Georgia at Work: Assessing the Jobs Landscape

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Executive Summary

In April 1991 Georgia seceded from the Soviet Union. In the first four years after independence, there was a coup d'état, and a civil war, causing GDP per capita (measured in 2011 constant US$) to fall sharply from about $8,000 to $2,200.\(^1\) It took Georgia more than two decades to return to pre-independence levels of per capita GDP. Since 1997, economic growth has been strong, GDP grew at about 5.5 percent per annum between 1997 and 2016. Georgia has mostly adopted a pro-market development model, following the Rose Revolution in 2003, and has repeatedly expressed interest in membership in the European Union and in the Organisation for Economic Co-operation and Development (OECD). In 2015, Georgian GDP per capita was $9,025 (PPP 2011 USD), which is less than half of the US$ 18,600 (PPP 2011 USD) average value for Europe and Central Asia (ECA) countries (excluding high income countries).\(^2\)

Economic growth has slowed recently, in large part because of events in partner countries. Lower remittance inflows from the Russian Federation and Greece, and weaker demand for Georgian exports in Azerbaijan, the Russian Federation, and China have impacted economic growth. In 2016, GDP growth fell to 2.7 percent, its lowest growth rate since the Great Recession (2008-09). Though foreign direct investment has remained stable, the current account deficit reached 13.5 percent in 2016. The exchange rate depreciated by 42 percent against the US dollar in 2015-16 and, because most of Georgia’s debt is denominated in US-dollars, external debt (public and private) increased to 108% of GDP. However, the central bank’s decision to maintain the flexibility of the Lari helped maintain a moderate level of reserves and controlled the decrease in competitiveness.

Sustained growth experienced since the mid-1990s has reduced poverty and boosted shared prosperity, but Georgia remains one of the most unequal countries in Europe and Central Asia. At the beginning of the millennium, 20 percent of the Georgian population was extremely poor, and almost half of the population was poor (see Figure ES1).\(^3\) By 2013, the extreme poverty rate had fallen to 11.5 percent and the poverty rate had fallen to 28.5 percent. While half of the total population lived in rural areas, two-thirds of the poor population lived in rural areas. This is partly because poverty in rural areas declined by a small amount, but in urban areas, poverty reduction was pronounced. Nationally, the mean consumption of people in the bottom 40 percent grew by 7.5 percent annually between 2010 and 2014, exceeding the growth enjoyed by the population overall (Figure ES1).\(^4\) Inequality is higher than in the Europe and Central Asia (ECA) region on average, with a Gini coefficient of 38.5 in 2015.

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\(^1\) World Bank, International Comparison Program database.
\(^3\) Poverty is measured using absolute poverty lines defined by the World Bank to allow comparability across countries all over the world. Extreme poverty is defined as living with less than USD 1 per day (2005 PPP) or 1.90 USD per day (2011 PPP). Poverty is defined as living with less than USD 2.5 per day (2005 PPP) or USD 3.1 per day (2011 PPP).
\(^4\) Consumption growth among the bottom 40 percent was 8.3 percent during 2010–2014 compared with 6.4 percent for the population.
This report analyses the main economic forces driving job creation in Georgia, and attempts to answer four questions. First, is the enabling environment for jobs conducive to good job outcomes? Second, how are formal sector job creators doing? Third, how does the Georgian workforce measure up? Finally, what policy reforms can improve jobs outcomes?

The enabling environment for jobs

Georgia has made considerable progress putting business-friendly policies in place. However, political instability remains a significant challenge for firms. Jobs outcomes have contributed significantly to poverty reduction, but job creation is not keeping pace with economic growth. The country has industrialized well, meaning that the share of manufactured goods has increased with GDP per capita, but more than half of the country’s jobs are in the agriculture sector.

Georgia, with a Doing Business ranking of 9 out of 190, has implemented the highest number of business regulation reforms since the launch of Doing Business in 2003—a total of 47. The country is the only low-middle-income country in the top 20 of the Doing Business index. Georgia also has the best business environment in Europe and Central Asia, followed by Russia (rank 35), Kazakhstan (rank 36), Armenia (rank 47), and Azerbaijan (rank 57). The country does particularly well registering property (rank 4), starting a business (4) and protecting minority investors (2). The country is working to improve the time to connect to electricity (30), trading across borders (62) and resolving insolvency (57) (Figure ES2).
Reducing the time, cost and number of procedures required to start a business has directly contributed to the country’s above-average new business entry density. The regulatory reforms adopted have led to about 17,000 new firms being created in 2014, which corresponds to almost 6 firms per 1,000 working-age adults. Notably, Georgia’s new business density is substantially higher than the regional average of 2.3 firms per 1,000 working-age adults, and above new business density in high income countries.

Challenges remain, and political instability has risen to the top of constraints for firms. In 2013, 42 percent of firms identified political instability as the biggest obstacle to doing business, up from 17 percent in 2008 (Figure ES3, panel b). Among large firms with more than 100 workers, 60 percent identified political instability as a major factor in 2013. The main constraints to doing business have also changed over time. In the early 2000s corruption, tax administration, or customs and trade regulations were among the top concerns; in 2013, more firms experienced difficulties accessing finance, and infrastructure components like transportation and electricity. Similarly, skills shortages are important; in 2013, one in ten firms rated an inadequately educated workforce as a major barrier to doing business (Figure ES3).

5 New business entry is defined as the number of newly registered corporations per 1,000 working age people, aged 15-64 years. Included are private, formal sector companies with limited liability.

http://www.doingbusiness.org/data/exploretopics/entrepreneurship
Figure ES3. Firms perceived improvements in most dimensions of the business environment

<table>
<thead>
<tr>
<th>a. Georgia’s firms report improvements in many dimensions; access to finance and infrastructure are major constraints</th>
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<tbody>
<tr>
<td>Tax administration</td>
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<tr>
<td>Corruption</td>
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<tr>
<td>Tax rates</td>
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<tr>
<td>Electricity</td>
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<tr>
<td>Customs and trade regulations</td>
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<tr>
<td>Crime, theft, disorder</td>
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<tr>
<td>Access to finance</td>
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<tr>
<td>Business licensing, permits</td>
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<tr>
<td>Transportation</td>
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<tr>
<td>Workforce inadequately...</td>
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<tr>
<td>Labor regulations</td>
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<table>
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<th>b. Political instability has become the biggest obstacle to doing business in Georgia</th>
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<tbody>
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<td>Political instability</td>
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<tr>
<td>Access to finance</td>
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<tr>
<td>Tax rates</td>
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<tr>
<td>Practices of informal competitors</td>
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<tr>
<td>Transport</td>
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<tr>
<td>Tax administration</td>
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<tr>
<td>Electricity</td>
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<tr>
<td>Inadequately educated workforce</td>
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<tr>
<td>Customs/trade regulations</td>
</tr>
<tr>
<td>Corruption</td>
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<td>Courts</td>
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<td>Labor regulations</td>
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<tr>
<td>Access to land</td>
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<tr>
<td>Business licensing and permits</td>
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<tr>
<td>Crime, theft, disorder</td>
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</tbody>
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Source: Enterprise Surveys, Georgia 2002-2013. Notes: Panel a: Percentage of firms reporting relevant dimension as a major constraint. Panel b: What is the biggest obstacle faced by your business?

Georgia’s poverty reduction record is driven by labor income, employment and social sector reforms. Between 2012 and 2015, the percentage of the population living on less than 2.5 dollars per day fell from 42.5 to 31.2, equivalent to a 27 percent reduction (Figure ES4). This reduction can be traced to improving jobs outcomes—mainly improved wages and new jobs—and social assistance, with the increase in the old age pension.

Figure ES4. Poverty was drastically reduced in the last 10 years due to social transfers and income from economic activities

(a) Poverty incidence, 2006-2015

(b) Main drivers of poverty reduction 2010-2015

Cons/Inc. | 0.6
PC/PAE | 0.0
Dependency rate | 0.1
Employment | -0.8
Labor income | -1.2
Agricultural sales | -0.3
Agricultural self-consumption | 0.1
Social Assistance | -1.3
Remittances | -0.1
Private transfers | -0.1
Property | 0.0

Source: Poverty note 2017, in progress (Poverty GP). Notes: Panel b shows the result of a Shapley decomposition of poverty incidence using the ECAPOV $2.5/day 2005 PPP poverty line.
Georgia is not creating as many jobs as its economic growth would predict. Despite 5.7 percent GDP growth between 2005 and 2015, employment only grew by 0.29 percent, implying a 5 percent growth elasticity of jobs (Figure ES5). Worldwide, the growth elasticity of jobs is 34 percent, meaning that for each percent of GDP growth, employment grows by 0.34 percent. For the Western Balkan countries i this elasticity was 16 percent for 2000-2010, and for EU-CEE countries it was 32 percent for the same period. ii This raises an important question: why is economic growth in Georgia not creating as many jobs as the rest of the world?

**Figure ES5. Growth has not created employment in Georgia**

Relationship between GDP and employment growth, 2005-2015

The job creators

A detailed analysis of data from Georgia’s Firm Registry, managed by Geostat, reveals important information about Georgia’s firms and their employment patterns, analysis is limited to registered firms only. Despite robust firm entry in Georgia, total employment growth is low because firms are mostly small, and employment is concentrated in larger and relatively older firms. Small and individual firms, while contributing to job creation in the short run, fail to grow to medium-sized firms; they also have high failure rates. Resources are also misallocated, meaning that too many workers are in the least productive firms within each industry.
In 2015, individual firms represented over 70 percent of total registered firms, but accounted for only 11 percent of total employment in registered firms. In the private sector, employment was concentrated in small firms (below 20 employees) or large firms (above 100 employees), this accounted for 40 percent of total employment each. As a result, there are disproportionately low levels of employment in medium sized firms and questions about the missing middle are being raised.

**Figure ES6. Employment by firm size and firm type**

(a) All Firms  
(b) Private Firms  
(c) Private firms (non individual)

*Source: Firms registry (Geostat)*

Despite robust firm entry, total employment growth is low because individual and small firms have high exit rates. Among all firms operating in 2012, over 50 percent of individual and small firms (less than 10 employees) exited before 2016. That is, more than half of all individual and small firms do not survive four years in business.

**Figure ES7. Net job creation**

(a) Net Job Creation: All firms  
(b) Net Job Creation: Private firms

*Source: Geostat Firms registry.*
A concern for policymakers in Georgia is that resources continue to be misallocated, both across and within economic sectors. If factors of production were allocated efficiently, total factor productivity could increase by up to 70 percent. This misallocation manifests itself in employment being concentrated in low-productivity sectors, such as agriculture; wholesale and retail trade; public and social services like education, and health and social work (ES8, panel a). Almost half of total employment is in agriculture, but the sector only contributes 7 percent to GDP. High productivity sectors (e.g., financial intermediation, telecommunications) have created only a few jobs in the last decade, or are still too small to significantly impact employment growth (ES8, panel b).

**Figures ES8. The largest economic sectors in terms of employment have low-productivity, while employment growth in high-productivity sectors has been modest**

(a) GDP per worker: 2006 vs. 2015. (b) Employment % growth (2006-2015) vs. GDP per worker (2015)

*Source: authors’ calculations based on GeoStat LFS data on employment and GEOSTAT Value added Statistics across sectors. Size of bubble: % on total employment in 2015*

Employment by industry is also concentrated in low-productivity firms. Comparison of productivity across exporting and non-exporting firms shows that exporting firms are more productive than non-exporters. Exporters and non-exporters had similar productivity levels in 2006, but average productivity among exporters increased relative to non-exporters until about 2010, when non-exporters also increased productivity. Firm productivity also increases with age, mainly because the most productive firms are the firms that survive in the market, and because firms learn how to become more productive over time. When there is too much dispersion in firm productivity as it is the case with Georgian firms, there is scope for gains by reallocating labor from less to more productive firms. The distribution of physical productivity shows little to no progress over time, despite the important reforms to the business environment (Figure ES9).

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6 Measured through the marginal returns to labor.
Skills shortages are limiting productivity and firm growth. In Georgia, firms value technical, cognitive, and socio-emotional skills; technical skills are most valuable. In a STEP employer survey, employers report that finding experienced workers with the right technical education is the most important constraint; and about 70 percent of companies say the education system is outdated. Two thirds of firms complain that labor market entrants do not have necessary skills.iii

**The Georgian workforce**

A key constraint to competitiveness and growth is a potential shrinking workforce. The population decline is significant among the working age population and children, while the elderly population is growing slightly (Figure ES10, panel a). Since 1990 fertility rates in Georgia have been below replacement rates, outmigration is also significant: between 2000 and 2010, 10 percent of Georgians are believed to have emigrated.
In 2016, the labor force participation rate was 72.9 percent, relatively high by international standards and high for upper-middle income countries (Figure ES11). Male labor force participation is high, at 83.1 percent; and female labor participation, at 64 percent, is the same as the regional and European averages. Labor force participation has risen significantly since 2006 for all groups, except for young people. The LFP rate was 66 percent in 2006 and reached 73 percent in 2016, a 10.1 percent growth rate. However, the gender gap in the labor force participation is almost 20 percentage points. This gap is smaller than the regional average or the average of upper-middle countries, but is three times larger than in Slovenia, Latvia or Lithuania.

Young people are displaying unusually high rates of inactivity. In Georgia, the proportion of young people not in employment, education, or training (NEET) is 30 percent (Figure ES11). In the Czech Republic, Slovenia, and Lithuania, youth NEET rates are less than 10 percent. High NEET rates indicate that Georgia’s young people are not investing in their human capital and are disproportionately at risk of labor market exclusion. The transition from education/training to work differs for men and women. While most young men transition from school to work, most young women remain inactive and out of school for longer periods.
### Figures ES11. Composition of the working age population in 2016

<table>
<thead>
<tr>
<th>Working age population</th>
<th>2,363,391</th>
</tr>
</thead>
<tbody>
<tr>
<td>In the labor force</td>
<td>1,722,146</td>
</tr>
<tr>
<td>Not in the labor force</td>
<td>641,245</td>
</tr>
</tbody>
</table>

| Employed               | 1,491,188 |
| Unemployed             | 230,958   |

Wage worker: 703,142 (47%)
Self-Employed: 421,174 (28%)
Unpaid: 349,262 (23%)
Entrepreneur: 17,610 (1%)

Not in agriculture: 138,848 (32%)
In agriculture: 286,326 (68%)

Source: IHS 2016. People in working age are aged between 15 and 64 years.

### Figures ES12. Low labor force participation for youth is not driven by increases in education

#### (a) LFP by age group

#### (b) NEET youth for selected ECA countries

Source: (a) WDI, labor force participation rate, total (modeled ILO estimate). (b) WDI, youth NEET rate, except for Georgia which is from ETF 2015.

Unemployment is 13 percent; this is high and many workers are engaged in jobs that they consider of low quality. About 42 percent of jobs are in agriculture, either working for themselves (19 percent) or unpaid workers (23 percent). Most of these jobs are not desirable and are low productivity. While there is variation in wage employment, about 47 percent of the employed work in wage jobs. Broadly speaking,
Job quality is correlated with skills. Low-skilled workers live in rural areas and generally work in agriculture for themselves or are unpaid workers; while highly skilled workers are in wage employment. Highly educated men above 30 years of age have some of the best job prospects, and young, low-skilled women have some of the poorest jobs prospects.

**Figure ES13. Low-skilled workers are self-employed in farms; highly skilled workers are generally salaried and work in offices in the city**

Distribution of employed workers across type of employment: wage work, entrepreneur, self-employment outside agriculture, self-employment in agriculture and unpaid work.

Source: authors based on IHS 2016.

### Policies to improve jobs outcomes

This Jobs Diagnostic points to four areas for policy reform: (i) policies enabling the overall business environment; (ii) policies enabling the firm-specific business environment and firms’ capacity to create more inclusive and high-productivity jobs; (iii) policies aiming at increasing the size of the workforce; (iv) policies aiming at increasing workforce productivity and skills.

Policies that enable the overall business environment. These include: (i) reducing the volatility of the exchange rate; (ii) continuing fiscal consolidation and reducing the current fiscal deficit; (iii) stimulating FDI and facilitating remittances; (iv) promoting greater Integration into global markets via international coordination, bi-lateral or tri-lateral agreements, via better investments in connectivity infrastructure and by removing existing barriers to trade; and (iv) enhancing political stability.

Policies enabling the firm-specific business environment and firms’ capacity to create more inclusive and high-productivity jobs could include: (i) designing fiscal incentives for export-oriented firms; (ii) providing incentives for private investments in R&D and worker training, especially for medium-sized firms; (iii) easing access to finance especially for small and medium firms; and (iv) increasing public investments in R&D, especially in high value-added sectors.
Policies aiming at increasing the size of the workforce include: (i) improving the quantity and quality of child care facilities; (ii) enhancing part-time female employment and flexible working arrangements; (iii) carrying out information campaigns; (iv) introducing activation measures for selected targeted groups; (v) improving job search activities of both firms and workers favoring the use of new technologies; (vi) improving labor market intermediation channels, both public and private; and (vi) reinforcing and improving the quality of public employment services.

Policies aimed at increasing workforce productivity and skills include: (i) enhancing worker skills for the new economy (revision of curricula, working closer with employers; digital technology; training on non-technical skills, especially soft-skills, and foreign languages); (ii) re-skilling the existing workforce (implement program of re-qualification, on-the-job training; develop labor market information system); and (iii) stimulating the use of new technologies for improving the match between demand and supply of skills.

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i Comprising Albania, Bosnia and Herzegovina, Kosovo, Macedonia FYR, Montenegro and Serbia.
ii For more details on the estimation of the Employment GDP elasticity and comparison with EU countries, see World Bank and wiw (2017).
iii Rutkowski 2013.