



## Section 2. Finance, monetary circulation and credit

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### OPERATIONS OF BANKS IN THE SECURITIES MARKET IN GEORGIA: PROBLEMS AND CHALLENGES

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#### Abstract

If we examine the example of economically developed countries in the world, we can identify two mechanisms for raising capital: bank loans and the stock market. The harmonious relationship between these two mechanisms contributes to the health and development of the country's economy. One of the mechanisms for raising money, the bank loan, holds absolute dominance in the Georgian reality, hindering the development of the second mechanism, the stock market. As a result, various business entities lack the opportunity to access long-term financial resources and are compelled to pay the high fixed loan rates of commercial banks.

**Keywords:** *bank loan, stock exchange, commercial bank, loan rate*

#### Introduction

A commercial bank is the primary component of the credit system, as it practically performs all types of banking operations. Commercial banks continually strive to adapt to the competitive environment. The introduction of new institutions and financial instruments into the market encourages commercial banks to broaden their scope of operations and become universal.

At the beginning of the 20<sup>th</sup> century, the governments of developed Western countries made the decision to prohibit banks from directly participating in the securities

market and imposed specific restrictions and barriers. Later, along with the development of the global economy, since the 70s of the XX century, the mentioned approach regarding commercial banks has gradually changed and the existing restrictions are being either lifted or eased. A prominent and highly significant example of this process is the repeal of the Glass-Steagall Act in 1933 in the United States. Nevertheless, it is worth noting that in some countries of the world, the activities of banks on stock markets are regulated by legislation. As a result, banks in these countries have to ex-

plore other ways, through trust, brokerage and investment companies.

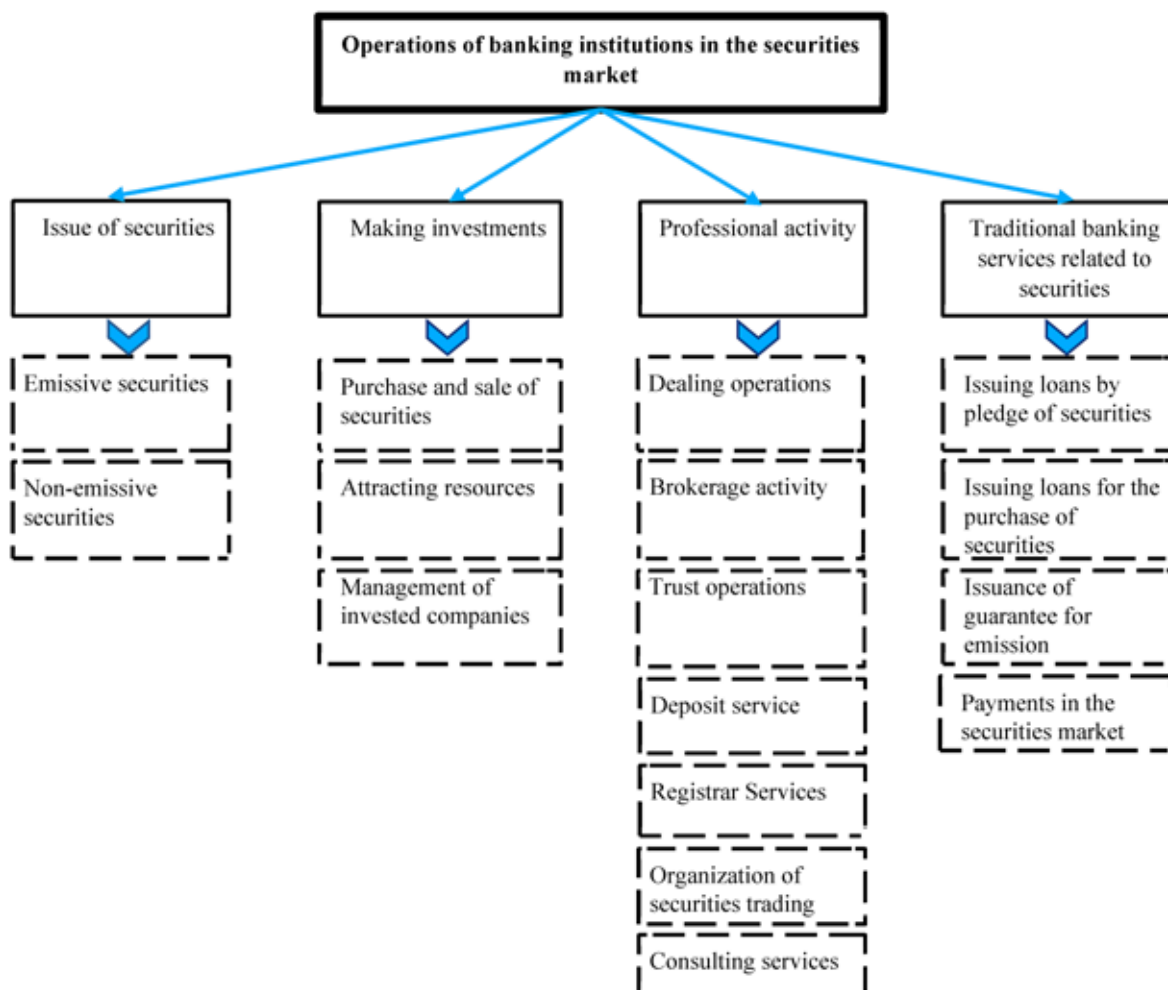
**Main part**

In the countries where commercial banks are granted the authority to engage in various securities-related transactions, they assume the roles of issuer, intermediary and investor.

For commercial banks, the restrictions of the mentioned operations are different and

are regulated by the legislation of a specific country. The restrictions related to the activities of commercial banks are regulated by the Law “On Commercial Bank Activities” (**Article 10. “Restriction of ownership rights, assets, ownership structure and group structure of commercial banks”**) in Georgia (**Modern Banking: Theory and Practice, 2022**).

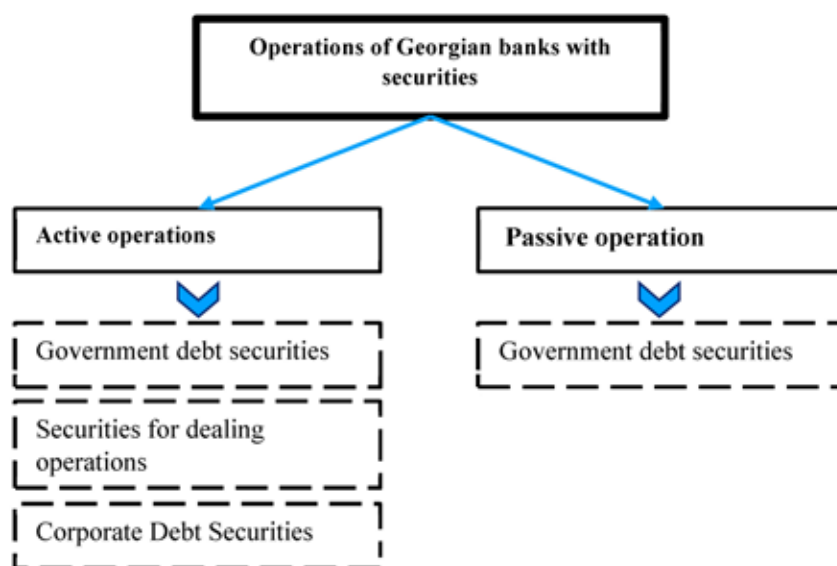
**Scheme № 1**



As for a security, it is a financial instrument in circulation. A set of securities forms a securities market, through which, as a result of their circulation, monetary resources are distributed between investors and issuers. The securities market holds an intermediary position between capital markets and money markets. Through it, monetary savings of the state, legal entities and individuals are accumulated and directed to the capital markets. Additionally, the securities market plays a complementary role within the banking credit system.

The securities market and the banking sector are essentially competitors, as both aim to attract temporarily free cash. However, these two instruments are not distinctly separated and are strongly interrelated. The securities market serves as a complement to the banking credit system. Savings are transformed into investments through the securities market. These investments are received by private businesses and the government. Both the private sector and the population, who have saved money, become investors and creditors.

Scheme № 1.1



The securities market cannot exist without the stock market. A stock exchange is an organized marketplace for securities. It facilitates the collection of proposals for the purchase and sale of securities and other financial instruments, organizes trading in accordance with established rules and procedures, and disseminates information about completed transactions and other price-related information.

The Georgian Stock Exchange (GSE), established on January 8, 1998, is the only operating organized securities market in Georgia. Established with the support of USAID, it operates within a legal framework developed in collaboration with American experts.

On October 18, 1999, at the session of the Supervisory Board of the Exchange, a decision was made – for fast, effective and reliable clearing and settlement of transactions concluded on the Exchange, the Exchange should establish an organization that will solve this problem. Consequently, the GSE established the “Georgian Central Securities Depository” LLC (GCSD) with 100% ownership.

On January 14, 2000, the National Securities Commission of Georgia issued stock license N90001 to GSE.

On January 18 of the same year, the commission recognized GSE as a self-regulating organization. On March 23, 2000, the first trade in the shares of “United Georgian Bank” took place. Since then, until today, stock trades have been conducted regularly at the stock (Nana Shonia, Tinatin Gugesashvili, 2009).

The dates mentioned above (1998–2000) were highly significant for Georgia as they marked the active initiation of the formation of the securities market, with the participation of leading experts from the US financial market. Given that banks in the new post-Soviet Georgia were relatively advanced, legislative measures were taken to prevent one sector from exercising excessive supervision over the other. A clear example of this is the Law “On Securities Market” adopted in 1998. According to this law, the two industries were entirely separated from each other, allowing the newly formed securities market to develop independently. The securities market was supervised by the National Securities Commission of Georgia. As a result, banks couldn’t participate directly in the market; it was only possible through subsidiary brokerage companies. Thanks to these and other supporting measures, the stock market achieved quite positive results from 2004 to 2007. Since 2007, the operation of the stock market has been disrupted due to specific factors.

One of the most significant reasons is legislative changes. March 31, 2007, is a crucial date in the history of the Georgian Stock Exchange because the Law of Georgia, “On Securities Market”, was amended. In particular, with the changes outlined in Article 18, Clauses 1 and 5, it became possible to execute transactions both on and off the stock exchange, with or without the involvement of a brokerage company. The mentioned date turned out to be the last one in the trading of

the Georgian stock exchange, when the volume of transactions and sales, in total, increased. The adopted legislative change led to a decrease in trading transactions on the GSE, and monetary turnover shifted outside the exchange. Since 2000, the supervision of the securities market has been carried out by the National Securities Commission of Georgia, which was a self-regulating system, and since 2008, the National Bank of Georgia has become the controller. After the National Bank acquired the function of securities market supervision and commercial banks were given the opportunity to participate directly in the market, most of the shares and bonds presented on the Georgian Stock Exchange are represented by commercial banks. As of September 29, 2023, there are 38 securities listed in various categories on the Georgian Stock Exchange. The largest portion of these securities consists of Liberty Bank shares, with a total volume of 5,502,254,354 securities (Georgian Stock Exchange (GSE), 2023). It should also be noted that the majority of transactions are carried out outside the exchange, that is, they are non-exchange and are made in a non-competitive environment through brokerage companies. In the period from January 1, 2023 to September 29, 2023, 19 transactions were carried out at the trading sessions of the Georgian Stock Exchange, the total value of which amounted to 50,209.04 GEL (Georgian Stock Exchange (GSE), 2023). The mentioned transactions were conducted exclusively in GEL. However, for non-stock transactions during the same time period, the results differ significantly from those carried out in trading sessions. In total, 91 transactions took place in GEL, USD, and EUR, with a total value of 3,218,354.40 GEL, 8,863,825.89 USD, and 1,573,564.97 EUR (Georgian Stock Exchange (GSE), 2023).

Currently, the Georgian stock exchange is represented by companies with high capitalization, but among them there were three companies that listed their shares on the London stock exchange. On November 24, 2006, Bank of Georgia became the first bank in Georgia and the second in the post-Soviet space to list its shares on the London Stock Exchange. Since 2012, it has met all the highest requirements in terms of financial strength, transparency, and high standards

of corporate management, which led to its move to the premium listing of the London Stock Exchange. As for TBC Bank, it joined the London Stock Exchange in 2014, and in 2018, JSC “Georgian Capital” was formed as a result of the division of the Bank of Georgia.

As of September 29, 2023, the results of the mentioned companies on the London Stock Exchange were as follows:

The price of “Bank of Georgia” (BGEO) shares has increased by 0.82%, and the current value of one share is 36.90 pounds. The company’s market capitalization currently stands at £1.81 billion. In the last six months, the shares of “Bank of Georgia” have increased by 32%.

TBC PLC shares rose by 1.88% over the week. One share of the bank is worth 29.85 pounds sterling. The company’s market capitalization currently stands at £1.64 billion. In the last six months, the price of “TBC” shares has increased by 20%.

The value of the shares of “Georgian Capital” (CGEO) decreased by 3.53%, as a result, the price of one share became 9.84 pounds sterling. As a result, the market capitalization of the company currently amounts to 458.56 million pounds sterling. In the last six months, the price of the company’s shares has increased by 20% (BUSSINES MEDIA, bm.ge., 2023).

The presence of Georgian banks on the London Stock Exchange is highly beneficial. For the banks, this means an unlimited opportunity for development, an expansion of their investor base, and the prospect of increasing share liquidity. Meanwhile, the local market gains access to even more stable, high-standard banking services. However, it is unfortunate that most Georgian companies are unable to sell their securities on foreign exchanges. At the same time, the Georgian stock exchange is not sufficiently developed to provide companies with access to the necessary financial resources. Consequently, they are forced to seek credit from commercial banks, resulting in using expensive credit.

### **Conclusion**

In Georgia, where there is a shortage of local investment resources, it becomes exceptionally crucial to ensure the sustainability of the securities market and stock exchange. The

dominance of banks in the financial sector leads to the underdevelopment of the securities market, which, in turn, presents a problem, as a developed securities market and stock exchange help to mobilize local savings more efficiently and create an opportunity to diversify

funding sources. Addressing this matter is of great significance as the share capital market serves as a vital alternative funding source for Georgian corporations. Currently, financial resources are not fully and efficiently leveraged for economic development at this stage.

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