

Trends and Changes in Project Environment in Georgia

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Annotation

The aim of the research was to identify and analyze main trends in the Georgian society that critically affect on the Project environment. The terms of reference specified that the study should focus on the status quo of the SME environment in general and to Tourism and Wine sectors in particular.

Research design and concept.

Research paradigm is designed in a way that most pragmatically conveys major aspects of societal transformation. Attempts have been focused to produce the relevant research design that would successfully address to research purposes. The analyze is done in order to recognize most vulnerable aspects of economic policies regarding to SME environment with particular focus on agro-business, tourism and wine sectors. Moreover, the spheres of potential risk-factors are identified. Consequently, the possible ways to remove the existing hurdles are presented by the perspective of the Project contribution.

The research design is mainly constructed by the Qualitative method. Desk research method is applied to collect and process necessary information (secondary data). It made possible to perform preliminary analysis of studied materials and communicate them to research purposes. The secondary data within the study are obtained from the following official sources:

- Parliament of Georgia
- Ministry of Economy
- Ministry of Food and Agriculture
- State Department of Tourism
- International Donor Institutions
- International Monetary Fund
- National bank of Georgia
- Georgian Media, etc.

The structure of the research is as follows:

- Annotation
- Sectoral analyze of major trends in 2006
- Specific findings of the Monitoring process
- Annexes

Analyze of each presented sector is accompanied by expected output from Project's side. Anticipation is done on a rational base, given priority to results achieved previously and positive experience of Project (wine, tourism).

Results of the Project accomplishments are estimated on a basis of subsequent questions:

- ✓ Has the programme performed expected progress towards its objectives?
- ✓ Have significant results been achieved?
- ✓ If so, do the results appear sustainable?
- ✓ Have there been multiplier effects?

Sectoral analyze of major trends in 2006

Export-import

For January-September, 2006 the volume of export in comparison with the same period of 2005 increased in Georgia by 20,6%. Aircrafts and ferroalloys are the basic items in the structure of export of Georgia for the given period.¹

During 9 month of 2006, ferroalloys were exported on the amount of 69,9 million dollars(by 11,7 million dollars more than in the same period of 2005) that made 9,7% of the total amount of export. During January-September, 2006 aircrafts were exported on the amount of 60, 2 million USD(by 21,5 million dollars more than in the same period of 2005) that made 8,3% of the total amount of export.

Copper ore and concentrates were exported on the amount of 54,8 million(by 23,6 million more than during 9 months of 2005). Export of copper ore and concentrates make 7,6% of total export of Georgia in the reporting period. Scrap of ferrous metals was exported on the amount of 53,3 million(by 18,4 million less than in the same period of 2005) that makes 7,4% of total export volume.

As for export of dry wine, export of the product from Georgia totaled 33,3 million, by \$21,6 million less than in the same period of the previous year. In the January-September 2006, export of wine made 4, 6% of the total export of Georgia, while the same index of 9 months of 2005 made 9, and 2%.

In January-September, 2006 in comparison with the same period of 2005 the volume of import was increased by 55,2%. Oil and oil products occupy the basic place in the structure of import. The volume of import of oil and oil products for the given period makes 13, 3% of the total amount of import. In the reporting period. Oil and oil products were imported on the amount of 345, 4 million dollars (by 110, 5 million dollars more than during 9 months 2005). The second place in structure of import is occupied by cars. In the reporting period, cars were imported on the amount of 208,4 million dollars(by 95,2 million dollars more than in January-September, 2005) that made 8% of the total amount of import. Import of grain makes 2, 5% of the total import of 9 months of 2006. Grain was imported on the amount \$64,5 million(by \$34,2 million more than during 9 months of 2005).

Foreign debt

Georgia owes its 16 creditor countries USD 610,5 million in total debt. In addition to these creditor countries, Georgia owes international institutions over USD 1 billion. Georgia's creditors are: Russia(USD 150 man), Austria(USD 92 man), Turkmenistan(USD 65,6mln), Turkey(USD 55,1 man), USA (USD 41,6 man), Kazakhstan(USD 27,7 man), Azerbaijan(USD 16,1 man), Armenia (USD 18,5 man), Iran(USD 12 man), Uzbekistan(USD 396 000), Ukraine(USD 362 000), China USD 3 man), Germany(USD 66,4).

Investment Climate

The estimated volume of investment in Georgia in 2007 is \$1.5 billion. To that end, the Prime Minister has ordered the Economic Development and Finance Ministers, as well as the State

¹ National Bank of Georgia.

Minister on Reform Coordination, to take essential steps. Government is working on the creation of liberal legislation aimed at fostering business development.²

Georgia led the global top 10 reformer rankings on the ease of doing business in 2005–2006, according to a Doing Business 2007 report prepared by the World Bank and the International Finance Corporation (IFC). Georgia improved in 6 of the 10 areas, studied by Doing Business – reduced the time, cost, and hassle for businesses to comply with legal and administrative requirements according to the report. Georgia leads the list of reformer-states, which includes Romania, Mexico, China, Peru, France, Croatia, Guatemala, Ghana and Tanzania. Doing Business 2007 also ranks 175 economies on the ease of doing business. Georgia jumped a spectacular 75 places and ranks 37th this year. Armenia ranks 34th, Kazakhstan 62nd, China – 93rd, Russia 96th and Ukraine 128th.

Turkish Businessmen express their interest to invest in Georgia. Turkish investment in Georgia in 2007 will reach \$1 billion³. Investment in 1992 totaled \$17.6 million, while according to latest data, has increased to \$500 million.

Turkish party is interested in making investments in tourism infrastructure, mainly in Batumi, constructing thermal power stations, construction sphere etc⁴.

Turkey is Georgia's important partner, and trade and economic links of the two countries are increasingly important amid escalating tensions between Georgia and Russia. It is planned to open new customs checkpoints at the Turkish border. Solution of the double taxation problem will contribute to the growth of capital investment in Turkey and Georgia.

Protection of Property Rights

Despite significant changes in the business environment, insufficient protection of contracts and property rights are problems for both Georgian and foreign business community in Georgia. The interests of investors have sometimes been harmed by biased court proceedings.

Disputes sometimes centered on alleged illegal or improperly handled privatization and bankruptcy proceedings. During 2004-05 media was covering the issue of undermined confidence in the impartiality of the Georgian judicial system and rule of law, and by extension, Georgia's investment climate. Both foreign and Georgian investors have expressed reservations about the competence, independence and impartiality of lower court decisions. Main structures of instability are lower courts that make decisions on questionable legal grounds. In 2004, the Supreme Court abrogated the property rights of the real estate company with 65% American ownership, to a centrally located plot of land in downtown Tbilisi in favor of a national union. The Supreme Court later cancelled its 2004 decision and returned the case to the District court for review. In 2005, a further Supreme Court ruling restored the property rights of the company. In another example, a foreign investor in the telecommunications sector effectively regained control lost earlier to a local partner in a lower court action through a higher court ruling. Another court decision that invalidated the acquisition of a foreign investor was later overturned only by presidential decree. In June 2004, the Tbilisi Municipality revoked the results of a 2003 tender by the World Bank that awarded management rights of the Tbilisi Water Supply Company to a foreign company. According to the Mayor's office, the tender had been conducted incorrectly and was therefore rescinded.⁵

² Zurab Nogaideli, prime Minister.

³ Turgul Erkin, the co-chairman of the Business Council of Georgia and Turkey

⁴ Sarke information Agency, 10,12,2006

⁵ Country commercial guide to Georgia.

Recently adopted amendments to the property expropriation law entailed great concerns of opposition parties in the Parliament of Georgia. The Property expropriation law gives the state the right to take possession of property for public use by right of eminent domain. The opposition MPs has serious doubt that if the amendments are approved, then it will be easy for high officials to confiscate the property of any citizen living in the central parts of the city and use this law saying it is necessary for the public”⁶

EBRD Regional Centre of Investment Projects in Tbilisi

EBRD opened a regional center in Tbilisi. The new center will be engaged in implementation of investment projects in the countries of South Caucasus and Moldova. Georgia was chosen because of its favorable geographical location.⁷

“The investment environment in Georgia has improved considerably, which resulted in the growth of investments made by EBRD”⁸. If in previous years the bank had 5-6 projects in Georgia annually with total amount of 50 million Euro, in 2005 they started 18 projects with a total sum of \$115 million. About 95% of the amounted was allocated to the private sector. This year’s total number of new projects will be 20-23 and total project costs will amount to 125-135 million Euro.⁹

German Company Heidelberg Cement Builds 10 Cement Factories in Georgia

Heidelberg Cement, which owns the controlling share of Kartuli Cement, plans to build 10 cement factories of various capacities throughout Georgia¹⁰. Heidelberg Cement is one of the leading companies in the world in cement production and its activities in Georgia will attract lots of big investors to our country. The move signaled Heidelberg Cement’s expanding interests in Georgia after it bought 51% of shares in the Georgian cement company Kartuli Tsementi in May, 2006. HeidelbergCement plans to extend the capacity of the plant up to 500 000 tones in 2008. Besides, the company plans to build cement plants in Terjola (West Georgia)

Recently it was announced that HidelbergCement purchased 75% of shares in Saqcementi LTD. Saqcementi is the market leader in Georgia with a share of around 60% and in addition supplies neighboring Azerbaijan(20% of market share) and Armenia.

Heidelberg Cement announced that the Company expects to benefit from the growth potential of the Caucasian market and establish a strong market position in this region¹¹.

Strategy of Economic Policy

Ministry of Economy elaborated “Medium-Term Action Strategy of the Government of Georgia 2007-2010”. The strategy classifies five priorities. Priority number one is “to coordinate the elaboration and the implementation of Economic Policy.” Next issue consists in streamlining the

⁶ Manana Nachkebia, New Rights, PM.

⁷ Oliver Dekam, Head of EBRD business group for South and East Europe

⁸ Oliver Dekam, Head of EBRD business group for South and East Europe

⁹ The Georgian business Week

¹⁰ David Tkeshelashvili, Minister of Environment Protection and Natural Resources

¹¹ Bernd Scheifele, Chairman of the Managing Board of HeidelbergCement.

investment attractiveness of the Georgian Economy, Trade liberalization and increase of competitiveness of Georgian product and Services. Third priority is to reform and liberalize the Regulator bodies in Construction sector. Fourth priority has an objective to finalize the process of State property transfer to Private Ownership. Last priority aims to progress and liberalize Transport System management and develop road infrastructure.

The Medium-Term Action Strategy is an elaboration of the programmed of the Government of Georgia “For Unified and Strong Georgia”, which was approved in 2004, as well as a further Specification of the priorities, taken into consideration the progress already achieved and the new challenges. The following documents, which reflect the State Policy, are part of the Strategy: National Security Concept, NATO Individual Partnership Action Plan (IPAP), Anti-corruption Strategy of Georgia, Government of Georgia Anti-corruption Action Plan, etc.

Russian embargo impact on Georgian economy

Political conflict with Russia echoed to economic sphere as well. Russian Administration accomplished unexpected measures in diverse spheres, economic spheres included. Economic pressure suffered Georgian Economy during the whole year. The chronological sorting of events give full sense of the solidity of crisis:

March 27

Russia banned the import of Georgian wine on March 27, claiming that they were contaminated with pesticides. After banning the import of Georgian wine in March, the Russian consumer protection agency warned in April that sanctions might also be applied to Georgian mineral waters. This decision was backed by a resolution of the Russian Parliament’s lower house passed on April 19 which hailed the ban as a measure to protect the health of Russian consumers.

April 18

The Russian consumer protection agency announced that it has found a large number of falsified and low quality Georgian mineral water Borjomi on the Russian markets. Eighty percent of Georgia’s most prominent mineral water Borjomi was exported abroad and more than half of this amounted to Russia, while 40 percent goes to 27 other countries around the world. Russia banned the import of Georgian wine on March 27, claiming that they were contaminated with pesticides.

May 5

Russia has banned the import of the Georgian mineral water “Borjomi,” Russian chief sanitary inspector Genady Onishchenko announced. “The reason for this very difficult decision was the fact that an inspection carried out recently in the regions - especially in the Moscow region - showed that these waters, which are being advertised as ‘Borjomi’ water, do not, in reality, correspond to the specifications of this water,” Onishchenko said. The decision to ban Borjomi comes five weeks after Russia banned Georgian wines and spirits.

May 6

One day after banning Borjomi mineral water, Russian chief sanitary inspector banned the import of another Georgian mineral water brand Nabeglavi, the Russian consumer protection agency reported. 100 percent of the 175,560 bottles of Nabeglavi that were inspected failed to meet standards in the Moscow region, the Russian consumer protection agency said.

The prognosis of potential economic loses for Georgian economy has been revealed frequently. According to estimates the economic blockade will make slow down economic growth by 1,5-2%.

Annual economic growth may be less than planned 10%.¹² The IMF statement reveals Inflation and aggravated relations with Russia as the impediment factors of economic growth. These Two challenges are most intimidating factors reasoning serious risks for the economy.

Aggravation of outlook to Georgia

Standard and Poor's has revised its outlook on the government of Georgia to stable from positive owing to increased geopolitical risk.¹³ Standard and Poor's gave a positive outlook to Georgia in an assessment unveiled last December. But in a recent report the agency said Georgia's weak external indicators are aggravated by tensions in its relationship with Russia, a key trading partner. "The outlook change reflects Standard & Poor's view that the geopolitical risks in the region have increased significantly and may impair positive trends in external liquidity, investor sentiment, and economic growth."¹⁴

Smuggling

The problem of smuggling is related to separatist regions of Georgia. The problem still remains as obstacle for economic development of Abkhazia and South Osetia. The area of concentration of smuggling is South Osetia, though some smuggling activities are also done in Zugdidi, close to Abkhazia.

According to calculations the state should be collecting GEL 292 million in taxes from cigarette purchases: Gel 213 million from imported cigarettes and Gel 79 million from local cigarette production.¹⁵ Georgia received GEL 51, 9 million from taxes on domestic cigarettes and Gel 35,5million from imported cigarettes for the ten months of 2006.¹⁶ Although the smuggled cigarettes are on the decline, the scale of smuggling is very large. According to estimations 60% of the tobacco business is illegal. South Osetian political problem is the ground for the circulation of illegal cigarettes all over the Georgia.

Conclusions

Numerous exogenous and endogenous factors are distressing Georgian economy for the period of 2006 year. Due to mentioned factors economic growth slowed down and serious shocks took place. The galloping inflation is imperative from endogenous ground. Global oil prices fluctuations and Russian Embargo are most important among exogenous factors. Due to political conflict all possible means of suppression are introduced by Russia to date:

- *Introduction of Economic Embargo*
- *Introduction of Visa prohibition regime*
- *Discrimination of ethnic Georgians in Russia, both citizens and non-citizens of Russia.*
- *Tolerance and political backing to separatist groups in the territory of Georgia providing them with arms and technical support.*
- *Increase of natural gas prices up to international prices levels*

¹² Kakha Bendukidze

¹³ Standard&Poors, November 21, 2006.

¹⁴ Luc Marchand, Credit Analyst, Standard&Poor.

¹⁵ The Messenger, December 6, 2006.

¹⁶ Ministry of Finance of Georgia.

Finances

Budget

In Georgia, since 2004, budgeting practice was significantly improved compared with the previous period. *Draft budget* for 2007, revenues and grants amount to GEL 3 billion 444 millions. State budget expenditures total to GEL 3 billion 870 millions and the deficit is about GEL 426 millions. It is significant, that the exchange rate, as one of the major macroeconomic parameters, is determined by the State Budget as 1US dollar = 1.75 lari. Annual growth of gross domestic product – 7.5%, what, expressed nominally, achieves 16 billion lari. The government expects that average annual inflation will be 6%.

Growth of revenues, generally, is due to the tax sector. This year growth will be GEL 2 billion 884 millions, compared with GEL2 billion 526 millions, for the last year. Actual growth is GEL358 millions. Capital revenues decrease significantly. In 2006 this type of revenues was GEL333 millions and for the next year there are expected only GEL100 millions, what, first of all, is conditioned by the completion of privatization process.

According to the 2007 draft budget, financing for ministries, which will increase by GEL 43 million compared with 2006, will be as follows:

Table #1. Budget allocation according to ministries.

| <i>Financing by Ministries in the 2007 Budget</i> | <i>Amount</i> | <i>Amount¹⁷ GEL (thous)</i> |
|---|--------------------|--|
| Ministry of Labor, Health Care and Social Welfare - | GEL 999.7 million; | 916 070,0 |
| Ministry of Defense | GEL 392.5 million; | 513 270,0 |
| Ministry of Finance | GEL 751,5 million | 751 500,0 |
| Ministry of Economic Development | GEL 456,8 million | 419 500,0 |
| Ministry of Energy | GEL 111,6 million | 217 254,0 |
| Ministry of Justice | GEL 92,2.million | 117 032,0 |
| Foreign Ministry | GEL 59,9 million | 49 850,9 |
| Interior Ministry | GEL 245,7 million | 297 786,0 |
| Ministry of Education and Science | GEL 396,8 million | 389 300,0 |
| Ministry of Culture, Protection of Monuments and Sport | GEL 57 million | 65 380,0 |
| Ministry of Refugees and Accommodation | GEL 50 million | 44 130,0 |
| Ministry of Agriculture | GEL 43,6 million | 47 980,0 |
| Ministry of Environment | GEL 31,4 million | 34 909,9 |
| Office of the State Minister for Conflict Resolution Issues | GEL 470,000 | 503,2 |
| Office of the State Minister for Coordination of | GEL 440,000 | 440,0 |

¹⁷ . Final version of 2007 Budget allocations adopted by recent Parliamentary Session in December 2006.

| Reforms | | |
|---|-------------|-------|
| Office of the State Minister for Euro-Atlantic Integration Issues | GEL 968,000 | 968,0 |
| Office of the State Ministry for Civil Integration Issues | GEL 200,000 | 200,0 |

A further GEL 496 million will be allocated on road construction and rehabilitation. According to the draft budget, GEL 250 million is set aside for the payment of Georgia's foreign debt, and GEL 74 million will be allocated for the payment of internal debt.

Priorities involve healthcare and social welfare. One billion lari will be allocated to the healthcare and social welfare sectors. For funding of state defense, public order and security there will be allocated GEL 638 millions and for road rehabilitation – GEL 496 millions. To the culture, energy and agriculture sectors there will be allocated GEL 200 millions in total.

15% of the country's GDP will be provided by the agricultural sector. Obtained revenues, basically, will be spent for the activities for updating of the agricultural plants and machinery. In 2007, the tractors will be distributed according to the district lots. E.g. the machines for maze laying-in will be transferred to Samegrelo.

In general, new Budget intends to reduce the programs to be funded in the regions. The Chairman of Sector Committee states that Draft Budget for 2007 intends to cancel all measures for promotion of Georgian wines, tourism and investments in general: "There is not intended even one Tetri for implementation of the projects for rehabilitation of the private enterprises."¹⁸

Expenses for general government services will be decreased significantly, by 13%, among them expenses for executive and representative bodies will be decreased by 21%.

Banks

Commercial banking sector in Georgia rapidly developed in 2006. This is confirmed by the banking sector statistical data for the passed period of 2006:

Table # 2. Data of performance of Commercial Banking sector.

| Item | Amount | Increase in % |
|---|--|--|
| Total loans | GEL 2502 millions(20 th September 2006) | 81.9% increase(compared with year 2005) |
| Loans in national currency | GEL 655.2 millions (20 th September 2006) | 112% increase, (compared with similar period in 2005). |
| Loans in foreign currency | GEL 1060 millions (20 th September 2006) | 75% growth |
| Total assets of Georgian commercial banks | GEL 3,788 bn | Increased by 66.7%. |
| Share capital | GEL575 millions(August, | increased by 41.8 |

¹⁸ N. Lekishvili, newspaper "Rezonansi"

| | | |
|-----------------------------------|---------------------|---|
| Return to assets | | 2.7% (compare with 3.3% in 2005). |
| Total deposits | GEL 161 millions. | Increased by 51.9% (compared with the similar period of 2005) |
| Deposits in the national currency | GEL 510.3 millions. | Increased by 81.5% (compared with the similar period of 2005) |
| Deposits in foreign currency | USD 637.4 millions. | Increased by 44.9% (compared with the similar period of 2005) |
| Dollar deposits, | | 68.5% (73.6 in 2005). |

International monetary reserves, as of 4th October 2006, increased by 43.1%, compared with similar period of the last year and amounted to \$ 632.9 millions. The similar figure for 2005 was 442.2 US dollars.

This year, in the banking sector, there were carried out number of efficient activities. Financial institutions of CIS and European countries express their interest towards Georgian commercial banking system. During year 2006, banks of Azerbaijan, Kazakhstan and Armenia expressed their interest. Purchase of 60% of the shares of Bank Republic by the Transnational Financial Group Societe Generale is especially significant fact. This is the first case of entering of the world-level financial leader to Georgian banking market.

Placement of the shares by the Bank of Georgia at London Stock Exchange is also of great significance. President of Georgia opened trading at the London Stock Exchange on November 29, 2006, in celebration of the listing of Bank of Georgia, the first Georgian company to be presented at LSE.

TBC Bank signed the agreement with the largest bank of the world, City Bank, dealing with \$35 million credit resource. This resource will be used for meeting of the demand from the corporative customers.

Against the background of development of the Georgian banking system, the low activity of the banking sector in the sphere of agriculture still remains a weak link. In this respect, we should admit the interest of French bank "Credit Agricole" to Georgian "Tao Bank". Supposedly, first intended project will be the agriculture development and farmers assistance project. Purpose of cooperation of "Tao Bank" and "Credit Agricole" is development of financial strategy of agrarian development in Georgia. Major direction of the project will be allocation of short- and long-term loans for the agricultural companies. The first stage of the project will include in situ study of the agrarian situation by experts, development of the action plan for Tao Bank and elaboration of the specific recommendations for implementation of the pilot project in Georgia. The experts have already visited Kakheti region and met with local representatives of agrarian sector. The second stage will include practical introduction of the project and its implementation. Such banking products will contribute to attraction of the credits for the vineyards. The farmers need such credits for their vineyards. In general, such credits would contribute to development of the raw material infrastructure and hence, the export opportunities of Georgian wines.

Credit Agricole has implemented similar projects in the CIS countries, in Armenia among them.

Georgian banks avoid work in agricultural sector, as they regard that agriculture, in Georgia, is of high risk and low efficiency.

International monetary reserves of national bank reached its maximum USD 720 mln. (increased by 248 mln since 2006.

As of Electronic money-transfer systems, USD 453 mln were transferred during 10 months of 2006. USD 306 mln were transferred from Russia, i.e. 67% of the total amount transferred. USD 46 mln were transferred from USA and USD 13,6 mln from Greece. USD 112 mln were transferred from Georgia to foreign countries during 10 months. After Russia imposed prohibition on transport and post communication with Georgia in October USD 33, 7 mln were transferred from Russian Federation to Georgia.(by 19,8% less than in September 2006.

Inflation

This year, World Bank has published the results of its studied, stating that Georgia has progressed greatly with respect of reformation of business environment.¹⁹. Georgia moved from 112th place in World Bank's classification to the 37th place and left behind such countries as Italy and Spain.

It is interesting that this information was published after the serious warning from the side of IMF to the government on macroeconomic instability, caused by inflation.

The factor of inflation expectation is significant for Georgian economy. During 15-year period of transition Georgia has passed all phases of inflation. In 1992, in Georgia there was a galloping inflation, when inflation rate increased from the two-digit figure to about 600-700%. Especially harmful for the economy was 1993-1994 period, when hyperinflation, finally, achieved 7000%.

At a current stage, the policy, recommended by IMF implies dramatic decrease of the money supply, what is extensively implemented by National Bank. Relevantly, the deposit certificates were issued, through current auctions, also increase of the rate of reserve requirements for the assets attracted by the commercial banks.

Stopping of growth of the monetary reserves and money supply by National Bank would cause revaluation of lari. Against the background of such measures, may be the inflation rate would fall, though, inevitably, the export prices would worsen, what would decrease its volumes.

Position of IMF was not active , at some extent, as there were no declarations about upcoming inflation danger, what would help the population to be more prudent against the economic danger. Only when the problem became the subject of extensive public discussions, IMF pointed out to Georgian Government and National Bank for 14.5% inflation rate. As we have already admitted, the main reason for inflation was increase of money supply. In July, the Parliament approved the amendments to the State Budget and supply was increased by GEL 323 millions. The expenditures were mainly intended for the Ministry of Defense – GEL 212.5 millions.

National Bank attempts to slow down inflation through various techniques²⁰. National Bank commenced sale of the deposit certificates. Through these securities the money is withdrawn from circulation, thus delaying the inflation process. The deposit certificates are new type securities, emitted by National Bank. Unlike the government securities, these certificates are intended for the commercial banks only, what implies that only commercial banks may

¹⁹ “ Doing Business Report 2007”, World Bank.

²⁰ According to IMF Mission recent Statement in flation rate is slowed down to 10%.(December 15, 2006)

participate in bids and physical and legal persons may not attend the trade session. Georgian National Bank commenced arrangement of the deposit certificate auctions from 18th September and total volume of transactions is about GEL 30mln.

Analysis of the auctions shows that the interest rate of the deposit certificates grew. Supposedly it will grow further. This process, at some extent, is associated with growth of prices of the credit resources, what, on its side, cause anti-inflation processes.

The most painful process, associated with inflation, is significant fall of the purchase power of the population. The household economies became aware of the danger about 1.5 years ago, when they noticed, that in conditions of slight change of the incomes the number of goods in the basket decreased significantly. Adequate response to growth of inflation expectation, from the side of population was investment of complete private savings into the real property. Investing of the savings into the construction sector shows that the trust of the population is at the lowest level. This is the clearest recognition of inflation from the side of public. Prompt "removal" of the monetary assets and investing into the only sector (construction), where the risk is lower, caused drastic increase of prices. Prices for the real property grew by about 200% for last two years and total investments into the construction industry were 383 millions in 2004 and 619 millions – in 2005.

Developments in the financial sector, during last year were characterized as by positive, also by negative results. As positive trends, we should admit developments in the commercial banking sector:

- ✓ *Growth of the banking market*
- ✓ *Entering of the international leaders to the banking market (Societe Generale, Vneshtorgbank, Credit Agricole)*
- ✓ *Remarkable improvement of operation parameters of the commercial banks.*

Among negative developments, there should be admitted:

Practice of administering non-synchronously with the banking industry requirements, causing increases of risks as in the banking sector, also generally, on the financial market.

National Bank's policy of decrease of money supply caused drastic growth of prices for the credit resources on the banking market. As a result, prices for goods and services produced by the enterprises, which received the credits, increased, thus increasing inflation rate.

Probably, in planning of future monetary and credit policy, there should be taken into consideration the fact that the monetization indicator in Georgia is one of the lowest among CIS countries. Consequently, further decrease of the money amount would dramatically decrease dynamics of economic activities. Growth of exchange rate of Lari is officially declared as a sign of strengthening of Georgian Lari. Actually, Purchase power of Georgian Lari gradually decreases. In addition, high rate of Georgian Lari further decreases competitiveness of Georgian export industry.

Wine

The factors that were entailed by the political conflict with Russia found a very dramatic development in the current year. It is natural that the crisis affected agriculture in general and particularly wine-making sector.

Before starting of vintage, the Ministry of Agriculture made prognosis that around 170 000 ton grapes would be gathered in Kakhetia. Out of gathered grapes, around 40 000 ton was purchased by wine companies, part was pressed out in families and the rest passed to different regions. About 400 companies purchased around 5 000 ton grapes based upon the President's "request". 57 companies bought grapes from peasants: "Alaverdi", "Kotekhi", "Khareba", "Velistsikhe", "Mukuzani", "Zegaani", "Badiauri", "Telavi Wine Cellar", "GWS", "Teliani Valley" - the sum composed 40 000 ton.

The companies purchased 65 000 ton grapes in 2005. The number had to increased up to 100 000 ton this year, however, on the contrary - reduction occurred. First 40 tetri then 60 tetri and lately again fewer prices were registered. It should be noted that large volume of grapes has been pressed out by peasant-thrifts in the currents year. Last year 4 mln litter wine was pressed out. In difference to the last year, wine will be elaborated by peasants and not by wine factories this year.

Closure of the Russian market had seriously affected the wine export business:

"Telavi Wine Cellar" has elaborated 5 000 ton grapes last year. This year they have received their own harvest in the amount of 150 ton and purchased only 100 ton grapes; "Tbilghvino" (Tbilisi Wine) has elaborated 2 200 tones grapes last year. This year they have not purchased grapes at all as they have big amount of last year wine supply left. Presumably, they will buy small amount in the Western Georgia; "Bagrationi" purchased 3 000 ton grapes last year. This year they only purchased 20 ton "Saperavi" for production of pink Champaign (sparkling wine).

Non-profile companies and institutions purchased 5 000 ton grapes by the President's instruction. These companies are: "Coca-Cola", "TBC Bank", pharmaceutical companies, "Tbilaviamsheni", "Azoti", "Black Sea Group", "Magti", building company "Arsi", Poti Sea Port, Wissol, Georgian Army (Ministry of Defence), etc.

The grape harvest has reduced almost by 4 times in the Western Georgia this year in comparison to the last year. Vintage started in the mid October there and ended at the beginning of November. 320 ton grapes were gathered in Racha region in the second half of October out of which 170 ton was purchased by the wine companies and 50 ton was pressed out by Racha peasants themselves. Mainly, 2 species are singled out: "Mujuretuli" and "Alexandrouli". Grape realization was taking place without any problem, in good prices, by 3 Lari. This, two or three times, exceeds Kakhetian grape price, demand on which, particularly on "Saperavi" has substantially reduced this year. "Rkatsiteli" minimal price on 1 kg was registered at 28 tetri and maximal at 60 tetri in Kakheti this year; "Saperavi" price composed 0,80 - 1,2 Gel. "Saperavi" minimal price was 1,8 - 2,0 Gel last year. The primary reason on Racha grape species demand increase is that the wines prepared by them are sold at the Western country markets and accordingly they do not depend on Russian market.

3 - 3,5 thousand ton grapes should have been gathered in Racha by the prognosis of the Ministry of Agriculture before starting of vintage, however, it is announced now that more than 700 ton should not be expected. Spring frosts and later unceasing rains were declared as reasons. 4 000 ton grapes were gathered in Racha region last year which were mainly purchased by the wine companies.

100 ton grapes were gathered in Lechkhumi this year, mainly "Ojaleshi" and "Tsolikauri". 7 companies develop wine in Racha-Lechkhumi already: "GWS", "Senakuri", "Teliani Valley", "Tbilvino", "Chumlaki Wine Factory", "Georgian Wine House in Racha" and "Bugeuli".

On October 26 European standards wine factory “Badagoni” was opened in the village Zemo (upper) Khodasheni of Akhmeta rayon. The aforementioned fact is interesting because in the conditions of the Russian embargo the investment in the wine sector was implemented by the Western company. Opening of the “Badagoni” wine factory is of particular importance as it is related to the newest technology issues. High-technology wine production is the main strategic issue and will easy penetration of the Georgian wine into the European and American markets in a long-term perspective. However, the circumstances that have later developed in this factory are beyond any imagination:

Feasible volume of wine export was estimated at around 100 mln USD in 2006. Export volume was equivalent of 63 mln USD in 2005 87% of which composed export to Russia. Based on the Government’s request, the Monetary Fund has estimated feasible loss in this sphere at the current period by losing the Russian market. According to the Monetary Fund, feasible loss of 100 mln USD is possible. It is a huge amount at first look, however, for the Georgian economy, the size of which is 6 billion USD this loss is not very important. According to the expressed opinions, the main loss will be in the sphere of micro economy. As a whole, it was considered that hindering in the economic growth would be within 1% and the economic growth indicator will reach about 6 – 7%.²¹

International Monetary Fund has special assisting tools for such trade shocks, however, as a representative of this institution had stated there is no need for this as there is not a substantial shock. Government reserves for such a moment are also important and accordingly there is no need for assistance.²²

Some Government officials expressed their opinion that banning of the Georgian production export to the wine market by Russia will substantially foster and compel Georgian wine-makers to improve the wine quality and look for new markets. Georgian wine-makers held a press-conference after their Russian visit and expressed believes that their return to the Russian market is their primary goal. At the moment of banning wine export to Russia certain measures were taken by the Ministry of Agriculture. It was decided at the meeting with the wine-producing companies that the Georgian wine samples would be sent to the International laboratories for testing. Following samples were sent:

- Switzerland: GWS “Saperavi”, Telavi Wine Cellar “Mukuzani”, Tbilvino “Saperavi” and Teliani Valley “Mukuzani”;
- Germany: GWS “Tamada Mtsvane” (Toastmaster Greene), Telavi Wine Cellar “Saperavi”, Tbilvino “Saperavi” and Teliani Valley “Teliani Tsiteli” (Teliani Red);
- France: GWS “Dzveli Tbilisi” (Old Tbilisi) and “Saperavi”, Telavi Wine Cellar “Tsinandali”, Tbilvino, “Rkatsiteli” and Teliani Valley “Tsinandali”.

The visit of the President of Georgia and the Wine Company Managers to the China Republic should be also highlighted. This visit was specifically advertised in Georgia and the opinions on the authority level were expressed that this visit would foster entering of the Georgian wine into the Chinese market.

Several events also took place during the current year for lobbying of the wine company activities and protection of the wine-making policy. Namely, the press-conference on foundation of the “Georgian Wine Producers’ Union” was held on March 21. The aforementioned Union represents non-entrepreneurial legal person the organizational-legal form of which is a union; it

²¹ R. Christiansen, IMF

²² R. Christiansen, IMF

was formed from 10 member initiative group of the Georgian wine-producing companies and passed its registration at the Ministry of Justice. The goals of the Union are:

- Fighting against falsification of Georgian wine and fostering the State fight – accent on export markets;
- Fostering revival-development of vine-growing and wine-making fields;
- Monitoring of the ongoing processes in vine-growing and wine-making fields and registering one's own position; also, giving out recommendations to all subjects working in this field – as to the State so to the private companies;
- Protecting consumers and entrepreneurs' interests and rights.

Chamber of Commerce and Industry of Georgia held an event for protection of Georgian wine quality reputation on September 25 – 28. Well-known journalists working on wine issues were within the invitees: Christian Callec, Slijters Vakblad, Jorgen Aldrich, Viktor Bruzevski, etc. The event was hosted by the following companies: "Askaneli", "Teliani Valley", "Vazi+" (Vine+), "Telavi Wine Cellar" and "Shum". Articles dedicated to Georgian wine will be published in foreign magazines and newspapers which will definitely foster popularization of Georgian wine on the International market.

A joint conference was organized in Tbilisi by the Georgian National museum and Georgian Chamber of Commerce and Industry on November 30, 2006. The topic of the subject of the conference was Georgian Wine Export: Opportunities and perspectives. The conference focused on themes important for the increase of Georgian wine export and diversification of export markets. The main message of the conference was that numerous efforts have to be done to modernize the image of Georgian wine. To this point it is no more enough to rely on only active slogan, like: "Georgia is the cradle of wine".

The issue of Georgian wine has been addressed at the America-Georgia business council 9th forum on December 5, 2006. The problem of Georgian wine in American market still remains the faked Georgian wines, which creates obstacles for promotion campaign. Hence, the advertising campaign has selective nature and relied on doing promotion exclusively for particular brands: Elian, Marana, and Oblivion. The number of export of Georgian wines in US in 2006 will be apparently 0, 4-0, 5 mln bottles.²³

The fact that certain novelties were registered in respect to wine-making in the academic sphere as well is also of interest. Namely, Wine Mastership Program has been presented at the Georgian-American University which will allow managers to enrich wine-making traditional teaching in Georgia with new Western technologies and knowledge.

Information on formation of Georgian Wine Information Agency in Georgia also gives basis for optimism. Georgian Wine Information Agency will be formed by initiative of the Sommelier Association of Georgia. Information on wines produced in Georgia will be collected on a special site and any interested person will have a possibility to introduce oneself to the wine history and origin.

In the current period, the wine companies implemented an attempt of holding fostering campaigns for selling their production at the Western markets by their own forces.

The agreement reached between the Castle Company and Georgian companies "Teliani Valley" and "Telavi Wine Cellar" is very interesting in this aspect. According to the reached agreement

²³ Mamuka Tsereteli- AGBDC Executive Director

the French company takes the responsibility of putting out production of both companies at its selling networks in France and Great Britain. The Castle selling networks comprise 800 shops in Europe.

Same substantial export strategies are carried out by “Kindzmarauli” Company. Its annual production volume composes 5 mln bottles in a year. The Company production is passed to the U.S., Ukraine, Canada, Central Asia and Baltic countries.²⁴

Current year political complications caused unprecedented shock in agriculture in general and particularly in wine production. Difficulties were caused by the fact that such banning occurred on the background of unprecedented increase of the wine export volume over the last two years. Accordingly, important investments were directed towards this sector. Banks had substantially increased their loan portfolio to the wine companies. New vine areas have impressively increased for the last years. Big number of companies implemented investments in the modern Western technologies and equipped factories in completely new ways. Peasant-thrifts were oriented to annual increase of their harvest since the last two year selling tendencies gave basis to their strong optimism. Accordingly, after such a shocking change in the trade environment, the entire circle of wine production became subject to serious risks: peasant- thrifts, wine companies, financial institutions, employment market, etc.

What is the economy reaction on such shock?

Reaction of the wine producing companies on banning was different from the Government reaction in the way that they have really perceived scales of the forthcoming crisis from the very beginning and started their activities for formation of new selling networks at other markets. First attempts were directed towards finding partners at the Ukrainian and Baltic markets, as to them, as to the composing part of the former Soviet Union market, Georgian wine was well known.

The wine companies have purchased less wine for production than planned at this year’s vintage, which is an indicator that last year wine supplies were left unsold.²⁵

Small peasant-thrifts are implanting certain novelties this year. Namely, we are speaking about a big volume of unsold grapes that were pressed out by the peasant-thrifts themselves and certain supplies were formed. Looks like small peasant-thrifts represent a serious segment which will fully occupy specific place – the place of small size enterprises which was completely undeveloped up to date. Supposedly, small thrifts will gradually increase their participation at the wine production market from now and will form as a stabile segment. Along with big companies they will become stabile providers at the wine market. Naturally, they will only supply local market at the starting stage.

Activities organized in Wine sector during 2006 year are numerous:

- *Eye-opener tours in European countries:*
 - to Austria (with 12 sector key-persons).
 - to Porto/ in Port wine region and to Portwine Institute, Portugal (with 14 sector key-persons).

²⁴ Kenchoshvili, CEO Kindzmarauli

²⁵ See Annexes, Table 3.

➤ *Participation in Fairs:*

- ✓ Participation with the “Georgian Wine Family” at sweet wine fair VINOBLE held in Jerez de la Frontera(to promote Georgian quality semi sweet and sweet wines).
- ✓ ExpoGeorgia at ProWein Fair, Düsseldorf (support incl. cross-promotion was given for Georgian

➤ *Promotion activities:*

- ✓ Production of Promotion material (movies) and placement in German TV
- ✓ Production of basic photo material of Georgian autochthon grape varieties for promotional material and for fair participations
- ✓ Active participation and support of organisation of sector roundtables and donor meetings regarding wine marketing and strategy
- ✓ Organization of tasting events and support in competence building for sector representatives, for Young Wine Makers and other unions in the sector

➤ *Advisory activities:*

- Experts advise given by 3 short-term advisers for the sector and regarding pilots in Racha, Adjara and Swaneti (mountainous wine trekking route) incl. development support for marketing and media concepts
- Advise to EXPOGEORGIA JSC, Tbilisi, for preparation of 1. International Wine & Spirits Fair in 2007

➤ *Diverse support activities*

- ✓ Support in foundation and in organization development of “Georgian Wine Family” Union was given
- ✓ Design and establishment of new sector BDS with a GTZ Competence Centre of Vine, Wine marketing & Wine tourism in kind & cash

In general, the assistance carried out by GTZ in 2006 ensured the reinforcement of Capacity Building process of wine companies in Georgia. Aforementioned participation provided excellent opportunity for wine sector to perform industry perfection and support to business entities to be familiar with the international standards.

The following Conclusions and Recommendation are revealed:

Efforts of the Government and partner donor organizations should be mobilized towards gradual formation of high-quality small peasant-thrifts wine production. This segment should be mobilized for gradual implementation of the quality management, marketing improvement, formation and realization of export strategy. Today small thrifts are the segment which has a real perspective as at the inner so at the external markets in the future. Huge experience, that the Western European wine exporting countries possess in this direction should be studied and applied to the Georgian reality.

Companies are forced to find Russia's alternative and form a serious strategy for mastering of new markets. Private companies can not afford this independently at present. European and the U.S. markets are particularly interesting as potential markets for Georgian wine and water. In case of appropriate action it will be possible to get much more income in 5 – 8 years than we had it from Russia beforehand. The country marketing should be held in Europe and America for this which will increase Georgia's recognizability in consciousness of the European and American Society. It should be noted that Armenia has already started such country recognizability marketing and the global world can get this advertising information through CNN.

As American wine market specifics indicate, such campaigns are always held after special support at the State level. Australia, Chile, Austria and even France spend huge amounts for marketing of their wines at the U.S. market. Aforementioned is implemented within the State program frames.

Tourism

On 25 June, 2006 the President announced about the “Presidential Program for Tourism Infrastructure Development”, according to which annually 2.5 million tourists should be attracted to the resorts of Georgia. During the meeting of Regional Governors it was discussed in detail, what had been already done in the regions in order to attract tourists. At the initial stage two tourist schools will be established in Tbilisi and Kobuleti to prepare qualified staff, which will work at the hotels and restaurants.²⁶ Later another school will be opened in Borjomi. The President also admitted that arranging tourist infrastructure in historic and cultural centers is the second part of the Presidential Program. According to him TV advertisements will be broadcasted about Georgia by both CNN and Euronews.

During January-June of the current year the number of the tourists having arrived to Georgia made up 294 209, which is 38 % more than the index of the same period for the previous year.²⁷ Most of the tourists, 189 935 persons, i.e. 64% of the total number are tourists from the CIS countries. Among them 67 879 are from Armenia, 65 000 – Azeri and 46 897 – tourists from Russia. The number of European tourists was 91 436, among them 62 642 – from Turkey. Especially grew the stream of tourists in Ajara. During January-August the number of local holiday-makers in Ajara made up 106 500, while the number of foreigners was 50 500. The number of guests from Armenia made up 37 870. A certain kind of revival can also be observed at the resorts of Shovi and Tskhaltubo, where the main stream of the holiday-makers is formed on the account of internal tourism.

Together with the Organization for World Tourism, UNDP and other donors a Master Plan will be prepared for development of tourism in Georgia. In this plan priority will be given to

²⁶ The President of Georgia M. Saakashvili, 25 June, 2006.

²⁷ Saba Kiknadze, Director of the Department for Tourism.

development of the resorts of Bakuriani and Gudauri. Also, a project on protection of the sanitary zone of Tskhaltubo will be prepared.

Establishing of the Tourist Information Centre in Telavi is one of the most interesting events. The Centre has been established within the framework of the joint project of the local administration of Kakheti Region and Department of Tourism. The task of the centre is provision of the tourists visiting Kakheti with information about the local cultural and geographic potential. According to the statement made by the Department of tourism a similar Centre will be soon launched in Mtskheta too.

What is the real picture like, which does not take into consideration the pathos of official propaganda?

Nowadays tourism is being developed only in three points. They are: Tbilisi, Adjara and mountainous winter resorts. The weak sides of tourism industry still remain to be low standard management and the insufficiency of skills of the human resources.

There are quite serious problems in the sphere of hotel business. Certification of the hotels by stars is carried out in a wrong way. Nowadays there are standards equivalent to the European ones, although they have no legal power, having only the status of instructions. Non-existence of certifying body and often wrong estimation of the hotels by private certifying companies is also a big problem. Tax Code for this sphere should be improved. Such “legal gaps” are often well used by the owners of the hotels. Nowadays the Department for Tourism is working on a special questionnaire. There will be 200 questions to be answered by the representatives of all those hotels, who wish to get stars or to add to those already received before. The answers will be checked by so called “Mr. Guest” technology, therefore, there will be no point in cheating.

There is a certain deficit of decent hotels in Georgia, which will be partially balanced by the following projects:

- ✓ Former Hotel Iveria – Silk Road Group
- ✓ Former Hotel Ajara – Acore
- ✓ Intercontinental in the former building of the Ministry of Agriculture
- ✓ Former Restaurant Aragvi – Hyatt.

Nowadays there are 3 five-star hotels and approximately 80 other hotels in Tbilisi. There were about 10 000 rooms²⁸ in the country last year. According to the standards, the house that has at least 10 rooms can be called a hotel, while the one with less than 10 rooms is a “guest house”.

From the investments in tourism sector we have to underline the following:

- ✓ Kazakh investments in 22 hotels in Ajara, Likani healing resort complex and Gudauri “Marco Polo”
- ✓ Turkish investments in Batumi “Intourist”

In order to realize various tourist resources a long term marketing strategy is needed, which does not exist in Georgia today. Certain initial activities have been carried out from the marketing standpoint, although of a low significance. Despite the problems existing in Georgia and conflict zones, according to the estimation of the specialists, it is possible to soon increase a tourism stream. Croatia is a good example to prove the above mentioned. Despite the tense situation in Balkans the stream of tourists in Croatia increased 6 times within 2-3 years. The legislative basis needs to be perfected as the law today is very general and is not relevant to regulate the sphere. It

²⁸ G. Kupradze, Deputy Director of the Department for Tourism

cannot attract the stream of investments. We are far behind the Black Sea neighboring countries in the sphere of tourism. They are developing very seriously due to long-term strategies which they have elaborated before starting expansion of Tourism industries in their respective countries.

Observations carried out in the sphere of tourism are revealing a wide range of problems:

- *Lack of relevant registration system*
- *Heavy sanitary and hygienic situation at the resorts*
- *Collapsed system of communications and transport*

Development of tourism industry in Georgia requires:

- *Creation of special investment legislation for tourism*
- *Reforms in auxiliary spheres of tourism*
- *Establishing of the standardizing system for the hotels*
- *Creation of a new educational standard oriented on modern services*
- *Creation of high level tourist schools, on the levels of both professional and high schools*

Following recommendations can be provided:

The lack of long-term vision in tourism sectors hinders to make Georgia as attractive area for small and medium scale investors. It will be impossible to build competitive industry without having Long-term Strategy of Tourism Development. The Strategic document should reflect the development concepts for both small-medium and large businesses. It is of vital importance for Government to conceptualize the general vision of transforming the tourism industry into competitive one. It should be avoided to rely exclusively on Government vision while drafting the concept. The knowledge and experience of International donor institutions alongside with private and non-governmental organizations is a matter of high significance.

- ✓ *It is necessary to create a perfect data base about tourism potential of Georgia. There is no full information base in the country about the tourist potential of Georgia, which would describe resorts existing in Georgia with their attractions.*
- ✓ *Parallel to the growth of tourist streams the requirement on competent personnel should be satisfied. It should be mentioned that most of the high educational institutions existing in Georgia prepare tourism specialists, but there are no schools specialized in tourism, that would be oriented on preparation of middle and junior level personnel, on which there is a real requirement in Georgia.*
- ✓ *The campaign to advertise widely cultural and historic monuments existing in the regions.*
- ✓ *It is necessary to prepare competitive unique tourist products and professionally present them to the customer. Under innovative products is meant development of “family” tourism, ecotourism, business tourism, adventure and cognitive tourism.*
- ✓ *It is absolutely necessary to arrange a good availability of communication systems – global distributor systems and internet technologies.*
- ✓ *The main objective for development of tourism industry at the given stage is mobilization of small and medium-scale ventures and assist them to run tourist business. Such strategy will enable us to neutralize the difficult social background existing in Georgia today and to activate such significant economic sector for Georgia as tourism.*
- ✓ *Serious support to small and medium-scale tourist business should be considered as a strategic objective of both economic and social policy of the country. The support should cover taxation (especially for mountainous regions), preparation of technological and human resources, as well as availability of financial resources.*

- ✓ *“The policy of maximal support”, providing full legalization of the tourist business and eradication of shadow tourism, should be worked out.*

Numerous activities are performed in Tourism sector during 2006 year:

Financial support/ subsidy of new private tourism school, Batumi (IBDIPC, ICTSE)

The Project activities to provide assistance in organizing adequate vocational system have huge importance. The shortage in qualified personnel harms the quality of hospitality industry throughout Georgia. Project involvement in short-term vocational programmed in Adjara made it successful.

Following courses were delivered to students:

- ✓ Hotel administration and management
- ✓ Restaurant Service Management
- ✓ Tour firm management

After completion of courses students acquired necessary theoretical knowledge and practical skills. The project has facilitated the development of human capacity in Adjara and provided the opportunity for people working already in hospitality and service sector to improve their qualification and achieve high quality service. In the frame of the programmed 22 students did their internship at different five stars hotels in Antalya, Turkey. The internship has given them an opportunity to make them familiar with high quality service standards and to get a chance to develop the skills necessary to be successful in hospitality sector.

Pilot project for Black Sea tourism statistics with Business School Batumi

The project helped to recognize major tendencies of summer tourism season in Adjara. Research made comprehensible the dominant tendencies like the most of the interest comes to the Republic of Armenia and therefore, to develop international tourism industry, there must be included the East-side countries, particularly Azerbaijan and middle Asia Countries. Project results specified several major tendencies of seasonal market which was not known before.

The importance of the mentioned project is high as analogous researches have not been conducted since Soviet era. Therefore, initiated project gave additional impulse to advance slow track tourism governance practice and pay particular attention to hidden aspects of the industry development.

Among successful steps done within the industry we may state the following activities in 2006:

- ✓ *General public-private dialogue support via project partners at all levels*
- ✓ *Support & participation in Kvirikoba festival, Zemo Swaneti*
- ✓ *Support to rural tourism Association MERIDIAN, Kvareli*
- ✓ *Support for 4 Georgian tourism students in travel&accomodation (Innsbruck,Götebourg)*
- ✓ *Participation and support to 1. orientation workshop of Department of tourism&resorts*
- ✓ *Subsidy to produce a English-Georgian Explanatory dictionary of tourism terms*
- ✓ *Advice and subsidy to new founded “Georgian Tourism Association”*
- ✓ *support to Georgias ITB 2006 press conference (Wilde&Partner, Munich)*
- ✓ *International press & media work /crossover promotion wine&tourism*
- ✓ *designing wine tourism projects and projects with Women’s Initiatives Supporting Group in Adjara*

Media and reflection on politics

The Georgian media sector portrays the landscape of Georgian political market. All developments in the political scene has immediate ricochet at media infrastructure.. Actually following companies are dominating on TV market:

- ✓ Rustavi2
- ✓ Imedi
- ✓ Mze
- ✓ Public Broadcaster
- ✓

Each TV Company is linked with influential political cluster, hence the tension between political groups immediately affects on the strategy of TV companies. By change in ownership of TV companies we may consider the possible scenario of developments in political landscape:

Rustavi2

Rustavi 2 television was established ten years ago in the provincial town of Rustavi, near Tbilisi. Over the last decade it has grown into one of Georgia's leading television companies. Rustavi 2 played a prominent role in the November 2003 bloodless revolution by supporting then-opposition leaders against ex-President Shevardnadze's regime

Imedi

Imedi television is among three leading Georgian national broadcasters. The two others are Rustavi 2 TV and the Public Broadcaster, uniting the first and second TV channels and a radio station. News Corporation under ownership of Rupert Murdoch has purchased shares of the Georgian media holding company Imedi, which unites the Tbilisi-based television and radio stations owned by tycoon Badri Patarkatsishvili²⁹. Deal between Imedi TV and News Corp is of "unprecedented importance" for the Georgian media market.³⁰

Public Broadcaster

The Public Broadcaster, which is a successor of the State TV and Radio Company, is still in transition and can hardly compete with Imedi and Rustavi 2.

Advertising market

Since the advertising market is developing, it becomes more and more attractive for global advertising companies. The market itself was growing very fast till 1998, then there was stagnation in 2002-2003, the annual growth was 10-15%. Over the last several years annual growth became 30%. Among outdoor advertising agencies "I see" and "Alma Plus" is named. So called media inflation (annual growth of advertising prices) is influenced by many factors, but most important is the growth of sales volume in the national economy and consequently the

²⁹ TV Imedi, April 29, 2006

³⁰ RFE, Ia Antadze, Political Analyst

augmentation of advertising budgets. This year the Georgian TV advertising market has grown 35%.

Printing media

*Printed media is undergoing less synchronized clashes compared to TV market. In this regard it's of vital importance to assist in **diversification of printing market**. New partnerships and commercial cooperation with foreign companies will streamline the autonomy of newspapers and printing industry companies. Consequently, the initiatives have to be addressed to establish commercial relationship between Georgian and **foreign companies**, that will bring effect to future growth and efficiency of media sector in Georgia. The attempt of intensification or cooperation with international partners will have twofold importance: to modernize their technologic capacities and strengthen independent media business structures vital for emerging Georgian Democracy*

Judiciary

Major factors affecting this system have negative impact on business climate and cause substantial deterioration of conditions for entrepreneurship. The progress already achieved in the judiciary system is that no complaints are fixed in regards to bribery. But the entrepreneurial community faces other kind of obstacles like it is the "Telephone based judiciary". The essence of the mentioned practice is based on the suppression performed by high-ranked officials which is done by phone calls. In fact it is impossible to win civil court case against the Government. Local or central level authorities in different structures are capable to "influence" over the decision of court if the dispute concerns Governmental interests.

Relations with International and donor institutions

Georgia has a special role in the neighborly policy of the EU. At the present stage relations between EU and Georgia are regulated by the Partnership and Cooperation Agreement (PCA). PCA was signed in 1996. It came into effect on the 1st of July, 1999 and is in action for 10 years with the possibility of the further extension. The aim of this agreement is to extend political, economical and cultural relations between European Union and Georgia.

Partnership and Cooperation Agreement is giving wide opportunities of cooperation and assists development of market economics in Georgia, an export of the Georgian production in EU market, drawing of European investments, introduction of international norms and standards in agriculture, education and energetic, as well as the establishment of law supremacy, inclusion of Georgia into the European transport and communication networks and others.

EU assistance programmes:

- ✓ Technical Assistance to the Commonwealth of the Independent States - TACIS
- ✓ South Caucasus Anti Drug Programmed - SCAD
- ✓ Food Security Programme - FSP
- ✓ Exceptional Financial Assistance - EFA
- ✓ European Initiative for Democracy and Human Rights - EIDHR
- ✓ European Experts Special Mission in Georgia "EUJUST THEMIS" and European Union Special Representative's Office in the South Caucasus- EUSR)

- ✓ Rehabilitation Programme - RP for Conflict Incurred Regions
- ✓ Decentralised Cooperation
- ✓ European Commission Humanitarian Office – ECHO

Along with the above mentioned programmes there were being carried out projects envisaged by the programme of Rapid Reaction Mechanism - RRM, that were completed in 2005.

At this stage important works have been done in relation to bringing the Georgian legislation near the European legislation. The most important laws have been adopted in the spheres of taxation, energetic, agriculture, protection of intellectual property and education.

Negotiations have been started for the Action Plan of the EU neighborly policy (ENP AP). EU shared approaches connected with priorities of the Georgian party.

Neighborly policy of European Union (ENP)

“Neighborly policy of European Union” is a political policy of the European Union, the aim of which is starting a process of political, economical and cultural approximation between EU and its “friends’ zone” instead of appearing new boundaries between them.

In spite of the fact that ENP is not directly connected with extension of EU it is an important means for favoring deepening of current integration processes in Europe and approaching political, economical and cultural processes of European countries. The most important thing for us is that a strategic document of ENP envisages an active participation in resolving conflicts existing in Georgia.

The priorities of the Georgian government for the Action Plan ENP are the following:

- ✓ Supporting in resolving conflicts;
- ✓ Strengthening of supremacy of law;
- ✓ Strengthening of safety and stability;
- ✓ Economical development and four freedom;
- ✓ Rehabilitation of an infrastructure;
- ✓ Education and science;
- ✓ Regional cooperation (considering cooperation in the region of the Black Sea).

Georgia became a member of ENP in June, 2004 and on the 29th of September 2004 the European Commission adopted a project of regulations connected with the European neighborly and partnership instruments, the mechanism of which will be more elastic, with opportunities of serious investment components and simplified administration methods. From the 1st of January, 2007 Georgia will receive the assistance within the above mentioned instrument. From 2007 the European assistance will be carried out by means of the following instruments:

Geographic (basic) instruments:

- ✓ European Neighborly and Partnership Instrument - ENPI (new neighboring countries and Russia);
- ✓ Pre-accession assistance (candidate countries – Turkey, Croatia, potential candidate countries – Balkan countries);

Thematic instruments are the following:

1. Stability instrument;
2. Humanitarian assistance instrument;
3. Macro-financial assistance instrument.

The assistance to Georgia from EU will mainly be carried out within the European Neighborly and Partnership Instrument (ENPI). Though Georgia might also use other appropriate thematic instruments.

The first projects of a strategic document (CSP) and national indicative programmed for 2007-2013 have been received from the European Commission. They have been given to branch ministries for making commentaries. On these documents a financial and technical assistance planned within ENPI will be based. On the background of the current relations with EU a special optimism of the Georgian society was caused by the fact that at the current stage Germany is running a presidential function. This fact has a special positive effect in the Georgian society from the point of view of German-Georgian relations and an attentive attitude of the German government towards Georgia that will help Georgia to improve and meet commitments before the EU.

The grounds for the optimism are given by the fact that the governmental negotiations between Georgia and Federal Republic of German were organized in September 1-22. There was discussed a current status of investment and technical assistance projects financed by the support of Germany, as well as the future plans of financial and technical assistance of Germany.

GSP+ system

The European Union in all spheres of economic activities has given to Georgia at least a most favored nation treatment, and in separate spheres - a national treatment. For Georgia as the countries with transitive economy, crucial importance has an opportunity to use the Generalized System of Preference (GSP), providing a preferential tariff mode for production imported from Georgia.

Currently preferential mode GSP, to Georgia was given by the European Union, the USA, Canada, Japan, Turkey and Switzerland. In 2005 EU, and since January 2006 Turkey was given to Georgia the expanded opportunity of use of tariff privileges (GSP+), that consists in granting a mode without duties on import of 7200 names of production. Since January 2006 Georgia enjoys the preferences of the GSP+ in its trade with the EU. This means that from 2006 to 2008 Georgia can export duty free almost all goods except for arms and ammunition and some agricultural goods to the EU. GSP+ covers 7200 goods to which another 2100 goods from the MFN with zero duty rates has to be added. These are 9300 duty free products out of about 10000 tariff lines of the EU Common Customs Code. If products, as e.g. wine (some type of wine are included in the GSP+ scheme), attract both an ad valorem duty and an ad quantum duty the nil rate will apply to the ad valorem duty only while the full amount of the ad quantum duty will still be payable. The application of GSP+ is conditional on firstly the ratification and application of 27 key international conventions and, secondly, on the existence of a poorly diversified economy, which means that the five largest sections of its GSP-covered imports to EU must represent more than 75 percent of total GSP covered

On the whole the support from EU is particularly important for Georgia from the point of view of development of the country. From the political point of view it is also remarkable to note that on the 3rd of October EU made an appeal to Russia to annul an economical blockade in relation to Georgia. At the same time EU is planning to conclude an agreement on free trade with Georgia. In the opinion of the Ministry of Economics the agreement on free trade will bring stability to Georgian economics and accelerate the economical growth³¹. According to the president's economic adviser, the former prime-minister of Estonia, Mart Laari, by performing

³¹Irakli Chogovadze, minister of economic development

the agreement on free trade with the countries of the European Union Georgian export industry will be favored and the export structure of the country will also be improved³².

NATO

The integration of Georgia into the North-Atlantic Alliance is announced as a main priority of foreign and safety policy of Georgia. At present relations of Georgia with the NATO is regulated by the Action Plan of the Individual Partnership (IPAP). This document is a list of reforms worked out by Georgia and the NATO, the commitments of which Georgia has taken to fulfill till the end of 2006. Officially IPAP is not a stage of becoming a member, but its successful fulfillment considerably defines integration perspectives of Georgia into the NATO.

On the 21st of September, 2006, in the headquarters of the United Nations, in New York, at the meeting of Ministers for Foreign Affairs of the NATO the Alliance announced its decision about starting an intensive dialogue with Georgia on becoming a member of the NATO.

Starting the intensified dialogue with Georgia is the first step taken from a partnership format to a membership candidate format. The intensified dialogue is a mutual cooperation mechanism between the Alliance and Georgia, the main object of which is to prepare a ground for transition to the Membership phase of the Action Plan (MAP). By the format of the intensified dialogue Georgia continues carrying out reforms in military, political, economical, and social and administration spheres and will permanently submit the NATO the results of carrying out the above mentioned reforms. Notes and recommendations of the NATO will be taken into account in the process of carrying out the reforms so that to achieve the compliance of the progress with NATO criteria.

What does a stage of an intensified dialogue mean for Georgia?

The cooperation in the format of the intensified dialogue with the NATO unambiguously expresses a successful development of the integration process of Georgia into the NATO and increasing the quality of the cooperation. The intensified dialogue includes political, military, financial and safety issues. The cooperation in this format will help Georgia to pass to the stage following the integration process, which is the phase of the Membership Action Plan (MAP) that is a mandatory pre-condition of the Alliance membership. MAP is perceived by the Alliance as a final stage of the cooperation with a candidate country before the membership. In the intensified dialogue format the country makes agreement with the Alliance on all the points, which it will have to work on while implementing MAP. So the intensified dialogue is the most significant preparatory stage towards the Membership Action Plan and finally achieving a status of a member.

This time, as always, the main question in the Georgian society is: what kind of reaction there will be from Russia, the main political opponent of Georgia, in relation to transferring to the phase of the intensified dialogue (ID) of Georgia-NATO relations?

Transferring to this stage confirms that democratic states of the West are supporting the course taken by Georgia. They acknowledge Euro-Atlantic intentions of Georgia and express their readiness to help with building a strong state of Georgia, based on democratic values. *As it is seen from practice, despite the general negative attitude the step taken to the membership of the NATO makes Russia more constructive in dual relations with these countries. After assigning a candidate and then a member status to a country Russia is conducting more restrained and*

³² Information Agency, October 27, 2006.

elastic policy to this country. There is an opinion among the Georgian society that approaching of Georgia to the NATO will make Russian policy towards Georgia more prognostic than the present policy from Russia.

As for the actions at the present stage Russia is extremely trying to compromise the Georgian attitude and abilities in relations with NATO. For example, in the middle of October Russian media was maximally repeating a phrase, said by one of the representatives of the NATO during his visit in Moscow: “Georgia is far from the NATO”³³. They were also mentioning a statement of the same author, that the NATO would not lead forces in Abkhazia and Oseti. Accordingly in the Russian government there was made a commentary that Georgia should be careful with Russia³⁴.

A very important act for supporting Georgia in approaching to the NATO is the decision taken by the U.S. Senate on supporting the joining Albania, Croatia, Georgia and Macedonia to the NATO³⁵. This decision was made a few weeks before the summit of the NATO. According to the representative of the Senate Washington will attempt to convince member countries of the NATO to support the proposal for membership of Albania, Croatia, Georgia and Macedonia³⁶.

Definitely, a NATO Riga summit declaration has reaffirmed that alliance member states will continue the Intensified Dialogue with Georgia and will encourage the Georgian authorities to continue in its reform process.

*Official statement announced that the Alliance will continue with Georgia and Ukraine its Intensified Dialogues which cover the full range of political, military, financial, and security issues relating to those countries’ aspirations to membership, without prejudice to any eventual Alliance decision.*³⁷

It was welcomed the commencement of an Intensified Dialogue with Georgia as well as Georgia’s contribution to international peacekeeping and security operations. It has been stated that member countries will continue to engage actively with Georgia in support of its reform process. They encourage Georgia to continue progress on political, economic and military reforms, including strengthening judicial reform, as well as the peaceful resolution of outstanding conflicts on its territory. It was reaffirmed that it is of great importance that all parties in the region should engage constructively to promote regional peace and stability.

The declaration announced at a news conference after the summit that the alliance has encouraged Georgia, “which made a tremendous efforts” on its way of reforms.³⁸

Donor activities of UN and other international institutions

UNDP along with the Georgian government has identified several areas for targeted assistance. The projects are pro-poor, pro-women, and environmentally sustainable. They are directed toward the following areas:

Democratic Governance

³³ Ray Eno, leader of the NATO Military Commission, October 16, 2006.

³⁴ Minister for Foreign Affairs of Russia

³⁵ U.S. Senate, November 16, 2006

³⁶ Richard Lugar, U.S. Senate member

³⁷ Riga Summit declaration, meeting of the North Atlantic Council, 29 November, 2006.

³⁸ Latvian President Vaira Vike-Freiberga

Governance is the largest recipient of UNDP resources. UNDP assists Georgia in overcoming governance challenges in the judiciary, legislative and executive branches. UNDP has developed projects for improving the governance system in the country including the assistance to the Public Service Bureau, largely responsible for public administration reform matters. The assistance was provided to individual ministries and other key public administration institutions with an aim to improve their capacity. The assistance is also provided to:

- Parliament of Georgia
- Public Defender's Office thereby improving the situation within the field of Human Rights and
- Chamber of Control to be able to exercise effective financial control thereby further reducing the corruption.
- Constitutional Court of Georgia thereby trying to help striking the right balance within the general governance system of the country.

Environmental Conservation and Management

The UNDP has implemented environmental projects - aimed at increasing public awareness and assisting the delicate process of environmental management at the Ministry of Environment. In addition it seeks to develop innovative energy related and environmental conservation projects - such as the renewable energy initiatives, the conservation of biological resources and others.

Poverty Reduction

Poverty is the main concern of the majority of Georgia's citizens - with all the implications on social and economic growth. The UNDP is dedicated to reducing the poverty levels and promoting economic growth right across Georgia. UNDP has assisted the Government in planning its Economic Development and Poverty Reduction Program. Its effective implementation will be crucial to reach the Millennium Development Goals, to which Georgia committed itself.

In this regard particular interest is given to 5 year compact of Government of Georgia with the Millennium Challenge Corporation (MCC, USA). The overall objective of this Compact is increased economic growth and poverty reduction in the regions of Georgia outside of Tbilisi , which is key to economic growth and poverty reduction in Georgia . The grant amount of **Millennium Challenge Georgia** (MCG) Program reaches USD 295, 3 mln prescribed to following projects:

Component 1: Regional Infrastructure Rehabilitation Project – USD 211, 7 mln:

Project 1: Samtskhe-Javakheti Road Project – USD 102, 2 mln

Project 2: Energy Rehabilitation Project – USD 49, 5 mln

Project 3: Regional Infrastructure Development project – USD 60 mln

Component 2: Enterprise development Project

Project 1: Investment Fund –USD 32, 5 mln

Project 2: Agribusiness development - USD 15, 0 mln

Numerous donations have been announced by respective Governments recently:

- Japan grant to “Georgian Railways” ltd., will finance the study of technical-economic capacities and present status of railway network. The grant was allocated by the Ministry of economy, trade and Industry of Japan on the basis of request of “Georgian Railways”.

Japan consulting firm PCI jointly with specialized agency of “Georgian Railways” will conduct study of technical-economic condition of the railway infrastructure.

- According to agreement signed on April 11 2006 between Georgia and China, the latter will allocate grant of USD 2, 5 man., to provide assistance to Ministry of Finances of Georgia.
- It was announced that Germany is to allocate 27 million Euro to Georgia for investments and technical projects.³⁹ The sum will be allocated to several projects. Specifically, 14 million Euros will be spent to develop and rehabilitate Batumi infrastructure (water supply system and sewerage); 4 million Euros will be allocated to Georgian commercial banks for using it as a credit resource; 2 million Euro will be delivered to “The Fund of Education and Experts”, within which technical and economic research and consulting services will be financed. Apart from this three winemaking projects will be financed with the funds. German financial assistance to Georgia during 1995-2005 amounts to 250 million Euro.⁴⁰
- The Department of Statistics in cooperation with UNDP signed an eight month project agreement on November 8 to gain an accurate picture of the size and scope of the shadow economy in Georgia. The project “Capacity Building for the Department of statistics for Obtaining Accurate estimates of the informal economy” will provide support to better measure the size and scope of the shadow economy using at least two internationally acknowledged methodologies, as well conduct surveys in sectors of the economy. The size of the project is USD 122 500. The project will also create an Analytical and Policy Recommendation Report, offering specific recommendations to policy makers about how to encourage the transition of informal workers into the formal economy.

Besides GTZ projects (“Support of establishment of the Regulatory Body of Wine and Wine Quality System in Georgia” and “Support to increase the qualification, education in Agricultural and Regional Development sector in the South Caucasus”) a number of other projects are in the phase of implementation within the Ministry of Agriculture and food:

- ✓ World Bank
- ✓ Environmental Management Plan of the Project on the control of Avian Influenza, pandemic and readiness for efficient reaction on it.
- ✓ Rural development Project – WB.
- ✓ EU-TACIS Project – Increase of financial management capacity within the Ministry of Agriculture
- ✓ Swedish Support to the Milk and Dairy Sector in Georgia, Swedish International Development Agency – SIDA
- ✓ RDP (World Bank)
- ✓ Agricultural Research-Extension and training Project (ARET)
- ✓ Irrigation and Drainage Community Development Project.
- ✓ World Food Program (WFP)
- ✓ AgVANTAGE
- ✓ Integrated Poverty Reduction Program in vulnerable rural households in Samtskhe-Javakheti; Social and Marketing Unions in Akhalkalaki.
- ✓ IFAD – Program of the development of Alpine and high Alpine Regions of Georgia International Fund of Agricultural Development.

Tendencies with regard to institutional development of Government

³⁹ Alexi Alexishvili, Finance Minister of Georgia, and Ambassador of Germany to Georgia.

⁴⁰ The Georgian Business Week.

Development of ongoing institutional and personnel changes carried out by the government for the latest period are quite dynamic and therefore - unpredictable. During the last two years institutional transformation initiated by the government was carried out nearly at all ministries and organizations subordinated to them. The main official reasons why number of ministries are being cut are as follows:

- ✓ Incapable and too centralized structures
- ✓ A huge number of civil servants inherited by this government from the Communist system

Public opinion about institutional reform of the government is quite critical due to two reasons:

- ✓ Institutional transformation became anti-social and its impact on the population employed in the public sector is very negative with regards to unemployment.
- ✓ Merging of ministries could not make efficiency of their functioning better and in a number of cases they gave even worse results.

One of the latest unsuccessful examples of institutional transformation practice can be the case of taking a decision that the Institute of Viticulture, counting back quite a lot of decades of its activities, has to leave its infrastructure in favor of the Ministry of Agriculture and Food.

The above mentioned Institute has been carrying out very important activities. It had achieved acknowledgement and respect throughout relevant international circles. This is the Institute having worked out concepts on rehabilitation and development of viticulture and fruit-growing, the "Georgian Law on Vine and Wine", new technologies, innovative proposals etc. The Institute has been working on identifying specific zones of viticulture. The aim of the program is to legally protect Georgian names of the wines, prevent means of forging wines and improve quality and authority of Georgian wines on international markets. The Institute has also been dealing with rehabilitation and maintenance of gene pool of species of vine and fruit-trees, cultivation of selection plots, providing intensive technologies for production of seedlings of both vine and fruit-trees, investigation of medical and nutritional values of Georgian wine and fruit, etc.

On the background of the decisions made by the government with regard to eviction of the institute, all priority scientific research activities are decreased.

The government is also planning a liquidation of the Research Institute of Economics. Institute financing is not envisaged in the project⁴¹ of the budget for 2007. According to the official position, functioning of the Institute is no more needed for development of the economic system of Georgia. Functions, related to economic analysis and necessary for the Ministry of Economic Development, are carried out by the Department of Economic Policy.

A lot of uncertainties are generated due to Government's recent initiative about creation a new agency by unifying the tax department, customs service and the Financial Police into a new structure - the Revenue Service - under the Finance Ministry⁴².

The proposal is part of an initiative started by President of Georgia, who said in August, 2006 that the authorities should "decriminalize financial relations" between the state and entrepreneurs. The statement was largely perceived as an attempt to cut the powers of the

⁴¹ Ministry of Economic Development

⁴² See Annexes, Slides ## 1,2,3.

influential Financial Police, which opposition lawmakers say is a tool “to terrorize business.” But at the November 24 hearings the draft law proposed by the Finance Ministry was slammed by opposition lawmakers, who said that the new structure with its law enforcer status will not help to decriminalize relations between the state and business.

Opponents to the proposal express fear that the new agency will help the state increase pressure on business. It is expected that by merging these three agencies the new agency will assume more law-enforcement functions. A representative of this agency can use batons, electric shock, dogs, etc against entrepreneurs. If the bill will be approved as it is, the business will suffer by dealing with a terrible monster dominated by financial police.

Elections

Elections date was announced by the authorities on September 27, which put the election administration under a significant time constraint, and the CEC has not been able to meet some legal deadlines.

October 5 was declared as the official date for local self-governance elections, taking opposition parties by surprise. It was officially announced that elections would be held in early December – a date that was slightly later than the one announced by the President this April.⁴³ News about the setting of October 5 as an elections date released late on August 27, when a press-release was posted on the official web-site saying that President signed a relevant decree on August 26. The decree was signed 40 days before the elections date, as envisaged by the law. According to opposition Parties, it is unacceptable when a decree on setting the date for elections signed on August 26 takes almost two days to become public.⁴⁴ Early December was a comfortable date for the opposition parties, as they thought there was enough time to define their tactics. In August the major opposition parties, which have been engaged in active consultations with each other throughout the summer about the possibility of forming a coalition, even took a pause and decided to resume talks in September. But when October 5 was set as the official election date most opposition politicians voiced their protests, saying that the authorities have left them no time to campaign and have effectively taken away their ability to compete with the ruling party

Tight timeframe of the local self-governance elections scheduled for October 5 triggered major problems during the pre-election period, while inaccuracies in the voter list remains an issue which needs to be addressed, interim reports by local and international observation groups say.

“The CEC failed to address an ambiguity in the Unified Election Code, with regard to the requirement to open campaign funds, in a consistent and a timely manner. As a result, some majoritarian candidates were denied registration. Ultimately, in some local majoritarian districts only one candidate was left on the ballot,⁴⁵”

International observers also note that District Election Commission in some regions were located in the same building as the local executive bodies (Gamgeoba), in other regions, the office of the ruling National Movement party was located in the Gamgeoba building. According to ODIHR report, this contributed to blurring the distinction between the District Election Commissions, the local administration and the ruling party.⁴⁶

⁴³ Giorgi Arveladze, Chief of the President’s Administration

⁴⁴ David Usupashvili, Republican party leader.

⁴⁵ ODIHR’s interim report .(The OSCE Office for Democratic Institutions and Human Rights)

⁴⁶ ODIHR report.

Some opposition parties, including a coalition of Republican and Conservative parties accused the ruling party officials of carrying out “instructions” to the election administration members in number of regions including in Batumi, Adjara Autonomous Republic.

Local observers also note the same problem, but say that unlike in previous years, the CEC is more enthusiastic to cooperate with the election watchdog groups and political parties.

“Despite number of problems there is a progress. There is clear readiness of the CEC and lower level election administrations to cooperate. But few districts remain anyway where election officials totally ignore any cooperation.”⁴⁷

Number of precinct election commissions was not technically well-prepared for elections. Inaccuracies in the voter lists remained another major problem ahead of polls. Officially announced number of voters – 3 201 168 – “constitutes a significant increase over past elections”.⁴⁸

Results of elections

Six political groups competed for a total of 1 736 seats in 69 local municipal councils, or as they are called in Georgian Sakrebulo, throughout Georgia. The number of seats in each Sakrebulo varied from 14 (in Kodori, breakaway Abkhazia, as well as in Eredvi, Kurta and Tigvi in breakaway South Ossetia) to 41 (in Zugdidi, western Georgia) depending on size of the regional municipality. 10 members of the Sakrebulo in all the regional municipalities were elected through a proportional party-list system, while rest of the seats are occupied by those elected through a majoritarian system in each of the village of the regional municipality.

Sakrebulo in major cities – Batumi in the Adjara Autonomous Republic; Rustavi to the south of Tbilisi, Poti and Kutaisi, both in the western Georgia – have 15 seats in the Sakrebulo each. Ten of these were elected through a party-list system, and the remaining 5 members through a majoritarian system; these towns have five single-mandate constituencies each. The newly-elected Sakrebulo in these cities are responsible for electing mayors.

Ruling National Movement party won overwhelming majority of seats all the local council – Sakrebulo throughout Georgia in the October 5 municipal elections. Results in the Abasha constituency in Western Georgia were annulled because of grave violations during the elections day. A total of 68 Sakrebulo (69th is Abasha Sakrebulo) were elected as a result of the October 5 elections.

Media coverage of elections

It was clear a low-key campaign ahead of polls, though then Mayor of Tbilisi was highly visible. Parallel to his election campaign, State and municipal authorities launched highly advertised social aid programmes. There has been only limited visibility of election-related events in the media. Moreover social aid programmes and other activities of the authorities have received extensive coverage. Rustavi 2 television has dedicated 36% and 30% of its political prime time news to the government.. 1st Channel of the Public Television had a similar coverage of the two aforementioned subjects as Rustavi 2 TV. The coverage of the authorities by both channels was

⁴⁷ Koki Ionatamishvili, New Generation-New Initiative (NGNI).

⁴⁸ ODHIR report.

largely neutral or positive in tone. The newspapers offered its readers a more critical approach, though they reach out to only a limited readership due to a relatively low circulation.

Conclusions and Recommendations

The Tourism services and wine export spheres has to be highlighted, with recommendations that more be done to support the responsible national authorities to work toward improving the situation.

The programme should further focus more efforts on linking Wine SME capacities to export oriented practices. Successful efforts in this regard has to be continued - Wine Competence Centre, organized by project may be considered as real implementation of result-oriented innovative thinking for wine industry in Georgia. There should be to provided support to SMEs in Georgia in order to ensure their conformity to more competitive and open trading conditions.

Further actions need to focus to primary objectives:

- ✓ To enhance the capacity of national SME, Tourism and Wine Associations to enable SMEs to enhance their competitiveness in a global market.
- ✓ To promote regional network as a means to reinforce institutional capacity and know-how.

Various SME concepts and methodologies may be initiated:

- ✓ The Product Network
- ✓ Approach benchmarking
- ✓ International Commercial standards introduction
- ✓ Trade Secrets Introduction, etc.

The project need to ensure further persistence in effective engagements related to regional development of Adjara, Kakheti, etc. Swaneti Tourism potential guide, prepared by Project became extremely useful tool for both Government and private sector institutions. Tourism development aspects in the mentioned regions need to be the sphere of utmost concentration of efforts for Project in close future.

Annexes

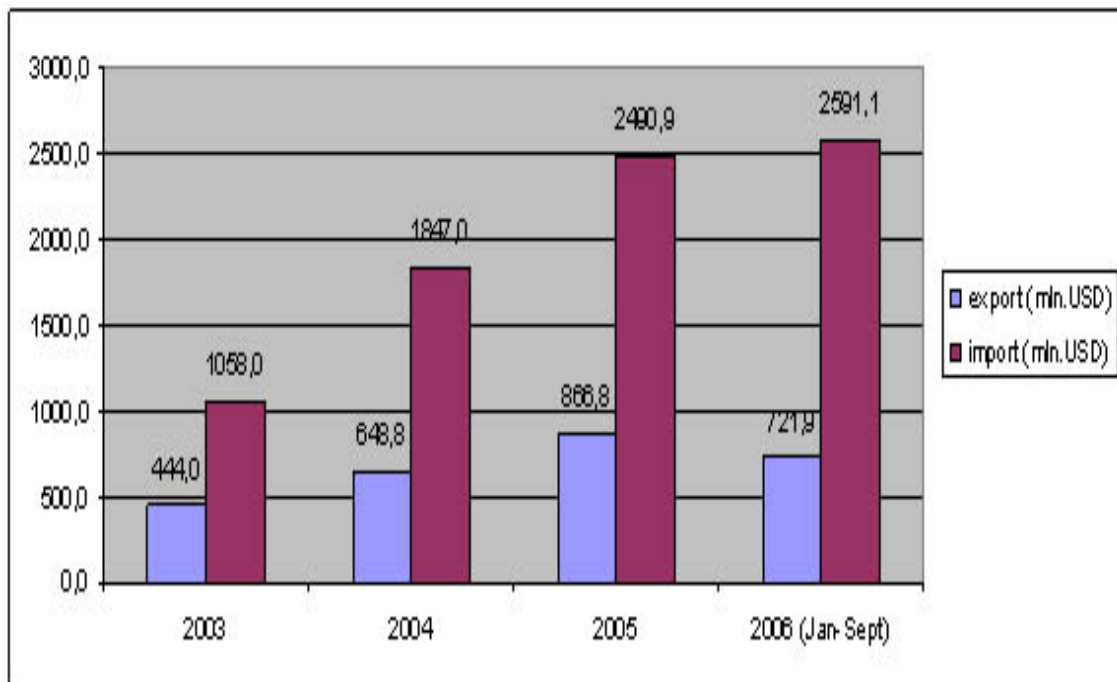
Table #3. Export of Georgian wine, January- September 2006

| Export of Georgian Wine(January-September 2006) | | | | | |
|---|------------------------|-----------|------------|--------------|--|
| | Country | D/Liter | Bottles | Bottles in % | |
| 1 | Russia(till April) | 814. 280 | 10.857.067 | 64% | |
| 2 | Ukraine | 230.549 | 3.073.987 | 18,1% | |
| 3 | Kazakhstan | 84.751 | 1.130.013 | 6,7% | |
| 4 | USA | 30.657 | 408.76 | 2,4% | |
| 5 | Bielorus | 27.281 | 363.747 | 2,1% | |
| 6 | Latvia | 24.918 | 332.24 | 2,0% | |
| 7 | Poland | 15.038 | 200.507 | 1,2% | |
| 8 | Litva | 7.394 | 98.587 | 0,6% | |
| 9 | Estonia | 6.507 | 86.766 | 0,5% | |
| 10 | Israel | 5.844 | 77.92 | 0,5% | |
| 11 | China | 3.258 | 43.44 | 0,3% | |
| 12 | Japan | 2.555 | 34.067 | 0,2% | |
| 13 | Canada | 2.452 | 32.693 | 0,2% | |
| 14 | Germany | 2.101 | 28.013 | 0,2% | |
| 15 | Czeck Republic | 2.021 | 26.947 | 0,2% | |
| 16 | UK | 2.005 | 26.733 | 0,2% | |
| 17 | Cyprus | 1.974 | 26320 | 0,2% | |
| 18 | Belgium | 1.859 | 24.787 | 0,1% | |
| 19 | Azerbaijan | 1.708 | 22.773 | 0,1% | |
| 20 | Tbilisi Aeroport | 789 | 10.52 | 0,1% | |
| 21 | Tadjikistan | 754 | 10.053 | 0,1% | |
| 22 | UAE(Emirates) | 690 | 9.2 | 0,15 | |
| 23 | Netherlands | 574 | 7.653 | 0% | |
| 24 | Moldova | 544 | 7.253 | 0% | |
| 25 | TOTAL | 1.270.503 | 16.940.046 | 100% | |
| | | | | | |
| | Total(Russia excluded) | 456.223 | 6.082.979 | | |
| | Total EU | 64.391 | 858.553 | | |
| | | | | | |
| | Total 2005 | 2.750.360 | 36.671.476 | | |
| | Russia 2005 | 2.407.795 | 36.671.476 | 88% | |

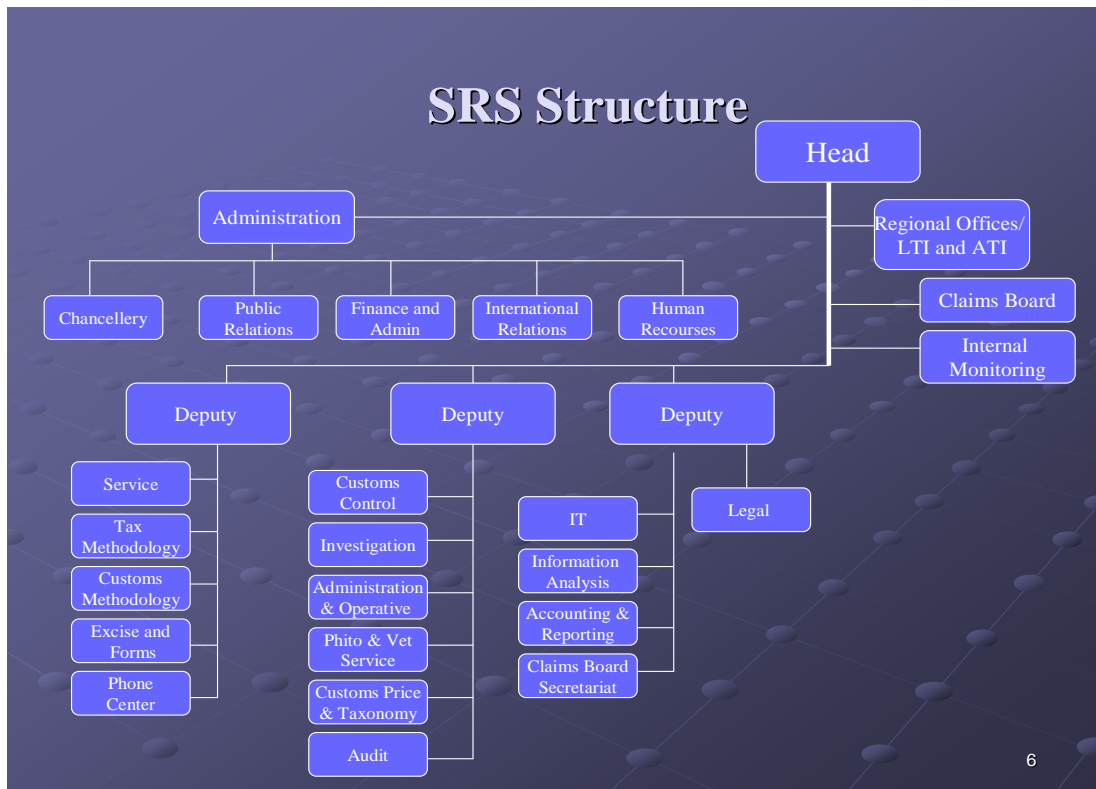
Table 4. Trends in Georgia's Balance in Trade

| | 2003 | 2004 | 2005 | 2006 (Jan-Sept) |
|--------------------------|--------|---------|---------|-----------------|
| export (mln.USD) | 444,0 | 648,8 | 866,8 | 721,9 |
| import (mln.USD) | 1058,0 | 1847,0 | 2490,9 | 2591,1 |
| trade balance (mln.USD) | -614,0 | -1198,2 | -1624,2 | -1869,3 |
| trade turnover (mln.USD) | 1502,0 | 2495,8 | 3357,7 | 3313,0 |
| GDP (mln.USD) | 3948,0 | 5200,0 | 6500,0 | |
| export/GDP | 11,2 | 12,5 | 13,3 | |
| trade/GDP | 38,0 | 48,0 | 51,7 | |
| trade balance/GDP | 15,6 | 23,0 | 25,0 | |

Chart 1: Dynamics of Georgian Exports and Imports (2003-2006)



Slide #1. State Revenues Service Structure model.



Slide #2. Activities for transitional period in State Revenues Service.

