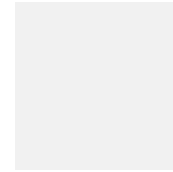


Project



GEORGIAN CAPITAL MARKET DEVELOPMENT CONCEPT



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The following concept document is designed to lead the interest of Georgian Government economic and financial groups and regulatory bodies, experts and specialists, participants of the capital markets, as well as business representatives and facilitate creation of larger task group, which will advance the concept document, facilitate public review, assure recognition of the concept of development of Georgian capital market and also assure preparation of appropriate plan-schedule.

OBJECTIVES OF CONCEPT

Establishment of the long-term conceptual vision

- To develop long-term vision of development of Georgian capital market, by involvement and sharing ideas of financial institutions, professional staff, experts and individuals who are interested in improvement of Georgian investment environment.

Support preparation of long-term capital market development strategy and action plan

- To facilitate preparation of long-term strategic development plan and schedule of relevant activities, which would undertaken by Georgian government's economic group/team, legislative bodies and market regulators

Assure the involvement of public and industry participants in the process of market development

- To establish practice for implementation of all legislative changes according to the pre-determined plan and provide involvement of market participants, investors, issuers and all interested parties in the process of discussion of initiatives.

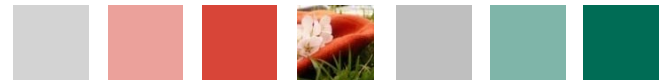
Facilitate introduction of international best practices

- The best international practice and modern trends of development of financial markets must be analyzed and reflected in the concept , by taking into account economical scale and potential of the country.



MAIN ISSUES/PROBLEMS

- Economic development of Georgia and **expansion of business activities** in the country
- Attracting foreign direct investments requires increasing effort because Georgian **financial market is not developed.**
- According to the Global Competitiveness Report (2012-2013), for improving **the competitiveness of Georgia and development of business activities** most problematic area is **accessibility to financial resources/capital.**
- Well-developed banking sector/industry is not enough for assuring access to financial resources/capital.

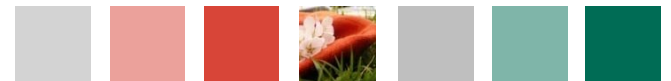


SOLUTION

- In order to raise capital at the Georgian market, the necessary appropriate and relevant environment should be developed, which may be **defined as transparent and reliable investment environment, where market entry-exit mechanisms are ensured.**
- Its necessary to ensure transition from ownership control (stakeholders) model to the **market model**

MAIN PRINCIPLES

- Establishment of the mechanism for motivation of private sector participants to the capital/securities market
- Formation of competitive, transparent, fair and credible environment at the capital/securities market
- Development of culture for investing in securities, motivating ownership dispersion and to easy investing process



TRANSPARENT AND SECURE INVESTMENT ENVIRONMENT WITH DEVELOPED MECHANISMS ENABLING MARKET ENTRY/EXIT

Transparency and protection of information

It ensures the reduction of information asymmetry

Reporting availability/accessibility

Legally enforced information confidentiality and protection of private property rights

Fair pricing

Integrated mechanisms of information dissemination

Diversity of investment instruments

It provides an alternative capital raising vehicles and turnover

Support and Promotion of public companies

Development of Debt securities segment

Availability of Local risk-hedging mechanisms

Ensuring Transparent Process of Privatization

Developed environment of capital market operations

It ensures easy enter-exit to financial markets

Organized stock exchange market with ensured liquidity

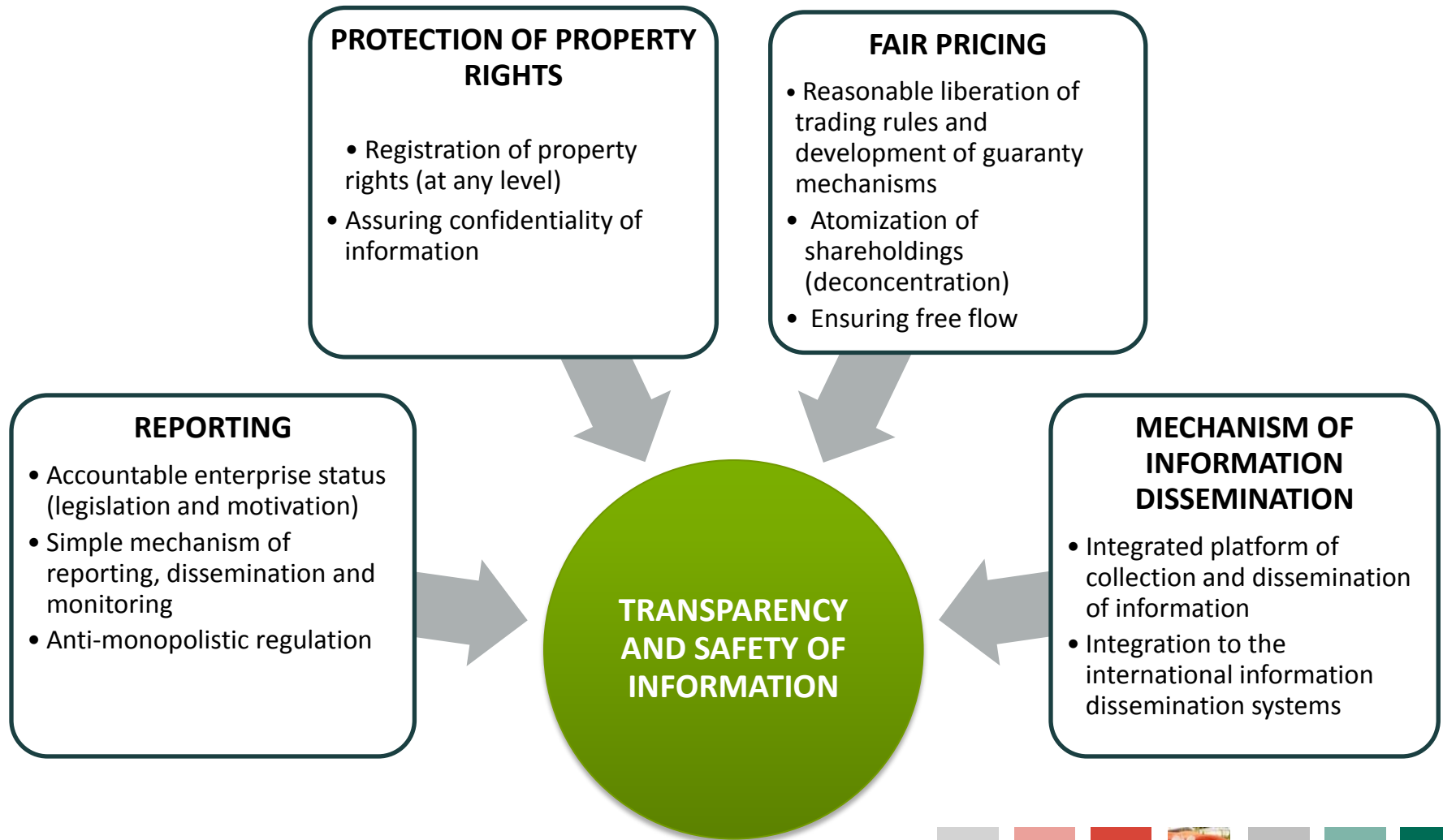
Developed Central Depository

Developed institutional infrastructure

Developed, segmented OTC market

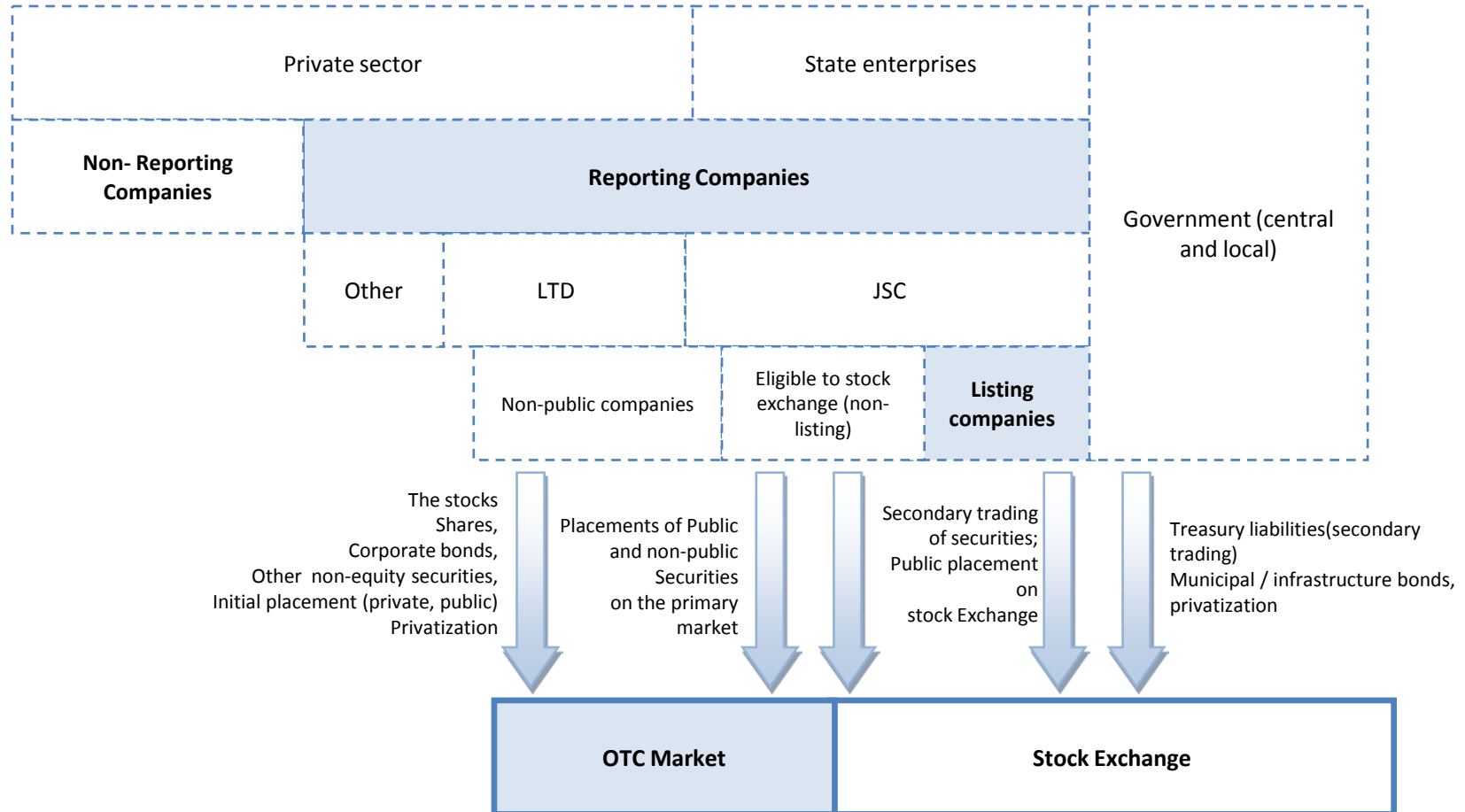


THE REDUCTION OF INFORMATION ASYMMETRY

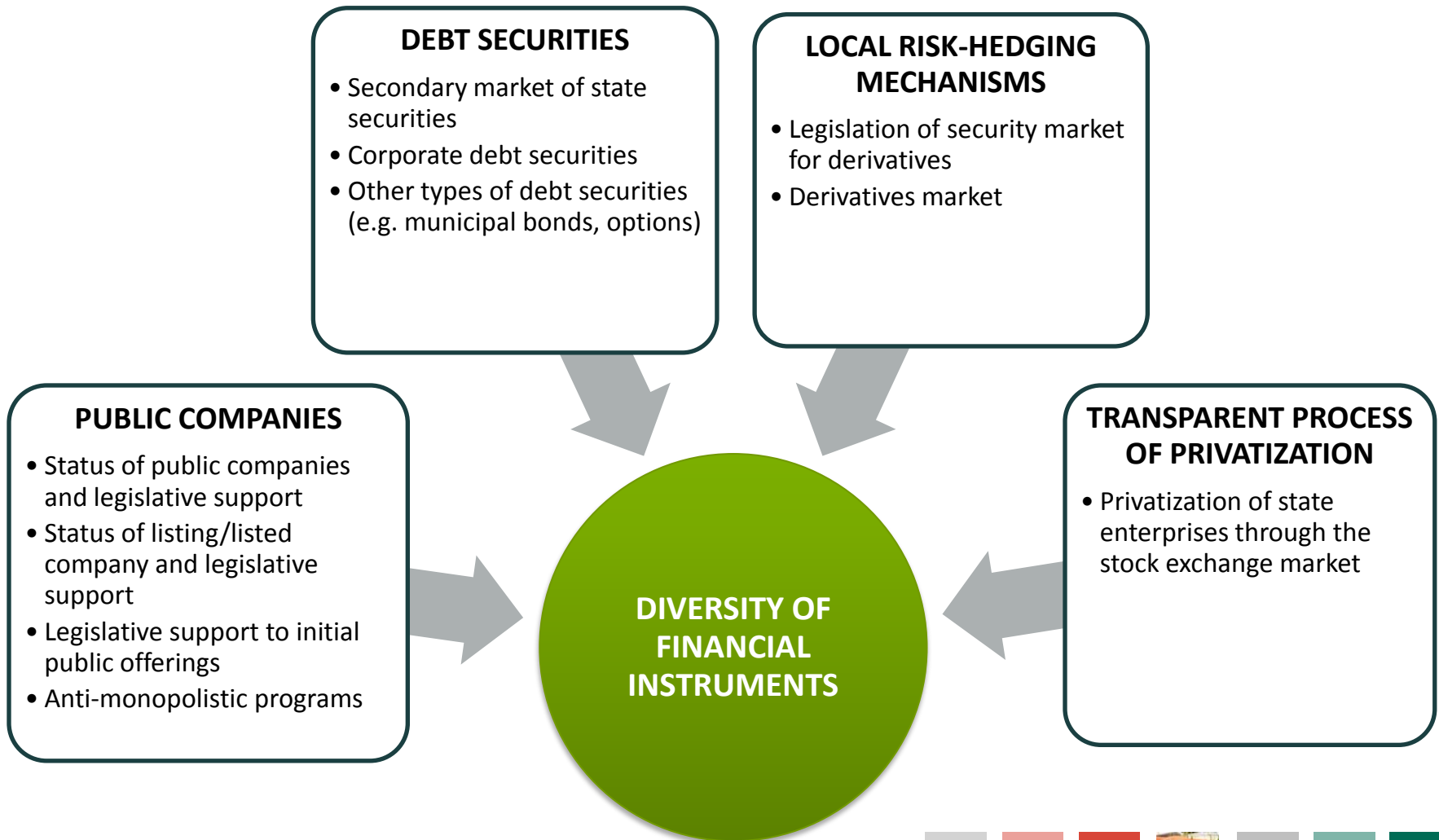


REDUCED ASYMMETRY OF INFORMATION

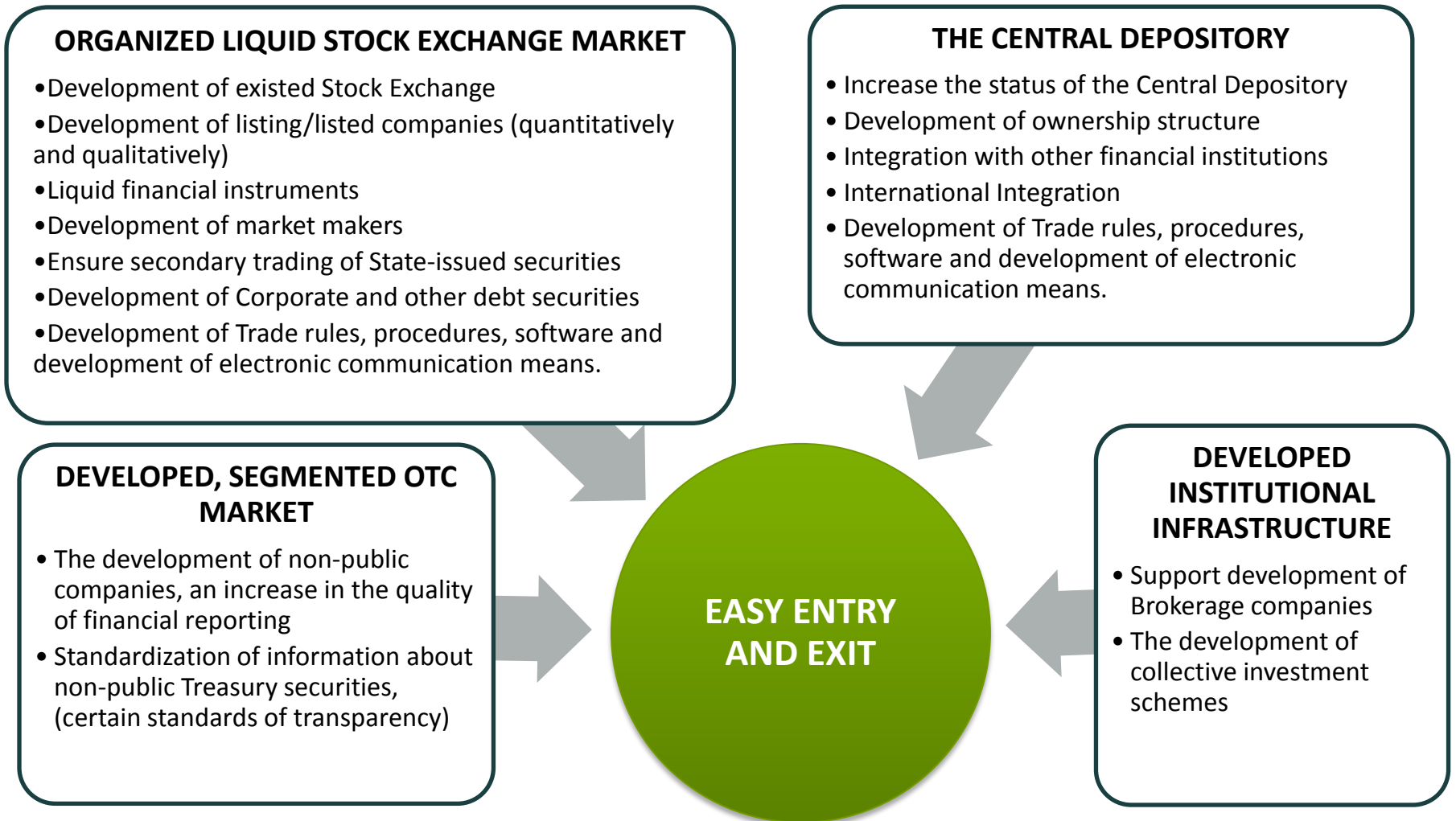
The structure of the market issuers



DIVERSITY OF FINANCIAL INSTRUMENTS



STRUCTURED INVESTMENT AND FINANCIAL MARKETS WITH ENSURED LIQUIDITY



ACTION PLAN

Ensuring information transparency and protection by relevant regulation mechanisms

Changes in legislation, creating unified regulation of non-bank financial markets;
Close cooperation and coordination with other field and antimonopolistic regulators.

Encouraging creation of various investment and financial instruments by information transparency and protection

Executing transparent process of privatization utilizing financial markets;
Encouraging development of local risk hedging instruments,
Encouraging IPOs for debt securities.

Ensuring the liquidity of financial and investment instruments

Encouraging financial infrastructure and market participants' institutional development;
Encourage development of competitive trading areas/systems to ensure financial and investment instruments circulation,
Ensuring liquidity



Agenda and Related Information

MAIN TOPICS OF CONCEPT



REGULATION

STATE REGULATORY AUTHORITY

According to the initiated changes in the Law on Securities Market by the Parliament of Georgia, the regulator of the market is National Commission for Securities and Exchanges

- Reasonable prospect is to establish non-bank financial markets unified supervision body
 - Non-bank financial instruments supervision regulator provides implementation of coordinated approach for financial market regulation and development.
 - Unified regulatory authority will enable the State utilize a synergistic effect by developing and combining the regulation of those industries, which have an important intersections.

COMMUNICATION BETWEEN REGULATORS

- The activity of mega regulator will be coordinated with an anti-monopolistic regulators' activity
- Mega regulator's activity should be coordinated with the field regulator's activity



SELF-REGULATION

SELF-REGULATION AND SELF-REGULATING ORGANIZATIONS (“SRO”)

- For creating healthy competitive environment:
 - Management principles of self-regulating organizations should be established, structure of participants, service quality standards, information and financial security frameworks and mechanisms for monitoring and control of compliance with mentioned limitations should be established as well.
 - In self-regulating organizations, regulating frameworks of Conflict of interest, unhealthy monopolies and professional ethic should be developed and activities of the participants and members of the governing body and control mechanisms for monitoring compliance with mentioned limitations should be established.
 - Functions that should be transferred from State regulators to self-regulating organizations must be clearly defined.
 - Self-regulating organizations should represent the example of institutional development, corporate governance and protection/compliance of financial reporting standards.



ISSUER AND REPORTING ENTERPRISES

ACCOUNTABILITY OF ENTERPRISES

- Establishment of regulation for voluntary accountability and development of its motivation mechanisms
- Establishment of accountability criteria and criteria monitoring.
- Clear separation of accountability and transparency status at legislative and regulatory levels

TRANSPARENCY AND POTENTIAL ISSUERS

- Transparency of information is one of the most important prerequisites to facilitate the entry of investors to the market
- Increasing the quality of financial reporting and transparency provides:
 - Manifesting potential issuers of financial instruments at capital market
 - To simplify and cheapen the evaluation/valuation of the market size , dynamics and investments
 - To satisfy public interest towards companies
 - To simplify relations with state agencies



TAX POLICY AND BENEFITS

- For stimulation of investments in the companies' shares by individuals and legal entities, the implementation of following methods should be considered:
 - Zero or reduced income tax rate on dividend for shareholders of companies, which become listed on the stock exchange
 - Zero or reduced income tax on capital gain revenues received from difference between the sale/purchase price of the listed securities
 - Taking into account the loss received by the difference between the sale price of the listed securities (for individuals)
 - The targeted tax breaks that are directed at specific sectors of the economy to invest in securities
 - Tax breaks in case of domestic corporate, compensation and investment scheme are developed



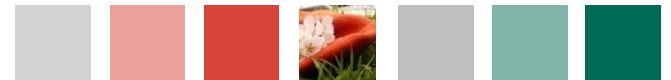
TAX POLICY AND BENEFITS

- To encourage issuance of companies' securities, implementation of following methods of promotion could be employed:
 - The formation of issuance fee's preferential schemes
 - Initial tax + Tax after placement of issue by submission of reports
 - Allowances about emission placement period (USA's analogy, when the placement is available for issuer's favorable time (415 SEC – Shelf Registration))
 - Involuntary issuance – as an alternative
 - Public issuance as other alternative of antimonopolistic measures
 - Issuance for the state debt repayment
 - Establishment of tax benefits for public and/or listing companies
 - E.g. reduced property tax – for companies, which make financial reporting by international standards (IFRS) and getting public audited reports, regularly



THE CORPORATE BOND MARKET

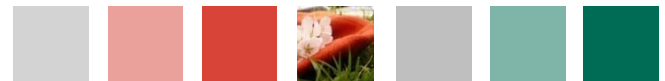
- Creation of foreign currency exchange risk insurance mechanisms and currency hedging liquid instruments.
- Corporate bonds should be encouraged for carrying out a public issuance and admission to the Stock Exchange Listing
- Approval of public issuance prospectus and acceptance of the bonds in Listing of Exchange should be allowed by considering a minimum amount and company's scale, rating, accountability and corporate governance standards of quality.
- Liquidity requirements should be set-up for of listed companies and existence of market maker for corporate bonds is essential.



PENSION REFORM AND INSURANCE

PENSION ACTIVITY

- Investment of Pension saving should be implemented in the local economy and their outflow from the country should not take place (Beside legally determined limited amount)
- On the initial stage of pension reform, the requirements for pension savings on relevant assets and relevant segments of Georgian stock market should be developed strategically
 - Clearly should be defined the list of relevant assets for the pension savings (Beside bank deposits), where investing of pension savings is accepted or prohibited
 - Will be defined requirements of the assets quality
- Will be created investment committee , which will be staffed by professionals



OWNERSHIP DISPERSION

- Large share (proportion) of small investors at the equity capital ensures high liquidity of market. Most of joint stock companies have concentrated equity structure, which prevents organizing liquid market.
- Unified strategic program of ownership atomization and de-concentration should be formulated and implemented (encouraged) long-term.
- Within the program framework, development and implementation of the following mechanisms is essential :
 - The formation or promotion of the free flow requirements for the securities or stimulation of free flow by the law and legal incentives (for example tax incentives)
 - Promoting internal corporate, compensation, investments, retirement plans schemes and ensuring protection of interests and risks of participant investors.
 - Development of voluntary individual investment scheme and ensure its functioning.



DEBT INSTRUMENTS

MUNICIPAL BONDS AND DEBT SECURITIES

Establishing regulatory legislation for municipal securities market
Motivating and facilitating issuance and flow of municipal securities

SECURITIZATION AND STRUCTURED FINANCING

Establishing regulating legislation of securitization process
Determining the securitizable group of assets
Determining those rights and obligations which will be acquired in this process

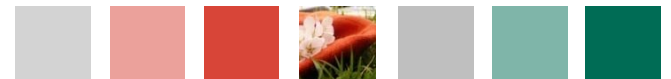
BONDS COLLATERALIZED BY PROJECTS

Mobilization of funds in industrial and infrastructural sectors
Legislation of projects collateralized bonds flow
Motivating and facilitating issuance of bonds



INFORMATION INFRASTRUCTURE

- Information infrastructure represents security market's informational production, collection, dissemination and delivery system to markets professional participants, issuers and investors.
- It's necessary to separate public and confidential information on Legislative and/or regulatory level.
- Necessary steps:
 - Creation of modern information platform
 - Formation and development of indicators system
 - Mandatory disclosure of OTC transactions and OTC turnover
 - Promoting the development of rating agencies and development of regulations for dissemination and recognition of their information
 - Ensure of dissemination of information of Georgian stock/capital market to international information dissemination systems
 - Providing access to investors to the information of financial markets. This information should include information about professional participants of market and also about market issuers



STOCK EXCHANGE MARKET

The Stock Exchange must have a diversified structure of ownership/shareholding and all leading participants of market should be present

Admission of securities to the stock exchange system should be determinant of securities' quality and a guarantee of its liquidity.

FOR DEVELOPMENT OF STOCK EXCHANGE MARKET:

Stocks of an accountable enterprises which are listed on the stock exchange should be traded only at stock exchange through the brokerage firms and commitment for transactions at stock exchange will be related just to the buy-sell trade.

The stock exchange must offer a high-quality, reliable, tailored service to the needs and demands of the market participants , which provides market transparency, fair pricing and easy entry/exit on the market



CENTRAL DEPOSITORY

- The requirements for structure of ownership of the central depository should be clearly defined
- It is necessary to enhance state approach for special importance of the central depository for the securities market in Georgia
- Central depository should represent the institution providing clearing-settlement operations with substantial financial resources
- Involvement of any commercial bank's to central depository clearing-settlement system should be accomplished by a simple procedure, without additional restrictions



REGISTRARS

DESSIMINATION OF INFORMATION

- Should be clearly defined list of persons to whom, in what circumstances and to what extent have the right to obtain information from the registrar

COLLATERAL REGISTRATION

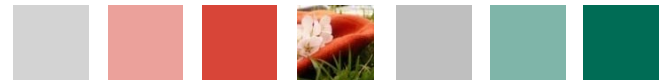
- It's inevitable that when securities are used as collateral the load and cancelation (blockage) should be performed by the Registrar of Securities

INFORMATION ABOUT MEMBERS OF THE GOVERNING BODY

- Regulate disclosure of information about members of governing bodies of joint stock companies, according to the law (should be required provide in business register), or fix the issue to registrar.

SOLUTION FOR SHAREHOLDERS IDENTIFICATION PROBLEM

- Joint stock companies and registrars should be allowed to apply for a state agency without having court decisions and obtain information about the identity of their shareholders



MARKET INTERMEDIARIES

- Establishment of the support approach to the brokerage activities: the number of brokerage companies should be enough for satisfying demand-supply prerequisite
- Minimum two types of license/status should be established, which will have diversified requirements, including capital requirements (**Investment bank** (general license) and **brokerage company**), which conducts just several types of services, according specialized license
- For hedging risks of market participants, the additional certificate and qualification improvement requirements for high risk operations (e.g. derivative securities' operations) should exist.



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