



Why is easy-to-do-business in Georgia?

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Arguments and measurement

- Crucial importance of economic freedom is proven by
 - Logical arguments
 - Austrian and many other economic schools
 - Empirical arguments
 - Economic Freedom of the World (Fraser Institute)
 - Index of Economic Freedom (The heritage Foundation)
 - Easy to do Business (World Bank)
 - International Property Rights Index (Property Rights Alliance)



Data's from EFW: Free is Prosper

- Economically free countries are advanced at all field compared to economically restricted countries
 - Average per-capita GDP: Free \$32443 vs. restricted \$3802
 - Average per-capita economic growth rate: Free 2.4% vs. restricted 0.9%
 - Life expectancy: Free 79 years vs. 59
 - Average score of environmental performance: Free 84.8 out of 100 vs. restricted 64.5
 - Corruption: Free 7.5 out of 10 vs. restricted 2.6
 - Political rights: Free 1.6 out of 7, where 1 is best result vs. restricted 4.4
 - Civil liberties: Free 1.6 out of 7, where 1 is best result vs. restricted 4.1

Major Question

- What is first:
Economic freedom
or prosperity?
 - Freedom is possible
because of
prosperity
 - or
 - Prosperity is possible
because of freedom



My Answer

- Analysis of correlation of Georgia's economic reforms during 2003-2010 with its economic performance shows that freedom is at first place
- Economic freedom leads to general prosperity and political emancipation



2003 - Public opinion for reforms



Reforms = Kakha Bendukidze & Co
+ Political will of new political elite

**When the
student is
ready, the
master appears**

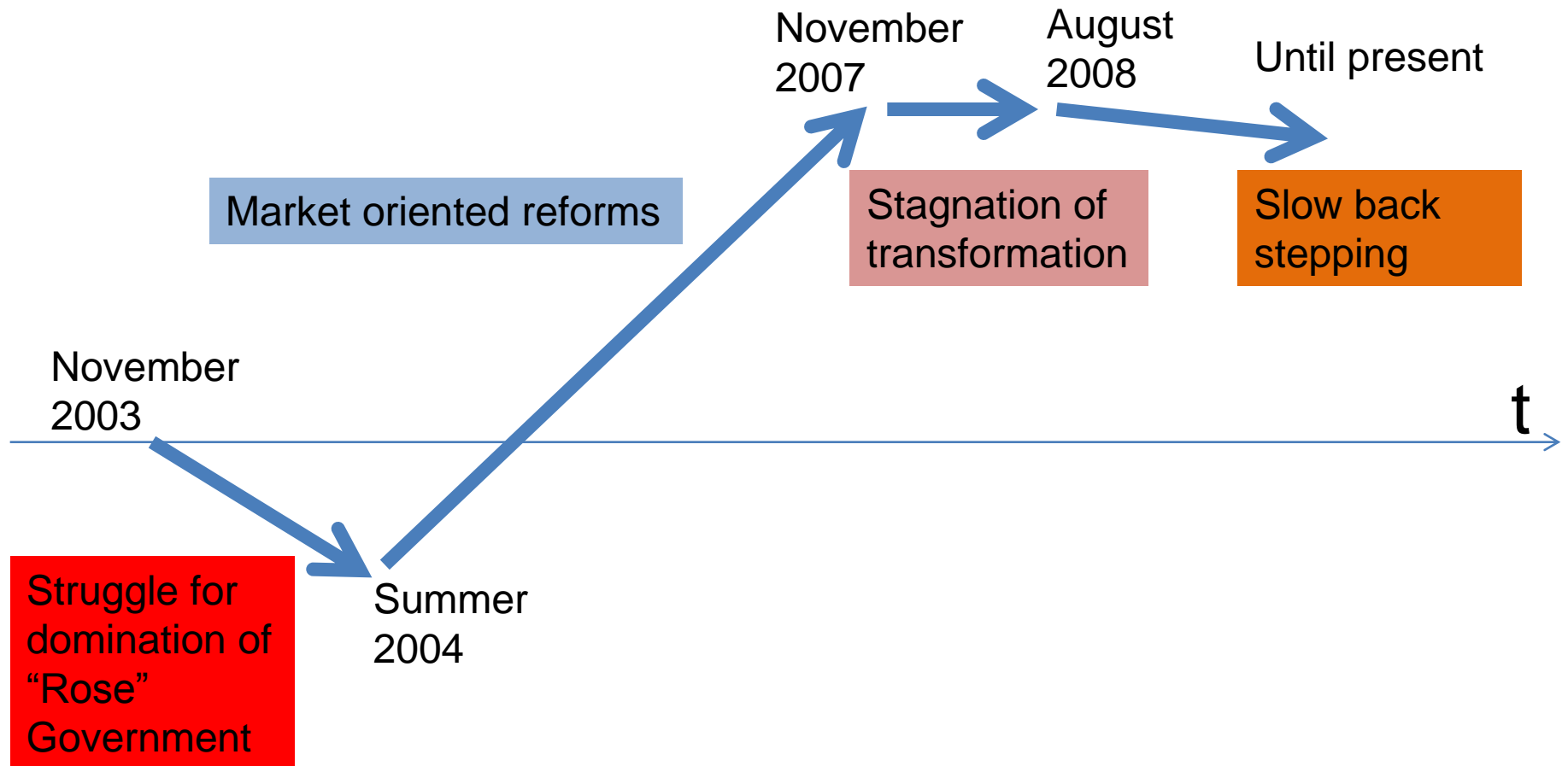


My look: Georgian economic reforms an example of



- Reforms via transformation or removal of governmental institutions
- Economic freedom - welcome

2003-2010: Major Trends of Development



Approach of Government (Since 2004)

- The rule of law & property rights
- Free entrance to the country – No visa
- Minimal state fiscal footprint
 - Few, low and flat taxes
 - Minimal social security burden on businesses
- Sound money
 - Inflation targeting, single-digit inflation
- Free trade, no customs tariffs or non-tariff barriers
- Flexible labor market, with minimal state interference in employer-employee relations
- Limited government
 - Deep de-regulation
 - Dramatically minimized and simplified licensing
 - Aggressive privatization
- Means-tested, focused state assistance to the poor
- Lean and efficient civil service sector – providing value for taxpayers' money

I ♥ CAPITALISM

**GOVERNMENT
is the problem,
Not the solution.**

Freedom of Movement

- No visa fee for most nations
 - Some nations could buy visa at boarder
- Ease to get Georgian citizenship and double citizenship
 - many ministers where and/or are citizens of pothor countries (including Kakha Bendukidze)



Anti-Corruption Strategy

- Public Sector Reform

- ✓ Maximum elimination of unnecessary interactions between public and private sectors
- ✓ Number of line ministries and government agencies dramatically reduced
- ✓ Number of public sector employees reduced by 50%, salaries of civil servants increased

- Education System

- ✓ New system, where merit matters and not payoffs
- ✓ The former school-based admission exams replaced by competitive national testing
- ✓ Finance system restructured -voucher system introduced



- Police Reform

- ✓ All police officers dismissed and recruited through an open competition
- ✓ Salaries were raised ten-fold, training and equipment
- ✓ Transparency



Full Range Privatization

- Monetary privatization, mostly auctioning, on competitive base becomes priority
- Major assets sold or rented out: Poti Port, HPPs, hotels, water and sewage companies, telecommunications, hospitals, forests, lakes, etc.

Capitalism
Creates jobs and wealth

Low-Tax Zone

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

- No payroll tax or social insurance tax
- No capital gains tax
- No wealth tax, inheritance tax or stamp duty
- Foreign-source income of individuals fully exempted
- Tax rates reduction timetable has been further accelerated in 2008

Special Taxation Regimes Adopted

- Special taxation systems have been adopted for the different regimes aimed at establishing new international financial institutions in the country, encourage economic growth, support sustainable development and the trade-transit function of Georgia

Type of Tax	An International Financial Company	Free Industrial Zone	Free Warehouse Company
Corporate Income Tax	(from financial services) 0%	(for International Companies) 0%	(from re-exporting of foreign goods) 0%
Value Added Tax	0%	0%	0%
Customs Tax	0%, 5% or 12%	0%	0%
Property Tax	up to 1%	0%	up to 1%
Personal Income Tax	20%	20%	20%

Double Taxation Avoidance Treaties

Effective Rates of Source Taxation

N	Country	Dividends	Interests	Royalties
1	ARMENIA	5%	5%	5%
2	AUSTRIA	0% / 5%	Exempt	Exempt
3	AZERBAIJAN	5%	5%	10%
4	BELGIUM	5%	5%	5% / 10%
5	BULGARIA	5%	5%	10%
6	CHINA	0% / 5%	5%	5%
7	CZECH REPUBLIC	5%	5%	0% / 5% / 10%
8	DENMARK	0% / 5%	Exempt	Exempt
9	ESTONIA	5%	5%	10%
10	FINLAND	0% / 5%	Exempt	Exempt
11	FRANCE	5%	0% / 5%	Exempt
12	GERMANY	0% / 5%	Exempt	Exempt
13	GREECE	5%	5%	5%
14	IRAN	5%	5%	5%
15	IRELAND	0% / 5%	Exempt	Exempt
16	ITALY	5%	Exempt	Exempt
17	JAPAN	5%	5%	0% / 10%
18	KAZAKHSTAN	5%	5%	10%
19	LATVIA	5%	5%	10%
20	LITHUANIA	5%	5%	10%
21	LUXEMBOURG	0% / 5%	Exempt	Exempt
22	MALTA	Exempt	Exempt	Exempt
23	NETHERLANDS	0% / 5%	Exempt	Exempt
24	POLAND	5%	5%	10%
25	ROMANIA	5%	5%	5%
26	SINGAPORE	Exempt	Exempt	Exempt
27	TURKEY	5%	5%	10%
28	TURKMENISTAN	5%	5%	10%
29	UKRAINE	5%	5%	10%
30	UNITED KINGDOM	0% / 5%	Exempt	Exempt
31	UZBEKISTAN	5%	5%	10%

Ratified Treaties (effectiveness pending)

1. Kuwait
2. Spain
3. Israel
4. Switzerland
5. Egypt
6. UK (Protocol)
7. Estonia (Protocol)

DTA treaties with 13 other states initiated. Negotiations to be held in the coming months.

Awaiting Signing or Ratification

1. Qatar
2. UAE
3. Cyprus
4. Bahrain
5. India
6. Slovenia
7. Slovakia
8. Latvia (Protocol)

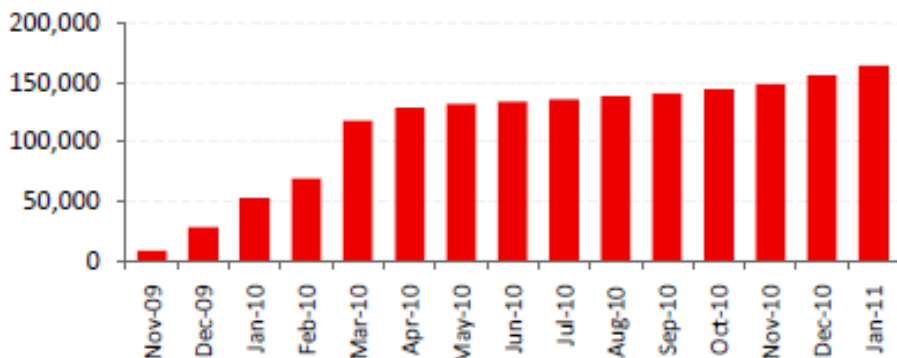
Tax Administration

Compliance Facilitation and Services

- Robust e-filing and e-payment systems
- Unified Cards for Customs and Tax Liabilities
- Principle of "Good Faith"
- Special Treatment of Micro and Small businesses
- Electronic VAT Invoices
- Electronic Administration System
 - Risk Based Selection of Taxpayers for Control
 - Electronic Assignments for Tax Officers
 - Electronic Performance Monitoring
- Risk Based Tax Audit
- Advance Ruling
- Accelerated Services
- Personal Tax Agent

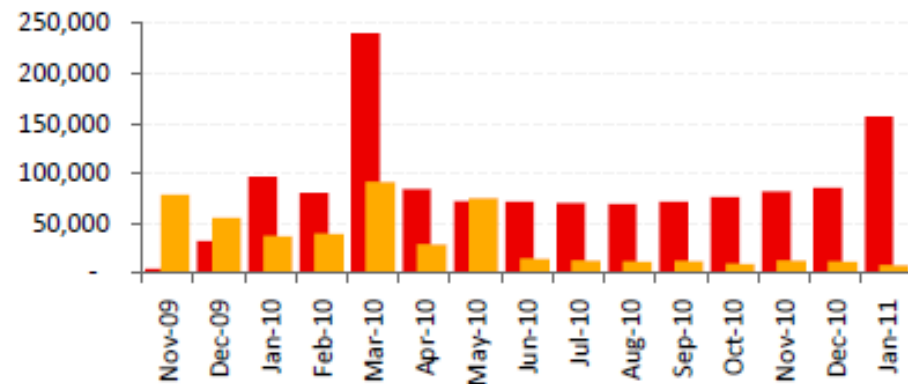
e-filing: Number of Registered Users

■ Number of Registered Users



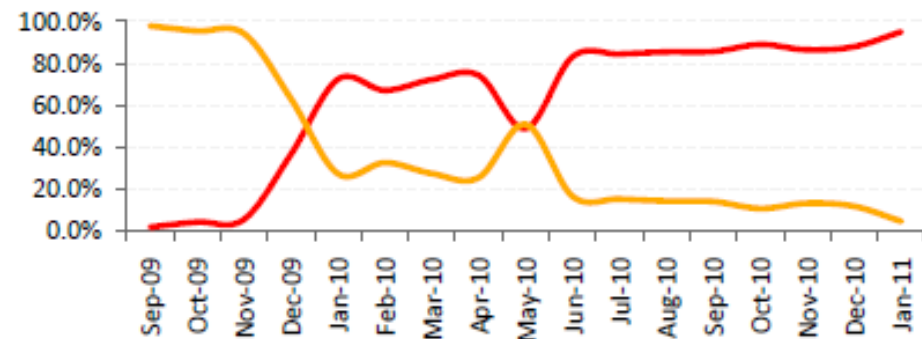
Monthly Declaration Statistics

■ Number of e-filings ■ Number of hard copy declarations



e-filing vs. hard copy declarations

— Share of e-filing — Share of hard copy declarations

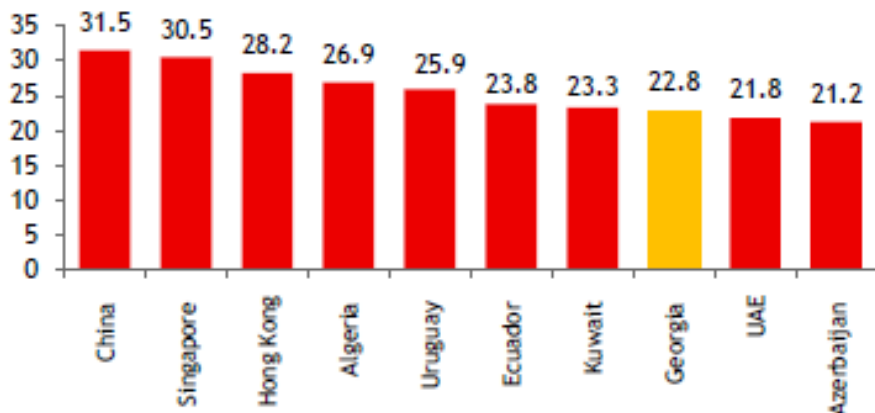


Robust Banking Sector

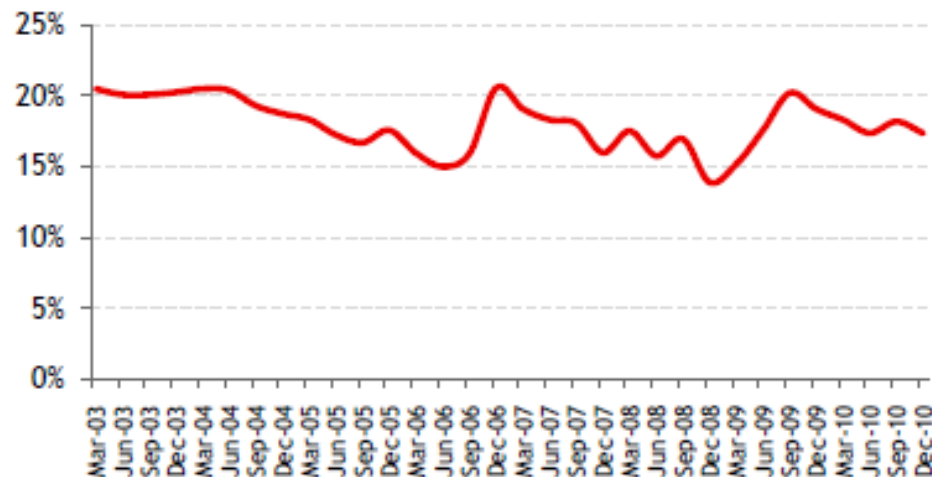
- Georgia's banking sector represents only a moderate contingent liability of the sovereign
- Entirely privately owned since 1995
- No restrictions on foreign ownership of banks
- Well capitalised with high average BIS capital adequacy ratio

World's Top Ten Saving Nations: 2003-2009

Household Savings as % of Disposable Income

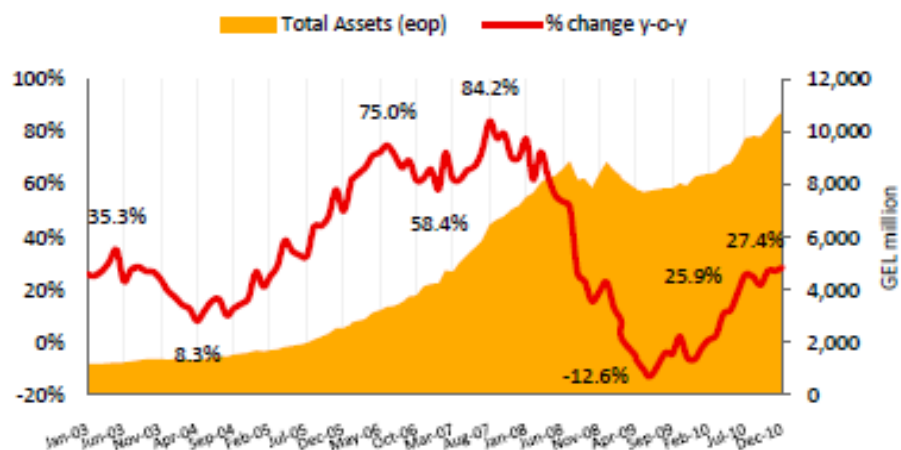


Capital Adequacy Ratio (CAR)

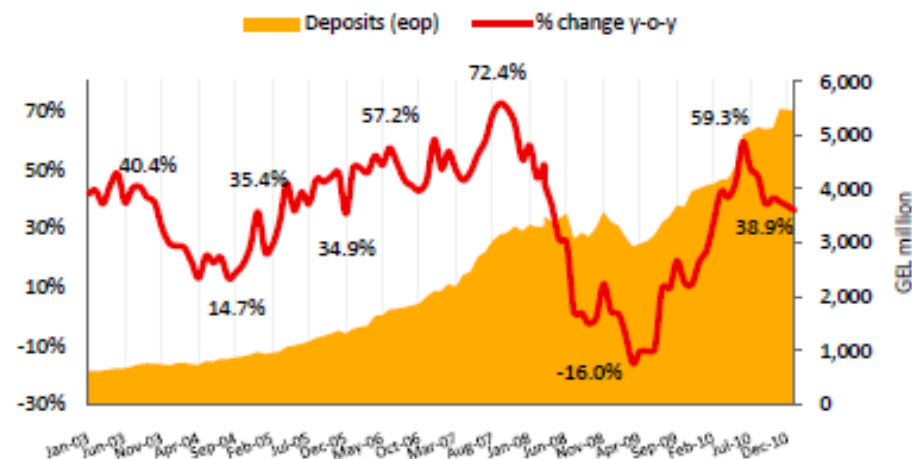


Rising Bank Assets and Deposits

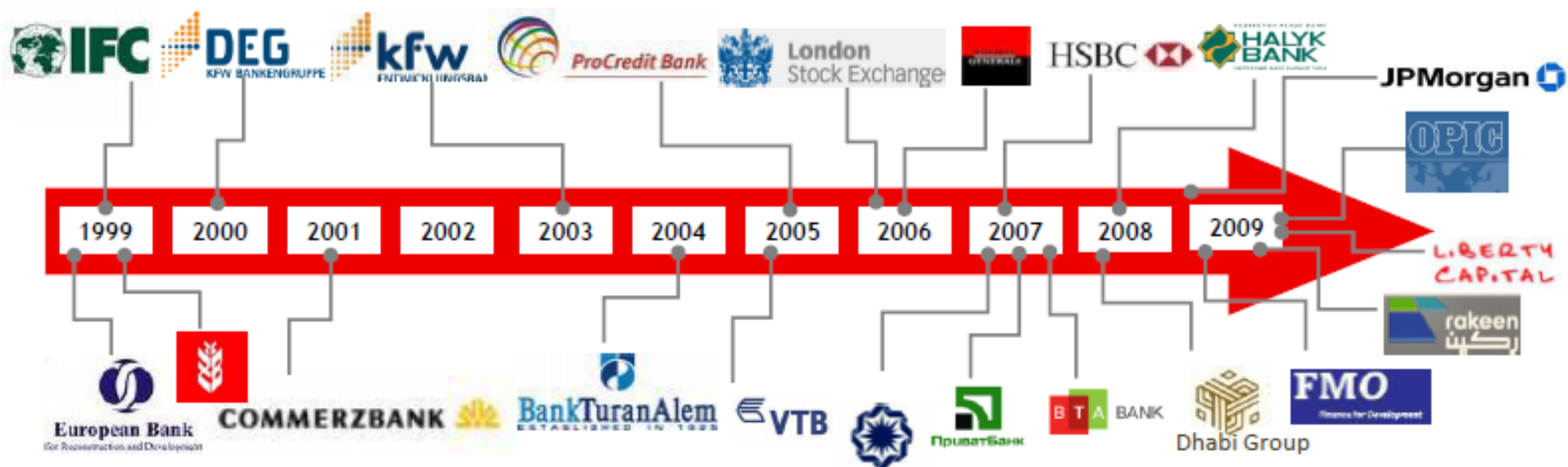
Bank Assets Are On The Rise...



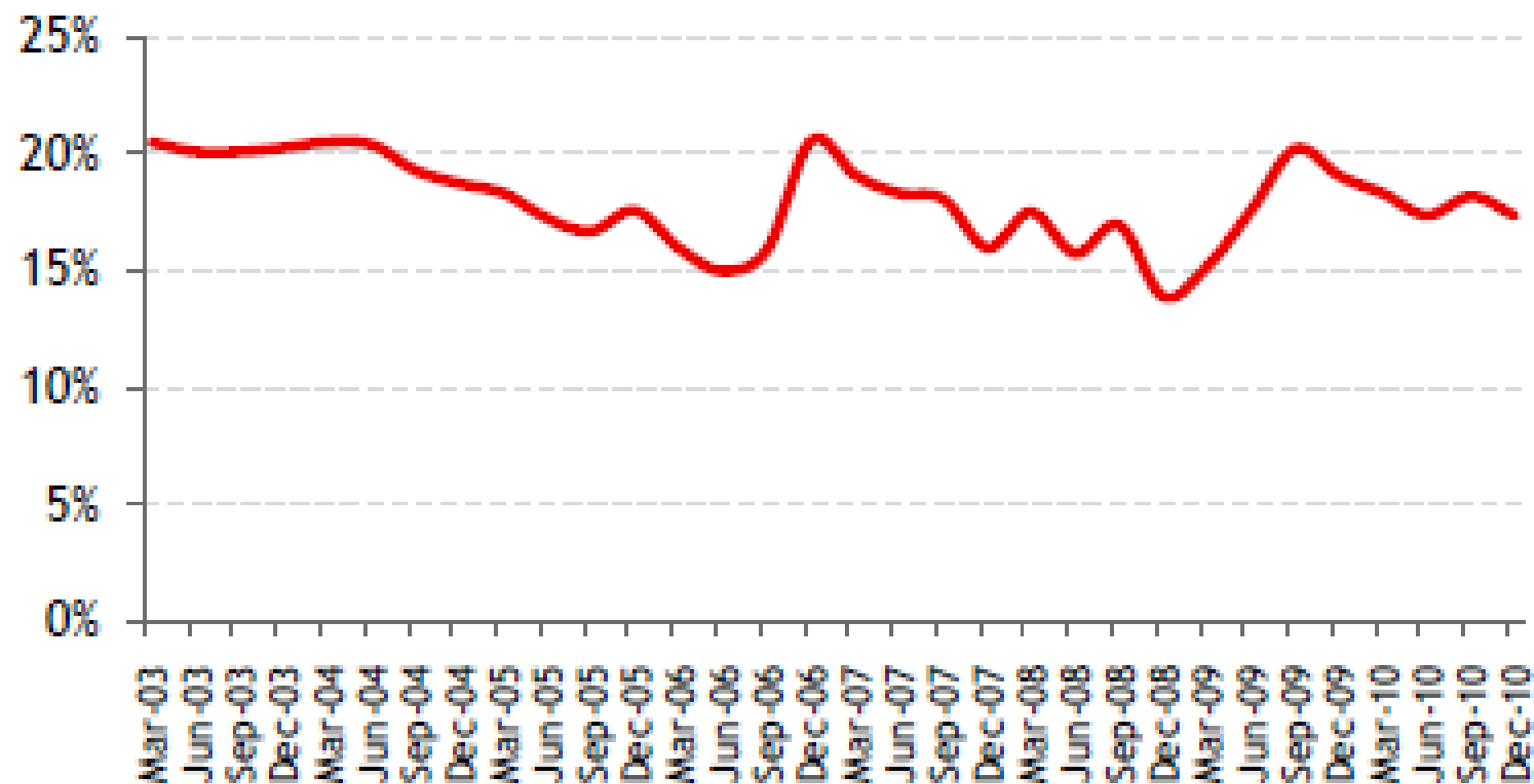
Bank Deposits Have Grown Beyond Pre-Crisis Levels



Openness of Banking Sector



Capital Adequacy Ratio



Money, Savings and Exchange rates

	2004	2005	2006	2007	2008	2009	2010
Money supply (M3)	847.2	1 071.0	2 689.9	4 027.5	4 305.1	4 656.8	6 275.7
Domestic credits, total	1 836.8	2 488.9	3 267.4	5 315.0	6 245.2	5 900.3	6 950.1
Deposits, total	905.6	1 188.6	1 862.5	2 875.4	3 222.6	3 427.3	4 902.7
Exchange rates							
USD/GEL (Period average)	1.9170	1.8127	1.7767	1.6707	1.4902	1.6705	1.7826
EUR/GEL (Period average)	2.3813	2.2600	2.2290	2.2859	2.1886	2.3307	2.3644

Decrease and Simplification in Licenses and Permits

Before

- 300 licenses and 600 permits existed
- Licenses and permits seen as source for grafting
- High entry barriers and corrupt practices



Note: Over 2000 construction permits were granted just in 2008, five-fold higher comparing to 2003, for around 2.5 mln sq. m. space in Tbilisi

After

- **70% cut in licenses (92) and 90% in permits (52)**
 - ✓ No sub-categories in the licensing activity
 - ✓ Legislative restriction on additional license inductions
 - ✓ No exclusive licences –non-discrimination applied
- **One-stop-shop in most government agencies**
- **Silence is Consent adopted**
 - ✓ 30 days for license and 20 days for permit

Property Registration

- Refined and simplified registration procedures
- Number of steps reduced from 6 to 3 and days from 9 to 2
- “Your’s is your’s”
- Electronic property registration introduced
- No restriction on foreign ownership of property and land
- Dispositional rights for both sides in mortgage execution
- Doing Business ranked Georgia 2nd in the world in ease of registering property



Labor market

- **No minimum wage**
- **2006 new Labor Code established freedom of parties to negotiate employment provisions**
 - ✓ Simple contractual relations between employers and employees
- **Low costs of hiring and firing workers**
- **Basic working conditions guaranteed**
 - ✓ Only specific circumstances, in line with ILO prerequisites, regulated (health safety, pregnancy, minors, dispute settlement, freedoms and rights of workers)



International Trade Liberalization

Before

- 52 days to import and 54 days to export
- 16 different tariffs applied



Note: Export increased by more than three-fold and import by more than 5.5 times comparing to 2003

After

- Simplified customs procedures since 2006
- Reducing paper work by more than half
- Slashed time requirements 4 days for import and 5 days for export
- Permits applying to only limited numbers of product groups
- One-stop-shop principle for issuance of certificates of origin
- 0% customs tariff on 95% good items and rates reduced 3 (0%, 5% and 12%)
- No quantitative restrictions, export, re-export or transit tariffs
- Risk management system and Gold List in place at customs

No Market Entry Barriers for Pharmaceuticals

- **Light touch regulation for those pharmaceuticals that are approved by OECD/EU respective authorities on their markets**
 - Registration days down from 60 to 7 days
- **Parallel import allowed**
 - For those pharmaceuticals already registered on Georgian market and entering with different labeling, only notice regime applies
- **Lifting restrictions on OTC medicaments to be sold in supermarkets/retail stores**



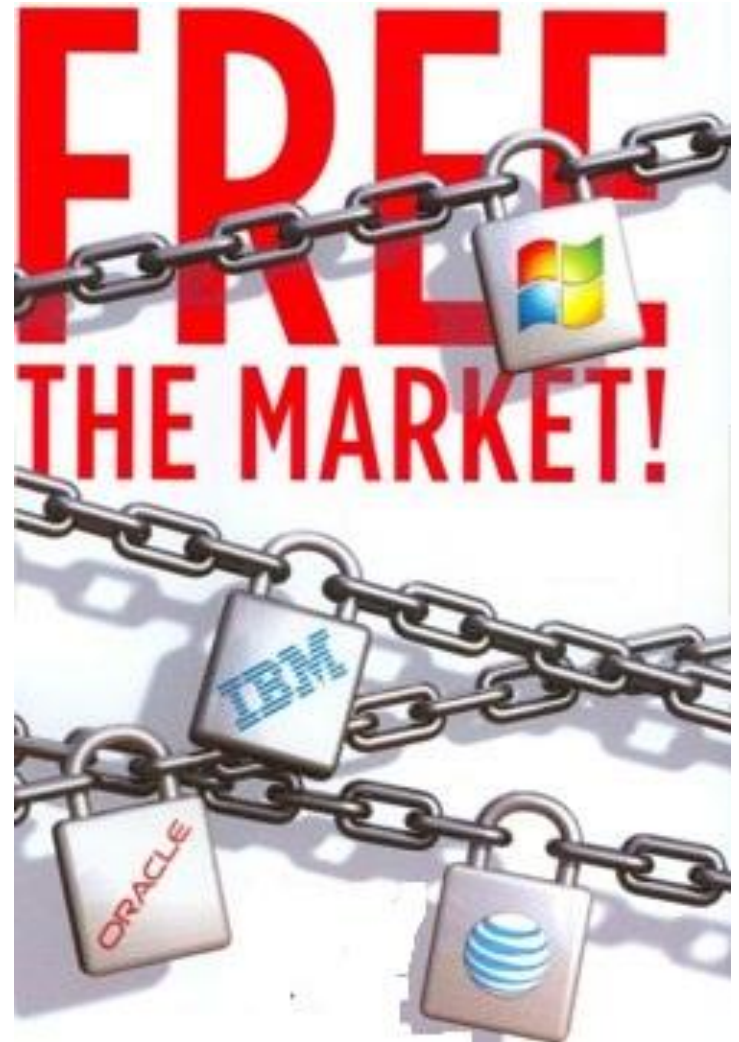
No Technical Barriers to Trade

- **Technical regulations only for activities that have direct influence on life safety of consumers**
 - Limited audit visits per year and no impediments in entrepreneurship activities
 - Respective (mutual) responsibilities for infringers and providers of entitlement
 - Voluntary standards in place
 - Recognition of EU and OECD technical regulations
- **Business is free from unreasonable and irrational technical regulations**
- **Easy, fast and low-cost export-import procedures for products under sanitary/phytosanitary control**
- **Voluntary standards (i.e. excluding safety concerns) allow businesses to operate without excessive investment conditions**

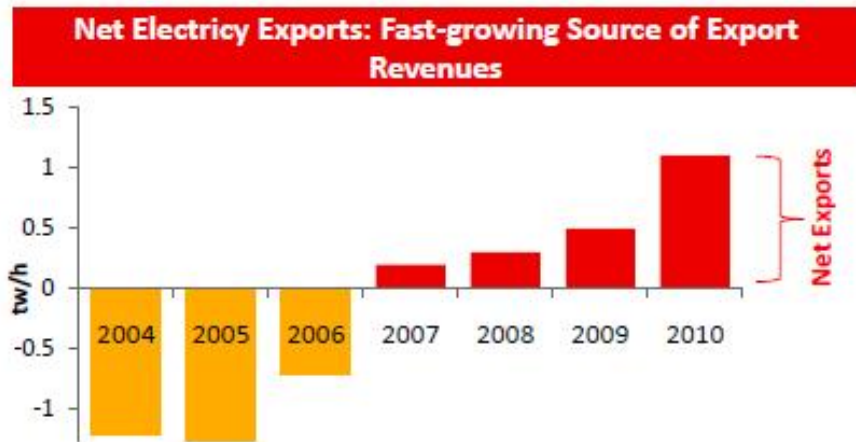
**The
Customer
is King**

No “traditional” Anti-Trust

- Free trade and competition Law vs. Old type Anti-Trust regulation of market shares
 - Law prohibits state institutions from giving privileges to any business
 - Entrance to market is equal



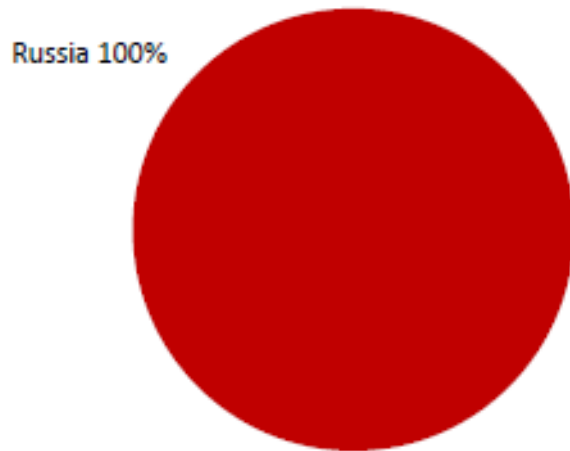
Net Exporter of Electricity



- New Energy Policy document adapted in 2006
- Complete rehabilitation of all HPPs and transmission lines
- Privatization of almost all HPPs and retail electricity distribution companies
- Newly built HPPs are fully deregulated from electricity generation tariffs
 - Only three permits for new HPP construction
 - No licence to export the electricity and no tariff set
- Wholesale generation tariffs are fully liberalized
- Small HPPs (less than 13 MW capacity) can sell electricity at unregulated tariffs

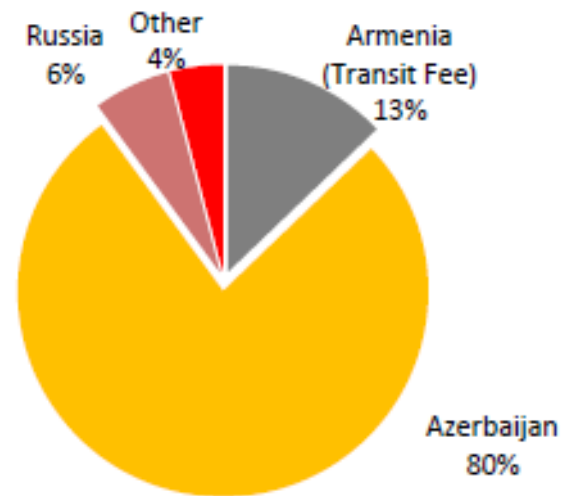
Diversified Sources of Energy Imports

Geographical Distribution of Natural Gas Import in 2005

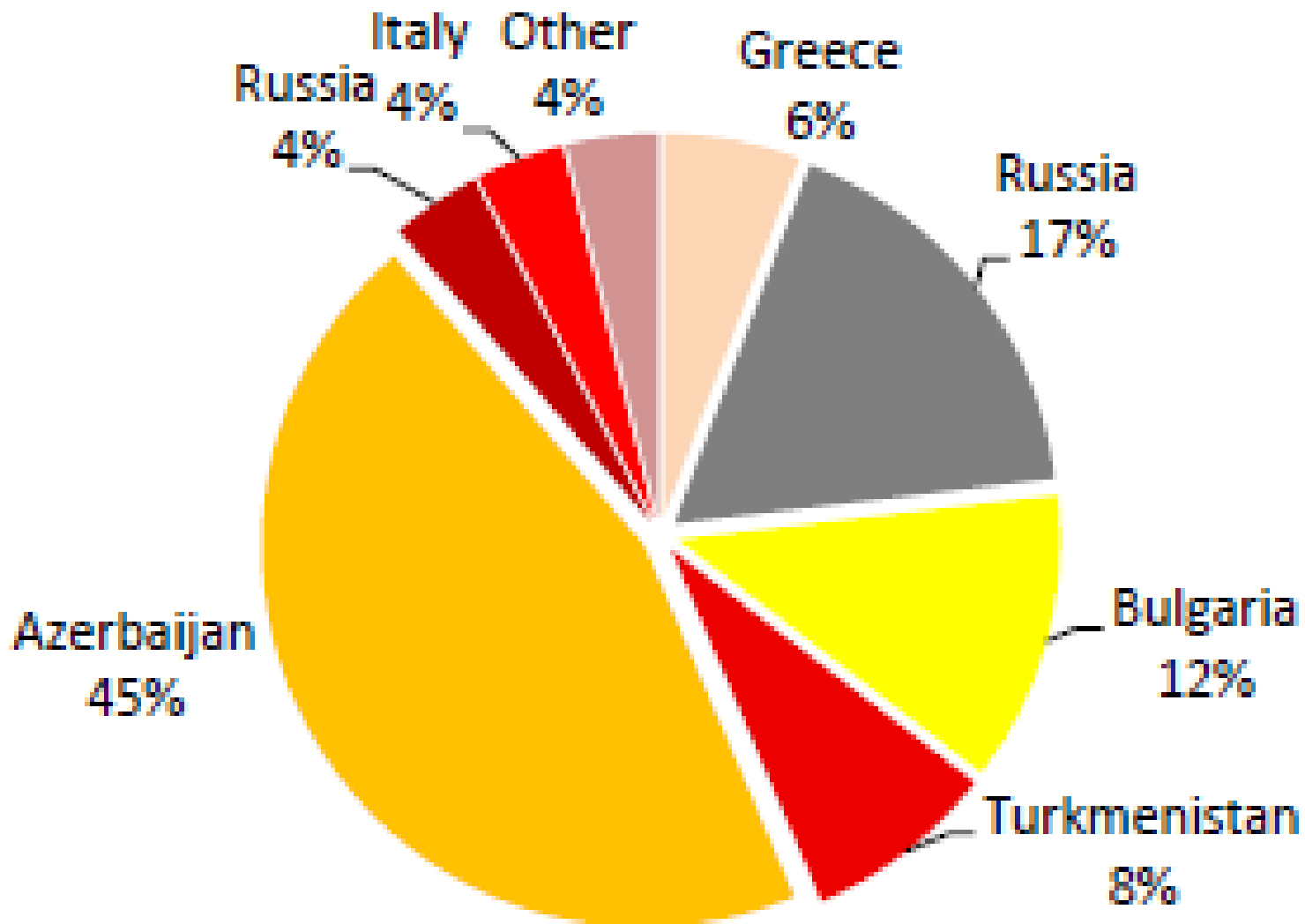


DIVERSIFICATION

Geographical Distribution Natural Gas Import in 2010

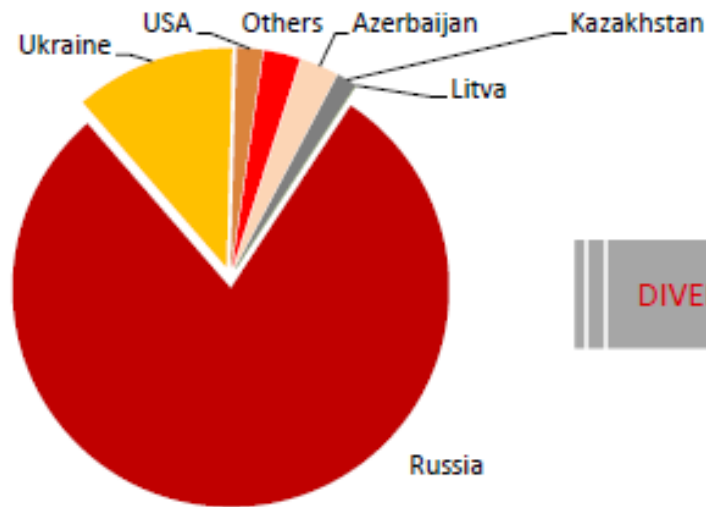


Geographical Distribution of Petroleum and Oil Product Import in 2010



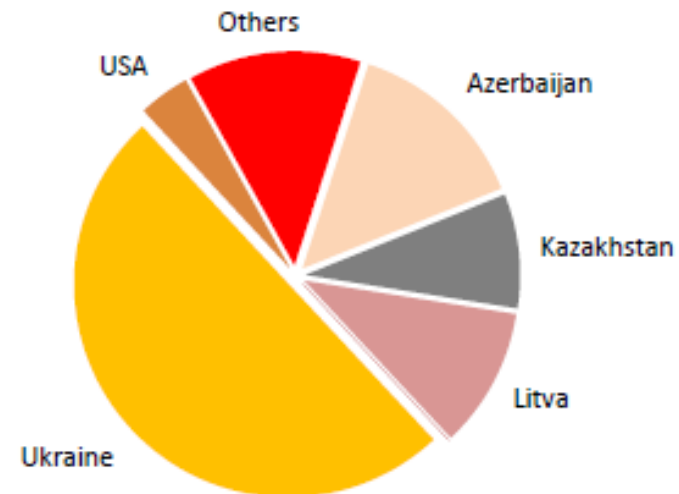
New Markets for Traditional Export Products - Wine

Geographical Distribution of Wine Export in 2005: before Russian Embargo



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Geographical Distribution of Wine Export in 2009: Substantial Diversification Benefits Achieved



New Markets for Traditional Export Products - Water

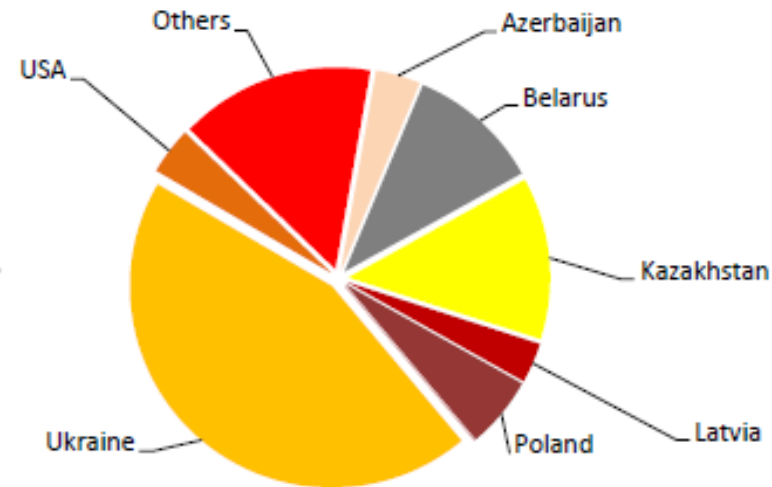
Geographical Distribution of Mineral Water Export in 2005: before Russian Embargo



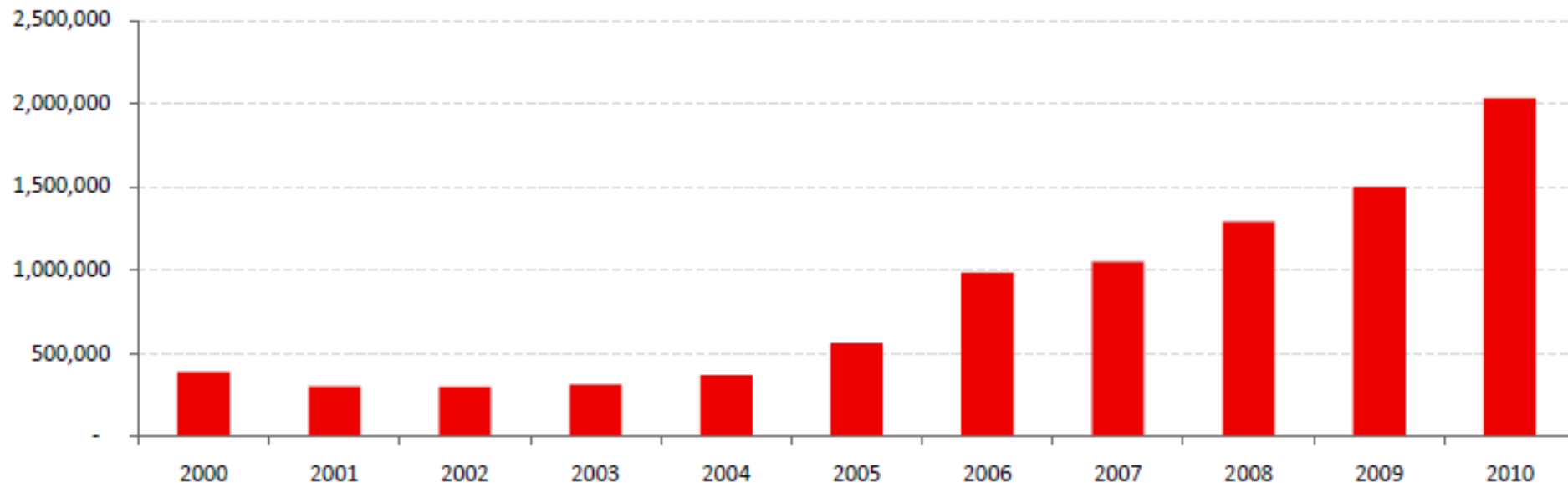
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DIVERSIFICATION

Geographical Distribution of Mineral Water Export in 2009: Substantial Diversification Benefits Achieved



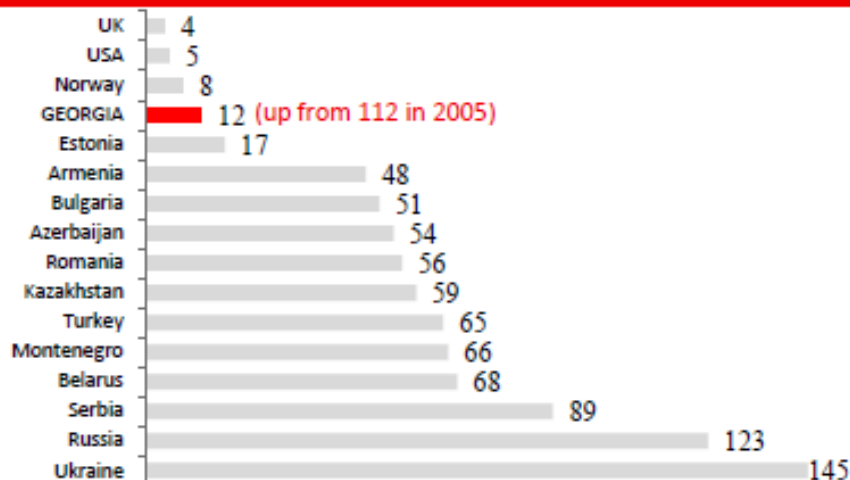
Rapidly Growing Tourist Arrivals



- Rebranding Georgia as tourism destination on international arena and transforming Georgia into regional tourism hub in the Caucasus
- Growth effects of the domestic road interconnectedness compounded by “vertical” approach to the revival of Georgia’s traditional tourism hubs (Tbilisi, Mtskheta, Batumi, Bakuriani, Gudauri etc.) and (re)discovery of new promising destinations (Svaneti, Anaklia, Signaghi, Kvareli etc.) capable of providing tremendous lasting boost to sea and mountain tourism, to ‘wine tours’ and green tourism.
- Domestic tourism development – area with significant unexplored growth potential
- Kobuleti and Anaklia Free Tourism Zone (plot of land for symbolic GEL 1 price, customized profit and property tax exemptions)
- Cultural sites inscribed on the UNESCO World Heritage List

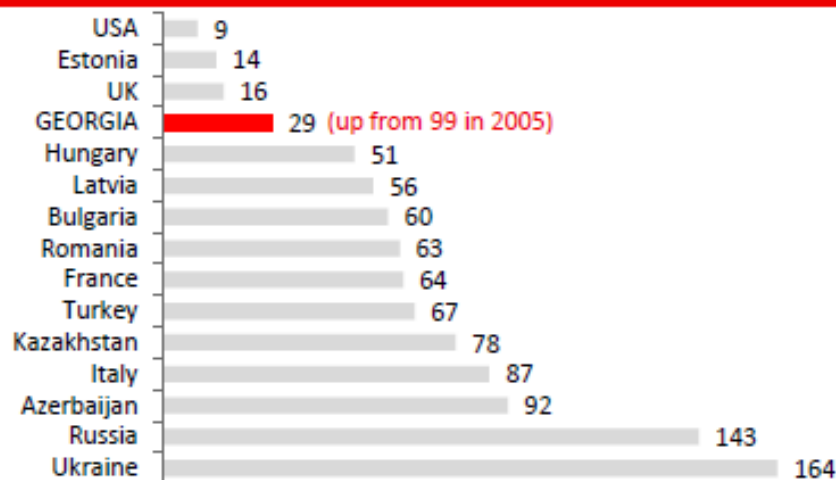
Recognition

Ease of Doing Business, 2011



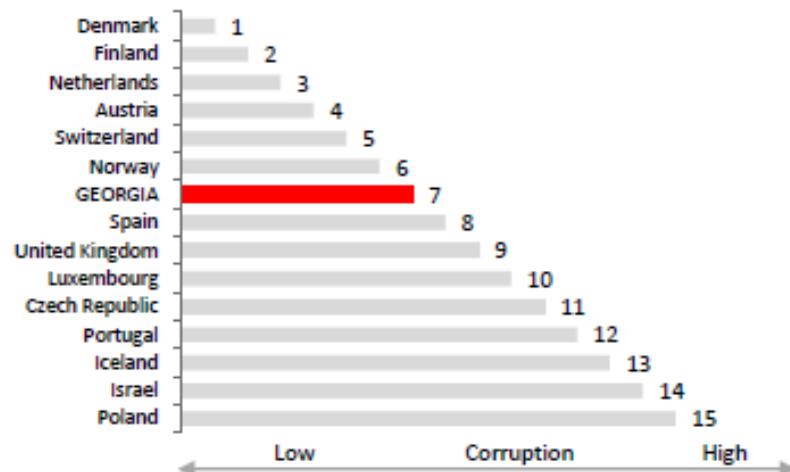
Source: World Bank, 2011 (Rank out of 183 countries)

Economic Freedom Index, 2010



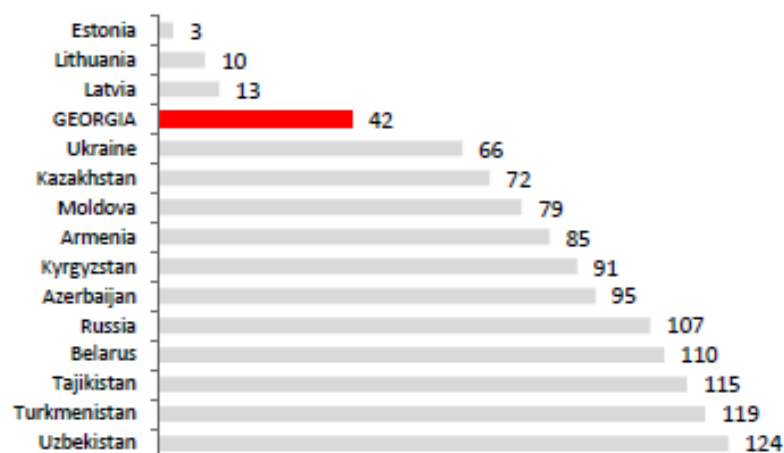
Source: The Heritage Foundation, 2010 (Rank out of 183 countries)

Global Corruption Barometer, 2009 (EU, Selected Countries & Georgia)



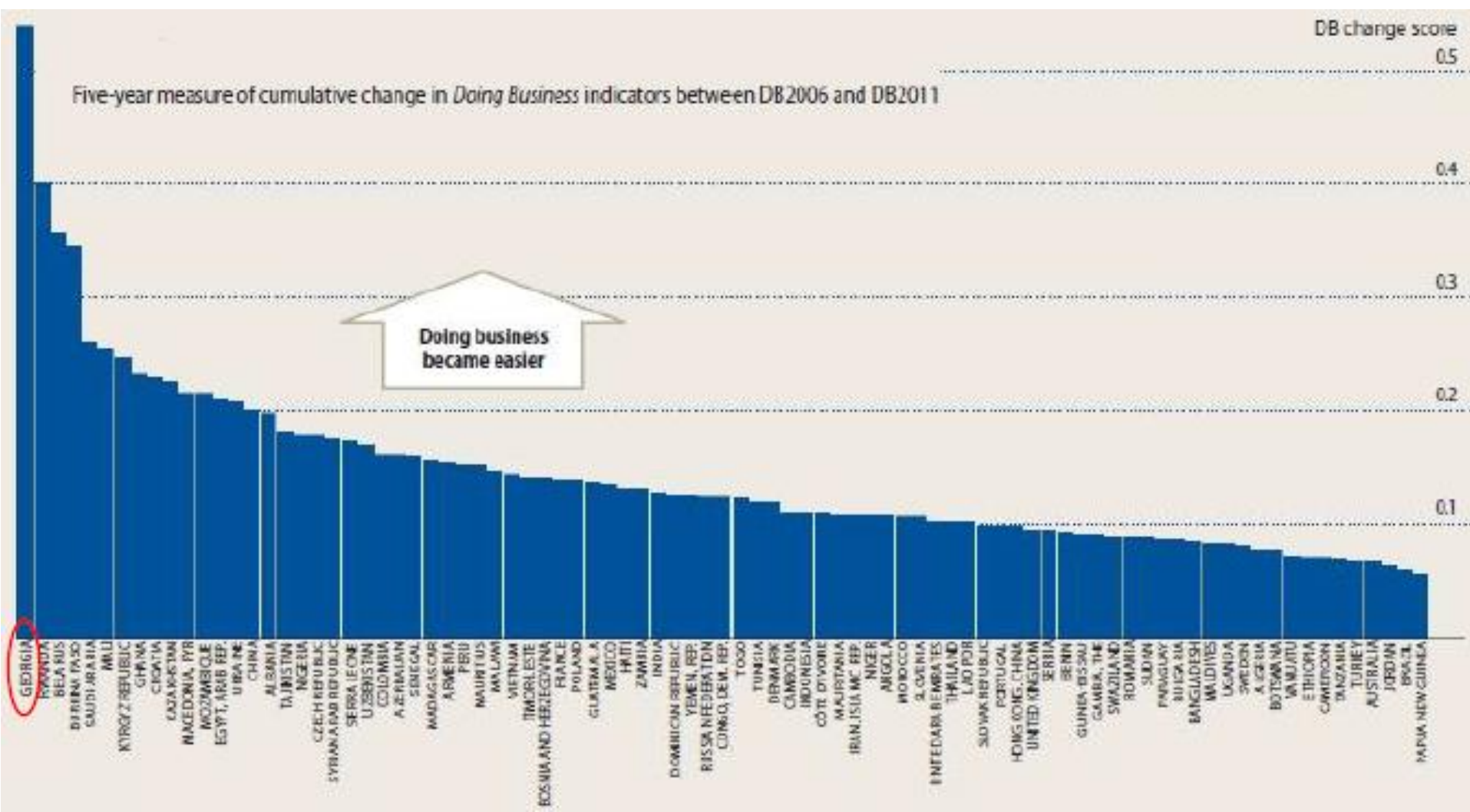
Source: Transparency International, 2009 (Rank out of 69 countries)

Bertelsmann Transformation Index, 2010



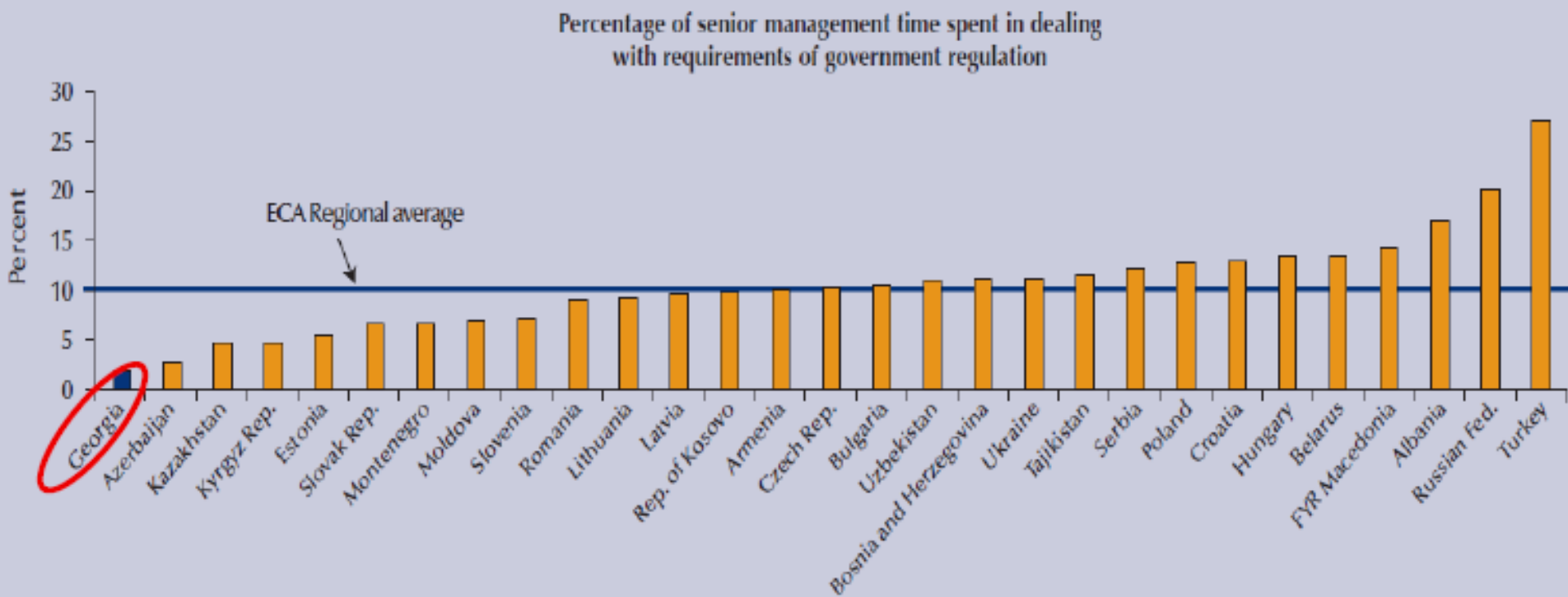
Source: Bertelsmann Stiftung, 2010 (Rank out of 125 countries)

Top Reformer 2005-2010



One of Few Best Business Climates

Figure 1 Firms Spend Less Time Dealing with Business Regulations in Georgia Than Elsewhere in the Region

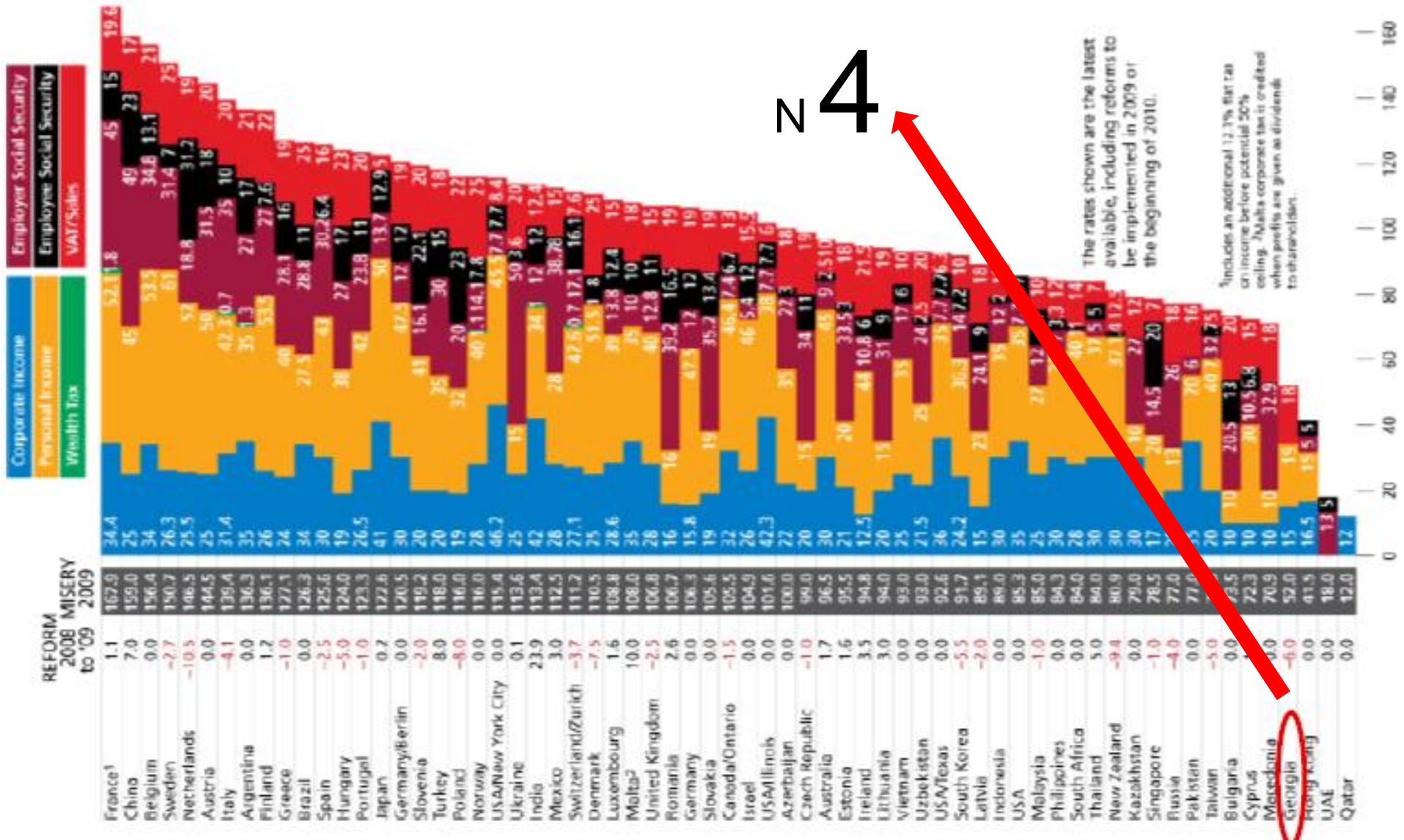


Openness for Foreign Investment

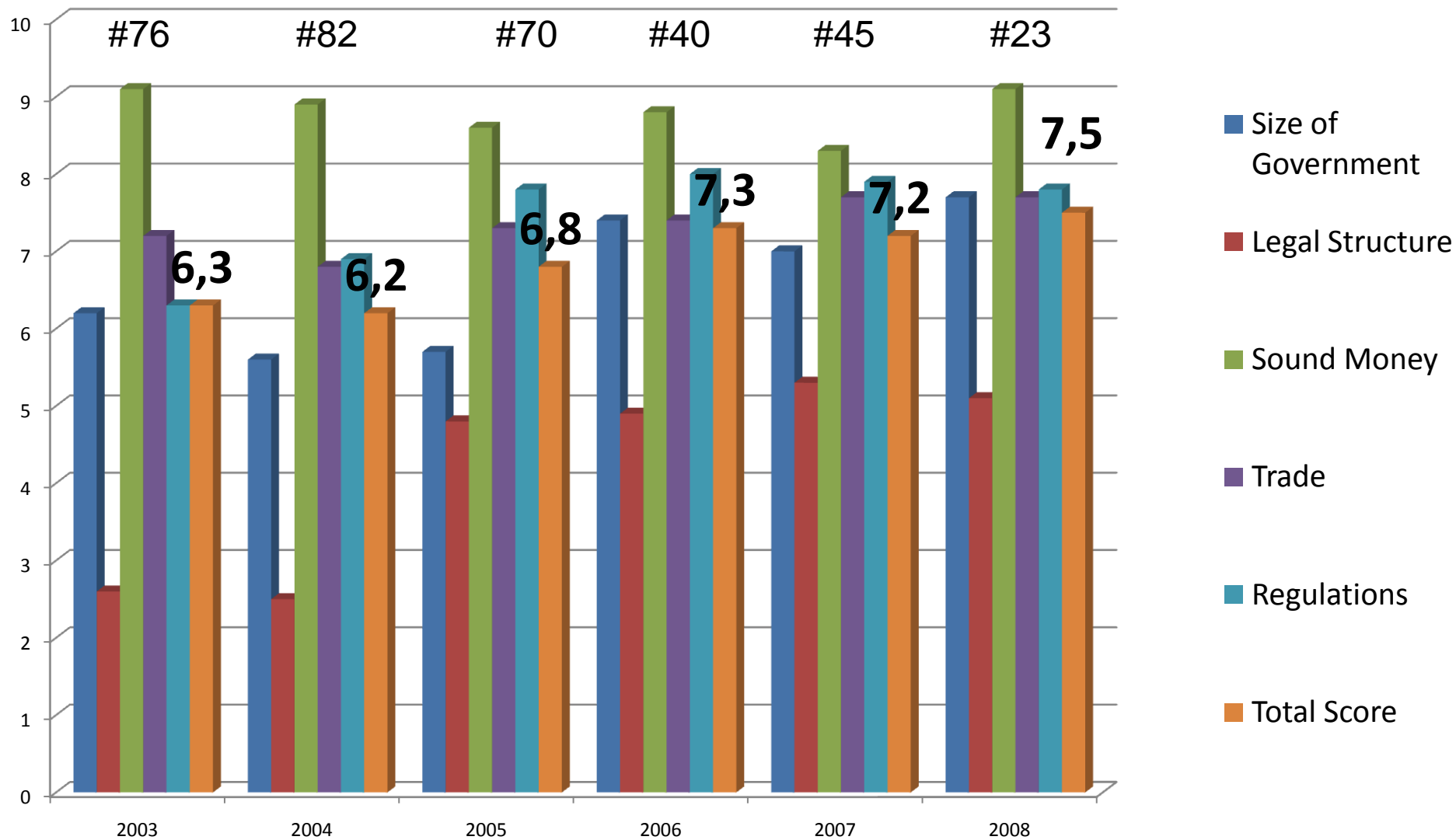
Sector	GEORGIA Score	Regional Average	Global Average
Mining, oil & gas	100	96.2	92
Agriculture & forestry	100	97.5	95.9
Light manufacturing	100	98.5	96.6
Telecom	100	96.2	88
Electricity	100	96.4	87.6
Banking	100	100	91
Insurance	100	94.9	91.2
Transport	100	84	78.5
Media	100	73.1	68
Construction, tourism & retail	100	100	98.1
Health care & waste management	100	100	96

“Georgia is one of the most open countries to foreign equity ownership as measured by the Investing Across Sectors indicators. All of the 33 sectors covered by the indicators are fully open to foreign investment. There are neither sectors with monopolistic or oligopolistic market structures nor any perceived difficulties in obtaining any required operating licenses” – Summary by the World Bank

Forbes Tax Misery & Reform Index



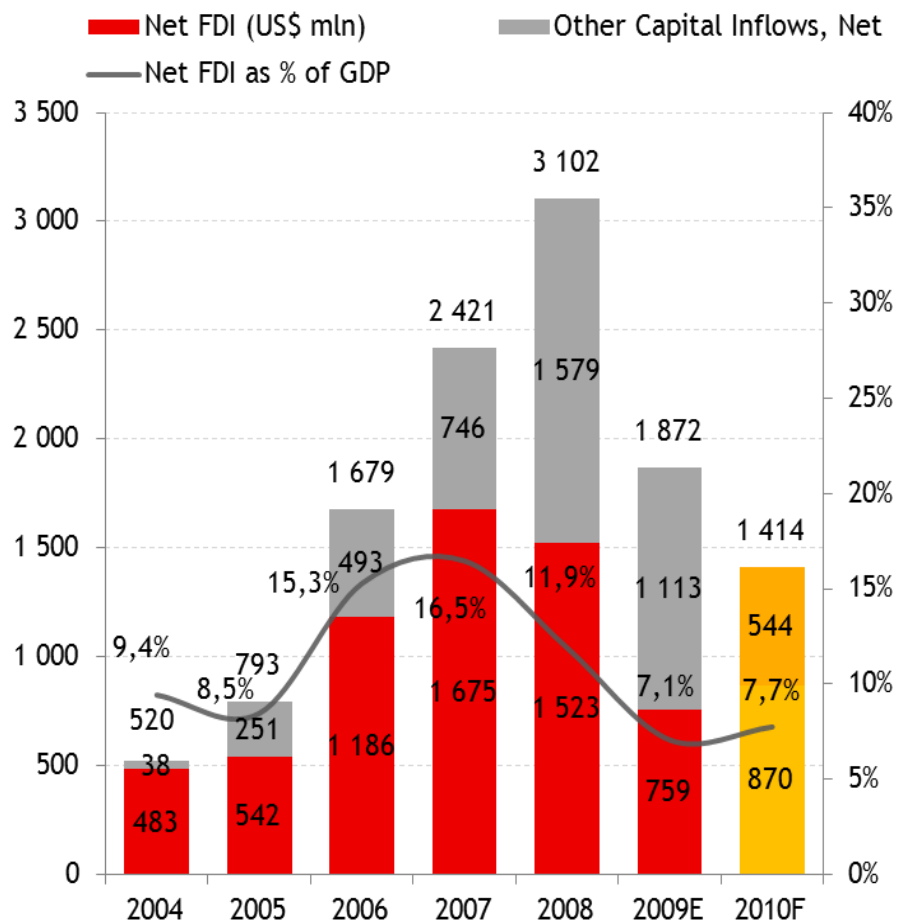
Georgia scores in EFW'2008



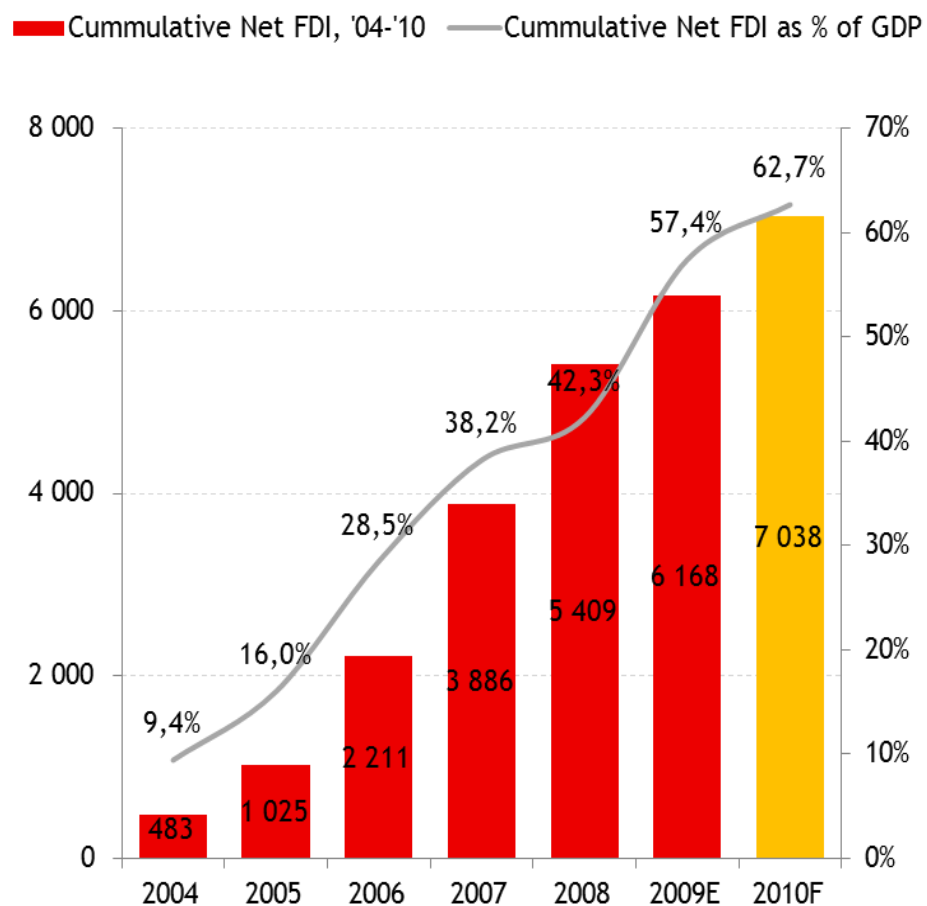
Business Registrations

Legal status	Number of entities
TOTAL	294334
Commercial legal persons	75880
Joint liability companies	2463
Limited partnerships	192
Limited liability companies	70107
Joint stock companies	1949
Cooperatives	1169
Non-commercial legal persons	10524
Individual enterprises	197392
Branches, representatives, etc.	6832
Entities of public law	3706

Investment Inflows (USD)



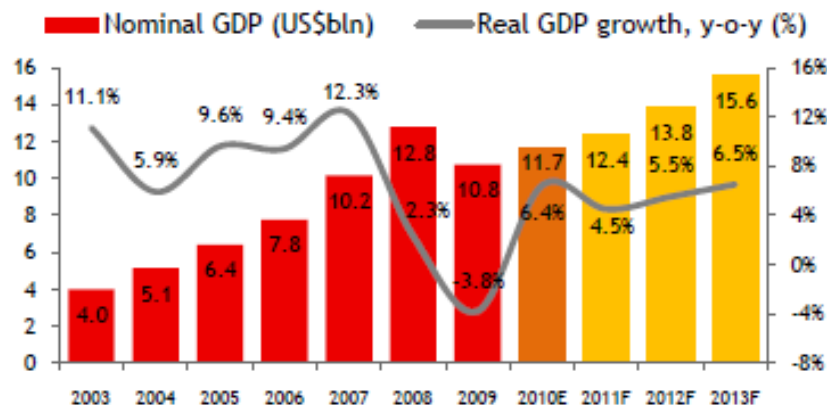
Source: National Statistics Office
of Georgia-GeoStat



Source: Central Bank of Georgia,
International Monetary Fund

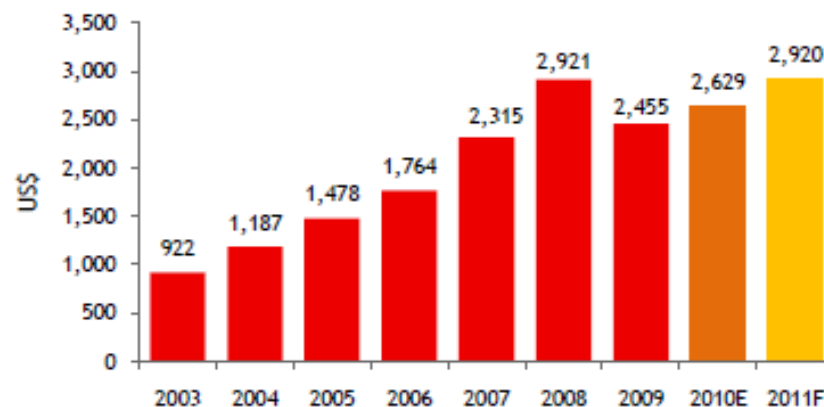
GDP

GDP



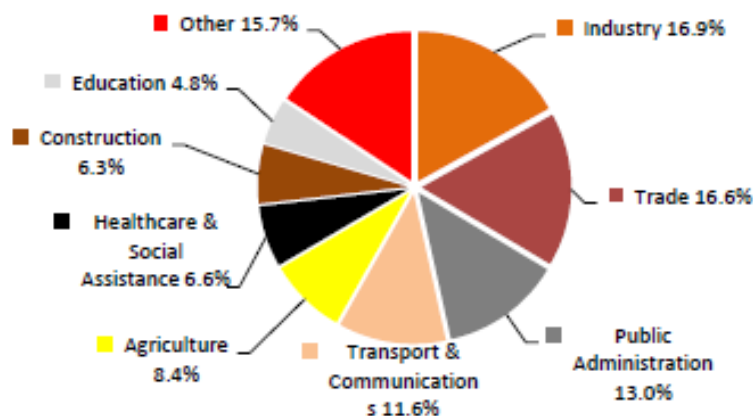
Source: National Statistics Office of Georgia-GeoStat, Ministry of Finance of Georgia

GDP Per Capita



Source: National Statistics Office of Georgia-GeoStat, Central Bank of Georgia

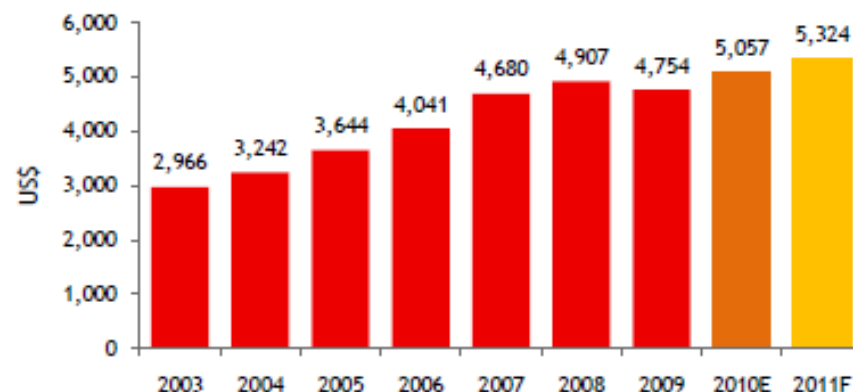
Components of Nominal GDP* (2010E)



* Calculated using GDP at basic prices

Source: National Statistics Office of Georgia-GeoStat

GDP Per Capita PPP

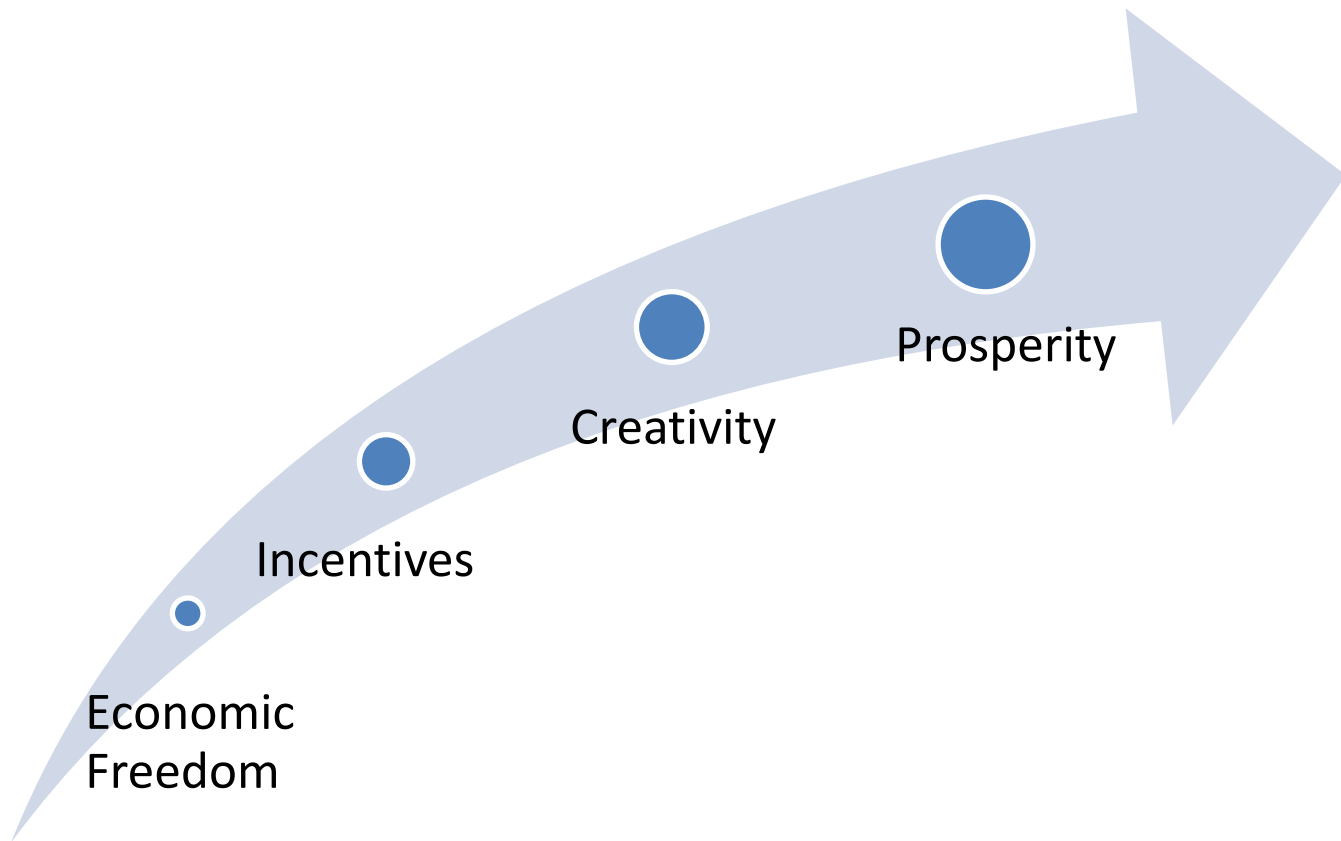


Source: National Statistics Office of Georgia-GeoStat, Central Bank of Georgia

Poverty

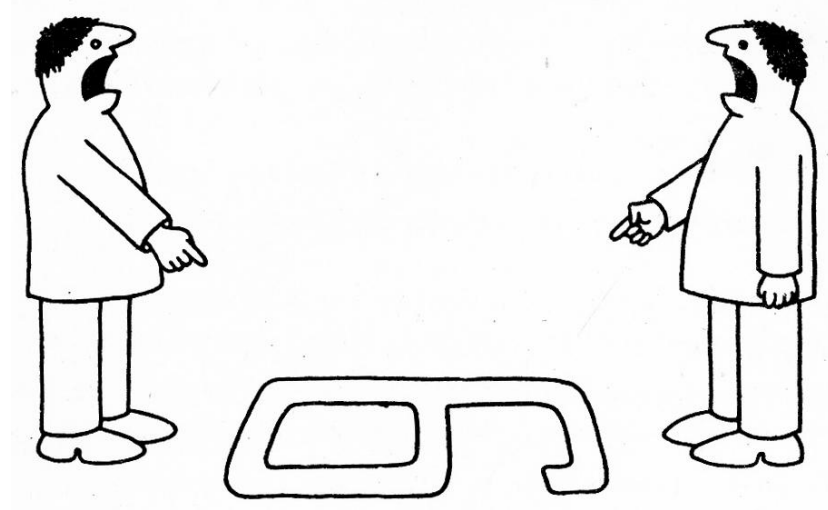
	2004	2005	2006	2007	2008
With respect to 60 percent of the median consumption (%)	24.6	24.1	23.3	21.3	22.1
With respect to 40 percent of the median consumption (%)	10.9	10.1	9.4	9.2	9.5

Lesson: Chain Effect



Now is Critical Time

- Potential obstacles for market oriented development
 - Trends inside of political elite
 - less attention to economic issues
 - Political clash
 - Elections 2012
 - Foreign interference in local policy
 - Economics harmonization – EU
 - Political changes – Russia



Warning: International Pressure

- Embargo
 - High cost of readjustment and redirection
 - Underground trade
- Military aggression & Occupation
- Support of destabilizing political forces



Breakdown of Remittances '10

Country	US\$ million	Share in Total
Russia	500.1	58.3%
USA	68.7	8.0%
Greece	59.0	6.9%
Ukraine	42.4	4.9%
Turkey	29.1	3.4%
Spain	21.3	2.5%
Germany	12.8	1.5%
Israel	10.7	1.2%
Other Countries	113.5	13.2%
Total	857.5	100.0%

Warning: International Pressure

- Critic of “Ultra Liberalization”
- Demand for harmonization
- Imitation of integration
- Accent to “democratic” and “election” issues



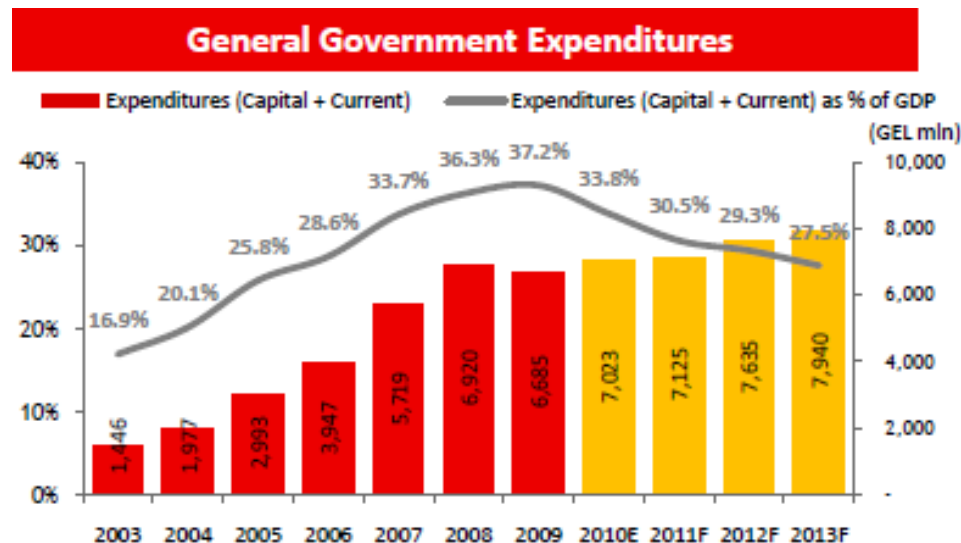
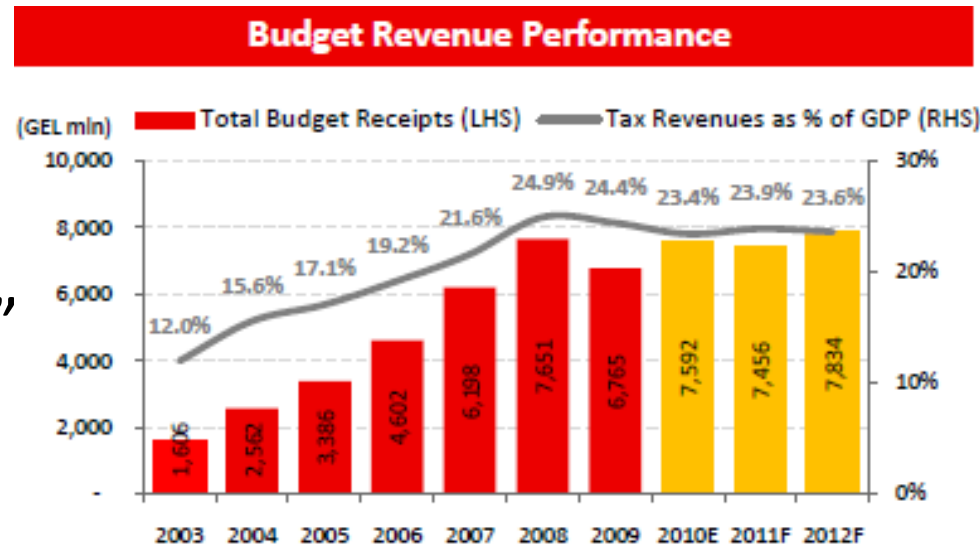
“...our [EU-Georgia] future partnership require a full engagement from them [the Georgian authorities] and it might not be fully compatible with some of the ideas of ultra-liberal economic environment to be created in Georgia.”

Štefan Füle

EU Commissioner for Enlargement and European Neighborhood Policy,
Czech Republic, Socialist

Warning: Big Government!!!

- Rise of government
 - Danger of step forward step in backward game
- Temptation “to do more” by the State
 - Budget expenditure in 2010 raised by 215 million Laries
 - 150 million laries from taxes
 - 65 million Laries from donors

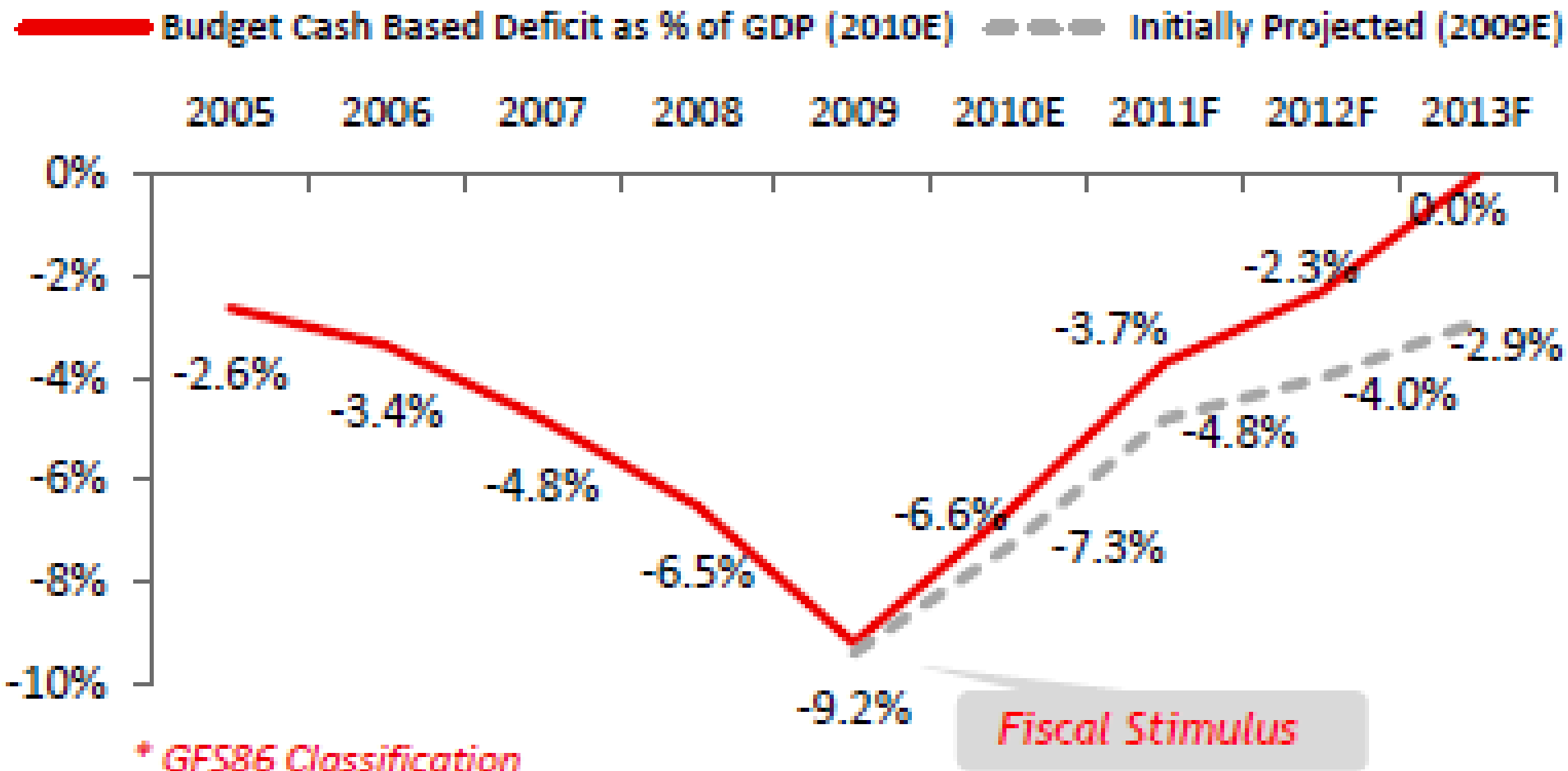


Areas of Government Spending

- Energy Infrastructure
 - Black Sea 500 kv. Regional Power Transmission Line
 - HPPs – Khudoni, Namakhvani, Oni
 - Underground Gas Storage Facility
- FIZ – Trade and Logistics Infrastructure
 - Poti FIZ
 - Kutaisi FIZ
- Social Infrastructure
 - Secondary Schools
 - Primary Healthcare
 - Hospitals
- Railway Infrastructure
 - Tbilisi By-Pass Project
- Roads Infrastructure
 - East-West Highway Improvement Project
 - Adjara Bypass Road
 - Vaziani-Gombori-Telavi Road
 - South Georgia Road
 - Secondary and Local Roads
- Communal Infrastructure
 - Rehabilitation of Communal Infrastructure Facilities in Major Cities
 - Regional and Municipal Infrastructure Development Fund Projects
 - Water and Sanitation Restructuring (Ltd. East Georgia & Ltd. West Georgia) and Rehabilitation

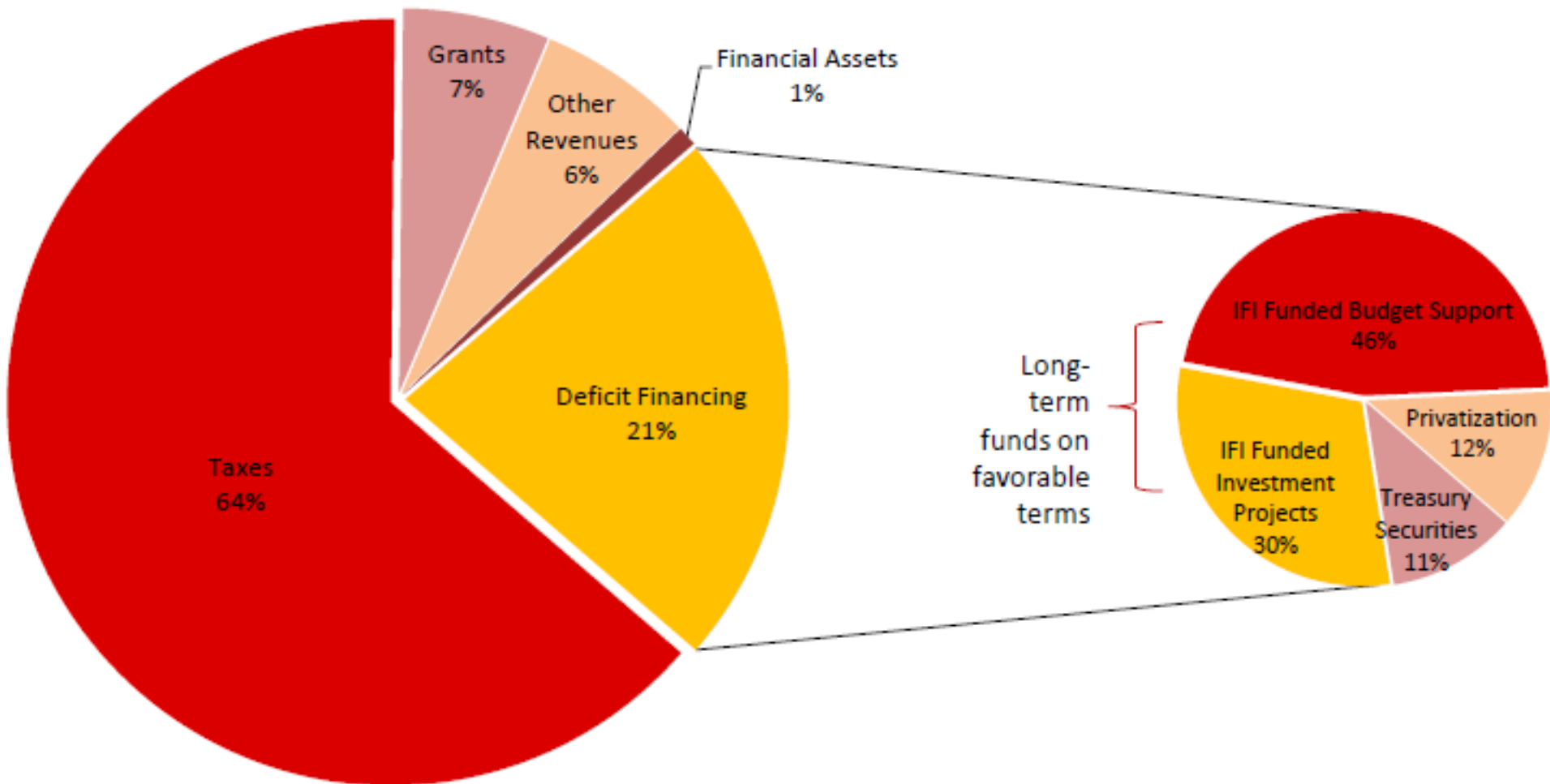


Conventional Fiscal Deficit (Cash Based)

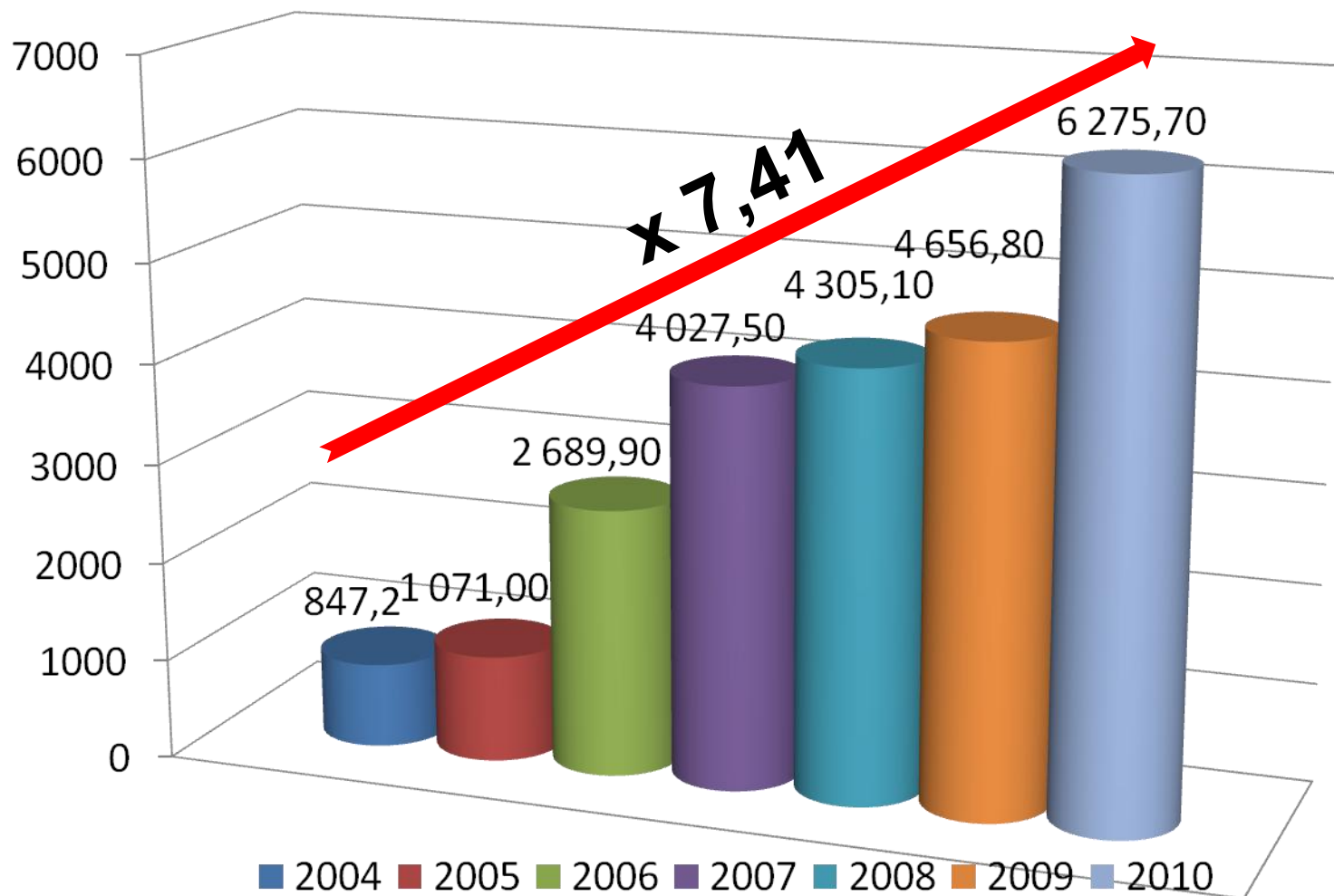


Source: Ministry of Finance of Georgia

2010 Budget Receipts and Deficit Financing Sources

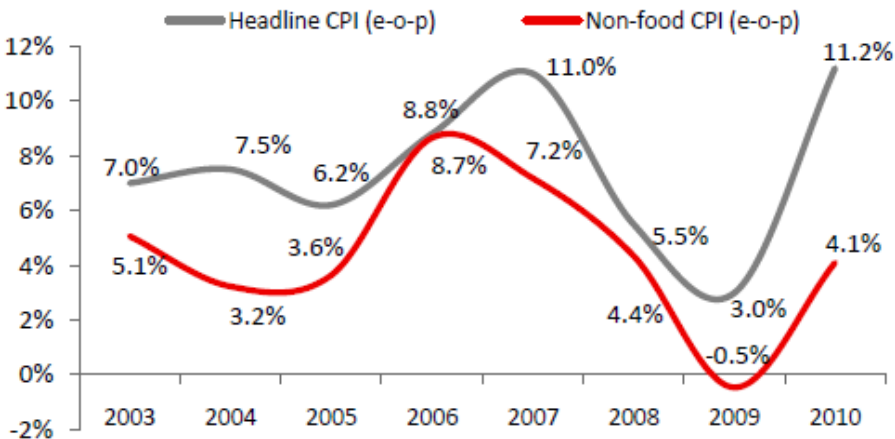


Increase of Money Supply in Mill. GEL (M3)

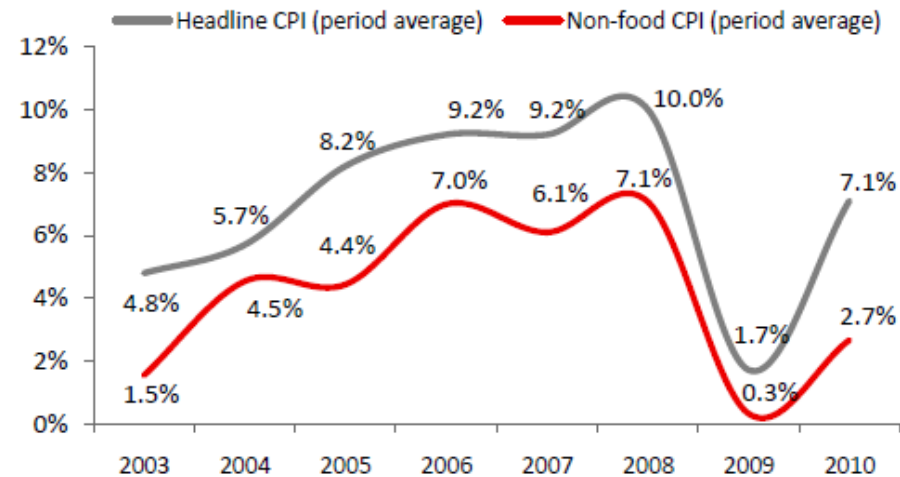


CPI: Double Digits - Critical point!!!

Consumer Price Index (e-o-p)



Consumer Price Index (period average)

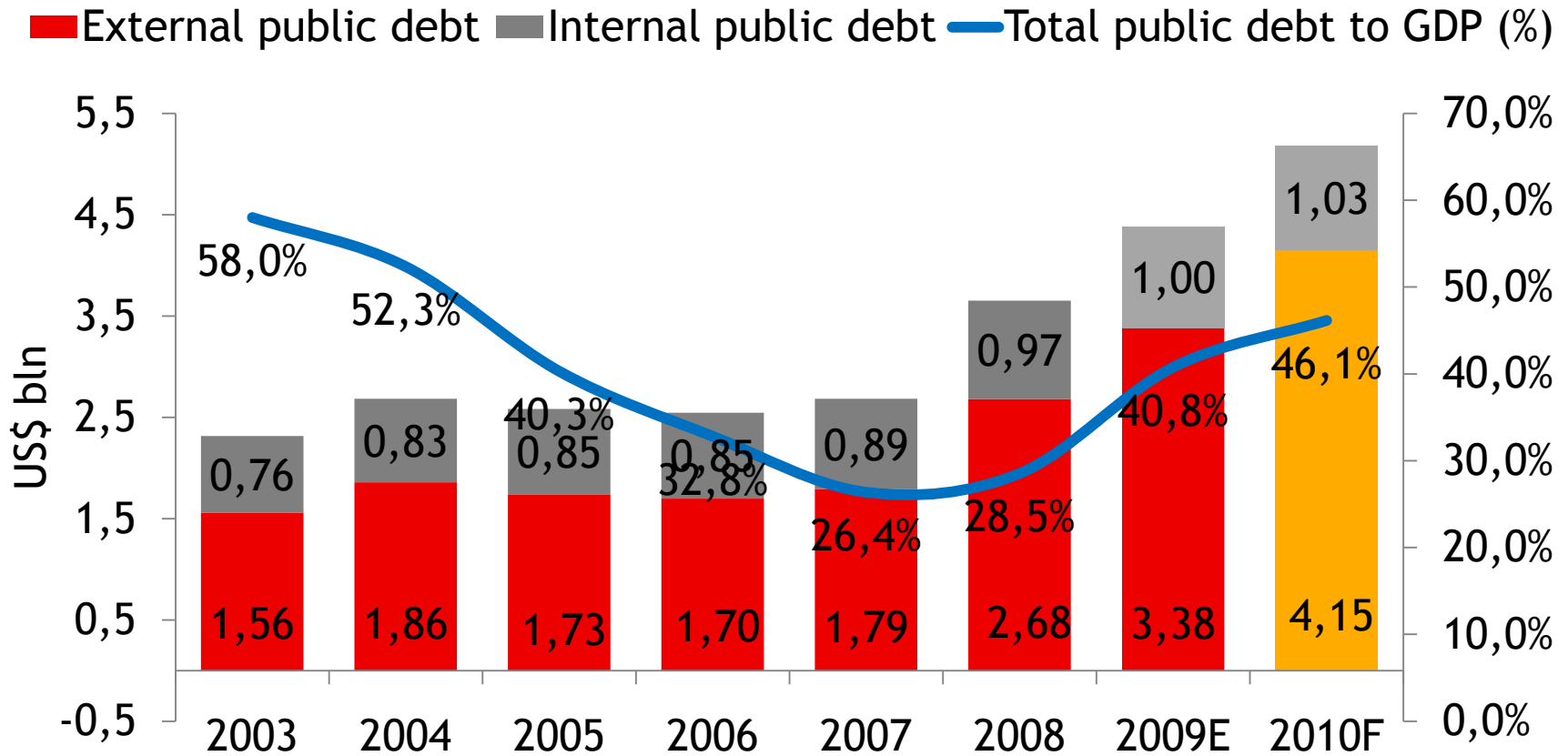


Beside high prices on oil there are no attempt to reduce excise tax on fuel!

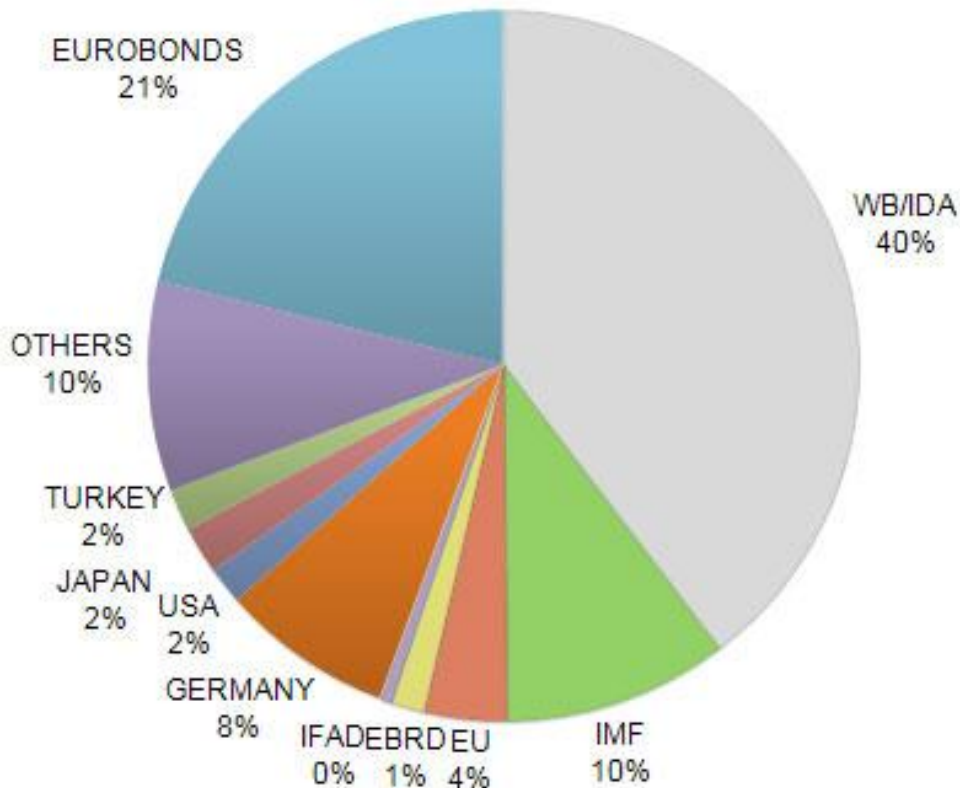
Warning: Foreign Subsidies (AID) – No Reforms toward free market!!!

Donor	US\$ million	Sector	US\$ million
USA	1,000	Finance and banking	1,105
EBRD	927	Transport infrastructure	682
EC	638	Non- sectoral support	586
World Bank	530	Energy infrastructure	381
IFC	350	Urban and municipal infrastructure	210
European Investment Bank	330	Other	1,571
Asian Development Bank	300	Total	4,535
Japan	200		
EU members	174		
Other states	88		
Total	4,535		

Warning: Public Debt 46,1% of GDP!!!



Composition of external debt

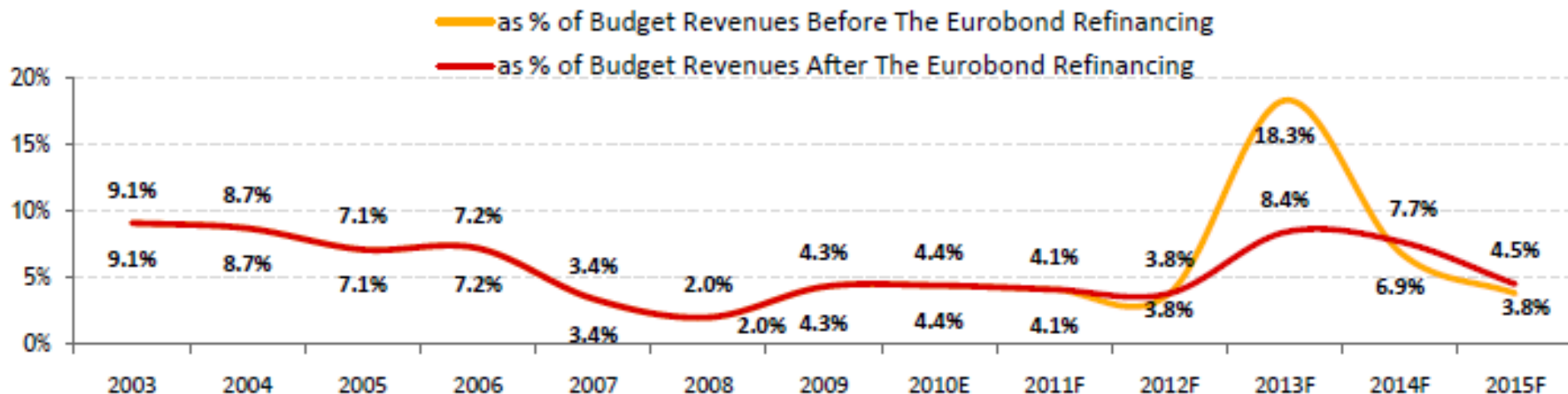


- International financial institutions are easily giving credit to Government!

Payment for Public Debt

- Debt is rising
- On April 7, 2011, Georgia priced a new 10-year \$500 million and in parallel redeemed \$417 million of its existing \$500 million 7.50% bond due 2013 through an “any and all” cash tender

Flat Repayment Profile: Government External Debt Service



Warning: Arbitrariness of Tax Administration!!!



Self-destructive behavior: Trying to get maximum NOW and not thinking about future of businesses too much

Understanding: The Liberty Act

- The government intends to submit to Parliament in October 2009 **the constitutional Law on Economic Liberty, Opportunity and Dignity** (the Liberty Act)
- The Liberty Act will contain a coherent package of bold measures to constitutionally enshrine our basic policies, reassuring investors that no policy reversal or policy drift is possible
- Returning to citizens to the power to tax – no new taxes or tax rate increases without a nationwide referendum
- Fiscal responsibility
 - Government expenditure capped at 30% of GDP
 - Budget deficit capped at 3% of GDP
 - Government debt capped at 60% of GDP
 - No budget earmarks
- No restrictions on currency convertibility or repatriation of capital & profit
 - Has been the case in Georgia since 1995
- Ban on state ownership of banks and on the imposition of price controls
 - No state-owned banks since 1995 and no price controls since the early 1990s
- Ban on an increase in the number of licenses and permits
- Ban on an increase in the number of state or independent regulators
 - Currently, independent regulators exist only in financial services, communications and utilities
- Means-tested assistance rendered through vouchers and other ways that empower citizens and give them choice (in healthcare, education, etc), rather than by funding directly state-owned service providers



Future Outlook – Fitch Rating

March 3, 2011

Foreign Currency

- Long Term: B+
- Short Term: B

Local Currency

- Long Term: B+
- Country Ceiling: BB-

Outlook: Positive



POSITIVE THOUGHT

it works
if you believe it

Good..., but game is not over:
Still more to be done!



- Strong Preference to what is Fine & Fair
- For more economic freedom:
 - Sound money (Based on precious metals)
 - Constitutionally limited and functionally decentralized Government
 - No more Government debt
 - Service Fee based Government instead of tax based Government

Georgia did! – Others could follow!



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