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Georgia—Recent Economic Developments

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GEORGIA

Recent Economic Developments

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Georgia: Basic Data, 1993-1997

I. Social and Demographic Indicators

Area	69,700 sq. km
Population density (1995)	77.0 per sq. km
Population (estimated 1995)	5.37 million
percent urban	55.6 percent
Rate of population growth (1990)	0.1 percent
Life expectancy at birth (1990)	72.6 years
Infant mortality rate (per 10,000 people-1990)	159
Hospital beds (per 10,000 people-1990)	108
GDP per capita, 1996	1,066
in lari	853
in U.S. dollars	

II. Economic Indicators

	1993	1994	1995	1996 Prel. Est.	1997 Proj.
(Percentage change)					
Real sector					
GDP volume	-25.4	-11.4	2.4	10.5	8-10
Consumer prices					
Period average	3,125	15,606	163	39	11-13
12 months to end of period	7,488	6,474	57	14	10-12
(In percent of GDP)					
Government finances					
Revenue and grants	9.7	7.7	7.1	9.4	11.4
Of which: Revenue	2.3	4.2	5.1	8.1	10.7
Expenditure and net lending	35.9	24.3	12.3	13.9	14.2
Balance (accrual)	-26.2	-16.5	-5.3	-4.5	-2.8
Balance (cash)	-26.2	-7.4	-4.5	-4.4	-3.5
(Percentage change, end-period)					
Money and credit					
Net domestic assets of the NBG	572	2,091.7	162.1	159.4	54.6
Credit to enterprises and households 1/	2,048	3,448.3	43.3	-14.8	25.6
Broad money					
Including foreign currency deposits	4,319	2,229.5	146.4	41.9	34.8
Excluding foreign currency deposits	2,462	1,796.7	362.5	38.2	36.3
(In millions of U.S. dollars)					
Balance of payments					
Merchandise exports	457	381	347	400	442
Merchandise imports	-905	-746	-686	-733	-817
Trade balance	-448	-365	-339	-332	-375
Current account before transfers	-485	-448	-407	-350	-362
Official reserves, end-period, (in millions of U.S. dollars)	1.0	41	157	157	170
(in months of imports)	-	0.7	2.7	2.5	2.5
Memorandum items:					
GDP, current prices (in millions of lari) 2/	16.4	1,373	3,694	5,724	7,052
Exchange rate, lari per U.S. dollar 3/					
Period average	...	1.10	1.29	1.26	1.3
End period	0.1	1.28	1.23	1.27	...

Sources: Data provided by the national authorities; and staff estimates.

1/ The sharp fall in 1996 reflects the carve out of a US\$41.6 million loan from the Turkish Eximbank to the Georgian former Eximbank. Had this loan been included, credit to enterprises and households would have grown by about 30 percent in nominal terms.

2/ The Georgian national accounts suffer from severe problems of coverage, measurement of deflators, and internal consistency.

3/ According to the Tbilisi Interbank Currency Exchange.

I. INTRODUCTION

1. During the past two years Georgia has made major strides in stabilization and structural reform. Following the implementation of tight financial policies and the liberalization of prices, trade and the exchange system, growth resumed in 1995 and accelerated in 1996, against the background of a stable exchange rate and declining inflation. At the same time structural reform has continued to advance, laying the ground for increased private sector activity and sustained growth in the medium term.
2. With the restoration of law and order, economic recovery has been fueled by strong growth in agriculture, construction and trade, in response to the substantial progress achieved in legal reform and privatization, as well as the liberalization of prices and of the exchange and the trade system. Inflation has declined steadily since the stabilization and reform program was launched in 1994. The average monthly rate of inflation fell from the hyperinflationary level of 62 percent in the first nine months of 1994 to about 4 percent in 1995 and about 1 percent in 1996.
3. Fiscal consolidation has been a key element of stabilization. The overall fiscal deficit (on a commitment basis and excluding grants) was reduced drastically from 20 percent of GDP in 1994 to 7.3 percent in 1995, and 5.7 percent in 1996. The fiscal adjustment in 1996 was mainly the result of improved revenue performance, while budgetary expenditures relative to GDP increased for the first time during the reform program. Tax revenue was boosted significantly through the removal of most tax exemptions, the imposition of new taxes, and as a result of the ongoing reforms in tax and customs administration. Despite these encouraging developments, the public finances remain weak and highly dependent on external financing.
4. Following the introduction of the lari in October 1995, a gradual remonetization of the economy took place and gross international reserves were replenished, reaching 2.5 months of import cover by the end of 1996. In view of declining inflation, relative exchange rate stability and some signs of increased financial intermediation, the strong growth in monetary aggregates during 1996 appears to reflect an increase in the demand for real money balances. Banking sector reform is at an advanced stage, following the introduction of new prudential regulations and enhanced banking supervision, which led to a significant downsizing of the banking sector. Despite notable progress, financial intermediation remains very low.
5. External developments in 1996 were marked by a continued reduction in the current account deficit and by substantial progress in normalizing relations with external creditors. In addition, Georgia accepted the obligations under Article VIII of the Fund's Articles of Agreement. Following a sharp decline of imports and exports in 1995, the former on account of reduced levels of wheat and energy imports, available data suggest a turnaround in trade developments in 1996. The recovery of output contributed, *inter alia*, to a strong export recovery, while imports were boosted mainly on account of higher disbursement of project loans, as well as increased foreign direct investment activity. Bilateral debt rescheduling

agreements were signed with seven creditors, including the two largest (the Russian Federation and Turkmenistan) in 1996 and early 1997.

6. The pace of structural reform accelerated in 1996. Restructuring of the agricultural and enterprise sectors and private sector development were pursued through privatization and the introduction of an appropriate legal framework. Privatization of small-scale enterprises is virtually complete and the privatization of medium- and large-scale enterprises has picked up considerably, mainly through mass privatization schemes, while most arable land is under private ownership. A number of laws were adopted during 1996 to boost private sector activity and investment; the agenda for 1997 includes further strengthening of the legal framework, with emphasis on improved enforcement. Energy sector reform gained momentum in 1996 with the restructuring of the domestic electricity utility and the announcement of a privatization program for the sector, to be launched in early 1997. Efforts to upgrade the organizational structure of the energy sector were accompanied by an improvement in collection rates and the decision to adjust electricity tariffs with a view to achieving cost-recovery in the sector.

7. The continued success in the implementation of Georgia's reform program will require the pursuit of prudent financial policies, including determined efforts to increase tax revenue and achieve further fiscal consolidation. These policies will need to be accompanied by the acceleration of structural reforms in order to reduce bottlenecks which could hamper growth prospects. External assistance will continue to play a vital role in ensuring the success of the authorities' reform efforts.

II. REAL SECTOR DEVELOPMENTS¹

8. *Economic recovery resumed in 1995 and accelerated in 1996, following the substantial progress in stabilization and the introduction of key structural reforms. Price liberalization is essentially complete, the trade system is virtually free of restrictions, and significant progress has been made in privatizing enterprises and agricultural land, restructuring the financial sector, and introducing a legal framework suitable for a market economy. For sustained economic growth, however, further progress is required in developing a sound banking sector, accelerating the privatization of medium- and large-scale enterprises, restructuring the energy sector, extending privatization to urban and industrial land, enforcing existing laws and regulations, and improving the country's infrastructure.*

¹Throughout the report, coupon figures for the period before the introduction of the lari have been converted to lari at the rate of one million coupons to one lari.

A. The output recovery and prospects for growth

9. Following a modest output recovery of 2.4 percent in 1995, real GDP grew by some 10 percent in 1996 (Appendix I, Table 1 and Figure 1). Agriculture, construction and trade led the recovery, responding favorably to the restoration of law and order, macroeconomic stability, the introduction of liberal trade and exchange systems, and the significant progress in privatization and legal reform. So far, the strong output response has come mainly from the reallocation and increased utilization of resources, while the recovery of savings and investment, although on the rise, has been rather slow (Appendix I, Table 2). With growing confidence in the authorities' reform program, Georgia is gradually becoming an attractive place for foreign investments.

10. **Agricultural production** continued to recover at a strong pace during 1996. Following an 18 percent real growth in 1995, agricultural output is estimated to have increased by 10–12 percent in 1996, mainly from an expansion in the area under cultivation, notably in the production of grain (Text Tables 1 and 2). However, the recovery in agricultural productivity has been hampered by adverse weather conditions and a shortage of financial and physical capital.

Text Table 1. Georgia: Selected Agricultural Output, 1990–96
(In thousands of tons)

	1990	1993	1994	1995	1996 (Prel. est.)
Cereals	666	440	479	526	630
Sunflower	8	8	8	8	7
Sugar beets	31	15	8	14	...
Tobacco	9	4	3	1	...
Vegetables	443	270	413	428	500
Potatoes	294	190	297	353	360
Tea	516	136	61	39	33
Grapes	691	157	251	422	350

Source: Ministry of Agriculture.

11. As of end-1996, the private sector accounted for over 85 percent of agricultural output. The structure of agricultural output has also changed significantly; the share of wheat and maize in total agricultural production has increased, while the share of traditional products, notably tea and grapes, has declined significantly. Agriculture is expected to remain Georgia's main engine of growth in the next few years, as price liberalization, private land

Figure 1. Georgia: Macroeconomic Indicators, 1992-96

Sources: Georgian authorities; and IMF staff estimates.

1/ Before December 1993, according to the Retail Price Index; after December 1993, according to a 295-good Laspeyres index using a methodology introduced by a STA mission.

ownership and other structural reforms result in increased productivity in this sector (see Section II. C below).

Text Table 2. Georgia: Area Under Cultivation, 1992–1996
(In thousands of hectares)

	1992	1993	1994	1995	1996
Grain	112.8	84.9	69.3	80.0	120.6
Maize	94.8	110.0	150.0	180.0	242.5
Sunflower	12.4	12.0	18.0	36.2	48.0
Potato	22.3	18.0	12.0	23.2	25.7
Vegetables	24.9	22.0	17.0	28.6	25.6

Source: Ministry of Agriculture.

12. Available data suggest that the decline of industrial output may have bottomed out. Industrial output is estimated to have increased by about 4–5 percent in 1996, compared with a 10 percent decline in 1995. Energy and agroprocessing industries are leading the industrial recovery, while other traditional activities including, *inter alia*, metallurgical, chemical, and machine-building industries, are ailing (Appendix I, Table 3). Further progress in privatization of medium- and large-scale public enterprises is expected to improve recovery prospects for industry.

13. The service sector has boomed since independence and is now a leading sector in Georgia's economic recovery. During 1996, trade and construction activities, both among the fastest growing sectors in Georgia, are estimated to have increased by over 8 percent and 16 percent, respectively. However, the recovery of the transport sector has been modest, reflecting in part a significant decline in transshipment of humanitarian aid through Georgia (Appendix I, Table 4). Improved performance in the service sector is expected to boost productivity in other sectors, given Georgia's favorable geographic location as well as its tourism potential. Transshipment of goods to the neighboring countries is expected to recover significantly as economic activity in the region picks up. In addition, with the restoration of law and order, recovery of tourism is also expected.

B. Prices, wages and employment

14. Following a sharp fiscal adjustment since end-1994, accompanied by the adoption of a prudent monetary policy, the inflation rate, as measured by the 12-month change in the Tbilisi CPI, declined from 6,474 percent in 1994 to 57.4 percent in 1995 and 13.9 percent in 1996 (Figures 1 and 2).² This favorable inflation performance, despite a significant increase in

² With Fund technical assistance, the authorities introduced in 1996 a national CPI, which includes the 5 largest cities of Georgia (Tbilisi, Kutaisi, Gori, Batumi, and Telavi). The change in the 12-month national CPI for 1996 is 13.5 percent, broadly in line with the 13.9 percent change in the Tbilisi CPI during the period.

Figure 2. Georgia: Inflation and Exchange Rates, 1994-96

Source: Georgian authorities.

1/ Price indices of tradables and non-tradables calculated on the basis of individual weights and price indices of the 295 goods and services included in the consumer price index.

2/ Price of tradables relative to non-tradables; increase means appreciation.

3/ Increase means depreciation.

monetary aggregates since the introduction of lari in October 1995, appears to be associated with an increased demand for real money balances, reflecting a growing confidence in government policies (see section IV. A below). The higher inflation in non-tradables compared to tradables during 1995 and 1996 was reflected in a real appreciation of the lari (Figure 2).³

15. Real wages continued to recover during 1996, but are still far below the level in most other states of the former Soviet Union. The average wage in budgetary organizations increased by about 70 percent in real terms during 1996.⁴ During this period, pensions and the minimum wage in budgetary organizations also increased in real terms, by about 24 percent and 31 percent, respectively (Appendix I, Table 6). In addition, the civil service wage structure was significantly decompressed in 1996, as a result of efforts to rationalize the wage structure so as to enable the government to retain qualified staff (Figure 3).⁵ Available information indicate that the average wage in the private sector was likely to be closer to about lari 50 per month (US\$40) as of June 1996.⁶ The average wage for the overall economy is reported to have increased by about 22 percent in real terms by mid-1996 relative to the end-1995 level, although these data appear to underestimate wages in the agriculture, trade, and other service sectors (Appendix I, Table 7).

16. Official data indicate that total employment as of mid-1996 increased slightly relative to the end-1995 level, reflecting a further shrinking of industrial sector employment and a continued increase in private sector employment (Appendix I, Table 8). Registered unemployment was about 53,000 as of end-November 1996, a decline of over 18 percent from the end-1995 level (Appendix I, Table 9). However, official estimates indicate that the number of jobless people who are actively seeking work is significantly higher, at about 500,000 by end-1996, or about 16 percent of total labor force.⁷ The decline in registered

³ For a discussion on real exchange rate developments and their implications for Georgia's real economy see section V.D below.

⁴ This increase reflected across-the-board increases of budgetary sector wages in February and in June to compensate for the bread price liberalization, as well as a doubling of education sector wages in September, while the end-period inflation rate was 13.9 percent during 1996.

⁵ For details on the civil service wage reform during 1996 see section III. D.

⁶ These data are subject to large margins of errors; according to a household survey conducted in Tbilisi in mid-1996, the average salary per employed person in the Tbilisi region was higher, at lari 58 per month (US\$46), while the salary of self-employed was about lari 160 per month (US\$126).

⁷ Data from the June 1996 household survey show that unemployment in Tbilisi is about 25 percent of the total labor force.

Figure 3. Georgia: Real Wages and Pension 1/

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Sources: Georgian authorities; and IMF staff estimates.

1/ Wages in budgetary organizations.

unemployment, currently at about 10 percent of estimated unemployed, is likely to be a result of very low unemployment benefits, which tend to discourage registration by the unemployed.

C. Structural reforms

Price liberalization

17. Price liberalization is essentially complete. The only prices remaining under control are: gas, electricity, municipal and communication services, pharmaceutical products, and trolley bus, railway, and subway tickets. In 1996, the government liberalized the bread price, following a series of administrative increases since 1992, and increased by about 100 percent on average the administered tariffs for communication services and for commuter train and urban transportation.⁸ The electricity tariff applied to households was also adjusted in early 1997 (see below).

Privatization and enterprise restructuring

18. Georgia has made quick progress in privatization, while eliminating budgetary subsidies to state-owned enterprises (SOEs) and introducing a legal framework conducive to private sector development. To eliminate bottlenecks to private sector development, an acceleration of the privatization process is required, together with further progress in developing capital markets and strengthening the court system to deal effectively with bankruptcy cases.

19. To promote an efficient restructuring of the state-owned enterprise sector, the authorities have adopted a strategy aimed at transferring quickly control over SOEs to the private sector, mainly through mass privatization schemes and open cash auctions, while at the same time creating a legal and regulatory framework for encouraging the private sector to carry out the restructuring of the privatized enterprises. This strategy was adopted on account of the large number of SOEs to be privatized, a severe shortage of budgetary resources, which undermined the Government's ability to restructure SOEs before privatization, and a lack of interest from foreign investors.

20. The privatization of SOEs has proceeded quickly. Small-scale privatization is now virtually complete and the privatization of medium- and large-scale enterprises accelerated during 1996. By mid-October 1996, about 88 percent of an estimated total of 9,308 small-scale enterprises, had been privatized (Text Table 3).⁹ In addition, about 515 medium-

⁸ The bread price increased by about 40 percent, following an administrative adjustment in February 1996, and by another 15-18 percent on average in June 1996, following the price liberalization.

⁹ The number of small-scale enterprises has continued to expand as some of them were
(continued...)

and large-scale SOEs were privatized by end-November 1996, out of a total of about 1,200 enterprises.¹⁰

Text Table 3. Georgia: Small-scale Privatization by Sector
(as of mid-October 1996)

Sectors	Total number of small-scale enterprises by sector	Number of privatized enterprises
Trade	3,556	3,184
Public service	3,608	3,239
Industry	319	195
Agriculture and food	548	201
Construction ¹	165	200
Transport ¹	73	75
Social sphere ¹	85	352
Power supply	31	23
Oil production	163	163
Health care	641	447
Bread production	119	79
Total	9,308	8,158

Source: Ministry of State Property Management.

¹The number of privatized enterprises in the construction, transport, and social sphere is higher than the original number of enterprises for the sector because of restructuring.

21. While cash payments were the primary privatization method for small-scale SOEs, the privatization of medium- and large-scale SOEs has so far been carried out mainly through mass privatization schemes (Text Box 1 and Text Table 4). This approach has led to a dispersed ownership structure (Text Table 5),¹¹ which was expected to slowdown somewhat the restructuring process of privatized SOEs. Nevertheless, a recent World Bank study indicates that the privatized SOEs in Georgia are performing better than the SOEs under

⁹(...continued)
segmented into smaller units.

¹⁰ Small-scale enterprises are defined as those with a book value of less than 50 million Russian rubles as of January 1993, while medium- and large-scale enterprises are those with a book value beyond this threshold.

¹¹ Since the expiration of privatization vouchers in June 30, 1997, cash auctions and international tenders open to domestic and foreign investors are the main methods of privatization.

majority state ownership.¹² Of the enterprises covered by this study, while the majority of the privatized SOEs had improved their financial performance through reductions in their labor force, better marketing, and introduction of new products, only a few of the enterprises remaining under majority state ownership had undertaken any deep restructuring, and were facing difficult financial conditions.

Text Table 4. Georgia: Distribution of Privatized Shares in Medium- and Large-Scale State-Owned Enterprises by Method of Sale
(as of October 15, 1996)

	Method of sale	Percent of shares
1.	Sales in cash	28.8
2.	Free to employees	5.8
3.	Voucher auctions	60.0
4.	Other	5.4

Source: Ministry of State Property Management.

Text Box 1. Georgia: Mass Privatization

The mass privatization methods used to privatize medium- and large-scale SOEs include voucher auctions and management/employee buy-outs.

Voucher auctions. The mechanism of privatization through voucher auctions, which expired on June 30, 1996, was the main method used in the initial privatization phase of the medium- and large-scale SOEs. Every Georgian citizen was eligible to receive one voucher. About 4.3 million vouchers were issued (about 84 percent of the registered population) at a nominal price of US\$30. At least 35 percent of the shares in medium- and large-scale SOEs were reserved for voucher privatization. During the period June 1995-June 1996 about 45 voucher auctions were conducted, with shares of about 800 medium- and large-scale SOEs being offered for sale. By June 30, 1996, about 95 percent of total vouchers issued had been used.

Management/employee buy-outs. The Government also granted to the managers and employees of the SOEs the right to buy 51 percent of the shares of their enterprises. This option, which expired in October 1995, required that 30 percent of the payment be made through privatization vouchers by November 15, 1995, while the remainder was to be paid in cash at a discounted price by July 1, 1996. However, if the first installment was not paid in full, the managers/employees would lose the right to purchase the remainder of the shares. About 600 SOEs applied for the management/employee buy-out option, of which only 140 paid the first installment in full. About 400 SOEs made a partial payment of the first installment, but lost the right to buy the remainder of the shares.

¹² In August 1996, the World Bank conducted a case study on the financial performance of the enterprise sector in Georgia. The study consisted of a sample of 21 enterprises, selected to include firms from a variety of sectors and geographic regions with diverse size and ownership structure. The sample size was small, however, and the enterprises were not randomly selected.

22. Enterprise restructuring and private sector development have also been promoted through the creation of a legal framework conducive to private activity and investment. During 1996, Parliament adopted a number of important new laws, including bankruptcy and anti-monopoly laws, as well as the law on the promotion and guarantees of investment activities in Georgia.¹³ In addition, in 1997 the authorities intend to extend land privatization to industrial and urban land, and also adopt a new securities law, which would establish rules for the disclosure, trading, and listing of securities.

**Text Table 5. Georgia: Distribution of Shares by Groups of Shareholders
in Medium- and Large-Scale SOEs
(as of October 15, 1996)**

Shareholders		Percent of owned shares
1.	Individuals	66.2
2.	Investment Funds	3.9
3.	Foreign Investors	19.8
4.	Other Legal Persons	10.2

Source: Ministry of State Property Management.

Agricultural reform

23. Restructuring of the agricultural sector gained momentum in 1995. Following the elimination of export taxes for agricultural products in late-1994, the Government abolished the state order system in June 1995. By the end of 1995, more than 75 percent of arable land slated for distribution in 1992 had already been distributed to private farmers, while at the same time most of the agricultural land, *de jure* under the control of state and collective farms, was already in private use. In addition, the legal basis for an efficient functioning of the land market is now in place. These reforms, together with the trade and price liberalization measures undertaken during 1993 and 1994, improved availability for farm inputs, and the development of private trade channels for agricultural products, contributed to a strong rebound in agricultural output in 1995. However, by end-1995 agricultural land reform was still at an early stage and activity in the sector continued to suffer from a virtual lack of financial services to private farmers.

24. A number of far-reaching structural reforms in the agricultural sector were implemented in 1996. With regard to agricultural land market reform, Parliament enacted a law on private ownership of agricultural land in March, a law on leasing of state-owned agricultural land to private farmers in September (which was amended in December), and a

¹³The later law replaced the previous Investment Law which granted, *inter alia*, generous taxation incentives for investment.

law on land titling and registration in November. These laws: (i) introduced the rights to sell, buy, lease and inherit agricultural land that was distributed to private farmers under the 1992 land reform program; (ii) established procedures for leasing state-owned agricultural land to the private sector on a competitive basis; and (iii) established the legal framework for developing a modern land registration and land cadastre system. The World Bank is assisting the authorities in developing a land registration and land cadastre system in two districts of Georgia under an agricultural sector credit, in accordance with the requirements of the new land titling and registration law. By October 1, 1996 about 50 percent of total arable land and 63 percent of all land under perennials had been distributed to private individuals; it is expected that by April 1997 all the remaining agricultural land slated for distribution to private farmers under the 1992 land reform program will be distributed and privatized, bringing private ownership of arable land and land under perennials to 62 percent and 82 percent, respectively.

25. Developing an efficient financial system to support agricultural activity is another key element of the Government's reform strategy in agriculture. Financing of private farmers is currently constrained by high transaction costs of small-scale rural lending as well as the inexperience of commercial banks in assessing risk in agricultural lending. To address the situation, the Government has undertaken important steps to promote the creation of small credit unions (CUs), which would mobilize local savings, reduce the need for collateral, and also cut transaction costs. The Government has established a Credit Union Development Center, which will encourage the development of rural CUs, approve on-lending to CUs, and ensure that CUs comply with the relevant prudential regulations.

Energy sector restructuring

26. The restructuring of the energy sector accelerated during 1996. Commercialization of electricity companies is already under way and their privatization process is expected to start by mid-1997. Collection rates of electricity improved significantly in 1996 relative to previous years, although a further improvement is necessary to restore financial balance. To rationalize domestic consumption and promote private sector participation in the sector, the electricity tariff to households was raised by over 30 percent effective January 1997 and is expected to be adjusted further by mid-1997. With financial assistance from international financial institutions and various bilateral official creditors, a number of important projects for the rehabilitation of the electricity infrastructure are currently under way.

27. Georgia inherited an energy intensive economy, which relied heavily upon imports of energy. The main domestic energy resource is hydropower, although during winter it is not sufficient to meet domestic demand for electricity. Other domestic power resources include oil, gas, and coal, all of which are scarce and do not meet domestic demand. Turkmenistan has historically been Georgia's main supplier of gas and the Russian Federation its main supplier of oil.

28. The energy sector entered a severe crisis following Georgia's independence. Inadequate government response to curb domestic demand for energy, in the face of a sharp

increase in import prices of energy, together with a collapse of domestic energy production and a deterioration of the balance of payments position led to a sharp accumulation of arrears to foreign suppliers of energy (see section V. B). In addition, due to the lack of proper maintenance and rehabilitation, as well as the severe damage of the electricity infrastructure during the civil war, the available capacity in the electricity sector by end-1996 was less than 30 percent of total installed capacity.

29. By the end of 1995, the Government had already undertaken a number of measures to improve the efficiency of energy use, as well as to adjust domestic consumption of energy to the available domestic supply and Georgia's limited capacity to pay for energy imports. These included, *inter alia*, introducing a series of increases in energy tariffs; eliminating guarantees for energy imports, effective June 1995; cutting off gas supplies to households since mid-1995, following a decline of collection rates to negligible levels;¹⁴ liberalizing oil product marketing and opening the energy sector to private initiative; and establishing a number of joint ventures in oil exploration and production with private foreign participation. These measures led to a drastic decline in domestic consumption and imports of energy, mainly from the productive sectors of the economy, including industry, agriculture, and transport, while households consumption actually increased slightly from the pre-independence levels (Figure 4). Despite the limited success in reducing domestic consumption of energy, however, at the beginning of 1996 the domestic demand for energy continued to exceed available supply, because electricity tariffs were set at below cost-recovery levels and collection rates remained very poor. In addition, the organizational structure of the energy sector by end-1995 had remained largely unchanged, hampering the recovery of the sector.

30. Several steps to advance energy reform were taken in 1996. With assistance from the World Bank, European Bank for Reconstruction and Development, USAID, European Union (EU), and other creditors (especially Germany and Japan), the Government embarked on a restructuring program aimed at (i) withdrawing the Government from commercial activities in the energy sector through privatization of energy companies; (ii) substantially raising collection rates; (iii) introducing cost-recovery tariffs while protecting vulnerable groups; and (iv) improving the regulatory framework so as to promote competition and private sector participation in the sector. In June 1996, the Government established an independent electricity regulatory commission, and also restructured the domestic electricity utility, Sakenergo, into three separate companies—for generation, transmission, and distribution, respectively. The transformation of these companies into joint stock companies is under way, and the Government announced in December 1996 a privatization program for generation and distribution companies, which is expected to be launched in April 1997. While transmission companies will remain, for the time being, under state ownership, to further rationalize domestic consumption of energy, effective from January 1, 1997, the electricity tariff to households was raised by over 30 percent, and all existing preferential tariffs applicable to various enterprises were removed. The Government is expected to adjust further the

¹⁴Delivery of gas to households started on a prepayment basis during the second half of 1996; as of end-1996 about 15,000 households were receiving gas supplies.

Figure 4. Georgia: Annual Imports of Natural Gas, 1990-96
(In billions of cubic meters)

Sources: Georgian authorities; and IMF staff estimates.

electricity tariff to households and unify it with the tariff applied on enterprises (currently 4.5 tetri per kW hour) with a view to achieving cost-recovery in the sector. During 1996, collection rates of electricity supplies improved significantly: compared to an average of below 20 percent in 1995, the collection rate reached about 50 percent in 1996.

31. In addition to the structural measures outlined above, the Government is also addressing as a matter of priority the rehabilitation needs of the energy network. Due to the significant financing requirements and the lack of budgetary resources, the necessary rehabilitation and repair of the existing network is currently being carried out mainly with financial assistance from international financial institutions and various bilateral creditors. Since 1995, about US\$170 million have been committed or are under consideration from these sources. According to World Bank estimates, the investment requirements for the energy sector through 2005 are about US\$800 million, of which about US\$300 million for the rehabilitation of the existing network and the rest for expanding its capacity after 2002. Initially, the bulk of this financing is expected to come from official external sources, but private sector participation is expected later as the legal framework improves and tariffs are set at cost-recovery levels.

III. FISCAL DEVELOPMENTS

32. *Following the collapse of output in the early 1990s, tax revenue declined to 2.3 percent of GDP in the first half of 1994 while the fiscal deficit (excluding grants and on a commitment basis) reached 50 percent of GDP. In late 1994 the Government began implementing an ambitious program to strengthen public finances. Dramatic adjustment of expenditure was effected through the virtual elimination of costly subsidies for bread and gas and by substantially downsizing Government. The 1995 fiscal position improved drastically compared to the massive deficit witnessed in 1994. In 1996, the bulk of the adjustment came through an improving revenue performance, owing mainly to ongoing tax and customs administration reforms, the removal of most tax exemptions, and the imposition of new taxes. Despite encouraging developments, tax revenue remains only sufficient to finance the most urgent expenditures. The Government's capacity to control expenditures and budget planning requires further improvement.*

A. Overview

33. At the start of 1995, the Government had already made major strides in fiscal adjustment (Figures 1 and 5). Although the fiscal deficit, excluding grants and on a commitment basis, was 20 percent of GDP in 1994, there was a substantial reduction in the second half, mainly through a sharp cut in subsidies. Nonetheless, a further strengthening of public finances was required in 1995, especially since external assistance was expected to decline relative to GDP. In the event, the deficit excluding grants was reduced to 7.3 percent of GDP, mainly because outlays were rationalized and efforts were under way to improve tax administration. In 1996, since further expenditure compression was unrealistic,

Figure 5. Georgia: Public Finances

Sources: Georgian authorities; and IMF staff estimates.

the authorities focused on a rationalization of tax policy, accompanied by a strengthening of tax and customs administration. The deficit excluding grants was scaled back further, to about 6 percent of GDP, driven by an increase in revenue equivalent to 3 percentage points of GDP. This allowed for an increase in expenditures relative to GDP for the first time since the reform program began (Text Table 6). At the same time, the ratio of total revenue to current expenditures increased further, reaching 63.2 percent in 1996 compared with 59.5 percent in 1995 and 19.6 percent in 1994 (Appendix I, Tables 10 and 11).

34. Over the past two years, the Government has adopted wide-ranging revenue and expenditure reforms. A key element of the 1995 program was the removal of about 120,000 health workers (22 percent of the government labor force) from the government payroll in August. In 1996, crucial measures included the elimination of a large number of tax exemptions, reforms in tax administration and the immediate increase of the statutory retirement age by five years in February. In addition, further progress was made in developing a Treasury at the Ministry of Finance.

35. As a result of an improving fiscal position, the Government has been able to reduce reliance on external support for budgetary financing. In 1996, external grants covered only 9 percent of expenditure commitments, compared with 14 percent in 1994 and 16 percent in 1995 (see section III. C below); similarly, net external loans funded only 12 percent of outlays, compared with 24 and 25 percent in the previous two years (Figure 6). Central bank financing of the budget deficit, however, reached 2.7 percent of GDP in 1996 compared to 1.6 percent of GDP in 1995 (Appendix I, Table 11).

Text Table 6. Georgia: Summary of General Government Operations
(In percent of GDP)

	1994	1995	1996		
			Jan.–June	July–Dec.	Annual
Total revenue	4.2	5.1	6.8	9.4	8.1
Grants	3.5	1.9	1.5	1.1	1.2
Expenditure and net lending	24.2	12.3	12.0	15.7	13.9
Deficit (on a commitment basis)					
Including grants	16.5	5.3	3.8	5.3	4.5
Excluding grants	20.0	7.3	5.3	6.4	5.8

Sources: Georgian authorities; and staff estimates.

36. In sharp contrast to 1994, the Government's capacity to control expenditures improved during 1995 and 1996, although this process is still far from complete. In 1996 expenditure commitments were not reduced in line with shortfalls in revenue targets and expenditure arrears increased further, reaching $\frac{1}{2}$ – $\frac{3}{4}$ percent of GDP at end-1996.

Figure 6. Georgia: Funding of Expenditures and Net Lending

Sources: Georgian authorities; and IMF staff estimates.

B. Institutional setting

37. From independence until end-1996, the State budget included the budgets of the Central ("Republican") Government and 65 local governments: the two autonomous republics of Abkhazia and Adzharia, ten administrative regions, and 53 administrative districts.¹⁵ Beginning in 1996, all extrabudgetary funds were integrated into the State budget, the largest being the Social Security Fund (SSF) for financing pensions and other social security benefits. Other extrabudgetary funds include the Employment Fund (EF); the Privatization Fund; the Health Fund; and the Road Fund (the latter two were set up in 1995) (Appendix I, Table 12). Starting from 1997, and in line with greater political autonomy granted to the regions, the "State" budget excludes all local government budgets, apart from the Republican Government transfer to them.

38. A Law on the State Budget was enacted in June 1996 providing for rules for designing and implementing the annual budget, which, *inter alia*, resulted in the establishment of a macroeconomic department within the Ministry of Finance (MOF). The budget cycle begins in May of the preceding year when the MOF receives initial budget proposals from the spending ministries and other budgetary organizations. Various rounds of discussion are then initiated. By October 1 a draft budget is sent to Parliament, which is required to enact the law 30 days prior to the beginning of the budget year on January 1. In implementing the budget, the annual budget appropriations are translated into monthly credits to the spending ministries. Since late 1994, the MOF limits these credits to projected revenues and available financing, taking the budget appropriations as an upper bound. The MOF monitors the budget execution using daily payment reports from the National Bank of Georgia (NBG) and monthly cash reports from the spending ministries.

39. The State Tax Service (STS) is the main agency responsible for collecting taxes. However, customs duties, VAT and excises on imports and exports are collected by the State Customs Department (SCD). Until end-1996, payroll taxes (social fund contributions) were collected directly by the SSF, EF and HF; but for 1997 it is planned that the STS will be responsible for collecting these taxes. For an interim period, various taxes for financing roads will continue to be collected by the Road Fund. Taxpayers typically deposit the amount of tax due in a local bank, which in turn allocates the revenues between the Republican and local governments according to the relevant revenue sharing formula (Appendix I, Table 13). The payment is then processed by the banking system and credited to the Republican Government account at the NBG or deposited in the bank account of the local government. Local STS and SCD offices provide information on tax payments to STS and SCD headquarters, which compile overviews of tax payments. Discrepancies exist between these overviews and data compiled by the MOF from the Republican Government revenue account at the NBG.

¹⁵Regional budget information is scarce, especially for regions where there has been a disruption of relations with the Republic. For Abkhazia, the State budget is confined to the transactions with the government in exile.

C. Revenues and grants

Revenues

40. Despite a significant improvement in revenue collection during the second half of 1995, at the beginning of 1996 revenue fell short of covering a sustainable level of recurrent expenditures. Georgia's tax revenue is significantly lower than its neighboring countries, although its tax rates are broadly in line with the rates in these countries.^{16 17} The main factors behind the weak tax revenues were: widespread statutory and *ad hoc* tax exemptions; an inefficient tax administration, which was unable to collect taxes from the growing number of private enterprises, particularly those in the informal sector; and an inefficient customs administration, which lacked the capacity to collect taxes at Georgia's porous borders.

41. A number of measures have been adopted to address these problems, of which the elimination of most exemptions in early 1996 was especially important. In addition, tax administration reforms are beginning to produce results, as the STS is in the process of being transformed into a modern and efficient tax administration. Although reforms of the SCD have begun more recently, they are producing rapid results as management problems have been addressed and tax collection on traded goods is improving, albeit from a low level.

42. These efforts resulted in a significant rise in total revenue, which exceeded 8 percent of GDP in 1996, an increase of over 3 percent of GDP relative to 1995. Increases were recorded in all taxes with the exception of profit taxes. More specifically, the main factors for this significant improvement in revenue performance include:

- **Removal of most tax exemptions**, which had led to a widespread abuse of the tax system, effective March 1, 1996. Previously there had been many legal exemptions, including for VAT on alcoholic beverages, certain foodstuffs, and other goods and services; import duty exemptions, including for personal imports over 300 lari per person per trip; and various exemptions from profit and personal income taxes. There were also many *ad hoc* exemptions for particular economic agencies and other entities.
- **Improvements in tax and customs administration**. Tax administration was suffering from the inability of the STS to enforce its authority on a large number of taxpayers, the lack of appropriate tax assessment, collection, and audit procedures, shortages of skilled staff, and other institutional bottlenecks, which contributed to widespread tax evasion. In particular, new privately-owned enterprises largely escaped taxation, as

¹⁶ In 1995, total revenue in Georgia was 5.1 percent of GDP, compared with an unweighted average of 27 percent of GDP in the other fourteen states of the former U.S.S.R.; revenue collection in these countries varied from 11 percent of GDP in Turkmenistan to 43 percent in Belarus.

¹⁷ An overview of the Georgian tax system is provided in Appendix II.

the STS was continuing to concentrate its collection efforts on state-owned enterprises. With Fund technical assistance, the authorities have made notable progress in ameliorating these difficulties (Text Box 2). As a result, the number of active registered taxpayers went up by 76 percent between January 1995 and January 1997 (Appendix I, Table 14).

- **New taxes** were introduced in September 1995 for financing road construction and maintenance. In particular, an entry tax was levied on all vehicles entering Georgia, and all vehicle owners must now pay an annual vehicle ownership tax. The objective of these taxes was to introduce "user pay" principles to road construction and maintenance. In 1996, there was a notable improvement in collections from these two new taxes.
- **Privatization revenues** also increased in 1996 relative to 1995, a reflection of the significant progress in the privatization of medium- and large-scale public enterprises;
- **The substantial increase in real wages**, as mentioned in section II. B above, widened the tax base for personal income taxes, and more importantly, for the payroll taxes that finance the Pension, Employment, and Health Funds. In the case of the social funds, this impact more than offset the lowering of total social fund contributions from 45 to 35 percent in the 1996 Budget.
- **Better recording** also affected the 1996 outcome, particularly for nontax revenues, under which budgetary organizations' "own" revenues are recorded (i.e. revenues not channeled into the MOF's revenue account at the NBG).

43. Tax arrears continued to increase during 1996, and reached the equivalent of 2.1 percent of GDP at end-year (Appendix I, Table 15). Arrears in contributions due to the Pension Fund constituted about one third of total arrears. For arrears of the other taxes, a large part of the increase occurred automatically, as interest of 0.5 percent per day was accrued on outstanding arrears. Overdue late payment penalties accounted for nearly 40 percent of the total stock of tax arrears to S.T.S. at end-1996. The stock would have been even higher at end-1996 had not the Government taken action to reschedule or forgive certain tax arrears outstanding at end-1995 through a presidential decree. This decree, dated September 1996: (i) rescheduled end-1995 arrears of selected enterprises over 1996-99, at an annual interest rate of 24 percent; (ii) netted out tax arrears of the Railways Department with budgetary arrears to that Department, (iii) netted out arrears of certain enterprises with the budgetary arrears regarding the shipment of goods to Turkmenistan by these enterprises; and (iv) forgave arrears caused by the blocking of enterprise accounts in the Central Bank of Russia. To address the problem of excessive penalties, in December 27, 1996, the interest rate on overdue payments was reduced to 0.1 percent per day; other excessive penalties (for under-reporting income, for not providing documentation to S.T.S., etc.) were reduced at the same time.

Text Box 2. Georgia: Improvements in Tax and Customs Administration

A program for strengthening tax administration started in late 1994, with the introduction of a number of legal measures to enhance the STS's authority to assess and collect taxes. These included:

- closure of businesses after prolonged wilful nonpayment of taxes;
- introduction of penalties on nonfiling;
- an increase in interest rates charged on tax arrears.

These initial reforms were followed by a wide-ranging program of tax administration measures that were implemented during 1995 and 1996 with Fund technical assistance. These included:

- the distribution of Taxpayer Identification Numbers (TINs) to existing taxpayers;
- a comprehensive survey to identify new taxpayers and issue TINs to them. The survey began in June 1996 and was continuing in 1997, in an effort to incorporate new enterprises in the tax net;
- reorganization of STS along functional lines;
- establishment of a Large Taxpayer Inspectorate, which covered 150 large taxpayers by mid-July 1996 and over 210 by early 1997;
- reduction of excessive penalties for late filing and payments, and for hiding income;
- computerization of STS Headquarters and two pilot Regional Tax Inspectorates (RTIs);

Reforms of customs administration have been more modest, although some initial steps were implemented during 1996, including:

- improved processing of imports (e.g. blocking entry of cargoes until full documentation; monitoring passage of transit vehicles, including escorting or compulsory checking at inland customs offices);
- information exchanges with customs offices of neighboring countries;
- incorporating in the tax net certain importers who were previously escaping the payment of excises;
- computerization and changes in management.

In 1997, tax and customs administration is planned to be improved further by:

- the enactment of the new Tax Code by mid-year, which further strengthens the STS's capacity to assess and collect taxes. In particular, there is provision for: allowing the STS to use presumptive and indirect methods for assessing tax obligations; quickly assessing and collecting taxes when legitimate tax collection is in jeopardy; and confiscation of assets for delinquent taxpayers;
- the use of the credit/invoice method for VAT through the retail stage, which will allow cross-checking of documents and improved collections;
- quantitative targets for a progressive reduction in tax arrears during the year;
- introduction of in-depth audits by regional tax offices;
- expansion of self-assessment by taxpayers;
- computerized processing of VAT returns by mid-year, and for the other major taxes by end-1997;
- reorganization of the Tbilisi tax office;
- an improved bonus system for tax inspectors;
- the enactment of a new Customs Code by mid-year, which clarifies customs procedures and introduces the legal basis for customs warehousing and a duty drawback scheme for exporters;
- extending the use of TINs to the State Customs Department (SCD);
- introducing financial or nonfinancial guarantees on all transit goods;
- improved cross-checking of valuation declared by importer;
- further computerization of Customs, including installing the ASYCUDA system in SCD posts.

44. Effective January 1, 1997, the authorities introduced a number of tax policy measures (Text Box 3) with a view to rationalizing further the tax system and reducing incentives for tax evasion. Together with the ongoing reforms in tax administration and the deepening of reforms in customs administration, these measures are expected to boost revenue in 1997. The removal of exemptions on VAT (at 20 percent) and Customs duties (at 12 percent) on petroleum products and cars, and the inclusion of diesel in the tax base¹⁸ are expected to raise significant revenues. In addition, profit tax revenue will be boosted by the removal of the 10 percent preferential rate for industry and construction, and the reduction in payroll taxes may be offset by the extension of its coverage to small businesses and the agricultural sector. On the other hand, the revision of personal income tax scales will significantly reduce average tax rates of low-income earners and thus is likely to be revenue-losing.

Text Box 3. Georgia: Tax Policy Measures for 1997

In an effort to further rationalize the tax system and reduce incentives for tax evasion, a number of tax policy measures became effective at the beginning of January 1997. The main measures were:

- a reduction in most excise tax rates except for certain hard alcohols, wine, high-quality cigarettes, and petroleum products (Appendix I, Table 16);
- the removal of VAT and customs duty exemption for petroleum products and automobiles, including for imports from CIS countries;
- the introduction of a 5 percent customs duty rate on a limited number of medical goods, raw materials, and capital goods, while the top rate of 12 percent was maintained for other goods.
- the unification of multiple corporate profit tax rates at 20 percent (Appendix II);
- an increase in personal income tax scales, to restore progressivity eroded by inflation (Appendix I, Table 17);
- a reduction in payroll taxes (contributions to social funds) from 35 to 33 percent.

External grants

45. Total grants in 1996 fell by $\frac{3}{4}$ percent of GDP; at 1.2 percent of GDP, this level of grant-financing was the lowest since the reform program was launched. Moreover, the nature of grants changed in 1996; whereas in 1995 nearly all the grants provided to the budget were from sales of wheat from the EU, in 1996, the United States provided wheat grants and the EU, in addition to wheat grants, provided a large cash grant equivalent to ECU 10 million for general budgetary support in December. In addition, the Netherlands provided US\$4.6 million, which was used for financing energy imports.

¹⁸ Previously only gasoline was taxed at a 15 percent "fixed" tax.

D. Expenditures and net lending

Expenditure developments

46. In sharp contrast to 1995, when there had been a drastic reduction in expenditures from the previous year in order to bring outlays more into line with financing capacity, expenditures on a commitment basis in 1996 increased to about 14 percent of GDP compared to 12.3 percent of GDP in 1995. Nonetheless, this outcome was still more than 10 percentage points of GDP lower than the unsustainable level of 1994 (Text Table 6). The increase in outlays was made possible by the increase in total revenue, and at the same time, there was further progress in reducing the fiscal deficit. However, only a modest beginning to increasing outlays has been made: there are still urgent needs for current spending as well as investment in critical infrastructure, which has been postponed. A further increase in outlays is expected to continue in 1997.

47. Expenditures on wages and salaries in 1996 increased as a percent of GDP. This was solely due to significant increases in salaries, since employment continued to fall. Generalized wage increases in July and November 1995, and February and June 1996 boosted the average monthly basic wage in budgetary institutions substantially, to lari 17.2. In addition, various bonuses add lari 5.9 a month, bringing the average total wage in July 1996 to lari 23.1 a month (Appendix I, Table 18). In September 1996, the salaries of some 140,000 employees in the education sector were doubled in lari terms and there was a significant decompression of the wage structure, with salaries of the highest grade workers increasing up to five-fold. Inclusive of bonuses, which range up to 60 percent for military personnel, the average government wage at end-1996 was nearly lari 30 per month (about US\$22). Concerning employment, in 1995 the number of civil servants was reduced markedly, spearheaded by the removal of some 120,000 health sector workers from the government payroll in August; important reductions also took place in other sectors. In contrast, in 1996, decreases in the government labor force were confined to a small (10,000) decrease in the education sector in September. Cumulatively, total central and local government employment fell from over 600,000 persons at the beginning of 1995 to around 360,000 at end-1996, a decline of about 40 percent.

48. Total spending on social transfers, including pensions, unemployment allowances, refugee benefits, and basic health care, rose from 2.6 percent of GDP in 1995 to 3.2 percent in 1996. This was mainly a result of the substantial increase in benefits, which followed the increases in civil service wages (Appendix I, Table 19). It also results from the full-year impact of the new health care package enacted in August 1995. Although a number of measures have been taken to target the social safety net to the truly needy (Text Box 4), the total number of beneficiaries has been barely reduced.

Text Box 4. Georgia: Social protection

Reforms of the Social Safety Net (SSN) and the health and education sectors are aimed at improving services and benefits, while increasing the sustainability of the social protection mechanisms by targeting the assistance to vulnerable groups.

The SSN provides low benefits to a large number of people (Appendix III describes the SSN in detail). As of January 1, 1997, 1.8 million beneficiaries (33 percent of the population) received an average monthly allowance of lari 10 (US\$7.6). The replacement ratio of the pension system, defined as the standard pension benefit as a percent of the average wage in budgetary organizations, is 41 percent, which is low considering that wages in non-budgetary organizations are generally significantly higher than government wages. The largest groups of beneficiaries are pensioners (1.1 million), followed by families with children (0.3 million) and refugees (0.3 million).

Efforts have been made to improve the targeting of the SSN. In 1995, nonworking pensioners became ineligible for pensions, and the previously-universal child allowances were provided only to families with two or more children. In February 1996, the retirement age was increased in one step from 55 to 60 years for women and from 60 to 65 years for men. Initially, this measure paradoxically increased the number of registered pensioners by 50,000, as previously unregistered elderly took advantage of the grandfathering provision to register before their eligibility expired. However, in the long run the increase in the retirement age is expected to reduce the number of pensioners by about 40 percent. In the 1997 budget, child benefits and single mother allowances, covering some 345,000 people will be abolished, and replaced by new benefits targeted at 120,000 particularly vulnerable families (see Appendix III). Finally, in 1996 the ineffective job creation schemes of the EF were eliminated; in 1995 the EF spent about 70 percent of its total expenditures on these job schemes.

A radical reform of the health sector was initiated in August 1995. The program aims at privatizing most health care facilities, including several hospitals, by mid-1998. The Government created a Health Fund (HF) designed to act as a financial intermediary and reimburse both public and private health care providers of basic preventative and curative health care services. Those not covered by the basic package would be paid for by user charges, although the poor would be eligible for an expanded set of services. The Government is also planning to introduce legislation in 1997 on private health care insurance for services not covered by the HF.

At the same time that the targeting of the SSN was improved, social benefits have been increased, generally in line with government wages (a description of the development of social benefits is provided by Appendix I, Table 19). Including the 15 percent increase in benefits on January 1, 1997, benefits have increased on average by over 200 percent, or about 100 percent in real terms, over the past two years (Figure 3).

49. Current spending on other goods and non-health services increased from 2.5 percent of GDP in 1995 to 3.4 percent in 1996. This partly reflects the increases in outlays for military and law enforcement, including for food, housing, and uniforms. The expansion of the number of army conscripts from 15,000 to 25,000 in accordance with regional military agreements in the third quarter of 1995 was mainly responsible for the increase in military expenditures, while internal security concerns prompted increases in outlays for law enforcement. It also reflects spending of the revenue from increased privatization receipts, as well as payments to domestic suppliers of goods delivered to Turkmenistan as part of a barter deal to reduce arrears on late payments of imports of petroleum products.

50. Domestic interest payments as a percent of GDP increased as a result of both the increase in debt outstanding to the NBG, as well as a rise in the share of debt bearing a

15 percent interest rate. In contrast, interest paid to external creditors fell. This was because debt servicing to principal bilateral creditors was confined to an US\$8 million quarterly goodwill deposit into a special account at the Netherlands Bank.

51. Local government expenditures remained constant as a percent of GDP. However, local governments probably kept more than their statutory share in tax revenues,¹⁹ resulting in higher total local government expenditure than that recorded by the MOF. The marked increase in unclassified expenditures in 1996 was mainly due to the purchase of 40,000 tons of wheat to build up a strategic reserve in anticipation of the bread price liberalization in June 1996, the purchase of oil products using the grant from the Netherlands and improved coverage of expenditures financed by resources controlled by budgetary organizations.

52. In the face of continued tight resource constraints, the Government was unable to increase the share of capital expenditure to GDP in 1996. Although priorities were shifted toward urgent projects, there was also a curtailing of some major projects. In particular, expenditures for a new customs post at the Turkish border and improvements of the Tbilisi airport tapered off. Net lending for the rehabilitation of the electricity generation capacity was also curtailed, as facilities built with the assistance of Germany to secure the supply of electricity came on stream. Concerning net lending, the outcome for 1996 was strongly affected by repayments of credits to the budget using nonbudget counterpart funds from the sale of EU wheat.

53. A Public Investment Program (PIP) has been prepared in cooperation with the World Bank. The objectives of the PIP-supported projects are to alleviate the bottlenecks for private activity in Georgia, primarily through the rehabilitation of the existing energy infrastructure and transportation networks; support for land reform; and improvement in the provision of education and health services. The bulk of financing for the projects included in the PIP comes from international financial institutions and other multilateral and bilateral donors.

Expenditure management and control

54. Expenditure control, though improving, was still deficient in 1996, leading to a distortion of the priorities laid down in the budget, as well as a further increase in expenditure arrears to 0.8 percent of GDP as of end-November 1996. Besides arrears to suppliers, there were also delays of about two weeks in paying pensions and refugee benefits, as well as a delay in paying interest on NBG debt. However, following the disbursement of a sizeable grant from the EU and a US\$30 million loan from the World Bank in late December, arrears were reduced by early January, although still exceeding ½ percent of GDP. These were mainly arrears to suppliers of goods and services, including for the Ministry of Defense, road maintenance, and health services.

¹⁹ Data on local government finances are deficient, and exclude certain types of nontax revenues that are not reported to the MOF and the expenditures financed with these revenues.

55. A treasury system is being established, with the aim of improving expenditure control. Under this system, spending ministries lose the authority to assume expenditure commitments without the prior approval of the Treasury. As of end-1996, the Treasury consisted of a Central Treasury Department in the MOF, which coordinates and manages the system, and thirteen Regional Treasury Offices (RTOs), which perform the treasury tasks for the budgetary organizations under their jurisdiction. During 1996, progress in closing revenue and expenditure accounts of spending units was slower than anticipated. As of December 1, 1996, 1094 expenditure accounts of the 1340 spending units' accounts had been closed. These figures exclude the Ministry of Defense and other law enforcement agencies, which were still outside the treasury system in 1996.

56. When fully implemented, the Treasury will carry out all budget execution functions of the MOF, using as its principal tools a single treasury account at the NBG and a system of treasury ledger accounts. This will enable the Treasury to control both expenditure commitments and cash outlays. However, at this stage, the MOF is still able to control only the cash transfers to spending agencies, i.e. it cannot yet control cash expenditures by those agencies, given its limited control over how and when the transfers to them are being spent. This has led to sizable accumulation of bank deposits by budgetary organizations during the course of a given year and to unexpected rundowns of these deposits.²⁰

57. Further improvements in the capacity of the MOF to monitor expenditures is urgently needed. The completion of the treasury project will be essential to reach this goal. During 1997, additional efforts will be undertaken to monitor expenditure commitments and arrears, establish a single treasury account at the NBG, implying the closing of both revenue and expenditure accounts outside the treasury, and incorporating all budgetary spending agencies in the system (which would eliminate the problem of uncontrolled bank deposits of budgetary organizations).

E. The 1997 Budget

58. The 1997 State budget was presented to Parliament in early 1997 (Appendix I, Table 20).²¹ Key features of this draft budget, include:

- an increase in the revenue/GDP ratio of general government in 1997 by over 2½ percent of GDP relative to 1996, to 10¾ percent of GDP.²² This is expected to be

²⁰ In December 1996 the deposits of budgetary organizations at commercial banks were unexpectedly reduced by lari 12.6 million.

²¹ As mentioned in section III. B, the 1997 State budget excludes local governments' revenues and expenditures.

²² The figures includes the revenue and expenditures of local governments in 1997, estimated
(continued...)

achieved by the new tax policy measures shown in Text Box 3 and, especially, by further improvements in tax and customs administration (see Text Box 2);

- a decrease in grants relative to 1996 (*inter alia*, the United States will provide loan, rather than grant, assistance);
- a further increase in the expenditure/GDP ratio, which, inclusive of local government spending, is projected to reach 14¼ percent of GDP. Priorities include: further increases in the purchasing power of civil servants' wages and the beneficiaries of social assistance; further rationalization of the size of Government; improved targeting of the social safety net; and increased resources in real terms toward basic health care and education.
- a further reduction in the overall deficit of the State budget,²³ consistent with a low inflation rate and available external resources.

IV. MONETARY AND EXCHANGE RATE DEVELOPMENTS AND BANKING SECTOR REFORM

A. Monetary developments

59. Recent monetary and exchange developments were marked by a gradual remonetization in domestic currency and relative exchange rate stability following the introduction of the lari in October 1995, together with a significant accumulation of international reserves. The strong growth in monetary aggregates in 1996 was accompanied by declining interest rates and some increase in financial intermediation, reflecting significant progress in banking sector reform.

Overview

60. Monetary developments in 1996 were characterized by a sharp increase in monetary aggregates, against the background of a stable exchange rate and declining inflation (Text Table 7 and Figure 7).²⁴ These trends, together with indications that banking sector reform has started to yield improvements in financial intermediation, suggest an increase in real money demand during the year. The remonetization of the economy in domestic currency initiated

²²(...continued)
at 178 million lari (2.5 percent of GDP).

²³The local governments are prohibited from borrowing externally or from the banking system, but can borrow from the central budget to cover short-term liquidity needs.

²⁴For monetary developments prior to 1996 see SM/96/231.

Figure 7. Georgia: Prices, Exchange Rates, and Broad Money
(Index, January 1994 = 100, log scale)

Sources: National Bank of Georgia; and Department of Social and Economic Information.

with the introduction of the lari in October 1995 was translated into a marked increase in currency in circulation (Figure 8). After a 170 percent increase in the last quarter of 1995, during 1996 broad money (including foreign exchange deposits) increased by 42 percent, or almost 25 percent in real terms, and reserve money grew by 36 percent, or about 19 percent in real terms (Appendix I, Tables 21 and 22). The money multiplier fluctuated significantly less than during the previous year, and rose by 5 percent compared to end-1995 as a result of declines in the currency/deposit ratio and the reserve/deposit ratio (Figure 8).

61. Despite the significant increase in monetary aggregates since the lari was introduced, the degree of monetization of the Georgian economy remains very low, and seignorage revenue has been reduced to about 1 percent of GDP (Appendix IV). The ratio of broad money to GDP at the end of 1996 was less than 5 percent of GDP, the lowest among the countries of the former Soviet Union. Observance of this low ratio is not surprising, considering that by early 1994 the country was at the brink of collapse and plagued by hyperinflation. However, it indicates that it may take a while before high levels of intermediation can be reached.

Text Table 7. Georgia: Monetary Indicators

	1995				1996			
	March	June	Sep.	Dec.	March	June	Sept.	Dec.
(Percentage change from same month in previous year)								
Monetary aggregates								
Reserve money	-2.2	24.9	28.3	275.2	1.2	12.5	35.4	35.9
Broad money	-26.3	-24.0	-8.6	146.3	5.0	11.0	31.1	41.9
Broad money (exc. Foreign currency deposits)	-10.0	-1.2	27.3	362.3	-4.5	11.8	28.2	38.2
Consumer prices	10.5	13.6	23.2	57.4	8.8	11.8	11.4	13.9
Memorandum item:								
Lari per U.S. dollar	1.28	1.30	1.30	1.23	1.26	1.26	1.27	1.27

Sources: National Bank of Georgia; Department of Social and Economic Information.

Monetary and exchange rate policies

62. The arsenal of *monetary instruments* available to the NBG to influence liquidity conditions is still very limited. There are no developed money and government securities markets, although activity in the *interbank credit auctions* increased significantly during 1996 (Text Box 5). Toward the end of the year, the NBG stepped up its intervention in the auctions with the objective of bringing market interest rates down (Figure 9). The *reserve requirement* has been used actively as an instrument of monetary control: following a decrease from 20 percent to 18 percent in January 1996, the required reserve ratio was lowered again to

Figure 8. Georgia: Currency in Circulation and the Money Multiplier

Sources: National Bank of Georgia; and IMF staff estimates.

**Figure 9. Georgia: Interbank Credit Auction
(In thousands of lari)**

15 percent in September, to reduce the implicit tax on banks and encourage intermediation.²⁵ A further reduction may be contemplated in mid-1997 in case of favorable monetary developments. However, in view of the low monetization of the economy, the effectiveness of this instrument to influence liquidity conditions remains limited.

Text Box 5. Georgia: Interbank Credit Auctions

Activity in the interbank credit auctions picked up considerably since they were introduced by the National Bank of Georgia (NBG) in May 1995 as the first step toward the development of a money market (Figure 9). In January 1996 the NBG expanded the range of maturities from 7-day credits to 30-, 60-, and 90-day credits, and increased the frequency of auctions from twice-monthly to twice-weekly. This market is gradually developing, with banks increasingly using the auctions as an instrument for liquidity management. The NBG has started to use the auctions to influence liquidity conditions; the increase in NBG-supplied credit at the end of 1996 reflected an attempt to drive down interest rates. In the absence of other developed financial markets in Georgia, the auction rates are becoming reference market rates.

Although the total volume of transactions in 1996 was 16 times larger than in 1995, it was still small (lari 39.2 million, or 0.7 percent of GDP). Nonetheless, market growth in 1996 was impressive: the average monthly volume of transactions rose from lari 0.5 million in the first quarter to lari 6.9 million in the fourth quarter. Most transactions were concentrated on the short-end of the market: of the total volume auctioned in 1996, 56 percent was for the 7-day maturity, 28 percent for the 30-day maturity, 16 percent for the 90-day maturity and only 0.4 percent for the 60-month maturity.

The NBG is still the main supplier of credit in the auction, but banks have gradually started to lend their excess funds, in view of the low risk of default; according to the rules, bank's required reserves may be used as collateral for borrowing in the auction and penalties are imposed daily until the reserve requirement is met. In addition, participation is viewed positively by the Banking Certification Commission. From the borrower's point of view, the auction is the cheaper way to obtain credit, while making use of their required reserves. Of the 50 participant banks in 1996, 18 were sellers, 39 were buyers and 7 were both sellers and buyers.

A change in the collateral requirement boosted activity in the auction significantly in the second half of 1996. Starting from June, the share of required reserves that certified commercial banks were allowed to use as collateral to borrow in the auction was raised from 75 percent to 90 percent; noncertified banks continue to be restricted to use up to 75 percent of their required reserves as collateral. Other amendments in the rules for participation in the auctions, starting from November 1, 1996 included: (i) a reduction in the commission applied on purchases/sales in the auction from 2.5 percent to 1 percent, 1, and (ii) a requirement for banks to replenish their required reserves completely after using them as collateral before they can be allowed to participate in the auctions.

²⁵ Required reserves are not remunerated. The reserve requirement is applied uniformly across all maturities and must be met in lari for both domestic and foreign exchange deposits.

63. The main instrument of monetary policy continues to be the *NBG's sales and purchases of foreign exchange* in the Tbilisi Interbank Currency Exchange (TICEX), but its use to influence liquidity conditions is constrained by the NBG's international reserves target. As in the previous year, NBG intervention in the foreign exchange market during 1996 aimed at sterilizing the liquidity impact of its lending to the Government, while maintaining an adequate level of reserves. In view of the strong expansion in NBG credit to the Government during 1996, sterilization was only partial. Nevertheless, the exchange rate remained relatively stable in the range of lari 1.23–1.28 per U.S. dollar (Appendix I, Table 23). Activity in the TICEX continued to expand in 1996, and the total volume transacted increased by 55 percent compared to 1995, while the NBG continued to be a dominant player in the market (Text Table 8). Interbank activity outside the TICEX has been picking up, indicating growing confidence among banks.²⁶

Text Table 8. Georgia: TICEX Transactions
(In millions of U.S. dollars)

	1995			1996				
	September	December	Total	March	June	September	December	Total
Total volume	24.2	15.5	69.4	29.0	14.5	21.6	42.5	107.6
Of which:								
NBG purchases	--	9.0	9.0	--	0.5	2.5	0.5	3.5
NBG sales	23.6	3.7	55.1	27.9	11.6	18.8	39.7	98.0

Source: National Bank of Georgia.

64. A major step toward indirect monetary management has been taken with the decision by the Georgian authorities to issue *Treasury bills* through an auction procedure, starting from mid-1997. The amounts auctioned in 1997 will be small and aimed at testing the market, with a view to paving the way for larger issues in the future. The Ministry of Finance will determine the terms of the issues (volumes and maturities), in consultation with the NBG, which will be in charge of the operational arrangements for the issuance of Treasury bills. The introduction of T-bills, over time, will provide an alternative source of budget financing. At the same time, the development of a government securities market will allow for increased reliance on indirect monetary instruments by the NBG. Progress in developing an appropriate framework for liquidity forecasting at the NBG will be crucial for future market operations.

65. The NBG's exchange rate policy since end-1994 has been not to resist a market driven appreciation but to stem a depreciation with foreign exchange sales if necessary, provided such a policy is consistent with maintaining an adequate level of gross official international reserves. The official exchange rate is determined in the TICEX, and has remained broadly stable since the introduction of the lari. Meanwhile, the NBG has rebuilt its

²⁶ TICEX transactions are guaranteed by the NBG, but are subject to a transactions fee.

gross international reserves to about 2.5 months of import cover, after they had been virtually exhausted by early 1994.

Commercial bank activity and interest rate developments

66. Despite the progress achieved to date in reforming the banking system and improving the regulatory framework for banking, commercial bank activity remains very limited and largely concentrated on short-term trade financing. The low degree of financial intermediation reflects the persistence of high credit risk and lack of sound investment opportunities, together with the adoption of tighter prudential regulations by the NBG, which constrain banks' activities.

67. Although bank credit to the private sector increased by 36 percent in 1996, it remained at 2.2 percent of GDP. The share of domestic currency credits hovered around 2/3 of total credits (Appendix I, Tables 24 and 25).²⁷ On-lending of external lines of credit began in mid-1996; since only certified banks were eligible to pass these resources to domestic borrowers, this contributed to the successful implementation of the bank certification program in the second part of the year (see Section II.B below). Commercial banks do not lend to the Government, but are expected to invest in Treasury bills in the second half of 1997.

68. Deposit mobilization by commercial banks improved in 1996, in tandem with the completion of the certification program and the gradual buildup of confidence in the banking system. Nevertheless, the deposit base continues to be very narrow (about 1.4 percent of GDP at year-end), reflecting the deep-seated preference for cash typical of transition economies. Total deposits increased steadily during the year, but fell in December, reflecting a sharp increase in currency held by the public, associated with end-year spending patterns. The substantial annual increase in total deposits (42.5 percent) was mostly due to a strong growth in foreign exchange deposits, although domestic currency deposits increased by 25 percent (Appendix I, Table 26).

69. Nominal interest rates continued to decline gradually as a result of successful stabilization and improvements in the banking sector (Appendix I, Table 27). This downward trend is also visible with respect to interbank credit auction rates (Figure 10). Indeed, the latter are a more reliable indicator of market trends, given the deficiencies in the data for commercial banks' interest rates.²⁸ Lending rates remain highly positive in real terms, and

²⁷ These figures were adjusted to take into account the removal of a loan from the Turkish Eximbank from the balance sheet of the United Georgian Bank in May 1996; this obligation was assumed by the Government.

²⁸ Lending and deposit rates vary considerably across banks. These data are indicative only and should be interpreted with caution. There are some unexplained anomalies. For example, interest rates on foreign exchange deposits are usually higher than on domestic currency deposits.

Figure 10. Georgia: Interest Rates, 1995-96
(In percent per annum, end period)

Source: National Bank of Georgia.

1/ Three-month maturity.

2/ Seven-day maturity.

although spreads have come down to about half of their level in March 1995, they are still very high, reflecting the high credit risk as well as banks' efforts to increase their capital in order to meet the higher minimum capital requirement. Over time, it is expected that increased efficiency and improved confidence in the banking sector will lead to lower credit risk and lower margins.

B. Banking sector reform

Overview

70. Since 1995 the NBG has implemented a comprehensive program for the restructuring and consolidation of the banking sector, with a view to promoting intermediation and increased private activity. This program was based on an upgrading of prudential regulations and the regulatory framework, together with increased monitoring of banks by the NBG. The key elements of the restructuring strategy were the *bank certification program*, the *privatization of the former state banks (FSBs)* and the adoption of *special agreements with these banks*, with the objective of restoring their financial viability.²⁹ The certification program, introduced in November 1995, aimed at identifying viable banks, which would form the "core" of a revamped banking system in the future, while restricting the operations of (and eventually closing) banks which failed to comply with prudential regulations. The special agreements signed with the FSBs imposed limits on their balance sheet growth, restricted the payment of dividends, and established schedules for improvements in their capital and liquidity positions, with the ultimate goal of obtaining certification.

71. The efforts to strengthen banking supervision and to instill discipline in the banking sector are starting to pay off. The number of licensed banks declined from 100 at the end of 1995 to 62 at the end of 1996 in an orderly fashion and commercial bank activity is gradually picking up. Although progress to date is encouraging, the role of banks in intermediation remains very small and much remains to be done to ensure a viable and sound banking system can develop in Georgia. To a large extent, progress in this area will depend on the successful implementation of other structural reforms and the development of a conducive environment for bank business, as well as on the credibility of the overall economic policies of the Government.

Commercial banks

72. The bank certification program has been successfully implemented and 47 banks in full compliance with prudential regulations had been certified by the end of 1996. Non-certified banks have had their licenses revoked; some banks are under liquidation, but this process has been moving slowly. As a result of the increase in the minimum capital requirement to the lari equivalent of US\$100,000 by June 1996, banks' capital rose significantly during 1996 (Text Table 9). To promote competition and enhance intermediation, the NBG raised the limit on

²⁹ The Government still holds a 27 percent stake at the Agrobank.

household deposits at certified banks to nine times their capital base and eliminated the restrictions on the number of bank accounts individuals and enterprises may hold.

Text Table 9. Georgia: Commercial Banks' Authorized Capital
(in millions of lari)

	December 1995	June 1996	December 1996
FSBs	8.0	13.2	16.2
Other banks	27.2	34.5	43.4
Total	35.2	47.7	59.6

Source: National Bank of Georgia.

73. The FSBs' special agreements were revised after completion of their audited 1996 financial statements. These banks are undergoing on-site examinations by the NBG, and the special agreements will be further revised in light of the results of these inspections. The FSBs have made significant progress to meet the standards required for certification, including by cutting costs, stepping up efforts to collect overdue loans, increasing staff training and improving accounting procedures. In addition, following the implementation of loan-loss provisions in September 1996, the FSBs took steps to write off their nonperforming loans. As a result, nonperforming loans of the banking system, as a percentage of the loan portfolio, declined from 30 percent in 1995 to about 7 percent in 1996 (Text Table 10). Owing to the loan writeoffs and the limits imposed on their activities, the share of the FSBs in the banking system dropped markedly during 1996.³⁰

Text Table 10. Georgia: Commercial Banks' Nonperforming Loans
(Stocks, in millions of lari)

Other commercial banks	1995	1996	Percentage change
Agrobank	4.6	3.1	-32.6
Bank of Georgia	3.8	0.3	-92.1
United Georgian Bank	32.7	0.7	-97.9
Other commercial banks	4.2	4.3	2.4
Total	45.3	8.4	-81.5

Source: National Bank of Georgia.

³⁰ Their share in total assets fell from 70 percent in 1995 to about 38 percent in 1996.

NBG

74. The NBG has continued its efforts to modernize its operations, build up an effective supervisory capacity and gradually improve its ability for monetary control. Progress has been steady in **banking supervision** and expertise is quickly developing, both for off-site and on-site examinations. A few medium-sized banks were examined in 1996 and penalties were imposed on some banks for violations of prudential regulations. The plans are to inspect most certified banks in 1997.

75. An **external audit** of the NBG will be carried out in early 1997; in preparation for the audit, the NGB wrote off some loans and made loan-loss provisions, including for the issuance of guarantees for wheat importers.³¹ Although the technical work for the implementation of **accounting reform** has been completed, implementation of the pilot project at the NBG has been postponed to March 1997 essentially due to delays in foreign assistance.

V. EXTERNAL SECTOR DEVELOPMENTS

76. *Bilateral debt rescheduling agreements were signed with 7 creditors, including the two largest (the Russian Federation and Turkmenistan) in 1996 and January 1997. The current account deficit narrowed significantly in 1996 in response to the continued implementation of tight fiscal and monetary policies but also the recovery in agricultural production and a lower need for food imports. With multilateral support remaining at a level comparable to 1995 and a continued rescheduling of obligations on pre-1995 debt, foreign exchange reserves were maintained at about 2.5 months of import cover, in spite of a considerable decline in bilateral financial support. Efforts to liberalize the exchange system culminated with Georgia's acceptance of the obligations under Article VIII, Section 2, 3, and 4 of the Fund's Articles of Agreement on December 20, 1996.*

A. External debt

77. Georgia entered independence with modest debt obligations, having signed the zero-option with Russia, but during 1991-1994 accumulated about US\$1 billion (Appendix I, Table 28). Through accumulating this debt, mostly on account of deliveries of energy, but also food, Georgia managed to mitigate the impact of the collapsing war-torn economy on the population. However, most of this debt was short term and had to be repaid by 1997: debt service due amounted to US\$150 million in 1994 (an estimated 31 percent of exports of goods and nonfactor services); US\$325 million in 1995 (69 percent of exports of goods and nonfactor services); and US\$121 million in 1996 (22 percent of exports of goods and nonfactor services) (Appendix I, Table 29). In terms of total government revenue (excluding

³¹ The NBG extended guarantees amounting to about US\$30 million for wheat importers during the fall of 1996.

grants), official debt service in 1995–96 amounted to more than 210 percent and 30 percent, respectively.

78. Faced with this high debt burden, low output and exports, and a virtual depletion of gross official reserves, Georgia accumulated payment arrears on external debt service of almost US\$400 million by end–1994, on a total stock of bilateral debt of about US\$945 million. The Government then requested a rescheduling of end–1994 debt from its bilateral creditors, asking for a 5 years grace, 10 years maturity as of end–1994, and an interest rate of no more than 4 percent. Pending the conclusion of agreements, since the beginning of 1995 Georgia has been making quarterly payments of US\$8 million into a special account at the Netherlands Bank to demonstrate its willingness to conclude negotiations.

79. During 1996 and January 1997 Georgia signed a number of bilateral rescheduling agreements. Stock reschedulings were agreed with Armenia (5 years grace, 10 years maturity, both from end–1995, and 4 percent interest), Austria (5 years grace, 15 years maturity, both from end–1996, and 4 percent interest, with an immediate payment of about US\$5 million in respect of debt service for 1995–96), Kazakstan (5 years grace, 10 years maturity, both from end–1995, and 4 percent interest), the Islamic Republic of Iran (5 years grace, 10 years maturity, both from end–September 1996, and 4 percent interest), Russia (5 years grace, 11 years maturity, both from end–1994, and 4 percent interest), Turkmenistan (3 years grace, 8 years maturity from end–March 1995, and 4 percent interest), and Uzbekistan (5 years grace, 10 years maturity, both as of end–1995, and 4 percent interest). The grace and maturity periods as well as interest rates stipulated in the agreements are in line with the Georgian authorities' requests, except for those agreed with Turkmenistan; however, Turkmenistan agreed to write-off about 10 percent of Georgia's stock of debt and stands ready to lengthen the grace period should Georgia's capacity to repay not recover adequately in spite of continued good economic performance.

B. Balance of payments

80. Supported by continued tight fiscal and monetary policies as well as a recovery of output, notably in agriculture, the current account deficit (excluding official transfers) narrowed further in 1996 to below 8 percent of GDP, down from 14 percent of GDP in 1995 and over 35 percent in 1994 (Text Table 11 and Appendix I, Table 30).

81. Available data on current account components, although deficient in a number of respects and therefore subject to wide margins of error, suggest a turnaround in trade developments in 1996, following a sharp decline in both exports and imports in the previous year. Imports staged a strong recovery, led by a rebound of capital goods linked to higher disbursements of project loans as well as increased foreign direct investment activity. While food imports dropped by more than an estimated 12 percent in volume terms on account of the recovery of agricultural output, import volumes of other consumer and intermediate goods rose significantly, by about 6 percent, as economic activity and incomes gradually recovered from previously low levels. Consistent with a pick up in economic activity, there has been a significant increase in gas imports (Appendix I, Table 31). Nevertheless, gas imports are still

estimated at little over one third of their 1994 level, reflecting the pass-through to consumers of the increase in energy prices and the elimination of Government's guarantees to gas importers. Merchandise exports grew by an estimated 18 percent.

82. Little is known about developments in nonfactor services, but transportation costs likely accounted for most of the estimated US\$109 million debit. Other nonfactor services credits reached an estimated US\$140 million in 1996. Under the US\$16 million credit for factor incomes, about three quarters reportedly were accounted for by compensation of Georgian employees working abroad or for nonresident organizations in Georgia. The remainder consisted of interest earned on holdings of foreign exchange reserves. Interest payments due—about US\$65 million—accounted for the bulk of factor income debits.

Text Table 11. Georgia: External Sector Indicators
(In millions of U.S. dollars)

	1994	1995	1996
Current account deficit (excluding grants)	-447.9	-407.7	-349.7
Of which:			
gas imports	-233.1	-68.7	-55.0
Official transfers	170.0	189.2	140.5
Capital account	-19.3	-85.5	43.9
Overall balance	-297.2	-303.7	-165.3
Memorandum items:			
Gross reserves	41.4	156.7	157.0
Stock of debt	986.7	1,213.7	1,388.8

Sources: State Committee for Statistics; and staff estimates.

83. Direction of trade data suggest that the reorientation of Georgia's imports away from the states of the former Soviet Union has ceased, partly on account of increased gas imports from these countries and reduced humanitarian assistance from other countries (Appendix I, Table 30). Outside the states of the former Soviet Union, Turkey has developed into Georgia's most important trading partner. Text Box 6 summarizes recent developments in Georgia's trade system.

Text Box 6. Georgia: Changes to Trade Regime

Since 1994, the government has abolished the main instruments by which trade was directed under the old economic system and opened up the economy to free trade. In late 1994 export taxes were abolished and a simple import tariff structure was introduced with a basic rate of 12 percent on imports—and 20 percent applied to barter imports. In January 1996, all import tariff rates were unified at 12 percent. The state order system was abolished in June 1995 together with the Government's withdrawal from guaranteeing payments for energy imports. There are no quantitative restrictions on imports and import licenses are generally not required. In 1996, the Government eliminated the remaining export prohibitions and requirements for licensing exports, except for reasons of environmental and cultural protection, health, arms control and, on a temporary basis, scrap metal. Similarly, ex-ante export contract registration requirements were abolished.

As from January 1997, a second import tariff band with a 5 percent rate was introduced. Only a few goods are covered under it, including certain capital goods, some medical goods previously nonexempt, and a very limited number of raw materials. The number of medicines exempt from duty was raised from 6 to 16 and literature published by Georgian citizens abroad was added to the list of exemptions. Imports remaining exempt from duties include humanitarian aid and various categories of food and medicines, as well as all CIS imports (except for fuel) since the beginning of 1997. Newly-formed joint ventures no longer benefit from an exemption on duties on imports. Instead, provisions for a system of bonded warehouses and a duty drawback scheme have been included in a draft customs code.

Georgia was granted observer status at the June 26, 1996 meeting of the World Trade Organization (WTO) and applied for full membership on June 27, 1996. A working party is considering its application.

84. Despite a decline of about 25 percent vis-à-vis 1995, official transfers covered about 40 percent of the current account deficit in 1996. Georgia's largest donors were the United States and the European Union, accounting for about 85 percent of an estimated US\$140 million in official transfers. Most of this aid was in the form of wheat, but toward the end of the year the European Union switched to cash support.

85. Amortization payments due reached about US\$98 million in 1996, on debt with short maturities accumulated before 1995 and related to imports of gas and food, as well as the conversion of correspondent account balances into new loans during 1991–94. In 1994 Georgia ceased servicing this debt and subsequently creditors agreed to a standstill on debt service during 1995–96. Disbursements under an IDA Rehabilitation Credit approved in 1995 were completed by end-March 1996 and reached US\$78 million. In addition, the World Bank disbursed a structural adjustment credit equivalent to about US\$60 million in two equal tranches in June and in December. EBRD disbursements started in 1995 and are estimated to have reached around US\$15 million by end-1996. Disbursements from bilateral creditors are estimated at about US\$25 million, Germany being the main one.

86. Foreign direct investments (FDI) are estimated to have reached US\$20 million in 1996, although FDI data are very weak, particularly regarding FDI not channeled through the banking system. The total value of FDI projects recorded with the Ministry of Trade amounted to about US\$100 million as of December 1996.

87. Fund resources disbursed under the ESAF arrangement, which was approved in February 1996, reached US\$81 million at the end of 1996 and the cumulative amount of rescheduled and written-off debt reached about US\$436 million. These resources allowed Georgia to reduce payment arrears by US\$352 million. Gross official reserves remained unchanged at year-end, at US\$157 million.

C. Exchange rate and exchange system developments

88. After the sharp appreciation that followed the end of the hyperinflation in mid-1994, the real appreciation of the lari slowed down during 1996 (Figure 11). In real effective terms, between the introduction of the lari and end-December 1996, it appreciated against the U.S. dollar by about 14 percent and against the Russian ruble by about 10 percent. Against the Deutsche Mark, the appreciation amounts to about 17 percent over that period, while against the Turkish lira it has been 16 percent. Another measure of the real exchange rate, namely the price of tradables relative to nontradables, suggests a higher appreciation in real terms during 1996, of about 53 percent (Figure 2).³² This reflects, *inter alia*, the significant increase in the bread price as well as in the administered tariffs for communication and transportation services during the year (see section II. C above). However, the meaningfulness of these indices for assessing the impact of exchange rate developments on competitiveness is limited in view of the structural changes under way in the Georgian economy. So far, real exchange rate changes have not affected adversely the current account.

89. Georgia has made considerable progress in liberalizing its exchange system during 1996, enabling it to accept the obligations under Article VIII, Sections 2, 3, and 4 of the Fund's Articles of Agreement in December 1996. Specifically, surrender requirements were abolished, daily foreign exchange auctions introduced, the official exchange rate set daily on the basis of TICEX auctions since August 1996 (Appendix V), and restrictions arising from the operation of correspondent accounts with certain states of the former Soviet Union eliminated. As a result, the Georgian exchange system is free of current and capital account restrictions—indeed, it is among the most liberal of the states of the former Soviet Union.

³²The calculation of price indices for tradables and nontradables is based on information for each of the 295 goods and services included in the consumer price index (CPI). Since the prices of tradable goods included in the CPI contain a significant nontradable component, this measure of the real exchange is imperfect. A better indicator of the price of tradables relative to nontradables would be the ratio of the wholesale price index (as a proxy for tradables) and the CPI (as a proxy for nontradables); however, the former is not available yet.

Figure 11. Georgia: Bilateral Real Exchange Rates, 1991-96 1/

Sources: Georgian authorities; and IMF staff estimates.

1/ Bilateral exchange rates, deflated by relative movements in consumer price indices.

Table 1. Georgia: GDP by Origin, 1992-96

	1992	1993	1994	1995		1996
				Jan.-Sept.	Annual	Jan.-Sept.
(In millions of lari)						
Nominal GDP	0.185	16.4	1,373.2	2,549.4	3,694.0	4,557.8
(Ratio as a percent of GDP) 1/						
Agriculture and livestock	54.5	67.7	28.7	39.3	38.0	32.6
Industry 2/	12.6	6.3	21.3	14.7	14.5	14.2
Construction	6.7	0.6	5.5	4.0	4.0	3.7
Transport and Communications	3.9	3.4	8.8	4.1	4.3	5.6
Trade and catering	1.7	6.9	6.4	20.9	21.4	23.1
Other	20.6	15.1	29.3	17.0	17.8	20.8
(Annual percentage change)						
Real GDP	-44.8	-25.4	-11.4	...	2.4	12.0 3/

Sources: Data provided by the Georgian authorities; and staff estimates.

1/ The data for 1994-96 are not comparable with earlier years because they include official estimates for informal sector. Such estimates are subject to large margins of error.

2/ Includes the turnover tax.

3/ Relative to January-September 1995.

Table 2. Georgia: Gross Fixed Investment, 1992-96

	1992	1993	1994	1995		1996
				Jan.-June	Annual	Jan.-June
(In percent of 1991 level; valued at 1984 prices)						
National economy	32.1	12.0	12.0	4.7	12.1	7.8
of which:						
Industry	25.9	4.8	4.2	4.3	15.1	8.2
Agriculture 1/	14.9	2.1	...	...	...	...
Construction	36.4	...	...	...	9.1	...
Transport/communications	50.0	9.5	59.5	18.6	26.2	27.6
Trade, sales and catering	8.3	...	...	...	...	...
Housing	28.7	20.3	14.7	5.6	9.8	7.3
(In percent of national economy)						
National economy	100.0	100.0	100.0	100.0	100.0	100.0
of which:						
Industry	18.9	9.5	8.2	11.5	29.1	9.8
Agriculture 1/	3.1	0.7	...	...	...	...
Construction	1.8	0.5	...	...	1.2	...
Transport/Communications	9.2	5.2	29.4	23.3	12.8	26.0
Trade, sales and catering	0.4	0.1	...	...	...	...
Housing	36.0	68.7	49.4	39.4	32.6	42.3

Source: Data provided by the Georgian authorities.

1/ Including forestry.

Table 3. Georgia: Production of Selected Industrial Commodities, 1992-96

(In thousands of tons, unless otherwise indicated)

	1992	1993	1994 1/	1995 1/		1996
				Jan.-June	Annual	Jan.-June
Fuel and energy						
Electric power (billions of kwh)	11.5	9.7	7.0	5.5	7.1	5.7
Coal	181.0	82.2	44.5	17.2	42.7	88.6
Oil	125.0	88.2	66.9	37.0	42.7	31.8
Natural Gas (millions of m3)	37.9	21.8	11.4	2.8	3.3	3.3
Gasoline	71.9	18.6	8.8	—	3.3	6.7
Diesel fuel	110.8	34.5	17.9	10.8	8.4	4.5
Lubricating oil	—	—	—	—	—	—
Mazut	189.1	72.0	24.8	16.1	11.7	6.8
Motor oil	5.0	2.0	1.4	...	...	...
Metallurgy						
Cast-iron	242.3	4.3	—	—	—	—
Steel	532.0	221.7	121.2	72.4	88	68.1
Finished roll steel	383.5	142.8	93.7	55.4	...	55.7
Rolled ferrous metal	429.6	185.6	100.0		69.5	
Steel pipes						
In millions of meters	12.4	5.5	2.2		1.7	
In thousands of tons	208.0	110.2	39.3	21.7	37.3	28.9
Manganese ore	292.5	36.8	29.3	40.3	41.9	66.9
Electro-ferro manganese	10.0	6.9	2.4	0.1	0.1	0.8
Metallurgical manganese (in tons)	290.0	164.0	171.0	0.1	0.1	—
Machine-building						
A/C motors (thousands of kw)	6.6	9.0	...	...	...	...
Machine tools (units)	1,001.0	348.0	109.0	77.0	57.0	16.0
Electric welding equipment (thousands of units)	5.7	3.9	1.1	0.3	...	0.1
Magnetic stations (thousands of units)	31.1	14.2	0.8	1.0	...	0.7
Flooding electric engines (thousands of units)	2.8	1.2	1.0	0.6	0.7	0.4
Lifting motors (thousands of units)	6.7	5.2	...	...	...	...
Chemical/timber products						
Mineral fertilizers 2/	76.6	58.6	34.0	41.7	42.7	52.9
Chemical fibers and threads	4.5	8.0	0.9	0.2	0.2	0.9
Synthetic ammoniac	117.3	91.0	52.8	51.6	65.6	71.5
Synthetic resin and plastic	7.6	10.2	2.1	—	0.6	—
Synthetic detergents and soap	2.5	2.2	1.2	...	...	...
Sawdust (thousands of m3)	35.6	9.5	3.5	4.0	...	30.0
Paper	2.2	0.3	0.1	—	...	0.2
Construction						
Asbestos tiles/slates (in millions)	9.9	4.1	0.6	0.1	0.1	0.2
Prefabricated ferro-concrete structures (thousands of m3)	208.3	85.8	13.0	5.6	6.7	3.4
Ceramic tiles (thousands of m3)	—	—	...	...	...	...
Building bricks (millions of units)	47.3	22.8	9.1	11.9	6.4	15.4
General merchandise and household appliances						
China and porcelain ware (millions of units)	0.8	0.1	0.1	0.2	...	0.2
Color TV (thousands of units)	8.0	0.9	0.1	0.2	0.2	0.4
Notebooks (millions of units)	11.8	—	...	—	...	0.2

Table 3 (concluded). Georgia: Production of Selected Industrial Commodities, 1992-96

(In thousands of tons, unless otherwise indicated)

	1992	1993	1994 1/	1995 1/		1996
				Jan.-June	Annual	Jan.-June
Light industry						
Silk thread (in tons)	110.0	37.2	11.6	...	...	...
Cotton yarn	5.0	2.6	0.8	0.8	1.0	0.4
Wool yarn	2.4	1.5	0.3	0.3	0.3	0.1
Nonwoven fabrics (millions of meters)	3.3	1.2	0.3	...	0.1	...
Hosiery (millions of pairs)	9.5	6.2	1.1	0.3	0.4	0.2
Knitwear (millions of units)	7.8	3.2	1.0	0.3	0.5	0.2
Footwear (millions of pairs)	2.6	1.0	0.2	0.04	0.1	0.02
Fabrics, total (millions of m2)	31.7	15.9	3.4	1.7	2.0	0.9
Cotton	12.9	7.5	1.5	0.5	0.6	0.3
Wool	3.6	1.9	0.5	0.5	0.5	0.1
Silk	10.1	4.7	0.9	0.6	0.8	0.5
Other	5.0	1.8	0.5	0.1	0.2	0.03
Carpets (millions of m2)	0.1	0.1	0.02	0.001	4.7	--
Basic foodstuff and food-processing						
Granulated sugar	2.0	0.8	0.2	0.2	0.21	12.8
Meat	6.5	3.4	0.4	0.05	0.1	0.02
Sausage	4.3	0.5	0.2	0.1	0.2	0.3
Fish	1.9	1.4	0.3	0.02	0.02	0.08
Butter	0.2	0.1	0.3	0.02	0.02	0.01
Dairy products (in terms of milk)	24.3	17.9	17.8	3.5	4.1	3.2
Fat cheese	2.8	0.9	0.4	0.3	0.3	0.2
Vegetable oil	1.4	0.5	0.01	--	0.01	0.01
Margarine	2.3	2.3	0.1	0.04	0.1	--
Canned food	93.0	44.3	9.8	6.6	9.4	1.6
Confectionary	1.9	1.9	0.4	0.2	0.3	0.25
Tea, primary processed	31.4	24.7	12.4	6.6	12.5	6.5
Natural tea	32.9	16.4	3.9	1.9	2.6	2.6
Macaroni products	18.6	8.2	4.6	3.0	3.0	0.4
Non-alcoholic beverages (millions of decaliters)	2.7	0.6	0.4	0.4	0.6	1.0
Mineral water (millions of 1/2 liters)	61.6	26.6	9.0	5.3	15.9	29.2
Cigarettes (thousand millions)	5.0	3.6	3.3	1.6	1.9	1.0
Soap	1.2	1.4	1.1	...	...	...
Vodka and liqueurs (thousands of decaliters)	647.0	1,187.0	105.0	72.4	86.4	60.1
Grape wine (thousands of decaliters)	17,970.0	10,425.0	4,363.0	3,849.5	4,123.0	1,976.5
Champagne (thousands of decaliters)	9,736.0	5,912.0	161.0	35.7	40.0	23.0
Cognac (thousands of decaliters)	1,358.0	1,023.0	241.0	100.8	112.2	57.3
Beer (thousands of decaliters)	2,352.0	1,204.0	648.0	578.0	671.3	462.8

Source: Data provided by the Georgian authorities.

1/ Data for Abkhazia and South Ossetia are not included.

Table 4. Georgia: Transportation by State Enterprises, 1992-96

	1992	1993	1994	1995		1996
				Jan.-June	Annual	Jan.-June
(Thousands of tons)						
Freight transport	40,161	20,400	14,295	8,473	13,611	8,341
Rail	7,695	5,321	2,851	2,168	3,283	2,503
Road	26,545	10,416	8,168	5,010	8,690	5,320
Sea	5,921	4,663	3,276	1,295	1,638	518

Source: State Department of Social and Economic Information (SDSEI).

Table 5. Georgia: Retail/Consumer Price Index in Tbilisi, 1993-1996 1/
(Index: December 1992=100)

	Consumer Price Index	Over Previous Month	Percentage Changes	
			Over Previous Quarter	Over Same Month Last Year
1993				
January	126.7	26.7		1,434.9
February	173.6	37.0		1,689.6
March	197.5	13.8	97.5	583.9
April	246.3	24.7		473.9
May	324.7	31.8		852.6
June	426.3	31.3	115.8	942.3
July	595.9	39.8		1,147.6
August	764.6	28.3		1,410.0
September	1,149.9	50.4	169.8	1,881.8
October	1,912.3	66.3		2,853.1
November	4,543.7	137.6		6,065.8
December	7,587.9	67.0	559.9	7,487.9
Average 1993	1,504.1	...	...	3,125.4
1994				
January	20,364.5	168.4		15,973.0
February	27,512.4	35.1		15,750.1
March	41,323.6	50.2	444.6	20,819.9
April	76,200.7	84.4		30,835.2
May	108,738.5	42.7		33,393.6
June	103,301.5	-5.0	150.0	24,133.8
July	109,706.2	6.2		18,309.3
August	187,597.7	71.0		24,436.2
September	583,803.9	211.2	465.1	50,669.1
October	534,764.4	-8.4		27,864.2
November	542,785.8	1.5		11,846.0
December	498,820.2	-8.1	-14.6	6,473.9
Average 1994	236,243.3	...	...	15,606.5
1995				
January	563,666.8	13.0		2,667.9
February	568,176.1	0.8		1,965.2
March	551,130.9	-3.0	10.5	1,233.7
April	545,619.6	-1.0		616.0
May	573,446.2	5.1		427.4
June	566,564.8	-1.2	2.8	448.5
July	571,550.6	0.9		421.0
August	590,411.7	3.3		214.7
September	614,618.6	4.1	8.5	5.3
October	758,439.4	23.4		41.8
November	759,197.8	0.1		39.9
December	785,010.5	3.4	27.7	57.4
Average 1995	620,652.7	...	...	162.7
1996				
January	804,792.8	2.5		42.8
February	829,258.5	3.0		46.0
March	855,297.2	3.1	9.0	55.2
April	869,837.3	1.7		59.4
May	874,186.5	0.5		52.4
June	877,683.2	0.4	2.6	54.9
July	867,151.0	-1.2		51.7
August	869,232.2	0.2		47.2
September	874,186.8	0.6	(0.4)	42.2
October	877,771.0	0.4		15.7
November	886,109.8	1.0		16.7
December	893,907.6	0.9	2.3	13.9
Average 1996	864,951.1	...	...	39.4

Source: Data provided by the Georgian authorities.

1/ Until December 1993, according to the Retail Price Index; after December 1993 according to a 295-good Laspeyres index using a methodology introduced with technical assistance from STA.

Table 6. Georgia: Pension and Minimum Government Monthly Wage, 1995-96 1/

	Minimum Monthly Wage		Monthly Pension	
	Nominal (in lari)	Real 2/ (Jan. 1991=100))	Nominal (in lari)	Real 2/ (Jan. 1991=100))
1995				
January	1.50	11.3	3.00	22.5
February	1.50	11.2	3.00	22.4
March	1.50	11.5	3.00	23.1
April	1.50	11.6	3.00	23.3
May	1.50	11.1	3.00	22.2
June	1.50	11.2	3.00	22.4
July	3.50	25.9	3.70	27.4
August	3.50	25.1	3.70	26.5
September	3.50	24.1	3.70	25.5
October	3.50	19.5	3.70	20.7
November	6.00	33.5	6.00	33.5
December	6.00	32.4	6.00	32.4
1996				
January	6.00	31.6	6.00	31.6
February	7.50	35.8	7.00	35.8
March	7.50	34.7	7.00	34.7
April	7.50	34.1	7.00	34.1
May	7.50	34.0	7.00	34.0
June	9.00	43.5	8.50	41.1
July	9.00	44.0	8.50	41.6
August	9.00	43.9	8.50	41.4
September	9.00	43.6	8.50	41.2
October	9.00	43.4	8.50	41.0
November	9.00	43.0	8.50	40.6
December	9.00	42.6	8.50	40.3

Sources: Ministry of Labor and Social Affairs; and Fund staff estimates.

1/ Includes only wages of budgetary organizations.

2/ The pension and minimum nominal wage are deflated by the CPI (Laspeyres).

Table 7. Georgia: Average Monthly Wages, 1992-96 1/ 2/
(In lari)

	1992	1993	1994	1995		1996
				Jan.-June	Annual	Jan.-June
Total economy	0.002	0.028	6.2	13.5	15.7	21.4
Industry	0.002	0.041	9.6	19.7	21.3	33.9
Workers	0.002	0.037	8.5	...	20.2	...
Agriculture	0.001	0.016	1.4	3.0	4.2	7.9
State farms, agricultural enterprises	0.001	0.017	1.1	2.4	3.8	7.0
Construction	0.002	0.046	12.6	30.7	40.3	69.9
Workers	0.002	0.045	17.3	...	50.3	...
Transportation	0.001	0.052	9.3	28.0	32.9	51.0
Railway transportation	0.002	0.061	10.5	34.6	37.2	49.3
Waterway transportation	0.003	0.094	9.9	37.8	43.9	46.3
Urban transportation	0.001	0.036	13.2	18.9	37.7	53.6
Communications	0.002	0.036	6.5	20.8	25.9	37.1
Trade and distribution	0.001	0.012	2.7	12.4	23.1	23.4
Computer services	0.002	0.028	3.6	7.8	11.1	22.8
Housing and communal services	0.001	0.028	8.8	16.6	20.4	26.4
Public health and social security	0.001	0.015	1.0	4.0	5.8	6.4
Public education	0.001	0.013	1.2	4.7	8.4	8.5
Culture	0.001	0.019	1.1	3.7	3.9	14.0
Art	0.001	0.021	1.8	4.8	5.8	21.2
Science and related services	0.001	0.023	1.7	7.4	9.5	16.9
Credit and state insurance institutions	0.005	0.064	5.1	19.9	29.3	35.6
State administration and management	0.005	0.025	2.9	6.7	8.5	18.8
Memorandum items:						
Average annual salary						
Total economy	0.018	0.335	73.8	162.0	188.4	256.8
Industry	0.022	0.494	115.7	236.4	255.6	406.8
Agriculture	0.010	0.188	16.3	36.0	50.4	92.4
Services 3/	0.023	0.354	...	...	...	...

Source: Data provided by the Georgian authorities.

1/ Wages include all cash, compensation, and value of goods-in-kind.

2/ These data are subject to large margins of error.

3/ Average for all services.

Table 8. Georgia: Population and Employment, 1992-96
(In thousands)

	1992	1993	1994	1995		1996
				Jan.-June	Annual	Jan.-June
Total population 1/	5,412.4	5,395.7	5,377.9	...	5,368.7	...
Males	2,578.3	2,570.0	2,559.9	...	2,555.5	...
Females	2,834.1	2,825.7	2,818.0	...	2,813.2	...
Urban	3,014.9	2,999.8	2,990.1	...	2,985.0	...
Rural	2,397.6	2,395.9	2,387.8	...	2,383.7	...
Under 16 years of age	1,395.3	...	...	...	...	...
In active years 2/	3,014.1	...	...	...	...	...
Over active age	1,003.0	...	...	...	...	...
Population employed 3/	1,984.2	1,792.0	1,749.7	1,736.3	1,730.0	1,759.1
State sector	1,375.6	1,160.0	1,095.7	1,010.0	985.3	964.4
of which:						
Industry and construction	422.1	337.1	278.1	237.6	251.7	234.2
Agriculture	160.3	113.6	107.4	91.3	90.0	94.0
Transportation and communications	72.4	97.8	98.7	70.2	78.1	63.1
Trade and other materials sectors	64.1	85.0	56.8	66.5	41.1	70.1
Health, education, and science	438.2	413.3	315.4	215.0	211.1	205.0
Administration and finance	50.2	59.7	45.3	40.5	44.1	45.8
Other nonmaterial sector	98.3	53.6	78.2	69.4	76.4	70.7
Cooperatives 4/	197.1	143.7	94.0	89.7	110.7	89.7
of which:	81.1					
Industry and construction	64.9	25.6	24.0	32.5	40.1	37.1
Agriculture	78.1	60.9	48.1	30.7	40.3	28.1
Other	54.1	57.2	21.9	26.5	30.3	15.9
Private sector	411.5	488.2	560.0	783.7	634.0	813.6
of which: self-employed	4.4	5.0	5.0	5.1	6.4	6.8
Retired (receiving pension)	1,079.6	1,139.6	1,140.8	1,140.8	1,140.7	1,104.7
of which: retirees employed	182.4	118.6	93.0	93.0	65.2	65.1

Source: Data provided by the Georgian authorities.

1/ Total population may be significantly overestimated because data include persons registered in Georgia but living abroad.

2/ Since February 20, 1996, working age is 16-60 for women, and 16-65 years for men. Prior to that date, working age was 16-55 for women, and 16-60 years for men.

3/ Excludes employment in the informal sector. Official estimates indicate that, as of end-June 1996 employment on the informal sector was about 750,000 persons.

4/ Including collective farms and consumer cooperatives.

Table 9. Georgia: Unemployment, 1992-96
(Number of persons, end of period)

	1992	1993	1994	1995	1996 1/
Registered unemployed	136,402	225,886	75,714	65,450	53,372
Of which:					
Receiving benefits	22,218	12,289	796	2,627	7,066

Sources: Ministry of Labor and Social Affairs and SDSEI.

1/ As of end-November 1996.

Table 10. Georgia: Summary of General Government Operations, 1994-1996
(In millions of lari)

	1994	1995			1996 1/		
		Jan.-June	July-Dec.	Annual	Jan.-June	July-Dec.	Annual
Total revenue and grants	106.0	95.4	163.5	260.9	233.4	303.4	536.8
Total revenue	58.2	71.2	118.8	189.9	192.5	273.2	465.7
Tax revenue (excluding extrabudgetary)	41.1	51.8	80.1	131.9	117.5	187.1	304.5
Taxes on income	3.4	7.1	13.7	20.9	16.8	27.7	44.5
Taxes on profits	11.6	13.5	15.1	28.6	16.0	21.9	37.9
VAT	16.6	20.7	37.7	58.5	51.2	82.7	133.8
Customs duties 2/	2.3	2.3	2.3	4.5	7.9	12.0	19.9
Other taxes 3/	10.3	9.0	11.2	20.3	23.5	53.3	81.8
Nontax revenue 4/	7.6	5.7	11.2	16.9	20.5	29.5	50.0
Extrabudgetary revenue 5/	9.4	13.7	27.5	41.2	54.5	56.7	111.2
Grants	47.9	24.2	46.7	71.0	40.9	30.2	71.1
Total expenditure and net lending	333.0	195.6	259.8	455.4	340.1	456.3	796.4
Total expenditure	322.8	177.8	250.3	428.1	340.1	465.2	805.3
Current expenditure	296.2	135.3	183.9	319.2	313.8	422.6	736.4
Wages and salaries	11.0	26.4	33.1	59.5	43.7	59.9	103.7
Other goods and services 6/	25.0	23.3	32.8	56.1	48.1	72.1	120.1
Subsidies and Transfers	190.1	16.6	22.5	39.1	29.7	29.3	59.0
Social assistance	15.9	14.7	18.5	33.2	28.9	28.9	57.8
Other 7/	174.2	2.0	4.0	5.9	0.8	0.4	1.2
Interest payments	33.8	27.3	27.3	54.6	24.6	32.6	57.3
Domestic	0.0	0.1	0.9	1.0	2.8	8.9	11.7
External - non-rescheduled	33.8	6.4	5.6	12.0	2.6	4.3	6.8
Interest on rescheduled debt	0.0	20.8	20.8	41.6	19.3	19.5	38.8
Other current expenditure 8/	21.7	19.6	30.1	49.7	47.9	53.4	101.4
Unclassified expenditure	8.4	2.0	8.5	10.4	26.8	55.6	82.4
Extrabudgetary expenditures 9/	6.2	20.1	29.8	49.9	47.2	56.6	103.8
Local government expenditures	22.6	23.4	46.6	70.1	45.7	63.0	108.7
Capital expenditure	4.0	19.1	19.7	38.8	26.3	42.6	68.9
Net lending	10.2	17.8	9.5	27.3	--	-8.9	-8.9
Overall balance (commitments)	-226.9	-100.2	-94.3	-194.5	-106.8	-152.9	-259.6
Expenditure arrears (-, reduction)	125.8	32.5	-5.7	26.8	3.0	5.0	8.0
External interest	32.6	6.4	5.6	12.0	2.1	-7.2	-5.1
Other 10/	93.2	26.1	-11.3	14.8	0.9	12.2	13.0
Overall balance (cash)	-101.2	-67.7	-100.0	-167.7	-103.8	-147.9	-251.6
Total financing	101.2	67.7	100.0	167.7	103.7	147.9	251.6
Domestic bank	18.9	27.1	32.4	59.4	57.6	99.2	156.8
External	82.2	40.6	67.6	108.2	46.1	48.7	94.8
Disbursements	82.2	40.6	67.6	108.2	46.1	48.7	94.8
Amortization	-160.5	0.0	-116.5	-116.5	-15.5	--	-15.5
Changes in arrears (-, reduction)	160.5	0.0	116.5	116.5	15.5	...	15.5

Table 10(concluded). Georgia: Summary of General Government Operations, 1994-1996

	1994	1995			1996 1/		
		Jan.-June	July-Dec.	Annual	Jan.-June	July-Dec.	Annual
Memorandum items:							
Revenue and grants/total expenditure	32.8	53.7	66.1	60.9	68.6	65.2	66.7
Revenue/total expenditure and net lending	17.5	36.4	45.7	41.7	56.6	59.9	58.5
Cash deficit/total expenditure and net lending	-30.4	-34.6	-38.5	-36.8	-30.5	-32.4	-31.6
Commitments deficit/total expenditure and net lending	-68.1	-51.2	-36.3	-42.7	-31.4	-33.5	-32.6
Total revenue/current expenditure	19.6	52.6	64.6	59.5	61.3	64.7	63.2

Sources: Data provided by the Georgian authorities; and staff estimates.

1/ Staff estimates, based on data for first eleven months of 1996.

2/ Until September 1994, includes VAT, excises, and customs duties. For 1995 and 1996, this is comprised of duties on imports.

3/ Includes excises, the land tax, enterprise property taxes, the presumptive tax, the ecological tax, and the "fixed" tax on petroleum products.

4/ Includes license fees, fines and other fees, and, as from September 1995, profit transfers from the NBS.

5/ Includes revenues of the Pension Fund, the Employment Fund, the Health Fund, the Privatization Fund and the Road Fund.

6/ Mainly office supplies, and food and lodging for the military and law enforcement agencies.

7/ Includes subsidies for newspaper printing and metro. For 1994, includes the expenditure counterparts of wheat grants, accrued gas payments until September, and operating costs of the Electricity Department until September. For 1995, includes subsidies to enterprises out of the Privatization Fund.

8/ Includes Health Fund outlays.

9/ Outlays on pensions and unemployment benefits; Road Fund expenditures are classified under capital outlays.

10/ Includes changes in domestic expenditure arrears and irreconcilable differences in monetary and fiscal data.

Table 11. Georgia: Summary of General Government Operations, 1994-1996 1/
(In percent of GDP)

	1994	1995			1996		
		Jan.-June	July-Dec.	Annual	Jan.-June	July-Dec.	Annual
Total revenue and grants	7.7	5.7	8.2	7.1	8.3	10.5	9.4
Total revenue	4.2	4.2	5.9	5.1	6.8	9.4	8.1
Tax revenue	3.0	3.1	4.0	3.6	4.2	6.5	5.3
Taxes on income	0.3	0.4	0.7	0.6	0.6	1.0	0.8
Taxes on profits	0.8	0.8	0.8	0.8	0.6	0.8	0.7
VAT	1.2	1.2	1.9	1.6	1.8	2.9	2.3
Customs duties	0.2	0.1	0.1	0.2	0.2	0.4	0.3
Other taxes	0.7	0.5	0.6	0.5	0.9	1.8	1.4
Nontax revenue	0.6	0.3	0.6	0.5	0.7	1.0	0.9
Extrabudgetary revenue	0.7	0.8	1.4	1.0	1.9	2.0	1.9
Grants	3.5	1.4	2.3	1.9	1.5	1.0	1.2
Total expenditure and net lending	24.2	11.6	12.9	12.3	12.0	15.7	13.9
Total expenditure	23.5	10.6	12.4	11.6	12.0	16.1	14.1
Current expenditure	21.6	8.1	9.1	10.5	11.1	14.6	12.9
Wages and salaries	0.8	1.6	1.6	1.6	1.5	2.1	1.8
Other goods and services	1.8	1.4	1.6	1.5	1.7	2.5	2.1
o/w netted out with taxes	13.8	1.0	1.1	1.1	1.1	1.0	1.0
Subsidies and Transfers	1.2	0.9	0.9	0.9	1.0	1.0	1.0
Social assistance	12.7	0.1	--	0.2	--	--	--
Other	2.5	1.6	1.4	1.5	0.9	1.1	1.0
Other current expenditure	1.6	1.2	1.5	1.3	1.7	1.8	1.8
Unclassified expenditure	0.6	0.1	--	0.3	0.9	1.9	1.4
Extrabudgetary expenditures	0.5	1.2	1.5	1.4	1.7	2.0	1.8
Local government expenditures	1.6	1.4	2.3	1.9	1.6	2.2	1.9
Capital expenditure	0.3	1.1	1.0	1.8	0.9	1.5	1.2
Net lending	0.7	1.1	--	--	0.0	-0.3	-0.2
Overall balance (commitments)	-16.5	-6.0	-4.7	-5.3	-3.8	-5.3	-4.5
Expenditure arrears (-, reduction)	9.2	1.9	-0.3	0.7	0.1	0.2	0.1
External interest	2.4	0.4	--	0.3	0.1	-0.2	-0.1
Other	6.8	1.6	-0.6	0.4	--	0.4	0.2
Overall balance (cash)	-7.4	-4.0	-5.0	-4.5	-3.7	-5.1	-4.4
Total financing	7.4	4.0	5.0	-4.5	3.7	5.1	4.4
Domestic Bank	1.4	1.6	1.6	1.6	2.0	3.4	2.7
External	6.0	2.4	3.4	2.9	2	1.7	1.7
Disbursements	6.0	2.4	3.4	2.9	1.6	1.7	1.7
Amortization	-11.7	--	--	3.2	--	--	-0.3
Changes in arrears (-, reduction)	11.7	--	--	3.2	--	--	0.3

Sources: Georgian authorities; and staff estimates.

1/ For footnotes see Appendix I, Table 10.

Table 12. Georgia: Accounts of Extrabudgetary Funds, 1/ 1995-1996
(In millions of lari)

	1995		1996	
	Jan.-June	July-Dec.	Jan.-June	July-Nov. 2/
Social Security Fund				
Revenue	21.2	43.8	46.1	27.5
Payroll taxes	16.2	28.8	26.3	15.8
Transfers from republican budget	4.2	12.2	16.5	9.5
For pensions	...	...	13.9	9.5
For child allowances	...	...	2.6	--
Other	0.8	2.8	3.3	1.5
Expenditure	22.7	43.8	48.6	28.2
Pensions	19.8	36.6	44.0	23.2
Child allowances	1.6	4.3	2.8	2.2
Sickness allowances 3/	0.6	1.1	0.9	0.6
Other	0.7	1.8	0.9	2.3
Balance (-, deficit)	-1.5	--	-2.5	-0.6
Employment Fund				
Revenue	0.8	1.4	1.2	0.6
Expenditure	0.9	1.4	0.6	0.6
Unemployment benefits	--	--	0.1	0.1
Job programs	0.6	1.0	--	--
Administration	0.3	0.4	0.4	0.4
Balance (-, deficit)	-0.1	--	0.6	0.0
State Health Fund 5/				
Revenue	--	8.4	11.3	6.7
Payroll tax	--	1.7	2.7	3.0
Privatization	--	--	0.4	0.2
Transfers from Republican budget	--	6.7	8.0	3.5
Other	--	--	0.1	0.1

Table 12 (concluded). Georgia: Accounts of Extrabudgetary Funds, 1/ 1995-1996
(In millions of lari)

	1995		1996	
	Jan.-June	July-Dec.	Jan.-June	July-Nov. 4/
Expenditure	--	8.5	10.9	6.8
Child health care	--	3.7	4.6	2.9
Psychiatric care	--	2.6	2.6	1.9
Care for vulnerable groups	--	0.4	0.4	0.3
Management reform	--	0.9	1.3	0.8
Other	--	0.9	2.0	0.9
Balance (-, deficit)	--	-0.1	0.4	-0.1
Road Fund 6/				
Revenue	--	--	6.9	12.7
Road user fees	--	--	1.3	4.6
Oil tax	--	--	0.3	0.3
Car tax	--	--	1.5	4.5
Cross-border tax	--	--	3.8	3.4
Expenditure	--	--	8.0	11.6
Maintenance and repairs	--	--	7.7	11.5
Construction	--	--	0.3	0.1
Balance (-, deficit)	--	--	-1.1	1.1
o/w financed by				
arrears accumulation	--	--	-0.7	--

Source: Georgian authorities.

1/ The Privatization Fund is not included because detailed data on this fund's activities are not available.

2/ For the Social Security Fund, the data relate to July-September, not July-November.

3/ Includes allowances for sickness, pregnancy and maternity.

4/ In the case of the Road Fund, the data relate to July-December.

5/ The State Health Fund was officially established on January 1, 1996, but started operations in August 1995.

6/ The Road Fund started in October, 1995.

Table 13. Georgia: Statutory Revenue Sharing Arrangements

Tax	Up until March 1, 1996		March-Dec. 1996		1997	
	Percentage Received by Republican Budget	Percentage Retained by Local Budget	Percentage Retained by Republican Budget	Percentage Retained by Local Budget	Percentage Retained by Local Budget	Percentage Retained by Local Budget
VAT 1/ 3/	90	10	70	30	100	--
Excises	100	--	100	--	100	--
Profit tax 2/	--	100	50	50	40	60
Income tax 2/	--	100	50	50	40	60
Customs duties 3/	70	30	100	--	100	--
Natural resource tax	--	100	--	100	--	100
Ecology tax	--	100	--	100	--	100
Land tax	50	50	50	50	--	100
Property tax	--	100	--	100	--	100
State duties	--	100	--	100	--	100
Exchange bureau tax	--	100	--	100	--	100
Fixed tax on oil imports 4/	--	100	--	100	--	100

Source: Georgian authorities.

1/ Before 1996, 10 percent of VAT revenues was retained by most local governments, although some received a larger share. The average local government share in VAT revenues was around 25 percent in 1995 and early 1996. As from March 1, 1996, the sharing rate for the city of Tbilisi is set at 35 percent.

2/ The city of Tbilisi keeps 55 percent of income tax and profit tax collections as from March 1, 1996.

3/ For 1997, the region of Adzharia retains 30 percent of VAT and 40 percent of Customs duties.

4/ This tax was integrated with excise, VAT and customs duties, as from December 27, 1996.

Table 14. Georgia: Number of Registered and Active Taxpayers, 1994-1997

	1994	1995		1996		1997
	July	January	July	January	July	January
Registered taxpayers 1/	73,884	74,408	74,438	77,029	69,250	64,873
Active taxpayers 2/	30,544	30,123	35,500	39,870	42,600	53,086
Memorandum items:	(In percent)					
Increase in registered taxpayers 3/	6.3	0.7	--	3.5	-10.1	-6.3
Increase in active taxpayers 3/	1.9	-1.4	17.9	12.3	6.8	24.6
Active/registered taxpayers	41.3	40.5	47.7	51.8	61.5	81.8

Source: Georgian authorities.

1/ Only enterprises are registered as taxpayers; in the case of wage earners paying personal income tax, the withholding enterprise is registered as the taxpayer.

2/ Active taxpayers are registered taxpayers who actually pay taxes.

3/ The increase for January 1995 is relative to October 1994, as data for earlier periods are not available.

Table 15. Georgia: Tax Arrears, 1995-96 1/
(beginning of period)

	1995		1996		
	January	July	January	July	December
(In millions of lari)					
Total tax arrears 2/	14.8	30.5	68.1	94.5	121.1
VAT	7.3	13.4	12.3	18.8	15.5
Profit tax	4.9	10.6	13.6	18.2	9.2
Personal income tax	0.0	0.1	0.2	1.6	0.8
Excise tax	0.4	2.3	2.4	3.9	4.6
Property tax	0.2	0.5	1.5	3.1	4.1
Land tax	--	--	10.9	7.4	7.8
Other taxes collected by STS	1.9	3.6	4.6	8.4	7.7
Taxes collected by Customs	--	--	--	--	1.6
Payroll taxes	--	--	22.8	23.1	39.2
Pension Fund	--	--	22.8	33.1	38.4
Employment Fund	--	--	--	--	0.8
(In percent of GDP) 3/					
Total tax arrears 2/	1.1	1.1	1.8	2.0	2.1
VAT	0.5	0.5	0.3	0.4	0.5
Profit tax	0.4	0.4	0.4	0.4	0.3
Personal income tax	--	--	--	--	--
Excise tax	--	0.1	0.1	0.1	0.1
Property tax	--	--	--	0.1	0.1
Land tax	--	--	0.3	0.1	0.2
Other taxes collected by STS	0.1	0.1	0.1	0.2	0.2
Taxes collected by Customs	--	--	--	--	--
Payroll taxes	--	--	0.6	0.7	0.7
Pension Fund	--	--	0.6	0.7	0.7
Employment Fund	--	--	--	--	--

Sources: Georgian authorities; and staff estimates.

1/ The coverage of tax arrears is more complete for 1996, since arrears in contributions to the Pension Fund are included. Also, as from December 1, 1996 the data include arrears of taxes collected by the State Customs Department and payroll taxes collected by Employment Fund. Arrears to the Health Fund, the Road Fund, and some local governments taxes are excluded.

2/ The data include unpaid penalties for overdue tax payment obligations, hiding income, etc.

3/ Presented as a percentage of GDP in the preceding four quarters.

Table 16. Georgia: Excise Tax Rates

	Feb. 1994-June 1995 1/	June 1995-Dec. 1996	As from Jan. 1997
Spirits (except vodka/brandy)	90	100	100
Liquors	60	100	100
Ethyl alcohol	--	--	100
Vodka	60	100	50
Brandy	75	100	50
Champagne	75	100	20
Wine 2/	56	15	15
Beer	30	100	15
Tobacco products 3/	40	100	100
Passenger cars	10	30	15
Car tires	5	50	15
Gasoline 4/	10	15	15
Jewelry	20	50	35
Carpets	40	30	--
Tea	30	--	--
Caviar, chocolate	40	--	--
Chewing Gum	20	--	--
China 5/	30	--	--
Crystal glass	40	--	--
Leather products	35	--	--
Fur garments	25	--	--

Source: Georgian authorities.

1/ Prior to June 15, 1995, differential rates were applied to imports and domestically-produced goods. For imported goods, the shown rates were levied on a tax-exclusive basis; for domestically produced goods, the same rates were applied (except for beer at 10 percent), but on a tax-inclusive basis.

2/ As from December 27, 1996, wine not made from grapes is taxed at 50 percent, as are other fermented alcoholic beverages (e.g. cider)

3/ A lower rate (55 percent) applies to Class 3 and 4 cigarettes.

4/ The excise tax on gasoline was increased to 15 percent on December 1, 1994.

5/ The excise tax on china was eliminated on January 30, 1995.

Table 17. Georgia: Marginal Rates of the Personal Income Tax

<u>Annual income</u>		<u>Marginal Rate</u>
<u>1994-96</u>	<u>1997</u>	
less than lari 10 1/	less than lari 200 1/	12 percent
lari 10-20	lari 201-350	15 percent
lari 20-30	lari 351-600	17 percent
lari 30 and above	lari 601 and above	20 percent

Source: Georgian authorities.

1/ A standard deduction of lari 3.5 per annum applied to all income taxpayers until June, 1996, when it was raised to lari 108 per annum (lari 9 per month).

Table 18. Georgia: Government Wages and Employment, July 1996

	Base Salaries		Bonuses		Total Wage Bill		
	Central Government	Local Government	Central Government	Local Government	Central Government	Local Government	Total
(Thousand of lari per month)							
National economy	344.2	32.8	30.0	3.0	374.2	35.8	410.0
Education	374.6	1556.0	30.0	120.0	404.6	1676.0	2080.6
Science, culture, sports	447.5	230.1	141.0	22.0	588.5	252.1	840.6
Legislative and executive	257.0	174.0	116.5	100.0	373.5	274.0	647.5
Defense and security services	2489.0	290.0	1490.0	140.0	3979.0	430.0	4409.0
Other	48.9	117.7	0.0	0.0	48.9	117.7	166.6
TOTAL	3961.2	2400.6	1807.5	385.0	5768.7	2785.6	8554.3

Number of Employees

(Number of people)

Average Monthly Wage

(Lari per month)

	Central Government	Local Government	Total	Central Government	Local Government	Total
National economy	24,592	2,738	27,330	15.2	13.1	15.0
Education	31,294	141,532	172,826	12.9	11.8	12.0
Science, culture, sports	31,354	22,958	54,312	18.8	11.0	15.5
Legislative and executive	11,506	12,241	23,747	32.5	22.4	27.3
Defense and security services	76,971	907	77,878	51.7	474.1	56.6
Other	4,081	10,703	14,784	12.0	11.0	11.3
TOTAL	179,798	191,079	370,877	32.1	14.6	23.1

Source: Georgian authorities

Table 19. Georgia: The Social Safety Net, 1995-1996. 1/

Main entitlements 2/			
Program	November 1995 - January 1996	February - May 1996	June - December 1996
Pensions (SSF)	lari 6 a month plus lari 3 a month for war veterans	lari 7 a month plus lari 3 a month for war veterans	lari 8.5 a month, except for war veterans who receive lari 11 a month .
Unemployment benefits (EF) 3/	lari 3.5 a month the first two months, lari 2.6 a month for the next two months, and lari 1.8 a month for the final two months	lari 4.5 a month for the first two months, lari 3.6 a month for the next two months, and lari 2.8 a month for the final two months	lari 6 a month for the first two months, lari 5.1 a month for the next two months, and lari 4.3 for the last two months
Child allowances 4/	only as of the second child lari 2 a month in the city and lari 1 a month in rural areas	only as of the second child lari 4 a month in the city and lari 2 a month in rural areas	only as of the second child lari 5 a month in the city and lari 3 a month in rural areas
Benefits for single mothers 4/	lari 2 a month per household	lari 3 a month per household	lari 6 per household
Refugee benefits	lari 6 a month in cash benefits, plus an additional monthly benefit of 20 percent for pensioners, a transportation allowance of lari 2.1 a month for refugees living in Tbilisi, and in-kind benefits (mainly housing)	lari 7 a month in cash benefits, plus an additional monthly benefit of 20 percent for pensioners, a transportation allowance of lari 2.1 a month for refugees living in Tbilisi, and in-kind benefits (mainly housing)	lari 8.5 a month in cash benefits, plus an additional monthly benefit of 20 percent for pensioners, a transportation allowance of lari 2.1 a month for refugees living in Tbilisi, and in-kind benefits (mainly housing) at a cost of lari 8 per month per refugee
Memorandum item: Lowest government wage	lari 6 a month	lari 7.5 a month	lari 9 a month

Source: Georgian authorities.

1/ As from the beginning of 1997, all entitlements were raised by 15 percent.

2/ Stipends are paid to students of higher education institutions; for 1996, the average level of stipends was about lari 4.3 per month.

3/ Employers must pay the first two months of unemployment benefits. The first two months in which the republican government provides a benefit is in months 3 and 4; the final two months are months 7 and 8.

4/ As from January 1997, the child allowance and single mother programs were replaced by a program targeted at four categories of needy families (pensioners living alone, pensioners with children under 18 years of age, unemployed people with children under 18 years, and single mothers not supported by alimony). One-member households are to receive 9 lari per month; 2-member households 7 lari per month per family member; 3-member households: 5 lari per month per family member.

Table 20. Georgia: 1997 Draft Budget
(Official Presentation of State Budget 1/)

	(In millions of lari)	(In percent of GDP)
Total revenues and grants	639.9	9.1
Total revenue	580.0	8.2
Tax revenue	419.4	5.9
Taxes on income	34.8	0.5
Taxes on profit	24.1	0.3
VAT	264.2	3.7
Excises	52.0	0.7
Customs duties	42.9	0.6
Other taxes	1.5	0.0
Revenue from privatization	10.0	0.1
Nontax revenue	43.0	0.6
Extrabudgetary revenue	107.5	1.5
Grants	59.9	0.8
Total expenditures (cash basis)	839.9	11.9
General public services	125.1	1.8
Defense	78.9	1.1
Public order and security	96.4	1.4
Education	51.3	0.7
Health care	47.6	0.7
Social protection	202.8	2.9
of which: Social insurance (pensions, etc.)	130.0	1.8
Social security (mainly for disabled)	12.1	0.2
Refugees, etc.	60.7	0.9
Housing	5.5	0.1
Recreation, Culture, Sports	34.2	0.5
Fuel, energy, mining and minerals	13.2	0.2
Agriculture, Forestry, and Fishing	16.6	0.2
Transport and communication	29.3	0.4
Other economic services	3.9	0.1
Other expenditures	135.2	1.9
of which: interest on debt	74.6	1.1
transfers to local governments	38.2	0.5
Deficit (cash)	-200.0	-2.8
Memorandum items:		
GDP(staff estimate)	7,052	
Revenue and expenditure of local governments	178	2.5
Number of employees 2/	191,000	--

Source: Georgian authorities.

1/ The State Budget excludes the revenues and expenditures of local governments (shown as a memorandum item).

2/ Excludes local government employees, amounting to about 191,000 people.

Table 21. Georgia: Accounts of the National Bank of Georgia 1/

	1994	1995	1996			
	Dec.	Dec.	Jan.	June	Sep.	Dec.
Stocks (end of period; in millions of lari)						
Net international reserves	3.3	59.8	4.7	25.2	-22.7	-35.9
Gold	1.5	1.5	1.5	1.5	1.5	1.5
Foreign exchange reserves	53.7	197.7	192.4	212.9	165.0	201.5
Use of Fund Resources	-51.9	-139.4	-189.1	-189.1	-189.1	-238.9
Other foreign assets (net)	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1
Net domestic assets	37.7	94.0	150.9	147.8	231.0	244.8
Net claims on General Government	27.7	94.6	148.7	167.4	248.9	249.0
Claims on banks	3.9	4.2	3.6	2.2	3.1	13.7
Temporary credit for gas	--	3.7	3.7	3.7	3.7	3.7
Other items, net 2/	6.1	-8.4	-5.1	-25.4	-24.7	-21.6
Reserve money	41.0	153.8	155.6	173.1	208.3	209.0
Currency in circulation	21.1	131.4	129.0	139.7	172.0	185.6
Required reserves	7.9	11.9	11.6	12.5	12.6	13.7
Balances on banks' correspondent a/cs	12.0	10.5	15.0	21.0	23.7	9.7
Flows (with respect to end of previous period; in millions of lari)						
Net international reserves	...	56.5	-55.1	20.5	-47.9	-13.2
Net domestic assets	...	56.4	56.9	-3.0	83.1	13.9
Net claims on General Government	...	66.9	54.1	18.8	81.5	0.1
Claims on banks	...	0.3	-0.6	-1.4	0.9	10.6
Temporary credit for gas	...	3.7	--	--	--	--
Other items, net	...	-14.5	3.3	-20.4	0.7	3.2
Reserve money	...	112.8	1.8	17.5	35.2	0.7
Currency in circulation	...	110.3	-2.4	10.7	32.3	13.6
Required reserves	...	4.0	-0.3	0.9	0.1	1.2
Balances on banks' corresp. a/cs	...	-1.5	4.5	6.0	2.8	-14.1
Change as a percent of reserve money at the end of the previous year						
Net international reserves		1.4	-0.4	-0.2	-0.5	-0.6
Percentage change (with respect to the end of the previous year)						
Net domestic assets	...	149.7	60.5	57.2	145.6	160.4
Reserve money	...	274.9	1.2	12.5	35.4	35.9
Currency in circulation	...	522.7	-1.8	6.3	30.9	41.2

Sources: National Bank of Georgia; and staff estimates.

1/ Valued at current exchange rates.

2/ Fluctuations in this account reflect movements in a blocked account with a initial balance of lari 12 million as the basis of guarantees for wheat imports.

Table 22. Georgia: Monetary Survey 1/

	1994	1995	1996			
	Dec.	Dec.	Mar.	June	Sep.	Dec.
Stocks (end of period; in millions of lari)						
Net foreign assets 2/	-19.2	20.4	-24.0	37.8	-12.6	-13.8
Net domestic assets 2/	92.4	160.1	213.6	162.5	249.4	270.1
Domestic credit	122.7	228.0	294.2	263.1	331.3	364.0
Net claims on General Government	19.8	79.0	125.9	136.6	222.1	235.8
Credit to the rest of the economy	102.9	149.0	168.3	126.5	109.1	128.2
Other items, net 3/	-30.2	-67.9	-80.6	-100.6	-81.9	-93.9
Broad money (M3)	73.3	180.6	189.6	200.3	236.8	256.3
Broad money, excl. forex deposits (M2)	34.1	157.7	150.6	176.2	202.1	218.0
Currency held by the public	18.1	124.8	120.1	130.5	157.7	176.8
Deposit liabilities (domestic currency)	16.0	32.9	30.5	45.7	44.4	41.2
Foreign currency deposits	39.2	22.9	39.0	24.1	34.7	38.3
Total deposit liabilities	58.7	55.8	69.5	69.8	79.1	79.5
Flows (with respect to end of previous period; in millions of lari)						
Net foreign assets	...	39.6	-44.4	61.8	-50.4	-1.3
Net domestic assets	...	67.7	53.5	-51.1	86.8	20.7
Domestic credit	...	105.4	66.2	-31.1	68.1	32.7
Net claims on general government	...	59.3	46.9	10.7	85.5	13.7
Credit to the rest of the economy	...	46.1	19.3	-41.8	-17.4	19.1
Other items, net	...	-37.7	-12.7	-20.0	18.7	-12.0
Broad money (M3)	...	107.3	9.0	10.8	36.5	26.6
Broad money, excl. forex deposits (M2)	...	123.6	-7.1	25.6	25.9	15.9
Foreign currency deposits	...	-16.3	16.1	-14.9	10.6	10.7
Change as a percent of broad money at the end of the previous year						
Net foreign assets		54.0	-24.6	9.6	-18.3	-18.9
Percentage change (with respect to the end of the previous year)						
Net domestic assets	...	73.2	33.4	1.5	55.7	68.7
Broad money (M3)	...	146.3	5.0	11.0	31.1	41.9
Broad money, exc. forex deposits (M2)	...	362.3	-4.5	11.8	28.2	38.2
Memorandum items:						
M3 multiplier 4/	1.87	1.17	1.22	1.16	1.14	1.23
M3 velocity 5/	19	25	24	34	25	22

Source: National Bank of Georgia; and staff estimates.

1/ Valued at current exchange rates.

2/ Large movements in NFA and NDA in June 1996 reflect the carve out of a US\$41.6 million loan from the Turkish Eximbank to the Georgian former Eximbank.

3/ Changes in Other Items, Net in 1996 reflect movements in a blocked account for wheat imports at the NBG, commercial banks' accumulation of capital and write-offs of nonperforming loans.

4/ M3 divided by reserve money (RM).

5/ End-period GDP divided by end-period M3.

Table 23. Georgia: Exchange Rates, June 1993-December 1996 1/

		Lari per U.S. Dollar		Lari per thousands of ruble	
		Average During Period	End of Period	Average During Period	End of Period
1993	Q3 ²	0.00	0.0136	0.01	0.011
	Q4	0.045	0.1023	0.04	0.084
	1993	...	0.102	...	0.084
1994	Q1	0.216	0.384	0.127	0.17
	Q2	0.839	0.814	0.43	0.41
	Q3	1.564	2.300	0.69	0.89
	Q4	1.791	1.280	0.55	0.32
	1994	1.102	1.280	0.45	0.32
1995	Q1	1.294	1.300	0.28	0.25
	Q2	1.300	1.300	0.25	0.24
	Q3	1.300	1.300	0.25	0.25
	Q4	1.258	1.230	0.25	0.25
	1995	1.288	1.230	0.26	0.25
1996	Q1	1.252	1.262	0.24	0.25
	Q2	1.259	1.255	0.22	0.22
	Q3	1.265	1.270	0.23	0.23
	Q4	1.275	1.274	0.22	0.22
	1996	1.263	1.274	0.23	0.22

1/ Lari exchange rates are those prevailing on the Tbilisi Interbank Currency Exchange (TICEX).

2/ August and September 1993 only.

Table 24. Georgia: Summary Accounts of Commercial Banks
(in millions of lari)

	1994	1995	1996		
	Dec.	Dec.	Mar.	June	Sep.
Net foreign assets	-26.6	-39.3	-28.7	12.6	10.1
NFA convertible	-26.7	-39.2	-28.8	12.4	10.1
Gold	0.3	0.4	0.2	0.2	0.2
Foreign exchange	33.1	21.1	31.6	20.6	18.6
Foreign liabilities	-60.1	-60.8	-60.6	-8.3	-8.8
NFA nonconvertible	0.1	-0.1	0.1	0.1	0.0
Net domestic assets	85.3	95.1	98.2	63.4	69.0
Domestic credit	98.5	133.5	145.5	95.7	82.3
Net claims on general government	-7.9	-15.5	-22.7	-30.8	-26.8
Net claims on republican government	-3.1	-7.3	-15.9	-20.2	-15.5
Claims on private sector	106.5	149.0	168.3	126.5	109.1
of which forex loans		63.7	56.5	32.4	37.6
Other assets (net)	-13.2	-38.4	-47.3	-32.2	-13.3
Deposit liabilities	58.7	55.8	69.5	76.0	79.1
Domestic currency deposits	19.5	32.9	30.5	45.7	44.4
Foreign currency deposits	39.2	22.9	39.0	30.3	34.7
Memorandum items					
Share of forex deposits (in percent)	66.75	41.09	56.16	39.83	43.91
Exchange rate (in lari, end-period)	1.28	1.23	1.26	1.25	1.27

Sources: National Bank of Georgia; and staff estimates.

Table 25. Georgia: Currency Composition of Commercial Bank Credit 1/

	1994	1995				1996			
	Dec	Mar	Jun	Sept	Dec	Mar	Jun	Sept	Dec
(In millions of lari)									
Credit to the economy 2/	102.9	112.2	117	132.6	149	168.3	126.5	109.1	128.2
Domestic currency claims	37	36.9	40	...	62.7	78.6	88.2	71.6	83.2
Foreign currency claims	65.9	75.2	77.1	...	86.2	89.6	38.2	37.6	45.0
Onlending of Turkish credit 3/	53.1	59.3	59.3	...	54.6	57.9	--	--	--
Other foreign currency claims	12.7	16	17.8	...	31.7	31.6	38.2	37.6	45.0
(In percent of total)									
Credit to the economy 2/	100	100	100	100	100	100	100	100	100
Domestic currency claims	35.9	32.9	34	...	42.1	46.7	69.7	65.6	64.9
Foreign currency claims	64.1	67.1	66	...	57.9	53.3	30.3	34.5	35.1
Onlending of Turkish credit 3/	51.6	52.9	50.7	...	36.6	34.4	--	--	--
Other foreign currency claims	12.4	14.2	15.2	...	21.3	18.8	30.3	34.5	35.1
Memorandum items									
Exchange rate (lari/US\$; end-period)	1.28	1.3	1.3	1.3	1.23	1.262	1.254	1.27	1.274

Sources: Georgian authorities; and staff estimates.

1/ Excluding claims of the Savings Bank before July 1995.

2/ Credit to the nongovernment sectors.

3/ The government of Turkey, through Eximbank (Turkey) extended a credit line in the amount of US\$50 million to Georgia in 1993. The loan was administered by Eximbank (Georgia) and guaranteed by the Government; the Government determined who received the loans. In May 1996 the Government assumed responsibility for this credit and carved it out of the balance sheet of the United Georgian Bank, which was formed by the merger of Eximbank (Georgia) with two other banks.

Table 26. Georgia: Structure of Commercial Bank Deposits

	1994	1995				1996			
	Dec.	Mar.	Jun.	Sept.	Dec.	Mar.	Jun.	Sept.	Dec.
(In millions of lari, end of period)									
Domestic currency deposits	19.5	15.6	17.7	35.2	32.9	30.5	45.7	44.4	41.2
Deposits of enterprises 1/	16.7	12.4	14.3	30.7	27.9	25.2	39.8	38.2	34.3
Deposits of households/individua	2.8	3.3	3.5	4.4	5	5.3	5.9	6.2	6.4
Foreign currency deposits	39.2	23.3	22	23.6	22.9	39	30.3	34.7	38.3
Total deposits	58.8	38.9	39.8	58.8	55.8	69.5	76	79.1	79.5
(Percent of total)									
Domestic currency deposits	33.2	40.2	44.6	59.8	58.9	43.8	60.1	56.1	51.8
Deposits of enterprises 1/	28.5	31.7	35.9	52.2	49.9	36.2	52.4	49	48
Deposits of households/individua	4.8	8.5	8.7	7.6	9	7.6	7.8	8	9
Foreign currency deposits	66.8	59.8	55.4	40.2	41.1	56.2	39.8	43.9	48.2
Total deposits	100	100	100	100	100	100	100	100	100
Memorandum items									
Foreign currency deposits (In US\$ millions) 2/	32.2	19	17.4	18.2	18.6	30.9	24.16	27.3	30.85
Exchange rate (lari/US\$; end-period)	1.28	1.3	1.3	1.3	1.23	1.262	1.254	1.27	1.274

Sources: Georgian authorities; and staff estimates.

1/ Including deposits of cooperatives, state companies, and so-called public organizations.

2/ Reported data in domestic currency, converted at end-period exchange rate.

Table 27. Georgia: Interest Rates, 1995-1996
(In percent per annum, compounded)

	Mar-95	Jun-95	Sep-95	Dec-95	Mar-96	Jun-96	Sep-96	Dec-96
Commercial banks (3 month) 1/								
Deposits	44.3	31.1	22.1	20.0	17.4	13.9	16.2	20.0
Domestic currency	62.1	39.4	22.1	16.1	18.6	14.3	12.5	19.7
Former state banks	66.9	38.9	22.7	20.7	21.5	9.7	7.9	24.4
Other	58.6	39.8	21.6	12.7	16.4	17.8	17.2	16.4
Foreign currency	28.3	23.1	22.2	24.1	16.3	13.6	20.0	20.3
Former state banks	38.0	30.2	28.1	29.3	18.0	14.6	25.6	24.4
Other	14.9	13.2	13.8	16.6	13.8	12.1	12.1	14.4
Loans	189.6	147.4	115.4	97.0	107.9	80.6	83.6	68.2
Domestic currency	199.9	142.6	112.6	90.4	102.6	80.6	77.6	65.3
Former state banks	328.4	171.9	116.3	95.0	107.0	91.3	84.2	61.6
Other	127.9	122.6	109.9	87.0	99.3	72.9	72.9	67.2
Foreign currency	179.7	152.3	118.2	103.9	113.3	80.6	89.8	71.2
Former state banks	203.5	179.6	140.4	138.2	131.6	95.6	92.5	82.2
Other	147.2	115.9	88.3	60.9	88.3	60.1	85.7	60.9
Interbank credit auction								
7 days	--	89.2	52.1	43.3	54.1	34.5	15.2	13.8
1 month	--	--	--	--	61.1	49.7	41.9	30.9
2 month	--	--	--	--	--	--	45.4	--
3 month	--	--	--	--	97.5	57.1	48.2	43.0
Memorandum items								
12-month inflation (annualized)	1,233.7	448.5	5.3	57.4	55.0	54.8	42.2	13.9
Interest rate spread 2/								
In domestic currency	65.7	58.3	57.7	51.1	55.6	47.1	47.0	33.2
In foreign currency	82.2	75.2	60.4	51.6	63.0	47.8	47.4	36.4

Source: National Bank of Georgia.

1/ Because of missing values, the sample of banks included varies by instrument; therefore comparisons across instruments should be interpreted with caution. Banks are weighted equally rather than by value, as are foreign currency and domestic instruments.

2/ Defined as lending rate minus deposit rate.

Table 28. Georgia: External Debt Outstanding

(In millions of U.S. dollars)

	1992	1993	1994	1995	1996
Total debt outstanding	94.8	543.6	986.8	1,214.7	1,372.9
Medium/long term	94.8	543.6	946.3	1098.8	1178.5
Public and publicly guaranteed	94.8	543.6	946.3	1098.8	1178.5
Official creditors	94.8	543.6	946.3	1098.8	1164.8
Multilateral	--	--	1.0	91.1	180.5
World Bank	--	--	1.0	83.9	165.3
Other	--	--	--	7.2	15.2
Bilateral	94.8	543.6	945.3	1007.7	987.9
FSU 1/	...	364.8	648.8	677.7	628.4
Russia	...	142.6	156.3	167.4	175.4
Turkmenistan	...	181.2 2/	440.3	453.2 3/	394.3
Armenia	...	11.0	18.1	19.7	19.7
Azerbaijan	...	7.6	8.0	8.7	9.3
Kazakhstan	...	22.4	24.1	26.7	27.8
Other	...	2.0	2.0	2.0	2.0
Non-FSU	94.8	178.8	296.4	330.0	359.5
European Union	14.0	88.5	146.9	156.0	150.4
Turkey	--	10.3	42.0	45.4	47.9
Austria 4/	79.9	79.1	92.0	98.8	105.0
Other	0.9	0.9	15.5	29.8	56.2
Private creditors	--	--	--	--	5.0
Private non-guaranteed	--	--	--	--	5.1
Short term	--	--	--	--	--
IMF	--	--	40.5	116.0	194.3
o/w ESAF	--	--	--	--	81.0
SBA	--	--	--	33.2	32.3
STF	--	--	40.5	83.0	81.0

Sources: Georgian authorities; and Fund staff estimates.

1/ Debts to FSU countries other than Turkmenistan initially arose out of the conversion of correspondent account balances and technical credits from 1992 and the first half of 1993 into interstate loans in 1993. Totals for 1992 do not include balances owed on correspondent accounts which were converted into loans in 1993.

2/ All gas arrears at end 1993 were converted into a 2 year loan at libor plus one percent.

3/ Under a preliminary agreement reached in February 1995, all of Georgia's obligations to Turkmenistan, including new gas arrears from 1994 and penalties were converted into a new debt of US\$452.8 million. After a reconciliation of accounts, concluded in May 1995, this figure was reduced to US\$440 million. About US\$46 million were written off in the context of a rescheduling agreement reached in March 1996.

4/ Refers to a credit from a commercial bank dating from 1989; included as official, since amounts due in 1993 and 1994 were rescheduled, with an Austrian government guarantee.

5/ Not included in debts listed above.

6/ Gas transit arrears were not included in the end-1993 agreement.

Table 29. Georgia: External Debt Service Obligations

(In millions of U.S. dollars)

	1992			1993			1994			1995			1996		
	Int.	Prin.	Total	Int.	Prin.	Total	Int.	Prin.	Total	Int.	Prin.	Total	Int.	Prin.	Total
Total debt service due 1/	1.5	1.0	2.5	11.5	3.8	15.3	32.1	117.8	149.9	50.5	274.1	324.7	31.6	89.2	120.8
Medium/long term	1.5	1.0	2.5	11.5	3.8	15.3	32.1	117.8	149.9	50.5	274.1	324.7	31.6	89.2	120.8
Public and publicly guaranteed	1.5	1.0	2.5	11.5	3.8	15.3	32.1	117.8	149.9	50.5	274.1	324.7	31.6	89.2	120.8
Official creditors	1.5	1.0	2.5	11.5	3.8	15.3	32.1	117.8	149.9	50.5	274.1	324.7	31.6	89.2	120.8
Multilateral	--	--	--	--	--	--	--	--	--	2.7	--	2.7	6.3	--	6.3
Bilateral	1.5	1.0	2.5	11.5	3.8	15.3	32.1	117.8	149.9	47.9	274.1	322.0	25.3	89.2	114.5
FSU	--	--	--	1.6	--	1.6	17.7	108.6	126.3	28.5	162.7	191.2	12.0	49.9	61.9
Non-FSU 2/	1.5	1.0	2.5	9.9	3.8	13.7	14.4	9.2	23.6	19.4	111.4	130.8	13.3	39.3	52.6
Private creditors	--	--	--	--	--	--	--	--	--	--	--	--	--	--	--
Private non-guaranteed	--	--	--	--	--	--	--	--	--	--	--	--	--	--	--
Short term	--	--	--	--	--	--	--	--	--	--	--	--	--	--	--
<u>Memorandum items:</u>															
Debt service/ratio 3/	0.4	0.3	0.7	2.2	0.7	2.9	6.6	24.4	31.1	10.8	58.2	69.0	5.9	16.5	22.4

Sources: Georgian authorities, and Fund staff estimates.

1/ Before stock reschedulings were agreed in 1996 with Armenia, Kazakstan, the Islamic Republic of Iran, Turkmenistan, and Uzbekistan. Following agreements on a standstill on debt service, actual debt service paid during 1995 amounted to US\$34.7 million and in 1996 to US\$47.1 million.

2/ Includes debt to the European Union.

3/ At percent of exports of goods and non-factor services.

Table 30. Georgia: Balance of Payments
(In millions of U.S. dollars)

	1992	1993	1994	1995 Est.	1996 Prel. Est.
Current account (before official transfers)	-318.8	-485.1	-447.9	-407.7	-349.9
Trade balance 1/	-377.9	-448.3	-365.0	-338.8	-341.9
Exports	266.6	457.0	380.7	347.2	400.2
FSU	106.0	228.4	195.6	167.0	228.9
Non-FSU	160.6	228.6	185.1	180.2	171.3
Imports	-644.5	-905.3	-745.7	-686.1	-782.7
FSU	-375.4	-444.7	-210.0	-202.5	-264.2
Non-FSU	-269.1	-460.6	-535.7	-483.3	-468.5
Non-factor services	22.7	-17.2	-47.5	17.0	31.8
Credits	87.9	72.7	102.0	121.8	140.4
Debits	-65.3	-89.8	-149.5	-104.8	-108.6
Factor services	36.4	-19.7	-35.4	-85.8	-49.1
Credits	50.1	0.4	0.3	1.0	15.5
Debits	-13.7	-20.1	-35.7	-86.8	-64.6
Official transfers	71.2	131.2	170.0	189.2	140.5
Capital account	247.7	305.6	-19.3	-85.2	53.4
Medium- and long-term borrowing	77.7	381.7	-23.7	-169.4	16.5
Disbursements	78.6	385.5	94.1	104.7	114.5
Amortization	-1.0	-3.8	-117.8	-274.1	-98.0
Other capital 2/	170.1	-91.2	4.4	84.2	27.6
Overall balance	0.2	-63.4	-297.2	-303.7	-165.3
Overall financing	-0.2	63.4	297.2	303.7	165.3
Increase in net international reserves (-) 3/	-0.2	-0.5	-1.0	-40.6	80.8
Exceptional financing 4/	--	64.0	298.2	344.3	84.6
Memorandum items:					
Gross usable reserves	0.7	1.0	41.4	156.7 5/	157.0
Debt service due	2.5	15.3	149.9	324.7 6/	129.6
Stock of debt	94.8	596.9	1001.8	1213.7	1388.8

(As a percent of GDP)

Current account, excl. transfers	-27.5	-42.0	-35.9	-14.1	-7.7
Gross usable reserves 7/	--	--	0.7	2.7	2.5
Debt service due before relief 8/	0.7	2.9	31.1	69.2	24.0
Stock of debt	8.2	51.7	80.4	42.1	30.2

Sources: State Department for Social and Economic Statistics; and Fund staff estimates.

1/ There have been significant changes in the coverage of trade data and, as a result, caution is needed in comparing annual totals.

2/ Includes errors and omissions.

3/ Includes a valuation adjustment.

4/ Arrears and debt relief.

5/ Excludes debt service paid into a special account at the Netherlands Bank.

6/ Before rescheduling.

7/ In months of imports.

8/ As a percent of exports of goods and nonfactor services. Debt service paid in 1995 amounted to the equivalent of 7.4 percent of exports, in 1996 to 8.7 percent.

Table 31. Georgia: Net Energy Imports

	1992	1993	1994	1995	1996
Total energy imports	103.0	395.1	261.8	185.2	252.9
Refined oil products					
Value (in millions of US\$)	0.6	2.6	26.5	94.9	160.0
Volume (in thousands of tons)	154.0	...	181.8	460.0	873.0
Price (US\$ per ton)	3.6	...	145.8	206.3	183.0
Natural gas					
Value (in millions of US\$)	80.2	362.5	213.9	72.8	...
o/w : transit 1/	...	43.6	79.5	...	...
Volume (in millions of m3)	4,982.6	4,265.7	2891.9	910.6	947.0
Price (US\$ per thousand m3)	16.1	85.0	74.0	80.0	...
o/w: transit 1/	...	10.2	25.9	66.9	...
Liquified gas					
Value (in millions of US\$)	0.1	0.1	0.5	0.4	2.1
Volume (in thousands of tons)	5.7	1.3	3.0	9.9	12.9
Price (US\$ per ton)	25.8	81.8	176.7	123.0	162.8
Coal					
Value (in millions of US\$)	--	1.5	0.8	--	0.6
Volume (in thousands of tons)	--	87.6	11.5	0.6	8.0
Price (US\$ per ton)	--	17.1	70.8	30.0	75.0
Electricity					
Value (in millions of US\$)	22.1	28.4	20.1	17.2	14.4
Volume (in millions on kWh)	1,272.2	1,050.7	948.7	754.3	409.5
Price (US\$ per thousand kWh)	17.4	27.0	21.2	22.8	35.1
Total energy exports	6.4	6.3	1.1	2.7	13.1
Electricity					
Value (in millions of US\$)	6.4	6.3	1.1	...	13.1
Volume (in millions of kWh)	256.0	339.0	...	...	313.6
Price (US\$ per thousand kWh)	25.0	18.7	...	...	41.8
Natural gas					
Value (in millions of US\$)	...	...	...	2.7	...
Volume (in millions of m3)	...	...	...	910.6	...
Price (US\$ per thousand m3)	...	...	...	80.0	...
Net energy imports	96.6	388.8	260.7	182.5	239.8

Sources: State Department for Social and Economic Information.

1/ Refers to fees payable for transit of gas by pipeline from the source country to Georgia.

Georgia: Tax Summary, January 1, 1997

Part I: Taxes to be maintained in the Tax or Customs Codes

Note: the four taxes marked with (*) were propositions – part of the *draft* Tax Code – as of January 1, 1997.

Tax	Tax Base and Nature of Tax	Tax Rates	Exemptions and Deductions
1. Value-added tax (VAT)	Value added is the tax base. Manufacturers are taxed on basis of the tax credit mechanism, while retailers and wholesalers pay taxes over the gross price margin. VAT is calculated on a tax exclusive basis using as a base the purchase price of domestically produced goods, while the customs value plus excise tax of imported goods is taxed. Non-oil CIS trade is taxed according to the origin principle (non-oil imports from CIS countries are zero-rated and exports are taxed), non-CIS trade and CIS oil products according to the destination principle (imports from non-CIS countries and oil from CIS are taxed, even if they arrive in Georgia through another CIS country, and exports are exempt). For most transactions, VAT becomes due at the moment of delivery of goods and services. VAT on domestically acquired assets is not immediately deductible, but converted in a two-year tax credit. The threshold for filing is 2,000 lari per annum of taxable transactions; below this amount taxpayers may register.	The general rate is 20 percent; a secondary rate of 10 percent applies to rye and wheat flour and bread.	Exempted from VAT are: goods and services for diplomats; housing rents; lease payments by former state enterprises, sales of confiscated property and other valuables that the state has acquired through inheritance or purchase; public transportation; wheat, children's food products and milk powder (until October 1, 1996); text books and notebooks for school; insurance and reinsurance; financial services as giving and receiving loans, operations with savings accounts, and operations connected with the circulation of domestic and foreign currency; post stamps; membership dues for children's hobby groups, tuition fees, fees for medical services to the old and disabled; funeral services; medicines classified under Chapter 30 of the Harmonized System; medical equipment, prosthetic applications, and technical facilities for the handicapped; re-exports of goods (via a reimbursement scheme); transit goods; re-imports of Georgian representatives abroad; imported goods stored at custom warehouses; imports of national and foreign currency, and securities; goods temporarily stored in Georgia; humanitarian aid; tuition fees; imports of capital goods and spare parts classified under Chapters 84, 85 and 90 of the Harmonized System; goods produced by the Patriarchate for ecclesiastical purposes, and construction and rehabilitation of its churches; domestically published printed materials for mass media; caring services; theater tickets; diabetics' goods; enterprises subject to the presumptive tax.
2. Excise tax	Excise taxes are levied on the sales of excisable goods: spirits; liquors; ethyl alcohol; vodka and cognac; tobacco products; nongrape wines and other alcoholic beverages; champagne and sparkling wines; grape wines; beer; cars; car tires; gasoline; and jewelry. Excises are calculated on the purchase price of domestically produced goods, excluding VAT and excise, and the import duty inclusive customs value of imported goods.	See Appendix I, Table 14.	Exempted from excises are: exports to non-CIS countries; re-exports (subject to a reimbursement scheme); goods in transit; goods temporarily imported; goods stored at customs warehouses; humanitarian assistance; and imports of oil products.

Georgia (continued): Tax Summary

3. Profit and income tax for enterprises	The tax base is profit defined as income less production expenses, including depreciation and wages, of enterprises, their independent branches, and non-commercial organizations engaging in commercial activities and residing in Georgia. In addition, returns on security investments, earnings from partnerships, revenues from gambling, video and audio tape rentals, and profits from mass concerts are taxed at separate rates. Losses can be carried forward for five years, with a yearly maximum of 30 percent of the profit tax due before allowances. The allowed depreciation differs by type of asset and industry.	On December 27, 1996, the standard rate was unified at 20 percent. [Previously industrial and manufacturing enterprises were taxed at 10 percent, and banks and credit institutions at 35 percent.] In addition, schedular rates apply to specific types of income: 10 percent tax on dividends and interest, received from shares, bonds and other securities of enterprises; 70 percent tax on income from gambling activities; 60 percent tax on the profits from mass concerts.	Exempted from the profit and income tax for enterprises are: enterprises that are subject to the presumptive tax; prosthetic and orthopedic enterprises; profits of companies producing technical means for the rehabilitation of invalids; profits of the Georgian patriarchy manufacturing ecclesiastical articles. Profits from agricultural production are exempt, except for industrial agricultural enterprises. For the calculation of the profit tax, reserves accumulations of up to 25 percent of funds paid in capital and 50 percent of profits are deducted from profits. These limitations do not apply to commercial banks; their reserve accumulation is exempt from profit tax as long as it is within the guidelines of the NBG. Allowance for the following items are deducted from the profit tax, with a maximum of 10 percent of taxable profit: expenditures for scientific research and restoring monuments; expenditures in the context of natural disasters; maintenance of houses for the elderly and handicapped and other specified social purposes.
4. Personal income tax	The annual income of natural persons residing in Georgia is the tax base.	See Appendix I, Table 15. Marginal rates vary from 12 percent to 20 percent. In addition, dividend income is taxed at 10 percent.	Exempted from personal income tax are: persons subject to the presumptive tax; handicapped persons (depending on the degree of handicap, they are for 50 percent or 100 percent exempt); war veterans; women with many children; social benefits; revenues from domestic state bonds; interest income from domestic banks and credit institutions; lottery prizes; alimony; revenues from property sales; and revenues from the sales of agricultural goods produced privately.
5. Customs duties	The tax base for customs duties is the customs value (fob) of imports, including barter trade, from non-CIS countries. In addition, a processing fee is levied the customs value (cif) of imports and exports, and on transshipments.	The main customs duty rate is 12 percent; effective end-1996, selected raw materials (see Attachment 1 of EBS/97/29) are taxed at 5 percent. The processing fee is 0.3 percent (increased from 0.2 percent as of July 1996), and a US\$10 fee applies to transshipments owned by a CIS resident and US\$100 if a non-CIS resident owns the goods.	Exempted from customs duties are: personal imports up to a value of lari 300; goods in transit and re-exports; non-commercial imports for cultural institutions; baby food; sixteen types of medicine; humanitarian aid; and diplomatic shipments.
6. Ecology tax	The ecology tax is levied on polluting activities: the use of fuel for vehicles, the dumping of solid waste, the dumping of waste in water or the atmosphere, and the sales of environmentally hazardous products (i.e. used materials sold for recycling).	The tax rates are based on damage factors, which depend on the type of pollution and whether pollution limits are exceeded. Rates are either expressed as a percentage of the minimum wage or fixed in lari, multiplied by the volume of the polluting substance. In the case of sales of environmentally hazardous products, the tax depends on the sales price.	None.

Georgia (continued): Tax Summary

7a. Enterprise property tax	The enterprise property tax is levied on the assessed value of non-financial assets, means of production, installed equipment, and unfinished constructions of the enterprise. Excluded from taxation are: housing, communal, social and cultural facilities; environmental and fire safety facilities; roads, communication services, and electric lines; land; and official measurement equipment. New enterprises get a tax holiday of 1 year, after which the tax rate is reduced by 50 percent for two years.	1 percent.	Exempted from the enterprise property tax are: budgetary enterprises and organizations, and property used for educational and cultural purposes.
7b. Individual property tax	The individual property tax is levied on the value of buildings and houses and means of transportation owned by natural persons.	For buildings and houses: 0.1 percent of the assessed value; For vehicles: 0.2 percent of the minimum wage per horsepower.	Exempted from the individual property tax on houses and buildings are: pensioners; enlisted military personnel and their families; war veterans and their families; and houses and buildings in rural areas. Exempted from the property tax on vehicles are: invalid owners of hand controlled automobiles and motorcycles with side-cars; and boats with engines not exceeding 10 horse powers.
8. Tax on property transfers (*)	The tax is levied on the amount paid, directly or indirectly, in the transfers of titles to immovable properties or leases of such property.	2 percent	Leases for less than 3 years; transfers to spouses, parents, sons and daughters; gratuitous transfers to budgetary, charitable, or religious organizations.
9. Social security contributions	Social security contributions are imposed on money wages, and are used for the financing of activities of the SSF, EF, and the Health Fund. Until 1996, these funds were responsible for collection of the contributions; in 1997, this responsibility was transferred to the STS.	State-owned and private enterprises pay a 27 percent levy to the SSF on the money wages they pay to their workers; 1 percent to the EF and 3 percent to the Health Fund. Budgetary organizations also pay 27 percent of their wage bill to the SSF. Workers pay 1 percent of their wages to the SSF and 1 percent to the Health Fund.	Employers can subtract the cost of providing benefits to their active workers, such as maternity benefits and sick pay, from their contribution to the SSF.
10. Vehicle tax	Tax on ownership of vehicles levied on an annual basis; the proceeds of this tax are paid into the Road Fund.	The tax is levied per horsepower in the domestic currency equivalent of: US\$0.2 for cars; US\$0.5-2 for buses (depending on number of seats); and US\$1-3 for trucks (depending on tonnage).	Exempted are city buses.
11. Vehicle cross-border tax	This tax is levied on vehicles registered abroad entering Georgia and domestic vehicles transporting transit trade; the proceeds of this tax are paid into the Road Fund.	Cars are taxed at US\$20; buses US\$20-130 (depending on number of seats); and trucks US\$130-300 (depending on tonnage).	Transit vehicles that reenter Georgia after having delivered goods to a third country and are returning to their home country.
12. Land tax	Tax levied on cultivated land, including pastures, and on land that could be cultivated.	Tax rates vary from the national currency equivalent of US\$0.3 per hectare to US\$1,000 per hectare, depending on the use, quality, and location of the land. During the first two years, newly established farms pay 50 percent of the tax.	Exempted are: cultural, educational, social welfare, environmental, and defense organizations and sports complexes; education and research institutions, experimental farms, hydro meteorological centers, environmental establishments and equipment funded by the Government; nature reserves, botanical gardens; national parks; natural historical and cultural monuments; cemeteries common-use lands, water pools, lands of monasteries and lands near state borders; pensioners, war veterans and invalids; newly cultivated land as well as state-owned property, while persons living in abandoned villages or who are moved in the context of government programs are exempt for five years.

Georgia (continued): Tax Summary

13. Tax on use of minerals (*)	Royalties and taxes on bonuses and excess profits associated with extraction of mineral resources.	To be established by contract.	To be established by contract.
14. Natural resources tax (*)	Tax on the use of natural resources, viz. Water, forest and wild plants.	Being established.	Use of natural resources for scientific or educational purposes; cutting of timber for conservation purposes or for the process of establishing quotas.
15. Gift and inheritance tax (*)	Tax is the property received by persons through the process of inheritances or gifts from other physical persons.	Tax rates (proposed) are based on the fair market value of the property at the time of receipt, minus certain deductions: 10 percent for heirs of the first order; 20 percent for heirs of the second order; 30 percent for other heirs and for legal persons.	[proposed] Gifts below 1,000 lari; inheritances below 100,000 lari; receipt of property from a deceased spouse, or the gifts of property from one spouse to another spouse.

Part II Taxes or fees not part of Tax or Customs Codes (but still applicable on January 1, 1997)

1. State tax	The tax is paid by juridical and natural persons for legal services provided by legal offices.	The tax rates are defined according to each action performed and document issued.	For persons under 16 years of age, the rate is reduced by 50 percent for documents needed for travel abroad. War veterans are exempted from the tax on prolonging documents certifying this.
2. Tax for state licensing of enterprises and business activities	The tax is paid by enterprises for registration of their business and business activities.	For legal entities who do not have authorized funds, the tax rate is three times the minimum wage; enterprises with authorized funds pay five times the minimum wage. Natural persons pay three times the minimum wage.	Not available.
3. Presumptive tax (fixed tax)	The presumptive tax is an annual tax levied on the business area of enterprises that occupy less than 20 m ² , and a flat tax in the case of exchange bureaus; it does not apply to enterprises and organizations of Tsekavshiri (state cooperative trade company) and communication enterprises. The presumptive tax replaces the VAT, profit tax, and personal income tax of entrepreneurs.	Enterprises with a business area of less than 10 m ² pay lari 13 per month, and enterprises occupying between 10 m ² and 20 m ² pay 1 lari per month for each additional m ² . The tax is reduced by 40 percent for enterprises located in the countryside and increased by no less than 30 percent for enterprises located near main roads and squares of cities. Exchange bureaus located in Tbilisi pay a flat tax of US\$100, while those outside of Tbilisi pay US\$70.	The same exemptions apply to natural persons as under the income tax.
4. Tax on hazardous products	The tax on hazardous products is levied on the production and sales of products that pose health risks (tobacco and tobacco products, liquor, and asbestos products). The proceeds of this tax are transferred to the Health Fund.	Production of cigarettes is taxed at a rate of lari 0.005 per 20 cigarettes, and the tax on the sales of cigarettes is lari 0.01 per 20 cigarettes. The tax on cigar sales is lari 0.01 per cigar. The production of other tobacco products, liquor, and asbestos products is taxed at 0.5 percent of the production value, while the sales of these products is taxed at 1 percent of the production value.	None.

Georgia (continued): Tax Summary

5. Road tax	Tax on the use of roads for commercial activities; the proceeds of this tax are paid into the Road Fund.	Enterprises who transport passengers or cargo by vehicles pay 2 percent of the profits from these activities; commercial banks pay 0.5 percent of their profits; while commerce enterprises and brokers pay 0.1 percent of turnover. For enterprises that have production, trade, service, or facilities located along roads (in inhabited areas within 50 meters and in uninhabited areas within 400 meters) the above rates are doubled.	Payments of the fuel and lubricants tax are subtracted from the Road Tax.
6. Fuel and lubricants tax	Tax on the sales of fuels and lubricants; the proceeds of this tax are paid into the Road Fund.	Production companies are taxed at 5 percent of the value of the production excluding VAT and excises, while wholesale and retail traders pay 5 percent of the difference between the purchase and the sales price.	None.
7. Underground communications and advertisement tax	Tax on the exploitation of underground communications (telephone, electrical wiring, gas pipes, water lines, etcetera) constructed near roads and advertisement posters and boards placed at road-sides; the proceeds of this tax are paid into the Road Fund.	Owners of underground communications pay the national currency equivalent of US\$0.1 per meter, while owners of advertisement posters or boards pay the equivalent of US\$5-20, depending on the kind of road.	None.
8. Water tax (to be replaced by the "natural resources tax" in the Tax Code)	Tax on the use of water by enterprises.	Tax rates vary from 0.025 to 0.057 times the minimum wage depending on the water source	None.
9. Natural resources tax (to be replaced by a "tax on use of mineral resources" in the Tax Code)	Tax on the conducting of geological surveys and prospecting operations, and the extraction of minerals.	Tax rates vary from 1 percent to 5 percent of expenditures for surveys, prospecting and construction for mining operations; from 1 percent to 15 percent for extraction, depending on the type of mineral extracted (5 percent to 10 percent for oil and gas); a 30 percent profit tax for mining enterprises; and 10 percent of profits for the use of water in mining operations.	None.

The Social Safety Net

SSN benefits are provided by the Social Security Fund (SSF), the Employment Fund (EF), and the Health Fund (HF). Pensions are provided by the SSF; child allowances (until end-1996), as well as sickness, pregnancy, and maternity allowances, unemployment benefits are provided by the EF, while basic health care services are reimbursed by the HF. The republican government also finances benefits for refugees, stipends for students through the higher education institutions, and benefits to single mothers.

The SSF was established in 1991, and provides old-age, invalidity and survivors' pensions on a pay-as-you-go basis. It collects its own revenue from payroll taxes. In 1996, these consisted of a 29 percent payroll tax for state-owned and private enterprises and a 26 percent payroll tax for budgetary organizations, and a mandatory contribution for workers of 1 percent of their wages. In 1997, employer contributions were unified at 27 percent. Employers are allowed to deduct benefits they pay to their active workers, such as sickness, pregnancy, and maternity benefits, from the payroll tax. In the 1997 budget, child benefits and benefits to single mothers were replaced with targeted assistance to families in need; the 1997 budget also requires that employers meet the remuneration for the first 5 days of sick leave, up to a maximum of 30 days per year.

In February 1996, the retirement age was increased from 55 to 60 years for women and from 60 to 65 years for men. However, disability pensions are still granted liberally. The pension benefit is low; the standard pension during June-December, 1996 was lari 8.5 (US\$6.8) per month while war veterans received lari 11 (US\$8.7) per month (see Appendix I, Table 19). Pensioners cannot receive multiple pensions and benefits are withheld from those who have work income, except for war veterans who are allowed to work and receive a pension.

The EF was also established in 1991 and, like the SSF, functions on a pay-as-you-go basis. Its revenues are derived from a 1 percent payroll tax on non-budgetary institutions. The EF provides an unemployment benefit for those who have been out of work for a period between 3 and 8 months. Moreover, the EF administers the labor exchanges, which collect information on vacancies and the unemployed, and actively look for job opportunities. As from January 1996, the EF eliminated its ineffective job creation schemes.

In the context of wide-sweeping changing in government funding of health care, the HF was set up in August 1995. The HF is designed to act as a financial intermediary for the reimbursement of both private and public health care providers, but it is limited to a basic package of preventative and curative health care services. Like the SSF and EF, the HF is funded by a payroll tax on enterprises (3 percent) and a mandatory contribution for workers of 1 percent of their wages. The republican government also provides a budgetary transfer to the HF to ensure that the most vulnerable population groups who are not contributing also benefit from the HF's provision of basic health care.

Considerable assistance is provided to about 287,000 refugees, and benefits are also provided to families with children, single mothers, and students. Refugees receive a flat cash benefit, supplemented by a benefit for pensioned retirees. Since July 1, 1995, refugees living in Tbilisi receive a benefit to compensate for the increased cost of transportation. In addition, the Government pays for rent and food for refugees housed in hotels and guest houses. During July 1995 to end-1996, families received allowances as from the second child, until they reach 18 years old of age and as long as they attend school and live at home. In the 1997 budget, universal child benefits were replaced by targeted assistance to four categories of poor families: pensioners living alone, pensioners with children under 18 years, unemployed persons with children under 18 years, and single mothers not supported by alimony. Finally, the republican government provides a limited number of stipends for students. Universities receive transfers from the MOF, which they allocate to students according to their study results.

The SSN provides benefits to a large number of people; out of a population of 5.4 million, about 1.8 million people received a benefit as of July 1, 1996. This number is likely to fall in coming years as the effect of raising the retirement age takes hold. However, without any change in policy, the ratio of benefit recipients to total population will rise in the longer run as the aging process continues.

In 1995 the SSN had a limited significance on poverty reduction because benefits were very low due to resource constraints and there was a large number of benefit recipients. The problem of low benefits is being addressed by increasing benefits faster than price increases. Also, the long-term financing of the pension system is being enhanced by setting up a framework for the creation of private pension funds. However, there is scope for tightening the eligibility requirements for the invalidity pension and eliminating the provision of benefits to refugees who receive an income from work.

Georgia: Seignorage and Inflation Tax¹

The loose fiscal and monetary policies adopted during 1993–94 led to hyperinflation and a collapse of Georgia's first national currency, the coupon.² The coupon was introduced in April 1993, following the termination of ruble supplies from the Russian Federation to the National Bank of Georgia (NBG) in late 1992. Faced with a drastic decline in tax revenues, the authorities failed to cut budgetary expenditures accordingly and instead relied heavily on central bank credit to finance the mounting fiscal deficit, which reached 50 percent of GDP in the first half of 1994.

As a result of hyperinflation, both seignorage collection and the inflation tax declined markedly during 1994. The seignorage collected by the Government during 1993 had exceeded 9 percent of GDP, while the inflation tax had reached about 18 percent of GDP. These were equivalent to over 450 percent and 900 percent, respectively, of the amount of conventional tax revenues collected during this period (Table 1 and Figure 12). Seignorage collection fell to about 3 percent of GDP in 1994 despite a 2,462 percent nominal increase of reserve money during the year. In view of the sharp increase in the opportunity cost of holding coupons, real money balances declined sharply, as the public switched almost entirely to foreign currency. In the process, the ratio of broad money relative to GDP declined to about 5 percent in 1994 from over 14 percent of GDP in 1993. The shrinking of the monetary base (the tax base of the inflation tax) also led to a decline in the inflation tax to 3.7 percent of GDP in 1994, despite a 62 percent average monthly inflation rate (the tax rate of the inflation tax) during the first nine months of 1994. The Government was not able to "collect" the full amount of the inflation tax because the public "evaded" the tax through demonetization.

Starting in the fourth quarter of 1994, the authorities introduced stringent monetary policies;³ these policies halted hyperinflation and paved the way for the introduction of a new currency, the lari, in October 1995. The introduction of the lari was followed by a significant reversal of

¹Seignorage, which measures the amount of real resources the Government is able to capture by printing money, is defined as:

Seignorage (real) = $[H(t) - H(t-1)]/P(t)$, where H = monetary base and P = price level
The inflation tax, which measures the decline in the value of real money balances caused by inflation, is defined as:

Inflation tax = $[H(t-1)/P(t-1) - H(t-1)/P(t)]$
it can be shown that seignorage = inflation tax + $[\frac{H(t)}{P(t)} - \frac{H(t-1)}{P(t-1)}]$

² Georgia's hyperinflation (generally defined as monthly inflation rates over 50 percent for a period of at least six months) started in September 1993 and continued until May 1994. During this period, inflation averaged over 70 percent per month.

³During the first nine months of 1995 reserve money increased by about 28 percent, compared with 1,037 percent in the first nine months of 1994.

currency substitution, which led to the accumulation of about US\$55 million in foreign exchange reserves by the monetary authorities during the fourth quarter of 1995. The seignorage collected during this period (the lari equivalent of the build-up in international reserves) amounted to about 9 percent of fourth quarter GDP, since reserve money at end-December 1995 increased by about 300 percent relative to the end-September 1995 level. The inflation tax increased slightly during the same period, to 2.2 percent of the fourth quarter GDP. Following the continuation of a prudent monetary policy, seignorage fell to about 1 percent of GDP in 1996 compared with 3.1 percent in 1995, and the inflation tax was brought down to less than 1/2 percent of GDP from about 1 percent in 1995. Therefore, as stabilization took hold, financing of the budget deficit through inflation was severely curtailed.

With regard to Georgia's prospects for seignorage revenue in the future, experience in other hyperinflationary cases suggests that despite a substantial growth in the months after hyperinflation has been brought under control, real reserve money recovers only slowly during the medium to long run (Table 2). Furthermore, given Georgia's extremely low monetary base, seignorage revenue is not likely to exceed 1-2 percent of GDP per annum if control over inflation is maintained.

Figure 12. Georgia: Seignorage and Inflation Tax, 1993-96
(In percent of GDP)

Table 1. Georgia: Seignorage and Inflation Tax, 1993-1996

	1993	1994	1995	1996
Reserve Money				
(in millions of lari)	1.6	41.0	153.8	209.0
(in percent of GDP)	9.8	3.0	4.2	3.7
Seignorage				
(in percent of GDP)	9.3	2.9	3.1	1.0
of which:				
- Inflation tax 1/ 2/				
(in percent of GDP)	18.3	3.7	0.9	0.4
- Change in Real Stock of Reserve Money (in percent of GDP)	-9.0	-0.8	2.1	0.6
Total tax revenue 3/				
(in percent of GDP)	11.3	5.9	6.7	6.3
Total tax burden 4/				
(in percent of GDP)	20.3	6.7	4.5	5.7
Seignorage over Nonseignorage Tax Revenue (in percent)	469.5	95.7	84.8	18.2
Inflation Tax over Nonseignorage Tax Revenue (in percent)	923.1	122.9	26.1	7.1
Memorandum items:				
Nominal GDP (in millions of lari)	16.4	1,373.2	3,694.2	5,724.0
12-month Inflation rate (in percent)	7,487.7	6,473.9	57.4	13.9
Tax revenue (in percent of GDP)	2.0	3.0	3.6	5.3
Velocity (ratio) 5/	5.3	40.3	25.3	22.9

Source: Georgian authorities; and Fund staff estimates.

1/ Calculated on the basis of monthly data.

2/ Using period-average reserve money (average of beginning-of-period and end-period).

3/ Tax revenue plus seignorage.

4/ Tax revenue plus inflation tax.

5/ Measured as a ratio of annualized fourth quarter GDP over end-period broad money.

Table 2. Reserve Money, Inflation and Seignorage in Selected Countries before and after Hyperinflation

Period 1/	Bolivia 2/			Germany 3/			Austria 4/		
	Reserve Money (in percent of GDP)	Seignorage (in percent of GDP)	Inflation Rate (in percent)	Reserve Money 5/ (in percent of GDP)	Seignorage (in percent of GDP)	Inflation Rate (in percent)	Reserve Money 5/ (in percent of GDP)	Seignorage (in percent of GDP)	Inflation Rate (in percent)
t-2	...	...	123.5	...	...	145.7	...	...	114.2
t-1	14.4	...	275.6	...	...	31.6	...	...	105.3
t	15.3	14.4	1,281.4	...	...	1,022.5	...	...	95.1
t+1	7.0	6.9	11,749.6	...	...	5.7	...	...	2,544.3
t+2	4.3	2.0	276.3	...	...	3.8	...	...	25.5
t+3	5.2	1.5	14.6	6.9	...	9.6	9.1	...	13.2
t+4	7.4	2.9	16.0	7.8	0.7	1.1	8.6	0.6	13.0
t+5	8.0	1.7	15.2	6.8	0.5	4.3	9.1	0.5	6.9
t+6	9.1	2.0	17.1	6.7	0.2	3.1	9.0	0.6	2.2
t+7	9.5	2.2	21.4	7.1	0.0	1.0	9.1	0.6	2.1
t+8	8.7	0.4	12.1	7.5	-0.3	-4.0	9.0	0.3	3.1
t+9	10.0	2.5	8.5	9.2	0.0	-8.3	9.4	0.0	-
t+10	9.2	0.4	7.9	8.2	-2.4	-11.4	11.4	0.8	-5.0

Source: International Financial Statistics; International Historical Statistics: Europe 1750-1988; and Fund staff estimates.

1/ Period t denotes the year when hyperinflation started.

2/ t = 1984; hyperinflation in Bolivia started in April 1984 and ended in September 1985.

3/ t = 1922; hyperinflation in Germany started in August 1922 and ended in November 1923.

4/ t = 1921; hyperinflation in Austria started in October 1921 and ended in August 1922.

Exchange, Trade and Payments Systems

Georgia accepted the obligations of Article VIII, sections 2, 3, and 4 of the Fund's Articles of Agreement on December 20, 1996.

Exchange arrangements

1. The currency of Georgia is the lari. The lari became the sole legal tender on October 2, 1995, replacing the coupon, which had been introduced on April 5, 1993, and was declared the sole legal tender on August 3, 1993. For all commercial transactions, the exchange rates of the lari are negotiated freely between the banks and foreign exchange bureaus that are licensed by the NBG, and their customers. In addition, the Tbilisi Interbank Currency Exchange (TICEX) holds sessions on each working day at which the NBG and the banks, judged by the TICEX to have sufficiently large foreign exchange turnover, participate. Auctions take place only for the U.S. dollar and the Russian ruble. At these sessions, all transactions take place at the single exchange rate for each currency which balances supply and demand.

2. Between January and August 1996, the official exchange rates for the U.S. dollar and the Russian ruble were determined as the exchange rates arising at the TICEX session of the previous Friday. Since August 12, 1996, the official rates are set daily. Official rates for other convertible currencies are determined on the basis of the cross rates for the U.S. dollar and the currencies concerned in the London market. For the currencies of other states of the former U.S.S.R., official exchange rates are determined on the basis of the official cross rates for the Russian ruble as determined in the Moscow market. Official exchange rates are used only for government transactions and accounting purposes. Compulsory sales of foreign exchange by exporters to the NBG have been abolished since January 1996.

3. On December 31, 1996, the official exchange rates were lari 1.274 per U.S. dollar and lari 0.00022 per Russian ruble.

Administration of control

4. The NBG is responsible for administering exchange control regulations, which are formulated in collaboration with the Ministry of Finance. Decree No. 259, of March 5, 1992, on "The First Stage of Liberalization of Foreign Economic Activity" established the legal basis for the conduct of foreign economic activities in Georgia. The main provisions of this decree: (i) allow all enterprises to engage directly in foreign trade; (ii) allow all residents to acquire and hold foreign currency and engage in foreign transactions with a licensed foreign exchange dealer; and (iii) authorize banks to open foreign exchange accounts for all residents.

5. The NBG has the authority to issue general foreign exchange dealing licenses to banks to permit them to engage in foreign exchange transactions with residents and nonresidents and to open correspondent accounts with banks outside of Georgia. The NBG also has the

authority to issue internal licenses to banks which permit them to engage in the same range of foreign exchange transactions as general license holders, except that holders of internal licenses may not open correspondent accounts with banks abroad; all transfers of foreign exchange by holders of internal licenses must be carried out through correspondent accounts held either with the NBG or with a bank that holds a general license. The NBG also has the authority to issue licenses for the establishment of exchange bureaus to engage in exchange transactions of all kinds in banknotes.

Prescription of currency

6. Residents of Georgia may make and receive payments and transfers in any convertible currency as well as in rubles.

Resident and nonresident accounts

7. Resident individuals and enterprises are permitted to open and operate foreign exchange accounts at banks in Georgia. The balances in these accounts may be used for all authorized transactions. The opening of foreign exchange accounts abroad by residents is subject to authorization by the Ministry of Finance and the NBG. Nonresidents may maintain foreign exchange and local currency accounts with banks in Georgia and may freely remit funds from these accounts offshore. The export of cash currency is permitted by non-residents up to a limit equal to the amount of currency originally imported; exports by non-residents of cash in excess of the amount imported by more than US\$500 but less than US\$10,000 are subject to a fee of 2 percent, beyond this amount the fee is 3 percent. The export of cash by residents is unrestricted up to an amount of US\$500. Beyond this amount, exports of cash, excluding amounts for business travel expenses, are subject to a 2 percent fee, with amounts over US\$10,000 subject to a 3 percent fee (Decree No. 1 of January 6, 1995 on Provisional Rules for the Export of Foreign Currency Notes by Citizens, as amended by Decree No. 158 of May 6, 1995).

Imports and import payments

8. Trade with countries other than the states of the former U.S.S.R. is controlled by the State Committee on Foreign Economic Relations (SCFER) (Decree No. 265 on Quotas and licensing of Merchandise Trade of March 31, 1993 and Decree No. 35 of January 23, 1995, on the State Regulations of the Export and Import of Goods and Services). There are no quantitative restrictions on imports, and licenses are generally not required. A customs duty of 12 percent is levied on most non-CIS imports as well as imports of fuel from CIS countries; certain goods are subject to a customs duty of 5 percent as of January 1, 1997, including specific capital goods, medical goods and equipment previously taxed at 12 percent, and certain raw materials. Humanitarian aid, literature published by Georgian citizen abroad, diplomatic shipments, non-commercial imports for internal consumption by cultural groups or certain institutions and activities of the patriarchate, gifts valued at less than US\$3,000 and personal belongings, goods in transit and for re-export, and various categories of foods and

medicines are exempt. All imports are subject to a general customs processing fee of 0.2 percent. Foreign exchange to pay for imports may be purchased freely from authorized banks at market rates.

Exports and export proceeds

9. Only a limited range of goods are subject to export prohibitions or licensing requirements. Export prohibitions apply only to scrap metals. Licenses are required for the export of woods in trunks and pine seeds; numismatic collections considered national treasures; certain biological (species of animals and plants), paleontological, archeological, and ethnographic goods; and raw materials for medicine production. All exports are subject to a general customs processing fee of 0.2 percent. Export contract registration requirements have been abolished as of December 1996.

Payments for and proceeds from invisibles

10. Residents may freely purchase foreign exchange to make payments for invisible transactions or use foreign exchange balances in their foreign exchange accounts with authorized banks without restriction. Proceeds from invisibles are subject to the same regulations and procedures as those applicable to the proceeds from exports. The importation of foreign currency bank notes is unrestricted, but amounts must be declared by non-residents.

Capital

11. Inward and outward capital operations are not restricted. Since July 15, 1996, the amount of cash lari that can be taken out of the country by a resident or nonresident without permission by the NBG is limited to four units of each currency denomination.

Gold

12. A license is required to conduct both international and domestic trade in gold.