



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

Youth Essay Competition

Future of DCFTA: Georgia's Prospects for Deeper Integration in European Single Market

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I am Elene Panchulidze from Georgia, an International Relations specialist working on various topics, including but not limited to Georgia's European integration, protracted conflicts, Russian propaganda, etc. Currently I am working for the OSCE/ODIHR election observation mission to Georgia. Besides, I am drafting my PhD thesis and writing research papers for the Georgian Institute of Politics (GIP) in the capacity of their affiliated policy analyst. Being a young researcher, I see myself in few years' time in the multinational environment, either in an international organization, or think tank or NGO, with the possibility to meet the new challenges and further improve my professional skills and competences.



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Executive Summary

The Association Agreement (AA), including its integral component on a Deep and Comprehensive Free Trade Area (DCFTA), between the European Union and Georgia fully entered into force on 1 July 2016. Despite the technical nature of the document, the political rationale of the agreement is still in line with Georgia's longer-term perspective to materialize its European choice and aspirations.

Against the background of enduring approximation with the EU *acquis communautaire*, growing bilateral trade under the DCFTA and success in the process of Visa Liberalization, the options are kept open for future formats for Georgia's more intensive engagement with the European Union. Even though DCFTA hasn't yet been fully operationalized and challenges still exist in the process of its full-fledged implementation, it is essential to analyze what it means for Georgia's European path as a new benchmark and deliverables to be attained. Bringing the European best practices to the reform agenda not only boosts the bilateral trade dynamics but greatly contributes to Georgia's long-lasting objective to build a European state with stable and functioning economy.

While the issue of opening the European Membership Perspective to EaP countries is highly politicized for the time being because of various internal and external factors in the EU, enhancement of ties in trade seems to be one of the viable opportunities in the foreseeable future. Georgia should be pragmatic and use all feasible tools and mechanisms on its way to EU membership. Deeper integration into the European Single [Internal] Market could be an important part of this effort.

Despite the bureaucratic nature of the European Union, the institution's corporate philosophy stands on openness and shows readiness to develop tailor-made ties with partner countries based on the case-by-case approach. Thus, upgraded formats, which can go beyond the existing frameworks of trade/economic cooperation, could serve the interests of both the EU and the partner countries.

The present Policy Brief overviews EU-Georgia economic relations in terms of DCFTA implementation; it also assesses existing achievements and challenges, as well as discusses the prospects of deepening the trade/economic ties and Georgia's further integration within the European Single Market.

EU-Georgia DCFTA

Signing the Association Agreement with the European Union including the DCFTA has been one of the most important achievements of Georgia on its ambitious European integration agenda.

While most of the economic content of the Agreement has been provisionally in force since 1 September 2014, its definitive and complete entry into force took place on 1 July 2016. Even though the Agreement is intensely technical, it bears geopolitical significance for Georgia, as it

affirms country's European identity and its foreign policy priority of deepening closer ties with the European Union.¹

The DCFTA - the economic core of the Association Agreement - differs from standard free trade agreements. It is aimed not only at enhancing trade relations between the EU and Georgia (trade-related aspects analogous to a conventional free trade area format) but also at facilitating convergence to EU standards in various business-related regulations in the areas of food safety, technical standards, public procurement, competition policy, intellectual and property rights, etc.²

Until 31 December 2016 Georgia benefited from the unilateral Generalized Scheme of Preferences (GSP). Under the GSP regulation Georgia qualified for a special incentive rewarding sustainable development and good governance (GSP+) with better access to the EU market. This transition period allowed business to adjust to the new preferential trade regime provided by the DCFTA.³ Compared to GSP+, which was offering limited preferences and had a temporary character, the DCFTA abolishes tariffs for almost all products and enables both EU and Georgia to address regulatory barriers.

Taking into consideration the economic and political context of Georgia, the DCFTA component could be perceived as a framework document paving the way to a steady transition process from the centrally planned to a European type of market economy. The shift to a predictable legal and institutional environment initiated and strengthened by the DCFTA substantively increases the economic attractiveness of Georgia. In addition, the access to the EU's Single Market accounting more than 500 million consumers, works as a very strong external anchorage pulling investors to choose Georgia as an economic partner.⁴

While the EU accounts for a quarter of Georgia's overall trade, according to the European Commission's latest Association Implementation Report⁵ on Georgia, this trade however remains fragile. The paper reads that Georgia has started using the DCFTA's opportunities and is exporting certain non-traditional food products to the EU, but substantial challenges lie ahead in terms of strengthening and expanding Georgia's production base and export capacity. Although Georgia has approximated its laws to many EU standards, the approximation of some EU regulations under the DCFTA has been spread over a number of

¹ Emerson Michael and Kovziridze Tamara; Deepening EU-Georgian Relations, What Why and How? Rowman and Littlefield International 2016 ; Accessed on 14.08.2017 <http://www.dcfta.gov.ge/public/filemanager/publications/pub1-Eng.pdf>

² Adarov Amat and Havlik Peter, "Benefits and Costs of DCFTA: Evaluation of the Impact on Georgia, Moldova and Ukraine" Accessed on 14.08.2017 https://www.bertelsmann-stiftung.de/fileadmin/files/BSt/Publikationen/GrauePublikationen/EZ_Studie_Benefits_and_Costs_of_DCFTA_2017_ENG.pdf

³ Official Website of the European Commission, Countries and Regions; Section of Trade with Georgia, Accessed on 14.08.2017, <http://ec.europa.eu/trade/policy/countries-and-regions/countries/georgia/>

⁴ Official Website of the EU Delegation to Georgia, Georgia Moving Towards DCFTA, Accessed on 17.08.2017, http://www.eeas.europa.eu/archives/delegations/georgia/documents/eu_georgia/dcfta2012_01_en.pdf

⁵ European Commission, Joint Staff Working Document, Association Implementation Report on Georgia, Brussels, 25.11.2016, Accessed on 01.08.2017, https://eeas.europa.eu/sites/eeas/files/1_en_jswd_georgia.pdf

years (up to 8 years in a few cases). This means that export opportunities to the EU market will also take some time to fully materialize.

The Trade Sustainability Impact Assessment, a report carried out for the European Commission's DG Trade and published in October 2012 included a forecast on expected economic effects of the EU-Georgia DCFTA: a 4.3 percent growth of GDP in the long run, 12 percent increase of exports and 7.5 percent rise of imports.⁶ The progress isn't yet visible in the predicted volume, especially in the situation when the DCFTA has been provisionally in force since 1 September 2014 only, and this period coincided with economic crisis in the CIS region. However, the dynamics of Georgia's economic grows, trade turnover and FDI flow for the last years still looks optimistic. The main economic indicators for Georgia looks like the following⁷:

Main Indicators

Indicator Source IMF (World Economic Outlook)	unit	2012	2013	2014	2015	2016
Population	Millions of inhabitants	4	4	4	4	4
GDP	Billions of euros	12	12	12	13	13
GDP per capita	Euros	3,215	3,213	3,333	3,391	3,471
Real GDP growth	%	6.4	3.4	4.6	2.9	2.7
Inflation rate	%	-0.9	-0.5	3.1	4.0	2.1
Current account balance	% of GDP	-11.7	-5.8	-10.6	-12.0	-12.4

And the charts⁸ below show the dynamics of EU-Georgia economic ties for the recent years, namely on trade in goods, services and foreign direct investments.

Chart I:

EU Merchandise trade with Georgia

indicator	unit	2012	2013	2014	2015	2016	Annual average growth
imports	Billions of euros	0.6	0.7	0.7	0.7	0.6	-1.4
exports	Billions of euros	2.1	2.0	1.9	1.8	2.0	-1.3
balance	Billions of euros	1.5	1.4	1.3	1.1	1.4	

⁶ Report "Trade Sustainability Impact Assessment in support of negotiations of a DCFTA between the EU and Georgia and the Republic of Moldova", ECORYS, Rotterdam, 27 October 2012, Accessed on 01.08.2017, http://trade.ec.europa.eu/doclib/docs/2012/november/tradoc_150105.pdf

⁷ European Commission, Georgia - Trade Statistics, 22 Feb 2017, Accessed on 04.08.2017, http://trade.ec.europa.eu/doclib/docs/2006/september/tradoc_111507.pdf

⁸ Ibid

Chart II:

EU Trade in services with Georgia

indicator	unit	2012	2013	2014	2015	2016	Annual average growth
imports	Billions of euros	0.2	0.3	0.3	0.3		6.7
exports	Billions of euros	0.4	0.5	0.6	0.6		18.4
balance	Billions of euros	0.1	0.2	0.3	0.3		

Chart III:

EU Foreign direct investment with Georgia

indicator	unit	2012	2013	2014	2015	2016	Annual average growth
stocks: inward	Billions of euros		0.1	0.1	0.1		7.2
stocks: outward	Billions of euros		2.9	3.8	3.6		11.6
stocks: balance	Billions of euros		2.8	3.7	3.5		
flows: in	Billions of euros		-0.0	0.0	-0.0		
flows: out	Billions of euros		0.1	0.2	0.1		59.1
flows: balance	Billions of euros		0.1	0.2	0.2		

In addition to concrete results in the short-term perspective, the process of approximation with the EU regulatory standards are going to bring long-term benefits to the country. In particular, the DCFTA will enhance competitiveness of Georgian products, improve the investment climate, attract stable FDIs and all these will eventually bring positive results for Georgia's socio-economic development. In broader perspective, “what is at stake is not simply the increase of EU-Georgia trade flows but market development, consumer protection, product quality; in other words, modernization of the country”.⁹

The transition process will contribute additional economic benefits. Many countries (particularly, Turkey and the Balkan countries) in the world use regulatory standards for trade similar to the EU; therefore compliance with those standards will facilitate Georgia’s trade relations not only with the European Union but with other partner countries too.¹⁰

Future of EU-Georgia DCFTA: Deeper Integration within European Single Market

Georgia is an important partner for the European Union both within the European Neighbourhood Policy (ENP) and its eastern dimension under the Eastern Partnership (EaP) initiative.¹¹ Furthermore, Georgia is considered and recognized as a frontrunner and best performer country of the EaP programme for a number of years already.

⁹ Official Website of the EU Delegation to Georgia, Georgia Moving Towards DCFTA, Accessed on 17.08.2017, http://www.eeas.europa.eu/archives/delegations/georgia/documents/eu_georgia/dcfta2012_01_en.pdf

¹⁰ Official Website of the EU Delegation to Georgia, Georgia Moving Towards DCFTA, Accessed on 17.08.2017, http://www.eeas.europa.eu/archives/delegations/georgia/documents/eu_georgia/dcfta2012_01_en.pdf

¹¹ European Union External Action EU-Georgia Relations, Factsheets Accessed on 12.08.2017 https://eeas.europa.eu/headquarters/headquarters-homepage/23634/eu-georgia-relations-factsheet_en

The 2015 ENP Review re-confirmed the EU's long-term engagement with the neighborhood countries, in particular with partners, such as Georgia, wishing to pursue deeper ties with the European Union. In addition, the EU's 2016 Global Strategy acknowledged Georgia as an example of the state and societal resilience in the eastern neighborhood.¹² While these conceptual documents reveal clear aspirations of the European Union to enhance engagement with partner countries, the shape and nature of potential extended formats are still vague.

The ENP Review document, a joint communication of the EU's High Representative and the European Commission¹³ is tangible evidence of the EU's need to unfold additional leverages and partnership tools while engaging with partner countries. It is becoming more and more apparent that existing formats, namely the ENP and the EaP, do not sufficiently reflect the aspirations of some partner countries, among them those that wish deeper political and economic integration with the EU and have an ultimate goal to join the Union.

While analyzing the potential ways of advancing Georgia on the path of more inclusive trade and economic engagement with the European Union, one of the feasible case-scenarios could be more integration and/or approximation to the European Economic Area (EEA), which was launched in 1994 to extend the European Single Market to countries in the European Free Trade Area (EFTA). "Membership in the EEA is contingent on full implementation of all EU single market legislation, the bulk of which is already covered by the DCFTA. A key difference between the DCFTA and the EEA is the former's incorporation of all four freedoms of the EU's internal market."¹⁴

The European Economic Area provides the free movement of persons, goods, services and capital within the European Single Market, including the freedom to choose residence in any country within this area.¹⁵ The EEA brings together the EU Member States and three of the EFTA States (Iceland, Liechtenstein and Norway) in a Single Market, also referred to as the "Internal Market". Switzerland is not part of the EEA Agreement, but has a set of bilateral agreements with the EU, which allow it also to participate in the internal market.¹⁶

The EEA Agreement specifies that membership is open to member states of either the EU or EFTA. Article 126 of the Agreement makes it clear that the EEA Agreement only applies to

¹² European Union External Action EU-Georgia Relations, Factsheets Accessed on 12.08.2017 https://eeas.europa.eu/headquarters/headquarters-homepage/23634/eu-georgia-relations-factsheet_en

¹³ Joint Communication to The European Parliament, The Council, The European Economic and Social Committee And The Committee Of The Regions, Review of the European Neighbourhood Policy; Accessed on 14.08.2017 http://eeas.europa.eu/archives/docs/enp/documents/2015/151118_joint-communication_review-of-the-enp_en.pdf

¹⁴ Lebanidze Bidzina, Georgia's European Integration: What comes after the Eastern Partnership; Georgian Institute of Politics, Accessed on 12.08.2017; <http://gip.ge/georgias-european-integrationwhat-comes-eastern-partnership/>

¹⁵ European Union, Topic of the European Union; One market without Borders; Accessed on 12.08.2017 https://europa.eu/european-union/topics/single-market_en

¹⁶ Website of The European Free Trade Association, The EEA agreement ; Accessed on 12.08.2017 <http://www.efta.int/eea/eea-agreement>

the territories of the EU, in addition to Iceland, Liechtenstein and Norway. It means that a country wishing to join the EEA should first become a member either of the EU or EFTA, unless an amendment were to be made in the EEA Agreement itself for special treatment of a particular country.¹⁷

The option of EFTA membership is no less challenging than becoming the EU member. According to the EFTA convention, “any State may accede to the Convention provided that the EFTA Council decides to approve its accession, on such terms and conditions as may be set out in that decision”. Moreover, unlike the European Union, EFTA lacks formal criteria for accession. The membership depends on the political will of the Council, the organization’s highest governing body. In the case of EaP countries, including Georgia, there are even less incentives to accept EaP countries into this “exclusive club”. Hence, “instead of entering long negotiations with the EFTA, the EaP countries with EU membership aspirations may be advised to launch negotiations on a similar framework agreement like the EFTA.”¹⁸

It is important to look into the contents of EU’s recent conceptual documents to analyze the prospects of deeper engagement and integration within EU’s Single Market:

- The ENP Review reads that implementation of AA/DCFTAs, accompanied by reforms, will result in the partners' comprehensive approximation with international standards and EU legislation and standards. And this will lead to the gradual economic integration of partners in the EU internal market and therefore to the **creation of an economic area**.¹⁹ Almost same wording was used when referring to the prospects of the AA/DCFTAs in the text of Council Conclusions [the EU’s main decision-making body] on the ENP Review, thus making the document weightier.²⁰
- Reference on “creation of an economic area” for DCFTA signatory countries is also made in a Global Strategy for the European Union’s Foreign and Security Policy. The document stipulates that European Union will think creatively about deepening tailor-made partnerships further and the possibilities include the **creation of an economic area** with countries implementing DCFTAs²¹.

¹⁷ Frequently asked question on EFTA and the EEA; Is it possible to become a party to the EEA Agreement without being a member of the EU or EFTA? Accessed on 12.08.2017; <http://www.efta.int/faq>

¹⁸ Lebanidze Bidzina, Georgia’s European Integration: What comes after the Eastern Partnership; Georgian Institute of Politics, Accessed on 12.08.2017; <http://gip.ge/georgias-european-integration-what-comes-eastern-partnership/>

¹⁹ Joint Communication of the European Parliament, the council, the European Commission and social committee and committee of the Regions; Review of the European Neighbourhood policy; 18, November 2015; Accessed on 14.08.2017 http://eeas.europa.eu/archives/docs/enp/documents/2015/151118_joint-communication_review-of-the-enp_en.pdf

²⁰ European Council; Council conclusions on the review of the European Neighbourhood policy; Accessed on 14.08.2017 http://eeas.europa.eu/archives/docs/enp/documents/2015/151118_joint-communication_review-of-the-enp_en.pdf

²¹ A Global Strategy for the European Union’s Foreign and Security Policy, June 2016, Accessed on 14.08.2017, http://europa.eu/globalstrategy/sites/globalstrategy/files/regions/files/eugs_review_web_0.pdf

None of the above-mentioned conceptual documents mention a timeframe for creating either the economic area or the details behind this idea. Those details are missing as well in the document²² developed recently by the European Commission and the European External Action Service. The joint working document "Eastern Partnership, focusing on key priorities and deliverables", aims to identify 20 key deliverables for 2020, intended to contribute to the joint work of EU Member States and EaP Partner countries.

Observations and Recommendations

As usual, the European Union prefers to deal with partner countries in their regional dimension rather than in an individual capacity, particularly in the situation when one talks about a small country like Georgia. It's less possible that the EU comes up with a new initiative only for Georgia, especially if it concerns upgrading the formats of political or economic cooperation.

The recent decision of Western Balkans leaders, supported by the EU to develop a Regional Economic Area to consolidate the market of Balkans is a good example of EU's preference to deal with partners in regional dimension. The European Commission is even going to support the implementation of this initiative with a package of €7 million.²³

The fact-sheet on the Regional Economic Area prepared by the European Commission makes it even clearer that the initiative will make the region more attractive and competitive. The document clarifies that engaging in a regional economic area sends a powerful message that the Western Balkans is a market of some 20 million consumers with enormous untapped potential. It would secure both integration within the region and with the EU and at the same time also foster the region's approximation to the European Union. The fact-sheet also mentions that in this way, the initiative will be an important milestone for preparation for EU accession.²⁴

It's clear there is some thinking, at least in its very preliminary stage, within the EU on future prospects for the DCFTAs. One of the most important conceptual documents for ENP countries – the ENP Review – explicitly mentions about the possibility of gradual economic integration of partners in the EU internal market and creation of an economic area. Another conceptual document – the Global Strategy – is repeating almost the same, adding that tailor-made partnerships should be further deepened and the creation of an economic area with countries implementing DCFTAs should be an option.

²² European Commission and the European External Action Service, Joint Staff Working Document, Eastern Partnership - Focusing on key priorities and deliverables, Brussels, 15.12.2016; accessed on 14.08.2017, https://eeas.europa.eu/sites/eeas/files/swd_2016_467_f1_joint_staff_working_paper_en_v3_p1_8733051.pdf

²³ European Commission, Western Balkans Summit 2017: delivering for the region, Brussels, 12 July 2017, accessed on 14.08.2017, http://europa.eu/rapid/press-release_IP-17-2007_en.htm

²⁴ European Commission, Fact Sheet, Western Balkans: Regional Economic Area, Brussels, 12 July 2017, accessed on 15.08.2017, http://europa.eu/rapid/press-release_MEMO-17-1967_en.htm

The fact that nothing is mentioned about creation of the economic area in the joint working document "Eastern Partnership – focusing on key priorities and deliverables" means that there seemingly are no plans to push ahead this idea at least before 2020. But it does not mean Georgia should be inactive until the existing document on deliverables expires and the new list of priorities is unveiled for EaP countries. Neither should Georgia should neither wait for the full implementation of the AA/DCFTA. The last deadline for harmonizing the Georgian legislation with the EU *acquis* fully in line with the Agreement is 31 December 2029.

The Western Balkans are a step ahead of Georgia, Ukraine and Moldova. They already have the European Membership Perspective. The EaP countries that have signed the AA/DCFTAs should follow carefully and analyze the measures being taken by Western Balkans on their path to the EU membership. Georgia, Ukraine and Moldova should start thinking of creating Balkan type of Regional Economic Area so that to make it with the market of about 50 million consumers economically more attractive and interesting for the European Union.

Concluding new free trade agreements (FTAs) and enhancing the existing trade ties with partner countries in the neighborhood and wider Europe region could be part of the above-mentioned strategy to come closer to the EEA step-by-step. Signature of the FTA between Georgia and EFTA on 27 June 2016, as well as Georgia's decision to apply and then join on 1 July 2017 the Regional Convention on Pan-Euro-Mediterranean (PEM) preferential rules of origin²⁵, are both steps ahead in right direction.

Potential options may also include negotiations with the EU on provision of the missing fourth freedom – the free movement of workers. The DCFTA already covers three freedoms and provision of the last missing freedom will deepen the partner country's integration into the European Single Market. In this case, the partner country will be lacking only the formal membership to the EEA.

²⁵ Kovziridze Tamara, Movchan Veronika, Gumene Vadim and Emerson Michael, Preferential Rules of Origin and its Benefits - A Comparative Analysis of its application for Georgia, Moldova and Ukraine, 10 August 2017; Accessed on 20.08.2017, <http://www.3dcftas.eu/system/tdf/PEM%20article%20FINAL.pdf?file=1&type=node&id=367&force=>