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# SMALL INNOVATIVE BUSINESS DEVELOPMENT PROBLEMS IN GEORGIA

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**Abstract.** The sustainable development of small innovative entrepreneurship is quite a difficult task and requires systematic work, which must involve both the state, academic and industrial circles. It is necessary to create connecting rings between these areas. Based on these trends, a whole set of measures should be developed and implemented, which should be aimed at the mass acquisition of innovations. It should be noted that only with the fruitful interaction of science, entrepreneurship, society, and state and municipal bodies will it be possible to ensure the rapid pace of economic development of the country and the establishment of an innovative economy.

Georgia has a positive attitude towards expected innovations along with the development of the country's economy. The relationship between income level (GDP per capita) and innovation is positive. A positive trend line indicates expected innovations in terms of revenue levels. Georgia's performance is in line with expectations of its level of development, the relationship between the input and output of innovation is negative. Georgia produces less innovative products compared to the level of innovative investments.

**KEYWORDS:** SMALL INNOVATIVE BUSINESS, REGULATORY IMPACT ASSESSMENT, INNOVATION INPUT SUB-INDICES, GLOBAL INNOVATION INDEX.

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## INTRODUCTION

Since the 90s, many reforms have been carried out in the field of economy in our country, but it still faces a number of challenges. The goals stated in the strategic and programming documents related to the significant reduction of poverty and unemployment are still unattainable. Georgia is still one of the most unequal countries in terms of inequality between Europe and Central Asia.

The strategy of economic development, in the absence of competition, has facilitated the benefits of free trade to be limited to specific groups in society. Consequently, economic wealth could not be created, so the transfer of public investment in human capital and technology was not enough, and free markets could not eliminate this shortage.

The main message of the country's economic policy is to encourage inclusive growth, thus increasing productive employment. In order to achieve high economic growth and reduce inequality, productive assets must be increased, which must be achieved by investing in human capital. But the State Policy is aimed at improving the conditions of the poor by redistributing policies rather than involving them in economic activity.

## Main body

Achieving innovative development dynamism is vital for the development of our country's economy. Activation of in-

novative processes requires constant development, improvement of the legal framework, development of methods for its implementation, spending solid funds on innovative ideas and projects, raising the level of intellectualization of the basic factors of production. (GGP, 2021-2024)

Creating a favorable business environment for entrepreneurship and attracting investments and stimulating an innovation-based economy is one of the activities of the Parliament of Georgia. In order to develop better regulations, the Parliament of Georgia decided to institutionalize the Regulatory Impact Assessment (RIA) system. (MP. Info Card, 2016).

The key is that policies and laws under the RIA must be designed to perform their tasks at minimal cost. "Better regulation" ensures that political decisions, which are made in an open, transparent manner. Present Drafting regulations, the consultation process is weak and ineffective, and mandatory requirement to consult with stakeholders and experts doesn't exist. (EC, Impact Assessment Guidelines, 2009)

The business sector often, in the case of important acts, receives information when the acts are already registered in the parliament and therefore there is less opportunity to respond to it due to time and legal restrictions. A number of negative initiatives have been named by business associations and experts, which were initiated in a short period of time as a result of such an inefficient consultation process and insufficient analysis of the impact of regulation.

In response to problems with the quality of regulations

and the challenges posed by the growing number of new regulations, the Georgian government has acknowledged that the policy-making process must be fully participatory and evidence-based, as evidenced by the 2015-2017 Policy Planning Reform Strategy. The Strategy Action Plan envisages the mandatory introduction of the RIA from 2017 to minimize the negative impact of regulations on citizens, businesses, trade and investment. (GP, SCEEP, Article 9, 10, 2021).

According to international best practice, the RIA methodology for developing countries should be light / simple, flexible and relevant to existing resources. And the RIA should target only those regulations that can have the most significant potential impact on business. (BDO, Program 'Produce in Georgia', Assessment, 2018)

The Government of Georgia has developed an updated strategy for the development of small and medium enterprises in 2021-2025, which aims to identify the specific interests of the country in the field of small and medium enterprises, adapt them to relevant policies through successful international practice and respond to the challenges of small and medium enterprises. (MESD, Draft Small Medium Entrepreneurship Development Strategy 2021-2025).

Government Program 2021-2024 "European State Building" continues to support investment projects of innovative and high-tech startups, with the involvement of regional technoparks and universities, programs to support new innovative ideas. (OECD. Introductory Handbook for Undertaking RIA, 2008)

Let's Review Government Programs Implemented to Promote Entrepreneurship and Improve the Entrepreneurial Environment. LEPL "Produce in Georgia" has been implementing projects since 2014, which combines several components. (Produce in Georgia, Annual Report 2015) these are:

- Access to finance;
- Provision of real estate;
- Consulting services.

As a result of the research we can identify the most problematic issues of the program.

Increase the level of proper awareness of entrepreneurs:

1. Develop a targeted communication strategy that will be tailored to the demands and needs of entrepreneurs. Will be tailored to the target audience, to strengthen and scale the technical assistance and consulting services component. It is desirable to create platforms where entrepreneurs can share their experiences with each other;

2. Audit and optimize the financial support component.

Increase the 2-year co-financing period, which will make the program more flexible and long-lasting. Lowering the loan repayment threshold (currently \$ 75,000) will provide an opportunity to finance a variety of projects. Additional funding will help cover unforeseen expenses for entrepreneurs and eliminate working capital shortages;

3. Tax policy review.

Reducing/eliminating VAT on equipment (fixed assets)

and importing raw materials will significantly improve business processes and improve the business environment. As well as reduction/cancellation of income tax on reinvested funds. The entrepreneur has to reflect the property and loan income, which is tax deductible after the release of the product;

4. More involvement of the agency in loan approval.

Increasing the role of the program will lead to the financing of interesting, promising projects that fail to fully comply with banking procedures and fail to receive funding;

5. Introduce the principle of one window.

It would be good if the agency "Produce in Georgia" on the principle of "one window" will provide assistance to the private sector, both in terms of planning and implementation of programs, as well as informing the state about various opportunities and obtaining professional advice;

6. Creating a unified electronic database of active entrepreneurs.

Unified electronic renewable database of interested and active entrepreneurs, accounting / analysis of those who have been denied funding by the bank, will help to identify such gaps as: sector, reason for refusal, amount requested, etc. Analysis will be very helpful for interested entrepreneurs for effective application planning;

7. Formation of monitoring and evaluation system.

A step forward is the fact that in the 2016 budget, (PG, Action Plan of the Committee on Sectoral Economics and Economic Policy, 2022) indicators are written in appropriate quantitative indicators, (MF, Data, 2022) which will give us adequate opportunities for program evaluation and civic engagement. (GYLA, Evaluation Report, 2021).

Since 2015, the Agency has been implementing a micro and small entrepreneurship promotion program in the regions of Georgia (Produce In Georgia. SME, 2020) - through financial assistance or consulting services, the state has provided funds from 5,000 to 15,000 GEL to start-up and expand entrepreneurship-winning entrepreneurs. (EDA Annual Report, 2016).

Changes in the micro and small grants program have been implemented since 2020, increasing the maximum amount of grant funds from 20,000 GEL to 30,000 GEL. The share of co-payments for new beneficiaries of the program has been reduced from 20% to 10%, and for existing beneficiaries from 50% to 25%. The program will fund more than 300 activities for this phase. (Produce in Georgia, Annual Report 2020).

In 2015-2018, 6,212 projects were funded under the program. The total amount disbursed by the Agency under the Micro and Small Grants Program amounted to 46.9 million GEL, while the investment exceeded 61 million GEL. More than 15,000 jobs were created.

The program covers any business activity, except for the production of primary agricultural products and related services. Priority is given to projects focused on accommodation and tourism services, starting a new business, starting / expanding a business by a female entrepreneur, in a rural / highland village, by IDPs.

The tools help entrepreneurs during the incubation period, for the first two years. After that, in terms of financial

co-financing, the agency terminates its relationship with the companies and provides consulting services after which the company itself continues to pay. If the entrepreneur is not solvent during these two years, the state will immediately stop co-financing the interest (Bochorishvili, 2014).

The agency conflicts with the content of the program regarding the financing new enterprises. Start-ups who do not have a loan business or related assets are not eligible for the program. Obstacles for an entrepreneur to start a new production are: 1. the interest rate, which is quite high for him, and 2. the collateral, which the entrepreneur cannot fully secure. The program is not for those who have only an idea.

Innovation Development Processes are coordinated by the Georgian Innovation and Technology Agency, which was established in 2014. (Order of the Ministry of Economy and Sustainable Development of Georgia, 2014).

The Agency also ensures the activities of the Research and Innovation Council, (Government Resolution, 2015, 3) which unfortunately has not yet started to work, therefore the state strategy in the field of innovation, the priorities of the strategy and the persons responsible for its implementation have not been created.

On June 22, 2016, the Government of Georgia also adopted the Law on Innovation, which aims to create and improve the national innovation ecosystem necessary for the socio-economic development of Georgia, build an economy based on knowledge and innovation in the country, promote the absorption of technologies created in other countries (Georgian Law on Innovation, 2016).

Relevant structures have been established in the regions to support innovative activities: investment-venture funds, technoparks, business incubators, business accelerators, technology transfer centers, innovation laboratories (FabLab, IILab, etc.).

As a result of the Agency's programs in 2014-2020, 941 residents, 785 businesses in e-commerce, 130 students in the innovation camp were trained. The total number of beneficiaries in 2014-2020 is 56,000, across the regions - 4,556. 135 startups - 100,000 GEL with a grant, 21 startups - 650,000 GEL with a grant, 423 startups - 15,000 GEL with a grant. A total of 579 startups, in which a total of 40 million GEL was spent.

If we look at the ranking of the most innovative countries in the world, which is mainly compiled by the World Intellectual Property Organization (WIPO) and the news agency Bloomberg, we are not so lucky.

Georgia is in the 63rd place with 32.40 points in this rating. Georgia lags behind the countries of the former Soviet Union: Estonia (25th), Latvia (33rd), Russia (45th), Ukraine (50th), Moldova (54th) and Armenia (59th).

According to the rating published by Bloomberg, Georgia could not be included in the list of 40 countries. Georgia lags far behind the other countries in the process of developing and implementing innovations. (South Korea, 2022)

The World Intellectual Property Organization uses more than 80 criteria to compile the Innovation Index. The Innovation Index is grouped by innovation input costs and innovation output.

According to the table, Georgia has a better position in innovating than in publishing. It is also clear that in 2021 Georgia has spent more on innovation than in 2019, while the output of innovations is lower than in previous years.

Georgia has a positive attitude towards expected innovations along with the development of the country's economy. The relationship between income level (GDP per capita) and innovation is positive. A positive trend line indicates expected innovations in terms of revenue levels. Georgia's performance is in line with expectations of its level of development. The relationship between the input and output of innovation is negative. Georgia produces less innovative products compared to the level of innovative investments.

Georgia is relatively strong in terms of market sophistication and the weakest in terms of infrastructure.

7 columns of the Global Innovation Index, Georgia ratings: Innovation input sub-indexes:

1. Institutions (political, legal and business environment) – 35;
2. Human resources and research (education, higher education, research and development R&D) – 60;
3. Infrastructure (information and communication technologies) – 85;
4. Market sophistication (credit, investment, trade, diversification and market scale) – 34;
5. Business sophistication - 61 (knowledgeable workers, innovative connections, knowledge absorption);  
Innovation Release Sub-Indices:
6. Release of knowledge and technology (knowledge creation, knowledge influence, knowledge diffusion) – 75;
7. Production of creative product (intangible assets, creative goods and services, online creativity) – 74.

For the past decade, the GII - Global Innovation Index - has been a leading tool for measuring innovation. Recognizing that innovation is a major driver of economic development, GII aims to provide an in-depth analysis of innovation in up to 130 economies.

The creation of venture funds, techno parks and busi-

**Table № 1. Georgia Ratings 2019 - 2021**

	GII	Innovation input	Innovation output
<b>2021</b>	63	49	74
<b>2020</b>	63	54	71
<b>2019</b>	48	44	60

Source: <https://www.globalinnovationindex.org/Home>

**Table № 2. Strengths and weaknesses of Georgian innovations**

Strong sides			Weak sides		
code	Indicator	Score	code	Indicator	Score
1.2.3	Extra cost	16	2.1.4	PISA (International Student Assessment Program. Low Assessment in Reading, Mathematics, and Science)	70
1.3.1	Start a business easily	2	2.3.3	Global corporate R&D investors	41
2.1.5	Student-teacher ratio, average	3	2.3.4	QS University Rating	74
4.1.1	Ease of taking credit	14	3.2.2	Logistic performance	111
4.2.1	Easy protection for a minor investor	7	3.3.3	Environmental Certificate	102
4.3.1	Average weighted interest rate	5	5.1.4	GERD funded by businesses	89
5.1.5	Employed women%	23	6.2.5	High-tech production	90
5.3.4	Foreign direct investment	9	6.3.1	Sale of intellectual property	97
6.2.1	Increase in labor productivity	24	7.1.4	Creating ICT and organizational model	101
6.2.2	New business	11	7.2.5	Export of creative goods trade%	104

Source: WIPO statistics, [https://www.wipo.int/global\\_innovation\\_index/en/](https://www.wipo.int/global_innovation_index/en/)

ness incubators does not automatically ensure the implementation of innovative policies in the process of economic development (Gudushauri, 2020). We are facing inappropriate spending of funds in this direction, therefore, moving Georgia on an innovative path of development requires a lot of effort.

It should be noted that innovations are still taking place in the country, but their realization does not take place inside most of the enterprises and are private initiatives of individual representatives of the business. This is due to the fact that in many enterprises the organization's staff is not ready to implement large-scale innovations, moreover, it is less interested in using its knowledge and skills to introduce innovation in the organization. The reasons for this can be many things: underdeveloped infrastructure, insufficient interest and motivation of the employee, lack of support for innovative thinking of the employee, lack of ordering innovations in the enterprise, lack of intellectual property, periodic cash flow, lack of cash flow, and lack of funding.

## CONCLUSION

The sustainable development of small innovative entrepreneurship is quite a difficult task and requires systematic work, which must involve both the state, academic and industrial circles. It is necessary to create connecting rings between these areas. Based on these trends, a whole set of measures should be developed and implemented, which should be aimed at mass acquisition of innovations. It should be noted that only with the fruitful interaction of science, entrepreneurship, society, state and municipal bodies will be possible to ensure the rapid pace of economic development of the country and the establishment of an innovative economy.

Unfortunately, the state does not have the potential for

small innovative businesses and its role in the development of the country's economy and the creation of innovations. The unserious and superficial attitude towards this issue is well seen in the legislative space, in particular in the legal acts and in the state documents where small entrepreneurship is mentioned. I am not talking about the term "small innovative entrepreneurship", which you will not find in any document. To date, a single concept of a small enterprise adapted to the real business environment of Georgia has not been established. For example, in the Law on Entrepreneurs there is only the concept of entrepreneur. Law of Georgia on Innovation In the definition of terms, you will meet a start-up business, which is defined as an entrepreneurial entity defined by the Law of Georgia on Entrepreneurs, which has not been registered for more than 2 years in accordance with the rules established by the legislation of Georgia. A special tax regime has been introduced in the Tax Code - for micro, small and individual enterprises, in the data of the National Statistics of Georgia you will find various commandments. The methodology for calculating the size of a small enterprise has also changed very often in recent years.

It is desirable to establish a single state body, which will be responsible to the government for the development and implementation of innovative economic policies and the importance of the role of small innovative businesses and projects in this regard. It can be said that the measures taken by the Government of Georgia are not enough to support small innovative businesses and move the Georgian economy on an innovative path, there is still much to be done in this regard.

At the moment, it is difficult to positively assess the development of small innovative businesses in Georgia despite the fact that we have adopted the Law of Georgia on Innovation. Until now, there has been no proper regulation of innovation processes in small businesses.

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