



Rural Non-Farm Economy Project
ETFG, Central Avenue, Chatham Maritime, Kent ME4 4TB, United Kingdom
Tel: + 44 (0)1634 880088; Fax: + 44 (0)1634 883706 Email: b.j.oakenfull@greenwich.ac.uk
WWW: <http://www.nri.org/work/rnfl-transition.htm>

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Junior Davis, Dirk Bezemer & Giorgi Meskhidze

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Introduction

To date for most multilateral donors, the single most promising way of achieving greater RNFE improvements (particularly in income) has been to put emphasis on employment and the creation of micro, small, and medium-sized enterprises (to which we collectively refer as SMEs). Many donors and non-governmental organisations (NGOs) have emphasised SME promotion and credit provision to SMEs as the core of their non-farm rural employment interventions in transition economies.

For the above reasons, this paper focuses on micro-enterprise (MSME) and small-medium-sized enterprises (SMEs), those who have “*successfully*” diversified out of full-time farming in Armenia. Here we evaluate the firms’ financial performance, identify characteristics of successful diversifiers, key lessons and factors which enhance the prospects for successful diversification. In this document, we provide a summarised overview of findings from a survey based on fieldwork conducted in Georgia during spring 2001. In this research, 18 operators of non-farm enterprises in rural locations in the districts Abasha, Telavi, and Akhaltsikhe were interviewed about various aspects of their rural non-farm enterprise’s structure, performance, their economic environment, and their motivations and plans. The paper follows

¹ The study was prepared as part of the Natural Resources Institute project entitled ‘Characterisation and Analysis of the Non-Farm Rural Sector in Transition Economies’ undertaken for the World Bank and Department for International Development (DFID). Junior Davis is affiliated with the Natural Resources Institute of the University of Greenwich. Giorgi Meskhidze is a private economic consultant in Georgia. Dirk Bezemer is affiliated with Imperial College at Wye, University of London.. Correspondence to j.r.davis@gre.ac.uk.

the structure of the questionnaire and does not go beyond a presentation of the main findings.

Poverty, coping strategies² and non-farm activities in rural Georgia

Since the collapse of the Soviet Union Georgia has experienced one of the most dramatic declines in living standards of any of the post-soviet republics. When people talk about poverty they often describe themselves as “on the edge of poverty” or “in the middle”. They stress their poverty when they compare the current situation with that of the past.

Among the rayons studied the poorest is Abasha, followed by Akhaltsikhe. Telavi is the richest among these three. We have ranked them according to the key aspects of rural poverty: (grades 1 bottom: to 10).

<i>Aspects</i>	<i>Abasha</i>	<i>Telavi</i>	<i>Akhaltzikhe</i>
Hunger	8	9	8
Lack of fuel	3	6	5
Lack of medical care	1	2	2
Overcrowded housing	8	9	8
Shame	2	3	5
Lack of information	3	3	2
Pervasive fear and insecurity about the future	1	1	1
isolation from cultural life	1	3	1

Most rural people cling to public sector employment, because it still provides a degree of social respectability, access to information and connections, even though salaries are very low and irregularly paid.

As to the coping strategies, most often this focuses on supplementing income from non-farm private jobs. Non-farm self-employment includes involvement in domestic or “shuttle” trading, working as babysitters, tutors, cooks, drivers, loaders etc. According to a survey conducted by the State Department of Social and

Economic Information (2000), 50% of households questioned said, that they had received money from some of the alternative non-farm sources of income listed below:

² See N.Dudwick, Georgia: qualitative study of impoverishment and coping strategies, World Bank report.

<i>Source</i>	<i>% of Households receiving money this way</i>
Sale of Flats	12
Sale of Household items	12
Assistance from friends/relatives	15
Use of servings	4
Charity	1
Interest of savings	2
Grants	3
Interest from lending	0.3
Renting out property	15
Other	5
Total	69.3

Source: State Department of Statistics

Rural non-farm activities are growing in Georgia, even though it is difficult to find a family in rural areas that is not busy in agriculture. The main reasons for an increase of rural non-farm activities are as follows;

1. Salaries in the public sector are not paid fully or on time and are very low (for example, a *rayon* Governor earns 120 GEL i.e. 56 USD per month), so many people start their own business,
2. There is no credit for agriculture, so people start finding other ways of raising funds by starting non-farm activities,
3. For some of the better-educated and well-connected (significant social capital) members of the community privatisation has provided some impetus to the development of non-farm SMEs. Although the latter may be classified as a demand-pull reason for diversification, it is clear that for the majority of rural dwellers non-farm diversification is a distress-push phenomenon.

In addition, several constraints to the development of rural non-farm activities should be noted, of which the main three are:

- High taxation
- High levels of corruption
- Lack of initial “start-up” capital – lack of credit

It is hard to find a business paying all its taxes. Estimates by the State Department of Statistics suggest that total taxes account for up to 67% of income. ‘Black’ accounting systems and low salary levels in the public sector together with a lack of transparency have led to significant corruption.

As will be shown below, a very important problem concerns the lack of start-up capital. Banks are ready to provide credit with an annual interest rate of 18-25% to those in Tbilisi if they own flats etc., as collateral. It is however, very difficult to access credit in rural areas unless you have friends or pay a bribe to bank officials. In the Kakheti region the EC-TACIS programme started providing credit with an annual interest rate of 24%. We have interviewed a businessman who received a small loan of (US \$5000) but was unable to pay it back.

A. General Rural Non-farm Enterprise Indicators

Seven of the 18 respondents are involved in food or agricultural/forestry processing of some sort – milling, wood processing, and soft drink production. Three are in repair services, two in petrol trade, two in health care, two in ‘direct trade’. Still the most frequent (6 times) self-reported sector is ‘trade’. Only three respondents spent time in agricultural production as well, reporting 20, 30 and 40 % of their time devoted to it. About two-third report their summary financial indicators over 1998 and 1999. There are very large variations, with three large enterprises having tens of thousands of Georgian Lari’s (GEL) of turnover, and the rest less than GEL 10,000.

Four firms report zero profit, and none losses. The enterprises were established between 1989 and 1999, most frequently (10 cases) in 1996-1998. Fourteen entrepreneurs who reported on their firms' origin founded the enterprises themselves, three bought it last year, and one took it over. Three lease their properties and 15 own it. Six run their business from home, 12 have dependent children under 16 at home. All but four report the legal status of their enterprise as an 'individual enterprise'. All but one sell to shops, in most (11) cases for 95-100 % of their sales. Three entrepreneurs sell to large enterprises, three to small enterprises, and three to wholesale traders, with widely varying shares of sales to these buyer types. Most (15) have the larger share of their customers located less than 25 km away. One sells 70 % of output to another CIS country, two do so for 10 and 5 % of sales. One sells 75 % to a EU country, one does so for 10 % of sales. Suppliers are more frequently outside the state in the CIS: in 8 cases for more than 70 % of inputs, in another 4 cases for less than that. Local (less than 25 km distance) and regional (between 25 and 50 km) suppliers are still most frequent. One respondent sells 85 % of output to the EU.

B. Enterprise Activity Indicators

Work time is most frequently (11 cases) roughly the same each week, and fluctuates substantially for only 2 respondents. The average working week is 50 hours, but over 60 hours for 5 respondents and under 30 for 6 of them. When asked to rank the importance of motivations to start up the business, respondents most often (13 times) mention 'to provide a main source of income; this factor is also ranked higher - 9.2 on a scale of 1 (unimportant motivation) to 10 (important). Second in average importance comes the motivation 'to avoid or prevent unemployment' (7 times mentioned, score 6.3 on average), and a close third- but more frequently mentioned- is 'to provide an additional sources of income' (10 times, score 6.3). The only other motivation with a score in the 'important' range (5-10) is 'to capitalise on my skills and training (6 times mentioned, score 5.7). Twelve

enterprises have employees, while in three – all without employees - the entrepreneur’s spouse works. One other respondent has a family member as an active partner, two have a full-time employed family member, and one has four family members frequently helping out. Non-family labour is more important. Two entrepreneurs have an active partner from outside their family, three have non-family members in full-time employment (1, 2 and 2 employees). Part-time employment is the most frequent employment option, with 11 entrepreneurs reporting this. The number of part-time employees ranges between 1 and 15. As to non-permanent labour, five enterprises have employees frequently helping out, three have employees occasionally helping out (45 in one case). One respondent own another, connected business as well (in wood processing). Quite a few (7) entrepreneurs have owned another business before (two shops, a petrol station, a chicken farm, and a soft drink production facility). Four respondents are also employees somewhere else: two permanently and part-time, two occasionally and full-time.

C. Location of the Business

The respondents’ distance to various businesses and institutions is depicted in table 1. Surprisingly, ‘training for employees’ is generally very close – a finding best understood by interpreting this as the local primary school. As in the Armenian findings, bank and post-office are also local, as is the main competitor. This is understandable given the fact that most enterprises serve the local market.

Table 1: Distance to businesses and institutions

	<i>Mean</i>	<i>Std. Deviation</i>
main competitor	10	11
bank	2	1
post office	8	12
training for employees	1	1
Chamber of Commerce	60	0
district council	1	2

insurance company

66

97

Notes: Number of respondents:16 or 17. No responses were given to questions on the distance to consulting services and business club, and only two responses to 'Chamber of Commerce'.

D. Plans

Respondents are equally split over feeling demand-constrained and seeing room for selling increased production (8/8) Two are uncertain in this respect. Two thirds (12) produce below capacity and only a minority (5) plan to expand the business. Expansion is constrained by space in 3 of these cases, by staff shortage in another 3 cases, and most frequently (9 cases) by capital shortage. In all these cases, capital constraints are reported to inhibit investments (not staff recruitment or turnover growth) and to be caused by lack of collateral or deposit. Additional causes include high interest rates (5 cases), lack of liquidity or funds, debt-aversion (both 3 cases), too high-risk assessment by the bank, and inability to obtain a subsidy (both 2 cases).

E. Running the Business

Annual turnover, averaged over the (generally short) business history, is 55,000 GEL on average in the sample. This is much larger than the 11,000 GEL and 16,000 GEL reported for 1999 and 2000³. Current profits are deemed sufficient for covering current expenses by 12 respondents (of which 5 say that this is difficult) of the total 18. Seventeen respondents replied to a question on whether they had applied for a loan in the past five years, all but one in the negative. Only one respondent received a 2,000,000 GEL loan. Also only one other respondent has applied for a grant, and was refused. In the near future, the next two years, most (10) respondents plan a slight expansion, three want to provide a stable development, and three aim at a substantial expansion. One plans to discontinue the business within two years, and one doesn't know what to do. In the longer term, over the next ten years, such uncertainty is the most frequent reply (9 cases). Next in importance is 'substantial expansion', while two entrepreneurs plan to hand the business over to a successor, one wants to sell the enterprise, and one plans to discontinue it.

When entrepreneurs sought business support over the last ten years, the most frequently (3 cases) approached institution was the farmers union, followed by contacts in industry. All the other institutions listed, including rural development agencies, local enterprises, business centres, the local and district councils, and training bodies, were approached. Given the fact that none of the 18 enterprise in the sample aren't even farms, these findings appear to indicate a deficiency in rural business support structures. That inference is confirmed by respondents' replies to what sort of institutions would have been useful. An overview of these is provided in table 2, where business support areas are top-down ranked by decreasing reported usefulness in the present.

³ A divergence that may indicate a misinterpretation of one of the questions.

Table 2: Business support areas that would have been useful: past and present

Business support areas	Reported usefulness (count)	
	... in the past	... in the present
7	4	7
11	4	6
13	5	6
8	3	5
14	3	5
2	5	4
9	4	4
3	3	3
5	4	3
6	5	3
10	4	3
12	4	3
1	8	2
4	2	2

Support in marketing, in the area of financial management and taxation, and in computing were most frequently mentioned as important in the present. Technology and market research were of importance to a slightly smaller number of respondents, while support in developing a business strategy and staff recruiting were less often deemed useful. Some of these results are understandable given the quite general demand constraint and lack of problems with staff recruitment; others are more surprising, such as the need for computing assistance in a supposedly mostly low-tech environment. In the past, respondents would have liked to have more support in developing a business strategy and negotiation skills, and in learning to advertise – plausible answers for enterprise operators who just started.

Conclusions

Both private property and private business are new for post-soviet countries in transition to a market economy. The level of institutionalization of economic relations and of a firm's capacity for strategic action in exploiting potential non-farm opportunities is low. The lack of professionalism is widespread (partly a function of low-skill levels) and causes a situation of "grabbing", where even an entrepreneur does not try to create a stable legal basis and reputation for their firm, which would reflect a long-term investment, but instead to solve directly current problems by any means possible.

The share of "informal" businesses is also high in Georgia (for example, unregistered small traders, processors, craftsmen and others). These businesses have almost no connection with the state. They do not fight to protect their interests, but adapt to the existing environment (to the informal unregistered situation). This is done primarily by informal methods, which include paying bribes, avoiding taxation etc.

Our survey shows that there are very few registered or fully capitalised enterprises in rural areas. Only where a village is close to a main, arterial road and if there was an industry developed in a particular territory previously, is it likely that there is a firm currently in existence there. The main legal non-farm enterprise status in rural areas is "individual entrepreneur", because in this case a lower registration fee has to be paid. Until recently, the registration fee for founding a Limited company was 1000 US dollars (2000 GEL), whereas (as above) this sum is often the amount of money a firm has as registered capital. This fee has recently (2001) been reduced to 500 US dollars.

Many firms and local people in rural areas do not know what a "business training course", or business association is, thus it is unlikely that we will observe any

significant enterprise clustering in rural Georgia in the near future. Besides these kinds of association and institutions have not yet developed in Georgia.

Very few of our respondents have answered questions on savings or credit. We would mainly explain this by the factor of fear. Besides the practice of saving money in a bank is not that well established in rural Georgia, especially after the years 1991-1994, when several banks collapsed and the population lost a great deal of money. Many people also remember that after the collapse of the Soviet Union the state requisitioned people's savings from banks and, in spite of many promises has never returned it to them.

The non-market nature of most RNF enterprise economic relations can mainly be seen in the two phenomena, which are the merging of business and power and growth/ prevalence of the shadow economy. These factors dramatically reduce prospects and effectiveness of uniting businesses into associations because of a high level of distrust in all areas of social and economic relations. This has a very negative impact on the development of economy in general as well as the RNFE.