GEORGIAN ECONOMIC TRENDS

Contents

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This publication is financed by the European Union's Tacis Programme, which provides grants finance for know-how to foster the development of market economies and democratic societies in the New Independent States and Mongolia.

ABOUT GEORGIAN ECONOMIC TRENDS

Georgian Economic Trends quarterly publication aims to provide all those interested in the progress of economic reform in Georgia with a review of developments. *GET* was established in 1995 and is published in Georgian and English. This and previous editions of GET are available on the internet at:

www.geplac.org

This edition draws on information from a wide range of government and non-government sources including in particular the State Department for Statistics, the National Bank of Georgia, the United State Social Safety Fund, the Ministry of Finance, the Ministry of Foreign Affairs, the Ministry of Economy, Industry and Trade, the Ministry of State Property Management, the Ministry of Health and Social Affairs as well as other Government ministries and departments. Wherever possible every care is taken to ensure that data sources are fully acknowledged since without the full co-operation and support of information providers, including regular consultation, it would not be possible to produce this review. The purpose of *GET* is to offer an independent analytical account of economic trends drawing on information made publicly available. As part of this work, comments and advice are offered on policy and on the collection and dissemination of economic and other information. These are always intended to support the process of economic reform in Georgia and represent the view of the authors and editors only and do not represent any official view of the European Commission, the Tacis Georgian-European Policy and Legal Advice Centre or the Government of Georgia. Readers may quote any information used provided it is properly acknowledged.

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CHAPTER ONE: SUMMARY

NATIONAL ACCOUNTS AND MAIN TRENDS

In Q2 2001 economic growth accelerated to 8.6 per cent. Real growth in GDP in H1 2001 was 5.2 per cent. This growth is mainly related to the recovery in the agricultural sector in H1 and the stable growth of service industries. Despite some revival in industry and construction in Q2 the lag that took place at the beginning of the year was not completely overcome in Q2. The positive trend of this year was the extension of the business sector.

In this year there has been substantial growth of the tobacco industry, and that has had a positive impact on foreign trade. Under the food security programme of the European Commission GEL 4.8 milllion were disbursed for the needs of agrarian sector over the first seven months of this year .

As of 31st July 2001, Georgia's national debt amounted to GEL 4,660 million, that is GEL 11.5 million less than at the end of 2000. Both foreign and internal debts have reduced. In accordance with Georgia's commitments to the official creditors of "Paris Club", bilateral negotiations should be finished by 31st August. The negotiations with the creditor countries are actively continuing, but the last deadline probably will slip.

GOVERNMENT FINANCE

According to the 2001State Budget, total revenues in the first half of the year were expected to reach GEL 407.4 million, that is 48 per cent of revenue expectations for the whole year, while expenditures were set at GEL 480 million, 40 per cent of the yearly target. The deficit, therefore was estimated at GEL 72.6 million. Actual state revenues were GEL 357.3 million, GEL 50 million less than planned. Not all the anticipated external payments were received. Actual expenditures were cut accordingly to GEL 397.5 million, that is to 82.8 per cent of the initial size. Tax administration improved with absolute and percentage increases over the year. The current reform in tax collection agencies is supposed to boost tax revenues further.

MONEY AND FINANCE

During January-August 2001, there were 14 28-day T-Bills auctions with a gross emission of GEL 18 million and 12 91-days auctions with a gross emission of GEL 18.6 million. In April 2001, the NBG made the decision to start reverse REPO operations, buying T-Bills from commercial banks for short term with an agreed later sale back again. However, there was only one reverse REPO auction in August 2001.

The nominal exchange rate fluctuated insignificantly during April-August within a narrow corridor. The nominal exchange rate changes did not have a considerable effect on prices. During January-August 2001, the CPI increased by 2 per cent that gives a possibility to say that the inflation level will be kept within the targets (annual 6 per cent).

INTERNATIONAL TRADE

SUMMARY

The negative trade balance of Georgia increased in H1 2001, compared to the respective period of the previous year. A trade deficit of USD 217 million is about USD 83 million more than in H1 2000. During H1 2001, the export coverage of import ratio decreased from 51 (in H1 2000) to 40 per cent. Despite the fact that, there was growth of exports to Turkmenistan (military aircrafts) of USD 14 million Georgia's exports to strategic partner countries - Azerbaijan, Ukraine and Germany decreased sharply.

The first half of 2001 was characterized by significant growth of exports of military aircrafts (mainly for Turkmenistan), which changed the structure of exports. The share of aircrafts exports has gone up to about 10 per cent of all export. The import structure is also changing gradually. The share of machinery and mechanical appliances and electrical machinery for the first time reached 16.5 per cent. This could be explained by increased investments. The share of food (milling industry, wheat etc) is slowly decreasing.

On 29th June 2001 the US President designated Georgia as a GSP beneficiary developing country and granted duty-free access to the USA market for certain products that are imported from Georgia.

In November 2001 in Dohar, the capital of Qatar, it is planned to hold a ministerial conference, which could facilitate the start of a new multilateral negotiations round. The forthcoming negotiations will cover all the sectors of trade in services fully respecting the demand and supply principle. Since commitments of Georgia within the WTO in comparison to other WTO member states foresee a very liberal regime of international trade in services, it is in the best interests of Georgia to eliminate or at least lessen disproportionaletly the liberalization of service markets in different states.

PRIVATISATION

The second quarter of 2001 saw little progress in terms of actual privatisation of medium and large enterprises (MLE). The Ministry of State Property Management (MSPM) proceeds with the preparation of enterprises for sale or liquidation. The objects easiest to privatise have been already transferred into private ownership, while the enterprises of special importance to the economy need more examination and time to be privatised. A tender to privatise the gas distribution company Tbilgazi and transfer into management the Tbilisi water supply and sewage system is under way. Bankruptcy cases raised against some large enterprises last year did not bring any results yet.

EMPLOYMENT, INCOMES AND THE SOCIAL SAFETY NET

LABOUR MARKET

Although the economic status figures seem to be slightly improving over those of recent years, the overall unemployment situation remains deeply flawed, and the employment trends remain largely unchanged reflecting grim prospects on the labour market. An overwhelmingly large share of the labour force is either unemployed, underemployed in terms of seeking more work or earning way less than is needed to keep their families out of poverty. Unsafe and unhealthy working conditions, as well as job and income insecurity and long-term unemployment are widespread.

Self-employment remains the dominating segment of the employment and the labour force. The non-agricultural self-employed are largely engaged in low-income and unstable activities, mostly in the informal sector. The share of hired employment in total employment is shrinking. The average monthly nominal salary of hired employees across the economy was GEL 82.8 in Q1 2001.

The national unemployment rate, according to the SDS household survey, was 12 per cent by the ILO "strict" methodology and 17.2 per cent by the ILO "loose" methodology in Q1 2001. As always, the unemployment rate figures are distorted by the rural ones that are always extremely low due to existing legislation rather than to the real situation in the villages. The participation rate was still rather high - 63.1 per cent in Q1 2001, though it has been falling in annual terms since 1998.

SOCIAL SAFETY NET

The vast majority of the population, including informal sector employees, the self-employed and the unemployed, as well as their family members, have no social protection whatsoever, and the problem of poverty in old age is particularly acute as the currently existing pension system proved to be insolvent. Social policy reform aimed at rendering the existing system sustainable is among the top priorities in the country. The system of social protection provided by the state requires fundamental restructuring, and an economically viable, affordable and equitable social safety net is to be created.

In order to provide a plurality of possibilities and availability of choice for those who can afford to make provisions for their future pensions, a *multi-pillar system* is being introduced that implies three pillars: a universal state pension scheme, a mandatory private pension scheme and a voluntary private pension scheme. In May, the first private pension insurance company in Georgia – Georgian Pension Investment Holding (GPIH) was founded.

The Secretariat to the Governmental Commission for Elaboration of the Poverty Reduction and Economic Growth Programme (PREGP) is currently preparing the final document of PREGP, the main goals of which are the elimination of poverty through support to economic growth leading to creation of new work places; raising the living standards of the population; and ensuring the participation of all citizens in the country's development process.

EU-GEORGIAN RELATIONS

The figures for January-July 2001 show an increase in the EU-Georgian trade compared to the same period of the last year. In January-July 2001, turnover amounted to USD 142.0 million. This is USD 18.3 million more than in the same period of 2000.

Economic relations between Georgia and Italy started in 1992. Trade relations between two countries intensified after 1995 and reached its highest level in 1998. In this year trade amounted to USD 37.7 million, with exports of USD 8.9 million and imports of USD 28.7 million. During this year imports from Italy to Georgia were USD 13.1 million.

CHAPTER TWO: NATIONAL ACCOUNTS AND MAIN TRENDS

GDP AND MAIN TRENDS

According to preliminary estimates of the State Department for Statistics (SDS), GDP in H1 2001 amounted to GEL 3,080.9 million (USD 1,500.7 million), compared to GEL 2,786 million (USD 1 405.6 million) in H1 2000. GDP per capita in H1 2001 was GEL 666.1 (USD 324.5), and for the corresponding period of last year, GEL 603.4 (USD 304.4). Real growth of GDP in Q1 was 1.7 per cent, while in Q2 it increased by 8.6 per cent. In total real growth in H1 was 5.2 per cent. The agricultural sector retains the leading position in domestic product, and was supported by a high growth rate of 9.9 per cent in this year. Stable growth trend has maintained in the following services sub-sectors: trade, transport, restaurant and hotels, telecommunications, and finance. Despite a revival in industry in Q2 the total added value in the first part of this year in industry and construction has decreased by 2 per cent compared with H1 2000. The growth rate in 2001 was highest in the telecommunication sector, that is mainly related to the extension of mobile telephone communication network in the country. Entrepreneurial activity in all kinds of enterprises is increasing primarily through private initiative; 63.1 per cent of all products and services created in this sector in H1 2001 came from private enterprises (compared with 53.8 per cent in the corresponding period of last year).

In the first four months of the year, the inflation rate was 2.3 per cent (induced mainly by the consequences of last year's drought), but in May-June prices fell, that is a peculiarity of the Georgian economy. The price index fell by 1.4 per cent. In total, over the first six months the inflation rate amounted to 0.9 per cent. The NBG is continuing a policy of purchasing US dollars, therefore for the same period the nominal average exchange rate of USD/GEL compared with the end of 2000 has reduced by 3.9 per cent.

Table 2.1: Dynamics and structure of GDP, H1 2001
(H1 2000=100)

	H1 2001 versus H1 2000	Share in GDP
Agriculture, forestry and fishing	**109.9**	**20.6**
Industry and construction	**98.0**	**20.4**
Industry	96.9	13.1
Domestic processing of agricultural products	105.2	3.5
Construction	94.9	3.8
Services	**103.7**	**53.2**
Trade	101.1	12.4
Hotel and restaurant	118.4	2.6
Transport	105.6	10.7
Telecommunication	124.5	2.8
Financial intermediation	101.9	1.6
Operation with real estate, commercial activities	103.5	6.8
State management, Defense	100.4	3.7
Education	105.5	4.1
Health care and social services	96	5.1
Other communal, social and personal services	95.8	3.1
Services hired by the households	72.2	0.3
Net taxes	24.5	6.8
Amendments by financial intermediation services	87.6	-1.1
GDP	**105.2**	**100**

Source: State Department for Statistics

SECTORS OF ECONOMY

Industry

A sharp reduction of industrial output in Q1 2001 had a serious impact on performance in H1 of this year. The recovery in Q2 could not compensate completely the slump in industry in the previous quarter. The stable supply of electricity contributes to the start up of most of large enterprises. According to the results of H1 compared with the previous year industrial output increased as follows: extraction of metal ore by 69 per cent; production of tobacco products by 3.3 times; rubber and plastics by 77.2 per cent; mineral products by 8.4 per cent; transport equipment by 62.7 per cent and electronic appliances and apparatus by 17.9 per cent. Especially notable is the fast growth of the national tobacco industry (657.6 million units, while in H1 2000 it was 177.6 millions units), more and more local consumers prefer local produce. As a result, the share of the tobacco industry in total industrial production in H1 increased up to 1.9 per cent compared with 0.6 in H1 2000. Consequently, the registered import of cigarettes has almost halved.

Oil

Ensuring the energy security of the country is one of the main objectives of Georgia's economic and industrial policy. Over H1 2001 about 52.4 thousand tonnes of oil were produced, while in H1 2000 - 55.5 thousand tonnes. The production of gas was also reduced in H1 2001 to 24.4 million m^3 (cubic metres) compared to 37.0 million m^3 in H1 2000[1]. Although the domestic production of fuel satisfied only a small part of local consumption, there are some prospects for expansion of production and refining of oil inside the country. It is related to the usage of domestic resources and the immediate proximity of Georgia to the oil rich Caspian Sea region. In total, it allows Georgia to reduce the import of energy resources and increase domestic capacity.

Several companies are now operating in these sectors. The largest producer of oil and gas in Georgia is Ninotsminda Oil Company Limited, an affiliated company of CanArgo Energy Corporation. It has been producing oil in the country since 1996 and gas since the end of 1999. During this period, CanArgo has invested over USD 55 million in production and exploration activities[2]. CanArgo's exploration programme and seismic data show very attractive gas prospects in the deeper cretaceous sequence in the Ninotsminda and Norio-Martkopi fields. In this year work has begun on drilling two wells. AES Corporation (that has electricity generating assets in Georgia) is quite interested and has even participated in the implementation of this project. As for the downstream business, GAOR (Georgian-American Oil Refinery) is a 51 per cent owned subsidiary of CanArgo. Situated close to the Ninotsminda field, the refinery is well positioned to supply the local market with diversified products (low-octane gasoline, kerosene, diesel and fuel oil). The capacity of GAOR is 4,000 bpd (barrels per day). However, the refinery has stood idle in the last few months. It was related mainly with the very high excise duties on additives of GAOR and difficulties concerning the guarantees of stable activity of the enterprise. On this background, CanArgo Energy Corporation is considering the opportunity of construction a big refinery in the country, that will be cost about USD 150-200 million with a capacity of 40,000 thousand barrels of oil per day. But the implementation of this project depends on the various factors, such as: matching the different interests within the region and the creation of a predictable environment for foreign investors. For these purposes, draft amendments to Georgian law on Oil and Gas have been prepared that imply the expansion of the existing regime in oil exploration and processing of production. Moreover, CanArgo is developing a retail sale network. It established CanArgo Standard Oil Products (CSOP) with Georgian partners. By May 2001 11 operational stations had been opened with plans for a further nine before the end of this year. CanArgo has already invested USD 3.5 million in the retail sector.

[1] Information provided by Saknavtobi.
[2] Information provided by CanArgo representative office in Georgia.

Ioris Valley Oil and Gas Limited (IVOG), operates on Block XI b in the Samgori/Patardzeuli oilfield, that covers 622 sq. km some 30 km east of Tbilisi. From 1995 until 30th May 2001 National Petroleum Ltd (NPL)[3] was co-owner of IVOG (with Saknavtobi). Despite the expenditure of some USD 34.3 million, the results of the exploration and appraisal drilling were disappointing and after an initial growth of production the flow rate declined, leading to some conflict between NPL and Saknavtobi. JKX, through a management contract, became involved in 1999 and began the process of restoring confidence and financial stability. On 30th May 2001, NPL signed a Production Sharing Contract (PSC) with the State Agency for the Regulation of Oil & Gas Resources and Saknavtobi. This brought the relationship between NPL (investor or "contractor") in line with the provisions of 1999 Law on Oil and Gas. NPL becomes completely responsible for exploration and production of oil and/or gas from the oilfield. As for the IVOG, its charter is amended so that it became a "non-commercial" agent to NPL for the approved work programme. It remains a limited liability company owned equally by NPL and Saknavtobi and continues to hold the licence for Block XI b. The PSA provides for a minimum level of work programme and expenditure, but in the case of failure to fulfil the programme, it will lead to forfeiture of the licences[4].

A USA-Georgian joint venture Frontera Eastern Georgia Limited, was formed by a USA company Frontera Resources and Georgian Saknavtobi to develop Block 12, that includes six oil fields in the southern-east of Georgia and covers area of 5,252 sq. km, within DedoplisTskaro region. Frontera Resources has already made substantial investments in Taribani oil field and explanatory work has been very positive. Test drilling indicates that the deposit holds substantial reserves of oil and gas. Additional technical, technological and geological activities on the Taribani oil field continue[5].

JKX Navtobi, a subsidiary of the UK company JKX Oil & Gas plc, is the contractor in the Kartli Production Sharing Contract (PSC) which covers around 2,400 km^2 to the west of Tbilisi. It has carried out geological field work and acquired 320 km of seismic data, in addition to the data previously acquired by Saknavtobi and following integration and analysis of the data, is now setting its priorities for the next stage of exploration. This work programme and budget for the rest of 2001 and into 2002 will be presented to the Board of Directors of the British Company for their approval in the very near future. Through another subsidiary, JKX Oil & Gas has a contract with the Swiss based National Petroleum Ltd for the management of their Block XI b PSC. JKX played a key part in the amendment of this contract to a PSC. JKX Navtobi also retains a 4 percent net profit interest in the “Offshore” PSC in the Georgian Black Sea where Anadarko Georgia Company is the contractor company[6].

The British company Ramco Energy signed with the National Oil Company Saknavtobi a Production Sharing Contract on development of Kacheti Block X. The agreement became effective at the end of 1999. "Kaheti Oil Limited" (a wholly owned subsidiary of Ramco) is the operator and contractor of Block X, that covers 3,350 sq km. of the Alazani Valley and foothills of the Greater Caucasus Mountains. Ramco's work programme has included the evaluation and interpretation of existing seismic and previous mapping. Ramco has also completed its own 202 sq. km seismic survey, which have identified several leads. Ramco is planning to drill a well on the acreage in the last quarter of 2001[7].

[3] National Petroleum Ltd (NPL) is Bermudan registered company based in Geneva, Switzerland.
[4] Information provided by JKX representative in Georgia.
[5] Source: Saknavtobi and Frontera Resources Corporation website.
[6] Information provided by JKX (Navtobi) representative office in Georgia.
[7] Information provided by Ramco Energy plc.

Anadarko Georgia Company, a wholly owned subsidiary of Anadarko Petroleum Corporation, is the contractor for a three block area covering approximately 8,900 sq. km in the Georgian Black Sea Continental shelf. Anadarko Petroleum Corporation is the world's largest independent oil and gas exploration and production company. Anadarko possesses the right to explore these blocks by virtue of its Amended Production Sharing Contract with the Joint Stock Company "Saknavtobi", the state Agency for regulation of oil and gas resources and JKX (Navtobi) Limited dated 26 June 2000. To date, Anadarko has completed its initial acquisition of seismic, aeromagnetic and other data and is continuing with further evaluation of the blocks[8].

The partnership of "Saknavtobi" with the German company GWDF started activity at the end of last year. The German company is intensively implementing the rehabilitation of existing deposits in the Supsa-Chaladidi area and developing new ones[9].

"Saknavtobi" (100 per cent Georgian state-owned national company) is carrying out its own geophysical exploration activities, produces oil and also represents the interests of state in relations with foreign investors.

Agriculture

Favourable weather conditions in H1 2001 contributed to the recovery in the agricultural sector. Average cereal yields by July 5th were 27.3 metric centners, while in the same period of last year it was only 9.9 metric centners. In this year the largest harvest of cereals, including wheat, was produced in the Kacheti region (over 3 tonnes per hectare). This region takes the lead in the production of cereals in the country. However, Georgia has not avoided the effects drought this year. The drought affected mainly Western Georgia (Imereti, Samegrelo, Guria, and Lechkhumi). It damaged from 70 to 100 per cent of crops, vegetable and fruit gardens, vineyards and hazelnut plantations. By 25th August 2001 the total damage induced by drought was estimated at GEL 175 million.

The prospects of stable growth the agriculture in Georgia significantly depend on the state of agrarian infrastructure. One of the main constituent parts of this infrastructure is the irrigation and drainage system. According to calculations of Georgian specialists about 200 thousand ha. will be irrigated in this year compared with the 146 thousand ha. last year, while the necessary infrastructure exists on about 469 thousand ha. However, for the last 10 ten years part of these facilities were put out of order or stolen. Another kind of problem affecting the functioning of this system, is the collection of taxes for consumed water from peasants. The average tax for 1000 m^3 of water is about GEL 4, that is about 10 times less than the cost price[10]. However, even these taxes are usually not paid by peasants. Moreover, it should be taken into account that the current irrigation and drainage system was built in Soviet times for large collective enterprises, such as, for instance, the Kolkhoz. The breaking up of agricultural land holdings into small land plots raises the problem of adjustment in the irrigation system to the needs of the small landowners (agricultural producers). In order to help solve this problem the World Bank has worked out a new programme (The world Bank Irrigation and Drainage Community Development Project). It is supposed to start at the beginning of 2002 and continue for 12 years. Under this programme USD 110 million will be allocated to the needs of the irrigation and drainage systems. The core of this programme is the establishment of water consumer communities on 255 thousand ha. of agricultural land, complete rehabilitation of the irrigation and drainage system on 125 thousand ha. and rehabilitating the internal network of water supply on 130 thousand ha. In the first phase that is scheduled for the first 5 years, it is planned to allocate USD 32 million, of which USD 27 million is form an IDA (International Development Association) credit and the rest from the

[8] Information provided by Anadarko Georgia Company.
[9] Information provided by Saknavtobi.
[10] Information provided by the State Department of Irrigation and Water Management.

Georgian government and the participation of local farmers. About USD 20 million will be directed as a capital investment for rehabilitation of the main and internal network of irrigation and drainage systems and the rest for support to the institutional development of water consumer communities. The terms of this loan are quite favourable. It will be repaid after 40 years, at an interest rate is 0.75 per cent (with the preferential first ten years period).

The Food Security Programme of European commission plays an important role in the rehabilitation of agricultural infrastructure in Georgia. Over the first seven months 2001, this programme disbursed about GEL 4.8 million to the agricultural sector. These funds were directed mainly to the needs of irrigation and drainage (GEL 3.45 million in H1 2001), as well as veterinary and plant protection sectors. Up to the end of this year it is planned to allocate an additional EUR 6 million under this programme. Part of these funds will be spent in the agricultural sector and the rest in the social sector. Considerable transfers were scheduled under the Food security programme of the EU commission in Georgia for 1996-1999, but because of non-fulfilment by the Georgian government of its obligations the assignment of funds was delayed. Consequently, Georgia has lost substantial financial aid of about EUR 14 million (secured funds by EU Commission). Negotiations for the prolongation of this programme in Georgia for 2002-2003 are currently underway. It could be said that weak financing of the agrarian sector by the state caused the country multi-million losses and a slower economic growth rate.

Internal Trade

The internal trade sector is one of the leading items in Georgia's domestic product (12.4 per cent in H1 2001). With the main large enterprises coming to a halt and with a large number of IDPs, the service sectors, including trade, have become one of the main sources of employment in the country. The domestic market is full of products and there is no deficit of goods. However, the development of this sector occurred completely spontaneously. "Wild and second-hand markets" grew up quickly. The turnover operation on these markets is beyond measure. They certainly support the widespread use of cash payments that bypass the banking system. Consequently, budget revenue collection is far short of its potential. The network of pure wholesale in Georgia is, however, underdeveloped. At the same time there are as yet no classification procedures for trade and public catering outlets (mini- and supermarkets, grocery stores, department stores, restaurants, cafés, etc.). It is necessary to define standards and classify these activities according to a uniform classification system. One of the way of solving this problem would be to set up a certification system of these objects, as provided by the Ministry of Economy, Industry and Trade.

There is already a broad legislative base for the regulation of trade and public catering sectors in Georgia, but its is badly implemented. The rights of consumers are poorly protected, since counterfeit and low quality products are often sold through retail outlets. More needs to be done in the state policy field, and that means, first of all, the protection of consumers and the establishment of uniform rules of the game for all market players.

Transport

Railway and motorway transports, and the handling of cargoes at Georgia's sea ports remain steadily growing sectors of the Georgian economy'. In H1, 14.6 million tonnes of cargoes were transported by railway with a turnover of 2,356.3 million tonne/kilometres, that is, respectively, 9.3 and 8.2 per cent higher than the previous year. Railway rolling-stock movement has also substantially increased as has activity at the railway ferries in Poti and Batumi sea ports. In H1 2001, there were 4,356 carriage arrival and departures (65.5 per cent more than in H1 last year). In total in Poti and Batumi sea ports in the first six months of this year 5.4 million tones of cargoes were processed while in the corresponding period of last year it was only 4.7 million tonnes. From Supsa sea port in H1 of this year was exported 2.8 million tonnes of oil. The turnover of cargoes and passengers by motorway have also increased, respectively, by 1.6 per cent and 2.2 per cent. The trend of reduction in the air sector has continued in this year. The transportation of passengers from Georgian airports and the turnover of Georgian air companies is going to decline. Despite of some renewal of the air fleet, (two Boeing 737s serve as flagships in one of the leading Georgian Air company-Airzena Georgian Airlines) the downward trend in air sectors is related to a reduction of local demand for air services (because of high prices of air tickets for Georgian citizens). As for the foreigners, they prefer their national air companies which have better reputations. The non-efficient customs regulation in Georgia and incompatible infrastructure have also retarded the growth in the air transportation sector.

Two years ago the company "Georgian Marine Navigation" owned 26 ships with offshore registration, most of them were arrested in foreign ports as the debts of company had reached USD 138.5 million. Most of this, USD 102 million, was owed to "Hamburgische Landesbank". According to the requirements of this bank along with the other measures and in order to avoid the complete loss of the fleet, Georgia's government established a new company "Georgia's International Navy", the successor of which is now "Ocean Shipping Company" Ltd (registered in Georgia). It is carrying out the management of most of Georgian fleet with a German company "Columbia Ship Management Ltd". Today the situation has changed drastically. The loan of USD 30 million from "Hamburgische Landesbank" was used to release the arrested Georgian ships and to repair them, as well as for the payment of salaries to crew members and to securing creditors. However, according to the conditions of the credit agreement 13 ships had to be sold. The rest of the ships were put into proper order, the qualification of sailors have improved, the accountability for the activity of the fleet has become more transparent. This ships have already received approval for the transportation of oil from such large oil companies as: Chevron, BP and Veba. Consequently, since December of last year the fleet has made an operating the profit, which in H1 of 2001 amounted to USD 12.5 million. However, these funds were directed to servicing the debt. In total, by end of H1 2001 the debt has reduced to USD 58 million. The return to profitability shows the real prospects of releasing the Georgian fleet from its debt burden by 2005. But by that time some of the ships will be 20 years old, and that decreases their charter value. This is why, it is necessary to think about the renewal of the national fleet. "Ocean Shipping Company Ltd" has signed a protocol of intention with the Chevron Corporation for the transportation of 5 million tonnes of Caspian Sea oil per year, that might be used as security for loans to buy new ships. At the same time it is considering the possibility of building tankers in Korea, where prices are relatively low and quality is satisfactory. It is probable that in this year the Georgian fleet will produce sales of USD 50-60 million. Half of these funds will go to cover expenditures and the rest to pay off debt and repair ships.

FOREIGN DEBT

The contracted external debt of Georgia at 31st July 2001, including state guaranteed commercial debt, made up USD 2,110 million. Over the first seven months of 2001 USD 46.9 million of foreign credits were received, of which USD 23.5 million was lent by the IMF, USD 3.4 million by the Government of Germany and 17.1 million USD by the World Bank. In accordance with agreement with the “Paris Club" Georgia is not paying the principal of debt to other countries in the period 2001-2002, but this does not apply to Georgia's obligations to international and regional financial organisations. By 31st July 31 under these items Georgia had paid about USD 11.5 million; of which USD 8.9 million was to IMF. Interest payments over the first seven months amounted to USD 23.2 million, mainly to EU, IMF, USA, World Bank, Austria, Russia, Turkey and Turkmenistan, and including rescheduled debt (USD 12.2 million). In sum, by 31st July Georgia's outstanding foreign state debt amounted to USD 1,540 million, USD 4 million less than at the beginning of the year. Definitely Georgia will in the short-term future need external financial assistance from international organisation and bilateral donors, but the conditions of new credits should be as favourable as possible and the surveillance on their efficient usage should be tougher.

As for the process of rescheduling Georgia's foreign debt, for Georgia's obligations to the creditor countries in the "Paris Club", his should be finished by 31st August 2001. However, It seems that the dates will be postponed. By 31st August, Georgia had achieved an agreement on the terms of rescheduling the debt with Austria and Turkey on very acceptable conditions (3 per cent per year). Also agreements with Iran, Azerbaijan, Ukraine, Russia had been initialled. As for the negotiations with other countries (Armenia, Uzbekistan, Kazakhstan, China, Turkmenistan, USA and Netherlands), they are continuing or at a preliminary stage.

INTERNAL DEBT

According to the state budget for 2001 the state's internal debt should amount to GEL 1,450 million, while at the end of last year it was GEL 1,497 million. At this time the debt has really been reduced and by 31 July 2001 was GEL 1,474 million. The reduction of debt has been achieved by the repayment of state securities issued by MoF for recapitalization of of assets of the NBG (GEL 28.08 million). However, the state liabilities in the form of Treasury Bills has increased from GEL 6.3 million to GEL 10.1 million.

In this year internal debt shows a downward trend. That is good. Moreover, the state should rely more on national resources to cover the state financial deficit. In this regard, the development of securities markets, including the issuance of Treasury bills and a gradually cut back on credits from NBG should be considered as a desirable trend. However, this process is related to the establishment of a secondary market for securities and also the level of investor confidence in State liabilities. Where the state frequently fails to fulfil its budgetary obligations, the risk of buying the state securities is quite high. This is why the main buyers of Treasury bills are commercial banks and not physical persons.

According to the 2001 state budget, the real estate and land plots meant for privatisation are to be distributed free of charge to compensate for the houses that were to be built.

BALANCE OF PAYMENTS

One of the main distinguishing features of H1 2001 was the growth of the trade balance deficit, that did not have significant impact on current account deficit. The trade deficit was USD 275.3 million[11] (USD 29.8 million more than in the corresponding period of last year). The sum of positive balances under the trade in services, incomes and current transfers items amounted to USD 136.7 million. Consequently, the current balance deficit was USD 138.6 million (only by USD 2.1 million more than last year).

According to the SDS, the repatriation of remuneration of the short-term Georgian workers has decreased substantially abroad in H1 2001[12]. The situation with investment inflows in Georgia over the last years (1999-2001) also deteriorated. In H1 2001, the level of the FDI's in Georgia was very low, at just USD 56.8 million, while in the corresponding period of 2000 it was USD 62.8 million. Portfolio investments still do not play any noticeable role in expansion of business activities.

The main stabilising items of Balance of Payments of Georgia in H1 2001 were the growth of trade credits to the non-governmental sector (USD 33.5 million), as well current transfers to general

[11] Including assessment of non-registered trade by SDS.

government and workers remittances (transfers from long-term workers abroad)[13], credits to state sector (including the use of IMF credits - USD 19.2 million) and further accumulation of short-term liabilities by the government (USD 51.9 million in H1 2001 compared to USD 45 million in the corresponding period of previous year).

Despite severe electricity cuts in Q1 2001, incomes from international, including personal tourism recorded in the Balance of Payments, grew to USD 47.4 million in H1 2001, compared to USD 37.7 million last year. The growth of revenues from tourism is related to improvement in the accounting of the travel sector and also to changing structure of foreign tourism in favour of non-CIS countries' citizens, who usually spend more money than Former Soviet Unions citizens. However, this figures are very small compared to the potential in the sector. Rapid growth of international tourism in Georgia is hampered by a number of factors: underdeveloped infrastructure, geographical proximity to Chechnya and worsening criminal situation.

Table 2.2: Balance of Payments, H1 1999, H1 2000, and H1 2001
(USD millions)

	1999		2000		2001	
	Q 1	Q 2	Q 1	Q 2	Q1	Q2
Current account Balance	**-68.7**	**-57**	**-72.8**	**-63.7**	**-73.5**	**-65.2**
Goods	**-154.2**	**-142.6**	**-128.6**	**-116.9**	**-141.3**	**-134**
Credit	52.2	75.5	97.8	128.1	94.5	124.2
Debit	-206.4	-218.1	-226.5	-245	-235.8	-258.2
Services	**-2.5**	**4.4**	**4**	**5.2**	**9.1**	**8.8**
Credit	46.6	63.3	50.6	48.4	61.1	67.4
Debit	-49	-58.9	-46.6	-53.7	-52	-58.6
Incomes	**30.6**	**32**	**21.1**	**29.7**	**13.1**	**12.4**
Credit	42.6	45.3	36.2	42.5	24.3	27.6
Debit	-12	-13.3	-15.1	-12.7	-11.3	-15.1
Current transfers	**57.3**	**49.1**	**30.8**	**28.6**	**45.7**	**47.6**
Credit	63.3	56.3	35.8	35.5	50.8	53.4
Debit	-6	-7.1	-5.1	-6.9	-5.2	-5.8
Capital and Financial account Balance	**80**	**68.4**	**25.8**	**22.3**	**64.7**	**47**
Capital account	**-1.7**	**-1.8**	**-1.2**	**-1.1**	**-1.6**	**-1.1**
Financial account	**81.7**	**70.2**	**27.1**	**23.3**	**66.3**	**48.1**
FDIs	19.2	22.1	33	30.2	21.3	35.6
Portfolio investments	0	0	2.5	0.2	-1.3	1.2
Other investments	43.7	36.5	-17.9	-20.1	51.4	12.5
Reserves	18.9	11.6	9.4	13	-5	-1.2
Net errors and omissions	**-11.3**	**-11.4**	**46.9**	**41.5**	**8.8**	**18.2**

Source: State Department for Statistics

[12] USD 49.5 million in H1 2001 and USD 78.7 million in H1 2000.
[13] The transfers of long-terms workers' in Georgia in H1 2001 amounted to USD 48.1 million and to general government USD 19.5 million, while in the same period of 2000 the corresponding figures were respectively, USD 42.2 million and 0.

CHAPTER THREE: GOVERNMENT FINANCE

According to the 2001 State Budget, total revenues in the first half of the year were expected to reach GEL 407.4 million, that is 48 per cent of total revenue expectations for the whole year., while expenditures were set at GEL 480 million, 40 per cent of the yearly target. The deficit therefore was estimated at GEL 72.6 million. Actual state revenues received were GEL 357.3 million GEL 50 million less than planned. Not all the anticipated external payments were received. Actual expenditures were cut accordingly, to GEL 397.5 million, that is to 82.8 per cent of the initial size. Tax administration improved in terms of absolute and percentage increases over the year. The continuing reforms in tax collection agencies are supposed to boost tax revenues further.

STATE BUDGET REVENUE

Initial revenue projections for the state budget in H1 2001 envisaged receipts of GEL 416.7 million. Actually receipts were GEL 357.3, 85.7 per cent of the planned amount. The shortfall of GEL 60 million is explained mainly by lower than projected revenues from customs and delays of transfers due from one of the regions of Georgia. Also some expected external grants were not received. The tax revenue target was set at GEL 251.6 million, 48 per cent of tax revenue projections for the whole year. Actual receipts of GEL 225.9 million were closer to projected figure and indicates a 89.8 per cent performance.

GEL 30.9 million in non tax revenues were short of target by 11 per cent. Of this amount GEL 22 million was profit of the National Bank of Georgia. Capital Revenues were 53.3 per cent of projection, in total GEL 2.4 million

A comparison of 2001 State Revenues with planned and previous year figures is provided in table below.

Table 3.1: State budget revenues H1 2000
(GEL millions)

	H1 2001 Projection	H1 2001 Actual	Performance compared to plan (per cent)	H1 2000 Actual	Growth over the year (per cent)
Total Revenue and Grants	416.7	357.3	85.7	273.4	31
Total Revenue	394.1	351.5	89.2	273.4	29
Tax revenue	251.6	226.0	89.8	195.7	15
Non-tax revenue	34.7	30.9	89.0	9.3	232
Special State Funds	107.8	94.6	87.8	68.4	38
Grants	22.6	5.8	25.7	0.0	

Source: Ministry of Finance

Despite the fact that actual revenues were below projections, the figures show a substantial improvement over the previous year. An increase of 232 per cent in non tax revenues over the year is a result of transfer of the National Bank's profit to the central budget. In 2000, a similar transfer took place later in the year. Nominal increased of 15 and 38 per cent in tax revenues and special state funds revenues indicate improvements in tax collection. Based on more than 6 per cent inflation between the periods and economic growth of 1.9 per cent, Ministry of Finance suggests that with same level of administration nominal growth of tax, collected by state tax department, over the year would have been 8.1 per cent. The growth over this figure is explained by improved administration.

38 per cent growth of revenues of special state funds, along with improved administration reflects changes in legislation which sets a minimum contribution per employee of GEL16. In the same way, considering exchange rate changes and import growth, the Ministry estimates the normal growth of taxes import at 15 per cent.

A detailed breakdown of tax revenues is presented in Table 3.2 below.

Table 3.2: Tax revenues of Central Budget, H1 2001
(GEL million)

	H1 2001 Projection	H1 2001 Actual	Performance compared to plan (per cent)	H1 2000 Actual	Nominal growth over the year (per cent)
Tax revenue	**251.6**	**226.0**	**89.8**	**195.7**	**15**
Income tax	**8.0**	**8.4**	**106.2**	**17.2**	**-51**
Profit tax	**5.8**	**3.2**	**54.7**	**14.5**	**-78**
VAT	**153.2**	**154.3**	**100.7**	**115.5**	**34**
On domestic products	*91.9*	*93.4*	*101.6*	*72.0*	*30*
On imports	*61.3*	*60.9*	*99.4*	*43.5*	*40*
Excise	**62.7**	**39.3**	**62.7**	**33.6**	**17**
On domestic products	*6.8*	*10.7*	*156.8*	*4.5*	*138*
On imports	*55.9*	*28.6*	*51.2*	*29.1*	*-2*
Customs duty	**34.7**	**30.9**	**89.2**	**14.6**	**112**

Source: Ministry of Finance

The decline in income and profit tax revenues over the year reflects changes in legislation. Now the Central Budget retains a lower proportion of receipts from these sources. For all levels of budget, collection (administration) of income tax improved by 20 per cent, while profit tax receipts worsened by 30 per cent. The shortfall in collection profit tax is partly conditioned by the complexity of its administration; on the other hand it is response of the business sector to an increased effective burden of other taxes.

The collection of VAT, both, on domestic products and imports has improved considerably with nominal growth of 30 and 40 per cent respectively. After adjusting nominal growth to macroeconomic changes, the Ministry of Finance suggests that administration of domestic VAT has improved by 14.7 per cent and for imported products by 9.9 per cent. The difference between the figures reflects the state of administrative reforms in tax collection bodies which was commenced in the State Tax Department much earlier than in Customs Department. The same applies to collection of excise duty, which shows a surplus on domestic products while receipts from imported goods were short of target by 50 per cent.

Revenues from excise goods

The administration of excise duty remains problematic. The central budget received GEL 38.8 million as taxes on oil products of which GEL 20.7 million comes from VAT and GEL 18.2 million from excise duty. The amount is twice as much compared to corresponding revenues of the previous year. Nevertheless, revenues from gasoline import was 88.1 per cent of projected figure and revenues from other oil products only 44.2 per cent. Improvements in customs administration are obvious but still it is far from being perfect as actually registered oil product imports are far below the consumption levels. In contrast, revenues from taxation of tobacco and alcohol is far below the previous year's level. Revenue collections on imported tobacco products was 23.2 per cent of target. The GEL 6.6 million received as excise on imported tobacco, was GEL 4.5 million less than H1 2000 revenues. In total, the central budget received GEL 14.4 million from taxation of tobacco products. Under excise on alcohol, budget revenues were GEL 1.7 million mainly from domestic products.

SPECIAL STATE FUNDS

Own revenues of Special state funds were expected to be GEL 18 million. Actually only GEL 94 million (87 per cent of target) were received.

Table 3.3: Revenues and expenses of the United State Social Safety Fund, H1 2001
(GEL million)

Revenues	**97.3**
Taxes	75.5
Transfer from central budget	21.8
Expenses	**96.7**
Pensions	91.8
Social benefits	3.5
Administration	1.4
Balance carried down	0.6

Source: Ministry of Finance

Own revenues of the **United State Social Safety Fund** were short of target by GEL 9 million, but still higher than in the previous year. The Ministry of Finance estimates that the administrative improvement here is 9.4 per cent. Only 80.8 per cent of the due transfer from central budget was received. Pensions were financed at 92 per cent while various social benefits were 67 per cent of budget. Administrative expenses were less than 2 per cent of total expenditures of social security fund.

In contrast, the administration of **unemployment fund** revenues has worsened by 11 per cent. This is surprising as the tax base for the social safety and unemployment funds are the same. Different progress in administrative improvement indicates the low financial discipline of taxpayers (employers) and the inability of tax collecting bodies to control them. Revenues of unemployment fund were GEL 2.3 million instead of the planned GEL 2.6 million. Unemployment benefit programmes were financed at 28.7 per cent; temporary employment programmes at 66.7 per cent; programmes of facilitation of employment were financed at 37.5 per cent of budget. Total expenditures of the fund for H1 2001 were GEL 1.1 million instead of planned GEL 2.5 million. Balance on the funds accounts at the end of the period was GEL 1.1 million.

The roads fund received GEL 16 million instead of the planned GEL 20 million. The main reason for the shortfall was low excise revenues. Expenditures of the fund were GEL 15.6 million of which, GEL 11 million was spent on road maintenance, GEL 1.1 million was paid to various enterprises for goods and services provided in previous years. GEL 1.7 million was directed for co-financing of programmes financed by external credits.

STATE BUDGET DEFICIT FINANCING

The State budget envisaged GEL 72 million under sources of deficit financing for H1 2001. Due to unexpectedly low revenues from privatisation, treasury bill issuance and external sources, the National Bank had to issue a GEL 24 million credit to government. The deficit of state budget was financed by GEL 63.2 million, that is by 87 per cent of expected. Detailed figures on deficit financing is provided in Table 3.4 below.

Table 3.4: Sources of State Budget deficit financing
(GEL millions)

	Budget H1 2001	Actual H12001	Compared to Budget (Per cent)
›tal Deficit Financing	72.6	63.2	87.1
Domestic sources	9.9	32.3	325.6
Privatisation of state property	4.5	2.1	52.7
Treasury bills	5.4	4.6	14.2
NBG loan	-	24.1	-
Balance brought down	-	5.0	-
External sources	62.7	31.8	49.2
Structural adjustment credit	30.4	-	-
World Bank investment credits	32.3	30.8	95.5

Source: Ministry of Finance

STATE BUDGET EXPENDITURE

The Initial law on the state budget of for 2001 Envisaged GEL 1120.8 million on expenditure side. Later, in March, the budget law was amended and the total expenditure figure for the year was set at GEL 1,195.6 million. From this amount, GEL 997.6 million was set as an expenditure target for the central budget. Amendments were mainly for central budget expenditures as follows: GEL 65 million for principal payments to the National Bank of Georgia; GEL 3 million for the Presidential Fund; GEL 3 million for electricity charges of IDP-s; and GEL 1.6 million for implementation of court decisions.

The Ministry of Finance has set the central budget expenditure target for H1 at GEL 381.4 million, 38 per cent of yearly figure. The low proportion for H1 is conditioned by expected higher expenditures later in the year. More than two thirds of principal and interest payments on foreign debt fall due in H2. The same applies to World Bank investment projects. Repayment of the NBG’s credit of GEL 65 million is planned in H2.

Actual spending of central budget in H1 was GEL 305.8 million, that is 81 per cent of budgeted. Nevertheless actual expenditures were GEL 31.5 million higher than in the previous year. The main priority was social security expenditures. The GEL 48.2 million spent under social security category was 91 per cent of budgeted. In contrast, funding for health care and education were among the lowest in terms of budgeted figures. About GEL 12 million wereapportioned for each category were that is about two thirds of the corresponding targets. In 2001 some educational institutions which had previously been financed from central budget moved to financing from Tbilisi municipality. Nevertheless, central budget spending on education was slightly more than in the previous year. Spending on health care was twice as much as in the previous year.

Security was financed in line with overall budget execution. Defence received GEL 16 million 83 per cent of budgeted while spending under “Law and Order” (Police, Courts etc) category of GEL 36.5 million were 81 per cent of target. For both categories increase in actual financing over the year was 52 per cent.

The largest spending category “other” is comprised of foreign debt repayments and transfers to local budgets. The GEL 96 million spent under this category in H1 2001 was GEL 7 million less than in 2000. Expenditures were reduced because of the restructuring of foreign debt.

66 per cent of initial expenditure target for H1 2001 comes on secured categories. The share of secured expenditures in actual spending was 72 per cent. Salaries of 150,000 employees are financed from central budget; 270,000 are eligible for various state benefits; 900,000 are pensioners; about 50,000 people benefits from transfers to local budgets. In total, about 1/3 (1.4 million) of the Georgian

population are in some way directly financed by the state budget. Principal and interest payments on state debt is another large secured category. The detailed breakdown of central budget expenditures by economic category is presented in Table 3.5 below.

Table 3.5: Central budget spending by economic category, H1 2001
(GEL thousands)

Category	Expenditure	Compared to budget (Per cent)
Salaries	35,322	83
Social Contributions	7,706	77
Business trips	2,161	71
Other goods and services	38,461	64
Interest payments	53,907	85
Subsidies and current transfers	107,643	89
Capital expenditures	642	40
Target programs	11,692	55
Net lending	48,312	83
Total	**305,846**	**80**

Source: Ministry of Finance

Salary expenses were 59 per cent higher compared to the previous year, while business trips declined by 10 per cent. Under “other goods and services”, office maintenance expenditures were 59 per cent of budget; utility charges were 73 per cent; transport maintenance 74 per cent, and food purchasing 94 per cent. Unlike previous years the above distribution proves the social orientation of Government spending priorities.

Under interest payments, GEL 21 million was for foreign debt servicing and GEL 31.6 million was paid as interest to the National Bank of Georgia. GEL 11.5 million was principal payment on external state debt under the “net Lending” category.

CHAPTER FOUR: MONEY AND FINANCE

MONETARY INSTRUMENTS

Government Treasury Bills

The IMF programme targets for 2001 stipulate that GEL 20 million of the deficit financing should be from T-Bills. It requires GEL 65-70 million of gross emissions during 2001. T-Bills are issued according to a special schedule worked out by the Ministry of Finance and the National Bank of Georgia (NBG). During January-August 2001, there were 14 28-days T-Bills auctions with a gross emission of GEL 18 million and 12 91-days auctions with a gross emission of GEL 18.6 million. Table 4.1 illustrates the volume of emissions, demand and weighted average interest rates fixed on the T-Bills auctions. T-Bills issued in H1 2001 completely repaid GEL 6.2 million of T-Bills debt outstanding from 2000.

Table 4.1: Results of T-Bills auctions, January-August 2001

Maturity	Date	Emission (GEL)	Demand (GEL)	Average Weighted Interest Rate (%)
28 days	10-01-01	1 000 000	1 650 000	19,77
	31-01-01	1 800 000	4 080 000	16,54
	21-02-01	1 750 000	1 950 000	18,17
	21-03-01	1 800 000	980 000	26,82
	28-03-01	1 000 000	350 000	26,82
	18-04-01	1 050 000	1 050 000	28,77
	25-04-01	550 000	992 300	26,54
	16-05-01	1 100 000	1 389 000	28,75
	30-05-01	1 000 000	1 293 000	32,16
	13-06-01	1 500 000	3 213 100	27,95
	27-06-01	1 500 000	3 525 000	20,39
	18-07-01	1 500 000	1 335 500	20,55
	8-08-01	1 000 000	2 050 500	22,37
	15-08-01	1 500 000	2 351 500	22,16
91 days	7-02-01	1 500 000	1 700 000	21,28
	28-02-01	1 950 000	800 000	20,97
	7-03-01	1 950 000	1 300 000	32,45
	10-05-01	1 600 000	2 366 100	32,28
	23-05-01	1 000 000	1 911 000	31,41
	6-06-01	1 500 000	1 744 400	41,44
	4-07-01	1 000 000	1 744 400	21,07
	11-07-01	2 000 000	3 022 500	21,32
	25-07-01	1 750 000	1 704 000	28,85
	8-08-01	1 750 000	1 962 300	40,96
	22-08-01	1 300 000	1 962 300	31,60
	29-08-02	1 300 000	1 220 600	34,35

Source: National Bank of Georgia

The devaluation of Lari and the deterioration of the trade balance, which took place in Q1 2001, increased the investment risk. As a result, in those months demand for T-Bills decreased. Emissions exceeded demand especially for 91 days maturity T-Bills (see Table 4.1).

The interest rates fixed on T-Bills auctions during these eight months were changeable. From January to May the interest rates for both maturities showd an upward trend. In the summer when there is seasonal growth of business activity, commercial banks express much interest towards investment into government securities. Since June, as the data show, there was increasing demand for T-Bills, thus the interest rate for T-Bills of both maturities fell. But in the next months and by the end of the year, we expect interest rates to increase. The reason is the fact that the Ministry of Finance plans to issue GEL 35-40 million to finance the budget (net financing will be GEL 5-7 million). It means that there is high probability that emissions will exceed demand and it will push up interest rates.

The structure of commercial banks holding T-Bills has changed since Q1, 2001. In March, one bank held about 75 per cent of all issued T-Bills. According to August 2001 data, the share of that bank fell to 25 per cent, but the remaining portion of outstanding T-Bills is distributed between the other three large commercial banks.

The secondary T-Bills market has not developed yet. There are several reasons for that. The volume of emissions is relatively small. The market is not diversified: there are only banking institutions that are participants on the market and their number is very limited. The income tax from deals with T-Bills on the secondary market is 20 per cent meanwhile tax from primary market deals is 10 per cent. The taxation rate from deals with T-Bills on the secondary market should be less to stimulate activity.

REPO Market

In Q1 2001, there were two deals on the REPO market. The NBG sold T-Bills from its portfolio to commercial banks. Such activity of the NBG was directed to stimulate the T-Bills market. However, further direct purchasing of T-Bills by the NBG could cause increases in the cost of government debt service. That was the reason why the NBG stopped REPO operations.

In April 2001, the NBG made a decision to start reverse REPO operation buying T-Bills from are bought from commercial banks for a short term and then sold back again. This operation might give the opportunity to commercial banks to use their T-Bills for obtaining short term liquidity. It might also stimulate the T-Bills market. However, there was only one reverse REPO operation (see Table 4.2 below). One can say that banks that have T-Bills are not interested in short –term liquidity.

Table 4.2: Results of a reverse REPO auction, 2001

Date	Volume of deals (GEL)	Number of deals	Maturity (days)	Annual interest rate (per cent)
13.08.01	5,000	1	7	7

Source: National Bank of Georgia

Interbank Credit Auctions

Table 4.3: Interbank Credit Auctions. Q1 2001

Month	Volume (GEL)				Annual weignted average (per cent)			
	7-days	30-days	60-days	90-days	7-days	30-days	60-days	90-days
April	0	727 000	0	0	-	18.5	-	-
May	0	389 000	0	480 000	-	16.5	-	20
June	1000 000	197 000	0	180 000	5	14	-	15
July	0	330 000	0	165 000	-	15	-	14
August	0	850 000	0	0	-	25	-	-

Source: National Bank of Georgia

On 7th July, there was only one 7-days auction with a total volume of GEL 1 million. The whole sum was purchased by the NBG. The probable reason for stagnation on this market was the relatively low interest rate (around 5 per cent annual) and liquidity holding banks are not interested to invest money at such rates.

During April-August 2001, the total turnover of 30-days credit auctions was GEL 2.5 million of which only GEL 26 thousand was bought by the NBG. The interest rates fixed on the auctions show upward trend reaching 23 per cent annual at the last auction on 30th August,2001.

During the same period, the total volume of 90-days credit auctions was GEL 825 thousand of which GEL 710 thousand were deals between commercial banks. The NBG bought GEL 115 thousand. The interest rate on 90-days auctions was less than on 30-days auctions and fell from 20 per cent annual in May to 14 per cent annual in July. There were no deals in August.

EXCHANGE RATE AND DOMESTIC FOREIGN EXCHANGE MARKET.

The seasonal outflow of foreign currency for payments of imports and falling exports caused the depreciation of the Lari that started in January and continued during Q1 2001. Low levels of tax revenues was also a serious reason of Lari depreciation. On 22nd February 2001, GEL/USD rate reached 2.165, the lowest price of GEL since the beginning of 1999. The monthly average nominal exchange rate of the Lari was GEL/USD 2.0636. In March, the official average GEL/USD rate was 2.0651. The nominal exchange rate in the next months did not show the stable trend towards an appreciation of the Lari as had been expected. It fluctuated insignificantly during April-August within a narrow corridor. The nominal exchange rate changes did not have significant effect on prices.

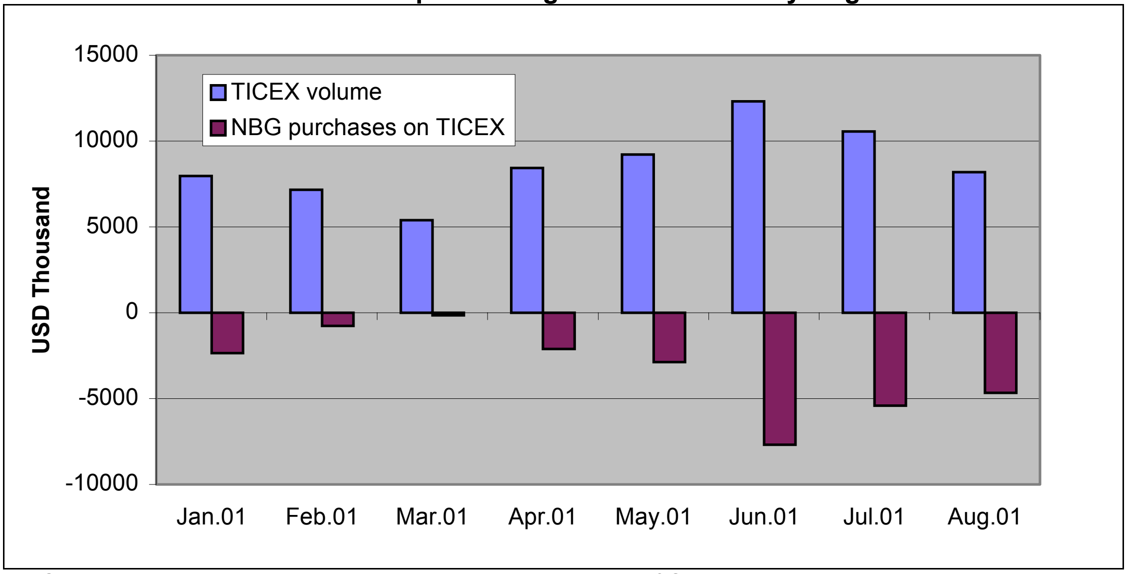
In April, the Lari appreciated slowly vis-à-vis the US dollar. The lowest rate of the official exchange rate of Lari was GEL/USD 2.0700, the average monthly exchange rate was GEL/USD 2.0511.

On 22nd May 2001, there was slight depreciation of the Lari against the US dollar. GEL/USD nominal official exchange rate reached 2.0801 the lowest level of the Lari during the month. The official average monthly exchange rate was GEL/USD 2.0654.

In June, the average nominal exchange rate appreciated up to GEL/USD 2.0600 but in July it depreciated to GEL/USD 2.0670. In August, the official nominal average GEL/USD exchange rate slightly appreciated to 2.0643. One can expect that in the next four months the nominal exchange rate will fluctuate around GEL/USD 2.0700.

In 2001, the NBG continued its policy of non-intervention in support of foreign exchange rate, while purchasing foreign exchange on TICEX to replenish its international reserves to a level covering about 1.025 months of imports of goods and services by end-2001. During the period from January to August the NBG bought USD 26 million.

Figure 4.1: TICEX volume and NBG purchasing on TICEX. January-August 2001

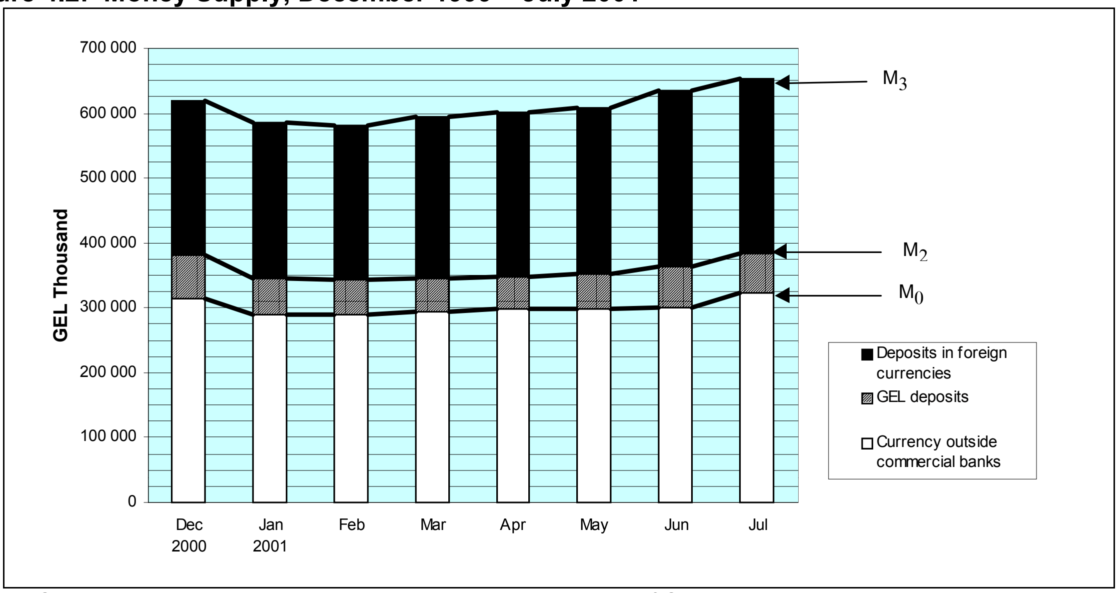


Source: GET calculations based on data provided by the National Bank of Georgia

The biggest partners of commercial banks' foreign currency trade outside TICEX are legal entities and individuals. Each month commercial banks sell about 50 per cent of the total amount sold to companies and buy from them about 65 per cent from the total amount purchased. The share of individuals is about 40 per cent from the total amount sold and about 25 per cent of foreign currency purchased by commercial banks.

MONEY SUPPLY

Figure 4.2: Money Supply, December 1999 – July 2001



Source: GET calculations based on data provided by the National Bank of Georgia

The NBG continued tight monetary policy in 2001. It foresees control over net domestic assets within the set up targets to avoid inflation emissions of money. During January-July 2001, money into circulation increased by GEL 14.7 million. Money outside commercial banks increased by GEL 7.3 million during the same period while deposit liabilities of commercial banks increased by GEL 27.6 million. As the result, M3 increased by GEL 35.1 million. Meanwhile M2 grew by GEL 1.3 million.

Table 4.4: Monetary Ratios

	2000	2001						
	Dec	Jan	Feb	Mar	Apr	May	Jun	Jul
Required reserves/ CBs Deposit Liabilities %	12,8	13,2	14	13,6	14,3	14,1	14,5	14,6
CBs Correspondent A/Cs in NBG/CBs Deposit Liabilities %	7,6	6,9	3,7	2,8	1,6	2,9	4,5	3,9
Cash in CBs/ CBs Deposit Liabilities %	4,7	5,4	6,5	5	5,6	5,1	5,8	6,5
Total CBs Reserves/ CBs Deposit Liabilities %	25,1	24,4	24,1	20,9	21,8	21,9	24,5	24,7
Dollarisation Ratio %	77,9	81,5	81,9	83,3	83,7	82,3	81,5	81,5
Money Multiplier (M2)	0,98	0,94	0,95	0,96	0,96	0,96	0,95	0,95
Money Multiplier (M3)	1,58	1,6	1,61	1,66	1,66	1,66	1,66	1,61

Source: National Bank of Georgia

During January-July 2001, deposits in foreign currencies increased by GEL 33.8 millions while deposits in Lari fell by GEL 6 million. Deposit dollarisation ratio is still high and in April it was about 84 per cent but by the end of July it fell to 81.5 per cent. The M2 money multiplier is less than one while M3 multiplier continues has continued to grow since the beginning of this year.

DOMESTIC INFLATION

Table 4.5: Consumer Price Index and Inflation

December 1998 = 100

Period		Price index	Inflation Rate (per cent) (i) From previous period
2000	Jan	111.30	0.40
	Feb	109.30	-2.00
	Mar	109.20	-0.10
	Apr	109.00	-0.20
	May	108.90	-0.10
	June	108.60	-0.30
	July	108.30	-0.30
	Aug	109.50	1.20
	Sep	111.30	1.80
	Oct	112.50	1.20
	Nov	112.56	0.6
	Dec	113.06	0.5
2001	Jan	113.13	0.7
	Feb	113.19	0.6
	Mar	113.19	0.0
	Apr	114.19	1.0
	May	113.19	-1.0
	Jun	113.15	-0.4
	Jul	113.08	-0.7

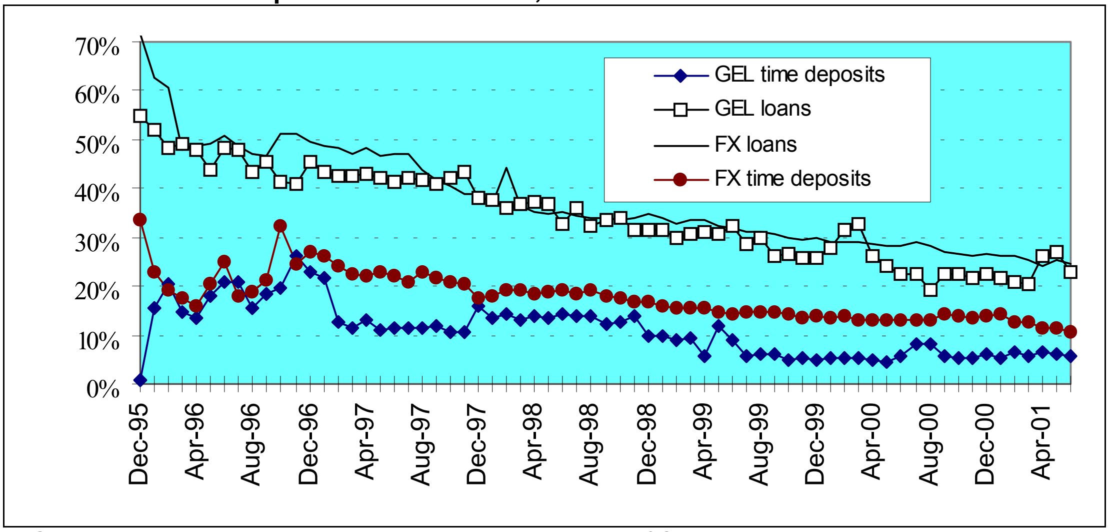
Source: GET calculations based on data provided by the State Department for Statistics

The level of inflation in Georgia strongly depends on the GEL nominal exchange rate. The NBG maintains tight control over emission of money into circulation that is a precondition of a stable exchange rate. According to "Main Trends on Monetary and Foreign Exchange Policy", the targeted inflation should be 6 per cent in 2001.

In May, June and July there was deflation (total –2.1 per cent) that was stipulated by a seasonal decreasing of prices on agricultural products. During seven months CPI increased by 2 per cent that gives a possibility to say that the inflation level will be kept within the annual targetof 6 per cent.

INTEREST RATES

Figure 4.3: Loans and Deposits Interest Rates, December 1995 - June 2001



Source: GET calculations based on data provided by the National Bank of Georgia

Interest rates for lending in Lari in April and May 2001 were higher than lending interest rates in foreign currencies. Interest rates for time deposits in Lari were stable while in foreign currencies they have been gradually decreasing.

BANKING

The main source of Georgian commercial banks' income is income from loans. During the period from January to June 2001, interest income from business loans was 65 per cent from interest and other incomes from loans, while the interest income from households was 34 per cent. Interest income from inter-bank loans was only one per cent.

The share of non-interest income is 45 per cent - less than income from loans, though this share of banks' income has grown during recent years. In non-interest income the share of fees and commissions is 33 per cent,, gains from conversion operations is 13 per cent. The biggest share of non-interest income of commercial banks in January-June 2001 was income from other non-interest income operations (53 per cent) that generally includes income from revaluation of assets in foreign currencies.

The structure of lending portfolio of commercial banks by the sectors of the economy remains unchangeable. According to the NBG data, in June 2001, 69 per cent of commercial banks' loans were issued to trade and industry (22 per cent), the shares of construction and agriculture were 6 and 3 per cent correspondingly.

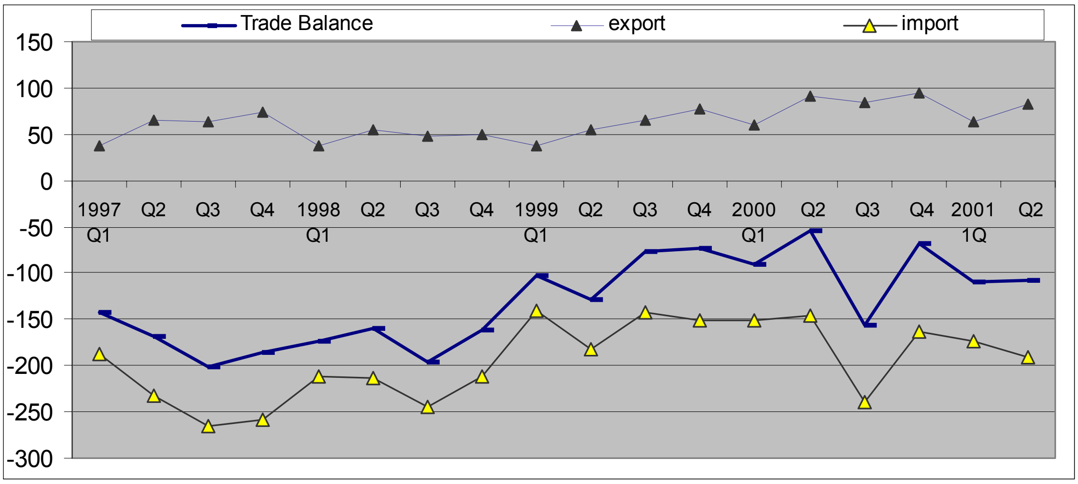
CHAPTER FIVE: INTERNATIONAL TRADE AND FOREIGN ECONOMIC RELATIONS

TRADE TURNOVER, TRADE BALANCE AND DIRECTION OF TRADE

The negative trade balance of Georgia increased in H1 2001, compared to the same period of the previous year. Recorded external trade turnover amounted to USD 511.1 million, of which exports were USD 147.1 million and imports USD 364 million. The trade deficit of USD 217 million is about USD 83 million more than in H1 2000. The best indicator of the country's position on the world market, which shows the trade balance of the country the export coverage ratio decreased during H1 2001 to 40 per cent. Georgia's export coverage ratio in H1 2000 was 51 per cent.

During the recorded period Georgia had trade deficit with 81 partner countries. The trade deficit with the CIS countries accounted for about 35 per cent of total deficit.

Figure 5.2: Registered exports, imports and trade balance, Q1 1997 – Q2 2001
(USD thousands)



Source: Data from the State Department for Statistics

The share of the ten main trade partners in the total registered trade was equal to about 75 per cent. As indicated in Table 5.1, the main partners in the first half of 2001 were Turkey, Russia, Azerbaijan and Germany. These countries together represented more than 40 per cent of Georgia's registered trade turnover.

The neighboring countries of Turkey, Russia and Turkmenistan are the main markets for Georgia's exports. Despite the fact that, there was growth of exports to Turkmenistan (military aircrafts) by USD 14 million, Georgia's export to strategic partner countries - Azerbaijan, Ukraine and Germany decreased sharply. For instance, exports to Azerbaijan went down from USD 20.7 million (1H 2000) to USD 5.1 million, exports to Ukraine went down from USD 11.5 to 4.8 million and exports to Germany decreased from USD 20.4 to 3.7 million.

Table 5.1: Registered International Trade Turnover and Direction of Trade, H1 2001
(USD thousands)

International Trade Turnover	Import (CIF)		Export (FOB)		Trade Turnover	
	USD	Per cent	USD	Per cent	USD	Per cent
Total	**364, 039.9**	**100**	**146, 079.4**	**100**	**511, 119.3**	**100**
Main partner countries (total)	267,940.8	73.6	114,408.8	78.3	*382,349.3*	**74.8**
Russia	*53,334.0*	*14.6*	*30,292.6*	*20.7*	*83,626.6*	*16.4*
Turkey	*50,397.7*	*13.8*	*33,090.5*	*22.6*	*83,488.2*	*16.3*
Azerbaijan	*37,532.6*	*10.3*	*5,141.4*	*3.5*	*42,674.0*	*8.8*
Germany	*33,587.3*	*9.2*	*3,716.2*	*2.5*	*37,303.5*	*7.3*
Ukraine	*28,393.9*	*7.8*	*4,785.0*	*3.3*	*33,178.9*	*6.5*
USA	*28,904.9*	*7.9*	*2,821.3*	*1.9*	*31,726.2*	*6.2*
Turkmenistan	*7,246.1*	*2*	*14,338.4*	*9.8*	*21,584.4*	*4.2*
UK	*12,416.4*	*3.4*	*6,077.0*	*4.2*	*18,493.3*	*3.6*
Italy	*10,054.7*	*2.8*	*5,114.2*	*3.5*	*15,168.9*	*3.0*
Switzerland	*6,073.2*	*1.7*	*9,032.2*	*6.2*	*15,105.4*	*3.0*
Others	**96,099.1**	**26.4**	**31,670.6**	**21.7**	**128,770.0**	**25.1**

Source: The State Department for Statistics

Table 5.2: Registered imports by region and country of origin, exports by destination, H1 2001

	Import		Export	
	USD thousands	Per cent	USD thousands	Per cent
CIS (including Russia)	138,955.7	38.2	62,968.2	42.8
EU	90, 360	24.8	27, 961	19
Turkey	*50,397.7*	13.8	*33,090.5*	22.5
USA	*28,904.9*	8	*2,821.3*	2
Others	55, 421.7	15.2	20, 238	13.7

Source: The State Department for Statistics

During the recorded period, the EU was the second largest trade partner of Georgia after the CIS (including Russia). The EU was a destination for 19 per cent of Georgia's registered exports.

COMPOSITION OF REGISTERED EXPORTS

Twelve product groups represented about 74 per cent of all registered exports during H1 2001. Ferrous scrap and ferroalloys (HTS chapters 7202, 7204) accounted for 16 per cent of all exports in the recorded period. The main markets for this product category were: Turkey, Russia, Italy, and Spain.

Precious metal ores and concentrates, copper ores and concentrates (HTS chapter 26 “Ores, slag and ash”) represented 10 per cent of all exports in the recorded period. Belgium and Switzerland were the main markets for this product category.

The first half of 2001 was characterized by significant growth of export of military aircrafts (mainly for Turkmenistan), which changed the structure of exports. The share of aircraft exports has gone up to about 10 per cent of all exports. This sector could be considered as a long run export oriented sector in which Georgia has some advantage.

The exports of wine of fresh grapes (HTS chapter 2204), compared to the respective period in the preceding year increased quite substantially- by 22 per cent. Destinations of exports of this category were Russia, Ukraine and USA.

Other main export items are mineral fuels (HTS chapters 2709, 2710, 2718), which represented 9.2 per cent of all exports in the recorded period, aluminum (HTS chapters 7602, 7601), nuts (HTS chapter 0802), natural and mineral waters (HTS chapters 2201, 2202), copper (HTS chapter 7404), and fertilizers (HTS chapter 3102).

Table 5.3 indicates the main registered export items according to the Harmonized Commodity Description and Coding System (HS).

Table 5.3: Composition of registered exports according to the Harmonized Commodity System by HTS 4-digit categories, H1 2001

	2001 H1	
	USD thousands	Per cent
Total exports	**147,079.4**	**100**
Ferrous waste and scrap; scrap ingots of iron or steel-7204, ferroalloys -7202	23, 305.6	15.8
Precious metal ores and concentrates-2616; copper ores and concentrates- 2603 and etc.	14, 849.8	10
Aircrafts, spacecraft, and parts thereof – 8802, 8803	14, 174.3	9.6
Wine of fresh grapes, including fortified wines -2204;	13,961.1	9.4
Petroleum oils and oils from bituminous minerals, crude –2709; petroleum oils and oils from bituminous minerals –2710; electrical energy –2716.	13, 630.8	9.2
Aluminum waste and scrap-7602; aluminum, unwrought – 7601 and etc.	10, 004.0	6.8
Nuts, fresh or dried – 0802;	5, 891.3	4
Waters, including natural or artificial mineral waters- 2201, 2202;	5, 489.7	3.7
Copper waste and scrap - 7404	3, 859.7	2.6
Mineral or chemical fertilizers, nitrogenous –3102.	3, 448.3	2.3
Other	38,464.8	26.2

Source: State Department for Statistics

COMPOSITION OF REGISTERED IMPORTS

The structure of imports is changing gradually. The share of machinery and mechanical appliances and electrical machinery amounted to 16.5 per cent. This could be explained by an increase of investments. The share of food (milling industry, wheat etc) is slowly decreasing. But Georgia's dependence on foreign energy has continued, imports are again dominated by mineral products in H1 2001.

Table 5.4 shows the largest imported product groups that together constituted about 59 per cent of total imports in H1 2001. The share of petroleum oils and gases (HTS chapters 2710, 2711) in total imports in H1 2001 was more than 20 per cent.

The import of machinery (HTS chapters 84, 85) for the firs time reached 16.5 per cent of all imports. Other major imported product groups are medicines (6.4 per cent), electricity (3.2 per cent), aircrafts (3.1 per cent), and others (see table 5.4).

Table 5.4: Composition of registered imports according to the Harmonized Commodity System by HTS 4-digit categories, H1 2001

	2001 H1	
	USD thousands	Per cent
Total imports	**364, 039.9**	**100**
Petroleum oils and oils from bituminous minerals (other than crude) – 2710	39, 576.9	10.8
Petroleum gases and other gaseous hydrocarbons -2711	35, 217.7	9.6
Machinery and mechanical appliances; parts thereof -8411, 8419, 8431 and 8471	25, 378.4	6.9
Electrical machinery and equipment and parts thereof –8504, 8517, 8525, 8529, 8536, and 8544	23, 753.6	6.5
Medicaments –3004	19, 958.2	6.4
Electrical energy – 2716	11, 669.6	3.2
Aircraft, powered (for example, helicopters, airplanes); spacecraft and spacecraft launch vehicles - 8802	11, 546.2	3.1
Measuring, checking, precision etc. instruments and apparatus; - 9018 9028 9031	10, 987.6	3
Cigars, cheroots, cigarillos and cigarettes, of tobacco or of tobacco substitutes –2402, 2401	10, 079.2	2.7
Milling industry products; malt; starches; wheat gluten – 1101, and 1107.	10, 004.5	2.7
Motorcars and other motor vehicles designed to transport people – 8703; motorcars and other motor vehicles designed to transport people –8702.	9, 142.0	2.5
Wheat -1001	6, 865.1	1.8
Other	149, 860.9	41.1

Source: The State Department for Statistics

EXPORT AND IMPORT OF SERVICES

Services account for a significant share of the international trade of Georgia. The negative recorded foreign trade balance is partly offset by the slightly positive balance of trade in services (see Table 5.5). According to data for the balance of payments[1] 57 per cent of registered exports of services was revenues from transportation in H1 2001. Travel amounted about 37 per cent of all services.

Given the relative difficulty of measurement of trade in services compared with measurement of trade in goods, the share of unrecorded trade is higher in services than in the case of trade in goods. For instance, the SDS does not record education, health, business etc. services at all.

Table 5.5: Registered Export and Import of Services, H1 2001
(USD thousands)

	H1 2001		H1 2000	
	Exports	Imports	Exports	Imports
Total services	**128,576**	**110,662**	**99,070**	**100,282**
Transportation services	73,209	45,841	56,853	44,134
- sea transport	13,999	16,492	15,308	21,421
-air transport	12,559	15,218	9,108	14,288
-railway transport	33,858	6,163	29,286	2,884
-auto transport	9,550	7,969	0	5,542
- pipe lines	3,243	0	3,153	0
Travel	47,343	51,032	37,675	48,580
Other Services	8,024	13,789	4,542	7,567

Source: The State Department for Statistics, Balance of Payments

[1] By the time this issue of GET was ready for publication, only H1 2001 of balance of payments was available.

USA President grants duty-free access to the USA market for certain products that are imported from Georgia

On June 29, 2001 the USA President designated Georgia as a GSP beneficiary developing country. This decision will encourage the development of Georgia's foreign economic relations, using the existing Generalized Systems of Preferences (GSP). The purpose of the GSP is to offer developing and transition countries lower customs tariffs than those applied to the developed nations. This gives their exports preferential access to the developed markets. Almost all the developed countries operate GSP schemes.

The USA Generalized System of Preferences (GSP) provides preferential duty-free entry for more than 4,650 products from approximately 140 designated beneficiary countries and territories. The GSP programme was instituted on 1st January 1976, and authorised under the Trade Act of 1974 for a 10-year period. The authorization was renewed several times. The last authorisation expired on June 30, 1999, and was extended through to 30th September 2001.

Products which are grown, produced or manufactured in a beneficiary country and which meet the following Rules of Origin criteria are eligible for duty-free access under the GSP: 1). An article/product must be imported directly from a beneficiary country. 2) A minimum of 35 percent value must be added in a single beneficiary country. Any product, which includes foreign components, must have been substantially transformed into a new and different article in a beneficiary country.

Certain articles are prohibited from receiving GSP treatment. These include most textiles, watches, footwear, handbags, luggage, flat goods, work gloves and other leather wearing apparel. In addition, any other article determined to be "import sensitive" cannot be made eligible; in this regard, the GSP law specifically cites steel, glass, and electronic articles. Six categories of textile products are eligible for GSP treatment when the GSP beneficiary has signed an agreement with the Government of the USA certifying that the items are handmade products of the exporting beneficiary. To date, such agreements have been signed with Botswana, Colombia, Egypt, Guatemala, Jordan, Macao, Malta, Morocco, Nepal, Pakistan, Peru, Romania, Thailand, Tunisia, and Uruguay. GSP benefits for duty-free treatment of handicraft textile exports are available to other beneficiary governments that are prepared to initiate the required exchange of letters. The six covered tariff categories are 5701.10.13, 5702.10.10, 5702.91.20, 5805.00.20, 6304.99.10, and 6304.99.40.

Despite the fact that the overall size of the GSP relative to total USA imports is small, many developing and transition countries use the USA GSP scheme very effectively. Among the former Soviet Union and east European countries the share of products exported under GSP in total exports (1999) to the USA is quite significant for Kazakhstan (83.2 per cent), Poland (36.3 per cent), Slovenia (35.1 per cent), Czech Republic (27.2 per cent), Slovakia (25.7 per cent) and Croatia (22.7 per cent)[2].

Box 5.1

USA Suspends Ukraine's Generalized System of Preferences Status

On 7th August, 2001 the United States of America Government decided to suspend the special duty-free - GSP status for Ukrainian products and issued a preliminary list of other products that could face sanctions, due to Ukraine's persistent failure to curb unauthorized production of optical media products (CDs, CD-ROMs, etc.). USA industries have estimated that this massive piracy has caused over USD 200 million in annual damages and has disrupted markets throughout the region and beyond. A year before the USA suspended GSP status for Belarus.

[2] Source: GEPLAC calculations based on the data provided by the USTR.

The USA Government had discussions with Ukrainian government officials over the past two years and despite a commitment by Ukraine to address the problem of rampant piracy; the unauthorised reproduction of optical disk media continues to grow.

Ukraine's special status comes from the USA Generalized System of Preferences (GSP), a programme designed to foster economic growth between the USA and developing country beneficiaries.

According to USA Government sources, Ukraine is the largest producer and exporter of pirated optical media products in Europe. Ukraine's exports of unauthorized compact discs (CDs) are disrupting markets throughout the region and beyond. For over two years, the United States of America has been urging Ukraine to take measures to stop this piracy and prevent its recurrence. Despite the commitments Ukraine its Government has failed to curtail the piracy. The two principal elements of these commitments were that Ukraine (1) would immediately use its existing law enforcement authority to stop the piracy and (2) by November 2000 would establish an optical media-licensing regime, which would serve to prevent a subsequent recurrence. Unfortunately, Ukraine still has not complied with either of those commitments.

Credible reports indicate that large volumes of optical media products continue to be pirated in Ukraine. Thus the USA Government felt compelled to suspend GSP treatment of Ukrainian products. This suspension entered into the force from 24th August 2001. If Ukraine continues to fail to honour its commitments to stop the ongoing piracy and to establish a strong optical media-licensing regime to prevent future piracy, then the USA Government may also act to impose trade sanctions on Ukraine.

Source: The USTR

GEORGIA AND THE WTO

At the moment the World Trade Organisation (WTO) unites 142 countries bound by international trade agreements adopted in the framework of the WTO. The most relevant issues are involvement of Georgia in the WTO “Millennium Round” where the results of Uruguay Round are to be reviewed and further developed with further multilateral negotiations on liberalisation of trade in services.

In November 2001 in Dohar the capital of Qatar it is planned to hold a Ministerial conference, which is the highest decision-making body of the WTO. Member states have expressed the hope that this Ministerial conference could facilitate the start of the new multilateral negotiations round which unfortunately failed in the last ministerial conference in Seattle.

Already in the Uruguay Round WTO member-states agreed to start multilateral negotiations on further liberalisation of international trade in services not later than five years after the date of effect of the General Agreement on Trade in Services. In April 2001 the WTO Council of Trade in Services approved guidelines and procedures for the new multilateral negotiations on trade in services. The forthcoming negotiations will cover all the sectors of trade in services fully respecting the demand and supply principle. Since commitments of Georgia within the WTO in comparison to other WTO member states foresee a very liberal regime of international trade in services, it is within the best interests of Georgia to eliminate or at least reduce differences in the liberalisation of service markets of different states.

Georgia, as a WTO member state, has the right to initiate formal bilateral and multilateral negotiations with countries currently in the process of accession to the WTO. Georgia has already carried out such negotiation rounds with Russia, Kazakhstan, Moldova, Ukraine and Azerbaijan focusing on market access for trade in industrial goods and services. At present it is also planned to start bilateral negotiations with other CIS countries, not members of the WTO.

CHAPTER SIX: PRIVATISATION

The second quarter of 2001 saw little progress in terms of actual privatisation of medium and large enterprises (MLE). The Ministry of State Property Management (MSPM) continues with the preparation of enterprises for sale or liquidation. The objects easiest to privatise have been already transferred into private ownership, while the enterprises of special importance to the economy need more examination and time to be privatised. A tender to privatise the gas distribution company Tbilgazi and transfer into management of the Tbilisi water supply and sewage system is under way. The bankruptcy cases raised against some large enterprises last year have not yet been concluded.

SMALL ENTERPRISE PRIVATISATION

The trend in privatisation of small enterprises remains unchanged. The majority of small enterprises have been transferred out of state hands. As of 1st July 2001, 13,566 small enterprises had been approved for privatisation and 15,680 had actually been privatised[1]. Table 6.1 gives a sectoral breakdown of the privatisation of small enterprises. In the first half of 2001, 262 small enterprises were transferred into private ownership. Most of the small enterprises are in the trade and service sectors - 34 and 44 per cent respectively. According to the regional breakdown given in the Table A6.2 of the Statistical Appendix, 31 per cent of privatised small enterprises are in Tbilisi. The autonomous republic of Achara is still lagging behind other regions in terms of privatisation of small enterprises - in 2001 there were no small enterprises privatised in the autonomous republic.

Table 6.1: Small Privatisation by Sector (MSPM classification) as of 1st July, 2001

	Sector	Approved	Privatised	% of total privatised	Privatised in 2001
1	Manufacturing	392	311	2.0	6
2	Energy	56	54	0.3	5
3	Bread products	142	120	0.8	3
4	Agriculture & food	764	835	5.3	26
5	Construction	436	364	2.3	17
6	Trade	4,674	5,333	34.0	37
7	Services	5,540	6,974	44.5	132
8	Oil products	172	174	1.1	1
9	Health	785	618	3.9	7
10	Social sphere	415	681	4.3	22
11	Transport	190	216	1.4	6
	Total	13,566	15,680	100.0	262

Source: Ministry of State Property Management

The amount of initially available objects is diminishing. A significant number of small enterprises has merged with Joint Stock Companies (JSCs) or has been liquidated (see table A6.2 of the Statistical Appendix). At the same time some small enterprises have been split into two or more enterprises and some small enterprises have been established as a result of restructuring of the medium and large enterprises. These developments keep the privatisation process going and indicate that the secondary market is operating. Efficient or potentially efficient small enterprises or assets are finding new owners. Thus, it seems that in privatising small enterprises the reform is carrying on quite successfully.

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[1] The number of enterprises actually privatised can exceed those approved for privatisation since some are split up during corporatisation. The total number of small enterprises, including those not approved for privatisation, is not available. Small enterprises are those with a book value of less than USD 44,000 on April 1st 1993.

MEDIUM AND LARGE ENTERPRISE PRIVATISATION

Privatisation of the MLEs is facing difficulties. The largest enterprises need more time and effort to be privatised. In some cases vested interests of various groups create constraints to privatisation. Some investors proved to be not financially strong enough to fulfil the conditions of the investment programme set by the tenders. Some investors have problems coping with specific working conditions like electricity shortages during the winter. The most attractive and efficient MLEs have been already privatised and the rest are huge companies requiring serious restructuring and substantial investment. In terms of privatising large enterprises the second quarter of 2001 saw little progress. More was achieved in approving MLEs for corporatisation and in the establishment of JSCs.

Table 6.2 shows that as of 1st July 2001, the number of the medium and large enterprises approved for establishment as JSCs has increased to 1,426. It should be noted that in the second quarter of 2001 the number of enterprise approved for corporatisation increased by 92. The total number of medium and large enterprises established as joint stock companies reached 1,359. During the second quarter of 2001 the number of established JSCs increased by 27.

Table 6.2: Corporatisation of MLEs by Sector (MSPM Classification) as of 1st July, 2001[2]

Sector	Approved	Established	Established in 2001
Manufacturing	230	303	4
Bread products	61	45	3
Agriculture and food	391	305	2
Architecture and construction	228	164	2
Retail and Wholesale Trade	86	62	1
Services	22	22	1
Oil products	49	36	0
Gas	60	47	2
Transport and Communications	120	131	2
Social sphere	57	58	3
Healthcare	56	56	21
Energy sector	66	130	4
Total	1,426	1,359	45

Source: Ministry of State Property Management

According to the conditions of the Structural Adjustment Credit III (SAC), the MSPM continues working on the privatisation of the list of large enterprises. Twelve enterprises have been privatised from the first priority list and 26 from the second priority list. In six enterprises liquidation/bankruptcy procedures have been started. Among them are JSCs Saktseoliti, Elva, Tami, Kimbochko, Saksamtometalurgia and Azoti. If properly implemented, bankruptcy procedures will result in improvement of the operation of the enterprises or facilitate the sales of their viable parts.

Some large enterprises that seem to be viable are in the restructuring process. The enterprises JSC Sakartvelos Traktori, Medea and JSC Kolkhida, have been restructured. The separated parts of the restructured enterprises are being prepared to be sold by different types of tender, by cash auctions or face bankruptcy procedures.

The JSC **Sakartvelos Traktori** has been restructured and divided into three companies - Saktraktori, Imeri and Rioni. In case of Saktraktori the MSPM is waiting for the proposal from a potential investor.

[2] The MSPM has introduced some changes in this table. The sector “Mining and Chemicals” is now included in the “Manufacturing” sector. The type of activity of some enterprises has been reconsidered and now they are under different sector then before. The sector “Services” also has been introduced.

If the investor refrains to make a proposal, 5 per cent of the enterprise will be sold at a zero reserve price auction or some property will be taken out of the charter capital at the expense of the state share. Each of these decisions will transfer the majority share of the enterprise into private ownership. JSC Rioni is offered at a cash auction, while the JSC Imeri will face bankruptcy procedures.

The Ministry of Finance is to consider the sale of the assets of the JSC **Medea**. Meanwhile the restructured part of the enterprise will face the bankruptcy procedures and the liqiudator is already appointed.

JSC **Kolkhida** has been restructured and the enterprise is divided into 3 JSCs and 8 Ltds. The privatisation of JSCs at cash auctions and the Ltds - by investment tenders is under consideration. Letters offering the shares in companies have been sent to 5 foreign companies.

The majority shareholding of JSC **Elmavalmshenebeli** has been offered by tender four times but without any success. None of the tenders have collected bids. After these developments a plan for restructuring of the enterprise has been worked out with the assistance of USAID experts. According to the plan, the assets not related to the production process have been separated from the charter capital of the enterprise. Now a tender to privatise 75 per cent of the shares of the enterprise with a symbolic selling price by a tender is under preparation.

Restructured or separated objects will become attractive to potential investors, who refrain from investing in the oversized, insolvent and inefficient enterprises.

To privatise other large enterprises the MSPM is using such methods as sales by tender with discounted or symbolic opening prices, sales at cash auctions and sales of shares with a zero reserve price.

The MSPM issued a decree according to which, the state shares of JSC **Electromekanikosi** should be offered by a tender at a 75 per cent discount. If the tender brings no result, the company will be offered at a symbolic price for direct sale. After the failure to privatise JSC **Sakabreshumi** by tender, the sale of the enterprise at a zero reserve price auction was under consideration. However, the Kutaisi Mayor's Office and the MSPM halted this process. It was decided to sell the shares after a drain factory is taken out from the charter capital of the enterprise. This issue should be resolved by the shareholder's meeting.

The MSPM also plans to offer 5 per cent of the shares of **Kutaisi Litofoni** plant at a zero reserve price auction. The state currently owns 53.1 per cent of this enterprise. Some property of the state in this enterprise (4 per cent of the charter capital) is to be privatised. This process will transfer the majority shareholding of the enterprise into private hands.

Among the methods of privatisation mentioned above, sale of shares with a zero reserve price is the most effective. The previous 6 zero reserve price auctions have been successful and all shares offered at these auctions have been sold. However, this method of privatisation may have a negative impact on the future operation of the enterprise. New owners have no commitments or obligations to carry out rehabilitation or restructuring of the privatised object. In many cases new owners just want to own an enterprise and hope that they will have opportunities to invest in it later. As at the zero reserve price auction the shares are distributed among all bidders, thus, it may allow acquisition of an enterprise by many different owners with no common strategy and different goals and ambitions. This may significantly delay efficient operation of the enterprise and even keep it idle. Although the zero reserve price auction is the last measure to privatise enterprises, after tendering at 50 and then 75 per cent discount of the selling price fails to collect bids, in some cases it may be better to start liquidation process of an enterprise without offering it at a zero price auction. This may save time and ensure that the assets of the enterprise are purchased by more focused buyers.

Water Supply and Sewage System

JSC Tbiltskalkanali (water supply company of Tbilisi) is to be transferred into management for 10 years. The name of a company managing the enterprise for future 10 years is expected to be known in November. To facilitate the rehabilitation of the field the World Bank is to allocate a credit worth USD 25 million. The credit is for 35 years and has a grace period of 10 years with interest at 0.75 per cent per annum. The credit will allow water tariff to remain unchanged in the beginning of the reform. The preliminary stage of choosing companies by the tendering commission has already started. To participate in the tender a company has to have an experience of providing service to 1.5 million customers, and an annual turnover not less than USD 50 million. Seven companies have met the preliminary conditions. These are leading western European companies with sound financial, technical and institutional standing. They have to present technical and financial proposals and afterwards the winner of the tender will be chosen. The winner is expected to start operations in the first quarter of 2002.

Telecommunications

A tender to privatise telecommunication sector assets Sakartvelos Elektrokavshiri and Georgian Telecom was announced on 1st February 2001 and offered 75 per cent of the shares of Sakartvelos Elektrokavshiri (the dominant local telecommunications company) and 51 per cent of Georgian Telecom (the leading long distance operator in Georgia). The potential investors had to submit their proposals by 31st of May 2001 to the consortium of companies led by Commerzbank acting as a financial adviser to the process of privatisation. Even though the information about the tender was published in the Economist and disbursed by different means of mass media and Internet it has brought no results. On 17th August a repeated tender was announced offering 75 per cent of the shares of Sakartvelos Elektrokavshiri. The deadline for bids is set at 15th October. Privatisation of the telecommunication assets is extremely important since it will rehabilitate and improve the operation of the sector, bring substantial revenues for the state and also encourage the reform.

Energy sector

The energy sector experiences problems in providing reliable electricity supply especially during winter period. For further improvement it is necessary to proceed with the privatisation process, since the privatised assets are being rehabilitated and show better performance. The Ministry of Fuel and Energy is co-operating with the International Finance Corporation in developing future privatisation processes. The electricity distribution companies that are still in the state ownership, excluding the companies in Achara, Abkhazia and Ossetia, are being grouped into one company. This company is to be privatised by international tender. A tender for the management of the JSC "Elektrogadatsema" (transmission), "Electrodispecherizacia" Ltd. (dispatch) was announced and the technical and financial proposals of two bidders are under consideration. As for a tender for the management of Electricity Wholesale Market, the winner was chosen in September. The Spanish company Iberdrola was awarded a management contract for 5 years. The company will start to manage Electricity Wholesale Market in a month's time after signing the agreement with the Georgian party. The aim of these tenders is to diminish state intervention in the operation of the system of electricity supply, reduce corruption in the sector and base the relationships between the parties involved on market principles.

The MSPM announced a tender to privatise Tbilisi gas distribution company Tbilgazi. The conditions of the tender are quite liberal. There are no limitations regarding the tariff scheme the amount of investment and investment schedule. The investor has to have a capital of USD 50 million and at least 5 years of experience in distribution of gas. The deadline for the tender was 27th August. An Israeli company Tahal has submitted its proposal to the tendering commission.

Privatisation of the assets of telecommunication and energy sectors and water supply system will involve rehabilitation and investing in these fields. This will lead to an improved operation and future development of these sectors, which will have a positive impact on the performance of other fields of economy and be beneficial to the overall situation in the country.

CHAPTER SEVEN: EMPLOYMENT, INCOMES AND THE SOCIAL SAFETY NET

LABOUR MARKET

Although the economic status figures seem to be slightly improving over those of the recent years, the overall unemployment situation remains deeply flawed, and the employment trends remain largely unchanged reflecting grim prospects on the labour market. An overwhelmingly large share of the labour force are either unemployed, underemployed in terms of seeking more work or earn much less than is needed to keep their families out of poverty. Unsafe and unhealthy working conditions, as well as job and income insecurity are widespread.

UNEMPLOYMENT

Registration-based unemployment figures are not the most reliable tool to judge the real extent of unemployment, and cover only a portion of those without jobs. At the same time, some of those registered at the Employment Fund offices might in reality be engaged in some alternative, informal employment. Currently, there are virtually no incentives to register as unemployed: social assistance is almost non-existent (the sum of the benefit is symbolic – at an equivalent of approximately USD 6 per month with eligibility lasting for the first six months of the unemployment only) and the chances of finding a job by registering as a jobless job-seeker are minimal to say the least.

However, the number of those who bother to register as unemployed job-seekers has been growing since the beginning of 1999, after it dropped dramatically in 1998. In Q1 2000, it grew by 3.5 per cent against the previous year, and in Q1 2001 by another annual 14.4 per cent, accounting for 48.4 per cent and 31.8 per cent of the survey-based unemployment figures by "strict" and "loose" methodologies respectively. The total number of unemployed did not change so drastically, however, being smaller than in Q1 1999, and the participation rate being generally on a downward trend (accounting largely for the improved unemployment rates) it is really difficult to find a good explanation for such a "registration boom". In addition, neither the procedure for registration nor the eligibility criteria, nor the size of the benefit have changed.

A likely explanation though could be that formal civil servants having lost their official jobs due to staff cuts in the budgetary organisations, have registered. It can be assumed that many of them would have to engage in or continue with their alternative informal or unregistered activities to earn a living. Such people would be counted as employed by the SDS survey, therefore, registration figures, growing or not, do not say much about unemployment as far as ILO definitions are concerned[1]. Mostly they show the changing attitude of people towards unemployment registration, which can also be interesting. Another information that can be drawn from the registration figures is the number of benefit recipients that has grown immensely in Q1 2001 over the year. Taking into consideration that unemployment benefit eligibility lasts for only first six months of the registration, this suggests that many of the registered unemployed are new to registration. This could be another reflection of the unfavourable situation on the labour market, when the despairing unemployed register having last hope of finding at least some kind of job through the Employment Fund offices. Formally such people cannot be called "discouraged", since they are taking formal steps looking for employment, however, in the existing situation it is difficult to call such steps active. On the other hand, given the extremely theoretical chances of finding a job through registration and the very poor quality of such jobs, it suggests that before making the decision to register they might have tried all other possibilities of active job search without any success.

[1] In accordance with the ILO definition, employment is based on any work done for an hour during the reference period (a week).

Since registration unemployment figures are rather confusing, figures from the SDS Labour Force Survey (LFS)[2] and the SDS Household survey[3], though not fully able to reveal the real extent of the dramatic situation on the labour market and the real size of unemployment or of poverty, are used here for the analysis of the economic status of the population. No set of figures in this area being ideal, the ones drawn from the surveys are deemed to be the most useful in making conclusions about and tracing trends in the unemployment and labour participation rates, labour force, unemployment, employment and the population outside the labour force structure.

Table 7.1: Economic Status, Q I 2000 – Q1 2001*

(Thousands)

Economic Status	Q I 2000	Q II 2000	Q III 2000	Q IV 2000	Q I 2001
Total population over 15 years old	**3, 123**	**3, 151**	**3, 133**	**3, 199**	**3, 277**
Total economically active population (labour force) (1)	**1, 951**	**2, 102**	**2, 064**	**2, 095**	**2, 066**
Total economically active population (labour force) (2)	**2, 087**	**2, 199**	**2, 181**	**2, 215**	**2, 195**
Employed	***1, 705***	***1, 890***	***1, 890***	***1, 878***	***1, 818***
Hired	679	695	675	691	681
Self-employed	912	1087	1095	1, 080	1, 034
Unemployed (1)	**246**	**212**	**174**	**217**	**248**
Unemployed (2)	**382**	**309**	**292**	**337**	**377**
Unemployment rate (per cent) (1)	**12.6**	**10.1**	**8.4**	**10.4**	**12.0**
Unemployment rate (per cent) (2)	**18.3**	**14.0**	**13.4**	**15.2**	**17.2**

Source: Data from the SDS Household Survey
Note: (1) ILO Standard (or "strict" methodology
(2) ILO "Loose" Methodology
** When this issue of GET was ready for publication, Household Survey results for Q2 2001 were not available.*
For a more detailed table and 1998-1999 figures see Statistical Appendix Table A7.1.

The national unemployment rate continued to grow by another 1.6 percentage points to 12 per cent by the ILO "strict" methodology in Q1 2001 (17.2 per cent by the ILO "loose" methodology), after growing by 2 percentage points over the quarter in Q4 2000. However, in annual terms this was 0.6 percentage points and 1.1 percentage points decrease by the ILO "strict" and "loose" methodologies respectively. In Q1 2001 rural unemployment was just 3.6 per cent excluding the "discouraged" workers and 8.4 per cent including them. The urban unemployment rate, as always, was nearly twice higher than the national one at 21.6 per cent by the "strict" and 27 per cent by the "loose" methodology, and the unemployment rate in Tbilisi was the highest.

As always, the unemployment rate figures are distorted by the rural ones that are always extremely low due to the existing legislation[4] rather than to the real situation in the villages. Moreover, a closer look at the unemployment figures shows that while "discouraged" workers accounted for 25.6 per cent of the unemployed in the cities, in rural areas their share in total unemployment was as high as 58.6 per cent. The national unemployment rate, biased by the rural "overwhelming" employment, creates a statistical effect of lower than real national unemployment rate and artificially increases the participation rate.

The participation rate is rather high in Georgia – 63.1 per cent in Q1 2001, though it has been falling in annual terms since1998 (see Statistical Appendix Table A7.1). Most likely the downward trend of the participation rate will not be reversed in the short and medium term. Usually, two different but closely linked processes account for decreasing participation rate: higher productivity on the one hand, and

[2] The SDS was implementing the Labour Force Survey (LFS) in 1998-1999 with assistance from the ILO and the UNDP.
[3] Since Q3 1996, the SDS has been implementing the continuous Household Survey with the financial support of the World Bank and in co-operation with Statistics Canada.
[4] According to the Law on Employment, each farmer owing at least 1 ha of agricultural land, or his/her family member are considered self-employed.

persisting long-term unemployment on the other. The economic situation in the country suggests that in Georgia it is rather the latter than the former: long-term unemployment is a widespread phenomenon, and agriculture, accounting for over half of employment, is extremely unproductive. Higher productivity in agriculture and abandoning the notorious “1 hectare definition” of the rural self-employment would, however, result in dramatic fall in the participation rate and sharp increase in the unemployment rate. Therefore, it is essential that the role of private industry, usually characterised by higher productivity, be expanding, and especially favourable conditions should be created and maintained that would encourage the growth of the number of small and medium sized enterprises.

Another peculiarity of the economic status figures is the annually growing gap between the unemployment rate measured by the ILO “strict” and “loose” standards of measurement: 2 percentage points on average in 1999 compared to 4.9 percentage points in 2000, and 5.2 percentage points in Q1 2001. This means that fewer and fewer people are actively engaged in job search, falling out of the labour force. This process results in a lower unemployment rate but also in a lower participation rate and does not give grounds for drawing optimistic conclusions, being a statistical reflection of the growing incidence of long-term unemployment.

The long-term unemployed run the risk of social isolation and social exclusion, as the longer workers have been unemployed, the smaller their chances of finding a job. The long-term unemployed have poor prospects of finding a job even if the overall macroeconomic situation improves, since their skill level deteriorates and employers are hesitant to employ them. Long-term unemployment is an important source of poverty. Both the economic and social dimensions of this persistent and serious problem are enormous and have to be tackled with policy measures and programmes aimed at raising the employability of the long-term unemployed and reintegrating them into the labour market.

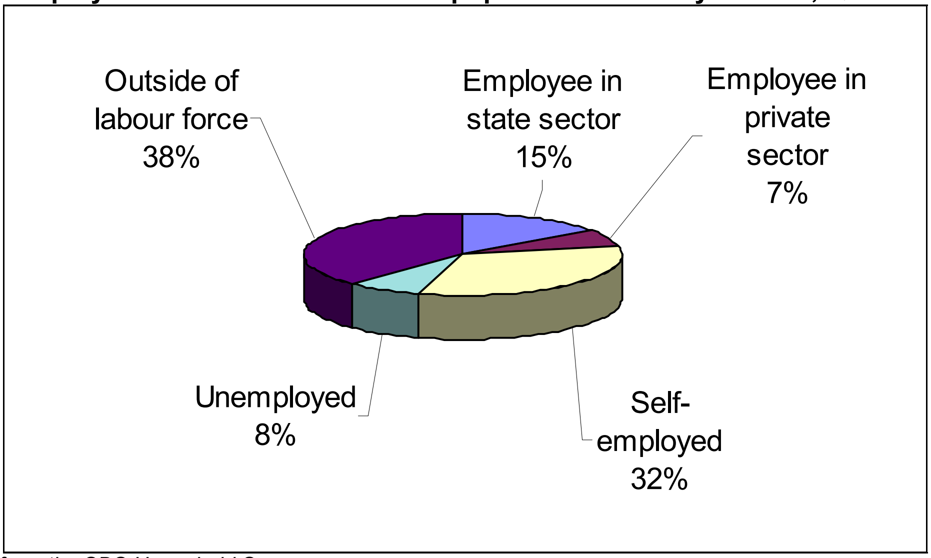
EMPLOYMENT

Self-employment remains the dominant segment of employment and the labour force comprising nearly 57 per cent of the former and 50 per cent of the latter (see table above). The majority ,of the self-employed are self-employed in agriculture – 82.5 per cent in Q1 2001, and many of them are attributed this status just by definition, i.e., in accordance with the current Law on Employment which considers anyone owning at least 1 hectare of agricultural land or his/her family members as self-employed. From the point of view of common sense, this assumption seems rather questionable, since it is difficult to allege that just 1 hectare could employ several family members (average family in Georgia is a four-member family, and in rural areas a household is usually larger than the average) or that it could guarantee them at least a minimum subsistence. Though, it should be noted that agricultural self-employment has been playing a role of the social amortisator in recent years. It is also apparent from anecdotal evidence and from the general situation on the labour market that the remaining 17.5 per cent of the self-employed – the non-agricultural self-employed - are largely engaged in low-income and unstable activities, mostly in the informal sector. Given all the above it is clear that, without knowing all this, the unemployment figures might present quite a misleading picture, and in reality many of the huge army of the self-employed are just the working poor.

The share of hired employment in total employment is shrinking. It saw a 6.5 per cent year-on-year decline in 2000 after a 1.6 per cent year-on-year decline in 1999. In Q1 1999, it accounted for 42.7 per cent of the total employment, a year ago this share fell to 39.8 per cent, and in Q1 2001 it was only 37.5 per cent. This trend is likely to continue at least in the short term, as long as an unfavourable business climate persists.

Another area of concern is the changing patterns of employment towards more extensive use of part-time workers and short-term contracts. The nature of a considerable share of employment is increasingly marginal, temporary or informal. Quite a substantial share of the hired employment is represented by so called “external groups”, i.e., agency or firm temporaries, outsourcing, subcontracting and casual workers. This process increases vulnerability and decreases the employability of these segments of the labour force, restricts their career prospects and their competitiveness on the market, adversely effecting their conditions of employment. Much of the part-time and temporary work is involuntary and tends to be poorer quality employment than full-time work in respect of pay, benefits, security and access to on-the-job training.

Figure 7.1: Employment characteristics of the population over 15 years old, Q1 2001



Source: Data from the SDS Household Survey
Note: Share of the population outside labour force is given according to the ILO ‘strict’ standard of measurement, i.e., including discouraged workers.

The two largest groups of the adult population are those outside the labour force and the self-employed (mostly with very low income) – correspondingly 38 and 32 per cent in Q1 2001 (Figure 7.1). Out of the remaining 30 per cent, in Q1 2001, 15 per cent were employed in the state sector (63.7 per cent worked in budgetary organisations with low and irregular salaries and most probably would have to engage in alternative employment to support the family), accounting for 67.3 per cent of the total number of hired employees and 23.5 per cent of the labour force; and 8 per cent were unemployed (excluding “discouraged” workers). It should be mentioned, that the share of the population over 15 years of age that was outside the labour force grew by 3 percentage points and that of the unemployed - by 1 percentage point over the quarter, while the share of the self-employed and that of the employees in the private sector shrank correspondingly by 3 and 1 percentage points. Only 7 per cent of the adult population (10.3 per cent of the labour force) had conventional jobs, i.e., were employed in private companies. Due to non-stability of the economic situation, especially for small and medium private companies, many of which operate in the informal sector, many of such jobs are low paid and insecure.

The majority of jobs, especially in cities, are created in the informal sector, and in low-productive agriculture; many of these are part-time or temporary jobs. Decline in unemployment are due partially to labour absorption in the informal sector, however, this process is difficult to trace using the household survey figures. Informal activities are largely unrecognised, unrecorded and unregulated small-scale, low-paying activities, dominated, as overall employment, by irregular self-employment. Underemployment is a widespread phenomenon, the majority of the employed being engaged in low-paying and insecure segments of the labour market and work under poor working conditions.

Stable long-term full-time jobs are rare, both in the formal and informal sectors. Hidden and disguised unemployment are widespread and growing long-term unemployment leads to the downsizing of the labour force, and, hence to the misleadingly low unemployment rate. The economic status figures fail to reflect all the drama of the situation, since the ILO methodology of counting the unemployed ignores the size of labour remuneration and its consistency with the size of the minimum subsistence.

According to the interim Poverty Reduction and Economic Growth Programme, establishment of an effective employment system, conducting a balanced taxation and investment policy and defining effective mechanisms of wages will help in the creation of new jobs, and to promote family, small and medium business development.

SALARIES AND WAGES

The average monthly nominal salary of hired employees across the economy was GEL 82.8 – a 3 per cent quarterly fall - in Q1 2001, according to the SDS household survey figures. The average monthly salary of approximately 43 per cent of all salary earners – those working in budgetary organisations[5] – was GEL 57.3 in Q1 2001. Since the concept of a minimum salary was re-introduced after a 4-year gap by a presidential decree in June 1999, salaries of this category of hired workers range between GEL 20 and GEL 66. Salaries of another 25 per cent of the hired workers – employees of public enterprises and organisations - was approximately GEL 72 on average.

Hired employees in private sector – approximately 28 per cent of all hired workers – were receiving a monthly remuneration of GEL 107 on average and monthly salaries of only around 2 per cent of hired employees – those working in foreign organisations or joint ventures - were GEL 262 on average.

Many public sector salaries remain low, even the majority of private sector salaries are lower than the minimum subsistence, instances of non-payment of salaries whatsoever remain widespread, building up arrears, and inflation hampers the growth of salaries in real terms.

MINIMUM SUBSISTENCE LEVEL

After the Government passed a decision "On Introducing Changes into Calculation Methodology and Re-calculation of the Minimum Subsistence Level" in August 1999 and a draft presidential decree "On Defining and Applying Subsistence Minimum" was drawn up, nothing has changed. Though a new methodology to calculate the minimum subsistence is ready at the SDS and is published as an "alternative minimum subsistence", the methodology, introduced in early 90s, is still being used and published as an "official" one. It can be argued which of the methodologies better takes into consideration the real basket that can secure reasonable minimum subsistence, however, it is clear that the minimum subsistence levels, calculated in accordance with the new "alternative" methodology are closer to the average salary levels in the economy. If the share of the average monthly salary in the minimum subsistence of a family of four, calculated by the old "official" methodology was, 41 per cent in Q1 2001, the same share in the minimum subsistence, calculated by the new "alternative" methodology would be almost 67 per cent.

[5] A budgetary organisation is a public organisation fully subsidised by the state budget.

The official subsistence minimum levels published by the SDS, were: GEL 115.8 for a working man, GEL 101.6 for an average consumer and GEL 201.6 for a family of four – on average at the end of Q1 2001, a 0.6 per cent year-on-year decrease and a 1.3 per cent quarterly growth. (As of end of Q2 2001 the levels were correspondingly GEL 119.2, GEL 104.5 and GEL 207.3). As usual, the minimum subsistence level in Tbilisi was higher than the national average.

SOCIAL SAFETY NET

The vast majority of the population, including informal sector employees, the self-employed and the unemployed, as well as their family members, have no social protection whatsoever, and the problem of poverty in old age is particularly acute as the currently existing pension system proves to be insolvent. The current social safety net system is largely the heritage of the soviet past and in the conditions of a transition economy appears to be ineffective in alleviating poverty. Social policy reform aimed at rendering the existing system sustainable is among the top priorities in the country. The system of social protection provided by the state requires a fundamental restructuring, and an economically viable, affordable and equitable social safety net is to be created.

Social reforms are acknowledged by the Government to be a long-term strategic objective. In November 2000, the Government, in its interim Poverty Reduction Strategy Paper (PRSP), has laid out structural reforms in five main areas to reduce poverty and stimulate economic growth: 1) social sector reforms to improve allocation of benefits to better target the poor; 2) supportive macroeconomic policies, such as tax and customs administration, to raise fiscal revenues while reducing the budget deficit; 3) public administration reform based on recommendations of the anti-corruption commission; 4) private sector development to foster investment in infrastructure as well as other areas; and, 5) agricultural reform.

The Secretariat to the Governmental Commission for Elaboration the Poverty Reduction and Economic Growth Programme (PREGP) is currently preparing the final document of PREGP, the main goals of which are the elimination of poverty through support to economic growth leading to creation of new work places; raising the living standards of the population; and ensuring the participation of all citizens in the country's development process. According to the interim PREGP, among the measures to be taken to achieve the reduction of poverty can be an effective employment policy, establishment of an adequate system for education of competitive staff, and introduction of universal household compensations for children. It is necessary to develop targeted social protection mechanisms to cover as many unprotected as possible.

State Social Allowance

The existing State Social Allowance is targeted at households comprised exclusively of non-working pensioners without a legal breadwinner, and/or orphans, representing, actually, a topping-up of symbolic pensions of the poorest elderly and a modest child allowance for the most destitute children. The State Social Allowance payable to recipients, in accordance with a presidential decree of 10 February 2001 is GEL 22 for a qualifying household consisting of one member, or for each orphan under guardianship, and GEL 36 for an eligible family of two or more.

Unemployment Benefit

The payment of the standard monthly Unemployment Benefit payable for the first six months of registered unemployment is fixed at GEL 14 for the first two months of unemployment, GEL 12 for the next two, and GEL 11 for the final two months of payment. To become officially eligible, a person should be registered as unemployed, therefore should have a certain working record in the official sector. As a result, the number of the unemployed who bother to register is usually at least half the actual one and the number of the benefit recipients is insignificant (2.5 per cent of the registered unemployed as of end of Q1 and 2.8 per cent as of end of Q2 2001).

Pension System

The current universal pay-as-you-go (PAYG) pension system provides fixed-rate, symbolic (equivalent to about USD 7 per month – GEL 14) old-age pensions to the majority of pensioners. Pensions are financed through the United State Social Safety Fund, whose revenue is formed from payroll tax proceeds[6] supplemented by budgetary transfers. Under the conditions of a narrow tax base, a big informal economy, and constant tax under-collection and non-compliance, the pension system has long proved to be unsustainable and insolvent and continues to accumulate arrears.

The current *dependency ratio*[7] is 1:1.2 while for a pay-as-you-go system to be sustainable it should be at least 3:1. The number of those who are evading payroll tax payment (both employees and employers) is large: budgetary salaries are often not paid in time, many companies are not functioning, and some contributors are not paying in full. Low wages and no link between the future benefits and current contributions result in no incentive for payment of contributions, and a relatively high payroll tax rate discourages tax compliance on the part of the employers.

The *replacement rate*[8] of the pension system is low. The average pension flat rate of the majority of pensioners was 17 per cent of the average hired employees' monthly salary as of the end of Q1 2001[9]. Pensions accounted for just 13.7 per cent of the minimum subsistence level of an average consumer as of end of Q1 2001 and for 13.4 per cent – as of end of Q2 2001.

The crisis the current PAYG pension system has been facing is severe and painful economically, politically and socially. Neglecting the short- and long-term consequences of the current situation will place the vulnerable at serious economic risk and may result in growing poverty, social disintegration, marginalisation and social exclusion, while elaboration and implementation of an effective social policy will offer a more solid base for long-term economic growth.

Reform of the pension system is now among Government's priorities, and a pension reform programme is being designed, aimed at establishing a financially sustainable modern pension system suited to changing demands of a transition economy. According to the Government's interim PREGP, the perfection of the pension system should imply re-introducing its collection, distribution and insurance functions, and defining and introducing alternative variants of multistage pension insurance mechanisms, to be carried out step by step. According to the Programme, it is essential to guarantee a transparent environment in the pension system; to draft appropriate legislation and improve existing normative acts; to ensure continuous payment of current pensions and gradual repayment of accumulated arrears; to implement personification and to introduce identification cards, and, finally, to ensure step-by-step transfer towards insurance principles and a differentiated pension system.

[6] The contributions from workers' wages, that form the United State Social Safety Fund (USSSF) revenue are 26 per cent of gross wages for budgetary organisations and 27 per cent for others paid by the employer and 1 per cent paid by employees.
[7] The number of pensioners as a per cent of the number of people employed, or contributor to beneficiary ratio.
[8] The average pension in terms of the average wage.
[9] When this issue of GET was ready for publication, the results of household survey for Q2 2001 were not available.

The current pension system, like any PAYG system, is based on a solidarity contribution[10] principle, and, being an element of the social safety net, can only provide minimum pensions to the elderly and is not in the position to provide adequate benefits to the elderly on its own. In order to provide a plurality of possibilities and availability of choice for those who can afford to make provisions for their future pensions, a *multi-pillar system*[11] is being introduced that is going to increase personal responsibility and create savings funds for investment. The multi-pillar system implies three pillars: a universal state pension scheme, a mandatory private pension scheme and a voluntary private pension scheme.

In May, the first private pension insurance company in Georgia – Georgian Pension Investment Holding (GPIH) was founded that will offer, in addition to the existing universal PAYG scheme, voluntary non-state pension insurance to the population. However, before the company starts actual pension fund activities at a full scale, the legal framework in this sphere is to be revised and adjusted. It is not likely, though, that a big share of the population would be able to afford participation and/or have confidence in private schemes, at least, in the short and medium term. Privately managed retirement savings systems might be more useful as a complement to rather than a substitute for the universal social insurance. The PAYG pillar is going to be mandatory under the reformed pension system and still very important for the majority of the pensioners. Therefore, the most imperative goal to aim at in the short term is to improve payroll tax collection and broaden the tax base.

[10] A compulsory contribution which is not expected to earn a specific benefit for the contributor but which is required by the social security system in order for it to provide benefits to others.
[11] For detailed definitions of the pillars and some other pension system terms see GET 1999 No. 3, Chapter 7.

CHAPTER EIGHT: THE EU-GEORGIAN RELATIONS

GEORGIA'S TRADE WITH THE EU

Figures for January-July, 2001 show an increase in the EU-Georgian trade compared to the same period of last year. In January-July, 2001 turnover amounted to USD 142.0 million. This is USD 18.3 million more than in the same period of 2000. The increase of imported products from EU countries and a reduction of exported products from the Georgia to the EU markets triggered this increase. During this period imports amounted to USD 109.0 million and exports to USD 33.0 million. The increase of imports from the EU market and reduction of exported products to the EU countries caused a further rise of Georgia's trade deficit with the EU. This deficit amounted to USD 76.0 million. The trade deficit increased by USD 35.9 million, compared to the same period of the last year. Georgia's exports to the EU market still remains quite low. This negatively effects Georgia's trade balance.

Table 8.1: Georgia's Trade with the EU Countries
(USD millionS)

Country	2000 January-July				2001 January-July			
	Turnover	Export	Import	Balance	Turnover	Export	Import	Balance
UK	14.9	3.9	11.0	-7.1	23.7	9.7	14.0	-4.3
Italy	15.2	6.0	9.2	-3.2	17.9	5.6	12.3	-6.7
Germany	52.2	23.6	28.6	-5.0	44.1	4.0	40.1	-36.1
France	6.3	0.6	5.7	-5.1	10.9	0.2	10.7	-10.5
Netherlands	4.5	0.9	3.6	-2.7	7.9	2.6	5.3	-2.7
Greece	8.6	3.4	5.2	-1.8	4.1	1.6	2.5	-0.9
Belgium	2.2	0.3	1.9	-1.6	11.3	6.6	4.7	1.9
Austria	2.5	0.0	2.5	-2.5	4.8	0.5	4.3	-3.8
Finland	0.7	0.0	0.7	-0.7	7.9	0.0	7.9	-7.9
Denmark	1.7	0.4	1.3	0.9	3.9	0.4	3.5	-3.1
Ireland	2.4	0.2	2.2	-2.0	0.7	0.0	0.7	-0.7
Portugal	0.7	0.0	0.7	-0.7	0.8	0.0	0.8	-0.8
Sweden	9.2	0.0	9.2	-9.2	1.7	0.7	1.0	-0.3
Luxembourg	0.0	0.0	0.0	0.0	0.1	0.0	0.1	-0.1
Spain	2.6	1.0	1.6	-0.6	2.2	1.1	1.1	0
Total	123.7	40.3	83.4	-43.1	142.0	33.0	109.0	-76.0

Source: State Department for Statistics

In January-July, 2001, Georgia had a negative trade balance with all EU member states except Belgium. UK, Germany and Italy remain the largest trade partners for Georgia. The trade of these countries with Georgia constitutes 60.3 per cent of total amount of Georgia-EU trade in 2001.

GEORGIA'S ECONOMIC RELATIONS WITH EU MEMBER STATES: ITALY

Trade

Economic relations between Georgia and Italy started in 1992, after the restoration of Georgia 's independence. Trade relations between two countries intensified after the 1995 and reached its highest level in 1998. In this year trade, amounted to USD 37.7 million, where exports constituted USD 8.9 million and imports USD 28.7 million. The next year saw a decline in trade and turnover constituted USD 23.9 million. During this year imports from Italy reduced by USD 15.7 million and constituted

USD 13.1 million. At the same period Georgia slightly increased its exports to the Italian markets. In 1999, import reduction from Italy could be explained by the financial and budgetary crisis in Georgia. In 2000, trade between two countries increased by USD 5.8 million compared to the previous year. During the current year (January-July) trade increased by USD 2.7, million compared with the same period of the year 2000.

Table 8.2: Georgia's Trade with Italy
(USD millionS)

	1998	1999	2000	2001
Export	8.9	10.7	12.4	5.5
Import	28.7	13.1	17.3	12.2
Turnover	37.6	23.8	29.7	17.7

Source: Italian Embassy in Georgia

From 1998 to 2001 Georgia imported from Italy wheat and flour; dish washing machines, machinery for cleaning or drying bottles or other containers; polyacetals; furniture, rice, pasta, electric instantaneous or storage water heaters, machine-tools for working stone, ceramics, concrete, asbestos, cement or like mineral materials and other goods..

In the first half of the 2001 Georgia mostly imported the wheat or flour, (which represents 15.9 per cent of total import from Italy), carboys, bottles, flasks, jars and other containers (13.2 per cent), polyacetals, other polyethers and epoxide resins in primary forms (10.0 per cent) and other goods.

During the period 1998-2001 Georgia exported to Italy mineral and chemical fertilizers, nuts, ferro-alloys trailers and semi-trailers, raw skins of sheep or lambs, aluminium waste and scrap, and ferrous waste and scrap.

In the first half of the 2001, Georgia mostly exported to Italian markets nuts (which represents 21.0 per cent of Georgia's total export to Italy), parts suitable for use solely or principally with the machinery (14.3 per cent), ferrous waste and scrap (14.0 per cent), aluminum waste and scrap (13.8 per cent).

Investments

During the last two years Italian companies invested in Georgia USD 3.2 million, which represents 1.4 per cent of total amount of Georgia's foreign direct investments. During the current year Italian companies invested in Georgia USD 0.9 million which is 4.2 per cent of total amount of Georgia's foreign direct investments in 2001. Among the EU countries, Italy along with France and the Netherlands represented major investors for Georgia in previous year.

The small size of Italian investments can be explained by the problems, which exists in the country. Mainly, weaknesses of public institutions, taxation policy, which is complex, unclear and "bureaucratic", corruption, smuggling, and unfair competition.

Unstable political situation in the region and armed conflict in neighboring Chechnya also serve as impediments for attraction of foreign investments in Georgia.

A lack of information among Italian businessmen about Georgia is another impediment for attracting Italian investments in the country. For this purpose in Padua, in June 2001, the forum “Presentation of Georgia” was held. This forum was organized by the Italian Institute for Foreign Trade (ICE) in cooperation with the Georgian Government. The Georgian delegation was presented by government officials and private sector representatives. The forum discussed the economic situation in Georgia. The Georgian delegation provided the Italian side with detailed information about Georgia’s foreign trade policy, privatization process, banking system, infrastructure development, transport and communication, and small and medium sized enterprises development.

Today, several Italian companies operate in Georgia. These companies operate in energy, consultancy, transportation, and service sectors. It is worth mentioning that the Italian government provides financial support to bilateral and plurilateral programmes which promote co-operation between Italian companies and other countries. This measure is regulated by Italian legislation, under the Law 212 (see Box 8.1). None of the company registered in Georgia is beneficiary of the Law 212.

Box 8.1

What is Law 212?

Law 212 is an instrument for financing bilateral and plurilateral programmes which promote co-operation between Italy’s and other countries’ organisations. Each year the Inter-ministerial Committee for Economic Policies (CIPE) selects a number of countries at which this financial support is directed in order to help them through their transition towards a market economy and integration into Europe.

Beneficiaries

- public and private institutions and bodies, in particular technical assistance agencies and vocational training institutions;

- trade associations, their federations and related services agencies;

- consortia, co-operatives, companies, in particular SMEs.

Target Countries

They are annually selected by a CIPE decision taken upon a proposal of the Minister for Foreign Affairs together with the Minister for Foreign Trade. For the year 2001, the countries are the following: Albania, Algeria, Armenia, Azerbaijan, Bosnia-Herzegovina, Bulgaria, Croatia, Egypt, Estonia, the Russian Federation, Georgia, Hungary, Kazakhstan, Kyrgyzistan, Latvia, Libya, Lithuania, Macedonia, Moldova, Morocco, Poland, Czech Republic, Federal Republic of Yugoslavia, Romania, Slovakia, Slovenia, Tunisia, Ukraine and Uzbekistan.

Activities eligible for funding

Projects shall not exceed a 24-month duration. They will cover the following types of activities:

- vocational, executive and cadres training;
- technical assistance;
- feasibility studies and projects in the sectors of transport,telecommunications, supply, social economy, energy, tourism, environmental and sanitary rehabilitation as well as in industrial and agricultural reorganisation and in the field of artworks restoration and urban rehabilitation;
- pilot projects aimed at promoting technology transfer agreements between the partners;
- feasibility studies (business plan and drafting of corporate documents) for the establishment of joint ventures as well as for the restructuring of joint enterprises participated by an Italian company.

Source: Italian Embassy in Georgia

CALENDAR OF EVENTS

JANUARY

10 **Oil and Gas** Refusal of part of the authorised dividends from the use of Baku-Supsa pipeline and Supsa oil terminal for the benefit of the national budget for several years to come was made by the Georgian International Oil Corporation (GIOC). According to the agreement signed with the Finance Minister at the end of last year, the national budget will receive corporation dividends not according to the sum of the financial year but during all year according to the schedule agreed with the Finance Minister. The Oil Corporation refuses dividends for the whole period while the national budget has problems before the construction of Baku-Tbilisi-Ceikhan.

11 **Oil** Celebration ceremony for the opening of the new oil well by the President Eduard Shevardnadze was held on the oil-fields in Ninotsminda in eastern Georgia. In Ninotsminda oil-fields 12 wells are functioning currently. Hydromagnetic inspections are being held on 3 wells. According to official information, total daily mining is equal to 300 tonnes of oil and about 240,000 cubic metres of natural gas. This will soon increase to 500-700 tonnes of oil and 1 million cubic metres of gas. The oil mined in Ninotsminda is refined by the Georgian-American company GAOR founded by the Georgian-British oil company – 19 per cent, Canargo company – 51 per cent and GeoOil stock company.

12 **Programme of the IMF in Georgia resumed** The Executive Board of the International Monetary Fund approved a three-year loan under the Poverty Reduction and Growth Facility (PRGF) in an amount equivalent to SDR 108 million (about USD 141 million) to support the government's economic programme. The first disbursement of SDR 9 million (about USD 12 million) under the new programme will become available immediately.

18 **Government** The presentation of the National Poverty Reduction and Growth programme was held. In the programme, special attention is attached to the rehabilitation of economy in the region, and the problems of refugees. The document will be reviewed every three years. For the next three years the programme aims at forming the foundations for more rapid economic growth and reducing poverty. In parallel, the problem of external debts will be settled. In the intermediate document worked out by the Government there are structural reforms in five basic spheres along with the strategy of poverty reduction. In particular, the reforms in the social sphere - for improving the distribution of assistance to the poor; macroeconomic policy to support growing fiscal revenues; improvement of administration, taking into account recommendations of the anti-corruption commission; development of a private sector for mobilizing investment and the reform of agriculture.

30 **Industry** A meeting dedicated to the problems of “Chiaturmanganese” in Chiatura took place. It was decided to give “Saga Print” a last opportunity to improve the situation at the enterprise.

Foreign Investments The meeting of President Eduard Shevardnadze with Turkish businessmen and potential investors was held in the "Sheraton-Ankara" hotel. It was mentioned that the business circles of Turkey consider Georgia to be one of the most important partners in trade and economic spheres and are interested in expanding co-operation. There are 150 Georgia-Turkish joint ventures . Investment by Turkish companies in Georgia make up about USD 45 million. In 1997, a Georgian-Turkish business council was founded. Turkish businessmen stress that the development of beneficial co-operation would be promoted by ratification of the agreement on avoiding double taxation between the two countries.

FEBRUARY

8 **Tbilisi natural gas network rehabilitation** The Parliamentary Committee on Sector Economy conducted a hearing aimed at considering programmes on the rehabilitation and upgrading of the Tbilisi network of natural gas. The meeting discussed issues relating to the implementation of a memorandum of mutual understanding signed by USAID, P & A Consulting, the Ministry of State Property Management, the Tbilisi Municipality, and Tbilgas in November 2000. The network requires urgent rehabilitation at a cost of nearly USD 100 million. According to the USAID P & A Consulting, the implementation of the programme was to start in February.

16 **Parliament** Parliament ratified the 1993 agreement On Regulating Assets and Liabilities of the Former Soviet Union between Georgia and Russian Federation, known as the 'zero variant' agreement. By the agreement, Georgia transfers to Russia its 1.62 per cent share in the former Soviet property. In exchange for ratification of the given agreement Russia promised to restructure USD 158 million of debt owed by Georgia.

20-21 **EU/Georgia relations** EU Ministerial Troika (Mr. Javier Solana – Secretary General/High Representative of CFSP, Mrs. Anna Lindth – Minister of Foreign Affairs of Sweden, Chris Patten – EU Commissioner for External Relations) visited Georgia. During the visit, the Troika held meetings with the Georgian President, State Minister and other High Officials. The Troika visit emphasized the EU's interest towards Georgia with a view to supporting peace, stability, prosperity and regional co-operation. The importance of strengthening the EU's political role in the region was uderlined.

22-23 **International Relations** The third session of joint Georgian-Ukrainian intergovernmental commission on economic co-operation was held in Kiev. According to members of the commission, reported trade (in goods) turnover increased by 149 per cent to USD 57 million. The parties discussed co-operation in the transport sphere. In connection with the liberalisation of tariffs, the Georgian side approved the decision on reduction of tariffs for transit transportation by 50 per cent. The parties also look at the question of the optic-fibre cable Trans-Asia-Europe (TAE) joining the system of Black Sea optic-fibre cable. One of the main priorities in the co-operation of the intergovernmental commission members was recognized to be joint participation of the two countries in global energy projects. To avoid penetration of counterfeited produce on the markets of both countries, the parties agreed to prepare a draft intergovernmental agreement on protecting industrial property.

26 **EU** The General Affairs Council adopted conclusions on the Southern Caucasus where it was stated that “The Council invited its competent bodies, with the assistance of the High Representative/Secretary General, and the Commission to make recommendations for the implementation of a reinforced EU policy, on the basis of preparatory work for and the results of the Troika visit and to report back in time for the Co-operation Councils with Georgia, Armenia and Azerbaijan under the Belgian Presidency.”

27 **Industry** The French company Castel Group plans to expand beer production in Georgia. Pierre Castel discussed the plans of future development with President Shevardnadze. According to the presidential press-service, the talks dealt with beer export growth and the potential for internal and external markets, in particular, in Russia and Ukraine.

MARCH

5 **TRACECA** Project of building a railway ferry route, which is to connect Georgia with Romania and Moldova, will soon be worked out in the framework of the TRACECA programme. President Eduard Shevardnadze, in his traditional radio report, stated that the European Union would finance the project.

7 **External Debt** Paris Club made a decision to re-schedule the external debts of Georgia. That allows Georgia not to re-pay the principal of foreign debt to creditor countries in the 2001-2002. In case of necessity, the preferential period could be prolonged until 2003. The servicing of the debt is scheduled from 30 June 2005 till 31 December 2021, and the interest rates should not exceed the terms of restructuring the debt (not more than annual 4 per cent). These are quite preferential terms, since under "Houston conditions", the debtor countries are usually given 18 years period and the interest rate is market based.

14 **Anti-corruption programme** American businessman and philanthropist George Soros, who visited Tbilisi on March 14th, declared that he would finance the first stage of the anti-corruption programme of Georgian Government.

20 **World Bank** The World Bank approved the first USD 25.9 million of a USD 60 million Education System Realignment and Strengthening Programme in Georgia, the first such operation financed by the World Bank in the country. The programme aims at rendering learning process more effective and at making more efficient use of financial, physical and human resources.

26 **WTO** Presidential decree “On development of relations with the WTO” was issued. A governmental Commission was established that is to co-ordinate relations with the WTO in the post-accession period, as well as ensure fulfilment of the obligations assigned in the field of foreign trade, and complete and effective utilisation of the full membership of the WTO.

29 **Credit Auction** Inter-bank auction for credit resources was held at the National Bank of Georgia. Two commercial banks participated in the auction. Deals worth GEL 200 thousand were made. Credit resources were allocated under the annual 18 per cent interest rate.

30 **EU/Georgia** Session of the governmental commission for promoting co-operation and partnership between Georgia and the European Union was held at the Ministry of Foreign Affairs. The session discussed working out the strategy for harmonising the legislation of Georgia with that of the European Union. At the first stage, Georgian-European Policy and Legal Advice Centre prepared a document " Proposals for a Strategy to Approximate Georgian Legislation to EU Legislation " and submitted it for consideration to the ministries and state agencies concerned.

APRIL

12 **Tourism** According to the chairman of the Department, a representative office of the Department of Tourism and Resorts of Georgia is to open in Tokyo in May.

17 **Banks** Cartu Bank officially signed the General Agreement at the National Bank of Georgia on taking over all the assets and liabilities of Absolutebank. Re-registration of the assets and liabilities of the Absolutebank is the first example of civilised western approach to improving of the situation of a bank by considering the interests of its investors and clients. By the General Agreement, Cartu Bank is to allocate between USD 3 million and USD 5 million to improve the situation of Absolutebank.

25-9 **IMF** An IMF mission visited Tbilisi and held discussions with the Georgian authorities for the 2001 Article IV Consultation and the first review of the programme supported under the Poverty Reduction and Growth Facility (PRGF). The mission reviewed general economic developments and progress in the implementation of the economic policies and reforms.

The positive trend in fiscal policy implementation during the second half of 2000 was not maintained during the first four months of 2001. Due to a shortfall in tax and customs revenues, targets on general government tax revenues and expenditure arrears were missed by large margins. The mission took the view that strong and credible fiscal measures were required to bring revenues back on track and safeguard social spending. Considering the shortfalls in excise collections, the mission advised the government and the parliament to reverse recent cuts in excise rates and take other measures to raise revenues and strengthen the administration of the tax and customs departments.

The mission agreed to monitor performance, based on monthly targets, and assess during a mission in July whether a sustained improvement is likely to be achieved, in line with original program objectives. The Fund mission projects GDP growth to increase from 1.75 per cent in 2000 to 3.5 per cent in 2001, resulting from a recovery of agricultural production.

The mission urged the government to resist protectionist pressures. Restrictions on exports of scrap metal and timber, as recently proposed, would sharply worsen the current account deficit and jeopardize macroeconomic stability. Macroeconomic policy implementation will be monitored during the second and third quarters of 2001.

27 **World Bank/Georgia** Five Georgian non-governmental organisations were awarded World Bank grants totalling USD 30,000 for the implementation of projects focused on critical development issues. The grant activities are focused on social and economic development problems such as poverty reduction, environmental protection, human resource development, anti-corruption and governance, and private sector development.

MAY

3 **World Bank/Georgia** The World Bank approved a USD 27.4 million equivalent (SDR 21.1 million) credit to make electricity supply in Georgia more reliable and efficient, and to improve financial and corporate management in the wholesale electricity market. The project will: (a) rehabilitate and upgrade metering system control, communications in the transmission network and electricity dispatch; (b) rehabilitate Zestafoni transmission sub-station; (c) finance private management contracts for the wholesale electricity market and for transmission and dispatch companies; (d) finance technical services for project implementation. The USD 27.4 million equivalent credit is to be provided on standard IDA terms. The project will be co-financed by Kreditanstalt fur Wiederaufbau (KfW) of Germany (USD 11.4 million), the European Bank for Reconstruction and Development (USD 0.9 million), and by the project beneficiaries (USD 16.9 million). The total cost of the project is USD 56.6 million equivalent.

4 **GUUAM Symposium** Symposium – “Role of the Chambers of Commerce of the GUUAM Countries in Strengthening the Economic Cooperation” opened in Baku. Representatives of business circles from the GUUAM member countries participated in the symposium (Georgia, Ukraine, Uzbekistan, Azerbaijan and Moldova). Delegates from Lithuania, Latvia, Kazakhstan, Turkey, Bulgaria, Hungary, Poland, Romania, Slovakia and Czech Republic also participated in the symposium.

5 **Industry** The agreement has been achieved between the companies working on the production of Borjomi: Georgian Glass and Mineral Waters, Big and Borjomi Producers' Union. According to the agreement, Borjomi will appear on the market under one license and one brand name. The agreement implied joint control over the quality of the mineral water and prevention of falsification. By this information, 85 per cent of total amount of produced Borjomi falls on Georgian Glass and Mineral Waters, 7-8 per cent on Big and 5 per cent on Borjomi Producers' Union**.**

8 **Pension System** The first private pension insurance company in Georgia – GPIH (Georgian Pension Investment Holding) – was founded that will offer, in addition to the existing universal PAYG scheme, voluntary non-state pension insurance to the population.

18 **Banking Sector** German Commerzbank signed an agreement on purchasing 15 per cent of the capital of the Microfinance Bank of Georgia (MBG). The MBG has five branches in Georgian regions.
The bank was founded in May 1999, and 75 per cent of its shares are owned by international financial organisations - German KfW bank, International Financial Corporation, Dutch financial company of development FMO, International Investment Company IMI and the European Bank for Reconstruction and Development.

19-21 **Banking Sector** The Black Sea Trade and Development Bank (BSTDB) opened new credit lines for Georgian Microfinance Bank and the Bank of Georgia - USD 1 million and USD 1.5 million respectively. The decision was made at the annual meeting of the BSTDB, held in Tbilisi. According to the National Bank of Georgia, the given credit resources will mainly go for the development of trading relations with BSEC participant countries.

JUNE

4 The Administration of the USA allocated USD 2 million for needy Georgians for electricity expenses for the coming winter.

5 Ministry of Finance starts paying off current year debts for pensions, wages and allowances in June. This statement was made by Zourab Nogaideli, Minister of Finance.

7-8 The second session of Eurasian round table was held in Tbilisi on corporate governance. The session was dedicated to “transparency and disclosure of information”. The session was organized by the World Bank, IFC and OECD.

11 The fourth round of negotiations on the construction of Shah Deniz-Tbilisi-Erzrum gas pipeline, between Georgia and Azrbaijan started in Frankfurt.

14 A third session of the joint Georgian-Turkish commission for economic cooperation started in Tbilisi.

18-20 Problems of developing trade, transport and telecommunication infrastructure were discussed at a seminar for support to trade in the Trans-Caucasus countries. The seminar was organised by the Ministry of Transport and Communications and the National Commission for Communications.

21 A session of national secretaries of TRACECA participant countries was held in Baku.

29 The USA President designated Georgia as a GSP beneficiary developing country. The USA GSP scheme offers developing and transition countries preferential access to the USA market. This decision entered into the force on 1st July, 2001.

JULY

5 Georgia started repaying debt to Turkmenistan for natural gas on a clearing basis and the debt has already been decreased by USD 12 million.

10 A Memorandum of Understanding was signed in the Ministry of the State Property Management, by which the USAID will allocate a USD 500,000 grant to the Government for investing in banks.

13 Six agreements on co-operation between Georgia and Uzbekistan in the customs sphere were signed at a fourth session of the joint inter-governmetal commission.

24 A mission of the International Monetary Found presented to the Government its recommendations for improving economic management.

AUGUST

1 Deadline for submission of applications for participating in the Tbilgas JSC privatisation tender was postponed until 27th August.

11 The Ministry of Economy, Industry and Trade of Georgia announced that industrial productivity rose by 12 per cent in January-July 2001, compared with the same period of the previous year.

12 Tbilisi municipality gives GEL 200,000 for the restoration of 3rd and 4th 150 megawatt blocks of Tbilisi station “Tbilgres”.

13-19 Japanese government extends GSP status to Georgia enabling increased access to the Japanese market.

17 A repeated tender was announced offering 75 per cent of the shares of Sakartvelos Elektrokavvshiri. The deadline for bids is set for 15th October.

22 Jonathan Dan was appointed as the new representative of the International Monetary Fund in Georgia.

APPENDIX I: THE FOREIGN DEBT CRISIS IN GEORGIA AND A WAY OUT

By Roman Gotsiridze, Head of Parliamentary Budgetary Office

INTRODUCTION

Interstate capital movements are an everyday occurrence in the world. The majority of states borrow money from other states. According to 1998 data, inter-country indebtedness has reached an enormous amount - more than - USD 4 trillion. Such countries as USA, Great Britain or France feel quite at ease borrowing form other states and in their turn they are lent money without any problem. The governments of America or Britain are not likely to go bankrupt and are sure to pay off their debts to creditors. It is a nonrandom fact that Japanese are the most active owners of the American short-term T-Bills - in their country they have got no other debtor as reliable as the US Treasury.

The governments of Asia, Africa, Latin America and the developing and post-socialist East-European countries incur as much foreign debt as they are accommodated. Although often reluctantly, they are granted foreign credits, as the developing countries give the highest interest yields in the world. Though there is a risk that these countries might not be able to repay the debt - they may either become insolvent or just evade it (there are many such examples). There are many countries which have no prospect of paying off their debts as the share of their foreign debt against their GDP and budget expenditure is rather high.

USA has the heaviest foreign indebtedness in the world (see Table 1), which certainly does not point to a weakness of its economy. The absolute value of the debt does not produce grounds to speak of the economic situation in the country. At the same time, the huge indebtedness of other countries to the USA is also to be taken into account .

Table 1: Foreign Debt Statistics of the Countries of the World, as of the beginning of 1998

Foreign Debt of over USD 100 billion	
USA	862
Brazil	258,1
Canada	253
Russia	164
China	159
South Korea	154
Mexico	154
Indonesia	136
Argentina	133
France	117,6
Total	**2,390,7**

Have no indebtedness or it is not acknowledged
Brunei
Hong Kong (China)
Macao
Holland
Norway
Liechtenstein
Andorra
Germany
Japan
Luxembourg
Puerto Rico
San Marino
Saudi Arabia
Singapore
Switzerland
Great Britain

Foreign Debt of USD 20 - 100 billion	
Turkey	93,4
India	93
Spain	90
Thailand	90
Sweden	66,5
New Zealand	53,2
Philippines	46,4
Italy	45
Denmark	44
Poland	42
Israel	41,1
Greece	40,8
Malaysia	39,8
Pakistan	34
Nigeria	32
Chile	31,5
Algeria	31,4
Venezuela	30,9
Cuba	30,1
Finland	30
Egypt	28
Peru	25,7
Austria	24,33
South Africa	23,5
Belgium	22,3
Hungary	22,1
Syria	22
Iran	21,9
Czech Republic	21,6
Morocco	20,9
Sudan	20,3
Total	**1,257,7**

Foreign Debt of USD 5 - 20 billion	
Columbia	18
Cote D'Ivoire	16,8
Congo (Rep)	16,7
Bangladesh	15
Congo (Dem. Rep.)	14
United Arab Emirates	13,1
Angola	13
Ecuador	12,5
Tunis	12,1
North Korea	12
Serbia and Montenegro	11,2
Ireland	11
Quatar	11
Ukraine	10,9
Slovakia	10,7
Ethiopia	10
Romania	10
Vietnam	9,8
Bulgaria	9,3
Sri Lanka	8,8
Cameroon	8,7
Tanzania	8,3
Croatia	8
Kazakhstan	7,86
Panama	7,7
Jordan	7,5
Kuwait	7,3
Zambia	7,1
Kenya	6,45
Nicaragua	6,1
Congo (Rep)	6
Ghana	5,89
Mozambique	5,7
Zimbabwe	5
Total	**343,5**

Foreign Debt of USD 1 - 5 billion	
Yemen	4,9
Uruguay	4,6
Madagascar	4,4
Slovenia	4,4
Burma	4,3
Bolivia	4,1
Gabon	4,1
Jamaica	4,1
Libya	4
Senegal	3,8
Dominican Rep.	3,6
Bosnia & Herzegovina	3,5
Honduras	3,4
Guatemala	3,38
Costa Rica	3,2
Papua New Guinea	3,2
Guinea	3,15
Mali	3,1
Lebanon	3
Oman	3
Uganda	2,9
Trinidad and Tobago	2,8
Salvador	2,6
Somali	2,6
Uzbekistan	2,6
Mauritania	2,5
Nepal	2,4
Afghanistan	2,3
Malawi	2,3
Cambodia	2,2
Iceland	2,2
Guyana	2,1
Bahrain	2
Liberia	2
Turkmenistan	1,7
Benin	1,6
Cypress	1,56
Togo	1,5
Latvia	1,4
Paraguay	1,3
Georgia *	1,3
French Guiana	1,2
Laos	1,2
Mavrikia	1,2
Moldova	1,2
Niger	1,2
Rwanda	1,2
Sierra Leone	1,15
Burundi	1,1
Macedonia	1,06
Belarus	1,03
Haiti	1
Tajikistan	1
Total	**132,63**

Foreign Debt of under USD 1 billion	
Guinea-Bissau	0,953
Central African Rep.	0,93
Chad	0,875
Armenia	0,7754
Faeroe Islands	0,767
Burkina-Faso	0,715
Lesotho	0,66
Albania	0,645
Botswana	0,61
Barbados	0,5814
Mongolia	0,5
Gambia	0,426
Bahama Islands	0,3817
Iraq	0,3275
Namibia	0,315
Belize	0,288
Aruba	0,285
Djibouti	0,276
Estonia	0,27
Sao Tome and Principe	0,267
Equatorial Guinea	0,254
Greenland	0,243
Antigua and Barbuda	0,24
Cape Verde	0,22
Comoro Islands	0,219
Fiji	0,217
Surinam	0,216
Latvia	0,212
Martinique	0,18
Maldives	0,179
Swaziland	0,175
Seychelles	0,17
Samoa	0,167
Cook Islands	0,16
Solomon Islands	0,145
Malta	0,13
Micronesia	0,129
Marshall Islands	0,125
Palestine Autonomy	0,108
Dominica	0,105
Azerbaijan	0,1
Palau	0,1
Bhutan	0,087
Saint Vincent and the Grenadines	0,0836
Taiwan	0,08
Grenada	0,074
Cayman Islands	0,07
Vanuatu	0,063
Tonga	0,062
Erithrea	0,046
Virgin Islands (Britain)	0,0348
Nauru	0,0333
Anguilla	0,0085
Kiribati	0,0072
Kirgizia	0,0014
Total	**15,293**

According to 1998 data, the indebtedness of the countries of the world totalled USD 4 trillion 140 billion

*** As of June 2001 Georgia's foreign debt totalled USD 2.077 billion**

Foreign debts of developing countries make up USD 1.8 trillion (see Table 2). While in 1986 the amount of foreign indebtedness in these countries totaled USD 1 trillion, in 1996 it reached USD 1.8 trillion.

In the 1990s a new group of countries with heavy arrears - the CIS countries - has been formed. By 1996, their foreign indebtedness made up USD 272 billion.

Table 2: The Structure of Foreign Debts of Developing Countries
(USD billions)

	1973	1979	1982	1990	1995
By term					
Short-term	18.4	88.1	146.1	185.3	304.9
Long-term	11.8	416.6	634.7	1042.7	1427.3
By creditor					
Interstate	51.0	163.5	239.7	579.3	791.4
Commercial banks	31.1	208.5	390.1	386.7	422.1
Other private structures	48.1	132.7	151.0	262.0	518.6
Total	**130.2**	**504.7**	**780.9**	**1227.9**	**1732.2**

Source: Managing the World Economy. Fifty Years After Bretton Woods, Ed. Kenen P.B.W., 1994; World Economic Outlook. IMF May 1997, p.192.

Formally, Georgia does not belong to the group of countries with huge foreign indebtedness, but by means of plain statistics it becomes obvious that the situation leaves much to be desired. Although, compared to many other countries, the share of Georgia's foreign debts against the GDP is relatively low: by the end of 2000 this parameter had reached 69.9 per cent. As it is, it does not mean much, as a similar indicator for such non-payer countries as Chad and Rwanda is 30 per cent.

The shares of foreign debts in the GDP for most countries of the world is as follows:

Table 3: Shares of foreign debts in the GDP of some of the countries, according to 1997 data

(Per cent)

Country	The share of foreign debts in the GDP
Albania	22
Algeria	65
Angola	206
Argentina	3
Azerbaijan	10
Bangladesh	20
Byelorussia	5
Benin	46
Bolivia	51
Botswana	9
Brazil	23
Brunei	0
Bulgaria	96
Burkina Faso	30
Burundi	58
Ghana	57
Germany	0
Guatemala	21
Guinea	65
Great Britain	0
Dominican Republic	27
Ethiopia	131
Egypt	28
Ecuador	72
El Salvador	25
Erithrea	4
Estonia	14
Venezuela	41
Vietnam	78
Zambia	136
Zimbabwe	52
Turkey	43
Turkmenistan	59
Jamaica	90
India	18
Indonesia	62
Japan	0
Jordan	110
Iran	9
Cambodia	52
Cameroon	93
Kenya	49
Columbia	27
Congo (Dem. Rep.)	215
Congo (Rep)	247
Korea (Rep.)	33
Costa Rica	34
Côte d'Ivoire	141
Laos	53
Latvia	8
Lesotho	35
Lebanon	32
Lithuania	15
Liechtenstein	0
Luxembourg	0
Madagascar	85
Macedonia	75
Malawi	45

Country	The share of foreign debts in the GDP
Malaysia	48
Mali	73
Mauritania	169
Morocco	53
Mexico	37
Moldova	52
Mongolia	49
Mozambique	135
Nepal	25
Nicaragua	244
Niger	56
Nigeria	72
Norway	0
Pakistan	38
Panama	88
Papua New Guinea	41
Paraguay	20
Peru	27
Poland	27
Puerto-Rico	0
Rwanda	30
Rumania	29
Russian Federation	27
San-Marino	0
Georgia	**33**
Armenia	26
South Africa	19
Saudi Arabia	0
Senegal	56
Sierra Leone	89
Slovakian Rep.	48
Singapore	0
Syria	114
Thailand	61
Tanzania	77
Tajikistan	34
Togo	59
Tunis	58
Uganda	31
Ukraine	21
Hungary	52
Uruguay	32
Uzbekistan	11
Philippines	51
Kazakhstan	19
Kyrgyzstan	39
Sri Lanka	35
Switzerland	0
Chad	30
Czech Republic	40
Chile	43
China	15
Central African Republic	53
Croatia	36
Haiti	21
Holland	0
Honduras	86
Hong-Kong, China	0

Source: World Bank, "World Development Report 1999/2000

1. STRUCTURE AND DYNAMICS OF GEORGIA'S FOREIGN DEBTS

By the end of 2000, Georgia's foreign indebtedness equaled USD 2,180.5 million, that is 69.6 per cent of GDP. The growth of Georgia's foreign debts by year is given in Figure 1 and Table 4.

Figure 1: Foreign Debt of Georgia, 1995 – 2000
(USD millions)

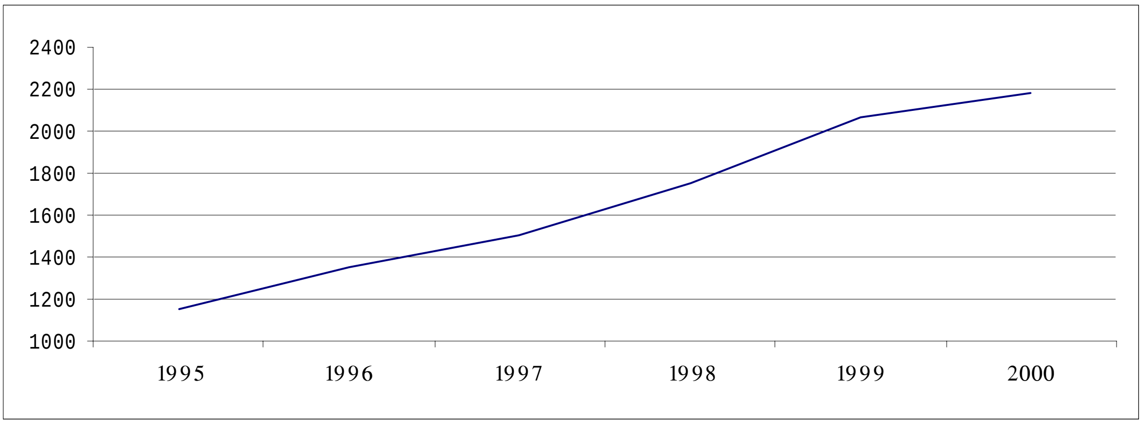


Table 4: Georgia's Foreign Debts Ratios
(USD millions)

As of	Foreign Debt	GDP	Foreign Debt Servicing	Consolidated Budget* Expenditures	Share of Foreign Debt Servicing in Consolidated Budget Expenditures (Per cent)	Share of Foreign Debt in GDP (Per cent)	Foreign Debt Per Capita
1995	1,149.7	2,955				38.9	239.5
1996	1,347.7	4,206		715.8		32.0	280.8
1997	1,508.7	4,946	40.99	753.9	5.4	30.5	314.3
1998	1,752.7	5,047	53.2	751.1	7.1	34.7	365.1
1999	2,039.2	4,142	81.6	655.0	12.5	49.2	424.8
2000	2,180.5	3,133	61.5	574.2	10.7	69.5	436.1

**State budget and local budgets*

The conditions under which credits were received by Georgia before 1994 have become onerous. Annual interest rates on credits from Armenia and Turkey were Libor+1[1] and for Kazakhstan it was Libor+2 on 6-months loans. An annual penalty rate from Turkey was Libor+3, while for Armenia it was 2x (Libor+2).

A high interest rate (7.25 per cent) was fixed on the third credit agreement concluded between the Ministry of Communications of Georgia and a German ***Siemens*** company and on credits of the European Bank for Reconstruction and Development (EBRD): 7.2 per cent; 6.59 per cent with Libor+1 plus a 1 per cent one-time commission fee. It is remarkable that credits arrangements with ***Siemens*** and EBRD are commercial and they benefit from a state guarantee.

[1] Libor - London Inter-bank Offered Rate

Acceptable terms and high grant-elements (share of credit amount which is almost equivalent to a grant) are mainly characteristic for credits from international organizations (IMF, WB, International Fund for Agricultural Development, German Reconstruction Credit Agency, Japanese Fund for Overseas Economic Relations).

The most favourable conditions are those for the 1st and the 2nd credits issued by the German Reconstruction Credit Agency with 10- and 13-year grace periods. Similar conditions also apply to the WB credits. After restructuring the credits of Azerbaijan, Armenia, Iran, Kazakhstan and Uzbekistan the grant elements are, on average, acceptable. Later, credits of China and Turkey have also been postponed under the same conditions. A complete structure of Georgia's foreign debts is given in Table 5 below.

Table 5: Foreign Debts of Georgia, as of June 2001
(USD millions)

	Creditor Countries	Amount of Credits Received	Amount Spent	Interest Rate	Grace Period	Share of Total	Credit Term	Date of Issue and Restructuring of Credits	Date of Ratification
1	**Russia ***	179.266	179.266	4%	3	8.63%	10	14/01/97	
2	**Armenia**	19.593	19.593	4%	5	0.94%	10	05/06/96.	
3	**Azerbaijan**	16.19	16.19	4%	5	0.78%	10	18/02/97	29/04/98
4	**Kazakhstan**	27.77	27.77	4%	5	1.34%	10	01/07/96.	
5	**Turkmenistan**	393.57	393.57	4%	3	18.95%	8	20/03/96	
6	**Uzbekistan**	1	1	4%	5	0.04%	10	28/05/96	18/09/96
7	**Ukraine**	0.915	0.915	4%	4	0.04%	8	14/02/97	
8	**Austria**	77.109	77.109	4%	5	3.71%	14	10/01/97.	
	Bank of Austria "Control Bank"	74.75	74.75						
	Bank of Austria "Credit Bank"	2.359	2.359						
9	**China ***	3.316	3.316	4%	5	0.16%	10	20/12/97	
10	**Germany**	98.864	50.893			4.76%			
	Vartsikhe Hydro Power Station Cascades Rehabilitation KFW	30.925		0.75%	10	1.49%	30	12.3.98	
	Assistance for Energy Sector Program - KFW	7.061	5.439	0.75%	10	0.34%	30	28/04/98	25/06/98
	Microcreditbank credit - KFW	2.435	2.254	0.75%	10	0.12%	40	04/03/98.	17/07/98
	Establishment of land cadaster and registration systems KFW	14.610	0.374	0.75%	12	0.70%	30	10.4.99	
	EBRD	4.87	4.86	0.75%	11	0.52%	3000%	23/05/95	
	Immediate assistance Energy Program I (Rehabilitation of block 9) KFW	9.74	9.655	0.75%	11	0.26%	3000%	26/06/96	27/06/98
	Immediate assistance Energy Program II KFW	6.331	6.319	0.75%	12	0.34%	3000%	16/01/96	15/05/96
	Agricultural program for private sector	3.41	3.03	0.75%	10	0.18%	3000%	12.2.94	
	Immediate assistance Energy Program III KFW	19.480	18.949	0.75%	12	1.03%	3000%	26/06/96	25/12/96
11	**Turkey ***	54.337	54.337	4.00%	4	2.62%	13	04/02/98.	
12	**Iran ***	12.826	12.826	4%	5	0.62%	10	03/11/96.	
13	**USA ***	40.00	39.62			1.93%			
	I credit on wheat	20.00	19.91	1,5% (2%)**	5	0.96%	30	06/03/97.	
	II credit on wheat	15.00	14.76	1,5% (2%)**	5	0.72%	30	27/02/98	
	III credit on wheat	5.000	4.956	LIBOR+0.25%	2	0.24%	9	31/07/98	24/12/98
14	**Japan**	50.867	2.912	2.3%	10	2.45%	30	19/01/98	15/05/98
15	**Kuwait**	16.500	0.184						
16	**International Monetary Fund**	334.665	334.665			16.11%			
17	**World Bank (26 bprojects)**	519.327	367.751			25.00%		1994-1999	
18	**EU**	104.753	104.753	Libor + 0,0005	10	5.04%	15		12.12.97
19	**EBRD**	99.85	45.96			4.81%			
	Rehabilitation Project -Saqenergo	18.10	18.09					19.12.94	
	Airport credit	11.00	11.00	6.59%	3	0.53%	10	13/07/95	30/10/98
	TBC Bank	3.00	2.68	LIBOR+1%	2.5	0.14%	9.5	12.12.96	30/05/97
	Tbilcombank	3.00	2.44	LIBOR+1%	2.5	0.14%	9.5	12.12.96	30/05/97
	Tbilcreditbank	3.00	3.00	LIBOR+1%	2.5	0.14%	9.5	12.12.96	30/05/97
	Tbiluniversalbank	1.00	0.77	LIBOR+1%	2.5	0.05%	9.5	18/03/97	
	Intellectbank	2.00	0.67	LIBOR+1%	2.5	0.10%	9.5	10.11.97	
	Enguri Hydroelectric Station Rehabilitation Project	38.75	1.163	7.30%	4	1.87%	15	22/12/98	22/07/99
	TransCaucasus Railway Project	20.00	0.20	LIBOR+1%	3	0.96%	12	22/12/98	23/07/99
20	**International Fund for Agricultural Development (IFAD)**	6.29	3.20	0.75%	10	0.30%	40	15/05/97	27/06/97
	Total	**2077.29**	**1662.99**						

* Restructuring of this country's debts took place in March 2001
** first 4 years - 1,5%. next 25 years - 2.0%.
Terms of debt restructuring agreed upon at Paris Club are not taken into account as the relevant agreements have not yet been concluded with any of the countries
The table has been completed basing on the crossrates by NBG

1 USD=	2.06 GEL	1 EUR=	0.84730 USD	1 SFR=	0.55660 USD
1 ATS=	0.06160 USD	1 JPY=	0.00810 USD	1 KWD	3.24480 USD
1 DEM=	0.43320 USD	1 SDR=	1.24584 USD		

The credits received by Georgia could be classified into three groups:

- Technical credits on arrears arising from trade and economic relationship with the former soviet republics (Russia, Armenia, Azerbaijan, Kazakhstan, Uzbekistan) in the amount of almost USD 229 million;
- Credits on arrears incurred from the import of products (such as gasoline, wheat, foodstuffs, medicaments, tractors, etc.) from Turkmenistan, Ukraine, China, Turkey, Iran, including EU credits;

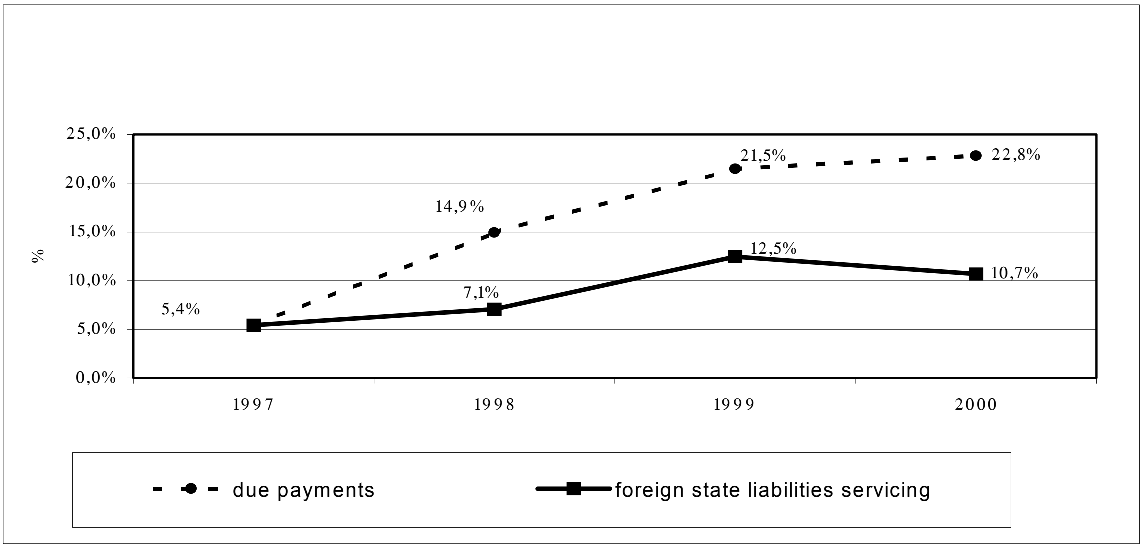
- Rehabilitation credits (II and III credits from Russia, German, IMF, WB, EBRD, International Agricultural Development Fund credits) which had to be directed to satisfy the needs of various sectors of the economy.

Difficulties with foreign debt servicing started with the payment of the principal on the Turkmenistan credit. In 1998-1999, a yearly amount payable on the principle was USD 78.8 million of which the amount actually paid over two years was only USD 39.4 million while USD 118.2 million is counted as an outstanding debt. Apart from the Turkmenistan and EU credits, the payments of principal on credits from Russia, Ukraine and China are also due to start by 2000.

Actually, it was necessary to pay USD 131 million from the budget to cover the payments due in 2000, USD 101.9 million of this was deemed to cover a part of the principal sum and about USD 29 million was to be paid as interest. In total this sum makes up 31 per cent of the actual State Budget expenses. With the current budgetary crisis, this presents rather a big challenge for the country.

Thus, since 1998 Georgia has, as far as possible, avoided payment of due arrears in full. This decision of the Georgian government is quite understandable, as with a full coverage of the payments, their share in total expenditure would actually double (see Figure 2). Given the conditions of a chronic budget deficit this would even further aggravate the current painful situation in the country.

Figure 2: The Share of Georgia's Foreign Debt Servicing in the Consolidated Budget



2. ECONOMIC PROBLEMS OF SOVEREIGN DEBTORS IN CASE OF NON-FULFILLMENT OF OBLIGATIONS

To overcome the debts crisis it is necessary to study the reasons for which this or that country may refuse to service its debts. In most cases, the state incurs foreign debts either directly or acts as a guarantor. So, decisions on non-payment of debts are made at the governmental level and not by a private debtor.

A decision made by a government on non-payment of foreign debt is a breach of obligations by a sovereign debtor as, in this case, the sanctions traditionally applied towards private persons could not be applied to the government in a similar situation. What really matters is which way is more advantageous to the state: to suspend debt servicing or to keep on paying.

When taking a decision on non-payment of foreign debt, the government has to take account of three principal losses it will incur in this case:

1. Arrest of assets. It is quite likely that creditors succeed in persuading their governments to arrest the assets of the debtor country. "Assets" mean international reserves of central banks of sovereign debtors, assets owned by residents of this country which are located in creditor countries and even goods imported to a creditor country.

2. Refusal of credit. There is a chance that, after the declaration of non-payment of foreign debts has been made, the state might temporarily be refused access to capital markets. Future creditors will treat proposals made by unstable states with a certain mistrust. In the case where a sovereign debtor succeeds in obtaining a new loan, old creditors may try to recover these reserves to cover the indebtedness. These processes produce a rather negative impact on the economy of developing countries. The government has to perform all home investments through its own scarce savings. Moreover, when the country has lost a flexible foreign capital attraction mechanism, during a temporary shortfall in real earnings, no consumption and investment means are available. Such fluctuations increase economic losses and provoke a further aggravation of the political situation in the country.

3. Reduction in earnings from international trade. A most serious loss for a country is a restriction of participation in international trade. To a certain extent, this is a resultof the above-referred reasons. As mentioned above, there is the possibility that goods exported to a creditor country might become arrested on account of debt coverage. Moreover, a worsening of the debtor country's positions on the foreign capital markets shall restrict its chances to contract commercial credits and to control operations performed on foreign bank accounts (as these accounts may also be arrested). When the country no longer has the means to perform currency transfers it will have to revert to barter trade.

By contrast, in some cases, making a decision on non-payment of debts has a certain advantage, the country shall no longer have to cover either the interest or the principle.

To measure the share of foreign debt servicing in the national accounts system there is a special indicator: the net outflow of resources from creditor to debtor (**RT**). This indicator is calculated as follows: volume of new credits received by the country (**L**) minus debt service (**S**), as well as net capital outflow from this country (**O**), i.e.:

$$RT=L-S-O$$

If RT is a positive value, new credits contracted by the country are exceeding over the volume of services paid to creditors, i.e. capital inflow to the balance of payments from abroad. If RT is a negative value we have a capital outflow, i.e. new credits are not exceeding the amount due to cover the existing indebtedness.

As seen from the table, for several years, in Georgia the values reflecting net outflow of resources from the creditor to the debtor have been positive (see Table 6). It is apparent that under such circumstances, the country will not make a decision on non-payment of debts as long as the net capital inflow from creditors remains positive. A state will always fulfill its debt servicing commitment if it receives these resources from new creditors without pains. However, with a negative RT, there is always a temptation to breach debt obligations. As a matter of fact, a debtor country does not make a decision on non-payment unless it is more beneficial compared to the anticipated losses incurred through the breach of credit arrangements.

Table 6: Net Outflow of Resources from Creditor to Debtor, in Case of Georgia.
(USD millions)

Name	1995	1996	1997	1998	1999	2000
Volume of new credits (L)	216	198	161.1	243.9	286.6	201.3
Paid interest and principal (S)	19.4	24.1	40.9	53.22	81.62	60.9
Net capital outflow (O) *	-210.3	-323.6	-280.6	-126.4	-121.8	-108
Net resources outflow from creditor to debtor (RT)	406.9	497.5	400.8	317.08	326.78	249.3

3. WAYS AND METHODS OF DEBT CRISIS MANAGEMENT: THE HIPC INITIATIVE

Debt crisis management is a rather complicated and diverse process involving the participation of the governments of both creditor and debtor countries as well as the International Monetary Fund, the World Bank and major commercial banks which have certain claims to developing countries.

The idea of writing off debts on a large scale is gradually striking root all over the world. Since the debt crisis of the 1980s, this process has been evolving:

- in 1982-1985 creditors made every effort to recover debts
- in 1985-1989 the Baker Plan - a debt crisis overcoming method - was operating
- since 1989 until now the Brady Plan, when there was a partial write off the debts, was operating

By the end of 1985, creditor countries offered these states a less tough policy known as the Baker Plan after James Baker, the then US Secretary of Finance (Treasurer of the United States). According to the new plan, creditor countries still opposing the reduction of the volume of debts, allowed debtor countries and commercial banks to negotiate debt servicing conditions themselves. Debtor countries were to receive long-term financial aid from the International Monetary Fund and World Bank. Debtor countries would commit themselves to long-term reforms under the supervision of the IMF and WB.

For their part, creditor countries relaxed the conditions for credits granted by them. While commercial banks and debtor countries conducted negotiations through the London Club, interstate credits were considered at the Paris Club. It is since that time that the International Monetary Fund has started to play the key role in the process of overcoming the debt crisis. A debtor country's reform programme had to be accepted by the IMF.

The Baker Plan failed to provide any appreciable advance to developing countries, as it offered only a deferral of payment. In most debtor countries the debt crisis continued implying the need for more effective measures.

The Baker Plan was based on a presumption that the debts would be gradually returned in full. Having admitted that this could not happen, in March 19989 the new Secretary of Finance - Nicholas Brady, worked out a new plan. He declared that a full return of debts was impossible and that it was necessary to exert pressure on banks to achieve some alleviation of the debt burden. At the same time, he urged that for the reduction of the volume of the debt payments the secondary market was to be expanded.

Compared to Baker's plan, Brady's plan was a step forward with a real reduction in debt liabilities. The banks had no other way but to acknowledge the impossibility of ever returning that colossal volume of debts in full. In their attempts to recover debts fully, banks might cause such destabilization in debtor countries that the final amount received would be much less than that could be received through negotiations.

A strategic policy also played a significant role. It became apparent that the debt crisis constituted a menace to the political stability of the Latin American countries. Democratic regimes established with so much difficulty in Mexico, Argentina, Brazil and other states were put under threat.

Meanwhile by 1989, banks had managed to improve largely their positions and despite enormous losses, the debt crisis could no longer cause a collapse of the world financial system, the danger of which had been real in 1982.

The Brady Plan comprised three main principles:

1. Commercial banks must "offer debtor countries a wider range of choice of alternative forms of financial aid, including reduction of the capital amount and accrued interest, as well as ensure granting new credits to them". Brady urged to refrain from filing a statement of claim for a while so that the bank and the debtor country could settle problems relating to the indebtedness.

2. IMF and WB were responsible for providing financing "for the reduction of the capital amount and due payments for debt servicing". Actually, international institutions could act as guarantors for the loan securities issued by a debtor country instead of the foreign debt or issue a credit "to fill a debtor country's reserves" so as to let them buy out their own debt liabilities on a secondary market.

3. It was necessary to change the practice requiring a debtor country to obtain consent of the old creditor commercial banks before obtaining a loan from IMF.

By 1991, under the Brady Plan, a number of countries had reached agreement with commercial banks. After long-lasting negotiations creditor banks reduced the amount of the debts by 35 per cent for Mexico, by 9.9 per cent for Venezuela, by 18.8 per cent for Uruguay, by 4.7 per cent for Philippines, by 65 per cent for Costa Rica and the foreign debt of Niger was written off completely. For other developing countries these negotiations were less successful, though.

Apart from the Brady Plan aimed at solving the problems of commercial banks, the creditor countries took measures for regulation of interstate debts. The interstate debts reduction policy for the poorest countries located south of Sahara was launched in 1987. In 1997, application of these measures was extended to other poor countries, as well and in the first place to Poland and Egypt. The interstate debts for these countries were cut by half by the Paris Club.

Like the Baker Plan, despite its positive effects and benefits the Brady Plan also proved unable to settle completely the problem of the debt crisis in the long run. Presumably, in this case too, it was only a postponement of the problem, as it failed to perform a full rehabilitation of the debt crisis participants.

The illusion that developing and post-socialist countries could be turned into normal debtors has been destroyed. These countries are incapable of repaying the interstate and other credits granted by the western commercial banks.

In the summer of 1999, on the initiative of the US President and under the decision of the "G7" with an active participation of the International Monetary Fund and World Bank a new stage of forgiving debts had commenced. This mainly concerned African countries. Those developing countries which are oriented towards democratic development and economic reforms shall have their foreign debts written off. The International Monetary Fund has started to work actively on a new ***Heavily Indebted Poor Country*** **(HIPC)** ***Initiative*** programme.

Georgia's participation in the new world initiative and its liberation from the debt burden has become urgent after the government of the United Kingdom put forward a proposal on joining Georgia and some other former soviet republics (such as Armenia, Azerbaijan, Moldova, Tajikistan) to this new programme.

Within the frames of this initiative, the reduction of debts has both positive and negative sides. Nevertheless, for a country in a similar situation to Georgia, the positive effect of amortization of debts is predominating over the negative one which might result from its joining the ranks of poor countries. The negative side of it is a tarnished image resulting in a certain restraint from foreign investors with regard to maintaining relationship with a country having a very low credit rating. It may also encounter certain difficulties in terms of obtaining new credits.

The above initiative is a broad approach providing for the reduction of arrears of the poorest countries. This programme requires the participation of all creditors. The main idea of this initiative is that the countries endeavor to regulate their macro-economic situation, perform structural reforms and improve social policy. At the same time, the initiative implies additional funding of the social sector and primary health care and education. Certain changes were made to the initial version of the initiative for a more rapid, deeper and broader relief of the debt burden and for interconnecting debt amortization, poverty reduction and social policy.

Of course, this initiative is not a panacea. Even if all creditors forgive these countries their debts they shall still continue to be dependent on foreign aid.

To join the initiative the country must satisfy some criteria: a debt burden beyond their capabilities, with limited chances for its reduction. Besides, the country must declare its readiness to pursue a deliberate economic policy. These countries includes Angola, Benin, Bolivia, Burkina Faso, Burundi, Cameroon, Central African Republic, Chad, Congo, Ivory Coast, Democratic Republic of Congo, Ethiopia, Gambia, Ghana, Guinea, Guinea-Bissau, Guyana, Honduras, Kenya, Laos, Liberia, Madagascar, Malawi, Mali, Mauritania, Mozambique, Mianma, Nicaragua, Niger, Nigeria, Rwanda, Sao Tomé and Sierra Leone, Somali, Sudan, Tanzania, Togo, Uganda, Vietnam, Yemen, and Zambia.

In 2000, a further analysis of its debts revealed that Yemen is quite capable of bearing the burden of its debts even by use of traditional facilitation means. It is also doubted whether Angola, Kenya and Vietnam will receive aid within the frames of this initiative. As to Laos, it has refused to participate in this programme.

All countries claiming aid within the frames of this program shall have to meet additional requirements, namely to elaborate a Poverty Reduction Strategy and successfully implement it during a period of one year.

At the first stage the country shall work out a programme together with the IMF and WB. During this period it shall receive traditional aid from relevant donors and shall also have the debt burden relieved from bilateral creditors, including the Paris Club. If as a result of a full-scale analysis of the foreign debt performed at the end of the first stage it proves to be exceeding the export indicator by 150 per cent, the country shall fall eligible for further aid under this initiative. In a special case, to ensure reduction of the debt to export ratio, countries shall also be counted eligible if their economy is too open (when the exports ratio to the GDP is above 30 per cent) and if the ratio between the size of debt and fiscal revenues is too high despite a good collection of revenues (more than 15 per cent of the GDP). Extension by the IMF and WB shall also be dependent on the position of other creditors with regard to the fulfillment of liabilities by these countries.

As a result, 22 states have been involved in this initiative, which led to the reduction of their indebtedness from USD 53 billion to USD 20 billion.

Notwithstanding certain difficulties, it would not be reasonable for Georgia to refrain from participation in this initiative. This is that very case when a further worsening of an already notorious reputation would be less problematic compared to the risk of increasing social and political tension.

APPENDIX II: TAX FEDERALISM CONCEPT: CONSENSUS VERSUS SEPARATISM

By Vladimer Papava, Senior Fellow of Georgian Foundation for Strategic and International Studies, Doctor of Economic Sciences, Professor

Today, when the country is in the severest of budgetary crises, the most important task is to do the utmost to find and use all the reserves to ensure the growth of budget revenues. In this respect, it is particularly important to choose such a pattern of regional arrangement of the fiscal system that can provide a maximum of budget receipts.

It should be noted from the very beginning that the aim of this article is not to discuss this or that type of taxes or the expediency of their amounts but to discuss a system of tax income distribution between Regions and the Centre of the country.

The tax system is an element of a financial and budgetary system and is to a large extent defining an income item of the budget. In its turn, the territorial aspect of the financial and budgetary system is predetermined by a territorial structure of the State. Economists usually use a term "financial and budgetary federalism" regardless of whether it is a federal or a unitary State (Hewitt, Michaljek, 1993, p. 392). It is necessary to underline that jurisprudence does not give a full definition of a concept of "Federal State" while some well-known legal experts even altogether reject the possibility of defining it (e.g. Gogiashvili, 2000, p. 23-28; Khubua, 2000, p.212-216).

The term "financial and budgetary federalism" covers both sides of the State's financial and budgetary system: on the one hand, it regulates tax incomes and on the other – it deals with the distribution of expenditures to be financed by the government between the central ("Centre) and territorial ("Regions) government authorities. In the case of a federal state, by "Agents of a Federation" we mean regions hereinafter provisionally referred to as "Federal Regions".

"Tax Federalism", i.e. the separation of taxation power between the Centre and the Regions in a unitary state and between the Centre, Federal Regions and Regions in a federal state is the most complicated task for economics and one can say that no common and at the same time generally acceptable and hence a faultless pattern is available (Hewitt, Michaljek, 1993, p. 395). Although modern economics does not possess any more or less cogent arguments concerning optimum ways of separating taxation powers, there is a smaller diversity of possible approaches to distribution of tax levying functions between Centre and Regions in unitary states than between the Centre, Federal Regions and Regions in the federal states of the West[1] (Hewitt, Michaljek, 1993, p. 392). This explains why "financial and budgetary federalism" and in particular, "tax federalism" is more interesting in the context of federal rather than unitary states.

The choice of this or that pattern of "financial and budgetary federalism" depends on what functions the Central Government intends to perform itself and what functions are to be delegated to Agents of Federation. To this end, the original problem is to define so-called "minimal functions" of the Central Government, which is a basic condition providing for the integrity of the state. These "minimal functions" include state defense, establishment of a common legal space, foreign relations, introduction of a common trade regime, emission of a common currency and control over its turnover,

[1] This is proved by the analysis of the practice of some Unitary and Federal States (Русакова, Кашин (ред.),p.235-456).

achievement of macro-economic stability, application of measures ensuring equalization of the social and economic development of regions. As international practice shows, any "other functions" could be, partially or fully, performed by the Agents of Federation.

In any democratic (or claiming to be such) state, a central government, usually, declares its readiness to give as much freedom to regional authorities as possible. This means the delegation of "more functions" to them and exactly in the same way, these last very often publicly claim their loyalty to the central government and their endeavours towards strengthening the unity of the state. Despite this, the practical evidence is such that almost none of the Federal States has succeed in a perfect realization of these publicly made declarations: there is always a number of problems discussed between the Centre and the Regions (especially between Centre and Federal Regions) with more or less ardour in the course of discussions on the separation of state functions.

In Federal States with a comparatively longer history of democratic development the frame for discussion is comparatively narrow and the discussion itself is correspondingly less arduous.

As proved by international practice, the following principal approaches are used in the above-referred confrontation between the Centre and the Regions:

The Centre as a rule, is practically never content with implementation of just "minimal functions" (though, certainly it does not declare it) and seeks to maintain some extra instruments of state management. To this end the Centre retains such mechanisms as transfers from the central budget intended for the regulation of problems both throughout the country and in separate regions. So, it is only natural that in many cases the Centre tries to extend the system of "transfers".

The Regions (especially Federal Regions) act through radically different mechanisms. They seek the growth of that part of tax revenues which is intended to remain in regions, at the expense of the coverage of the types of taxes and so through delay the process of tax incomes distribution to their benefit. This, in its turn, results in "pulling over" the functions to be performed by the government at a regional level. Apart from these legal methods Regions in some cases also use illegal mechanisms. Namely, as mentioned in one of the general surveys conducted by IMF, in some Federal States, where transfers of their shares by the Agents of Federation to the Central Budget are made in conformity with relevant laws in a full amount and a due time frequently, there is one such Agent of Federation who contrary to law retains a part of income which belongs to the Central Budget; in such cases, the Centre cuts transfers for the offending "Federal Region" by a corresponding amount but a winner in this confrontation is still the "Agent of the Region" as such action gives him a strong financial instrument empowering him to influence the policy pursued by the Centre; consequently the conclusion is that proceeding from common state interests, the Centre should be able to collect payments directly from those who participate in economic activities without consensus of the Agents of Federation (Hewitt, Michaljek, 1993, p. 392).

Conceivably, the Budgetary Office of the Georgian Parliament was guided by these concepts when it considered inadmissible to let the budget of the Autonomous Republic (AR) of Ajara retain a part of the proceeds from VAT payments, excise, and customs taxes according to the long-term budget norms (Budgetary Office of the Parliament of Georgia, 2000, p.4).

According to the above-mentioned IMF survey, at first it is difficult not to agree to the concept referred to by the Budgetary Office of the Parliament. We discuss this issue In more detail below.

Economics, as already mentioned , does not have any strict criteria, on the basis of which it would be clearly defined whether this or that kind of tax is federal or local by its nature. The only thing that could be said thereof is that a more of less precise theoretical statement as to their "hierarchical" nature could be found with regards to just two kinds of taxes: real estate tax (including land) and customs duty. The first one is considered as local for accumulation of property occurs on a certain territory and the second one is federal, for the customs belongs to the entire country and not to its separate regions. There have been frequent attempts to give a logical explanation as to why to VAT and excise duty should also be regarded as federal. Theoretical grounds to this end are so artificial that they could by no means be considered satisfactory.

It should also be underlined that developed countries, where there is a federal structure, use various schemes for the division of the taxation functions and there are no criteria for choosing the best among them (in terms of effectiveness); at the same time it also remarkable that there is no explanation for proving why "collection" of several taxes by the Centre and the Regions at one and the same time is impossible.

Let us consider the particular situation existing in Georgia on the grounds of the international practice and economic recommendations on the basis of which it will be possible to find the most appropriate decision at this stage.

As noted above, according to the position of the Budgetary Office of the Parliament of Georgia it is inadmissible that the budget of the AR of Ajara retains a part of the VAT, excise duty and customs duty under the long-term budget normatives. Presumably, the budgetary office of the Parliament of Georgia is even more against of leaving a part of the VAT in Tbilisi or a part of customs duty in Poti (being quite an acute issue between them) to say nothing of other regions of Georgia (for instance, Imereti, where the analogous proposals are being actively implemented by the authorities).

It should also be noted that an approach suggesting a strict separation of taxes in accordance with the hierarchy is becoming more and popular with the governmental structures of Georgia, when let us say, VAT shall be counted as a federal tax and recovered 100 per cent in the Central Budget while for example an income tax shall be counted as a local tax and shall also be recovered 100 per cent by the local budget, respectively. Within this context it is remarkable that as proved by the international practice, in more than one Federal or Unitary State an income tax is also federal (and not local) by a hundred percent and in some of them it is divided between the Centre and the Regions (See Table 1).

Such approach, to our mind, is the main principle of the tax federalism pattern. At one glance it seems quite attractive, as the scheme of division of taxation powers is simplified, which to some extent gives grounds for an actual exclusion of objective possibilities to illegally retain or "hide" the tax income due to the Central Budget by an Agent of Federation. Recently, one of the main subjects for dispute between the Central Government and local authorities of the AR of Ajara was compatibility of the amounts of all kinds of taxes transferred to the Central Budget with the regulations prescribed by Legislature. Under the above referred approach, the issue at point becomes irrelevant as the Law states that the proceeds from this or that tax revenues should be transferred to the Central Budget either a hundred percent or not transferred at all. The fact that in this case the subject for dispute disappears and the action of the federal region becomes rather transparent does not at all guarantee that, as proceeding from the above-mentioned international experience, the Agent of the Federation would not be left a chance to avoid Law in order to have a political impact on the Centre.

Table 1: Distribution of income taxes among various levels of government[2]

	Countries	Upper Level Central Government	Medium Level (states, lands, etc.)	Lower Level (local authorities)
I.	Unitary States			
	Developed states			
	Belgium	90.9	_	9.1
	Great Britain	100.0	_	0.0
	Netherlands	100.0	_	0.0
	Norway	47.6	_	52.4
	France	100.0	_	0.0
	Sweden	24.7	_	75.3
	Developing and Post-communist states			
	Zimbabwe	100.0	_	0.0
	Israel	100.0	_	0.0
	Kenya	100.0	_	0.0
	Poland	75.9	_	24.1
	South Africa	100.0	_	0.0
	Thailand	100.0	_	0.0
	Hungary	71.9	_	28.1
	Chile	100.0	_	0.0
II.	Federal States			
	Developed states			
	Australia	100.0	0,0	0.0
	USA	81.1	17,2	1.7
	Germany	39.1	40,8	20.1
	Spain	92.9	1,2	5.9
	Canada	63.5	36,5	0.0
	Developing			
	Argentina	34.2	65,8	0.0
	Brazil	100.0	0,0	0.0
	India	100.0	0,0	0.0
	Mexico	98.1	1,3	0.6

At the same time the above approach, when the division of taxation power according to the types of taxes is made on the principle "all or nothing", ultimately lead us to "taxation separatism", when the interests of the Agents of Federation are totally isolated from the national taxation interests with negative consequences for the integrity of the Federal State. Proceeding from this, we call the application of the above-referred approach in separation of taxation power the " doctrine of taxation separatism".

In order to give a full description of this issue, it is also necessary to underline that apart from the above-referred defect the "doctrine of taxation separatism" owing to its nature, is also practically unrealizable. The case is that development in the regions of any state is marked by inequalities both from the social and economic viewpoint and because of this situation tax collection taxes varies between taxes and from region to region. Consequently, this means that there is a big possibility that while ascribing a regional title to the several types of taxes, an amount collected and retained in one of the regions might appear to be so small that it would need to be supplemented through transfers from the central budget, whereas in any other region tax collection according to the same types of taxes, makes up such a large amount that it would exceed the demand of this region for current budgetary expenditures and it would be reasonable to use it together with this surplus for the above-mentioned central budget transfer. Thus, in practice, the principle "all or nothing" might also come to an obvious disagreement with the maintenance/development of the country's state integrity.

Proceeding from all the above, it becomes apparent that the "Doctrine of taxation separatism" is generally unacceptable for any Federal State and for Georgia in particular.

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[2] The table has been completed based on Norregaard, 1995, p.250.

In Georgia, at a contemporary stage of building up its statehood, when restoration of its territorial integrity is not yet covered by the question of its administrative-territorial system, great importance is attached to economic instruments creating incentives for regions to ascribe to a so-called "regional consensus" so as, in the first place, to make them economically interested in amplification of the state integrity of Georgia.

The concurrent mobilization of taxes both in central and local budgets, could be used as such instruments.

Again it should be stressed that there is no more or less cogent argument in economics which would at the least prove why it is impossible to recover this or that type of taxes at one or another level of state hierarchy.

As mentioned above, the most "impressive" is the definition of real estate tax as local and of custom tax payment as federal. But, let us suggest that a natural or a legal entity owns real estate within (and not only within) various regions of the country, then it becomes difficult to decide unambiguously whether this payment should be paid to the local budget or to the Central Budget According to the location of the real estate it would be logical if the taxes are paid to local budgets but insofar as the property belongs either to a natural entity which can without restriction move within the territory of his own country or to a legal entity, which might be functioning in several regions at one and the same time, the grounds for mobilizing this payment to the Central Budget should not be considered less justified. International practice proves that the real estate tax is regarded as entirely federal only in some unitary states, in other states (except Kenya, where it is regarded as entirely local) this payment is distributed between the various levels of government (see Table 2).

Customs payment could also be made subject to similar considerations. Namely, as customs belongs to the state as a whole and not to any separate region, the idea of mobilization of customs payment to the Central Budget solely, looks quite justified theoretically, though in practice customs-houses are located only in a few separate regions (peculiarly at the country's borderlines, seaports or airports), which creates some extra "burden" for these regions and therefore the reason for retaining at least a small portion of the revenues by a local budget of the region could be as successfully argued.

Therefore, a concurrent mobilization of all types of payments to the Central and Local budgets is a viable economic mechanism for attaining "regional consensus" in a federal state; to determine proportions for such distribution, first of all it is necessary to take in consideration the statute of the Agent of Federation and at the same time the ratio of actual tax collection with regard to any type of taxes in each region to distribution of the budgetary expenses between the Centre and the Regions.

Table 2: Distribution of real estate taxes among various levels of government[3]

	Countries	Upper Level (Central Government)	Medium Level (States, Lands, etc.)	Lower Level (Local Government)
I.	Unitary States			
	Developed states			
	Belgium	100.0	_	0.0
	Great Britain	99.2	_	0.8
	Netherlands	65.1	_	34.9
	Norway	37.9	_	62.1
	France	100.0	_	0.0
	Sweden	100.0	_	0.0
	Developing and Post-communist states			
	Zimbabwe	11.5	_	88.5
	Israel	12.3	_	87.7
	Kenya	0.0	_	100.0
	Poland	48.3	_	51.7
	South Africa	25.5	_	74.5
	Thailand	81.9	_	18.1
	Hungary	100.0	_	0.0
	Chile	19.7	_	80.3
II.	Federal States			
	Developed states			
	Australia	2.4	57.8	39.8
	USA	6.0	6.7	87.3
	Germany	2.0	61.2	36.8
	Spain	5.8	50.5	43.7
	Canada	0.0	16.2	83.8
	Developing			
	Argentina	49.2	50.8	0.0
	Brazil	2.2	40.5	57.3
	India	33.7	66.7	0.0
	Mexico	1.2	0.0	98.8

Proceeding from the above-mentioned approach, inasmuch as Ajara enjoys the status of an autonomous republic defined by the Constitution its claim for a comparatively large part of income from this or that type of taxes seems quite natural; in its turn, it is no wonder that Tbilisi, as proceeds from its status as the capital of Georgia, claims a part of the actually recovered VAT payment; proposals made by the other regions of Georgia, including such regions as Imereti, Kvemo Kartli and the city of Poti, concerning establishment of "Tax Federalism" in the country, is to be taken into account as well.

In order to mobilize additional reserves of tax incomes, together with the budget normatives defined by the budget of tax proceeds, it is also necessary to approve increased budget normatives in the corresponding budgets of each of the regions of the country to be used if the target of budgetary receipts is overdrawn.

Let us call the above-referred approach, where the distribution of recovered tax revenues between the Centre and the Regions is applicable to all types of taxes a "doctrine of tax consensus". It can play a significant role in the formation of federal structure in Georgia and for reinforcement of its statehood. The importance of the "tax consensus" principles in the peaceful settlement of the problems concerning Abkhazia and former South Osetia is also to be taken into account.

As noted above, none of the patterns of the "financial and budgetary federalism" exclude a breach of the Budget Law on the part of any non-payer region (first of all "federal region") when it illegally retains amounts due to the central budget, but the "doctrine of tax consensus" to a great extent serves to ease

[3] The table has been completed based on Norregaard, 1995, p.250.

tension between the Centre and the Regions and under other equal conditions it might even minimumise the above-mentioned cases of non-payment.

Today, Georgia as a state is not institutionally ready to implement a complete pattern of the "doctrine of tax consensus". To this end, the most important impeding factor is that the process of territorial arrangements is still underway in Georgia. It is also remarkable, that for realization of a complete pattern of the "doctrine of tax consensus" the country must have a united, strong Ministry of Finance comprising Taxation, Customs and Treasury so as to conceive the system of "financial and budgetary federalism" of Georgia (i.e. not only expenditure but also revenues) within a single context. Nevertheless, all elements of the "doctrine of tax consensus" are to be gradually realized with regard to all regions of Georgia, which in its turn shall make the prospects for territorial arrangement of Georgia more clear.

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STATISTICAL APPENDIX

CONTENTS *

* Note: First digit in the number of an appendix table indicates the number of the chapter to which it belongs.

Table A3.1: Consolidated Budget, January-June 2001

(GEL millionS)

	Central budget	Special State Funds	Local Budgets	Consolidated Budget
TOTAL REVENUES AND GRANTS	262,6	107,4	168,5	490,2
Total Revenues	256,8	85,7	141,9	484,4
Tax revenues	225,9	85,7	132,9	444,5
Non-Tax revenues	30,9	-	9	39,9
Foreign Grants	5,8	-	-	5,8
Transfers Received From Central Budget		21,8	26,6	-
EXPENDITURES AND NET LENDING	306	107,7	168	479,9
Debt servicing	53,9			
Transfers form central budget	48,3			
DEFICIT	66,8	0,3	0,4	43,6

Source: State Department for Statistics

Note: Figures provided in the table are preliminary and may differ from figures quoted in the text,however it is the best available information on local budgets.

Table A4.1: Accounts of the National Bank of Georgia
(GEL thousands)

	2000	2001						
	Dec	Jan	Feb	Mar	Apr	May	Jun	Jul
Net International Reserves	**-409 388**	**-421 572**	**-429 077**	**-430 397**	**-433 199**	**-424 397**	**-408 967**	**-400 743**
Net Foreign Assets (convertible) (1)	-332 773	-341 367	-350 712	-353 856	-354 291	-350 069	-335 716	-324 518
Use of IMF resources	*-549 832*	*-576 215*	*-578 433*	-595 634	-601 251	-590 190	-578 370	-582 171
Net Foreign Assets (nonconvertible)	-76 614	-80 205	-78 364	-76 541	-78 909	-74 328	-73 251	-76 225
Net Domestic Assets	**801 124**	**787 471**	**789 784**	**789 721**	**796 458**	**790 642**	**792 414**	**805 687**
Net Claims on General Government	754 118	770 865	772 850	735 492	738 306	743 121	753 822	763 845
Net Claims on Banks	2 619	1 468	1 752	-708	2 360	2 198	2 315	405
Claims on the rest of Economy	77 878	81 378	79 505	77 659	80 013	75 440	74 329	77 322
Other assets net	-33 491	-66 240	-64 324	-22 721	-24 222	-30 117	-38 052	-35 885
Reserve Money (M1)	**391 737**	**365 898**	**360 707**	**359 324**	**363 258**	**366 245**	**383 447**	**404 944**
Currency in circulation	329 157	306 326	309 333	309 988	314 716	313 480	319 906	343 861
Banks' deposits	62 580	59 572	51 375	49 336	48 542	52 766	63 541	61 083
Required reserves	*38 943*	*39 029*	*40 640*	*40 872*	*43 608*	*43 745*	*48 585*	*48 301*

Source: National Bank of Georgia

Notes: (1) Since September 2000 NFA (convertible) includes gold, SDR holdings, foreign exchange, Duch account and use of IMF resources.

Table A4.2: Consolidated Accounts of Commercial Banks
(GEL thousands)

	2000	2001						
	Dec	Jan	Feb	Mar	Apr	May	Jun	Jul
Net Foreign Assets	**-12 610**	**-12 549**	**-18 114**	**-3 312**	**-10 522**	**-4 432**	**6 188**	**-19 467**
Foreign exchange	104 953	114 923	113 595	129 673	122 713	135 193	140 268	113 275
Foreign currency liabilities	-117 602	-127 487	-131 719	-132 996	-133 238	-139 628	-134 083	-132 746
Other foreign assets (net) (1)	39	15	11	11	4	4	4	4
Net Domestic Assets	**315 572**	**308 932**	**308 157**	**303 523**	**314 474**	**315 301**	**328 405**	**350 180**
Domestic Credit	**422 187**	**419 246**	**429 366**	**426 367**	**438 737**	**444 162**	**442 447**	**469 553**
Net Claims on General Government	-16 159	-12 794	-14 556	-16 285	-17 033	-19 241	-20 377	-19 223
Claims on the Rest of the Economy	438 346	432 040	443 923	442 653	455 770	463 403	462 824	488 775
Claims on Enterprises (GEL)	*57 136*	*49 807*	*51 259*	*51 399*	*51 490*	*58 059*	*67 223*	*70 539*
Claims on Individuals (GEL)	*33 422*	*35 191*	*33 590*	*31 206*	*30 939*	*32 830*	*33 039*	*33 614*
Foreign Currency Loans	*347 787*	*347 042*	*359 074*	*360 048*	*373 340*	*372 514*	*362 562*	*384 622*
Other Assets Net	**-106 615**	**-110 314**	**-121 209**	**-122 844**	**-124 263**	**-128 861**	**-114 042**	**-119 373**
Deposit Liabilities	**303 248**	**296 384**	**290 044**	**300 210**	**303 952**	**310 869**	**334 593**	**330 713**
GEL Deposits	67 094	54 765	52 496	50 249	49 521	54 939	61 993	61 052
Of which: Enterprises' Current A/Cs	*51 102*	*47 660*	*45 557*	*43 361*	*41 286*	*47 679*	*54 319*	*53 016*
Foreign Currency Deposits	235 868	241 619	237 548	249 962	254 431	255 930	272 600	269 660

Source: National Bank of Georgia

Note: (1) Includes Gold and NFA in soft currencies

Table A4.3: Monetary Survey
(GEL thousands)

	2000	2001						
	Dec	Jan	Feb	Mar	Apr	May	Jun	Jul
Net Foreign Assets	**-421 997**	**-434 121**	**-447 190**	**-433 710**	**-443 721**	**-428 828**	**-402 778**	**-420 210**
Foreign exchange	321 004	348 765	340 309	370 444	368 667	374 307	381 897	369 903
Foreign liabilities	-744 047	-783 908	-788 516	-805 171	-813 397	-804 145	-785 704	-791 141
Other foreign assets (net) (1)	1 046	1 021	1 017	1 017	1 010	1 010	11 028	1 028
Net Domestic Assets	**1 039 966**	**1 020 757**	**1 027 777**	**1 028 838**	**1 045 443**	**1 037 255**	**1 037 880**	**1 073 257**
Domestic Credit	**1 254 183**	**1 271 489**	**1 281 722**	**1 239 518**	**1 257 056**	**1 262 723**	**1 270 597**	**1 310 719**
Net Claims on General Government	737 959	758 070	758 294	719 206	721 273	723 880	733 445	744 622
Net Claims on Republican Government	*752 217*	772 484	775 086	737 469	739 709	746 249	759 997	769 695
Net Claims on Local Government	*-4 629*	*-2 434*	*-1 378*	*-3 229*	*-2 311*	*-2 068*	*-3 573*	*-2 567*
Net Claims on Pension Fund	*-2 983*	*-15*	*-10*	*-3*	*-83*	*-201*	*-388*	*-65*
Other Extra-Budgetary Funds	*-6 647*	*-11 966*	*-15 404*	*-15 032*	*-16 042*	*-20 100*	*-22 591*	*-22 440*
Claims on the Rest of the Economy	516 224	513 418	523 428	520 312	535 783	538 843	537 153	566 097
Other items, net	**-214 217**	**-250 732**	**-253 944**	**-210 680**	**-211 613**	**-225 467**	**-2 327 117**	**-237 463**
Broad Money (M3)	**617 969**	**586 636**	**580 587**	**595 128**	**601 722**	**608 427**	**635 102**	**653 047**
Broad Money, excl. foreign currency deposits (M2)	382 101	345 017	343 040	345 166	347 291	352 497	362 502	383 387
Currency in circulation	315 007	290 253	290 543	294 918	297 770	297 558	300 509	322 334
Currency outside banks (MO)	*329 157*	*306 326*	*309 333*	*309 988*	*314 716*	*313 480*	*319 906*	*343 861*
Cash in commercial banks	*14 151*	*16 073*	*18 789*	*15 070*	*16 946*	*15 922*	*19 398*	*21 527*
Deposit Liabilities (GEL)	67 094	54 765	52 496	50 249	49 521	54 939	61 993	61 052
Foreign Currency Deposits	235 868	241 618	237 548	249 962	254 431	255 930	272 600	269 660

Source: National Bank of Georgia

Notes: (1) Includes Gold and NFA in soft currencies

Table A5.1.1: Registred Foreign Trade Balance, H1 2001
(USD thousands)

Countries	Export (FOB)	Import (CIF)	Balance
Total foreign trade	147 079	364 040	-216 961
CIS	62 968	138 956	-75 988
Armenia	5 948	7 321	-1 373
Azerbaijan	5 141	37 533	-32 392
Belarus	305	1 104	-799
Kazakhstan	1 750	2 590	-840
Kyrgizstan	0	135	-135
Moldova	59	87	-28
Russia	30 293	53 334	-23 041
Tajikistan	36	121	-85
Turkmenistan	14 338	7 246	7 092
Ukraine	4 785	28 394	-23 609
Uzbekistan	313	1 089	-776

Source: State Department for Statistics

Table A5.1.2: Registred Foreign Trade Balance, H1 2001
(USD thousands)

Countries	Export	Import	Balance
EU	27 961	93 360	-65 399
Austria	481	3 354	-2 873
Belgium	6 553	4 251	2 302
Denmark	335	3 036	-2 701
Finland	0	7 414	-7 414
France	171	9 698	-9 527
Germany	3 716	33 587	-29 871
Greece	1 463	1 918	-455
Ireland	0	667	-667
Italy	5 114	10 054	-4 940
Netherlands	2 475	4 601	-2 126
Portugal	63	512	-449
Spain	866	847	19
Sweden	647	1 005	-358
UK	6 077	12 416	-6 339
USA	2 821	28 905	-26 084
Turkey	33 090	50 398	-17 308

Source: State Department for Statistics

Table A5.1.3: Registred Foreign Trade Balance, H1 2001
(USD thousands)

Countries	Export	Import	Balance
Other countries			
Australia	16	251	-235
Afghanistan	0	2	-2
Anguilla	0	35	-35
Algeria	241	0	241
Argentina	0	10	-10
Bahamas	227	36	191
Butan	0	10	-10
Bosnia	3	2	1
Brazil	3	1 125	-1 122
Bulgaria	134	5 480	-5 346
Canada	6	245	-239
China	609	1 711	-1 102
Columbia	0	18	-18
Croatia	0	127	-127
Cyprus	63	1 128	-1 065
Czech Rep,	195	1 227	-1 032
Ecuador	0	373	-373
Egypt	3	23	-20
Estonia	0	17	-17
Gibraltar	363	248	115
Guinea	46	0	46
Honduras	0	147	-147
Hong-Kong	1	254	-253
Hungary	270	2 861	-2 591
Island	0	27	-27
India	2 790	854	1 936
Indonesia	2	2 301	-2 299
Iran	1 859	2 286	-427
Israel	288	305	-17
Jamaica	0	3	-3
Japan	691	1 381	-690
Jordan	116	0	116
Korea PDR	0	7	-7
Korea Rep.	25	548	-523
Lebanon	11	1 270	-1 259
Latvia	226	601	-375
Liechtenstein	37	38	-1
Lithuania	1 591	3 892	-2 301
Luxemburg	0	112	-112
Macedonia	25	34	-9
Malavi	0	138	-138
Malaysia	3	51	-48
Maroco	0	18	-18
Mauritania	0	28	-28
Mongolia	80	0	80
Mozambique	5	0	5
Norway	0	95	-95
New Zealand	0	455	-455
Newer	0	1 167	-1 167
Virjinia	20	204	-184
Philippine	20	0	20
Poland	384	1 939	-1 555
Romania	370	2 894	-2 524
Saudi Arabia	21	2	19
Singapore	21	123	-102
Slovakia	1	338	-337
Slovenia	3	4 763	-4 760
South Africa	58	12	46
Sri-Lanka	0	50	-50
Switzerland	9 032	6 073	2 959
Syria	252	222	30
Taiwan	0	174	-174
Tanzania	0	4	-4
Thailand	0	4	-4
Tonga	0	11	-11
United Arab Emirates	121	3 786	-3 665
Yugoslavia	5	237	-232
Zimbabwe	0	583	-583

Source: State Department for Statistics

Table A5.2.1: Georgia's Registred Exports and Imports by Harmonized Tariff Schedule (HTS) Chapters, H1 2001

(USD thousands)

HTS Category	Export	Import
01 - Live Animals	8	59
02 - Meat and edible meat offal	92	6623
03 - Fish and crustaceans, molluscs and other aquatic invertebrates	302	628
04 - Dairy produce; birds eggs; natural honey; edible products of animal origin, not elsewhere specified or included	14	3304
05 -Products of animal origin, not elsewhere specified or included	0	4
06 -Live trees and other plants; bulbs, roots and the like; cut flowers and ornamental foliage	7	82
07 -Edible vegetables and certain roots and tubers	293	1938
08 -Edible fruit and nuts; peel of citrus fruit or melons	5960	1326
09 -Coffee, tea, maté and spices	2721	2212
10 -Cereals	0	7133
11 -Products of the milling industry; malt; starches; inulin; wheat gluten	516	10250
12 -Oil seeds and oleaginous fruits; miscellaneous grains, seeds and fruits; industrial or medicinal plants; straw and fodder	444	118
13 -Lac; gums, resins and other vegetable saps and extracts	470	3
14 -Vegetable plaiting materials; vegetable products not elsewhere specified or included	4	8
15 -Animal or vegetable fats and oils and their cleavage products prepared edible fats; animal or vegetable waxes	31	3318
16 -Preparations of meat, of fish or of crustaceans, molluscs or other aquatic invertebrates	59	2227
17 -Sugars and sugar confectionery	1171	6683
18 -Cocoa and cocoa preparations	32	1061
19 -Preparations of cereals, flour, starch or milk; bakers' wares	93	1311
20 -Preparations of vegetables, fruit, nuts or other parts of plants	836	728
21 -Miscellaneous edible preparations	318	4096
22 -Beverages, spirits and vinegar	22193	3016
23 -Residues and waste from the food industries; prepared animal feed	8	282
24 -Tobacco and manufactured tobacco substitutes	426	10080
25 -Salt; sulfur; earths and stone; plastering materials, lime and cement	786	1500
26 -Ores, slag and ash	14840	15
27 -Mineral fuels, mineral oils and products of their distillation; bituminous substances; mineral waxes	13631	87826
28 -Inorganic chemicals; organic or inorganic compounds of precious metals, of rare earth metals, of radioactive elements or of isotopes	1978	1422
29 -Organic chemicals	71	603
30 -Pharmaceutical products	2807	21529
31 -Fertilizers	3448	53
32 -Tanning or dyeing extracts; tannins and their derivatives; dyes, pigments and other coloring matter; paints and varnishes; putty and other mastics; inks	234	955
33 -Essential oils and resinoids; perfumery, cosmetic or toilet preparations	976	3232
34 -Soap, organic surface-active agents, washing preparations, lubricating preparations, artificial waxes, prepared waxes, polishing or scouring preparations, candles and similar articles, modeling pastes, "dental waxes" and dental preparations with a basis of plaster	64	1959
35 -Albuminoidal substances; modified starches; glues; enzymes	0	297
36 -Explosives; pyrotechnic products; matches; pyrophoric alloys; certain combustible preparations	0	222
37 -Photographic or cinematographic goods	0	135
38 -Miscellaneous chemical products	59	1062
39 -Plastics and articles thereof	325	7256
40 -Rubber and articles thereof	101	1204
41 -Raw hides and skins (other than furskins) and leather	1209	573
42 -Articles of leather; saddlery and harness; travel goods, handbags and similar containers; articles of animal gut (other than silkworm gut)	1	167
43 - Furskins and artificial fur	0.3	0

Source: State Department for Statistics

Table A5.2.2: Georgia's Registred Exports and Imports by Harmonized Tariff Schedule (HTS) Chapters, H1 2001

(USD thousands)

HTS Category	Export	Import
44 -Wood and articles of wood; wood charcoal	2470	1245
45 -Cork and articles of cork	30	659
46 -Manufactures of straw, of esparto or of other plaiting materials; basketware and wickerwork	0	5
47 -Pulp of wood or of other fibrous cellulosic material; waste and scrap of paper or paperboard	0	33
48 -Paper and paperboard; articles of paper pulp, of paper or of paperboard	75	6581
49 -Printed books, newspapers, pictures and other products of the printing industry; manuscripts, typescripts and plans	340	1905
50 -Silk	0	27
51 -Wool, fine or coarse animal hair; horsehair yarn and woven fabric	15	476
52 -Cotton	0	182
53 -Other vegetable textile fibers; paper yarn and woven fabric of paper yarn	0	14
54 -Man-made filaments	7	654
55 -Man-made staple fibers	66	332
56 -Wadding, felt and nonwovens; special yarns, twine, cordage, ropes and cables and articles thereof	1	348
57 -Carpets and other textile floor coverings	5	247
58 -Special woven fabrics; tufted textile fabrics; lace, tapestries; trimmings; embroidery	1	64
59 -Impregnated, coated, covered or laminated textile fabrics; textile articles of a kind suitable for industrial use	1	135
60 -Knitted or crocheted fabrics	2	48
61 -Articles of apparel and clothing accessories, knitted or crocheted	49	1206
62 -Articles of apparel and clothing accessories, not knitted or crocheted	442	1173
63 -Other made up textile articles; sets; worn clothing and worn textile articles; rags	574	2858
64 -Footwear, gaiters and the like; parts of such articles	609	2701
65 -Headgear and parts thereof	0	23
66 -Umbrellas, sun umbrellas, walking sticks, seatsticks, whips, riding-crops and parts thereof	0	60
67 -Prepared feathers and down and articles made of feathers or of down; artificial flowers; articles of human hair	0	4
68 -Articles of stone, plaster, cement, asbestos, mica or similar materials	18	965
69 -Ceramic products	13	2156
70 -Glass and glassware	689	5355
metals, metals clad with precious metal and articles thereof; imitation jewelry; coin	62	26
72 -Iron and steel	23306	6070
73 -Articles of iron or steel	1705	13339
74 -Copper and articles thereof	3873	125
75 -Nickel and articles thereof	0	3
76 -Aluminum and articles thereof	10004	1753
78 -Lead and articles thereof	38	191
79 -Zinc and articles thereof	17	15
80 - Tin and articles thereof	_	1
81 -Other base metals; cermets; articles thereof	197	35
82 -Tools, implements, cutlery, spoons and forks, of base metal; parts thereof of base metal	256	1610
83 -Miscellaneous articles of base metal	357	1031
84 -Nuclear reactors, boilers, machinery and mechanical appliances; parts thereof	4430	34346
85 -Electrical machinery and equipment and parts thereof; sound recorders and reproducers, television image and sound recorders and reproducers, and parts and accessories of such articles	2613	31448
86 -Railway or tramway locomotives, rolling-stock and parts thereof; railway or tramway track fixtures and fittings and parts thereof; mechanical (including electro-mechanical) traffic signalling equipment	1356	1519
87 -Vehicles other than railway or tramway rolling stock, and parts and accessories thereof	1427	12650
88 -Aircraft, spacecraft, and parts thereof	14290	12660
89 -Ships, boats and floating structures	0	111
90 -Optical, photographic, cinematographic, measuring, checking, precision, medical or surgical instruments and apparatus; parts and accessories thereof	282	13823
91 -Clocks and watches and parts thereof	1	57
92 -instruments; parts and accessories of such articles	14	10
93 -Arms and ammunition; parts and accessories thereof	179	216
stuffed furnishings; lamps and lighting fittings, not elsewhere specified or included; illuminated sign illuminated nameplates and the like; prefabricated	121	6079
95 -Toys, games and sports requisites; parts and accessories thereof	44	434
96 -Miscellaneous manufactured articles	495	526
97- Works of art, collectors' pieces and antiques	79	6

Source: State Department for Statistics

Table A6.1: Establishment of JSCs by Region, as of 1st July, 2001
(Number of enterprises)

Region	Approved for privatisation	Total number of established and registered JSCs
Abkhazia	**34**	**0**
Achara	**86**	**35**
Tbilisi	**432**	**417**
Guria	**56**	**61**
Lanchkhuti	12	14
Ozurgeti	35	39
Chokhatauri	9	8
Racha-Lechkhumi and lower Svaneti	**12**	**9**
Ambrolauri	6	3
Lentekhi	2	3
Oni	1	1
Tsageri	3	2
Samegrelo and upper Svaneti	**180**	**194**
Abasha	10	9
Zugdidi	54	62
Martvili	12	12
Mestia	1	0
Senaki	27	30
Chkhorotsku	16	18
Tsalenjikha	23	24
Khobi	12	13
Poti	25	26
Imereti	**234**	**245**
Kutaisi	80	87
Tkibuli	16	12
Tskaltubo	18	17
Chiatura	17	16
Bagdati	12	12
Vani	11	10
Zestafoni	24	24
Terjola	16	14
Samtredia	17	27
Sachkhere	5	9
Kharagauli	7	6
Khoni	11	11
Kakheti	**120**	**111**
Akhmeta	13	13
Gurjaani	22	19
Dedoplistskaro	10	7
Telavi	27	28
Lagodekhi	10	10
Sagarejo	15	17
Signagi	14	12
Kvareli	9	5
Mtsketa-Tianeti	**41**	**39**
Akhalgori	1	0
Dusheti	12	8
Tianeti	2	0
Mtslheta	23	27
Kazbegi	3	4
Samtskhe-Javakheti	**54**	**47**
Adigeni	2	2
Aspindza	3	1
Akhalkalaki	8	8
Akhaltsikhe	16	15
Borjomi	24	20
Ninotsminda	1	1
Kvemo Kartli	**99**	**118**
Rustavi	33	38
Bolnisi	10	12
Gardabani	20	33
Dmanisi	6	4
Tetritskaro	11	9
Marneuli	17	20
Tsalka	2	2
Shida Kartli	**78**	**83**
Tskhinvali	0	0
Gori	36	38
Kaspi	15	16
Kareli	12	10
Khashuri	15	19
Java	0	0
Total	**1 426**	**1 359**

Source: Ministry of State Property Management
Note: This table represents in the first column enterprises approved for privatisation, and in the second those that have actually been valued and established as joint-stock companies. It does not represent enterprises actually privatised. The numbers in the second column can exceed those in the first since some enterprises are split up when being corporatised.

Table A6.2: Small Privatisation by Region, as of 1st July, 2001
(Number of enterprises)

Region	Approved for privatisation	Total privatised	Privatised in 2001	Merged with medium or large enterprises	Liquidated
Abkhazia	8	-	-	-	-
Achara	324	171		21	-
Tbilisi	4 578	4 912	113	412	-
Guria	312	430	-	3	71
Lanchkhuti	60	94		-	17
Ozurgeti	195	241		3	40
Chokhatauri	57	95	-	-	14
Racha-Lechkhumi and lower Svaneti	168	256	3	2	50
Ambrolauri	58	96	3	1	18
Lentekhi	32	47	-	-	23
Oni	47	55	-	1	9
Tsageri	31	58		-	-
Samegrelo and upper Svaneti	1 103	1 483	7	184	278
Abasha	86	91	-	3	13
Zugdidi	211	274	-	7	-
Martvili	53	51	-	2	19
Mestia	12	23	-	3	3
Senaki	249	430	-	140	104
Chkhorotsku	39	58	2	-	23
Tsalenjikha	51	64	1	15	15
Khobi	145	136		2	59
Poti	257	356	4	12	42
Imereti	2 669	3 010	37	187	582
Kutaisi	608	781	7	71	211
Tkibuli	223	197	5	-	49
Tskaltubo	268	306	6	10	29
Chiatura	239	302	5	68	44
Bagdati	69	110	1	-	36
Vani	68	101	2	1	17
Zestafoni	410	385	7	12	52
Terjola	132	148	-	-	20
Samtredia	429	430	-	19	59
Sachkhere	94	78	-	-	16
Kharagauli	65	73	4	5	14
Khoni	64	99	-	1	35
Kakheti	1 076	1 254	11	71	182
Akhmeta	178	176	-	18	28
Gurjaani	136	153	-	13	19
Dedoplistskaro	87	107	2	34	3
Telavi	215	263	7	3	36
Lagodekhi	71	74	2	-	15
Sagarejo	128	124	-	3	10
Signagi	137	214	-	-	34
Kvareli	124	143	-	-	37
Mtsketa-Tianeti	315	365	-	21	71
Akhalgori	17	18	-	-	5
Dusheti	87	111	-	1	12
Tianeti	57	58	-	8	12
Mtslheta	128	149	-	12	42
Kazbegi	26	29	-	-	-
Samtskhe-Javakheti	582	888	19	9	95
Adigeni	80	100	5	-	5
Aspindza	30	47	-	1	-
Akhalkalaki	56	80	-	1	10
Akhaltsikhe	242	365	3	7	56
Borjomi	148	261	11	-	20
Ninotsminda	26	35	-	-	4
Kvemo Kartli	1 132	1 536	43	20	154
Rustavi	354	451	6	4	60
Bolnisi	61	132	2	6	-
Gardabani	267	282	10	-	36
Dmanisi	20	70	-	-	7
Tetritskaro	112	226	9	4	17
Marneuli	284	337	15	6	10
Tsalka	34	38	1	-	24
Shida Kartli	878	954	3	47	161
Tskhinvali	-	5	-	5	-
Gori	310	355	-	19	52
Kaspi	197	159	-	-	15
Kareli	139	171	-	-	62
Khashuri	232	264	3	23	32
Java	-	-	-	-	-
MSPM	421	421	26	-	-
Total	**13 566**	**15 680**	**262**	**977**	**1 644**

Source: Ministry of State Property Management

Note: Number of enterprises actually privatised can exceed those approved for privatisation since some are split up during corporatisation.

Table A7.1: Economic Status, Q 1 1998 - Q1 2001

(Thousends)

	Q I 1998	Q II 1998	Q III 1998	Q IV 1998	Q I 1999	Q II 1999	Q III 1999	Q IV 1999	Q I 2000	Q II 2000	Q III 2000	Q IV 2000	Q I 2001
Total population over 15 years old	**3, 099**	**3, 136**	**3, 194**	**3, 008**	**3, 032**	**3, 049**	**3, 092**	**3, 018**	**3, 123**	**3, 151**	**3, 133**	**3, 199**	**3, 277**
Total economically active population (labour force) (1)	**2 ,332**	**2, 462**	**2,146**	**1,990**	**2, 018**	**2, 052**	**2, 058**	**1, 917**	**1, 951**	**2, 102**	**2, 064**	**2, 095**	**2, 066**
Total economically active population (labour force) (2)	**2 ,457**	**2 ,555**	**2,195**	**2,042**	**2, 058**	**2, 093**	**2, 106**	**1, 975**	**2, 087**	**2, 199**	**2, 181**	**2, 215**	**2, 195**
Employed	***2, 101***	***2 ,283***	***1,887***	***1,741***	***1, 725***	***1, 784***	***1, 792***	***1, 633***	***1, 705***	***1, 890***	***1, 890***	***1, 878***	***1, 818***
Hired	714	737	786	741	737	743	741	710	679	695	675	691	681
Self-employed	1, 387	1 ,546	1,092	990	973	1, 023	1, 030	905	912	1, 087	1, 095	1, 080	1, 034
Unemployed (1)	***231***	***179***	***260***	***249***	**292**	**268**	**266**	**284**	**246**	**212**	**174**	**217**	**248**
Unemployed (2)	***356***	***272***	***309***	***301***	**333**	**308**	**314**	**342**	**382**	**309**	**292**	**337**	**377**
Unemployment rate (per cent) (1)	**9,9**	**7,3**	**12,1**	**12,5**	**14.5**	**13,0**	**12,9**	**14,8**	**12,6**	**10,1**	**8,4**	**10,4**	**12,0**
Unemployment rate (per cent) (2)	**14,5**	**10,6**	**14,1**	**14,7**	16.2	**14,7**	**14,9**	**17,3**	**18,3**	**14,0**	**13,4**	**15,2**	**17,2**
Labour force participation rate	***75,3***	***78,5***	***67,2***	***66,2***	***66,6***	***67,3***	***66,6***	***63,5***	***62,5***	***63,9***	***65,9***	***65,5***	***63,1***
Self-employment share in total labour force	*59.5*	*62.8*	*50.9*	*49,7*	*48,2*	*49,8*	*50,1*	*47,2*	*46,7*	*51,7*	*53,0*	*51,6*	*50,1*
Self-employment share in total employment	*66.0*	*67.7*	*57.8*	*56,9*	*56,4*	*57,3*	*57,5*	*55,4*	*53,5*	*57,5*	*57,9*	*57,5*	*56,9*

Source: The State Department for Statistics, Labour Force Survey, Household Survey

Note: (1) ILO Standard (or “strict” methodology)

(2) ILO “Loose” Methodology

ABBREVIATIONS

ACDI	Agricultural Co-operative Development International
BSEC	Black Sea Economic Co-operation
CASE	Centre for Social and Economic Research
CIS	Commonwealth of Independent States
CPI	Consumer Price Index
DMB	Deposit Money Bank (Commercial Bank)
EBRD	European Bank for Reconstruction and Development
ECU	European Currency Unit
ESAF	IMF Enhanced Structural Adjustment Facility
EU	European Union
EUR	Euro
FAO	Food and Agricultural Organisation
FDI	Foreign Direct Investment
FSU	Former Soviet Union
FXB	Foreign Exchange Bureau (x)
GATS	General Agreement on Trade in Services
GATT	General Agreement on Tariffs and Trade
GCT	General Customs Tariff
GDP	Gross Domestic Product
GEL	Georgian Lari
GEPA	Georgian Export Promotion Agency
GEPLAC	Georgian-European Policy and Legal Advice Centre
GET	Georgian Economic Trends
GNP	Gross National Product
GSP	General System of Preferences
H	Half year
ha	hectares
HS	Harmonised Commodity Description
HTS	Harmonised Tariff Schedule
IDP	Internally Displaced Person
ILO	International Labour Organisation
IMF	International Monetary Fund
IFAD	International Fund for Agricultural Development
ISIC	International Standard Industrial Classification
JPY	Japanese Yen
JSC	Joint Stock Company
KWh	Kilowatt hour
LFS	Labour Force Survey
LIBOR	London Inter-bank Offered Rate
MFA	Multi-fiber Agreement
MFN	Most Favoured Nations status
MoF	Ministry of Finance
MoHSS	Ministry of Healthcare and Social Safety
MoLSA	Ministry of Labour and Social Affairs
MSPM	Ministry of State Property Management
MWh	Megawatt hour
NBG	National Bank of Georgia
NDA	Net Domestic Assets
NFA	Net Foreign Assets

NMP	Net Material Product
NTR	Normal Trade Relations
OECD	Organisation for Economic Co-operation and Development
PAYG	Pay-as-you-go pension system
PCA	Partnership and Co-operation Agreement
PPI	Producer Price Index
PRGF	Poverty Reduction and Growth Facility (IMF)
PSI	Pre-shipment inspection
Q	Quarter year
RM	Reserve Money
RUR	Russian Ruble
SAC	World Bank Structural Adjustment Credit
SCD	State Customs Department
SDR	Special Drawing Rights
SDS	State Department for Statistics
SIS	State Institute of Statistics of Turkey
STI	State Tax Inspectorate
TBT	Technical Barriers on Trade agreement
TICEX	Tbilisi Interbank Currency Exchange
TRACECA	Transport Corridor Europe-Caucasia-Asia
TRIMs	Trade-Related Investment Measures
TRIPS	Intellectual Property Rights
TRL	Turkish Lira
UNDP	United Nations Development Program
USAID	United States Agency for International Development
USD	United States Dollar
USITC	United States International Trade Commission
USSSF	United State Social Safety Fund
USTR	United States Trade Representative
VAT	Value Added Tax
WTO	World Trade Organisation