Export problems of nationally produced goods in terms of deep and comprehensive free trade area with the EU

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Abstract. The optimal use of this agreement has great importance for countries with deep and comprehensive trade with Europe. The aim of the research is to study export potentials and factors which influence the growth of export of post-socialist and euro-integration supporting countries participating in this agreement. The aim of research is also to identify the importance of deep and comprehensive trade with the EU for economic development of the countries. The move to a new formulation led to the disruption of industrial forces in most of the countries, and also eliminated the traditional manufacturing fields in which these countries had a comparative and absolute advantage. The result is that the main problem of local producers is that most of them do not know the preferences that are given to the EU market, also, most manufacturers fail to produce the number of products that would satisfy the customer and most of the do not have quality certifying certificates. In order to improve the situation, the article provides the measures and marketing recommendations to be implemented by the country, which, we think, is common to those countries that have signed the free trade regime with Georgia and face similar problems.

1. Introduction

After gaining independence, Georgia is going through the difficult ways of development. Economic and political problems are of vital importance from many problems. The most important basis of political problems is tense relations with Russia. According to a number of scholars, the main problem with Georgia’s northern neighbor stems from the fact that Georgia has a favorable geopolitical location, which is expressed by the existence of many international pipelines and gas pipelines. Largest transit potential of country is obviously clear – it enables Europe to cheaply and uninterruptedly get Caspian, Asian oils in general and natural gas bypassing Russia.

Georgia’s aspiration for European integration has not only political but also economic importance - Georgia has been depended on Russian market for years. Since 2006 the country export potential has been reduced dramatically, as Russia banned Georgian export in 2006, that caused necessity for diversification of foreign markets and, first of all, for adopting European markets. Regarding this, it is very important to note that since September 1, 2014, a large part of the Association Agreement has entered into force, including part of the Deep and Comprehensive Free Trade Area (DCFTA) of the Association Agreement. In December 2015, the ratification process for the Georgia-EU Association Agreement was completed by the EU member states.

The purposes of this particular research are to:
1. Provide a comparative study on the export potential of Georgia, determining the range of products that Georgia can offer to the EU markets;
2. Identify the relative advantages of producing goods for export in the post-communist/post-socialistic countries, which are currently supporting the idea of European integration;
3. Determine those factors due to which Georgia cannot fully use the advantages the Agreement grants;
4. Study the actual willingness of Georgian entrepreneurs to export their products to the EU markets.

2. Research Methodology
During the preparation process, the normative acts have been elaborated and analyzed, which was published by the Government of Georgia after the Association Agreement has been signed. Also, export data of Georgia carried out in 2007-2016 was used. Realized export per person of population is calculated and is compared with the similar figures in Ukraine and Moldova. The basic method of research are the grouping of statistical information and analysis, as well as the comparison method. In the process of research, the data from 2007-2016 are used, and the trend is identified for the ongoing processes. The information was taken from the website of the National Statistics Office of Georgia. In the theoretical part of this paper, the general data is analyzed, while the practical part covers a number of tables, graphs, and dynamics indicators, which are compared to each other. Based on the survey conducted, it is analyzed that Georgian manufacturers are ready to export products produced on the EU market. The final conclusions conform to the tasks set out at the beginning of the research.

3. Current Situation of Export Potential of Georgia
After gaining independence, the Georgia’s main challenge is to increase the export potential of the nationally produced goods. Improvement of country’s socio-economic situation, local currency stability, and employment growth depend on this opportunity. In 1999, Georgia became the WTO member country.

As a result of joining the WTO:

- Georgia’s integration into the world economic system has been strengthened;
- The Georgian legislative base has been harmonized with the European one, which is vital for achieving a strategic goal of integration with the EU;
- International market conditions for Georgian export products have been improved. Georgian entrepreneurs are protected from discrimination by the WTO multilateral agreements on these markets;
- Georgia received an opportunity to fairly solve the disputed issues raised in the goods and service trade field;
- Environment for attracting foreign investments was improved, because the investor got a guarantee of long-term trading policy, and international markets were open for Georgian products;
- Georgia received a full member vote for participation in the WTO bilateral and multilateral negotiations.

Prior to DCFTA, Georgia enjoyed benefited from the EU’s Generalized System of Preferences (GSP +) regime. It allowed privileges on 7200 products, which means 90% of trade turnover used advantage of zero tariffs in trade with the EU.

Agricultural products have particular importance in export potential of Georgia. Although agriculture is only 9.1 % of the GDP (gross domestic product), its export potential is noteworthy. Hazelnuts and other types of nuts are the basic export products. For 2016, it accounted 8,5% of the
whole exported products. The largest export market for Georgian hazelnut (60% of market) includes the European countries.

According to data from January-September 2017, the main Georgian export products are copper ores, ferro-alloys, re-export of sedan automobiles, wine, and medicines.

![Figure 1. Share of commodity positions by exports January-September 2017.](image)

The diagram shows that the main export potential of the country is the natural resources and re-export of sedan automobiles. Such kind of situation is typical for the countries with less developed manufacturing process. They can not create the export products and are satisfied with only exporting resources. In relation to the export of wine, its volume is increasing year by year. Despite the free and comprehensive trade regime with the EU, the Georgian export is directed to the close foreign countries. First of all, exports are linked to the Russian Federation (14.1% in 2017), followed by Azerbaijan (8.6%), Turkey (8.5%), and Armenia (7.5%), and China (8.3%). Such distribution of the export directions is mainly derived from the fact that the Russian Federation market, despite the lack of diplomatic relations with Georgia, remains in the historical memory and is attractive for the local manufacturers. The main Georgian product exported to the northern country is alcoholic drinks, subtropical fruits, and mineral water. The war between Russia and Georgia in 2008 changed the situation, this relationship was practically reduced, but in 2012, after parliamentary elections, the Russian market became more or less accessible for Georgian manufacturers.

In terms of exports, Russia, Turkey, and China are the main trading partners of Georgia. 26% of total export is made to these countries. The EU member countries have a bit different situation (Table 1).

| Table 1. External trade of Georgia by European Union countries. |
|---------------------------------------------------------------|
| **Year** | **2012** | **2013** | **2014** | **2015** | **2016** |
| Total Exports | 2376.6 | 2901.3 | 2861 | 2204.7 | 2113.1 |
| of which: European Union countries | 353 | 607.2 | 624.2 | 645.2 | 572.1 |
| | 14.90% | 20.90% | 21.80% | 29.30% | 27% |

As the table shows, Georgian export to the EU countries is growing annually, but it is insufficient, because a small amount of export cannot guarantee performing the task that Georgia needs.

4. Importance of DCFTA for Increasing Export Potential
The DCFTA is a mechanism of Georgia’s economic integration with the EU, which allows Georgia to receive gradually three out of four freedoms of the EU internal market: free movement of goods,
services, and capital. As for the fourth one, visa liberalization, the changed regulation N539/2001 of the European Union Council was published on March 8, 2017 in the official journal of the European Union, according to which Georgia has moved into the list of countries with a visa-free regime. The DCFTA is capable to change the situation on the local market, too. As manufacturing is being developed according to the EU standards, it means that the local customers are consuming the products produced by European standards.

Generally, free trade promotes abolishing of tariffs and the most common barriers of trading and establishes them only if export surpasses the respective quota (if any) or exceeds the agreed number of exported products, which are determined by the anti-counterfeiting mechanism. The main barrier is technical, and these barriers are: technical regulations, standards, certification procedures, etc. which differ by countries. Accordingly, the export product has problems in the country with strict regulations. This list also contains agricultural products produced in Georgia, which in some cases fail to meet the EU regulations and standards and endanger health of their country’s population, too.

The benefit resulting from DCFTA means:

- GDP growth by 1.7% in a short term perspective and 4.3% growth in a long term perspective;
- Export growth by 9% in a short term perspective and 12% growth in a long term perspective;
- For the next five years, there is a great prospect for exporting of raw and processed vegetable products, which increase may count 4%; the average salary increase by 3.6% in a long term perspective;
- Consumer price reduction by 1% and 0.6% in a long term perspective;
- Annual saving about 10.8 million EUR by the EU importers and saving about 84.2 million Euros by their Georgian partners;
- Diversification of the sales market by Georgian manufactures in the countries having most stable, open, and transparent game rules and growing demand;
- Increasing investments in Georgia and new work places; promoting new enterprises and supporting the growth of export products;
- Improvement of agro-food safety standards not only for the export products but also for the products placed on the local market;
- Export of Georgian products to the EU (if technical requirements are met) with zero customs tariff; increasing competitiveness of Georgian companies on the international market.

The benefits received from the DCFTA are not so obvious yet. However, the DCFTA covers 9,600 titles, including agricultural products that previously did not use the EU preferences. According to the DCFTA, customs duty is canceled for the products made in the EU and imported to Georgia, as well as for Georgian products made in Georgia and exported to the EU. There are also exceptions which must be taken into consideration when exporting to the EU.

5. First Results of the Association Agreement with the European Union: Export Data Comparison

On 27 June 2014, Moldova and Georgia signed the Association Agreement with the EU in Brussels. According to the agreement, these countries adopted the deep and comprehensive free trade regime (DCFTA). According to the EU Commission statistics, Moldavian product export to Europe was increased by 20.4% and reached 1 billion 159 million EUR in the same year, comparing with the previous year. In contrast, the Georgian export fell by 1.5%, up to 657 million EUR. The EU introduced the ENP action plan to Moldova (as with Georgia) in 2005 and also granted with the additional autonomous trade preferences (ATP) after three years.

The Georgian exports share was 21% in the European Union countries in 2014. It has just been increased by 2% for last ten years. Azerbaijan takes the first place (24%) among the export countries,
Russia’s export share was 16% in 2004, but its share fell by 2% in 2008 (due to embargo) and increased to 10% last year.

The export of agricultural products from Moldova to the EU increased by 31% comparing with a previous year and reached 375 million EUR in 2014. Vegetables took the leading place and supply increased by 54% and reached 203 million euros. It should be noted that the territory of Moldova is twice smaller than Georgia (34 square km), though it has a good climate and located mainly on the plains. Accordingly, agriculture holds more than 20% of the country’s economy. Georgia’s agricultural products exported to the EU in 2014 amounted only 155 million EUR; however, if compared to the previous year, a 26% growth was detected. As for the vegetables, this indicator was estimated by 113 million Euros.

As for Ukraine, despite the Association Agreement with the EU, country’s investment and export index was deteriorated. The key reason for this is the armed conflicts in Donbass and the political crisis. According to the data of 2014, export of Ukraine to the EU was raised only by 5%. Nearly half of Ukrainian exports are the metallurgical industry products, agricultural products, and raw materials. Industrial products, chemical industry, mechanical engineering, and oil refining products export are very significant as well.

Table 2. Export for 1 person 2007-2016 Years ($).

| Years | Country | Export, billion | Population, million | Export for 1 person, $ |
|-------|---------|-----------------|---------------------|-----------------------|
| 2007  | Georgia | 1,113           | 4,394               | 253,3                 |
|       | Ukraine | 58,3            | 42,5                | 1371,7                |
|       | Moldova | 1,97            | 3,581               | 550                   |
| 2008  | Georgia | 1,326           | 4,382               | 302,6                 |
|       | Ukraine | 78,7            | 46,2                | 1703                  |
|       | Moldova | 2,21            | 3,572               | 618                   |
| 2009  | Georgia | 0,990           | 4,385               | 225,7                 |
|       | Ukraine | 49,3            | 46,0                | 1072                  |
|       | Moldova | 1,62            | 3,567               | 454                   |
| 2010  | Georgia | 1,380           | 4,4                 | 311,1                 |
|       | Ukraine | -               | 45,7                | -                     |
|       | Moldova | 1,93            | 3,56                | 541                   |
| 2011  | Georgia | 1,7             | 4,52                | 378,8                 |
|       | Ukraine | 82,1            | 45,6                | 1799                  |
|       | Moldova | 2,77            | 3,56                | 778                   |
| 2012  | Georgia | 1,606           | 4,6                 | 357,1                 |
|       | Ukraine | 82,3            | 45,6                | 1807                  |
|       | Moldova | 2,74            | 3,6                 | 769                   |
| 2013  | Georgia | 1,812           | 4,483               | 404,1                 |
|       | Ukraine | 63,3            | 45,4                | 1393                  |
|       | Moldova | 2,91            | 3,56                | 817                   |
| 2014  | Georgia | 1,873           | 3,714               | 504,3                 |
|       | Ukraine | 53,9            | 43,0                | 1253,5                |
|       | Moldova | 2,97            | 3,557               | 834                   |
| 2015  | Georgia | 1,637           | 3,720               | 440                   |
Ukraine 38,1 427,6 891
Moldova 2,4 3,555 675

2016
Georgia 1,657 3,718 445,6
Ukraine 44,9 42,6 1054
Moldova 2,01 3,553 565

As the Table clearly demonstrates, the export indicator is growing annually in Moldova and in Georgia. In Ukraine, its indicator has been reduced recently, caused by the war situation, political, and economic crises and a tense relationship with Russia. For comparison, the export index is calculated for per capita. Among all these three countries, Ukraine holds the first place followed by Moldova and Georgia. The demonstrated growth of Georgia is due to decrease of population and not because of the growing economic and export potential. Population of Georgia has been reduced nearly by 1% recent years.

6. Local Entrepreneurs’ Readiness for Free Trade Regime with the EU

The Association Agreement with the EU allows Georgian entrepreneurs to get into the EU markets, which are stable in terms of the growing demand on natural and organic products. The most important thing for Georgian entrepreneurs is that there are consumers with high buying power. Currently, up to 50 Georgian companies meet with the requirements of Food Safety Management - ISO 22000. Wine and alcoholic beverages are the main source of agricultural products. These products enter to the European markets every year, but there are also some seasonal products that do not get into foreign market with a large number. For example: hazelnuts and other types of nuts.

For the EU market, only those manufacturers are interesting that guarantee to provide continuous supply, production quality and quantity. According to these three criteria, Georgian companies’ readiness can be analyzed to meet these requirements and have the quality certificate. In July-September 2017, we surveyed people from more than 100 companies in Georgia, especially on the territory of Ajara Autonomous Republic. They operate not only on the local market but also export their products abroad (not to the EU markets). The key reason to additionally focus on the Autonomous Republic of Ajara was its favorable location.

The key goal of this research was to determine the willingness of Georgian manufacturers to use free trade component and export their product to the EU markets.

We divided companies into three categories: small (number of employees is no more than 50 people), average (50-100), and large (more 100) ones. Most of the respondents are from small and medium companies.

Our research demonstrates that the manufacturing, agricultural companies hold a large place, mainly focusing on seasonal subtropical production, including a total of 7 nut processing enterprises. The table was made based on the obtained results, which display enterprises’ readiness to export their products to the EU markets. The data also allow to identify the hindering factors that have to be overcome by the state and enterprises’ joint efforts.

Table 3. Manufacturers survey results

| Types of enterprises | The number of respondents | Do you export or not? | Do you have a desire to export? | Do you have a quality certificate? | Problems | Solutions |
|----------------------|--------------------------|-----------------------|---------------------------------|------------------------------------|----------|----------|
| Small scale          | 48                       | Only 3                | yes-20, no-15, I do not know-13 | 0                                  | Financial; lack of production | 1. Providing more information; 2. State participation in |
| Medium scale         | 40                       | Only 7                | yes-30, no -10                  | 3                                  | Lack of information         |          |
| Large scale          | 12                       | Only 2                | Yes - 12                        | 4                                  | Cannot meet                |          |
The main problems of Georgian manufacturers’ could be conditionally divided into three parts: qualitative-quantitative, informational, financial and marketing ones.

Most of enterprises fail to continuously provide a large number of products to the EU markets and guarantee international and European standards of product. The means of majority enterprises do not correspond to the modern manufacturing needs, most of them are outdated, largely affecting the product quality and quantity. The reason is not only the absence of quality certificates but also low standards of their products. As the survey showed, most of the manufactures do not have the standard certificate; it is impossible to export to the EU without that certificate. All entrepreneurs have a desire to own the certificate, but low revenues do not allow them to do that. At the same time a big number of manufacturers had no idea on preferences given by free trade agreement with the EU.

- It turned out that only 15 % of the interviewed respondents were more or less familiar with the issues of the EU partnership. The rest of the enterprises do not have information on benefits they could get from exporting to the EU. Some manufacturers do not want to produce export products. That itself hinders the process of innovative improvement. The lack of information is also evident in that fact that the enterprises do not have the direct contact with the customer, do not study market needs, and do not plan manufacturing on the bases of relevant preliminary studies;
- The key financial problem is that most of enterprises do not have a working capital. The solution is to take business loans that are less available for enterprises because they do not have the right amount of the main resources that can afford the loan. The majority of Georgian banks are funded by European Bank of Reconstruction and Development and they issue “European Business loans”, the loan volume is from 100,000 to 3,000,000 USD, the main period is 5-10 years. According to the data of World Bank, the average interest rate for business loan in Georgia is 12.5%. In such circumstances, it is unfavorable to take loans for the local companies because the risk factor is quit high.
- The key marketing problem is that the new marketing approaches are needed to grow the export potential of the company in order to identify the export markets where the production can be exported successfully. The essential term for increasing the export potential in our economic practice is to master the methods and techniques of modern international marketing by the management and the staff of the company. Many companies, while having all technological potentials to manufacture quality goods, are just not capable to work effectively on the foreign markets. Partially, it is caused by the fact that the company does not have the relevant marketing strategy that can be focused on the target groups of foreign countries, competitive advantages, etc.

In sum, the Georgian manufacturer is not ready yet to fully use the deep and comprehensive trade conditions with the EU. This situation demands a number of actions to be taken.

7. Conclusions
In order to get the Georgian manufacturer ready to export the products to the EU markets, it is necessary to carry out the specific activities with maximum results. In this respect, the policy pursued by the state is important. One of the expressions of this is that the Agency would be established in Georgia with the purpose to ensure the risks associated with export transactions of products or services. The agency will promote the export potential of Georgia and enhance Georgian companies’
competitiveness on the international markets by insuring credit risks, offering financial instruments, providing additional financial opportunities. Apart from these, it is necessary to carry out such activities, in which state authorities would cooperate with the enterprises themselves. These activities can be divided as the (a) state stimulating and (b) enterprise marketing activities:

- The state has to better inform the manufactures about various opportunities about advantages of adopting the deep and comprehensive trade regime with the EU;
- Promoting the manufacturers quality assurance means assisting in obtaining the European standard certificate;
- The financial provision of the manufacturers can be acceptable if the state sets an exporting financial support fund that would provide long-term, low-cost loans to those enterprises which have a prospect to export its products to the EU;
- Applying international marketing methods, which is inevitable for successful sales in the foreign markets;
- Adjusting the right price policy is the key of marketing program and significantly impacts goods competitiveness; at the same time, it is the peculiar guarantee of maintaining the commercial risk;
- Continuous improvement of the product quality, which supports increasing of the product competitiveness and export potential in the foreign markets;
- It is significant that the companies exporting goods must think of product packaging;
- Increasing awareness about a number of competitive Georgian products, which would support customer confidence.
- Gaining a competitive advantage is the ground of success in the foreign markets; development prospects of any company and evaluation of the export products’ potential have to be determined by the strategic marketing analyses.

Implementation of these activities can facilitate the export of nationally produced goods to the deep and comprehensive free trade area (DCFTA), which would be the ground for Georgia to be integrated in Europe.

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