

**ინოვაციური ეკონომიკა
და მართვა**

**INNOVATIVE ECONOMICS
AND MANAGEMENT**

ნანა შონია,
ეკონომიკის დოქტორი,
აკაკი წერეთლის სახელმწიფო
უნივერსიტეტი,
პროფესორი,
ქუთაისი, საქართველო
nana.shonia@atsu.edu.ge
orcid.org/0000-0001-7689-3800

ზურაბ მუშკუდიანი,
ბიზნესის ადმინისტრირების
დოქტორი,
ბათუმის ნავიგაციის სასწავლო
უნივერსიტეტი,
ასოცირებული პროფესორი,
ბათუმი, საქართველო
z.mushkudiani@bntu.edu.ge
orcid.org/0000-0003-0987-3564

*შემოსულია რედაქციაში:
თებერვალი, 2019
რეცენზირებულია:
მარტი, 2019*

NANA SHONIA,
Doctor of Economic,
Akaki Tsereteli State University, Professor,
Kutaisi, Georgia
nana.shonia@atsu.edu.ge
orcid.org/0000-0001-7689-3800

ZURAB MUSHKUDIANI,
Doctor of Business Administration,
Batumi Navigation Teaching University, Associate Professor,
Batumi, Georgia
z.mushkudiani@bntu.edu.ge
orcid.org/0000-0003-0987-3564

*Received: February, 2019
Accepted: Mart, 2019*

JEL Classification: E42, E44, E52, G15,

**ფასიანი ქაღალდების საჯარო
შეთავაზება და ქართული რეალობა**

**PUBLIC OFFERING OF STATE SECURITIES
AND GEORGIAN REALITY**

ანოტაცია. აღნიშნულ სტატიაში წარმოდგენილია საქართველოს სახელმწიფო ფასიანი ქაღალდების განვითარების შესახებ, წარსული და მიმდინარე პერიოდის გამოცდილების განხილვა, დადებითი და უარყოფითი მხარეების შედეგების დემონსტრირება და რეკომენდაციების შეთავაზება. სტატიაში გაანალიზებულია საქართველოს სახელმწიფო ფასიანი ქაღალდების ბაზარი, საერთაშორისო გამოცდილება და ასევე აისახება ამ ინსტრუმენტის მნიშვნელოვანი ფუნქციები საბაზრო ეკონომიკაში. სტატიაში ასახულია საქართველოს სახელმწიფო ფასიანი ქაღალდების ბაზრის მნიშვნელობა და აუცილებლობა, კანონის ის დებულებები, რაც ბაზრის ფუნქციონირების საფუძველს წარმოადგენს, საქართველოს სახელმწიფო ფასიანი ქაღალდების ბაზრის მონაწილეები და მათი ფუნქცია-მოვალეობები. კვლევის მიზანია საქართველოს მთავრობის ფასიანი ქაღალდების ბაზრის ამჟამინდელი მდგომარეობის შესწავლა, ანალიზი, ქვეყნის ეკონომიკაში მისი როლის, განვითარების და შესაძლებლობების განსაზღვრა.

საკვანძო სიტყვები: სახელმწიფო ფასიანი ქაღალდები; ფინანსური ბაზარი; სახელმწიფო შეთავაზება; ფინანსური ნაკადები; მონეტარული მიმოქცევა.

ABSTRACT. The paper presents information of the development of state securities of Georgia, review of the past and current period experience, demonstrating positive and negative side effects and Enhancement of recommendations. In this paper there is analyzed Georgian government securities market, International experience, and, also there are reflected the important functions of this instrument in the market economy. In this paper there is showed the meaning and importance of Georgian government securities market, the provisions of the law, which is fundament of markets functioning, Georgian government securities market's participants and their functions and responsibilities. The purpose of the research is study of current condition of the Georgian government securities market, analyze, defining its role in the economy of the country and to determine the opportunities for the development of this market.

Keywords: State Securities; Financial Market; State Offering; Financial flows; Monetary circulation.

INTRODCUTION

Securities, as a market object, perform a number of functions in the market economy [1, 2]: it can be accumulated as well as the accumulation of cash savings in the population, as well as mobilizing temporary free cash flows to finance budget expenditures; This instrument is regulated by monetary circulation; It is the source of investment for the creation of new enterprises, as well as the development of existing ones; It is

used as a tool for carrying out credit-settlement operations. State securities performs other functions as well: the state of securities emissions are monitored by the economic spheres and fields, territories and countries of the population, groups and layers of the population, the population and the state Redistribution; By issuing state securities, the state receives and creates a state debt[3, 5,7]:.

The value of the state debt in the world community is of particular interest. Joint state debt is the sum of state securities issued individually by all state bodies [9]:. This indicator is frequently published through mass media and is viewed during various television or political debates, although the total number is not a great deal if it is not specified. First of all, inflation refers to the specification [10]:. The nominal value of the bond is the amount that will be paid when covering the bond. This amount is known to the buyer from the very beginning [14]:. However, the fair value of the bond is the sum of goods and services that can be purchased by this bond in a specific period [12]:. The nominal value of the bond is unchanged and it does not change after the change in the inflation rate, but its daily real value changes.

In financial literature, it is considered that the state's securities are the worst type of instrument (Van Horne .2005: 263), but as the global financial crisis of 2007- 2010, this view is far from truth, as many states have failed to provide for securities issued by him. This event is known by default (ie bankruptcy and insolvency [11]). Other than that, this instrument is accompanied by other risks - impairment of the national currency of a given country, low liquidity and the risk of inflation [8]:.

OBJECTIVE OF THE STUDY

The purpose of this paper is to analysis of the current situation State Securities Market in Georgia and its role in the country's economy, to generalize the experience of the past period, securities development opportunities and ways to overcome problems, also to define and elaborate recommendations for the financial-economic development of Georgia

RESEARCH METHODOLOGY

The methodology used for this study was literature survey. The study was completely based on compiling the studies conducted so far on financial markets and state securities. The researchers collected different studies on the topic from different libraries, universities, and book stores. In reviewing the literature, both theoretical and empirical studies were taken into consideration. In total, several studies were collected for the review.

THE NOTION OF THE PUBLIC OFFERING OF SECURITIES

A public offering of securities may generally be defined as an offer made on behalf of the issuer to sell securities directly or indirectly to at least 100 persons or unspecified number of persons [15]:. The issuer shall enter into a contract which offers securities with a brokerage company or a financial institution with the relevant license for the distribution of securities.

When making a public offering of securities by the issuer, the holder of the securities at the same time shall have the right to propose to the issuer to include, in the established manner, the securities held by it in the public offering.

Offering and sale of securities shall not be considered as a public offering only in case of sophisticated investors, i.e. offering securities to sophisticated investors does not require procedures for the public offering of securities [4, 6]:.

A sophisticated investor is a person who has sufficient experience, property or income to sustain the financial losses caused by investment activities. A sophisticated (experienced) investor is a high net worth individual, a financial institution, a director of a financial institution, a legal entity whose capital is more than 1 million GEL or any other person recognized as such by the National Bank of Georgia. In addition, a high net worth individual is a person, whose proven property is more than 3 million GEL or whose annual income is more than 200, 000 GEL for the previous 3 years [18]:.

THE PROCEDURE FOR PREPARATION AND APPROVAL OF THE EMISSION PROSPECTUS

A public offering shall be made only through an emission prospectus prepared by the issuer based on the appropriate procedures, and prepared and approved in compliance with the requirements of the regulations established by the National Bank of Georgia.

The emission prospectus provides the potential investor with the information required for the decision on investment.

The emission prospectus is classified into 3 types according to its preparation, approval and offering procedure:

- A preliminary prospectus
- An approved prospectus
- A final prospectus

For the approval of the emission prospectus of the public offering of securities, the issuer shall submit an application of the public offering at the National Bank of Georgia, which includes:

- An application prepared in accordance with the procedure prescribed by the National Bank of Georgia;
- 3 copies of a preliminary prospectus

The National Bank of Georgia is authorized to have additional requirements for providing other information for the purposes of the public offering [16]:.

If the issuer is a reporting company and has submitted all the necessary reports for the previous 2 years, the National Bank of Georgia is entitled, based on its regulations, not to require the submission of the entire prospectus or require the submission of part of the information necessary for the prospectus.

If the securities of an issuer are admitted to at least one of the foreign recognised stock exchanges, such issuer may issue securities in Georgia in accordance with the stock exchange rules, without additional regulation [17]:. In that case, the issuer shall notify the National Bank of Georgia of the issuance of securities and the National Bank of Georgia, if necessary, shall assign a national identification number to the securities[13]:

PRELIMINARY PROSPECTUS

A preliminary prospect, as mentioned above, is a prospectus submitted to the National Bank of Georgia for approval.

The preliminary prospect shall include:

- information about the issuer, more specifically, its name (title), address and date of establishment, number and class of distributed securities (if any); the name of each holder controlling the issuer; if the issuer is a company - the names of the members of its governing body; if necessary - the name of the registrar of securities selected by the issuer, information about the possible conflict of interest related to the aforementioned persons;
- description of the activity of the issuer for the previous 2 years and possible major risks related to this activity. If the issuer carries out the activity for less than 2 years, it will present this information for the period between its establishment and submission of the application;
- individual financial statements certified by the auditor and in case of existence - consolidated financial statements for the previous 2 business years. If the issuer carries out the activity for less than 2 years, it will present this information for the period between its establishment and submission of the application.
- Information about securities to be issued including
 - information about the class and indicative number of securities;
 - the details of the procedure of signing, and if a brokerage company or a financial institution with the relevant license has signed a contract of the offering of securities and agreed to purchase a portion of the entire issue of securities - approximate details of such transaction;
 - information on whether securities are offered on behalf of holders of securities, and in case of such offering - names of the holders and the number of the securities offered by each of them;

- the method of calculation of interest on debt securities if the securities are interest bearing; information about the validity date of securities and the terms for any allowed forms of coverage;
- information about the possible use of the revenue received from the offer.

If the issuer is a reporting company and has submitted all the necessary reports for the previous 2 years, the National Bank of Georgia is entitled, based on its regulations, not to require the submission of the entire prospectus or require the submission of part of the information necessary for the prospectus.

The preliminary prospectus shall be signed by the chairperson of the supervisory council of the issuer and the authorized representative.

APPROVAL OF THE PROSPECTUS

Within 15 days after the submission of the application of offering to the National Bank of Georgia, the National Bank of Georgia shall consider it and if

- A) considers that the preliminary prospectus does not comply with this Law or the procedures established by the National Bank of Georgia, it shall send a written reply to the issuer, asking for further information which is necessary for the interpretation and clarification of the presented information; or/and it shall request the documents verifying the accuracy of the information included in the preliminary prospectus. After rectifying the above deficiencies, the issuer may submit the amendments to the application of offering. These amendments shall be considered again;
- B) approves the emission prospectus, in case of a written request by the issuer, it shall give the issuer a written consent on the approval of the emission prospectus;
- C) considers that the submitted information does not comply with this law or the rules established by the National Bank of Georgia, or if the issuer refuses to submit documents, data or clarifications referred to in this article, it is entitled to issue a written refusal to approve the prospectus;
- D) the issuer is not provided information in writing in accordance with subparagraphs "a", "b" or "c" of this paragraph, after 15 days the emission prospectus is considered to be approved.

On the basis of the final prospectus the National Bank of Georgia registers securities and assigns the national identification number to them in compliance with the procedure defined by the rule established by it.

The issuance of the emission prospectus shall be prohibited before it has been approved by the National Bank of Georgia.

Offering the sale of the relevant securities by the issuer or a brokerage company acting on behalf of the issuer or a financial institution with the relevant license, or gaining the consent on purchasing the relevant securities from the other person by the aforementioned entities shall be prohibited before the emission prospectus has been approved by the National Bank of Georgia.

THE FINAL PROSPECTUS

The current financial information included in the final prospectus may not be older than 18 months. The description given in the text shall correspond to the possible recent date.

Within 10 days or more as determined by the procedure established by the National Bank of Georgia, from the day when the prospectus is deemed to be approved, the issuer shall submit 3 copies of the final prospectus to the National Bank of Georgia. The number and price of the offered securities and the terms of the agreement of offering of securities shall be indicated on the first page of the prospectus. The final prospectus shall be applied for the public sale of publicly offered securities.

The approval of the emission prospectus by the National Bank of Georgia confirms that the information submitted by the issuer complies with this Law or the procedure established by the National Bank of Georgia, but it does not

verify the accuracy of the presented information. At the same time, it shall not be regarded as a recommendation of the National Bank of Georgia. The first page of each preliminary, approved and final prospectus shall clearly display the following words on its front page: “The approval of the prospectus by the National Bank of Georgia relates to its form and may not be considered as an opinion on the accuracy of its contents or on the value of the investments described therein”.

OFFERING PROCEDURES

The final prospectus shall be provided to investors prior to, at the moment of or during the sale. In case of necessity to change any material fact (more specifically, to change the number of securities or the closing date for the offering by the issuer in the emission prospectus or any other material fact) during the public offering, the issuer

- A) shall submit to the National Bank of Georgia the amendment to the application of offering in which all the changes made to it shall be defined;
- B) shall publish a notice in a newspaper or in other media prescribed by the procedure established by the National Bank of Georgia; shall declare the cancellation of the offer in its current form and suggests cancelling all contracts for sale of securities before the specified date without any price reduction.

If an amendment to the emission prospect is related to a material fact, the subscribers have the right to renounce the purchase of securities, and the issuer is obliged to return the paid sum to them without making any deductions, within 10 days after the refusal of the subscribers. The subscribers who do not renounce their purchase of securities are subject to new terms of the offering.

If after the commencement of a public offering the National Bank of Georgia becomes aware that a certain material fact has been misstated or omitted in the emission prospectus approved by it, the National Bank of Georgia is authorized to request the issuer to comply with the relevant procedures.

If other information included in the emission prospectus approved by the National Bank of Georgia was changed during the period of public offering, the issuer is obliged to submit a copy of the document reflecting the change (new information) to the National Bank of Georgia before including this change in the emission prospectus in accordance with the procedure defined by the National Bank of Georgia.

SUSPENSION AND REVOCATION OF THE APPROVED PROSPECTUS

If the issuer or a brokerage company acting on behalf of the issuer or a financial institution with the relevant license fails to comply with the requirements of the law, or if the information included in the emission prospectus by them is essentially inaccurate or incomplete, the National Bank of Georgia is entitled to suspend the approved prospectus and determine the period for eliminating such deficiencies. If the deficiencies are not rectified within the set period, the National Bank of Georgia shall have the right to revoke the approved prospectus.

If the National Bank of Georgia suspends or revokes the approved prospectus, the public offering of securities shall be prohibited and the buyers have the right to renounce their purchase.

SECURITIES ISSUANCE AND DISTRIBUTION REPORT

Within one month after the completion of the public offering of securities the issuer submits the report on emission and distribution of securities to the National Bank of Georgia. The report includes information about the exact number and price of the offered and sold securities. If the securities are not fully distributed, the issuer shall submit the report on actually distributed securities.

The National Bank of Georgia shall review the submitted report within 14 calendar days after it has been received. The National Bank of Georgia shall be authorized to request the explanation of the submitted information or changes in it, which shall be ensured and submitted by the issuer.

If the issuer of public securities is not a company, it shall submit to the National Bank of Georgia annual, semi-annual and current reports including financial and other kind of information and distribute them to the registered holders.

Based on the aforementioned information, the following issues are worthy of note:

1. The definition of a “sophisticated investor“ remains obscure:
 - It has been explained that a “sophisticated investor“ shall have ”sufficient experience“. However, the way of measuring this ”sufficient experience“ is not indicated anywhere;
 - It is unclear whether a “sophisticated investor“ should have ”experience“ and ”property/income“ or ”experience“ or ”property/income“;
 - It has been explained that a “sophisticated investor“ is a financial institution as well as its director, but why cannot a broker of the same company having the work experience of at least 5 (or more or less) years be a “sophisticated investor“?
 - It has been explained that a “sophisticated investor“ is a legal entity whose capital is more than 1 million GEL, although there is no evidence of his/her awareness in the field of securities however great his/her capital may be;
 - It has been explained that a “sophisticated investor“ is also considered to be a “high net worth individual” whose proven property is more than 3 million GEL or annual income for the previous 3 years is more than 200,000 GEL. The word “individual“ also implies a legal entity. Pursuant to the previous paragraph, the capital of a legal entity shall total 1 million GEL for the legal entity to be regarded as a “sophisticated investor“. Naturally, there is a question: does a legal entity need 1 million GEL or 3 million GEL to be deemed as a “sophisticated investor“?
 - Actually, no distinction has been made between physical and legal persons even when defining a “high net worth individual”. In my point of view, the amount of property/income required for a physical person should be several times less than that required for the legal entity;
 - In general, I believe that the definition of a “sophisticated investor“ should be predominantly based on knowledge and experience rather than on material assets/income, and most importantly, the definition should be unambiguous and clear so that the definition would not remain only an explanation and can be easily applied in practice, which is its real purpose.
2. In relation to the requirements of the preliminary emission prospectus necessary for the public offering of the issuable securities, it is worthy of note that there is no requirement for the term of the offer, which allows the offer to be valid for an indefinite period, even permanently, which is unrealistic. Therefore, it shall be necessary for the issuer to specify the term of the offer in the prospectus. If the issuer needs to prolong the period, it may be possible by making changes in the prospectus in a standard way. Apart from this, the maximum term should be defined by the law or the relevant regulatory rule of the supervisor. The maximum term may be used as the term of the offering of the prospectus not to allow the issuer to indicate an unrealistically long term (e.g. 10 or 20 years, etc.);
3. The indicative number of issuable securities is required in the preliminary prospectus of emission, although the price of distribution is not mentioned. I think the indicative price of distribution should also be required to provide an opportunity for the interested person to get an approximate impression of purchasing them;
4. The preliminary emission prospectus is subject to the approval by the regulatory body of the market of securities - the National Bank of Georgia (NBG). However, nothing is stated about whether the same approval is required for the final prospectus. I think the final prospectus should also be approved by the NBG in order to prevent the possible risks related to the inaccuracy of information;
5. It is quite obscure and therefore problematic to find out when a public offering of securities is permitted - after the approval of the preliminary prospectus or through the use of the final prospectus (which will be submitted to the NBG within 10 days after the approval of the preliminary prospectus). I believe it should be clearly explained

that after the approval of the preliminary prospectus it is possible to make a public offering of securities for prospective buyers, aiming to determine the potential interest of the buyers, and the number and price of the issuable securities, which will be included in the final emission prospectus. For this purpose 10 days (the interval between the approved preliminary emission prospectus and the final prospectus) may not be sufficient for the feedback from the clients and it is desirable to extend the period to 17-20 days;

6. When there are changes to a material fact during the period of a public offering, the issuer shall submit a statement about the changes of the offering to the NBG and shall publish the relevant notification in a newspaper. There are two moments to be taken into consideration: first, the response of the NBG is not required for these changes, which is logically inadmissible since the original information was approved by the NBG within the framework of the preliminary emission prospectus; next, based on the given entry the issuer can publish a relevant statement in a newspaper without a response from the NBG, which I think can be possible only after the response/approval of the NBG;
7. When there are changes to a material fact during the period of a public offering, the subscribers have the right to renounce the purchase of securities and the issuer has the obligation to return the fee within 10 days. The maximum duration of the period during which the subscribers have the right to renounce the purchase is not determined. I think 7 days would be normal.
8. In my point of view, the requirements of the emission prospectus do not sufficiently support the fundamental principle - equal terms of offering for everyone, which primarily means offering an equal price to everyone. The existing entry allows the price of the offer/distribution to be indicated in the prospectus as follows: not less than 1 GEL, which creates the basis for sale to different buyers at different prices. There was a practical case when JSC “Nikora Trade” made a public distribution of shares based on the approved emission prospectus (http://nikorasupermarket.ge/modules/for_partners/uploads/57_georgian.pdf) in which the price of distribution was not less than 2.18 GEL and the sales took place at different prices. Therefore, the prospectus should emphasize the principle of equal terms of the offering for everyone.
9. In general, the increase in public offering of securities or their provision is conducive to the development of the capital market. However, the demanding party should also be taken into consideration - its interest and ability to purchase what has been offered. In this respect an abundance of public offers of reliable and reputable companies is important. In fact, the standards of the current prospectus of a public offering/emission of securities are rather low and many of the newly established companies will meet them. Nevertheless, afterwards, as it makes an offering of securities and becomes a reporting company, it is automatically obliged to deal with a number of occasional financial, managerial or other accounts before the state regulatory bodies or the stock exchange (where it is traded), which is often a problem and the basis for their removal from the public circulation. Consequently, I believe that it is important to take care of the “quality” and reputation of companies from the very beginning. A newly established company should first show the case of successful 2-3-year activities, ensure financial accounting appropriate for international standards and be able to make a public offering of its securities only after that.
10. The state can also contribute to the existence of “quality” and reliable companies – express its will and promote a public offering of securities of large companies in which it holds its shares - companies such as Georgian Railway, Georgian State Electricity System, JSC Telasi, Georgian Oil and Gas Corporation, etc. Public distribution of even small shares/securities of these large companies will considerably increase the interest of investors, contribute to the existence of liquid financial instruments and result in a strong basis for the development of the Georgian capital market.

CONCLUSION

Filling of State Budget State Securities emissions shall affect the economic subjects not only during emission, but in subsequent periods. This is the result of expectations. In addition, it is quite difficult to predict the size and timing of this event. Based on this conclusion, the following recommendations should be made: the targeted emission of state securities as a state budget deficit, as well as profits, ensuring the short-term and long-term stable growth of the economy. State securities emissions and in this way the state budget deficit is required when the economy is in the economic slump and economic crisis. This opinion is based on the fact that the resource received by the state securities emissions will cover the reduced taxes during the economic decline and, at the same time, may reduce the rate of taxes, which will ease the economic condition of the general population of the population.

REFERENCES:

1. **Barro, R. J.** (1979) "On the determination of the public debt," *Journal of Political Economy* 87: 940-971.
2. **Barro, Robert J.** (1989) "The Ricardian Approach to Budget Deficits." *Journal of Economic Perspectives* 3 (37-54).
3. **Butkiewicz, J. L.** (1983): "The Market Value of Outstanding Government Debt: Comment." *Journal of Monetary Economics* 11 373-379.
4. **Bark, J Marzo, P. De.** "Corporate Finance: The Core," Global Edition, 3/E.
5. **Cox, W. M.** (1985) "The Behavior of Treasury Securities: Monthly, 1942-1984." *Journal of Monetary Economics* 16): 227-240.
6. **Ricardo D.** (1888) "Essay on the Funding System" in *The Works of David Ricardo. With a Notice of the Life and Writings of the Author*, by J.R. McCulloch, London: John Murray,
7. **Madura J.** (2006); - *Financial Institutions and Markets* ; Florida Atlantic University,
8. **Hull J.** (2009)- *Options; Futures and Other Derivatives*; University of Toronto,
9. **Valdez S.** (2010) *Global Financial Markets*, Macmillan
10. **Michael T.** (2011) "Bankrupt: entitlements and the federal budget," *Policy Analysis #673*, Washington, DC: Cato Institute.
11. **Kokiauri L, Shonia N.**(2008). "Securities Market",
12. Group of authors. (1998) "Stock Exchange and Securities Market",
13. **Jibuti M, Koranashvili K:** (2004) *Comments on Law of Georgia on Securities Market*,
14. **Aslanishvili D.** (2013) *An analysis and perspectives of Georgian State Securities financial market*. Bakhtadze L. (2006) *Financial market*,
15. **Lortkipanidze M.** (2005) *The infrastructure of Financial market*
16. *Georgian Stock Exchange. Annual Reports.*
17. *Law of Georgia on Securities Market.*
18. *Law of Georgia on Entrepreneurs.*