



GEORGIAN FOUNDATION FOR
STRATEGIC AND INTERNATIONAL STUDIES

**THE EXPORT OF GEORGIAN AGRICULTURAL PRODUCTS
THE IMPACT OF THE DCFTA SIGNED BETWEEN GEORGIA
AND THE EUROPEAN UNION**

VICTOR ALEXANDRI

67

EXPERT OPINION





საქართველოს სტრატეგიისა და საერთაშორისო ურთიერთობათა კვლევის ფონდი
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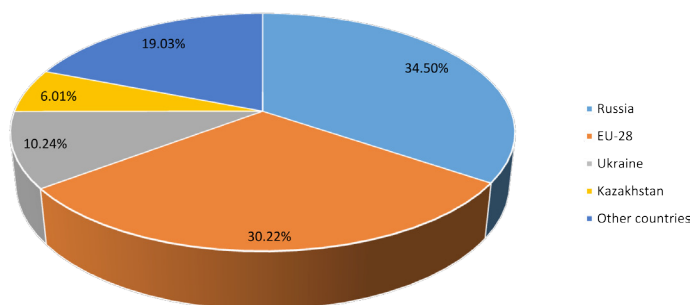
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Introduction

Agricultural exports remain and will be very important for Georgia's trade patterns. In 2014, almost 30% of Georgian exports worldwide were agricultural products with copper ores and motor cars as other important commodities being exported worldwide. Russia, other CIS states and the European Union are the largest importers of Georgian agricultural products (see Figure 1). Georgia has maintained good trade relations with former Soviet countries and has also been able to expand its exports of agricultural products to new partners from Europe such as Germany, Italy and France. Interestingly enough, no more than 4% of Georgia's total agricultural exports from 2014 are destined for Armenia and Azerbaijan (Comtrade, 2016), meaning that this type of trade is rather insignificant between the South Caucasus countries. Russia is still the main importer of Georgian agricultural products, although it is a rather unpredictable trade partner. Georgian agricultural exports are mostly comprised of a limited group of products which generally has a low amount of added value: hazelnuts, wine (made from fresh grapes), alcoholic beverages (especially spirits) and mineral water. Other products which are exported on a smaller scale are fresh and processed fruit and vegetables, live animals and cereals (Comtrade, 2016). Georgia is a net importer of agricultural products with imported goods, mostly brought from the European Union or Russia, having a higher added value.

Figure 1: Main Export Destinations for Georgian Agricultural Products (2014)



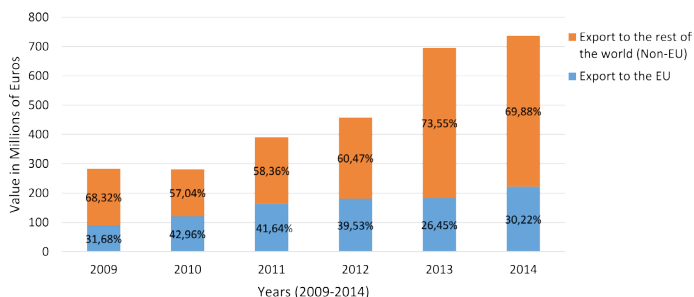
* Source: comtrade.un.org 2016

Similarly to many countries with a relatively small average income, Georgia's largest employment sector is agriculture. More than half of the employed population has a source of income in this primary sector which only contributed about 9.2% of value added to Georgia's GDP in 2014 (World Bank, 2016b). Most of the agricultural land is used by individual farmers with the average size of a farm at about 1 ha while the number of larger farms is relatively low (EJADE, 2006: p. 279) which means that subsistence farming is prevalent in Georgia. Big farms, which are larger than 500 ha, comprise only 5% of Georgia's agricultural land and are usually vineyards or associations of farms (Bluashvili/Sukhanskaya, 2015: p.14). The absence of a significant number of large or medium-sized farms makes it hard to produce standardized products with a higher added value which could be more easily exported abroad. Georgian agricultural production is quite varied, ranging from animal products to vegetables, fruit and cereals which could bring more value added if their production were improved. That is why only a handful of important agricultural products are successfully exported from Georgia. Agricultural exports are not diversified and specific products are targeted towards specific countries. For example, most exported beverages, including spirits and wine, are sold mostly on some CIS markets and most hazelnuts are exported to a small number of European countries.

Georgia's Agricultural Exports to the EU

The EU is the largest single market in the world with a high-income population which is relatively close in proximity to Georgia. Although the EU is an attractive trade partner, it is still not the largest importer of Georgian agricultural products. More than 50% of Georgian goods were sold on the CIS markets in 2014 (see Figure 1). By signing the DCFTA in 2014, Georgia may have given the sign that it wants to change its trade patterns. The potential for growth of agricultural exports to the EU is large but Georgia must create a long-term trade policy environment in order to tap the full potential. From 2009 to 2014, the export of Georgian food products to the European market has grown steadily and reached a value of EUR 184,58 million in 2014 (Comtrade, 2016).

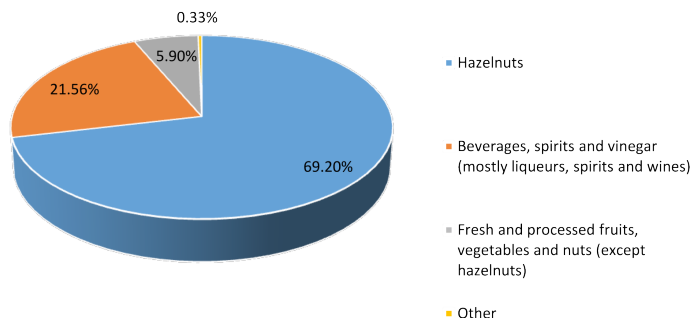
Figure 2: Georgia's Agricultural Exports to the EU in Comparison with the Rest of the World



* Source: comtrade.un.org 2016

This could mean that some Georgian exporters were trying to enter the EU market in the period before 2014 while others wanted to keep their traditional trade partners from the ex-Soviet space. As already mentioned, the structure of agricultural exports depends enormously on the destination markets. For example, Georgian wine and spirits producers were more interested in keeping good trade relations with partners from Russia, Ukraine and Kazakhstan than promoting their goods on the European markets. This is why almost all of these types of beverages are being exported exclusively to only a small number of countries. The same has happened with the export of Georgian hazelnuts which has grown steadily in the last years. In 2014, almost all exported hazelnuts were sold on the European market and made up more than two-thirds of Georgian agricultural exports to the European Union (see Figure 3).

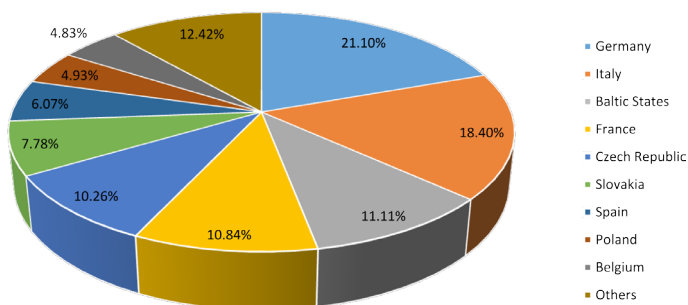
Figure 3: Structure of Georgian Agricultural Exports to the EU in 2014



* Source: comtrade.un.org 2016

The production of nuts is also being promoted by the Georgian government which has introduced a VAT free taxation system for all types of nuts (ENPARD, 2015). The government has also been helping hazelnut producers by giving them loans to develop their businesses and make investments. This has made Georgian hazelnuts more competitive on the European market where there is a growing demand for most types of nuts. Georgian entrepreneurs also have done a good job by working with individual medium or small-sized farms to harvest hazelnuts more efficiently. These collective farms need to invest in their productivity as they have a relatively low yield ratio per hectare with demand volumes on the part of European buyers on the rise. The average price for hazelnuts has more than doubled in the past years with Turkey, as Georgia’s main competitor, having decreased productivity in the past years due to unfavorable weather conditions. Dried and shelled hazelnuts are a non-perishable good, unlike fresh fruits and vegetables, which may also lower transportation costs for their export to the European Union. This is why the value of Georgian hazelnut exports to the EU increased by three times in the period from 2009 until 2014 and have beneficial prospects for Georgian entrepreneurs (Comtrade, 2016).

Georgia’s Main EU-export Partners for Agricultural Products



* Source: comtrade.un.org 2016

The most important importers of Georgian hazelnuts are Germany and Italy which are also Georgia’s biggest export partners inside the EU (see Figure 4). Both countries imported amounts of hazelnuts that exceeded EUR 60 million. Germany is also the main European importer of Georgian fresh or processed fruits and vegetables (especially dried fruit). Nevertheless, the value of the fruit and vegetables sold on the German market in 2014 was quite small and did not exceed EUR 6.5 million. The Czech Republic, Slovakia and Spain mainly import hazelnuts while France imports more

beverages, spirits and wines. Interestingly enough, Poland and the Baltic States almost exclusively import spirits and wines from Georgia (Comtrade, 2016). Lithuania was the second largest importer of Georgian beverages (including alcoholic) after France in 2014. Each country imported beverages valuing more than EUR 10 million. Another interesting fact has been that Georgian wine exports to the EU have been rather insignificant (Comtrade, 2016). Approximately 6% of the total of Georgian agricultural exports to the EU is comprised of wine products. This may come as a surprise because Georgian wines are renowned in Europe, especially among wine connoisseurs, and have a relatively high quality. Nevertheless, they are popular in countries with almost no wine culture such as Poland, Slovakia, the Czech Republic and the Baltic States but also in France where Georgian wines have penetrated the market. Until now, it was noticeable that Georgian producers were focusing more on wine quality and diversity rather than on its pricing. With a more competitive price and sustained promotion, Georgian wines could easily have a greater foothold on the European markets. This could somewhat ease the dependency of Georgian winemakers on Russian consumers. The export of Georgian live animals, meat and dairy products to the EU market is almost non-existent. This may be because of two main reasons: a low productivity and standardization of these goods and the non-compliance with EU sanitary norms which are very strict when it comes to meat products, for example.

The diversification of Georgian agricultural exports to the EU must be a priority for Georgian producers and the government. Established products like wine must enter the EU in greater amounts and there are signs that new types of products, such as kiwis and herbs, are currently trying to penetrate the EU market (ENPARD, 2015). Georgia has an agricultural trade deficit with the EU which mainly exports processed goods to Georgia. In contrast to Georgian agricultural exports, European agricultural products sold in Georgia have a higher added value and thus bring more benefits for European producers. Georgia not only imports processed foods but also primary agricultural commodities.

As for transportation costs and efficiency, Georgian products cannot generally be exported that easily. There are four separate documents needed when exporting all types of products, including agricultural ones, and a mean export time of about nine days (World Bank, 2016a). The overall logistics performance index is at 2.6 (1 = lowest, 5 = highest) with the greatest logistical setbacks for Georgian exports found within a lower quality transport related infrastructure and a rather inefficient customs

clearance process. International trade from Georgia to Europe is only possible by road and sea but will also be possible by train after the Kars-Baku line is finished. Perishable agricultural goods are most likely transported by truck as it may be faster and cheaper. The World Bank Traders without Borders puts Georgia in the 78th position in its index related to the logistical process of trade (see Table 1). Georgia ranks lower than Moldova, which also started to implement the DCFTA two years ago, and Turkey, its biggest competitor when it comes to the export of agricultural products in the region, but higher than other countries like Azerbaijan or Morocco.

Table 1: Time and Costs to Export Goods from Georgia (2014)

Country	Trading Across Borders Rank	Time to Export (Border Compliance) Hours	Time to Export (Documentary Compliance) Hours	Cost to Export (Border Compliance) Euros	Cost to Export (Documentary Compliance) Euros
Georgia	78	14	48	340	178
Armenia	29	3	2	0	133
Azerbaijan	94	34	35	333	267
Turkey	62	8	2	316	77
Moldova	33	3	48	68	39
Ukraine	109	26	96	67	259
Serbia	23	4	2	42	59
Morocco	102	76	26	219	95
Europe and Central Asia		27,6	30,7	195	128

*Source: World Bank (2016) doingbusiness.org/data/exploretopics/trading-across-borders

The costs for obtaining, preparing and processing documents before and during border handling is relatively high in Georgia and account for

more than EUR 500 per shipment. Georgia surpasses most countries in its vicinity when it comes to these bureaucratic costs. Additionally, the mean time for preparing and submitting the documents needed to export goods is also relatively high at about two days. The cost of transportation for a shipment within Georgia is on average about EUR 1.1 per kilometer (World Bank: 2016a). There are also more than 1,500 kilometers dividing Georgia from the European Union if the shipment of goods is made by road. All in all, it could be said that Georgia could improve its transportation logistics in the next years by steadily improving its infrastructure and simplifying its bureaucratic export procedures.

Nevertheless, one of the most important issues for Georgian agricultural exports to the EU is the compliance with European sanitary and phytosanitary norms (SPS) (Von Cramon-Taubadel, 2014: p. 10) and other food security regulations imposed by the majority of European supermarket chains. This is why Georgia was unable to export meat and dairy products to the EU and has been only successful in selling nuts, fruits and alcoholic beverages where standards are not that restrictive. It will be difficult to change or diversify Georgia's structure of agricultural exports to the EU on a short-term basis. In the long run, this is possible but it depends on Georgia's effectiveness in applying reforms in its agricultural exports and implementing the DCFTA. For example, exporting Georgian meat products and live animals will be not possible until new technologies and stricter food security norms are introduced. The EU's tracking system for animals to be imported into the market from third countries (TRACES) will have to be strictly implemented in Georgia. Additionally, the electronic exchange of the specific documentation for these animals will have to happen. Therefore, in the case of the export of meat products, Georgia will have to build large, organized and technologically improved farms which would be compatible with the EU's sanitary and phytosanitary norms. All of these financially arduous investments could be painful on a short-term basis but results will be received in a long-term perspective.

Benefits of the Implementation of the DCFTA

The implementation of the DCFTA has somewhat changed the tariff barriers for Georgian agricultural goods entering the EU. Under the DCFTA signed between Georgia and the EU in 2014, existing import duties on Georgian food products (except garlic)* entering the European market

* So called annual tariff rate quota on Garlic is 220 t. Up to this volume this product is also excepted from the customs duties.

have been abolished from September 2014. Indeed Georgian products already enjoyed a preferential entry into the EU markets under the GSP+ (Generalized System of Preferences). According to this trade arrangement, Georgia received trade concessions from the EU which meant that approximately 91% of tariff lines for Georgian products were 0% duty (European Commission, 2012, p. 8). This means that 9% of the tariff lines, mostly concerning agricultural products, were still subject to duty. Until the end of this (2016) year, Georgian producers can choose if they want to export their products under the DCFTA or the GSP+ trade arrangement. Important Georgian food products like hazelnuts, walnuts and most fresh or refrigerated fruits and vegetables which have already penetrated the EU market, were not subjected to any tariff barriers under the GSP+ (Official Journal of the European Union, 2012). However, exporting other goods with a higher added value, such as bottled mineral water, wine or fruit juices, to the EU implied paying duty. Of course, wine producers may benefit greatly from the changes brought by the DCFTA because their wine can now enter the EU duty-free. It is estimated that they will save up to EUR 0.23 per every regular bottle (0.7 liters) which they paid on import duties (European Commission, 2014). All in all, it is improbable that the elimination of tariff barriers on almost all products will have a significant direct impact on the growth of Georgian agricultural exports to the EU. Other factors, such as the compliance of products with EU sanitary and phytosanitary norms, the promotion of Georgian brands or goods on the European market or the willingness of producers to invest time and money to stimulate their exports towards European countries may be much more important.

An important advantage for Georgia's agricultural export to the EU after signing the DCFTA is that many food products can receive permanent export certificates issued in Georgia. For example, the export procedures for hazelnuts, which is the main agricultural good exported to Europe, have become easier (ENPARD, 2015). Until recently, hazelnut farmers were only issued temporary licenses in the EU. In the case of other products, like honey, whose export to the EU was not possible until the signing of the DCFTA, things have changed. Until 2014, there was no local certified laboratory which issued standard certificates for honey products which meant that Georgian beekeepers were unable to export to the European market (Khurtsia, 2015). The Georgian-origin export certificate, which is issued in Tbilisi by the laboratory of the Ministry of Agriculture, is also valid in the EU. Other producers exporting fruits and vegetables to the EU have

received global G.A.P. standard certificates in order to be able to export to the EU. This is the case for kiwi farmers from Western Georgia who mainly export their fruit to Germany or the Herbia lettuce producers who sell their products to Bulgaria (ENPARD, 2015). But the G.A.P. standard certificate is not easily awarded to producers as all production, packing, storing and distribution processes are being monitored. Even harvest details, such as soil management, are being analyzed. Although the implementation of the DCFTA may not have many direct incentives for Georgian producers to export to Europe, it has helped them indirectly to do so. Georgia's agricultural exports seem to be diversifying little by little and a part of Georgia's agricultural production is becoming more efficient. Since 90% of Georgian farmers own on average about 1 hectare, they have very big production costs and mostly have a small yield. If Georgian producers want to export more to the EU and benefit from the implementation of the DCFTA, they should be creating farming cooperatives and common export brands and applying for common standard certificates for their products. This policy of creating free associations between farmers is also being sustained by ENPARD, the EU's program for supporting agriculture and rural development, but it will likely be unsuccessful in the long run because of farmer mentalities which view collective farms with fear as they associate them with Soviet-style *kolhoz* farms.

It is estimated that the implementation of the DCFTA will further boost the export of some types of agricultural products from Georgia to the EU. For example, the export of fruits, vegetables and nuts could expand in the long run by approximately 20% (Ecorys and CASE, 2012: p. A96) and the export of animal products by approximately 8% (Ibid: p. A41). Georgian agricultural exports to the EU have risen significantly from 2014 (ENPARD, 2015) and the growth has been larger than that of the imports from the EU. Additionally, exports to CIS countries have risen by almost 50% from 2014 to 2015 which proves that the implementation of the DCFTA will not diminish agricultural exports to the ex-Soviet space. It can be said that some impacts of the implementation of the DCFTA can be seen but the greater results will probably be obtained in the long-term future. The growth and diversification of Georgia's agricultural exports must also be interconnected with the reform and modernization of its agriculture and food industries.

Recommendations

- The diversification of Georgia's agricultural exports as there is potential for expanding the types of products to be sold on a larger scale to the EU such as wine, for example. Additionally, if the price of the main commodities exported drops, the total value of Georgian agricultural exports will also collapse.
- The diversification of Georgia's export partners. Georgian producers of certain products are currently dependent on particular markets where they sell their products. For example, most winemakers sell their products to Russia while most hazelnut producers export to a limited number of EU countries. This makes the exporting producers vulnerable as some countries might change their trade policies or some markets could have a change in their demand for a specific product.
- Promotion of products. Georgian producers must be more competitive on the European market and promote their products more courageously. High added value products like mineral water, wine or spirits, which have already entered the markets of some EU countries, need more promotion so that their export can be expanded.
- Reforming the structure of Georgia's agricultural industry. Creating larger farms or free associations between farmers should be a long-term priority for the Ministry of Agriculture. These changes are hard to make and may be slow but they would lead to a more efficient agricultural production and, consequently, a growth in agricultural exports.
- Delivering information to farmers or producers about the benefits of the DCFTA and on how their products can reach the EU market. They may not be well informed about export procedures or EU sanitary or phytosanitary regulations.

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