

THE IMF IN GEORGIA: EVALUATING THE FUND'S UNIQUE VISION OF ECONOMIC SUCCESS

Lasha TCHANTOURIDZÉ

*Adjunct Professor of Politics,
Research Associate, Center for Defense and
Security Studies, the University of Manitoba
(Winnipeg, Manitoba, Canada)*

Introduction

Many things have changed in Georgia after the Rose Revolution of November 2003. Certain changes are very positive and praiseworthy, such as the abolition of deeply corrupt and universally hated traffic police, and its replacement with the Western style patrol police. Reforms in the armed forces are also heading toward a positive direction. However, the economy does not seem to be the new government's priority. The leader of the Rose Revolution and the current president of Georgia Mikhail Saakashvili has made it clear a number of times that he was not interested in solving economic problems of the country as much he was interested in dealing with security and defense issues. When presenting a newly composed government in February 2005, Saakashvili was quoted by saying: "I can build the army, I can build the police, but development of the economy is up to the entire society."¹ Prior to that President of Georgia voiced similar sentiments at his address to the country's parliament.²

Indeed, compared to reforms in the military and law enforcement agencies economic reforms in Georgia have fallen far behind. This was partially acknowledged by Saakashvili in his above-mentioned address to the Parliament. According

to Mr. Demur Giorkhelidze, a Georgian economist, no one in the Georgian government has an idea whether the country has a general program dealing with the economy or not. Instead, some government officials have "fragmented" views about certain issues related to the economy.³ The government of Georgia has no master plan for economic development and rehabilitation. In any case, it has no published plan or program whatsoever.

A superficial review of the country's economic performance in recent years does not produce a full picture. Georgia has been both praised and criticized for its economic reforms or the lack thereof. The International Monetary Fund (IMF) has given positive evaluations to the Georgian economy. In a statement published on 13 June, 2005, Rodrigo de Rato, Managing Director of the IMF, declared that Georgia has "accelerated the transition to an open, market-based economy, most visibly in the reform of the tax code..."⁴ At the same time, according to the annual publication by the U.S. based Heritage Foundation in cooperation with *The Wall Street Journal*, 2005 *Index of Economic Freedom*, Georgia remains in

³ See: "Sakartvelos mosaxleobis naxevarze meti gharibia," *Rezonansi*, No. 260, 29 September, 2005.

⁴ "Statement by IMF Managing Director Rodrigo de Rato at the Conclusion of His Visit to Georgia," The International Monetary Fund [<http://www.imf.org/external/np/sec/pr/2005/pr05140.htm>].

¹ "Saakashvili Speaks of Successes, Presents New Cabinet," *civil.ge* [www.civil.ge], 15 February, 2005.

² See: "Saakashvili Addressed the Nation, Parliament," *civil.ge* [www.civil.ge], 10 February, 2005.

the group of “mostly unfree” countries, with its index worsening in 2005. The publication lowered Georgia’s index by 0.15 points compared to 2004, and gave it the 100th spot on the list of 161 countries.⁵ In September 2005, the World Bank named Georgia among the top reformers in the world, and ranked it number one among the former Soviet states, and number two globally (after Serbia and Montenegro).⁶ Meanwhile, another U.S. based think-tank, the Cato Institute, which monitors economic freedoms around the world, ranks Georgia the 66th in the world among the 127 countries sur-

⁵ See: *2005 Index of Economic Freedom*, The Heritage Foundation [<http://www.heritage.org/research/features/index/countries.cfm>].

⁶ See: “Doing Business in 2006: CIS Economies Pick Up the Pace of Reform,” The World Bank news section, 12 September, 2005 [www.worldbank.org].

veyed.⁷ The data used by the Cato Institute was collected in 2003, and since then a number of things have changed negatively for the Georgian economy.

Tbilisi follows IMF recommendations without reservations. This is the reason why the IMF and the World Bank are praising Georgia. That does not, however, translate into improved economic conditions and alleviation of poverty. The latter remains especially acute problem for Georgia—with a negligible number of families below the poverty line in 1991, now more than 50 percent of the population lives in deep poverty, according to the World Bank itself.⁸

⁷ See: “Economic Freedom of the World,” The Cato Institute [<http://www.cato.org/pubs/efw/>].

⁸ See: “Sakartvelos mosaxleobis naxevarze meti gharibia.”

Georgia’s Economy and Finances

The country’s foreign debt has increased to more than \$1,700 million by the beginning of 2005. It has stabilized at that level in 2005, but likely to increase further as Georgia will get more loans from the IMF, World Bank, and other sources, as an IMF poster boy for economic reforms.⁹ This is a huge amount for a country with the population of around 4 million people.¹⁰ At the same time, Georgia’s trade deficit in the first six months of 2005 was more than \$500 million, and it reached \$733 million by the end of August 2005.¹¹ The country is not making hard currency while its debt to foreign creditors is set to grow further. In September 2005, the World Bank approved another cache of loans for Georgia in the amount of \$143 million for the period of 2006-2009.¹² The loan is earmarked for economic growth, job creation, and strengthening of the public sector. While the fulfillment of these projects is a theoretical possibility, Georgia faces a real danger of falling into a debt spiral, which will further undermine the country’s economic base. The current debt accumulated over 14 year period since 1991,

⁹ See: *Bulletin of Monetary and Banking Statistics (January-August 2005)*, The National Bank of Georgia [<http://www.nbg.gov.ge/>].

¹⁰ Various sources estimate Georgia’s population to be more than 5 million. This figure derives from the 1989 Soviet census, and now seems to be much exaggerated. At the 1989 census, Georgian authorities artificially inflated population numbers of their republic to get higher allocation of funds from Moscow—the Soviet system depended on the centralized distribution of funds for almost all aspects of life. Further, after the collapse of the Soviet Union, out-migration from Georgia achieved staggering proportions. More conservative estimates put the number of those who left the country at one million. Finally, Georgia’s separatist regions of Abkhazia and South Ossetia also experience demographic problems of their own. More than 300 thousand people have been either expelled or left Abkhazia and South Ossetia since 1991, most of them were Georgians the majority of whom remained in Georgia, but among them were ethnic minorities as well (Jews, Greeks, Ukrainians, Russians), and there were Ossetians who left the Tskhinvali and other regions for the Russian Federation. Therefore, it is unlikely that the population of Georgia currently is much higher than 4 million people.

¹¹ See: *Bulletin of Monetary and Banking Statistics (January-August 2005)*.

¹² See: “World Bank Approves USD 143 Million for Georgia,” *civil.ge*, [www.civil.ge], 16 September, 2005.

with the rate of more than \$120 million a year. Less than 10 percent of this amount would have been sufficient to improve job creation and eradicate poverty, had they been spent properly. Georgia's debt to GDP ratio reached 44 percent in 2003, but it decreased to 34 percent by the beginning of 2004,¹³ and remains within 35-40 percent range in 2005.

It is noteworthy that Georgia's trade deficit almost doubled during Saakashvili's first year in office. In 2004, Georgia's trade deficit was \$1,199 million, compared to \$675 million in 2003. According to the first seven month figures of 2005 (\$733 million), the trade deficit is very likely to increase by the end of 2005.¹⁴ Georgia's trade deficit is somewhat off-set by grants and aid money from foreign donors, plus Georgia has a positive balance in service trade. Therefore, the current account deficit even decreased in 2004 compared to 2003 from \$346 million to \$308 million.¹⁵ What should be noted here is that the trade deficit figures only reflect the so-called "registered trade," while smuggling and extra-legal (non-registered) trade activity is very widespread in Georgia. In Tbilisi's wholesale markets and bazaars one could see an assortment of smuggled goods, as well as goods imported by shuttle traders from Azerbaijan, Turkey, Russia, Syria, China, and other countries. Such non-registered trade in Georgia (also common in other post-Soviet states) is mostly comprised of such imported items as alcohol, tobacco, clothing, jewelry, etc. Further problems in proper accounting are presented by still corrupt customs officials, who could register lesser values for imported goods (in exchange for bribes, of course).

A trade deficit itself may not be a bad thing for a developed industrialized country. According to a conventional (neo-liberal) view, a country with a trade deficit normally experiences a rise in direct foreign investments.¹⁶ At least, this is an IMF principle, which also serves as a "comfort food" for this organization when it praises poor developing countries with large trade deficits. Theory of trade deficits promoting investments definitely works for the United States—the U.S. currency being the most widespread means of exchange in the world. It may work for industrialized countries with hard currencies. However, it is very unlikely to ever work in poor developing countries. Why would anyone keep soft currency or invest large sums in an unstable environment, especially these days when everything from natural disasters to terrorists affect smaller economies on daily bases? As it was noted above, Georgia's trade deficit almost doubled from 2003 to 2004. At the same time, foreign direct investments increased only marginally from \$340 million in 2003 to \$499 million in 2004.¹⁷ Moreover, this increase was due to only one project: the five billion dollar Baku-Tbilisi-Ceyhan oil pipeline. The pipeline, which runs from Azerbaijan's Baku to Turkey's Mediterranean Ceyhan, was completed in 2005, and the numbers for foreign direct investments in Georgia for 2005 are due to decline.

In June 2005, the International Monetary Fund cited "the real GDP growth of 6.2 percent in 2004" (compared to the average of 4.9 percent from 1998 to 2003, the last five years of Mr. Shevardnadze's rule).¹⁸ However, with growing foreign debt and disproportionately large trade deficit for a small country, this economic growth is mostly fuelled through loans and aid coming from foreign sources. According to the owner and publisher of the *Rezonansi*, a leading Georgian newspaper, there is almost no internal investment and business development in the country.¹⁹ Georgia experienced growth

¹³ See: "Annual Reports" for 2003 and 2004, The National Bank of Georgia.

¹⁴ See: *Bulletin of Monetary and Banking Statistics (January-August 2005)*; "Annual Reports" for 2003 and 2004.

¹⁵ Ibidem.

¹⁶ See: Th.D. Lairson, D. Skidmore, *International Political Economy: The Struggle for Power and Wealth*, Thomson Wadsworth, Toronto, 2003, p. 24.

¹⁷ See: *Bulletin of Monetary and Banking Statistics (January-August 2005)*.

¹⁸ "Analysis of Recent Growth in Low-Income CIS Countries," *IMF Working Paper* No. 04/151, p. 7 [www.imf.org]; "IMF Mission Assesses Fiscal Situation in Georgia," *civil.ge*, 10 June, 2005.

¹⁹ Interview with Mr. Zurab Macharadze, Tbilisi, 25 August, 2005.

in domestic business enterprises in 1997-1999, but since then there has been a steady decline, and the revolutionary regime of Mr. Saakashvili has not been able to reverse it. It should also be noted that the sustained growth in GDP numbers since 1998 may be due to other factors than government policies or foreign direct investments. According to Ariel Cohen of the Heritage Foundation, "close to 1 million Georgians are repatriating their earnings to their homeland to the tune of up to one-fourth of Georgian GDP."²⁰

Government's reconstruction projects mostly include nonproductive infrastructure: rebuilding roads, repainting buildings, and repairing schools. Although all these help to improve basic infrastructure of the country, and the image it presents to the visitors, they are not nearly enough to address the real issues of economic devastation, deep poverty and hardship. Georgian regions outside Tbilisi have suffered a tremendous economic decline since the beginning of the 1990s. The economic situation has got even worse with the Saakashvili administration, with unemployment rising and residents of rural areas getting further impoverished. According to residents of the Guria Region in western Georgia, they mostly survive through subsistence farming, and whatever little cash they make comes from their hard work for very little pay during the tourist season in summer.²¹ Guria was one of the wealthiest regions in Georgia and the former Soviet Union; now vast majority of its residents make less than one dollar a day. Overall, there is a large gap between the living standards in Tbilisi and rural Georgia. Vast majority of Georgia's poor population resides in rural areas and small towns.²²

According to Georgian newspaper and TV reports, agricultural sector in the country faces a serious crisis.²³ There is a danger that farmers and peasants in eastern Georgia will abandon the tradition of grape harvesting, which is thousands of years old.²⁴ In 2004, a lot of grape harvest went to waste, and in 2005 the farmers were facing the same prospect. Georgia abandoned agricultural subsidies as it was demanded by the IMF and the World Trade Organization (WTO). In western Georgia similar problems exist for growers of citrus cultures, especially in the Ajaria Autonomous Republic, which until last spring was under authoritarian rule of Mr. Aslan Abashidze. Mr. Abashidze, who is in self-imposed exile in Moscow, was deposed through the efforts of local population and pressure from Tbilisi. The people of Ajaria invested a lot of hope and trust into the new government of the region appointed by Mr. Saakashvili. However, so far this government delivered very little to rural residents of the autonomous region.

To escape hardship and poverty rural population pursues illegal and extralegal logging operations. Georgia as a mountainous country is wealthy with forests and rivers. However, often clear-cut logging operations are conducted without any planning and nearby densely populated villages. This contributes to the rise of flooding and landslides in the country. The year of 2005 witnessed the highest number of major floods and landslides in Georgia in recent memory. In spring, the second largest city, Kutaisi was flooded by rising waters. In spring and summer flooding and landslides were experienced in almost all parts of Georgia. In Svaneti, a regional center Lentekhi was almost completely destroyed, and some villages were fully erased from the map. In August, major

²⁰ A. Cohen, "Our Challenge in Georgia," The Heritage Foundation [<http://new.heritage.org/Press/Commentary/ed011504a.cfm>].

²¹ Interviews with Guria residents in Poti, Ozurgeti, and Lanchkhuti districts, July 2005.

²² According to City of Tbilisi officials, no one really knows what is the current population of Tbilisi. Conservative estimates put it around 50 percent of the country's total.

²³ TV and newspaper reports in September 2005.

²⁴ The Ministry of Agriculture of Georgia tried to convince the grape farmers that their lot will improve "next year." They are projecting increased wine exports for 2006. The grape harvest in 2005 was more than 145 thousand tons in the Kakheti Region only, while winemakers only need about 70 thousand tons (see: "Kurdzeni iafdeba," *Rezonansi*, No. 242, 11 September, 2005).

floods and landslides were registered in Guria and Ajaria.²⁵ Ironically, in one case in Guria floods and landslides damaged and destroyed property of local small logging companies.²⁶ Illegal logging is fueled by demands in the neighboring Turkey, very cheap Georgian labor, and rising local demand for fire wood. Increasing number of city residents, and vast majority of rural residents use fire wood for winter heating.²⁷ Eighty percent of residents in Georgian regions do not have access to natural gas—either it is not available or they cannot afford it.²⁸ Natural gas will become even more expensive before this winter: to retaliate for reneged privatization of the Georgian gas pipeline system, the Russian gas giant Gazprom is planning to double the price for natural gas it is supplying to Georgia.²⁹

Hardship and economic devastation is accompanied by the spread of illiteracy and crime. Many families in rural areas cannot afford to send children to school—they do not have winter shoes and/or clothing, do not have access to school supplies or children have to work to support their families. Georgia had close to 100 percent literacy in the beginning of the 1990s. According to the research published by the Prime-News agency in July 2005, currently about 20 percent of young people cannot read and write.³⁰ Crime is on the rise as well. A significant number of crimes committed are basically thefts of food, and minor property—anything that could be sold at local markets for few laris (\$1 equals to 1.8 lari). According to newspaper reports, violence among family members is rising significantly, and the major cause of this is quarrel for money or material resources.³¹ According to the Ministry of Interior, in 2004 there were 302 murders registered in Georgia, and in the first three months of 2005 there were 65 murders. The Ministry of the Interior does not offer separate statistics for domestic violence, but Georgian news-media estimates that a large number of these murders are committed among family members vying for limited resources.³²

Despite all these, there are developments that give reasons for optimism. The signing of a compact between the governments of the United States and Georgia under the U.S. sponsored Millennium Challenge Corporation (MCC) on 12 September, 2005, during the visit of the President of Georgia to the United States for the U.N. summit, will no doubt help to alleviate certain problems that mainly stem from bad administrative and managerial decisions by the Georgian government. For instance, the compact which allocates more than \$295 million over a five-year period, prohibits selling of the main Georgian gas pipeline, and earmarks funds, about \$49 million for its rehabilitation. Earlier in 2005, the Georgian government was getting ready to sell this strategic pipeline to the Russian *Gazprom*.³³

The compact, which also addresses problems of economic development of Georgian regions, and private enterprises, is the most important economic aid project offered to Georgia since its gain-

²⁵ Newly appointed governor of Guria, Mr. Irakli Giorgadze has pointed out that the authorities are aware of the problems related to illegal loggings, and that they will address it in due time. "This country was looted for 14 years, and now you cannot demand it to be restored in one," he told *Guria-News* weekly (see: "Irakli Giorgadze: khe-tkis problema mogvarebulia..." *Guria-News* weekly, No. 32-33, 13 September, 2005).

²⁶ Georgian TV reports, 25-27 August, 2005.

²⁷ See: "Sakartveloshi cxovreba 30-40 protsentit gadzvirdeba: mosaxleoba masobrivad sheshis ghumelze gadadis," *Rezonansi*, No. 243, 12 September, 2005.

²⁸ Ibidem.

²⁹ See: "Ruseti bunebriv airs gvidzvirebs," *Akhali Taoba* weekly, No. 251, 11-17 September, 2005.

³⁰ See: "15 Years Old Boy Cannot Afford Himself To Get Education," The Prime-News agency [<http://eng.primenewsonline.com/?c=134&a=1588>], 27 July, 2005.

³¹ See: "Zaza lomidzem sakutar dedas keli gamochra," *Akhali Taoba* weekly, No. 250, 10 September, 2005; "Roman potskhverashvilma shelaparakebisas sakutari dzma mokla," *Akhali Taoba* weekly, No. 253, 13 September, 2005.

³² See: "Sakartveloshi ojaxuri mkvlelobebis faqtebi katastrofulad matulobs: khashurshi shvelma dedas keli gamochra, terjolashi dzmam dzma sanadiro topit mokla," *Rezonansi*, No. 244, 13 September, 2005.

³³ See: "Millennium Challenge Corporation Signs \$295.3 Million Compact with Georgia." For more detailed information on the MCC Georgia program, and information about the Millennium Challenge Program itself, see: [<http://www.mca.gov/>].

ing independence from the Soviet Union in 1991. In its scope and magnitude, the Millennium Challenge Corporation is the most important global economic initiative by the U.S. government since the creation of the Bretton Woods system in 1945. The success of the program will depend on the effective management of the projects not only in Georgia but in other beneficiaries of the MCC: these nations are not only very poor, they are also very corrupt.³⁴

Fiscal and Monetary Policies

In 2004, the Georgian government under Saakashvili initiated tax reforms that lifted some burden from business. A number of business taxes were either combined or eliminated altogether. However, the new government was not able to reduce by much the biggest burden businesses have to carry, the European style value added tax. From the mid-1990s, at the insistence by the IMF, the value added tax was 20 percent. The Saakashvili team had promised prior to reduce this tax, but after they were elected they only managed to reduce it by 2 percent. The IMF simply did not allow a further reduction.³⁵ The IMF pushed such a high tax in the mid-1990s, amid the lack of basic market structures and the absence of necessary legal and political frameworks. Such rushed policies and exaggerated expectations contributed to social tensions, impeded capital accumulation, and worsened allocation of savings.³⁶

The value added tax is the single biggest source of tax evasion and extralegal economic activity in Georgia. For a number of years now, corrupt officials and private entrepreneurs have devised a number of illegal schemes that allow most businesses not to pay value added tax or to pay it partially or to get refunds where no refund is due. Value added tax may be working in European countries, but in Georgia's tax system it has been the single biggest disaster since 1991. Value added tax also discourages many small businesses to register their activity, and to pursue their business through legal channels. Under the previous government headed by Mr. Shevardnadze, Georgian extralegal economy was estimated at 50 to 60 percent of its GDP.³⁷ The levels are not as high anymore; however, it is clear that a considerable portion of Georgian economic activity is still outside the legal system. Every private enterprise in Georgia, big or small, has some kind of loophole, scheme or a "roof" to reduce its tax burden.³⁸

Mainly because of widespread extralegal business activity, Georgian banks are not very eager to loan funds to upstart businesses. Bank interest rates are very high in the country, again a policy advised and supported by the IMF. Annual interest rates range between 16 and 24 percent. At the same

³⁴ Besides Georgia, MCC has signed Compacts with Madagascar, Cape Verde, Honduras, and Nicaragua.

³⁵ According to Professor Joseph Stiglitz, a Nobel Prize winner in Economics, and former Vice-President of the World Bank, the IMF is very fond of such taxes, since they are regarded as sure ways to raise revenues (see: J.E. Stiglitz, *Globalization and Its Discontents*, New York: W.W. Norton & Company, 2003).

³⁶ See: O. Kandelaki, "Georgia: Economic Policy After the 'Revolution of Roses,'" *Central Asia and the Caucasus*, No. 5 (29), 2004.

³⁷ See: H. de Soto, *The Mystery of Capital: Why Capitalism Triumphs in the West and Fails Everywhere Else*, Basic Books, New York, 2000, p. 69.

³⁸ The institution of the "roof" or "*krysha*" in Russian, are a sets of arrangements between a business or a group of businesses and influential politicians or civil servants. According to such arrangements, government officials provide a cover for businesses under their protection. Such covers could protect businesses from warranted or unwarranted investigations, harassments, etc. by government agencies. This institution in Georgia is not nearly as big and violent as it is in Russia, where "roofs" are needed to protect businesses from both government agencies, and organized crime.

time, banks pay around 10 percent a year on deposits (held for a year, on longer-term deposits interest rates are higher). IMF's "wisdom" here is obvious: it is believed that higher interest rates on savings will convince people to save more, and it also will attract foreign investors. Indeed, high interest rates on savings partially fulfilled such sentiments, savings rates in Georgia have risen over the last ten years; however, there is no increase in the interest of foreign investors to keep savings in Georgian banks or to invest in anything for that matter.³⁹

At the same time, in the existing climate of economic decline and poverty, small and medium size businesses have very hard time to raise funds and create jobs. High taxes combined with high interest rates on bank loans do not favor small and medium manufacturing businesses. The most widespread type of economic activity in Georgia is trading, namely shuttle trading. Small and medium size merchants flood Georgian markets with cheap goods from Turkey, Syria, China, Russia and some other countries. Such shipments could change hands a number of times before the goods reach consumers, with each pair of hands making a small profit. Trading is advantageous for entrepreneurs since they could get away from customs and tax officials after paying small amounts in bribes, if necessary. Exporters do not own shops or other expensive infrastructure, instead they sell their goods to tens of thousands of small shop traders who are only happy to sell the products and make a couple of dollars of profit a day. Anyone who owns a more or less large enterprise in a fixed location could become subject to constant shakedowns by various government agencies (of course, in the absence of a proper "roof").

Such government sanctioned shakedowns intensified under the present Georgian government. Presumably, they have been conducted to recover unpaid or concealed taxes. Georgia's budgetary surplus has been largely due to such operations conducted by much feared financial police of Georgia. The other major source of the increase in budgetary income is the fact that taxes collected in Ajaria do not anymore end up in the pockets of the Abashidze clan.

Georgian customs and tax authorities, in cooperation with the financial police, occasionally initiate new forms of tax collection that are normally illegal. For instance, in August 2005, they started charging one thousand laris (about \$560) per cubic meter of imported goods at the country's land entry points. This meant that an entrepreneur importing soft toys for which he had paid around \$3 per cubic meter, had to pay \$560 at the customs.⁴⁰ It has not become clear yet who initiated this customs duty. The rumors had it that the new duty was invented by the financial police. Cases of the invented one thousand lari duty were widely reported by Georgian media, to the extent that Georgia's ombudsman got involved in the case. Such fiscal innovations are clearly illegal under the Georgian Tax Code, but in weird ways they do take place. Importers normally do not go to courts for they know that the judges are useless—they basically do whatever high executive government officials tell them to do. There are other kinds of abuses by tax and customs officials.⁴¹ State sanctioned shakedowns of exporters,

³⁹ See: *Bulletin of Monetary and Banking Statistics (January-August 2005)*.

⁴⁰ Interviews with Georgian business people, end of August 2005. The importer brought a container of soft toys from China. His entry point to Georgia was Poti, a sea port at the Black Sea. There he was asked to pay GL 1,000 (\$560) duty per cubic meter of imported goods, for which he paid approximately GL 4 (\$2.20) in China. The importer knew this demand was illegal, and probably an innovation of local customs officials. He decided to clear customs in the capital city, Tbilisi, which is legal under Georgian law. However, he was asked to pay the same duty in Tbilisi. Unable to meet such demands, the importer decided to keep the imported goods at a customs terminal. Subsequently he cleared customs through his friend, a government official, who negotiated a duty equaled to 35 percent of the product value (an average import duty in Georgia).

⁴¹ Interviews with Georgian business people, and government officials. Customs officials frequently exaggerate the value of imported products. In one case, a businessman was importing blankets. He had paid for each blanket approximately GL 2 (\$1.11), but the product was evaluated at GL 35 (\$19.4) by Georgian customs (although such blankets retail for GL 7 (\$3.90) each in Georgian shops). Therefore, the importer was required to pay GL 12.25 (\$6.80) duty per GL 2 blanket, which made no economic sense. Unable to meet such demands, the importer offered the blankets to the state, he ex-

normally foreigners taking souvenirs abroad, are also common.⁴² It is clear that the IMF never studied tax and customs practices in Georgia, but offered its praises noted above based on the data supplied by the government. The main result of innovative approaches by Georgian tax and customs officials is a four kilometer long truck line-up on the Turkish side of the Georgian-Turkish border in Sarpi. A more general implication of such fiscal innovations is the message that business activity in Georgia still depends on whims of high-level officials with wild imagination.

Real Estate

In 2004-2005, Georgian banks have been mostly funding real estate development projects in Tbilisi, the capital city of Georgia. Real estate prices have risen considerably, and in some cases reached astronomical levels for a poor country. Real estate is especially expensive in Tbilisi, where the price for a new apartment reached \$1,500 per square meter. Single family housing is even more expensive. Banks are investing heavily in new real estate projects, and in more prestigious older areas of the city, where it is believed the demand for residential and commercial real estate will rise in the future. If Georgian banks get heavily dependent on such real estate projects, expectations may become unrealistic and this potential real estate bubble could drag down the whole banking system of the country.

Real estate speculation in Tbilisi is further fuelled by the presence of many residential buildings that had to be condemned many years ago. Buildings that are more than hundred years old in hilly areas of Tbilisi are damaged, some of them heavily, and all of them are still occupied. Some of these buildings are missing walls or have huge cracks in ceilings and walls. Tbilisi is located in a seismic area, and the next big earthquake will destroy these buildings, and produce hundreds of casualties. Real estate developers and banks expect that the national or the city government would step in and relocate people from the damaged buildings. If that happens the vacated property would become available for new developments. In September 2005, two damaged buildings collapsed in Tbilisi, with few casualties. The authorities currently do not seem have any program to relocate residents or to allow banks and developers to rebuild damaged areas. The previous mayor of Tbilisi, who was removed by President Saakashvili in June 2005, had a plan developed to relocate residents from damaged buildings with proper compensation. However, with his ouster this plan has died.⁴³

Concluding Remarks

In the first half of the 1990s, Georgian economy declined sharply, with the GDP indices falling more than 30 percent every year from 1992 to 1995, and whopping levels of inflation that turned into wild hyperinflation of 1994. Inflationary processes stabilized in 1995, after the introduction of lari, the new Georgian currency. For the ten years of its existence, lari remained very stable. Georgia has followed very closely to the policy recommendations it got from the IMF and the World Bank. These

pressed his willingness to donate the imported blankets to some worthy cause. Georgian customs refused to accept the donation. In the end, the importer cleared the customs through an influential friend, who negotiated the price down to GL 8, which was still higher than the retail value of the product, but much better than the original demand.

⁴² Such cases were reported by an English language Georgian *Business Week* in July and August 2005.

⁴³ Interview with the Deputy Chief of City of Tbilisi Service Department, 1 October, 2005.

institutions pay a lot of credence to financial and economic austerity. However, the stable currency and austere policies have not changed much for vast majority of Georgian citizens. The National Bank of Georgia, the country's central bank, has been obsessed with inflation, just like most Western and IMF supported central banks around the world. This obsession at times goes too far. From 2001 to 2004, the country's monthly consumer price index dropped a number of times,⁴⁴ while such commodities as fuel, housing, tuition have been steadily increasing in prices. Such deflationary tendencies changed more recently—now Georgia is on a steady inflationary curve (so far it remains in single digits), which is not great but much better than deflation.

Georgia has served as an example for IMF's economic reform programs. Tbilisi and other capitals of developing and poor countries need IMF's positive evaluations in order to present themselves in "pro-business" or "pro-Western" light. This is the main reason why high government officials in Georgia, even those who disagree with the IMF, do not criticize the organization. Criticism has been voiced, however, to the displeasure of the IMF.⁴⁵

Georgians have invested a lot of hope into the country's new leadership. President Saakashvili and his team have to pay more attention to the economy, if they want to justify that investment. So far nothing much has been done in the country to alleviate acute poverty and hopelessness. Georgia's youth is still hoping to "go West"—in a random poll among young Tbilisi residents by TV channel *Mze* conducted in July 2005, all respondents indicated that one of their main goals in life was to emigrate to the West.

The economic situation in Georgia is far from being satisfactory. By the World Bank's own estimates, for the next ten years Georgia will not be able to reduce its poverty levels even by half.⁴⁶ Despite such dire predictions, the country's leadership has to do more to give future generations hope, and provide basics for its population. For this they need not follow blindly policy recommendations from the IMF or elsewhere, but the government has to develop its own industrial and trade policies to remedy Georgia's abysmal foreign trade performance. Even if society could build the economy, the government has to guide it through promoting the manufacturing cycle and exports. No country with a large trade deficit has ever developed into a better society, and Georgia will be no exception.

⁴⁴ See: *Bulletin of Monetary and Banking Statistics (January-August 2005)*.

⁴⁵ A former Minister of the Economy of Georgia, 1994-2000, Vladimer Papava has provided critical examination of IMF's activities in Georgia in his "On the Role of the International Monetary Fund in the Post-Communist Transformation of Georgia," *Emerging Markets, Finance, and Trade*, Vol. 39, No. 5, 2003; and *Splendours and Miseries of the IMF in Post-Communist Georgia*, Laredo, TX: we-publish.com, 2003.

⁴⁶ See: "The WB's Forecasts are Not Consoling," Prime-News Agency [www.primenewsonline.com], 29 September, 2005.