commission was established to resolve disputes with the National Bank of Georgia. This commission collegially reviews the complaints of payment service users, as well as disputes between them and payment service providers.

## PROFESSIONAL DEVELOPMENT OF EMPLOYEES

In 2023, the National Bank of Georgia continued to take care of the professional development of employees. To enhance the effectiveness of the employees' professional skills, the employees of the National Bank of Georgia attended 202 trainings at the Bundesbank of Germany, the Central Bank of Italy, the Central Bank of France, the National Bank of Poland, the Central Bank of Switzerland, the National Bank of the Czech Republic, the National Bank of Austria, the Central Bank of Armenia, the Central Bank of Turkey, the Asian Development Bank, as well as the World Bank, the International Monetary Fund and the Central Banks of other countries.

In addition to the above trainings, the National Bank of Georgia systematically implements training and holds

introductory presentation events by employees of different departments, which helps to share knowledge within the organization.

In 2023 71 employees of the National Bank of Georgia passed the certification course “International Financial Reporting Standards and International Accounting Standards” and “IFRS 9 - Financial Instruments”. Employees were also encouraged to improve their English skills. The invited trainer conducted a training at the National Bank of Georgia “Increasing Efficiency by Self-Development” attended by 47 employees.

## PROFESSIONAL DEVELOPMENT OF FINANCIAL SECTOR EMPLOYEES

The National Bank of Georgia continuously promotes the professional development of banking sector employees. To this end, the experts of the Financial Technology Transfer Research Agency of Luxembourg conducted 2 trainings in Tbilisi in 2023, and 2 trainings remotely, in which the employees of both the NBG and commercial banks participated. A total of 75 participants attended the seminars.

## HYBRID WORK AND ENHANCING TEAM SPIRIT

In 2023, the National Bank of Georgia operated in a hybrid working mode, which allowed employees to work remotely for a certain number of days during the month based on their needs and preferences.

One of the main goals of the Human Resource Management and Development Unit was to boost team spirit and improve internal communication. To achieve this, a number of remote and traditional events were planned and implemented, including meetings with

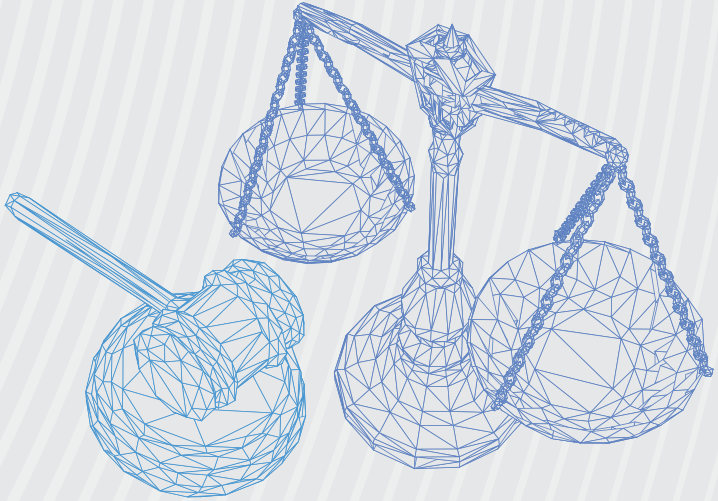
celebrities, rafting competitions, cognitive activities, social responsibility events, and charity events.

The employee evaluation, selection, and orientation-adaptation processes in the NBG are carried out through the SAP Success Factors system. In 2023, 556 employees were evaluated through this system, 96 vacancies were announced and closed (including simplified, open, and closed competitions), and 93 new employees were selected.

## COOPERATION WITH HIGHER EDUCATION INSTITUTIONS

The National Bank of Georgia cooperates with higher education institutions to provide students with the opportunity to learn about the specifics of the bank, internships, and practical skills that will help them become professionals. In 2023, 47 interns were recruited on the basis of the Memorandum on Mutual Cooperation signed with higher educational institutions, 6 of whom are now employees of the NBG. Moreover, the National Bank of Georgia provides an opportunity for Georgian students studying abroad to undertake summer internships and get acquainted with the specifics of the National Bank of Georgia. This initiative aims to spark the interest of Georgian students towards the NBG and encourage them to return to Georgia after completing their studies and apply the knowledge gained in Georgia.

The Human Resource Management and Development Department organized a three-day orientation-adaptation training for new employees and interns. The training aimed to introduce the main elements of the organizational culture, the structure of the bank, basic procedures, and presentations related to the activities of different departments of the National Bank of Georgia.



# DEVELOPMENT OF LEGAL FRAMEWORK

17

## LEGISLATIVE REGULATION OF THE FINANCIAL CONGLOMERATE

In 2023, the Parliament of Georgia adopted the Law of Georgia *On Additional Supervision of Regulated Enterprises Included in the Financial Conglomerate* and related legislative amendments. The purpose of the submitted legislative amendment was to fulfill the obligation provided for by Article 323 of Chapter 7 of the Agreement between Georgia, of the one part, and the European Union and the European Atomic Energy Community and their Member States, of the other part. This obligation requires Georgia to approximate its national legislation to the EU legislative acts referred to in Annex XV-A of the Association Agreement, in particular the Directive 2002/87/EC of the European Parliament and of the Council of 16 December 2002 on the additional supervision of credit institutions, insurance companies, and investment companies in the financial conglomerate.

As a result of the adoption of the legislative package, the legislation of Georgia took into account the definition of a financial conglomerate, defined the criteria and procedure for recognition as a financial conglomerate, and established a framework for additional supervision over it. In addition, the law also indicated that additional supervision will be carried out in parallel with sectoral supervision.

The law defined the explanation of the coordinator, the procedures for his/her election, and gave him/her the authority to adequately and effectively carry out additional supervision of the financial conglomerate. The legislative amendments defined the tasks to be carried out by the coordinator within the framework of additional supervision. These tasks, in addition to other powers provided for by the legislation of Georgia, include collecting and providing relevant information on the usual activity cycle and crisis situations of enterprises in the financial conglomerate to supervisory bodies, reviewing and assessing the financial condition of the financial conglomerate, as well as assessing its compliance, structure, organizational arrangement, and internal control system with the requirements specified by law.

The legislative package defined the scope of additional supervision of regulated enterprises and the list of enterprises included in the financial conglomerate, which are subject to additional supervision independently of the Regulations of sectoral supervision. It was also established that regulated enterprises within the financial conglomerate should have adequate risk management processes and an internal control mechanism at the financial conglomerate level, including reasonable and effective administrative and reporting procedures. Legislative amendments were also reflected in the Law of Georgia on Investment Funds, and the supervisory authority was given the power to carry out additional supervision at the level of the relevant entity within the financial conglomerate in accordance with the Organic Law of Georgia on the National Bank of Georgia and the Law of Georgia on Additional Supervision of Regulated Enterprises within the Financial Conglomerate.

By the amendment to the Law of Georgia on the Securities Market, the National Bank of Georgia became entitled to apply the sanctions defined by the same law to the regulated participant of the securities market and/or a member of its governing body if the regulated participant of the securities market and/or a member of its governing body violated the requirements of the Law of Georgia on Additional Supervision of Regulated Enterprises contained in the Financial Conglomerate.

## LEGISLATIVE CHANGES RELATED TO THE RESOLUTION FUND

In 2023, the Parliament of Georgia adopted the Organic Law of Georgia on Amending the Organic Law of Georgia on the National Bank of Georgia and related legislative amendments. The main reason for the implementation of the amendment to the Organic Law of Georgia on the National Bank of Georgia was the recommendations developed in 2022 within the framework of the technical assistance mission of the International Monetary Fund (IMF) for representatives of both the National Bank of Georgia and the LEPL Deposit Insurance Agency and the Ministry of Finance of Georgia.

One of the recommendations was to increase access to financial funds during the crisis of the financial system for the effective implementation of the goals of the resolution. To achieve this, the recommendation was to accumulate cash in advance in the resolution fund, which the banking sector provided through preliminary contributions. This would contribute to the increase of access to financial funds during the crisis of the financial sector. According to the law, it became mandatory for commercial banks to make contributions to the Resolution Fund in order to allow the accumulation of preliminary funds to the Resolution Fund.

It was clearly defined in the Organic Law of Georgia on the National Bank of Georgia, that the authority of the National Bank of Georgia in a special case to issue a last instance loan to a commercial bank whose solvency is doubtful, applies to the commercial bank in the resolution mode as well. The amendments also stipulate that in order to finance the resolution process, the Ministry of Finance of Georgia will issue temporary state funding if it is necessary to ensure the stability of the financial system and if the funds accumulated by the branches of commercial banks and foreign banks (ex-ante) are not/will not be sufficient and cannot be retrieved from a non-state source of funding or such funding is not/will not be sufficient. In addition, contributions are determined on the basis of objective and proportional criteria.

The implementation of preliminary contributions to the Resolution Fund, use of funds deposited in the Resolution Fund, suspension of preliminary contributions in case of ex post contributions by commercial banks, requesting information from the National Bank of Georgia's LEPL Deposit Insurance Agency, administration of the Resolution Fund, and other issues were prescribed by the amendments. In addition, it was clarified that the National Bank of Georgia is authorized to transfer the Resolution Fund to the LEPL Deposit Insurance Agency for administration, since the LEPL Deposit Insurance Agency already has

relevant experience in mobilizing, controlling, and managing such deposits from commercial banks. The amendment to the law established that issues related to the administration of the Resolution Fund and ex ante contributions, including investment, are regulated by the Legal Act of the Governor of the National Bank of Georgia, and issues related to the administration of the Resolution Fund regarding ex post contributions will still be regulated by the Joint Legal Act of the Governor of the National Bank of Georgia and the Minister of Finance of Georgia.

The above-mentioned legislative package includes the draft Law of Georgia "On Amending the Law of Georgia on the Activities of Commercial Banks", which changed the order of claims of creditors of the commercial bank during the liquidation process. This was based on a recommendation from the Financial Sector Assessment Program (FSAP) to simplify the hierarchy of creditors' claims and align it with the regulation related to insured deposits defined by the Law of Georgia on Deposit Insurance System.

The recommendation also stated that the requirements arising from loan financing of a commercial bank under liquidation should have the same priority as the unsecured claims of the National Bank of Georgia. The amendments to the Law of Georgia on the Activities of Commercial Banks clarified that the Pledgee of Financial Pledge has the right to predominantly meet the demand within the scope of the value of the financial pledge and established an updated order of claims of creditors' of a commercial bank.

The amendment to the Law of Georgia on Microbanks' Activities, which was part of the same legislative package, aligned the hierarchy of microbank creditors with the order of claims of creditors' of commercial bank and accordingly, the best international practices. Additionally, amendments were made to the Law of Georgia on Deposit Insurance System and the Law of Georgia on Enforcement Proceedings.

## LEGISLATIVE AMENDMENTS RELATED TO DEMATERIALIZED SECURITIES

In 2023, the Law of Georgia on the Ownership of Dematerialized Securities and related legislative amendments were adopted by the Parliament of Georgia, which established a legal framework for dematerialized securities in the country. The law defined dematerialized securities as "*securities that exist only as a record in a securities account*" and specified the issues of their circulation, the origin and distribution of the right to pledge, and the distribution of financial pledges.

According to the law, a person may hold securities directly or indirectly, and the crediting of dematerialized securities on an account opened for an investor generates the investor's right to equity ownership in proportion to the number of securities credited to that account. The law also clarified that the norms governing common property and shared rights provided for by the Civil Code of Georgia do not apply to this right. Since the securities are not individually identifiable, the investors' rights do not exist in specific securities, but they have co-ownership of a group of identical securities.

The law established that the investor has the right to exercise ownership rights over the dematerialized securities only with respect to the account producer with whom he holds the securities or the central depository, if the investor holds the securities directly with him/her. However, the law determined exceptional cases from this general Regulation. It is further specified that in case of liquidation of the account producer, the claim for the set of identical securities placed in the account producer's name with a central depository or in an omnibus segregated account opened with another account producer, including a foreign account producer, shall be made collectively by the liquidator on behalf of all account holders, and if the aggregate of identical securities credited to the omnibus segregated account is not sufficient to fully refund the dematerialized securities credited to the respective accounts, it shall be distributed among the account holders in proportion to their rights.

The law also defined the obligation of the central depository to take appropriate measures related to reconciliation to ensure that the number of dematerialized securities issued under a single emission in the central depository or the sum of the dematerialized securities on the central depository accounts of the emission portions placed in the central depository is accurate.

In addition to this, the amendments to the Law of Georgia on the Securities Market clarified the issues of issuance and accounting of public and private securities, the terms of licensing and operation of the central depository, the issues of liquidation of the brokerage company and the central depository, and the terms of operation of the registrar of securities.

It was also clarified that the dematerialization of units of authorized or registered investment funds is achieved by recording them (units) in the central depository, as a result of which unit owners will be able to own units only through the central depository, directly (in the case of ownership of units by a participant of the central depository system for his own benefit) or indirectly (in the case of holding units by a participant of the central depository system for the benefit of its clients).

The amendment to the Law of Georgia on Promoting the Prevention of Money Laundering and Terrorism Financing extended the requirements of the legislation on the prevention of money laundering and terrorist financing (AML/CFT) against the accountable person to the asset management company and the central depository.

The amendments made to the Law of Georgia on International Private Law specified that the origin, alteration, transfer, and termination of the right to registered securities provided for by the Law of Georgia on the Securities Market shall be regulated by the law of the country where the relevant securities account is opened, and the law to be applied to dematerialized securities shall be defined in accordance with the Law of Georgia on the Ownership of Dematerialized Securities.

The amendment to the Law of Georgia on Entrepreneurs touched upon the definition of the share and established that the share is a registered or dematerialized security. The law also established cases where it is mandatory to have shares in dematerialized form, unless otherwise provided by special legislation, and changed the Regulations of registry, as the law established different regulation of the form of shares and their ownership in case of dematerialized shares.

## OTHER LEGISLATIVE CHANGES

The Law of Georgia on the Transformation in Securities and its subsequent legislative amendments have established a regulatory framework for securitization in Georgia. Securitization is a financial instrument that enables an initiator to remove basic assets, which are future cash flows, from their balance sheet and mobilize funds. With the introduction of this regulatory framework, it has become possible for issuers to issue securitized financial instruments and for investors to acquire them.

Furthermore, if a securitized financial instrument has obtained an appropriate credit rating, it can be included in the portfolio of the pension agency. This helps to diversify the pension agency's investment activities.

The legislative package in Georgia has defined the legal nature of the special target unit of securitization, as well as legal issues related to the securitization company and the securitization fund, their establishment, management, and powers. The package has also established conditions for mandatory authorization of the special target unit of securitization, the grounds for granting authorization, payment of fees, and denial of authorization. The authorization fee has been set at GEL 5,000. The National Bank of Georgia is obliged to create a registry of special target units of securitization and publicize it through its official website.

The law has additionally regulated issues related to securitized risks. However, resecuritization is prohibited by law, except in circumstances where it

is necessary to prevent liquidation or for liquidation purposes of a commercial bank, brokerage company, or other financial institution. The law has also defined the rights of investors, special requirements for institutional investors, and requirements for offering the securitization tool to unaware investors.

The National Bank of Georgia has been granted the authority to supervise the securitization transaction and the relevant entities. The National Bank of Georgia will authorize the special target units, which are obliged to be authorized according to the regulations of the law.

In 2023, the Law of Georgia on Amending the Law of Georgia on Funded Pension and related legislative amendments were adopted by the Parliament of Georgia. The purpose of the legislative changes was to increase the effectiveness of administration and management of the funded pension scheme. As a result of the amendment, the authority of the National Bank of Georgia was determined to inspect the investment activities of the pension agency/asset management company within the framework of prudential regulation. The National Bank of Georgia was also instructed to reflect in its annual report the compliance of the pension agency and asset management company(s) with the Law of Georgia on Funded Pension and the requirements of the National Bank of Georgia. The National Bank of Georgia has been granted the right to carry out the function of a specialized depository of the funded pension scheme, as well as to authorize asset management companies for the purpose of managing pension assets in cases specified by the Law of Georgia on Funded Pension.

The amendment to the Law of Georgia on Enforcement Proceedings has subjected the individual administrative-legal acts of the Pension Agency on imposition of a penalty as a sanction, as well as the payment of an unfunded pension contribution, to enforcement. However, when applying compulsory enforcement measures, it is prohibited to apply these measures to the pension agency, accumulatively to

the assets of the specialized depository and asset management company of the pension scheme, which are located on the account of the nominal owner and/or which are not his/her property and belong to the assets of his/her client.

## BYLAWS OF THE NATIONAL BANK OF GEORGIA

### Regulation of the Supervisory Framework and Resolution of Commercial Banks

There were important updates in 2023 in the regulation of commercial banks.

According to the Decree № 11/04 of the Governor of the National Bank of Georgia of January 23, 2023, *on the determination of commercial banks of systemic importance and the imposition of a systematic buffer for them*, the methodology for the determination of commercial banks of systemic importance was regulated, scores of systemic importance with corresponding indicators and weights were established and the corresponding rates of the systematic buffer were established. The purpose of the decree was to ensure greater transparency of the updated approaches used by the National Bank of Georgia in determining the systemic significance of commercial banks and the systemic significance of buffer for them, to update and impose systemic significance buffers in accordance with these approaches.

On March 15, 2023, the Financial Stability Committee of the National Bank of Georgia decided to impose a countercyclical buffer on the neutral (base) rate of 1%. On March 15, 2023, the Financial Stability Committee of the National Bank of Georgia decided to set the neutral (base) rate of the countercyclical buffer at 1%. Based on the mentioned decision, Decree No. 57/04 of the Governor of the National Bank of Georgia of March 15, 2023 on the amendment of the Decree No. 173/04 of the Governor of the National Bank of Georgia dated December 18, 2017 *"on establishing the countercyclical buffer rate"* was adopted and the countercyclical capital buffer rate was set at 1%. In addition, commercial banks were required to meet the countercyclical

capital buffer rate of 0.25% by March 15, 2024, 0.5% by March 15, 2025, 0.75% by March 15, 2026, and 1% by March 15, 2027. Based on the decision of the Financial Stability Committee of the National Bank of Georgia on November 29, 2023, the decree was amended by the decree of the Governor of the National Bank of Georgia No. 359/04 of December 8, 2023, according to which, in order to alleviate the impact of globally tightened financial conditions on the local economy, a decision was made to allow the gradual compliance with the 1% rate and setting the deadline for meeting the said requirement until March 2027.

To comply with best international practice, the decree № 68/04 of the Governor of the National Bank of Georgia of March 31, 2023, *"On Approval of the Regulation on Disclosure of Information by Commercial Banks under Pillar 3"* was adopted to amend the Decree № 92/04 of the Governor of the National Bank of Georgia dated June 22, 2017, by which the nonperforming loans were newly interpreted. In particular, nonperforming loans have been defined as level 3 credit risk financial instruments defined in accordance with International Financial Reporting Standard 9 (IFRS 9) and purchased or originated credit impaired (POCI) financial instrument.

The decree № 90/04 of the Governor of the National Bank of Georgia of May 31, 2023 on setting the minimum requirement for allowed liabilities and capital instruments was approved. The Minimum Requirement for Allowed Liabilities and Equity Instruments (MREL) is a percentage obtained from the ratio of allowed liabilities and equity instruments to supervisory equity and total liabilities. This requirement allows commercial banks of systemic importance to maintain the minimum amount of capital instruments and liabilities allowed, which will be required in the possible resolution process, for the use of a write-off of liabilities or a conversion resolution instrument (Bail in).

The objective of setting the minimum requirement for allowed liabilities and capital instruments (MREL)

is to follow the recommendations of the Financial Sector Assessment Program (FSAP) by the Joint Mission of the International Monetary Fund (IMF) and the World Bank (WB).

According to the decree, the National Bank of Georgia has set a minimum requirement for allowed liabilities and capital instruments (MREL) for systemically important commercial banks.

The minimum requirement rate for allowed liabilities and equity instruments (MREL) was determined in accordance with the following amounts and terms:

- a) in the amount of 10% from January 1, 2024;
- b) in the amount of 15% from 31 December 2025;
- c) in the amount of 20% from 31 December 2027.

In addition, considering the interests of systemically important commercial banks, it was determined by the decree that if the minimum requirement of allowed liabilities and capital instruments (MREL) allowed by the National Bank of Georgia for a commercial bank of systemic significance is less than the requirement specified by the same decree, then the failure of the commercial bank of systemic significance will not be considered as a violation of this requirement. In this case, a commercial bank of systemic importance is obliged to meet the minimum requirement specified according to the methodology, but not less than 10%.

An amendment was made to the decree № 241/04 of the Governor of the National Bank of Georgia № 241 of December 29, 2020, *on writing off or approving the commercial bank's obligations for the purpose of recapitalization of the commercial bank in the resolution mode*. The development of the changes was mainly due to the fact that in 2022, within the framework of the technical assistance mission of the International Monetary Fund (IMF) and the joint mission of the World Bank (WB), practical recommendations were developed within the framework of the Financial Sector Assessment Program (FSAP). One of the recommendations was the development of a regulation that would make it mandatory to take into account

the bail-in contractual condition in contracts that are subject to foreign regulatory legislation and apply to them the scope of the bail-in instrument. This facilitates and ensures that the resolution is enforced without significant hindrance. The purpose of the amendment was also to bring banks closer to the Resolution and Recovery Directive (BRRD) and to achieve compliance with European law. Due to this, commercial banks had an obligation to include bail-in contractual conditions according to which parties agree that the National Bank of Georgia is authorized to apply following resolution instruments: write-off or conversion of commercial bank's obligations for recapitalization of a commercial bank in resolution mode according to the legislation of Georgia and the Regulation in contracts containing obligations to which the operation of the resolution instrument provided for by the Regulation applies, and at the same time, this contract is fully or partially subject to the legislation of foreign countries. The amendment specifies in what cases the contractual terms may not be taken into account.

In light of the above, an amendment was made to the Decree № 100/04 of the Governor of the National Bank of Georgia, dated October 28, 2013, on the Approval of on Capital Adequacy Requirements of Commercial Banks to harmonize with requirements of the Regulation 575/2013 of the European Parliament and of the Council, dated June 26, 2013 and the requirements of Directive 2013/36/EU and to enhance the stability of capital in the banking system.

In accordance with the changes, the criteria for the classification of instruments to be included in additional primary (CET tier 1) capital and secondary (tier 2) capital have been revised. Specifically, the Capital Instrument Agreement shall mandatorily include the terms of writing off or conversion of commercial bank liabilities for the purpose of recapitalization, in a manner that is enforceable within the framework of the resolution provided for by the legislation of Georgia with respect to the said instrument.

Furthermore, a relevant amendment was made to the

Decree № 242/01 of the Governor of the National Bank of Georgia, dated December 25, 2009, on the *Approval of the Regulation of Determination and Imposition of Monetary Penalties against Commercial Banks and their Administrators*. The amendments provide that in case of a violation of the requirements stipulated in the relevant article of the *Regulation on Write-off or Conversion of Commercial Bank's Obligations for Recapitalization of a Commercial Bank in Resolution Mode*, approved by the Decree № 241/04 of the Governor of the National Bank of Georgia, dated December 29, 2020, the commercial bank shall be subject to a monetary penalty. The amount of the penalty shall not exceed GEL 100,000 (one hundred thousand) but shall not be less than GEL 10,000 (ten thousand). The amount of the specific monetary penalty shall be determined by taking into account the amount of the principal obligation under the Agreement and the seriousness and/or systematicness of the violation.

The amendment was made in Decree № 26/04 of the Governor of the National Bank of Georgia “*On Approval of the Regulations for the Management of Conflict of Interest*” of March 10, 2015. The purpose of the amendment was to align the regulations with international practices and to address the shortcomings identified in the financial sector and practice. Significant changes were made to the definition of a related party, which covers the requirement of identification of related persons on a list and, in some cases, to include existing related persons on the list for a period of further 12 months. Also, as an exception, in certain cases, the list of related persons does not include international financial institutions and their related persons, unless there are certain exceptional cases. The amendments also outlined general requirements related to collateral, the list of permissible collaterals was set for commercial banks to create a risk position with related parties and the documentation of assessment/substantiation of compliance of said collaterals with the requirements of the regulation. The changes also included an analysis of compliance with the arm's length principle and clarifications on prohibited transactions.

On August 1, 2023, Decree № 194/04 of the Governor of the National Bank of Georgia “*On Amending the Decree № 47/04 of the Governor of the National Bank of Georgia of June 13, 2014 on Approval of the Regulation on Operational Risk Management by Commercial Banks*” was adopted. The aim of the decree was to manage risks of commercial banks and to approximate to the recommendations of the European Banking Authority (EBA) and best international practices, including the Operational Risk Management Principles developed by the Basel Committee. The decree clarified outsourcing and the circumstances in which the process should be critically and/or significantly reviewed. The requirement for the National Bank of Georgia to issue confirmation of the initiation of an outsourcing relationship to commercial banks was also revoked, and commercial banks are now only required to notify the National Bank of Georgia of outsourcing processes, related products, and systems.

On August 1, 2023, Decree № 195/04 of the Governor of the National Bank of Georgia “*On Approval of the Manual for the Use of Cloud Outsourcing Services by Financial Organizations*” was adopted as a result of the supervisory strategy of the National Bank of Georgia and due to the increasing adoption of cloud outsourcing services by financial organizations. The manual approved by the decree is a preventive mechanism that requires financial organizations to ensure that the decision on cloud outsourcing services is based on strategic need, and that the security risks associated with the cloud outsourcing environment are appropriately assessed. The financial organization is also required to obtain appropriate credentials on cybersecurity and information security practices from the service provider and to develop a strategy for withdrawing from cloud outsourcing services in advance.

On August 1, 2022, Decree № 193/04 of the Governor of the National Bank of Georgia on the amendment to Decree № 93/04 of the Governor of the National Bank of Georgia of August 3, 2022 on the approval of the Regulation of classification of loans and reporting

according to the taxonomy of sustainable financing was adopted. The amendment is technical in nature and provides for the removal of references to the provisions of the invalid decree.

In order to simplify the real estate inspection process and avoid imposing additional obligations on property owners, Decree No. 382/04 of the Governor of the National Bank of Georgia dated December 26, 2023 on amendments to the Decree No. 84/04 of the Governor of the National Bank of Georgia dated May 14, 2018 "On Approving Real Estate Appraisal Instructions for Commercial Banks" was adopted. The decree clarified that the mandatory requirements for commercial banks to submit a measurable drawing prepared by the surveyor in case of a difference between the actual area of the real estate to be appraised and the area registered in the LEPL National Agency of Public Registry, as well as to register the real area of the appraised property in LEPL the National Agency of Public Registry, acquire a recommendatory character. The decree also clarified that in case of restructuring and/or growth of liability/demand for financial instruments belonging to the first level credit risk category, the revaluation of the real estate will be mandatory if 2 years and more have passed since the last assessment, instead of 1 year.

In order to clarify the periodicity of the disclosure of information by the National Bank of Georgia on the financial condition of commercial banks and the timing of the reporting process, the Decree No. 398/04 of the Governor of the National Bank of Georgia dated December 29, 2023 on amendments to the Decree No. 92/04 of the Governor of the National Bank of Georgia dated June 22, 2017 "on approval of the regulation on disclosure of information by commercial banks under Pillar 3" was adopted. The decree determined the periodicity of the disclosure of information by the National Bank of Georgia on the financial condition of commercial banks. In particular, within 30 (thirty) calendar days after the end of the reporting month, the National Bank of Georgia will publish information on the financial condition of commercial banks. The deadlines for publishing quarterly reports have also

changed. In particular, commercial banks are required to publish quarterly statements within 40 (forty) calendar days after the end of the reporting quarter.

The amendment was made to Decree № 10/04 of the Governor of the National Bank of Georgia of February 11, 2011 on "Approval of the Regulation of Compliance with Minimum Reserve Requirements". In order to mitigate the impact of globally tightened financial conditions on the local economy, the Financial Stability Committee and the Monetary Policy Committee of the National Bank of Georgia decided on November 29, 2023, that it was appropriate to reduce the upper limit of the reserve norm from 25% to 20% of funds attracted by foreign currency.

Changes due to the transition to International Financial Reporting Standards (IFRS) of the banking system:

- The Decree No. 166/04 of the Governor of the National Bank of Georgia dated June 30, 2023 on amendments to the Decree No. 192/04 of the Governor of the National Bank of Georgia dated December 29, 2022 "on approving the regulation on determining risk categories of financial instruments and expected credit loss" was adopted. The submitted amendment abolished the parallel reporting period, which implies that for supervisory purposes the commercial bank is obliged to act according to international financial reporting standards;
- The amendment was made to the Decree №71/04 of the Governor of the National Bank of Georgia of April 22, 2019 on *Approval of the Regulation on Net Stable Funding Ratio*. Considering that after the transition to international financial reporting standards there is no longer a standardized asset and its definition, reference to first-level credit risk financial instruments was made to the decree, as well as the relevant definitions were specified;
- The amendment was made in the Decree № 70/04 of the Governor of the National Bank of Georgia of May 15, 2017 on "Approval of the Regulation on Liquidity Coverage Ratio of Commercial Banks". Con-

sidering that after the transition to international financial reporting standards there is no longer an asset classified as *standard* asset, reference to the first level of credit risk financial instruments in the decree has been made and the relevant definition has been specified. Furthermore, the amendment clarified the obligation to notify the National Bank of Georgia in case of a violation of the limit of ratios defined by the regulation. The notification is now required to be made according to currencies, as opposed to the previous record, which was directed towards the violation of the total liquidity coverage ratio.

- The amendment was made to the Decree №201 of the Governor of the National Bank of Georgia of July 20, 2006 "On Approving Regulations on Establishing, Calculating and Complying with the Limit of the General Open Currency Position of Commercial Banks". According to this amendment, it was determined that the composite foreign exchange position represented by the international financial reporting standards should be shortened by the expected credit loss of the foreign currency defined in the "Regulation on Defining Risk Categories of Financial Instruments and Expected Credit Loss" approved by the decree of the Governor of the National Bank of Georgia. In addition, the instructions related to the chart of accounts were removed from the decree;
- The Decree №117/04 of the Governor of the National Bank of Georgia of August 10, 2017 "On Approval of the Regulation on the Classification of Assets by Commercial Banks and Establishment and Use of Reserves for Possible Losses" was declared invalid, which is due to the changes caused by the transition of the banking system to the International Financial Reporting Standards (IFRS). Because from January 1, 2023, commercial banks are guided by the Decree № 192/04 of the Governor of the National Bank of Georgia of December 29, 2022 "On the definition of risk categories and expected credit losses of financial instruments", the above-mentioned decree was declared invalid. In view of this, the decree № 284/04 of the

Governor of the National Bank of Georgia of October 19, 2023 "On Approval of the Regulation of Credit Risk Management" was adopted, which aims to put a number of requirements regarding commercial banks under the regulation, which are important for conducting an effective supervision process and are not covered in the decree of the Governor of the National Bank of Georgia "On Determination of Risk Categories and Expected Credit Losses of Financial Instruments". The Decree also establishes the obligations of commercial banks/microbanks, the fulfillment of which ensures the assessment of the quality of the financial instrument, together with the regulations for determining the risk categories of financial instruments and expected credit losses. The commercial banks, microbanks and overseas bank/microbank branches operating in Georgia are obliged to comply with the requirements provided for by the decree;

- The decree № 258/04 of the Governor of the National Bank of Georgia of September 28, 2023 on the amendment to the decree № 214/04 of September 26, 2018 "On Approval of the Regulations on the Requirements of the Leverage Ratio for Commercial Banks" was adopted. The development of the decree is due to changes caused by the transition to International Financial Reporting Standards (IFRS) of the banking system. In accordance with the amendment, for the purposes of calculating the Leverage Ratio, commercial banks should use the numbers calculated on the basis of the International Financial Reporting Standards (IFRS) instead of the "Chart of Accounts for Georgian Banking Institutions and Application Instructions" approved by the Commission of Accounting Standards of the Parliament of Georgia on October 26, 2000. In addition, the terms of the provision approved by the aforementioned decree were clarified from a terminological point of view.

The Decree № 290/04 of the Governor of the National Bank of Georgia, dated October 27, 2023, amended the Decree № 176/04 of the Governor of the National Bank of Georgia, dated December 18, 2017 on the

determination of capital buffers for commercial banks within the framework of Pillar 2. The amendment clarified the methodology for calculating the credit risk adjustment (CRA) buffer, specifying that only the sum of the positive differences between the reserve volume of each scenario and the amount of expected credit loss created for the respective level financial instruments based on the International Financial Reporting Standards (IFRS) by the Commercial Bank and calculated for the balance sheet should be used. The effective date of this section was set for April 30, 2025, considering that this requirement will increase capital requirement for some commercial banks. Additionally, a new, third component was added to the CRA buffer, which includes other supervisory adjustments identified during the supervisory process. The timeframes for the imposition of the net stress test buffer on the CET 1 capital as well as for commercial banks to comply with the requirement of this buffer were set, in addition deductible buffers with the net stress test buffer were also defined. The calculation of the non-heated foreign exchange credit risk (CICR) buffer was clarified, specifying that only balance sheet elements in loans should be used for the purposes of calculating the dollarization of loans.

The Decree № 321/04 of the Governor of the National Bank of Georgia, dated November 20, 2023, amending the Decree № 100/04 of the Governor of the National Bank of Georgia, dated October 28, 2013) on the approval of the regulation on capital adequacy requirements of commercial banks was adopted. The change presented adjusted the principle of calculation of retained earnings to be included in the underlying primary capital. In particular, the principle of foreseeable dividend valuation was added, with the obligation to deduct from the profit to be included in the principal primary capital of which shall arise upon its foreseeability by a commercial bank.

The Decree № 363/04 of the Governor of the National Bank of Georgia, dated December 12, 2023, amending the Decree № 215/04 of September 26, 2018 on the approval of the Corporate Governance Code of

Commercial Banks was adopted. The amendment specified that commercial banks, in particular, the Supervisory Board of commercial banks, should be guided by the environmental, social and governance (ESG) Guidelines developed by the National Bank of Georgia and published on its official website when considering ESG issues and disclosing ESG risks. The purpose of the decree is to promote the proper integration of ESG issues into the activities of commercial banks, to effectively manage ESG risks and to improve disclosure of ESG issues. The ESG Guidelines aims to assist banks in developing and improving ESG issues integration and ESG risk management practices and to ensure appropriate, compatible and international best practice standards are met, which is important for ensuring financial stability.

Furthermore, the Decree № 380/04 of the Governor of the National Bank of Georgia, dated December 26, 2023, amended the "Corporate Governance Code of Commercial Banks", determining the authority of the National Bank of Georgia, at any time, in case of reasonable doubt, to require the commercial bank or to verify the suitability of independent members of the Board itself, and in case of a discrepancy, to request the commercial bank to terminate the status of independent membership of the Supervisory Board. The duration of being considered an independent member of the Board was also changed, with the aim of ensuring that the Board is composed of individuals with such experience, for whom the bank's strategy and goals are perceived in an in-depth and systematic, historical context. The present amendments clarified the issue of the deadline for submitting the minutes of the meeting of the General Meeting of the Bank, the Supervisory Board and the Committees established at the Supervisory Board level to the National Bank of Georgia, as well as the periodicity of conducting the Supervisory Board self-assessment and evaluation of the external assessor was specified.

The Decree № 93/04 of August 3, 2022 of the Governor of the National Bank of Georgia "On Approval of the Regulation of Classification and Reporting of Loans according to the Sustainable Finance Taxonomy" was

amended. The amendment approved new editions of Annex №1 and Annex №2 of the Decrees due to the need for technical changes.

The Joint Decree, № 10/01- № 51 of February 1, 2010 *on the approval of the regulation on the issuance, circulation, accounting and repayment of treasury obligations and treasury bonds by the Ministry of Finance of Georgia*, of the Governor of the National Bank of Georgia and the Minister of Finance of Georgia was also amended under the new joint decree No. 176/04- No. 268 of July 14, 2023 of the Governor of the National Bank of Georgia and the Minister of Finance of Georgia. The amendment clarified the definition of the term "Settlement Day" in the regulation approved by the decree. In addition, instead of the Ministry of Finance of Georgia, reference was made to the buyer in general. The formula for calculating the settlement price of the Treasury bonds of up to 6 months was also added. This change was made because the Ministry of Finance of Georgia, for the purposes of debt management, carries out the redemption operations of these types of securities.

The basis for the elaboration of amendments in the same decree made by the joint decree № 399/04 – №515 of December 29, 2023, of the Governor of the National Bank of Georgia and the Minister of Finance of Georgia was the fact that the Ministry of Finance of Georgia, for the purposes of state debt management, planned to initiate state securities exchange operations. Therefore, the amendments added to the *Regulation on Issuance, Circulation, Accounting and Repayment of Treasury Obligations and Treasury Bonds by the Ministry of Finance of Georgia* the stages of the state securities exchange operation and related details.

The amendment was made to the Decree № 32/04 of the Governor of the National Bank of Georgia dated March 27, 2014 on Approval of the Regulation of Action of the Common Program for Risk Assessment of Commercial Banks. The amendment removed the norms on the relevant units of the Specialized Risk Department and the Supervisory Policy Department

of the National Bank of Georgia. Instead, a general reference was made to these departments.

## MICROBANK SUPERVISORY FRAMEWORK

In 2023, based on the Law of Georgia "On the Activities of Microbanks", legal acts regulating the activities of microbanks were issued, thereby fully creating the regulatory legal framework for microbanks. The Decree № 105/04 of June 21, 2023 of the Governor of the National Bank of Georgia "On Approval of Microbank Licensing Regulation" was adopted. This decree provides details on the process of submitting a written application to the National Bank of Georgia for obtaining a microbank business license, as well as the list of information and documentation that should be attached to the application. The licensing requirements for microbanks are similar to those for commercial banks and are based on the standards set by the Euro Directive (Directive of the European Parliament and of the Council of June 26, 2013 (2013/36/EU) "On access to the activities of credit institutions and prudential supervision of credit institutions and investment companies (CRD Directive 2013/36/EU)) and the European Banking Authority.

The Decree № 119/04 of June 21, 2023 of the Governor of the National Bank of Georgia on Approval of the Regulation on the Eligibility Criteria for Administrators of Microbanks was also adopted. This decree establishes the regulations and procedures for assessing the eligibility criteria of microbank administrators, including the joint suitability issues of the Board of Directors and the Supervisory Board. It also provides a list of information and documentation that should be submitted for each criterion to ensure the eligibility assessment of a candidate.

In accordance with the Law of Georgia on the activities of Microbanks, the decree defines five criteria for the suitability of administrators:

- good reputation, trustworthiness, and conscientious attitude to work;
- proper knowledge, skill, and experience necessary

- for the conduct of microbank activities;
- independence of judgment;
- enough time to properly perform their duties; and
- the number of positions held simultaneously.

The decree also specifies the list of circumstances that should be considered for each criterion when assessing the suitability of a candidate.

Furthermore, a candidate eligibility questionnaire has been developed to simplify the process of submitting voluminous information by the candidate.

The eligibility requirements of microbank administrators are not substantially different from the relevant requirements for commercial banks and, like the latter, are based on the requirements set out in the relevant EU Directive (Directive 2013/36/EU, CRD) and the guidelines of the European Banking Authority.

The Decree № 106/04 of June 21, 2023 of the Governor of the National Bank of Georgia on Approval of the Regulation on the Acquisition of a Significant Share of Microbank was adopted, which clarified the content of the eligibility criteria for holders of a significant share of Microbank defined by the Law of Georgia on the Activities of Microbanks, stipulated the list of information/documentation to be submitted, the content of individual concepts related to the acquisition of a significant share and established the procedure for determining an indirect acquirer of a significant share.

By the decree, in accordance with the Law of Georgia on the Activities of Microbanks, 5 criteria for suitability of holders of significant shares were defined:

- the reputation of the applicant, which includes its reliability and adequate competence;
- compliance of the person selected by the applicant as a microbank administrator (if any) with the requirements specified by the Law and the National Bank of Georgia Legal Act on the Suitability Criteria of Administrators;
- financial rigor of the applicant;
- compliance of the microbank with the prudential supervisory requirements after the purchase of a share by the applicant;
- lack of risks of money laundering and terrorist financing related to the applicant/operation (transaction).

The decree also defined the list of circumstances under which the applicant's eligibility assessment should be based on each of the above criteria. In addition, the issue of using tests of control and multiplication of shares necessary for determining the indirect acquirer of a significant share of the microbank was determined.

The requirements established by the *Regulation on the acquisition of a significant share of microbanks* are not substantially different from the relevant requirements for commercial banks and, like the latter, are based on the requirements defined by the relevant EU Directive (Directive 2013/36/EU, CRD) and the European Banking Authority guidelines.

The decree № 116/04 of the Governor of the National Bank of Georgia "On setting the countercyclical buffer rate for microbanks" was adopted on June 21, 2023, by which 1% was defined as the counter-cycle capital buffer rate for microbanks. A 1-year deadline was set for Microbanks to meet this requirement.

The decree №114/04 of the Governor of the National Bank of Georgia "On determining the minimum amount of supervisory capital for microbanks" was adopted on June 21, 2023, according to which the minimum amount of supervisory capital of a legal entity interested in obtaining a microbank business license shall be gel 10 (ten) million.

The Decree № 107/04 of the Governor of the National Bank of Georgia on Approval of the Conflict of Interest Management Regulations for Microbanks was adopted on June 21, 2023, which aims to ensure adequate supervision and control over transactions with parties connected to microbanks in order to avoid conflicts

of interest as much as possible. The decree defined the issues to be regulated for the purposes of conflict of interest management, including the obligation of microbanks to identify and monitor related persons and transactions, and observe an arm's length principle with regards to transactions with them.

The decree №121/04 of the Governor of the National Bank of Georgia on "Approval of the Microbank Liquidation, Insolvency and Bankruptcy Regulation" was adopted on June 21, 2023, by which the issues related to the liquidation, insolvency and bankruptcy of the microbank were determined similar to the relevant provisions for commercial banks. Also, the authority of the National Bank of Georgia has been clarified in the regulation, - in special cases when the microbanks lack the funds to cover liquidation costs, - to provide the funds to cover the necessary costs for the smooth running of the liquidation process.

Decree №123/04 of the Governor of the National Bank of Georgia of June 21, 2023 on the Approval of the Regulation of Determination and Imposition of Monetary Penalties against Microbanks and its Administrators was adopted. The development of the decree was prompted by the Law of Georgia on Microbanking Activities. The law says that the National Bank of Georgia shall be entitled to impose a sanction (monetary penalty) on the microbank and its administrator and/or the controlling person in accordance with the principle of proportionality, in the manner and in the amount prescribed by it, together with or without the supervisory measure. Hence, the decree detailed the issues of determining and imposing monetary penalties on microbanks and its administrators by the National Bank of Georgia. The decree of the Governor of the National Bank of Georgia *"On the approval of Regulation of determination and imposition of monetary penalties against microbanks and its administrators"* does not differ substantially from the decree № 242/01 of the Governor of the National Bank of Georgia *"On the approval of Regulation on determination and imposition of monetary penalties against commercial banks and its administrators"*

of December 15, 2009, and the amounts of monetary penalties and categories of violations were determined for microbanks similar to commercial banks.

Decree №108/04 of the Governor of the National Bank of Georgia of 21 June 2023 on the Approval of the Regulation of General Program for the Assessment of Microbank Risks was adopted. The regulation approved by this decree establishes a microbank risk assessment process aimed at assessing the microbank risk level and determining appropriate supervisory measures. Risk assessment is a continuous supervisory cycle and mainly relies on the GRAPE assessment framework, the Banking Supervision Basel Committee's "Core Principles for Effective Banking Supervision" document and other advanced international supervisory practices.

The decree №112/04 of the Governor of the National Bank of Georgia "On Approval of the Corporate Governance Code of Microbanks" was adopted on June 21, 2023, which aims to define the basic principles of corporate governance for microbanks, insofar as effective and sound corporate governance in microbanks will contribute to the effective functioning and sustainability of the banking sector and the financial sector in general.

The Decree №113/04 of the Governor of the National Bank of Georgia of 21 June 2023 "On Approval of the Regulation of Binding Audit of the Consolidated Financial Statements of Microbanks and Disclosure in Notes" was adopted. In accordance with the decree, Microbank and its subsidiary organizations are obliged to invite an auditor annually and conduct audits of financial statements in the manner prescribed by the National Bank of Georgia.

The decree №110/04 of the Governor of the National Bank of Georgia "On Approval of the Regulation of Disclosure of Information by Microbanks under Pillar 3" was adopted on June 21, 2023, which aims to promote stronger market discipline through disclosure requirements. The disclosure requirements defined in this regulation make basic microbank information

available to market participants, which results in increased transparency and confidence in the adequacy of microbank risks and supervisory capital. In addition, it includes obligation of microbanks to publish the first annual report of Pillar 3 as defined by this regulation and submit it to the National Bank of Georgia as of the end of the license year, no later than May 15 of the following year.

Decree №117/04 of the Governor of the National Bank of Georgia of 21 June 2023 “On the Approval of the Regulations on Concentration of Risk Positions in Microbanks and Large Risks” was adopted aiming to promote the stability and healthy functioning of microbanks and the financial sector in general by setting requirements related to the concentration of risk positions and the management of large risks arising therefrom. The requirements set out in the regulations approved by the decree are based on the framework defined by the Basel Committee on Banking Supervision, Regulation 575/2013 of the European Parliament and of the Council on the Prudential Requirements of Credit Institutions and Investment Firms of 26 June 2013 and Directive 2013/36 of the European Parliament and of the Council on the Prudential Supervision of Credit Institutions and Investment Firms of 26 June 2013.

The decree №118/04 of the Governor of the National Bank of Georgia “on approval of real estate appraisal instructions for microbanks” was adopted on June 21, 2023, which defined the regulations and principles of real estate appraisal for microbanks; these, among other things, are based on “International Valuation Standards” (IVS). The purpose of this instruction is to enhance the quality of real estate valuation in the banking sector and to establish greater transparency of appraisal process and principles to contribute to the stable and efficient functioning of this sector.

Decree №111/04 of the Governor of the National Bank of Georgia of 21 June 2023 on Approval of the Regulation on Microbank Capital Adequacy Requirements was adopted. The regulation approved by this decree was developed on the basis of the Law of Georgia on the Activities of Microbanks, according to which the

microbank is obliged to observe the limits related to the ratio of capital classified assets of different types in the manner prescribed by the National Bank of Georgia. The issues provided for in the regulation are not basically different from the “Regulation on the Adequacy Requirements of the Capital of a Commercial Banks”. Specifically, the minimum capital requirements, elements of regulatory capital and capital classification criteria, supervisory adjustments, approaches to calculating credit, operating and market risk-weighted risk positions, credit risk mitigation forms, issues related to counterparties' credit risk are defined similarly. However, in the case of microbanks, no systemic risk buffer is defined. In addition, several issues are additionally regulated, such as the regulation of determining capital buffers for microbanks under Pillar 2. Unlike commercial banks, microbanks within Pillar 2 have only set requirements for a net GRAPE buffer and a Credit Risk Adjustment (CRA) buffer.

The Decree № 109/04 of the Governor of the National Bank of Georgia of 21 June 2023 on Approval of the Statute on the Requirements of the Leverage Ratio for Microbanks was adopted. The issues envisaged in the statute approved by this decree are not basically different from the “Regulation on the requirements of the Leverage Ratio of Commercial Banks”. The minimum requirement for the leverage ratio, the elements and standards for calculating the leverage ratio are defined similarly, applied to all commercial banks operating in Georgia. However, in the case of microbanks, the use of a method of linking the value of the risk position of the derivative instruments to an alternative market price is not defined, and neither is the use of netting of the funds receivable and payable under a transaction financed by securities with the same counterparty in case of obtaining a permit from the National Bank of Georgia.

The Decree №120/04 of the Governor of the National Bank of Georgia of 21 June 2023 on Approval of the Regulation on Risk Categories of Financial Instruments for Microbanks and Determination of Expected Credit Loss was adopted. The Regulation approved by this decree was developed with the need to bring the

National Bank of Georgia's supervisory strategy closer to international standards and to bring the principles of accounting and financial reporting in line with the International Financial Reporting Standard (IFRS) for supervisory purposes. The Regulation is based on IFRS 9 and also specifies some principles. The purpose of this regulation is to make the approaches used by microbanks to calculate the expected credit losses of financial instruments comparable to each other and to contribute to the improvement of the financial reporting process.

The decree №122/04 of the Governor of the National Bank of Georgia *"On the introduction and approval of the regime of temporary administration in microbank"* was adopted on June 21, 2023, which detailed the circumstances related to the introduction and abolition of the regime of temporary administration in microbank, the eligibility criteria of the temporary administrators and their rights and responsibilities.

The Decree №115/04 of the Governor of the National Bank of Georgia of 21 June 2023 *"On Approval of the Regulations for the Establishment of Branches, Representations and Other Similar Subdivisions by Microbanks"* was adopted, which determined the regulations and conditions for the creation of the microbank branch, other similar subdivision and representation licensed by the National Bank of Georgia. By the decree, microbanks were granted the right to establish a branch, another similar subdivision and representation, both on the territory of Georgia and abroad. The requirements established by microbanks for the establishment of branches, representations and other similar subdivisions are not substantially different from the relevant requirements for commercial banks.

The decree №104/04 of June 21, 2023 of the Governor of the National Bank of Georgia *"on amendments to Decree No. 13/04 of February 2, 2021 "On the Approval of the Principles of Ethics of Banking and Securities Market Participants and the Code of Professional Conduct"* was

adopted, as a result of which the principles of ethics and regulations of professional conduct established by the decree shall apply, including to microbanks.

The decree №135/04 dated June 26, 2023 of the Governor of the National Bank of Georgia on amending the Decree №151/04 of the Governor of the National Bank of Georgia of August 17, 2020, *"On Approval of the Risk Management Regulation of Data-Based Statistical, Artificial Intelligence and Machine Learning Models"* was adopted, by which the requirements and obligations imposed on commercial banks fully apply to microbanks as well.

The Decree №134/04 of the Governor of the National Bank of Georgia of 26 June 2023 *on Approval of the Statute on Net Stable Funding Ratio for Microbanks* was adopted. The requirements of the regulations approved by the decree are based on the Basel Committee on Banking Supervision and other internationally recognized standards. This statute regulates the net stable funding ratio, the purpose of which is to support the appropriate funding structure of microbank assets and off-balance sheet operations. Stable funding structure reduces the risk of solvency of microbank, while, net stable funding ratio limits dependence on short-term funding and stimulates better assessment of funding risk.

Decree №132/04 of the Governor of the National Bank of Georgia *"on Approval of Instruction on Requirements for Microbank Pricing Models"* was adopted on 26 June 2023. The instruction approved by this decree defines the principles of sound pricing for banking products and the criteria for its determination, for the purposes of adequately assessing and monitoring the risks associated with the pricing. The purpose of the instruction is to reduce the risks of microbank profitability and solvency by having a sound pricing policy, which positively impacts the stability of the financial sector, contributes to the efficient operation of the financial system and the establishment of a competitive environment.

Decree №140/04 of the Governor of the National Bank of Georgia of June 26, 2023 *on Approval of the Statute on Operational Risk Management by Microbanks* was adopted. The statute approved by this decree provides for the development of an operational risk management framework for microbanks in accordance with their size and complexity, which should be fully integrated into the entire microbank risk management process.

The Decree №136/04 of the Governor of the National Bank of Georgia of June 26, 2023 *on Approval of the Statute on the Management of the Interest Risk of the Banking Book of Microbanks* was adopted. The requirements of the statute approved by this decree are based on The Basel Committee on Banking Supervision and other internationally recognized standards. The purpose of the regulation is to identify, assess, manage the interest risk arising in the Banking Book and to promote the stability and sound functioning of the financial sector by imposing related requirements.

Decree №138/04 of the Governor of the National Bank of Georgia *"On Approval of the Statute of the Microbank Liquidity Coverage Ratio"* of June 26, 2023, aimed at ensuring that microbanks have liquid assets sufficient to cover the total net cash outflow during financial stress. This requires the microbank to maintain an adequate liquidity supply that will allow it to cope with the expected difference between liquid funds inflow and outflow under 30-day stressful conditions.

The decree №131/04 of June 26, 2023 of the Governor of the National Bank of Georgia amending the Decree No. 11/04 of the Governor of the National Bank of Georgia dated January 23, 2023 *"on determining systemically important commercial banks and establishing a buffer of systemicity for them"* was adopted. The decree defines the criteria for changing the system buffer limit for a commercial bank, which depends on the commercial bank's share in the total non-bank deposits in the system (except for secured deposits received from state institutions and organizations subject to state control). Since, according to the Law of

Georgia *"On the Activities of Microbanks"*, a microbank is authorized to attract interest-bearing and interest-free demand and term deposits, it was considered appropriate to incorporate the funds raised by microbanks in the calculation of the total non-bank deposits in the market.

Decree №137/04 of the Governor of the National Bank of Georgia of June 26, 2023 *on Approval of the Statute on Management of Dealing Operations for Microbanks* was adopted. The purpose of this decree is to ensure the identification/detection of microbanks' dealing financial instruments with the increase of the volume of financial instruments intended for trading on balance sheet accounts and the creation of appropriate internal policy and procedures by microbanks.

Decree №133/04 of the Governor of the National Bank of Georgia of 26 June 2023 *"on the establishment, calculation and approval of the limit of the general open currency position of microbanks"* was adopted. The purpose of determining the limit of the general open currency position envisaged by the regulation approved by this decree is to reduce the possible risk in case of a change in the exchange rate of foreign currency as a result of performing foreign exchange operations, as such change may adversely affect the profit, capital, liquidity and solvency of microbanks.

Decree №139/04 of the Governor of the National Bank of Georgia of 26 June 2023 *on Approval of the Regulation of Exchange of Information on Operational Risk Events"* was adopted. The requirements imposed on commercial banks by this decree were similarly extended to microbanks and they came under common regulation. In the manner approved by the decree, it was also regulated that in the database module without operational risks, the commercial bank/microbank will be obliged to upload information on monthly operational risk losses, and the NBG will share with commercial banks/microbank consolidated data of operating risk losses of commercial banks/microbank received on a quarterly basis.

The decree №157/04 of the Governor of the National Bank of Georgia of June 27, 2023 amending the decree №172/04 of the Governor of the National Bank of Georgia of December 7, 2021 on Approval of the Corporate Governance Code for Public Securities Issuers" was adopted. According to this decree, due to the fact that the scope of the Corporate Governance Code for Public Securities Issuers today does not include licensed commercial banks, whose corporate governance issues are regulated by the Special Statutory Act of the National Bank of Georgia, it is likewise advisable that the said Code does not apply to either of the licensed microbanks, since a special corporate governance framework will apply to them as well.

The decree №143/04 of the Governor of the National Bank of Georgia dated June 27, 2023 "On Amendments to the Decree No. 8/04 of the Governor of the National Bank of Georgia dated January 22, 2015 on the Approval of the Regulation on the Performance of Payment Operation" was adopted. The development of the decree was prompted by the need to extend this regulation to a new supervisory entity - microbank. The provisions of the regulation apply to microbanks in the same way as commercial banks.

The decree №148/04 of the Governor of the National Bank of Georgia dated June 27, 2023 amended the Decree №33/04 of March 31, 2022 of the Governor of the National Bank of Georgia on "Approving the regulation on limiting operations by payment service providers with gaming business companies". In accordance with the decree, the provisions of the regulation apply similarly to microbanks of commercial banks.

The decree №144/04 of the Governor of the National Bank of Georgia of June 27, 2023 on the amendment to the Decree № 99/04 of the Governor of the National Bank of Georgia, dated July 4, 2017, "On Approval of the Reporting Forms on Payment Services and Instructions for its Completion" was adopted. the amendment to the instruction approved by this decree envisages the dissemination of the provisions of the instruction to commercial banks in the same way as to microbanks. The decree №158/04 of the Governor of the National

Bank of Georgia dated June 27, 2023 on amending the decree №223/04 dated December 16, 2020 of the Governor of the National Bank of Georgia "On approval of the regulation on recognition of a person as a knowledgeable investor" was adopted. Based on the fact that the Law of Georgia on the Activities of Microbanks in case of approval of the National Bank of Georgia, allows microbanks to engage in one or more brokerage activities, as stipulated by the Law of Georgia on the Securities Market, in the Regulation, the Microbank was also defined as an intermediary of the Securities Market.

The Decree №146/04 of the Governor of the National Bank of Georgia of June 27, 2023 on amending the decree №122/04 of September 16, 2022 on "Approval of the Regulation for Determining Technical Requirements for Credit Transfer and Direct Debit Performance Denominated in Euros" was adopted. By this decree, the provisions of the Regulation apply to microbanks in the same way as commercial banks.

The decree №145/04 of the Governor of the National Bank of Georgia dated June 27, 2023, on amendments to the decree №44/01 of the Governor of the National Bank of Georgia dated March 17, 2010 "On approving the instruction on the use of international bank account numbers in banking institutions of Georgia" was adopted. According to the decree, the provisions of the instruction apply similarly of commercial banks to microbanks

The decree №149/04 of the Governor of the National Bank of Georgia of June 27, 2023, regarding the amendment to the decree №1/04 of the Governor of the National Bank of Georgia dated January 6, 2016 "On approval of the regulation on providing necessary information to the customers during the implementation of payment services" was adopted. By this decree, the provisions of the regulation apply to microbanks in the same way as commercial banks.

The Decree №156/04 of the Governor of the National Bank of Georgia, dated June 27, 2023, on amendments to the decree №181/04 of the Governor of the National

Bank of Georgia dated October 7, 2020, "On Approval of the Regulation for Transparency of Information on the Issuer and Appointment of the Registrar of Securities to the Issuer" was adopted. The Regulation was amended to include a reference to microbanks, as the Law of Georgia on the Activities of Microbanks allows for the purchase and sale of securities with their own funds as one of their activities, as well as, in case of approval of the National Bank of Georgia, the implementation of one or more brokerage activities provided for by the Law of Georgia on the Securities Market.

The Decree №153/04 of the Governor of the National Bank of Georgia, dated June 27, 2023, on amending the Decree №156/04 of the Governor of the National Bank of Georgia of September 2, 2020 "On Approval of the Strong User Authentication Regulation" was adopted. The amendment applies the provisions of the Regulation to microbanks in the same way as commercial banks.

The decree №152/04 of the Governor of the National Bank of Georgia of June 27, 2023, on amending the decree №155/04 of the Governor of the National Bank of Georgia dated September 2, 2020 "on approving the regulation on the card instrument" was adopted. The amendment applies the provisions of the Regulation to microbanks in the same way as commercial banks.

The Decree №147/04 of the Governor of the National Bank of Georgia, dated June 27, 2023, on amending the Decree №24/04 of the Governor of the National Bank of Georgia dated April 7, 2011, "On Approval of Instruction on Opening Accounts in Banking Institutions" was adopted. The amendment applies the instruction to microbanks in the same way as commercial banks and also eliminates certain technical deficiencies in the instruction, including clarification of the terms.

The Decree №151/04 of the Governor of the National Bank of Georgia, dated June 27, 2023, on amending the Decree № 253/04 of the Governor of the National Bank of Georgia dated November 30, 2018, "On Approval of the Regulations Concerning the Information Concurrent with Transfer" was adopted. The amendment applies

the provision to microbanks in the same way as commercial banks.

The decree №159/04 of the Governor of the National Bank of Georgia was adopted on June 27, 2023, approving the regulation of granting and revoking consent to Microbank by the National Bank of Georgia to carry out activities authorized for the brokerage company. The conditions for the implementation of brokerage activities by the microbank were established in the manner approved by this decree, including the criteria that must be met by the microbank before the implementation of brokerage activities. The applicant is obliged to submit to the National Bank of Georgia for obtaining consent: a list of the types of brokerage activities to be carried out; if any, the name of the provider of the trading platform and description of the technical characteristics; information about the business model of the microbank in the context of the brokerage activity and its strategic plan; information and documents proving the suitability of the person responsible for the microbank brokerage direction. The grounds for revoking the consent granted to the microbank are similar to the grounds for revoking the brokerage license. The norms of the regulation have been defined, which will be relevant and mandatory for the microbank to carry out in the course of brokerage activities.

The decree №155/04 of the Governor of the National Bank of Georgia was adopted on June 27, 2023, amending the decree № 198/04 of the Governor of the National Bank of Georgia dated November 11, 2020, "On Approval of the Regulation of Liquidation of the Investment Fund". Based on the fact that the Law of Georgia on the Activities of Microbanks envisages (within the relevant restrictions and limits) the opening of cash accounts (current, deposit) as one of the activities of Microbank, as well as, in case of approval of the National Bank of Georgia, the implementation of one or more brokerage activities provided for by the Law of Georgia on the Securities Market (which may include the storage of securities), the reference to Microbank was added to the relevant norms of the regulation.

The decree №154/04 of the Governor of the National Bank of Georgia dated June 27, 2023 on amendments to the decree №259/04 of the Governor of the National Bank of Georgia dated November 30, 2018 "On approval of the regulatory procedure of the specialized depository of the cumulative pension scheme" was adopted. Due to the fact that the Law of Georgia on the Activities of Microbanks provides for the issuance of guarantees as one of the activities of a microbank, the microbank has been added as a guarantor entity in connection with capital replenishment in the regulation approved by the decree.

Decree №150/04 of the Governor of the National Bank of Georgia was adopted on June 27, 2023, on the amendment to the Decree №287/04 of the Governor of the National Bank of Georgia of December 28, 2018 "On Approval of the Procedure of Liquidation of the Payment Service Provider". The development of the change was caused by the need to extend the payment service provider's liquidation regulation to a new supervisory entity - microbank. According to the Law of Georgia on the Activities of Microbanks, the provisions of the regulation apply to microbanks in the same way as commercial banks.

In order to implement and develop a unified, organized approach to cybersecurity management in microbanks, the Decree №165/04 of June 30, 2023 of the Governor of the National Bank of Georgia on Approval of the Microbanks Cybersecurity Management Framework was adopted. The framework takes into account the requirements of authoritative industry standards and regulations in the field of security, as well as the size and complexity of microbanks. The implementation of this framework will involve integrating cybersecurity issues within the framework of the strategic goals of microbanks, realizing effective mechanisms in parallel with modern cyber challenges. The framework envisages the implementation of periodic mandatory safety audits, penetration tests, which is a way to gain credentials in the effectiveness of the implemented approach.

The decree №169/04 of the Governor of the National Bank of Georgia was adopted on July 5, 2023, imposing additional requirements arising from the Law of Georgia on the Activities of Microbanks. According to the decree, microbanks have set additional limits on the return on cash, equity, and property investments attracted from individuals.

The decree №173/04 of the Governor of the National Bank of Georgia was adopted on July 12, 2023, amending the decree №32/04 of the Governor of the National Bank of Georgia "On Approval of the Regulation for the Protection of Consumer Rights in the Provision of Services by Financial Organizations". The present amendment extends the requirements of the consumer protection regulation in the provision of services by financial organizations, like other financial organizations, to microbanks.

The Decree №172/04 of the Governor of the National Bank of Georgia was adopted on July 12, 2023, amending the Decree №14/04 of the Governor of the National Bank of Georgia of February 17, 2022 "On Approval of the Code of Ethics Relating to the Loan Recoveries by Financial Organizations". The amendment presented extends the requirements of the Code of Ethics related to the loan recovery by financial organizations, like other financial organizations, to microbanks.

The decree №189/04 of the Governor of the National Bank of Georgia was adopted on August 1, 2023, amending the decree № 68/04 of the Governor of the National Bank of Georgia of May 28, 2021, "On the submission and approval of the market analysis and concentration notice". The amendment extends the regulation approved by the said decree, like other entities under the supervision of the National Bank of Georgia, to the microbanks.

The decree №190/04 of the Governor of the National Bank of Georgia was adopted on August 1, 2023, amending the decree №67/04 of the Governor of the National Bank of Georgia of May 28, 2021, "On the investigation of the case related to potential

competition violation". The amendment extends the regulation approved by the decree, like other entities under the supervision of the National Bank of Georgia, to the microbanks.

Decree №192/04 of the Governor of the National Bank of Georgia "On Classification of Loans and Approval of Reporting Regulation according to the Sustainable Finance Taxonomy for Microbank" was adopted on August 1, 2023. The purpose of this decree is to implement a system of classification of loans according to the sustainable finance taxonomy developed by the National Bank of Georgia. In particular, microbanks are instructed to assign a green loan category to the loan when issuing the loan in the manner specified by the same decree. Additionally, microbanks should submit monthly statements of green loans to the National Bank of Georgia. In the Environmental, Social, and Governance (ESG) reporting and disclosure form within the framework of the annual reporting of Pillar 3, microbanks are obliged to act in accordance with the Regulation. This ensures the existence of a common definition of green, social, and sustainable loans in the financial sector and the collection of data on green loans. This decree will help to increase the transparency of microbanks towards sustainable finance and ensure comparable and consistent disclosure of information.

The decree №201/04, of August 3, 2023, of the Governor of the National Bank of Georgia was adopted amending the decree №195/04 of August 27, 2018 of the Governor of Georgia "On providing information to the Credit Information Bureau on the territory of Georgia, on registering information in the database of the Credit Information Bureau and on approving the Regulation of accessibility". The amendment added the microbank to the definition of the lending organization and extended all the requirements provided for by the mentioned decree to it, which applies to other lending organizations. Additionally, the Credit Information Bureau imposed additional requirements regarding the proper setup of the electronic information system. The decree №213/04 of August 4, 2023 of the Governor of the National Bank of Georgia was adopted, amending

the Decree №160/01 of December 16, 2010 of the Governor of Georgia on "Approval of the Regulations of Monetary Operations of the National Bank of Georgia". The amendment is conditioned by the fact that microbanks have the opportunity to conduct monetary operations with the National Bank of Georgia, as well as commercial banks, in accordance with the Organic Law of Georgia on the National Bank of Georgia.

The decree №214/04 of the Governor of the National Bank of Georgia of August 4, 2023 "On Approval of the Regulation of Calculation of TIBR Indices" was adopted, amending the Decree №146/04 of the Governor of the National Bank of Georgia of October 12, 2021 "On Approval of the Regulation of Calculation of TIBR Indices". The amendment is conditioned by the fact that it is necessary to participate in the calculation of the indicative index TIBR index reflecting the interest rates of the GEL monetary market together with the transactions of commercial banks conducted by microbanks in accordance with the same regulation.

The decree №215/04 of the Governor of the National Bank of Georgia was adopted on August 4, 2023, amending the Decree №362 (of the Governor of the National Bank of Georgia of December 29, 2008 "On Approval of the Forms of International Transaction Reporting System for Commercial Banks of Georgia and Instructions for their Completion". The amendment is conditioned by the fact that the forms of the international transaction reporting system are received from microbanks in the same way as in the case of commercial banks. Additionally, it was clarified that the submission of these forms should be done by uploading to the relevant portal, instead of sending it to the e-mail.

The Decree №212/04 of the Governor of the National Bank of Georgia was adopted on August 4, 2023, amending the Decree №142/04 of the Governor of the National Bank of Georgia of July 21, 2020 "On Approval of the Regulations of Activities of the Participants of the Foreign Exchange Market". The amendment is conditioned by the fact that the same approaches to

intermediary activities carried out by microbanks in the foreign exchange market are applied as are envisaged for other participants. This will facilitate competition in the market on equal terms.

The decree №209/04 of the Governor of the National Bank of Georgia was adopted on August 4, 2023, amending the Decree № 49/04 of the Governor of the National Bank of Georgia of May 3, 2012 "On Approval of the Regulation of Standard Certificates of Deposit for Commercial Banks". The amendment is due to the need to establish the same conditions and requirements for issuing standard certificates of deposit for microbanks as are currently the case for commercial banks. It should be noted that for the purposes of the regulation approved by the mentioned decree, the certificate of deposit issued by the microbank will also be considered as a deposit, as a result of which the relevant restrictions provided for by the Law of Georgia on the Activities of Microbanks will apply to it.

The decree №211/04 of the Governor of the National Bank of Georgia was adopted on August 4, 2023, amending the Decree № 10/04 of the Governor of the National Bank of Georgia of February 11, 2011 "On Approval of the Regulation of Compliance with Minimum Reserve Requirements by Commercial Banks". The amendment is conditioned by the fact that the minimum reserve requirements apply to microbanks, as established for commercial banks, in accordance with the Organic Law of Georgia on the National Bank of Georgia.

Decree №210/04 of the Governor of the National Bank of Georgia was adopted on August 4, 2023, amending the Decree №141/04 of the Governor of the National Bank of Georgia, of July 21, 2020 "On Approval of the Regulation of Electronic Trade in Currencies Using the Bloomberg Trading System". The change is due to the need to disseminate the same approaches to activities undertaken by microbanks in the Bloomberg system as is the case for other participants, which will facilitate competition in the market on equal terms.

The decree №236/04 of the Governor of the National Bank of Georgia of September 7, 2023 on amending the Decree №1/04 of the Governor of the National Bank of Georgia dated January 5, 2018 "on approving the procedure for conducting operations related to cash and other valuables in commercial banks" was adopted. The said decree extends the procedure for the conduct of transactions related to cash and other valuables to microbanks, similar to commercial banks.

Resolution №5 of the Board of the National Bank of Georgia was adopted on September 8, 2023, on Amending the Resolution №5 of May 28, 2018, of the Board of the National Bank of Georgia on Approval of the Regulation of Destroying Lari Banknotes and Coins. Like commercial banks, this amendment envisages the implementation of the process of calculation and destruction of GEL banknotes without a commission in automatic mode by means of a sorting machine in the process of recalculation and sorting of GEL banknotes received from microbanks.

Resolution №6 of the Board of the National Bank of Georgia was adopted on September 8, 2023, on Amending the Resolution №3 of September 30, 2022 of the Board of the National Bank of Georgia on Establishing the Regulation of Response to the Detection of False Cash on the Territory of Georgia. The resolution envisages, like commercial banks, the dissemination of the Regulation of responding to fake cash on the territory of Georgia to microbanks.

Resolution №4 of the Board of the National Bank of Georgia was adopted on September 8, 2023 on amending the Resolution №4 of the Board of the National Bank of Georgia of June 27, 2011, "On Approval of the Criteria for Determining the Eligibility of Lari Banknotes and Coins and the Regulations for their Acceptance and Exchange". The resolution provides for the extension, like commercial banks, of criteria for determining the suitability of Lari banknotes and coins and the procedure for their acceptance and exchange to microbanks.

In order to simplify the real estate inspection process and avoid imposing additional obligations on the owner of the property, Decree №118/04 of June 21, 2023, of the Governor of the National Bank of Georgia "On Approval of the Instruction for Appraisal of Real Estate for Microbanks" was adopted which amended the decree №381/04 of the Governor of the National Bank of Georgia of December 26, 2023. The decree also clarified that in case of restructuring and/or growth of liability/demand for financial instruments belonging to the first level credit risk category, the evaluation of the real estate will be mandatory if 2 years and more have passed since the last evaluation, instead of 1 year.

The Decree №108/04 of June 21, 2023 of the Governor of the National Bank of Georgia on "Approval of the Regulation on the General Risk Assessment Program for the Microbanks" was amended, where a general reference was made to the Specialized Risk Department and the Supervisory Policy Department of the National Bank of Georgia, and the norms on the respective divisions of the above departments were removed.

## REGULATION OF PAYMENT SYSTEM AND PAYMENT SERVICES

Based on the amendments made to the Law of Georgia on Payment System and Payment Services, an updated version of the Regulation of Registration and Regulation of the Payment Service Provider was developed and the Decree №77/04 of the Governor of the National Bank of Georgia, of May 1, 2023 on "Approval of the Regulation of Registration and Regulation of the Payment Service Provider" was adopted. The decree defined the services according to the payment services as established by the Law of Georgia on Payment System and Payment Services. Accordingly, the changes also affected the list of registration documents. In addition, the decree defined the obligation of the interested entity to submit information about the administrators, the beneficial owner/owner of a significant share/entity with significant influence. The decree also provides for the obligation to submit a compliance table of the list of documents submitted for registration. The new decree defined the criteria for granting and cancelling

the provider's important provider status, clarified the criteria for the suitability of the administrator, the records related to the submission of the business plan and electronic system requirements during the registration of the interested entity as a provider, the requirements related to the provider's head office, work space, the equipment, as well as the data recorded in the electronic system, the requirements related to the internal policies and risk management of the provider and the treatment of customer complaints.

Based on the amendments made to the Law of Georgia on Payment System and Payment Services, the Decree №79/04 of the Governor of the National Bank of Georgia of May 1, 2023 "On Approval of the Regulation on the Requirement of Capital Adequacy of Payment Service Providers" was adopted, which established the minimum regulatory capital requirements and the methodology for calculation. According to the decree, the volume of the minimum regulatory capital depends on the list and types of payment services carried out/ to be carried out by the provider, and the volume of the required regulatory capital is calculated according to the transactions carried out by the provider and/ or the weighted value of the issued and covered electronic money or the average daily issued electronic money (balance). The decree also sets out the criteria that capital instruments must meet in decree for the provider to be able to incorporate them into tier 1 or tier 2 capital and meet the minimum regulatory capital requirements. The decree also established the obligations and prohibitions of the provider in case of violation of the regulatory capital requirement.

The decree №78/04 of the Governor of the National Bank of Georgia of May 1, 2023 amended an earlier Decree №1/04 of the Governor of the National Bank of Georgia of January 6, 2016, "On Approval of the Regulation of Providing Necessary Information to Customers in the Implementation of Payment Services", which technically changed the definition of a small-scale payment instrument. In particular, instead of being referred to another legal act, the definition of a small payment instrument was fully indicated in the aforementioned decree.

The Decree №80/04 of May 3, 2023, of the Governor of the National Bank of Georgia "On Approval of the Regulation of Inclusion in Open Banking" outlines the necessary requirements for various financial entities, including brokerage companies, microfinance organizations, lending entities, payment service providers, commercial banks, and currency exchange points, to be involved in Open Banking. The decree also specifies the list of information and documents to be submitted for inclusion in Open Banking, the terms of inclusion, the criteria, and the obligations of the entities involved in Open Banking. Additionally, the decree requires commercial banks to ensure the existence of a test environment and make it available to entities wishing to register as a provider of access to account information and a provider of payment initiation services. The National Bank of Georgia is responsible for making the decision on inclusion in Open Banking.

The Decree №299/04 of the Governor of the National Bank of Georgia "On Approval of the Payment System and Payment System Operator Supervision (Oversight) Regulation" was adopted on November 3, 2023. The development of the regulation was conditioned by the amendments made to the Law of Georgia "On Payment System and Payment Services".

The amendments to the law defined the authority of the National Bank of Georgia to grant the payment system the status of a systemically important payment system or an exceptionally important payment system. The criteria for a systemically important payment system and an exceptionally important payment system were also defined, and requirements for that system and/or its operator were established.

In accordance with the recommendations of the Georgian Financial Sector Assessment Program (FSAP) implemented by the International Monetary Fund and the World Bank, the principles of the CPSS-IOSCO Financial Market Infrastructure (PFMI) of the Payment and Settlement Systems Committee and the International Organization of Securities and Exchange Commissions shall be implemented for payment systems.

The Decree is developed in compliance with the principles of CPSS-IOSCO financial market infrastructure, their publicity framework and implementation methodology, the application of PFMI (Application of the Principles for financial market infrastructures to central bank FMIs) and European Central Bank payment systems oversight standards.

The decree applies to payment systems and their operators in Georgia, including payment systems managed by the National Bank of Georgia. The decree defined the managerial structure of the payment system, minimum standards for legal, credit, liquidity, operational, investment and general business risk management, established requirements for payment system settlement and the assets used in it, established requirements for payment system participant default Regulations and procedures and other issues.

The Decree envisages the division of payment systems into systemically important, exceptionally important and other payment systems and establishes the relevant requirements for each of them.

The Decree № 298/04, "On the determination of the subcategories of the important system and the approval of the procedure for granting the status of the important system to the payment system" issued by the Governor of the National Bank of Georgia on November 3, 2023, establishes the subcategories of important payment systems and outlines the procedure for granting them the status of systemic importance. Developed in accordance with the standards of the European Central Bank's payment systems oversight, the Decree applies to existing cash payment systems and their operators in Georgia, including those operated by the National Bank of Georgia.

The significant payment systems are divided into two categories: systemically important and exceptionally important. A payment system is considered systemically important if it has the potential to lead to systemic risk. The Decree sets out criteria for each category of important system and specifies the process for granting and revoking the status.

However, the Decree also authorizes the NBG to maintain the status of an important payment system, even if it no longer meets the criteria for that status, in order to preserve public trust, ensure the stability of the financial system, and/or recognize the social or public importance of the payment system.

Amendments were made to the decree №156/04 of the Governor of the National Bank of Georgia of September 2, 2020 "On Approval of the Strong User Authentication Regulation":

- By the decree №70/04 of the Governor of the National Bank of Georgia of April 11, 2023, the authority of the provider was established not to incorporate offline transactions in the calculation of payment transactions for specified purposes, since there may not always be a technical possibility to do so. And the obligation to justify the absence of technical capability was imposed on the issuer provider itself;
- On August 25, 2023, the decree №223/04 of the Governor of the National Bank of Georgia determined that the responsibilities and duties between the payment service providers are regulated by the agreement between them. It was additionally determined that the provider (as the provider of the payer) is not allowed to impose liability on the legal entity (consequently, the second provider) for unauthorized, incorrect or delayed execution caused by weaknesses in its respective processes/protocols and faulty operation;
- By the decree №373/04 of the Governor of the National Bank of Georgia of December 22, 2023, the obligation of the payment service provider to ensure the performance of e-commerce operations in compliance with the requirements of the regulation was deferred until January 1, 2025. Also, until April 1, 2024, the obligation of the payment service provider to implement a real-time monitoring mechanism for card payment transactions was extended. In addition, according to the decree, the deadline for conducting the

first audit envisaged by the regulation has been extended to July 1, 2024.

The Decree №99/04 of the Governor of the National Bank of Georgia, of July 4, 2017, "On Approval of the Reporting Forms on Payment Services and Instructions for its Completion," was amended. The purpose of the amendment is to require payment service providers to submit the reporting forms defined by the decree through the NBFI Remote Supervision Portal, rather than sending them to the relevant e-mail address at the National Bank of Georgia. Additionally, in order to improve the data based on supervisory practice, relevant changes were also made to the annexes of the decree.

The amendment to the Decree №80/04 of the Governor of the National Bank of Georgia of May 3, 2023 "On Approval of the Regulation of Inclusion in Open Banking" was made. The need for the amendment arose from the amendment to the Law of Georgia on Payment System and Payment Services, which authorized the Credit Information Bureau, along with other entities, to perform payment initiation services and/or account information access services (open banking) in accordance with the legal act of the National Bank of Georgia. As a result, the Credit Information Bureau was added to the list of relevant entities in the decree.

## LEGAL FRAMEWORK GOVERNING THE ACTIVITIES OF THE DISPUTE RESOLUTION COMMISSION

On December 1, 2023, the Commission for the Review of Disputes in the Field of Payment System and Payment Services with the National Bank of Georgia commenced its operations. The Commission is responsible for considering disputes between payment service users and providers regarding rights and obligations arising from the Organic Law of Georgia on the National Bank of Georgia, the Law of Georgia on the Payment System and Payment Services, and their respective bylaws.

During 2023, the Commission was established and the legal framework governing its activities was created in the form of bylaws. Resolution №1 July 26, 2023 of the Board of the National Bank of Georgia "On the Approval of the Selection, Submission, Appointment, Release and Remuneration Regulations of the Dispute Resolution Commission with the National Bank of Georgia" was approved. The regulation outlines the selection, submission, and appointment of the Commission's members and Chairperson, as well as the termination of their powers and remuneration for those members who are not employees of the National Bank of Georgia.

Several amendments were made to Resolution №1 July 26, 2023 of the Board of the National Bank of Georgia on the Selection, Submission, Appointment, Release and Approval of the Regulations of Remuneration of the Members and the Chairperson of the Dispute Resolution Commission of the National Bank of Georgia and were subsequently adopted:

- Resolution №7 of the Board of the National Bank of Georgia of September 8, 2023, which amended the Regulation to reference the Department of Consumer Rights Protection, as the Department of Consumer Rights Protection and Financial Education was divided into two separate departments.
- Resolution №9 of the Board of the National Bank of Georgia of October 27, 2023, which clarified several issues related to the activities of the Competition Commission, including the determination that the Deputy Chairman performs the duties of the Chairman in his absence, and the Chairman and Secretary of the Commission sign the protocol.
- Resolution №11 of the Board of the National Bank of Georgia of December 28, 2023, which established an exceptional regulation for the temporary election and appointment of the Chairman of the Dispute Resolution Commission, until the initial full staffing of the Commission. The amendments also specified the functions of the Chairman, including the authority to approve the symbols of the Commission,

such as the emblem and form pattern, and the manner in which they are used.

The Resolution №2 of July 26, 2023, of the Board of the National Bank of Georgia "On the Approval of the Regulations of Activity of the Dispute Resolution Commission with the National Bank of Georgia," was approved. The Regulation outlines the operational procedures of the Commission and establishes a special complaint form to be submitted to the Commission.

The Regulation covers the process of receiving complaints, identifying defects in the complaints, refusing to discuss the complaints, reviewing the complaints, dealing with the parties to the dispute, investigating the circumstances of the case, and other related issues. The support department of the Dispute Resolution Commission of the Department of Payment Systems of the National Bank of Georgia is designated as the Commission's office, and the regulation also includes provisions regulating the activities of the office.

Resolution №12 of December 28, 2023 of the Board of the National Bank of Georgia, amending the Resolution №2 of July 26, 2023 "on the Approval of the Regulations of Activity of the Dispute Resolutions Commission with the National Bank of Georgia", was adopted. The amendment is based on the fact that complaints can be submitted to the Dispute Resolution Commission in both material and electronic form, and the pages indicated in the complaint form may not be sufficient to describe the actual and/or legal circumstances of the complainant. As a result, a note has been added to the special complaint form approved by the resolution, allowing the complainant to attach additional numbered sheets to the complaint form.

## REGULATION OF VIRTUAL ASSET SERVICE PROVIDERS

Based on the amendments to the Organic Law of Georgia on the National Bank of Georgia and the Law of Georgia on the Prevention of Money Laundering and Terrorism Financing, enacted on January 1, 2023 ,

the Decree №94/04 of June 13, 2023 of the Governor of the National Bank of Georgia “on the Approval of the Regulation of Registration, Cancellation and Regulation of the Virtual Asset Service Provider at the National Bank of Georgia” was approved. The decree related to the registration of companies providing virtual asset services in Georgia and companies wishing to implement these services was developed to facilitate the prevention of money laundering and the financing of terrorism. The decree defined the registration requirements, eligibility criteria for the administrator and significant shareholder/beneficial owner, control of share participation in the company, requirements for the virtual asset service provider's head office, branches, self-service kiosk and electronic system, and other relevant issues. The decree does not consider the prudential supervision of the registered virtual asset service providers. After registration, the virtual asset service providers will be supervised only in terms of money laundering and preventing the financing of terrorism.

The amendments to the Organic Law of Georgia on the National Bank of Georgia on September 9, 2022, obligated the National Bank of Georgia to issue a legal act on the regulation of determining the transfer of a virtual asset before January 1, 2024. As a result, an amendment was made to the decree № 253/04 November 30, 2018 of the Governor of the National Bank of Georgia "On Approval of the Regulation on Information Accompanying Transfers". The amendments added a reference to the determination of accompanying information during the transfer of a virtual asset to the decree of the Governor of the National Bank of Georgia and the title of the regulation approved by this decree.

The requirements of the Regulation have been extended to virtual asset service providers and representatives of the financial sector who are authorized by the legislation regulating the activities to perform virtual asset services. The main purpose of the changes was to promote transparency and traceability of virtual

asset transfer transactions and to comply with the requirements of the recommendations related to the Virtual Asset of the Special Financial Action Task Force (FATF).

In view of good international practice, Regulation (EU) 2023/1113 of the European Parliament and of the Council of 31 May 2023 on information accompanying transfers of funds and certain crypto-assets and amending Directive (EU) 2015/849 was adopted while working on the amendments. The changes defined what information should accompany the transfer of a virtual asset and the following issues were also defined: execution of virtual asset transfer transactions as a bundle file, discovery of an incomplete concurrent transfer transaction by the asset recipient/virtual asset service intermediary provider with incomplete information about the asset transferor or the asset recipient, and internal policies, procedures, and controls of the payment service provider and the virtual asset provider to ensure the implementation of restrictive measures.

Changes were made to:

- Decree №77/04 of the Governor of the National Bank of Georgia of May 1, 2023 on Approval of the Regulation of Registration and Regulation of the Payment Service Provider;
- Decree №94/04 of the Governor of the National Bank of Georgia of 13 June 2023 “On Approval of the Regulation, Cancellation of Registration and Regulation of the Virtual Asset Service Provider at the National Bank of Georgia”;
- Decree №16/04 of the Governor of the National Bank of Georgia of February 5, 2020 “On the determination, imposition and enforcement of monetary penalties against the microfinance organization and its administrators”;
- In the Decree №123/04 of the Governor of the National Bank of Georgia of 21 June 2023 on the Approval of the Regulation of Determination and Imposition of Monetary Penalties against microbanks and their administrators;

- Decree №242/01 of the Governor of the National Bank of Georgia of December 25, 2009 “On the determination and imposition of monetary penalties against commercial banks and its administrators”;
- Decree №8/04 of the Governor of the National Bank of Georgia of January 22, 2015 “On Approval of the Regulation of Execution of Payment Operation”;
- Decree №87/04 of the Governor of the National Bank of Georgia of June 13, 2017 “On the determination, imposition and enforcement of a monetary penalty against the payment service provider and its administrators”.

The Decree № 376/04 of December 25, 2023 of the Governor of the National Bank of Georgia was approved, amending the Decree № 94/04 of the Governor of the National Bank of Georgia of June 13, 2023, on the Approval of the Regulation of Registration, Cancellation, and Regulation of the Virtual Asset Service Providers. The purpose of the amendment was to extend the additional period specified by the said decree for reviewing and making a decision on the documentation submitted by the interested parties for the registration of the virtual asset service provider.

The need to increase the additional deadline was due to the large volume and complexity of the information and documentation submitted by the interested parties. In order to fully review the documentation, an amendment was made to the regulation approved by the decree, determining that, if necessary, with appropriate justification, the National Bank of Georgia is entitled to extend the deadline for making a decision on registration twice, in each case for 60 calendar days.

Additionally, it was determined by the amendments that the virtual asset service provider is obliged to submit to the National Bank of Georgia information on any changes to the electronic system used for the implementation of virtual asset services.

## REGULATION OF CURRENCY EXCHANGE BUREAUS AND LENDING ENTITIES

The Regulation was adopted by the decree №15/04 of January 25, 2023 of the Governor of the National Bank of Georgia to amend the decree №217/04 of September 27, 2018 of the Governor of the National Bank of Georgia on the approval of the procedure for registration with the NBG, cancellation and regulation of the lending entity, by which the circle of entities entitled to registration as a lending entity was newly defined. The lending entity may function only in a limited liability or joint stock company legal form, and the individual entrepreneur can no longer be registered as a lending entity. As for the already registered individual entrepreneur who wants to continue as a lending entity, he/she is obliged to apply to the National Bank of Georgia for re-registration in the legal form of an entrepreneurial entity. Before NBG decides to allow re-registration, the lending entity registered as an individual entrepreneur shall be entitled to continue its activities in the prescribed manner. However, the individual entrepreneur, who did not apply to the National Bank of Georgia for re-registration no later than July 1, 2023, will be canceled as a lending entity. Registration will also be canceled for an entity who was refused re-registration by the National Bank of Georgia.

The decree №377/04 of the Governor of the National Bank of Georgia dated December 25, 2023 regarding amendments to the decree №37/04 of the Governor of the National Bank of Georgia dated February 28, 2018 "On approval of the regulation on registration and regulation of currency exchange bureaus" was approved. The amendments were made to approve the requirements related to the video surveillance system of currency exchange bureaus in accordance with the Decree №101 of March 2, 2022, of the Government of Georgia. The changes also specified the technical characteristics of automatic photo and video equipment and the manner of their operation, as well as the list of buildings on the outer perimeter of which it is mandatory to place/install automatic photos and/or video equipment.

Additionally, it was determined by the amendments that lending entities no longer need to register as currency exchange bureaus in order to carry out currency exchange operations. Furthermore, certain amendments were made to the above-mentioned decree, which is related to the enactment of the Law of Georgia on the Activities of Microbanks.

The Decree № 378/04 of the Governor of the National Bank of Georgia “On Amending the Decree № 217/04 of the Governor of the National Bank of Georgia of September 27, 2018 on the Approval of the Regulation of Registration, Cancellation and Regulation of the Lending Entity was adopted.

With the amendments, the list of buildings on the outer perimeter of which it is mandatory to place/install automatic photos and/or video equipment was approved. Additionally, the lending entity was allowed to carry out currency exchange operations without the need to register as a currency exchange bureau.

Furthermore, the amendments defined the requirements related to the conduct of currency exchange operations by the lending entity, which apply to currency exchange bureaus under the current legislation. Certain additional amendments were also made to the above decree, which is related to the enactment of the Law of Georgia on the Activities of Microbanks.

## SUPPORTING THE PREVENTION OF MONEY LAUNDERING AND FINANCING OF TERRORISM

To ensure compliance with the sanctions regimes the Decree №208/04 of the Governor of the National Bank of Georgia of August 4, 2023 “On Approval of the Regulation of Execution of Sanctions by Accountable Entities Subject to the Supervision of the National Bank of Georgia” was adopted, aimed at establishing requirements related to compliance with the sanctions regimes defined by the National Bank of Georgia for the financial sector. The Decree provides for the

commitment of the financial sector in this regard to the development and implementation of effective internal control mechanisms. The sanctions regimes defined by the decree include sanctions imposed by the United States, the European Union and the United Kingdom (USA, EU, UK) against the Russian Federation and the Republic of Belarus. In addition, the decree outlines the requirements for separate written instructions issued by the National Bank of Georgia in order to reduce the risks of violation/circumvention of the sanctions regimes. The decree also established restrictions on the supply of cash foreign currency, the obligation to submit reports, obligations related to noteworthy persons, as well as the authority of the National Bank of Georgia to issue written instructions to representatives of the financial sector and to apply supervisory measures and/or sanctions provided for by the legislation of Georgia. In order to fully realize the rights and freedoms of the Georgian citizen guaranteed by the Constitution of Georgia, the said decree was amended by the decree №253/04 of the Governor of the National Bank of Georgia of September 19, 2023 and Article 51 was added to the approved Regulation, which regulated the cases related to the spread of the sanctions regime.

For the effectiveness of the process of compliance with the sanctions regimes, the decree №273/04 of the Governor of the National Bank of Georgia “On Approval of the Regulation on Screening the Notification of the Society for Worldwide Interbank Financial Telecommunications (SWIFT)” was adopted, which aims to establish a unified approach to screening the SWIFT messages. The decree considers the categories and fields of SWIFT notifications, as well as the lists to be screened for and the requirements for the screening process and measures to be taken. The decree also provides for the introduction of the coincidence algorithm in an appropriate manner to identify small differences/alterations and transliterations, as well as the requirement to identify repeated operations and the coincidence review process. In addition, the decree established the obligation to test the coincidence algorithm for its effective functioning.

The Decree №313/04 of the Governor of the National Bank of Georgia was adopted on November 10, 2023, titled "Approval of the Regulation on Completing and Submitting the Report on the Supervision of the Risk of Money Laundering and Terrorism Financing of Commercial Banks." The decree regulates the procedure for filling out and submitting the Statement of the Risk Supervision of Money Laundering and Terrorism Financing by commercial banks.

In particular, the decree approves the *Regulation on Completing and submitting the Report for the supervision of the risk of money laundering and terrorism financing of Commercial banks*, the main form of reporting, and the list of offshore zones for reporting purposes.

"The Regulation on Completing and Submitting the Report for the Supervision of Risk of Money Laundering and Terrorism Financing of Commercial Banks" sets out the basic principles that should be taken into account by commercial banks in the process of submitting the relevant statements. The procedure also details in depth the timelines and procedure for submitting the reports.

The Decree №312/04 of the Governor of the National Bank of Georgia was adopted on November 10, 2023, titled Approval of the Regulation on Completing and Submitting the Report on the Supervision of the Risk of Money Laundering and Terrorism Financing of Microbanks. The decree approves "*the Regulation on Completing and Submitting the Report for the Supervision of the Risk of Money Laundering and Terrorism Financing of Microbanks*", the main form of reporting, and the list of offshore zones for reporting purposes.

"The Regulation on Completing and Submitting the Report for the Supervision of the Risk of Money Laundering and Terrorism Financing of Microbanks" sets out the basic principles that microbankers should incorporate in the process of submitting the relevant reports. The procedure also details in depth the timelines and procedure for submitting the reports.

## SECURITIES LAW

On the basis of the Law of Georgia on Mortgage Covered Bonds, the Decree № 56/04 of the Governor of the National Bank of Georgia of March 15, 2023 on Approval of the Regulation on Mortgage-Backed Bonds was adopted, which established the detailed regulations and conditions for the issuance of authorization for the issuance of mortgage bonds and the issuance of consent by the National Bank of Georgia for the implementation of the mortgage bond program. The decree also defined the periodic disclosure by issuers to investors and the National Bank of Georgia regarding bonds, the periodicity of calculation of the amount of assets secured by issuers and the possibility of using appropriate stress tests for this purpose, additional requirements for liquid assets of consolidation of assets used as collateral, as well as the regulations for record keeping and securing assets of the asset registry by the issuer. In addition, it was determined that the mortgage loan should be classified as a first-level credit risk financial instrument in accordance with the regulations approved by the National Bank of Georgia before the collateral assets are incorporated into the union. If the mortgage loan subsequently no longer meets this criterion, it may be considered for collateral in the amount of no more than 5% of the nominal value of the residual principal amounts of the mortgage bonds.

Considering the analysis of the common legislative situation and the development of specific stock exchanges, the decree №72/04 of April 21, 2023 of the Governor of the National Bank of Georgia, amended an earlier decree №178/04 of October 7, 2020, of the Governor of the National Bank of Georgia *on the approval of the list of recognized stock exchanges of a foreign country, the issuer of securities admitted to trading on them, the procedure of the public offering of securities in Georgia issued by an international financial institution and a development organization created with the participation of a foreign state*".

The new decree includes an updated list of stock exchanges, including Intercontinental Exchange

(United States; Intercontinental Exchange: <https://www.theice.com/>), Boerse Stuttgart Holding (Germany; Boerse Stuttgart Holding GmbH: <https://www.boerse-stuttgart.de/>), Singapore Stock Exchange (SGX-ST) (Singapore; <https://www.sgx.com/>), etc.

The amendment was made to the Decree №168/04 of September 22, 2020 of the Governor of the National Bank of Georgia on the Approval of the Regulations of Activities of the Specialized Depository. The purpose of the amendment was to avoid the need for financial institutions to submit the same information twice to the National Bank of Georgia in order to provide services of the Specialized Depository to both the accumulative pension scheme and to the investment funds.

As a result of the amendment, the consent granted to the financial institution pursuant to Decree №168/04 was aligned with the authorization granted to the financial institution in accordance with the "Regulation of the Specialized Depository of the Accumulative Pension Scheme" approved by the Order №259/04 of November 30, 2018 of the Governor of the National Bank of Georgia.

However, the amendment also specifies that the Authorized Specialized Depository shall be obliged to act in accordance with Decree №168/04 with respect to investment funds.

The amendment was made to the Decree №179/04 of the Governor of the National Bank of Georgia of October 7, 2020 on Approval of the Regulation of Report on Public Offering and Disposition of Securities. The amendment provides for simplified requirements of the Emission Prospectus for the public offering of bonds of commercial banks. In particular, the simplified issuance prospectus for bank bonds includes only basic information about the issuer and the terms of the offered securities, and the detailed financial information/indicators of the issuer will be included in the prospectus as a reference to the (annual, semi-annual, quarterly) statements issued by the commercial bank.

## CONSUMER RIGHTS PROTECTION

The Decree №4/04 of January 6, 2023 of the Governor of the National Bank of Georgia amended an earlier decree №32/04 of March 9, 2021 of the Governor of the National Bank of Georgia, titled "On Approval of the Regulation of Protection of Consumers' Rights when providing services by financial institutions". The purpose of the amendment is to promote transparency in the prices of financial products offered to consumers in combination, protect consumer rights, enhance the quality of their information, and spark competition in the market.

As a result of the amendment, financial organizations are now obliged to ensure transparency of the price of each financial product and appropriate disclosure to consumers when offering more than one financial product in combination. In particular, the financial organization should indicate and inform the customer about the prices assigned to the financial product as part of the combined offer, as well as about the selling prices of the financial product as an independent product.

However, the obligation to set a price does not apply to a financial product that is not available to the consumer as an independent financial product.

To ensure the protection of rights of consumers' of the financial sector, the decree №355/04 of December 5, 2023 of the Governor of the National Bank of Georgia "On amending the decree №32/04 of the Governor of the National Bank of Georgia of March 9, 2021 on approving the "On Approval of the Regulation of Protection of Consumers' Rights when providing services by financial institutions" was adopted, which restricted the offering/advertising of high-risk credit products/services by the financial organizations to a socially vulnerable person without the unequivocal consent of the customers. This will help prevent unconscious decision-making.

## REVISED REGULATION ON CONDUCTING A COMPETITION FOR EMPLOYMENT IN THE NATIONAL BANK OF GEORGIA

In order to further refine the selection system of candidates to be employed in the National Bank of Georgia, the decree №365/04 of the Governor of the National Bank of Georgia on *“Conducting a Competition for Employment in the National Bank of Georgia, Establishment of a Competition Commission and Approval of the Regulations of Activities”* was adopted on December 15, 2023, by which the National Bank was given the opportunity to ensure the formation of an even more transparent system for admission to work. The decree defines the essence and principles of the competition, the selection process of candidates and the stages of the selection contest. The decree also provides for the procedures for appointing a person as a professional civil servant and employing a candidate under an employment contract.

## REGULATION ON CONSIDERING INFORMATION CONFIDENTIAL

The Resolution №3 of August 25, 2023 of the Board of National Bank of Georgia amended an earlier resolution №4 of the Board of National Bank of Georgia dated November 1, 2021 titled *“considering information as confidential, the procedure for issuing it and the list of confidential information”*, according to which the minutes of the meetings of Audit Committee at the National Bank’s Board and audio recordings of the meetings were added to the list of the first category of confidential information, as the Audit Committee at the National Bank’s Board discusses issues related to financial reporting, risk management, internal control system, internal audit activities and audit services, which are confidential.

The Resolution №4 of the Board of National Bank of Georgia of November 1, 2021 titled *“considering information as confidential, the procedure for issuing it and the list of confidential information”*, was amended by the Resolution №8 of the Board of National Bank

of Georgia of September 8, 2023, which reworked terms such as the "Balance Sheet" and the "Profit and Loss Account", in addition, the public nature of this information was emphasized.

## UNIFIED FINANCIAL AND STATISTICAL INFORMATION SYSTEM OF THE NATIONAL BANK OF GEORGIA

The Decree №58/04 of March 17, 2023 of the Governor of the National Bank of Georgia on Amending the Decree №112/04 of November 26, 2015 on the Use of the Unified Financial and Statistical Information System of the National Bank of Georgia – NBGStat is aimed at improving the statistics of bank transfers, in particular, the amendment makes it possible for bank transfers (made abroad and from abroad) to be separated by countries.

Decree №279/04 of the Governor of the National Bank of Georgia dated October 18, 2023 amended an earlier decree №112/04 of the Governor of the National Bank of Georgia dated November 26, 2015 *On the use of the unified financial and statistical information system of the National Bank of Georgia - NBGStat, expanding the area of operation for NBGStat.*

In particular, the updated PCS data family of "Payment Card Statistics" was enacted with these changes and the production of the data family of the same name has changed since February 6, 2018. This decision significantly expanded the statistical database at the disposal of the National Bank of Georgia and made it possible to obtain information about the scope of use of payment instruments in a broad context. Also, according to the Law of Georgia on the Activities of Microbanks, the provisions of the decree apply to the microbanks in the same way as commercial banks.

## REGULATION ON USING THE NBFİ REMOTE SURVEILLANCE PORTAL

The decree №69/04 of April 13, 2020 of the Governor of the National Bank of Georgia *“On Approval of the Regulation for the Use of the NBFİ Remote Surveillance*

Portal” amended by the decree №14/04 of January 25, 2023 of the Governor of the National Bank of Georgia, aims to ensure submission of individual reports to be submitted to the National Bank of Georgia through the NBF Remote Surveillance Portal instead of sending them via email.

amended by the decree №97/04 of the Governor of the National Bank of Georgia dated June 15, 2023 clarified that the NBF remote surveillance portal can also be used by the microfinance organizations, the lending entities, the currency exchange bureaus and the non-bank depository institutions - credit unions to send a notification about the payment of a fine to the National Bank of Georgia and to upload a copy of the payment order confirming the payment.

## LENDING TO INDIVIDUALS

The Decree №168/04 of the Governor of the National Bank of Georgia of July 4, 2023 on amending the Decree №44/04 of the Governor of the National Bank of Georgia "On Approval of the Regulation on the Lending to Individuals" was approved. In accordance with the amendment, the microbanks, like the commercial banks, were defined as lending organizations and the regulation applicable to the commercial banks was extended to them. However, according to the change, it is possible for lending organizations to offer retail loans that initially have a lower interest rate, and after a certain period of time the rate will change to a significantly higher rate, therefore, the monthly payment will also increase materially. Contextually, this represents the grace period established on the loan, so the margin of difference between monthly payments was established, which was reflected in the definition of the grace period in the regulation.

The decree №291/04 of the Governor of the National Bank of Georgia of October 27, 2023 on amending the decree №44/04 of the Governor of the National Bank of Georgia "On Approval of the Regulation on Lending to Individuals" was adopted. Considering that the high growth rate of unsecured consumer loans recorded in 2022 has decreased, and the activity is maintained

at a sustainable level, according to the change, the maximum term limit of these types of loans has increased from 3 to 4 years.

## REGULATION ON ISSUING LOANS/BANK CREDITS UP TO 300,000 GEL BY THE LENDING ORGANIZATION

In accordance with the decision of the Financial Stability Committee of the National Bank of Georgia of October 18, 2023, in order to mitigate the risks caused by dollarization, the Decree №374/04 of the Governor of the National Bank of Georgia "On Determination of the Regulation of Loan/Bank Credit Issuance by Lending Organizations of up to 300,000 GEL" was approved. According to the decree, from January 1, 2024, a new loan of foreign currency will be issued only in the conditions of hedged currency risk. At the same time, it is clarified that when calculating the total liabilities of GEL 300,000, the obligations undertaken under the guaranty should not be taken into account. In addition, in order to encourage competition in the financial sector, the requirements of the decree will not apply not only to the case of refinancing/carefully modifying/restructuring the loan in the same currency, but also to the case of implementation by any other lending organization, unless the existing obligations of the borrower increase.

## THE REGULATION OF SALE OF GEL BANKNOTES/COINS, GOLD BARS AND NUMISMATIC VALUABLES

The resolution of the Board of the National Bank of Georgia №10 of November 30, 2023 on approval of the Regulation of sale of GEL banknotes/coins, gold bars and numismatic valuables was adopted. The purpose of the resolution is to determine the basic principles of calculation of the sale price of GEL banknotes/coins, gold bars and numismatic values and to ensure transparency of the sale activity. Among other changes, the method of calculating the selling price of gold bars was changed and improved. In particular, considering that gold ingots are ultimately an investment product, it was considered appropriate to determine their

selling price in the same way as the National Bank of Georgia's investment coins, once a day, on the website of the London Independent Precious Metals Authority (LBMA) at the price fixed in the previous afternoon (at 15:00 London time) for 1 ounce of gold in US dollars and according to the official exchange rate of the US dollar against the GEL by the National Bank of Georgia; the commission shall be determined within 3-80 percent. The decree no longer provides for pre-ordering, as conditions existing through the sale by preorder may vary in each case and therefore it was deemed appropriate to re-define the conditions each time, depending on the requirements at the moment, by the head of the National Bank of Georgia.

## THE REGULATION OF GOLD CERTIFICATES OF THE NATIONAL BANK OF GEORGIA

The Decree №315/04 of November 10, 2023 of the Governor of the National Bank of Georgia on *Approval of the Regulation of Gold Certificates of the National Bank of Georgia*, was adopted, according to which microbanks will also be involved in the process of buying and selling gold certificates. However, out of the 2 types of gold certificates available, the “gold bar investment certificate” has been cancelled, as it was not in high demand in previous periods, it is no longer issued since 2019 and this kind of certificate is not in circulation at all. Also, according to the regulation, the State Mints of OECD member countries of A and/or a higher long-term credit rating were added to the list of mints producing gold bars acceptable to the National Bank of Georgia.

ased on this, the amendment was made to the Decree №1/04 of January 5, 2018 of the Governor of the National Bank of Georgia on Approval of the Regulation of Conducting Operations Related to Cash and Other Values in Commercial Banks and Microbanks. in accordance with the amendment, the gold investment certificate was revoked. consequently, there is no longer any need to take into account the related regulation in this decree.

## THE CREDIT INFORMATION BUREAU

The decree №202/04 of August 3, 2023 of the Governor of the National Bank of Georgia amended an earlier decree of the Governor of the National Bank of Georgia №193/04 of August 27, 2018, “On the Approval of the Regulation of Registration, Cancellation and Regulation of the Credit Information Bureau in the National Bank of Georgia”. The need for this change was identified in practice based on discussions of the business model of the Credit Information Bureau - Platform. After the relevant consultations, it was deemed appropriate to reduce the number of penetration testing to be conducted by the Platform during the year.

## REGULATION ON PROACTIVELY PUBLISHING PUBLIC INFORMATION

The decree №89/04 of the Governor of the National Bank of Georgia of September 25, 2013 “On Proactively Publishing Public Information and Approving the Request Regulation in Electronic Form” was amended. With the amendment made to the regulations of the National Bank of Georgia, the Department of Public Relations and International Cooperation was separated from the Office of the Governor of the National Bank of Georgia and part of the public relations was transferred to the newly established Communication Department. Based on this, in the text of the decree, reference was made to the Communication Department instead of the Public Relations Department/Office.

## STRUCTURAL CHANGES IN ENFORCEMENT OF THE COMPETITION POLICY

The Decree №14 of the Board of the National Bank of Georgia of July 26, 2023 amended the Decree №10 of the Board of the National Bank of Georgia of April 8, 2015, on the approval of the regulations of the National Bank of Georgia.

The amendment added the exercise of the powers defined by the competition legislation to the functions of the Legal Department of the National Bank of

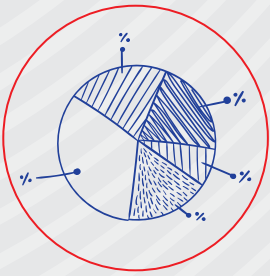
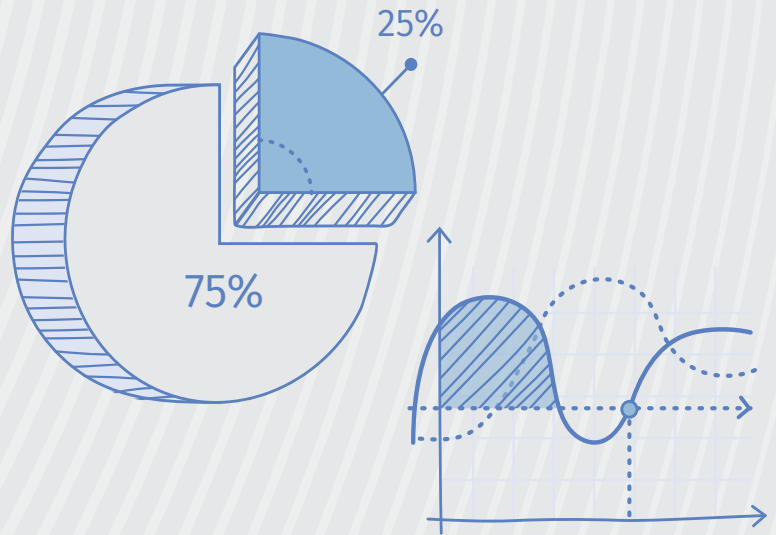
Georgia. For this purpose, a new structural unit, the Competition Division, was formed within the mentioned department.

The basis of formation of the Competition Division was the fact that, in accordance with Article 47<sup>8</sup> of the Organic Law of Georgia on the National Bank of Georgia, the National Bank of Georgia is responsible for enforcement of the competition policy in the financial sector. In particular, the National Bank of Georgia is responsible for considering complaints/applications on possible violations of competition by representatives of the financial sector and notifications of concentration.

In this process, the National Bank of Georgia is guided by the Law of Georgia on Competition and the relevant bylaws, in particular, "Rules of procedures for investigation, complaint/application submission and

consideration of cases related to alleged distortion of competition" approved by the order №67/04 of May 28, 2021 of the President of the National Bank of Georgia and "On the approval of the rule of market analysis and submission and consideration of notification of concentration" by the order №68/04 of May 28, 2021 of the President of the National Bank of Georgia. These statutory acts are based on best international practice and the recommendations of the World Bank experts.

Based on the above, the functions of the Competition Division were defined as: to ensure the consideration of cases provided for by the Law of Georgia on Competition; to determine the need to apply other sanction and/or supervisory measures together with a monetary penalty against the competition violator; to ensure the review of the notification of concentration; to monitor relevant products and/or services market in order to assess the competitive environment, etc.



# STATISTICAL ACTIVITIES

18

The year 2023 was marked by new initiatives in the field of monetary and financial statistics production. Significant results were achieved in the implementation of two large-scale projects, methodological changes were made in the production of various reports and indicators, and the need to introduce modern machine learning models arose due to the increasing volume of data processing.

At the end of 2023, the data sources of interactive reports published on the official website of the National Bank of Georgia were modified. Specifically, a data visualization and analysis platform using the Data Processing ETL (Extract, Transfer, Load) tool in the Tableau BI environment was implemented to increase performance by partitioning data time intervals. This ensured a more efficient data structure and, in addition, a mechanism for generating data hyper files was developed. Hyper files of these modified data sources were placed on a separate dedicated server and communicated with the reports published on the website in a direct way. As a result, this strategic change eliminated the direct link between reporting and primary databases, which increased the security level of the data view and significantly improved the performance of openly published interactive reporting.

Two years ago, in the interests of users and modern methodological trends in statistics production, two large-scale projects, expanding the data families of money transfers and transactions in foreign currencies, were planned. The introduction of the money transfers data family was given priority, and during 2023, this process moved into an active phase. In particular, in the system of financial and statistical data acquisition, processing, storage, and dissemination of the SebStat, software preparation works were completed, and the technical infrastructure allocated for testing was held. A number of consultative meetings were held with representatives of commercial banks and microfinance organizations, where challenges re-

lated to the implementation of the mentioned project were identified, and the technical capabilities of the involved parties were studied in detail. Consequently, technical documentation, a package of requirements, and methodological materials were prepared and presented to the parties involved in the project. It should be noted that only commercial banks have been involved in the SebStat system so far. As part of this project, several additional microfinance organizations are participating. The relevant package of updated money transfers data in the environment intended for SebStat testing is being actively tested, and the project is scheduled to be completed by the end of the second quarter of 2024. Accordingly, the data on money transfers will be presented in additional sections on the official website of the NBG. In particular, the sectoral distribution of the parties involved in the transactions, the age groups, and the geographical location of the transfer withdrawal will be available at the municipality level, allowing users to analyze and forecast the cash flows in detail.

Statistics of operations performed in foreign currencies and financial derivatives are necessary for a large-scale and comprehensive understanding of financial markets, risk management, economic trends, and investment strategies. It is the basis for informed decision-making by market participants and regulators. Accordingly, the second important project implemented by the National Bank of Georgia is related to the expansion of the data family of operations performed in foreign currencies. This means the collection of detailed daily data on spot operations and financial derivatives of forward and swap types. This project, due to its complexity and scalability, is associated with a number of challenges and technical difficulties on the part of both the NBG and the commercial banks participating in the project. During 2023, the relevant technical infrastructure in the SebStat system was held, for which technical documentation was prepared. Issues are still being discussed in the

format of workshops with commercial banks, and the project will move to the testing stage next year.

The National Bank of Georgia annually conducts the Financial Access Survey (FAS), which includes information on loans, deposits, other financial instruments, and indicators. It reflects the level of financial involvement of the public across the country and provides general information about the financial education of the public. The National Bank of Georgia conducts this reporting on the initiative and recommendation of the International Monetary Fund. Georgia is the leading country in the region in terms of the production of these reports, and the data has the opportunity to be presented in different contexts compared to other countries. This is the result of the introduction and application of modern standards and trends by the National Bank of Georgia in its statistics production activities. The National Bank of Georgia participates in seminars dedicated to the production of financial engagement reports annually. In November 2023, at a seminar organized by the International Monetary Fund (CCAMTAC) in the city of Almaty, recommendations were issued. According to these recommendations, the information presented in the financial availability statement should be added to the financial data presented in a gender, age groups, and regional context in accordance with recent challenges. In terms of the recommended data collection, the National Bank of Georgia has developed an appropriate strategy and will reflect additional data in the financial accessibility statement as requested in the following year.

Since 2023, commercial banks are required to submit monthly financial statements to the NBG in accordance with the IFRS international standard methodology. In connection with this change, in order to bring the data of the SebStat system in line with the IFRS standard, a package of changes has been developed. This includes the development of additional financial instruments and an additional parameter on the

data type. During 2023, consultations with commercial banks were underway, and the methodological approaches to the monthly financial statements to be submitted to the SebStat system were updated accordingly. An action plan was developed, and the commercial banks were set the appropriate deadlines for migration to the updated model.

Implementation of the modified methodological approach developed by the International Monetary Fund (IMF) during 2023 for the production of Financial Stability Indicators (FSI) was effectively implemented. The calculation of FSI indicators was devoted to significant efforts and resources for representatives of other sub-sectors of the financial sector. The IMF places a significant emphasis on the use of financial stability indicators as critical tools for analysis and informed decision-making in various sectors of the economy. Consequently, IMF experts are scheduled to visit Georgia in the first quarter of 2024. The primary objective of this visit is to provide technical support and to ensure effective use of the modified methodological approach.

In 2023, data presentation was optimized on the official website of the National Bank of Georgia. This initiative focused on the units, format and structure of data presented in a spreadsheet format, which is one of the important elements of NBG's financial statements. In response to customer demands and commitment to transparency, measurement units were calibrated. Consequently, the data presented in thousands and units has been transformed into millions. This adjustment not only simplifies data interpretation, but also meets global reporting standards, enabling stakeholders to clearly perceive financial performance. The data structure presented in the table format was carefully reviewed in order to provide a user-friendly interface. The format has undergone a redesign that simplifies navigation, highlights critical information, and improves overall presentation of financial data.

Over the past decade, as a result of increasing activity in the financial sector, the need to use machine learning (ML) as a modern tool models has arisen for the processing and validating increased volumes of data, which has given rise to the need for its in-depth study and implementation. ML models significantly contribute to the improvement of predictive analytics in fi-

nancial statistics. Using historical data, these models can identify trends and potential correlations, making it easier to draw analytical conclusions and make decisions. This year, it was planned to find appropriate models and find ways to effectively adapt to the business process.





# FINANCIAL STATEMENTS

NATIONAL BANK OF GEORGIA

For the Year Ended  
31 December 2023

19

<b>STATEMENT OF MANAGEMENT’S RESPONSIBILITIES FOR THE PREPARATION AND APPROVAL OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2023</b>	<b>274</b>
<b>INDEPENDENT AUDITORS’ REPORT</b>	<b>275 – 276</b>
<b>FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2023:</b>	
Statement of profit or loss and other comprehensive income	277 – 278
Statement of financial position	279 – 280
Statement of changes in equity	281
Statement of cash flows	282
Notes to the financial statements	283 – 325

## NATIONAL BANK OF GEORGIA

### STATEMENT OF MANAGEMENT RESPONSIBILITIES FOR THE PREPARATION AND APPROVAL OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2023

Management is responsible for the preparation of the financial statements that present fairly the financial position of the National Bank of Georgia (the "Bank") at 31 December 2023, the results of its operations, cash flows and changes in equity for the year then ended, in accordance with International Financial Reporting Standards ("IFRS").

In preparing the financial statements, management is responsible for:

- Properly selecting and applying accounting policies;
- Presenting information, including accounting policies, in a manner that provides relevant, reliable, comparable and understandable information;
- Providing additional disclosures when compliance with the specific requirements in IFRS are insufficient to enable users to understand the impact of particular transactions, other events and conditions on the Bank's financial position and financial performance; and
- Making an assessment of the Bank's ability to continue as a going concern.

Management is also responsible for:

- Designing, implementing and maintaining an effective and sound system of internal controls, throughout the Bank;
- Maintaining adequate accounting records that are sufficient to show and explain the Bank's transactions and disclose with reasonable accuracy at any time the financial position of the Bank, and which enable them to ensure that the financial statements of the Bank comply with IFRS;
- Maintaining statutory accounting records in compliance with legislation and accounting standards adopted in Georgia which are IFRS;
- Taking such steps that are reasonably available to them to safeguard the assets of the Bank; and
- Preventing and detecting fraud and other irregularities.

The financial statements for the year ended 31 December 2023 were authorized for issue on 26 April 2024 by the Council of the Bank.

**On behalf of the Council of the Bank:**

\_\_\_\_\_  
**Acting Chairman of the Council**

**Natela Turnava**

\_\_\_\_\_  
**Head of Finance and Accounting  
Department  
Andria Manelashvili**



KPMG Georgia LLC  
 5<sup>th</sup> Floor GMT Plaza  
 Mtatsminda District, Liberty Square N4 (plot 66/4)  
 0105 Tbilisi, Georgia  
 IN 404437695  
 Telephone +995 322 93 5713  
 Internet www.kpmg.ge

# Independent Auditors' Report

## To the Council of the National Bank of Georgia

### *Opinion*

We have audited the financial statements of the National Bank of Georgia (the "Bank"), which comprise the statement of financial position as at 31 December 2023, the statements of profit or loss and other comprehensive income, changes in equity and cash flows for the year then ended, and notes, comprising material accounting policies and other explanatory information.

In our opinion, the accompanying financial statements present fairly, in all material respects, the financial position of the Bank as at 31 December 2023, and its financial performance and its cash flows for the year then ended in accordance with IFRS Accounting Standards as issued by the International Accounting Standards Board (IFRS Accounting Standards).

### *Basis for Opinion*

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the *Auditors' Responsibilities for the Audit of the Financial Statements* section of our report. We are independent of the Bank in accordance with the International Ethics Standards Board for Accountants International Code of Ethics for Professional Accountants (including International Independence Standards) (*IESBA Code*) together with the ethical requirements that are relevant to our audit of the financial statements in Georgia, and we have fulfilled our other ethical responsibilities in accordance with these requirements and the IESBA Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

### *Other Information*

Management is responsible for the other information. The other information comprises the information included in the annual report, but does not include the financial statements and our auditors' report thereon.

Our opinion on the financial statements does not cover the other information and we do not express any form of assurance conclusion thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated.

If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

### *Responsibilities of Management and Those Charged with Governance for the Financial Statements*

Management is responsible for the preparation and fair presentation of the financial statements in accordance with IFRS Accounting Standards, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.



**National Bank of Georgia**  
Independent Auditors' Report  
Page 2

In preparing the financial statements, management is responsible for assessing the Bank's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Bank or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Bank's financial reporting process.

### **Auditors' Responsibilities for the Audit of the Financial Statements**

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditors' report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

As part of an audit in accordance with ISAs, we exercise professional judgment and maintain professional scepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Bank's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Bank's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditors' report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditors' report. However, future events or conditions may cause the Bank to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

The engagement partner on the audit resulting in this independent auditors' report is:

Vakhtang Kezheradze

KPMG Georgia  
Georgia, Tbilisi  
26 April 2024



**NATIONAL BANK OF GEORGIA**  
**STATEMENT OF PROFIT OR LOSS AND OTHER COMPREHENSIVE INCOME**  
**FOR THE YEAR ENDED 31 DECEMBER 2023**  
*(in thousands of Georgian Lari)*

	Notes	Year ended 31-Dec-23	Year ended 31-Dec-22
<b>Interest income from international reserves</b>			
Cash and cash equivalents		82,532	20,413
Investments measured at fair value through other comprehensive income ("FVOCI")		351,290	105,079
Other		45,818	15,305
		<b>479,640</b>	<b>140,797</b>
<b>Interest income from monetary policy operations</b>			
Due from resident financial institutions		143,176	356,846
Investments measured at fair value through other comprehensive income		214,429	157,006
Negative interest on financial liabilities		-	5,209
		<b>357,605</b>	<b>519,061</b>
<b>Other interest income</b>			
Investments measured at amortised cost		8,488	11,847
Negative interest on financial liabilities		-	110
		<b>8,488</b>	<b>11,957</b>
<b>Total interest income calculated using the effective interest rate method</b>			
		<b>845,733</b>	<b>671,815</b>
<b>Interest expense from monetary policy operations</b>			
Debt securities issued		(6,063)	(6,628)
Due to resident financial institutions		(100,317)	(74,318)
		<b>(106,380)</b>	<b>(80,946)</b>
<b>Other interest expenses</b>			
Due to the International Monetary Fund		(102,343)	(46,347)
Due to customers		(1,544)	(562)
Interest expense on lease liabilities		(119)	(117)
Negative interest on financial assets (International reserves)		-	(1,204)
		<b>(104,006)</b>	<b>(48,230)</b>
<b>Total interest expense</b>			
		<b>(210,386)</b>	<b>(129,176)</b>
<b>NET INTEREST INCOME</b>			
		<b>635,347</b>	<b>542,639</b>
Impairment charge	28	(1,542)	(8)
<b>NET INTEREST INCOME AFTER IMPAIRMENT CHARGES</b>			
		<b>633,805</b>	<b>542,631</b>
Net gains/(losses) from foreign currencies:			
<i>Translation gain/(losses)</i>		59,689	(475,157)
<i>Dealing gains</i>		15,115	147,720
Fee and commission income	4	6,044	4,981
Fee and commission expense	4	(3,077)	(3,717)
Net realized losses on instruments measured at fair value through other comprehensive income		(75,098)	(24,490)
Net realized gains on financial instruments measured at fair value through profit or loss		5,345	47,698
Net unrealised gains on financial instruments measured at fair value through profit or loss		(17,384)	34,647
Other income	5	11,796	3,452
<b>NON-INTEREST INCOME/(EXPENSE), NET</b>			
		<b>2,430</b>	<b>(264,866)</b>

The statement of profit or loss and other comprehensive income is to be read in conjunction with the notes to, and forming part of, the financial statements.

## NATIONAL BANK OF GEORGIA

### STATEMENT OF PROFIT OR LOSS AND OTHER COMPREHENSIVE INCOME FOR THE YEAR ENDED 31 DECEMBER 2023 (CONTINUED)

(in thousands of Georgian Lari)

	Notes	Year ended 31-Dec-23	Year ended 31-Dec-22
Personnel expenses	6	(44,102)	(32,955)
General and administrative expenses	6	(15,676)	(13,269)
Money printing expenses		-	(12,076)
Depreciation and amortization	6	(7,493)	(8,210)
Other expenses	5	(9,806)	(4,176)
<b>NON-INTEREST EXPENSES</b>		<b>(77,077)</b>	<b>(70,686)</b>
<b>PROFIT FOR THE YEAR</b>		<b>559,158</b>	<b>207,079</b>
<b>Other comprehensive income</b>			
<i>Items that are or may be reclassified subsequently to profit or loss:</i>			
Net change in fair value of investments measured at fair value through other comprehensive income		47,602	(156,546)
Net change in fair value of investments measured at fair value through other comprehensive income reclassified to profit or loss		75,098	24,490
<b>Total other comprehensive Income/(loss)</b>		<b>122,700</b>	<b>(132,056)</b>
<b>TOTAL COMPREHENSIVE INCOME FOR THE YEAR</b>		<b>681,858</b>	<b>75,023</b>

The financial statements as set out on pages 12 to 54 were approved by management on 26 April 2024 and were signed on behalf of the Council of the Bank by:

\_\_\_\_\_  
Acting Chairman of the Council  
Natela Turnava

\_\_\_\_\_  
Head of Finance and Accounting Department  
Andria Manelashvili

## NATIONAL BANK OF GEORGIA

### STATEMENT OF FINANCIAL POSITION AS AT 31 DECEMBER 2023

(in thousands of Georgian Lari)

	Notes	31-Dec-23	31-Dec-22
<b>ASSETS:</b>			
<b>Foreign currency assets</b>			
<b>International reserves</b>			
Cash and cash equivalents	7	2,123,328	3,867,452
Special Drawing Rights holdings with the International Monetary Fund	9	1,214,799	1,249,154
Assets related to derivative instruments	10	15,738	45,653
Investments measured at fair value through profit or loss	11	272,264	272,372
Investments measured at fair value through other comprehensive income	12	9,846,621	7,809,221
<b>Other foreign currency assets</b>			
Other assets	17	1,345	657
		<b>13,474,095</b>	<b>13,244,509</b>
<b>National currency assets</b>			
<b>Monetary policy instruments</b>			
Due from resident financial institutions	8	3,738,771	3,456,584
Assets related to derivative instruments	10	-	734
Investments measured at fair value through other comprehensive income	12	2,668,266	2,272,589
<b>Other national currency assets</b>			
Investments measured at amortised cost	13	81,194	121,390
Right-of-use assets	14	483	1,537
Property and equipment	15	51,575	54,127
Intangible assets	16	9,234	5,312
Other assets	17	12,481	4,744
		<b>6,562,004</b>	<b>5,917,017</b>
<b>TOTAL ASSETS</b>		<b>20,036,099</b>	<b>19,161,526</b>

The statement of financial position is to be read in conjunction with the notes to, and forming part of, the financial statements.

## NATIONAL BANK OF GEORGIA

### STATEMENT OF FINANCIAL POSITION AS AT 31 DECEMBER 2023 (CONTINUED)

(in thousands of Georgian Lari)

	Notes	31-Dec-23	31-Dec-22
<b>LIABILITIES AND EQUITY:</b>			
<b>LIABILITIES:</b>			
<b>Foreign currency liabilities</b>			
<b>Monetary policy instruments</b>			
Due to resident financial institutions	18	4,312,166	5,499,478
<b>Other foreign currency liabilities</b>			
Due to resident financial institutions	18	14,040	217,265
Due to the Ministry of Finance of Georgia	19	753,038	623,860
Due to the International Monetary Fund	9	2,339,583	2,408,008
Other liabilities	17	35,051	8,621
		<b>7,453,878</b>	<b>8,757,232</b>
<b>National currency liabilities</b>			
Money issued in circulation	21	5,934,138	5,040,547
<b>Monetary policy instruments</b>			
Debt securities issued	22	59,225	59,135
Due to resident financial institutions	18	1,758,885	1,225,303
Liabilities related to derivative instruments	10	-	1,649
<b>Other national currency liabilities</b>			
Due to the Ministry of Finance of Georgia	19	1,692,692	1,155,878
Due to the International Monetary Fund	9	1,780	2,175
Due to customers	20	7,578	7,187
Other liabilities	17	311,705	475,183
		<b>9,766,003</b>	<b>7,967,057</b>
<b>TOTAL LIABILITIES</b>		<b>17,219,881</b>	<b>16,724,289</b>
<b>EQUITY:</b>			
Capital		15,000	15,000
Reserve fund		1,153,535	939,559
Foreign currency revaluation reserve		1,680,180	1,620,491
Other revaluation reserve		31,299	48,683
Revaluation reserve of investments measured at fair value through other comprehensive income		(63,796)	(186,496)
Retained earnings		-	-
<b>TOTAL EQUITY</b>	23	<b>2,816,218</b>	<b>2,437,237</b>
<b>TOTAL LIABILITIES AND EQUITY</b>		<b>20,036,099</b>	<b>19,161,526</b>

The financial statements as set out on pages 12 to 54 were approved by management on 26 April 2024 and were signed on behalf of the Council of the Bank by:

\_\_\_\_\_  
Acting Chairman of the Council  
Natela Turnava

\_\_\_\_\_  
Head of Finance and Accounting Department  
Andria Manelashvili

The statement of financial position is to be read in conjunction with the notes to, and forming part of, the financial statements.

## NATIONAL BANK OF GEORGIA

### STATEMENT OF CHANGES IN EQUITY FOR THE YEAR ENDED 31 DECEMBER 2023

(in thousands of Georgian Lari)

	Capital	Reserve fund	Foreign currency revaluation reserve	Other revaluation reserve	Revaluation reserve of investments measured at FVOCI	Retained earnings	Total equity
1-Jan-22	15,000	754,750	2,095,648	14,036	(54,440)	-	2,824,994
<b>Total comprehensive income</b>							
Profit for the year	-	-	-	-	-	207,079	207,079
<b>Other comprehensive income</b>							
<i>Items that are or may be reclassified subsequently to profit or loss:</i>							
Net change in fair value of investments measured at fair value through other comprehensive income during the year	-	-	-	-	(156,546)	-	(156,546)
Net change in fair value on investments measured at fair value through other comprehensive income reclassified to profit or loss	-	-	-	-	24,490	-	24,490
Total other comprehensive loss	-	-	-	-	(132,056)	-	(132,056)
<b>Total comprehensive income for the year</b>	-	-	-	-	(132,056)	207,079	75,023
<b>Transactions recorded directly in equity</b>							
Transfer to the Ministry of Finance from 2022 profit under the Law* (Note 23)	-	-	-	-	-	(462,780)	(462,780)
Transfer to reserve fund from 2022 profit under the Law* (Note 23)	-	184,809	-	-	-	(184,809)	-
Transfer from foreign currency revaluation reserve under the Law* (Note 23)	-	-	(475,157)	-	-	475,157	-
Transfer to other revaluation reserve under the Law* (Note 23)	-	-	-	34,647	-	(34,647)	-
<b>Total transactions recorded directly in equity</b>	-	184,809	(475,157)	34,647	-	(207,079)	(462,780)
31-Dec-22	15,000	939,559	1,620,491	48,683	(186,496)	-	2,437,237
<b>Total comprehensive income</b>							
Profit for the year	-	-	-	-	-	559,158	559,158
<b>Other comprehensive income</b>							
<i>Items that are or may be reclassified subsequently to profit or loss:</i>							
Net change in fair value of investments measured at fair value through other comprehensive income during the year	-	-	-	-	47,602	-	47,602
Net change in fair value on investments measured at fair value through other comprehensive income reclassified to profit or loss	-	-	-	-	75,098	-	75,098
Total other comprehensive income	-	-	-	-	122,700	-	122,700
<b>Total comprehensive income for the year</b>	-	-	-	-	122,700	559,158	681,858
<b>Transactions recorded directly in equity</b>							
Distribution to the Ministry of Finance from 2023 profit under the Law* (Note 23)	-	-	-	-	-	(302,877)	(302,877)
Transfer to reserve fund from 2023 profit under the Law* (Note 23)	-	213,976	-	-	-	(213,976)	-
Transfer to foreign currency revaluation reserve under the Law* (Note 23)	-	-	59,689	-	-	(59,689)	-
Transfer from other revaluation reserve under the Law* (Note 23)	-	-	-	(17,384)	-	17,384	-
<b>Total transactions recorded directly in equity</b>	-	213,976	59,689	(17,384)	-	(559,158)	(302,877)
31-Dec-23	15,000	1,153,535	1,680,180	31,299	(63,796)	-	2,816,218

\* Organic Law of Georgia on the National Bank of Georgia

The financial statements as set out on pages 12 to 54 were approved by management on 26 April 2024 and were signed on behalf of the Council of the Bank by:

\_\_\_\_\_  
Acting Chairman of the Council  
Natela Turnava

\_\_\_\_\_  
Head of Finance and Accounting Department  
Andria Manelashvili

The statement of financial position is to be read in conjunction with the notes to, and forming part of, the financial statements.

## NATIONAL BANK OF GEORGIA

### STATEMENT OF CASH FLOWS FOR THE YEAR ENDED 31 DECEMBER 2023

(in thousands of Georgian Lari)

	Notes	Year ended 31-Dec-2023	Year ended 31-Dec-2022
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>			
Interest received		672,866	663,498
Interest paid		(204,662)	(118,239)
Fees and commissions received		6,044	4,981
Fees and commissions paid		(3,077)	(3,717)
Net realized gains on financial instruments at fair value through profit or loss		8,324	47,698
Net realized gains from dealing in foreign currencies		15,116	147,720
Other income received		(1,906)	3,442
Personnel expenses paid		(44,102)	(32,955)
Cash paid for printing money		(4,520)	(9,633)
Other general and administrative expenses paid		(13,284)	(14,083)
<b>Net cash inflow from operating activities before changes in operating assets and liabilities</b>		<b>430,799</b>	<b>688,712</b>
<i>Net (increase)/decrease in operating assets:</i>			
Due from resident financial institutions		(283,130)	(308,699)
Special Drawing Rights holdings with the International Monetary Fund		35,121	(4,421)
Assets measured at fair value through profit or loss		(403)	(6,083)
Other assets		(9,431)	(348)
<i>Net increase/(decrease) in operating liabilities:</i>			
Money issued in circulation		893,591	451,513
Due to resident financial institutions		(829,577)	1,903,599
Due to the Ministry of Finance of Georgia		640,552	200,721
Due to customers		391	6,582
Liabilities related to derivative instruments		(1,649)	1,649
Other liabilities		30,326	1,945
<b>Net cash inflow from operating activities</b>		<b>906,590</b>	<b>2,935,170</b>
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>			
Purchase of property and equipment		(1,480)	(3,617)
Purchase of intangible assets		(6,378)	(1,884)
Purchase of investments measured at fair value through other comprehensive income		(14,224,651)	(13,267,050)
Proceeds from redemption and sale of investments measured at fair value through other comprehensive income		12,167,258	11,485,798
<b>Net cash used in investing activities</b>		<b>(2,065,251)</b>	<b>(1,786,753)</b>
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>			
Transfer to the Ministry of Finance of Georgia	23	(462,780)	(356,060)
Debt securities issued		254,027	253,383
Debt securities redeemed		(254,495)	(253,968)
Repayments to the International Monetary Fund	9, 26	(79,863)	(46,991)
<b>Net cash used in financing activities</b>		<b>(543,111)</b>	<b>(403,636)</b>
Effect of exchange rates changes on cash and cash equivalents		(42,352)	(501,258)
Net increase in cash and cash equivalents		(1,744,124)	243,523
<b>CASH AND CASH EQUIVALENTS, at the beginning of the year</b>	7	<b>3,867,452</b>	<b>3,623,929</b>
<b>CASH AND CASH EQUIVALENTS, at the end of the year</b>	7	<b>2,123,328</b>	<b>3,867,452</b>

The financial statements as set out on pages 12 to 54 were approved by management on 26 April 2024 and were signed on behalf of the Council of the Bank by:

Acting Chairman of the Council  
Natela Turnava

Head of Finance and Accounting Department  
Andria Manelashvili

The statement of financial position is to be read in conjunction with the notes to, and forming part of, the financial statements.

## NATIONAL BANK OF GEORGIA

### NOTES TO THE FINANCIAL STATEMENTS AS AT AND FOR THE YEAR ENDED 31 DECEMBER 2023 *(in thousands of Georgian Lari)*

---

#### 1. ORGANIZATION

The National Bank of Georgia (the “Bank”) is the central bank of Georgia and the banker and fiscal agent of the Government of Georgia. The Bank was founded on 2 August 1991 based on the law of Republic of Georgia “On the National Bank of Republic of Georgia”. Currently, the Bank operates in accordance with the Organic Law of Georgia “On the National Bank of Georgia” enacted effective 1 December 2009 (the “Law”).

The responsibilities of the Bank focus on the goals of price stability, financial system stability and efficiency, national currency issuance, and efficient management of international reserves. These responsibilities are carried out as part of the broad functions described below.

##### **Monetary policy**

The main objective of the monetary policy of the Bank is to maintain price stability. Price stability implies the existence of a moderate and predictable rate of inflation, which is a necessary precondition for long run economic growth. Furthermore, the Bank supports financial system stability and promotes the country’s economic growth as long as the latter objectives do not contradict its main goal – maintaining price stability. Monetary and exchange rate policies serve the objective of preserving the purchasing power of the national currency, raising the growth potential of gross domestic product, and improving the investment climate.

##### **Supervision and financial stability**

The main objective of the Bank is to ensure the stability and efficiency of Georgia’s financial system. In achieving those objectives, the Bank is responsible for the supervision and regulation of separate participants on the financial market – commercial banks, micro banks, banking groups, non-bank depository institutions, micro-finance organisations, independent securities registrars, brokerage companies (except for insurance brokerage companies), the stock exchange, central depository, specialised depository, asset management companies, publicly accountable enterprises, foreign currency exchange offices, investment funds, payment system operators, payment service providers, credit information bureaus, loan issuing institutions, virtual asset service providers and the Pension Agency of Georgia (with respect to its investment activities).

Within the relevant regulatory framework, the National Bank of Georgia supports the protection of consumer and investor rights. Moreover, the Bank, with the involvement of different stakeholders from the Government institutions, the private financial sector and civil society has developed the National Strategy of Financial Education as a complement to financial consumer protection and inclusion efforts, with a view to supporting financial stability and financial well-being of individuals.

##### **Currency issuance**

The Bank is the only body in the country authorized to issue Georgian Lari banknotes and coins on the territory of Georgia. The Bank determines the design, composition and other features of the Georgian Lari banknotes and coins, printed and minted by leading international suppliers.

##### **International reserve management**

The Bank maintains a portfolio of foreign currency reserves for policy and operational purposes, for instance, to protect the country from external vulnerability by maintaining sufficient liquidity to absorb shocks during a financial crisis and to support day-to-day foreign currency payment needs of the Georgian Government and those of the Bank.

##### **Payment systems**

The Bank operates the largest payment system in the country – the Real Time Gross Settlement (RTGS), which processes and settles interbank and Government payments in the national currency.

## NATIONAL BANK OF GEORGIA

### NOTES TO THE FINANCIAL STATEMENTS AS AT AND FOR THE YEAR ENDED 31 DECEMBER 2023

(in thousands of Georgian Lari)

#### Governance

As at 31 December 2023 and 2022, the members of the Council of the Bank (“the Council”) were as follows:

Position	Name (2023)	Name (2022)
Chairman	Ms. Natela Turnava (Acting Governor, first Vice-governor)	Mr. Koba Gvenetadze (Governor)
Member	Ms. Ekaterine Galdava (Vice-governor)	Mr. Archil Mestvirishvili (Vice-governor)
Member	Ms. Ekaterine Mikabadze (Vice-governor)	Mr. Papuna Lezhava (Vice-governor)
Member	Ms. Nana Keinishvili	Mr. Nikoloz Gagua (Vice-governor)
Member	Mr. Teimuraz Khomeriki	Mr. Robert H. Singletary
Member	-	Ms. Ekaterine Galdava
Member	-	Ms. Ekaterine Mikabadze
Member	-	Ms. Natela Turnava

The Council is defined to consist of 9 members. As at 31 December 2023, position of 4 members of the Council was vacant (2022: 1 positions).

Mr. Koba Gvenetadze’s term expired effective March 2023. Ms. Natela Turnava (first Vice-governor) is acting as Governor and head of the Council as of the date of issuance of these financial statements.

The Bank’s main office is located at 1 Zviad Gamsakhurdia Embankment, 0114, Tbilisi, Georgia. As at 31 December 2023 and 2022, the Bank operated one cash service center. The Bank employed 601 and 538 personnel as at 31 December 2023 and 2022, respectively.

## 2. BASIS OF PREPARATION OF FINANCIAL STATEMENTS

#### Statement of compliance

These financial statements have been prepared in accordance with International Financial Reporting Standards (“IFRS”).

Presentation of these financial statements is framed within an economic and accounting framework that fairly reflects the financial position of the Bank, and at the same time, contributes to the economic analysis of the Bank’s operations. Assets and liabilities within the statement of financial position are segregated as captions of foreign and national currencies, which better reflects economics and risks underpinning the Bank’s operations. The Bank’s assets in foreign currencies are mainly related to its international reserve management function. At the same time, the Bank’s assets and liabilities in national currency are mainly recognised as a result of operations related to the conduct of monetary policy, issue of money in circulation and other functions of the Bank, as defined under the Law. For these reasons, the economic concepts of international reserves and monetary policy are additionally grouped under the sub-captions “international reserves” and “monetary policy instruments”, respectively. Statement of Profit or Loss and Other Comprehensive Income separately presents interest income/expenses and non-interest income/expenses by functional operations of the Bank. Statement of cash flows is presented using the direct method.

#### Basis of measurement

These financial statements are prepared on the historical cost basis, except for financial instruments measured at fair value through profit or loss and investments measured at fair value through other comprehensive income.

#### Functional and presentation currency

The Bank’s main objective is to maintain price stability, which implies that open-market operations play a significant role in the development of the monetary policy, accordingly, its main activity is the issuance of banknotes and coins in Georgian Lari, which is the national currency of Georgia and which has been defined as the functional and presentation currency for the purpose of preparing these financial statements. Consequently, all balances and transactions denominated in currencies, other than the Georgian Lari are considered as denominated in “foreign currency”.

## NATIONAL BANK OF GEORGIA

### NOTES TO THE FINANCIAL STATEMENTS AS AT AND FOR THE YEAR ENDED 31 DECEMBER 2023 (in thousands of Georgian Lari)

---

These financial statements are presented in thousands of Georgian Lari (“GEL”), unless otherwise indicated.

Financial information presented in GEL is rounded to the nearest thousands, except when otherwise indicated.

### 3. MATERIAL ACCOUNTING POLICIES

The Bank has consistently applied the following accounting policies to all periods presented in these financial statements.

#### Financial Instruments

A financial instrument is defined as any contract that gives rise to both a financial asset of one entity and a financial liability or equity instrument of another entity.

The Bank’s portfolio of financial instruments comprise Georgian Lari-denominated securities, foreign government, supranational or agency securities, interest rate futures and options, holdings in the International Monetary Fund (IMF), cash and cash equivalents, due from financial institutions, due to commercial banks, the Ministry of Finance of Georgia, the IMF and other financial assets and liabilities. The Bank accounts for its financial instruments in accordance with IFRS 9–*Financial Instruments* and reports these instruments under IFRS 7–*Financial Instruments: Disclosures* and IFRS 13–*Fair Value Measurement*.

#### Classification

The Bank classifies its financial assets in the following categories: measured at amortised cost (AC), measured at fair value through other comprehensive income (FVOCI) and measured at fair value through profit or loss (FVTPL). The classification depends on business model under which the financial assets are managed and their cash flow characteristics. The Bank classifies its financial liabilities as subsequently measured at amortized cost except for derivatives liabilities, which are measured at fair value through profit or loss. Classification of the financial assets and the financial liabilities is determined at initial recognition.

A financial asset is measured at amortised cost if it meets both of the following conditions and is not designated as at FVTPL:

- the asset is held within a business model whose objective is to hold assets to collect contractual cash flows; and
- the contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

A debt instrument is measured at FVOCI only if it meets both of the following conditions and is not designated as at FVTPL:

- the asset is held within a business model whose objective is achieved by both collecting contractual cash flows and selling financial assets; and
- the contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

For debt instruments measured at FVOCI, gains and losses are recognised in other comprehensive income, except for the following, which are recognised in profit or loss in the same manner as for financial assets measured at amortised cost:

- Interest income using the effective interest method;
- Expected credit losses (further referred to as “ECL”) and reversals; and
- Foreign exchange gains and losses.

## NATIONAL BANK OF GEORGIA

### NOTES TO THE FINANCIAL STATEMENTS AS AT AND FOR THE YEAR ENDED 31 DECEMBER 2023

*(in thousands of Georgian Lari)*

---

When a debt financial asset measured at FVOCI is derecognised, the cumulative gain or loss previously recognised in other comprehensive income is reclassified from equity to profit or loss.

All other financial assets are classified as measured at FVTPL.

On initial recognition, the Bank may irrevocably designate a financial asset that otherwise meets the requirements to be measured at amortised cost or at FVOCI as FVTPL if doing so eliminates or significantly reduces an accounting mismatch that would otherwise arise.

#### *Business model assessment*

The Bank makes an assessment of the objective of a business model in which an asset is held at a portfolio level because this best reflects the way the business is managed and information is provided to management. The information considered includes:

- Objectives of holding a portfolio;
- Frequency, value and timing of sales (both past and future);
- How the performance of the business model and financial assets are evaluated and reported to the Bank's key management personnel;
- The risks that affect the performance of the business model, in particular, the way in which those risks are managed (to meet the objectives); and
- Whether collection of contractual cash flows (e.g. interest income received) represents significant portion of the portfolios' returns.

#### *Assessment whether contractual cash flows are solely payments of principal and interest*

For the purposes of assessment of whether the contractual cash flows are solely payments of principal and interest, the 'principal' is defined as the fair value of the financial asset on initial recognition. 'Interest' is defined as consideration for the time value of money and for the credit risk associated with the principal amount outstanding during a particular period of time and for other basic lending risks and costs (e.g. liquidity risk and administrative costs), as well as profit margin.

In assessing whether the contractual cash flows are solely payments of principal and interest, the Bank considers the contractual terms of the instrument. This includes assessing whether the financial asset contains a contractual term that could change the timing or amount of contractual cash flows such that it would not meet this condition. In making the assessment, the Bank considers:

- contingent events that would change the amount and timing of cash flows;
- leverage features;
- prepayment and extension terms;
- terms that limit the Bank's claim to cash flows from specified assets (e.g. non-recourse asset arrangements); and
- features that modify consideration of the time value of money – e.g. periodical reset of interest rates.

#### **Initial recognition of financial assets and liabilities**

The Bank recognises financial assets and liabilities in its statement of financial position when it becomes a party to the contractual obligations of the instrument. Regular way purchases and sales of financial assets and liabilities are recognised using settlement date accounting.

Financial assets and liabilities are initially recognised at fair value plus, in the case of a financial asset or financial liability not at fair value through profit or loss, transaction costs that are directly attributable to the acquisition or issue of the financial asset or financial liability. Transaction costs directly attributable to the acquisition of financial assets or financial liabilities at fair value through profit or loss are recognised immediately in profit or loss. The accounting policies for subsequent re-measurement of these items are disclosed in the respective accounting policies set out below.

## NATIONAL BANK OF GEORGIA

### NOTES TO THE FINANCIAL STATEMENTS AS AT AND FOR THE YEAR ENDED 31 DECEMBER 2023 *(in thousands of Georgian Lari)*

---

#### Derecognition of financial assets and liabilities

##### *Financial assets*

The Bank derecognises a financial asset only when the contractual rights to the cash flows from the asset expire, or when it transfers the financial asset in a transaction in which substantially all the risks and rewards of ownership of the financial asset are transferred to another party or in which the Bank neither transfers nor retains substantially all the risks and rewards of ownership and it does not retain control of the financial asset. If the Bank neither transfers nor retains substantially all the risks and rewards of ownership and continues to control the transferred asset, the Bank recognises its retained interest in the asset and an associated liability for amounts it may have to pay. If the Bank retains substantially all the risks and rewards of ownership of a transferred financial asset, the Bank continues to recognise the financial asset and also recognises a collateralised borrowing for the proceeds received.

On derecognition of a financial asset in its entirety, the difference between the asset's carrying amount and the sum of the consideration received and receivable and the cumulative gain or loss that had been recognised in other comprehensive income and accumulated in equity is recognised in profit or loss.

On derecognition of a financial asset other than in its entirety (e.g. when the Bank retains an option to repurchase part of a transferred asset), the Bank allocates the previous carrying amount of the financial asset between the part it continues to recognise under continuing involvement, and the part it no longer recognises on the basis of the relative fair values of those parts on the date of the transfer. The difference between the carrying amount allocated to the part that is no longer recognised and the sum of the consideration received for the part no longer recognised and any cumulative gain or loss allocated to it that had been recognised in other comprehensive income is recognised in profit or loss. A cumulative gain or loss that had been recognised in other comprehensive income is allocated between the part that continues to be recognised and the part that is no longer recognised on the basis of the relative fair values of those parts.

##### *Financial liabilities*

The Bank derecognises financial liabilities when, and only when, the Bank's obligations are discharged, cancelled or they expire. Where an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification, is treated as a derecognition of the original liability and the recognition of a new liability. The difference between the carrying amount of the financial liability derecognised and the consideration paid and payable is recognised in profit and loss.

#### Measurement principles

##### *Fair value*

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date in the principal, or in its absence, the most advantageous market to which the Bank has access at that date. The fair value of a liability reflects its non-performance risk.

When available, the Bank measures the fair value of an instrument using quoted prices in an active market for that instrument. A market is regarded as active, if transactions for the asset or liability take place with sufficient frequency and volume to provide pricing information on an ongoing basis.

When there is no quoted price in an active market, the Bank uses valuation techniques that maximise the use of relevant observable inputs and minimise the use of unobservable inputs. The chosen valuation technique incorporates all the factors that market participants would take into account in these circumstances.

## NATIONAL BANK OF GEORGIA

### NOTES TO THE FINANCIAL STATEMENTS AS AT AND FOR THE YEAR ENDED 31 DECEMBER 2023

*(in thousands of Georgian Lari)*

---

The best evidence of the fair value of a financial instrument at initial recognition is normally the transaction price, i.e., the fair value of the consideration given or received. If the Bank determines that the fair value at initial recognition differs from the transaction price and the fair value is evidenced neither by a quoted price in an active market for an identical asset or liability nor based on a valuation technique that uses only data from observable markets, the financial instrument is initially measured at fair value, adjusted to defer the difference between the fair value at initial recognition and the transaction price. Subsequently, that difference is recognised in profit or loss on an appropriate basis over the life of the instrument, but no later than when the valuation is supported wholly by observable market data or the transaction is closed out.

The Bank uses quoted market prices to determine fair value of the Bank's investment securities. The quoted market prices for international securities are provided daily by Bloomberg and are based on current bid prices. In Management's opinion, such prices reflect reasonably the value of investments in international securities, considering the current market information and the accounting policies established by the Bank's Management.

If the market for investments is not active, the Bank establishes fair value by using discounted cash flow analysis and other relevant valuation techniques. Valuation techniques include using recent arm's length market transactions between knowledgeable, willing parties, reference to the current fair value of another instrument that is substantially the same and discounted cash flow analysis, making maximum use of market inputs and relying as little as possible on entity-specific inputs.

#### *Amortised cost*

The amortised cost of a financial asset or liability is the amount at which the financial asset or liability is measured at initial recognition, minus principal repayments, plus or minus the cumulative amortisation using the effective interest method of any difference between the initial amount recognised and the maturity amount, minus any reduction for cumulative allowance for expected credit losses. Premiums and discounts, including initial transaction costs, are included in the carrying amount of the related instrument and amortised based on the effective interest rate of the instrument.

### **Financial assets**

#### *Cash and cash equivalents*

Cash and cash equivalents consist of cash on hand in foreign currency, unrestricted balances on correspondent accounts and amounts due from financial institutions, including time deposit accounts and overnight deposits, that mature within ninety days from the date of origination. Cash and cash equivalents are subsequently measured at amortised cost.

#### *Membership in the International Monetary Fund (the "IMF") and other international financial institutions*

Based on the provision of Article 5 of the Law, being the representative of Georgia, the Bank may undertake obligations and carry out operations related to participation of Georgia in the activities of international organizations (i.e. the IMF, World Bank), including payment of membership fees to such organizations.

#### *Financial assets measured at amortised cost*

In the normal course of business, the Bank maintains loans, deposit, current accounts, and other receivables for various periods with financial institutions. Objective of the business model under which these assets are managed is achieved by collecting contractual cash flows. Contractual terms of these assets give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding. Amounts due from financial institutions and other financial assets are considered in this category. The Bank's investments measured at amortised cost also include Georgian Government bonds.

## NATIONAL BANK OF GEORGIA

### NOTES TO THE FINANCIAL STATEMENTS AS AT AND FOR THE YEAR ENDED 31 DECEMBER 2023

*(in thousands of Georgian Lari)*

---

Any premium or discount of the instruments representative of debt measured at amortised cost is recognised with the calculation of the amortised cost by applying the effective interest rate method, recognising the accrued interest in respective caption of the statement of profit or loss and other comprehensive income. The effective interest method uses the rate inherent in a financial instrument that discounts the estimated future cash flows over the expected life of the financial instrument so as to recognise interest on a constant-yield basis.

#### *Investments measured at fair value through profit or loss*

The Bank's investments measured at FVTPL comprise part of international reserves managed by the Bank for International Settlements ("BIS") which represent investments placed in the Bank for International Settlements Investment Pool (BISIP CNY). The objective of the business model under which the investment is managed is achieved by collecting contractual cash flows. However, contractual terms do not give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

#### *Derivative financial instruments*

The Bank uses interest rate futures and options contracts on overseas exchanges to manage interest rate risk on its portfolio of foreign securities. Exchange traded interest rate futures are futures contracts with an underlying instrument that pays interest, which allows the Bank to lock in the price of an interest-bearing asset for a future date. An interest rate option on exchange traded interest rate futures is a financial derivative that allows the holder to benefit from changes in interest rates. The Bank also uses foreign currency derivative instruments to manage currency risk for some of its foreign currency investments.

Interest rate futures and options positions are classified as at fair value through profit or loss (FVTPL). Derivatives are initially recognised at fair value at the date a derivative contract is entered into and are subsequently re-measured to their fair value at each reporting date. The positions are marked to market on the reporting date at the relevant bid price provided by Bloomberg and valuation gains and losses are taken to net unrealized gains/losses in the statement of profit or loss and other comprehensive income. Derivatives are carried as assets when their fair value is positive and as liabilities when it is negative.

#### *Investments measured at fair value through other comprehensive income*

The Bank's investments measured at FVOCI comprise debt securities issued by Georgian and foreign governments, international financial institutions and agencies. The securities are either part of the Bank's international reserve portfolio or represent monetary policy instruments. The objective of the business model under which the debt securities are managed is achieved by both collecting contractual cash flows and selling financial assets. The debt securities are classified as investments measured at FVOCI given that their contractual terms give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

#### **Expected credit losses**

The Bank recognises loss allowances for expected credit losses (ECL) on debt financial instruments that are measured at amortised cost or FVOCI.

The Bank measures loss allowances at an amount equal to lifetime ECL, except for the following, for which they are measured as 12-month ECL:

- debt investment securities that are determined to have low credit risk at the reporting date; and
- other financial instruments on which credit risk has not increased significantly since their initial recognition.

## NATIONAL BANK OF GEORGIA

### NOTES TO THE FINANCIAL STATEMENTS AS AT AND FOR THE YEAR ENDED 31 DECEMBER 2023

*(in thousands of Georgian Lari)*

---

The Bank considers debt investment securities to have low credit risk when their credit risk rating is equivalent to the globally accepted definition of 'investment grade'. Considering the Bank's strict investment guidelines, which allow for holding of only top credit-rated investments, financial instruments held as international reserves are considered to have low credit risk. In addition, the Bank considers exposure to the Georgian Government, which is denominated in Georgian Lari, to bear low credit risk. Such approach reflects the general assumption that sovereign debt denominated in national currency is considered to have a minimal risk of default (usually referred to as "risk-free" from market participant perspective) as well as the fact that due to the unique link between the Bank and the Government of Georgia, the Bank maintains the main current account of the Ministry of Finance of Georgia. The Bank does not apply the low credit risk exemption to any other financial instruments.

#### *ECL calculation*

Lifetime ECLs are the ECLs that result from all possible default events over the expected life of the financial instrument. 12-month ECL are the portion of ECL that result from default events on a financial instrument that are possible within the 12 months after the reporting date.

ECL are a probability-weighted estimate of credit losses. They are measured as follows:

- financial assets that are not credit-impaired at the reporting date: as the present value of all cash shortfalls (i.e. the difference between the cash flows due to the Bank in accordance with the contract and the cash flows that the Bank expects to receive). Shortfalls are estimated based on historical corporate and sovereign default and recovery rates;
- financial assets that are credit-impaired at the reporting date: as the difference between the gross carrying amount and the present value of estimated future cash flows.

#### *Credit-impaired financial assets*

At each reporting date, the Bank assesses whether financial assets carried at amortised cost and debt financial assets carried at FVOCI are credit-impaired financial assets. A financial asset is 'credit-impaired' when one or more events that have a detrimental impact on the estimated future cash flows of the financial asset have occurred. Evidence that a financial asset is credit-impaired includes the following observable data:

- significant financial difficulty of the borrower or issuer;
- a breach of contract such as a default or past due event;
- the restructuring of a loan or advance by the Bank on terms that the Bank would not consider otherwise;
- becoming probable that the borrower will enter bankruptcy or other financial reorganisation; or
- the disappearance of an active market for a security because of financial difficulties.

All financial assets measured at amortised cost or FVOCI, which are overdue for 90 days or more, are considered to be in default except for exposure to the Government of Georgia which would be considered to be in default if overdue for more 180 days. This represents a rebuttal of the presumption under IFRS 9 that the default does not occur later than when the financial asset is 90 days past due. However, it reflects the circumstances of the Government's budgetary approval processes and the Bank's unique relationship with the Government as it acts as the banker and fiscal agent of the Government.

#### *Presentation of allowance for ECL in the statement of financial position*

Loss allowances for ECL are presented in the statement of financial position as follows:

- financial assets measured at amortised cost: as a deduction from the gross carrying amount of the assets;
- debt instruments measured at FVOCI: no loss allowance is recognised in the respective caption of the statement of financial position because the carrying amount of these assets is their fair value. However, the loss allowance is disclosed and is recognised in the revaluation reserve of investments measured at fair value through other comprehensive income.

## NATIONAL BANK OF GEORGIA

### NOTES TO THE FINANCIAL STATEMENTS AS AT AND FOR THE YEAR ENDED 31 DECEMBER 2023

*(in thousands of Georgian Lari)*

---

#### *Write-offs*

Financial assets measured at amortised cost or FVOCI are written off (either partially or in full) when there is no reasonable expectation of recovering a financial asset in its entirety or a portion thereof. This is generally the case when the Bank determines that the borrower does not have assets or sources of income that could generate sufficient cash flows to repay the amounts subject to the write-off. This assessment is carried out at the individual asset level.

Recoveries of amounts previously written off are included in the caption for impairment (recovery)/charge in the statement of profit or loss and other comprehensive income.

#### **Financial liabilities measured at amortised cost**

Issued financial instruments or their components are classified as liabilities, where the substance of the contractual arrangement results in the Bank having an obligation either to deliver cash or another financial asset to the holder. Such instruments include amounts due to the Government, amounts due to resident financial institutions, amounts due to customers, debt securities issued, liabilities to the International Monetary Fund and other financial liabilities. These are initially recognised at fair value of the consideration received less directly attributable transaction costs. After initial recognition, these financial instruments are subsequently measured at amortised cost using the effective interest method.

#### **Money issued in circulation**

Money issued in circulation represents banknotes and coins issued by the Bank in accordance with the Law and its function as the central bank. Banknotes and coins in circulation are recorded in the statement of financial position at their nominal value net of cash in the Bank's cash desks.

The expenses for the production of notes and coins are expensed as incurred.

When notes and coins are returned to the Bank by the commercial banks, they are removed from money in circulation and depending on their condition or tender status, are either sent for destruction or held by the Bank as cash in vaults outside of the statement of financial position.

#### **Provisions (included in other liabilities)**

Provisions are recognised when the Bank has a present legal or constructive obligation as a result of past events, and it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate of the obligation can be made.

#### **Non-monetary gold and other precious metals (included in other assets)**

Gold investment coins and gold bars are recognised and subsequently measured in accordance with the requirements of IAS 2-*Inventories*. Gold investment coins and gold bars are initially measured at cost, including expenses on minting, transportation and other direct costs, subsequently measured at the lower of cost and net realizable value. When investment coins and bars are sold, respective income and expense is recorded in the statement of profit or loss and other comprehensive income. Expenses on other commemorative coins and bars are recognised as current expenses when produced and reflected in the statement of profit or loss and other comprehensive income.

#### **Property and equipment**

Property and equipment are carried at historical cost less accumulated depreciation and recognised impairment loss, if any. Land is not depreciated.

Where an item of property and equipment comprises major components having different useful lives, they are accounted for as separate items of property and equipment.

## NATIONAL BANK OF GEORGIA

### NOTES TO THE FINANCIAL STATEMENTS AS AT AND FOR THE YEAR ENDED 31 DECEMBER 2023

(in thousands of Georgian Lari)

Depreciation is charged on the historical cost of property and equipment and is designed to write off assets over their useful economic lives. Depreciation commences on the date of acquisition or, in respect of internally constructed assets, from the time an asset is completed and ready for use. Depreciation is charged to profit or loss on a straight-line basis at the following annual prescribed rates:

	%
Buildings	2
Computers, office equipment and fixtures	10-20
Vehicles and other	20

Expenses related to repairs and maintenance are charged when incurred and included in other expenses unless they qualify for capitalization.

The carrying amounts of property and equipment are reviewed at each reporting date to assess whether they are recorded in excess of their recoverable amounts. The recoverable amount is the higher of fair value less costs to sell and value in use. Where carrying values exceed the estimated recoverable amount, assets are written down to their recoverable amount; impairment is recognised in the respective period in the statement of profit or loss and other comprehensive income. After the recognition of an impairment loss the depreciation charge for property and equipment is adjusted in future periods to allocate the assets' revised carrying value, less its residual value (if any), on a systematic basis over its remaining useful life.

#### Intangible assets

Intangible assets include computer software and licenses.

Intangible assets acquired separately are measured on initial recognition at cost. Following initial recognition, intangible assets are carried at cost less any accumulated amortization and any accumulated impairment losses. The useful lives of intangible assets are assessed to be either finite or indefinite. Intangible assets with finite lives are amortised over the useful economic lives and assessed for impairment whenever there is an indication that the intangible asset may be impaired. Amortization periods and methods for intangible assets with finite useful lives are reviewed at least at each financial year-end.

#### Leases

From time to time, the Bank may lease particular assets for its administrative purposes.

The Bank recognises a right-of-use asset and a lease liability at the lease commencement date. The right-of-use asset is initially measured at cost, which comprises the initial amount of the lease liability adjusted for any lease payments made at or before the commencement date, plus any initial direct costs incurred and an estimate of costs to dismantle and remove any improvements made.

The right-of-use asset is subsequently depreciated using the straight-line method from the commencement date to the end of the lease term. In addition, the right-of-use asset is periodically reduced by impairment losses, if any, and adjusted for certain remeasurements of the lease liability.

The lease liability is initially measured at the present value of the lease payments that are not paid at the commencement date, discounted using the interest rate implicit in the lease or, if that rate cannot be readily determined, the Bank's incremental borrowing rate. Generally, incremental borrowing rate is used as the discount rate.

The lease liability is measured at amortised cost using the effective interest method. It is remeasured when there is a change in future lease payments or in assessment of whether the Bank will exercise extension or termination option. A corresponding adjustment is made to the carrying amount of the right-of-use asset, or the amount is recorded in profit or loss if the carrying amount of the right-of-use asset has been reduced to nil.

## NATIONAL BANK OF GEORGIA

### NOTES TO THE FINANCIAL STATEMENTS AS AT AND FOR THE YEAR ENDED 31 DECEMBER 2023

*(in thousands of Georgian Lari)*

---

The Bank presents right-of-use assets as separate line-item and lease liabilities in 'other liabilities' in the statement of financial position.

The Bank has elected not to recognise right-of-use assets and lease liabilities for leases of low-value items and short-term leases. The Bank recognises the lease payments associated with these leases as an expense on a straight-line basis over the lease term.

#### **Taxation**

According to the Law, assets, property and income of the Bank, as well as its activities and operations are exempt from all taxes and other levies.

#### **Contingencies**

Contingent liabilities are not recognised in the statement of financial position but are disclosed unless the possibility of any outflow in settlement is remote. A contingent asset is not recognised in the statement of financial position but disclosed when an inflow of economic benefits is probable.

#### **Recognition of income and expense**

Revenue is recognised when the Bank satisfies a performance obligation by transferring a promised good or service (i.e. an asset) to counterparties. An asset is transferred when (or as) the counterparties obtain control of that asset.

#### *Interest and similar income and expense*

For all financial instruments that are measured at amortised cost or fair value through other comprehensive income interest income or expense is recorded at the effective interest rate, which is the rate that exactly discounts estimated future cash receipts or payments through the expected life of the financial instrument or a shorter period, where appropriate, to the gross carrying amount of the financial asset or the amortised cost of financial liability. The calculation takes into account all contractual terms of the financial instrument (for example, prepayment options) and includes any fees or incremental costs that are directly attributable to the instrument and are an integral part of the effective interest rate, but not future credit losses. The gross carrying amount of the financial asset or the amortised cost of financial liability is adjusted if the Bank revises its estimates of payments or receipts. The adjusted carrying amount is calculated based on the original effective interest rate and the change in carrying amount is recorded as interest income or expense.

#### *Interest income recognition base*

The original effective interest rate is applied to the gross carrying amount (carrying amount without reduction by expected credit loss allowance) of financial assets for which:

- credit risk has not increased significantly since initial recognition;
- credit risk has increased significantly since initial recognition, but which are not credit-impaired.

For financial assets which are credit-impaired, the original effective interest rate is applied to the net carrying amount (carrying amount after reduction by expected credit loss allowance).

#### *Presentation of negative interest on financial assets and liabilities*

Negative interest on financial assets is considered as expense and is presented under interest expenses as a separate line-item. Similarly, negative interest on financial liabilities is considered as income and is presented under interest income as a separate line-item.

## NATIONAL BANK OF GEORGIA

### NOTES TO THE FINANCIAL STATEMENTS AS AT AND FOR THE YEAR ENDED 31 DECEMBER 2023

(in thousands of Georgian Lari)

#### *Fee and commission income and expense*

The Bank earns fee and commission income from a diverse range of services it provides to its counterparties. Fee and commission income includes cash operations fees and fund transfer fees, which are recognised as the services are provided. Fee and commission expense consists of cash operations, settlement fees and fees paid to the external manager, which are recognised as expense as the services are rendered.

#### **Foreign currency translation**

The financial statements are presented in Georgian Lari, which is the Bank's functional and presentation currency. Transactions in foreign currencies are initially recorded in the original currency and converted into the functional currency using the rate of exchange ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are translated at the functional currency rate of exchange ruling at the end of reporting date. Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates as at the dates of the initial transactions. Non-monetary items measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value was determined. Gains and losses resulting from the translation of foreign currency transactions are recognised in the statement of profit or loss and other comprehensive income as net gains/(losses) from foreign currencies - translation differences.

Differences between the contractual exchange rate of a transaction in a foreign currency and the Bank's exchange rate on the date of the transaction are included in net gains/(losses) from dealing in foreign currencies.

#### **Rates of exchange**

The exchange rates used by the Bank in the preparation of the financial statements as at year-end are as follows:

	<b>31-Dec-23</b>	<b>31-Dec-22</b>
GEL/1 US Dollar (USD)	2.6894	2.7020
GEL/1 Euro (EUR)	2.9753	2.8844
GEL/100 Japanese Yen (JPY)	1.8982	2.0495
GEL/1 Canadian Dollar (CAD)	2.0285	1.9959
GEL/1 Special Drawing Right (SDR)	3.6083	3.5959

#### **Offset of financial assets and liabilities**

Financial assets and liabilities are offset and reported net in the statement of financial position when the Bank has a legally enforceable right to set off the recognised amounts and the Bank intends either to settle on a net basis or to realise the asset and settle the liability simultaneously. In accounting for a transfer of a financial asset that does not qualify for de-recognition, the Bank does not offset the transferred asset and the associated liability. No offset of financial assets and liabilities have been made as of and during the reporting periods ended 31 December 2023 and 2022.

#### **Reclassification of financial assets**

Financial assets are not reclassified subsequent to their initial recognition, except in the period after the Bank changes its business model for managing these financial assets.

#### **Areas of significant management judgment and sources of estimation uncertainty**

The preparation of the Bank's financial statements requires management to make estimates and judgments that affect the reported amounts of assets and liabilities at the reporting date and the reported amount of income and expenses during the period ended. Management evaluates its estimates and judgments on an ongoing basis. Management bases its estimates and judgments on historical experience and on various other factors that are believed to be reasonable under the circumstances. Actual results may differ from these estimates under different assumptions or conditions.

## NATIONAL BANK OF GEORGIA

### NOTES TO THE FINANCIAL STATEMENTS AS AT AND FOR THE YEAR ENDED 31 DECEMBER 2023

(in thousands of Georgian Lari)

Significant areas of critical judgments and estimates are described in the following notes:

- Classification of financial assets: assessment of the business model within which the assets are held and assessment of whether the contractual terms of the financial assets are solely payments of principal and interest on the principal amount outstanding – Note 3;
- Application of low credit risk exemption and rebuttal of the presumption that the default does not occur later than when the financial asset is 90 days past due – Note 3;
- Fair valuation of financial instruments - Note 27.

### Application of new and revised International Financial Reporting Standards (IFRS)

#### New and revised standards:

The following are effective from 1 January 2023:

- IFRS 17 Insurance Contracts and amendments to IFRS 17 Insurance Contracts;
- Disclosure of Accounting Policies (Amendments to IAS 1 and IFRS Practice Statement 2) ;
- Definition of Accounting Estimates (Amendments to IAS 8);

The amendments mentioned above did not have significant effect on the Bank's financial statements.

The following new and amended standards are not expected to have a significant impact on the Bank's financial statements. The pronouncements are effective for annual periods beginning after 1 January 2023 and earlier application permitted:

- Classification of Liabilities as Current or Non-Current and Not-current Liabilities with Covenants (Amendments to IAS 1);
- Supplier Finance Arrangement (Amendments to IAS 7 and IFRS 7);
- Lack of Exchangeability (Amendments to IAS 21);
- Lease Liability in a Sale and Leaseback (Amendments to IFRS 16).

## 4. FEE AND COMMISSION INCOME AND EXPENSE

Fee and commission income and expense comprise:

	Year ended 31-Dec-23	Year ended 31-Dec-22
<b>Fee and commission income:</b>		
Funds transfer	4,483	3,765
Cash operations	1,547	1,193
Other	14	23
<b>Total fee and commission income</b>	<b>6,044</b>	<b>4,981</b>
<b>Fee and commission expense:</b>		
Fees paid to external manager	(1,627)	(1,635)
Custodian and settlement fees	(1,144)	(959)
Cash operations	(306)	(1,123)
<b>Total fee and commission expense</b>	<b>(3,077)</b>	<b>(3,717)</b>

The Bank owns and manages a real-time gross settlement system, which is an interbank payment system for national currency settlement operations. Funds transfer fee represents billing charges paid by the participants for settlement transactions.

## NATIONAL BANK OF GEORGIA

### NOTES TO THE FINANCIAL STATEMENTS AS AT AND FOR THE YEAR ENDED 31 DECEMBER 2023 (in thousands of Georgian Lari)

#### 5. OTHER INCOME

Other income comprises:

	Year ended 31-Dec-23	Year ended 31-Dec-22
Income from sale of commemorative coins	10,528	2,435
Revenue from fines	860	32
Other	408	985
<b>Other income</b>	<b>11,796</b>	<b>3,452</b>

Other expenses comprise:

	Year ended 31-Dec-23	Year ended 31-Dec-22
Expense related to commemorative coins	(8,448)	(3,108)
Other	(1,358)	(1,068)
<b>Other expenses</b>	<b>(9,806)</b>	<b>(4,176)</b>

#### 6. OPERATING EXPENSES

Operating expenses comprise:

	Year ended 31-Dec-23	Year ended 31-Dec-22
Salaries and bonuses	40,909	30,446
Paid vacation and sick leave	3,193	2,509
<b>Total personnel expenses</b>	<b>44,102</b>	<b>32,955</b>
Software maintenance fees	3,283	2,822
Subscription to information services	2,674	2,734
Social benefits expenses	2,624	2,297
Utilities	1,799	1,729
Business travel and related expenses	730	530
Security	717	527
Personnel training	638	196
Repairs and maintenance	478	210
Cash packing	412	53
Legal and consultancy	236	332
Fuel expenses	194	223
Other	1,891	1,616
<b>Total general and administrative expenses</b>	<b>15,676</b>	<b>13,269</b>
Depreciation charge (Note 15)	5,705	6,186
Amortization charge (Note 16)	1,788	2,024
<b>Total depreciation and amortization charges</b>	<b>7,493</b>	<b>8,210</b>

#### 7. CASH AND CASH EQUIVALENTS

Cash and cash equivalents as at 31 December 2023 and 2022 comprise:

	31-Dec-23	31-Dec-22
Cash on hand in foreign currencies	395,565	351,428
Current accounts	432,215	2,064,016
Time deposits with credit institutions	1,295,548	1,452,008
<b>Total cash and cash equivalents</b>	<b>2,123,328</b>	<b>3,867,452</b>

As at 31 December 2023 and 2022, GEL 1,544,705 thousand and GEL 3,042,432 thousand, respectively, were placed in current accounts and time deposits up to ninety days with seven (31 December 2022: seven) internationally recognised banks and central banks from the Organization of Economic Co-operation and Development member countries (OECD).

## NATIONAL BANK OF GEORGIA

### NOTES TO THE FINANCIAL STATEMENTS AS AT AND FOR THE YEAR ENDED 31 DECEMBER 2023 (in thousands of Georgian Lari)

As at 31 December 2023 and 2022, annual interest rate range of time deposits with credit institutions varied from 4% to 5.61% and 4.15% to 4.47%, respectively.

## 8. DUE FROM RESIDENT FINANCIAL INSTITUTIONS

Due from resident financial institutions as at 31 December 2023 and 2022 comprise:

	31-Dec-23	31-Dec-22
<b>Due from resident financial institutions under monetary policy instruments</b>		
Refinancing loans	3,003,152	2,442,215
Overnight loans	735,619	240,155
One-month open market instruments	-	401,219
Fixed rate loans	-	372,995
<b>Total due from resident financial institutions under monetary policy instruments</b>	<b>3,738,771</b>	<b>3,456,584</b>

Refinancing loans are the Bank's Monetary Policy instruments that are issued to Georgian commercial banks for liquidity purposes and have 7 days of maturity. Similar to refinancing loans, through one-month open market instruments, overnight loans and fixed rate loans the Bank supplies short-term liquidity to the national banking system.

As at 31 December 2023 and 2022, respectively, the Bank had a concentration of refinancing loans of GEL 2,662,792 thousand due from three resident commercial banks at annual interest rates of 9.571% - 9.5791%, and GEL 2,066,874 thousand due from three resident commercial banks at annual interest rates of 11% - 11.1020%, respectively.

As at 31 December 2023 and 2022, the Bank had a concentration of overnight loans of GEL 560,472 thousand due from one resident commercial bank at an annual interest rate of 10.25% and GEL 240,154 thousand due from one resident commercial bank at an annual interest rate of 11.75%, respectively.

As at 31 December 2023, the Bank did not have outstanding one-month open market instruments. As at 31 December 2022, the concentration of one-month open market instruments was GEL 328,698 thousand due from three resident commercial banks at annual interest rates of 11.067% - 11.23%.

As at 31 December 2023, the Bank did not have outstanding Fixed rate loans. As at 31 December 2022, the concentration of fixed rate loans was GEL 301,479 thousand due from two resident commercial banks at an annual interest rate of 11.0402%.

For none of the exposures due from resident financial institutions has credit risk increased significantly since initial recognition. For credit risk disclosure, see also Note 28.

### Collateral and other credit enhancements

The eligible type of collateral and criteria for each type of collateral is defined by the Council of the Bank.

The accepted types of collateral are: a) debt securities issued by the Bank and by the Government of Georgia, denominated in Georgian Lari; b) debt securities issued by international financial institutions, denominated in Georgian Lari; c) debt securities issued in accordance with the "Law of Georgia on Securities Market" by resident and non-resident legal entities and securities issued as a private placement till 1 January 2018, denominated in Georgian Lari, but excluding debt securities issued by the commercial banks operating in Georgia; d) claims to eligible loan assets of commercial banks; e) foreign currency deposits in the Bank; In special cases, the Council of the Bank may determine other type of assets for loan collateral; haircuts to each type of collateral are periodically defined by the Monetary Policy Committee (MPC) of the Bank to the nominal amount of eligible assets. The Bank has the first lien on borrowers' assets according to the Law.

## NATIONAL BANK OF GEORGIA

### NOTES TO THE FINANCIAL STATEMENTS AS AT AND FOR THE YEAR ENDED 31 DECEMBER 2023

(in thousands of Georgian Lari)

As at 31 December 2023 and 2022, types and fair values of financial assets pledged for amounts due from resident financial institutions were as follows:

	<u>31-Dec-23</u>	<u>31-Dec-22</u>
<b>Government securities (treasury bills/notes)</b>	2,353,661	1,386,426
<b>Loan portfolio of commercial banks</b>	1,839,284	2,320,899
<b>Bonds issued by International Financial Institutions and development banks, denominated in GEL:</b>		
Asian Development Bank (ADB)	138,462	-
Netherlands Development Finance Company	26,111	93,279
International Finance Corporation (IFC)	-	86,954
European Bank for Reconstruction and Development (EBRD)	-	83,446
<b>Bonds issued by the private sector</b>	35,264	37,808
	<u><b>4,392,782</b></u>	<u><b>4,008,812</b></u>

The Bank monitors the value of collateral, requests additional collateral in accordance with the underlying agreement, and monitors the value of collateral obtained during its review of the adequacy of the allowance for expected credit losses. As at 31 December 2023 and 2022, none of the financial instruments issued by the Bank were pledged as collateral.

## 9. SPECIAL DRAWING RIGHTS HOLDINGS WITH THE INTERNATIONAL MONETARY FUND

Balances with the International Monetary Fund (the "IMF") comprise:

	<u>31-Dec-23</u>	<u>31-Dec-22</u>
<b>Assets:</b>		
Special Drawing Rights (SDR) holdings	<u>1,214,799</u>	<u>1,249,154</u>
<b>Liabilities:</b>		
<b>IMF current accounts</b>		
Current account # 1	1,770	2,163
Current account # 2	10	12
	<u>1,780</u>	<u>2,175</u>
<b>Borrowings from the IMF</b>		
Extended Fund Facility (EFF)	1,083,861	1,159,590
General SDR allocation	1,137,494	1,130,877
Special SDR allocation	118,228	117,541
	<u>2,339,583</u>	<u>2,408,008</u>
<b>Total due to the IMF</b>	<u>2,341,363</u>	<u>2,410,183</u>
<b>Off-balance sheet balances:</b>		
IMF Quota	708,272	865,409
Security held in custody by the Bank in respect of IMF quota and as collateral of IMF granted facilities	(2,209,486)	(2,792,228)

### SDR Holdings

SDR holdings represent the account of the Bank with the IMF used for borrowings and settlements with the IMF. SDR holdings are primarily obtained from the SDR allocations provided by the IMF under its Articles of Agreement. Interest accrued in respect of SDR holdings is calculated using the rate set by the IMF weekly on the basis of short-term market rates in major money markets. The annual nominal interest rate range on the SDR holdings during 2023 and 2022 was 2.999%-4.198% and 0.050%-2.916%, respectively.

### IMF current accounts

The Bank is required to maintain two separate accounts: IMF current account number 1 and IMF current account number 2. IMF current account number 1 is for settlement of the IMF's operational transactions, whereas IMF current account number 2 is used for operational expenses incurred by the IMF in Georgian Lari.

## NATIONAL BANK OF GEORGIA

### NOTES TO THE FINANCIAL STATEMENTS AS AT AND FOR THE YEAR ENDED 31 DECEMBER 2023 (in thousands of Georgian Lari)

---

#### IMF granted facilities

Facilities received from the IMF include the Extended Fund Facility (EFF) loan with a carrying amount of GEL 1,083,861 thousand as at 31 December 2023 (31 December 2022: GEL 1,159,590 thousand). The EFF loan provides assistance to Georgian authorities in support of their comprehensive program to preserve macro and financial stability and advance structural reforms to bolster growth. The 36-month Extended Fund Facility (EFF) was approved on 12th of April 2017 with access to SDR 210.4 million (100 percent of quota). On 14th of April 2020, an augmentation of access to 130 percent of quota was approved, bringing total access under the EFF to SDR 484 million (230 percent of quota). No Funds were utilized under the facility by the Bank during 2023 and 2022. Repayments started in 2021 and the loan is scheduled to be fully repaid by 2031. The lending rate is tied to the IMF's market-related interest rate, known as the basic rate of charge linked to the Special Drawing Rights (SDR) interest rate, which amounted to 5.103% as at 31 December 2023 (31 December 2022: 3.916%).

All facilities received from the IMF are denominated in SDRs.

#### SDR allocations

The SDR allocation is an unsecured, interest-bearing distribution of SDRs by the IMF through general and special allocations. The general allocation is made by the IMF according to the Articles of Agreement to all participants in its SDR Department in proportion to countries' quotas in the IMF. General allocations to Georgia were made in 2009 (SDRs 111,419 thousand) and 2021 (SDR 201,658 thousand). In 2009, the Fourth Amendment to the IMF Articles of Agreement providing for a special one-time allocation of SDRs entered into force, according to which Special SDR allocation of SDR 32,540 thousand was made to Georgia. Members and prescribed holders may use their SDR holdings to conduct transactions with the IMF. The Bank treats the allocation as a foreign currency liability to the IMF.

Georgia, as a member country of the IMF and a recipient of the allocations, is obliged to pay to the IMF an amount equal to its net cumulative allocation and any other amounts that may be due and payable because of the membership termination or liquidation of the IMF's SDR Department.

The annual interest rate range on the SDR allocations throughout 2023 and 2022 varied within the ranges of 2.9160%-4.1980% and 0.050%-2.9160%, respectively.

#### IMF Quota

The IMF Quota of Special Drawing Rights (SDRs) of 210,400 thousand, represents the membership subscription of Georgia with the IMF which is non-interest bearing and is effective from 26 January 2016 as a result of the 14<sup>th</sup> General Review of Quotas by the Board of Governors of the IMF, the Fund's highest decision-making body. The IMF receives its resources from its member countries. Each member country of the IMF is assigned a quota, based broadly on its relative position in the world economy. A member's quota delineates basic aspects of its financial and organizational relationship with the IMF. As the Bank is the fiscal agent between the Government of Georgia and the IMF, this instrument is not presented in the statement of financial position.

#### Security held in custody by the Bank in respect of the IMF Quota and as collateral of the IMF granted facilities

As at 31 December 2023, security held in custody comprises GEL 708,272 thousand in respect of the IMF Quota and GEL 1,501,214 thousand held as collateral for the IMF granted facilities (GEL 2,209,486 thousand).

As at 31 December 2022 security held in custody comprises GEL 865,409 thousand in respect of the IMF Quota and GEL 1,926,819 thousand held as collateral for the IMF granted facilities (GEL 2,792,228 thousand in total).

The security was issued by the Government of Georgia in 1992 in settlement of the IMF Quota. The security used as collateral includes the total nominal value of the IMF granted facilities to Georgia: to the Bank and to the Government. As this security is held by the Bank in custody, it is accounted for as an off-balance sheet item and presented at nominal value.

## NATIONAL BANK OF GEORGIA

### NOTES TO THE FINANCIAL STATEMENTS AS AT AND FOR THE YEAR ENDED 31 DECEMBER 2023 (in thousands of Georgian Lari)

#### 10. ASSETS AND LIABILITIES RELATED TO DERIVATIVE INSTRUMENTS

	Book value	Notional principal	Book value	Notional principal
	31-Dec-23	31-Dec-23	31-Dec-22	31-Dec-22
<b>Assets related to derivative instruments under international reserve management</b>				
<b>Interest rate futures</b>				
Futures margin	4,575		10,282	
<b>FX-Forwards</b>				
FX-Forward assets	-		2,702	
Amount receivable	-	-	-	488,381
Amount payable	-	-	-	(519,320)
<b>Net FX-Forward</b>	<b>-</b>	<b>-</b>	<b>2,702</b>	<b>(30,939)</b>
<b>Net interest futures</b>				
Interest rate futures assets	11,163	890,191	32,669	43,232
Interest rate futures liabilities	-	(1,452,276)	-	(4,571,514)
<b>Net interest futures position</b>	<b>11,163</b>	<b>(562,085)</b>	<b>32,669</b>	<b>(4,528,282)</b>
<b>Net assets related to derivative instruments under international reserve management</b>				
	<b>15,738</b>	<b>(562,085)</b>	<b>45,653</b>	<b>(4,559,221)</b>
<b>Assets related to derivative instruments under monetary policy operations</b>				
<b>FX SWAPS</b>				
FX SWAP assets	-		734	
FX-SWAP liabilities	-		(1,649)	
Amount receivable	-	-	-	385,822
Amount payable	-	-	-	(386,737)
<b>Net FX SWAPS</b>	<b>-</b>	<b>-</b>	<b>(915)</b>	<b>(915)</b>
<b>Net assets related to derivative instruments under monetary policy operations</b>				
	<b>-</b>	<b>-</b>	<b>(915)</b>	<b>(915)</b>

At their inception, derivatives often involve only a mutual exchange of promises with little or no transfer of consideration. However, these instruments frequently involve a high degree of leverage and are very volatile. A relatively small movement in the value of the asset, rate, or index underlying a derivative contract may have a significant impact on the profit or loss of the Bank.

The futures contracts are contractual agreements to buy or sell a specified financial instrument at a specific price and date in the future. The futures contracts are transacted in standardized amounts on regulated exchanges and are subject to daily cash margin requirements. The credit risk related to future contracts is considered minimal because the cash margin requirements of the exchange help ensure that these contracts are always honored and are settled on a net basis.

The Bank has been trading Eurodollar Futures since March 2012, as part of active portfolio management. In April 2023, Eurodollar futures have been converted into the corresponding SOFR (Secured Overnight Financing Rate) contracts. Both LIBOR and SOFR futures are listed on CME (Chicago Mercantile Exchange & Chicago Board of Trade), hence they are exchange traded and standardized. SOFR is based on transactions in the Treasury repurchase market and is preferable to LIBOR since it is based on data from observable transactions rather than estimated future borrowing rates.

## NATIONAL BANK OF GEORGIA

### NOTES TO THE FINANCIAL STATEMENTS AS AT AND FOR THE YEAR ENDED 31 DECEMBER 2023

*(in thousands of Georgian Lari)*

---

While three-month Eurodollar futures settle to a three-month LIBOR rate at the end of the contract, SOFR futures settle to the average of an overnight rate during the last three months prior to the expiration of the contract – referred to as the reference period of the contract. Despite this difference, SOFR futures share several characteristics with Eurodollar futures. Eurodollar futures and SOFR futures represent consecutive three-month forward segments of the yield curve – for unsecured borrowing in the case of Eurodollars and for secured borrowing in the case of SOFR. When trading CME futures, the Bank faces credit risk originating solely from the clearing house, where purchases and sales of futures contracts offset one another.

The Bank is taking positions in Eurodollars and SOFRs for hedging purposes, by means of buying/selling US Treasuries or Spread Products (Agency and Supranational Securities) and entering opposite positions of corresponding amounts of Eurodollar Futures, matching the risk (duration and curve). The main purpose of such strategies is to reduce the portfolio's exposure to interest rate risks and to benefit from credit spreads.

Both Eurodollar and SOFR futures held in the Bank's portfolio are not held for trading purposes, i.e. the Bank does not aim to generate profits from favorable movements in their prices.

From April 2020, in addition to standard refinancing loans, the Bank started to provide liquidity support to the market through FX SWAP operations. FX SWAP operations represent monetary policy instruments aimed at delivering liquidity to the market. Through the FX SWAP transactions, the Bank used to buy foreign currency with the national currency for a period of one month at a spot rate, provided that it was sold back at the predetermined forward rate.

## 11. INVESTMENTS MEASURED AT FAIR VALUE THROUGH PROFIT OR LOSS

As at 31 December 2023 and 2022, investments measured at fair value through profit or loss comprised funds managed by the BIS (Bank for International Settlements). The portfolio is related to the investment placed in the Bank for International Settlements Investment Pool (BISIP CNY), a fund comprising Chinese government bonds (CGBs), managed for the investment of international reserves of central banks, with the main objective of transferring know-how and providing consulting services to the Bank. The quota holders of the fund may request partial or complete withdrawal of their investments at any time.

As at 31 December 2023, carrying amount of funds managed by BIS amounted to GEL 272,264 thousand (31 December 2022: 272,372 thousand).

## NATIONAL BANK OF GEORGIA

### NOTES TO THE FINANCIAL STATEMENTS AS AT AND FOR THE YEAR ENDED 31 DECEMBER 2023 (in thousands of Georgian Lari)

## 12. INVESTMENTS MEASURED AT FAIR VALUE THROUGH OTHER COMPREHENSIVE INCOME

As at 31 December 2023 and 2022, investment securities measured at fair value through other comprehensive income comprised:

	31-Dec-23	31-Dec-22
<b>Government securities</b>		
US Department of Treasury, Washington	7,368,915	5,485,360
Government of Canada, Ottawa	301,315	343,123
Governments of France	132,185	-
Government of Germany	121,462	-
Government of Austria	85,859	-
Government of Finland	46,834	-
Government of Belgium	29,211	-
Government of the Netherlands	28,764	-
Grand Duchy of Luxembourg	28,624	-
Government of Denmark	22,394	-
Bank of Japan, Tokyo	-	172,194
	<b>8,165,563</b>	<b>6,000,677</b>
<b>Supranational securities</b>		
European Investment Bank, Luxembourg	185,663	264,265
Asian Development Bank, Manila	135,211	112,173
Inter-American Development Bank, Washington D.C.	119,946	69,571
African Development Bank, Abidjan	63,978	67,211
Nordic Investment Bank	52,789	-
European Bank for Reconstruction and Development	50,076	-
International Bank for Reconstruction & Development, Washington	31,749	25,946
European Union	28,985	-
Inter-American Investment Corporation	2,634	-
New Development Bank, Shanghai	2,885	5,685
EUROFIMA, Basel	1,641	-
European Stability Mechanism	-	104,878
Bank for International Settlements, Basle	-	94,291
	<b>675,557</b>	<b>744,020</b>
<b>Agency and other securities</b>		
CPPIB Capital Inc, Toronto	115,137	86,104
Oesterreichische Kontrollbank AG, Vienna	78,498	36,417
Nederlandse Waterschapsbank N.V.	73,159	68,789
Province of Quebec Canada, Quebec	72,267	31,673
Caisse D'Amortissement de la Dette Sociale	72,117	-
Province of Ontario Canada, Toronto	57,108	36,167
Svensk Exportkredit AB, Stockholm	49,062	75,254
Kommunalbanken AS	42,411	-
Bank Nederlandse Gemeenten, Den Haag	38,599	41,868
Agence Francaise de Developpement	36,885	-
Kreditanstalt fuer Wiederaufbau, Frankfurt	35,237	84,065
Erste Abwicklungsanstalt, Dusseldorf	34,252	78,323
Landeskreditbank Baden-Wuerttemberg Foerderbank	32,758	28,925
Municipality Finance PLC	31,121	-
OMERS Finance Trust	29,090	38,466
CDP Financial In, Montreal	27,114	28,770
North Rhine-Westphalia	13,803	43,968
Kommuninvest I Sverige AB, Orebro	8,420	105,977
Korean Development Bank	7,687	61,687
Japan Bank for International Cooperation, Otemachi	-	74,666
Province of Alberta Canada	-	48,282
Other	150,776	95,123
	<b>1,005,501</b>	<b>1,064,524</b>
<b>Total investments measured at fair value through other comprehensive income in foreign currency</b>	<b>9,846,621</b>	<b>7,809,221</b>
<b>Marketable government securities in national currency</b>		
Georgian government bonds	2,668,266	2,272,589
<b>Total investments measured at fair value through other comprehensive income in national currency</b>	<b>2,668,266</b>	<b>2,272,589</b>

## NATIONAL BANK OF GEORGIA

### NOTES TO THE FINANCIAL STATEMENTS AS AT AND FOR THE YEAR ENDED 31 DECEMBER 2023

(in thousands of Georgian Lari)

Analysis of interest rates (coupon) and maturities on investments measured at fair value through other comprehensive income comprise:

	31-Dec-23		31-Dec-22	
	Interest rate p.a.	Maturity	Interest rate p.a.	Maturity
<b>In foreign currency:</b>				
Government securities	0.125%-6.75%	2024-2027	0.125%-2.875%	2023-2026
Supranational securities	0.25%-4.875%	2024-2027	0.25%-4.125%	2023-2027
Agency and other securities	0.25%-5.66%	2024-2028	0.25%-4.75%	2023-2027
<b>In national currency:</b>				
Government bonds	7%-11.6%	2024-2030	7%-11.6%	2023-2028

Investments measured at fair value through other comprehensive income include funds managed under the RAMP program, which corresponds to the outsourcing of the management of a portion of the international reserves to the World Bank treasury specialized in portfolio management (external manager), with the main objective of transferring know-how and providing consulting services to the Bank. The manager receives a management fee, established in the contract, and is evaluated based on the net asset value of the transferred funds. The assets within the external manager portfolio are held on behalf of the Bank, under the responsibility of a global custodian selected for the purpose of investing in and reinvesting the securities. The Bank may, from time to time, by notice to the external manager, make additions to, or reductions of, the investment amount. As at 31 December 2023, fair value of funds managed under the RAMP amounted to GEL 615,261 thousand (31 December 2022: GEL 597,133 thousand).

For none of the financial assets measured at fair value through other comprehensive income has credit risk increased significantly since initial recognition, see also Note 28.

### 13. INVESTMENTS MEASURED AT AMORTISED COST

	31-Dec-23		31-Dec-22	
	Carrying value	Nominal value	Carrying value	Nominal value
<b>Georgian Government securities</b>				
Georgia government bonds	81,194	80,846	121,390	120,846
<b>Total investments measured at amortised cost in national currency</b>	<b>81,194</b>	<b>80,846</b>	<b>121,390</b>	<b>120,846</b>

Analysis of interest rate (coupon) and maturity of investments measured at amortised cost:

	31-Dec-23		31-Dec-22	
	Interest rate p.a.	Maturity	Interest rate p.a.	Maturity
Georgian government bonds	9.566%	2024-2025	9.549%	2023-2025

Georgian government bonds denominated in the national currency represent interest-bearing securities issued by the Ministry of Finance of Georgia according to the agreement formed between the Government of Georgia and the Bank in March, 2006 to convert, without cash settlement, borrowings of the Government of Georgia into debt securities. The security was issued exclusively for the Bank and is a non-transferable, a non-tradable instrument. Therefore, the investment is carried at amortised cost. The government bonds are repaid by issuance of new bond instrument in the amount of GEL 40,000 thousand annually, which are classified as investments measured at fair value through other comprehensive income. Interest rate of the bond is subject to annual repricing considering market rates.

For none of the financial assets measured at amortised cost has credit risk increased significantly since initial recognition, see also Note 28.

## NATIONAL BANK OF GEORGIA

### NOTES TO THE FINANCIAL STATEMENTS AS AT AND FOR THE YEAR ENDED 31 DECEMBER 2023

(in thousands of Georgian Lari)

#### 14. RIGHT-OF-USE ASSET

The Bank leases premises for administrative purposes for part of its personnel and recognises respective right-of-use asset and lease liability.

Change in the outstanding balance of the related right-of-use asset is provided below:

	2023	2022
<b>Balance as at 1 January</b>	<b>1,537</b>	<b>387</b>
Increase in right-of-use asset	-	2,108
Depreciation charge for the year	(1,054)	(958)
<b>Balance as at 31 December</b>	<b>483</b>	<b>1,537</b>

Change in outstanding balance of lease liability is provided below:

	2023	2022
<b>Balance as at 1 January</b>	<b>1,576</b>	<b>373</b>
Remeasurement of lease liability	-	2,108
Interest expense for the year	119	117
Repayments for the year	(1,176)	(1,020)
<b>Balance as at 31 December</b>	<b>519</b>	<b>1,576</b>

#### 15. PROPERTY AND EQUIPMENT

	Land and buildings	Computers, office equipment and fixtures	Vehicles and other	Assets under construction	Total
<b>At initial cost:</b>					
<b>1-Jan-22</b>	<b>52,848</b>	<b>18,651</b>	<b>26,276</b>	<b>36</b>	<b>97,811</b>
Additions	-	2,293	795	-	3,088
Disposals	-	(434)	(451)	-	(885)
<b>31-Dec-22</b>	<b>52,848</b>	<b>20,510</b>	<b>26,620</b>	<b>36</b>	<b>100,014</b>
Additions	-	207	2,955	-	3,162
Disposals	-	(274)	(58)	-	(332)
<b>31-Dec-23</b>	<b>52,848</b>	<b>20,443</b>	<b>29,517</b>	<b>36</b>	<b>102,844</b>
<b>Accumulated depreciation:</b>					
<b>1-Jan-22</b>	<b>(9,387)</b>	<b>(12,632)</b>	<b>(18,495)</b>	-	<b>(40,514)</b>
Depreciation charge	(1,054)	(2,644)	(2,489)	-	(6,187)
Disposals	-	407	407	-	814
<b>31-Dec-22</b>	<b>(10,441)</b>	<b>(14,869)</b>	<b>(20,577)</b>	-	<b>(45,887)</b>
Depreciation charge	(1,054)	(2,539)	(2,112)	-	(5,705)
Disposals	-	269	54	-	323
<b>31-Dec-23</b>	<b>(11,495)</b>	<b>(17,139)</b>	<b>(22,635)</b>	-	<b>(51,269)</b>
<b>Carrying amounts:</b>					
<b>As at 31 December 2023</b>	<b>41,353</b>	<b>3,304</b>	<b>6,882</b>	<b>36</b>	<b>51,575</b>
<b>As at 31 December 2022</b>	<b>42,407</b>	<b>5,641</b>	<b>6,043</b>	<b>36</b>	<b>54,127</b>

## NATIONAL BANK OF GEORGIA

### NOTES TO THE FINANCIAL STATEMENTS AS AT AND FOR THE YEAR ENDED 31 DECEMBER 2023

(in thousands of Georgian Lari)

#### 16. INTANGIBLE ASSETS

	<b>Software and other</b>
<b>At cost:</b>	
<b>1-Jan-22</b>	<b>17,560</b>
Additions	1,906
Disposals	(299)
<b>31-Dec-22</b>	<b>19,167</b>
Additions	5,728
Disposals	(429)
<b>31-Dec-23</b>	<b>24,466</b>
<b>Accumulated amortization:</b>	
<b>1-Jan-22</b>	<b>(12,114)</b>
Charge for the year	(2,023)
Disposals	282
<b>31-Dec-22</b>	<b>(13,855)</b>
Charge for the year	(1,788)
Disposals	411
<b>31-Dec-23</b>	<b>(15,232)</b>
<b>Carrying amounts:</b>	
<b>As at 31 December 2023</b>	<b>9,234</b>
<b>As at 31 December 2022</b>	<b>5,312</b>

#### 17. OTHER ASSETS AND LIABILITIES

	<b>31-Dec-23</b>	<b>31-Dec-22</b>
<b>Other assets in foreign currency:</b>		
Prepayments	1,299	485
Other debtors	46	172
<b>Total other assets in foreign currency</b>	<b>1,345</b>	<b>657</b>
<b>Other assets in national currency:</b>		
Commemorative gold coins and gold bars	6,921	138
Prepayments	4,742	3,919
Inventory	521	487
Loans to employees	79	99
Other debtors	261	155
	<b>12,524</b>	<b>4,798</b>
Allowance for expected credit losses on other assets	(43)	(54)
<b>Total other assets in national currency</b>	<b>12,481</b>	<b>4,744</b>

As at 31 December 2023 and 2022, other financial assets, net of loss allowance, amounted to GEL 1,642 thousand and GEL 831 thousand, respectively.

Allowance for expected credit losses on other assets represents allowance for expected credit losses on loans to employees. The movements in allowance for expected credit losses are presented in Note 28.

Other liabilities comprise:

	<b>31-Dec-23</b>	<b>31-Dec-22</b>
<b>Other liabilities in foreign currency:</b>		
Amounts due to suppliers	3,145	8,083
Other liabilities	31,906	538
<b>Total other liabilities in foreign currency</b>	<b>35,051</b>	<b>8,621</b>
<b>Other liabilities in national currency:</b>		
Profit payable to the Ministry of Finance of Georgia	302,877	462,780
Amount due to suppliers	4,164	4,116
Liability for realized banknotes and coins	2,091	1,935
Lease liability (Note 14)	519	1,576
Deferred income	72	3,119
Other liabilities	1,982	1,657
<b>Total other liabilities in national currency</b>	<b>311,705</b>	<b>475,183</b>
<b>Total other liabilities</b>	<b>346,756</b>	<b>483,804</b>

## NATIONAL BANK OF GEORGIA

### NOTES TO THE FINANCIAL STATEMENTS AS AT AND FOR THE YEAR ENDED 31 DECEMBER 2023 (in thousands of Georgian Lari)

As at 31 December 2023, other financial liabilities amounted to GEL 43,807 thousand (31 December 2022: 17,905 thousand).

## 18. DUE TO RESIDENT FINANCIAL INSTITUTIONS

Due to resident financial institutions comprise:

	<u>31-Dec-23</u>	<u>31-Dec-22</u>
<b>Due to resident financial institutions under monetary policy instruments</b>		
Correspondent accounts in national currency	1,591,879	1,013,149
Overnight deposits in national currency	167,006	212,154
<b>Total due to resident financial institutions under monetary policy instruments in national currency</b>	<b>1,758,885</b>	<b>1,225,303</b>
Obligatory reserves of banks in foreign currency	4,312,166	5,499,478
<b>Total due to resident financial institutions under monetary policy instruments</b>	<b>6,071,051</b>	<b>6,724,781</b>
<b>Due to resident financial institutions, other</b>		
Correspondent accounts in foreign currency	14,040	217,265
<b>Total due to resident financial institutions, other</b>	<b>14,040</b>	<b>217,265</b>
<b>Total due to resident financial institutions</b>	<b>6,085,091</b>	<b>6,942,046</b>

As at 31 December 2023 and 2022, included in due to resident financial institutions are balances with the three largest local commercial banks of GEL 4,780,993 thousand and GEL 5,415,423 thousand, respectively, that represent 78.57% and 78.01% of the total balances due to resident financial institutions, respectively.

Resident commercial banks are required to maintain obligatory reserves with the Bank. As at 31 December 2023, obligatory reserves are calculated as 5% of their eligible liabilities denominated in national currencies (31 December 2022: 5%), and from 10% to 20% of their eligible liabilities denominated in foreign currencies, which depend on the deposit dollarization rate of a particular commercial bank (31 December 2022: from 10% to 25%).

For foreign currency borrowed funds with a remaining maturity of 1-2 years, the reserve requirement rates vary from 10% to 15%, depending on the deposit dollarization rate of a particular commercial bank (31 December 2022: 10% to 15%). As at 31 December 2023 and 2022, the annual interest rate on GEL denominated obligatory reserves was 9.5% and 11.0%, respectively. As at 31 December 2023 and 2022, annual interest rate on USD/EUR denominated obligatory reserves were 0.0%/0.0% and 0.0%/0.0% respectively. Borrowings with remaining maturities of over one year in the national currency and over two years in a foreign currency are exempt from reserve requirements.

## 19. DUE TO THE MINISTRY OF FINANCE

Amounts due to Ministry of Finance comprise:

	<u>31-Dec-23</u>	<u>31-Dec-22</u>
<b>Due to the Ministry of Finance of Georgia</b>		
Current accounts in foreign currency	753,038	623,860
Current account in national currency	1,692,692	1,155,878
<b>Total due to the Ministry of Finance of Georgia</b>	<b>2,445,730</b>	<b>1,779,738</b>

## NATIONAL BANK OF GEORGIA

### NOTES TO THE FINANCIAL STATEMENTS AS AT AND FOR THE YEAR ENDED 31 DECEMBER 2023 (in thousands of Georgian Lari)

## 20. DUE TO CUSTOMERS

Amounts due to customers comprise:

	<u>31-Dec-23</u>	<u>31-Dec-22</u>
<b>Due to customers in national currency</b>		
Due to the Deposit Insurance Agency	6,375	3,729
Due to international organizations	1,203	3,458
<b>Total due to customers in national currency</b>	<b><u>7,578</u></b>	<b><u>7,187</u></b>

## 21. MONEY ISSUED IN CIRCULATION

Money issued in circulation represents the amount of national currency of Georgia issued by the Bank. Movements during the year ended 31 December 2023 and 2022 were as follows:

	<u>2023</u>	<u>2022</u>
<b>Balance as at 1 January</b>	<b><u>5,040,547</u></b>	<b><u>4,589,034</u></b>
Banknotes issued into circulation	9,410,423	8,808,704
Coins issued into circulation	103,455	99,188
Banknotes withdrawn from circulation	(8,535,225)	(8,372,258)
Coins withdrawn from circulation	(85,062)	(84,121)
<b>Balance as at 31 December</b>	<b><u>5,934,138</u></b>	<b><u>5,040,547</u></b>

## 22. DEBT SECURITIES ISSUED

	<u>Interest rate p.a.</u>	<u>Maturity</u>	<u>Nominal value</u>	<u>Carrying value</u>
Certificates of deposit as at 31-Dec-23	9.00%-9.30%	25 Jan - 21 Mar, 2024	60,000	59,225
Certificates of deposit as at 31-Dec-22	9.96%-10.11%	26 Jan - 23 Mar, 2023	60,000	59,135

## 23. EQUITY

As stated in the Law, the Bank's capital is comprised of its subscribed and fully paid-up capital and reserve fund.

### Authorized capital

The authorized and fully paid-up capital of the Bank amounted to GEL 15,000 thousand as at 31 December 2023 and 2022.

### Capital management

The Bank defines capital as its total equity measured in accordance with IFRSs. Pursuant to Article 24 of the Law, net income of the Bank for each financial year is calculated as the sum of net operational profit or loss and unrealised gain or loss from revaluation. Net operational profit or loss shall be calculated after deducting from revenues of the reporting year all operating expenses intended for the core operations. Retained earnings are transferred to different reserves based on the requirements of the Law after approval of the Council. Following approval of the annual report of the Bank by the Council, the remaining portion of the retained earnings is transferred to the State budget within six months after the end of financial year.

## NATIONAL BANK OF GEORGIA

### NOTES TO THE FINANCIAL STATEMENTS AS AT AND FOR THE YEAR ENDED 31 DECEMBER 2023

*(in thousands of Georgian Lari)*

---

#### Reserve fund

According to the amended Article 25 of the Law, the Reserve Fund shall make up 15% of the reserve money, which comprises the national currency in cash put into circulation by the Bank together with the correspondent accounts of commercial banks in national currency and is established by allocations from the realised profit for the year, which comprises net profit for the year excluding net foreign currency translation and other revaluation gains and losses. The Council is entitled to determine the establishment of the Reserve Fund of less than 15% of the reserve money. ,

The Reserve Fund may only be used to offset losses of the Bank. Following the transfers to the Reserve Fund, the residual balance of realised profit of the Bank shall be transferred to the State Budget of Georgia.

In 2023 and 2022, the Bank transferred to reserve fund GEL 213,976 thousand and GEL 184,809 thousand from realized profits of 2023 and 2022 respectively.

In accordance with Article 25(c) of the Law, residual amount of GEL 302,877 thousand from realized profit of 2023 is distributed to the Ministry of Finance and will be paid within 6 months after reporting period end. Residual amount of GEL 462,780 thousand was distributed to Ministry of Finance from realized profit of 2022 and was transferred in 2023.

#### Foreign currency and other revaluation reserves

According to the Article 25(a) of the Law, the Bank transfers net unrealized gains from foreign currency revaluation to the foreign currency revaluation reserve and net unrealized gains arising from changes of the FVTPL financial assets' market prices are transferred to the revaluation reserve created for this purpose. These special reserves shall be used for counteracting (compensating) future losses.

During 2023, net unrealized gain on translation of foreign currencies of GEL 59,689 thousand was transferred from Retained Earnings to Foreign Currency Revaluation Reserve (2022: unrealized loss of GEL 475,157 thousand was transferred from Foreign Currency Revaluation Reserve to Retained Earnings). During 2023, other revaluation loss of GEL 17,384 thousand was transferred from Other Revaluation Reserve to Retained Earnings (2022: revaluation gain of GEL 34,647 thousand was transferred from Retained Earnings to Other Revaluation Reserve).

#### Revaluation reserve for investments measured at FVOCI

This reserve records fair value changes of investments measured at FVOCI.

## 24. COMMITMENTS AND CONTINGENCIES

In the normal course of operations, the Bank is a party to financial instruments with off-balance sheet commitments. The Bank uses the same risk management policies in undertaking off-balance sheet commitments as it does for on-balance operations.

#### Capital commitments

No material capital commitments were outstanding as at 31 December 2023 and 2022.

#### Operating environment

As an emerging market, Georgia does not possess a well-developed infrastructure that would generally exist in a more mature market economy. Therefore, especially sharp changes of operating environment (including global environment) could affect the Bank's results of operations and financial position in a manner not currently determinable.

## NATIONAL BANK OF GEORGIA

### NOTES TO THE FINANCIAL STATEMENTS AS AT AND FOR THE YEAR ENDED 31 DECEMBER 2023

(in thousands of Georgian Lari)

Over the last few years the Government of Georgia and the Bank have made a number of developments that positively affect the overall investment climate in Georgia, specifically implementing the reforms necessary for creating efficient banking, judicial, taxation and regulatory systems, as well as, using various measures to fulfill the liquidity needs of the economy and to stabilize the exchange rate of the national currency. This has resulted in a stable macroeconomic environment with higher real growth rates and inflow of foreign investments. The existing tendency aimed at the overall improvement of the economy is expected to persist.

However, future development of the economy of Georgia is largely dependent upon these reforms and developments, and the effectiveness of economic, financial and monetary measures undertaken by the Government and the Bank. Management believes that all the necessary measures are implemented to support the Bank's role in maintaining macroeconomic and financial stability.

#### Legal proceedings

The Bank is subject to legal actions and complaints. Management believes that the ultimate liability, if any, arising from such actions or complaints will not have a material effect on the financial position or the results of operations of the Bank. Management is of the opinion that no material unaccrued losses will be incurred and, accordingly, no provision has been made in these financial statements.

#### Credit commitments and contingent liabilities

As at 31 December 2023 and 2022, the Bank has no material credit commitments and contingent liabilities.

## 25. RELATED PARTY TRANSACTIONS

The Bank, as a state entity, is related to the Government of Georgia entities. To achieve its policy objectives, the Bank maintains a position of structural and functional independence from the Government of Georgia through its ability to fund its own operations without external assistance and through its management and governance.

Under key management personnel are regarded those persons having authority and responsibility for planning, directing and controlling the activities of the Bank, directly or indirectly. Key management personnel comprise the members of the Council, Chief Executive Officer and heads of departments.

In the normal course of its operations, the Bank enters into transactions with related parties, and material transactions and balances are presented in these financial statements, based on substance of the relationship, and not merely the legal form.

The Bank had the following transactions and outstanding balances with related parties:

	Year ended 31 December 2023		Year ended 31 December 2022	
	Related party transactions	Total category	Related party transactions	Total category
<b>Key management personnel compensation:</b>				
– short-term employee benefits	(5,528)	(44,102)	(4,459)	(32,955)

## NATIONAL BANK OF GEORGIA

### NOTES TO THE FINANCIAL STATEMENTS AS AT AND FOR THE YEAR ENDED 31 DECEMBER 2023

(in thousands of Georgian Lari)

	Notes	31-Dec-23		31-Dec-22	
		Related party balances	Total category	Related party balances	Total category
<b>Statement of financial position</b>					
<b>Assets:</b>					
Investments measured at fair value through other comprehensive income in national currency- <i>Government of Georgia</i>	12	2,668,266	2,668,266	2,272,589	2,272,589
Investments measured at amortised cost in national currency- <i>Government of Georgia</i>	13	81,194	81,194	121,390	121,390
Loans to employees-key management personnel	17	35	79	43	99
<b>Liabilities:</b>					
Due to the Ministry of Finance	19	2,445,730	2,445,730	1,779,738	1,779,738
Other Liabilities - <i>Profit payable to the Ministry of Finance of Georgia</i>	17	302,877	302,877	462,780	462,780
<b>Statement of profit or loss and other comprehensive income</b>					
Interest income		222,917	845,733	168,851	671,815
- <i>Government of Georgia</i>		222,916		168,850	
- <i>Key management personnel</i>		1		1	

In 2023, unrealized fair value gain on government securities measured at fair value through other comprehensive income amounted to GEL 2,436 thousand (2022: loss of GEL 5,863 thousand).

## NATIONAL BANK OF GEORGIA

### NOTES TO THE FINANCIAL STATEMENTS AS AT AND FOR THE YEAR ENDED 31 DECEMBER 2023 (in thousands of Georgian Lari)

## 26. LIABILITIES RELATED TO FINANCING ACTIVITIES

Table below shows reconciliation of movements of liabilities to cash flows arising from financing activities:

	Note	Cash movements			Non-cash movements		
		1-Jan-2023	Interest paid	Net proceeds from financing activities	Accrued interest	Translation differences	Distribution to the Ministry of Finance from 2023 profit
<b>Liabilities arising from financing activities:</b>							
Debt securities issued	22	59,135	(5,505)	(468)	6,063	-	59,225
Due to the International Monetary Fund	9	2,410,183	(97,756)	(79,863)	102,343	6,456	2,341,363
Other liabilities	23	462,780	-	(462,780)	-	-	302,877
<b>Liabilities arising from financing activities:</b>							
Debt securities issued	22	59,124	(6,032)	(585)	6,628	-	59,135
Due to the International Monetary Fund	9	2,948,217	(35,853)	(46,991)	46,347	(501,537)	2,410,183
Other liabilities	23	356,060	-	(356,060)	-	-	462,780

## NATIONAL BANK OF GEORGIA

### NOTES TO THE FINANCIAL STATEMENTS AS AT AND FOR THE YEAR ENDED 31 DECEMBER 2023 *(in thousands of Georgian Lari)*

---

## 27. FAIR VALUE OF FINANCIAL INSTRUMENTS

IFRS defines fair value as the price that would be received to sell an asset or paid to transfer a liability in orderly transactions between market participants at the measurement date.

### Fair value of the Bank's financial instruments measured at fair value on a recurring basis

Some of the Bank's financial instruments are measured at fair value at the end of each reporting period. The following table gives information about how the fair values of these financial assets are determined (in particular, the valuation techniques and inputs used).

Financial instruments measured at fair value are broken down for disclosure purposes into a three level fair value hierarchy based on the observability of inputs:

- Quoted prices in an active market (**Level 1**) – Valuations based on quoted prices in active markets that the Bank has the ability to access for identical assets or liabilities. Valuation adjustments and block discounts are not applied to these financial instruments. Since valuations are based on quoted prices that are readily and regularly available in an active market, valuations of these products do not require a significant amount of judgment. This level entails financial instruments under international reserve portfolio which are classified as derivative financial instruments, investments measured at fair value through profit or loss and investments measured at fair value through other comprehensive income. The instruments are valued on a daily basis, based on the bid prices obtained from Bloomberg at the closing of the markets of the current day.
- Valuation techniques using observable inputs (**Level 2**) – Valuations based on inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly. Level 2 inputs include the following:
  - a) quoted prices for similar assets or liabilities in active markets;
  - b) quoted prices for identical or similar assets or liabilities in markets that are not active;
  - c) inputs other than quoted prices that are observable for the asset or liability, for example:
    - interest rates and yield curves observable at commonly quoted intervals;
    - implied volatilities and
    - credit spreads;
  - d) market-corroborated inputs

Georgian government securities, measured at fair value through other comprehensive income, are measured using observable inputs under Level 2, in particular, market yields on similar securities issued by the Georgian government. For fair value assessment, a discounted cash flow model is used based on a current interest rate yield curve appropriate for the remaining term to maturity.

- Valuation techniques incorporating information other than observable market data (**Level 3**) – Valuations based on inputs that are unobservable and significant to the overall fair value measurement. The Bank does not have any financial instruments valued based on unobservable inputs.

The Bank considers that the accounting estimate related to valuation of financial instruments where quoted markets prices or other observable inputs are not available is a key source of estimation uncertainty because: (i) it is highly susceptible to change from period to period because it requires management to make assumptions about interest rates, volatility, exchange rates, the credit rating of the counterparty, valuation adjustments and specific feature of the transactions and (ii) the impact that recognising a change in the valuations would have on the assets reported in the statement of financial position as well as its profit or loss could be material.

## NATIONAL BANK OF GEORGIA

### NOTES TO THE FINANCIAL STATEMENTS AS AT AND FOR THE YEAR ENDED 31 DECEMBER 2023 (in thousands of Georgian Lari)

The table below analyses financial instruments measured at fair value at 31 December 2023 and 2022, by the level in the fair value hierarchy into which the fair value measurement is categorised. The amounts are based on the values recognised in the statement of financial position:

	Note	Fair value as at		Fair value hierarchy	Valuation techniques and key inputs	Significant unobservable inputs
		31-Dec-23	31-Dec-22			
<b>Financial Assets</b>						
<b>International reserves</b>						
Derivative financial assets	10	15,738	45,653	Level 1	Quoted bid prices in an active market	N/A
Investments measured at fair value through profit or loss	11	272,264	272,372	Level 1*	Quoted bid prices in an active market	N/A
Investments measured at fair value through other comprehensive income	12	9,846,621	7,809,221	Level 1	Quoted bid prices in an active market	N/A
<b>Monetary policy instruments</b>						
Investments measured at fair value through other comprehensive income	12	2,668,266	2,272,589	Level 2	Market interest rate for similar instruments	N/A
Derivative financial assets	10	-	734	Level 1	Quoted bid prices in an active market	N/A
<b>Financial liabilities</b>						
Derivative financial liabilities		-	1,649	Level 1	Quoted bid prices in an active market	N/A

\* The Bank's investments measured at fair value through profit or loss comprise a portion of international reserves managed by the Bank for International Settlements ("BIS"), which represents investments placed in the Bank for International Settlements Investment Pool (BISIP CNY). The investments represent instruments, which have quoted prices in active markets that the Bank has the ability to access for identical assets or liabilities. Therefore, the investment's fair valuation is considered to be Level 1 within fair value hierarchy.

There were no transfers between Level 1, 2 and 3 during the years ended 31 December 2023 and 2022.

Gains and losses included in other comprehensive income relate to investments measured at fair value through other comprehensive income and are reported as changes in revaluation reserve of investments measured at FVOCI.

Net unrealized gains/(losses) from securities and derivatives included in profit or loss relate to derivative financial assets and investments measured at fair value through profit or loss as changes in fair value during the reporting period.

#### **Fair value of financial assets and financial liabilities that are not measured at fair value on a recurring basis (but fair value disclosures are required)**

For fixed interest-bearing financial assets and liabilities that have a short-term maturity, it is assumed that the carrying amounts approximate their fair value. This assumption is also applied to demand deposits and savings accounts without maturity.

For variable interest-bearing financial assets (Georgian government bond classified as investments measured at amortized cost) and liabilities (borrowings from the IMF), it is assumed that the carrying amounts approximate their fair value. Moreover, management of the Bank believes that due to their specific nature, borrowings from the IMF represent a separate segment of borrowings from international financial organizations to support developing countries. As a result, these borrowings were considered to have been received in an "arm's length" transaction.

## NATIONAL BANK OF GEORGIA

### NOTES TO THE FINANCIAL STATEMENTS AS AT AND FOR THE YEAR ENDED 31 DECEMBER 2023 (in thousands of Georgian Lari)

## 28. RISK MANAGEMENT

### Introduction

The activities of the Bank are exposed to various types of risks. These include financial risks in the form of market, credit, and liquidity risks. The Bank's activities are also exposed to a diverse range of non-financial risks. Due to its unique role and functions, the Bank's risk management and control is not only based on the institutional risk and return considerations, but also takes into account the national interests, in line with its statutory responsibilities prescribed in the relevant legislation. The Bank views risk management as an integral part of overall management process and an essential element of good corporate governance. The Council of the Bank is ultimately responsible for the oversight of the risk management framework, overseeing the management of the key risks and reviewing its risk management policies and procedures.

To support the effective and efficient risk management system the Bank established a three lines of defense model. The model allocates clear roles and responsibilities for business departments, risk management, and internal audit.

### First line of defense: Departmental management

The first line of defense (the Bank's departments) is responsible to identify, assess, and manage the risks in their respective departments by designing, implementing and maintaining an adequate and effective systems of control.

### Second line of defense: Centralized risk management function

The second line of defense (Centralized Risk Management Department) is responsible to define and implement an effective non-financial risk management framework that is consistent with standards and approaches of best international practices. The Centralized Risk Management Department provides independent forward-looking assessment of the risks, facilitates, risk management processes and provides business continuity support. The department is accountable to the Governor of the Bank.

### Third line of defense: Internal audit

Internal Audit represents the third line of defense, which ensures the effectiveness, and appropriateness of the risk management and internal control systems. Internal audit examines both the adequacy of internal controls and the Bank's compliance with the procedures on a regular basis and reports its findings and recommendations to the Chairman of the Council.

### Organization of risk management department

Nature of risk	Management	Guidelines	Supervision
		policies issued by	
Financial risks	At department level	Monetary policy committee	Board
		International reserve management committee	
Non-financial risks	At department level	Centralized risk management department	Internal Audit, Audit Committee

### Financial risks

The Bank uses financial instruments as a means of achieving its monetary policy objectives and for managing international reserves. These two portfolios have different risk policies and characteristics, both of them are managed by the financial market department. The description of financial risks below presents the main risks to which these two portfolios of financial instruments are exposed, as well as the management policy of these risks.

### Credit risk

Credit risk is the risk that one party to a financial instrument will cause a financial loss for the other party by failing to discharge an obligation.

## NATIONAL BANK OF GEORGIA

### NOTES TO THE FINANCIAL STATEMENTS AS AT AND FOR THE YEAR ENDED 31 DECEMBER 2023 (in thousands of Georgian Lari)

The table below shows the maximum exposure to credit risk for financial instruments of the Bank for which impairment requirements are not applied:

	Notes	Maximum exposure 31-Dec-23	Maximum exposure 31-Dec-22
<b>Foreign currency assets</b>			
<b>International reserves</b>			
Assets related to derivative instruments	10	15,738	45,653
Investments measured at fair value through profit or loss	11	272,264	272,372
<b>National currency assets</b>			
<b>Monetary policy instruments</b>			
Assets related to derivative instruments	10	-	734
<b>Total credit risk exposure</b>		<b>288,002</b>	<b>318,759</b>

Exposure to credit risk for instruments where impairment requirements are applied are represented by carrying amounts of the respective assets in the statement of financial position.

#### International reserve portfolio

According to the Law, the Bank is eligible to hold and manage an international reserve portfolio. The Bank maintains a portfolio to support its monetary and exchange policies and normal functioning of domestic and foreign payments. Reserves are also employed to protect the country from external vulnerability by maintaining sufficient liquidity to absorb shocks during a financial crisis. Therefore, the multiple objectives of holding international reserves feature safety, liquidity, and profitability. Hence, assets under the international reserve portfolio are invested on a conservative basis to facilitate these objectives, with an emphasis on liquidity and capital preservation. For instance, the Bank's Investment Guidelines prioritizes the preservation of capital and a high level of liquidity of reserves. Once these conditions are met, return is to be maximized.

The portfolio is managed in line with investment guidelines approved by the Council. The Reserve Management Committee (the "Committee") of the Bank is responsible for monitoring and implementation of risk mitigation measures prescribed in the investment guidelines and making sure that the Bank operates within the established risk parameters. Typical activities of the Committee are reviewing the monthly reports, approving the list of eligible counterparties, approving changes to the strategy before submitting them to the Council and occasionally making important tactical decisions on asset allocation. The Risk Management and Control Division (the "Division") of the Bank is responsible for the overall day-to-day risk management and compliance functions, ensuring the implementation of common principles and methods for identifying, measuring, managing, and reporting risks.

#### Monetary policy portfolio

The monetary policy is executed mainly through financial instruments such as Georgian government securities, loans to commercial banks, certificates of deposit, minimum reserve requirements for commercial banks and derivative financial instruments. The monetary policy committee is responsible for monitoring and implementation of risk mitigation tools, such as collateral requirements for refinancing loans.

#### a) Financial instruments under the international reserves portfolio – internationally rated

In order to control the credit risk of the financial instruments used in the international reserves operations, the strategic asset allocation limits the exposures to credit risk of countries, counterparties and issuers, by setting concentration limits and minimum long-term credit rating, established by the international rating agencies (Standard & Poor's, Moody's and Fitch). For instance, investment guidelines define the minimum level of the credit rating for investing in any debt Instruments (Bonds, Bills) as well as for bank deposits and other financial instruments as A-. However, minimum credit rating of BBB is acceptable for counterparties used only for Nostro accounts.

## NATIONAL BANK OF GEORGIA

### NOTES TO THE FINANCIAL STATEMENTS AS AT AND FOR THE YEAR ENDED 31 DECEMBER 2023

(in thousands of Georgian Lari)

Additionally, the investment guidelines limit the concentration into non-benchmark financial instruments and the portfolio is diversified into various money market instruments, as well as fixed income and floating rate securities (Government Bonds, Agencies including Regional Governments and Supranational Securities) and other liquid, highly secure instruments.

While selecting the Bank's counterparties, the counterparty's credit rating, the country of its residence, the volume of its assets and capital, the experience of working in international markets and with corporate clients and the spectrum of the services and instruments offered to its clients are taken into consideration. In case of downgrade of the long-term credit rating of the Bank's counterparty by the above-mentioned rating agencies, the counterparty will be withdrawn from the list of eligible counterparties.

When different credit ratings are designated by the rating agencies (Standard & Poor's, Moody's and Fitch) for the assets, the second-best credit rating is used for credit risk assessment.

#### Credit quality analysis

The table below shows, by class of financial instruments, gross carrying amount of assets within the international reserve portfolio for which impairment requirements are applied according to second-best credit rating based on international ratings:

Second-best credit rating (credit ratings range)	31 December 2023				31 December 2022			
	12-month ECL	Lifetime ECL not credit-impaired	Lifetime ECL credit-impaired	Total	12-month ECL	Lifetime ECL not credit-impaired	Lifetime ECL credit-impaired	Total
<u>Cash and cash equivalents (excluding cash on hand)</u>								
AAA (from AA+ to AAA)	191,765	-	-	191,765	2,001,824	-	-	2,001,824
AA (from A+ to AA+)	894,257	-	-	894,257	479,552	-	-	479,552
A (from BBB+ to AA-)	641,741	-	-	641,741	1,034,648	-	-	1,034,648
<b>Gross carrying amount</b>	<b>1,727,763</b>	<b>-</b>	<b>-</b>	<b>1,727,763</b>	<b>3,516,024</b>	<b>-</b>	<b>-</b>	<b>3,516,024</b>
Loss allowance	-	-	-	-	-	-	-	-
<b>Net carrying amount</b>	<b>1,727,763</b>	<b>-</b>	<b>-</b>	<b>1,727,763</b>	<b>3,516,024</b>	<b>-</b>	<b>-</b>	<b>3,516,024</b>
<u>Special Drawing Rights holdings with the International Monetary Fund</u>								
AAA	1,214,799	-	-	1,214,799	1,249,154	-	-	1,249,154
<b>Gross carrying amount</b>	<b>1,214,799</b>	<b>-</b>	<b>-</b>	<b>1,214,799</b>	<b>1,249,154</b>	<b>-</b>	<b>-</b>	<b>1,249,154</b>
Loss allowance	-	-	-	-	-	-	-	-
<b>Net carrying amount</b>	<b>1,214,799</b>	<b>-</b>	<b>-</b>	<b>1,214,799</b>	<b>1,249,154</b>	<b>-</b>	<b>-</b>	<b>1,249,154</b>
<u>Investments measured at fair value through other comprehensive income</u>								
AAA (from AA+ to AA)	1,568,291	-	-	1,568,291	7,023,663	-	-	7,023,663
AA (from A+ to AAA)	8,275,847	-	-	8,275,847	534,904	-	-	534,904
A (from A to A+)	2,483	-	-	2,483	250,654	-	-	250,654
<b>Net carrying amount - fair value</b>	<b>9,846,621</b>	<b>-</b>	<b>-</b>	<b>9,846,621</b>	<b>7,809,221</b>	<b>-</b>	<b>-</b>	<b>7,809,221</b>
Loss allowance (recognised in other comprehensive income)	(1,789)	-	-	(1,789)	(236)	-	-	(236)

## NATIONAL BANK OF GEORGIA

### NOTES TO THE FINANCIAL STATEMENTS AS AT AND FOR THE YEAR ENDED 31 DECEMBER 2023 (in thousands of Georgian Lari)

#### b) Financial instruments under the monetary policy portfolio – internally rated

Credit risk is associated with open-market operations and facilities that inject liquidity to the financial system. The Bank's securities portfolio is comprised exclusively of securities issued by the Government of Georgia, considered as assets with low credit risk. To mitigate the risk associated with loans to banking institutions, the Bank requires collaterals eligible according to their credit quality, which are valued at market prices at the time of their receipt and subject to the application of discounts or haircuts according to the instrument specific characteristics. As at 31 December 2023 and 31 December 2022 credit rating of monetary policy instrument was assessed as AAA, in accordance with internally developed ratings (for expected credit loss estimation purposes, the internally rated AAA grade corresponds to BB grade, determined with the reference to country risk ratings, as established by the international rating agencies).

The Bank classifies its financial assets other than international reserves based on internally developed ratings as follows:

AAA grade – borrowers with excellent financial performance, having no changes in the terms and conditions of loan agreements and no overdue in principal and interest.

AA grade – borrowers with stable financial performance, having no changes in the terms and conditions of loan agreements and no overdue in principal and interest.

A grade – borrowers with satisfactory financial performance, having changes in the terms and conditions of loan agreements and no overdue in principal and interest.

B grade – loans issued to borrowers with satisfactory financial performance, having changes in the terms and conditions of loan agreements and overdue in principal and interest.

It is the Bank's policy to maintain accurate and consistent risk ratings across the credit portfolio. The attributed risk ratings are assessed and updated regularly.

The table below shows, by classes of financial instruments, gross carrying amounts of monetary policy and other financial assets, for which impairment requirements are applied, based on the Bank's internal credit rating system:

	31 December 2023			31 December 2022		
	12-month ECL	Lifetime ECL credit-impaired	Total	12-month ECL	Lifetime ECL credit-impaired	Total
<b>Foreign currency assets</b>						
<u>Other financial assets</u>						
AAA grade	1,300	-	1,300	485	-	485
A grade	39	-	39	166	-	166
B grade	6	-	6	6	-	6
<b>Gross carrying amount</b>	<b>1,345</b>	<b>-</b>	<b>1,345</b>	<b>657</b>	<b>-</b>	<b>657</b>
Loss allowance	-	-	-	-	-	-
<b>Net carrying amount</b>	<b>1,345</b>	<b>-</b>	<b>1,345</b>	<b>657</b>	<b>-</b>	<b>657</b>
<b>National currency assets</b>						
<u>Monetary policy instruments</u>						
<u>Due from resident financial institutions</u>						
AAA grade	3,738,771	-	3,738,771	3,456,584	-	3,456,584
<b>Gross carrying amount</b>	<b>3,738,771</b>	<b>-</b>	<b>3,738,771</b>	<b>3,456,584</b>	<b>-</b>	<b>3,456,584</b>
Loss allowance	-	-	-	-	-	-
<b>Net carrying amount</b>	<b>3,738,771</b>	<b>-</b>	<b>3,738,771</b>	<b>3,456,584</b>	<b>-</b>	<b>3,456,584</b>
<u>Investments measured at fair value through other comprehensive income</u>						
AAA grade	2,668,266	-	2,668,266	2,272,589	-	2,272,589
<b>Carrying amount - fair value</b>	<b>2,668,266</b>	<b>-</b>	<b>2,668,266</b>	<b>2,272,589</b>	<b>-</b>	<b>2,272,589</b>
<b>Other national currency assets</b>						
<u>Investments measured at amortized cost</u>						
AAA Grade	81,194	-	81,194	121,390	-	121,390
<b>Gross carrying amount</b>	<b>81,194</b>	<b>-</b>	<b>81,194</b>	<b>121,390</b>	<b>-</b>	<b>121,390</b>
Loss allowance	-	-	-	-	-	-
<b>Net carrying amount</b>	<b>81,194</b>	<b>-</b>	<b>81,194</b>	<b>121,390</b>	<b>-</b>	<b>121,390</b>
<u>Other financial assets</u>						
A Grade	298	-	298	200	-	200
B Grade	-	43	43	-	54	54
<b>Gross carrying amount</b>	<b>298</b>	<b>43</b>	<b>341</b>	<b>200</b>	<b>54</b>	<b>254</b>
Loss allowance	-	(43)	(43)	-	(54)	(54)
<b>Net carrying amount</b>	<b>298</b>	<b>-</b>	<b>298</b>	<b>200</b>	<b>-</b>	<b>200</b>

## NATIONAL BANK OF GEORGIA

### NOTES TO THE FINANCIAL STATEMENTS AS AT AND FOR THE YEAR ENDED 31 DECEMBER 2023

(in thousands of Georgian Lari)

The following table shows reconciliation of opening and closing balances of the loss allowance by classes of those financial instruments for which expected credit losses are recognised:

	2023			2022		
	12-month ECL	Lifetime ECL credit- impaired	Total	12-month ECL	Lifetime ECL credit- impaired	Total
<b>Foreign currency assets</b>						
<b>International reserves</b>						
<b>Investments measured at FVOCI</b>						
<b>Balance at 1 January</b>	<b>236</b>	-	<b>236</b>	<b>218</b>	-	<b>218</b>
New financial assets recognised	1,678	-	1,678	147	-	147
Remeasurement of loss allowance	34	-	34	(71)	-	(71)
Foreign exchange and other movements	-	-	-	(13)	-	(13)
Financial assets that have been derecognized - repayment	(159)	-	(159)	(45)	-	(45)
<b>Balance at 31 December</b>	<b>1,789</b>	-	<b>1,789</b>	<b>236</b>	-	<b>236</b>
<b>National currency assets</b>						
<b>Other national currency assets</b>						
<b>Other assets</b>						
<b>Balance at 1 January</b>	-	<b>54</b>	<b>54</b>	-	<b>74</b>	<b>74</b>
New financial assets recognized	-	-	-	-	-	-
Remeasurement of loss allowance	-	-	-	-	-	-
Financial assets that have been derecognized, including repayment	-	(11)	(11)	-	(20)	(20)
<b>Balance at 31 December</b>	-	<b>43</b>	<b>43</b>	-	<b>54</b>	<b>54</b>
<b>Total balance at 1 January</b>	<b>236</b>	<b>54</b>	<b>290</b>	<b>218</b>	<b>74</b>	<b>292</b>
<b>Total balance at 31 December</b>	<b>1,789</b>	<b>43</b>	<b>1,832</b>	<b>236</b>	<b>54</b>	<b>290</b>

#### Excessive risk concentration

Concentrations arise when a number of counterparties are engaged in similar business activities, or activities in the same geographic region, or have similar economic features that would cause their ability to meet contractual obligations to be similarly affected by changes in economic, political or other conditions. Concentrations indicate the relative sensitivity of the Bank's performance to developments affecting a particular industry or geographical location.

In order to minimize excessive concentrations of risks, the Bank's policies and procedures include specific guidelines to focus on maintaining a low credit risk profile. The concentration risks by counterparties and asset quality are disclosed in relevant notes to the financial statements.

## NATIONAL BANK OF GEORGIA

### NOTES TO THE FINANCIAL STATEMENTS AS AT AND FOR THE YEAR ENDED 31 DECEMBER 2023 (in thousands of Georgian Lari)

#### Geographical concentration

The Bank's financial assets and liabilities are generally concentrated in Georgia, except for the international reserve portfolio and borrowings from the IMF. The below table provides information on geographical concentration for these financial assets and liabilities outside of Georgia:

As at 31 December 2023	Notes	US	EU*	Australia	Canada	International	Other	Total
<b>Assets:</b>								
<b>International reserves</b>								
Cash and cash equivalents (excluding cash on hand)	7	276,571	892,093	5	2,271	-	556,823	1,727,763
Special Drawing Rights holdings with the IMF	9	-	-	-	-	1,214,799	-	1,214,799
Assets related to derivative instruments	10	-	-	-	-	-	15,738	15,738
Investments measured at fair value through profit or loss	11	-	-	-	-	272,264	-	272,264
Investments measured at fair value through other comprehensive income	12	7,375,570	920,995	24,516	696,230	646,573	182,737	9,846,621
		<b>7,652,141</b>	<b>1,813,088</b>	<b>24,521</b>	<b>698,501</b>	<b>2,133,636</b>	<b>755,298</b>	<b>13,077,185</b>
<b>Liabilities:</b>								
Due to the IMF	9	-	-	-	-	2,341,363	-	2,341,363
<b>Net position</b>		<b>7,652,141</b>	<b>1,813,088</b>	<b>24,521</b>	<b>698,501</b>	<b>(207,727)</b>	<b>755,298</b>	<b>10,735,822</b>
<b>As at 31 December 2022</b>								
<b>Assets:</b>								
<b>International reserves</b>								
Cash and cash equivalents (excluding cash on hand)	7	287,623	2,650,812	1	122	-	577,466	3,516,024
Special Drawing Rights holdings with the IMF	9	-	-	-	-	1,249,154	-	1,249,154
Assets related to derivative instruments	10	-	-	-	-	-	45,653	45,653
Investments measured at fair value through profit or loss	11	-	-	-	-	272,372	-	272,372
Investments measured at fair value through other comprehensive income	12	5,485,359	562,906	19,284	642,509	744,020	355,143	7,809,221
		<b>5,772,982</b>	<b>3,213,718</b>	<b>19,285</b>	<b>642,631</b>	<b>2,265,546</b>	<b>978,262</b>	<b>12,892,424</b>
<b>Liabilities:</b>								
Due to the IMF	9	-	-	-	-	2,410,183	-	2,410,183
<b>Net position</b>		<b>5,772,982</b>	<b>3,213,718</b>	<b>19,285</b>	<b>642,631</b>	<b>(144,637)</b>	<b>978,262</b>	<b>10,482,241</b>

\*EU-including Norwegian agency securities.

## NATIONAL BANK OF GEORGIA

### NOTES TO THE FINANCIAL STATEMENTS AS AT AND FOR THE YEAR ENDED 31 DECEMBER 2023 (in thousands of Georgian Lari)

#### Liquidity risk

Liquidity risk considers the risk that an entity will encounter difficulty in meeting obligations associated with financial liabilities that are settled by delivering cash or another financial asset.

#### c) Financial instruments under the international reserve portfolio

The purpose of the management of the liquidity risk is to ensure that the Bank fulfills all the financial commitments that it has assumed. Accordingly, the Bank diversifies maturities and also establishes limits aiming to ensure that the securities purchased may be traded in the secondary market without causing abrupt changes in the prices of the assets. Due to these guidelines, even securities with longer maturities have immediate liquidity.

The Bank's Monetary Policy and International Reserves Management Committees set limits on the minimum proportion of maturing funds available to cover cash outflows. The liquidity management policy of the Bank requires:

- Projecting cash flows by major currencies and considering the level of liquid assets necessary in relation thereto;
- Maintaining a diverse range of funding sources;
- Managing the concentration and profile of debts;
- Maintaining a portfolio of highly marketable assets that can easily be liquidated as protection against any interruption to cash flows; and
- Maintaining liquidity and funding contingency plans.

The Financial Markets Department receives information from business units regarding the liquidity profile of their financial assets and liabilities and details of other projected cash flows arising from projected future transactions. The Bank's liquidity risk relates to foreign currency cash flows.

The table below summarizes the maturity profile of the Bank's financial liabilities in foreign currency as at 31 December 2023 and 2022 based on contractual undiscounted repayment obligations. The financial assets in foreign currencies are presented in "less than 3 months" category on the basis that the Bank can realize them within the period not exceeding 3 months to meet the liquidity requirements:

As at 31 December 2023	Notes	Less than 3 months	3 to 12 months	1 to 5 years	Over 5 years	Total
<b>Foreign currency assets</b>						
<b>International Reserves</b>						
Cash and cash equivalents (excluding cash on hand)	7	1,727,763	-	-	-	1,727,763
Special Drawing Rights holdings with the IMF	9	1,214,799	-	-	-	1,214,799
Assets related to derivative instruments	10	15,738	-	-	-	15,738
Investments measured at fair value through profit or loss	11	272,264	-	-	-	272,264
Investments measured at fair value through other comprehensive income	12	9,846,621	-	-	-	9,846,621
<b>Other foreign currency assets</b>						
Other financial assets	17	1,345	-	-	-	1,345
<b>Total foreign currency assets</b>		<b>13,078,530</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>13,078,530</b>
<b>Foreign currency liabilities</b>						
Due to resident financial institutions	18	4,326,206	-	-	-	4,326,206
Due to the Ministry of Finance	19	753,038	-	-	-	753,038
Due to the IMF	9	1,270,910	150,068	867,732	256,110	2,544,820
Other liabilities	17	34,822	-	229	-	35,051
<b>Total foreign currency liabilities</b>		<b>6,384,976</b>	<b>150,068</b>	<b>867,961</b>	<b>256,110</b>	<b>7,659,115</b>
<b>Net position</b>		<b>6,693,554</b>	<b>(150,068)</b>	<b>(867,961)</b>	<b>(256,110)</b>	<b>5,419,415</b>

## NATIONAL BANK OF GEORGIA

### NOTES TO THE FINANCIAL STATEMENTS AS AT AND FOR THE YEAR ENDED 31 DECEMBER 2023

(in thousands of Georgian Lari)

As at 31 December 2022	Notes	Less than 3 months	3 to 12 months	1 to 5 years	Over 5 years	Total
<b>Foreign currency assets</b>						
<b>International Reserves</b>						
Cash and cash equivalents (excluding cash on hand)	7	3,516,024	-	-	-	3,516,024
Special Drawing Rights holdings with the IMF	9	1,249,154	-	-	-	1,249,154
Assets related to derivative instruments	10	45,653	-	-	-	45,653
Investments measured at fair value through profit or loss	11	272,372	-	-	-	272,372
Investments measured at fair value through other comprehensive income	12	7,809,221	-	-	-	7,809,221
<b>Other foreign currency assets</b>						
Other financial assets	17	172	-	485	-	657
<b>Total foreign currency assets</b>		<b>12,892,596</b>	<b>-</b>	<b>485</b>	<b>-</b>	<b>12,893,081</b>
<b>Foreign currency liabilities</b>						
Due to resident financial institutions	18	5,716,743	-	-	-	5,716,743
Due to the Ministry of Finance	19	623,860	-	-	-	623,860
Due to the IMF	9	1,260,572	268,578	662,156	422,807	2,614,113
Other liabilities	17	3,978	870	-	-	4,848
<b>Total foreign currency liabilities</b>		<b>7,605,153</b>	<b>269,448</b>	<b>662,156</b>	<b>422,807</b>	<b>8,959,564</b>
<b>Net position</b>		<b>5,287,443</b>	<b>(269,448)</b>	<b>(661,671)</b>	<b>(422,807)</b>	<b>3,933,517</b>

#### d) Financial instruments under the monetary policy portfolio

Considering the inherent characteristics of a monetary authority, which includes controlling the liquidity of the financial system, the Bank is not exposed to the limitations resulting from a mismatch between assets and liabilities in national currency

#### Market risk

Market risk is the risk that the value of financial instruments will fluctuate due to changes in market variables such as interest rates and foreign exchanges rates. Market risks comprise currency risk, interest rate risk and other price risk. Market risk arises from open positions in interest rate and currencies, which are exposed to general and specific market movements and changes in the level of volatility of market prices.

#### e) Financial instruments under the international reserve portfolio

Market risk implies possible losses due to variations in the prices of investments.

The Strategic Asset Allocation (SAA) process limits the market risk based on the risk tolerance of the Bank. Strategic benchmarks are defined for individual portfolios to maximize returns, after assessing various interest rate scenarios, while staying within the market risk limit. Currency exposures are defined based on the analysis of the foreign debt and diversification effects are also considered to decrease overall currency risk (refer to note on currency risk below).

All portfolios are actively managed versus strategic benchmarks. Active market risk versus benchmarks is defined during the risk budgeting process and active market risk limits are established for each portfolio through limiting ex-ante tracking error and duration deviation. Regular stress testing is conducted to assess resilience of active portfolios to market shocks.

Strategic Benchmark Durations and Active Market Risk Limits for the international reserve portfolio are as follows:

## NATIONAL BANK OF GEORGIA

### NOTES TO THE FINANCIAL STATEMENTS AS AT AND FOR THE YEAR ENDED 31 DECEMBER 2023

(in thousands of Georgian Lari)

Tranches	2023		2022	
	Benchmark Duration (Duration Deviation Limits)	Ex-Ante Tracking Error Limits	Benchmark Duration (Duration Deviation Limits)	Ex-Ante Tracking Error Limits
Liquidity Portfolio in USD*	1.5 year (+/-3 Months)	15 Basis Point	6 months (+/-3 Months)	15 Basis Point
Investment Portfolio in USD*	2 years (+/-3 Months)	30 Basis Point	9 months (+/-3 Months)	30 Basis Point
Investment Portfolio in CAD*	2 years (+/-3 Months)	30 Basis Point	9 months (+/-3 Months)	30 Basis Point
Investment Portfolio in EUR*	1 year (+/-3 Months)	30 Basis Point	-	-

\* Due to the annual SAA decision, the Benchmark Durations for the Liquidity and Investment Portfolios have increased from February 2023.

Market risk is monitored through daily measurement of the duration and composition of currencies, and by the follow-up of ex-ante tracking error. The international reserve management daily report, prepared by the Financial Markets Department, includes measurements of performance and risk in an absolute manner and as compared to a benchmark, and presents an evaluation of the implemented investment strategy.

The Bank's exposure to fair value interest rate risk arises principally through its investments in International Reserves portfolio, which are exposed to fluctuations because of changes in market interest rates.

Interest rate risk for Foreign Currency Reserves is the risk of changes in fair value of financial instruments due to changes in market interest rates.

The Bank's internally managed Foreign Currency Reserve's portfolio is divided into tranches and the Bank measures interest rate risk for its tranches, in all currencies, based on a 1% change in interest rates that indicates a change in the fair market value of financial instruments per 1% change in market yields. The fair market values of tranches held by the Bank are exposed to fluctuations, however these variations would not affect the ability of the Bank to fulfil its obligations.

#### Market yield sensitivity of the Bank's International Reserve tranches

The table shows the sensitivity of reserve tranches to a 1% increase or decrease in market yields to the asset values (figures are provided in thousands of USD):

Currency	2023		2022	
	Increase in market yield	Impact on equity	Increase in market yield	Impact on equity
Investment Tranche in USD	1%	(48,280)	1%	(13,872)
Investment Tranche in CAD	1%	(2,753)	1%	(836)
Investment Tranche in EUR	1%	(2,454)	-	-
Investment Tranche in CNY				
External (BIS)	1%	(3,278)	1%	(2,945)
Liquidity Tranche in USD	1%	(9,804)	1%	(3,121)
Working Capital Tranche in USD	1%	(8)	1%	(1,127)
Working Capital Tranche in EUR	1%	(49)	-	-

Currency	2023		2022	
	Decrease in market yield	Impact on equity	Decrease in market yield	Impact on equity
Investment Tranche in USD	1%	49,791	1%	14,114
Investment Tranche in CAD	1%	2,832	1%	850
Investment Tranche in EUR	1%	2,512	-	-
Investment Tranche in CNY				
External (BIS)	1%	3,278	1%	3,106
Liquidity Tranche in USD	1%	10,087	1%	3,172
Working Capital Tranche in USD	1%	8	1%	1,142
Working Capital Tranche in EUR	1%	49	-	-

## NATIONAL BANK OF GEORGIA

### NOTES TO THE FINANCIAL STATEMENTS AS AT AND FOR THE YEAR ENDED 31 DECEMBER 2023

(in thousands of Georgian Lari)

#### f) Financial instruments under the monetary policy portfolio

For open-market operations, this risk is mainly associated with changes in the market value of Georgian government bonds, and the change in value of collaterals received in liquidity injection transactions. For collaterals the risk of value loss is mitigated by using margins and haircuts that write-down their value and allow the effective amount lent to be lower than the collateral received.

#### Market yield sensitivity of the Bank's financial assets

Interest rate risk arises from the possibility that changes in interest rates will affect future cash flows or the fair value of financial instruments. The following table demonstrates the net effect of 1% change in interest rates, with all other variables held constant, on the Bank's statement of profit or loss and other comprehensive income, taking into account the effect of derivatives.

The sensitivity of equity is calculated by revaluing fixed-rate investments measured at fair value through other comprehensive income at 31 December 2023 and 2022 for 1% change in market interest rates:

	2023		2022	
	Increase in market yield	Impact on equity	Increase in market yield	Impact on equity
Georgian Government bonds	1%	(46,858)	1%	(42,195)

	2023		2022	
	Decrease in Market Yield	Impact on equity	Decrease in Market Yield	Impact on equity
Georgian Government bonds	1%	49,425	1%	43,913

#### Currency risk

Currency risk is the risk that the value of a financial instrument will fluctuate due to changes in foreign currency exchange rates. Subject to the currency profile of assets, the value of assets of the Bank is exposed to the risk of changes in exchange rates of major foreign currencies. Within the overall exposure and to a limited extent, foreign currency risk can be partially mitigated by holding assets across a diversified portfolio of currencies. Since 14 December 2015, the target currency composition is 80% USD, 10% EUR, 10% Other (Canadian dollars, Chinese yuan and other currencies up to 10%). Under SAA, +/-10% is allowed for the U.S. dollar, the Euro, and other currencies' target currency composition.

#### Sensitivity to foreign currency

The table below provides the concentration of the Bank's financial assets and liabilities by major currencies and analyses of the effect of a 1%, 5%, 10% and 15% movement of the currency rate against Georgian Lari, with all other variables held constant, on the statement of profit or loss and other comprehensive income. A negative amount in the table reflects a potential net reduction in the statement of profit or loss and other comprehensive income, while a positive amount reflects a net potential increase.

As at 31 December 2023	USD	EUR	SDR	JPY	CAD	Other	Total
Foreign currency assets	9,949,273	1,610,555	1,216,098	272,264	424,353	1,552	13,474,095
Foreign currency liabilities	(3,470,413)	(1,626,729)	(2,339,583)	-	-	(17,153)	(7,453,878)
<b>Net position</b>	<b>6,478,860</b>	<b>(16,174)</b>	<b>(1,123,485)</b>	<b>272,264</b>	<b>424,353</b>	<b>(15,601)</b>	<b>6,020,217</b>

## NATIONAL BANK OF GEORGIA

### NOTES TO THE FINANCIAL STATEMENTS AS AT AND FOR THE YEAR ENDED 31 DECEMBER 2023 (in thousands of Georgian Lari)

As at 31 December 2022	USD	EUR	SDR	JPY	CAD	Other	Total
Foreign currency assets	8,901,630	1,895,533	1,249,639	522,071	402,426	273,210	<b>13,244,509</b>
Foreign currency liabilities	(4,735,934)	(1,604,371)	(2,408,008)	-	-	(8,919)	<b>(8,757,232)</b>
<b>Net position</b>	<b>4,165,696</b>	<b>291,162</b>	<b>(1,158,369)</b>	<b>522,071</b>	<b>402,426</b>	<b>264,291</b>	<b>4,487,277</b>

#### Effect on total comprehensive income and equity

	2023						Total
	USD	EUR	SDR	JPY	CAD	Other	
Increase in currency rate of 1%	64,789	(162)	(11,235)	2,723	4,244	(156)	<b>60,203</b>
Increase in currency rate of 5%	323,943	(809)	(56,174)	13,613	21,218	(780)	<b>301,011</b>
Increase in currency rate of 10%	647,886	(1,617)	(112,349)	27,226	42,435	(1,560)	<b>602,021</b>
Increase in currency rate of 15%	971,829	(2,426)	(168,523)	40,840	63,653	(2,340)	<b>903,033</b>
Decrease in currency rate of 1%	(64,789)	162	11,235	(2,723)	(4,244)	156	<b>(60,203)</b>
Decrease in currency rate of 5%	(323,943)	809	56,174	(13,613)	(21,218)	780	<b>(301,011)</b>
Decrease in currency rate of 10%	(647,886)	1,617	112,349	(27,226)	(42,435)	1,560	<b>(602,021)</b>
Decrease in currency rate of 15%	(971,829)	2,426	168,523	(40,840)	(63,653)	2,340	<b>(903,033)</b>

#### Effect on total comprehensive income and equity

	2021						Total
	USD	EUR	SDR	JPY	CAD	Other	
Increase in currency rate of 1%	41,657	2,912	(11,584)	5,221	4,024	2,643	<b>44,873</b>
Increase in currency rate of 5%	208,285	14,558	(57,918)	26,104	20,121	13,215	<b>224,365</b>
Increase in currency rate of 10%	416,570	29,116	(115,837)	52,207	40,243	26,429	<b>448,728</b>
Increase in currency rate of 15%	624,854	43,674	(173,755)	78,311	60,364	39,644	<b>673,092</b>
Decrease in currency rate of 1%	(41,657)	(2,912)	11,584	(5,221)	(4,024)	(2,643)	<b>(44,873)</b>
Decrease in currency rate of 5%	(208,285)	(14,558)	57,918	(26,104)	(20,121)	(13,214)	<b>(224,364)</b>
Decrease in currency rate of 10%	(416,570)	(29,116)	115,837	(52,207)	(40,243)	(26,429)	<b>(448,728)</b>
Decrease in currency rate of 15%	(624,854)	(43,674)	173,755	(78,311)	(60,364)	(39,644)	<b>(673,092)</b>

## NATIONAL BANK OF GEORGIA

### NOTES TO THE FINANCIAL STATEMENTS AS AT AND FOR THE YEAR ENDED 31 DECEMBER 2023

*(in thousands of Georgian Lari)*

---

#### Other risks

##### **Settlement risk**

Settlement risk (i.e., the risk that the counterparty may not be able to complete a transaction) is mitigated in a number of ways. The Bank will only transfer funds after sufficient collateral has been secured. For outright transactions in securities, settlement risk is eliminated through the use of systems that are based on delivery versus payment, that is, the simultaneous exchange of securities and cash. Additionally, the settlement of the cash component is performed through the payment system referred to as Real Time Gross Settlement, which is owned and managed by the Bank, which determines the position of each participant in real time on an individual payment-to-payment basis. This automatically avoids overdrafts and as it simultaneously uses accounts in the Bank as settlement asset, it mitigates credit risk.

##### **Non-financial risks**

Non-financial risks to which the Bank is exposed are: reputational and operational risks. Operational risks originate from inadequate or failed internal processes, people and systems or external events. The Bank is exposed to the following sub-categories of operational risks: legal, information technology, human resources, security (physical and information), third-party, business continuity, fraud and compliance risks. Realization of non-financial risks may result in financial loss, damage to reputation or failure in achieving the Bank's business objectives. Hence, the Bank developed Centralized Risk Management (CRM) system in order to minimize the impact of non-financial risks and ensure solid internal control system.

CRM framework is comprised of non-financial risks management, incident management and business continuity systems and is supported by internal control system of procedures. Non-financial risk assessment is based on qualitative method (5-scale) and includes all bank-wide processes, where risks could jeopardize the achievement of the objectives. Incident Management system captures and analyzes incidents in order to avoid the repetitive occurrence of incidents. To expand and improve operational risk assessment, the Bank selected and accepted quantification method - Standardised Measurement Approach (SMA). In order to finalize the implementation, the Bank will continue working on financial loss data, consequent processes and procedure development. The Bank applies model risk management framework to register, describe and assess the models used by the Bank, which supports to create unified documentation for each model and non-financial risk assessment process. Business continuity management system continuously improves the resilience of the Bank's critical processes and provides adequate procedures, regular testing and expansion of scenarios.

The Bank defined the aggregate level (Risk Appetite) of non-financial risks the Bank is willing to assume within its risk capacity to achieve its strategic objectives and goals. Overall, the Bank has conservative approach to operational and reputational risks and operates within low-risk appetite and tolerance levels. Hence, the Bank makes resources available and sets effective governance processes to control and maintain non-financial risks at low risk level. Risk appetite statement is reviewed and approved annually by the Council of the Bank.

## 29. EVENTS AFTER THE REPORTING PERIOD

Up to the date these financial statements were authorized for issue, no significant subsequent events have occurred that require adjustment of, or disclosure in, these financial statements.



