

Running a Business in Georgia

New data from the Enterprise Surveys indicate that senior managers in Georgian firms devote only 2 percent of their time to dealing with the requirements of government regulation (figure 1). This is the lowest figure in all of Eastern Europe and Central Asia (ECA). The average number of visits or required meetings with tax officials fell significantly for firms interviewed in both years from 8.0 in 2005 to only 0.5 in 2008 after the implementation of new tax legislation. Despite this improvement, several other areas of concern remain in Georgia: Business loans require extremely high levels of collateral, and both capacity utilization and exports are low by regional standards. In fact, capacity utilization among Georgian manufacturing firms is the lowest in the ECA region and has decreased since 2005.

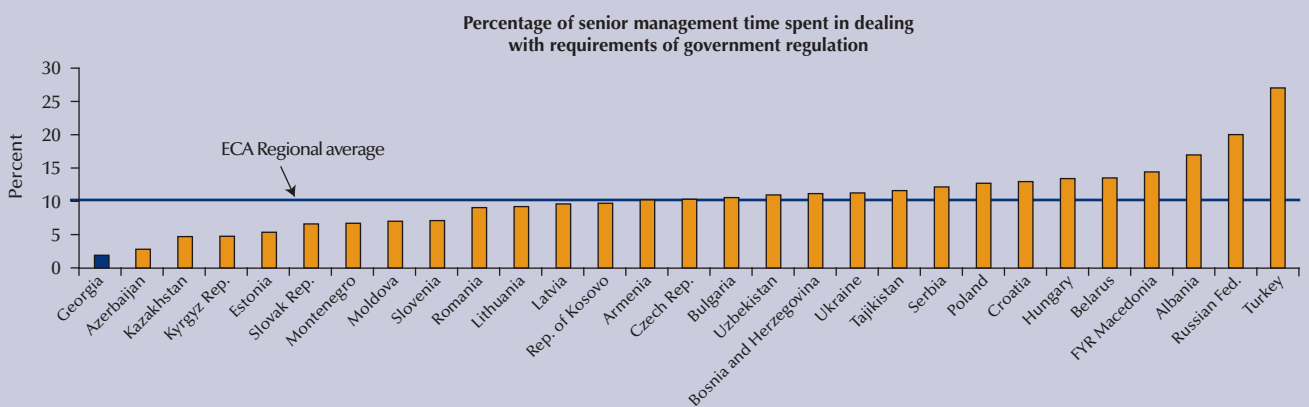
The Enterprise Surveys¹ use standard survey instruments to capture data on the business environment and its effect on competitiveness and firm performance, the relative importance of various constraints to employment and productivity, and the business perceptions of the biggest obstacles to enterprise growth. The survey is designed to be representative of a country's private nonagricultural economy, and firms sampled are stratified by size, location, and sector (figure 2)² to ensure that most major types of firms are covered. Only firms with five employees or more are included in the sample. In Georgia, 373 firms were surveyed from April through August 2008. The information collected refers to the firms' characteristics at the moment it was surveyed or during fiscal year 2007.³

What Is the Average Firm in Georgia?

In Georgia small firms are most common and ownership structure is related to size. Small and medium firms in Georgia are much more likely to be owned by locals: Large firms average 65 percent private domestic ownership, whereas small and medium firms average 94 and 93 percent, respectively. Government participation in the ownership of private firms is not common in Georgia.

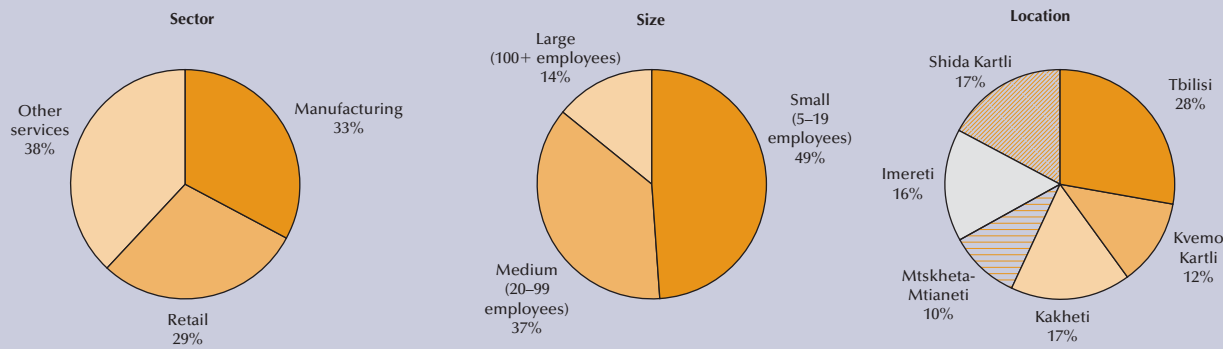
Employment levels vary considerably across sectors. Manufacturing and retail firms tend to have fewer permanent, full-time workers than firms in other sectors, with 32 in manufacturing and 23 in retail, versus 49 workers on average in other sectors. Firms that export are significantly

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



Source: Enterprise Surveys.

Figure 2 Characteristics of the Firms Interviewed



Source: Enterprise Surveys.

larger, with an average of 107 workers versus 35 for nonexporters, as are firms in Tbilisi, where firms employ an average of nearly 54 permanent full-time workers.

Temporary workers are more common in Georgia than in any other ECA or EU-10 country; the average Georgian firm⁴ employs nearly 24 temporary workers. Large firms in Georgia employ an average of more than 100 temporary workers, though retail firms employ fewer temporary workers than manufacturing firms.

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Firms in Georgia are younger than the regional average. The average firm in Georgia is just over 10 years old and is younger by about four years than the average firm in other ECA countries and EU-10 countries (table 2). Only 3 percent of firms are at least 20 years old, and around a quarter of firms are five years old or younger. At the average firm, the top manager has nearly 19 years of experience working in the firm's sector; however, top managers at large firms have an average of only 13 years of experience in their firm's sectors.

Table 1 How Does Georgia 2008 Compare with Eastern Europe and Central Asia?

Ranking 1 assigned to the largest value	Descending ranking (out of 29 countries)
% of Firms Formally Registered when Started Operations in the Country	6
Private Domestic Ownership (%)*	16
Private Foreign Ownership (%)*	9
Government/State Ownership (%)*	19
% of Firms with Female Participation in Ownership	11
Bank Finance for Investment (%)	12
% of Exporter Firms	23
Domestic Sales (% of Sales)	6
% of Firms with Internationally Recognized Quality Certification	20
% of Firms with Annual Financial Statement Reviewed by External Auditor	8
Capacity Utilization (%)	29
% of Firms Using Their Own Web Site	23
% of Firms Using Email to Communicate with Clients/Suppliers	27
Ranking 1 assigned to the smallest value	Ascending ranking (out of 29 countries)
Value of Collateral Needed for a Loan (% of the Loan Amount)	28
Number of Power Outages in a Typical Month	15
Senior Management Time Spent in Dealing with Requirements of Government Regulation (%)	1
Average Number of Visits or Required Meetings with Tax Officials	4
Incidence of Graft Index **	10
Losses Due to Theft, Robbery, Vandalism, and Arson against the Firm (% of Sales)	26

Source: Enterprise Surveys.

Table 2 The “Average Firm” in Georgia 2008

	Georgia	ECA†	EU-10‡
Age (years)	10.1	14.0	14.1
% of Firms Formally Registered When Started Operations in the Country	99.6	96.8	98.7
Most Common Legal Form	Closed	Closed	Closed
	Shareholding Co.	Shareholding Co.	Shareholding Co.
Private Domestic Ownership (%)*	91.2	91.3	90.2
Private Foreign Ownership (%)*	7.2	6.2	7.5
Government/State Ownership (%)*	0.5	1.2	0.5
% of Firms with Female Participation in Ownership	40.8	36.7	39.1
% of Firms with Female in Top Management Position	19.8	19.1	22.7
Experience of the Top Manager (Years)	18.9	16.1	17.1
Average Number of Temporary Workers	23.6	5.7	3.4
Average Number of Permanent, Full-Time Workers	39.3	44.0	37.3
% of Full-Time Female Workers	42.8	38.7	40.5

Source: Enterprise Surveys.

Over three-quarters of all Georgian firms are privately held limited liability companies; this legal form is also the most common in other ECA and EU-10 countries (table 2). Although only 9 percent of all firms are publicly listed, 29 percent of large firms, 15 percent of medium-size firms, and 2 percent of small firms are publicly listed. Sole proprietorships are much more common among small firms, with 15 percent of small firms registered as sole proprietorships.

While 41 percent of firms have at least one female owner, in only 20 percent of firms is the top manager female (figure 3). The percentage of full-time female workers is substantially higher in firms with female participation in ownership. In such firms, nearly 60 percent of workers are female, whereas firms without female participation in ownership have only about 31 percent female workers.

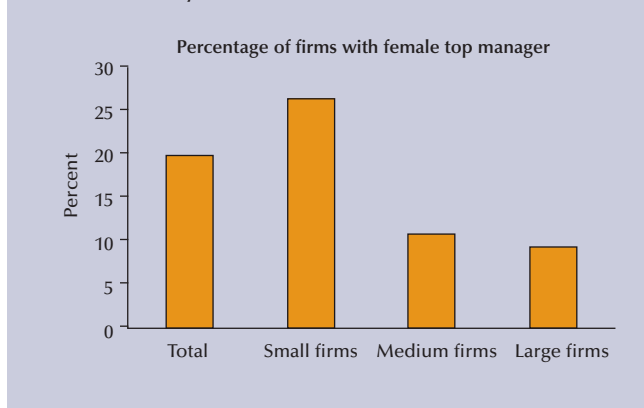
How Do Businesses Operate in Georgia?

Bank financing is not the norm in Georgia. The majority of investment in the average Georgian firm is financed through internal funds, while a quarter of investment is financed through bank loans (table 3). The vast majority of firms have a checking or savings account. When Georgian firms

finance investment through bank loans, collateral is needed 87 percent of the time. The average value of collateral used as a percentage of the loan is the second highest figure in the entire ECA region. Collateral equal to 100 percent of the loan amount or more was required for 62 percent of firms that financed investment through bank loans. Manufacturing firms need particularly high levels of collateral in order to finance their investment through bank loans (figure 4).

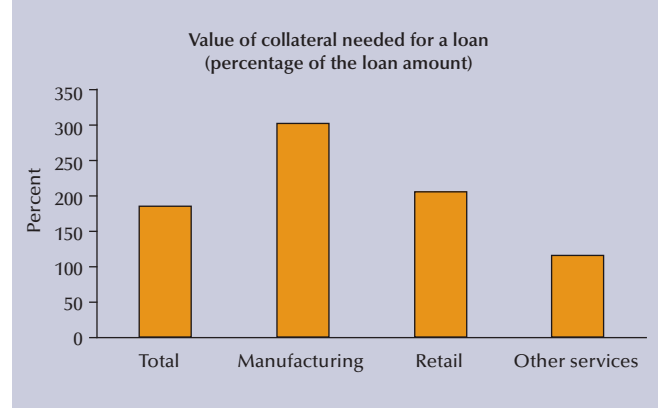
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Figure 3 More Women-Run Small Firms Than Any Other Firm Size



Source: Enterprise Surveys.

Figure 4 Manufacturing Firms Need More Collateral to Get a Bank Loan



Source: Enterprise Surveys.

Table 3 Choices by the “Average Firm” in Georgia 2008

	Georgia	ECA†	EU-10‡
Internal Finance for Investment (%)	62.4	62.2	62.3
Bank Finance for Investment (%)	26.9	23.8	26.7
Value of Collateral Needed for a Loan (% of the Loan Amount)	185.1	132.8	124.6
Loans Requiring Collateral (%)	87.3	81.1	74.3
% of Firms with a Checking or Savings Account	90.8	88.9	85.2
% of Exporter Firms	10.0	21.8	28.3
Domestic Sales (% of Sales)	96.4	91.0	88.6
Sales Exported Directly (% Sales)	3.4	7.0	9.2
Sales Exported Indirectly (% Sales)	0.2	2.0	2.2
Sales That Are Prepaid (%)	16.4	22.9	10.9
Sales Sold on Credit (%)	18.3	49.4	66.5
% of Firms with Internationally Recognized Quality Certification	16.0	19.9	25.6
% of Firms with Annual Financial Statement Reviewed by External Auditor	47.5	37.9	38.7
Capacity Utilization (%)	49.7	73.7	81.3
% of Firms Using Their Own Web Site	30.7	48.5	63.4
% of Firms Using Email to Communicate with Clients/Suppliers	40.5	73.2	88.5

Source: Enterprise Surveys.

Georgian firms are not very active in foreign trade. About 10 percent of firms export some of their output, which is well below the ECA average of 23 percent. Only 6 percent of firms export at least 2 percent of their output. However, 36 percent of large firms and 19 percent of medium firms export, while only 1 percent of small firms export.

Georgian firms operate below their potential both in terms of technology use and in terms of resource use. Average capacity utilization in Georgia is 50 percent, which is the lowest value for all of ECA (table 1). Only 18 percent of firms have a capacity utilization of 80 percent or higher. Georgia also appears to lag behind the rest of ECA in several technological areas. Only 31 percent of firms have their own Web site, and 41 percent of firms use email to communicate with clients or suppliers. Both of these figures are well below ECA averages. Firms located in Tbilisi appear to have bet-

ter access to technology—44 percent of firms in Tbilisi have their own Web site and 55 percent of firms in Tbilisi use email to communicate with clients or suppliers.

No Georgian firms reported that gifts were necessary to secure government contracts.

What Constrains Firms in Georgia?

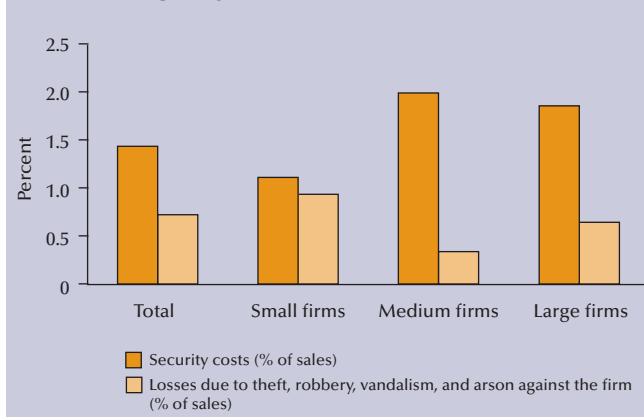
Georgian firms appear to be much less burdened by government regulation than firms in other ECA countries. One example of a relatively unconstrained business climate is the average number of visits or required meetings with tax officials in a year, which is only 0.6 in Georgia, the fourth lowest figure in ECA.

Only Slovenia, Estonia, and Poland have fewer visits or required meetings.

An even more revealing indicator of the flexible business climate in Georgia is the limited amount of time spent by firms dealing with government bureaucracy. Senior management spends 2 percent of its time on average dealing with the requirements of government regulation, which is the lowest figure in all of ECA (figure 1). Ninety-two percent of firms report spending less than 10 percent of their time dealing with the requirements of government regulation.

These results are not surprising, given that Georgia was ranked highest in the region in terms of the ease of doing business in the *Doing Business 2009* report. The 2008-09 Global Competitiveness Report (GCR) published by the World Economic Forum lends further support. In this index, Georgia was ranked sixth in the world and first in ECA in terms of ease of complying with administrative requirements.

Georgian firms also face less corruption than do firms in other ECA countries. The Incidence of Graft Index, which

Figure 5 All Sizes of Firms Are Affected by Crime

Source: Enterprise Surveys.

Table 4 Constraints on the “Average Firm” in Georgia 2008

	Georgia	ECA†	EU-10‡
Number of Power Outages in a Typical Month	3.3	5.8	2.5
Senior Management Time Spent in Dealing with Requirements of Government Regulation (%)	2.1	10.6	9.5
Average Number of Visits or Required Meetings with Tax Officials	0.6	1.7	1.1
% of Firms Expected to Pay Informal Payment to Public Officials (to Get Things Done)	4.1	16.8	7.4
Incidence of Graft Index**	5.1	9.9	4.7
Losses Due to Theft, Robbery, Vandalism, and Arson against the Firm (% of Sales)	0.7	0.5	0.4
% of Firms Paying for Security	65.0	57.7	62.0

Source: Enterprise Surveys.

is an indicator of the importance of bribery in dealing with government officials, is below the ECA average. Only 4 percent of Georgian firms are expected to make informal payments “to get things done”, which is the fourth lowest number in the ECA region. Furthermore, no Georgian firms reported that gifts were necessary to secure government contracts.

Security is a major problem in Georgia. The average Georgian firm experiences losses due to theft, robbery, vandalism, and arson that are equivalent to 0.7 percent of sales. This is the fourth highest value in all of ECA. Only firms in Russia, Estonia, and Kazakhstan report higher values. These losses due to crime occur despite the fact that 65 percent of Georgian firms pay for security, which is a higher percentage than the regional average. It is interesting to note that crime and security affect all firms independently of size, sector, or location (figure 5).

One measure of the quality of the infrastructure, the number of power outages per month, puts Georgia in the middle of the 29 ECA countries. This result is consistent with the results of the 2008-09 Global Competitiveness Report, in which Georgia is ranked 13th out of the 26 ECA countries that are surveyed. Firms in Tbilisi report only 2.8 power outages per month, compared to 3.3 for the country as a whole.

How Has the Business Environment Changed over the Past Three Years?

The Enterprise Surveys data provide the ability to monitor business environment progress over different rounds of surveys. In Georgia, of the 373 firms surveyed in 2008, 68 were also surveyed in 2005.⁵ Since the same firms are interviewed over time, this subset of data is more appropriate to evaluate the evolution of the business environment and the impact of business environment reforms than the full datasets for both years. The use of the full datasets would introduce

effects that are the result of variations in the sample composition over the two years.⁶ Therefore, the following analysis refers only to those firms that were interviewed in both rounds of surveys.

Between 2005 and 2008, Georgian firms surveyed in both rounds of the Enterprise Survey increased their number of permanent workers by an average of 23, from 61 to 84. These increases in employment were largely concentrated among large firms, which grew from an average of 256 to 369 permanent workers. These increases may be associated with two major labor law reforms that occurred during this period that were aimed at increasing labor market flexibility, as reported in *Doing Business 2006* and *2007*. However, average capacity utilization in manufacturing has fallen over time, dropping from 67 percent to 50 percent. As only 19 firms provided information on capacity utilization in both years, this result may not be representative of the whole economy.

The Enterprise Survey data show that, for the panel sample of firms, the average number of visits or required meetings with tax officials per year fell significantly from

Georgian firms surveyed in both rounds of the Enterprise Survey increased their number of permanent workers by an average of 23.

Figure 6 Fewer Interactions with Tax Officials after the Tax Reform



Source: Enterprise Surveys.

8.0 in 2005 to only 0.4 in 2008 (figure 6). This result can be related to a significant tax reform that went into effect in Georgia at the start of 2005 and is described in the *Doing Business 2006* report: the new tax code reduced the number of categories of taxes from 21 to 9 and also lowered tax rates.

Using new data from the Enterprise Surveys, we present evidence that firms are experiencing a more business-friendly regulatory environment. Georgia stands out in the region in that compliance with business regulations, including taxes, does not appear to be particularly burdensome. However, the business environment goes beyond regulation and there is room for improvement in other areas. For instance, loans to Georgian firms require extremely high levels of collateral. Additionally, internet usage by businesses is quite low, as are capacity utilization and export rates. Policy makers may wish to focus future reform efforts in these areas.

Notes

1. The Enterprise Surveys, when implemented in Eastern Europe and Central Asia countries, are also known as Business Environment and Enterprise Performance Surveys (BEEPS) and in this region are conducted jointly by the World Bank and the European Bank for Reconstruction and Development.

2. This figure presents the unweighted distributions by size, sector, and location of the firms interviewed without any inferences to the whole economy.

3. Over 99 percent of the 2008 data was collected prior to Russia's invasion of Georgia's South Ossetia province in August 2008.

4. The term "Average Firm" is used to convey the average firm characteristics from the Georgia 2008 Enterprise Survey. The sample of firms interviewed is representative of the manufacturing and services sectors of the economy. For more information on the survey methodology please consult <http://www.enterprisesurveys.org/Methodology/>.

5. The information collected in 2005 refers to the characteristics of the firm at the moment of the survey or to fiscal year 2004.

6. The firms surveyed in both years may not be representative of the Georgia's private nonagricultural economy since these are a subset of the full sample. Firms with fewer than five employees may be included among the firms surveyed in both years. The analysis presented is purely descriptive and does not aim at establishing causality between reforms and their intended effects.

† ECA includes Albania 2009, Armenia 2009, Azerbaijan 2009, Belarus 2008, Bosnia and Herzegovina 2009, Bulgaria 2009, Croatia 2009, Czech Republic 2009, Estonia 2009, Georgia 2008, Hungary 2009, Kazakhstan 2009, The Republic of Kosovo 2009, Kyrgyz Republic 2009, Latvia 2009, Lithuania 2009, FYR Macedonia 2009, Moldova 2009, Montenegro 2009, Poland 2009, Romania 2009, Russian Federation 2009, Serbia 2009, Slovak Republic 2009, Slovenia 2009, Tajikistan 2008, Turkey 2008, Ukraine 2008, and Uzbekistan 2008.

‡ EU-10 includes 2009 data from Bulgaria, Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Romania, Slovak Republic, and Slovenia.

* The ownership variables represent the average ownership composition within a firm. These variables do not represent the ownership composition across firms.

** Incidence of Graft Index is the proportion of instances in which firms were either expected or requested to pay a gift or informal payment over the number of total solicitations for public services, licenses or permits for that country. The Graft Index is defined in Gonzalez, Alvaro S., Ernesto Lopez-Cordova, J., and E. Valladares, Elio, *The Incidence of Graft on Developing-Country Firms*. World Bank Policy Research Working Paper Series, 2007.

The Enterprise Surveys measure the business environment in over 100 countries in the world. A standardized questionnaire, universe under study, and implementation methodology is used to make sure information is comparable across countries and time. The full data and documentation explaining the methodology are available at www.enterprisesurveys.org.

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