

UDC 332.1

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SOCIAL CHANGES AND ECONOMIC DEVELOPMENT IN GEORGIA

After the collapse of the Soviet Union Georgia experienced a protracted crisis during which the country lost its territories as a result of conflicts and gross domestic product (GDP) has been cut by 2/3 since 1990. Since then Georgia has faced a serious problem with its development that was caused by the necessity of transition. The course to European values, taken by Georgia, had no alternatives. Despite achieving considerable success in political, economic and social fields, living standards and quality of the population still remains extremely poor. Satisfaction of public requirements significantly lagged behind the high rates of economic growth. At present, Georgia is facing a number of economic problems, which need to be solved in timely manner, otherwise macroeconomic stability of the country will face serious threats.

Key words: Economic development, GDP, inflation, social change, governmental finance.

Tabl.4, fig.1, ref.7

Ш. Шабурішвілі**СОЦИАЛЬНЫЕ ИЗМЕНЕНИЯ И ЭКОНОМИЧЕСКОЕ РАЗВИТИЕ
ГРУЗИИ**

После распада Советского Союза Грузия пережила тяжёлый кризис, результате конфликтов страна потеряла свои территории, валового внутреннего продукта (ВВП) сократилась на 2/3. Грузия столкнулась с серьезными проблемами в процессе трансформации экономики. Курс взятый Грузией на европейские ценности не имеет альтернативы. Несмотря на достижение значительных успехов в политической, экономической и социальной областях, уровень и качества жизни населения по-прежнему остается крайне низкими. Удовлетворение общественных потребностей значительно отстают от высоких темпов экономического роста. В настоящее время Грузия сталкивается с целым рядом экономических проблем, которые необходимо решить своевременно, в противном случае макроэкономическая стабильность страны столкнется с серьезными угрозами.

Ключевые слова: экономическое развитие, ВВП, инфляция, социальные изменения, государственные финансы.

Introduction. Immediately after regaining its independence, Georgia began to build a democratic, legal state oriented to market economy. However, during the transition period the country faced serious difficulties (civil war, military activities in Abkhazia and former South Ossetian Autonomous Region, hyperinflation, economic collapse, loss of old and traditional markets, energy and transport blockade, extremely tense criminal situation, Georgia-Russia war, etc.). However, due to the reforms, the country began to overcome economic and social problems gradually. Constitution of the country was adopted, various laws were developed, Georgian national currency was adopted and a number of reforms were carried out almost in all spheres of public life[1]. However, the reforms were often random and not successive, as a result, they could not bring the desired result. Although, in recent years there were high rates of economic growth, majority of the population didn't benefit from that, task of reducing poverty and unemployment was not performed. Many other extremely important and pressing economic and social threats also remain in the agenda. Solution of these problems requires serious, reasonable and thoughtful activities.

The main goal of the following study is to analyze the social-economic situation of Georgia and detection of the existing issues throughout the internationalization process. Therefore, the main focus of this article are the macro-economic parameters reflecting

county's social-economic situation, these are: economic growth, inflation, unemployment, governmental finances. Also, the study specifically focuses on analyzing such indicators crucial to the process of internationalization, those are: foreign trade and foreign direct investments.

Economic growth. There was a clear growth tendency of the economic indicators in Georgia only the exception was 2009 (-3.7 %) and it was caused by the consequences of global economic crises and Russian-Georgian war. From 2015 the economic growth pace started decreasing and amounted 2.8%. Such a slowdown of economic growth tendencies on the one hand were caused by foreign factors – difficult political situation in the region and global economic meltdown. On the other hand, the change in economic policy orientation of the new government which is reflected in the transformation from liberal to socially oriented model.

Inflation. In 2012 the decline of prices on goods and services was to be clearly seen in the situation where the national bank of Georgia estimated 6 % of target indicator and that trend was maintained in 2013 as well. In coming year the inflation rate increased, however, it still was behind the target indicator. The prices increase was triggered by the deepening deficits into current accounts and currency shocks. Between 2014 and 2015 Georgian national currency (GEL) has devaluated towards USD by 40 %. Mentioned process had negative impact on economic growth because it was the consequence of reduction of overall demand in export share, hence, active growth did not take place.

Table 1. Inflation¹

	2007	2008	2009	2010	2011	2012	2013	2014	2015
Yearly Average form prior year average	109.2	110.0	101.7	107.1	108.5	99.1	99.5	103.1	104.0
December from prior December	111.0	105.5	103.0	111.2	102.0	98.6	102.4	102.0	104.9

Unemployment. In recent years the population of Georgia is characterized by declining tendency. Population has been reduced from 5424.4 thousand to 3729 thousand people from 1990 to 2015. 57 % of countries population lives in the cities, while 43% lives in the villages. The Decline tendency of population number is obvious, as well as rising tendency of the population in the cities. Due to the low standard of living and unemployment, migration indicator is high. By expert settlement, during last 20 years 30 % of Georgian population is emigrated to other countries. The amount of money sent by the emigrants to their relatives in Georgia is over a billion US dollars.

In previous years the average salary has been increased significantly. In 2015 nominal salary in the whole economy has been risen by 5 times compared to 2004. Despite the high rate of grows of income, it's average salary is considerably low not only compared to developed countries, but also, similar indicator of post-soviet countries.

In the last 2 years despite the unprofitable economic conjuncture, ongoing demographic process in Georgia, particularly economically active population approaching the pension age and migration, supported the unemployment decrease. At the same time, the low indicator of employment in youngsters addresses that unemployment still remains one of the main social and economic issues. As a results of implementation of the recent reforms and budget sector structural transformation, thousands of people have lost their jobs. Hence, in the recent period foreign investment was partly followed by foreign labor what reduced jobs for the locals.

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¹ The source of the data given here and hereafter is the National Statistics Office of Georgia. www.geostat.ge

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Table 2. Unemployment level²

	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015
Economically active population (working force in thousands)	023.9	021.8	965.3	917.8	991.8	944.9	959.3	029.1	003.9	991.1	021.5
Employed-in thousands	744.6	747.3	704.3	601.9	656.1	628.1	664.2	724.0	712.1	745.2	779.9
Unemployed – in thousands	79.3	74.5	61.0	15.8	35.6	16.9	95.1	05.1	91.8	46.0	41.6
Unemployment level in percentages	3.8	3.6	3.3	6.5	6.9	6.3	5.1	5.0	4.6	2.4	2

In the perspective the solution of employment problems will be significantly depend on the quality of the economic development, small and medium size businesses development, improvement of the investment environment, raise of quality of labors and its competitiveness.

Governmental finances. There was a boost of Georgian economy after the global crisis in 2010 which has a positive reflection on decreasing of the budget deficit. The high level of the budget incomes supported strengthening government fiscal positions. There was 12% increase in revenues in 2015 compare to precious year and exceeded forecasted indicator by 3.7%. However, aforementioned growth is connected with the GEL devaluation, hence, increase in taxes. Moreover, there was increase in non-tax payments by 24% because of foreign subsidies reflected in higher volume in national currency. State expenditure remained in the planned frames and its fulfillment increased 96 percent. Planned expenditures were only exceeded by health sector. High indications of budgetary incomes and disciplined expenditures stipulated fiscal deficit of GDP down to 0.8%.

According to the fulfillment of budgetary incomes it can be said that the business environment has not been worsened in this component, moreover, there are some reserves in order to improve it by adopting tax liberalization. For that to be achieved government may employ an initiative of releasing businesses form taxes on reinvested profit.

Despite decreasing the deficit it is expected that state debt will increase from 35% to 46% of its GDP. It is caused by the situation that 80% of state debt is in USD therefore 40% GEL deflation has negative reflection on the budget. However, according to the flexible nature of the foreign debt of Georgia and the means ratio necessary to keep it at a safe level has not lost to the export counterpart significantly.

Foreign trade. At the current stage, foreign trade policy of Georgia greatly determines the main vector of the country's economic development. This is caused by low level of the country's economy, technical and technological backwardness and lack of investments. The world practice knows two different regimes of foreign trade – protectionism and free trade. Georgia chose the free trade regime, as a result nowadays it has one of the most liberal

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foreign trade policy.

Table 3. Average tariffs on imported goods in Georgia, %³

	2006	2007	2008	2009	2010	2011	2012	2013	2014
All goods									
Superior tariff- average	8,68	0,72	0,75	0,72	0,68	1,04	0,85	0,88	0,87
Preferential tariff - average	8.16	0.69	0.73	0.69	0.65	0.99	0.81	0.72	0.72
Agricultural goods									
Superior tariff - average	12,65	9,92	10,44	9,86	9,16	9,03	6,05	7,22	7,1
Preferential tariff - average	12.05	9.59	10.1	9.5	8.7	8.58	5.74	5.98	5.88
Manufacturing goods									
Superior tariff - average	8.42	0.08	0.08	0.08	0.07	0.46	0.47	0.46	0.46
Preferential tariff - average	7.91	0.07	0.07	0.07	0.06	0.44	0.45	0.38	0.38

Foreign economic policy of Georgia is characterized with preferential foreign trade regimes. Due to the reforms in customs system and technical regulations of customs unions, foreign trade regimes and customs procedures were simplified, import tariffs reduced and non-tariff regulations reduced to minimum. 16 import duties, existing in Georgia since 2006 reduced to 3 (0.5 and 12%), tariffs on almost 85% of imported goods and seasonal tariffs has been almost fully abolished. Tariffs on imported goods are regulated by tax code of Georgia. Export and re-export is free from customs duties. Georgia has free trade regimes with Turkey and CIS countries. Based on this regime trade with these countries is free from custom duties. Georgia benefits from Most-Favored-Nation regime (MFN) with the WTO countries. Georgia benefits from a Generalized System of Preferences (GSP) when trading with the European Union, the USA, Canada, Japan, Switzerland and Norway.

In 1995, Georgia was granted Generalized System of Preferences (**GSP**) by the EU. In 1996 Partnership and Cooperation Agreement (PCA) was signed between Georgia and the EU and some institutions were established to realize this agreement. Since 2005, Georgia benefits from new GSP+ regime when trading with the European Union. The GSP+ covers around 7,200 products and means removal of tariffs on products exported to the EU from Georgia. In November 2013, Georgia and the EU signed a memorandum of Association Agreement (AA) hoping to be finally signed in 2014. A very important part of this document is the agreement on Deep and Comprehensive Free Trade Area (DCFTA), which aims to support economic integration of Georgia in the EU, increase the volume of trade between Georgia and the EU by removing of tariffs and quotas, make the laws and regulations on trade closer to the EU's and finally to create deep and comprehensive free trade area.

Georgia signed Double Taxation Avoidance Agreements with 33 countries and agreements on encouragement and mutual protection of investments with 32 countries. Georgia's trade with the WTO countries is based on the principle of Most Favored Nations (MFN).

Direction of the foreign economic policy of Georgia is largely determined by active participation of the country in different international and regional organizations and programs, including with the following organizations in frames of the Black Sea regional cooperation:

- Black Sea Economic Cooperation (BSEC) – main objective of the organization is

³ITC, Market Access Map.

<http://www.macmap.org/CountryAnalysis/AverageTariffResult.aspx?country=SCC268%7cGeorgia&bysection=0>

to develop both bilateral and multilateral cooperation between the member states in the following fields: small and medium business, energy, agriculture, mining and processing industry, transport and communication systems, tourism, etc. Georgia actively cooperates with other member states of the organization.

- GUAM – members of the organization are Georgia, Ukraine, Azerbaijan and Moldova. The objective of cooperation between these countries is to strengthen economic ties between European and Central Asian countries. GUAM actively cooperates with Japan and the USA. It is planned to establish relations with Korea. In January 2013, Georgia became the chair of GUAM.

- CIS – the organization was established in 1991 and Georgia was the last country to join it in 1994. All the post-soviet countries were the members of the organization except the Baltic States. The aim of CIS was cooperation in economic, political and cultural fields. In 1993, the member countries signed the agreement to create economic union. After Russia occupied Georgian territories and recognized their independence in 2008, Georgia decided to withdraw from CIS. This didn't prevent the country to strengthen trade and economic ties with other members of the organization and it has a growing tendency.

Table 4. Trade partners of Georgia according to 2014 turnover⁴

Countries	export		import		turnover	
	thousand \$	%	thousand \$	%	thousand \$	%
Total turnover	2,860,670.6	100.0	8,593,325.4	100.0	11,453,996.1	100.0
Turkey	239,295.9	8.4	1,727,390.6	20.1	1,966,686.5	17.2
Azerbaijan	544,504.8	19.0	637,582.4	7.4	1,182,087.2	10.3
Russia	274,675.0	9.6	575,443.8	6.7	850,118.8	7.4
China	90,392.8	3.2	732,996.7	8.5	823,389.5	7.2
Ukraine	139,920.7	4.9	546,121.3	6.4	686,042.0	6.0
Germany	69,191.6	2.4	465,907.8	5.4	535,099.4	4.7
Armenia	288,084.7	10.1	210,138.2	2.4	498,222.9	4.3
USA	207,332.6	7.2	287,091.5	3.3	494,424.1	4.3
Bulgaria	167,104.8	5.8	209,825.6	2.4	376,930.4	3.3
Japan	3,285.0	0.1	368,173.8	4.3	371,458.8	3.2
Total 10 countries	2,023,787.9	70.7	5,760,671.6	67.0	7,784,459.6	68.0
Rest of the countries	836,882.7	29.3	2,832,653.8	33.0	3,669,536.5	32.0

In recent years, Georgia's trade relations have obviously deepened with the neighboring countries, especially with Azerbaijan, Turkey, Armenia and Ukraine. Since 2013, a new direction becomes visible in trade relations with Russian Federation. After restoration of state independence of Georgia and collapse of the Soviet Union, trade relations between Georgia and Russia did not break off. However, as political relations between two countries tensed in 2006, Russia declared an embargo on the import of agricultural goods, including wine, from Georgia. As a result of military conflict between Russia and Georgia in 2008 and occupation of Georgian territories, two countries completely broke off diplomatic relations. Consequently, economic relations between the countries ceased. In 2013, the new government of Georgia decided to restore trade relations with Russia. As a result, export of Georgian agricultural products (wine, nuts, grapes, pear, quince, citrus, etc) to Russia began. Georgia's largest trade partner countries in 2014 are shown in Table 4.

Foreign direct investments. Between 2004-2005 foreign direct investments were estimated not more than half a billion USD. In 2006 it grew rapidly and reached 1.2 billion USD. However, it peaked in 2007 outreaching the number of 2 billion USD. In coming years it started decreasing and only in 2011 slightly exceeded 1 billion USD. In 2015 the inflow of

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foreign direct investments in Georgia was estimated 1564,5 mm USD which is significantly lower compare to the prior year (1758,4 mm USD). Therefore, it can be said that in past years there was no clear growth tendency in terms of foreign direct investments inflow in Georgia.

Whilst analyzing foreign direct investments in Georgia it is important to discuss their dissemination by the economic sectors.

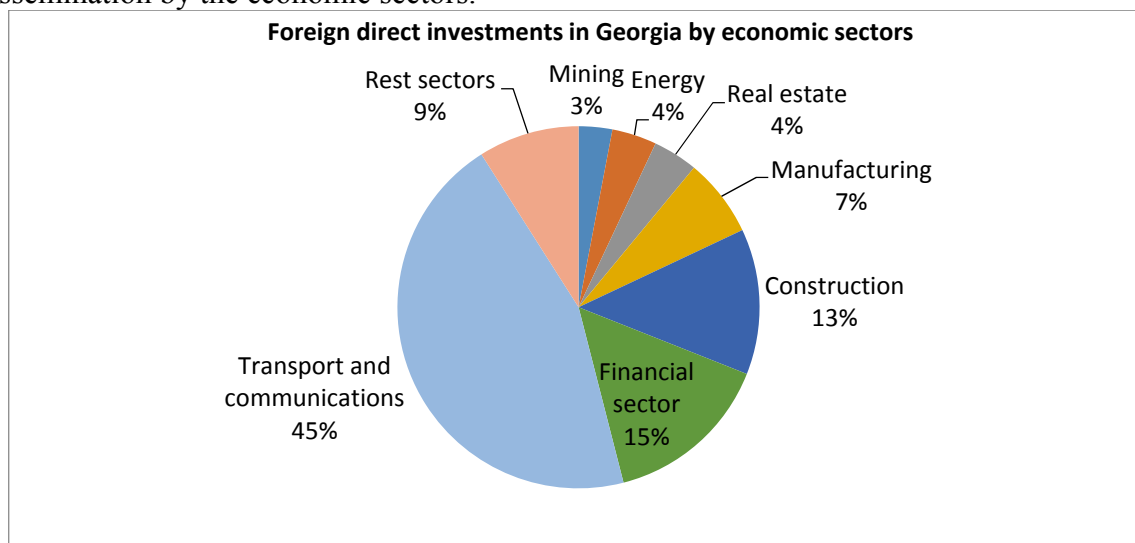


Diagram 1. Foreign direct investments in Georgia by economic sectors (2015 year)⁵

The process of privatization is the lifeblood of foreign direct investments in Georgia. Investors are mostly interested in such sectors, like: transport and communications, financial sector, Construction sector, real estate energy and mining. Rest of the sectors appears to be less attracted by investors for instance despite declaring the agricultural sector as a priority by Georgian government did not spawn more than 3% of overall investments. The same situation can be observed in the sector of modern technologies. Accordingly, investments in Georgia have positive impact on the infrastructure. Whereas, manufacturing and export machinery sectors are less successful.

According to the official statistics from 1996 to 2015 foreign direct investments in Georgia is estimated by 14,5 billion USD. Almost, half of the investments came from EU (42%). After launching the association agreement more investments are thought to be flowing in. although, It has to be said that there is a high share of investments from off shores what means the low reputation and dubious individuals of companies are investing in the country. As it is well-known this is not serious style and form of activities which might alter the direction of the national economy. These types of investors mainly are interested in high profit goods which might be damaging to the economy.

To sum up it can be said that the inflow of foreign direct investments in Georgia is not sustainable. The declining number of privatization object will be reflected in decrease of foreign direct investments which can expose the threat to the macro-economic stability of the country.

Conclusion. In conclusion it can be said that the slowdown of the economic growth of Georgia is determined by the difficult political situation in the region and global economic meltdown. Also, the change in economic policy orientation of the new government was reflected in the transformation from liberal to socially oriented model. The increase in prices was caused by currency shocks from deficits into current accounts. Despite the unfavorable economic situation the demographic processes (aging population and migration) declined unemployment level. However, low employment level in younger population and low average salary indicates that unemployment still is an issue to the country's economy.

⁵ The source of the data given here and hereafter is the National Statistics Office of Georgia. www.geostat.ge

According to the fulfillment of budgetary incomes it can be said that the business environment has not been worsened in this component. However, this situation is connected with the GEL devaluation, hence, increase in taxes.

The liberalization of the foreign economic policy deepened Georgian integration into world economic processes. The inflow of foreign direct investments was not characterized with clear growth tendencies. Chiefly, Foreign direct investments had positive influence on country's infrastructure but was less effective by manufacturing and exporting machinery. The foreign trade turnover is yearly increasing but balance of trade is still in deficit which is a significant economic threat. There is a new orientation highlighted in recent years. The most important is the signing the association agreement between EU and Georgia and also, resuming trade relations with Russia.

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