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FOREIGN EXPERIENCE OF CREDIT SYSTEM MANAGEMENT AND ITS CHALLENGES IN GEORGIA

Abstract: World experience showed that without formation of the modern effective system for providing agrarian credits it would be impossible to develop agrarian sector in Georgia. Agrarian credits play significant role in development of agriculture. Low availability of the financial resources reduces agriculture development growth pace. Therefore, it is significant to support formation of such credit system that would be tailored to the socioeconomic situation in Georgia and provide access to cheap agrarian loans to the small and medium farmers.

Currently, in agrarian sector of Georgia, loans granted by the commercial banks comprise 1-3% of the total loans. The causes are complex. Among them there should be distinguished low profitability of this sphere today and long period required for business setup and this reduces the level of trust of banking sector to small and medium farmers. As a result, commercial banks are unable to contribute to effective functioning and development of the agrarian sector as they regard that providing financial resources to the agricultural production is of high risk for their successful activities.

Goal of our research is to study and analyze condition of the financial institutions operating in Georgia, evaluate availability of credits for the agricultural cooperatives and determine possibility of use of the experience of EU countries in this sphere.

The reports of the National Statistics Office of Georgia, FAO, ACDA, ENPARD consortium member organizations, provisions of Georgian Law on Agricultural Cooperatives, Georgian Law on Non-Banking Deposit Institutions – Credit Unions, Georgian Law on Entrepreneurs and other normative acts were studied and analyzed.

For the purpose of information collection there was used unstructured in-depth interviews with the experts of credit sphere and representatives of the cooperatives.

Key words: Credit System, agrarian sector, credit cooperation.

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Introduction

Agriculture is one of the priorities of development of Georgian economy. Over 50% of the country's population is engaged in agriculture, while its share in GDP is only around 8%. The situation is further aggravated by the fact that the lands in Georgia are quite fractured. Work on small land parcels limit development of the farm economies, they cannot take advantage of the economies of the scale, cannot acquire innovations available at market and work with the traditional, obsolete methods result in low productivity. Therefore, since 2012, the government makes

significant steps to implement whole set of programs in agriculture.

Georgian government and the European Union have signed the EU Neighborhood Programme for Agriculture and Rural Development (ENPARD). The program was launched in 2013 and its main objective is to increase agricultural production in Georgia and poverty reduction in rural areas.

In this respect, Government of Georgia has made certain steps, among them the most important include adoption of the Law on Agricultural Cooperatives in 2013 and establishment of the Agricultural Cooperatives Development Agency (ACDA), liberalization of the tax legislation for the

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agricultural cooperatives. Tax legislation of our country exempts the primary production of the agricultural cooperatives from two of 6 types of taxes (income tax and profit tax) and exempts from value added tax, if their total turnover is less than GEL 200.000. From the date of ENPARD programme implementation up to present, ACDA has granted the status of agricultural cooperative to 1,342 cooperatives all over Georgia. Thus since 2014, there are the institutional bases for cooperatives development in Georgia [11, p.119] and significant support of government and international organizations.

1. History of the cooperatives' development

Creation of the cooperatives commenced in Georgia as early as in 1869, when Iliа Chavchavadze has established the first cooperative "Momchirneoba". Since then, in aggregate 4471 cooperatives were established in Georgia. In 20th century, after soviet occupation, there were forcedly established cooperative unions – kolkhozs. After decomposition of the kolkhozs the population's attitude towards the cooperatives was negative. Liberal tax policies and grant programs implemented from 2012 up to present yielded significant results. In 2013, project of the Ministry of Agriculture "Preferential Agricultural Credit" was launched. It is implemented by the Agricultural Projects Management Agency.

It should be noted that development and activation of the state programs have impacted statistics of granting of agricultural credits. This implies co-financing of the loan interests. The loans are issued by the project participant banks and microfinance institutions. Of course, the banks still request for credit issuance the relevant security from the entrepreneurs engaged in agriculture and this is reasonable. Involvement of the state in these processes implies subsidizing of the interest rate, i.e. partial co-financing of the bank interests. Hence, the outcome of the policy is reduction of the loan interest expenses for those, who would receive the loan but the interest rate would be so high that it would be hard to repay the interests within the term stated by the bank or even it would not be hard. In the latter case the state co-participation would simply be an additional benefit for the entrepreneur subject. Thus, in many cases, the credits are used by relatively large agricultural producers for whom the credits would be affordable without the state assistance while for the small entrepreneurs the problem of credit availability is still quite significant.

Georgian government has to play significant role in implementation of such programs that would promote the population's education, improvement of their awareness, attraction of the investments and

development of the relevant services. State programs are mostly oriented towards issuance of grants and no proper attention is paid to the delivery of the trainings to the entrepreneurs, their familiarization with the modern standards and improvement of their awareness in such areas, as business planning, management, marketing and negotiation skills. Even where such trainings are delivered, they are not well organized, two-tree-day trainings are delivered to the entrepreneurs spontaneously, on different issues, in different periods and hence, such trainings components are not result-oriented.

Current economic situation in Georgia shows that the problem could be actually resolved only through formation of the agrarian credit system.

2. German experience of agrarian credit system development

The formation and development of cooperatives in the world started almost two hundred years ago as a result of the fundamental changes in agriculture following the Industrial Revolution in Europe [4, p.367]. Currently the cooperatives operate in all countries all over the world with over billion people involved. The agricultural (30%), trade (23%), insurance (22%) and credit (19%) cooperatives are the most widespread ones [9, p. 133].

Legal regulations for the agricultural cooperatives are provided in the Law on Agricultural Cooperation (1947). Here, the agricultural cooperatives imply production, marketing, and procurement of the production factors, consultations, credit and insurance cooperatives [8, p. 62]. In Georgia, for formation of agrarian credit system is significant to share foreign experience. For example, Germany is regarded as the native land of credit cooperatives. Here the credit and agricultural cooperatives' development takes place since 50s of 19th century. Founder of this movement was Friedrich Raiffeisen, who wrote in 1866 the work titled "Credit Unions – Means for Poverty Elimination". In 1846-1847, in many Prussian provinces drought caused poor harvests and many small entrepreneurs and farmers were on the verge of bankruptcy.

Development of the farm economies required long-term investments and credits that would no one provide. Then Raiffeisen became the head of typical German city, in 1846, the society of bread and wheat self-supply was established. Employees of this organization bought flour from local farmers, baked bread and provided it to the poor citizens. In 1854, in Heddesdorf, the cooperative was established where there were unified the farmers

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desiring to sell their products at better conditions. To defeat poverty, said Raiffeisen, we have to defeat dependence first. Special formula helps people in this: self-assistance, self-governance, self-responsibility. He established the cooperative that met with all requirements of the banking institution. One of the central functions of such cooperative was making partnership relations with the banks. The banks used to grant long-term loans much easier to such partnerships than to the individual farmers. Usually, the cooperative members used to live within the same area, knew one another personally and used to take credits as required. The members and organization management were well informed about what was going on in each of the member farms. The cooperatives provided solidary responsibility of the members with respect of the loan repayment. This obligated the cooperative members to collaborate with one another and provide mutual assistance. This contributed to interest of the large banks in the partnerships. The capital of the cooperative was composed mostly of the partners' contributions and bank credits. Loan taken by the cooperative from the bank was repaid from the profits and gradually the cooperatives gained their own assets – the capital. Gradually the people believed that the cooperatives were trustworthy.

Key principles of agricultural cooperation development stated by Raiffeisen were as follows: joint and several responsibilities of the cooperation members for the society's liabilities, rejection of all contributions, work without payment, strict localization of the area of activities, stated number of the members, use of the financial assistance for production purposes and prohibition of membership in the other companies.

Such cooperative credit system proved to be highly viable. Cooperatives were able to withstand not only severe economic crises, commotions caused by the world wars and fascist dictatorship but they have even strengthened their position in the banking system of the country.

In 1972, two independent branches of credit cooperation – Raiffeisen's agricultural credit societies and Schulze-Delitzsch societies merged. Today Raiffeisen's union unifies all agricultural, crafts and service credit cooperatives and cooperative banks all over the territory of Germany.

Friedrich Wilhelm Raiffeisen has established the banking network, with 425 units in Germany and 120 units in Austria. This system has further developed and expanded and formed into the Raiffeisen group with the head office in Austria – Raiffeisen ZentralBank. Since 1980 this bank has opened branch offices in the countries of Central and Eastern Europe.

According to the data of Forbes Magazine, among 2000 world's largest corporations Raiffeisen Bank is at 1061 position. Its bank capitalization is USD 4.3 billion. All over the world, this bank employs 51,965 people. In 2015, the corporation's turnover was over USD 50 billion. As for the cooperative movement, Raiffeisen organization is one of the largest employers in German economy, especially in the sphere of agriculture. Currently, in agricultural cooperatives of Germany over 200,000 people are employed.

Cooperative agrarian credit system is principally different from the general banking-credit system with its purpose; functioning of the credit systems at local, regional and central levels; clearly defined and distinguished functions at each management level; compliance with the solidarity principles; possibility of returning of the profits gained by agrarian credit system into the own capital and increasing of the loan scales; solidarity of the lenders, their trust and common responsibility that should be strengthened by membership of the cooperative union.

Main goal of the cooperative agrarian credit system functioning is support to development of production and non-production infrastructure of agricultural food production sector, support to agriculture development, regulation of the investment processes, regulation of the demand for agricultural products at domestic market and stimulation of the export production.

3. Credit system in Georgia

There are quite significant social, economic, political and ethnical-cultural differences between Georgia of 21st century and Germany of 19th century. Certainly, it is impossible to replicate Raiffeisen's credit cooperative model in Georgian reality. While in credit system development process in Germany the role of the government was minimal and the above credit cooperative system was created by the individuals, in our country the state policies supporting agricultural cooperatives was launched in 2012. Today most of the cooperatives have no sufficient experience of cooperative activities, they have not suffered significant market commotions and their viability was not revealed. The process of formation of the credit cooperatives in Georgia is absolutely different as well. Though, the state can play significant role in the mentioned processes. Before formation of the agricultural cooperatives, it is necessary that the state and organizations engaged in agriculture implemented consistent policies and programs. This can be partial investments into the authorized capital of the credit cooperatives, information meetings and relevant training courses

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dealing with establishment of the credit cooperatives.

In Georgia, activities of the credit institutions are regulated by Georgian Law on Non-Banking Deposit Institutions – Credit Unions. According to the Law, non-banking deposit institution is an enterprise registered in a form of cooperative, accepting deposits from its members only, issues the loans and performs activities allowed by this Law. The Law states that the main goal of the non-banking credit institution is not gaining of the profits. In addition to registration with the business registry, for operation of the business, the credit unions have to receive the license from the National Bank of Georgia. Credit unions have the right to perform the following banking activities: accept deposits from their members only, grant the loans to their members and perform investment activities within the scopes provided for by the law. In addition, the credit unions are entitled to undertake the loan obligations for the purpose of attraction of the financial resources.

Non-banking deposit institution – credit union – is the enterprise registered in organizational-legal form of the cooperative that accepts deposits from its members only and grants loans to them, performs banking activities permitted by this Law, its main goal is not gaining of the profit [1, p.1]. The above Law is applicable to the non-banking deposit institutions – credit unions and its purpose is legal regulation of their activities in accordance with Organic Law of Georgia on the National Bank of Georgia, Georgian Law on Entrepreneurs and other legislative acts. [2, p.1]. Principles of activities of the credit unions stated by the law include: voluntary membership, their direct participation in credit union management. Credit union may accept the deposits from its members only and grant the loans to its members only, make investments in treasury obligations, commercial banks, in a form of short-term deposits and grant short-term loans to the other credit unions.

Activities of the credit union are governed by the general meeting, supervisory board and executive board. The supreme body of the credit union is general meeting that makes decisions within the authorities granted by the legislation and charter.

Control over the management board of the credit union is provided by the supervisory board, accountable, in turn, to general meeting. Supervisory board is elected by general meeting for 2-year term; number of board members shall be from 3 to 15.

Executive board is elected by the general meeting for 2-year term, number of members shall

be from 3 to 9. Management board is headed by the executive director. Authorities of the general meeting, supervisory board and executive board shall be determined by Articles 7, 8 and 9 of the Law on Non-Banking Institutions – Credit Unions.

In Georgia the credit unions are basically specialized on support to development of small and medium business. They are distinguished from the banking sector with high interest rates, each depositor for them is a shareholder and the profit is distributed between them as well.

Certainly, in Georgia, formation of the agrarian credit system of cooperative type similar to Germany would create real conditions for development of the agricultural food sector funding and crediting system. World practice showed that in agrarian sphere significant effects cannot be achieved without the state intervention. Therefore, the role of the state in the processes of creation and regulation of the agricultural food sector crediting system is quite significant.

Certainly, creation of the effective agricultural credit system should be based on the effective use of the members' assets that could be achieved through relatively simple conditions for obtaining of the loan, low interest rate, mutual trust, joint and several responsibility and exclusion of the corruption.

Implementation of the above measures would contribute to expansion of production scale in agrarian sector of Georgia, formation of the competitive environment, development of the cooperative associations and dealing with the food security problems.

Conclusions and recommendations

Development of the agrarian credit system of cooperative type requires from the government implementation of the systemic and complex changes that should be oriented towards agrarian industrial integration. Studying and analyzing of the issues of agrarian credit system management allowed us to make the following conclusions:

- State programs implemented by the government of Georgia cannot ensure support to rural development, oriented towards long-term effect. Analysis of the enterprises' survival statistics allows to make this conclusion as well, it showed that the rate of survival of the enterprises in 2 years is less than 50%;
- Capabilities of the state institutions are limited and oriented towards realization of the approaches of international organizations that are supported by the relevant financial resources;
- Formation of the farmers' groups is mostly motivated by gaining of the grants and subsidies only, frequently they are not able to appreciate

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profitability of their business launching or development;

- It is significant to provide support to the cooperatives that are oriented towards long-term goals and strategies, with the members oriented towards sustainable development of the farm economies and commence organized management of their activities. It is desirable that the farmers properly appreciated the benefits of cooperative-type associations [11, p. 124].

- For the purpose of approaching with the EU legislation in the sphere of food safety, Georgian government should implement the relevant regulations for stimulation of farmers' unification in cooperatives and improvement of the visibility of products created by the cooperatives.

- Commercial banks operating in Georgia cannot ensure normal functioning and development

of agrarian sector, as they regard that funding of agricultural production cannot contribute to the success of their business. The only actual solution to this problem is to form special agrarian credit system.

- Creation of the credit cooperatives would contribute to financing of small farmers and their equipping with the relevant technologies, create real conditions for development of the agrarian sector. Stimulation of availability of credit and insurance system would allow introduction of the new technologies and effective management of the agrarian terms [8, p. 75], though, without active intervention of the state implementation of systemic changes and obtaining of significant effect would be impossible.

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