

GEORGIA'S TRADE PERFORMANCE IN THE LIGHT OF EU-GEORGIA DEEP AND COMPREHENSIVE FREE TRADE AREA

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Abstract

The EU-Georgia Association Agreement (AA) with its integral part on Deep and Comprehensive Free Trade Area (DCFTA) is an important step towards Georgia's close political association and gradual economic integration with the EU. The EU-Georgia DCFTA is considered as the best mechanism available to Georgia to promote exports, attract foreign direct investments and achieve high economic growth rate. In recent years Georgia's trade analysis demonstrates some optimistic developments in trade performance. However, in short period since provisional application of the DCFTA, its positive outcomes are not significant. Georgia's gains from the AA/DCFTA directly depend on scope and speed of legal approximation and regulatory convergence with the EU, which is challenging process, especially in short term. Nevertheless, it is clear that Georgia should continue economic reforms, namely reforms in all trade related areas in order to fully benefit from close economic and political relations with the EU foreseen by the agreement.

Key Words: Association Agreement, Deep and Comprehensive Free trade area, EU, Georgia, Trade

JEL Classification: F13, F14, F15

I. INTRODUCTION

In 27 of June, 2014, The European Union and Georgia signed Association Agreement (AA), which came into force from 1 of July, 2016. It should be noted, that many titles of the agreement, including Title IV (Trade and Trade-related Matters) have been provisionally applied since 1 September, 2014. The Association Agreement with its integral part on Deep and Comprehensive Free Trade Area (DCFTA) is perceived as a key mechanism to bring Georgia close to the EU in both, political and economic dimensions. Noteworthy, that studies conducted before signing the Association Agreement, predicted DCFTA's positive effects on trade, investments and economic growth in Georgia, especially in the long-run (UNDP, 2007; Case/Global Insight, 2008; Ecorys/CASE, 2012). Although, Georgia started implementation of Association Agreement, including DCFTA a short time ago, it is important to analyze Georgia's trade performance during recent years in order to estimate DCFTA induced initial transformation of Georgia's trade relations.

The aim of this article is to observe a concept of the DCFTA and the EU's trade policy towards Georgia, as well as analyze recent key developments in Georgia's trade relations in the light of the EU-Georgia DCFTA agreement.

II. EU'S RECENT TRADE POLICY DEVELOPMENTS AND THE EU-GEORGIA DCFTA

During recent years, the EU's trade policy priorities have been significantly transformed. The EU remains an active supporter of the conclusion of the Doha Development Round negotiations under the World Trade Organization (WTO), however, the EU simultaneously attempts to gradually deepen its trade relations on a bilateral level through new Free Trade Agreements (FTAs). The most important reasons of this transformation are: difficulties to reach an agreement on the global level regarding trade issues in the framework of WTO and increased competition in the world economy. As it was indicated in the European Commission's Communication "Doha remains our top priority. However, the bilateral is not the enemy of the multilateral. The opposite may hold truer: liberalization fuels liberalization" (European Commission, 2010, p. 3). Moreover, as Guerrieri and Dimon (2006) noted "During the past decade the formerly unquestioned European leadership in regional integration and preferential trade agreements has been increasingly challenged by dynamic US regionalism on a global scale" (p. 89). Accordingly, the EU was trying "To match the FTAs negotiated as part of the US 'competitive liberalisation' strategy" (Woolcock et al. 2007, p. 236). As a result, the EU has broadened the area of bilateral agreements and involved more countries in its trade agenda.

In general, the EU's recent bilateral trade policy was based on two approaches. First approach was declared in communication "Global Europe: Competing in the World" (Commission of the European Communities, 2006). According to the communication the EU will start negotiations with selected countries and "to have positive impact

FTA's must be comprehensive in scope, provide for liberalization of substantially all trade and go beyond WTO disciplines" (p. 8). As Koopmann and Wilhelm (2010) noted "In general, the new bilateral trade agreements of the EU are meant to be "WTO plus", i.e. exceed the scope of the agreements already reached in the WTO through both the opening of new policy areas and the deepening or strengthening of existing provisions, obligations and disciplines". Therefore, the EU's "new FTAs should also include provisions for investment, IPR, public procurement and competition" (Fojtíková, 2012, p. 81). According to the abovementioned communication key criteria for conclusion of comprehensive trade agreements were economic criteria such as market potential (economic size and growth) and the level of protection against EU export interests (tariffs and non tariff barriers). Respectively based on economic criteria particular countries and regional integration groups were chosen as priority countries/country groups to conclude comprehensive FTAs (Commission of the European Communities, 2006). To the EU's already concluded "new generation" FTA's belongs Agreements with South Korea, Colombia-Peru-Ecuador, Central America (CA) and Canada (Comprehensive Economic and Trade Agreement (CETA)) (European Commission, 2018a). In addition, it should be noted that "Comprehensive FTAs in force with countries such as Chile and South Korea envision a - selective - approximation of standards and norms and constitute attempts to influence global economic governance while extending EU standards and rules" (Manoli, 2013, p. 51-52). So, EU's "new generation" FTA's mostly are based on economic criteria and driven by economic considerations.

Second approach was designed for European Neighborhood Policy (ENP) countries. This approach was highlighted in the EC Communication on "A Strong European Neighborhood Policy" (Commission of the European Communities, 2007). The EU's trade policy towards European Neighborhood Policy countries reflected importance of geographical proximity and political considerations, such as some eastern neighbor countries aspirations to achieve close economic and political relations with the EU and their readiness to implement reforms in the trade-related areas and assume obligations under the agreement. According to abovementioned communication "Tailor-made deep and comprehensive free trade agreements (DCFTAs), including measures to reduce non-tariff barriers through regulatory convergence, are the keys to increased economic integration with ENP partners" (ibid, p. 4). Therefore, "the DCFTAs consist of two parts: tariff reduction (built on WTO commitments) and adoption of the EU trade *acquis*, going beyond tariff reductions to cover more extensively the dimensions of investment protection, public procurement, and competition policy" (Manoli, 2013, p. 52). As a result, these agreements effectively combine liberalization and regulation and "due to the objective of gradual integration into the EU's internal market, DCFTAs go beyond "new generation" FTAs and represent a unique type of trade agreement (European Commission, 2017a, p. 14). Hence, the EU's favored trade agreements with ENP countries were Deep and Comprehensive Free Trade Agreements (DCFTAs), which in contrast to the EU's already concluded or negotiating "new generation" trade agreements are driven mostly by geography and politics (geographical proximity and stable neighborhood), rather than economic considerations. However, as Woolcock et al. (2007) noted, "A few EU bilateral agreements have been commercially motivated" (p. 237). This is especially relevant in case of eastern neighborhood considering that Moldova and Georgia are EU's 63rd (0.1% of EU's total trade) and 73rd (0.1% of EU's total trade) trade partners respectively; Ukraine is the 25th trade partner with around 1% of its total trade (European Commission, 2018b).

First DCFTA's concluded by the EU were agreements with three ENP eastern countries - Ukraine, Moldova and Georgia, as integral part of Associations Agreements with these countries. Although AA/DCFTAs did not envisage membership of the EU "the prospect of increasing exports to the EU and access to single market has been a strong incentive for structural reforms in neighboring economies with EU membership aspirations" (Manoli, 2013, p. 63). At the same time "The implementation of the DCFTA is thus not only expected to bring benefits via granting access to the large EU market, but also by inducing deep changes to the business environment in the beneficiary countries, making their economies more competitive and efficient" (Adarov and Havlik, 2016, p. 16). Consequently, DCFTAs foreseen regulatory approximation and convergence in many trade-related areas were a primary novelty in trade policy towards eastern neighbors, which lead to considerable policy changes in many areas of economy in countries involved, including Georgia (Eterea, 2013).

The EU's approach to launch negotiations with Georgia on DCFTA was based on conditionality to provide the regulatory convergence and legal approximation in some areas. It should be noted that this approach, considering broad area of reforms Georgia had to undertake, was criticized by some researchers (Messerlin et al. 2011; Dreyer, 2012). However, taking into account the political importance of close relations with the EU, the Government of Georgia prepared strategies and action plans in all relevant areas (Technical barriers to trade (TBT), Sanitary and Phytosanitary issues (SPS), Intellectual Property Rights (IPR) and Competition Policy) and started the implementation process.

Noteworthy, that before signing the Association Agreement, Georgia benefited from preferential trade regime with the EU in the framework of the EU Generalized System of Preferences (GSP+), incentive arrangement for sustainable development and good governance, which was granted to Georgia in 2005. The EU GSP+ covered 7200 products and allowed Georgian exports almost tariff-free access to the EU market. After signing Association Agreement there was transition period from GSP+ to DCFTA until December 31, 2016.

It should be noted that “The EU-Georgia agreement is centred around a “deep and comprehensive free trade agreement” and a broad programme of approximation of Georgia’s legislation to EU laws” (Kawecka-Wyrzykowska, 2015, p. 78). In particular, Georgia should accomplish the regulatory convergence and legal approximation in many areas of the economy, such as intellectual property rights, sanitary and phytosanitary issues, food safety, customs legislation, labor code, services, environment, public procurement, technical regulations, standards and conformity assessment procedures, company law, taxation, competition policy and state aid, enterprise policy, public internal financial control, etc. In addition, Georgia should “...undertake any action needed to reflect the developments in EU law in its domestic legislation (the concept of the so called dynamic approximation)” (European Commission, 2017b, p.3). Noteworthy, that concept of dynamic approximation is foreseen also by AA/DCFTAs with Ukraine and Moldova.

In 2015-2018 Georgia has achieved some progress in implementation AA/DCFTA commitments. As it was indicated in the EU Commission recent report on Association Implementation “The process of approximation of Georgia's legislation in trade-related areas advanced in 2018” (European Commission, 2019, p. 8). At the same time “It should be noted that the timeline for approximation of Georgian legislation was back-loaded by Georgia in the negotiation process to the extent that approximation intensifies in 2018 and will continue....)” (European Commission, 2018b, p. 94). In general, Georgia implements its commitments under AA/DCFTA in accordance with agreed timeline.

III. MAJOR DEVELOPMENTS IN GEORGIA’S RECENT TRADE RELATIONS

The abovementioned Studies carried out in order to evaluate DCFTA’s effects on Georgia’s economy in general and particularly on exports were positive. According to the recent study, “Exports are estimated to increase by 9 and 12 percent in the short and long run respectively, with imports going up by 4.4 and 7.5 percent respectively” (Ecorys/CASE, p. 37). At the same time “The short- and long-run does not refer to a specific time period, but to the time it takes for economic effects to adjust.... The long-run effect is generally expected to take place over a period beyond 5-10 years from the moment of implementation of the DCFTA” (ibid. p. 26). However, more than 4 years passed since provisional application of trade related Title of the Association Agreement and initial effects of the DCFTA on Georgia’s trade performance could be observed.

Therefore, Georgia’s recent trade data for the period of 2011-2018 is analyzed. Study period is divided into two parts. First period includes 2011-2014 or pre-DCFTA period and second, 2015-2018 or post-DCFTA period. This division allows revealing new developments in Georgia’s trade relations in recent years. More specifically, trade data of Georgia with the EU and Commonwealth of Independent States (CIS) during 2011-2018 is examined. CIS countries alongside with the EU are Georgia’s largest trade partners. Noteworthy, that Georgia has free trade regime with CIS countries on the basis of simple Free Trade Agreements (FTAs).

Georgia’s trade relation analysis is divided into 4 stages. At the first stage, trade with the EU is analyzed during abovementioned two study periods. In particular, to reveal initial effects of DCFTA in trade with the EU annual average growth rates of Georgia’s exports to the EU and imports from the EU in pre-DCFTA and post-DCFTA periods is examined.

During 2011-2014, annual average growth rate of Georgia’s exports to the EU was 23,8%, while annual average growth rate of imports from the EU was 14,1%. In contrast to pre-DCFTA period, during 2015-2018 annual average growth rate of Georgia’s exports to the EU was 4,6%, while annual average growth rate of imports from the EU was 3,3% (Fig. 1).

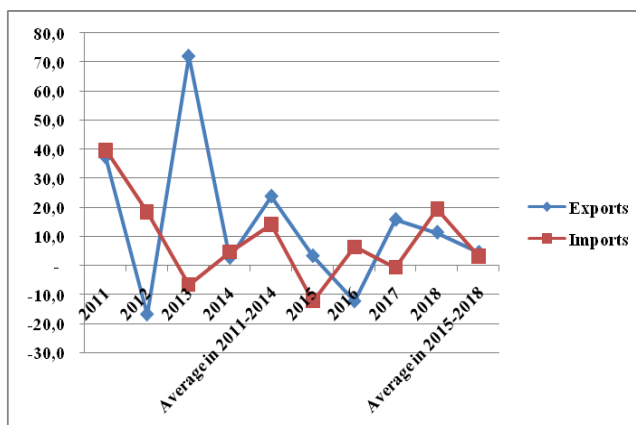


Figure 1. Georgia's Export-Import with the EU (Growth (%)) in 2011-2018

Source: Own figures based on data from National Statistics Office of Georgia. www.geostat.ge

It should be noted that “Throughout the first three years of DCFTA implementation Georgia started to export some new products to the EU e.g. kiwi and blue berries” (European Commission, 2018b, p. 88). However, it is clear that in 2015-2018 annual average growth rates of Georgia’s exports to the EU and imports from the EU significantly decreased. A sharp decrease of Georgia’s exports to the EU during post-DCFTA period was observed in 2016. In 2016 “... the price drop for a number of commodities at world level is one of the main causes of declining value of exports from Georgia to the EU, whereas in volume terms the level of exports remained stable” (European Commission, 2017b, p. 5). Noteworthy, that in 2018 Georgia’s exports to the EU in absolute terms compared to exports in 2014 increased by 16,9% (from 624, 2 Mil. USD to 730,3 Mil. USD), while imports from the EU compared to 2014 increased by 10,8% (from 2371,9 Mil. USD in 2014 to 2629,1 Mil. USD in 2018).

At the second stage, data regarding trade relations of Georgia not only with the EU, but also with CIS countries throughout pre-DCFTA and post-DCFTA periods is analyzed. This makes possible to compare Georgia’s trade performance with those integration/country groups with DCFTA and simple FTA respectively.

It is notable that during 2011-2014 annual average growth rates of Georgia’s exports to the EU and CIS were almost the same (23.8 and 23.6% respectively). During 2015-2018, annual average growth rate of Georgia’s exports to the CIS countries also decreased as it was in case of the EU. However, it still remained higher (11,8%) than annual average growth rate of exports to the EU (4,6%) (Fig. 2).

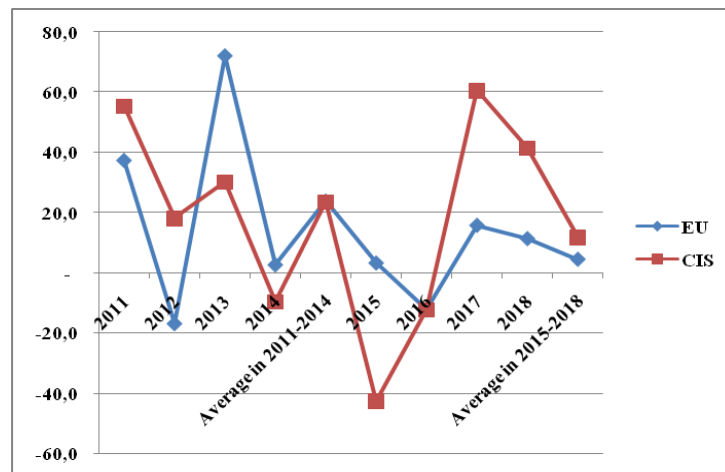


Figure 2. Georgia's Exports to the EU and CIS compared (Growth (%)) in 2011-2018

Source: Own figures based on data from National Statistics Office of Georgia. www.geostat.ge

Moreover, in 2011-2014 annual average growth rate of Georgia’s imports from the EU (14,1%) was higher than from CIS countries (8,1%). It should be noted, that during the post-DCFTA period annual average growth rate of imports from the CIS countries also decreased, but it remained higher than annual average growth rate of imports from the EU (6,6% and 3,3% respectively) (Fig. 3).

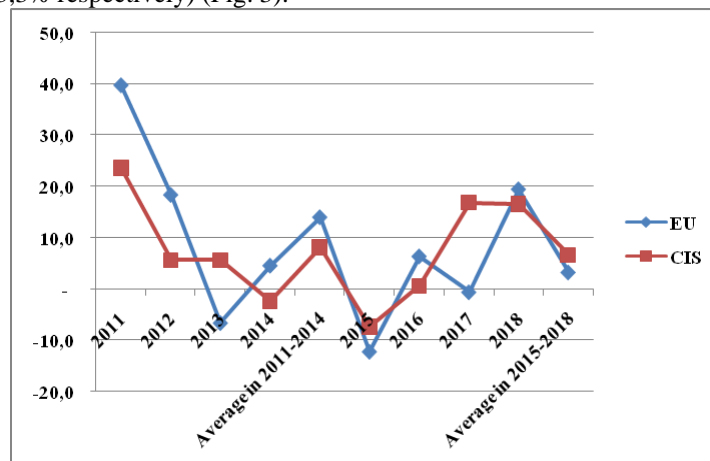


Figure 3. Georgia's Imports from the EU and CIS compared (Growth (%)) in 2011-2018

Source: Own figures based on data from National Statistics Office of Georgia. www.geostat.ge

In addition, annual average growth rate of Georgia’s total exports during 2011-2014 was 14,9%, while annual average growth rates of exports to the EU and CIS were much higher (23,8% and 23,6% respectively). Hence, in 2011-2014 exports growth with the EU and CIS almost equally contributed to the total exports growth of Georgia. However, during 2015-2018 average annual growth rate of Georgia’s total exports was 6,3%, which is higher than annual average growth rate of Georgia’s exports to the EU (4,6%), but less than annual average growth

rate of Georgia’s exports to the CIS countries (11,9%) (Fig. 4). Therefore, in 2015-2018 exports growth to CIS countries was more important factor of total exports growth of Georgia than exports growth to the EU.

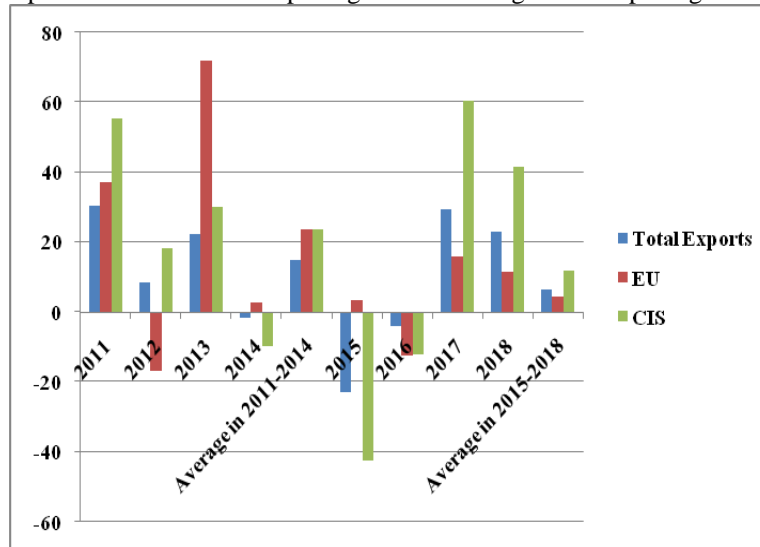


Figure 4. Georgia's total Exports, Exports to the EU and CIS compared (Growth (%)) in 2011-2018
 Source: Own figures based on data from National Statistics Office of Georgia. www.geostat.ge

Furthermore, annual average growth rate of Georgia’s total imports during 2011-2014 was 13,9%, while annual average growth rate of imports from the EU was higher (14,1%) and from CIS countries turned out lower (8,1%). Hence, in 2011-2014 imports growth from the EU was more important determinant of total imports growth. In contrast, during 2015-2018 annual average growth rate of Georgia’s total imports was 2,1%, while annual average growth rates of imports from the EU and CIS were higher (3,3% and 6,6% respectively). Accordingly, in post-DCFTA period total imports growth was mainly due to imports growth from CIS countries rather than from the EU (Fig. 5).

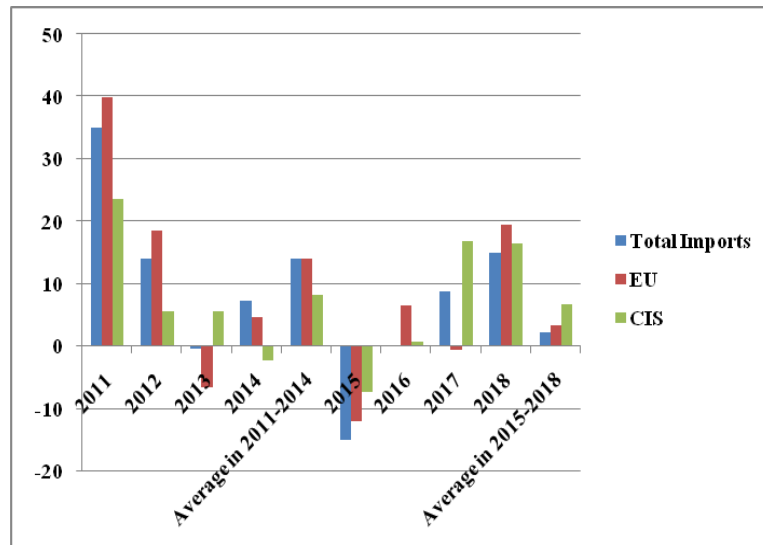


Figure 5. Georgia's total Imports, Imports from the EU and CIS compared (Growth (%)) in 2011-2018
 Source: Own figures based on data from National Statistics Office of Georgia. www.geostat.ge

Consequently, it is clear that during pre-DCFTA period Georgia’s trade relations with the EU was increasing more rapidly than with CIS countries, while during 2015-2018, in contrast to pre-DCFTA period, trade relations with CIS has grown faster than with the EU.

At the third stage, Georgia’s exports to the EU and CIS as a share in total exports as well as at Georgia’s imports from the EU and CIS as a share in total imports during pre-DCFTA and post-DCFTA periods is analyzed. In 2011-2014, exports to CIS countries composed 51,8% on average in total exports of Georgia, while exports to the EU was 19,2% on average throughout this period. During 2015-2018, exports to CIS countries as a share in total exports decreased and composed 41,5% on average, while exports to the EU as a share in total exports has increased and reached 25,3% on average. However, it is noteworthy that in 2016-2018 share of Georgia’s exports to the EU in

total exports were decreasing (from 26,7% in 2016 to 21,7% in 2018), while share of exports to CIS has increasing trend (from 34,9% in 2016 to 49,8% in 2018) (Fig. 6).

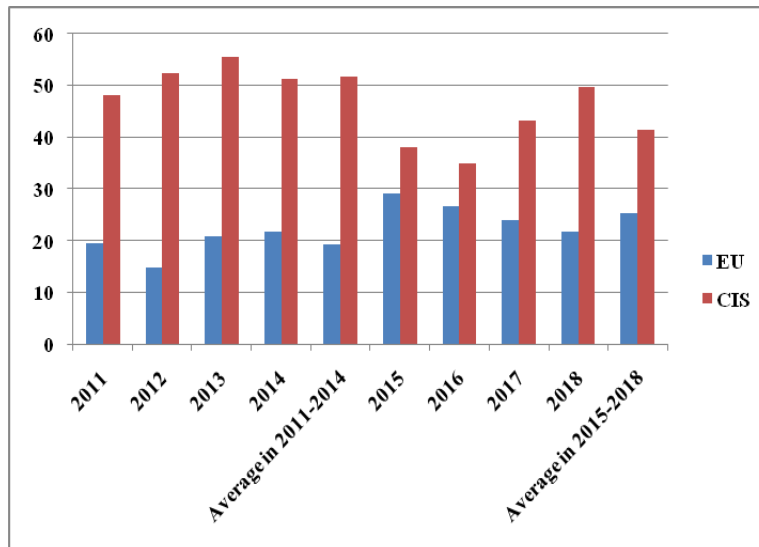


Figure 6. Georgia's Exports to the EU and CIS (share in total Exports (%))

Source: Own figures based on data from National Statistics Office of Georgia. www.geostat.ge

In 2011-2014, imports from the EU composed 28,6% on average in total imports of Georgia, while imports from CIS was 26,2% on average during this period. In 2015-2018, imports from the EU slightly increased and reached 28,8% on average, whereas imports from CIS countries as a share in total imports also increased and composed 28,1% on average (Fig. 7). It is clear that imports from the EU and CIS has not changed significantly during study period and the DCFTA had not lead to import decrease from CIS countries. On the contrary, in 2017-2018 shares of imports from CIS countries in total imports, compared to other years in study period, were higher than imports share from the EU.

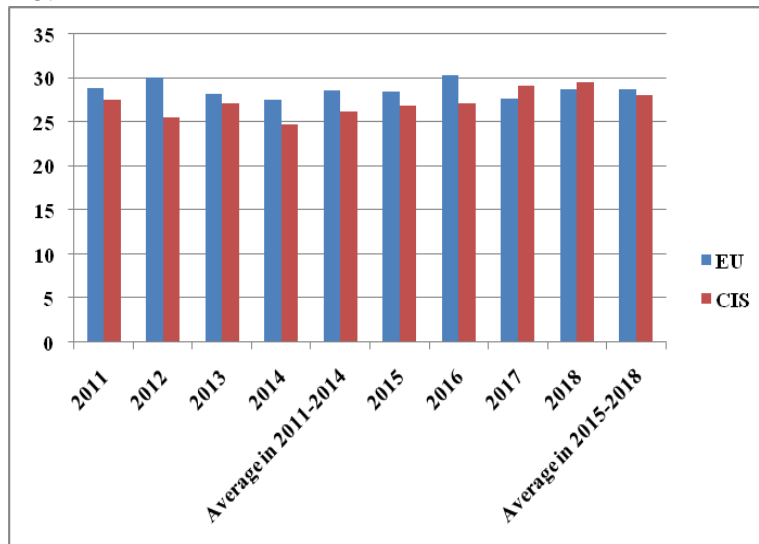


Figure 7. Georgia's Imports from the EU and CIS (share in total Imports (%)) in 2011-2018

Source: Own figures based on data from National Statistics Office of Georgia. www.geostat.ge

At the final stage, data on Georgia's trade turnover with the EU and CIS as a share in total trade turnover is examined. In 2015-2018 Georgia's average trade turnover with the EU as a share in total trade turnover has slightly increased compared to pre-DCFTA period (26,4% on average) and reached 27,9% on average, while Georgia's average trade turnover with the CIS countries as share in total trade turnover has slightly decreased (from 32,5% on average in 2011-2014 to 31,5% on average). It should be noted that in 2016 the EU's share in total trade turnover was a little higher, than share of CIS countries. However, in 2016-2018 share of CIS countries in total trade turnover significantly increased (from 28,9% in 2016 to 35% in 2018), while the EU's share decreased (from 29,5% in 2016 to 26,9% in 2018) (Fig. 8).

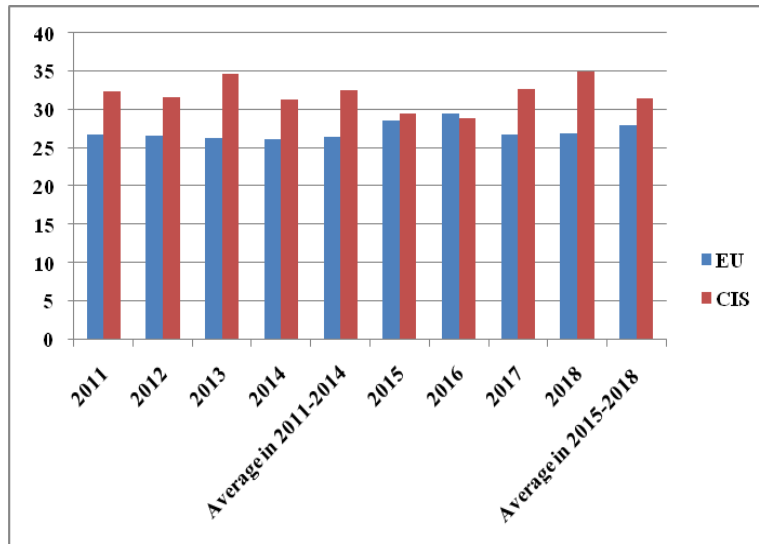


Figure 8. Georgia's Trade turnover with the EU and CIS (share in total trade turnover (%))
Source: Own figures based on data from National Statistics Office of Georgia. www.geostat.ge

Thus, main results of conducted trade analysis of Georgia during 2011-2018 are as follows: First, in 2015-2018 annual average growth rates of Georgia's exports to the EU and imports from the EU significantly decreased compared to pre-DCFTA period; second, in 2011-2014 Georgia's trade relations with the EU grow faster, than with CIS countries; third, despite the DCFTA in 2015-2018 trade relations with CIS countries has grown more rapidly and exports growth to CIS largely contributed to Georgia's total exports growth than exports growth to the EU; Finally, in 2015-2018 compared to pre-DCFTA period average share of exports to the EU in Georgia's total exports as well as average trade turnover with the EU in Georgia's total trade turnover has increased.

As trade analysis demonstrates the EU-Georgia DCFTA has not yet changed significantly Georgia's trade performance. However, it should be noted that these are initial, short term results of DCFTA and it does not necessarily indicate continuity of abovementioned trends. It is clear that gains from the DCFTA, especially increase of Georgia's exports to the EU depend on the level of legal approximation and regulatory convergence with the EU and Georgia should continue reforms in all trade related areas. Moreover, it is crucial precondition to increase exports to the EU, considering that "The results of the free trade area are to be seen rather in mid-term period and once approximation of Georgian legislation progresses" (European Commission, 2017b, p.5). However, it should also be noted that the concept of dynamic approximation, which does not give clear definition regarding timeframe and scale of approximation of Georgia's legislation with those of the EU, makes legal approximation process even more complex issue for Georgia.

IV. CONCLUSIONS

The EU-Georgia Association Agreement based on conditionality via establishing the EU compatible economic system is considered as the best instrument to promote exports, attract foreign direct investments and foster economic development of Georgia. However, conducted trade analyses reveal that despite some positive developments the DCFTA's effects on trade performance of Georgia are not yet significant. It is clear, that DCFTA's positive outcomes directly depend on the level of legal approximation and regulatory convergence, which considering dynamic approximation of Georgia's legislation with those of the EU, are not straightforward process. Nevertheless, Georgia based on well-determined and consecutive reforms, has to transform its economy in order to timely establish the EU compatible legislative and regulatory environment, which is crucial precondition for AA/DCFTA's positive outcomes.

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