The Role of Foreign Investment in Financial System for Development of Economy in Transition Countries: A Case of Georgia

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Abstract

The transition from a centrally planned to a market economy means first of all the change in the allocation mechanism of financial resources: from centralization to decentralization. As a result, the role of banks in the transition will change as well because banks and capital markets play an important role in the allocation of the financial resources in a market economy. Hence, the transformation debate puts up different approaches to the financial system reform in transition economies. The growing presence of foreign-owned financial institutions during the 1990s is one of the most striking structural changes. Currently, more than half of the banks in the region are foreign-owned, accounting for about two-thirds of total bank assets. In some countries the share of foreign bank assets relative to total assets of the banking system is even more than 75%.This study analyzes the foreign investment in banking sector as a case of Georgia.

Keywords: *Foreign investment, transition countries, Georgia, banking and economic development*

Introduction

The development of a financially sound and market-oriented banking system is often thought to be fundamental to a successful transition from a communist to a market-based economy. Although bank intermediation in transition economies remains stunted, particularly where progress in reforms is limited (Fries and Taci 2002), the financial systems of transition countries have changed dramatically over the past decade. The growing presence of foreign-owned financial institutions during the 1990s is one of the most striking structural changes. Currently, more than half of the banks in the region are foreign-owned, accounting for about two-thirds of total bank assets. In some countries the share of foreign bank assets relative to total assets of the banking system is even more than 75% (Naaborg et al. 2004).

Financial markets in the transition countries have grown in size and complexity. They are still dominated by the banking sector but stock markets, bond markets and even private equity have become important aspects of the region's financial systems. Nevertheless, financial markets are still less developed than in other countries at comparable levels of income.

Further development of the financial sector would yield significant returns in terms of economic growth, particularly in the countries with the lowest current levels of financial depth. Access to finance has a significant effect on the ability of firms to invest and increase revenues, particularly smaller firms.

There is a growing interest in the impact of foreign banking on the financial system and the economic development of emerging and transition countries (Claessens et al. 2001; Iakova and Wagner 2001; Mathieson and Roldos 2001). During the past decade, many former communist countries have made substantial progress in the transition from a centrally planned economy to a market-based economy. In recent years, progress has

been particularly significant in restructuring and consolidating the banking sector. This has mainly been accomplished through the privatization of state owned banks and the opening up of the banking sector to foreign ownership. The increasing foreign bank presence since the 1990s is one of the most striking developments in the banking system in the transition economies. I find that, on average, foreign-owned banks account for more than half of the total number of banks in 2000 and hold more than two-thirds of total bank assets in most transition economies. However, the importance of foreign banks varies a lot among countries. Still, foreign bank presence in all transition countries is considerably higher than in the European Union countries. (Claessens et al. 2001; Noyer 2001)

Determinants of Foreign Investment in Some Selected Transition Countries

Foreign investment in CIS is relatively lower than foreign investment in European Transition countries. The main drawback of low investment made by Western Countries in CIS is geographic farther distance than European Transition countries. I present some indicators of the foreign investment in banking sector of Georgia with very close countries in the same region (see figure 2 and table 1). A striking feature in the financial evolution of the transition countries has been the rapid growth of foreign banks. In the more advanced countries foreign banks account for a dominant share of assets in domestic markets. Foreign ownership of local banks remains much lower in the CIS. It has been argued that foreign banks introduce into the host country the skills and range of services prevailing in the home country. However, foreign banks – particularly new entrants to an existing market – tend to have poor information on local borrowers, especially small firms, and may restrict their lending to larger enterprises. Moreover, foreign banks tend to focus on household loans, as relatively little information is needed for these and no collateral is generally required. Despite these possible limitations, foreign banks appear to have a positive effect on financial development. An alternative explanation would be that foreign banks are entering markets that have already achieved a high level of development and have no discernible impact. The quality of institutional development also affects both the level of financial development and the entry of foreign banks. Foreign banks appear to have no positive effect on financial development. Table 1 shows that domestic credit to private sector (in most literate this ratio determines the financial development indicator) increased while foreign bank's share in total assets also increased in Georgia and CIS countries (see figure and table 1).

Domestic credit to private sector in CIS countries increased from 13 per cent to 38 per cent in 2009, at the same time foreign bank increased by 50 percent. This rejects the main consensus which says that foreign bank enters to market after country has sufficient and enough financial development.

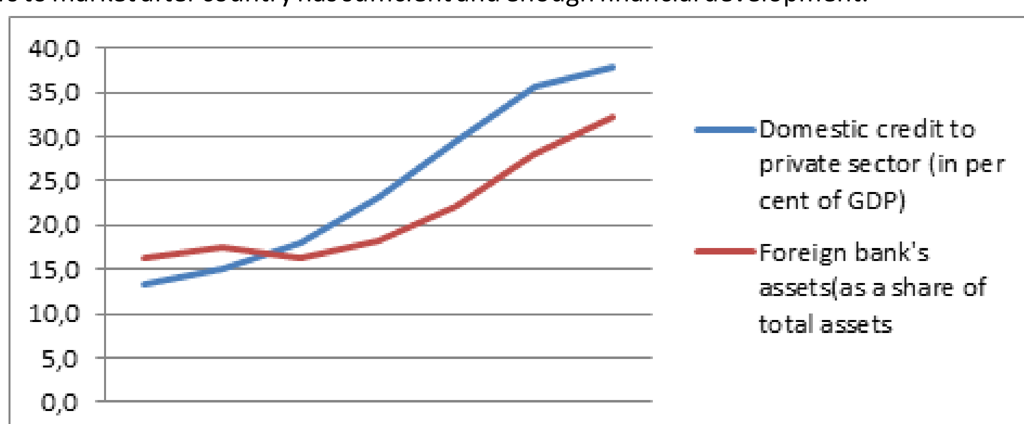

Figure 1. Financial development and Foreign Banks' share, 1999-2009

Sources: EBRD Transition Reports 2008, Central Banks of Georgia, Azerbaijan, Armenia, Ukraine, Russia.

Table 1. Financial development and Foreign Banks 'share in selected CIS countries

	2003	2004	2005	2006	2007	2008	2009
Domestic credit to private sector (in per cent of GDP)	13,4	15,1	18,06	23,08	29,46	35,54	37,82
Foreign bank's assets(as a share of total assets)	16,3	17,6	16,4	18,3	22,2	28,1	32,2

Sources: Central Banks of Georgia, Azerbaijan, Armenia, Ukraine, Russia

The single most important fact about financial systems in transition economies is that they have less depth and breadth than those of market economies at comparable levels of development (where development is measured, for simplicity, by per capita GNP).

Banking sectors in transition countries differ from their counterparts in many developing and emerging market countries by the high percentage of assets held in banks with majority foreign ownership. The change in foreign participation in banking in these countries from the early transition years to the later ones is dramatic. This paper investigates the impact of extensive foreign ownership on the performance of banks in Georgia. Besides I want to give also small ownership for some selected CIS (Common Independent States).These countries are Armenia, Azerbaijan, Russia Federation and Ukraine.

Since the end of central planning, when the financial sector was almost entirely controlled by the state, transition banking has evolved in four stages. The first involved the establishment of banks in the early 1990s. The second witnessed bank failures and systemic crises that affected almost all transition countries in the mid-1990s. The third stage involved lengthy restructuring through privatization and the entry of foreign banks. By the end of the century, most banks were privately owned, and foreign banks dominated the sector in many transition countries. In the fourth and current stage, banks in most transition countries have established sound balance sheets, and the industry has become well regulated and broadly competitive. By 2005 the foreign bank asset share was over 70 per cent in most CEB, SEE. The bank ownership structure in the Commonwealth of Independent States (CIS) is rather different. While there is substantial foreign ownership in Georgia and Armenia, no state ownership, state ownership is still considerable in Azerbaijan, Russia. Elsewhere in the CIS, domestic private banks prevail. In the larger economies of Azerbaijan and Russia, foreign ownership was about 10 per cent of assets in 2005 while in Ukraine it was about 20 per cent. In many CIS countries an uncertain economic environment and the threat of asset appropriation continue to pose significant risks to foreign banks.

Entry by foreign banks, together with the extent and maturity structure of foreign lending, provides an indicator of whether countries have succeeded in establishing safe, transparent and enforceable rules and regulations for financial markets. Foreign ownership and entry also presuppose the existence of private banks or considerable bank privatization, since otherwise foreign institutions are unable to invest in local banks and are not enthusiastic about competing with domestic banks that enjoy public subsidies. Foreign participation as measured by the share of foreign-owned banks in the total assets of the banking system is unusually low in the transition economies. Two of these countries, where foreign participation has reached significant levels, are Latvia and Hungary, which have made considerable progress in bank privatization. In Latvia, both Nordic and Russian banks have gained a significant presence. Hungary, which has long had the most liberal policy towards foreign bank entry of any east European country, has attracted foreign banks from many advanced economies

Figure 2 and Table 2 illustrates the development of the relative number of foreign and domestic banks in selected some CIS countries for the period 1999–2009, while Table 2 gives the absolute number of foreign banks for the individual countries. In 1999, 64 foreign banks were present in the countries in our sample, accounting for almost 16 per cent of all banks. In 2008-2009, their number had risen to 173, accounting for more than 30 per cent of all banks. In particular, in Georgia foreign bank has 90 per cent of total assets, in Armenia and Ukraine foreign banks has about 50 percent of total assets , in Russia and Azerbaijan financial

system is not yet liberalized and foreign bank has little share ,18 per cent and 9 percent. In Georgian, Ukraine and Armenia, the number of foreign banks grew very strongly compared to total number of banks in the sector. Number of foreign banks increased from 9 in 1999 to 15 in 2009 in Georgia .In Russia and Azerbaijan, the number of foreign banks was about the same during 1999-2009

Figure 1 and Table 1 show foreign bank assets as a percentage of total bank assets in CIS and Georgia countries. It appears that foreign bank participation increased considerably during 2004-2009. After several banking crises hit most transition countries in the mid-2000s (see Caprio and Klingebiel 2002 for an overview of the different crises), bank privatization furthered foreign participation. Initially, most sales involved medium-sized banks. Later on, the larger state-owned saving banks were sold too.

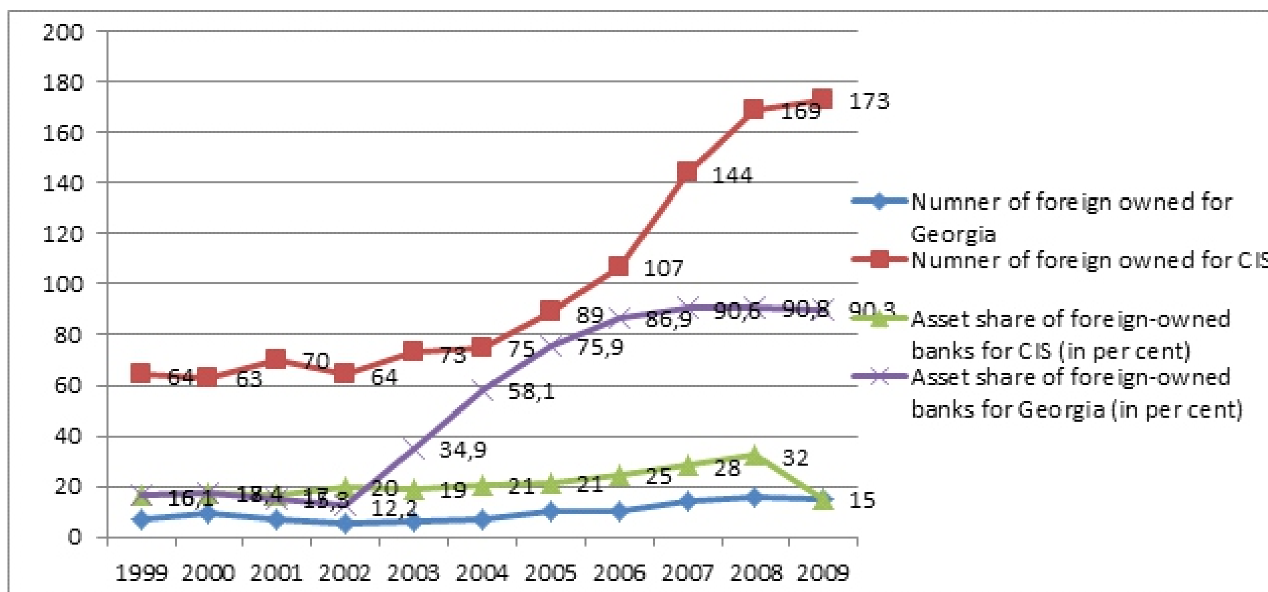

Figure 2. Number of Banks and Total Bank Assets in selected CIS Countries : Foreign versus Domestic, 1999–2009

Source: Foreign and domestic banks: CIS Countries: Georgia, Azerbaijan, Armenia, Ukraine, Russia. Central banks of Azerbaijan, National Bank of Georgia, Azerbaijan, Ukraine, Relative amount of foreign and domestic bank assets: all the above countries.

How should we expect foreign ownership to affect the performance of individual banks in these transition countries? Claessens, Demirgüc-Kunt and Huizinga (2001) investigate performance differences between domestic and foreign banks in eighty countries, both developed and developing, over an eight-year period from 1988 to 1995. These authors find that foreign bank entry was followed by a reduction in both profitability and the overhead expenses of domestic banks. Hence, these authors suggest that foreign participation improves the efficiency of domestic banking. However, banking sectors in transition economies are different from their counterparts in the developed or the developing countries due to the legacies of central planning.

Another cost of foreign bank entry is pointed out by Agenor (2001). Since foreign investors may not be familiar with the emerging markets, they tend to retreat promptly and massively at the first encounter of difficulty. This may lead to deeper crises in domestic financial markets.

Table 2. Number of Foreign Banks and shares According to Central Banks,1999-2009

Georgia	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009
Number of banks	39	32	29	27	24	21	19	17,0	19	20	19
Numner of foreign owned	7	9	7	5	6	7	10	10	14	16	15
Asset share of state-owned banks (in per cent)	0.0	0.0	0.0	0.0	0,0	0,0	0,0	0,0	0,0	0,0	0,0
Asset share of foreign-owned banks (in per cent)	16,1	17,4	15,3	12,2	34,9	58,1	75,9	86,9	90,6	90,8	90,3
Armenia											
Number of banks	31	31	30	20	19	20	21	21	22	22	21
Numner of foreign owned	12	11	14	8	9	9	9	10	12	12	13
Asset share of state-owned banks (in per cent)	3.5%	3.8%	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Asset share of foreign-owned banks (in per cent)	44,4	45,7	57,7	54,3	51,3	56,7	48,7	45,8	49,0	50,5	n.a
Russia											
Number of banks	1349	1311	1319	1329	132	1299	1253,0	1189	1136	1108	1102
Numner of foreign owned	32	33	35	37	41	42	52	65	86	102	103
Asset share of state-owned banks (in per cent)	n.a	n.a	n.a	n.a	na	na	na	na	na	37,5	na
Asset share of foreign-owned banks (in per cent)	10,6	9,5	8,8	8,1	7,4	7,6	8,3	12,1	17,2	18,2	0,0
Azerbaijan											
Number of banks	70	59	53	46	46	44	44	44	44	46	46
Numner of foreign owned	5	5	5	4	4	5	5	5	6	9	9
Asset share of state-owned banks (in per cent)	82.5%	60.4%	58.3%	62%	55.3%	56.1%	55.2%	0,5	42.4%	42.5%	0,4
Asset share of foreign-owned banks (in per cent)	0,0	4,4	5%	4,1	5,2	5,8	6,6	6,1	7,5	9,1	9,4
Ukraine											
Number of banks	161	154	152	157	158	160	165	170	175	184	181
Numner of foreign owned	15	14	16	15	19	19	23	27	40	46	48
Asset share of state-owned banks (in per cent)	12.5%	11.9%	11.8%	12.3%	9.8%	9.8%	9.4%	8.9%	8.0%	11.5%	12.7%
Asset share of foreign-owned banks (in per cent)	10,5	11,1	12%	13,0	12,1	12,1	21,3	35,0	39,4	51,1	51,4

Sources: Central Banks of Georgia, Azerbaijan, Armenia, Ukraine, Russia

The investment climate in the CIS countries is dominated by a complex set of relationships between the still–pervasive public sector and incumbent firms, as well as the public sector's interference in private sector activity. Extensive government regulation in the form of business licensing, inspections, and certification, combined with low civil service salaries and more generally weak public administration, provide incentives for rent–seeking by public officials. In turn, barriers to entry, impediments to competition (including weaknesses in domestic competition policy and trade barriers), ineffective bankruptcy procedures, and weak corporate governance allow inefficient incumbent enterprises to remain in operation.

Financial intermediation to finance investment, especially by small and medium sized enterprises (SMEs), is limited by underdeveloped banking systems and capital markets. In turn, weak property rights,

contract enforcement, and bankruptcy procedures present obstacles to further strengthening of the banks. The remainder of this section describes the main factors influencing the quality of the investment (FDI investment) climate in the CIS countries based on information supplied by country.

In Georgia, a liberal foreign investment policy (including unlimited tax–free repatriation of capital and profits, no currency controls, access of foreign investors to all but a few strategically significant sectors), membership in the WTO, and stable foreign exchange and inflation rates (except for a temporary surge following the Russian crisis) have favorably affected the investment climate, as have Georgia's strategic location as a conduit for Caspian oil exports to the west and relatively favorable conditions for tourism and agricultural development. However, several factors were perceived as having negatively affected. The unstable border area with Russia, instability of politics and security has reportedly also adversely affected investor confidence till 2002. However, FDI increased 212 million dollars on average in 1995-2005 after Rose revolution and then after it reached to 1170 million dollars in 2006.

Aggregate investment in the CIS countries contracted sharply following the breakup of the Soviet Union. More efficient use of existing investment could undoubtedly be made through better governance. Nevertheless, FDI generally has fallen dramatically short of levels needed to offset the low domestic investment rates. There is a huge gap between the levels of cumulative net FDI inflows per capita into some of the transition economies of Central and Eastern Europe and Common Independent states (CIS). Average annual levels of net FDI inflows, CIS countries have 62384 million dollars while CEE has 69948 million dollars and World has 1114189 million dollars (EBRD (1994, 2000)

As Table 3 and figure 3 determine, after collapsed of Soviet Union, FDI to former Soviet Countries and CIS increased as expected. These countries were the new markets for the foreign companies. FDI increased in Russia was much more than other CIS countries. FDI in Georgia was average 4 % of GDP and 109 million dollars. FDI in Georgia increased from 212 million dollars in 1995 to 1564 million dollars in 2008.After conflict with Russia, FDI dropped dramatically to 764 million dollars.

Table 3. Foreign Direct Investment (FDI), million Dollars

	1995-2005 (annual average)	2006	2007	2008	2009
Georgia	212	1170	1750	1564	764
Armenia	121	453	661	1132	838
Azerbeijan	1215	-584	-4799	14	473
Russia	5527	29701	55073	75461	38722
CIS	11104	44717	78124	10985	62384
World	741045	1459133	2099973	1770873	1114189
CEE	13279	54669	90968	122588	69948

Sources: World development Indicator

Lastly, Regulation may also affect the activities of foreign banks. In Slovenia, for example, liberalization of foreign borrowing by residents and the abolition of interest-rate ceilings on deposits have created a more competitive environment, but only since 1999 (EBRD 2001). Likewise, Hungary did not initially permit banks to provide financial and insurance services. Changed legislation in 1999 resulted in a movement towards a model of universal banking (ECB 2001). Once established abroad, foreign banks focus their activities mainly on large enterprises. The activities of foreign banks are also dependent on the mode of entry. A takeover goes along with the acquisition of the existing client base.

Banks with foreign investment in Georgia

It is remarkable that in terms of ownership structure the banking sector is represented by powerful

investors, which are capable of injecting additional capital/liquidity, if needed. This situation actually took place during the current recession in 2008-2009. Along with parent institutions, the role of international financial institutions should be pointed out not only in terms of injections but, in the context of virtually guaranteed additional support.

As of 2009 the Georgian banking system consisted of 19 banks. The total assets of the banking sector equaled 46.2% of GDP. 13 Georgia-based banks and 2 branches of foreign banks operated in Georgia with foreign capital participation. The non-residents' share in banks' authorized capital amounted to 79.7%. The international financial organizations accounted for 10.3%, private banks – for 55.6%, and other investors – for 34.2%. The banks created with foreign capital participation controlled 89.1% of total assets. The banks also accumulate 89.2% of the total loan portfolio and 90.9% of non-banking deposits. (see Table 2 and Figure 4)

I demonstrate all banks registered officially in National Bank of Georgia according to years and ownership of banks in Appendix C and Appendix D. In 2008 the Georgian banking system comprised 20 banking institutions, of which 18 commercial banks represented Georgian resident banks, and the remaining 2 were subsidiaries of a Turkish and an Azerbaijani bank. In the same period there were 683 units of commercial banks (125 branches and 559 service centers). For comparison, at end-2007 there were 540 structural units operating. The shareholders of the bank are the „HSBC Europe (Netherlands) BV" registered in the Netherlands (accounting for 70% of the stocks) and the „Wings Establishment" registered in Lichtenstein (30% of the stocks). The JSC „Progressbank" is fully owned by the LLC „Kala Capital".

Georgian banks made an agreement with the International Finance Corporation, the European Bank for Reconstruction and Development, the US Overseas Private Investment Corporation, the German Kreditanstalt für Wiederaufbau, the Dutch Development Finance Company (FMO), the parent banks and finance groups on allocation of additional funds in 2008. As a result, the Georgian banks obtained funds in the form of loans, subordinated loans, and direct participation in equity capital. In total, these funds were sufficient for the banks' needs to meet their foreign liabilities without shrinking loan portfolio.

As we indicate the GDP growth and investment in chapter 2 that Georgia enjoyed a successful year in terms of economic performance in 2007. According to preliminary estimates of the Department of Statistics, the real growth rate of the gross domestic product reached a record high level in recent years equaling 12.4% in 2007. The 2007 GDP growth rate exceeded the 2006 level by 3.1 percentage points. The main factor contributing to the economic upturn represented foreign capital inflows. Net foreign capital inflows in 2007 exceeded 20% of the GDP. (see Figure 3)

The amount of foreign direct investment in Georgia in the first half of 2008 made 955.4 million USD, which is 16.1% more than in the first half of 2007. The largest investments in the Georgian economy in the first half of 2008 came from the United Arab Emirates (202.8 million USD).

Figure 3 shows the largest share of foreign direct investments made in Georgia in the first half of 2008 were made in the industrial sector (620.7 million USD, which is 65% of total investments). 260.9 million USD was invested in privatization (27.3% of total FDI) and 73.7 million USD in the banking sector (7.7% of total FDI). You can see from the Table 3, the FDI in each sector. On average FDI in banking sector is 6.7 % of total.

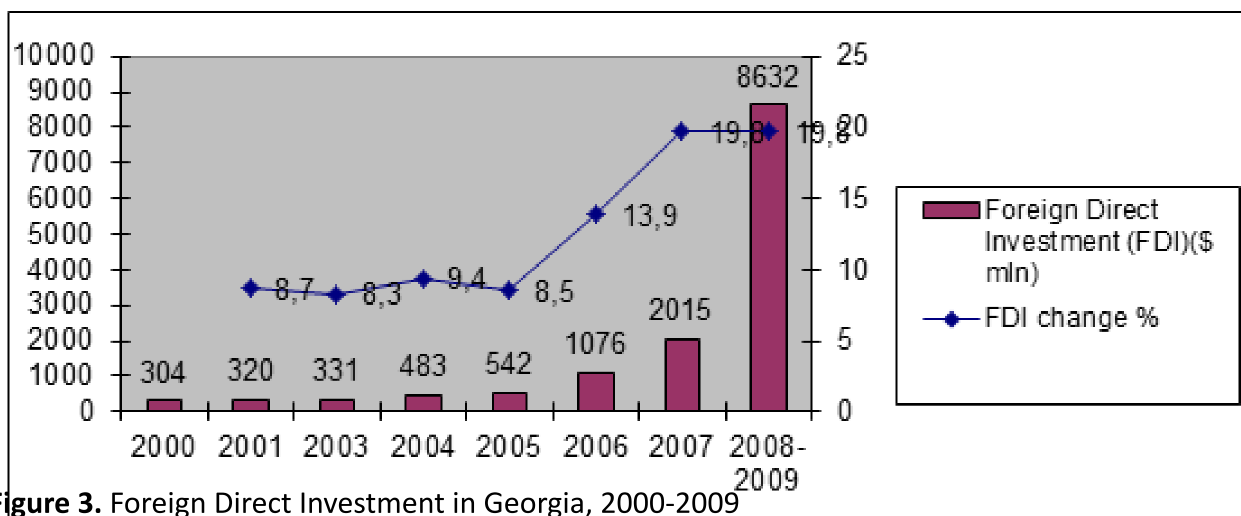

Figure 3. Foreign Direct Investment in Georgia, 2000-2009

Sources: National Bank of Georgia, Websites of Banks in Georgia

Since 2003, Georgia has implemented liberal regulations in order to secure financial stability of the local commercial banks and to promote Georgian banking sector as the favorable investment destination. Favorable bank reforms have increased the interest of large foreign banks in the Georgian banking market. In March 2006 Group “Societe Generale” acquired the controlling stake in Bank Republic. In October 2005, Kazakh bank Turan Alem, one of the largest banks in the CIS acquired the controlling stake in Silk Road Bank. In January 2005, VTB bank of Russia acquired 51% of shares of United Georgian Bank, one of the top three banks in Georgia. In addition, subsidiaries and branches of commercial banks from Greece, Turkey, Azerbaijan and Germany are operating in the Georgian market. You can see the shareholders of banks in Georgia from the table 3. Growth rates of ”financial intermediation” are significantly lower than in the previous year, but still remain high. In recent years this sector showed the highest growth rates.

In last trends, Halyk Bank Georgia, a subsidiary of Kazakhstan's Halyk Bank (People's Bank), obtained its license for operation in Georgia in early 2008 and invested approximately USD 50m. A study of the Georgian business environment, which “proved suitable for stable economic activities,” was a key motivation for First British Bank as well. Shares of the bank are owned by London-based Monte Cristo Capital, which holds a 67% stake, while Georgia's TbilAviaMsheni holds the remaining stake. Monte Cristo Capital Limited set up the bank through its purchase of Bank Tetri for 8.5 million GEL in 2007. Standard Bank's acquisition by UAE Investment Company, Dhabi Group, and subsequent name change to Kor Standard Bank also made business news headlines in March 2008. Salford Capital, which had owned the bank since 2005, sold Standard Bank for around USD 42m to Kor Bank, a newly registered commercial bank in Georgia wholly owned by Dhabi Group.

As of December 31, 2007 the Georgian banking system included 20 banking institutions, of which 18 represented Georgian resident commercial banks and 2 were subsidiaries of the Turkish and Azerbaijan commercial banks. By the end of 2007 20 commercial banks and 539 structural units (415 subsidiaries and 124 service centers) of 13 commercial banks operated, compared to 18 commercial banks and 416 structural units of 13 commercial banks operating by end-2006.

Georgian commercial banks, as indicated in Table 2 accounts for 86.9% of total banking sector assets. Foreigners had more than 50% of these banks' capital. Nonresidents control 73.5% of the banking sector assets.6 out 10 banks obtained foreign investments from different foreign and international financial organizations, in particular, the European Bank of Reconstruction and Development (EBRD), the International Financial Corporation (IFC), the German ”Deutsche Elasmobranchier Gesellschaft” (DEG), the German ”Kreditanstalt fur Wideraufbau” (KfW), JCS ”Procredit Holding”, the German ”Kommerzbank”, the Russian ”Vneshtorgbank”, the Kazakh ”Bank Turan Alem”, the Austrian ”Bank Austria Kreditnastalt”, the Armenia

"Cascade Bank", the French bank "Societe Generale", etc.

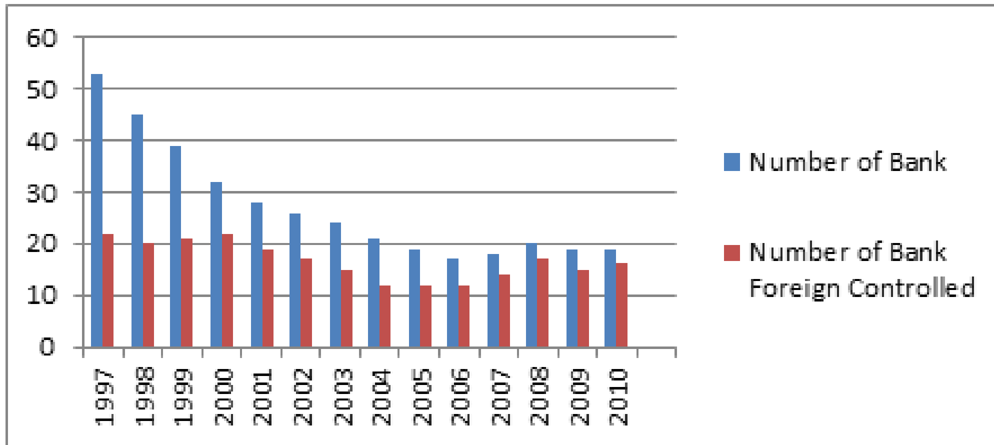

Figure 4. Georgian Bank Composition, 1997-2010

Sources: National Bank of Georgia

In 2005, the Georgian banking system was represented by 19 banking institutions, of which 2 were branches of Turkish and Azeri banks. During the last decade, despite decrease in the number of banks, the banking sector was characterized by dynamic increase rate. The rate of banking system growth exceeded that of other sectors of economy. The year of 2005 was especially successful for the development of banking system. Namely, the total assets of the banking system increased by 50% and, based on preliminary estimates amounted to 21.3% of GDP, net loans increased by 83%, liabilities by 56%, deposits by 31%, capital by 29%, and annual profit by 2.2 times.

The interest towards the Georgian banking system also increased, and was followed by the growth of foreign investments. As a result, the share of foreign investments in Georgian resident commercial banks increased from 33% of the total capital of the banking sector up to 50%. 10 commercial banks, with foreign investments in their capital, operated in Georgia, and their share in the total assets of the banking sector was 76%. Foreigners owned more than 50% of the banks' capital.(see table 4) Out of 10 commercial banks operating with the participation of foreign capital, 6 banks have investments of different foreign and international financial organizations, among them: European Bank of Reconstruction and Development –EBRD, International Financial Corporation– IFC, DEG, KFW, Procredit Holding, German "CommertsBank", Russian Vneshtorgbank", Kazakh "Bank Turan Alem", "Bank Austria Kreditanshtalti", Armenian "Kaskad Bank". In 2005, following commercial banks are withdrawn 'TbiluniversalbanK' and 'cartul bank'

Table 4. Ownership of Banks and Mode of Entry Indicator in Georgia, 1999-2010 years in ml GEL

	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
Total Assets	579	725	878	1114	1332	1699	2548	3124	9497	11308	11107	9916
% Domestic	97.4	94.8	87.2	73.9	70.6	61.0	42.8	35.3	32.2	20.7	20.4	14.3
% Foreign	2.6	5.2	12.8	26.1	29.4	39.0	57.2	64.7	67.8	79.3	79.6	85.7
% De Novo	87.9	40.4	15.8	4.6	4.7	3.3	3.2	4.0	1.6	5.7	4.0	14.0
% M&A	12.1	59.6	90.3	95.4	95.3	96.7	96.8	96.0	98.4	94.3	96.0	85.7
Total Deposit	292	433	600	874	1121	1303	2256	2444	7881	3481	3632	5399
% Domestic	99.5	98.7	88.2	73.8	70.1	59.4	35.5	35.8	28.9	23.4	17.5	20.6
% Foreign	0.5	1.3	11.8	26.2	29.9	40.6	64.5	64.2	71.1	76.6	82.5	79.4
Total Loan	78	428	489	629	780	964	1730	2025	5210	5369	5729	5438
% Domestic	99.6	93.8	84.7	71.3	68.2	59.9	22.8	33.8	33.7	17.4	19.8	16.6
% Foreign	0.4	6.2	15.3	28.7	31.8	40.1	77.2	66.2	66.3	82.6	80.2	83.4

Sources: National bank of Georgia, websites of banks and author calculations.

Conclusion

Georgian authorities and banking decision makers deserve to be given special attention and enough credit for their achievements in building market-oriented banking systems from almost scratch in such a short time period. They were successful in certain areas of structural reforms such as effective design and implementation of the privatization process, competitive policies, and prudential regulatory framework. With regard to privatization and foreign bank participation, the private sector currently holds 100 percent of the assets in banking. The entry of foreign banks had an important impact on the modernization of domestic banking systems through the introduction of modern banking practices, and product and service innovation.

Georgian authorities should keep their markets open to well established foreign banks and institutions rather than adopting strictly selective policies in order to take advantage of maximum benefit to increase the competitiveness and efficiency of banking market.

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