DOI: https://doi.org/10.57125/FEL.2026.09.25.01

How to cite: Mushkudiani, Z., Shalamberidze, K., & Surmanidze, N. (2026). Filling the gap: How Georgian firms and policy programs respond to a thin domestic capital market. *FuturityEconomics&Law, 6*(3), 4–21. https://doi.org/10.57125/FEL.2026.09.25.01

Filling the Gap: How Georgian Firms and Policy Programs Respond to a Thin Domestic Capital Market

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Received: April 9, 2026 |**Accepted:** June 28, 2026 |**Available online:** July 21, 2026

Abstract: Institutional voids theory holds that firms in emerging and transition economies must compensate for missing or underdeveloped market-supporting institutions, with capital market depth being one of the most consequential such institutions for firm financing and growth. Although this theory has been extensively applied to large emerging economies, it has not previously been applied to Georgia, a small, open, transition economy whose capital market remains comparatively thin despite recent growth. This paper examines how Georgian firms and a specific government program have responded strategically to the documented shallowness of the domestic capital market. The paper applies institutional voids theory and related international business literature on firm-level institutional strategies to a structured documentary analysis of verified financial market data, drawing on data from the World Bank, the National Bank of Georgia, and Georgian financial market reporting. The analysis documents a persistent reliance on foreign-currency and bank-centered financing among the largest

Georgian corporates, the listing of Georgia's largest firms on the London Stock Exchange rather than the domestic exchange, and a targeted government bond-support program, the Enterprise Georgia Capital Market Support Program, aimed specifically at small and medium-sized enterprises. Despite recorded growth in the domestic corporate bond market between 2018 and 2025, market participants and regulators continue to describe the market as shallow by international standards. Practical value: the paper provides Georgian managers with an evidence-based account of why local and foreign-currency bank financing, internationally listed equity, and targeted public bond-support programs have each emerged as practical responses to capital market depth constraints and offers policymakers a documented basis for evaluating whether such targeted programs are succeeding in deepening the market over time.

Keywords: capital market development, corporate bond market, firm financing strategy, Georgia, institutional voids, small and medium-sized enterprises, transition economies.

Introduction

A well-functioning capital market allows firms to raise long-term financing from a broad base of investors, at a price set by competition among lenders and investors rather than by negotiation with a single bank. Where such a market is thin, illiquid, or accessible only to the largest firms, companies and policymakers must find other ways to fund growth. Leff (1976) was among the first to observe that in less developed economies, the group, a coalition of firms operating under common entrepreneurial and financial control, frequently emerges specifically to compensate for the absence of efficient capital markets, functioning as a private substitute for the screening, monitoring, and capital-allocation functions that formal financial institutions perform in more developed economies. Khanna and Palepu (1997, 2010) later formalised and substantially extended this insight, terming the broader condition of missing or underperforming market-supporting institutions an institutional void, and showing that firms in emerging economies respond to such voids through a range of identifiable strategic adaptations.

The capital market dimension of institutional voids has received particularly sustained attention because it is among the most directly measurable and consequential for firm strategy. Hoshi et al. (1991) and, in the emerging-market context, Khanna and Palepu (2000a, 2000b) showed that internal capital markets, the redistribution of funds among affiliated firms within a business group, can substitute effectively for absent or costly external financing, allowing group-affiliated firms to invest and grow at rates that comparable unaffiliated firms, facing the same external capital market void, cannot match. Khanna and Palepu (1999) further showed that foreign institutional investors, where present, can serve a valuable monitoring function precisely because they are positioned to evaluate group-affiliated firms with more scrutiny than under-resourced domestic investors typically apply, a finding directly relevant to the role international listing plays in the Georgian case examined in this paper.

Georgia presents a clear and well-documented example of a capital market institutional void, and one that has not previously been examined through the lens of this literature. The World Bank's Financial Sector Assessment Program for Georgia found that domestic capital markets are dominated by government bonds with a largely inactive secondary market, and that approximately 80 per cent of the debt obligations of the country's 500 largest non-financial corporates were held in foreign currency, reflecting a structural reliance on bank lending and foreign-currency financing rather than on a developed local-currency capital market. At the same time, the domestic corporate bond market has grown substantially in recent years, expanding from approximately USD 205 million in 2018 to roughly USD 800 million by the end of 2023, and to a reported GEL 2.7 to 3.2 billion, approximately USD 1.0 to 1.1 billion, by early 2026, even as market participants and the National Bank of Georgia itself continue to describe the market as shallow by international standards. A further institutional development relevant to this growth is the establishment, in 2018, of the Pension Fund of Georgia, the country's first mandatory, defined-contribution pension system, which has since become an active participant in domestic bond issuances, including, as documented later in this paper, a first-time purchase of microbank bonds.

Research Problem

This combination, genuine recent growth alongside a persistent and openly acknowledged structural shallowness, raises a specific and answerable question for management and finance research. Institutional voids theory predicts that firms facing a capital market void will adopt identifiable compensating strategies. Whether and how Georgian firms and Georgian policymakers have done so has not previously been documented in the academic literature, despite the availability of clear, publicly available financial market data that would allow such documentation.

Research Focus

This paper's focus is narrow and specific by design. Rather than examining institutional voids across the Georgian economy in general terms, the paper concentrates on a single, well-documented institutional void, the depth and liquidity of the domestic capital market for corporate financing, and traces, using verified data, how specific firms and a specific government program have responded to it.

Research Aim and Research Questions

The aim of this paper is to document and analyse, using verified financial market data, the firm- and policy-level strategic responses to Georgia's capital-market institutional void. The paper addresses three research questions: first, what verified evidence exists of a capital market institutional void in Georgia, and how it has changed over time; second, what financing strategies have Georgia's largest firms adopted in response to this void; and third, what role has the Enterprise Georgia Capital Market Support Program played in addressing the void for smaller firms.

Literature Review

The Origins of Institutional Voids Theory

The theoretical starting point for this literature is Leff's (1976) observation that the group, understood as a set of firms bound together by common entrepreneurial and financial control, functions as a private response to capital-market imperfections in less-developed economies. Where formal capital markets cannot adequately screen borrowers, monitor their performance, or enforce repayment, a group structure allows its controlling family or management to perform these functions internally, using the group's own accumulated reputation and information advantages in place of the institutions a developed capital market would otherwise supply.

Khanna and Palepu (1997) substantially extended this insight in their influential analysis of Indian conglomerates, arguing that the absence of efficient capital markets, credible auditors, and reliable labour-market intermediaries makes internal diversification a rational, rather than merely traditional or inefficient, response for firms operating in such environments. This reframed a strategic choice, namely unrelated diversification, that mainstream Western strategic management theory had generally treated at the time as value-destroying, showing instead that its value depends critically on the institutional context in which it occurs. Khanna and Palepu (2010) subsequently generalised the underlying concept across six categories of institution, political, legal, social, product, labour, and capital markets, establishing institutional voids as a multidimensional construct that can vary independently across these categories within a single economy.

Capital Markets and Internal Financing Substitutes

A substantial body of subsequent research has examined the capital market dimension of institutional voids in particular depth. Khanna and Rivkin (2001) demonstrated empirically that business group affiliation improves firm profitability, particularly in economies with weak capital market development, because group affiliates can draw on each other's resources and reputations in place of external financing channels that are unavailable or prohibitively costly for unaffiliated firms. Khanna and Palepu (2000a, 2000b) found, using Indian and Chilean data respectively, that internal capital markets, the redistribution of funds among affiliated firms, allow group-affiliated firms to sustain investment levels that comparable unaffiliated firms facing the same external capital market void cannot match, a mechanism subsequently formalised and extended by Hoshi et al. (1991) in the Japanese context and by Gopalan et al. (2007), who showed that intra-group loans serve specifically to support financially weaker affiliates during periods of external financing constraint.

Khanna and Palepu (1999) added an important refinement directly relevant to the present paper: examining the relationship between business groups and foreign institutional investment, they found that foreign institutional investors serve a valuable monitoring function precisely because they apply more rigorous scrutiny than typically under-resourced domestic investors, and that more transparent group structures are correspondingly more likely to attract such investment. This finding offers a theoretical lens for understanding why Georgia's largest and most internationally visible firms have chosen external listing on a deeper, more rigorously monitored foreign exchange rather than relying solely on internal group financing or the domestic market, a pattern documented later in this paper.

Kock and Guillen (2001) framed unrelated diversification as an evolutionary response to the absence of specialised financial and other intermediaries, while Dau (2013) found that business group diversification continued to generate value for affiliated firms in Latin American economies even after market-supporting reforms had been implemented, suggesting that informal financing substitutes, once established, do not necessarily dissolve quickly when formal capital markets begin to develop. This finding is directly relevant to the persistence of foreign-currency and bank-centred financing documented in Georgia, even as the domestic bond market has grown.

Beyond the Business Group: A Broader Repertoire of Strategic Responses

Marquis and Raynard's (2015) review identifies a broader repertoire of firm-level institutional strategies beyond business group formation, including relational strategies, in which firms substitute personal and institutional relationships for absent formal financing mechanisms, and infrastructure-building strategies, in which firms or public programs invest directly in the market infrastructure that private capital markets have not yet supplied at sufficient scale. This latter category is directly relevant to the present paper, since targeted public bond-support programs of the kind examined here are a clear instance of infrastructure-building undertaken jointly by a government agency and participating firms, a category of response that the original, predominantly firm-centred institutional voids literature did not place at its centre.

Nayyar and Luiz (2024) introduced institutional void severity as a graded, rather than binary, construct, arguing that voids vary in intensity and that this intensity shapes the type of firm response likely to be effective. This framing is useful for the Georgian case, where the capital market void is neither a complete absence of capital markets, since a functioning stock exchange and a growing bond market both exist, nor a fully resolved condition, since market depth and liquidity remain limited by international comparison even after recent growth. Meyer and Peng (2016) further argue that emerging-economy contexts should be used not merely to test existing theory but to refine it, a position this paper adopts by examining a context, a small, open, transition economy with a recently growing but still shallow capital market, that has not previously been documented in the institutional voids literature.

The Historical Development of Georgia's Capital Market Infrastructure

Understanding the current state of Georgia's capital market requires some account of its institutional history, since the present shallowness documented in this paper is not simply a starting condition that the country has not yet outgrown, but the outcome of a specific historical sequence of institution-building, partial retrenchment, and renewed growth. Georgia's Mass Privatisation Program, launched in 1994, transformed approximately 1,300 state-owned enterprises into joint-stock companies and created roughly half a million individual private shareholders almost overnight. However, for the following five years, from 1994 to 1999, the absence of an appropriate legal framework and organised market infrastructure meant that secondary trading in these shares, and over-the-counter market activity generally, remained nearly non-existent, leaving the privatisation program's shareholders with formally issued securities they had little practical means of trading.

The basic infrastructure intended to remedy this gap, the Georgian Stock Exchange itself, the Georgian Central Securities Depository, and an initial network of independent securities registrars, was established between 1999 and 2000, with support from the United States Agency for International Development and the Barents Group, and a Law of Georgia on Securities Market was developed shortly afterwards. Between 2000 and 2007, the number of joint-stock companies admitted to trading reached 282, and the number of active brokerage firms grew to 42 by the 2004 to 2008 period, suggesting a securities market infrastructure that, for a period, expanded broadly in line with the original policy intention.

This period of expansion did not continue. Following regulatory changes enacted in 2007 and 2008, the National Securities Commission of Georgia, the dedicated securities regulator, was abolished, with its powers transferred to the National Bank of Georgia, an institution whose primary regulatory mandate concerns the banking sector. The number of active brokerage firms fell sharply following this change, and by the mid-2010s, only seven members remained active on the exchange, of which three were independent firms, and four were subsidiaries of commercial banks. A Tbilisi State University analysis of this period (Aslanishvili, 2014) further documents that bidding rule changes in the early 2000s, and subsequent reversals of those changes, contributed to what researchers have termed as a problem of closed bidding, limiting free price formation on the exchange during a period when the market might otherwise have continued to deepen. A policy analysis from the Institute for Development of Freedom of Information further argues that successive governments showed limited interest in broadening domestic share ownership, preferring instead the more easily controlled financing relationships that a small number of large banks could provide, and notes that proposals were at various points made to list major state-linked companies, such as Georgian Railway, on foreign exchanges in Shanghai or London rather than on the domestic exchange.

This historical sequence, an initial period of broad infrastructure-building and broker-firm growth, followed by a period of regulatory retrenchment and brokerage-firm consolidation into the banking sector, helps to explain why the present-day market remains both genuinely active, with 28 companies admitted to trading and a total market capitalisation of approximately USD 2.24 billion as of April 2024, according to the exchange's own published data, and simultaneously shallow by international comparison, with on-exchange turnover that has at various points, including during the 2020 pandemic period, contracted to negligible annual levels even as overall market capitalisation continued to grow. The bank-centred financing pattern documented in this paper's Results section and the more recent emergence of bond-market alternatives through the Enterprise Georgia program can therefore be understood as continuations of a structural pattern with roots dating back at least two decades, rather than as a purely recent development.

Geographically, the existing capital-market-focused institutional voids literature has concentrated heavily on India, the original context for the theory and the source of the great majority of empirical business group studies (Khanna & Palepu, 1997, 1999, 2000a; Khanna & Rivkin, 2001), and on Latin America, where business group persistence through periods of market reform has been documented in detail (Aguilera et al., 2017; Dau, 2013). Chile (Khanna & Palepu, 2000b), Japan (Hoshi et al., 1991), and a smaller number of Chinese and Korean studies (Gopalan et al., 2007) extend this geographic base only modestly. No published study has examined the depth of Georgia's domestic capital market, or that of any South Caucasus economy, through the lens of institutional voids theory, despite the availability of detailed, regularly updated financial market data from the World Bank, the National Bank of Georgia, and

Georgian financial market reporting sources that make such an examination directly feasible. This represents a clear and addressable gap in the existing literature that this paper fills.

Materials and Methods

This paper employs a documentary, evidence-based case analysis, an established and appropriate method in international business and strategic management research, to examine how a specific, well-defined institutional condition manifests in a particular economy (Khanna & Palepu, 1997; Doh et al., 2017). The analysis is structured around publicly available, independently verifiable financial market data rather than primary survey or interview data, consistent with the paper's aim of documenting an observable market condition and the corresponding firm and policy responses.

Sample and Data Sources

Six categories of sources were used. First, the World Bank's Financial Sector Assessment Program report for Georgia provided foundational evidence on capital market structure and the currency composition of corporate debt. Second, statements and data from the National Bank of Georgia, reported by Georgian financial media, provided figures on the size and growth of the corporate bond market. Third, Georgian financial market and investment reporting sources, specifically Investor.ge and Georgia Today, both of which report on Georgian Stock Exchange activity, corporate bond issuances, and the Enterprise Georgia program, provided firm-level transaction data. Fourth, independent market data providers, specifically Asia Frontier Capital's published country analysis, provided market capitalisation figures for Georgian firms listed on the London Stock Exchange. Fifth, an academic analysis published through Tbilisi State University and a policy analysis published by the Institute for Development of Freedom of Information provided historical and institutional context on the development of the Georgian Stock Exchange and its regulatory environment between 1994 and the mid-2010s. Sixth, the Georgian Stock Exchange's own published institutional data, together with an independently compiled summary of that data, provided current listing and market capitalisation figures as of the end of 2024.

Data Verification Procedure

Each figure reported in this paper was checked against the source and, where possible, against a second independent source. Where sources reported different figures for a related but not identical measure, for example, the number of companies admitted to trading on the Georgian Stock Exchange compared with the number of companies with actively traded equity, this paper reports the specific measure and its specific source rather than treating the figures as interchangeable, to avoid overstating precision that the underlying data does not support.

Data Analysis

As a documentary case analysis, the method is qualitative and descriptive rather than statistical. The data presented in Tables 1 and 2 are organised to show, first, the scale and trajectory of the documented capital market void, and second, the specific, named, verifiable firm and policy responses to it. No inferential statistical test is applied, and no claim is made beyond what the cited sources themselves report.

Justification for the Documentary Case Method

The choice of a documentary, evidence-based case method over a survey-based or experimental design merits direct justification given that institutional voids research has, in some of its most cited contributions, relied on large-sample quantitative analysis of firm-level data, particularly in the Indian context, where Khanna and Rivkin (2001) and Khanna and Palepu (2000a) drew on extensive firm-level financial databases unavailable for an economy of Georgia's size and market development. No equivalent firm-level financial database, of the kind the Centre for Monitoring Indian Economy's Prowess database has provided for Indian business group research, exists for Georgian corporates outside the small number of exchange-listed and bond-issuing firms already captured in this paper's Results section. A documentary method focused on verifiable, publicly reported transactions and regulatory data is, therefore, the most rigorous approach available for establishing, at this stage of the literature, that the phenomenon under examination exists and takes the specific forms documented, while explicitly reserving causal and comparative-statistical claims for the firm-level survey and longitudinal research proposed in this paper's concluding section.

This sequencing, establishing a documented phenomenon through case evidence before proceeding to quantitative hypothesis testing, follows a recognised pattern in the institutional voids literature's own development: Khanna and Palepu's (1997) original Harvard Business Review contribution was itself a qualitatively argued case-based analysis of Indian conglomerates, and only the subsequent decade of research (Khanna & Palepu, 2000a, 2000b; Khanna & Rivkin, 2001) developed the large-sample statistical evidence now closely associated with the theory. The present paper occupies an analogous early position in the specific application of institutional voids theory to Georgia and the South Caucasus, a literature that, as established in the preceding section, did not previously exist in any form prior to this paper.

Results

Table 1 presents verified data documenting the scale and recent trajectory of Georgia's domestic capital market.

Table 1

Verified Indicators of Georgia's Domestic Capital Market Scale and Development

Indicator	Value	Source
Domestic corporate bond market size, 2018	USD 205 million	Georgia Today, 2024, citing TBC Capital and Galt and Taggart
Domestic corporate bond market size, end of 2023	Approximately USD 800 million	Georgia Today, 2024
Domestic corporate bond market size, end of 2025	GEL 2.7 to 3.2 billion (approximately USD 1.0 to 1.1 billion)	National Bank of Georgia; Investor.ge, 2026; Rustavi2, 2026
Year-on-year growth of public corporate bond volume, 2025	33.3 percent	National Bank of Georgia Governor Natia Turnava, reported by Rustavi2, 2026
Share of the largest 500 non-financial corporates' debt held in foreign currency, 2018	Approximately 80 percent	World Bank Financial Sector Assessment Program, Georgia
Number of large institutional investors active in the domestic market, 2023	321	Investor.ge, 2024, citing TBC Capital analysis
Share of new 2025 corporate bond issuances carrying a credit rating	79 percent	National Bank of Georgia Governor Natia Turnava, reported by Rustavi2, 2026

Source: compiled by the author from the cited sources.

The data in Table 1 show genuine growth in the domestic corporate bond market, with the reported market size roughly quadrupling between 2018 and the end of 2023 and continuing to grow into 2025 and early 2026. At the same time, the persistence of foreign-currency-dominated corporate debt as of the most recent comprehensive assessment, and the continued characterization of the market as shallow by both market participants and the National Bank of Georgia itself, even after this growth, together indicate that the underlying institutional void, limited domestic capital market depth and liquidity relative to firms' financing needs, has not been resolved by growth alone.

Table 2 documents specific responses, named firm-level and policy-level, to this void, drawn directly from the cited sources.

Table 2

Documented Firm-Level and Policy-Level Responses to the Capital Market Void

Firm or programme	**Documented response to the capital market void**	**Source**
The largest 500 Georgian non-financial corporates	Approximately 80 percent of debt obligations are held in foreign currency, reflecting reliance on foreign-currency bank lending rather than a deep local currency bond market	World Bank Financial Sector Assessment Program, Georgia
TBC Bank Group PLC and Lion Finance Group PLC (formerly Bank of Georgia Group PLC)	Both of Georgia's two largest banks are listed on the London Stock Exchange rather than the domestic Georgian Stock Exchange, with market capitalizations of more than USD 3.4 billion and USD 6.0 billion, respectively, as of February 2026	Asia Frontier Capital, 2026
Georgia Capital	Listed on the London Stock Exchange rather than domestically, with a market capitalization of USD 1.6 billion as of February 2026; also active as a domestic bond issuer	Asia Frontier Capital, 2026; Georgia Today, 2024
Enterprise Georgia Capital Market Support Program	A government program offering technical and financial incentives specifically to encourage small and medium-sized enterprises to issue bonds, used by a total of 12 companies in a single reported year to raise approximately GEL 900 million (USD 334 million)	Investor.ge, 2026
Alma (outdoor advertising company)	First advertising company to be traded on the Georgian Stock Exchange, issuing its debut bond under the Enterprise Georgia program	Investor.ge, 2026
MBC (microbank)	Issued two-year bonds in two tranches (GEL 21.3 million and GEL 30 million) under the Enterprise Georgia program, with the second tranche oversubscribed; also drew on financing from the Swiss platform Symbiotics, the European Fund for Southeast Europe, and the Armenian bank Inecobank	Investor.ge, 2026
Pension Fund of Georgia	Established in 2018 as the country's first mandatory, defined-contribution pension system, participated as an investor in the May 2025 MBC bond issuance, marking its first-time purchase of microbank bonds and reflecting the gradual emergence of a domestic institutional investor base for corporate bonds	Institutional Investor, 2025; Investor.ge, 2026

Source: compiled by the author from the cited sources.

Two distinct response patterns are evident in Table 2. The first is exit to a deeper external market: Georgia's two largest banks and its most prominent diversified holding company are listed not on the domestic exchange but on the London Stock Exchange, where they can access a deeper pool of capital and a more liquid secondary market than the domestic exchange currently provides. Consistent with Khanna and Palepu's (1999) finding on foreign institutional investor monitoring, this pattern suggests that Georgia's largest and most established firms judge the benefits of access to a deeper, more rigorously monitored market to outweigh the costs of meeting that market's higher disclosure and governance requirements. The second is targeted public infrastructure-building aimed specifically at the segment of the market least able to use the first strategy: the Enterprise Georgia Capital Market Support Program provides technical and financial incentives specifically to help small and medium-sized enterprises, which lack the scale to list internationally, access domestic bond financing instead.

A third, more incremental pattern is also visible in the emergence of a domestic institutional investor base. The Pension Fund of Georgia's 2025 purchase of MBC's bonds, its first investment in microbank debt, indicates that the pool of domestically managed capital available to smaller Georgian issuers is beginning to widen beyond the two large banks that have historically dominated the market's demand side. This is consistent with the broader pattern noted in Georgian financial market reporting that the number of large individual investors active in the domestic market grew to 321 by 2023, and that resident individuals accounted for 20 per cent of investment activity that year, suggesting a gradual, though still limited, deepening of the domestic investor base alongside the growth in market size already shown in Table 1.

Credit Information Infrastructure as a Partial Offset

Not every market-supporting institution relevant to SME lending is absent from the Georgian financial landscape, and acknowledging this is necessary for an accurate characterisation of the void this paper documents. JSC Credit Information Bureau CreditInfo Georgia has operated since 2005 under the supervision of the National Bank of Georgia, maintaining a centralised database, including a Defaulting Debtors Database compiling records from courts, tax authorities, and participating lenders, that supplies the kind of borrower credit history information that, in many emerging and transition economies, is itself absent and that the broader international literature identifies as a frequent constraint on SME lending. The National Bank's own supervisory reporting indicates that both the bureau and participating lending institutions are subject to regular inspection, and that the regulatory framework governing the bureau, including the rules determining what data lenders must report and how consumers may consent to verification, has continued to be refined, with amendments introduced as recently as 2020 clarifying electronic consent requirements.

The persistence of high SME loan rejection rates and elevated collateral requirements documented above, despite the presence of this credit information infrastructure since 2005, suggests that the binding constraint on Georgian SME lending lies less in lenders' ability to obtain borrower credit history, a function the credit bureau appears to perform adequately. More in the underlying risk characteristics of the SME segment itself and in the absence of complementary mechanisms, such as movable collateral registries or asset-based lending frameworks of the kind the World Bank's SME finance literature identifies as effective complements to credit reporting, that would allow lenders to extend credit against forms of collateral more readily available to smaller, asset-light Georgian firms than the real estate collateral that conventional bank lending in Georgia has historically required.

The Underlying SME Financing Gap That the Enterprise Georgia Program Addresses

The Enterprise Georgia Capital Market Support Program, documented in Table 2 as a targeted response to the capital market void, sits against a broader, independently documented background of constrained SME access to finance in Georgia, evidence of which further substantiates this paper's characterisation of the void as severe for smaller firms specifically. A World Bank Enterprise Survey, summarised in a report prepared for the United Nations Global Compact's Georgia network, found that Georgian businesses identify access to finance, alongside political instability and inadequate workforce education, as a principal obstacle to doing business, and that despite near-universal possession of checking or savings accounts among Georgian SMEs, only 51 percent of small and 53 percent of medium enterprises had actually obtained a bank loan, a gap the survey attributes substantially to a high rate of loan rejection.

A policy paper prepared by the PMC Research Centre in Tbilisi further quantifies this rejection pattern, reporting that 38 per cent of Georgian SMEs carry bank debt. In comparison, approximately 21 per cent of SME loan applications are rejected, and identifying lack of collateral as a leading obstacle, with

Georgian banks requiring collateral averaging 191 per cent of the loan amount, a ratio that the European Investment Bank's Bank Lending Survey similarly identifies as a primary constraint specific to smaller, less established borrowers. These collateral and rejection-rate figures help to explain, at the level of individual lending decisions, the more aggregate, market-level shallowness already documented in this paper's Results section: a financing environment in which banks systematically require collateral well in excess of the loan principal is one in which alternative, non-collateral-dependent financing channels, including the corporate bond market access that the Enterprise Georgia programme specifically targets, carry particular value for smaller firms unable to meet conventional bank collateral requirements.

The Georgian government's policy response extends beyond the Enterprise Georgia bond program already discussed. The OECD's 2026 SME financing scoreboard documents a separate, complementary instrument, a Credit Guarantee Scheme under which the state covers up to 80 percent of loan principal for SMEs unable to meet existing bank collateral requirements, with guaranteed loan volumes increasing from GEL 210 million to GEL 259 million between 2023 and 2024, and total guarantees issued rising from GEL 151 million to GEL 185 million over the same period. Considered together, the Enterprise Georgia bond-support programme and the Credit Guarantee Scheme indicate that Georgian policy has developed two parallel, and apparently growing, instruments addressing the same underlying SME financing constraint through different mechanisms, the former by facilitating direct capital market access, and the latter by reducing the collateral burden of conventional bank lending, both consistent with this paper's broader finding that the Georgian state, rather than the market alone, has taken a leading role in addressing the capital market void's most severe effects on smaller firms.

Foreign Direct Investment as a Further Window on the External-Financing Pattern

Georgia's foreign direct investment statistics provide an independent, cross-validating window on the external-financing pattern already identified among the country's largest firms. According to United Nations Conference on Trade and Development data reported through the International Trade Portal, Georgia's total inward FDI stock stood at approximately USD 24.35 billion at the end of 2023, equivalent to around 79.8 per cent of the country's GDP, with annual inflows of USD 1.59 billion in 2023, USD 1.33 billion in 2024, and USD 1.7 billion in 2025. The United Kingdom has consistently ranked among the largest single-country sources of this investment, recorded at 19.6 per cent of total FDI stock and as the single largest annual investor in both the 2024 and 2025 reporting years.

This United Kingdom figure, however, requires careful interpretation rather than a literal reading of foreign capital newly entering the Georgian economy. Georgian financial reporting on the 2025 FDI results states that the United Kingdom's leading position is driven substantially by the fact that Georgia's two largest financial institutions, TBC Bank and Bank of Georgia, both already documented in this paper's Results section as listed on the London Stock Exchange rather than the domestic exchange, are legally registered in the United Kingdom, with the implication that at least part of their recorded operations and capital flows are captured in Georgia's FDI statistics as foreign rather than domestic activity. This paper relies on financial journalism rather than a primary methodological statistics document for this specific attribution, and the precise statistical treatment applied by Georgia's National Statistics Office to UK-domiciled, Georgian-operating financial groups has not been independently verified here; the claim should accordingly be read as a plausible and reported explanation for the United Kingdom's prominence in Georgia's FDI statistics rather than as an independently confirmed methodological fact. If accurate, this pattern would be consistent with, and would help to explain, this paper's central finding regarding large-firm external listing, since the same institutional choice that leads Georgia's largest banks to access deeper capital and disclosure standards abroad, documented qualitatively in this paper through Asia Frontier Capital's market capitalisation data, could also inflate Georgia's recorded inward FDI figures if UK-domiciled holding structures for operationally Georgian banks are indeed captured by national statistics as foreign rather than domestic.

Beyond this UK-specific pattern, Georgia's financial sector as a whole attracted the largest single share of FDI by sector in 2024, at 39.5 percent of total inflows that year, continuing a pattern in which financial and insurance activities had also led sectoral FDI in 2023, at 25.4 percent of that year's total, a concentration that the World Bank's Financial Sector Assessment Program situates within a broader balance-of-payments structure in which Georgia's current account deficit is financed predominantly by FDI, an accumulation of external liabilities, and worker remittances, rather than by domestic capital market intermediation. This financing structure is consistent with, and provides further context for, the approximately 80 per cent foreign-currency share of large-corporate debt already documented in Table 1, since an economy financing its external imbalance primarily through foreign capital inflows and foreign-currency external liabilities would be expected to exhibit a correspondingly high degree of foreign-currency-denominated corporate financing, independently of the specific depth of its domestic bond and equity markets.

Discussion

Theoretical Implications

These results extend institutional voids theory in three distinct ways. First, they show that the strategic response to a capital market void is not limited to internal diversification of the kind Khanna and Palepu (1997, 2000a, 2000b) originally documented in India and Chile, where group-affiliated firms substitute internal capital allocation for an absent or costly external market. In the Georgian case, the dominant large-firm response documented here is external listing, accessing a deeper foreign capital market directly, rather than building an internal substitute at home. This is consistent with Marquis and Raynard's (2015) broader taxonomy of institutional strategies. Still, it specifically extends the capital-market-void literature, which has focused predominantly on internal capital markets and business group formation, by documenting external market access as an equally available and, in this case, apparently preferred response for the largest firms in a small, open economy where the domestic market's scale constraints, as distinct from its institutional quality, may be the more binding limitation.

Second, the Enterprise Georgia program illustrates a distinct mechanism not centered in the original institutional voids framework: void-filling initiated by the state rather than by firms acting independently. Where Khanna and Palepu's (1997, 2010) original framework treats firms as the primary actors compensating for institutional absence, the Georgian case shows a public program explicitly designed to address a documented gap, specifically, the inability of smaller firms to access bond financing on their own, by directly subsidising and de-risking the specific firms least able to use the large-firm strategy of external listing. The documented results of this program- twelve companies raising approximately GEL 900 million in bonds in a single reported year, with at least one tranche oversubscribed- indicate a program that is achieving real, measurable uptake, though the data presented here cannot establish whether this uptake reflects a durable deepening of the market or a temporary effect of targeted subsidy. This finding is consistent with, but extends, Nayyar and Luiz's (2024) argument that institutional void severity shapes the type of response that is likely to be effective: where the void is severe enough that even a well-run firm cannot access financing independently, as appears to be the case for Georgian small and medium-sized enterprises, a state-initiated infrastructure response may be necessary to complement, rather than wait for, a purely firm-led or market-led solution.

Third, the gradual emergence of the Pension Fund of Georgia as a participant in corporate bond issuances suggests a slower, more incremental third pathway: the organic development of a domestic institutional investor base that can, over time, supply some of the monitoring and capital-allocation functions that, in Khanna and Palepu's (1999) account of the Indian case, foreign institutional investors were shown to provide. Whether Georgia's pension fund and its retail investor base will, over a longer period, come to play a comparable monitoring role is a question this paper's documentary method cannot resolve, but the direction of the trend documented here, a pension system established only in 2018 already participating in microbank bond issuances by 2025, suggests this pathway is at least beginning to develop alongside the two firm-led responses already discussed.

Fourth, the Georgian case offers a useful empirical referent for Nayyar and Luiz's (2024) proposal that institutional void severity be treated as a graded rather than binary construct. The evidence assembled in this paper indicates that Georgia's capital market void is severe along some dimensions and comparatively moderate along others, a pattern that a binary present-or-absent classification would obscure. Basic market infrastructure, an operating stock exchange, a central securities depository, and an independent securities registry system have existed since 1999 and remain functional, placing Georgia well above a complete-absence baseline on this dimension. Market depth and liquidity, by contrast, remain severely constrained relative to the financing needs of even modestly sized corporates, as evidenced by the near-total reliance of the largest 500 non-financial corporates on foreign currency rather than local-currency debt. Regulatory architecture occupies an intermediate position: a dedicated securities law and a specialised securities regulator were established by 2000, but that dedicated regulator was abolished in 2007 and 2008 and its functions folded into a bank-focused central bank mandate, a change in institutional form that this paper characterises as a regression in dedicated regulatory capacity, even though the National Bank of Georgia has subsequently overseen genuine growth in the corporate bond market documented in Table 1, including a rising share of credit-rated issuances. This combination, a 2007 to 2008 reduction in specialised securities-market regulatory capacity alongside more recent, NBG-supervised bond market growth, suggests that the regulatory architecture's trajectory is itself non-monotonic rather than simply regressive, and that institutional void severity may vary not only in degree but in direction over time within a single sub-dimension, a refinement to the severity construct that this paper’s documentary evidence supports but that would require dedicated future research, of the kind proposed below, to test more rigorously.

Practical Implications for Management and Policy

For Georgian managers, particularly at small and medium-sized firms, these findings carry a direct practical implication: bond issuance support through the Enterprise Georgia program has, in the documented cases, produced real financing outcomes, including oversubscribed issues, and represents an evidenced financing channel rather than a purely theoretical option. For larger firms with the scale to consider it, the experience of Georgia's largest banks and Georgia Capital indicates that international listing remains a viable and used route to capital that the domestic market does not yet offer at comparable depth. However, this route entails higher disclosure and governance obligations that, per Khanna and Palepu (1999), make a firm more attractive to the more rigorous foreign institutional investors it seeks to reach.

For policymakers, the combination of genuine market growth alongside persistent shallowness suggests that continued, and potentially expanded, targeted programs of the Enterprise Georgia type may be necessary to extend capital market access beyond the largest and most internationally visible firms. The gradual entry of the Pension Fund of Georgia into corporate bond markets further suggests that policies supporting the growth and diversification of domestic institutional investors, rather than focusing solely on issuer-side incentives, may complement the existing program by building the demand-side capacity needed to absorb a larger volume of future issuances without relying primarily on bank and foreign-currency financing.

Banking Sector Concentration as a Structural Counterpart to the Capital Market Void

The capital market void documented in this paper does not exist in isolation from the structure of Georgia's banking sector, and understanding that structure helps explain why bank-centred financing has remained the dominant alternative to bond and equity markets for Georgian firms. The World Bank's Financial Sector Assessment Program found that Georgia's banking sector is heavily concentrated across all major banking products, with TBC Bank and Bank of Georgia individually accounting for approximately 38 percent and 36 percent of total banking assets respectively as of the assessment period, and with the top three banks, including the smaller Liberty Bank, together exceeding 79 percent of total banking assets, a combined top-three concentration that the World Bank reports vastly exceeds the top-three market share observed in a set of regional peer countries including Armenia, Azerbaijan, Turkey, Serbia, North Macedonia, and Romania, where Herfindahl-Hirschman Index concentration measures rarely exceed 1,500 points. More recent reporting from the Banking Association of Georgia placed the combined asset share of the same two banks at 76.6 per cent as of the first eight months of 2025, alongside an even higher concentration of sector profits, with the two banks accounting for over 91 per cent of total commercial banking net profit in early 2025.

This concentration has a direct and verifiable connection to the external-listing pattern already documented in this paper's Results section. A 2016 presentation on the Georgian banking market prepared for an international financial regulators' forum (Utiashvili, 2016) noted explicitly that because the two largest banks are listed on the London Stock Exchange rather than the domestic exchange, the practical effect, at that time, was that almost half of the entire Georgian banking sector, measured by assets, was traded on a foreign rather than a domestic exchange, a proportion broadly consistent with the more recent 2025 and 2026 reporting on the same two banks' continued combined market share discussed above. This is a striking illustration of the scale of the pattern this paper documents: the firm-level decision to access deeper foreign capital markets, observed for Georgia's largest financial institutions, is not a peripheral feature of an otherwise domestically oriented financial system, but extends to roughly half of the banking sector that itself supplies the great majority of credit to the rest of the Georgian economy.

The concentration of Georgia's banking sector appears, based on the evidence presented here, to reinforce rather than merely coexist with the shallowness of the domestic capital market documented in this paper. A banking sector in which two institutions hold close to four-fifths of assets and the overwhelming majority of profits is, almost by definition, well placed to supply the great majority of corporate financing through traditional lending relationships, reducing the immediate commercial pressure, from either the supply or demand side, to develop deep and liquid alternative channels such as domestic corporate bond or equity markets. This dynamic offers one plausible explanation, alongside the regulatory history discussed earlier in this paper, for why bank-centred and foreign-currency financing has remained dominant even as Georgia's domestic bond market has grown in absolute terms since 2018.

Comparison with Other Small, Open Transition Economies

The Georgian pattern documented in this paper is not unique to post-Soviet or South Caucasus economies, and situating it alongside comparable cases helps clarify which features of Georgia's capital market shallowness are a function of its specific transition-economy history and which are a more general feature of small, open economies regardless of their institutional development. The European Bank for Reconstruction and Development's own assessment of the Baltic states, Estonia, Latvia, and Lithuania, three economies considerably further advanced in their post-Soviet transition than Georgia, with full European Union membership, the euro as their currency, and what the EBRD itself describes as strong institutions, found that these countries nonetheless continue to exhibit small and shallow capital markets that have left companies, and small and medium-sized enterprises in particular, struggling to secure sufficient financing for growth. The specific structural features the EBRD identifies as barriers-concentrated banking sectors, thin issuer and investor bases, limited availability of nonbank finance, and limited depth in local corporate bond markets sufficient to absorb larger transactions- are substantially the same features documented for Georgia in this paper's Results section.

This comparison is theoretically informative in two respects. First, it suggests that capital market depth may be constrained not only by the institutional quality variables that the original institutional voids literature emphasises, contract enforcement, investor protection, auditor credibility, but also by the sheer scale limitations of operating a domestic capital market within a small national population and economy, a constraint that EU membership and institutional convergence, as the Baltic case shows, do not by themselves resolve. Second, it suggests that the specific policy responses observed in the Baltic states, including a regionally coordinated effort by the three countries' finance ministries, beginning with a memorandum of understanding signed in 2017, to harmonise covered bond regimes and launch a joint regional equity index in 2023 specifically to pool issuer and investor bases across national borders, represent a response category, regional capital market integration, that is not yet observed in the Georgian case examined here, and that may offer a relevant model for Georgia and other small Eastern Partnership economies to examine in future research, regardless of the particular pace or sequencing of any individual country's broader institutional development.

The Baltic comparison also offers an important caution against treating the Georgian capital market void as simply a problem that further institutional development will mechanically resolve. If three economies as institutionally advanced as Estonia, Latvia, and Lithuania, fully integrated into the EU single market and the eurozone, continue, by the EBRD's own account, to exhibit shallow capital markets and SME financing constraints, then the relationship between formal institutional quality and capital market depth is evidently more complex than a simple linear progression, a point consistent with this paper's broader observation that genuine market growth, as documented for Georgia in Table 1, and persistent structural shallowness can coexist for an extended period rather than the latter being quickly resolved by the former.

The European Union's Own Experience of Capital Market Fragmentation

A further, and in some respects even more striking, comparator is the European Union as a whole. Since 2015, the European Commission has pursued the Capital Markets Union initiative, a large-scale, long-term policy program explicitly designed to tackle fragmentation across the Union's capital markets, remove regulatory barriers to cross-border investment, and increase the supply of capital available to businesses, with small and medium-sized enterprises identified from the outset as a particular priority. The European Court of Auditors, in a 2020 special report, characterised progress under the initiative's first five years as a slow start towards an ambitious goal, and the European Commission's own 2020 assessment, accompanying a renewed action plan of sixteen further legislative and non-legislative measures, acknowledged that, despite progress since 2015, EU capital markets remain fragmented along national lines, with integration lagging behind levels seen before the global financial crisis.

The scale of this fragmentation, even within one of the world's largest and most institutionally developed single markets, is informative for the Georgian case. The World Economic Forum, drawing on data compiled by the Association for Financial Markets in Europe, reported that risk capital, encompassing venture capital, private equity, and related financing, comprised only 2 to 5 percent of total small and medium-sized enterprise financing across the EU from 2018 onward, compared with more than 10 percent in the United Kingdom, and that the United States risk capital sector was between five and 7.5 times larger relative to the size of its economy than the EU's over the past decade. The same report noted a 72 percent year-on-year drop in 2023 in the volume of European risk-capital-backed companies transitioning to initial public offerings, and observed that the EU's venture capital and private equity markets remain heavily concentrated in a small number of member states, principally France, Germany, the Netherlands, Denmark, and Sweden, leaving SMEs in smaller or less central member states facing financing conditions not unlike those documented for Georgia in this paper, despite operating within the formal legal and regulatory framework of the EU single market.

This comparison reinforces, from a different direction, the conclusion already suggested by the Baltic case: capital market depth is not solely, or even primarily, a function of formal legal harmonisation or institutional convergence, since the EU has pursued exactly such harmonisation for a decade without resolving the underlying fragmentation and SME financing gap that its own Capital Markets Union initiative was created to address. The European Commission's acknowledgement that there is no single measure capable of establishing a strong and integrated capital market, and that supervisory, insolvency, and tax fragmentation across member states continues to constrain progress, suggests that the mechanisms generating capital market shallowness operate at multiple, interacting levels, regulatory, institutional, and structural, a multi-level character that this paper's Georgian case study illustrates at a national rather than supranational scale. For Georgian policymakers, the relevant implication is not that EU-aligned market regulation is unnecessary, but that such alignment should be understood as one input among several that contribute to capital market depth, rather than as a measure expected, on its own, to resolve the void documented in this paper.

Limitations

This paper's documentary method, while well-suited to establishing that a capital market void exists and is documented, and that specific, named responses to it have occurred, cannot establish causal relationships between program participation and firm-level outcomes such as growth, survival, or profitability. Nor can it determine, from the data presented, whether the documented growth in market size between 2018 and 2026 will continue, plateau, or reverse. These limitations motivate the future research agenda set out below.

Conclusions and Implications

This paper documented, using verified financial market data, a specific and consequential institutional void in the Georgian economy, namely the limited depth and liquidity of the domestic capital market relative to firms' financing needs, and traced three distinct, evidenced strategic responses to it: external listing on a deeper foreign exchange by Georgia's largest firms, targeted public bond-support infrastructure, the Enterprise Georgia Capital Market Support Programme, aimed at smaller firms lacking the scale for the first strategy, and the gradual, organic emergence of a domestic institutional investor base, evidenced by the Pension Fund of Georgia's first purchase of microbank bonds in 2025. The paper further situated the present condition of the market within its own institutional history, showing that an initial period of broad-based securities market infrastructure-building between 1999 and 2007 was followed by a period of regulatory retrenchment and brokerage-firm consolidation into the banking sector, a sequence that helps explain why bank-centred and foreign-currency financing remain dominant even as the corporate bond market has grown substantially in absolute terms since 2018.

Comparison with the Baltic states further indicated that capital market shallowness of the kind documented here is not simply a marker of an incomplete post-Soviet transition that will be mechanically resolved by further institutional development. Estonia, Latvia, and Lithuania, despite full European Union and eurozone integration and institutional quality considerably more advanced than Georgia's, continue, by the EBRD's own account, to exhibit small and shallow capital markets constraining firm financing, and have responded through a distinct strategy, regional capital market integration across the three countries, not yet observed in the Georgian case. Together, these findings extend institutional voids theory beyond its original focus on internally generated, firm-led substitutes, of the kind Khanna and Palepu (1997, 2000a, 2000b) documented in India and Chile, by documenting externally directed, state-initiated, and organically emerging investor-base responses, and by showing that scale constraints specific to small economies may interact with, and persist independently of, the institutional quality variables that the original literature emphasises.

The underlying SME financing gap documented in this paper, evidenced by loan rejection rates of approximately 21 percent and collateral requirements averaging 191 percent of loan value, further indicated that the Enterprise Georgia bond-support programme operates alongside a second, complementary state instrument, the Credit Guarantee Scheme, both of which have grown in scale in recent years and both of which address, through different mechanisms, the same underlying constraint on smaller firms' access to financing that this paper's institutional voids framework identifies as a central feature of the Georgian capital market void.

Suggestions for Future Research

Four directions for future research follow from this paper's documentary analysis. First, firm-level survey or interview research with Georgian small and medium-sized enterprises that have and have not participated in the Enterprise Georgia program would allow direct testing of whether program participation produces measurable financing or growth advantages, a question this paper's documentary method cannot itself resolve. Second, longitudinal tracking of the specific market depth and liquidity indicators presented in Table 1 over a longer period would clarify whether the documented growth trend represents durable capital market deepening or a temporary expansion that may not persist. Third, comparative research applying the same documentary method to other small, open, transition economies with similarly thin capital markets, including other Eastern Partnership economies and smaller EU member states beyond the Baltic states examined here, would establish whether the response patterns identified in this paper are general features of firm and policy adaptation to capital market voids in small economies or specific to the Georgian case. Fourth, and following directly from the Baltic comparison, future research could usefully examine whether a regionally coordinated capital market integration strategy, of the kind Estonia, Latvia, and Lithuania have pursued since 2017, holds practical relevance for Georgia in cooperation with other South Caucasus or Eastern Partnership economies facing comparable scale constraints, independently of the pace of any individual country's broader institutional development.

Acknowledgements

None.

Conflict of Interest

None.

Funding

The authors received no funding for this research.

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