The EU’s Association Agreement with Georgia: Assessing the Domestic Political and Economic Implications

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Introduction

EU-Georgia relations have entered a new phase. Georgia took a step closer to the European Union at the third Eastern Partnership Summit in Vilnius in November 2013 when it initialed an Association Agreement (AA) with a Deep and Comprehensive Free Trade Area (DCFTA). The agreement is to be signed later this year, provided that Georgia meets all necessary conditions.

The AA represents a bilateral dimension of the EU’s Eastern Partnership (EaP) initiative, launched at the Prague Summit in May 2009. The overall objective is to support the political and economic approximation to the EU of the latter’s six eastern neighbors, Georgia included.

Structurally and policy-wise, the AA/DCFTA is the most advanced of the cooperation mechanisms that the EU has offered to Georgia (and to other eastern partners) over the past twenty years. The weight of the AA lies in its relatively enhanced conditional structure, i.e., clear future benefits linked to the imposition of domestic reforms. This does not imply reactive enforcement, such as application of penalties in case of non-compliance. Instead, it consists of clearly formulated programmatic benchmarks for the implementation of EU requirements. Within the scope of the AA, the EU embarks on a so-called “more for more” approach, meaning that the EU offers concrete carrots in exchange for commitments to deep and comprehensive political reforms. Although the agreement does not open a possibility for accession to the EU, the benefits of the AA/DCFTA are still attractive: deepened and intensified political dialogue, full access to the EU market, and visa liberalization.
The EU-Georgia AA is a thick and comprehensive document of around 1,000 pages. The European Commission released the text of the agreement after its initialization at the EaP Summit at the end of November 2013. The AA is structured into three major parts. The first part focuses on political dialogue, association, and respective reforms; cooperation and convergence in the field of foreign and security policy; and convergence in areas of justice, freedom, and security. The provisions of the DCFTA, which is an integral part of the AA, are covered in the second (economic) and third (sectoral) parts of the agreement. This includes convergence and cooperation in fields such as: trade and trade-related matters, national treatment and market access for goods, technical barriers to trade, sanitary and phytosanitary measures, customs and trade facilitation, intellectual property rights, and competition. In addition, the agreement covers sectoral areas, such as tourism, agriculture and rural development, consumer protection, cooperation on employment and social policy, public health, education, culture, sports, civil society, and cross-border and regional cooperation.

The convergence reforms that the EU has set forth in the scope of the association process are complex and require serious domestic political and economic commitments. This raises questions about the AA’s potential benefits, as well as the anticipated costs and risks of compliance. This memo analyzes the potential domestic implications of the AA for Georgia.

**Georgia’s European Way**

The political implications of the AA for Georgia are multifaceted. To begin with, the EU association process is a litmus test for Georgia’s new political administration to demonstrate (domestically and internationally) its European way and commitment to fundamental democratic reforms.

The country’s previous ruling elite, under President Mikheil Saakashvili, proclaimed its European identity and made EU integration a major foreign policy objective. However, the government’s public discourse was never consistently followed by an adequate level and quality of reforms necessary for European approximation. The previous administration was not enthusiastic about implementing the EU’s “deep and comprehensive” regulatory reforms due to high convergence costs. Instead of targeting long-term sustainable
development and growth, Tbilisi proceeded with marginal reforms and used the possibility of EU approximation as a political tool to sustain EU support and financial assistance.\(^1\)

Georgia’s 2012 parliamentary election and 2013 presidential election brought a new administration to power. Over the past year, the new government has demonstrated a somewhat accelerated speed of reforms for EU approximation, the fruits of which were reaped at the Vilnius summit. Yet the government’s main political challenge is ahead. Now that the AA has been initialized, it is time to commence implementation of its provisions. This means that the government has to embark on large-scale “deep and comprehensive” reforms both at legislative and policy levels, as well as at the institutional level. The AA’s political section requires extensive convergence to EU norms and requirements in the field of justice, freedom, and security. Particular importance is attached to the consolidation of the rule of law and the reinforcement of institutions at all levels in the areas of administration in general, and law enforcement and the administration of justice in particular. Cooperation will notably aim at strengthening the judiciary, improving its efficiency, safeguarding its independence and impartiality, and combating corruption. Respect for human rights and fundamental freedoms will guide all cooperation on justice, freedom, and security.

The process of democratization in Georgia is still at its beginning. The recent presidential elections marked further progress in Georgia’s democratic credentials. However, it is vital that Georgia remain a pluralistic democracy with effective checks and balances and further strengthens its democratic institutions. Although elections are an important step, they are just a first step and need to be followed by substantial political reform. The ruling elite, among many important aspects of democratic consolidation, need to ensure that political power (that was fully concentrated in the hands of the executive over the last decades) is both *de jure* and *de facto* distributed between executive and legislative branches. For building genuine democracy, it is also crucial that the courts are freed from political pressure, media freedom is guaranteed, and the rule of law prevails.

Another implication of the AA is that closer association with the EU creates stronger international guarantees for the security and territorial integrity of Georgia. The EU is neither an influential nor a unitary international actor in power politics, particularly when confronting Russia. Yet, the EU’s firm support for

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\(^1\) For more, see Tamar Khuntsaria, “Prospect of Deep and Comprehensive Free Trade Area (DCFTA) – Is there a European Way for Georgia?” Center for Social Sciences, Tbilisi State University, September 2012
Georgia’s territorial integrity and non-recognition of Abkhazia and South Ossetia is vital for the country’s diplomatic efforts to resolve these conflicts and in its fragile relationship with Russia. The EU shall continue to remind Russia that it has to comply with the “six-point agreement.” Concerns regarding “borderization” activities along the administrative boundary lines have grown, and reiterated EU support to Georgia is one of the few diplomatic instruments with which the country may confront any aggression from Russia. It is in Georgia’s interest that the EU remain fully engaged in conflict resolution efforts, using the variety of tools at its disposal (including the EU Monitoring Mission, the Geneva discussions, pressing on the possibility of reopening the OSCE mission in Georgia, and political statements and support).

However, there is another side to the coin—an enhanced EU-Georgia dialogue and intensified “Europeanization” of Georgia provides an impetus for Russia’s expansionist appetite, which in turn endangers Georgia’s security and territorial integrity. To this end, it is intriguing that the anticipated signature of the EU-Georgia AA coincides with the NATO summit in London in September 2014. Georgia’s aspiration to NATO membership and expectations to elevate its “aspirant status” at the upcoming NATO summit are likely to increase Georgia’s security concerns vis-à-vis Russia. Therefore, in the process of association, the EU and Georgia should ensure that constructive dialogue with Russia prevails, making it clear that this is not a choice between Moscow and Brussels, and that both the EU and Georgia seek good relations and cooperation with Russia.

Finally, Georgia’s commitment to the EU has significant political implications for the future of the EU’s Eastern Partnership at large. The situation has dramatically changed since Vilnius. The idea of the Eastern Partnership has weakened and its future become blurred as Armenia and Ukraine withdrew from the association process before the summit in favor of the Russian-led Customs Union. The future of the EU’s engagement and political impact in the region is now in doubt. Among the original six EaP partners, only Georgia and Moldova have proclaimed European integration as foreign policy priorities and expressed a readiness to conclude their association deals. To save the EaP and sustain its political levers in the region, it is important for the EU to take hold of Georgia and Moldova and strengthen programmatic and financial support.
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Having learnt a bitter lesson, the EU has put Georgia and Moldova on the AA fast track, aiming to sign agreements “as soon as possible and no later than the end of August 2014.”\(^2\) However, this unconditional acceleration of the timetable gravely limits EU conditionality concerning the required reforms in Georgia and Moldova and may lead the quality and level of their democratic performance to stagnate.

**Trade and Economic Growth**

One of the most important implications of the DCFTA for Georgia is the possibility of diversifying its export market by deepening trade with Europe. Export diversification has become vitally important for Georgia since Russia’s 2006 embargo and 2008 war, which ultimately closed the vast Russian market for Georgians. Even as trade is reopened, it is probable that the market will remain unstable and unpredictable due to the existing political and security context. Therefore, for sustainable development of its exports, Georgia needs to penetrate the EU market, one of the world’s largest, most stable, and strictly regulated. In addition, approximation to European norms in the long term offers the best chance of stable and incremental growth for the Georgian economy.

Currently, the EU is one of Georgia’s main trading partners. Nearly 26% percent of Georgia’s external trade is with the EU.\(^3\) However, total bilateral trade with the EU, Georgian exports in particular, is very low. According to Eurostat\(^4\), EU exports to Georgia increased by 29.5 percent in 2012, while exports of Georgian products to the EU decreased by 4.9 percent. In 2012, EU imports exceeded Georgian exports by more than 3.5 times, while the latest statistics of the second quarter of 2013 shows that the EU imports exceeded Georgian exports by about 2.5 times. See the table below for the import/export trends over the past 5 years.

**Total goods: EU Trade flows and balance, annual data**

<table>
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<tr>
<th>Period</th>
<th>Imports</th>
<th>Exports</th>
<th>Balance</th>
<th>Total trade</th>
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<tbody>
<tr>
<td></td>
<td>Value</td>
<td>Growth*</td>
<td>Share in Extra-EU</td>
<td>Value</td>
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\(^2\) Conclusions of the European Council, EUCO 217/13, 19/20, December 2013
\(^3\) Geostat: www.geostat.ge/cms/site_images/_files/english/bop/FTrade_06_2013_ENG.pdf
Thus, there is need for further diversification of Georgian exports to the EU market, which can be achieved with the help of the DCFTA. Once fully implemented, the DCFTA is expected to have a significant economic impact in Georgia. According to a Trade Sustainability Impact Assessment study commissioned by the EU, the DCFTA can increase Georgia’s exports to the EU by 12 percent and imports by 7.5 percent. In the long term, Georgia’s GDP could increase by 4.3 percent (292 million euros), provided that the DCFTA is implemented and its effects are sustained.\(^5\)

Moreover, the DCFTA provides Georgia with an opportunity to reform and strengthen its trade-related legislation and respective institutions. Georgia has enjoyed its current trading scheme with the EU, the EU Generalized System of Preferences (GSP+), since 2005. This has implied removal only of tariff barriers, however, and does not deal with non-tariff barriers (such as strict food safety standards or sanitary and phytosanitary requirements). Correspondingly, it has not had the desired impact on growth of Georgian exports to the EU.

The economic impact of the DCFTA, however, will not be immediate. Time is needed to develop and stabilize the domestic business climate, ensure proper functioning of related state and non-state institutions, help business adapt to a new economic reality, and comprehend ways to explore emerging export markets. Ample financial resources and patience are needed to implement the reform package. The short-term effects of the DCFTA are associated with more challenges than gains, and the cost of the reforms is to be shared by state, business, and customers alike. Moreover, the government is likely to face social discontent as a result of

\(^5\) Ecorys-Case, “Trade Sustainability Impact Assessment in support of negotiations of a DCFTA between the EU and Georgia and the Republic of Moldova,” Final Report, October 2012
The possible closing down of businesses in some sectors and job losses. Also, competition for foreign direct investment and the costs of modernization may be much higher than available investments, and companies (particularly SMEs) are likely to face transitional problems. In the view of some experts, the regulatory changes imposed by the European Commission in terms of development policy may be burdensome and equivalent to taxing Georgian production, endangering its growth and economic sustainability. Customers will enjoy better quality and more diversified products and services on the market. However, these benefits may be accompanied by higher prices for goods and services, as well as an increased gap between the wages of skilled and unskilled labor, possible job losses, and potentially declining incomes.

**Conclusion**

The process of concluding the AA/DCFTA with the EU will be challenging for Georgia both politically and economically. EU approximation requires the government to undertake extensive reforms that may not be immediately popular among voters. On the security front, deepening political ties with the EU raises the risk of escalated tension and aggression with Russia. Notwithstanding these challenges, EU association is an irreversible strategic development route for Georgia, which has no better alternative. Above all, it promises the country long-term, stable, and sustainable development, an enhancing of its economy, and a strengthening of its democracy.

At the moment, there is time to prepare. To enter into force, the AA has to be signed, then ratified by all 28 EU member states’ parliaments, the European Parliament, and by the Georgian parliament. This is a lengthy and complicated process. During these years, sustaining the government’s political determination and firm commitment to the European perspective, as well as the EU’s strong support, will be crucial.

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