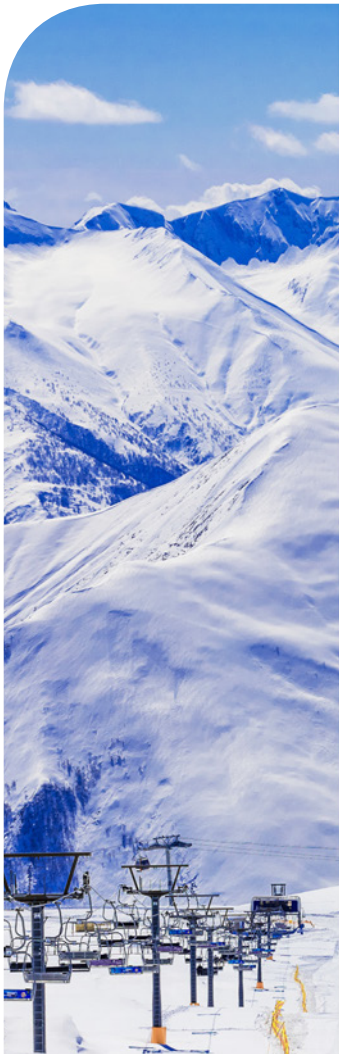




GALT & TAGGART
RESEARCH

Georgia's Tourism Sector *Shifting into High Gear*



Georgia | Tourism
Industry Overview
June 21, 2016

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Executive Summary

After a resilient 2015, the tourism industry in 2016 has shifted into high gear.

International arrivals in 5M16 were up 15.3% y/y to 2.1mn visitors, with Azerbaijan and Russia posting double-digit growth rates. Georgia has benefited from an influx of Russian visitors who have shied away from Turkey and Egypt due to political tension and safety concerns. Secondary source markets have also posted strong performances. The number of Iranian visitors in 5M16 has increased 4.6x to almost 26,000, as visa-free travel to Georgia was reinstated for Iranian citizens in February 2016. We forecast an estimated 6.7mn foreign visitors to Georgia in 2016, up 14.1% y/y, on the back of high expected growth from Russia, Azerbaijan, and secondary markets. Travel inflows were up 8.3% y/y to US\$ 1.9bn in 2015 and based on our estimates, tourism in 5M16 has generated an additional US\$ 100mn in comparison to the same period last year.

The focus of Georgia's tourism strategy moving forward should be on the quality and diversity of visitor arrivals.

Georgia Tourism Strategy 2015-2025 targets 11.0mn international visitors (7.1% CAGR) and US\$ 5.5bn in tourism inflows (13.2% CAGR) by 2025. In order to attract more high-yielding visitors, the industry needs to focus on high-potential niche tourism products such as winter tourism, wine tourism, medical and wellness tourism, MICE tourism, and gaming. The state has invested heavily and continues to do so in developing Georgia's ski regions. The Partnership Fund, a state-owned investment fund, is actively facilitating the development of spa tourism in strategically important resort areas. The World Bank is providing the necessary infrastructure to incentivize the private sector to invest in less-developed regions.

Development of international brand hotels in Georgia is in a hyperactive phase.

An estimated US\$ 1.0bn will be invested in this segment over 2016-2018. Tbilisi accounts for the majority of the pipeline, but a number of branded hotels are slated to open in regional cities as well. In our view, the international upscale hotel segment in Georgia is likely to become oversaturated in the medium term. We see the first signs of hotel investors recognizing this probability and shifting attention to the international midscale segment, with five mid-market brands to enter the Tbilisi market over the next three years.

Georgia was ranked 71st out of 141 countries in the Travel & Tourism Competitiveness Index 2015.

Ease of doing business in Georgia, an investor-friendly tax environment, ease of hiring foreign labor, safety, and visa-free entry for most are among the country's competitive advantages highlighted in the index. The key challenges, on the other hand, are availability of skilled labor in this sector, air transport infrastructure, openness of bilateral Air Service Agreements, and stringency and enforcement of environmental regulations.

The Government of Georgia aims to spur further development of the tourism and hospitality industry through its latest initiatives.

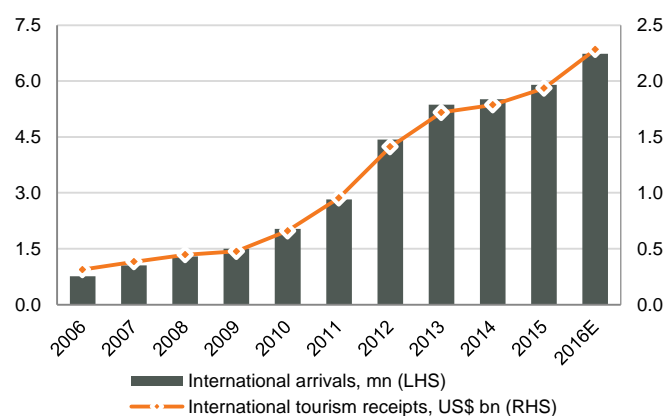
The government has initiated a program to incentivize hotel development in the Georgian periphery by co-financing management fees, interest payments, and consulting services, along with providing a partial collateral guarantee. Film in Georgia is another government initiative, which provides financial incentives for film production in Georgia. Several high-profile events are lined up for 2016, with the 25th Annual Session of the OSCE Parliamentary Assembly being the leading one, as it attracts policy experts, diplomats, foreign media, and members of parliament from the organization's 57 participating States.



Tourism growth exceeds expectations

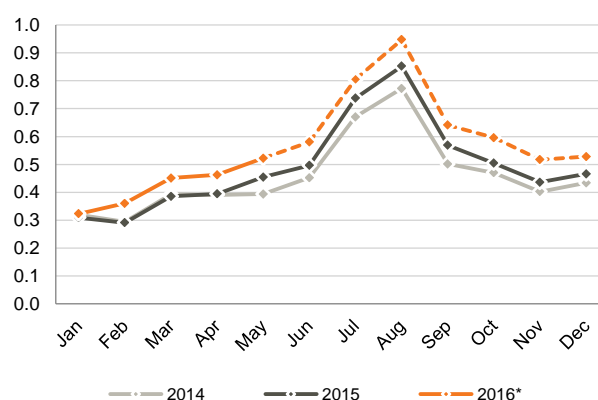
One of the fastest growing sectors in Georgia, tourism has generated an impressive **25.5% CAGR in visitor numbers over 2006-15**. After a subdued performance in 2014 (+2.3% y/y), the sector demonstrated strong resilience in 2015, with arrivals increasing 7.0% y/y to 5.9mn, in a year when foreign remittances and goods exports took significant hits. Travel inflows rose 8.3% y/y to US\$ 1.9bn in 2015, accounting for 13.9% of GDP, up from 5.7% of GDP in 2010. Based on our estimates, tourism in 5M16 has generated an additional US\$ 100mn in comparison to the same period last year. The share of tourism revenues in service exports has been on the rise, reaching 61.8% of service exports in 2015, up from 41.2% in 2010. Net FDI in the hotels and restaurants sector over 2010-2015 amounted to US\$ 230.0mn, after FDI in the sector peaked in 2007-2008. The importance of the sector is best illustrated by its increasing role in financing Georgia's goods trade deficit – net service exports financed 33.8% of the goods trade deficit in 2015, up from only 19.8% in 2010.

Figure 1: Total international arrivals, tourism receipts



Source: GNTA, NBG

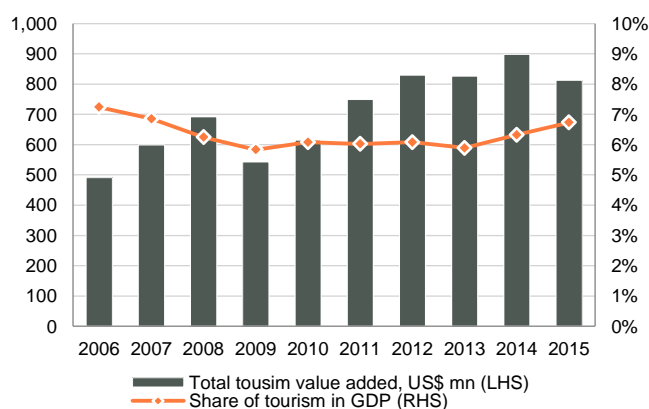
Figure 2: Monthly arrival dynamics, mn (2014-2016E)



*Solid line indicates actual numbers, dotted line indicates Galt & Taggart Research estimates.
Source: GNTA, Galt & Taggart Research

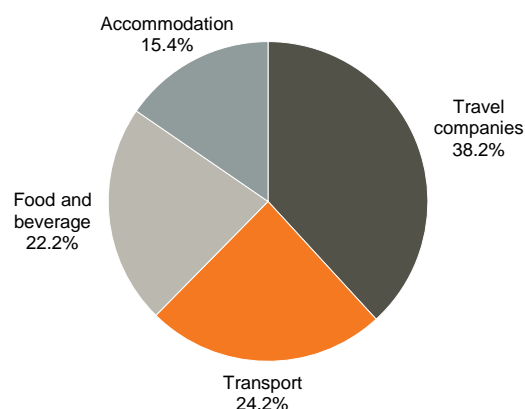
The value added from tourism increased **16.2% y/y to GEL 1.8bn in 2015**, accounting for **6.7% of GDP**. Travel service companies were the main driver (+29.1% y/y), contributing 10.0ppts to the overall growth and making up 38.2% of tourism-related services. The transport segment holds the second largest share with 24.2% of total, but posted a stagnant performance (+0.1% y/y) in 2015. In US\$ terms, value added from tourism declined 9.6% y/y to US\$ 812.4mn, largely due to the 28.6% depreciation in the average GEL/US\$ rate in 2015.

Figure 3: Share of tourism in Georgia's GDP



Source: GNTA, GeoStat

Figure 4: Composition of tourism-related services, 2015

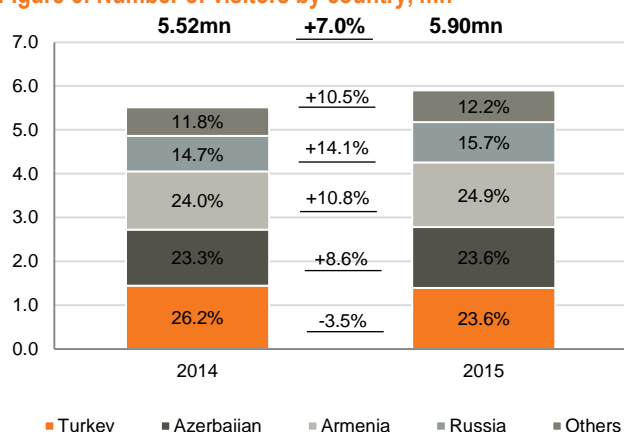


Source: GNTA



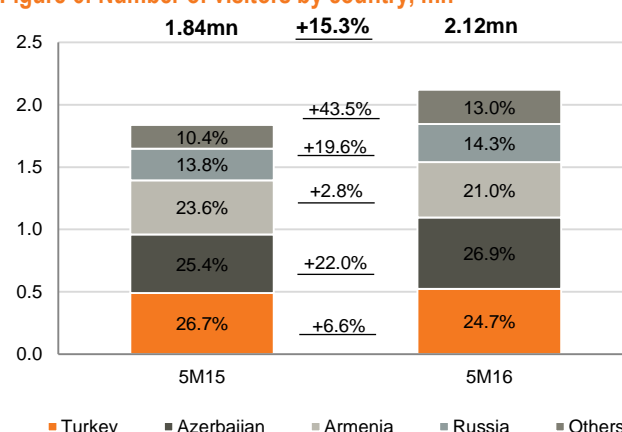
Tourism in 2016 has shifted into higher gear. International arrivals to Georgia have posted double-digit growth rates for the fourth month in a row. After a slow January, arrivals growth in February through May has averaged 17.9% y/y, bringing the 5M16 annual growth rate to 15.3%. The largest contributors to the increase in 5M16 were Azerbaijan (+22.0% y/y), Russia (+19.6% y/y), and Turkey (+6.6%), with Azerbaijan now holding the largest share in total arrivals of 26.9%. In the case of Turkey, the growth can be partly attributed to the low base effect, as the number of arrivals from Turkey was down 5.7% y/y in 5M15.

Figure 5: Number of visitors by country, mn



Source: GNTA

Figure 6: Number of visitors by country, mn



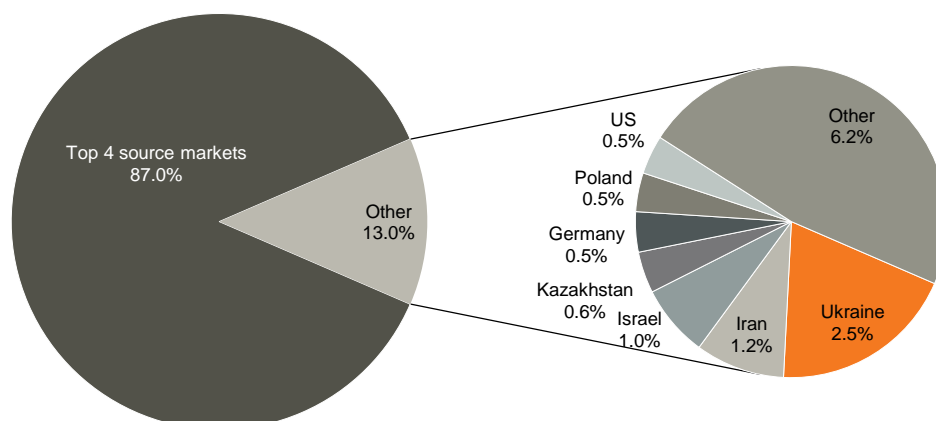
Source: GNTA

Georgia has benefited from an influx of Russian visitors who have shied away from Turkey and Egypt due to recent developments. The tense relationship between Russia and Turkey, following the downing of the Russian military plane by Turkish jets in November 2015, coupled with multiple terrorist attacks across Turkey, has resulted in a 64.8% y/y decrease in the number of Russian tourists visiting the country December 2015 through April 2016. In the wake of the Metrojet crash in October 2015, Russia halted all flights to and from Egyptian airports. Fears that the Egyptian airliner crash in May 2016 was also the result of terrorism is likely to keep Russian tourists out of Egypt for quite some time. In the 12 months prior to those events, some 3.7mn Russian visitors traveled to Turkey and another 2.9mn to Egypt. In 5M16, the number of Russian visitors to Georgia increased 19.6% y/y to almost 304,000 and we expect the growth to be even stronger in the summer months.

While the top four source markets make up 87.0% of inbound visitors, secondary markets have posted strong increases. The number of Iranian visitors in 5M16 has increased 4.6x y/y to almost 26,000, which we attribute to the reinstatement of visa-free travel to Georgia for Iranian citizens on February 15, 2016. The number of Israeli visitors during the same period has increased 2.1x y/y to almost 21,000 visitors. Ukraine, which is the 5th largest source market, posted a 23.8% y/y increase in 5M16, more than compensating for the drop in Ukrainian visitors due to the political unrest in the country in 2015. We forecast full-year growth at 14.1% y/y to 6.7mn foreign visitors to Georgia in 2016, on the back of high expected growth from Russia, Azerbaijan, and secondary markets.



Figure 7: Secondary source markets for Georgia, 5M16

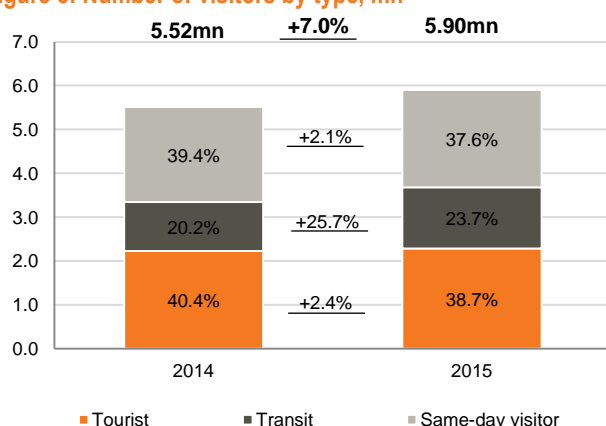


Source: GNTA

Per-visitor spending in Georgia remains low in comparison to peer countries.

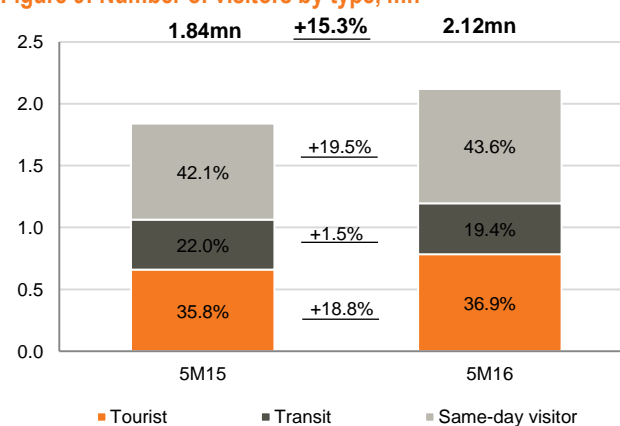
The low spending figure is largely the result of a low proportion of 'tourists' – visitors who stay over 24 hours, as transit and same-day visitors spend significantly less than tourists do. As the total number of visitors to Georgia almost tripled over 2010-2015, the share of tourists decreased from 52.5% to 38.7%. The low spend is also attributable to lower-yielding visitors dominating the arrival mix. Over 70% of visitors come from Armenia, Azerbaijan, and Turkey and spend significantly less than visitors from Russia and non-neighboring countries do. This leaves substantial upside potential if the country can manage to attract more high-yielding visitors. In that respect, the trend in 2016 is positive - the increase in the number of tourists has outpaced overall visitor growth, as has the growth in the number of Russian visitors.

Figure 8: Number of visitors by type, mn



Source: GNTA

Figure 9: Number of visitors by type, mn



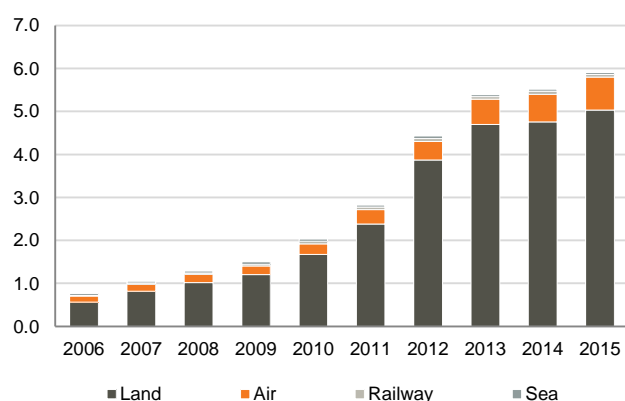
Source: GNTA

Road travel continues to be the leading form of arrival transportation with an 85.3% share in 2015. The share of visitors arriving by air increased from 11.7% in 2014 to 13.0% in 2015; rail and sea accounted for the rest. Road travel continues to dominate due to the large share of short-haul visits from neighboring countries in the total number of visits.



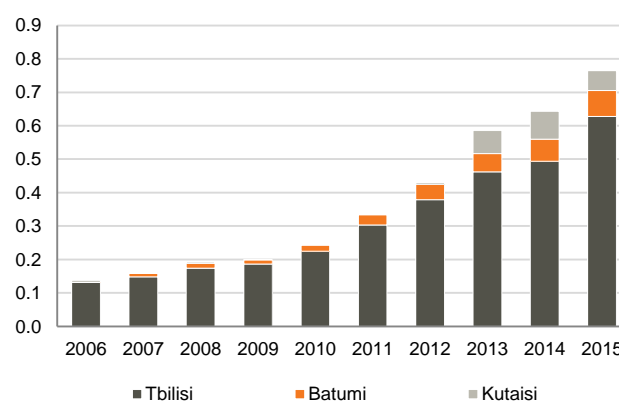
The launch of new direct flights drove 18.9% y/y growth in air arrivals to 0.8mn in 2015. The great majority of air arrivals (82.1%) came in through the Tbilisi International Airport, while Batumi and Kutaisi accounted for a further 10.1% and 7.7%, respectively. Tbilisi was the main driver behind the strong growth, with arrivals up 27.1% y/y. Batumi also posted strong double-digit growth of 18.3% y/y. Arrivals in the Kutaisi airport, on the other hand, dropped off significantly (-29.2% y/y), as Wizz Air Ukraine suspended operations in April 2015. However, Wizz Air announced in February 2016 that it will begin base operations in Kutaisi starting in September 2016. The low-cost airline will launch new twice-weekly service from Kutaisi to Berlin Schönefeld, Munich Memmingen, Dortmund, Milan Bergamo, Larnaca, and Sofia, expanding its network to 11 routes to eight countries. The first branded hotel in Kutaisi, Best Western, is due to open in 2016 to fill the existing gap in mid-market accommodation in the city. We expect these new low-cost connections to major European cities, coupled with affordable quality accommodation, to boost inbound traffic from leisure travellers.

Figure 10: Visitor breakdown by transportation types, mn



Source: GNTA

Figure 11: Visitor breakdown at international airports, mn



Source: GNTA

The number of direct routes out of Georgia has increased from 35 in June 2015 to 55 in May 2016, with flights added to all three airports. 5 new airlines entered the Georgian market since June 2015, bringing the total to 30 carriers offering regular flights from Georgia. Notably, two of those are Iranian airlines, Qeshm and ATA. As Iranian citizens can once again travel visa-free to Georgia, the airline operators have stepped in to cater to the new demand. Following the resumption of flights between Russia and Georgia at the end of 2013, 2015 saw the addition of several new routes, as Ural Airlines now operates flights out of Batumi to St. Petersburg, Samara, and Yekaterinburg, in addition to Moscow (*complete list of flights in Appendix 1*). Turkish Airlines holds the largest share of passengers at 19.8% of all travelers in 2015. Georgian Airways holds second place with 11.6%, followed by Ukraine International Airlines (9.7%) and Pegasus (6.6%). The picture of the top 4 is largely unchanged.



Diversification of Georgia's tourism offer

The focus of Georgia's tourism strategy moving forward should be on the quality and diversity of visitor arrivals, not the number, as Georgia's Tourism Strategy 2015-2025 rightly points out. The strategy targets a 7.1% CAGR in arrivals, but a 13.2% CAGR in tourism inflows over 2014-2025, as opposed to the trend in the past five years, for which the two growth rates were almost equal. These targets translate into 11.0mn international arrivals and US\$ 5.5bn in international tourism receipts by 2025. In order to attract more high-yielding visitors, the industry needs to focus on several niche areas, in which Georgia has great potential – winter tourism, wine tourism, medical and wellness tourism, and gaming.

Winter tourism in Georgia has expanded at a respectable pace over the last five years. The country boasts four distinct ski regions – Gudauri and Tetnuldi/Hatsvali in the north and Bakuriani and Goderdzi in the south. Gudauri has been the leading ski destination in Georgia since its construction in the 1980's. The number of visitors to Gudauri has increased 2.3x over the last five years to over 200,000, while Bakuriani hosted over 86,000 visitors in the 2015/2016 season. Goderdzi mountain resort in the Adjara Region opened in December 2015 and hosted almost 7,000 visitors during the season. Tetnuldi resort in the Svaneti region opened in February 2016. Significant advances, from artificial snowmaking to new and rehabilitated lifts and equipment, have been made by the Mountain Resorts Development Company (MRDC), a state enterprise tasked with managing and developing ski resorts in Georgia.

There is greater potential for winter tourism in Georgia that remains to be realized. Additional infrastructural enhancements will be crucial in this regard. The government announced in December 2015 that US\$ 150mn will be invested in the New Gudauri development project, created by Ecosign, a world leader in mountain resort planning. In 2016, MRDC plans to expand the snowmaking capability in Gudauri by constructing an artificial lake, which will also serve as an additional recreation area off-season. Three new gondola lifts will be constructed to support the creation of a new Kobi-Gudauri ski zone. A toboggan run, which will operate year-round, is to be constructed in Bakuriani, to expand the entertainment options on offer at the resort. The completed and expected improvements have prompted branded hotel entry in Georgian winter resorts. Mgzavrebi Hotel Chain will open Best Western Plus hotels in Gudauri and Bakuriani in 2016-2017, while Red-Co's Radisson Blu in Gudauri is expected to open in 2017. Gudauri is still lacking in terms of the food and entertainment variety on offer. We expect the expanded infrastructure and a growing visitor base to prompt the private sector to fill the gap.

An 8,000-year history of winemaking and 525 indigenous grape varieties make Georgia a natural destination for wine enthusiasts. Wine tourists in Georgia primarily come from the USA, Canada, Japan, China, the Baltic countries, and the EU. The Georgian wine tourism market is still in its infancy. The uniqueness of Georgian wine, made in clay pots and not in oak barrels, with little or no additives, has grown organically over the years. However, coordinated effort from wine makers, tour operators, and Georgian National Tourism Administration (GNTA), along with the development of infrastructure, will be necessary to monetize Georgia's rich endowment into a product that can compete on the global wine tourism market. There are a handful of 'chateau'-type wineries that cater to wine tourists, but collaboration among them in designing integrated wine tours will be crucial. GNTA's promotional efforts in this regard have had some results: the inaugural UNWTO Global Conference on Wine Tourism will be held in the Kakheti wine region in September 2016. Furthermore, Lonely Planet included Georgia on its list of 'Ten of the World's Most Intriguing Wine Regions' in 2015.

Medical tourism is another niche product with great potential for Georgia in the medium term. Visitors from CIS countries, who dominate the arrival mix, have a level of comfort with Georgia and for the most part, do not have very high-quality healthcare in their home countries. Georgia's healthcare is very price-competitive vs Turkey, which is currently the regional center for medical tourism. As a result of major



upgrades in its healthcare system, the number of medical tourists in Turkey increased from 74,000 to 0.5mn over 2008-14 (with a sizable number of Georgian patients, among them) and generated an estimated US\$ 2.5bn in revenue in 2014. The state of medical infrastructure in Georgia (mostly in secondary and tertiary care, which are the main attraction for medical tourists) has improved significantly over the last few years and key private sector players are investing heavily in further improvements in facilities, technology and service. Notably, in November 2015, Georgia Healthcare Group PLC became the first healthcare company in the region to be listed on the premium segment of the London Stock Exchange – an important catalyst for elevating the image of the Georgian healthcare system. The key challenges for Georgia to become a medical tourism destination are the quality of healthcare, attracting foreign-educated medical professionals, and international accreditation of Georgian hospitals.

Development of medical tourism brings far-reaching benefits to a country. First and foremost, medical tourism is a source of foreign currency inflows in the form of payments for medical care and tourism services. Notably, medical tourists typically spend significantly more on non-medical tourism services than regular tourists do. As the segment develops, there is a spillover effect resulting in an improved healthcare offering not only for visitors, but for the local population as well. A developed medical tourism industry also facilitates the return of highly qualified, foreign-educated medical professionals to the country. Furthermore, political ties between the countries are typically strengthened in the process. If Georgia can follow the example of Turkey, it stands to reap these benefits by retaining its domestic patients and attracting medical tourists from the region in the medium term.

Wellness and spa tourism is another high-potential target for Georgia. Tskaltubo, a well-known resort area in the Imereti region that promoted healthy living, relaxation, and medical tourism in the Soviet era, is a case in point. The Partnership Fund is actively facilitating its development into a modern, internationally competitive spa destination. The Fund enlisted the help of international consultancies to devise a master plan for the privatization of the 18 state-owned buildings in the resort town, three of which have already been sold to local and foreign investors. Furthermore, the government has attracted support from the World Bank and an estimated US\$ 28mn will go toward overhauling water and sanitation systems and renovating public buildings and a 70 hectare public park in Tskaltubo. The Partnership Fund is also partnering with Redix Group on the development of a high-class hotel in Abastumani, another strategically important resort area. The estimated investment volume of the project is US\$ 26mn.

The gaming industry in Georgia has large potential as most countries in the region restrict gambling. Strong development has taken place in Batumi, which is now home to 11 casinos. The estimated number of visits to Batumi casinos has increased 2.1x over 2013-2015 to 614,000, while the amount collected by the local government in gaming business fees has expanded 2.7x to US\$ 8.9mn over the same period. We expect even faster growth next year, as five of the existing casinos opened at the end of 2015 and their full contribution will be seen in 2016.

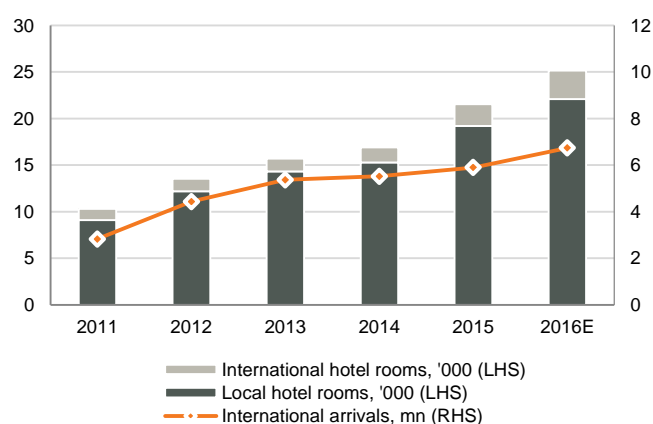
Incentives are in place for the development of gaming tourism in resort areas. The annual license fee for operating a casino in the country ranges from GEL 100,000 to GEL 5.0mn, depending on the region. Casinos commencing operations in Kazbegi, Tskaltubo, Sighnaghi, Bakuriani, and Gudauri are exempted from the annual license fee, as the government targets those areas for tourism development. In addition, newly built hotels in Georgia's seaside resort towns with more than 100 rooms (80 in some cases) are exempt for 10 years. Other regions have highly discounted license fees ranging from GEL 100,000 to GEL 250,000.



Hospitality sector

Georgia's hotel industry has experienced strong growth over the past 4 years. The 20.3% CAGR in the number of hotel rooms over 2011-2015 has been in line with arrival growth over the same period (20.2% CAGR). The growth in room supply was evenly distributed between international and local brands (see *Appendix 2 for existing branded hotels in Georgia*). Hotel turnover in US\$ terms has also increased at a strong CAGR of 13.0% over 2011-2015, reaching US\$ 177.8mn in 2015.

Figure 12: Hotel room supply in Georgia, 2011-2016E



Source: GNTA, Galt & Taggart Research

Development of international brand hotels in Georgia is in an active phase. Based on the current pipeline of confirmed projects, an estimated US\$ 1.0bn will be invested in brand hotel development over 2016-2018. The pipeline is heavily skewed toward international brands, with room supply in this category expected to increase by an unprecedented 41.5% CAGR to over 6,700 rooms. Tbilisi accounts for the majority of the pipeline (63.5% of rooms), with 11 new international brands to enter the market, but there is a strong pipeline in regional cities, as well. The shift away from independently operated to brand hotels is noticeable worldwide – based on April 2015 data, five of the largest branded hotel companies together accounted for 65% of the global development pipeline of hotel rooms.

The international upscale hotel segment in Georgia is becoming oversaturated, taking into consideration the extensive pipeline. This is largely in line with the trend in international hotel development in emerging markets, where the focus in major cities has been on luxury and upscale segments. Granted there are no major cancellations in the project pipeline, we expect the oversupply to exert pressure on occupancy levels and room rates by end-2017. There is potential to mitigate this pressure if the country can position itself as a MICE tourism destination, greatly expanding the number of business visitors who stay in upscale international hotels. The first steps in this direction were the EBRD's Annual Meeting in May 2015 and the Silk Road Forum in October 2015. However, for this potential to materialize, an important gap will need to be filled – convention centers that are in line with international standards. Some development in this regard is already in the works.

We see the first signs of hotel investors in Georgia recognizing the probability of oversaturation in the international upscale segment in the medium term and consequently, shifting attention to the international midscale segment. Hilton Garden Inn, Ramada Encore, Golden Tulip, Park Inn Radisson, and Moxy by Marriott are the midmarket brands in the Tbilisi pipeline for 2016-2018. Furthermore, Best Western hotels are expected to open in Batumi, Kutaisi, Bakuriani, and Gudauri in 2016-2017.



Table 1: International brand hotel pipeline in Georgia, 2016-2018

Hotel name	Investor	City	Opening year	Number of rooms
Millennium Hotel	Dhabi Group Georgia	Tbilisi	2016	216
Intercontinental Hotel	Adjara Group Hospitality, EBRD	Tbilisi	2017	259
Sheraton Metekhi Palace	RAKIA Georgia LLC	Tbilisi	2017	255
Radisson Blu Telegraph	Silk Road Group	Tbilisi	2017	189
Rixos	City M LLC	Tbilisi	2017	143
Hilton Garden Inn	Redix, EBRD	Tbilisi	2017	160
Ramada Encore Kazbegi Ave	m2 Real Estate	Tbilisi	2017	152
Ramada Encore Melikishvili Ave	m2 Real Estate	Tbilisi	2017	125
Golden Tulip	Block-Invest LLC	Tbilisi	2017	80
Pulmann - Axis Towers	Axis, Georgian Co-Investment Fund	Tbilisi	2018	220
Marriott Autograph Collection - Panorama Freedom Square	Georgian Co-Investment Fund	Tbilisi	2018	220
Park Inn Radisson	Block-Invest LLC, Partnership Fund	Tbilisi	2018	200
Marriott Autograph Collection - Panorama Sololaki	Georgian Co-Investment Fund	Tbilisi	2018	187
Hyatt Regency	Loyal Capital Group, Partnership Fund	Tbilisi	2018	170
Moxy by Marriott	GMT Group, OPIC	Tbilisi	2018	130
Best Western VIB	Mgzavrebi Hotel Chain	Batumi	2016	54
Crowne Plaza	Adjara Group Hospitality	Batumi	2017	170
Le Meridien	Red-Co	Batumi	2017	110
Swissotel	AdogGeorgia LLC	Batumi	2017	180
Kempinski	GIMG LLC	Batumi	2018	253
Courtyard Marriott	Alliance Group	Batumi	2018	150
Marriott Autograph Collection - Hotel & Spa Resort	Georgian Co-Investment Fund	Shekvetili	2016	220
Best Western	Capitol Real Estate, Partnership Fund	Kutaisi	2016	45
Radisson Blu Tsinandali	Silk Road Group, Partnership Fund	Tsinandali	2017	120
Best Western Plus	Mgzavrebi Hotel Chain	Bakuriani	2017	68
Best Western Plus	Mgzavrebi Hotel Chain	Gudauri	2016	80
Radisson Blu Gudauri	Red-Co	Gudauri	2017	105
Total				4,261

Source: Galt & Taggart Research

Research shows that the presence of international hotel chains has a significant positive effect on a destination's competitiveness. Chain hotels contribute to the visibility of a destination through the use of their global distribution systems and strong brand awareness. They bring in the latest technologies and contribute to the quality of the local labor force in the hospitality sector by introducing industry best practices and developing local talent through various training programs. Furthermore, the presence of international brands serves as a signal to other businesses considering entry into the market that the host country business environment is favorable for investors.

A hotel management contract is the dominant model in the branded hotel segment in Georgia. The model implies the hotel investor/owner hiring an international brand to manage the hotel and provide essential operational expertise. The operator is compensated through a combination of base and incentive fees, typically calculated as a percentage of revenue and/or gross operating profit. There are some exceptions, like Holiday Inn Tbilisi and Best Western, which are owner-operated franchises. The first 'manchise' agreement – a mix between a management and franchise contract – in the Georgian international hotel segment is in the works for the Intercontinental Hotel, due to open by early 2017. Under a hotel franchise agreement, the hotel owner retains full operational control and pays franchise fees for the use of the franchisor's brand name, logo, marketing, and referral and reservation systems. Franchising is the leading model and the preferred means of expansion for many hotel brands, as it allows them to expand at a fast pace with little capital at stake, low market risk, and no operating risk. Hotel chains typically turn to management contracts in emerging markets, where there might be insufficient industry know-how, to ensure proper ramp-up. As Georgia accumulates such expertise, we expect to see more franchising arrangements in the international hotel segment.



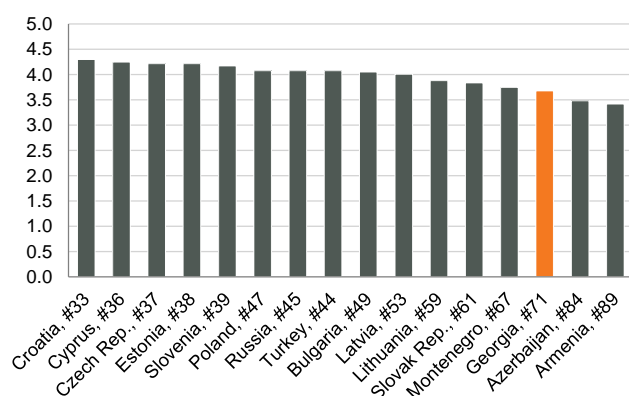
A relatively recent trend to watch in Tbilisi is the rise of alternative accommodation in the form of short-term apartment rentals. The trend is a global one – across the top 10 capital cities in the world, the share of apartments for rent has reached 14% of total accommodation stock. Apartment rentals in Tbilisi cater to the existing gap in the mid-market hotel segment. Several local websites have sprung up, followed by Airbnb, that feature extensive listings of apartment rentals for short stays. Families traveling with children, large groups of friends, and business travelers on extended visits often opt for the comfort of having an entire house or apartment to themselves and the distinctive experience of living in a local neighborhood. The hosts, on their part, are motivated by higher expected revenues than they would earn through long-term rentals. The supply of accommodation in the segment is of increasing quality, as hosts have become quite discerning of the standards expected by travelers.



Travel & Tourism Competitiveness Index

Georgia was ranked 71st out of 141 countries in the Travel & Tourism Competitiveness Index (TTCI) 2015, published biennially by the World Economic Forum (WEF). Georgia's position in the index has hovered between 66th and 73rd since the index was launched in 2007. The four key areas evaluated in the index are 1) Enabling Environment, 2) Travel & Tourism Policy and Enabling Conditions, 3) Infrastructure, and 4) Natural and Cultural Resources. Georgia ranks quite highly in the first two subindices (43rd and 44th, respectively), but performs rather poorly in the last two (72nd and 120th, respectively).

Figure 13: Travel & Tourism Competitiveness Index, 2015



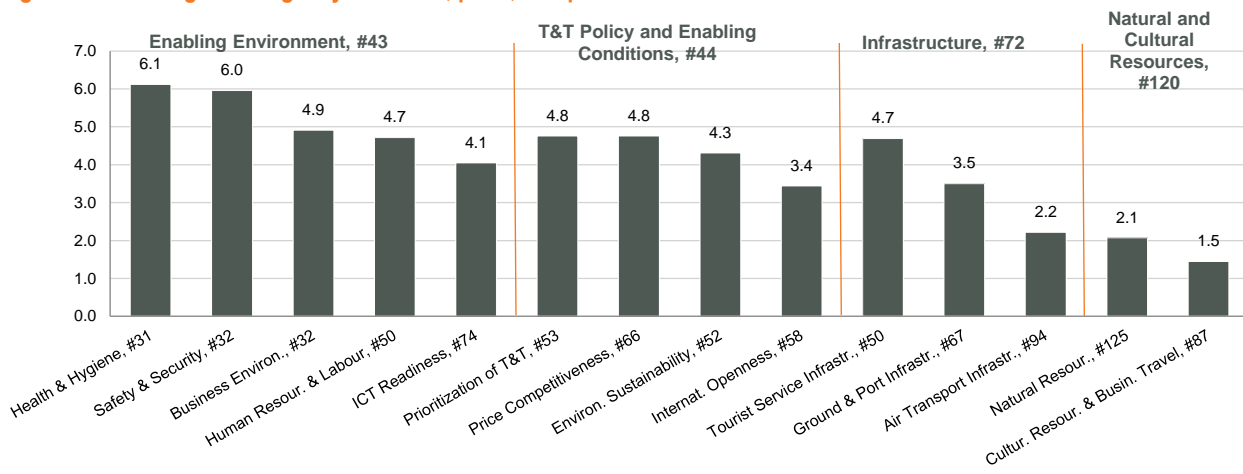
Source: World Economic Forum

Georgia's high rankings in various subcomponents underline the work that has been put in to increase the country's competitiveness as a tourism destination. Ease of doing business in Georgia, an investor-friendly tax environment, and ease of hiring foreign labor are among the country's competitive advantages highlighted in the index. Georgia is ranked highly in safety/security and health/hygiene - requirements that must be met for a country aspiring to develop a successful tourism industry. Last but not least, the index highlights Georgia's openness to foreign visitors, ranking its visa regime among the top three out of 141 countries.

The key challenges to further development of Georgia's tourism industry are also evident in the index. The availability of skilled labor is a challenge in this sector, as indicated by very low rankings across several relevant indicators and confirmed by industry players. The country's low score in air transport infrastructure rightly underscores the fact that Georgia's air transport network is in need of further development, especially when it comes to the major Western outbound markets, whose share in the total arrival mix is currently negligible. A low score in the openness of bilateral Air Service Agreements further stresses this issue. This leaves significant upside potential, if air connectivity to these high-value target countries can be improved. Lastly, Georgia has some of its lowest marks under stringency and enforcement of environmental regulations and wastewater treatment.



Figure 14: Ranking of Georgia by subindex, pillar, and position



Source: World Economic Forum



Government initiatives

Georgia's National Tourism Strategy 2015-2025 identifies the key challenges in the sector and outlines the development goals for 2025. The strategy was developed by GNTA, with support from the World Bank. The challenges highlighted are largely in line with the findings of the TTCL: air and road infrastructure, tourism infrastructure, preservation and promotion of cultural heritage sites. In addition, the need for targeted educational opportunities, enhanced market research, and improved marketing efforts is identified.

The World Bank has been in active collaboration with the Georgian government to support the increased contribution of tourism to the local economy. Its latest Regional Development Project for Georgia (RDP III) focuses on Samtskhe-Javakheti and Mtskheta-Mtianeti regions, with total funding of US\$ 75mn. The project will finance 1) urban regeneration of old towns and villages, including restoration of building facades and roofs, public spaces, museums, roads and water, and enhancement of cultural and natural heritage sites; and 2) institutional development to support institutional capacity and performance of implementing partner agencies, including GNTA and the Municipal Development Fund (MDF). These projects are crucial for incentivizing private sector investment in the region.

The Georgian government aims to incentivize the development of the hotel industry in the Georgian periphery. Hotel development has been concentrated in Tbilisi and Batumi in recent years and a big portion of the pipeline is in those two cities. In order to stimulate the hospitality industry in the regions, the government has initiated a hotel component under its Produce in Georgia program, administered by Enterprise Georgia. If an investor is developing an international branded hotel outside of Tbilisi and Batumi, the program provides for:

- the co-financing of franchising or management fees of up to GEL 300,000 per year for the first two years
- the co-financing of interest on a bank loan (10% for GEL loans, 8% for FX loans), up to a GEL 5mn loan size
- a partial collateral guarantee (50% of the loan) of up to GEL 2.5mn
- co-financing of consulting services.

The above program is also applicable for local hotel development. For non-branded hotels, the program still co-finances interest payments and consulting services and provides a partial collateral guarantee, albeit at lower limits. Investors can also apply for the program if they are planning the expansion of an existing hotel, in which case the investor must be 1) adding at least 10 new rooms and/or 2) developing external infrastructure or integrating new services.

The Georgian government has initiated a program to incentivize film production in Georgia, leveraging the diverse nature of Georgian landscapes and low labor costs. The program provides a cash rebate of 20% for qualified expenses incurred in Georgia during the production. The program provides further cash incentives if the production includes certain elements that would serve to popularize Georgia, such as employing Georgian actors in significant roles, distributing the final product in the EU, US, or Canada, and depicting UNESCO cultural heritage sites in Georgia, among others. Promotion of the program in India and USA has already brought the first results. Leading Indian directors of Bollywood action films met with Georgian government representatives in May and agreed on directing the production of their next movie in Georgia. Two other film projects are under consideration.

The government budget allocation for the support of tourism development has increased 27.6% y/y to GEL 23.0mn. The promotional activities of the Georgian National Tourism Administration include participation in international exhibitions, marketing campaigns in target markets, press tours and introductory tours for the world's leading tour operators and mass media representatives, and developing light tourism infrastructure in cities attractive for tourists, among others. In addition, the Georgian government has allocated GEL 29mn for the organization of CheckIn



Georgia, a series of entertainment events to be held across Georgia in 2016. The main draw for tourists will be concerts by world-renowned artists, while other events will include art, film, theatre, wine, and music festivals. The inaugural UNWTO Global Conference on Wine Tourism will be held in the Kakheti wine region in September 2016. The traditional Black Sea Jazz Festival this year will be held over 10 days, as opposed to four, and will feature what's inarguably the best lineup the festival has ever had.

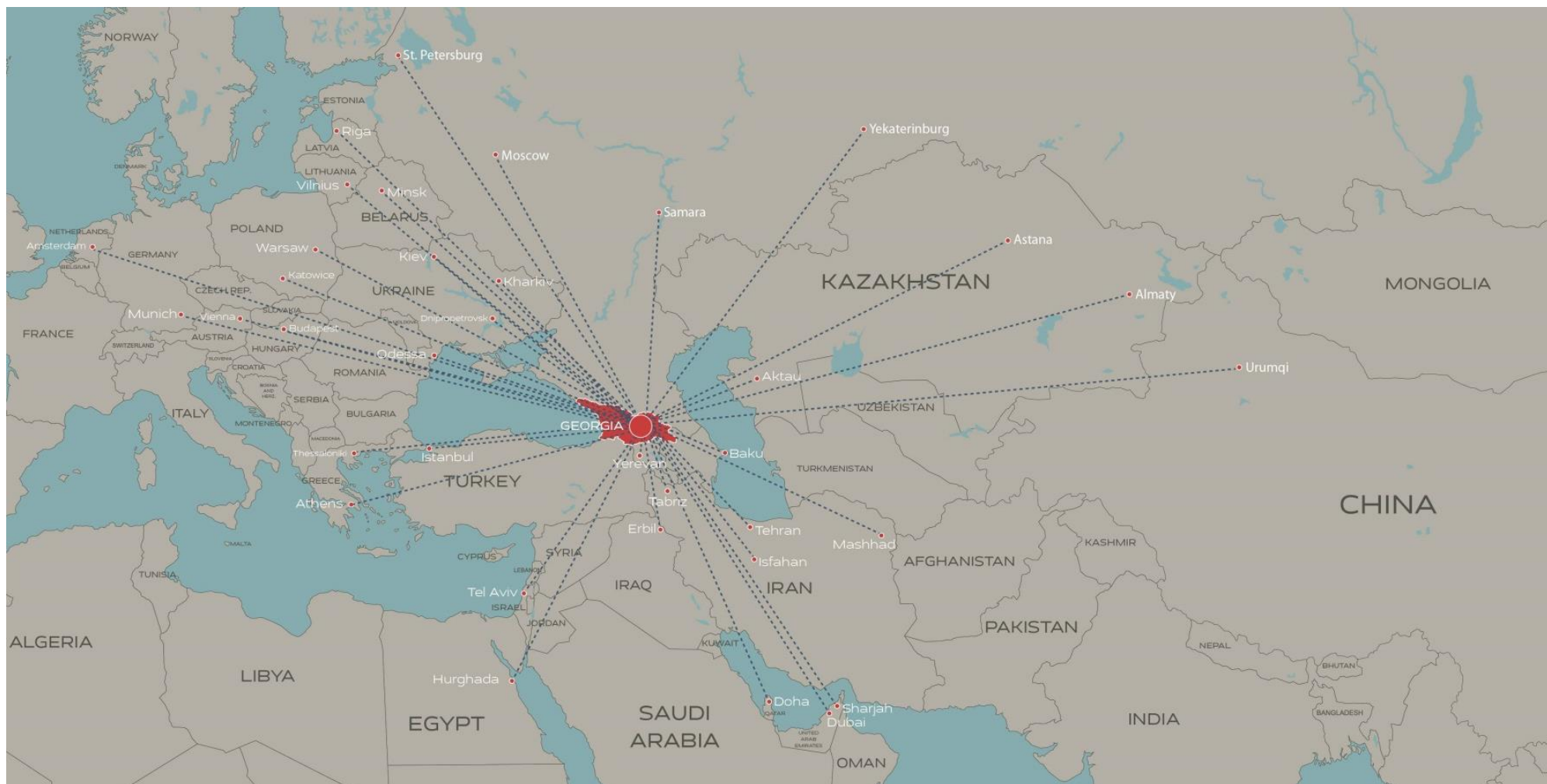
Several high-profile business events are lined up for the second half of 2016.

The 25th Annual Session of the OSCE Parliamentary Assembly, the largest event on the OSCE PA calendar, will take place at the ExpoGeorgia Exhibition Center in Tbilisi in July 2016. The Annual Session attracts policy experts, diplomats, representatives of international organizations, and members of the media, in addition to some 300 members of parliament expected to attend from across the Organization's 57 participating States. The Silk Road Forum is expected to be held in Tbilisi in November 2016 for the second year. Such events serve to attract foreign visitors, generate welcome publicity, raise awareness, and enhance the image of the country as a favorable destination.



Appendix 1: Air connectivity

Map 1: Flight connections to/from Georgia



Source: Civil Aviation Agency of Georgia



Table 2: Direct flights

Flight	Company
Batumi-Aktau	SCAT Airlines
Batumi-Dnipropetrovsk	Dniproavia
Batumi-Istanbul	Turkish Airlines
Batumi-Kiev	Yanair
Batumi-Minsk	Belavia
Batumi-Moscow	Georgian Airways, Ural Airlines, S7 Airlines
Batumi-Odessa	Dniproavia, Yanair
Batumi-Saint Petersburg	Ural Airlines
Batumi-Samara	Ural Airlines
Batumi-Sharjah	Air Arabia
Batumi-Tel Aviv	Georgian Airways, Arkia, El Al Israel Airlines
Batumi-Yekaterinburg	Ural Airlines
Kutaisi-Bergamo	Wizz Air
Kutaisi-Berlin	Wizz Air
Kutaisi-Budapest	Wizz Air
Kutaisi-Dortmund	Wizz Air
Kutaisi-Katowice	Wizz Air
Kutaisi-Kharkiv	Ukraine International Airlines
Kutaisi-Kiev	Ukraine International Airlines
Kutaisi-Larnaca	Wizz Air
Kutaisi-Memmingen	Wizz Air
Kutaisi-Moscow	Ural Airlines
Kutaisi-Sofia	Wizz Air
Kutaisi-Thessaloniki	Wizz Air
Kutaisi-Vilnius	Wizz Air
Kutaisi-Warsaw	Wizz Air
Tbilisi-Aktau	SCAT Airlines
Tbilisi-Almaty	Air Astana
Tbilisi-Amsterdam	Georgian Airways
Tbilisi-Astana	Air Astana
Tbilisi-Athens	Aegean Airlines
Tbilisi-Baku	Azerbaijan Airlines
Tbilisi-Dnipropetrovsk	Dniproavia
Tbilisi-Doha	Qatar Airways
Tbilisi-Dubai	Flydubai
Tbilisi-Erbil	Georgian Airways
Tbilisi-Hurghada	Air Cairo
Tbilisi-Istanbul	Turkish Airlines, AtlasGlobal, Pegasus Airlines
Tbilisi-Isfahan	Taban Air
Tbilisi-Kiev	Ukraine International Airlines, Yanair
Tbilisi-Mashhad	Taban Air
Tbilisi-Minsk	Belavia
Tbilisi-Moscow	Georgian Airways, Aeroflot, S7 Airlines
Tbilisi-Munich	Lufthansa
Tbilisi-Odessa	Yanair
Tbilisi-Riga	airBaltic
Tbilisi-Saint Petersburg	Georgian Airways
Tbilisi-Sharjah	Air Arabia
Tbilisi-Sharm el-Sheikh	Air Cairo
Tbilisi-Tabriz	Taban Air
Tbilisi-Tehran	ATA Airlines, Qeshm Airlines
Tbilisi-Tel Aviv	Georgian Airways, Israir Airlines, Arkia, El Al Israel Airlines
Tbilisi-Thessaloniki	Ellinair
Tbilisi-Urumqi	China Southern Airlines
Tbilisi-Vienna	Georgian Airways
Tbilisi-Warsaw	LOT Polish Airlines
Tbilisi-Yekaterinburg	Ural Airlines
Tbilisi-Yerevan	Georgian Airways

Note: shaded lines indicate flights that commenced or resumed after June 2015
Source: GNTA, Georgian Civil Aviation Agency



Appendix 2: Accommodation

Table 3: Existing international brand hotels in Georgia

Hotel name	Investor	City	Opening year	Number of rooms
Tbilisi Marriott	GMT Group	Tbilisi	2002	127
Courtyard Marriott	GMT Group	Tbilisi	2004	118
Radisson Blu Iveria	Silk Road Group	Tbilisi	2009	249
Citadines	Amtel Properties Georgia	Tbilisi	2009	66
Holiday Inn	Adjara Group Hospitality	Tbilisi	2011	270
Rooms Hotel*	Adjara Group Hospitality	Tbilisi	2014	126
Best Western	Best Western LLC	Tbilisi	2014	48
Hotels & Preference Hualing Tbilisi	Hualing Group	Tbilisi	2015	247
Mercure Tbilisi Old Town	Maqro Construction	Tbilisi	2015	108
Sheraton	Nurol Holding Inc	Batumi	2010	202
Radisson Blu	Silk Road Group	Batumi	2011	168
Divan Suites	Unidentified	Batumi	2014	65
Hilton	Hestok Limited, Orix Investor Corp	Batumi	2015	247
Rixos	Kazmunaigaz Service Ltd, Partnership Fund	Borjomi	2015	151
Crowne Plaza	Park Hotel LLC	Borjomi	2016	101
Rooms Hotel*	Adjara Group Hospitality	Kazbegi	2012	156
Total				2,449

*Member of Design Hotels
Source: Galt & Taggart Research



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