

Georgia

Status Index (Democracy: 6.10 / Market economy: 5.36)		5.73	Management Index		5.91
HDI	0.732		Population	4.6 m	
GDP p. c. (\$, PPP)	2,588		Population growth²	-0.3%	
Unemployment rate¹	11.6%		Women in Parliament	9.4%	
UN Education Index	0.90		Poverty³	2.7%	
			Gini Index	36.9 (2001)	
Source: UNDP: Human Development Report 2005. Figures for 2003 – if not indicated otherwise. ¹ IMF Country Report 2005. ² Annual growth between 1975 and 2003. ³ Population living below \$ 1 (2001).					

A. Executive summary

Democratic and economic transition in Georgia have been stalled since 2001. In its response to internal splits and the emergence of an uncontrollable opposition, the performance of the Shevardnadze government deteriorated in nearly all policy areas. Even though the country had previously been known for its liberal climate, harassment of politically active NGOs and independent media outlets became a new norm in Georgia. Though the government made the manipulation and transgression of democratic rules a new habit, it stopped short of abolishing these rules altogether. Progress toward a market economy was severely hampered by pervasive corruption and declining fiscal and budgetary discipline. The notorious failure to consolidate state finances alienated the international donor community, which finally decided to withdraw support in 2003, thus breaking the backbone of the Shevardnadze government.

The success of the so-called “Rose Revolution” added a decisive twist to the development of Georgia. The new government has made tremendous efforts to revamp stalled structural reforms and dismantle systemic corruption. After one year in office, progress has been made in many areas, including in fiscal performance and law enforcement. The government has contributed to a strengthening of state structures and the reemergence of a rudimentary trust in official institutions. The adoption of a new tax code is expected to result in the creation of an environment conducive to investment and business development.

The challenge of consolidating democracy lies still ahead, however. To secure the success of early achievements, more efforts are needed to overcome the heritage of a deeply entrenched clientelistic culture. There is still no party system in place that is capable of articulating and aggregating social interests. Most civil society organizations are donor driven advocacy groups, far removed from the social groups they claim to represent. Local government bodies still lack the resources and the competencies necessary to function effectively. So far, the current government is backed by a rather vague popular sentiment. It cannot rely on organizational structures for support. The ruling party is a rather fragile umbrella

movement, consisting of the personal entourage of its three leading figures and is thus highly vulnerable to internal fragmentation. It still does not have any appeal at the local level and does not serve as a recruitment pool for local administrators. Against the backdrop of all these institutional deficiencies, destabilization remains a viable possibility.

B. History and characteristics of transformation

Political and economic transformation in Georgia clearly lacks a linear dynamic toward the consolidation of democracy and a market economy. Under the heavy burden of two unresolved ethnic conflicts and sharp economic decline aggravated by pervasive corruption and extremely weak state structures, Georgia's development has been marked by a series of interruptions and setbacks.

The first breakthrough to a democratic political regime in Georgia was accomplished with the parliamentary elections of October 1990, won by a heterogeneous umbrella movement under the leadership of former dissident Zviad Gamsachurdia. Despite his landslide victory in the May 1991 presidential elections, he failed to consolidate his rule. His power rested mainly on charismatic mobilization. He missed the opportunity to build up a coherent political organization. As a result, he was easily driven from office by a violent coup d'état at the beginning of 1992.

The brief interlude of chaos that ensued after the ouster of Gamsachurdia was terminated with the return of former party head Eduard Shevardnadze, who assumed the newly created position of head of state in March 1992. In the first three years of his rule, Shevardnadze was mainly occupied with the restoration of public order. He tried hard to get rid of the competing gangs of criminals that had originally placed him in power. The adoption of a constitution and the successful organization of elections in 1995 signaled a fragile consolidation. Notwithstanding quite impressive achievements in terms of ending violence and introducing the formal requisites of democratic statehood, and despite massive international assistance, Shevardnadze did not succeed in basing his rule on stable institutions. His political survival depended heavily on the application of two strategies, both of which placed certain constraints on the consolidation of democracy.

Firstly, he used access to administrative resources and to international development funds as a means to accommodate fluid clientelistic networks. The government thus never acted as a coherent team. Severely weakened by frequent reshuffles, the government gained notoriety for its fierce competition over the distribution of spoils between different ministries. With few exceptions, parliament fell short of fulfilling its oversight functions. Many of its members took part in corruption games by using their regulatory power as a means to grant exemptions to interested clients.

Secondly, Shevardnadze manipulated and frequently changed procedural norms regulating access to power. The only continuous feature was a clear dominance of the executive, which was firmly controlled by Shevardnadze. In contrast, the shape of parliament was adapted to varying needs. Until 1995, the abolishment of any kind of threshold ensured a highly fragmented legislature. After the creation of the Civic Union of Georgia (CUG) in 1993, which was designed to serve as Shevardnadze's party of power, the introduction of a barrier bestowed a stable majority on the CUG. Pluralism was thus mainly confined to intra-elite competition inside the ruling party, which was composed of former Soviet apparatchiks and a group of young reformers.

These two strategies ceased to function effectively after 2001. The distribution of official fiefdoms among the different cliques of the elite severely hampered economic growth and thus gave rise to popular unrest. As the international donor community became aware of the increasing gap between legal fiction and corrupt practices, it demonstrated a growing reluctance to continue funding assistance programs. Confronted with a decline in its authority, the ruling party was compelled to adopt authoritarian measures, a move that provoked an internal split. The attempt to crack down on the independent TV station Rustawi 2 in October 2001 became a turning point. Prominent representatives of the young reformers, headed by Saakashvili, Zhvania and Burjanadze, formed a new opposition that assumed power in the aftermath of popular protests against the rigging of parliamentary elections in November 2003.

The relative ease with which Shevardnadze was overthrown can be explained partly by the existence of democratic facades erected under his rule. A dense network of NGOs, which had mushroomed during the 1990s, carried out parallel vote counts and organized public protests. Independent media outlets, which had never experienced serious threats to their existence, supported popular mobilization by providing uncensored information. An independent judiciary, established under the influence of the young reformers, canceled the officially announced results.

After the peaceful revolution, the triumvirate of Saakashvili, Burjanadze and Zhvania rushed to stabilize the situation. With Saakashvili's overwhelming victory in the January 2004 presidential elections and with control of 90% of the seats in parliament, the new elite was awarded with a more than comfortable starting point. Control over the executive and the legislative branch of government makes implementation of the far-reaching reform agenda a much easier job. However, the reformers have still failed to translate the nearly charismatic legitimacy they enjoy into organizational capacity. Despite outstanding achievements in terms of curbing corruption and strengthening weak governance structures, it is far too early to speak of a successful consolidation of stateness.

C. Assessment

1. Democracy

1.1. Stateness

Georgia's stateness is cast into doubt by the total loss of control over the separatist territories of Abkhazia and South Ossetia. To date, all efforts achieve a resolution to these conflicts have failed. In addition, the political stalemate in the unrecognized Republic of Abkhazia following the disputed presidential elections of October 2004 and the resulting political vacuum are likely to produce a spillover effect in the neighboring regions of Samegrelo and Imereti in western Georgia. The personal representatives of President Saakashvili have made anti-corruption efforts in both regions a high priority. Despite some successes, raids often fail because of the collusion between local law enforcement agencies and criminal groups. Similar problems exist in Shida Kartli, the eastern Georgian region bordering South Ossetia. Attempts to crack down on smuggling have triggered a violent response, including a car bombing at the administrative center of Gori in January 2005. This situation exposes the underlying weakness of Georgia's regional political institutions, which lack a popular mandate.

In the territory controlled by the Georgian state, all citizens have the same civil rights. The integration of the South Ossetian and Abkhazian population, however, remains a problem as the people of those territories do not accept Georgian rule.

Though there is a separation of church and state, the Orthodox Church enjoys special treatment. Its status is regulated by a controversial concordat signed in October 2002, which provides for various privileges, such as the provision of religious education in schools and broad powers to decide on the status of other religious communities. This degree of influence enabled the Orthodox Church to prevent the signing of an agreement between the state and the Catholic Church. Georgia is the only former Soviet Republic without a law defining the rights and obligations of religious communities.

There is a set of administrative structures in place, but despite some tangible improvements, the efficiency of these structures is still hampered by a heritage of corruption, the sheer size of the shadow economy and a lack of funds.

1.2. Political participation

There are no restraints on free and fair elections at the national level. On the local and regional level, elections have been delayed and representatives are appointed by the central government.

The government's effective power to rule is not constrained by visible veto powers. However, its ability to ensure implementation of decisions is still disputed.

There are no restrictions on freedoms of association and assembly, although there have been some reports of the excessive use of force by police to breakup demonstrations.

Though freedom of press and opinion is formally institutionalized, there are deep concerns regarding massive intervention by the state in the media sector. Numerous reports cite examples of reprisal against journalists and media outlets. For example, immediately after presidential elections in January 2004, three independent TV stations cancelled their late night talk shows, all of which were well known for their critical commentary on political events. The TV station Rustavi 2, which gained prominence for the active support it provided to the leaders of the so-called Rose Revolution, appears to enjoy preferential treatment, including receiving a generous offer by the state to reschedule its debts. Other stations suspected of having close ties to the Shevardnadze regime, however, have been subjected to government raids on the basis of accusations of tax evasion, for example. Despite these shortcomings, the existence of a pluralistic media scene is not under threat.

1.3. Rule of law

Even though the powers of the executive, legislative and judicial branches of government are institutionally differentiated, the proper functioning of a system of checks and balances is hampered on two different levels. On the one hand, the amendments to the constitution adopted on February 6, 2004 have decisively enhanced the authority of the executive. The amendments granted the president the right to dissolve parliament if legislators fail to approve the state budget in three successive votes and as well as the right to appoint judges. On the other hand, the stable majority of the pro-presidential "National Movement – Democrats," which controls 90% of the seats in parliament, acts as a constraint on the legislature's ability to exercise its oversight functions. The establishment of an upper chamber of parliament has been further postponed until the settlement of the unresolved conflict with the separatist territories of Abkhazia and South Ossetia.

The decision of the Supreme Court to cancel the results of the rigged parliamentary elections of November 2, 2004 serves as proof of the independence of the judiciary. However, a draft bill presented by the president in December 2004, which calls for the possibility to dismiss Supreme Court and Constitutional Court judges before the expiration of their terms, hints at serious attempts on the part of the executive to regain control over the judicial branch.

The current government is displaying serious intentions to address the problem of pervasive corruption. A number of high profile arrests serve as proof of these intentions. However, some Georgian NGOs have expressed concern that the authorities are selectively targeting certain individuals for political reasons and that the law is not being applied equally to all.

To some degree, civil liberties seem to be negatively affected by the revolutionary style of implementing far-reaching reform measures. Particularly in the context of the struggle against corruption, the limits set by laws are not always respected. Examples of this include allegations of due process violations including torture and ill-treatment.

1.4. Stability of democratic institutions

Existing democratic institutions still have to strive for stabilization. The fragility of Georgia's democratic institutions are underscored by the series of re-organizations since the inauguration of President Saakashvili in January 2004, frictions between different government ministries on questions such as the proper strategy regarding the separatist territories of Abkhazia and South Ossetia, and ongoing rumors about rising tensions inside the pro-presidential camp, which have been aggravated further by the mysterious death of Prime Minister Zhvania in January 2005.

The existing democratic institutions are mostly accepted by all relevant political and social players. Some NGOs do take a critical stance with regard to the strengthening of executive powers. The downsizing of government agencies, the anti-corruption drive and the attempt to curb smuggling has encountered some resistance on the part of those being targeted by these measures. This is, however, counter-balanced by widespread popular support.

1.5. Political and social integration

The existing party system is still marked by a high degree of fluidity and a low level of social entrenchment. Deprived of access to administrative resources, the Civic Union of Georgia, which had dominated the political scene between 1993 and 2001, has ceased to exist. The bloc "For a new Georgia," cobbled together by Shevardnadze in 2003 in a desperate attempt to regain control through a merger of former rivals, fell apart immediately after the Rose Revolution. The ouster of Adzarian strongman Abashidze in March 2004 has inflicted the same fate on the coalition of parties grouped around his "Union of Democratic Revival," which polled second in the parliamentary elections of 1995, 1999 and 2003.

The only parties with a longer record of existence to gain representation in the new parliament elected in March 2004 are "New Rights" and "Industry will save

Georgia,” which united in a single bloc called “Right Opposition” and gained 7.56%. In contrast, the components of the ruling coalition “National movement - Democrats,” which heavily dominates the current legislature with a share of 90% of the seats, emerged only in the wake of the highly contested elections in November 2003. However, due to a quite high threshold of 7%, the fragmentation of the existing party system is effectively restricted. Its main feature is a lack of social rooting and a high degree of voter volatility. With the exception of the “Right Opposition,” which represents the interests of a small layer of entrepreneurs, the existing political forces do not reflect social interests but rather quite vague popular sentiments. Since the CUG and UDR have dissolved, none of the remaining political parties has the organizational structure to reach local levels.

The influence of classical social interests groups is close to zero. Trade unions do exist, but with the possible exception of the solidarity organization of schoolteachers, they are hardly visible. This is primarily due to high rates of unemployment and self-employment. As the few bigger entrepreneurs still prefer informing bargaining to promote their interests, organizations representing business interests are of no real significance. Civil society organizations in contrast form a dense network. However, their capability to act as mediators between society and the state is severely constrained by their lack of social rooting. Moreover, since the Rose Revolution and the appointment of many of their most active members to government positions, they have experienced a kind of brain drain. Thus, the consolidation of democracy and even the development of a sustainable reform strategy are still hampered by the fact that large social interests remain underrepresented.

Popular support for democracy is quite high. In an opinion poll carried out in 2003, 73% of respondents agreed to the statement that democracy is better than any other form of government. However, the fact that freedom of speech and self-rule ranked quite low among the items associated mostly with democracy raises some questions with regard to the sustainability of this strong commitment.

Due to a deep-rooted culture of clientelism, until recently reliably reproduced by an institutional incentive structure that gave priority to informal bargaining over the distribution of spoils, vertical bonds of dependence are still regarded as the most effective means of pushing through one’s interests. The emergence of authentic forms of social self-organization is thus severely impeded by widespread distrust. Until recently, anyone who claimed to represent broader societal interests was immediately suspected of simply pursuing his own narrow agenda of personal interests. The existence of NGOs does not in and of itself dispel this common perception as their emergence is mainly donor driven. Moreover, most NGOs resemble advocacy groups staffed by urban intellectuals whose bonds to the interests of those they claim to represent are very loose.

2. Market economy

2.1. Level of socioeconomic development

The level of socioeconomic development is remarkably low even in comparison to average CIS standards. With \$830, GNI per capita amounts to less than one third of the respective Russian value. Despite considerable growth rates of up to 8% in previous years, the Georgian economy has still not recovered from the deep shock it experienced following the break-up of the Soviet Union and the civil wars of the early 1990s. By 2002, the economy had contracted to 38% of its adjusted GDP purchasing power in 1989. Fifty-four percent of the population lives below the poverty line and approximately 15-17% are extremely poor. Poverty is unequally distributed throughout the country. In many cases, higher poverty levels correlate with geographical isolation and low density of arable land. Structural causes of poverty include a high rate of unemployment and obstacles to the growth of the agricultural sector, which employs more than 50% of the physically active population but contributes only 21% to the GDP.

2.2. Organization of the market and competition

The institutional foundations of a market economy were established in the early 1990s. The price system is fully liberalized, subsidies to state enterprises have been abolished and restrictions to foreign trade were removed with the introduction of uniform custom duties before Georgia joined the WTO in 2000. However, until recently, informal practices as well as formal regulation contributed to a massive distortion of competition. On the one hand, pervasive corruption had ensured selective application of ostensibly uniform rules. Entrepreneurs closely linked by personal ties to members of the political elite were regularly granted exemption from enforcement of a wide range of regulations. Examples include an astonishingly high degree of tolerance toward tax arrears and overdue payments to state-owned utilities. On the other hand, a contradictory tax code, which listed 21 different taxes and provided for a lot of exceptions valid only under highly specific circumstances, created the loopholes necessary for granting privileges to some while penalizing others. Consequently, the share of the informal economy had surpassed 67% of all productive activities according to even conservative World Bank estimates.

Despite the existence of anti-monopoly legislation strongly prohibiting the creation of market access barriers, individual entrepreneurs were successfully shielded from competitive pressures for many years.

Notwithstanding a substantial liberalization of the formal regime, the ability to engage successfully in foreign trade activities was generally confined to a privileged class. Politically influential business circles gained advantages through informal exemptions from the payment of customs duties. Moreover, the issuing

of licenses, required for the import of certain goods, provided yet another possibility for state intervention in favor of certain clients.

Against the backdrop of such a poor starting point, the ambitious reform agenda launched by the new government surely needs time to produce tangible results. However, initial progress in terms of giving all businesses fair opportunities to compete is already visible. Widespread smuggling, tax evasion, bribery and other forms of abuse of power are being combated through harsh sanctions. In terms of structural improvements, the adoption of a simplified tax code, which would reduce the number of taxes from 21 to eight, is expected to reduce the level of corruption as well as the scope for arbitrary action on part of the tax officials.

Reform of the banking sector began in 1995. The state has largely divested itself of banks. The National Bank of Georgia has assumed a supervisory role and increasingly imposes stringent reporting requirements on commercial banks. Despite these steps, the banking sector continues to display a number of structural deficits. It remains focused on short-term lending rather than on long-term finance. At 7.5%, the share of non-performing loans was still quite high at the end of 2003. Moreover, nine banks – comprising one-tenth of total bank assets – were rated CAMEL 3 or worse. The fact that only 3% of Georgians have bank accounts reflects widespread mistrust in the financial stability of the institutions.

However, regulatory and supervisory measures taken by the current government have already started to improve the health of the banking system. In less than one year, the share of non-performing loans in the total portfolio declined by 2.1%. In compliance with statutory requirements and in line with European standards, banking institutions are mandated to raise their capital to at least 12 million lari by the end of 2008. Whereas these steps will probably suffice to facilitate further consolidation of the system and to filter out weak and financially non-viable banks, the most salient problem – the lack of incentives for the issuing of long-term credits – still has to be addressed.

2.3. Currency and price stability

Since the crisis of the early 1990s, macroeconomic stabilization has been a top priority for all Georgian governments. In the last few years, external debt never dropped below 50% of GDP and the fiscal deficit constantly hovered around 2.5% of GDP. However, the generally prudent and stringent interventions of the National Bank – the independence of which has never been questioned – kept inflation under control and ensured stable currency exchange rates.

Since Saakashvili took office in January 2004, Georgia has adopted a clearly marked tendency toward more fiscal and budgetary discipline. Improvements have been put into place in all steps of the budgetary process. They include institutional safeguards that will render any relapses into old habits more difficult.

Efforts to strengthen tax administration and the crackdown on tax evasion resulted in a 37% increase in tax receipts. A new law on the budget systems, which took effect in January 2004, has increased transparency in the execution of the budget through the introduction of a single treasury account. The law also extends the application of commitment controls to extra-budgetary funds. As a result, for the first time since independence, the year 2004 ended with an overall fiscal surplus of 2.1% of GDP - compared to a 1.8% deficit in the same period of 2003.

2.4. Private property

Formally, property rights are protected by law and there are legally prescribed procedures for the acquisition of property. However, there are problems with these rights in terms of implementation. Under Shevardnadze, property rights were often infringed during raids carried out under the pretext of tax evasion investigations. Contract enforcement through court decisions suffered as a result of extraordinarily high fees, which on average amounted to one-third of the debt's value. Privatization of state-owned property was rarely transparent. Many transactions were marred by the practice of clearing enterprise or state debt with the price charged for sale.

In 2003, the opposition fiercely attacked the Shevardnadze government for selling off parts of the country's energy sector to Russia's Gazprom and RAO EES. The new government has been praised for its promise to streamline procedures in accordance with official rules. It stepped back, however, from its original promise to renationalize those plants that had been sold at suspiciously low prices to individuals close to Shevardnadze. There have also been allegations of deviation from prescribed regulations with regard to the current sale of the Georgian Shipping Company and the manganese mining factory of Chiatura.

Private companies are permitted in Georgia, but currently more than 180,000 people (or nearly one-quarter of the workforce) are still employed by 1,800 state-owned enterprises. However, the new government unveiled a massive privatization plan, according to which all of these state-owned companies will be privatized by 2007.

2.5. Welfare regime

The social security system is not able to mitigate widespread poverty. There is no state support for the unemployed. Pensions and assistance paid to the approximately 300,000 internally displaced persons (IDPs) are far from sufficient for survival. Until recently, this form of assistance was also typically paid only after significant delay. The main problem facing the welfare system is not only a lack of funds, but also the government's failure to target the most vulnerable segments of the population. In view of the scarcity of resources, the maintenance

of uniform rates for pension and IDP allowances appears to be rather dysfunctional as it complicates attempts to reach the neediest. Additionally, corruption has distorted the effectiveness of the welfare system. Examples include embezzlement of allowances by state officials and trade in IDP documents.

Equality of opportunity is far from assured. The overall high level of poverty and unemployment deny some segments of the population equal opportunities. Typical high-risk groups include the elderly, families with a large number of children, orphans and persons with disabilities or chronic illnesses. People living in the poorest districts or remote areas with weak or no access to infrastructure and basic services are also at risk. Outside the capital, there are quite a number of places completely cut off from energy supplies during the winter months. Women have equal access to education, but are underrepresented in the political system.

2.6. Economic performance

Measured in terms of GDP growth rates, which have increased annually by more than 5% since 2000, the Georgian economy has performed quite well. This has been achieved mainly through extensive foreign investment in the construction of the Baku-Tbilisi-Ceyhan oil pipeline. The is figure contrasts, however, with a poverty rate that rose from 51.8% to 54.5% in the same period and with a negative trade balance that never dropped below 11% of GDP. Economic growth driven by single events rather than by structural improvements did not translate into a reduction of unemployment rates.

2.7. Sustainability

Ecological concerns are raised from time to time by environmental NGOs. The construction of the BTC oil pipeline, which is suspected to have a negative impact on a nature reserve near Borjomi, provoked protests by the local population. Given the heavy dependence on this project for economic growth, however, these concerns have been largely ignored by the government.

Due to years of neglect and under-financing, the education system Georgia inherited from the Soviet Union is at the verge of breaking down. State-run schools and universities not only suffer from a deteriorating physical infrastructure, but teaching staffs also earn extremely low wages. High rates of absenteeism among pupils are the norm. Bribery and the outright sale of diplomas is widespread, especially among university teachers. As a result, the quality of education is in sharp decline. There is a growing tendency toward the recruitment of individuals with university degrees from Western countries for elite positions.

3. Management

3.1. Level of difficulty

The level of structural difficulties faced by the political elite is quite high. One of the few advantages, the presence of a well-educated labor force, does not really pay off in the absence of reasonable expectations for economic recovery. Serious obstacles to economic growth include the interruption of transportation lines connecting the country to its main markets of sale and the loss of control over its borders. Both obstacles are hard to remove without a resolution to the conflicts in the separatist territories of Abkhazia and South Ossetia. As long as Russia does not abstain from the old strategy of exercising influence by means of backing the secessionist governments in Tskhinvali and Batumi, an effective solution to the problem is unlikely.

Notwithstanding the existence of a great number of NGOs, there is no authentic tradition of civil society in Georgia. A high degree of distrust in public institutions, which has resulted from a long history of foreign domination, acts as a severe constraint on the emergence of effective governance.

The level of conflict intensity is quite low at the moment. The social structure lacks stable and clear-cut cleavages. There are no organizations capable of mobilizing broader constituencies. There is the possibility for the re-emergence of entrepreneurs of violence with an interest in stirring up conflicts to their advantage.

Profile of the Political System

Regime type:	Democracy	Latest parliamentary election:	28.03.2004
System of government:	Parliamentary	Electoral disproportionality	6.8
		Effective number of parties:	2.9
1. Head of State:	<i>Eduard Shevardnadze</i>		
2. Head of State:	<i>Michail Saakashvili</i>	Cabinet duration:	02/2004-02/2005
Head of Government:	<i>Surab Shvania</i>		
3. Head of Government:	<i>Surab Nogaideli</i>	Cabinet duration:	02/05- present
		Number of ministers:	14
<p>Source: BTI team, based upon information by country analysts, situation in July 2005. Electoral disproportionality (Gallagher index) reflects the extent to which electoral rules are majoritarian (high values) or proportional: $\frac{1}{2} \sum (v_i - p_i)^2$; v_i is the share of votes gained by party i; p_i is the share of parliamentary mandates controlled by party i. Effective number of parties denotes the number of parties represented in the legislature, taking into consideration their relative weight (Laakso/Taagepera index) = $1 / \sum p_i^2$; p_i is the share of parliamentary mandates controlled by party i. Number of ministers denotes the situation on 1 January 2005.</p>			

3.2. Steering capability

The so-called Rose Revolution, which occurred in November 2003, marked a turning point in the political development of Georgia. Because this watershed event deeply affected the management capabilities of the administration that

followed, the periods before and after the ouster of former President Shevardnadze will be treated here separately.

Whereas the Shevardnadze administration not only lost the ability to formulate a long-term policy, but also the organizational coherence to achieve its short-term goals of strengthening its grip on power by authoritarian means, the new government of Saakashvili succeeded in consolidating its rule. After having taken power through a peaceful revolution, Saakashvili's government also took decisive steps toward the formulation and implementation of a highly ambitious reform agenda. Despite some shortcomings in terms of implementation, these measures were generally consistent with the aim of consolidating democracy and strengthening effective governance structures. Nevertheless, the continuing lack of vision for long-term economic recovery represents a weak point.

In the last phase of his rule, Shevardnadze was mainly concerned with a desperate struggle for political survival and consequently neglected implementing any kind of reforms. In the wake of the parliamentary elections in November 2, 2003, he hastily implemented ad-hoc measures primarily aimed at weakening the new opposition. Appealing to a population frustrated by economic hardship, frequent breakdowns of power supplies and pervasive corruption, the opposition movement gained in strength and was thus able to pose the first real challenge to Shevardnadze's claim to power since 1995.

Forced to act under the conditions of authentic pluralistic competition, the former president openly violated democratic norms without properly calculating the possible consequences in terms of losing international support and provoking popular protest. The relapse into an authoritarian style of rule clearly overstretched the capacity of a government bereft of coherent and efficient power agencies. The decision to target the vibrant NGO sector and independent media outlets, which were increasingly subjected to physical harassment, bureaucratic impediments and legal sanctions, served only to accelerate the galloping loss of credibility. In addition, the attempt to ensure electoral victory by means of organizing massive fraud served only to verify the shortsightedness of a government that failed to take into account the ability of the opposition to carry out parallel vote counts and mobilize popular protest.

The ease with which Shevardnadze was driven out of office on November 23, 2003 thus once more revealed the underlying weakness of his rule. Having honed his skills in the manipulation of organized pluralism between 1995 and 2001, Shevardnadze fell victim to authentic opposition forces that had blossomed behind the democratic facades erected under his rule. In this situation, he was neither able to regain popular and international support by the implementation of an effective reform policy, nor was he capable of adapting to changing circumstances by returning to authoritarianism. The steady loss of any kind of steering capability thus contributed heavily to his downfall.

After their rise to power, the new political forces under their charismatic leader Saakashvili launched an ambitious reform agenda aimed at restoring good governance and ensuring territorial integrity. The results are so far mixed. The government has taken important steps to improve public administration. In accordance with policy recommendations formulated by international donor agencies, it has begun to curb corruption, to crack down on smuggling, to downsize government agencies and to simplify a contradictory tax code.

The successful ousting of local strongman Abashidze has contributed to a solution to the strained relations and fiscal problems with the autonomous Republic of Adjara, which had been refusing to make fiscal payments into the central budget for years. As a result, state revenues have been raised significantly enabling the government to repay arrears in pensions and wages. Despite these impressive achievements, the Saakashvili administration has so far failed to invest in the build-up of legitimate and coherent institutions capable of reaching the periphery. This applies to both regional and local structures of governance as well as to the organizational structures of the ruling party. Deprived of a popular mandate and organized support, centrally-appointed politicians at the regional and local level are severely hampered in their fight against informal criminal groups that act partly in collusion with corrupt officials.

Emphasizing the urgency of necessary reform measures and making use of the charismatic legitimacy he enjoys, Saakashvili has so far given priority to strengthening his presidential powers. He has thus missed an opportunity to create a set of institutions that would be stabilized by procedural legitimacy and capable of mediating conflicts. As evidenced by the fate of the first Georgian President Gamsachurdia, this always entails the danger of falling victim to highly volatile public opinion, which may easily turn against Saakashvili as soon as unrealistic expectations are disappointed. In the realm of economics, the government has still not managed to design a long-term strategy to overcome structural deficits.

The Shevardnadze government displayed an astonishing low level of learning capabilities in the period under review. Despite a growing loss of credibility and a simultaneous increase in the strength of the opposition, it adhered to a harmful policy designed to keep it in power but actually contributed to its sudden downfall. The Shevardnadze government did not even respond to the alarming withdrawal of international support.

It is still too early to assess the flexibility of the Saakashvili government, which took power only one year ago and thus has had little time to reflect on its mistakes. Looking at the two top priorities of the current leadership, the evidence at hand is so far rather mixed. The successful combination of carrots and sticks in the fight against corruption is clearly indicative of innovations. With regard to the restoration of territorial integrity, the results are less impressive.

While the half-hearted decision to launch a small-scale invasion of the conflict zone near Tskhinvali in August 2004 may be interpreted as a relapse into the Shevardnadze style of politics, the renewed peace initiative of President Saakashvili suggests the opposite. For example, Saakashvili declared in January 2005 his readiness to grant the unrecognized Republic of South Ossetia greater autonomy within Georgia than the Republic of North Ossetia has within the Russian Federation. However, it is difficult to determine whether this move really means that the leadership has learned a lesson from its failed attempt to repeat the successful reintegration of Ajara under the completely different circumstances of South Ossetia or whether it only delineates another round in a policy characterized by permanent tactical shifts.

3.3. Resource efficiency

The resource efficiency of the Shevardnadze administration significantly deteriorated in the last phase of its rule. The near total breakdown of all reform efforts triggered not only a massive budget crisis but also severely strained relations with international financial organizations. The World Bank and IMF suspended their respective aid programs. In response to bureaucratic interference, the strategic investor AES Telasi which owned 16% of Georgian power generating capacities and managed 23% of the distribution networks, decided to leave the country. The subsequent decision to sell the heavily underfinanced Georgian energy sector to Russia's Gazprom and RAO EES provoked not only fierce attacks from the opposition, which feared the expansion of Russian influence, but also threatened to undermine Georgia's perspectives of becoming a strategic link in the energy corridor linking the Caspian Sea basin to Western markets.

Since the new government under Saakashvili assumed power, the situation shows clear signs of improvement. The massive downsizing of government agencies, which amounted to the dismissal of 19,000 police officers, 2000 tax inspectors and 1500 custom officers, not only removed a heavy burden from the state budget, but also contributed to a reduction of a bureaucracy that had served as an ideal breeding ground for corruption and heavy interference into business activities. The results achieved so far are impressive and were rewarded with the renewal of international financial assistance and a rescheduling of foreign debts. In the first half of 2004, tax revenues increased by 35%, non-tax revenues by 280%. Beyond these measures which aimed primarily at the mobilization of additional state revenues, the adoption of a new tax code, which abolished a number of excessive fees and introduced a flat rate for income taxes, is expected to contribute to an improvement of the business climate.

Despite these outstanding accomplishments, the current leadership has so far missed an opportunity to tackle some structural problems. In terms of administrative reforms, this refers firstly to the formulation of a comprehensive

decentralization policy capable of empowering local legislatures to fulfill their oversight functions in relation to regional and local executives. Due to the fact that the existing system of local self government is not able to make local and regional executives accountable to strong legislatures, the central state is doomed to permanent interventions, which may greatly test its capabilities. At the level of central government, Saakashvili is criticized for relying too heavily on a small circle of close allies.

To cite one prominent example, Saakashvili's Irakli Okruashvili has served as prosecutor general, as minister of internal affairs and as minister of defense. In these different functions, he was charged with those tasks that received priority at a given moment, i.e. the arrest of high profile officials of the former government, the reorganization of the notoriously corrupt Georgian police, the preparation of a small scale intervention in South Ossetia and the completion of far-reaching reforms in the Georgian military as a precondition for its possible integration into NATO. The government has yet to propose a viable long-term economic strategy. The most urgent need is for an action plan for the agricultural sector, which employs more than 50% of the population. The lack of a long-term economic strategy can be linked to the undue priority given to the unrealistic goal of achieving a fast solution to the two unresolved ethnic conflicts in Abkhazia and South Ossetia.

Mainly occupied with its political survival, the Shevardnadze administration demonstrated little inclination toward policy coherence and thus failed to ensure the efficient use of resources. Shevardnadze's government was known for the fierce competition between the different ministries, which were rooted in a struggle for the distribution of spoils.

After the Rose Revolution, the successful implementation of an overall reform agenda has been to a certain extent limited by internal divisions within the central government. Most visibly, policies toward South Ossetia suffered from an unresolved conflict between the so-called hawks, who favored a forceful resolution, and a peace camp, which gave priority to improving the economic situation as a means to making reintegration into the Georgian state attractive to the secessionists. As both camps are represented by Irakli Orkurashvili and Ghia Baramidze, two cabinet members regarded to be the protégés of President Saakashvili and Prime Minister Zhvania respectively, a clear-cut solution could endanger the power sharing agreement and the still fragile coalition between these two leaders.

A similar, though more latent, conflict exists over privatization policies. Whereas former Finance Minister Nogaideli gave priority to increasing state revenues, former Minister of Economics Bendukidze was interested in accelerating the whole process regardless of the possible budgetary gains. Prime Minister Zhvania intervened in the most prominent cases. President Saakashvili has addressed these

political conflicts by twice reorganizing his government, largely to readjust the balance of forces in favor of his supporters.

However, the real test has just come with the mysterious death of Prime Minister Zhvania. According to some local observers, Zhvania's death may be somehow connected with the above mentioned conflicts. Saakashvili's decision to appoint Nogaideli, a close ally of Zhvania's, to the post of prime minister points to his growing cautiousness. Given Nogaideli's lack of political experience, it is less than clear to what extent a return to a politics of balances will be efficient. Highly problematic in terms of achieving policy coherence seems to be the fact that compromises rely more on personal approaches than on factual questions.

During Shevardnadze's rule, corruption crippled economic development and stifled attempts at reform. It deprived the government of urgently needed revenues, which never exceeded 15% of BIP. Corrupt officials, provided with plenty of legal loopholes, severely frustrated possible investors. Open collusion between the ministries and criminal groups engaged in smuggling, trade in weapons and kidnapping for the extortion of ransom, greatly contributed to the emergence of an unstable environment. The open misappropriation of resources in the energy sector caused frequent breakdowns of the power supply.

Despite a framework of anti-corruption legislation and the existence of government agencies charged with tackling the problem, prosecution for corruption had been extremely rare. In fact, the government was known to buy the support of public servants by tolerating corrupt practices. Corrupt deals increasingly influenced even important decisions like the adoption of a parliamentary resolution in February 2003, which led to the invalidation of the licenses of Turkish Airlines and British Airways. Consequently, in 2003 Georgia ranked 124th out of 133 countries surveyed in the Corruption Perception Index of Transparency International.

In contrast, Saakashvili's government launched a massive attack on corruption, making quite efficient use of resources through the skillful combination of different strategies. Publicly announced, high profile arrests of officials charged with corruption and abuse of power instilled a new level of credibility into the law enforcement agencies. Significant pay rises for police officers, financed partly by staff reduction and partly by donor money, decreased their vulnerability to bribes. The recent passage of a law offering financial amnesty to those who have corrected their infractions set positive incentives for the legalization of business activities. Performance efficiency could have profited from greater transparency and from the inclusion of broader segments of society, such as NGOs or local councils. Allegations of due process violations, including suspicions of torture and ill-treatment in the case of Molashvili, a former chairman of the control chamber, have raised concerns that the new authorities are selectively targeting certain individuals for political reasons while turning a blind eye toward their own misdeeds.

3.4. Consensus-building

In their public statements, all major political actors are committed to the cause of building democracy and a market economy. With regard to the Shevardnadze government, these commitments were cast into doubt by a highly dubious practice that, in the end, provoked massive protest.

By contrast, Saakashvili successfully argued for the urgent need to overcome the emergency situation caused by the omissions of the previous government and was thus able to build up a broad coalition of support for his reform drive. However, he failed to translate this rather vague support into a stable power base.

Neither Shevardnadze nor Saakashvili faced the challenge of excluding or co-opting anti-democratic veto-actors. Shevardnadze failed to absorb the democratic opposition, which had emerged inside his own ruling party.

Thus far, Saakashvili enjoys massive popular support, which is rooted in somewhat unrealistic expectations concerning his ability to improve the existing situation. As is shown by previous experiences, this does not preclude the possibility of destabilization brought about by a minority of well organized actors.

For quite a long time, the politics of manipulating the fluid networks of patronage dominant under Shevardnadze had prevented political cleavages from surfacing. Conflicts were kept latent and dispersed through a strategy of distributing administrative spoils among rivaling patrons. As a result, the landscape of political forces frequently changed its shape. In 2003, however, the emergence of an opposition that rejected this kind of politics as a matter of principle and was successful in mobilizing popular protest against the anti-democratic nature of the Shevardnadze rule led to an escalation of the conflicts. As the existing system was not prepared to deal with these kinds of actors or with real political conflicts, its accommodation capabilities proved to be of little use and it broke down entirely. Shevardnadze's readiness to reject the use of violence ensured a peaceful handover of power.

Due to the comfortable majority he currently enjoys in parliament and in view of his broad presidential powers, Saakashvili has not yet really felt the need to engage in the management of political cleavages, which have hitherto been concealed by a wave of popular enthusiasm in support of his leadership. At a time of crisis and in the absence of institutional channels for the expression and reconciliation of conflicting interests, this omission may easily backfire.

Paradoxically, the Shevardnadze government managed to combine an openly corrupt style of politics with an active tolerance for the emergence of one of the liveliest NGO scenes in the post-Soviet region. This seeming miracle can be explained at least partly by the lack of social entrenchment characteristic of most

of the NGOs. Their contribution to the build-up of authentic social trust ought to be questioned.

Even after the Rose Revolution, which seem to have signaled an end to the previously dominant atmosphere of cynicism and widespread distrust, the potential of the third sector to function as a mediator between the state and broad sectors of the society remains underdeveloped. While the revolution was mainly carried out by an urban and young intelligentsia, the majority of the rural population is still alienated from national politics.

Beginning in 2002, the attitude of the government grew hostile toward NGOs. Organizations that became involved in public protest activities and played an important role in bringing about the Rose Revolution, such as Open Society Georgia Foundation, were occasionally subjected to physical harassment.

With Saakashvili's rise to power, the strained relations with civil society organizations were eased – at least in the beginning. The NGO sector even became an important resource pool for the recruitment of government personnel. However, though the government leadership sometimes seeks to convene with NGO representatives for an exchange of ideas, the influence of NGOs on political decisions seems to be rather low. The government's ignorance toward concerns raised by some NGOs with regard to the hasty adoption of constitutional amendments, bureaucratic harassment of independent media outlets under the pretext of tax evasions or human rights violations in the case of former officials charged with corruption and held in pretrial detention, suggests the honeymoon period has ended.

During Shevardnadze's rule the only political forces to be regularly excluded from all power games were the followers of former President Gamsachurdia, who had been ousted in the course of a violent coup d'état at the beginning of 1992 and subsequently launched an uprising in 1993 before being killed in what was probably an officially sanctioned murder. Though marginalized in national politics, the Zviadist have enjoyed some support in Samegrelo, the region of Gamsachurdia's birth, where the situation remained tense.

In contrast to Shevardnadze's reluctance to deal with the problem, in one of his first appointments, Saakashvili named Guram Absandze, a former member of the Gamsachurdia government, Deputy Prime Minister for National Reconciliation.

3.5. International cooperation

While relations with international organizations experienced a sharp deterioration in the last phase of Shevardnadze's rule, Saakashvili quickly declared his government's readiness to cooperate with the international donor community.

In 2003, the leadership's increasing inability or reluctance to fulfill the IMF's and the World Bank's policy prescriptions, which had included demands for decisive steps toward budget consolidation, active measures against pervasive corruption and reforms of state regulation of water and electricity supplies, led to a suspension of their respective aid programs. Annoyed by persistent reform failures and especially by Shevardnadze's unexpected decision to sell strategic parts of the Georgian energy infrastructure to Russian investors – a decision that cast into question Georgia's reliability as a partner in U.S.-led projects for the construction of an energy corridor linking the Caspian Sea basin to Western markets – Washington declared its intention to reduce bilateral aid.

Due to its inconsistent and contradictory policy, the Shevardnadze government not only lost desperately needed sources of income. It also pushed the international donor community and particularly U.S. aid agencies to take the side of the opposition. The frequent high profile visits of American diplomats virtually ensured the passage of amendments to the election law to the advantage of the opposition. Massive financial support, training and consulting provided mainly by the Soros foundation, NDI and IRI strengthened the mobilization and organizational capacities of the emerging protest movement and contributed to the successful ouster of Shevardnadze.

The new leadership under Saakashvili did its utmost to regain the trust of the international donor community. Impressive efforts at re-launching stalled reforms in accordance with international policy recommendations were accordingly rewarded with massive financial aid. At a joint European Council/World Bank conference held in Brussels in June 2004, bilateral and multilateral donors pledged 850 million euro.

However, despite this generous expression of confidence in the new leadership, European governments stopped short of encouraging Saakashvili's aspirations to join the European Union and NATO in the near future. Possibly due to persistent instability in South Ossetia and Abkhazia, which entails the risk of triggering wider destabilization, the perception of improved performance in Georgia still did not translate into increased foreign investment.

While Georgian efforts at developing cooperative relations with its neighbors were always limited by Russia, which is determined to use its influence in the secessionist territories as a means to prevent stabilization and thus regain influence, the abilities of different governments to handle these structural constraints varied to a certain degree. Shevardnadze's less than prudent policy, his reluctance to withdraw hidden support from the Georgian partisans and to clear the Pankisi gorge from Chechen terrorists further increased Georgia's vulnerability to Russian pressure.

Saakashvili, on the other hand, renewed attempts to normalize strained relations with Russia, paying the first visit of Georgian head of state to Moscow and

proposing the establishment of a joint border patrol on both sides of the Pankisi gorge. These initial steps of rapprochement were to be rewarded with Russian agreement to oust Abashidze and return Ajara to the control of the Georgian state. However, an assault led by Tskhinvali-born Interior Minister Irakli Okruashvili on an area near the South Ossetian capital in August 2004 led to renewed confrontation with Russia.

4. Trend of development

The assessments in the following chapter will refer exclusively to the period following the Rose Revolution of November 2003.

4.1. Democratic development

Though on a formal level the core institutions of a democratic system had already been established in Georgia before the period under review, their proper functioning had been severely hampered by pervasive corruption and the constant manipulation of existing rules to the advantage of entrenched elites. The year 2003 saw a sharp deterioration in the government's respect for democratic norms, culminating in the massive election fraud of November 2. In many respects, the Rose Revolution marked a new beginning for Georgia. The new authorities carried out presidential and parliamentary elections that were widely accepted as being free and fair. They launched a massive attack on corruption and smuggling, thus contributing to the strengthening of state institutions, and they expressed the intention to restore the rule of law in many areas. But to a certain extent, their commitment to democratic norms is questionable given the limited progress made with regard to freedom of the press and respect for the human rights of prisoners.

As the ability of the newly elected authorities to implement far-reaching reforms rests primarily on the charismatic legitimacy they enjoy, the level of democratic consolidation has not yet changed significantly. Georgia is still vulnerable to destabilization, which may be brought about either by an externally supported minority of well-organized entrepreneurs of violence or by a sudden shift in popular attitudes.

4.2. Market economy development

The socioeconomic situation improved slightly in the period under review. GDP growth was achieved mainly through extensive foreign investment in the construction of the Baku-Tbilisi-Ceyhan oil pipeline and thus did not translate into tangible gains for the vast majority of the population. Though it did allow for the repayment of pension and wage arrears accumulated by the state in previous years, the considerable increase of state revenues in 2004 did not ease social

tensions as current incomes are still far from sufficient to cover even the minimum costs of livelihood.

Table: Development of macroeconomic fundamentals

	2000	2001	2002	2003	2004
Growth of GDP in %	1.9	4.7	5.5	11.1	n/a
Export Growth in %	48.2	-11.1	5.5	28.9	n/a
Import growth in %	9.3	-1.21	-0.2	33.7	n/a
Inflation in %	4.0	4.7	5.6	4.8	n/a
Investment in % of GDP	21.6	21.9	22.0	24.4	n/a
Tax Revenue in % of GDP	14.2	14.3	14.4	14.5	n/a
Unemployment in %	10.3	11.1	12.3	11.6	n/a
Budget deficit in % of GDP	4	2	2	2.5	n/a
Current account balance in Million \$	-132	-205	-196	-286	n/a

Source: IMF; UNDP

Nevertheless, the economy is expected to profit from the current reform drive over the long term. Although current reforms do not imply significant changes in the institutional framework, the promise to impartially and equally implement rules has the potential to enhance predictability, a necessary precondition for economic recovery. Moreover, the new tax code adopted in 2004 introduced a new incentive structure that is much more favorable to profit-seeking business activities.

D. Strategic perspective

Georgia clearly stands at a crossroads. The reforms initiated by the current government promise to combat corruption, improve law enforcement and strengthen weak governance structures. The restoration of a public order capable of assuring predictability through the application of uniform rules undoubtedly has the potential to contribute to economic recovery. The realization of this could still be endangered from two sides.

On the one hand, all those who had gained substantial profit from the predatory modus of rule in the Shevardnadze era have strong incentives to impede the progress of reforms. They may become allies of the Russian government, which has an interest in cultivating instability in Georgia as a means to regain regional influence.

On the other hand, the government itself may decide to deviate from its course of reforms. Some indispensable but costly measures like increases in energy and water tariffs to a level of cost-efficiency still lie ahead. The new authorities may easily shrink back from decisions that are highly recommended by international organizations but are loaded with the risk that they may lose the confidence of a frustrated population. Because it has thus far failed to translate somewhat vague

popular support into more stable support backed by organizational capacity, the current leadership is quite vulnerable to sudden shifts in public opinion. As has already been demonstrated, this may easily give way to the temptation to distract attention from economic hardship by engaging in adventures in South Ossetia.

In such a situation, the donor community should abstain from any kind of softening of the terms of conditionality. Moreover, it should shift its emphasis from rewarding policy outcomes to sponsoring a change in politics. Primarily, it should press for structural change in two areas: strengthening of local government and introducing recruitment procedures based on meritocracy in all branches of civil administration. Accordingly, the donor community should keep an eye on the old habit of reshuffling government agencies and administrative bodies too frequently.