



**POVERTY REDUCTION AND ECONOMIC  
GROWTH PROGRAM OF GEORGIA**

**Intermediary Document**

**Government's Statement**

**Tbilisi, November 2000**

# Intermediary Document of Poverty Reduction and Economic Growth Program in Georgia

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# **Poverty Reduction And Economic Growth Program Of Georgia**

## **Interim Document**

### **G o v e r n m e n t ' s   S t a t e m e n t**

#### **Introduction**

1. The Government of Georgia, with support of the International Organizations and society at large, is preparing the Poverty Reduction and Economic Growth Program of Georgia, the main goals of which are the elimination of poverty, support to economic growth, improvement of social conditions, raising the living standards of the population and ensuring the participation of poor citizens in the country's development process.

2. As a result of the reforms carried out by the President and the Government of Georgia in 1994-1997, significant economic growth and sharp reduction of inflation were shortly achieved. The ground was laid for the development of democratic institutions and civil society. Fundamental reform of health system was conducted and judicial reform has been launched. But the global financial crisis of 1998 and the unfavourable natural conditions (severe droughts in 1998 and 2000 in Georgia) negatively influenced our country's fragile economy and clearly revealed systemic problems. This year showed a dramatic decline in economic growth since the reforms have been launched, causing a reduction in mobilized budgetary resources. This was caused primarily due to the institutional weakness of the appropriate agencies, the large-scale shadow economy and corruption. It is necessary to raise the efficiency of the budgetary process, to ensure transparency and the fair distribution of State resources. Unless these problems are solved, the rate of poverty in the country will be further increased, destructive socio-economic inequality will be further deepened and the economic growth of the country will be restrained, thus endangering the statehood, welfare and the future of its population.

3. The existing poverty rate in Georgia and its severity indicates the necessity to approach this problem from a long-term perspective, in order to fully and effectively address the issue. This process is closely related to the joint initiative of the World Bank and the IMF called "Highly Indebted Poor Countries" Initiative and the prospective future program of the IMF in Georgia (Poverty Reduction and Growth Facility). It should be also mentioned, that the main objectives of the Program are in full correspondence with the International Development Goals (IDGs). Coming from all the above-mentioned, the Government of Georgia, with the support of the society at large, has worked out this Interim Document of Poverty Reduction and Economic Growth Program of Georgia, the timetable for drafting the final Program and the plan for monitoring the actual implementation of the agreed goals and actions.

4. The indicators presented in this Document are based on the concept that poverty is a comprehensive phenomena and the fight against it must have a complex nature.

5. The poverty rate existing in Georgia is expressed in different forms and there are many reasons causing it. The most widely spread form is the inadequate level of population's income to satisfy its minimal requirements.

6. During the past several years, poverty studies have been intensified and significant progress has been achieved, which enabled us to use internationally accepted definitions and objective means for assessing the current poverty rate in the country.

#### **Chapter I**

##### **1. DEFINITION OF POVERTY IN GEORGIA**

###### **1.1. Description of Poverty Rate**

7. The first years of Georgia's independence proved to be extremely difficult. After the disintegration of the Soviet Union, the traditional economic relations among the Member Republics were ruined, yielding a tremendous decline in economic activity. The situation deteriorated further due to the civil war in 1992,

hyperinflation of 1993-94, and Abkhazian and South Osetian conflicts, resulting in a migration of refugees both inside and outside the country. All these events led the population to the edge of extreme poverty.

**8.** The economic reforms and stabilization program implemented in Georgia in 1994-1997 significantly improved the level of country's development and made it possible to establish order in the society. These factors permitted certain reduction of the poverty rate in specific regions, primarily in cities and suburbs. Unfortunately, in recent years one can observe the growth of the poverty rate countrywide, which is caused by negative events that took place since 1998.

**9.** The share of the Georgian population, whose consumption is below the poverty line, reached 60% in 1999 (in contrast to 44.4% in 1997). It means that more than 2.5 million of Georgian citizens consume less than 2 USD per day. Of these citizens, most of them are living in extreme poverty. Out of this number, approximately 20% are chronic poor, while the material situation of the remaining 80% is unstable over the year. The constant inability to execute the State Budget since 1998 caused delays in paying salaries, pensions and IDP allowances, resulting in the accumulation of significant arrears within the Budget, which, according to the August 2000 data, constitute 3.25% of the GDP.

**10.** An increasing tendency is also observed in the relative indicators of poverty (60% of median consumption versus 40%), consequently 22.7% versus 9.7% in 1997, and 28.6% versus 12% in 1999. The poverty depth indicator has also been increased. This indicator measures the average distance by which the poor are away from the poverty line. If in 1997 this indicator in contrast to the minimum wage was 16.1 %, in 1999 it reached 25%.

**11.** The socio-economic inequality among the population has sharply increased. The inequality rate based on income distribution – "Gini Coefficient" – in Georgia is 0.53, which is just 0.3 less than the same index of 1997. But it should be noted here, that the inequality rate is measured much better by means of Gini Coefficient based on the consumption (due to the large-scale shadow economy, the factual difference between the cash income and the actual consumption is very high), which in 1999 constituted 0.40, whereas the same index of 1997 was 0.36. For comparison, the Gini Coefficient in Georgia is better than that of certain Latin American countries (which are known to be socially unequal countries), but is much worse than the figures of the Central European countries in transition.

**12.** In August 2000, according to the average prices in Georgian cities, the minimum wage for a working-able person reached 112.2 GEL, for an average consumer – 98.5 GEL, and for an average family – 195.2 GEL. By the end of the first half of 2000, in various sectors of economy the average monthly salary constituted 72 GEL, which is just 64.2% of the minimum wage for a man with the working capacity. It should be also noted here, that during the past several years the minimum wage has a tendency to increase, whereas the actual average salary remains unchanged.

**13.** The poverty rate is further aggravated by a high level of unemployment. According to data from the State Department of Statistics (SDS), the unemployment rate in Georgia reached 12.6% in September 2000. The number of people registered in the unemployment centers reached 116,900, which is 13.8% higher than the same number of the previous year. The official statistical data does not reflect the actual reality existing on the labour market of Georgia. Among the people who have job places, 55% are so-called "self-employed" (for instance rural population having 1 hectare or bigger piece of land). Besides, a significant portion of the unemployed population does not consider it necessary to register in the unemployment centers, because the social protection for unemployed is extremely low and there is practically no hope that registration will assist job seeking. Salaries in the public sector are absolutely inadequate, and, moreover, the payment of these salaries is not done on a regular basis. The majority of employed are in the informal sector of economy, where the productivity and remuneration is very low and there are no social benefits or guarantees.

## **1.2. Social Sector**

**14.** There are two important indicators for measuring poverty in Georgia, namely – health care and education availability for the low-income families. During 1990-1995, the State expenditures in mentioned sectors decreased by 90-95%, if compared with the Soviet period. The material and technical basis deteriorated and the majority of buildings require considerable repairs.

**15.** The results of the crisis developed in 1998 had the biggest negative impact on the health care system. In 1999, expenditures on health care constituted only 0.9% of the GDP, and the State financing per capita fell to 7 USD (according to the World Health Organization criteria, it is not possible for the health care system to

function properly without at least 60 USD financing). Due to the scarce resources, the Government is able to finance only 30% of direct costs, while the patient himself pays the remaining 70%. This is a heavy burden for the poor families. The State financing of health care system includes only limited resources aimed towards the preventive measures. Due to the inability of the bigger part of the population to use the health care system, along with the increase of chronic diseases familiar to the developed countries, the increase of illnesses spread in developing countries is observed; in particular: tuberculosis, hepatitis, AIDS, sexually transmitted diseases and other socially dangerous infections, as well as the sharp increase of drug users.

*16.* The Government has been trying to solve the problems existing in the health care system by means of reforms. In 1995, the health care reforms were launched with the support of the World Bank Health Care Rehabilitation Project. The future perspective of the health care system is deemed to be the introduction of the social insurance model. State financing for the health care programs is provided by the State Medical Insurance Company, which mobilizes its resources through the obligatory insurance deposits charged to the labour remuneration funds of different enterprises and organizations, as well as through the subsidies from the Central Budget. In order to finance this sector, the State tries to allocate not less than 7% of the total budgetary resources into the health care system. It is also envisaged to restructure existing hospitals, to optimize the number of the personnel involved in the sector, and to arrange attestations in order to raise the qualification of the staff.

*17.* The education sector is also in a disastrous condition. Among the biggest problems, the absolutely inadequate level of State financing and the poor level of primary and secondary education must be mentioned. The State financing for education sector in 1999 constituted only 122.2 million GEL, which is 2.2% of the GDP. Despite the fact that the primary education till 9<sup>th</sup> grade is free of charge, parents are forced to carry out unofficial expenditures, such as, for instance, heating of the classrooms during the winter period, making cosmetic repairs of the classrooms, etc. Expensive textbooks are yet another burden for the poor families; due to this fact there is a dramatic decline in the attendance rate of the students in primary and secondary schools. Another problematic issue is to optimize the number of schools and teachers. It is practically impossible to maintain an appropriate level of material and technical facilities of the schools due to the insufficient State funding.

*18.* According to data provided by the State Department of Statistics, the level of education in Georgia is quite high. The number of illiterate population is less than 1 percent. The number of people with higher education is more than 25 percent. If we take into account the rule that there is a universally acknowledged link between education and welfare, existing poverty rate in Georgia points that the high level of education among the population and its desire to get educated are considered to be of great value. If raising the quality of education will become one of the priorities of the State and its society, the low-quality level can be improved.

*19.* The establishment of a system of private tutors reflects the low level of primary and secondary education, which, often times, is not enough to enroll into the higher education. This has an additional negative impact on the poorer parts of the society that are unable to cover the unofficial costs.

### **1.3. Development of Human Resources and the Human Development Index**

*20.* The development of human resources, which represents the process of increasing the number of options for a person through broadening the capacity and improving the skills of a human being, is the guarantee for rapid economic growth and, consequently, one of the primary aspects for poverty reduction.

*21.* According to UNDP data of 2000, the Human Development Index (HDI) of Georgia (which is comprised of the indicators related to the life expectancy, total number of students in the education system, and the GDP per capita) is 0.762, and in the world classification Georgia has 70<sup>th</sup> position out of 174 countries (it has advanced by 15 places if compared with the previous year HDI). Georgia is in the group of the countries with medium development level (0.500 – 0.799)

*22.* If we compare the HDI's of the neighbouring counties, only the Russian Federation is ahead of Georgia, but it should also be mentioned here that there are differences between the quantitative and qualitative indicators of the HDI's comprising parts (which are mentioned in the previous paragraph). In case of successful implementation of the Poverty Reduction and Economic Growth Program in Georgia, the positive results will certainly be reflected on the Human Development Index as well.

## 1.4. Infrastructure

### *a) Link between the Infrastructure Development and the Poverty Reduction*

23. The existing social-economic problems in Georgia and the low standard of living of the population are closely related to the insufficient effectiveness of the economy. The vast majority of the population is employed in the informal sector of the economy, where labour efficiency and social guarantees are extremely low. In the beginning of the year 2000, the share of the shadow economy in the GDP was estimated at 26-27 percent. In addition, this figure is significantly higher in some branches of the economy, such as, for instance, trade (68%), transport and communications (50%), industry (40%). The informal sector prevents the development of small and medium businesses in the formal branch of economy. Due to this fact, the State Budget is lacking a significant amount of revenues, which makes the Government unable to provide adequate social protection.

24. One of the most important factors for development of the economy is the effective sectorial structure. Therefore, one of the major goals of the Government is to support the development of optimal sectorial infrastructure, which will be efficient and market-oriented. Besides, in order to achieve poverty reduction in relatively short period of time after the necessary development of infrastructure takes place, the following measures should be undertaken: 1) to promote those priority branches, which are able to produce significant additional revenues; 2) to legalize the shadow economy, thus promoting efficient mechanisms of income distribution received from the private sector.

25. Let us discuss certain separate branches of the Georgian economy:

### *b) Energy Sector*

26. There is a difficult situation in the energy sector. After the collapse of the Soviet Union, Georgia lost cheap energy resources supplied under the centralized economy. This event has caused a number of problems in the energy sector that are a heavy burden on the population, enterprises and other businesses. There are frequent interruptions in power supply, hampering the normal development of enterprises and lowering the living conditions of the population.

27. The reform of the energy sector is an integral part of the reforms implemented in Georgia. The sector is undergoing a restructuring process aimed at attracting investments through the process of privatization. This is supported by the World Bank Energy Sector Adjustment Credit (ESAC). As a result of this restructuring, regulatory functions has been separated from commercial activities, monopoly power has been maximally regulated and a competitive environment has been created. The independent Wholesale Electricity Market and National Energy Regulatory Commission were established. Certain measures were carried out to improve the tariff policy on electricity and gas.

28. Existing energy tariffs are a heavy burden for poor families. Since 1997, the energy tariff has increased by 2.4 times, and by September 1, 2000 the price for 1 KW/h constituted 9.8 Tetri in Tbilisi, and 8.3 Tetri for the rest of Georgia. According to the data of the SDS, the average monthly expenditure for electricity consumption for one family reached 15.5 GEL in the first half of 2000, which is 21.5% of the average monthly salary in the country.

29. It should be noted that until recently the Government was using the energy sector as means for providing social protection to the population. For unlimited provision of electrical energy allowances were adopted for 2 categories of the population: 1) pensioners with special status and IDPs (100% allowance); and 2) certain types of civil servants (50% allowance). The costs for electricity used by the above-mentioned categories of citizens were covered by the State Budget. This approach proved to be inefficient; as a consequence, the Government gradually abandoned the system of energy allowances and introduced the system of targeted budgetary support to the poorest parts of the population.

30. The privatization process of some distribution companies has been successfully accomplished; substantial amounts of foreign investment were attracted and a significant improvement of energy distribution has been achieved. The owner of one of the biggest distribution companies of Georgia "Telasi" became a US company AES, due to which significant investments were attracted and the revenues from the usage of electricity increased.

31. Despite the actions implemented, the financial situation of the sector has not improved. In recent years immense debts were accumulated (approximately 550 million USD) as a result of low collections, inefficient

management and corruption dominating in the sector. However, the problem can be solved only through a continued and more enhanced reform process. Energy generation sector is in fact in the worst shape, due to which there are frequent blackouts within the whole country.

### ***c) Transport***

32. In contrast to other sectors, the development of the transport sector of Georgia is relatively stable. Certain improvements were achieved in this sector in 1999. According to the preliminary data of the year 2000, in the period from January through July, the volume of the cargo transported by all kinds of general transportation facilities constituted 16.8 million tones, which exceeds the same indicator from the previous year by 22.8%. The relatively stronger performance of the transport sector indicates the favourable geopolitical situation of the country, which serves as a transport corridor for Eurasia. The project of constructing the Baku-Supsa oil pipeline has been already implemented and, according to the 7 months' data from this year, 2.4 million tones of crude oil has been shipped from the Supsa Terminal. It should be mentioned, that construction of a bigger pipeline connecting Baku-Tbilisi-Ceyhan is also projected, the capacity of which according to the project estimates is going to be 50 million tones per year. The transit function of Georgia is not limited only to oil transportation. It is absolutely necessary for the country to have modern motorways in accordance to the international standards. For this purpose, the President of Georgia issued a Decree in 1996, by which the Presidential Program for Rehabilitation and Modernization of the Roads was adopted. The implementation of this Program was declared to be a high priority for the economic development of Georgia.

33. In recent years, the indicator of the number of passengers transported by the public transportation facilities has increased. In the first 7 months of this year this number has increased by 6.7% compared to the same period of the previous year. This is caused primarily by the improvement of service level in this sector. In the same period, the city electric transportation usage (which is used mostly by the poorer parts of the population because of the cheap tariffs) has also increased (84.6 million people) by 16.5% compared to the previous year figures. Despite the fact that the number of passengers is constantly growing, transportation costs are a significant portion of average income, totaling 13 GEL during the 1<sup>st</sup> half of 2000 (according to the data provided by the SDS). During the winter period, due to the frequent electricity cuts, the population is forced to use more expensive means of transportation. There were State transportation allowances provided from the Budget to certain categories of the population, but again, as it was the case with the electricity allowances, this idea was gradually abandoned and substituted by the targeted budgetary support to the most vulnerable parts of the society (for instance, individual tickets for using the metro were purchased for the IDPs).

### ***d) Communications***

34. According to 1998 data the usage of communication facilities by the Georgian population (per each 1000 citizens, excluding organizations and other legal entities) is: – 115 telephone lines; 0.1 public phones; 11 cellular phones; 472 TVs; 0.15 Internet users. For the year 2000 the progress can be observed regarding the above mentioned statistical data, especially in the field of telephone communications: approximately 25 telephone lines per 100 citizens in urban areas, and 10 telephone lines in rural areas. The liberalization of the communication sector promoted competition in this field, due to which it became possible to achieve competitive prices and to provide free choice for the population as to which service to choose.

35. As for the Internet and data transmission, this branch is still in the process of development. However, the positive tendency in this respect should be also mentioned – in 1999, there were more than 6000 Internet users countrywide, and this number is constantly increasing.

### ***e) Water Supply and Sanitation***

36. Georgia is very well known for its huge water resources, but in recent years serious problems occurred in this sector as well. The regulation and management of water supply and sewage systems, as well as their normal functioning, include several aspects: 1) economy and management; 2) public health (epidemiology and sanitation); 3) environment protection; and 4) natural conditions.

37. The economic regulation and management of this field was conducted by the State and the local authorities. Ineffective management brought the sector into a disastrous condition. There was no control over the water supply tariffs. The water pipes and sewage systems were technically in a miserable condition, due to



which there were several occasions, when the population was exposed to health risks. There are problems regarding the unimpeded water supply in urban areas, and, in some cases, interruptions in the water supply last for several days, or even weeks.

38. During recent years, control over water quality has decreased, which negatively affects not only the population, but the environment condition as well. Control over the wastewater is not regulated, and this might result in massive infections of the citizens. The 2000 drought had tremendous negative impact on the agricultural sector and it denied the farmers practically the only subsistence means – the irrigation systems got completely deteriorated.

### ***f) Industrial Sector***

39. The current situation and the progress achieved in the industrial sector in 2000, if compared to the previous years, can be evaluated as positive.

40. The most important and positive aspect in this branch is the fact that practically all segments (21 out of 29) of the industrial sector are characterized with the growth during January-August of 2000. The growth of total industrial production reached 8.8% compared to the same period of the previous year.

41. Another positive trend is the increased activity of small businesses, the total number of which reached 2,296 organizations, by October 2000. The volume of the goods produced by small businesses accounts to 94.3 million GEL, which is 14.5% of the total industrial production. This figure has grown by 11,1% in comparison to the same period of 1999, while the growth of total sector is 8%.

42. As for the activities in different branches of industry, the growth can be observed in the areas such as: mining – 58.9%, processing industry – 19.0%, supply of electricity, gas and water – 7.2%. The difference between the growth rates in various branches is noteworthy. This applies particularly to the energy generation and its supply, which is characterized by the smallest rate of growth.

43. One of the most negative factors in the industrial sector is the volume of informal and shadow production, which reached 1,153.9 million GEL, or 177.6% of the officially produced goods (which is just 649.6 million GEL) in January-August of 2000. The above-mentioned fact points to the significant potential existing in the industrial sector of Georgia.

44. Another negative fact is unequal share of production among the industries – 43.8% (or 284.8 million GEL) is produced by only 52 organizations out of 2,713 industrial companies (598 of them, or 22%, do not operate at present). This indicates the low level of diversification within various industries. This circumstance endangers the whole sector, since it is very much dependent on each of the mentioned big industries: failure or success of any of such industries will have huge impact on the whole industrial sector.

45. If we take into account the ongoing privatization process and the reforms, which are currently implemented in the country, the fact that 53% of the total industrial production is produced by the State-owned enterprises is certainly unsatisfactory. If we also take into account the low level of diversification of the sector, an assumption can be made that the most important and productive enterprises are still in the hands of the State. This fact cannot promote either the development of the sector, or establishment and rapid development of market relations in the country.

## **1.5. Current Situation in the Agriculture Sector**

46. The development of the agricultural sector, deriving from its volume and the number of people employed in it, plays significant role in the economic growth of the country. Agriculture and agro-business appear to be the major source of income for the population. This fact itself plays major role in the elimination of poverty in rural areas of Georgia.

47. The liberalization of prices and the creation of a progressive environment for trade was one of the most important goals in the early stages of the country's reforms. In this respect, significant progress was quickly achieved in the agriculture sector. State interference in goods market of goods was totally eliminated, and a liberal trade regime was created. Georgia's accession to the WTO is also an important step forward towards further implementation of reforms.

48. Efficient measures were undertaken for privatization of State-owned assets in the agriculture sector, including the privatization of agricultural lands and agro-processing enterprises. The Land Reform in Georgia

started in 1992; it was followed by the Land Leasing Program (1996). The results of these two programs are the facts that 57% of agricultural land is now in the private ownership, and 27% is being leased from the State by private entrepreneurs. Privatization of State-owned enterprises is currently underway, as a result, 60% of the agro-processing industries are already in private hands.

49. Despite the fact that the majority of the agro-business enterprises are in the private sector already, this did not contribute to the significant growth of production volume. The reason is that the owners of those enterprises do not have the possibility to attract necessary capital, to develop modern systems of management, and to conquer new markets. The inability to fully use the existing export potential is also related to the above-mentioned problem. Foreign investments are deemed to be the major means for solving these issues, and, therefore, the creation of favourable investment climate is a crucial element to improve the situation.

50. Promotion and implementation of scientific achievements and training of farmers is an important measure to be undertaken in the agricultural sector. There are approximately 1 million small-scale farmers nowadays in Georgia. Practice has shown that their work would have been much more productive and environmental friendly, if there was more consultancy and education provided to them.

51. It is noteworthy, that the implementation of necessary reforms will foster economic growth in the agriculture sector, which is an essential prerequisite for alleviation of poverty.

## 1.6. Current Situation in the Environment Protection

52. The poverty rate and environmental protection are closely related to each other. Due to the lack of choice, the poor population has to live and work in a degraded environment. On the other hand, the poor cannot afford the best environmental protection practices, therefore the pressure on the living environment is increased and it is worsening. As a result, the poor receive the worst part of environment and natural resources, which they use in a very inefficient way (for instance: uncontrollable disposal of garbage in populated areas, usage of inefficient energy devices, usage of timber instead of commercial fuel, which damages forestry, etc.).

53. Escaping from this vicious circle requires implementation of multi-sectoral and complex measures from the Government. Correct planning of these measures and activities is essential to avoid the opposite effect.

54. In recent years, the relationship between the environmental protection and poverty entered a new and rather dangerous phase. The following list is sufficient to give an example:

- Drought in 2000 brought 450 million GEL loss to agriculture of the East Georgian regions (predominantly small entrepreneurs). The scale of this loss increased dramatically due to the lack of local resources, which could have been used for preventive measures.

- After several years characterized by a shortage of rainfall, it is possible that the ordinary characteristics of rivers might alter, which will have a negative influence on the irrigation and other water-based systems, especially for the poor. In a long-term perspective, this situation might get even worse, if we take into account climatic change.

- In several regions of the country one can observe the creation of desertified land caused primarily by the above-mentioned reasons.

- The inability of the poor to use modern energy sources increases the consumption of timber in rural (and sometimes also in urban) areas; this creates an unsustainable environment in the forestry.

- The lack of financing for the water supply and sewage systems in the urban areas on the one hand, and the current tariff system stimulating the inefficient usage of these facilities on the other hand, brings this sector into a hazardous condition.

- A similar situation exists regarding the quality of automobile fuel. Due to the inefficient quality control system, the poor consume low quality fuel, which, in the long run, is too costly not only for the actual consumers, but to the whole society as well.

55. This list is certainly incomplete. In spite of certain progress achieved in drafting appropriate legislation and working out environmental policy, the implementation of measures directed to the improvement of environment protection encounters problems related to institutional, legislative and especially financial difficulties.

## Chapter II

### 2. POVERTY, MACROECONOMIC SITUATION, STRUCTURAL ADJUSTMENTS AND INVESTMENT ENVIRONMENT

#### 2.1. Macroeconomic Situation

56. In the beginning of 1994, after the implementation of the anti-crisis program, which was worked out in close consultation with the international financial organizations, macroeconomic stability was shortly achieved. A whole series of important measures have been undertaken to achieve this stability, in particular: the National Bank of Georgia (NBG) established strict control over the issuance of credits to the Government and the commercial banks, as well as over the domestic and international reserves of the NBG; the State Budgetary accounts of the Ministry of Finance (MoF) were transferred to the NBG, and the control over the international reserves, which before used to be the competence of the MoF, was transferred to the NBG as mentioned above. In order for the commercial banking system to become credible and strong, and in order to protect the interests of bank clients, the privatization of the State-owned banks was launched; certification and licensing rules became stricter; actions against problematic banks were carried out through either liquidation, or mergers, etc. The NBG made a request to the commercial banks to increase their authorized capital to at least 5 million GEL before the end of 2000.

57. Laws were adopted which support the improvement of the financial-budgetary process in the country. Tax legislation was developed. In order for the revenues and expenditures of the country to become centralized, State Treasury Department was established. Despite the mentioned positive trends, the conformable effectiveness of budgetary process, its transparency and fair distribution of recourses has not been achieved. Coming from the above-mentioned, achievement of desirable results in the short-term period requires implementation of more efficient measures.

58. Due to the implementation of the above-mentioned economic stabilization measures, the average annual GDP growth rate constituted 10% in 1995-1997. Hyperinflation was overcome; if in 1993 the average inflation rate was more than 13,000%, in 1997 the same indicator constituted only 7.3%. At the same time, no significant progress has been achieved in strengthening of the State finances. The share of the budgetary tax revenues was low, if compared as a percentage of the GDP.

59. Starting from 1998, budgetary problems emerged, which were aggravated by financial crisis in Russia – Georgia's major trading partner – resulting in a worsening of the trade balance (within the country). All these events caused a significant worsening of macroeconomic and financial situation in the country. GDP growth has been reduced, and in 1998 it constituted only 2.9%, in comparison to 11% in 1997. The monthly inflation rate in December of the same year reached 12.1%, while according to 11 months' data, the average monthly inflation rate was only 0,1%. Taking into consideration the above mentioned, the average annual inflation rate for 1998 was determined by 10.1%, whereas the same indicator in 1997 was 7.3%, as mentioned above.

60. Due to the worsening of the balance of payments, domestic financial markets were short of foreign exchange supplies. In December 1998, the National Bank stopped its intervention on the financial market.

61. During 1999, the Government of Georgia tried to reduce the outcomes of the crisis and to reestablish the macroeconomic stability in the country. During that period, the economic growth rate was 2.9%, while the inflation for the end of this period constituted 10,9%. In the year 2000, there was a positive tendency projected towards the growth of the GDP, but severe drought has significantly damaged the agricultural sector, resulting in the alteration of the GDP structure and hampering its growth. In other sectors of economy (except agriculture) the growth is expected to be 5%, thus bringing the total growth of the GDP 2000 to 1.2-1.5%, and the annual inflation rate is projected to be around 6-7%.

#### 2.2. Structural Reform Policies

62. Structural reform policies have been carried out in Georgia with the support of the World Bank. This process was supported by 3 Structural Adjustment Credits (SAC) of the World Bank.

63. The structural adjustment program included perfection of the existing legislation in order to improve business environment. The Parliament adopted the laws on "State procurement" and on "Licensing of business

activities”, which correspond to the international standards. Normative acts were adopted to simplify the registration procedure of entrepreneurial activities.

**64.** Important measures were implemented to develop the land market. The privatization of agricultural land, embraced the privatization of non-agricultural lands as well. Mechanisms for leasing the State-owned lands were elaborated. Appropriate laws and normative acts were adopted. The process of registration of land began with the support of international organizations and donor countries. Due to the land market development, tangible results are achieved in selling/buying and mortgaging the lands in order to receive credits from the banks.

**65.** Special attention must be paid to the privatization process, carried out within the framework of this program. After the small-scale privatization was conducted in 1993-1998, during which more than 12,800 objects of trade and service were sold, the privatization of bigger companies was launched. After amending the law on “Privatization of the State property”, it became possible to start privatization in energy, communication and transport sectors. Privatization of “Telasi” and 9<sup>th</sup> and 10<sup>th</sup> blocks of “Tbilsresi” was carried out. The work is currently underway to elaborate the strategies for privatizing energy distribution and energy generation branches, as well as communications sector and the seaport of Poti. Privatization of large industrial objects is also envisaged (under the SAC III conditionality 15 first class industries and 29 second class industries must be privatized), and at the same time, liquidation or restructuring of those industries, which are of no interest to the investors, will be carried out.

**66.** Alongside the above-mentioned 3 Structural Adjustment Credits received from the World Bank, which aim at global structural changes in the different branches of economy, 2 other projects (Georgian Social Investment Fund and Municipal Development and Decentralization Project) must be mentioned separately, since the prime objectives of these projects are directed towards reduction of poverty in Georgia. The implementation of these projects yielded some very positive results, which are described in the following sections.

#### ***a) Georgian Social Investment Fund (GSIF)***

**67.** The Decree of the President of Georgia, dated August 16, 1996, established the Georgian Social Investments Fund (GSIF) in order to overcome the problems existing in the Georgian social sector. This represents a joint initiative of the Georgian Government, the World Bank and the USAID.

**68.** The main objectives of the GSIF are:

- 1) Support for the rehabilitation of social infrastructure of Georgia by means of restoration of small-scale objects. This covers 3 fields, in particular: social, economic and environment protection;
- 2) Active participation of the local population in the process of object selection, rehabilitation, further exploitation and possession; support to the process of decentralization and development of ownership customs among the population;
- 3) Support to the development of private small businesses (especially in construction field) and reduction of unemployment rate (especially in the areas where the project is carried out);

**69.** The total cost of the project is 28.3 million USD, to which additional 5 million German Marks are added – a grant from the German Bank for Reconstruction (KFW). This grant is intended for the project titled “Employment program in Borjomi-Kharagauli National park zone”. International Fund of Agricultural Development (IFAD) is yet another donor of the GSIF, which provided a grant worth of 1 million USD, to implement development programs in highland regions.

**70.** Apart from that, the GSIF has signed cooperation agreements with several non-governmental organizations of the USA that are taking part in the tender announced by the USAID regarding the project called “Mobilization of local communities in Georgia”. This project aims at development of local communities in the eastern and western parts of Georgia and rehabilitation of infrastructure.

**71.** The positive and efficient work of the GSIF is reflected in the following figures: from June 5, 1998 till August 1, 2000, rehabilitation of 127 objects is completed, 54 objects are currently underway (total - 181 objects, out of which 68 schools, 63 supply of drinking water, 11 health care objects, 12 kindergartens, 8 culture clubs, 5 roads and other objects).

72. More than 1 million citizens are users of the GSIF services, and more than 10 thousand people were employed in construction activities.

73. GSIF's activity is based on the evaluation of the condition of social infrastructure and the poverty rate in different regions of Georgia that was conducted together with the World Bank. This very research was used to estimate the disbursement of Fund's resources in different regions, as well as the order of priority among the regions, where the GSIF started its activities. GSIF is planning to start its activity in South Ossetia, which is going to be one of the first international rehabilitation projects in the post-conflict zones of Georgia.

74. It must be noted that GSIF's ongoing project and its second stage, which is going to start after 2002, will be significant support to the Poverty Reduction and Economic Growth Program; thus, appropriate planning and efficient implementation of GSIF's future objectives have vital importance for Georgia.

### ***b) Municipal Development and Decentralization***

75. On September 15, 1997 the Government of Georgia and the International Development Association (IDA) signed the development credit agreement concerning the implementation of Municipal Development and Decentralization Project (MDDP). The main objectives of the project are: 1) to give the opportunity to the regions and cities participating in the project to define, make estimations, and find sources for financing of priority investments; 2) to provide the regions and cities participating in the project with the possibility to assess necessary loans and define terms of their repayment; 3) to create Municipal Development Fund (MDF), which will be a vital financial mechanism for promoting local investments; 4) to support the regions and cities participating in the project to improve the necessary legislation for achieving the above-mentioned objectives.

76. The Government of Georgia defined 12 municipalities (Ambrolauri, Akhalkikhe, Gori, Zugdidi, Tbilisi, Telavi, Ozurgeti, Rustavi, Poti, Batumi, Kutaisi, Kazbegi) that will participate in the MDDP.

77. For the implementation of the MDDP, the Government of Georgia, together with the World Bank, established two implementation agencies: the Coordination Center for Implementation of Municipal Programs (CCIMP) that will ensure the implementation of institutional part of the project, and the Municipal Development Fund (MDF), that is responsible for the implementation of the investment part of the project.

78. For the financing of the investment part of the project, the IDA provided 16 million US dollars.

79. The primary goal of the MDF is to mobilize funds from international financial institutions, donor agencies, central and local administration, and to make them available to the municipalities for investing into city infrastructure and service sector.

80. Nowadays the MDF completed following preparatory works: perfection of the investment project selection, evaluation and implementation mechanisms; elaboration of criteria for receiving loans for municipalities, and flexible mechanisms for their repayment. To provide maximum efficiency to investment projects, Rustavi, Poti, Gori and Telavi water-supply systems were studied and consequent detailed technical reports were prepared. Currently, foreign experts are making technical reports for 12 big projects. In the nearest future, the problems existing in Tbilisi electric transport sector will be studied and detailed technical reports will be prepared. Besides, the MDF started implementation of several investment projects. One of them is completed and two are at the completion stage. Up to today, investments totaling 1,040,000 USD have been disbursed. The MDF is currently planning to start new projects in the near future. The investments are determined in following sectors: water supply, health care, transport and roads. Coming from the specifics of the project, one of its major goals is to ensure successful investments in infrastructure sector of different cities of Georgia that will be oriented towards improvement of socio-economic situation, and to provide the Georgian population with the benefits achieved by the program.

### **2.3. Promotion and Support for Attracting Investments**

81. As a result of economic stability achieved in Georgia by means of ongoing economic reforms, potential investors express a growing interest in Georgia. Many normative acts were instituted to ensure protection of investors' property, free exchange into foreign currency, and unimpeded repatriation of profits abroad. In June 1995, the Law on Foreign Investments was adopted. This was a very liberal Law, granting many benefits to foreign investors. However, the above-mentioned Law was replaced by a new Law on Promotion and Guarantees of Investment Activities, which was passed by the Parliament in November 1996. The Law grants

no particular benefits to foreign investors, but it is notable for abolishing the old system of licensing requirement for investors (except for those types of activities that are enumerated in Article 9 of this Law, in particular: production of weapons; production of medicines; exploitation of natural resources and forestry; banking activity; insurance business; TV and radio broadcasting; etc.), ensuring unimpeded repatriation of capital and income, etc. It should be also mentioned that the 1996 Law is applied both to domestic and international investors, in comparison to the previous Law of 1995.

**82.** Besides subjective reasons existing in the country, there are some objective reasons, caused mainly by the unstable situation in the Caucasus that delay foreign investments. Georgia needs to make extra efforts in this direction to compensate for existing risks by creating more favorable conditions for investments.

**83.** With this in mind, by the Decree 87 of the President of Georgia dated March 30, 1997, the Foreign Investment Advisory Council (FIAC) was established under the President of Georgia. Due to intensive cooperation with international organizations, donor countries and foreign investors, more than 140 projects were prepared and presented for discussion to the Investment Council. Among the issues discussed were the projects of the World Bank, European Union, USA, Japanese and German Governments, UNDP, EBRD and private investment proposals.

**84.** Creation of the Foreign Investment Advisory Council has solved the problem of existence of a single coordinating body within the country, because FIAC is the only consultative body where all the issues related to mobilization and coordination of external resources are being discussed.

**85.** With the implementation of positive socio-economic reforms, it is expected that the investment activity will rise in the future. This will increase the volume of proposals concerning financing of different development programs, promote country's further economic development, generate additional sources of revenues to the State Budget, support the formation of new job places and reduce unemployment, improve infrastructure, and ensure bringing modern technology to various branches of industry.

## Chapter III

### 3. MAIN STRATEGIC DIRECTIONS OF THE POVERTY REDUCTION AND ECONOMIC GROWTH PROGRAM IN GEORGIA

#### 3.1 Main Directions in Social Sector

86. Reduction of poverty and elimination of extreme poverty in the country can be reached by:

87. Reducing the possibility of poverty risk (prevention). This can be achieved through: effective employment policy, establishment of an adequate system for education of competitive staff (reforms in professional and high education systems, training, establishment of continues educational system), issuance of universal household compensations for children that will enable these families to come out of the chronic poverty, etc.

88. Softening the influence of anticipated poverty risk. This can be achieved through establishment of different mechanisms of social insurance.

89. Special attention should be paid to the post-conflict zones, the existence of which creates unfavourable socio-economic condition in the whole country. Hence, elaboration and implementation of concrete large-scale rehabilitation projects and measures oriented towards revival of economic relations in these zones should become one of the major priorities.

90. In order to implement these objectives, the following measures must be undertaken:

- Establishment of an effective employment system, which means ensuring the training and re-training in order to have qualified and competitive personnel, conducting a balanced taxation and investment policy, defining effective mechanisms of wages. That will help us to generate new working places and to efficiently use the existing working places both in traditional and new branches, to promote family, small and medium-size business development, especially for the labour force with low competitiveness.

- The reform of education system means the improvement of secondary, professional-technical, higher and continuous education system that will serve for preparation of human recourses in accordance to the current and prospective labour market demands. More concrete measures to be undertaken in the education sphere will be elaborated in the final PREGP of Georgia.

- Social protection reform can be achieved through perfection of the pension system by means of reintroducing its collecting, distributing and insuring functions, defining and introducing alternative variants of multistage pension insurance mechanisms, which will be carried out on a step-by-step basis; Development of insurance system for unemployed, temporarily and constantly disabled people, as well as life insurance and socio-medical insurance systems. Development of social protection system means transformation towards family assistance principle. It is necessary to develop targeted cash and non-cash social protection mechanisms in order to cover as many highly unprotected individuals and families as possible.

- The Government of Georgia acknowledges the necessity to carry out social reforms, which is a long-term strategic objective of Georgia. It is essential to conduct step-by-step reform and to guarantee a transparent environment in the pension system; to draft appropriate legislation and improve existing normative acts (Laws on “Compulsory Social Insurance” and “State Pension System”, etc.); to ensure continuous payment of current pensions and gradual repayment of accumulated arrears by the end of 2003; to implement personification and to introduce identification cards by the year 2003. After implementation of the above-mentioned measures and mobilizing sufficient financial resources, to ensure step-by-step transfer towards insurance principles and differentiated pension system. Structural reorganization (introduction of automotive management system) should be conducted to achieve these goals. It is also necessary to improve bank service system and to introduce actual modeling and forecasting methods.

- It is necessary to improve IDP’s identification and personification mechanisms and to carry out measures towards their further perfection. Implementation of a self-sufficiency project and introduction of new approaches towards IDPs drafted by UNDP, UNHCR, UNOCHA, the World Bank, USAID and other international organizations and donor countries is also very important. It is essential to provide IDP’s with an effective social safety net and to continue further cooperation with the World Food Program to ensure full involvement of IDP’s in the “Food for Work” project.

- Reorganization of labour relation system means establishment of new labour relations answering to market economy requirements and development of adequate social safety net mechanisms for employees.
- Implementation of health care policy should be conducted according to the National Health Care Policy drafted and approved by the Government of Georgia in association with the World Health Organization. More concrete measures to be undertaken in the health care system will be elaborated in the final PREGP of Georgia.
- It is necessary to achieve a high level of human resource development and a significant increase of salaries due to effective personnel policy including training, attestation and establishment of competitive system of recruitment;
- There is a need for the formation of appropriate legislation and further perfection of the existing normative acts to support implementation of the above-mentioned reforms.

### **3.2. Main Directions of Fiscal Policy**

**91.** One of the major objectives of the Government will be the targeted reduction of the Budget deficit as a share of the GDP. By the year 2003, the budgetary deficit in relation to the GDP is projected to be 1.2%. Besides, while financing this deficit, an emphasis shall be placed on raising the share of State Treasury Bills. The State will proceed to provide debt servicing, and will not allow interruptions regarding the repayment of interest rates; to this extent, negotiations for debt restructuring will be continued. Restructuring of State external debts will allow the country to allocate the spared financial resources for the social needs of the population. Only highly effective State programs will be financed by external credits, thus the Government will say no to the non-concessional credits in the future.

**92.** The gradual reduction of the deficit will be accomplished through bringing the budgetary revenues and expenditures in full accordance to each other. The Government clearly understands that in order to achieve the growth of State revenues, along with other activities, it is important to improve tax policy and its administration. For this to be implemented, it is envisaged to undertake structural reforms in the State Customs and Tax Departments. Revision of the Tax Code is projected in order to revise the tax base and to optimize existing tax rates, and to improve the mechanisms of tax administration. Taxation policy will be worked out to promote attraction of investments and development of small businesses.

**93.** In order to achieve Budget consolidation, yet again special attention will be paid to bringing the budgetary revenues and expenditures in full accordance to each other. In order to reduce social tensions existing in the country, priority budgetary expenditures will be timely payment of salaries, pensions, allowances to IDPs and other secured Budget lines. The problem of recently accrued arrears will be considered. In this respect, the 2001 State Budget envisages 80 million GEL (which is 1.25% of the GDP). Repayment of these arrears will be carried out in accordance with a schedule to be approved beforehand. Improvement of State expenditures will be carried out systematically, i.e. distribution of State resources among the budgetary organizations will be based on timely financing of social expenditures, in order to avoid accumulation of new arrears in this sphere.

**94.** The work of the Treasury will be centralized to improve control over budgetary expenditures and to strengthen its management. The mechanisms for controlling liabilities and their accounting shall be worked out and implemented. It is also envisaged to carry out an audit of budgetary arrears, accrued by line Ministries, in order to determine unjust requests to be financed from the State Budget. Efficient methods and mechanisms for controlling the Budgetary expenditures and for their auditing will also be worked out.

### **3.3. Main Directions of Monetary Policy**

**95.** The National Bank of Georgia shall continue conducting moderately strict monetary policy: cash supply will be provided taking into account the economic growth, provision of credits to the Government by means of emission will be reduced to a minimum, and the growth of the reserve money will be achieved primarily by means of accumulating international assets of the Bank. At the same time, moderately strict monetary policy shall be implemented, resulting in the annual inflation rate of 4% by the year 2003, in order to maintain price stability.

**96.** Foreign exchange policy should be based on the floating exchange rate, which will provide balanced dynamics of GEL exchange rate in accordance to the inflows of the foreign exchange into the country, and will weaken the influence of external shocks on the real sectors.



97. Supplying the economy with adequate cash (broad money growth) should be implemented not by means of reserve money growth, but by channeling the cash existing outside the banking system (both GEL and foreign exchange) into this system, and by improving the quality of intermediation function of the banks, thus ensuring the growth of money multiplier.

98. Adequate conditions should be created to strengthen the credibility of the banks; for this purpose international accounting standards shall be widely introduced, and favorable conditions will be created to attract foreign banks to Georgia. To create a healthy and sustainable banking system, as well as to mobilize the savings of the population into the banking sector, the banking supervision shall become stricter, radical measures shall be undertaken towards problematic banks, and the condition of having minimal capital requirement shall be met by all means. Efforts must be also undertaken to improve the general level of management of the banks, to strengthen risk management and the usage of collateral. These measures will raise both the quantity and the quality of credit portfolios of the banks and will promote credit opportunities to small businesses. All the above-mentioned activities on the one hand, will stimulate attraction of money existing outside the banking system into this system, and to generate new credit facilities, and on the other hand, to reduce interest rates, and, as a result, to expand investment activities.

99. As for the development of financial markets, emphasis should be placed on reducing internal State debt, which will free up additional resources, will create a favorable background for reducing interest rates, and will broaden facilities for granting credits to the private sector.

### 3.4. Main Directions of Infrastructure Development

100. Among the *objective reasons* for difficulties in development of infrastructure and decrease of living standards are:

- Structural adjustments needed for transition to the market economy, as result - breakdown of economic relations established during the Soviet system and the collapse of industrial output;
- Reduction of gross supply, as a result of high crime rate and political instability in 1992-1994;
- Low competitiveness of local production, caused by increase of prices of energy and other industrial resources, by obsolete facilities and technologies, by inefficient management and labor administration, and by smuggling from post-conflict regions;
- The influence of the Russian crisis on local industry, as well as unfavorable climate conditions (severe droughts in the second part of 1998 and first part of 2000).

101. Among significant *subjective reasons* are:

- Insufficient level of investment promotion by the State;
- Weaknesses of structural policy, inefficient structure of production funds, problems in State property management and privatization;
- Unstable and incompletely regulated legislation;
- Orientation towards short-term fiscal goals of budgetary and taxation policy, caused by budgetary difficulties;
- Lack of a market mentality and inefficient management forms, lack of qualified staff both in public and private sectors;
- Unprotected local production against unjust competition in the consumer market;
- Shadow economy and corruption;

102. It is necessary to lay a foundation to rejuvenate social-economic spheres of the country and to promote economic growth during the short-term period (2001-2003).

#### **Ways to implement the program:**

103. Defined objectives can be carried out in two ways, in particular: general measures, which are applicable more or less to all the branches of infrastructure, and specific actions to be taken in concrete fields.

**104. a) General measures are:**

- Improvement of investment climate, promotion of foreign as well as local investments (improvement of taxation system, development of insurance and banking systems, creation of competitive environment, making the responsibilities for breaching the terms of contracts with investors more strict, promotion of leasing companies).
- Definition and implementation of an optimal strategy for privatization of property, which is still in the hands of the State.
- Acceleration of enterprise restructuring, perfection of existing production assets, making State property management more efficient, improvement of legislation and bankruptcy procedure;
- Promotion of small and medium businesses;
- Promotion of free competition, reinforcing supervision over the natural monopolies, perfection of mechanisms for defining State regulated tariffs;
- Promotion of social-economic development of regions by the Government, with maximum utilization of their capacities;
- Reduction of the shadow economy within various sectors of national economy, promotion of business legalization and decrease of illegal employment share.

**105. b) Specific actions in concrete fields** will be oriented towards restructuring of enterprises in different sectors of economy, accelerating their development, creating new job places and solving general social problems, such as:

**106. In the Industry Sector:**

- To promote manufacturing industries to become oriented towards use of local raw-materials, giving incentives to import-replacing industries (light and food industry, forestry, wood and furniture production, chemical and pharmaceutical production, mechanical engineering, manufacturing of construction materials, etc);
- To promote prospective industrial sectors oriented towards servicing TRACECA transport corridor;
- To encourage the introduction of modern technologies;
- To provide the population with the production of vitally important goods;
- To provide the restructuring of privatized enterprises and to promote the operation of promising enterprises.
- To improve State procurement mechanisms and to provide a rational distribution of State orders among different industries.

**107. In Transport Service and Communications Sectors:**

- To define full volume of cargo to be transited through the Europe-Caucasus-Asian Transport Corridor (TRACECA), to ensure its functioning in accordance to the international standards; coming from this objective, to define the basic directions of development of different branches of the transport sector (with corresponding infrastructure);
- To promote safer traffic and enhancing the volume of cargo passage in the railway sector; modernizing certain parts of the existing railway, as well as locomotives and carriages; bringing the communications to the international standards;
- To work out and implement a strategy for overcoming crisis in the maritime sector; to ensure the reflection of the activities carried out by the maritime sector in the economic indicators of the country;
- To accelerate rehabilitation and modernization of the roads and to bring them maximally close to the international standards;
- To carry out the privatization process in communications sector, to encourage healthy competitive environment in accordance to the recommendations worked out by international organizations;

- To promote modernization of obsolete and physically depreciated rural telephone networks, to equip the telecommunications sector with modern technology.

**108. In Fuel and Energy Sectors:**

- To attract investments in the sector of hydro-energy;
- To introduce a flexible system of tariffs, which will take into account seasonal and entrepreneurial interests regarding the consumption of energy and natural gas;
- To accelerate rehabilitation of the energy sector infrastructure, and to write off outdated energy equipment on the basis of agreements with owners of the privatized power facilities;
- To accelerate privatization process of the power facilities and natural gas processing objects, along with existing infrastructures;
- To promote development of untraditional power (in particular – usage of wind energy).

**109. In Construction Sector:**

- To improve legislation in correspondence with the demands of the market economy;
- To develop progressive industrial entities in the construction sector, and to promote competitiveness, demonopolization and decentralization of the construction industry;
- To modernize the construction industry and manufacturing of construction materials; to promote investments in this sector;
- To elaborate and implement flexible attitudes towards legalization of existing informal parts of the construction sector.

**110. In Housing and Communal Services:**

- To reform housing and communal services of Georgia and to provide improvement of the sewerage and water supply sanitary-technical conditions;
- To promote privatization and attraction of investments in this field;
- To perfect tariff policy.

**111. In the Tourism and Hotel Business Sectors:**

- To encourage and attract private investments, taking into account the servicing of the TRACECA Corridor;
- To introduce new progressive forms for servicing tourists, taking into account natural potential and other specific conditions of the country;
- To promote small and medium size hotel businesses;
- To accelerate defining sanitation protected zones;
- To promote development of resorts and to carry out the measures in the places of resorts for preserving and developing natural healing resources.

**112. Policy of Regional Economy:**

- To match the development of separate branches of infrastructure with the global development programs of different social-economic regions of the country;
- To assess economic potentials of different territorial units of the country and to promote maximum utilization and further development of these capacities.
- To promote the socio-economic development of regions with low economic potentials (such as for instance highland zones).

### **Results of the Program:**

113. In order to improve the living conditions of the population and to overcome poverty, it is important to boost economic growth. The aim of the Government is to continue ongoing structural reforms in order to achieve 4.5% annual average growth of the real GDP during the short-term (3 years) period. As a result, the 2003 GDP shall grow by approximately 14% in comparison with the 2000 GDP. Along with the mentioned macro-parameters, an optimal structure of the national economy must be established, based on different sectors. During the 3-year period following growth rates for the development of different sectors is projected: industry – 14%, agriculture – 7-8%, construction – 20%, trade and service – 10%, transport services – 7-8%, energy sector – 8%. The volume of goods produced by small business should amount to 485 million Lari (if compared to the beginning of 2000, this means 11% growth). The share of private investments in all sectors during the 3-year term should increase on the average by 50%. The share of shadow economy within the GDP must be reduced by one third.

### **3.5. Main Directions of Agriculture and Environment Protection**

#### ***a) Development of Agricultural and Food Sector***

114. The Agriculture and Food sector, characterized with high employment level, will keep its important place in the national economy in the future, although its place and role must be strictly defined.

115. Taking into account the peculiarity of the Sector, Agriculture sector is easily influenced by the climate changes. The drought of summer 2000 was yet another proof to this fact. Hence, the measures to be taken in the Sector will be oriented towards decreasing the vulnerability against climatic shocks, thus providing stability to the people employed in this Sector.

116. The primary objective will be *development of rural infrastructure and re-equipment and restoration of inputs and material-technical basis*. Taking into consideration the lack of State financial resources, practical steps towards attraction of foreign investments should be made in order to ensure rehabilitation of irrigation and drainage nets, main structures, magisterial and distribution channels, and pumping stations. It is necessary to establish Water Users Associations (WUA) that will privatize small farmland schemes on the first stage. The next step requires privatization of secondary schemes by WUAs. Hence, the State will preserve its responsibility on maintaining only the main schemes that will save significant financial resources.

117. The material-technical basis is in a distressing situation and it requires provision of agricultural machinery and trailers for farmers in the framework of active participation of donor countries and organizations; it is also important to establish a favorable business environment for private investments and to focus on purchasing of large amounts of comparatively cheap and qualitative agricultural machinery, that will give possibility to service-centers to renovate depreciated machinery in several years. Establishment of private and mixed service-centers in the regions will be useful for this purpose.

118. The development of agro-processing enterprises, which represent a link between farmers and credit institutions, is also a measure of great importance. Attention should be paid to the enlargement of the local goods market that can be achieved through a policy oriented on improving product quality and safety. It is essential to strictly control useful and dangerous material tolerance in the products.

119. In order *to preserve soil fertility* it is necessary to conduct soil research and to develop appropriate recommendations. It is essential to use efficiently agricultural machinery and technologies, to introduce crop rotation, proper utilization and protection of soil, and to elaborate a seed rotation system suitable for small farms.

120. The formation of a Rural Credit Policy is a means to promote sustainable entity formation, to establish Guarantee Funds, to raise the interest of Credit Unions' towards the Agriculture Sector, and to introduce insurance mechanisms, etc. This will reduce the risk factor that is a heavy burden on poor people employed in the Sector. Stimulation of the process for creation of rural savings and re-investment should be ensured.

121. It is reasonable to optimize existing tax and customs regime in accordance with the WTO regulations.

122. It is necessary to conduct a targeted regional policy envisaging specificities of the Sector development within a regional framework. Establishment of regional and district consulting centers for farmers will increase business awareness of micro, small and medium enterprise holders (including farmers). Special attention should

be paid to the elaboration of special program of poverty elimination in highland regions and its phased implementation.

### **b) Land Management**

**123.** For the purpose of the Poverty Reduction and Economic Growth Program, special attention must be paid to the following measures of the land management:

- Further privatization of vacant state-owned agricultural lands – total area 100.6 thousand hectares, of which: 48.0 thousand hectares are arable land, 20.7 thousand hectares – land under perennials, and 31.9 thousand hectares – grasslands;
- Privatization through purchasing of rented agricultural lands, which were leased by the State – total area 259.7 thousand hectares, of which: 178 thousand hectares are arable land, 22.6 thousand hectares – land under perennials, and 59.1 thousand hectares – grasslands;
- Introduction of a relevant cadastre and land registration system for the country and further improvement of corresponding legislative base;
- Elaboration of State targeted program of soil fertility upgrading and identification of respective sources of finance;
- Development of land and real estate market through the involvement of banking and insurance system and establishment of private institutions of real estate evaluators, soil specialists, surveyors and lawyers. It is also necessary to support cooperation of small landowners and land consolidation;

### **c) Protection of Environment and Natural Resources**

**124.** To overcome the problems that exist in this Sector, the Government is required to implement multi-pronged and complex policy. The correct planning of these measures and activities is essential to ensure stability of the sector. These measures are as follows:

**125.** Improvement of Environmental and Health Care Protection:

- Institutional improvement of city water supply and cleaning system, revising of tariff policy, establishing the ways to subsidize the primary needs of the population;
- Elaboration and implementation of a State program oriented towards improvement of gas quality;
- Evaluation of the current waste disposal system and its improvement;
- Evaluation of the potential of tourist resorts and finding the ways for its improvement.

**126.** Ensuring Sustainability of Property and Income Sources towards the Environmental Factors:

- To preserve and improve the fertility of natural resources (continue the project of protected territories taking into account social components);
- To consider environmental factors in the State taxation policy;
- To improve planning of measures oriented towards environment protection (further perfection of legislative base with an estimation of the impact on the environment, elaboration of efficient estimation strategies for regional projects)
- To provide access to mechanisms of reducing the risk (micro credit, insurance) caused by changes in the environmental situation;
- To define vulnerable sectors and groups, influenced by the climate changes, and to elaborate the mechanisms of prevention and compensation;
- To provide a detailed analysis of the tendency of desert-creation, and to prepare short and long run forecasts. It is essential to elaborate State and regional programs against the above-mentioned process;
- To implement a complex of measures oriented against soil erosion process;
- To support small scale renovation energy sector development, especially in far regions with low income (nontraditional energy sources);

- To create instructions for housekeepers and small enterprises about the prudent and effective usage of energy;
- To design and to promote the efficient household devices for decreasing the indoor pollution;
- To ensure the development of small scale local and private water supplying and water cleaning systems;
- To introduce and to promote of sound practices for plant disease management and optimal use of pesticides;

**127. Management of Natural and Anthropogenic Disasters:**

- To conduct preventive measures in order to avoid essential environmental crisis (estimation of hot spots, risk analysis, implementation of urgent measures);
- To elaborate State programs and mechanisms in order to reduce the results of natural disasters and environmental crisis;
- To improve forecasting mechanisms and to plan preventive measures.

**128. Increase Efficiency of Environmental Protection and Control Management:**

- To increase knowledge about environmental issues in society;
- To ensure active cooperation with mass media in order to provide population with comprehensive information about mentioned issues;
- It is necessary to use participatory process in decision-making and to implement Arhus Convention

**d) Development of Forestry**

**129.** For the development of forestry the following measures should be implemented:

- To conduct phased privatization of forest areas. For this purpose it is important to accelerate the process of elaboration of the draft law on privatization of forests in Georgia;
- To develop timber processing and furniture production sectors;
- To activate the Forestry Sector Development Project, elaborated under the aegis of the World Bank,;
- To improve mechanisms regulating functioning of former collective farms' forests and recording of their income;
- To improve the legislative base regulating the forestry sector;
- To develop targeted and specialized plantations (trees of walnut, hazelnut, pecan, almond, acacia, wild rose, fir-tree, pomegranate, laurel, mulberry, chestnut, etc).

**3.6. Governance, Public Administration Reform and Fight Against Corruption**

**130.** Effective implementation of the Poverty Reduction and Economic Growth Program in Georgia greatly depends on the normal and consistent functioning of all public services. Unfortunately, this task is frequently complicated because of large-scale corruption.

**131.** Given this fact, the Poverty Reduction and Economic Growth Program results should be assisted by the implementation of parallel and sequential measures against corruption.

**132.** By the Decree of the President of Georgia #296, dated July 9, 2000, a working group was established to draft a national Anti-Corruption Program. The Intermediary document of the National Anti-Corruption Program drafted by this working group consists of the following strategic directions:

**a) Liberalization of Business Environment:**

**133.** In Georgia corruption directly influences the welfare of citizens through the direct impact on their economic activity. The money extortion system used by public servants of various governmental agencies in relations with entrepreneurs creates an informal tax chain where the unofficial payments received exceed the

real tax revenues State Budget. As a result, a substantial part of the economy is localized in the informal or “shadow” sector that greatly damages the condition of public servants dependent on the budget and socially unprotected groups.

**134.** The activities aimed at liberalization of the entrepreneurial environment must be implemented in the following ways:

- Optimization of the system of controlling organizations;
- Creation of a transparent mechanism for issuance of licenses and permissions for entrepreneurial activity;
- Improvement of tax legislation and ensuring a strict tax administration system;
- Improvement of financial accounting procedures;
- Simplifying and perfecting the system of standardization and certification;
- Increasing the effectiveness of anti-monopoly legislation;
- Consistent implementation of the program for legalizing the shadow economy drafted by the Ministry of Economy, Industry and Trade;
- Strict criminal liability for unjust competition, falsification and other economic misdemeanors in order to protect the rights and interests of honest entrepreneurs.

***b) Financial Management of State Resources***

**135.** The State cannot implement its functions on a substantial level because of the ineffective expenditure of available limited resources. The main reasons creating this situation are the insufficient determination of State policy priorities and the non-existence of systematic financial management of State resources.

**136.** The effective administration of State resources can be achieved through the realization of the following activities:

- Budget organization (perfection of legislation that regulates budget organization, provision of budget transparency, and channeling of non-budgetary revenues into the budget system);
- State procurement (to reduce the volume of direct procurement envisaged by law to the minimum; to determine persons liable for state procurement in each State service; to create a list of unreliable firms that have violated the law based on data provided by international organizations);
- Introduction of controlling mechanisms over the current expenditures of the Budget (ensuring promulgation of financial accounts by all Budgetary organizations in a transparent manner);
- Management of State shares in enterprises (giving priorities to targeted investment programs and subsidies in the real sector, ensuring liability, improving legal mechanisms for distribution of dividends and net benefits received in the organizations created by the State share participation);
- Management of strategic material State recourses;
- Foreign credits and assistance (create active and transparent mechanisms of disposal, strict state supervision and administration procedures in order to ensure their practical use).

***c) Increasing effectiveness of Public Administration:***

**137.** Despite the fact that the General Administrative Code provides a foundation for ensuring transparency in the Public Administration, in reality the majority of the Governmental agencies try to avoid accomplishment of its requirements.

**138.** Public Administration optimization can be reached by carrying out the following main activities:

- Increasing wages of public servants by increasing budget incomes and decreasing the number of public servants;
- Creating a mechanism to analyze and check data provided in officials’ financial and property declaration;

- Strengthen liability for not accomplishing obligations outlined in the Administrative Code and for violating legislation about freedom of information and not performing tasks;
- Ensuring material and disciplinary liability for those officials who have brought damage to Georgian citizens and the State through their activities;
- Strengthen judicial departments existing in supreme governmental structures;
- Bringing Charters of the Governmental agencies in line with the Constitution of Georgia, the Law on the “Structure and Activity of the Executive Authority” and the Law on the “Budget system and authority”;
- Structural unification of functions through adoption of standard charters for Ministries and State Agencies;
- Wide-ranging implementation of modern informational technologies in the Administration system;
- Adopt a law concerning the ranking of public servants in order to determine rights of use of governmental privileges;

***d) Improving law-enforcement and justice system:***

**139.** These institutions play an important role in anti-corruption activities; hence to conduct an effective fight against corruption, their reform is of paramount importance and must be considered as a priority sphere in anti-corruption policy.

**140.** Reform of law-enforcement structures should involve three main directions:

- Structural and institutional reform (perfection of external and internal control mechanisms, eradication of redundancy and alleviation of superfluous and inconsistent functions, adoption of unified system to prosecute misdemeanors);
- Staff reform (optimization of structure and number of staff, implementation of public qualification examinations, drafting unified criteria for hiring and promotion and establishing a competitive system to hold a given position);
- To ensure a material-technical and financial base (computerization of working process, increase of wages);

**141.** It is essential to perfect the Justice system by improving criteria for judge selection, drafting a long-term program of training for judges, introducing modern methods of case management in courts and adopting a code of ethics.



## Chapter IV

### 4. PARTICIPATORY PROCESS, COMMUNICATION STRATEGY AND THE TIMETABLE FOR DRAFTING THE FINAL DOCUMENT OF THE POVERTY REDUCTION AND ECONOMIC GROWTH PROGRAM IN GEORGIA

#### 4.1. Participatory Process

*142.* The role of the participatory process in working out important issues of the county is very well comprehended in Georgia. From this point of view, fighting such a comprehensive problem as poverty cannot be fruitful unless the participatory process is fully realized.

*143.* The work on the Intermediary Document of the Poverty Reduction and Economic Growth Program in Georgia (PREGP) revealed that there was rather high participatory activity both on governmental and non-governmental level. This process made it clear that while drafting the final Poverty Reduction Program, priority should be given to an active participatory process. The realization of the objectives of the Program will depend to great extent on the activity of the participants and their cooperation.

*144.* Considering the above-mentioned, here is the list of participants that worked on the Intermediary Document, and will work on drafting the Final Document of Poverty Reduction and Economic Growth Program in Georgia:

- Government representatives;
- Non-governmental organizations;
- Representatives of civil society: mass media, professional associations, etc.;
- Representatives of private sector;
- Representatives of International Organizations and Donor Countries;

#### 4.2. Communication Strategy for the Poverty Reduction and Economic Growth Program

*145.* The Government of Georgia has drafted a Communication Strategy for the Poverty Reduction and Economic Growth Program. The primary objective of this Communication Strategy is carrying out an active public awareness campaign through informational and educational activity, in order to establish a dialogue with the public.

*146.* The Communication Strategy was drafted by the Information Center for Economic Reforms with the support of the World Bank. This Strategy considers usage of different communication tactics to create public awareness and support of the new initiative by granting each citizen of Georgia an opportunity to receive concrete answers to questions regarding the solution of social problems and reduction of poverty.

*147.* This Communication Strategy envisages systematic meetings with the society in Tbilisi and in the regions of Georgia; preparation of a special weekly analytical television program to be broadcast on the first channel of Georgian Television. Involvement of private TV companies to ensure full coverage of Poverty Reduction campaign is also envisaged.

*148.* Apart from this, an active informational campaign is scheduled not only on television, but also on different radio channels, and through other sources of mass media. Pamphlets and booklets will be issued and distributed countrywide, in order to transmit the core aspects of the Poverty Reduction and Economic Growth Program to each and every family of Georgia in an easily comprehensible way.

*149.* Establishing a dialogue with a public remains an important focus. This will be achieved through conducting research and organizing regional trips with participatory channels.

#### 4.3 Institutional Organization

*150.* Considering the complexity and continuing nature of drafting the Final Document of Poverty Reduction and Economic Growth Program in Georgia, the essential condition is the direct participation and close

cooperation of all the relevant parties on each stage of elaboration process. In order for this to be achieved and utilized effectively, priority role is given to ensuring efficient coordination of elaboration process.

*151.* By the Presidential Decree #678 of July 1, 2000 on "Promoting Organizational Activities for Elaboration of the Poverty Reduction and Economic Growth Program in Georgia", a Special Governmental Commission was set up. The Chairman of the Commission is the President of Georgia. The Commission is divided into 5 Sub-commissions, namely: 1) Sub-commission on Social Issues; 2) Sub-commission for Governance and Public Administration Reforms; 3) Fiscal and Monetary Policy Sub-commission; 4) Sub-commission on Agriculture and Environmental Protection; and 5) Sub-commission on Infrastructure Issues.

*152.* To ensure effective and coordinated activity of the above-mentioned Sub-commissions, the role of the Secretariat to the Governmental Commission, responsible for coordination of the whole elaboration process, has been assigned by the same Decree of the President of Georgia to the Service for Economic Reforms and Cooperation with International Organizations of the State Chancellery of Georgia.

*153.* The fact of close cooperation with non-governmental organizations, international organizations and donor countries on all stages of elaboration of the Intermediary Document of PREGP process should be mentioned and highly commended.

*154.* In order to elaborate the comprehensive final Document of Poverty Reduction and Economic Growth Program of Georgia, the Sub-Commissions, established for this purpose, as well as various Ministries and agencies, will define the costs of each reforms and measures to be undertaken in the framework of the PREGP, and will agree these costs with the Ministry of Finance of Georgia.

#### **4.4. Timetable for Drafting the Final Document of the Poverty Reduction and Economic Growth Program in Georgia**

*155.* The work on the Final Document of Poverty Reduction and Economic Growth Program in Georgia covers the time period from March of 2000, through March of 2001. Below is the timetable listing the major activities to be undertaken during the mentioned period:

##### **March 2000**

- Working Group on Social Issues was established;

##### **May 2000**

- Working Groups on Infrastructure, Fiscal and Monetary policy, Agriculture and Environment Protection were established;

##### **July 2000**

- Presidential Decree #678 on "Promoting Organizational Activities for Elaboration of the Poverty Reduction and Economic Growth Program in Georgia" was issued;
- The Sub-commission on Governance and Public Administration Reforms was established;

##### **September 2000**

- Majority of the Sub-commissions presented corresponding parts of the Poverty Reduction and Economic Growth Program in Georgia;
- The work on unification of received materials and compilation of a single Intermediary Document of the Poverty Reduction Program began at the Service for Economic Reforms and Relations with International Organizations of the State Chancellery of Georgia.

##### **October 2000**

- Visits of the missions of the International Monetary Fund and the World Bank to Georgia and discussion of the Interim Document of Poverty Reduction Program with these missions;
- Preparation of the Participatory Strategy;
- Preparation of the Communication Strategy for the Program.

##### **November 2000**

- A conference held in Moscow, Russian Federation, regarding the work on elaboration of Poverty Reduction Strategies in 6 FSU countries, organized by the World Bank and the International Monetary Fund;
- Conducting dialogues with Sub-commissions and other interested agencies about the perfection and definition of measures that must be realized in various sectors;

- Organization of a workshop for discussion of the final Intermediary Document of PREGP and Communication Strategy with participation of all the sub-commissions, representatives of international organizations and donor countries, NGOs, private sector representatives and mass-media;
- Discussion and approval of the final Intermediary Document of PREGP by the Governmental Commission.

#### **December 2000**

- Preparation of detailed action plan for elaborating the Final Document of PREGP;
- Discussion of the Intermediary Document of PREGP by the Board of Directors of the International Monetary Fund.

#### **January 2001**

- Perfection and revision of indicators reflecting the poverty rate in Georgia, that will help to determine more efficient instruments for poverty reduction;
- Consultations with the civil society.

#### **February 2001**

- Estimation of expenditures needed for actual implementation of the PREGP;
- Conduction of consultations with the World Bank, IMF and other donor organizations on the above mentioned issue;
- Consultations with the civil society.

#### **March 2001**

- Conduction of consultations with international organizations, donors and other interested parties regarding the final draft of the PREGP;
- Incorporation of comments received regarding the final draft of the PREGP.

#### **April 2001**

- Organization of a workshop for discussion of the final Document of PREGP with participation of all the sub-commissions, representatives of international organizations and donor countries, NGOs, private sector representatives, mass-media and the civil society;

#### **May 2001**

- Discussion and approval of the final Document of PREGP by the Governmental Commission.

#### **June 2001**

- Start of actual implementation of the Poverty Reduction and Economic Growth Program in Georgia and its further coordination and monitoring.

## **5. MONITORING SYSTEM OF THE PROGRAM AND ITS INDICATORS**

*156.* One of the primary tasks of a contemporary State is to supervise the production of national resources and their further distribution and, consequently, to implement such political measures that will ensure the targeted and efficient use of these resources.

*157.* The work on the Intermediary Document of PREGP showed that in order to define the socio-economic indicators of public welfare, a well-functioned statistical system is needed for planning socio-economic activities and for monitoring of their actual implementation. Unfortunately, due to some objective reasons, the statistical system in Georgia is not functioning properly nowadays.

*158.* Coming from the above-mentioned, in order to achieve maximal efficiency while implementing the PREGP, it is necessary to introduce flexible monitoring system, based on the realistic data. This task first of all requires the improvement of the existing data gathering system and introduction of certain new mechanisms for monitoring. Apparently, monitoring requires complete utilization of the participatory process (described in previous chapter), because otherwise gathering of realistic data will be very much delayed. Along with the Department of Statistics and various Ministries, an important role is placed on non-governmental organizations and international institutions, which are actively cooperating directly with the civil society. This is one of the best ways to receive necessary first-hand information. The importance of sociological surveys, carried out by different scientific-research institutes and various research centers, must also be noted here.

*159.* As for the organizational issues, the coordination of the monitoring system will be carried out by the Service for Economic Reforms and Cooperation with International Organizations of the State Chancellery of Georgia, which, as mentioned above, is also acting as the Secretariat to the Special Governmental Commission

for elaboration of PREGP. This Service will significantly support the effective work of the Commission and will be responsible not only for actual monitoring of the process, but also for analyzing the data gathered by means of monitoring activities.

**160.** Regarding the indicators reflecting the implementation of PREGP, they are listed in Annex 5 below (except for macroeconomic indicators that are presented in Annex 1). The figures and targets given in the first and fifth Annexes will be revised and are subject to change in the final PREGP.

## **6. GOVERNMENT'S STATEMENT**

**161.** In response to the prolonged expectations of the Georgian population, poverty reduction became one of the major priorities in the country. Elimination of poverty is one of the most significant problems in practically every state. The welfare of its population and the strife for better life and future is the cornerstone of a country's power. In this document, the Government of Georgia expressed its will to fight against the poverty. The major objectives of this Strategy are provision of basic needs, such as comprehensive education, normal living conditions, adequate health care and creation of middle class, to each and every poor citizen of Georgia.

**162.** The aim of this Strategy Document is to improve social conditions and economic environment, which are major elements of state's welfare. It envisages practical steps for actual implementation of defined objectives. It is impossible to achieve improvement of social conditions in the country by means of conducting structural reforms in only this direction. There is a whole set of factors that has strong influence on the life of the country.

**163.** Among the actions to be undertaken within the framework of this Strategy, the highest priority will be given to the following measures:

### **164. In Social sector:**

- Reducing the possibility of poverty risk through its prevention and softening the influence of existing poverty level;
- Reforms in Social Protection, including the Pension Reform;
- Reform of education system;
- Reform of health care system;
- Provision of unimpeded social protection to the IDPs and perfection of their identification and differentiation.

### **165. In Fiscal and Monetary spheres:**

- Promotion of rapid and sustainable economic growth;
- While maintaining the floating exchange regime, to achieve annual average inflation at 4% level;
- Gradual repayment of accumulated arrears and external debts;
- Step-by-step reduction of the budgetary deficit;
- Orientation of the budgetary process primarily towards social issues;
- Strict control over the budgetary expenditures and centralization of the Treasury Department.

### **166. In Infrastructure sector:**

- Improvement of investment climate, promotion of foreign and domestic investments;
- Promotion of small and medium size businesses;
- Promotion of tourism development;
- Fostering privatization process;
- Restructuring of enterprises;
- Reducing the scales of shadow economy and business legalization;

- Implementation of relevant reforms in different sectors of Infrastructure.

**167. *In Agriculture and Environment Protection:***

- Development of rural infrastructure and re-equipment and restoration of inputs and material-technical basis;
- Preservation of soil fertility;
- Conducting targeted rural credit policy;
- Improvement of environment and health care protection;
- Increasing efficiency of environment protection and control management;
- Further development of forestry and its optimization.

**168. *In Governance, Public Administration Reforms and Anti-Corruption measures:***

- Liberalization of business environment;
- Improvement of Public Administration;
- Reforms in law-enforcement and justice systems.

**169.** The document is drafted not only by the Government of Georgia, but it also expresses the will of the whole nation. The Document clearly defines the existing situation of country's development, as well as necessary measures to improve present conditions. The Strategy has its time framework. The timing for concrete actions is determined by 3-year (short-term), 7-year (medium-term) and 15-year (long-term) periods, efficient implementation of these actions will yield positive results for bringing the poverty rate to moderate level. The Intermediary Document envisages drafting of the final and more comprehensive strategy, which shall have a complete list of actions to be undertaken in a particular sector of economy, and the methods for their implementation.

**170.** The Government of Georgia is determined to achieve welfare for its population, to improve the living standards, and to ensure substantial social protection. The future strategy of country's development will be directed towards achievement of these values, and all the possible efforts shall be carried out to let Georgia obtain an honourable place within the International Community.

**Annex 1: Macroeconomic Indicators 1996-2003**  
(Adjustment Scenario)

|   | 1996  | 1997   | 1998   | 1999   | 2000<br>Proj. | 2001<br>Adjustment Scenario | 2002   | 2003   |
|---|---|--------|--------|--------|---------------|-----------------------------|--------|--------|
| <b>Output and Prices</b>                                  | (Percent change)  |        |        |        |               |                             |        |        |
| Real GDP  | 10.5  | 10.7   | 2.9    | 2.9    | 1.2           | 3.8                         | 5.0    | 5.0    |
| Consumer price index (end-of-period)                      | 13.7  | 7.2    | 10.7   | 10.9   | 6.8           | 5.9                         | 4.0    | 4.0    |
| <b>External Sector</b>                                    | (In millions of U.S. dollars)                             |        |        |        |               |                             |        |        |
| Current account balance 1/<br><i>Of which:</i>            | -275  | -375   | -389   | -218   | -233          | -233                        | -202   | -164   |
| Export of goods and nonfactor services                    | 511   | 661    | 720    | 762    | 888           | 974                         | 1,088  | 1,199  |
| Imports of goods and nonfactor services                   | -867  | -1,368 | -1,437 | -1,281 | -1,411        | -1,507                      | -1,596 | -1,686 |
| <b>Public Finances:</b>                                   | (In percent of GDP)                                       |        |        |        |               |                             |        |        |
| Overall deficit (commitment basis)                        | -7.4  | -7.0   | -6.4   | -6.9   | -4.3          | -2.0                        | -0.7   | -0.7   |
| Overall deficit (cash basis)                              | -7.2  | -6.3   | -5.1   | -5.1   | -3.2          | -3.2                        | -1.9   | -1.2   |
| Privatization   | 0.5   | 0.6    | 1.5    | 1.0    | 0.3           | 1.2                         | 0.3    | 0.5    |
| Domestic financing  | 4.1   | 3.6    | 2.0    | 2.4    | 1.0           | 0.3                         | 0.9    | 1.2    |
| External financing (net)                                  | 2.5   | 2.2    | 1.5    | 1.2    | 1.8           | 1.7                         | 0.7    | -0.5   |
| <b>Monetary Aggregates:</b>                               | (Percent change)  |        |        |        |               |                             |        |        |
| Reserve money   | -   | 33     | -6     | 18.8   | 13            | 12.5                        | 12.6   | 9.6    |
| Private sector credit                                     | -   | 35     | 38     | 31.8   | 17.1          | 11.4                        | 12.9   | 13.8   |
| Broad money (M3)  | -   | 46     | -1     | 20.7   | 23.1          | 17.8                        | 18.2   | 18.3   |
| Velocity level of the broad money (Ratio) 2/              | -   | 15.27  | 13.29  | 12.4   | 11            | 10.5                        | 9.7    | 8.9    |
| Broad money multiplier (Ratio)                            | -   | 1.35   | 1.42   | 1.44   | 1.57          | 1.64                        | 1.73   | 1.86   |
| <b>Saving and Investment 3/</b>                           | (In percent of GDP)                                       |        |        |        |               |                             |        |        |
| Gross domestic saving                                     | -1.2  | 4.9    | 13.3   | 6.7    | 8.5           | 9.6                         | 11.5   | 13.3   |
| General government 4/                                     | -1.0  | 0.3    | 1.8    | 1.0    | 2.7           | 5.0                         | 6.0    | 5.9    |
| Non-government sector                                     | -0.2  | 4.6    | 11.5   | 5.6    | 5.8           | 4.6                         | 5.5    | 7.4    |
| Investment  | 7.9   | 15.6   | 24.4   | 14.6   | 16.1          | 16.5                        | 17.0   | 17.5   |
| General government  | 1.8   | 1.6    | 1.3    | 0.9    | 1.3           | 1.4                         | 1.5    | 1.3    |
| Non-government sector 5/                                  | 6.1   | 14.0   | 23.0   | 13.8   | 14.8          | 15.1                        | 15.5   | 16.2   |
| <b>External Public Debt and Foreign Exchange Reserves</b> | (In millions of U.S. dollars; unless otherwise indicated) |        |        |        |               |                             |        |        |
| External debt, end-of-period                              | 1,357   | 1,506  | 1,652  | 1,723  | 1,807         | 1,989                       | 2,135  | 2,190  |
| External debt service (after rescheduling)                | 47.2  | 39.7   | 66     | 99     | 109           | 102                         | 128    | 200    |
| External debt service/exports GNFS (%)                    | 9.2   | 6.0    | 9.1    | 13.0   | 12.3          | 10.5                        | 11.8   | 16.7   |
| Gross official reserves                                   |   |        |        |        |               |                             |        |        |
| (In millions of USD)                                      | 158   | 173    | 118    | 132    | 136           | 199                         | 264    | 301    |
| (In month of imports of goods & services)                 | 2.2   | 1.5    | 1.0    | 1.2    | 1.2           | 1.6                         | 2.0    | 2.1    |

*Sources: Government of Georgia and the IMF Staff (estimates)*

1/ Including transfers; (-) means current account deficit.

2/ Defined as annual GDP divided by end-period M3.

3/ National accounts statistics suffer from serious methodological problems, including, inter alia, inconsistent adjustments for the informal economy.

4/ Fiscal deficit on a commitment basis (excluding external grants) minus government investment. For 1998, the fiscal adjustment excludes the programmed reduction in expenditure arrears, the general government dissavings in 1998 would have been equivalent to 1.5 percent of GDP, or an improvement of 1.8 percent of GDP relative 1997.

5/ The decline in private investment in 1999 relative to the 1998 level reflects the scaling down of imports related to the construction of the oil pipeline from Azerbaijan.

**Annex 2: Dynamics of Absolute and Relative Poverty Rate Indicators**  
**According to Quarters, 1996-2000**  
(Observance on Georgian Households)

|          |         | Relative to living wage |       |          | Relative to 60% of median consumption |       |          | Relative to 40% of median consumption |       |          |
|----------|---------|-------------------------|-------|----------|---------------------------------------|-------|----------|---------------------------------------|-------|----------|
|          |         | Rate                    | Depth | Severity | Rate                                  | Depth | Severity | Rate                                  | Depth | Severity |
| 1996 III | Urban   | 57,4                    | 23,3  | 12,4     | 28,1                                  | 9,0   | 4,2      | 11,6                                  | 3,5   | 1,6      |
|          | Rural   | 42,5                    | 15,2  | 7,6      | 17,0                                  | 5,1   | 2,4      | 6,8                                   | 2,0   | 0,9      |
|          | Average | 50,9                    | 19,2  | 10,3     | 23,2                                  | 7,33  | 3,4      | 9,5                                   | 2,8   | 1,3      |
| 1996 IV  | Urban   | 54,3                    | 22,2  | 12,2     | 23,2                                  | 8,8   | 4,7      | 12,5                                  | 4,3   | 2,4      |
|          | Rural   | 49,4                    | 17,7  | 9,0      | 19,2                                  | 6,0   | 2,8      | 7,6                                   | 2,3   | 1,2      |
|          | Average | 52,1                    | 20,2  | 10,8     | 21,4                                  | 7,6   | 3,9      | 10,3                                  | 3,4   | 1,8      |
| 1997 I   | Urban   | 36,8                    | 14,3  | 7,6      | 22,9                                  | 8,1   | 4,0      | 11,6                                  | 3,5   | 1,7      |
|          | Rural   | 42,8                    | 15,9  | 8,2      | 25,4                                  | 8,6   | 4,2      | 11,9                                  | 3,7   | 1,8      |
|          | Average | 39,5                    | 15,0  | 7,9      | 24,0                                  | 8,,3  | 4,1      | 11,7                                  | 3,6   | 1,7      |
| 1997 II  | Urban   | 40,6                    | 13,5  | 6,2      | 20,3                                  | 5,6   | 2,4      | 6,7                                   | 1,9   | 0,8      |
|          | Rural   | 42,7                    | 15,9  | 8,1      | 23,9                                  | 7,8   | 3,8      | 9,9                                   | 3,4   | 1,7      |
|          | Average | 41,6                    | 14,6  | 7,1      | 22,0                                  | 6,6   | 3,0      | 8,2                                   | 2,6   | 1,2      |
| 1997 III | Urban   | 54,6                    | 20,3  | 10,4     | 24,3                                  | 7,6   | 3,5      | 9,9                                   | 3,0   | 1,3      |
|          | Rural   | 45,9                    | 17,2  | 8,6      | 19,9                                  | 5,8   | 2,5      | 7,3                                   | 1,9   | 0,8      |
|          | Average | 50,5                    | 18,9  | 9,5      | 22,3                                  | 6,7   | 3,0      | 8,7                                   | 2,5   | 1,1      |
| 1997 IV  | Urban   | 46,0                    | 16,6  | 8,5      | 23,4                                  | 8,0   | 3,9      | 10,8                                  | 3,5   | 1,7      |
|          | Rural   | 39,4                    | 13,7  | 6,7      | 19,7                                  | 6,0   | 2,7      | 7,7                                   | 2,3   | 1,0      |
|          | Average | 42,9                    | 15,2  | 7,6      | 21,7                                  | 7,0   | 3,4      | 9,3                                   | 2,9   | 1,4      |
| 1998 I   | Urban   | 53,8                    | 20,8  | 11,0     | 23,9                                  | 8,1   | 4,2      | 10,5                                  | 3,7   | 2,0      |
|          | Rural   | 49,6                    | 18,8  | 10,2     | 19,9                                  | 7,7   | 4,3      | 10,0                                  | 4,1   | 2,4      |
|          | Average | 51,9                    | 19,9  | 10,6     | 22,1                                  | 7,9   | 4,3      | 10,3                                  | 3,9   | 2,2      |
| 1998 II  | Urban   | 57,2                    | 23,6  | 12,9     | 29,0                                  | 9,7   | 4,8      | 12,7                                  | 4,1   | 2,0      |
|          | Rural   | 46,2                    | 18,1  | 9,6      | 21,3                                  | 7,0   | 3,4      | 9,1                                   | 2,9   | 1,4      |
|          | Average | 52,1                    | 21,1  | 11,4     | 25,4                                  | 8,5   | 4,1      | 11,0                                  | 3,6   | 1,7      |
| 1998 III | Urban   | 56,6                    | 23,5  | 13,0     | 28,4                                  | 10,2  | 5,3      | 13,5                                  | 4,8   | 2,6      |
|          | Rural   | 45,7                    | 16,2  | 8,1      | 17,2                                  | 5,6   | 2,7      | 6,8                                   | 2,3   | 1,2      |
|          | Average | 51,6                    | 20,2  | 10,8     | 23,3                                  | 8,1   | 4,1      | 10,4                                  | 3,6   | 1,9      |
| 1998 IV  | Urban   | 49,7                    | 18,8  | 9,9      | 25,6                                  | 8,9   | 4,3      | 12,8                                  | 3,7   | 1,8      |
|          | Rural   | 40,0                    | 14,5  | 7,4      | 18,4                                  | 6,3   | 3,2      | 8,9                                   | 2,9   | 1,4      |
|          | Average | 45,2                    | 16,8  | 8,7      | 22,3                                  | 7,7   | 3,8      | 11,0                                  | 3,3   | 1,6      |
| 1999 I   | Urban   | 59,4                    | 23,0  | 11,9     | 29,1                                  | 9,3   | 4,5      | 12,                                   | 3,9   | 1,9      |
|          | Rural   | 33,9                    | 12,5  | 6,6      | 15,5                                  | 5,4   | 2,8      | 7,5                                   | 2,6   | 1,4      |
|          | Average | 47,6                    | 18,1  | 9,4      | 22,8                                  | 7,5   | 3,7      | 9,9                                   | 3,3   | 1,7      |
| 1999 II  | Urban   | 67,4                    | 29,5  | 16,4     | 28,9                                  | 9,4   | 4,5      | 13,3                                  | 3,9   | 1,8      |
|          | Rural   | 49,0                    | 19,2  | 10,4     | 16,5                                  | 5,9   | 3,3      | 7,3                                   | 2,9   | 1,7      |
|          | Average | 58,7                    | 24,6  | 13,6     | 23,0                                  | 7,8   | 3,9      | 10,5                                  | 3,4   | 1,8      |
| 1999 III | Urban   | 61,1                    | 24,1  | 12,8     | 27,1                                  | 8,7   | 4,2      | 11,4                                  | 3,6   | 1,7      |
|          | Rural   | 44,3                    | 16,7  | 8,9      | 18,4                                  | 6,3   | 3,1      | 8,7                                   | 2,7   | 1,3      |
|          | Average | 53,4                    | 20,7  | 11,0     | 23,1                                  | 7,6   | 3,7      | 10,2                                  | 3,2   | 1,5      |
| 1999 IV  | Urban   | 52,7                    | 20,7  | 10,7     | 29,3                                  | 9,1   | 4,2      | 11,3                                  | 3,5   | 1,6      |
|          | Rural   | 37,0                    | 13,9  | 7,3      | 18,1                                  | 6,4   | 3,2      | 8,7                                   | 2,8   | 1,3      |
|          | Average | 45,7                    | 17,7  | 9,2      | 24,3                                  | 7,9   | 3,7      | 10,1                                  | 3,2   | 1,5      |
| 2000 I   | Urban   | 56,4                    | 22,5  | 11,9     | 28,5                                  | 9,1   | 4,3      | 12,4                                  | 3,8   | 1,7      |
|          | Rural   | 41,2                    | 17,3  | 10,0     | 21,2                                  | 8,4   | 4,6      | 11,1                                  | 4,4   | 2,4      |
|          | Average | 49,4                    | 20,2  | 11,0     | 25,2                                  | 8,8   | 4,5      | 11,8                                  | 4,0   | 2,0      |
| 2000 II  | Urban   | 60,4                    | 24,0  | 12,5     | 26,2                                  | 8,1   | 3,6      | 10,7                                  | 2,8   | 1,2      |
|          | Rural   | 45,3                    | 17,9  | 9,9      | 19,6                                  | 7,    | 3,8      | 10,0                                  | 3,5   | 1,9      |
|          | Average | 53,4                    | 21,2  | 11,3     | 23,1                                  | 7,6   | 3,7      | 10,4                                  | 3,1   | 1,5      |

### Annex 3: Indicators of the Population's Income in 1995-1999

| Title                               | Unit          | 1995    | 1996    | 1997    | 1998    | 1999    |
|-------------------------------------|---------------|---------|---------|---------|---------|---------|
| Cash revenues of the population     | Millions GEL  | 1,164.0 | 2,500.0 | 1,800.0 | 1,751.8 | 1,723.7 |
| Cash expenditures of the population | Millions GEL. | 1,077.0 | 2,454.6 | 2,390.0 | 2,534.6 | 2,677.2 |
| General average monthly salary      | GEL           | 13.6    | 29.0    | 42.5    | 127.6   | 114.4   |
| Growth of the real monthly salary   | %             | 134.4   | 152.9   | 139.8   | 123.2   | 103.6   |
| Consumption basket minimum          | GEL           | 41.3    | 47.7    | 182.7   | 183.9   | 193.5   |
| Minimal food basket                 | GEL           | 28.9    | 33.4    | 128.0   | 128.7   | 135.5   |

*Source: State Department of Statistics*

### Annex 4: State Budget Expenditures in 1997-2000, (millions of US dollars)

| Expenditure  | Year  |       |       |       |
|--|-------|-------|-------|-------|
|  | 1997  | 1998  | 1999  | 2000  |
| <b>Total</b>   | 597.5 | 570.7 | 452.4 | 493.3 |
| General State servicing                              | 73.7  | 44.9  | 61.7  | 96.0  |
| Defense  | 51.9  | 40.3  | 17.9  | 13.6  |
| State order and security                             | 71.8  | 46.4  | 37.9  | 32.5  |
| Education  | 35.6  | 21.7  | 14.6  | 13.9  |
| Health care  | 19.7  | 19.5  | 7.9   | 15.7  |
| Social protection and insurance                      | 146.1 | 154.3 | 123.5 | 136.7 |
| Accommodation  | 4.5   | 5.2   | 2.6   | 2.1   |
| Culture, sport, religion                             | 27.8  | 23.6  | 12.5  | 9.5   |
| Energy   | 9.2   | 2.3   | 6.3   | 10.6  |
| Agriculture, forestry and fishery                    | 13.4  | 16.2  | 7.8   | 7.2   |
| Chemical industry, processing and construction       | 2.1   | 1.4   | 0.4   | 0.3   |
| Transport and communications                         | 29.7  | 38.9  | 17.9  | 18.1  |
| Environment protection and other economic activities | 2.6   | 8.6   | 1.3   | 0.7   |
| Elsewhere unmentioned                                | 109.6 | 147.1 | 140.3 | 136.5 |

*Source: Ministry of Finance, Budgetary Office of the Parliament*



## Annex 5: Matrix of Social and Economic Policy of the PREGP

| Area                 | Measures to be implemented   | Responsible Agent   | Dates      | Indicators   |
|----------------------|--|---|------------|--|
| <b>Social Sector</b> |  |   |            |  |
| Employment           | To create the balance of labor resources, to identify the indicators of labor market development and to start monitoring in the whole country and especially in its “poor” regions. To find out the reasons, level and risk groups for unemployment, and to elaborate main trends regarding potential future employment. | Ministry of Health, Labor and Social Protection   | Jan., 2001 | Poverty coefficient per capita;  |
|                      | To create effective model on governmental and private levels, which will provide training and retraining in order to have competitive personnel and to provide consulting for unemployed persons.  |   | Dec., 2000 | Poorest fifth’s share of National consumption;                                       |
|                      | To define effective mechanisms of wages taking into consideration the existing reality.  |   | Feb., 2001 | Employment rate of working-able population’ age;                                     |
|                      | To elaborate regulating mechanisms for labor migration (internal and external); to adopt the law on labor migration.   |   | Dec., 2000 | Unemployment rate;   |
| Education            | To optimize the number of teachers; the payment of compensations to the dismissed teachers shall be carried out in accordance with the existing legislation of Georgia.  | Ministry of Education   | 2002       | Percentage of employment in informal sector in comparison with total employment;     |
|                      | To provide universal access to the basic education and to ensure its completion.   |   | 2005       | Indicator of attendance to primary and secondary schools;                            |
| Social insurance     | To elaborate suggestions oriented towards improvement of social taxation system and tax collection at the expense of the self-employed population and people employed in the agricultural sector.  | Ministry of Health, Labor and Social Protection, State Pension Fund and Ministry of Finance | Nov., 2000 | Percentage of pupils who completed the courses from I class to V, and from VI to IX; |
|                      | To work out adequate pension system for Georgia.   |   | Dec, 2000  |  |
|                      | To regulate accounting system, to carry out personification and to introduce international accounting standards.   |   | Jan, 2002  |  |
|                      | To ensure consecutive reforms in the pension system and to create transparent environment; to adopt/amend relevant legislation (Laws on “Compulsory social insurance”, “State pensions” and to draft amendments to Tax code according to personification of private pension funds).                                      |   | 2001-2003  |  |

|                   |  |   |                 |   |
|-------------------|--|---|-----------------|---|
|                   | To ensure continues payment of current pensions and gradual repayment of arrears accumulated in previous years.  |   | 2003            |   |
|                   | To implement personification and to introduce identification cards.  |   | 2003            |   |
|                   | To gradually change the existing pension system towards insurance-based and differentiated principles.   |   |                 |   |
|                   | To improve banking service and to introduce modeling and forecasting systems.  |   | 2001-2003       |   |
| Social safety net | To identify adequate criteria for poverty and differentiate forms in accordance with different determinants (level of income, etc.).                   | Ministry of Health, Labor and Social Protection | From Feb. 2001  |   |
| Labor relations   | To prepare and to adopt the labor code.  | Ministry of Health, Labor and Social Protection | From Feb. 2001  |   |
|                   | To elaborate the model of labor dispute's settlement and social partnership.   |   | From Jul., 2001 |   |
|                   | To elaborate the norms of labor safety.  |   | From Dec. 2001  |   |
| Health care       | To provide the majority population with medical-prophylactic service.  | Ministry of Health, Labor and Social Protection | Jan. 2002       | % of population who has access to primary health care service;<br>State expenditures on health care (% in GDP);<br>Infant mortality rate;<br>Mortality rate among the children under 5; |
|                   | To provide the financing of primary health care system from State budget.  |   | Jan. 2003       |   |
|                   | To provide the financing of additional expenditures on medical services of the people living under the poverty line from State budget.                 |   | Feb. 2002       |   |
|                   | To provide the cure of socially dangerous diseases due to compulsory medical insurance.  |   | 2000            |   |
| Refugees          | To identify the refugee families each member of which has the daily income (including different pensions and other refugee allowances) less than 1 \$. | Ministry of Refugees                            | Mar. 2001       |   |
|                   | To prioritize the mentioned families within special employment programs.   | Ministry of Refugees                            | 2001-2003       |   |
|                   | To increase the pension and refugee allowance for all kinds of pensioners from mentioned families.   | Ministry of Refugees, Ministry of Finance       | 2001-2003       |   |
|                   | To provide financing of all kind of medical services from state budget for all members of mentioned categories.  | Ministry of Refugees, Ministry of Finance       | Jan, 2002       |   |

|                                    |   |   |                       |   |
|------------------------------------|---|---|-----------------------|---|
|                                    | To identify the refugee families each member of which has the daily income (including wages, different pensions and other refugee allowances) more than 1\$, to conduct further stepwise canceling of the refugee allowances to these families and to distribute saved financial sources among the extremely poor refugee families. | Ministry of Refugees  | March – December 2001 |   |
|                                    | To improve the rules of drafting of State purposeful programs and relative legislative base, and to craft an adequate evaluating system of prospective outcomes of purposeful State social programs.  | Ministry of Health, Labor and Social Protection                       | Jan. 2001             |   |
|                                    | To conduct total census of population.  | State Department of Statistics  | Feb. 2002             |   |
|                                    | To craft adequate monitoring system of poverty reduction program, to establish basic indicators (poverty line, level, depth, and severity).   | Ministries of Health, Labor and Social Protection                     | Feb. 2001             |   |
| <b>Fiscal and Monetary Policy</b>  |   |   |                       |   |
| Macroeconomic stability and growth | To conduct moderate/strict fiscal-monetary policy.  | Government of Georgia   | 2001-2003             | Average GDP growth 4.5% and decrease of inflation to 4% |
| Budget policy                      | To adopt a new law on budget system.  | Ministries of Finance, Taxation Revenues and corresponding Ministries | 2001                  |   |
|                                    | To adopt a law on local budget systems.   |   | 2001                  |   |
|                                    | To adopt a law on property of local self-government institutions.   |   | 2001                  |   |
|                                    | To increase share of the State obligations in the process of deficit financing from internal sources.   |   | 2001-2003             |   |
|                                    | To pay off current budget arrears and to avoid further allocation.  |   | 2001-2003             |   |
|                                    | To perfect account system norms and standards for budgetary institutions.   |   | 2001-2003             |   |
|                                    | To account and to reflect the special revenues and expenditures of budgetary institutions in the State budget.  |   | 2001                  |   |
|                                    | To transfer to the system of program financing in order to increase the effectiveness of budgetary expenditures.  |   | 2002-2003             |   |
|                                    | To improve methodology of planning of budgetary expenditures on the basis of expenditure's rationing.   |   | 2001-2003             |   |
|                                    | To elaborate the automatic system of management of budgetary revenues and expenditures due to full computerization of Budget Department and Treasury.   |   | 2002-2003             |   |
|                                    | To improve the system of state purchasing.  |   | 2001-2003             |   |

|                               |  |  |           |  |
|-------------------------------|--|--|-----------|--|
|                               | To improve the treasury system structure, centralization of treasuries, strengthening internal control system and establishing of responsibilities' control system in order to improve the effectiveness of management of expenditures and the process of fulfilling the State Budget. |  | 2001-2003 |  |
|                               | To elaborate and implement State investment policy.  |  | 2001-2003 |  |
|                               | To restructure the State foreign debt.   |  | 2001-2003 |  |
| Tax policy and administration | To create the real progressive scale of profit tax and to equalize the minimal non-taxable profit to the amount of minimal pension.  | Ministries of Finance, Tax Revenues and corresponding Ministries | 2001      |  |
|                               | To gradually increase the number of persons who are eligible to fill in the financial and property statements (declarations).  |  | 2001-2003 |  |
|                               | To change property taxation rates.   |  | 2001      |  |
|                               | To regulate the agricultural sector taxation system.   |  | 2002-2003 |  |
|                               | To optimize the excise's taxation system.  |  | 2001-2003 |  |
|                               | To optimize the taxation of financial institutions (banks, insuring companies).  |  | 2002-2003 |  |
|                               | To regulate the taxation system of small business and investments.   |  | 2002-2003 |  |
|                               | To re-new and to regulate the existing appropriate normative acts.   |  | 2001-2003 |  |
|                               | Inadmissibility of increasing of delayed state payment responsibilities.   |  | 2001-2003 |  |
|                               | To conduct structural reforms at taxation and custom services in order to increase effectiveness of their work.  |  | 2001-2003 |  |
|                               | To conduct measures in order to improve the coordination of taxation and custom services.  |  | 2001-2003 |  |
|                               | To elaborate the effective methods of control due to usage of strict accountant facilities with fiscal memory.   |  | 2001-2002 |  |
|                               | To make taxation and custom procedures more simple and effective.  |  | 2001-2003 |  |
|                               | To elaborate the mechanisms of net profit distribution from enterprises created by the State share.  |  | 2001      |  |
|                               | To elaborate effective tax system for real estate, including land.   |  | 2001-2005 |  |

|                                     |   |   |           |  |
|-------------------------------------|---|---|-----------|--|
| Financial management of state funds | Budget organization (To perfect legislature regulating budget organization, to assure budget transparency, to comprise non-budget revenues in budget system);   | Ministry of Finance   | 2001      |  |
|                                     | State procurement (to establish independent, transparent agency of state procurement, to minimize the State direct procurements envisaged by law, to determine persons liable for state procurement in each State service, to create list of unreliable firms that based on date provided by international organizations were revealed in law violation,);  | Ministry of Economy, Industry and Trade                                   | 2001      |  |
|                                     | To establish current controlling mechanisms over expenditure of budget resources (to establish independent internal audit organizations in budget organizations, to ensure promulgation of financial accounts by all budget organizations in an easily perceptible way for the society);  | Ministry of Finance   | 2001      |  |
|                                     | To manage the State shares in enterprises (to allot budget policy priorities to the purposeful investment programs and subsidies in real sector, to ensure liability issue, to perfect legal mechanisms for distribution of dividends and net benefits received in organizations created by the State share participation and to establish supervisory council in such organizations, to negotiate and to agree all economic activities with the state in those enterprises where the control packet of shares is hold by the State); | Ministry of State Property Management                                     | 2001      |  |
|                                     | Foreign credits and assistance (to craft active and transparent mechanism of disposal, to strict State supervision and administration procedures in order to ensure their purposeful usage).  | Investment Council, Ministries of Finance and Economy, Industry and Trade | 2001      |  |
| Improvement of financial system     | To review custom policy in accordance with WTO regulations.   | National Bank of Georgia  | 2001-2003 |  |
|                                     | To perfect the legislation on bank secrecy.   |   | 2001      |  |
|                                     | To create the competitive environment in the sector due to establishment equal conditions for all banks.  |   | 2001-2002 |  |
|                                     | To increase transparency in bank sector.  |   | 2001-2003 |  |
|                                     | To conduct periodical review of the minimal reserve demand in the direction of reducing.  |   | 2001-2003 |  |
|                                     | To increase the level of bank's capitalization.   |   | 2001-2003 |  |
|                                     | To create favorable environment for international banks to enter the Georgian market.   |   | 2001-2003 |  |
|                                     | To promote development of new financial markets and establishment of new mechanisms in order to improve the management of liquidity.  |   | 2001-2003 |  |

| <b>Infrastructure</b>   |  |  |           |  |
|---|--|--|-----------|--|
| Improvement of the investment environment   | To perfect the taxation legislature;   | Ministries of Finance, Taxation Revenues, Economy, Industry and Industry   | 2002      | Increase of share of foreign investment in GDP from 2.3% (1999) to 3.8% (2003) |
|   | To promote insurance and banking systems;  | National Bank, Ministries of Finance, Taxation Revenues, Economy, Industry and Trade, State service for Insurance Supervision                    | 2001-2002 |  |
|   | To promote competitive environment, to reinforce the supervision over natural monopolies and to perfect State-regulated tariff rate defining mechanisms.               | Ministry of Economy, Industry and Trade (Antimonopoly Service, Price Inspection)   | 2001      |  |
|   | To define more strict responsibilities for violating agreements with investors.  | Ministry of Justice  | 2001      |  |
|   | To promote expansion of the leasing companies' net.  | National Bank, Ministry of Economy, Industry and Trade   | 2002      |  |
| Provide efficient consumption of the industrial sector potential, create new working places | To define and to carry out optimal strategy for the State-owned property privatization.  | Ministry of Property Management and corresponding Ministries   | 2003      |  |
|   | To accelerate the process of enterprise restructuring, to increase efficiency of the State property management and to perfect procedure and legislation on bankruptcy. | Ministries of Property Management, Economy, Industry and Trade, corresponding Ministries   | 2001-2002 |  |
|   | To promote small and medium business development.  | Ministries of Economy, Industry and Trade, Finance and corresponding Ministries  |           |  |
|   | To promote social-economic development of the regions due to State programs and to provide maximum realization of regions' potential.                                  | Local boards of management, Ministries of Economy, Industry and Trade, Finance, Taxation Revenues, Transport and Communications, Fuel and Energy | 2003      |  |
| Shadow economy  | To carry out program towards legalization of shadow economy in the sectors of national economy.  | Ministry of Economy, Industry and Trade and corresponding Ministries   |           | Reduce share of shadow economy in GDP twice                                    |

|                                     |  |   |  |   |
|-------------------------------------|--|---|--|---|
| Promote industry development        | To provide State promotion of processing industry oriented on local raw-material basis and import replacing production.  | Ministry of Economy, Industry and Trade and corresponding Ministries                                  |  | Industry output growth rate – 14% (2003);   |
|                                     | To promote perspective sectors oriented on Eurasian Transport Corridor service.  | Ministries of Economy, Industry and Trade, Finance and corresponding Ministries                       |  | Rise the share of processing industry in export by 20 points;                     |
|                                     | To promote introduction of progressive technologies.   | Ministry of Economy, Industry and Trade and corresponding Ministries                                  |  | Reduce of trade deficit by 2003 twice.  |
|                                     | To provide production vital for country's population.  | Ministries of Economy, Industry and Trade, Finance, Agriculture and Food and corresponding Ministries |  |   |
|                                     | To promote the process of restructuring of post-privatized enterprises and to ensure full capacity operation of promising enterprises.   | Ministries of Property Management, Economy, Industry and Trade and corresponding Ministries           |  |   |
|                                     | To perfect State procurement mechanisms and rational allocation of the State orders among industrial enterprises.  | Ministries of Economy, Industry and Trade, Finance and corresponding Ministries                       |  |   |
| Transport and communication systems | To guarantee functioning of the Eurasian Transport Corridor with full capacity through Georgia by defining freight turnover and hence define the main trends for the separate sectors of transport sphere (with corresponding infrastructure); | Ministries of Economy, Industry and Trade, Transport and Communications                               |  | 5.5% growth rate in the freight turnover for all kinds of the transport for 2003; |
|                                     | To develop the railway traffic freight and to provide its security and to bring this sphere into line with modern demands;   |   |  | Investments in the road-building (growth % rate);                                 |
|                                     | To carry out and to implement in a short run the strategy for overcoming the crises existing in the seaworthy and provide detailed reflect seaworthy-trade fleet in the economic data;   |   |  | !9% growth rate in the outcome Communications and Postal service;                 |
|                                     | To accelerate rehabilitation and modernization of the roads and to bring them to the international standards;  |   |  | Number of the telephone users   |
|                                     | To implement the process of privatization, to promote healthy competitive environment on the basis recommendations of international organizations and to provide maximum transparency to the process of investment;                            |   |  |   |
|                                     | To promote the modernization of obsolete telephone network in rural areas and to provide the telecommunication sector with modern equipment;   |   |  |   |

|                                     |   |  |  |  |
|-------------------------------------|---|--|--|--|
| Fuel and energy complex             | To promote the investments in the hydro-energy sector   | Ministries of Economy, Industry and Trade, Fuel and Energy               |  | 18% growth rate of the industrial production in the field;<br><br>Power-capacity of the industrial production (%).         |
|                                     | To introduce flexible tariff system for the power and natural gas consumption taking into account seasonality and entrepreneurs' interests;   |  |  |  |
|                                     | To get rid of the obsolete and non-vital power equipment, to promote the modernization of equipment, which more or less meets the modern requirements due to agreements with the privatized power facilities' owners; |  |  |  |
|                                     | To accelerate privatization of natural gas and power distribution system, also of the liquid gas storage facilities;  |  |  |  |
|                                     | To promote the development of non-traditional energy sector (namely wind energy usage);   |  |  |  |
| Constructive activities development | To perfect the normative basis and to bring it into line with the demands of the market economy;  | Ministries of Economy, Industry and Trade, Construction and Urbanization |  | Constructive outcome growth rate – 20% (housing construction – 26%);<br><br>Investments in the fixed capital.              |
|                                     | To establish progressive entrepreneurial structures in the constructive sector, to promote the process of decentralization, demonopolization and to establish competitive environment;                                |  |  |  |
|                                     | To modernize construction industry and building materials, to promote of investments;   |  |  |  |
|                                     | To elaborate flexible measures for informal sector legalization in the field and their further implementation;  |  |  |  |
| Municipal service development       | To reorganize the municipal service and to provide improvement of the sanitation-technical conditions and sewerage system;  |  |  | Growth rate of investments in the field; percentage of population with access to safe water and to adequate sanitation     |
|                                     | To promote investments in the field;  |  |  |  |
|                                     | To perfect existing tariff policy;  |  |  |  |
| Tourism promotion                   | To encourage attraction of private investments oriented towards the Eurasian transport corridor service;  | Ministry of Economy, Industry and Trade, State Department for Tourism    |  | Outcome growth rate – 87%;<br><br>Number of tourists per year – 800 thousands;<br><br>Volume of investments in the sector. |
|                                     | To introduce new progressive forms of tourist service taking into account natural potential of the country and other specific terms;  |  |  |  |
|                                     | To promote small and medium business development;   |  |  |  |
|                                     | To accelerate definition of the sanitation protection zones;  |  |  |  |
|                                     | To promote development of the health-resort sectors and implement necessary measures for the development and preservation of natural and healing resources;   |  |  |  |



|  |   |   |           |  |
|--|---|---|-----------|--|
| Promote regional social-economic development | To coincide the development programs for separate sectors with regional and complex targeting programs for the social-economic development of the territorial units;                      | Ministry of Economy, Industry and Trade, Administrations of corresponding territorial units |           |  |
|  | To register economic potential of the separate territorial units and promote the realization of measures oriented towards development;  |   |           |  |
|  | To promote development of the regions with low economic potential (highlands, etc.).  |   |           |  |
| <b>Agriculture Sector</b>                    |   |   |           |  |
| Infrastructure and material-technical base   | To rehabilitate irrigation and drainage systems;  | Ministry of Agriculture and Food  | 2005      |  |
|  | To establish Water Users Associations, to preserve the State responsibility of functioning/repairing of only primary systems, to privatize secondary systems by Water Users Associations; |   | 2005      |  |
|  | To attract international investments for rehabilitation of main structures, main and distribution canals and pumping stations;  |   | 2005      |  |
|  | To rehabilitate rural roads and to build the new ones;  |   | 2001-2010 |  |
|  | To support the formation of regional wholesale markets;   |   | 2001-2010 |  |
|  | To elaborate the program of providing farmers with agricultural machinery and trailers with participation of donor countries and organizations;   |   | 2001-2003 |  |
|  | To establish private service centers and centers with combined form of ownership in collaboration with government;  |   | 2001-2005 |  |
|  | To orient on purchase of comparatively cheap and qualitative agricultural machinery, that will give possibility to service to renew the depreciated machinery on their own;               |   |           |  |
| Develop of agro-processing enterprises       | To support the establishment of local product promotion and advertising network   | Ministry of Agriculture and Food  |           |  |
|  | To enlarge market of local products;  |   | From 2001 |  |
|  | To cooperate with respective state organizations for strict control of useful and dangerous material tolerance in the products;   |   |           |  |
|  | To promote attraction of investments.   |   |           |  |

|  |  |                                  |           |                                |  |
|--|--|----------------------------------|-----------|--------------------------------|--|
| Soil fertility preservation            | To activate the correspondent legislation, to introduce the more efficient methods of machinery utilization and technologies, to crop rotation, to proper utilization and protection of soil, to elaborate seed rotation system, suitable for small farms; | Ministry of Agriculture and Food | 2001-2003 |                                |  |
|  | To implement plant and animal protection timely, To conduct variety of testing actions in accordance with internal and international standards;  |                                  |           |                                |  |
| Formation of agriculture credit policy | To promote the process of formation credit unions, cooperatives, to implement governmental efforts to establish guarantee funds;   | Ministry of Agriculture and Food | From 2001 |                                |  |
|  | To receive international financial help for development of credit relations, to impose control on financial resources for credit relations and conduct analysis in order to avoid inefficient expenditures;  |                                  |           |                                |  |
|  | To establish close cooperation with world's leading agricultural banks and to share their experience;  |                                  |           |                                |  |
|  | To create necessary economic conditions that will provoke commercial interest of credit institutions to establish regional offices;  |                                  |           |                                |  |
|  | To improve insurance mechanisms in agriculture;  |                                  |           |                                |  |
| Improvement of land management         | To privatize State-owned not rented agricultural lands – total area 100.6 thousand ha, of which: 48.0 thousand ha is arable land, 20.7 thousand ha – land under perennials and 31.9 thousand ha – grasslands;  | Ministry of Agriculture and Food | 2001-2002 |                                |  |
|  | To privatize rented agricultural lands due redemption – total area 259.7 thousand ha, of which: 178 thousand ha is arable land, 22.6 thousand ha – land under perennials and 59.1 thousand ha – grasslands;  |                                  |           |                                |  |
|  | To complete introduction of multi-purpose cadastre and land registration system;   |                                  | From 2001 | 2005                           |  |
|  | To improve legislative base (elaboration of draft laws on further privatization of agricultural lands, cadastral and information systems, land evaluation and differentiation of land management powers);  |                                  |           | 2000-2001                      |  |
|  | To elaborate state targeted program of soil fertility upgrading and to identify respective sources of finance;   |                                  |           | As soon as resources are found |  |
|  | To involve banking and insurance system in land real estate market;  |                                  | 2000-2005 |                                |  |

|   |   |   |             |  |
|---|---|---|-------------|--|
|   | To develop private institutions, which will join the soil specialists, surveyors and lawyers;   |   | 2000-2005   |  |
|   | To support cooperation of small landowners and to consolidate land;   |   | Permanently |  |
| Regional development                                  | To establish regional and district consultative centers for farmers;  | Ministry of Agriculture and Food, and local administration  | 2001-2003   |  |
|   | To develop land and other natural resources utilization rules and actions of their upgrading on regional level;   |   | 2001-2003   |  |
|   | To elaborate specific program of poverty elimination in mountainous regions and its stepwise implementation;  |   | 2000-2010   |  |
|   | To estimate the potential of agro-tourism sector and to elaborate state strategy for its activation;  |   | 2001-2002   |  |
| Agrarian research and farmer's training development   | To train farmers and producers in planning of their farms, mobilization of personal savings and establishment of direct relations with credit institutions;   | Ministry of Agriculture and Food, and local Administrations | Since 2000  |  |
|   | To establish effective consultative centers for farmers;  |   | 2001-2004   |  |
|   | To establish specialized "summer camps" for students in order to ensure agricultural orientation among them;  |   | From 2001   |  |
| Tax and Customs Code                                  | To optimize existing regime;  |   |             |  |
|   | To consider liabilities taken before the World Trade Organization;  |   |             |  |
| Development of environment protection and health care | To conduct institutional improvement and restructuring of schemes in the sphere of drinking water supply and cleaning in urban area, to find out additional ways of subsidizing the mentioned sector oriented towards real consumption; | Ministry of Environment Protection and Natural Resources    |             |  |
|   | To elaborate and to implement the State program oriented towards gas quality's improvement;   |   |             |  |
|   | To evaluate and to improve existing waste's allocation system;  |   |             |  |
|   | To evaluate resorts and find out the ways of improvement.   |   |             |  |
| Management of natural and anthropogenic disasters     | To conduct preventive measures to avoid essential environmental crisis;   | Ministry of Environment Protection and Natural Resources    |             |  |
|   | To elaborate natural disasters' forecasting and preventive mechanisms;  |   |             |  |
|   | To elaborate state programs and mechanisms in order to reduce the results of natural disasters and environmental crisis.  |   |             |  |

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| Provision of sustainability towards environmental factors, which are the base for income                  | To preserve and to improve natural resources base's fertility (Continuing the project of protected territories taking into account social components);   | Ministry of Environment Protection and Natural Resources |  |  |
|   | To consider environment protective factors in taxation State policy;   |  |  |  |
|   | To improve planning in the sphere of environment protection (further perfection of legislative base on evaluation of impact on environment, elaboration of evaluation strategies for regional projects); |  |  |  |
|   | To access mechanisms of the risk reduction (micro credit, insurance) because of the environmental situation;   |  |  |  |
|   | To define the vulnerable sectors and groups (in case of climate changes) and to elaborate the mechanisms of prevention and compensation;   |  |  |  |
|   | To provide detailed analysis of deserting process and prepare short and long period forecasts, to elaborate the State and regional programs against deserting;   |  |  |  |
|   | To implement the complex of measures oriented against soil erosion process;  |  |  |  |
|   | To support the small scale renewable energy sector development, especially in far regions with low income (nontraditional energy sources);   |  |  |  |
|   | To create instructions for housekeepers and small enterprises about the prudent and effective usage of energy;   |  |  |  |
|   | To work out and to recommend economical facilities for air cleaning;   |  |  |  |
|   | To provide the development of small scale local and private water supplying and water cleaning systems;  |  |  |  |
|   | To elaborate the strategy about pesticides' and plant protection.  |  |  |  |
|   | Increase of environmental protection and control management  |  | To conduct institutional restructuring and to optimize Ministry of Environment Protection and Natural Resources, to improve the role of regional entities; | Ministry of Environment Protection and Natural Resources |
| To rise public awareness about environmental issues, to create permanent information centers;             |  |  |  |  |
| To cooperate with mass media in order to provide population with full information about mentioned issues; |  |  |  |  |
| To use participatory process in decision making, to implement Arhus Convention.                           |  |  |  |  |

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| Development of forestry  | To privatize about 10% of total forest areas step wisely (about 300 thousand ha);  | Ministries of Environment Protection and Natural Resources, Agriculture and Food, State Forestry Department | Gradually  |  |
|  | To develop timber processing and furniture production sectors;   |   | Since 2002 |  |
|  | To regulate activities of current milling workshops;   |   | 2001       |  |
|  | To activate the Forestry Sector Development Project, elaborated under the aegis of the World Bank. Its implementation is planned for 2001-2008 using the World Bank 40 years preferential credit of USD 20 millions; |   | 2001-2008  |  |
|  | To develop targeted and specialized plantations (trees of walnut, hazelnut, pecan, almond, acacia, wild rose, fir-tree, pomegranate, laurel, mulberry, chestnut).  |   | 2001-2011  |  |
| <b>Governance, Public Administration Reform and Fight Against Corruption</b>   |  |   |            |  |
| Liberalization of business environment   | To optimize system of controlling organizations;   | Chamber of Control  | 2001       |  |
|  | To craft transparent mechanism on issuant licenses and permissions for the entrepreneurial activity;   | Ministry of Justice   | 2000       |  |
|  | To liberalize tax rates and strict tax administration;   | Ministry of Finance   | 2000-2001  |  |
|  | To arrange the financial accounting procedures and simplify the assignation;   | Ministry of Finance   | 2001       |  |
|  | To simplify and to perfect system of standardization and certification;  | Ministry of Economy, Industry and Trade   | 2001       |  |
|  | To increase effectiveness of Anti-Monopoly legislature;  |   | 2001-2003  |  |
|  | To implement consistent legalization program of shadow economy drafted by the Ministry of Economy, Industry and Trade;   |   | 2001-2003  |  |
| To strict criminal liability for unjust competition, falsification and other economic misdemeanors in order to protect rights and interests of honest entrepreneurs; | Ministry of Justice  | 2001  |            |  |
| Increase Public Administration effectiveness   | To increase wages of Public servants by increasing budget incomes and decreasing number of Public servants;  | Ministry of Finance   | 2001-2003  |  |
|  | To craft mechanism to analyze and to check date provided in officials' financial and property declaration;   | Chamber of Control  | 2001       |  |
|  | To strength liability for not accomplishing obligations embraced in Administrative Code, for violating legislature about information freedom and for not performing tasks;   | Ministry of Justice   | 2001       |  |
|  | To ensure material and disciplinary liability of those officials that have brought damage to Georgian citizens and State by their activity;  |   | 2001       |  |
|  | To strength judicial services in supreme governmental structures;  | Corresponding Ministries  | 2001       |  |

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|------------------------|--|--|-----------|--|
|                        | To bring Charters of governmental agencies in correspondence with the Constitution, law about “The Structure and Activity of Executive Authority” and law about “Budget System and Authority”;                                     | Bureau of the State Service                      | 2001      |  |
|                        | Structural unification of functions through adoption of standardized charters for the Ministries and State Agencies  | Ministry of Justice, Bureau of the State Service | 2001      |  |
| Law-enforcement system | Structural and institutional reform (to perfect external and internal control mechanisms, to eradicate redundancy and alleviate from superfluous and inconsistent functions, to adopt unified system for misdemeanors accounting); | Law Enforcement Bodies                           | 2001      |  |
|                        | Personnel reform (to optimize structure and number of staff, to implement public qualification examinations, to draft unified criteria for hiring and promotion and to establish competition system to held a position);           | Law Enforcement Bodies                           | 2001      |  |
|                        | To ensure material-technical and financial base (computerization of working process, increase wages);  | Law Enforcement Bodies, Ministry of Finance      | 2001-2003 |  |
| Justice system         | To improve criteria for judge selection;   | Supreme Court of Georgia                         | 2001      |  |
|                        | To draft long-term training program for judges;  |  | 2001      |  |
|                        | To implant modern methods of case management in courts;  |  | 2001      |  |
|                        | To adopt code of ethics for judges.  |  | 2001      |  |