



*Understanding the EU's Association Agreements  
and Deep and Comprehensive Free Trade Areas  
with Ukraine, Moldova and Georgia*

# Georgia-China FTA: A side effect of the EU-Georgia DCFTA?

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## **Abstract**

The present article analyses the content of the recently concluded free trade agreement between Georgia and China and places it in a broader framework of economic relations between the two countries. Since recently China is among Georgia's top three trade partners and Chinese investment to Georgia has grown as well. The paper argues that the Georgia-China FTA is a positive consequence of the DCFTA as Chinese interest in Georgia as a trade and investment hub increased after the conclusion of the DCFTA with the EU. The FTA between Georgia and China offers extensive tariff liberalisation as well liberalisation of trade in services that to some extent goes beyond the WTO obligations of the two countries. Otherwise, it widely references the WTO rules and obligations and unlike the DCFTA does not contain any legislative approximation obligations. The anticipated benefits for Georgia could be increased Chinese investment with the purpose of exporting 'made in Georgia' products, among others textile, to the EU under the DCFTA, whereas Chinese interest in the FTA with Georgia should be viewed in the context of opportunities offered to China through Georgia's free trade regime with duty-free access to the EU market.

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**Contents**

- 1. Introduction ..... 1
- 2. Georgian-Chinese economic and trade relations: recent intensification ..... 1
  - Trade ..... 3
  - Investment..... 5
  - Tourism ..... 6
  - Transport and Air Connections..... 7
- 3. China and Georgia: trade policy analysis and recent trends in trade structure..... 8
- 4. Negotiated deal: key facts and features..... 8
  - Tariffs ..... 9
  - Rules of origin..... 10
  - Non-tariff barriers ..... 11
- 5. Prospective benefits of the Georgia-China FTA ..... 12
- 6. Conclusions ..... 13
- References ..... 14

**List of Charts and Tables**

- Chart 1. Trade between Georgia and China in 2000-2016, in million USD ..... 3
- Chart 2. Trend of Chinese FDI to Georgia in 2000 – 2016, in \$ millions..... 6
- Chart 3. Chinese visitors to Georgia in 2005-2016 ..... 7
  
- Table 1. Comparison of Georgia and China..... 2
- Table 2. Georgia’s main exports to China (thousand USD) ..... 4
- Table 3. Georgia’s main imports from China (thousand USD) ..... 5
- Table 4. Chinese FDI and its share in total in 2010-2016..... 6
- Table 5. Outcome of tariff negotiations in the Georgia-China FTA ..... 10

# Georgia-China FTA: A Side Effect of the EU-Georgia DCFTA?

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## 1. Introduction

The recently negotiated Georgia-China FTA, signed in May 2017, is one of the positive consequences of the Deep and Comprehensive Free Trade Area (DCFTA) between the EU and Georgia that entered into force in September 2014. In line with its liberal trade policy approach, Georgia had been proposing the conclusion of an FTA to China for several years, but Chinese interest in free trade with Georgia emerged only after the DCFTA became a reality.

Quite obviously, access to the wider EU market is what interests China in this case, which means that the DCFTA between the EU and Georgia in combination with the Georgia-China FTA can potentially result in increased investment and trade opportunities for all the three players. For Georgia it could mean more Chinese investment in processing of goods that can be exported further to the EU using the benefits of the DCFTA. For China it means increased access to the EU market via Georgia with fully liberalized customs tariffs, provided that the goods can qualify for the EU rules of origin under the DCFTA. For the EU, it could mean increased and diversified imports from Georgia, but more importantly new business and investment opportunities for European companies that might be interested in joint business projects with China, whereby they produce in Georgia (with Chinese investment) and import to the EU.

It is in this context that the Georgia-China FTA has to be viewed and analysed. Together with the recently concluded FTA between Georgia and EFTA and the FTA between Georgia and Hong-Kong (negotiated but yet to be signed), Georgia-China free trade agreement is certainly one of the most positive medium-term consequences of the DCFTA, ultimately leading to a greater trade liberalization and positive free trade effects. Although the impact of the DCFTA on the EU-Georgia trade has been very modest in 2014-2016 in terms of trade volume as well as product diversification, since its entry into force, its wider trade liberalizing impact has been more impressive, with three more FTAs mentioned above being made possible primarily due to the existence of the DCFTA. Interestingly, Georgia and India started exploring the opportunities for a free trade agreement, currently being at the stage of feasibility assessment.

The present paper provides the analysis of the main elements of the Georgia-China FTA, tries to identify its potential benefits and places this analysis in the wider context of Georgian-Chinese relations which have been intensified in recent years.

## 2. Georgian-Chinese economic and trade relations: recent intensification

Georgia and China are two economies of extremely different nature and development model as well as, of course, size. Georgia has emerged as an open and liberalised market, which is small but tries to play a role of a regional hub with its attractive business environment, easy rules of doing business, and free trade regimes with economies whose population (including

China now) amounts to about 2,2 billion people. Georgia aspires to be a destination for FDI in any field whereby processed products could be exported further to its free trade partners using preferential tariff regimes, thus widening the potential market for investors interested in producing in Georgia and selling abroad.

As for China, it is the largest market of the world in terms of its GDP (PPP-adjusted) and a fast growing economy. China has not yet been acknowledged as a market economy by WTO members as its economic development model is a mixed one, with slow and gradual market reforms. According to the World Bank, it is the largest exporting country worldwide.

The Table 1 below summarizes the main characteristics of the Georgian and Chinese economies and trade, stressing the difference in size and scale.

*Table 1. Comparison of Georgia and China*

|  | Georgia   | China   |
|--|---|---|
| Population (2015)  | 3,717,100 (132 <sup>th</sup> worldwide)   | 1,371,220,278 (1 <sup>st</sup> worldwide)   |
| Territory  | 69,490 sq km  | 9,388,211 sq km   |
| GDP (2015)   | 35,682 billion USD (PPP)  | 19,815 trillion USD (PPP)   |
| GDP per capita (2015)  | 9,599.482 USD (PPP)   | 14,450.712 USD (PPP)  |
| Trade volume (2016)  | 9.7 billion USD   | 3,448 billion USD   |
| Exports (2016)   | 2.9 billion USD   | 2,011 billion USD   |
| 5 main trade partners (2016) in order of importance  | <ol style="list-style-type: none"> <li>1. EU</li> <li>2. Russia</li> <li>3. China</li> <li>4. Turkey</li> <li>5. Armenia</li> </ol> | <ol style="list-style-type: none"> <li>1. EU</li> <li>2. United States</li> <li>3. Hong Kong</li> <li>4. Japan</li> <li>5. South Korea</li> </ol>   |
| FTAs   | EU, EFTA (not in force yet), CIS, Turkey, China (signed, to be ratified), Hong-Kong (negotiated, to be signed)                      | Australia, South Korea, Switzerland, Iceland, Costa Rica, Peru, Singapore, New Zealand, Chile, Pakistan, ASEAN countries, Hong Kong, Macao, Georgia (signed, to be ratified)<br>Ongoing: Norway, Israel, Maldives, Sri Lanka, Gulf Cooperation Council (GCC), China-Japan-Korea FTA |
| Simple average tariffs (2015)  | 7,3% (bound); 1,5% (applied)  | 10% (bound); 9,9% (applied)   |
| <ul style="list-style-type: none"> <li>• Average Agri tariffs</li> <li>• Average industrial tariffs</li> </ul> | <ul style="list-style-type: none"> <li>• 12,5% (bound); 6,3% (applied)</li> <li>• 6,5% (bound); 0,7% (applied)</li> </ul>           | <ul style="list-style-type: none"> <li>• 15,7% (bound); 15,6 (applied)</li> <li>• 9,2% (bound); 9% (applied)</li> </ul>   |
| WTO membership   | Since 2000  | Since 2001  |

Sources: WBG; WTO; World Tariff Profiles 2016, published by WTO, ITC, UNCTAD; Georgian National Statistical Office.

As the table above demonstrates Chinese GDP is 555 times bigger than that of Georgia and its trade volume is 355 times larger than that of Georgia.

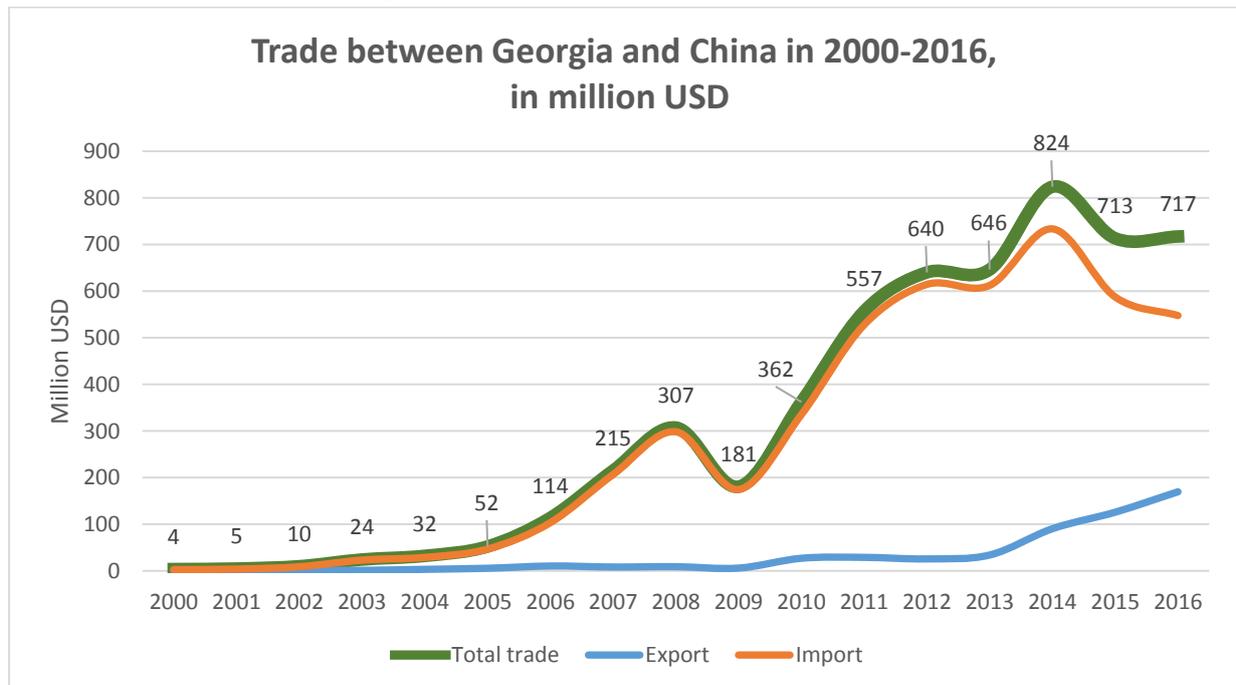
In recent years, Georgian-Chinese economic relations have been intensified. This trend is most vividly visible in the recently increased trade volume between between the two countries. In what follows, a brief overview of Georgian-Chinese economic relations and an economic context in which the recent FTA was negotiated is provided.

### Trade

Trade between Georgia and China increased substantially in the past years. In the last 10 years, namely in 2007-2016, trade increased by 534%, with Georgian exports to China increasing from a low base by 1,967%, and imports by 164%. Annual average growth rate of trade in this period was 35%. In 2016 China emerged as a major trading partner for Georgia with a 6% share in its total trade. China is 3<sup>rd</sup> largest export destination for Georgian products, with its exports growing by 35% in 2016. Among the main export products are copper ores, manganese ores, wine, copper scrap and cars. As for import, it is dominated by flat-rolled products of iron or non-alloy steel, automatic data-processing machines, new pneumatic tyres of rubber, air conditioners, rubber footwear.

The Chart 1 below summarises trade dynamics since 2000, whereas the Table 2 and Table 3 list main import and export products in trade between China and Georgia in the last 3 years (2014-2016), with their volume as well as share in total bilateral export and import respectively.

Chart 1. Trade between Georgia and China in 2000-2016, in million USD



Source: GeoStat, National Statistics Office of Georgia

The following two tables include data on export and import between Georgia and China in 2014-2016. Main products are captured in each case based on the statistical data of 2016 and export and import dynamics for these main products is demonstrated for the past three years. As is visible from the trade dynamics of the past three years, strong growth of export has been recorded in the case of products such as wine (199%), copper ores and concentrated and manganese concentrates. Moreover, Georgia started to export products such as beer and mineral waters to China. Notably, cars are exported to China through Georgia as well, export of this item increasing steadily, which is a demonstration of Georgia's function as a distribution hub in the wider region.

Table 2. Georgia's main exports to China (thousand USD)

| Georgia's main export to China |                              |          |            |                  |           |                  |
|--------------------------------|------------------------------|----------|------------|------------------|-----------|------------------|
| HS code                        | Product                      | 2014     | 2015       | 2014-2015 growth | 2016      | 2015-2016 growth |
| 2603                           | Copper ores and concentrates | 67,391.4 | 101,220.90 | 50%              | 131,692.4 | 30%              |
| 2602                           | Manganese concentrates       | 0.1      | -          | -                | 15,986.2  | -                |
| 2204                           | Wine                         | 4,664.9  | 8,652.2    | 85%              | 13,953.9  | 61%              |
| 7404                           | Copper waste                 | 17,371.3 | 14,928.7   | -14%             | 4,108.1   | -72%             |
| 2208                           | Spirits                      | 219.3    | 99.3       | -55%             | 875.8     | 782%             |
| 2205                           | Vermouths                    | -        | -          | -                | 186.2     | -                |
| 2201                           | Mineral waters               | 16.1     | 55.7       | 246%             | 132.3     | 138%             |
| 2203                           | Beer                         | -        | 6.1        | -                | 103.6     | 1598%            |
| 8703                           | Automobiles                  | 36.4     | 93.5       | 157%             | 2,191.8   | 2244%            |
|                                | Sum                          | 89,699.5 | 125,056.4  | 39%              | 169,230.3 | 35%              |
|                                | Others                       | 693.8    | 743.8      | 7%               | 356.6     | -52%             |
|                                | Total export                 | 90,393.3 | 125,800.2  | 39%              | 169,586.9 | 35%              |

Source: GeoStat, National Statistics Office of Georgia

Table 3. Georgia's main imports from China (thousand USD)

| Georgia's main import from China |   |           |           |                  |           |                  |
|----------------------------------|---|-----------|-----------|------------------|-----------|------------------|
| HS code                          | Product   | 2014      | 2015      | 2014-2015 growth | 2016      | 2015-2016 growth |
| 7210                             | Flat-rolled products of iron                          | 21,530.8  | 19,874.0  | -8%              | 22,884.9  | 15%              |
| 8471                             | Calculators   | 43,026.6  | 24,384.1  | -43%             | 18,377.3  | -25%             |
| 4011                             | New tires   | 14,834.8  | 11,384.4  | -23%             | 15,205.8  | 34%              |
| 8415                             | Air-conditioning machines                             | 12,650.7  | 12,489.7  | -1%              | 14,823.3  | 19%              |
| 6402                             | Rubber shoes  | 5,305.1   | 3,595.6   | -32%             | 13,175.5  | 266%             |
| 8517                             | Electrical apparatus for line telephony               | 25,911.8  | 13,350.5  | -48%             | 12,002.5  | -10%             |
| 9405                             | Light bulbs   | 11,360.5  | 11,852.0  | 4%               | 10,209.9  | -14%             |
| 9403                             | Furniture   | 18,325.7  | 12,532.1  | -32%             | 9,161.1   | -27%             |
| 8528                             | Equipment for receiving TV connection                 | 14,901.9  | 19,215.3  | 29%              | 9,037.0   | -53%             |
| 6404                             | Shoes with rubber, leather and basic textile material | 6,820.0   | 6,337.2   | -7%              | 8,751.8   | 38%              |
|                                  | Sum   | 174,667.9 | 135,014.9 | -23%             | 133,629.1 | -1%              |
|                                  | Others  | 558,799.6 | 452,363.9 | -19%             | 413,874.1 | -9%              |
|                                  | Total import  | 733,467.5 | 587,378.8 | -20%             | 547,503.2 | -7%              |

Source: GeoStat, National Statistics Office of Georgia

To summarize, China's role in Georgia's trade structure was increased and diversified in the past years, whereby China emerged among Georgia's top trade partners.

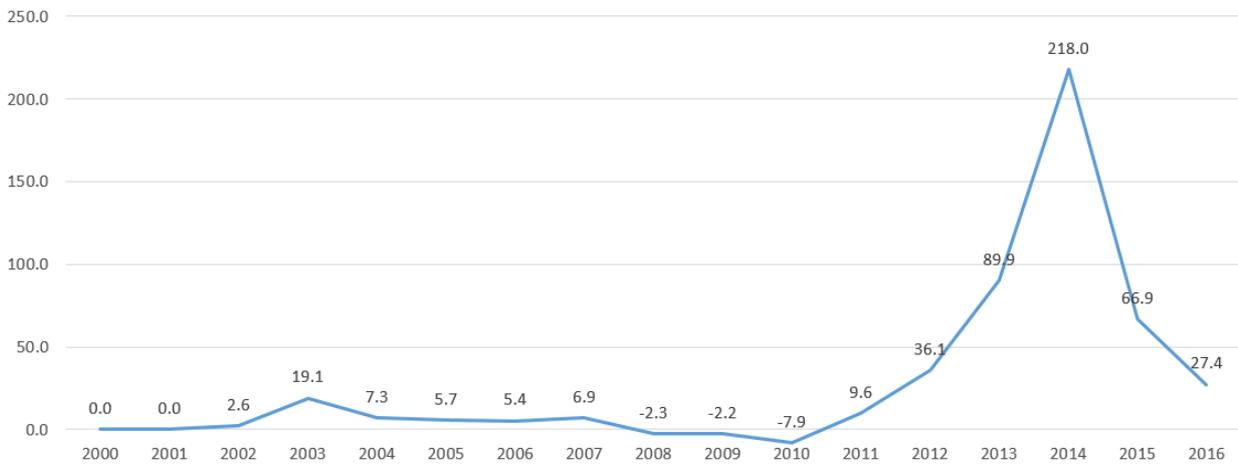
## Investment

Chinese investment was minimal until 2010. There was then a spectacular growth, reaching a peak in 2014, with over \$217 mln and a share of 12,4% in total FDI (Chart 2). This growth consisted mainly of Chinese investment in construction and real estate in 2014. Notably, in the past 7 years, the annual average growth rate of inward FDI from China was 66% and the share of Chinese FDI in the total foreign direct investment to Georgia was 5% on average.

Chinese companies have invested in real estate, infrastructure, banking and energy sector. The Chart 2 below gives information about Chinese FDI to Georgia since 2000 and the Table 3 provides data on the volume of total Chinese FDI to Georgia as well as its share and growth rate in the period between 2010-16.

Importantly, China and Georgia have bilateral agreements on investment protection as well as on avoidance of double taxation, in force respectively from 1995 and 2005.

Chart 2. Trend of Chinese FDI to Georgia in 2000 – 2016, in \$ millions



Source: GeoStat, National Statistics Office of Georgia

Table 4. Chinese FDI and its share in total in 2010-2016

| Year | Chinese FDI to Georgia, ml USD | Share in total FDI |
|------|--------------------------------|--------------------|
| 2010 | -7.9                           | -                  |
| 2011 | 9.6                            | 1%                 |
| 2012 | 36.1                           | 4%                 |
| 2013 | 89.9                           | 10%                |
| 2014 | 218.0                          | 12%                |
| 2015 | 66.9                           | 4%                 |
| 2016 | 27.4                           | 2%                 |

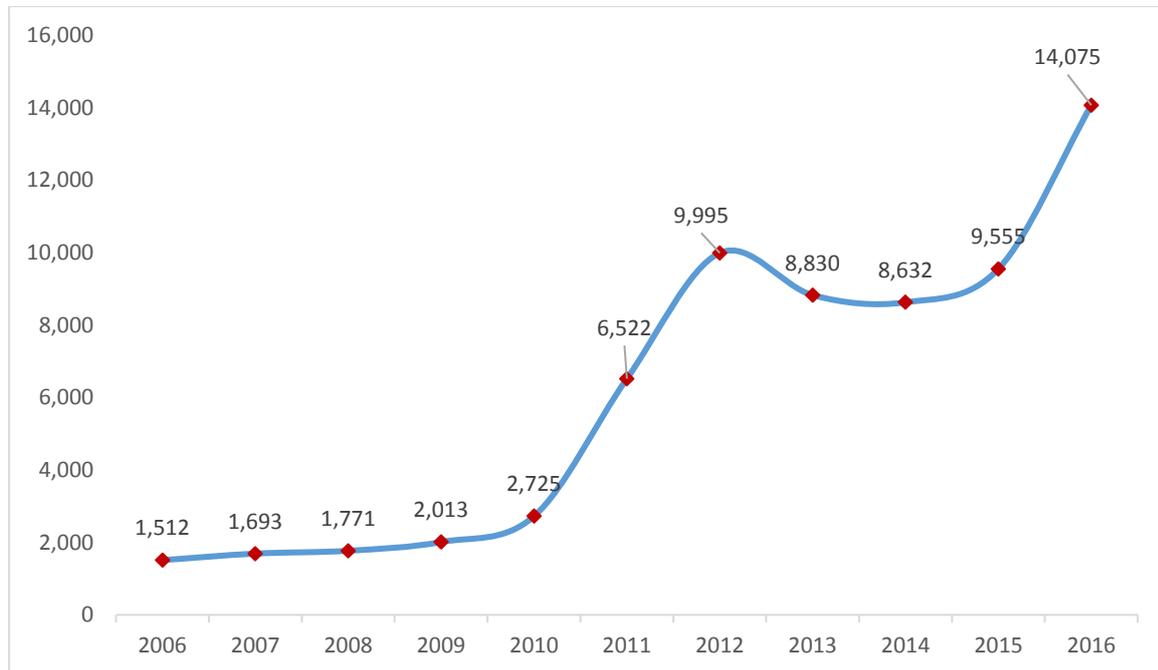
Source: GeoStat, National Statistics Office of Georgia

## Tourism

Since 2012 Georgia enjoys an Approved Destination Status (ADS) from China, which means that the Chinese state regards Georgia as an officially recognized destination to travel for its citizens. Such a status is an important step forward – a necessary but not a sufficient condition for the increase of Chinese tourism into Georgia. Notably, although Georgia grants visa-free regime to around 100 country worldwide only those Chinese citizen holding diplomatic and official passports may travel visa free to Georgia.

The number of Chinese visitors to Georgia has increased in the past years. Between 2006-16 annual average growth of Chinese visitors was 35% whereby the number increased from 747 visitors in 2005 to 13, 973 in 2016. Overall, the figure is not high and in the past 5 years the Chinese had an average annual share of just 0,2 % in the total (rapidly growing) number of tourists to Georgia. However, a growing tendency is clearly visible, as demonstrated in the Chart 3 below.

Chart 3. Chinese visitors to Georgia in 2005-2016



Source: Georgian National Tourism Administration.

Given that Chinese outbound tourism worldwide has experienced a sharp rise in recent years and currently the Chinese are the most active travelers worldwide, with a projected rising trend, China is an important prospective source of tourism to Georgia. According to the World Tourism Organization (WTO), China has emerged as the fastest growing source market and the top spender in international tourism since 2012, facilitated among others by rising disposable incomes and improved travel connections and less restrictions on foreign travel. Chinese tourists worldwide are projected to grow to reach over 230 million by 2020.

### Transport and Air Connections

Georgia and China have direct air connections, namely Tbilisi – Urumchi, since 2011. Since September 2016 flight connections from Tbilisi to Beijing and back are also operating via Urumchi. This provides increased opportunities for visitors from both countries, in particular in the context of increased trade flows and recently negotiated FTA as well as in the framework of intensified tourist flows and future perspectives in this area.

Notably, Georgia and China signed a memorandum on the Silk Road economic belt development cooperation in 2015. The memorandum is supposed to be followed by a three-year action plan for cooperation between the two countries aimed at joint actions in 2016-2018, but this process still needs to be finalized. Importantly, at the initiative of the President Xi, China has set up a fund of \$40 bln to support the projects in the framework of the New Silk Road – Economic Belt initiative. The fund aims at participation in large infrastructure projects in countries joining in the new silk road initiative.

As a geopolitical and geographical hub that connects Europe and Asia Georgia positions itself as a suitable place (both symbolically and practically) for a dialogue on the revitalization Silk Road. The Government of Georgia initiated the idea of establishing the “Tbilisi Silk Road Forum”, with a high level meeting of all interested states and international organizations, which was held on October 15-16, 2015, in Tbilisi. The meeting explored new initiatives for enhancing partnership in 4 main areas of cooperation, transport, energy, trade and people-to-people contacts.

### **3. China and Georgia: trade policy analysis and recent trends in trade structure**

Being very unequal partners in terms of the size of their economies as well as economic policy, China and Georgia have different trade policies in view of market access and openness to import. As outlined in Table 1 above, China’s bound as well as applied MFN tariffs are higher than those of Georgia, both for agricultural as well as industrial goods.

Whereas in Georgia no import duty applies on 80% of tariff lines, in China only 8.4% of goods can be imported free of import tariffs. Thus, the existence of tariffs on 91.6% of goods requires more elaborate tariff negotiations with China than with Georgia, the latter having abolished import tariffs on most goods. The highest applied tariff in Georgia is 12% whereas in China it is 65%. Both in Georgia and China, tariffs on agricultural products are higher than on non-agricultural products, whereby Georgia’s tariffs are overall substantially lower (see the Table 1 above).

Georgia has conducted autonomous trade liberalization in 2006 and abolishing most tariff lines as mentioned above. In parallel it activated efforts to conclude bilateral free trade agreements with as many countries as possible, currently comprising a market of 2.2 billion population.

As for China, besides its existing FTAs it has ongoing negotiations with a number of countries, as indicated in the Table 1 above. With the existing FTAs in place, China has free trade regime with markets having a population of 977 mln. Notably, Georgia’s FTAs are more liberal compared to those of China, as Georgia has no import tariffs and exemptions with CIS countries (except Russia) and the EU, and only the Georgia-Turkey and Georgia-EFTA FTAs envisage TRQs and exemptions.

In the following chapter the basic features of the Georgia-China FTA are given, including tariffs as well as non-tariff barriers to trade

### **4. Negotiated deal: key facts and features**

The free trade agreement between Georgia and China was signed in May 2017 and still needs to be ratified by both parties to enter into force.

Overall, out of all the FTAs concluded by Georgia, the one with China is most similar to the Georgian-Turkish FTA of 2007 in that it a) does not fully liberalise tariffs (unlike the agreements with the CIS countries and the EU) although it goes beyond the parties’ MFN commitments b)

does not contain any legislative harmonization provisions between the parties to the agreement, and c) takes the WTO agreements and existing obligations as major points of reference in various areas related to non-tariff barriers to trade, and does not go beyond WTO commitments other than in the services sector

However, in terms of the topics and non-tariff barriers (NTB), the Georgia-China FTA is more similar to the DCFTA than the Georgian-Turkish FTA as it covers a broader range of cooperation and NTBs. More specifically, the FTA consists of the following chapters:

| Chapters of Georgia - Chinese FTA |  |     |                                   |
|-----------------------------------|--|-----|-----------------------------------|
| 1.                                | Initial Provisions and Definitions         | 11. | Intellectual Property             |
| 2.                                | Trade in Goods                             | 12. | Areas of Cooperation              |
| 3.                                | Rules of Origin                            | 13. | Investment                        |
| 4.                                | Customs Procedures and Trade Facilitation  | 14. | Electronic Commerce               |
| 5.                                | Sanitary and Phyto-sanitary Measures (SPS) | 15. | Transparency                      |
| 6.                                | Technical Barriers to Trade (TBT)          | 16. | Institutional Provisions          |
| 7.                                | Trade Remedies                             | 17. | Dispute Settlement                |
| 8.                                | Trade in Services                          | 18. | General Provisions and Exceptions |
| 9.                                | Environment and Trade                      | 19. | Final Provisions                  |
| 10.                               | Competition                                |     |                                   |

The schedules annexed to those chapters where trade in goods and services is liberalised further than the Parties' WTO commitments. As outlined below, this concerns both trade in goods as well as the services chapter.

## Tariffs

As far as tariff liberalization is concerned, China made substantial concessions in favor of Georgia, whereas from Georgia's perspective the outcome is certainly not the most liberal, as tariffs are not fully eliminated for Chinese import. However, the Georgia-China FTA still provides substantial tariff cuts. Georgia maintained tariffs on 3.5% of goods, instead of 20% in its standard MFN schedule. As for China, it maintained tariffs only on 6% of goods. Thus, given the MFN tariffs structure, whereas Georgia opened the market for an additional 16.5% of tariff lines and abolished import tariffs on these goods, China opened the market for Georgian goods on 85,6% of goods, given that it has MFN tariffs higher than 0% on most goods.

On the Chinese side, the outcome of tariff negotiations can be divided in three parts: (i) complete liberalization immediately, (ii) liberalization with a transition of period of 4 years and (iii) exemptions from free trade. On the Georgian side the complete nomenclature of goods

includes (i) products subject to immediate and full liberalization and (ii) exemptions. Thus, there is no gradual tariff liberalization with transition periods, whereas for China it is 4 years.

Some other FTAs signed by China have longer transition periods for tariff liberalization as well as more modest tariff concessions in certain cases. For example, in its FTA with Switzerland (in force since 2014) the transition periods for tariff liberalization from the Chinese side are up to 15 years, with New Zealand (in force since 2008) – up to 12 years, and with Chile (in force since 2006) also up to ten years. In the FTA with Pakistan (in force since 2009), although transition period is only up to 5 years, exemptions apply to approximately 15% of goods – higher than in the case of Georgia.

The Table 5 below summarizes the outcome of tariff negotiations per category of goods.

*Table 5. Outcome of tariff negotiations in the Georgia-China FTA*

|                     | Georgia |         | China |         |
|---------------------|---------|---------|-------|---------|
|                     | Total   | % share | Total | % share |
| Total tariff lines  | 10,255  | 100%    | 8,285 | 100%    |
| Full liberalisation | 9,891   | 96,5%   | 7,529 | 91%     |
| Exemption from FTA  | 364     | 3,5%    | 504   | 6%      |
| Transition period   | none    | none    | 252   | 3%      |

As far as product coverage is concerned, from the Chinese side exemptions include products such as beef, coffee, different oils, sugar and sugar products, tobacco and tobacco products, paper products, three tariff categories of textile products, automobiles, parts of TVs, etc.

From the Georgian side exemptions include some beef and poultry meet types, milk and cream, honey, canned fruits and vegetables, fruit juices, mineral water, wine, tobacco raw materials, cigarettes, white cement, granite, etc.

### Rules of origin

The Georgia-China free trade regime will apply the following rules of origin: originating products are considered those either wholly produced in a party or goods where domestic content of the value is no less than 40%, i.e. minimum 40% of the value has to be domestically obtained. The annex to the rules of origin chapter contains a list of products where specific rules of origin other than the general rule of 40% domestic value apply.

Specific rules of origin include the following categories:

- a) wholly obtained products such as cereals, cane or beet sugar, animal or vegetable fats and oils, wines and various spirits and various types of cotton.

- b) goods where non-originating materials used in the production have undergone a change in tariff classification at two-digit level of the Harmonised System (HS) such as fish, fruits and nuts, tea, cocoa, preparations of meat and fish, tobacco.
- c) goods where non-originating materials used in the production have undergone a change in tariff classification at four-digit level of the HS, primarily applied to chocolate and sugar confectionary.
- d) goods where minimum domestic value requirement are higher than the general rule of 40% – namely 60%. Such goods include roasted coffee and alcohol containing ethyl such as spirits, liqueurs and other spirituous beverages. Notably the 60% rule applies in combination with the rule of the tariff change four-digit level mentioned above.

Notably, the above listed specific rules of origin apply mainly to agricultural products. Tobacco and non-agricultural products, other than some types of rubber and cotton, are treated under the rule of 40% domestic content value.

### Non-tariff barriers

As for the non-tariff barriers, the Georgia-China free trade agreement has 14 chapters covering a wide range of areas as listed above. Unlike the DCFTA, in most areas this FTA makes references to the WTO obligations of both sides and does not go beyond it. Whereas in tariff liberalization the FTA goes far beyond the WTO schedules, compliance with the Parties' obligations in the WTO remains the basic objective as far as the non-tariff part is concerned.

However, the services sector sees some exceptions, where both sides went further than WTO commitments in liberalizing trade in services and opening their respective markets.

More specifically, China opened its market for Georgian travel agencies (as joint ventures) to engage in the activities of the Chinese citizens travelling abroad. Georgia is China's only trade partner with such a liberalization in the services sector. In maritime transport as well Georgia receives a favorable treatment. Namely, China will accord the same treatment to the vessels flying under the Georgian flag as it accords to its own vessels with regard to access to ports, the use of infrastructure and auxiliary maritime services of those ports, as well as related fees and charges. Further, China made enhanced commitments with regard to social services (namely, services for the aged), selling and marketing of air transport services, passenger transportation by road transport services and others.

For its part Georgia went further than its WTO commitments in areas such as freight transportation, rental of vessels with crew, maintenance and repair of vessels and pushing and towing services.

Notably, market liberalization in the Georgia-China FTA is restricted to goods and services mentioned above. The agreement does not contain a separate chapter on public procurement or any commitment by the parties to open respective procurement markets to each other's business operators beyond the general WTO obligations.

To summarise, the Georgia-China FTA provides substantial tariff liberalization for Georgia as well as liberalization of trade in services going beyond WTO commitments. Other than that the agreement overall stays within the limit of existing WTO obligations of both parties.

## 5. Prospective benefits of the Georgia-China FTA

As mentioned above, the Georgia-China FTA is one of the most positive side effects of the EU-Georgia DCFTA, having a broader trade liberalizing impact, whose benefits however will be seen over the years after its entry into force. This agreement, together with Georgia's other FTA's (especially with the EU), and its transport and transit infrastructure, business friendly environment and access to regional and international markets, will provide increased opportunities for investment, export diversification and economic growth.

The potential benefits were assessed through a feasibility study conducted jointly by the PMC Research Center in Georgia and the University of International Business and Economics in China in 2015 prior to initiating the talks on the FTA. Broadly speaking, it is anticipated that in the long-term (10 year) period, while the Georgia-China FTA will promote trade and economic relations between the two countries, it will bring proportionately bigger potential benefit for Georgia. The methods used by the Georgian and Chinese experts were partial-equilibrium and general equilibrium models.

Based on the general equilibrium analysis, the elimination of tariffs would promote bilateral trade significantly. After elimination of import tariffs on both sides, Georgia's exports to China would increase by an additional 29.1% (\$24.5 million), and China's exports to Georgia by 6.7% (\$53.0 million). The higher figure for Georgia reflects the fact that the tariff liberalisation by China was more important, since Georgia's tariffs were already largely liberalised. GDP in Georgia would grow modestly, by only an additional 0.05% (\$7.5 million). China's GDP increase would be negligible, by approximately 0.0001% (\$5 million). Notably, a significant increase in Georgia's export of vegetables and fruits (by 125.2%), wine (by 34.6%) and machinery (by 75.5%) is anticipated by the feasibility study.

Based on the partial equilibrium analysis, Georgian exports to China will increase somewhat faster by 9.3%. Substantial increase is expected in exports of wines (+28.5%), mineral waters and other non-alcoholic beverages (+36.7%). Georgian wine exports to China is a promising area, to be further encouraged by the FTA, as Chinese wine consumption has grown over recent years and China emerged among the top grape wine consumers as well as wine importer countries.

According to the above-mentioned calculations, the FTA is expected to further increase and diversify export and have a positive albeit very limited impact on GDP growth. However, such model exercises only partially capture the future possible impact. In particular, the models cannot anticipate the potential synergies to be obtained from the combination of the FTAs with both China and the EU. If the strategy of attracting Chinese FDI for onward exports to the EU market actually works in practice, then the benefits could become much greater.

Taking into account similar examples, such as Georgia-Turkey FTA, Chinese investment to Georgia is expected to grow as a result of the Georgia-China FTA combined with other favorable factors encouraging trade and investment such as liberal business environment as well as Georgia's free trade regimes with the EU, CIS and other. The Georgian-Turkish FTA is a good case in point. Turkish investment to Georgia grew by 157% between 2010 and 2016, three years after the entry into force of the bilateral FTA (notwithstanding the global financial crisis). In particular, the Georgia-Turkey FTA resulted in increased Turkish investment in the textile industry, with ready-made Georgian products being exported back to Turkey. As a consequence, textile product exports from Georgia grew substantially, from \$16.0 million in 2007 (when Georgia-Turkey FTA was signed) to \$81.0 million in 2016. This is mainly through export of products to Turkey, which accounts to 70% of textile export from Georgia.

More specifically, Chinese investors could benefit by producing in Georgia and exporting to Georgia's FTA partners with which China does not have a free trade regime, notably the EU, Turkey, CIS and some EFTA members (except Iceland and Switzerland as China has FTAs with them). Thus Georgia provides a suitable platform for China in its efforts to access new markets, using the Georgian market as a production hub.

A further stimulus can be expected to come from Georgia's accession (on July 2017) to the Pan Euro Mediterranean preferential system for rules of origin, which will allow for 'diagonal cumulation' of origin with other economies of the European region with which Georgia has FTAs. The diagonal cumulation of origin may be an interesting opportunity for Chinese investors.

## 6. Conclusions

The present paper gives an overview and analysis of the recently signed free trade agreement between Georgia and China and places it in a broader context of the bilateral trade and economic relations between the two countries.

Undoubtedly, Georgia-China FTA is a positive consequence of the DCFTA with the EU, which increases Georgia's attractiveness for Chinese traders and investors. The agreement envisages substantial tariff liberalization, in particular from the Chinese side, since Georgian tariffs were already largely liberalised since 2006. Notably, China fully liberalized its tariffs on 91% of goods of Georgian origin and introduced a transition period for liberalization on 3% of tariff lines. On the Georgian side, only a small portion of tariff lines (3.5%) is exempted from free trade. In the non-tariff part, the agreement mainly refers to the two countries' WTO commitments, although in the services sector the parties embarked on further liberalization beyond their WTO obligations.

Georgia-China free trade agreement has to be seen in the context of recently intensified economic relations between Georgia and China, whereby China has become Georgia's 3<sup>rd</sup> largest trade partner. There have also been some major direct investments by China, notably

in 2014. In the past 7 years, the annual average growth rate of inward FDI from China to Georgia was 66%.

Importantly, Georgia-China FTA should bring benefits for the EU as well as for both FTA partners. For Georgia it could mean more Chinese investment in the processing of goods that can be exported further to the EU benefiting from the DCFTA. For China it means increased access to the EU market via Georgia with fully liberalized customs tariffs, provided that the goods can qualify for the EU rules of origin under the DCFTA. For the EU, it could mean increased and diversified imports from Georgia, but more importantly new business and investment opportunities for European companies that might be interested in joint business projects with China, for production in Georgia with Chinese investment and import into the EU.

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Statistical data and information available from the National Statistical Office of Georgia (<http://geostat.ge/index.php?action=0&lang=eng>) and WBG's World Development Indicators (<http://data.worldbank.org/data-catalog/world-development-indicators>).