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65th ROSE-ROTH SEMINAR

**GEORGIA TOWARDS EURO-ATLANTIC
INTEGRATION**

SECRETARIAT REPORT

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1. NATO Parliamentarians, Georgian and Alliance country officials and independent experts attended the 65th Rose Roth Seminar in Tbilisi, Georgia, from 19-21 April 2007. The seminar focused on a range of issues shaping Georgia's aspirations and prospects for Euro-Atlantic integration. It featured a number of prominent Georgian speakers, including President Mikheil Saakashvili, Vice-Prime Minister and State Minister for European and Euro-Atlantic Integration Giorgi Baramidze, the Speaker of the Parliament Nino Burjanadze, the Minister of Foreign Affairs Gela Bezhuashvili, the Deputy Minister of Defense Batu Kutelia and the Minister of Economy Giorgi Arveladze. Senior officials from NATO, the European Union, the Organization for Security and Co-operation in Europe (OSCE) and the International Monetary Fund (IMF), including EU Special Representative Peter Semneby and OSCE Ambassador Roy Reeve, as well as Latvian Foreign Minister Artis Pabriks and speakers from NGOs and academic communities also addressed the gathering.
2. Georgia's aspirations for NATO membership are realisable. This was the clear message that emerged from the deliberations. Three other related themes dominated the proceedings. Firstly, the Georgian government and the Georgian people are very focused on Euro-Atlantic integration. President Saakashvili told participants that joining NATO is now the government's and, indeed, the public's highest foreign policy priority; even the political opposition in parliament has endorsed this goal. Having nearly completed the Individual Partnership Action Plan (IPAP) and now engaged in Intensified Dialogue (ID), Georgian officials are optimistic that the Alliance will be prepared to initiate a Membership Action Plan (MAP) at the next NATO summit. This would put Georgia on the road towards NATO accession. For their part, NATO officials stressed that membership of NATO is performance based. The determination of NATO members to extend a MAP to Georgia will be based on a collective judgement that Georgia has made sufficient progress in a broad range of reforms.
3. Secondly, Georgia has made good progress in implementing a range of economic, political and administrative reforms which have not only helped reconstitute state authority since the Rose Revolution in 2003, but which have also moved the country closer to the Euro-Atlantic community. Last year, the World Bank rated Georgia as the most successful reformer among the world's developing countries, and it moved to number 35 in the global rankings of best business climates. Government officials stressed that they are determined to continue pushing radical liberal reforms and administrative modernization. To achieve these ends, they are employing best practices learned from other transition cases and, in particular, are drawing many lessons from the Baltic States, which have strongly supported the Georgian reform process. Both NATO and the EU have also offered very important support for the transition process.
4. Thirdly, although Georgia's progress across the board is indeed impressive, its transition is far from complete. There are concerns about democratic and judicial practices that elicited admonitions from several speakers. They reminded Georgian participants that their government must adhere to best democratic practices, not only to fulfil their ambitions for Euro-Atlantic integration, but also to ensure the sustainability of the political, administrative and economic reform process. The message here was that concrete actions are needed to ensure that national elections in two years are fully fair and transparent and that judicial reforms, in particular, are implemented to ensure both the independence and incorruptibility of Georgia's judges. Although the economic outlook is very positive, there are still outstanding problems including price volatility, the management of government surpluses and the current account balance.
5. Finally, the seminar also focused on the problem posed by breakaway regions in Georgia, the role of Russia in these conflicts and the possible implications of failing to advance the reconciliation process. Here too there was a sense that more can be done on both sides of the divide to foster a

climate of trust that might advance reconciliation. At the same time, Allied countries will not accord any country in the region a veto on Georgia's membership aspirations, nor are they prepared to allow intransigence on the part of the leaders of breakaway regions, or their sponsors, to become an excuse to thwart Georgian goals, particularly if Georgia is acting in good faith to resolve the conflicts.

GEORGIA'S EURO-ATLANTIC ASPIRATIONS AND PROSPECTS

6. NATO PA President José Lello laid out several principles of NATO membership that have typically guided the thinking both of aspirant nations and member states that ultimately invite candidate countries to full membership. Candidates must be willing to share the responsibilities of the Alliance, and their accession should bolster stability and reinforce good neighbourly relations. He noted that the conflict regions within Georgia remain a concern, but that Georgia's candidacy should not be held hostage to those conflicts if Georgia is acting in good faith to resolve outstanding differences. The decision to invite countries to join the Alliance is collective and depends both on whether members are convinced that the candidate is ready and if it can make a contribution to the general security order. Georgia, Mr. Lello noted, will have to be firm, patient, and continue its reform process while "rolling with the punches." He suggested that the Assembly is prepared to assist in the process.

7. As Giorgi Baramidze outlined in his remarks, Georgia agreed to an IPAP with NATO and this has helped shape and discipline the internal reform process. All the assessments Georgia has undergone in the IPAP process have been positive, and another positive assessment is expected on 16 May. The hope, and indeed the expectation of Georgia's leaders is that a MAP will follow, which Georgian leaders strongly feel would help sustain the country's momentum.

8. Latvia's Foreign Minister Artis Pabriks also focused his remarks on the enlargement question. He noted the myriad parallels between the Baltic experience and that of Georgia; Latvia, he said, has strongly supported Georgia's reform process and its efforts to ready itself for Alliance membership. He suggested that it is misleading to see enlargement as a process destined to poison relations with Russia. Latvia has managed to preserve good relations with Russia since it joined NATO. The minister felt that the door should be open for Georgian accession, and he also suggested that the EU must work to engage Georgia more deeply in the institutional life of the Union. Georgia cannot stay where it is and cannot go backwards. It can only go forward, and this dynamic will invariably shape its political and economic life in fundamental ways

9. Every Georgian speaker who addressed the seminar pointed to a very strong national commitment to Euro-Atlantic integration, and most suggested that acceding to NATO remains the country's highest foreign policy priority. Polls now indicate that 80% of the public supports integration with NATO, as do all the opposition forces in the national parliament. This is indeed a very high percentage and helps explain why the Georgian government is so focused on the issue. President Saakashvili noted that NATO's values are particularly attractive to his country and are lending support to Georgia's internal reform efforts.

10. Georgian speakers, including Nino Burjanadze, were also very quick to point out that they do not feel that their country will simply be a "consumer" of security. Georgia, they asserted, has the assets, capabilities and the political will to project security, based on the shared values common to all NATO members. Georgian officials are very aware that their security is defined by events far away from Georgia's territory and, for that reason, have deployed troops to Iraq, Afghanistan and Kosovo. Although the keynote speaker, Oksana Antonenko, suggested that Georgia's distance could pose some problems for the Alliance were Georgia to join, its geographical location could also bolster

Western leverage in a highly unstable region near Iran and the Middle East. Donald Maclaren, the Ambassador of the United Kingdom to Georgia, also pointed out that Georgia would play a pivotal role in any European effort to tighten crucial links with Central Asia and, indeed, to revive old land trading routes to the Far East.

11. Georgian officials also readily acknowledged that Russia sees NATO enlargement as a threat to their own security. The Georgian response is that they want to have a close and mutually beneficial relationship with Russia and they do not believe that NATO membership would have any negative long-term effects on that relationship or on Russian security. They cite the Baltic States' relations with Russia and the fact that those states hardly pose a threat to Russian national interests. That the three Baltic states are able to deal with Russia in a confident manner creates conditions for a healthy and mutually beneficial relationship.

12. Oksana Antonenko prefaced her remarks by noting that she believes Georgia will eventually be a member of NATO and also noted the high level of commitment to this end demonstrated by the Georgian people. Still, there are questions about the wider context of Georgia's accession, the general security environment of the South Caucasus and the potential challenges to NATO involved with extending the full security umbrella to this region.

13. Antonenko noted that the South Caucasus has very quickly become part of the Euro-Atlantic community. This would have been unimaginable a few years ago. A number of factors lie behind this change including Georgia's rapid transformation, growing energy security concerns and the mounting strategic importance of the South Caucasus. Turkey's push for accession to the EU, as well as Bulgaria and Romania's accession to the EU and NATO, are all transforming the Black Sea Region and drawing it closer to the West. The danger is that this area remains a potential tinderbox and there are very evident security problems both in the North and South Caucasus.

14. Another challenge is that internal transformation in the region is not yet completed. Democratic reforms have not produced stable sustainable political systems and even Georgia has yet to work through a stable democratic succession. Freedom House continues to call Georgia an incomplete democracy, although it also notes the striking improvements that have been registered there. The message from the West is clearly that Georgia must work on its democracy in parallel with its reforms of the state and the economy; yet no one in Georgia is seriously suggesting that a Pinochet model might be the path for Georgian progress, particularly as this would exclude it from integration with the Euro-Atlantic community. Several Georgian participants stressed that Georgia's democracy is very young and the current government is very popular. It can hardly be faulted for not having lost an election. The problems in Azerbaijan and Armenia are, by comparison, more severe. Still there are questions, according to Antonenko, as to whether Georgia is quite yet ready for membership and if membership for Georgia can be contemplated at a moment when Russian troops are still deployed on its territory and secessionist problems are not yet resolved. There are also questions as to whether all NATO members are prepared to extend a membership prospect in light of this situation.

15. Internal instability, Antonenko continued, is compounded by international tensions. Russia and the West have failed to find a *modus vivendi* with regard to the region, which has indeed become a focal point of Great Power rivalry. Georgia is paying a price for this, as has been made evident by the Russian trade embargo. But Russia is not the only problem. There are also enormous tensions between Armenia, Azerbaijan and Turkey, and this renders the security situation in the region very tenuous and creates at least the potential for escalation.

16. All that said, Georgia's NATO aspirations have helped consolidate the reform process and Georgia's political elites have encouraged Georgians to deal with internal disputes in ways designed to avoid the use of force. As one participant suggested, Georgia has no positive and viable alternatives to the course it has taken. Georgia's success is being watched and could be a factor, for example, in Ukraine's approach to NATO. It has also demonstrated to Russia that it should not simply assume that it will dominate its neighbours to the south; Russia needs to think about new and more positive ways to engage with its neighbours in the region.

17. Georgia's military transition has made rapid progress since the Rose Revolution, although there is still more to achieve. The focus has been on making Georgian forces smaller and more professional while introducing modern planning, budgeting and acquisition techniques. Ensuring democratic control over the national military has also been a top priority. Georgia has paradoxically benefited from the fact that it never had a large and entrenched military structure, and this has accorded it a degree of agility in adopting more modern defence strictures including advanced planning and budgeting techniques. The Georgian Deputy Minister of Defense, Batu Kutelia, noted that the government is about to embark upon a Strategic Defense Review looking to the year 2015. This will be done in close consultation with NATO member states. Georgian forces are expected to remain light and well under CFE (Conventional Forces in Europe) limits but still capable of defending Georgian interests. The quality of Georgian forces has increased substantially, in part, because of the standards established through the IPAP process.

18. James Mackey from NATO Euro-Atlantic Integration and Partnership Directorate argued that NATO is present in Georgia because it is a region of strategic interest to the West and also because it clearly subscribes to the values that animate the Alliance. NATO has dedicated a great deal of attention to Georgia's IPAP in which Georgia has laid out the reforms it plans to undertake. NATO, in turn, has provided a series of activities designed to support that effort.

19. An Intensified Dialogue with NATO began in 2006 and deals directly with Georgian aspirations for membership and ways in which its reform process might be shaped to help it accede to the Alliance. This is dealing with a range of political, military, human rights and legal issues. NATO recognizes that Georgia has made tremendous progress on all of these fronts in recent years, but it is too early to say if it has made sufficient progress to be extended a Membership Action Plan. It is all the more difficult as there are no precise guidelines on this, and it will be up to each of the members to determine Georgia's readiness. That said, the Allies have been impressed by the economic resilience of Georgia's economy in the face of the Russian embargo. Liberalization has advanced quickly in Georgia with very tangible results. Georgia has also moderated its policies toward the breakaway regions in a way that appears to be creating new opportunity for dialogue and resolution. This is very welcome.

20. On the other hand, as the OSCE and ODIR (Office for Democratic Institutions and Human Rights) have noted, recent local elections suggest that Georgia has further to go in terms of the development of its democracy. It needs to reform its judiciary and establish that branch's absolute independence. It also needs to manage better its budget surpluses, which, although impressive, are also tempting spending practices that may not be sustainable. Finally, Georgia will have to work hard to ensure that it stays within the plans of its strategic defence review by matching short-term acquisitions with long-term planning.

21. Mackey concluded that Georgia needs to make the most of criticism from its friends. It has time to correct some of the problems pointed out by OSCE and ODIR but it needs to begin right away to work to address these shortcomings. The Alliance, meanwhile, will have to decide under what

conditions Georgia might be invited to join it given the existence of conflict zones on its territory. They must do so, keeping in mind that this process should not be held hostage to those with an interest in sustaining the conflict no matter how flexible Georgia is.

22. Georgia also has long-term aspirations to join the European Union, but it recognizes that the prospects for doing so are more distant. Its relationship with the EU is structured under the European Neighbourhood Action Plan, which was endorsed in 2006. The parliament is working to introduce European legal standards into the corpus of Georgian law where this is possible. It hopes to gain greater access to the EU's internal market and is intent on the establishment of free trade arrangements with the EU, particularly in light of the recent Russian embargo.

23. Peter Semneby, the EU's Special Representative for the South Caucasus, spoke of the EU's interest in the region, which has increased as a result of the EU's enlargement, but also because of the EU's special relationship with both Russia and Turkey. There are several countries in the region with European ambitions and this puts the EU in a difficult position. It wants to encourage reform and integration but it does not want to disappoint expectations. The EU is thus compelled to acknowledge the aspirations of these countries without endorsing them. The strategy is working, he argued, given the positive reforms that are taking hold in much of the region and the EU's improved relations with the countries there. The EU is paying close attention to the security challenges in the region. It has seen the Rose Revolution as a positive development and sees the consolidation of democracy in Georgia as critical to the region. There are also important elections in Armenia, which the EU judges to be a critical marker for the democratic evolution of the region. The EU sees the so-called frozen conflicts as important barriers to this process, particularly as young people in Abkhazia have had no contact with Georgian society and have been raised on a diet of highly polarizing propaganda. There is an effort underway to give greater prominence to conflict resolution issues within the EU's Neighbourhood Policy.

THE BREAKAWAY REGIONS

24. Georgian officials were also anxious to demonstrate that the government is committed to adapting greater flexibility with regard to the breakaway regions in Abkhazia and South Ossetia and wants to begin an open dialogue. It also recognizes that any solution will have to involve some degree of decentralization or autonomy. In this regard, it was interesting that European models for ethnic reconciliation are being examined in Georgia. Italy's policies in the Sud Tyrol is one of these.

25. President Saakashvili and several government ministers, including Deputy State Minister for Conflict Settlement George Kaladze, insisted that they do not want to resolve these problems with military force but through peaceful negotiation. The president noted that all political forces in the parliament have endorsed this approach. Old models have failed to solve outstanding differences and the Georgians appear intent on using conflict resolution techniques, reintegration, IDP (Internally Displaced Persons) return, and confidence building to remedy the tensions. The government, however, will not agree to any division on Georgian territory and is accordingly very concerned about a proposed EU-Russian visa facilitation arrangement that could result in the EU implicitly recognizing passports Russia has issued in breakaway regions of Georgia. At several points during the conference the question was raised whether a decision to grant Kosovo full sovereignty might establish a precedent in the Caucasus. Some felt that this would not be helpful to Georgia, while others suggested that the situations were so different as to defy comparison.

26. George Kaladze noted that the government has undertaken a major anti-criminal operation in upper Abkhazia, but its general approach now is to solve the conflicts peacefully. It has committed

itself to demilitarising the regions around the disputed territory and the government has accordingly pulled back military installations and trenches. Georgia also hopes to foster economic rehabilitation in the breakaway regions which are isolated and impoverished.

27. Atanas Baltov, from the United Nations Observer Mission in Georgia (UNOMIG), noted that the UN is also working to promote dialogue, but he too lamented the lack of progress in Abkhazia. The Abkhaz side has refused negotiations and is insisting on Georgian withdrawal from the upper valley. Killings this past January in the Gali district and recent Abkhaz self-styled elections have hardened the stalemate. Roy Reeve, Head of the OSCE Mission to Georgia, also discussed the work of his organization in monitoring the situation in the breakaway missions and is working to facilitate dialogue among the parties. The OSCE has a small military mission in Tskhinval. It is also working on economic confidence building among the various communities while supporting NGO capacity building efforts. The OSCE is trying to work a three-stage process in South Ossetia involving confidence building, demilitarisation and economic rehabilitation and hopes that this effort will ultimately lead to talks to resolve outstanding differences. Despite some signs of progress, very little has been achieved on the ground. There are myriad security incidents, weapons are widely available, and various armed groups are moving through the zone of conflict. He noted that the Georgians have tabled a peace proposal, but no one has taken this up and Russia has rejected it. Tskhinvali has produced its own plan now but there is little consensus in South Ossetia about what the ultimate goal should be. Magdalena Frichova, the Caucasus Project Director at the International Crisis Group, noted that part of the problem is that there is not even a consensus on what kind of conflicts these are. Where Georgia sees political conflict, many in the breakaway regions see ethnic differences as the root of tensions. The situation, she said, is extraordinarily tense and could explode in violence if it is not properly managed. Economics is the one area where progress is possible, but there also are economic differences fuelling conflict. Those benefiting from lucrative smuggling and counterfeiting operations in South Ossetia will resist any reassertion of state authority. Still, many of the elite in South Ossetia are convinced that Russia is not the answer to their problems and is not a reliable partner.

28. Jonathan Cohen from the Joint Reconciliation Center focused his remarks on the Georgian-Abkhaz dispute. He pointed to the absence of an international consensus on how the problem ought to be resolved, which effectively means that an enabling environment for a solution remains elusive. There is also a fundamental asymmetry insofar as the conflict is an all-consuming matter in Abkhazia but not in Georgia. Compromise becomes very difficult in these conditions, and neither side, Cohen argued, has shown itself ready to make genuine concessions. The peace process is thus frozen. Efforts to sign a non-resumption of hostilities in 2005 and 2006 were intense and the road maps proposed by each side could have been the foundation for a genuine dialogue. But the opportunity was squandered. Events in Kodori in 2006 effectively ended efforts to do just this.

29. The Abkhaz have much narrower room for manoeuvre than do the Georgians. They are resisting change with the hope that Russia will somehow help and are, in the meantime, trying to build a more functional quasi state. They have had only limited success in doing so. For their part, the Georgians want a new dynamism injected into the peace process but seem hesitant about carrying out a genuine dialogue. Russia is obviously a key player in all of this, but sometimes the Georgians seem to discount any of the Abkhaz concerns by claiming it has been instrumentalized by Russia.

30. Confidence building is needed but so too are efforts to demonstrate that Georgia can be attractive to Abkhazia. Georgia's dynamic growth could help in this regard but is hardly sufficient to overcome the ethno-political dimension of the conflict, according to Cohen. Trade restrictions on Abkhazia will invariably prove counterproductive. Georgia could also more forcefully communicate its

sense that the start of the conflict represented a genuine tragedy. It is in a good position to do so, as the Rose Revolution was such a fundamental break with the previous governments of Georgia, which undoubtedly mishandled events in Abkhazia. Finally, there remains a great deal of work to do with civil society and NGO's, both of which are needed to create constituencies for peace and reconciliation.

GEORGIA'S TRANSITION

31. Georgia has passed through an extraordinarily rapid transition. As President Mikheil Saakashvili noted in his remarks, prior to the Rose Revolution four years ago, Georgia was, for all intents and purposes a failed state and many outside observers were sceptical that it could quickly build a viable democratic order. Vice Prime Minister and State Minister for European and Euro Atlantic Integration, Giorgi Baramidze, recalled that the last time Georgia hosted a Rose Roth Seminar, state structures were extremely weak, there were serious problems with the police and the military, and the government was having terrible difficulties asserting control over the Pankisi Gorge and the Autonomous Republic of Ajara. What has transpired since then has been nothing short of remarkable. From a point of administrative chaos, the virtual non-existence of an open national economy and the strangle hold of mafia like organizations, Georgia has moved rapidly to reconstitute the state's authority, abandon the structures and practices that made corruption endemic, launched a campaign to fight criminality, liberalized the national economy and opened it up to new disciplines and opportunities to play in global markets. President Saakashvili suggested that in the space of four years, Georgia had not only constructed a real state but had also emerged as one of the world's fastest growing economies.

32. Throughout the conference there was a sense that Georgia's impressive efforts to build state authority on more solid foundations could be undermined if democratic rules are not respected. Georgian government officials stressed that elections have been free and fair, although other observers including the OSCE and ODIR have suggested that recent municipal elections were not up to standard. There are concerns about the judicial system which has been used to fight crime but which some feel is not sufficiently independent. Giorgi Baramidze indicated that the government has a blue print for judicial reform and is using European systems as a model for court reform including the introduction of District Courts and Courts of Appeals. New magistrates are being selected. The president has also asked the EU to send justices to hear both criminal and business cases. Police powers are another area of concern, and there are worrying patterns of police brutality. Sectarian tensions are also a source of concern, and NGO representatives suggested that Georgian society still has very traditional elements that have linked nationalism to the country's orthodox traditions. This has inspired instances of xenophobic discrimination against those practicing other faiths. More efforts are needed to reach out to these minority groups in order to give them a stake in Georgia's democratic transformation. Greater decentralization of political authority is also needed.

33. On the other hand, a number of speakers, including US Ambassador to Georgia, John Tefft, were confident that Georgia has ample time before the next elections to reinforce those areas of its democratic structure which, outside observers argue, need to be strengthened. Georgia also enjoys a very open and unregulated media and this source of transparency and is helping to create a culture of accountability.

34. Georgian officials, however, were prepared to acknowledge that more needs to be done. Gela Bezhuashvili noted that Georgia is progressing from electoral to institutional democracy and there are signs that the process continues to advance. Relations between the governing coalition and the opposition have improved. The speaker of the Parliament, Nino Burjanadze, has worked hard to strike

up a dialogue with the opposition, which has returned to participate in the parliament after boycotting the institution. Dennis Sammut suggested that parliament has recently engaged itself in matters pertaining to conflict resolution and that this role needs to be further developed. He suggested that Georgian politics is maturing and the potential conflict resolving powers of the democratic processes are increasingly understood. Efforts to engage the opposition more actively are indicative of this.

GEORGIA'S RELATIONS WITH RUSSIA AND THE REGION

35. Georgia's primary ambition in its own region, according to Gela Bezhuashvili, is for the creation of a peaceful and stable region characterized by dialogue and with a capacity to play a positive role in the world. Georgia sees itself as part of the South Caucasus, an integral element of the Black Sea Region and, above all, a European nation. It has welcomed the enlargement of the EU to Romania and Bulgaria as this has extended the borders of Europe to the Black Sea. This will invariably have a munificent impact on the region as a whole. The Georgians also feel that successful liberal economic reforms are providing a model for the rest of the region and helping to open trade relations with neighbouring states. These ties are vital and have important implications, not only for the economy, but also for energy security.

36. Georgia's relations with Russia have suffered gravely over the past year, and the sources for these tensions are numerous and not only related to Georgia's Euro-Atlantic aspirations. Russia has used its energy and market leverage to pressure Georgia. The price of Russian gas exports rose substantially last year and in a manner that many Georgians believe was more than a simple market correction. At the same time, the embargo on a number of Georgian exports, the forced repatriation of some Georgians working in Russia, harassment of Georgians remaining in Russia and continued Russian intransigence with regard to the breakaway regions - including issuing Russian passports to citizens of Georgia living in those regions - have simply reinforced Georgia's desire to move to the West. They provide few other alternatives from the Georgian perspective and have made any "Russian option" unpalatable to the Georgian people. Russia's policy has effectively consolidated the Western consensus in Georgia. Beyond gas and its important internal market, Russia is offering very little to Georgia in terms of prospects for a fruitful relationship. From the Georgian perspective, Russia's mistake has been to assume that pressure would intimidate the state into compliance. In fact, it has had the opposite effect. According to the foreign minister, Georgia feels that the Commonwealth of Independent States (CIS), of which it has been a member, has lost its meaning and purpose and hardly represents a community of values to which it would want to adhere. Georgia, according to its foreign minister, is reconsidering the relationship.

37. The Director of the Fourth CIS States Department at the Russian Ministry of Foreign Affairs, Andrey Kelin, argued that the South Caucasus is so unstable as to make it impossible for Russia to achieve its own interests in the region, which are to establish good neighbourly relations. He noted that relations with Azerbaijan have improved and Armenia is a close ally and the goal is to have similar relations with Georgia. He argued that Georgia has chosen a radically different course without consulting the rest of the region; this has led to tension with Russia and has complicated efforts to deal with the problem of Georgia's integrity. Mr. Kelin asserted that Georgia is not yet ready for NATO membership, and he said accession would have "serious" consequences, although these were never fully spelled out. He disagreed with the link between the prospects for NATO membership and democratic reform and argued that NATO is not in the business of building democracies. He argued that NATO has become something of a Cold War relic which, since 1999, has played a destabilizing role in Europe. He also suggested that the West had reneged on promises on the rearmament of East Germany made by Manfred Woerner during the 2 plus 4 talks. Clearly, the extension of NATO into the Caucasus is thus seen in fully negative terms by Russia. Participants responded sharply to what they

saw as the implicit Russian threats to Georgia should it accede to the Alliance and also disputed the notion that the Alliance had somehow reneged on promises made during the 2 plus 4 talks.

THE ECONOMY

38. If the Rose Revolution made it possible for the construction of a functional state in Georgia, it also laid the foundations for a series of economic reforms that have launched commercial activity in the country. Of course, the two are interrelated. Economic take off, according to the Georgian Minister of Economy, Giorgi Arveladze, first required the dismantling of a stifling bureaucracy, massive privatisation, the eradication of a web of regulations and an effort to drive criminality out of national economic life. The EBRD, according to the Minister, has called Georgia the leading country in the fight against corruption. The policy has focused not only prosecuting those engaged in corruption, but also eradicating the conditions that made that behaviour possible and tolerated.

39. The government's leaders decided early on that only radical measures would work and, as suggested above, the results have been extraordinary. The international community has taken notice. Last year Georgia jumped from 120th to 37th position in the global rankings of best countries to do business. The goal this year is to leap into the top ten.

40. Tax reform has been critical. The tax system has been radically simplified and tax rates have been slashed. The country now has only seven different tax rates. Licensing new companies and permits have also been simplified, and if a company has not received a justified rejection for a permit within a short period after filing, it is automatically granted the permit. This eradicates opportunities for corruption and compels the state to be responsive to the needs of the business community.

41. Georgia has also eliminated minimal salaries, minimum hours and legal requirements on job protection. This has bestowed the country with impressive labour market flexibility and has, in turn, sparked job creation. The country has privatised virtually the entire commercial patrimony of the state with the exception of the railroad. This has been largely beneficial, although it has precipitated budgetary management challenges with which Georgia must deal. The health care system, which was in utter collapse, is also being turned over to the private sector *en masse* with guarantees from investors for new hospital construction. There will be a massive shakeout in that industry, but this has occurred in other sectors as well. Restructuring along liberal lines has effectively required streamlining and this, in turn, has both eliminated jobs and created new ones. Such draconian strategies bear certain political risks, but as the government was elected with 96% of public support, it was decided that there was ample political capital to take tough measures, which, while not immediately popular, would ultimately bear fruit. This was the thinking behind the decision to fire the entire traffic police force which had become utterly corrupt. The government, however, has undertaken measures to help those who have lost jobs retrain for new ones. The government is also working to restructure social spending so that state funding is available only to those most in need of public support. Means testing has been introduced, and this has allowed the government to concentrate its social policies on the most needy strata of Georgian society.

42. Georgia's increasing appeal as a place to do business is reflected in rising foreign investment. President Saakashvili noted that while Foreign Direct Investment in 2003 stood at only \$50 million, the government is expecting foreign investments this year to reach \$2 billion. The largest investors last year were the United States and the United Kingdom followed by Kazakhstan and Turkey. At first, these inflows were driven by privatisation, but they increasingly reflect investor willingness to establish their own presence in Georgia.

43. Georgia is also reorienting its trade – a process that has been made all the more imperative in light of Russia's trade boycott. Turkey has replaced Russia as Georgia's leading trade partner, and a free trade agreement with that country is currently being negotiated. Turkish investors have embarked on several major infrastructure investments including the airport in Tbilisi and a second in Batumi, which will serve both Georgian and Turkish citizens living in the region. A deal has been struck with Azerbaijan to build a railroad link to Turkey which will ultimately be a link between Beijing and London.

44. Georgia's growth has been impressive and will be roughly 10% in 2007. The sources of growth are also shifting away. In 2004 the construction sector drove growth but the manufacturing sector, trade and finance are becoming relatively more important.

45. Despite the very positive performance of the Georgian economy, there are several points of concern. According to Robert Christiansen from the IMF, the greatest challenge to Georgian officials lies in managing the influx of foreign exchange which could become a source of high inflation. There are also potential problems in the balance of payments given Georgia's very high current account deficit. Investment inflows are helping to finance these deficits but there are concerns about the sustainability of this arrangement. Fiscal deficits are also quite large relative to the money supply and this, too, is pouring liquidity into an economy that could overheat as a result.
