

How Rosy Are Real Prospects of Georgia's Economy?!

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First Years of Transition

- Georgia restored independence 1991
- Political turmoil (Military coup, armed conflicts, secessionist moves supported by Russia)
- Price Liberalization, output decline, hyperinflation, high budget deficits, tax collection collapsed (2.3% to GDP in 1993), decline in the standard of living
- An energy crisis, permanent shortages in electricity supply and heating
- High degree of corruption

First Reforms of 1995-1998

- Macroeconomic stabilization (low inflation, stable exchange rate, two tier banking reform)
- Currency reform – introduction of Georgian Lari, national currency
- Reduced trade barriers
- Privatization (Mass Voucher Privatization), establishment property rights
- Created new legislation for market economy

Non reform years 1999 -2003

- Relevant macroeconomic stability
- Low tax revenues
- High level of corruption
- Now substantial reforms in Energy sector, health and education

First reform years of 2004 -2006

“Rose Revolution”

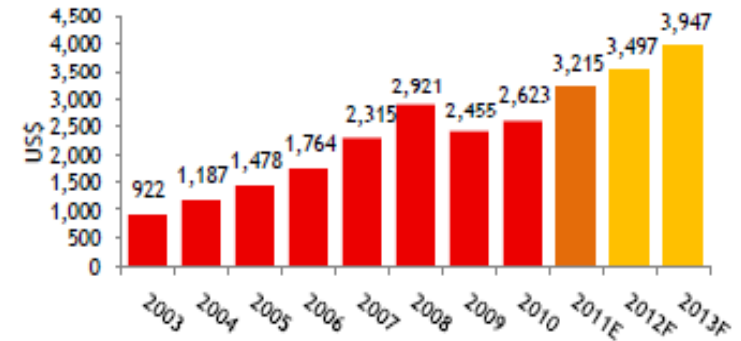
- An effective fight against corruption.
- The abolition of the old soviet traffic police and the creation of a western-style patrol police.
- The combat of corruption in the energy sector resulted in the overcoming of the energy crisis
- A fourfold growth of the national budget revenues.
- Reducing the number of licenses and permits.
- Reducing number of taxes from 21 to 6 and cutting tax rates

GDP



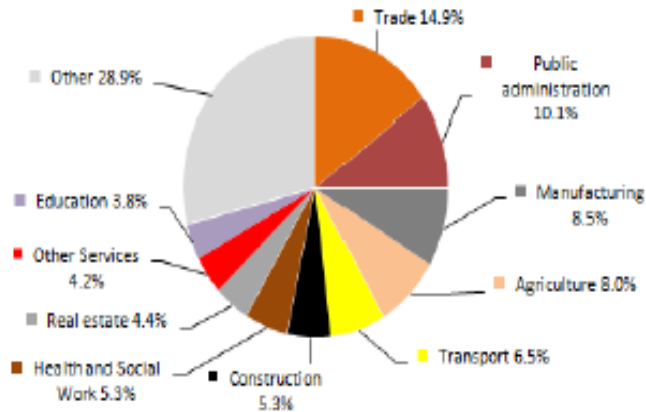
Source: National Statistics Office of Georgia-GeoStat, Ministry of Finance of Georgia

GDP Per Capita



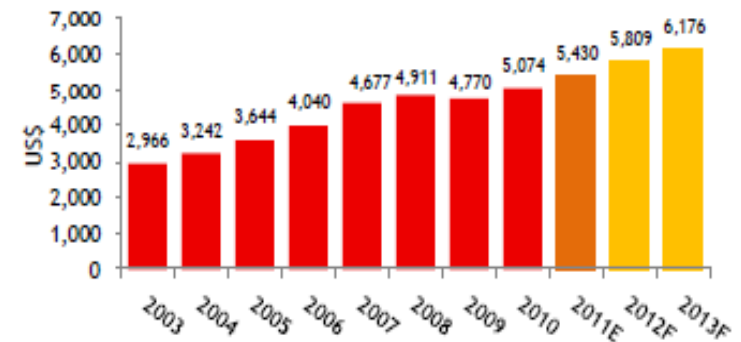
Source: National Statistics Office of Georgia-GeoStat, Ministry of Finance of Georgia

Components of GDP 2011E



Source: National Statistics Office of Georgia-GeoStat, Ministry of Finance of Georgia

GDP Per Capita PPP



Source: IMF

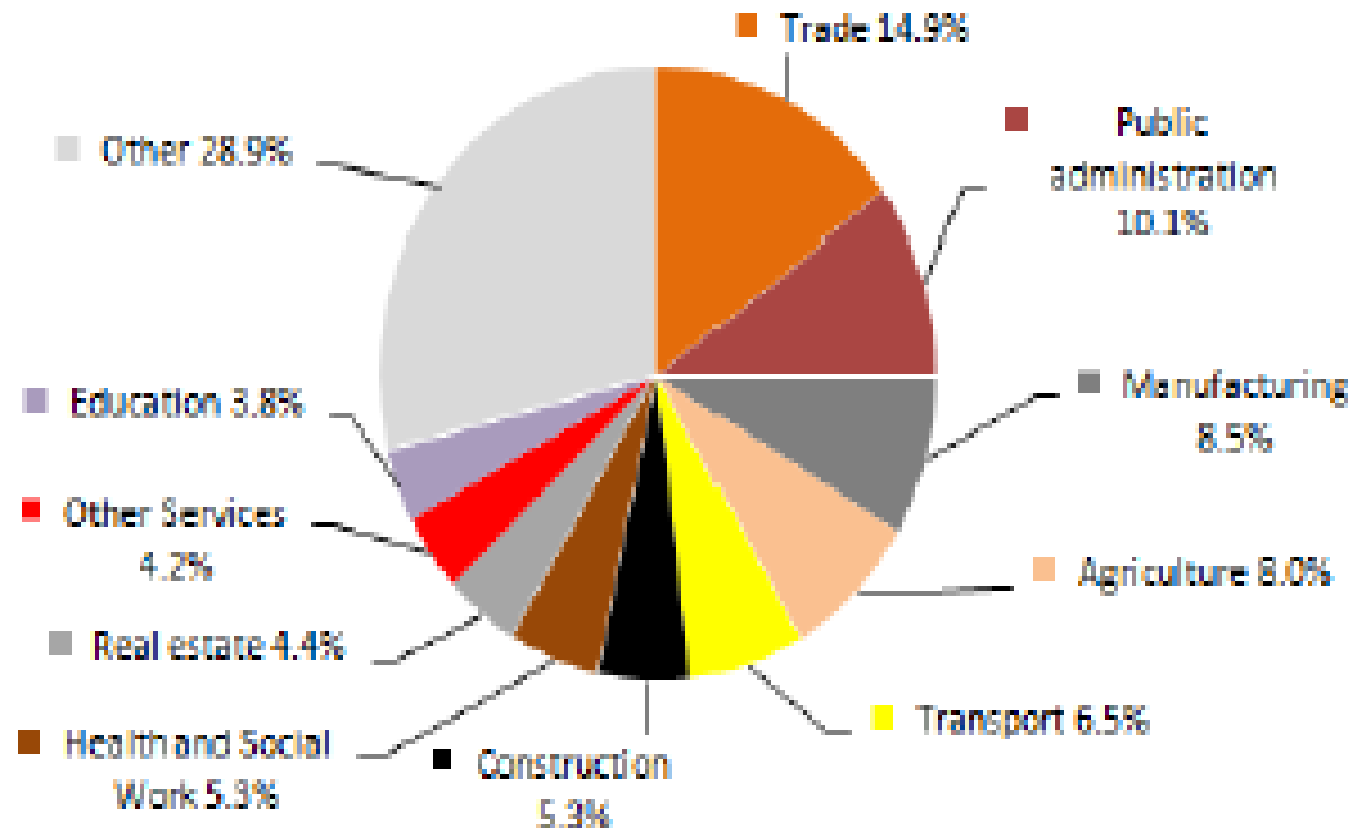
Table A.2 GDP (percentage change in real terms)

																					GDP level as percent of 1989 ^a		
	1989	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2008	2009
Albania	9.8	-10.0	-28.0	-7.2	9.6	8.3	13.3	9.1	-10.9	8.6	13.2	6.5	7.1	4.2	5.8	5.7	5.7	5.5	6.0	7.0	2.8	163	168
Armenia	14.2	-7.4	-11.7	-41.8	-8.8	5.4	6.9	5.9	3.3	7.3	3.3	5.9	9.6	13.2	13.9	10.1	14.0	13.2	13.8	6.8	-14.2	153	131
Azerbaijan	14.2	-7.4	-11.7	-41.8	-8.8	5.4	6.9	5.9	3.3	7.3	3.3	5.9	9.6	13.2	13.9	10.1	14.0	13.2	23.4	10.9	9.3	177	193
Belarus	8.0	-3.0	-1.2	-9.6	-7.6	-11.7	-10.4	2.8	11.4	8.4	3.3	5.8	4.7	5.0	7.0	11.4	9.4	9.9	8.2	10.0	0.2	161	161
Bosnia-Herzegovina		-23.2	-12.1	-50.0	-60.0	0.0	20.8	86.0	37.0	15.6	9.6	5.5	4.3	5.5	3.0	6.3	3.9	6.7	6.8	5.4	-3.4	84	81
Bulgaria	0.5	-9.1	-11.7	-7.3	-1.5	1.8	2.9	-9.4	-5.6	4.0	2.3	5.4	4.1	4.5	5.0	6.6	6.2	6.3	6.2	6.0	-5.0	114	108
Croatia	-1.6	-7.1	-21.1	-11.7	-8.0	5.9	6.8	5.9	6.8	2.5	-0.9	2.9	4.4	5.6	5.3	4.3	4.3	4.8	5.5	2.4	-5.8	111	105
Czech Republic	1.4	-1.2	-11.6	-0.5	0.1	2.2	5.9	4.2	-0.7	-0.8	1.3	3.6	2.5	1.9	3.6	4.5	6.3	6.8	6.1	2.5	-4.2	142	136
Estonia	8.1	-6.5	-13.6	-14.2	-8.8	-1.6	5.0	5.0	10.8	5.4	-0.1	9.6	7.7	7.8	7.1	7.5	9.2	10.4	7.2	-3.6	-14.1	147	126
Georgia	-4.8	-12.4	-20.6	-44.8	-25.4	-11.4	2.4	10.5	10.6	2.9	3.0	1.9	4.7	5.5	11.1	5.9	9.6	9.4	12.4	2.1	-3.9	61	59
Hungary	0.7	-3.5	-11.9	-3.1	-0.6	2.9	1.5	1.3	4.6	4.8	4.2	5.2	4.1	4.1	4.2	4.8	4.0	4.1	1.2	0.6	-6.3	136	127
Kazakhstan	-0.4	-0.4	-11.0	-5.3	-9.2	-12.6	-8.2	0.5	1.7	-1.9	2.7	9.8	13.5	9.8	9.3	9.6	9.7	10.7	8.9	3.2	1.2	141	143
Kyrgyzstan	2.8	5.7	-7.9	-13.9	-15.5	-20.1	-5.4	7.1	9.9	2.1	3.7	5.4	5.3	0.0	7.0	7.0	-0.2	3.1	8.2	7.6	2.3	102	104
Latvia	6.8	2.9	-10.4	-34.9	-14.9	2.2	-0.9	3.9	8.4	4.7	3.3	6.9	8.0	6.5	7.2	8.7	10.6	12.2	10.0	-4.6	-18.0	118	97
Lithuania	1.5	-5.0	-5.7	-21.3	-16.2	-9.8	1.2	5.1	8.5	7.5	-1.5	4.1	6.6	6.9	10.3	7.3	7.9	7.7	9.8	2.8	-15.2	120	102
Macedonia, FYR	0.9	-9.9	-6.2	-6.6	-7.5	-1.8	-1.1	1.2	1.4	3.4	4.3	4.5	-4.5	0.9	2.8	4.1	4.1	3.7	5.9	4.8	-0.7	102	101
Moldova	8.5	-2.4	-17.5	-29.1	-1.2	-30.9	-1.4	-5.9	1.6	-6.5	-3.4	2.1	6.1	7.8	6.6	7.4	7.5	4.8	3.0	7.2	-6.7	55	51
Mongolia	4.2	-2.5	-9.2	-9.5	-2.9	2.3	6.3	2.4	4.0	3.5	3.2	1.1	1.0	4.0	5.9	10.1	7.3	8.6	10.2	8.9	-1.6	167	164
Montenegro	1.3	-7.9	-10.8	-21.0	-24.9	0.7	6.2	13.9	4.2	4.0	-6.7	3.1	1.1	1.9	2.5	4.4	4.2	8.6	10.7	7.0	-5.3	92	87
Poland	0.2	-11.6	-7.0	2.6	3.8	5.2	7.1	3.9	-6.1	-4.8	-1.1	2.1	5.7	5.1	5.2	8.5	4.2	7.9	6.0	7.1	-7.1	128	119
Romania	-5.8	-5.7	-12.9	-8.8	1.5	3.9	7.1	3.9	-6.1	-4.8	-1.1	2.1	5.7	5.1	5.2	8.5	4.2	7.9	6.0	7.1	-7.1	128	119
Russia	1.6	-3.0	-5.0	-14.8	-8.7	-12.7	-4.0	-3.6	1.4	-5.3	6.4	10.0	5.1	4.7	7.3	7.1	6.4	7.4	8.1	5.6	-7.9	108	99
Serbia	1.3	-7.9	-11.6	-27.9	-30.8	2.5	6.1	7.8	10.1	1.9	-18.0	5.2	5.1	4.5	2.4	9.3	6.3	5.5	6.9	5.5	-3.0	72	70
Slovakia	1.4	-0.4	-15.9	-6.7	-3.7	6.2	5.8	6.1	4.6	4.2	1.5	2.0	3.4	4.8	4.8	5.2	6.6	8.5	10.4	6.2	-4.7	164	156
Slovenia	1.8	-7.5	-8.9	-5.5	2.8	5.3	4.1	3.7	4.8	3.9	5.4	4.1	3.1	4.0	2.8	4.3	4.3	5.9	6.8	3.5	-7.8	156	144
Tajikistan	3.0	-32.6	-7.1	-28.9	-11.1	-21.4	-12.5	-4.4	1.7	5.3	3.7	8.3	10.2	9.1	10.2	10.6	6.7	7.0	7.8	7.9	3.4	61	63
Turkmenistan	-6.9	2.0	-4.7	-5.3	-10.0	-17.3	-7.2	-6.7	-11.3	6.7	16.5	18.6	20.4	15.8	17.1	14.7	13.0	11.4	11.6	10.5	6.0	226	240
Ukraine	4.0	-4.0	-10.6	-9.7	-14.2	-22.9	-12.2	-10.0	-3.0	-1.9	-0.2	5.9	9.2	5.2	9.6	12.1	2.7	7.3	7.9	2.2	-15.1	70	59
Uzbekistan	3.7	1.6	-0.5	-11.1	-2.3	-4.2	-0.9	1.6	2.5	4.3	4.3	3.8	4.1	4.0	4.2	7.7	7.0	7.3	9.5	9.0	7.0	163	174

Source: EBRD economic statistics and forecasts, available at <http://www.ebrd.com/country/sector/econo/stats/index.htm>, EBRD (2010), Eurostat figures for the Czech Republic from 2008, available at <http://ec.europa.eu/eurostat>

^a Calculated from the annual percentage changes.

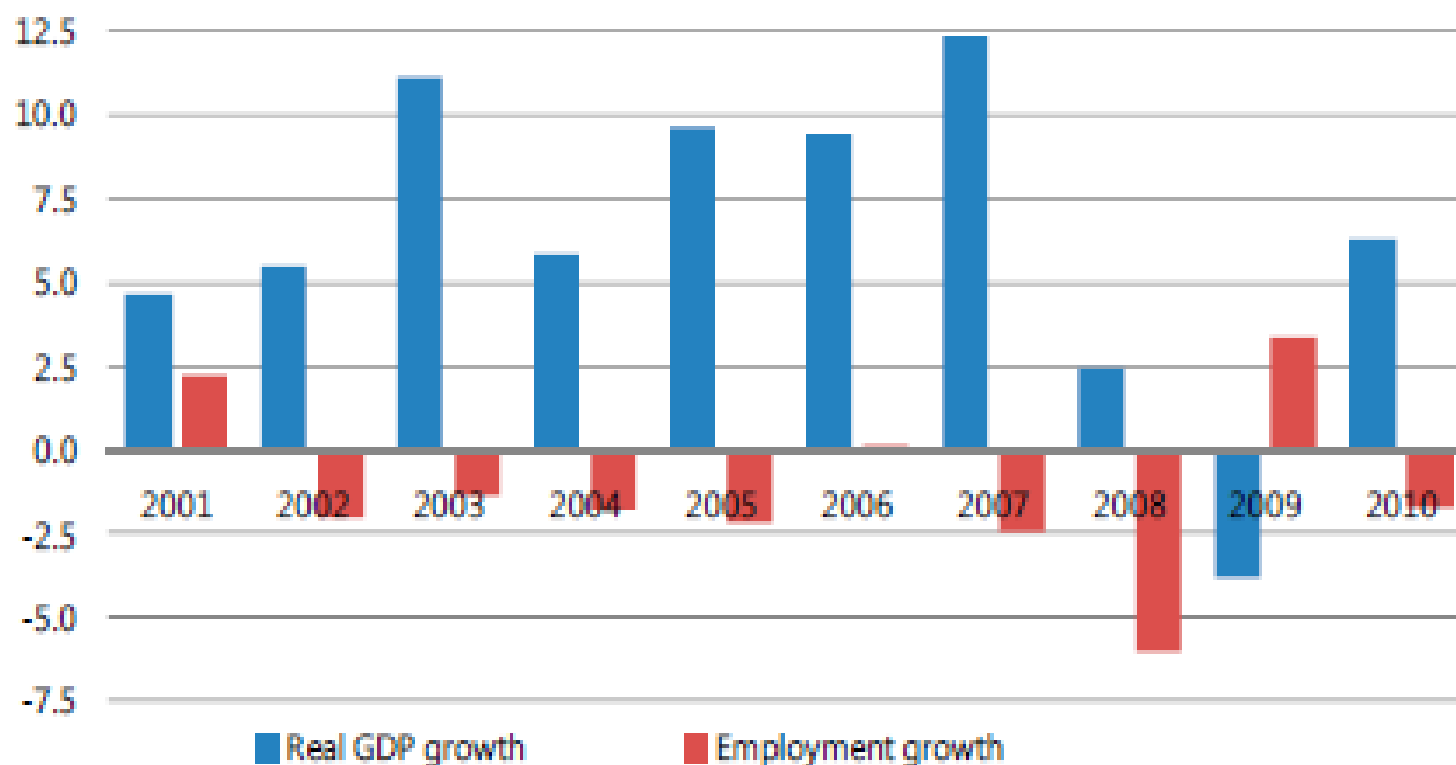
Components of GDP 2011E



Source: National Statistics Office of Georgia-GeoStat, Ministry of Finance of Georgia

Real GDP and Employment Growth, 2001-10

(In percent)

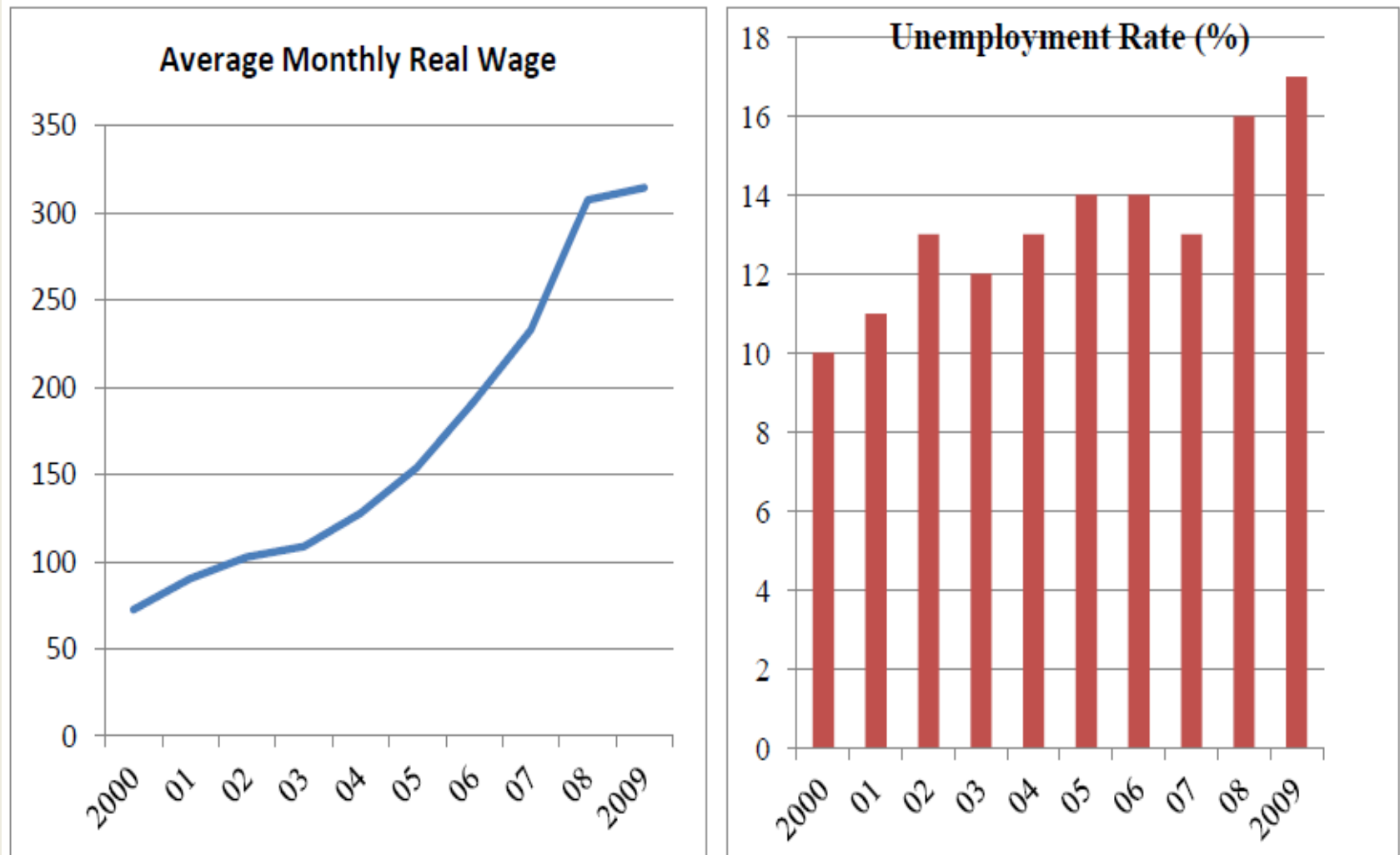


Sources: Georgian authorities; and Fund staff estimates.

Economic Growth and Unemployment

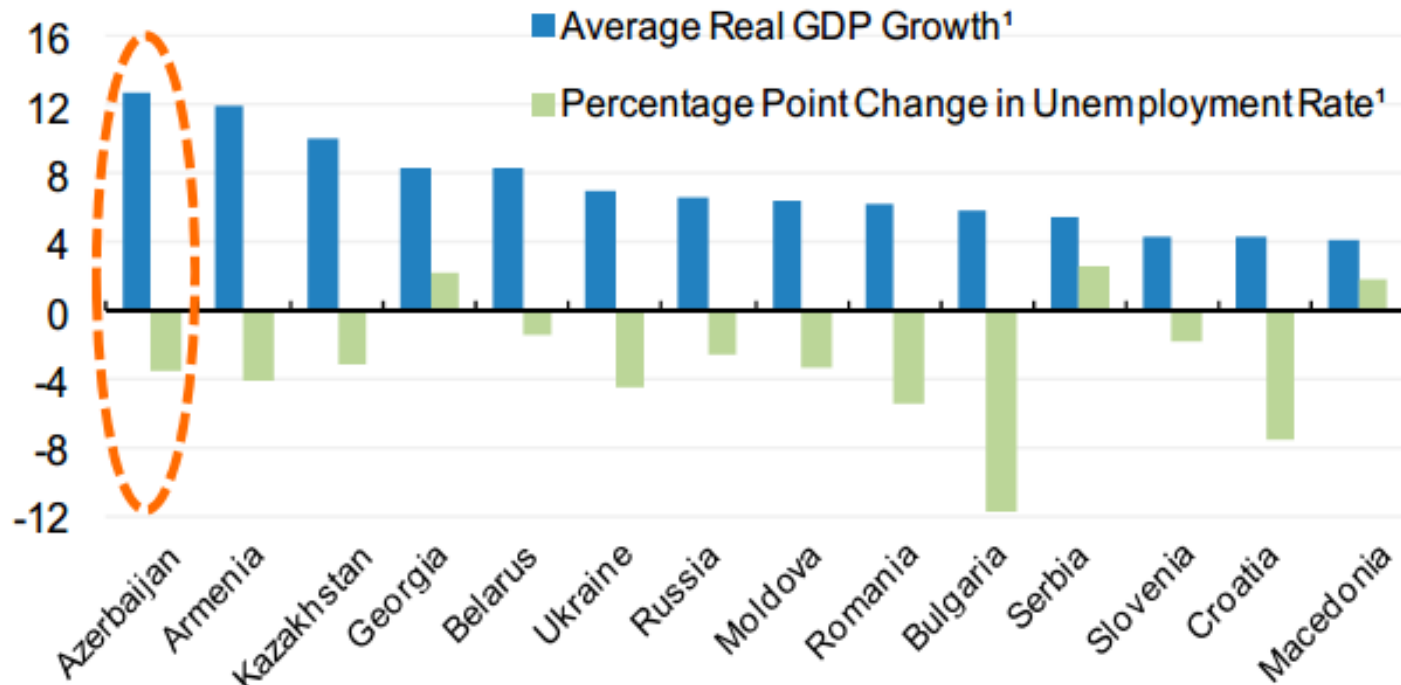
- Economic growth in Georgia was not accompanied by sufficient job creation; this may largely explain lack of a adequate reduction in poverty.
- Labor market characteristic variables—such as the unemployment rate—worsened, rather than improved, during the growth years.
- On the other hand, there was a substantial increase in wages for those who were employed.

Figure 7: Average Nominal Wage and Employment Rate



Source: Georgia Statistical Office 2010

Economic Growth and Unemployment Change During the Economic Boom



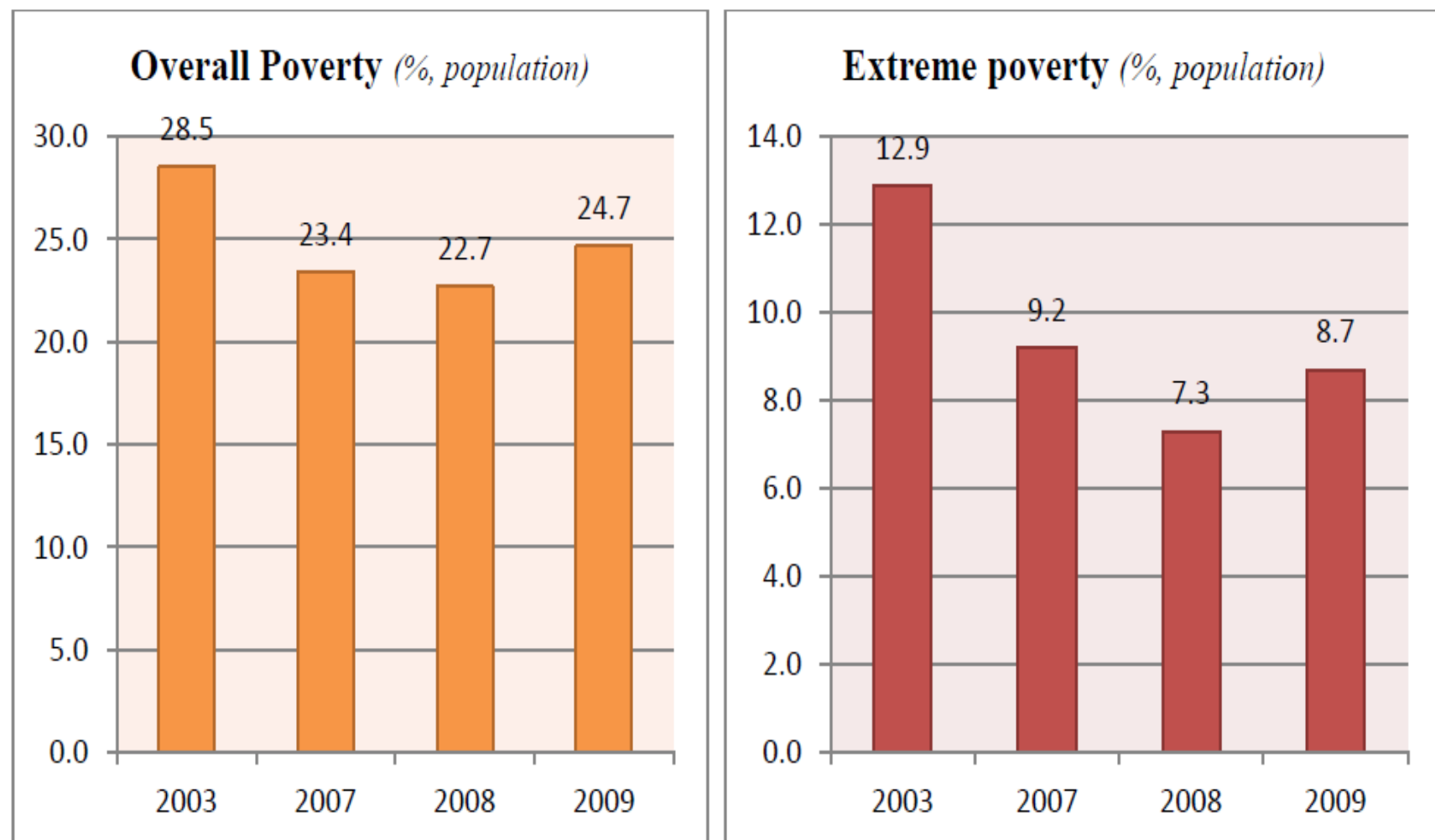
Sources: IMF, *World Economic Outlook*.

¹ Shock year is the year after 2001 when real GDP growth drops most sharply. It is 2008 for Georgia and Kazakhstan, and 2009 for others. Non-oil GDP is used for Azerbaijan and Kazakhstan. Average over 2001 through the year before the shock is used for GDP growth; the change in unemployment refers to the difference between 2001 and the year before the shock.

The World Bank: Georgia Poverty Dynamics 2003 – 2012

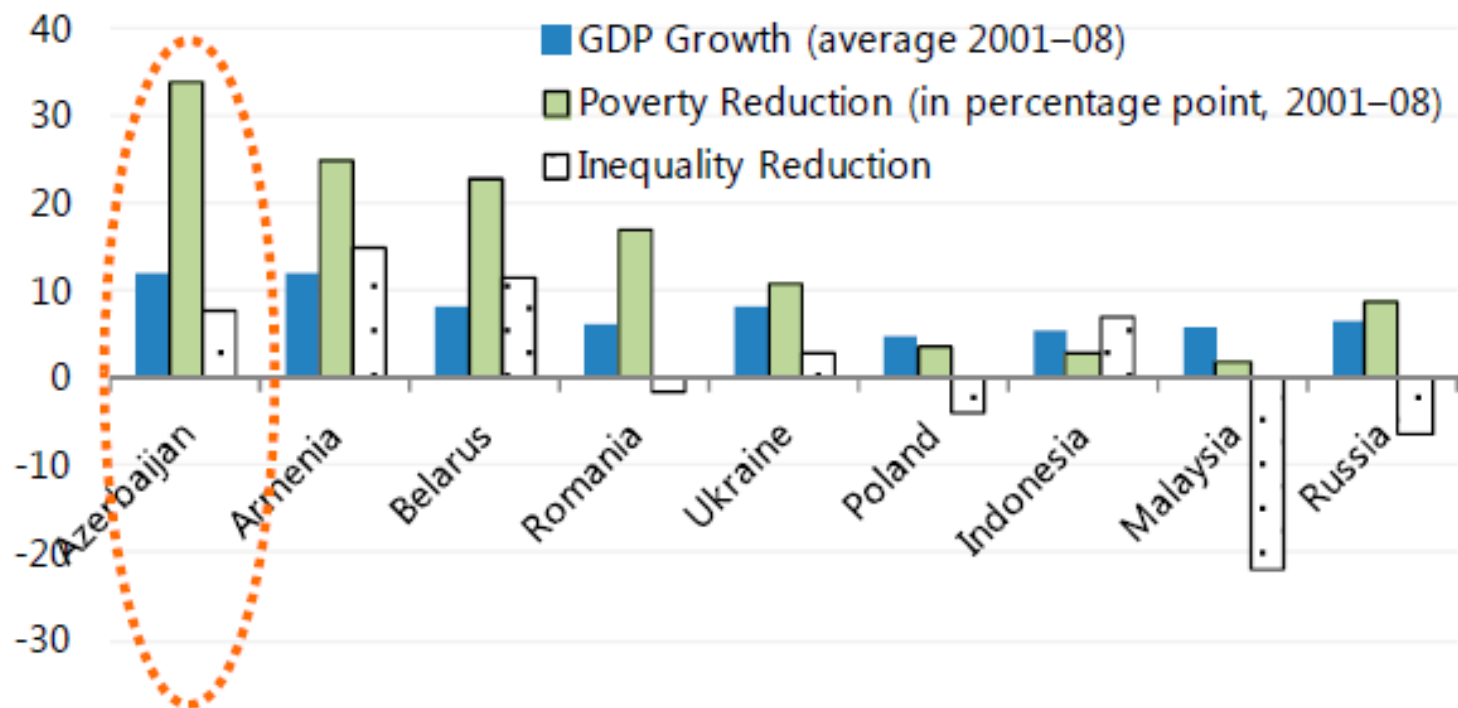
- The gap between urban and rural areas in Georgia has widened since the Rose Revolution.
- About 64% of Georgia's poor now live in rural areas, despite accounting for less than half of the total population.
- Overall poverty increased from an estimated 22.7% in 2008 to 24.7% in 2009. This was a much faster rate of poverty increase than its rates of decrease during the 2003-2007 episode of growth.

Figure 4: Poverty Headcount in Georgia during the 2000s.



Source: Calculations based on 2007 LSMS, 2003 IHS, and 2008-2009 IHS.

Poverty, Inequality Reduction and GDP Growth 1/ 2/

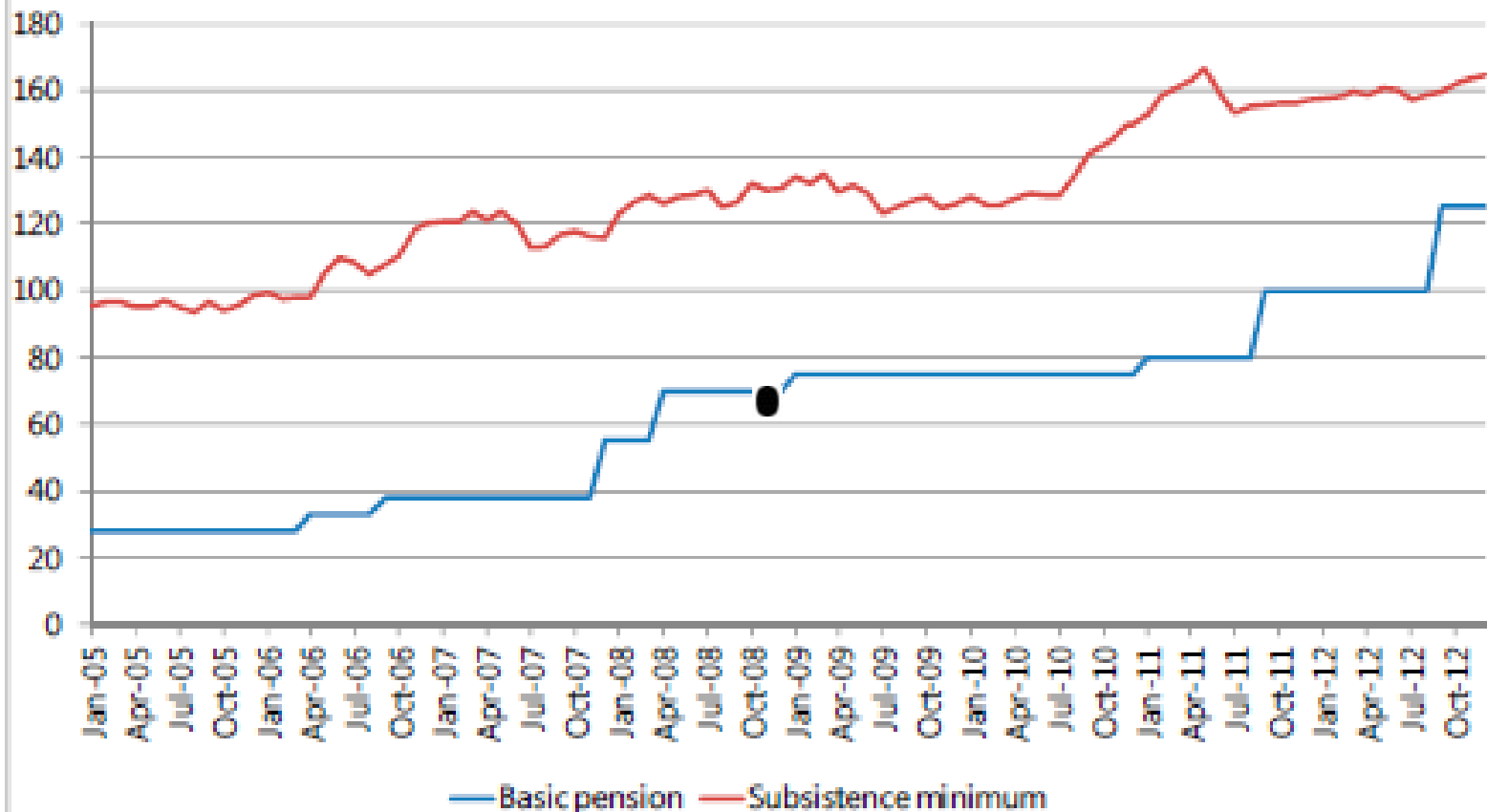


Sources: World Development Indicators and national authorities' data.

1/ Non-oil growth is used for Azerbaijan. Poverty reduction is the drop in the poverty rate, from 2001 to 2008 or closest year available. For Poland, the poverty-at-risk rate in 2005 and 2009 are used. GDP growth is the average over the corresponding period.
 2/ Inequality reduction is the Gini coefficient drop from 2001 to 2008 (in percent of base year). 2002 and 2008 data are used for Ukraine; 2005 and 2009 for Indonesia and Malaysia.

Georgia: Basic Pension and Subsistence Minimum, 2005–12

(In lari per month)



Sources: GEOSTAT; and Fund staff estimates.

	'04A	'05A	'06A	'07A	'08A	'09A	'10A	'11F	'12F	'13F	'14F
Number of Taxes	21	7	7	7	6	6	6	6	6	6	6
VAT	20%	20%	18%	18%	18%	18%	18%	18%	18%	18%	18%
Income Tax	12-20%	12% flat	12% flat	12% flat	Social Tax + Income Tax 32% → 25%	Social Tax + Income Tax → 20%	20%	20%	20%	18%	15%
Social Tax	33%	20%	20%	20%	-	-	-	-	-	-	-
Corporate Profit Tax	20%	20%	20%	20%	15%	15%	15%	15%	15%	15%	15%
Dividend & Interest Income Tax	10%	10%	10%	10%	10%	5%	5%	5%	5%	3%	0%

■ No payroll tax or social insurance tax

■ No capital gains tax

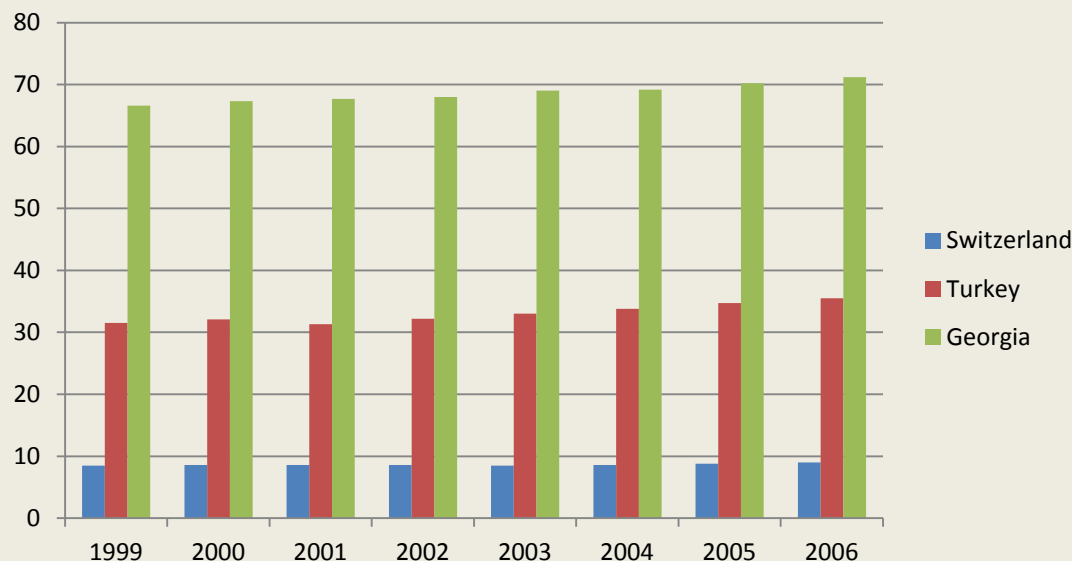
■ No wealth tax, inheritance tax or stamp duty

■ Foreign-source income of individuals fully exempted

■ Tax rates reduction timetable has been further accelerated in 2008

SHADOW ECONOMIES ALL OVER THE WORLD

New Estimates for 162 Countries from 1999 to 2007



- The countries with the smallest shadow economy are now Switzerland, the United States, and Luxembourg with an average value over the period 1999 to 2006 of 8.6, 8.8, and 9.8%.
- In the middle we find Namibia, Venezuela, and Turkey with an average shadow economy size over 1999 to 2006 of 32.2, 32.6, and 33.0%.
- The three countries with the highest shadow economy are now Peru, Bolivia, and Georgia with an average value over the period 1999 to 2006 of 61.5, 67.8, and 68.7%.



Non-Reform years of 2007-2012

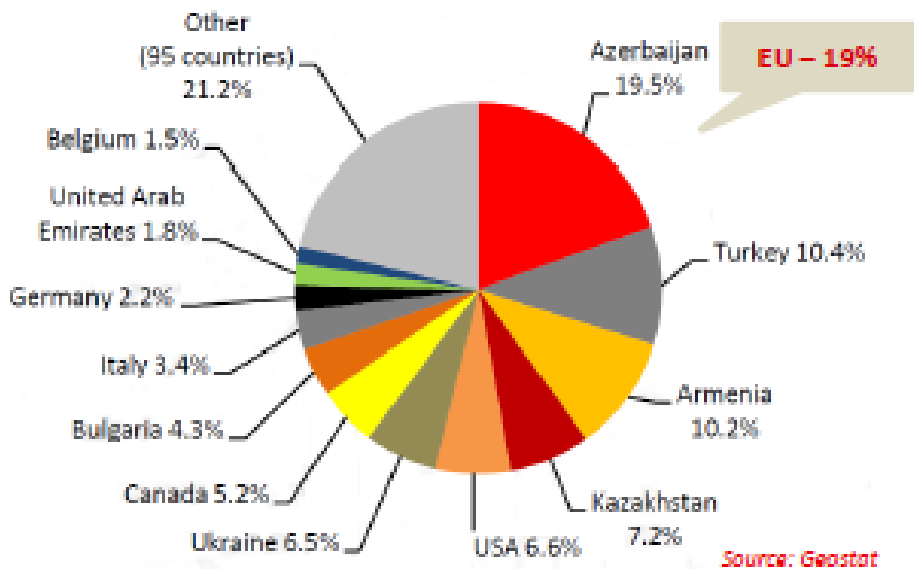
Results of Wrong Economic Policy during 2007-2011

- Higher Poverty - over 1.8 million persons live at or below poverty level
- Higher Unemployment: in Tbilisi – over 30%; In Georgia more than 40% (Official statistics show unemployment at only 17%)
- Foreign debt has doubled in over 2009 -2011. Now over \$4 B USD
- Trade deficit : Imports 7 B USD is 3,3 times higher than export at \$2.1 B USD
- Drastic decline of foreign investments from \$2B (2007) to \$0.6 B in 2009, 0.8 in 2010 and \$0.9 B in 2011.

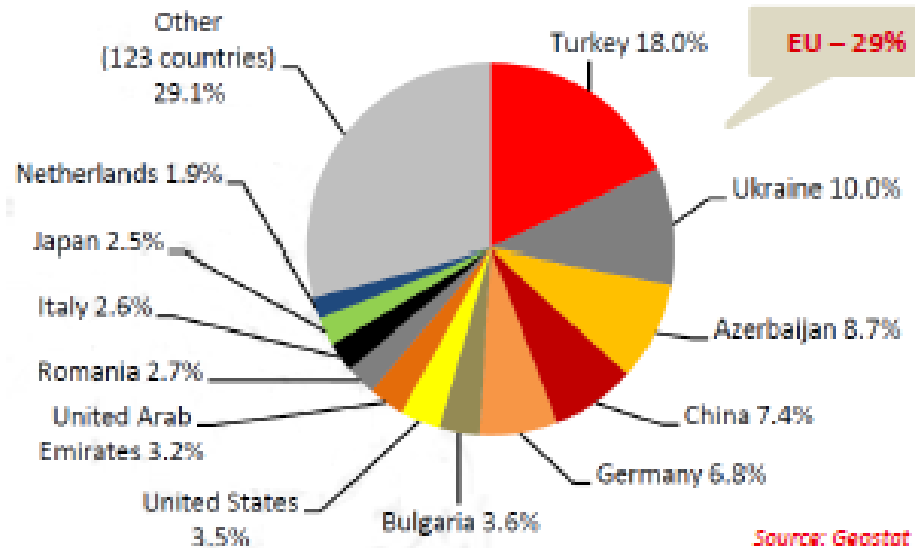
False Liberal Economic Policy

- Absence of anti-monopolistic legislation and regulations
- Limited free market competition with emerging monopolists and cartel pricing: energy, advertising, state lottery, precious metals retailing, Gulf oil franchise, entertainment
 - Only 5 companies import fuel to Georgia today
 - Before 2005 there were than 100
 - The Anti-Monopoly Committee that once regulated costs has been disbanded
 - Georgian drivers pay more than \$.18 equivalent per liter more than reasonable cost
 - Average liter costs \$1.39 equivalent, whereas in Armenia the average cost is equivalent to \$1.14 yet the same fuel must cross Georgia
- Food safety regulations
- Violation of property rights
- Authoritarian governance and weak institutions : weak accountability to public and media, political nepotism, budget spending not transparent
- Privatization is not-transparent
- Elite corruption

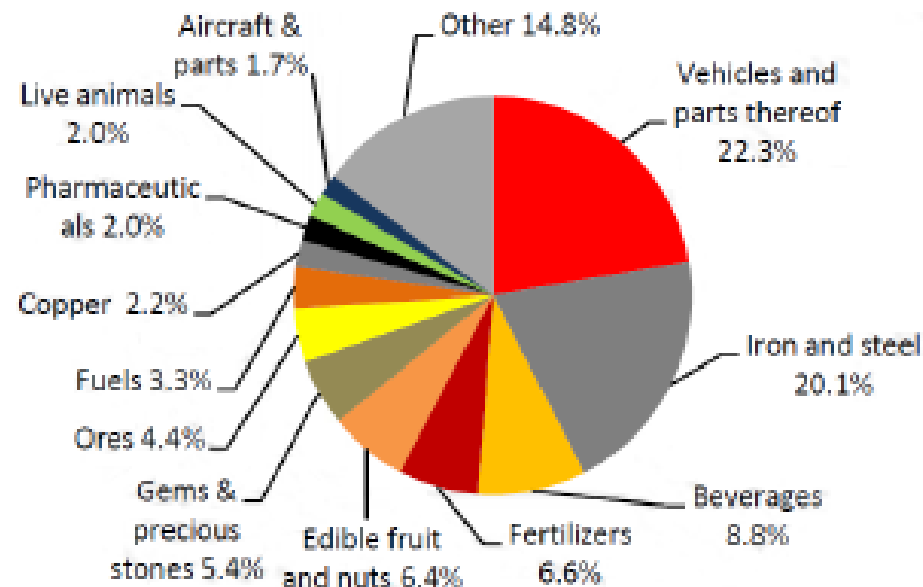
Export Structure by Country 2011



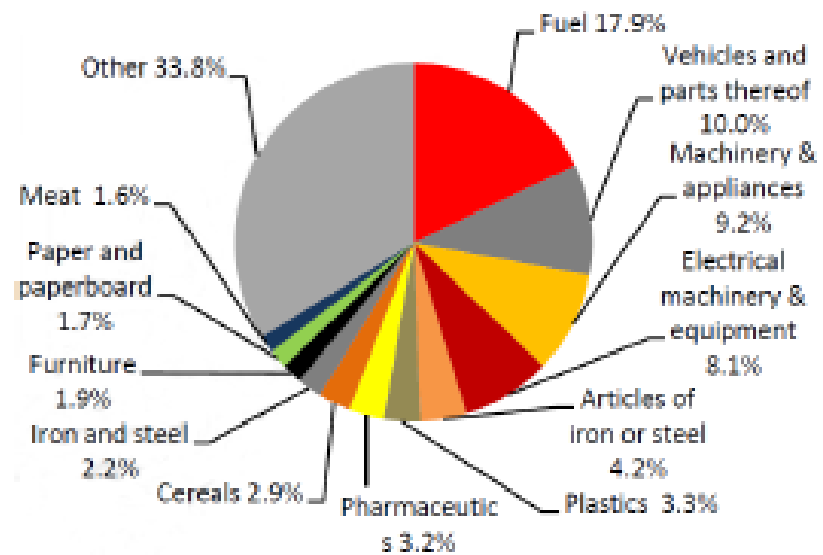
Import Structure by Country 2011



Export Structure by Product 2011



Import Structure by Product 2011



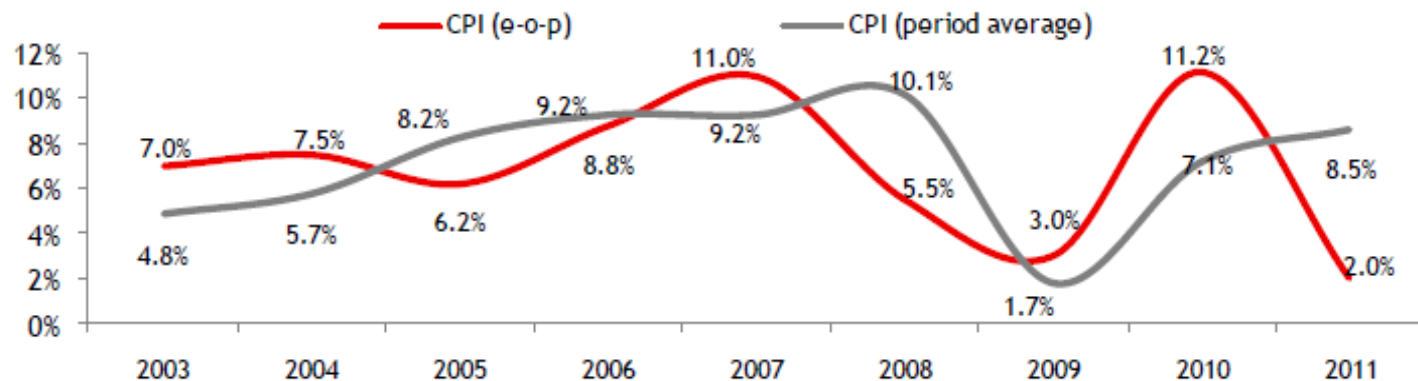
Fiscal and Monetary Performance

Conventional Fiscal Deficit (Cash Basis)



Source: Ministry of Finance of Georgia

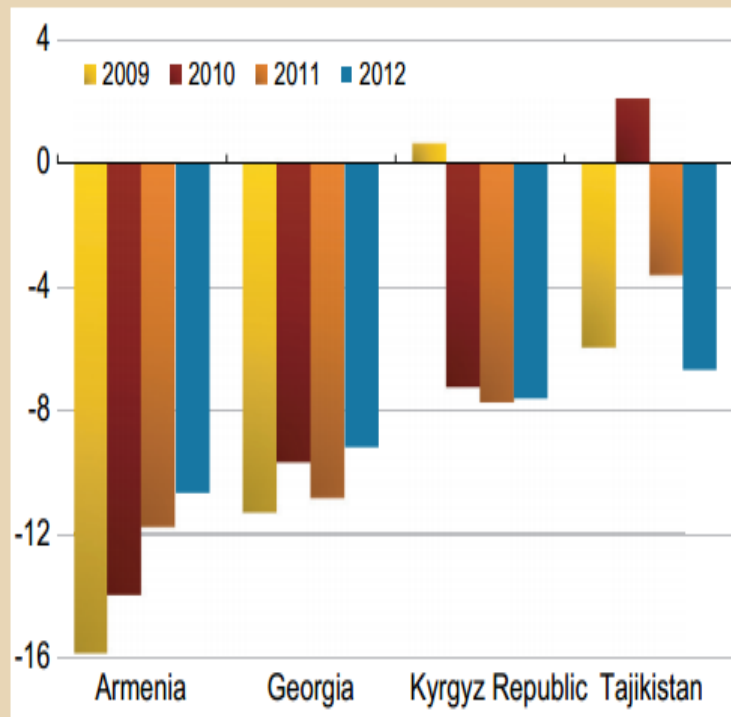
Consumer Price Index



Source: National Bank of Georgia

Current Account Balance

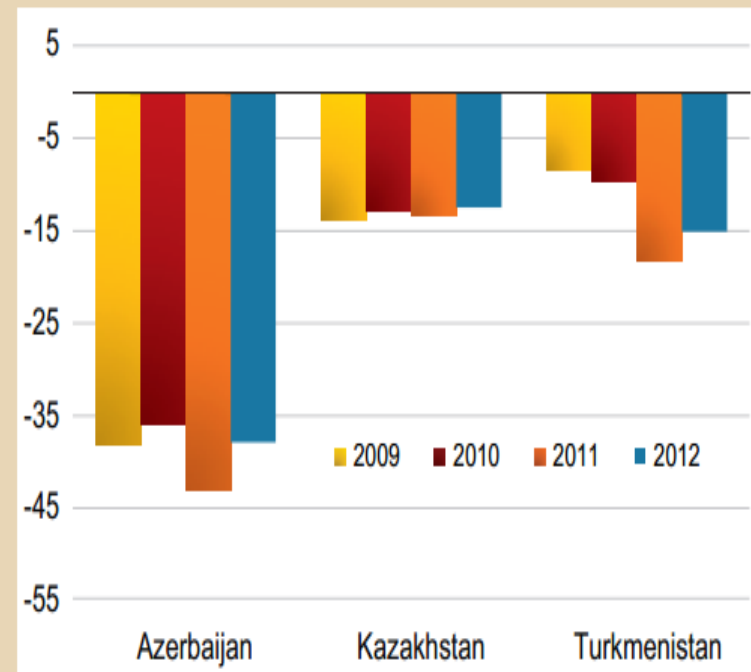
(Percent of GDP)



Sources: National authorities; and IMF staff calculations and projections.

Oil and Gas Exporters: Non-Oil Fiscal Balance

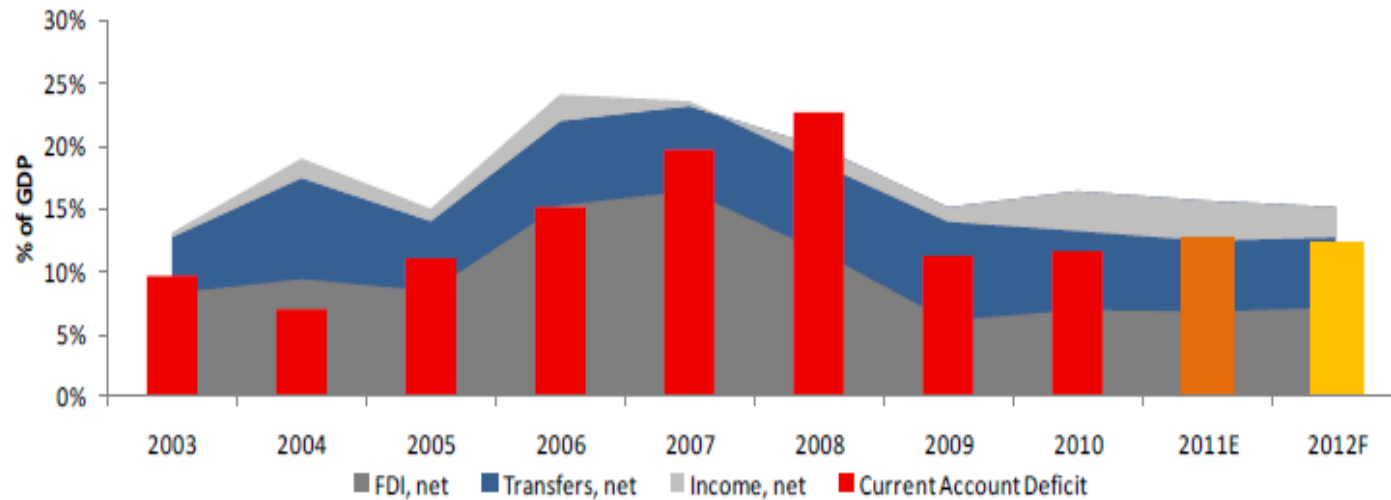
(Percent of non-oil GDP)¹



Sources: National authorities; and IMF staff calculations and projections.

¹Uzbekistan does not report non-oil fiscal balance.

Current Account Deficit



Source: Ministry of Finance of Georgia

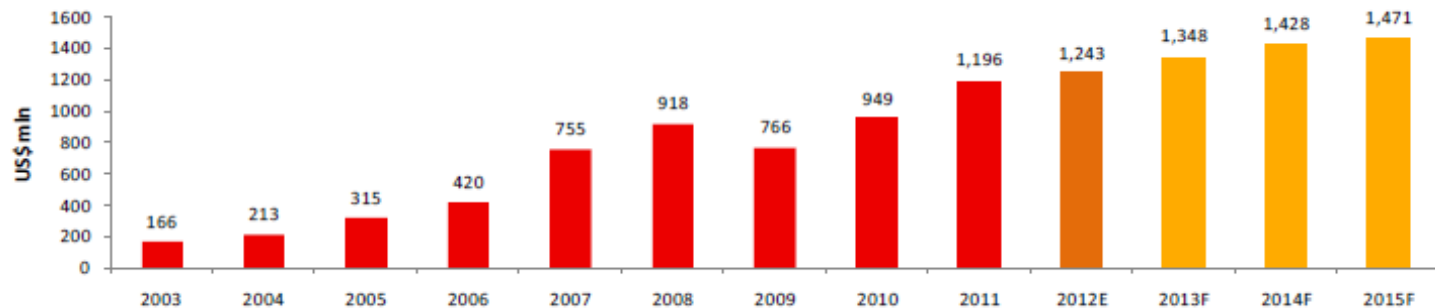
www.georgia.gov.ge

Remittances

Breakdown of Money Transfers in 2011

Country	US\$ million	Share in Total
Russia	635	53.1%
Greece	143	11.9%
Italy	110	9.2%
USA	74	6.2%
Ukraine	32	2.7%
Spain	30	2.5%
Kazakhstan	24	2.0%
Turkey	23	1.9%
India	14	1.2%
Other	1,196	100.0%

Money Transfers *

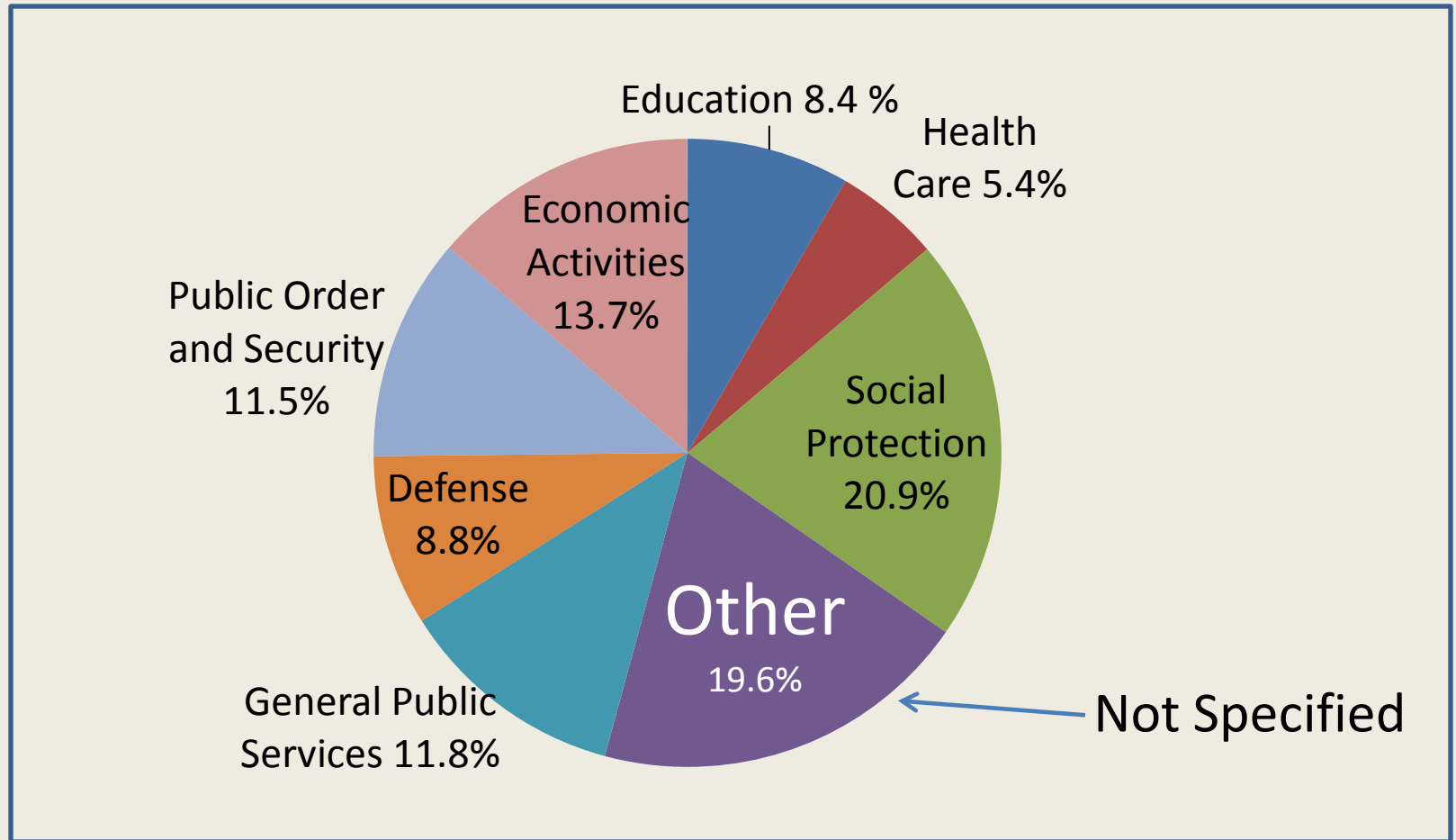


* Money transfer statistics includes only transactions made through quick money transfer operators by commercial banks and by micro finance institutions (from 2010). *Source: National bank of Georgia*

Fiscal Policy

- High Budget Deficit
- Wrong Budget priorities
- Non transparent budget expenses, 20% is other expenses
- Government Officials not providing spending records (salary, bonuses, traveling and other expenses) to public
- Excessive bureaucratic expenses

Georgian Government Expenditures



Source: Ministry of Finance, Georgia

WB Easy Doing Business 2010

Georgia's global rank is 11.

- Ease of opening a new firm - 3rd
- Registering property – 2
- Getting credit - 30
- Protecting investors – 41
- Paying taxes – 64
- Closing business - 95

Business Environment

- Business harassment by tax authorities
- Business shut down while checking inventory
- Tax investigation continues in average more than 6-8 month
- Inadequate and discriminating fines often leads business shut down and/or bankruptcy
- Contributions to opposition party will significantly damage business or leads to bankruptcy

World Economic Forum Ratings

By WEF Global Competitiveness Index Georgia is
88 among 139 countries in 2011:

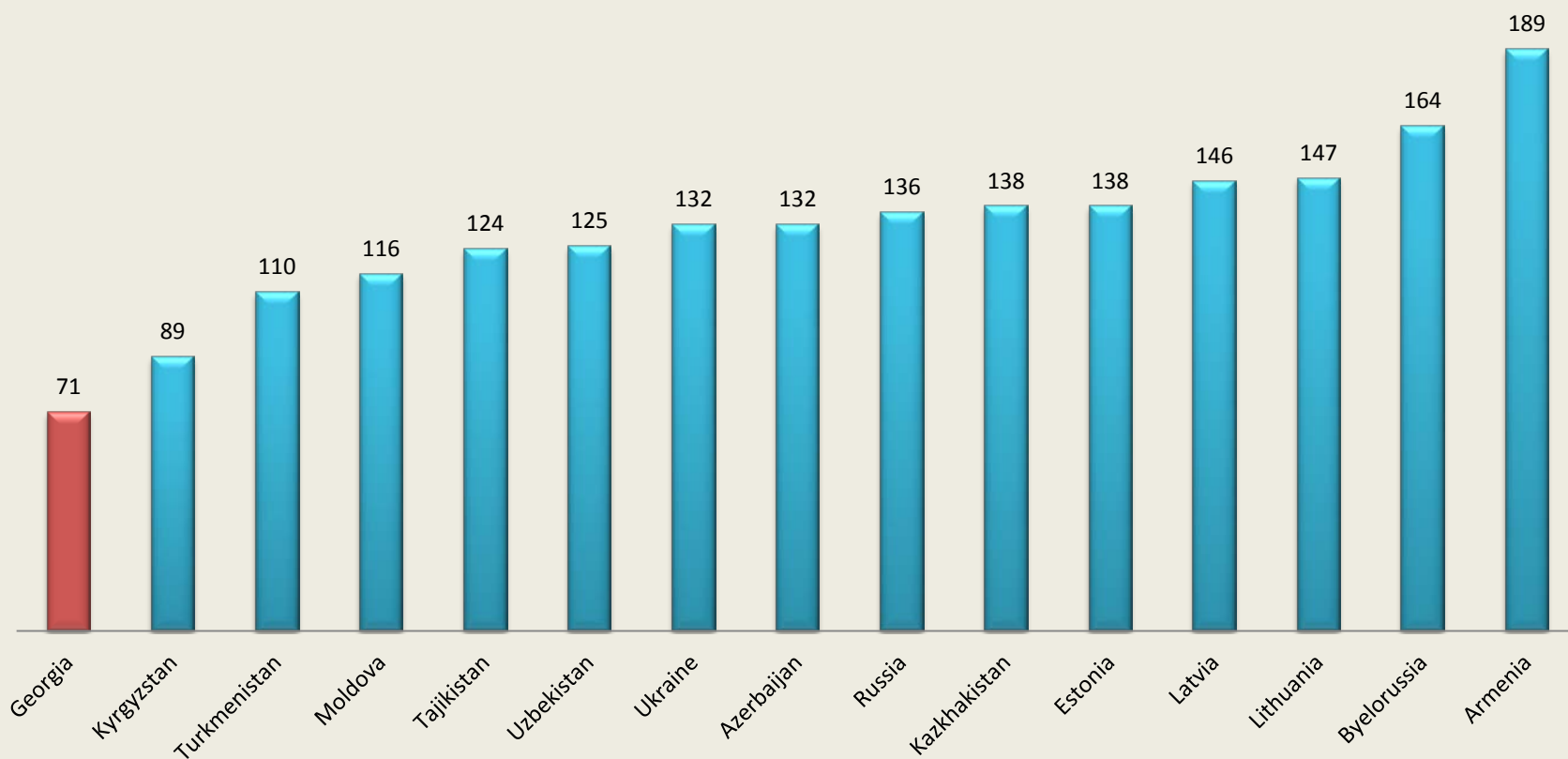
- Judiciary Independence 91
- Credit Rating, Education quality: 104th
- Property rights protection: 118th
- Local competition 124th
- Macroeconomic environment: 130th
- Antimonopoly policy: 135th

No State Strategy in Agriculture

- During 2006 – 2011 Agriculture production and infrastructure collapsed
- According state statistics 50% of the population is engaged in agriculture, while its share to GDP is 8%.
- Lack of public and private investment
- Majority of peasants, farmers owning small farmland
- Lack of none-trade barriers allowed by WTO and utilized by other countries; absence of proper food safety system. Local products can not compete with low quality third countries product
- Russian embargo
- Over 80% of agriculture products are imported

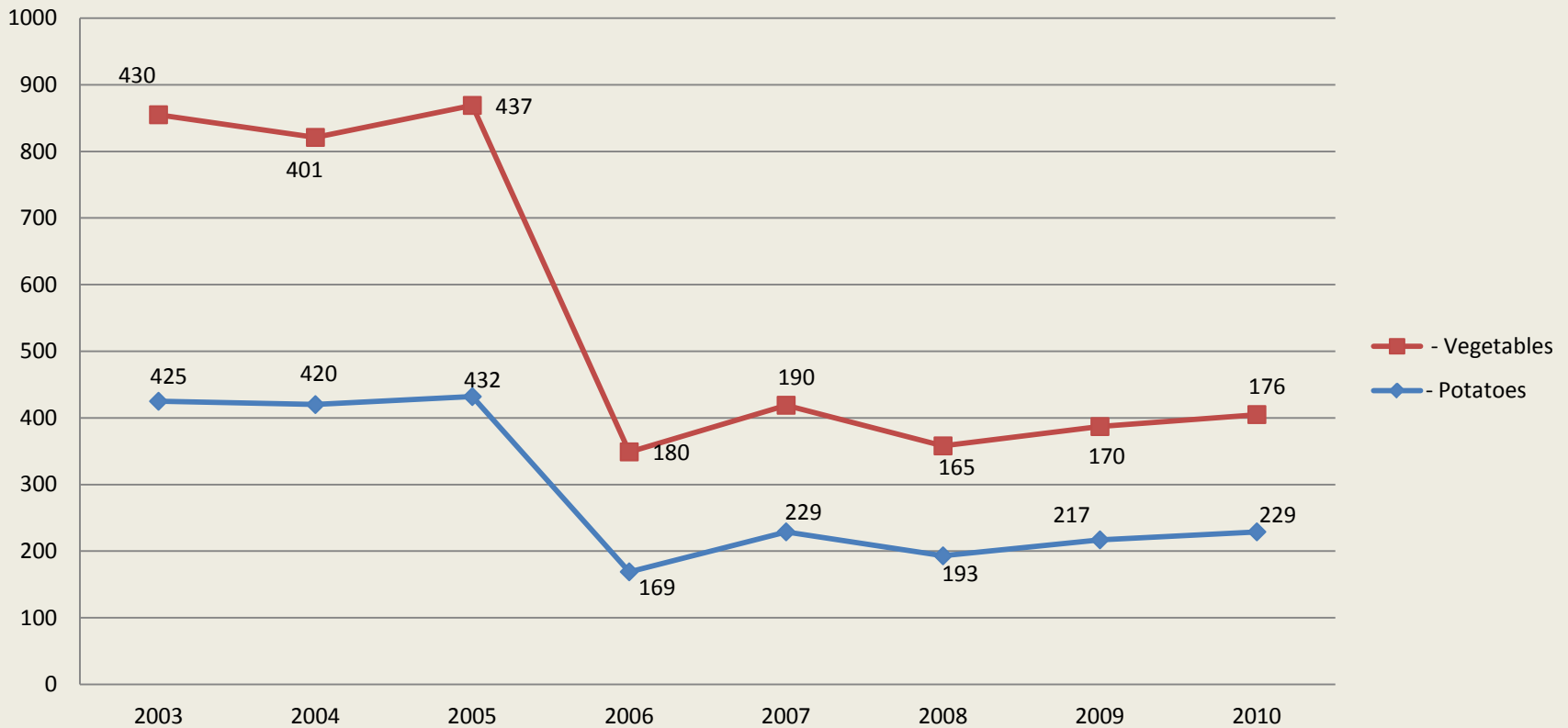
2009 Agriculture sector growth

(as a % of 2005 base)



Production of potato and vegetables (thousand tons)

Production of Potatoes and Vegetables (thousands of tons)



Production of Wheat and Corn (thousand tons)



Who gained from Rose revolution?

- “Between 2003 and 2009, the top 20% of the population saw their consumption increase by over 26%.
- The bulk of the Georgian **middle class** have not seen significant improvements in their living conditions since the Rose Revolution.
- The **consumption of the bottom 20%** increased by about 10% between 2003 and 2009, but most of the gain occurred between 2007 and 2008.
- *“Economic growth in Georgia has not been pro-poor. The poor, the middle class, and the rural households have captured a very small share of the growth if any. (“Georgia: Poverty Dynamics 2003-2010, The World Bank” 2011)*

New Economic Policy

To establish a competitive, free market economy and ensure a sustainable growth; to overcome extreme poverty; to create new jobs and a guaranteed social safety system.

To achieve this purpose it is necessary:

- to strengthen private property institutions and guarantee protection of the property rights.
- to support of personal initiative and fair market competition will ensure emergence of a strong middle class in Georgia
- to ensure macroeconomic stability through a strict monetary policy and allow inflation rate
- to have balanced and transparent budget,
- to maintain liberal taxation system,
- stable banking and financial system with enhanced functions for its supervision
- to development of agriculture is feasible through attracting investments in this field
- create small business development and agriculture development funds

Nations in Transit Ratings and Averaged Scores

	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011
Electoral Process	5.00	5.25	5.25	4.75	4.75	4.50	4.75	5.25	5.25	5.00
Civil Society	4.00	4.00	3.50	3.50	3.50	3.50	3.50	3.75	3.75	3.75
Independent Media	3.75	4.00	4.00	4.25	4.25	4.00	4.25	4.25	4.25	4.25
Governance*	5.00	5.50	5.75	n/a	n/a	n/a	n/a	n/a	n/a	n/a
National Democratic Governance	n/a	n/a	n/a	5.50	5.50	5.50	5.75	6.00	6.00	5.75
Local Democratic Governance	n/a	n/a	n/a	6.00	5.75	5.50	5.50	5.50	5.50	5.50
Judicial Framework and Independence	4.25	4.50	4.50	5.00	4.75	4.75	4.75	4.75	4.75	5.00
Corruption	5.50	5.75	6.00	5.75	5.50	5.00	5.00	5.00	5.00	4.75
Democracy Score	4.58	4.83	4.83	4.96	4.86	4.68	4.79	4.93	4.93	4.86

** Starting with the 2005 edition, Freedom House introduced separate analysis and ratings for national democratic governance and local democratic governance to provide readers with more detailed and nuanced analysis of these two important subjects.*

NOTE: The ratings reflect the consensus of Freedom House, its academic advisers, and the author(s) of this report. The opinions expressed in this report are those of the author(s). The ratings are based on a scale of 1 to 7, with 1 representing the highest level of democratic progress and 7 the lowest. The Democracy Score is an average of ratings for the categories tracked in a given year.

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