

## THE MAJOR VECTORS OF GEORGIA'S CUSTOMS POLICY IN THE POST-CORONAVIRUS REHABILITATION PROCESS

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### Abstract

*The customs policy is one of the most effective instruments for stimulating the economy, which, through its mechanism, contributes to the realization of the competitive environment and free market principles. The modification of existing policies will have positively impact to stimulate local business sectors and facilitate the post-crisis rehabilitation process.*

*That is why, in the process of rehabilitation from the economic crisis which is caused by Coronavirus, the customs policy should ensure that the main vectors of post-crisis policy are defined, so that, country can involve in the global chain of international business with minimal losses.*

**Keywords:** *Coronavirus, Economic Crisis, Customs Policy, Modified Vectors, Economic Rehabilitation.*

### I. INTRODUCTION

The economic crisis caused by Coronavirus is a completely new challenge for the modern global economy by its essence and scale. The crisis is unambiguous by its global exposure that covered all the subjects of the world's economic civilization.

Indeed, the economic crisis caused by the pandemic, is a big challenge for Georgia and as well as the rest of the world, since our country is an active member of economic globalization.

The measures taken against Coronavirus have quickly deformed the globalization, and the countries that have transitional economy like Georgia, have impacted massive issues and problems in effective restructuration of foreign trade and customs policy.

Customs policy by its essence determines the country's ability to maintain and strengthen its positions and importance in the space of the global economy. It should be perfectly solid and constantly renewed, in order to ensure stability of the country's economy, especially in such environment of crisis. Negative economic environment caused by the pandemic has required taking measures towards to efficient management of promoting an export and substituting an import. Recommendations in this regards, should produce effective and modified vectors of customs policy for the economic recovery in the post coronavirus period.

### II. LITERATURE REVIEW

Implementation of Georgia's customs policy strategy and techniques has started since 1992, when national customs tariffs and import (customs) tax were introduced. Independence of the Country was a key point, when its economy has switched closed trading method into free one. Originally, implementation of customs policy mechanisms disregarded the characteristics of the local market, which had negative impact at early stages, and such inertia continues to this days.

This issue becomes especially relevant in the process of evaluating the critical effects of the Coronavirus and implementing customs strategy in the post-crisis period. Customs strategy should play the role of the engine of the economy, by mitigating existing problems related to international trade through strategy modifications.

In this stage, it is important to minimize implementing of ungrounded experimental practices in customs policy. The reference point for customs policy should be deep exploration of the case, analysis and evaluation of the local market, whereas, the sharing and modification of practices of other countries should a priority. Constant analysis of statistical data and modification-implementation of customs policy based on this analysis is vitally important.

### III. KEY VECTORS OF GEORGIA'S CUSTOMS POLICY AND THE EVALUATION OF POST-CRISIS PERIOD.

Globalization process has helped to strengthen demand-supply circle among the countries, ensuring their participation in international trade and foreign economic affairs. Processes following coronavirus and especially,

virus-preventing measures, forced countries to engage in economic isolation, which in their turn damaged globalization-led economic connections.

Customs policy is the best instrument of influencing economic impulses of globalization. Virus-preventing, isolation measures by random countries affected international trade in a negative way, as expected. Those economic agents who were actively involved in foreign trade were forced to limit their production and reduce goods and services they produce.

One of the core principles of Georgia’s economic policy is liberal foreign trade policy. The Country carried out reforms both on tariff and non-tariff (technical) barriers, after which Georgia has one of the most liberal foreign trade policy. This policy implies simplified foreign trade regime and customs procedures, low import tariffs and minimal non-tariff regulations.

Main objective of any regulation imposed by the government is to protect vital political, economic and cultural interests of the society, in a manner that does not hurt an economic growth. Protection of consumer rights should be one of the main objectives of regulation, referring that all the mechanisms of the regulation should coexist with the interests of the society.

Virus-preventing isolation measures by various countries are those to blame for actual economic losses. By its nature, the virus forces people to travel less and not to engage in various economic activities which in turn reduces demand on goods and services, forcing suppliers to shut down their operations to minimize costs and survive. All these, along with preventing measures, create significant shortcomings in supply chains. It is important to consider the issues of elasticity, as the demand for primary goods is highly inelastic, meaning that the increase in the price of such product affects its demand insignificantly, or does not affect the demand at all. In contrast, even slight increase in prices of goods and services that are highly elastic, such as luxury goods for instance, demand on those drops quickly. Demand-Supply elasticity is nothing else but the measure of the reaction of certain determinants of demand or supply.

**Consumer Price Index compared with the previous year’s data**

**Table №1**

Groups	CONSUMER PRICE INDICES IN GEORGIA Same month of the previous year					
	2019			2020		
	I	II	III	I	II	III
Total	101.3	100.3	101.0	100.7	100.3	100.7
Food and non-alcoholic beverages	103.2	100.1	101.3	102.3	101.3	102.0
Alcoholic beverages and tobacco	105.8	106.7	104.2	101.8	100.4	100.2
Clothing and footwear	95.5	95.4	99.6	96.5	96.9	100.5
Housing, water, electricity, gas and other fuels	100.9	100.1	99.9	100.3	100.4	99.7
Furnishings, household equipment and routine maintenance of the house	100.1	99.9	100.3	100.4	100.3	100.5
Health	100.5	100.1	99.9	100.5	100.5	100.0
Transport	99.5	100.2	98.7	99.9	99.3	99.2
Communication	99.7	99.8	100.6	99.9	99.7	100.1
Recreation and culture	100.2	97.9	107.7	95.5	98.5	100.5
Education	100.1	99.9	100.1	100.0	99.9	100.5
Restaurants and hotels	100.5	100.0	100.1	100.8	100.5	100.3
Miscellaneous goods and services	99.8	100.4	100.2	100.5	100.6	100.3

Source: National Statistics Office of Georgia

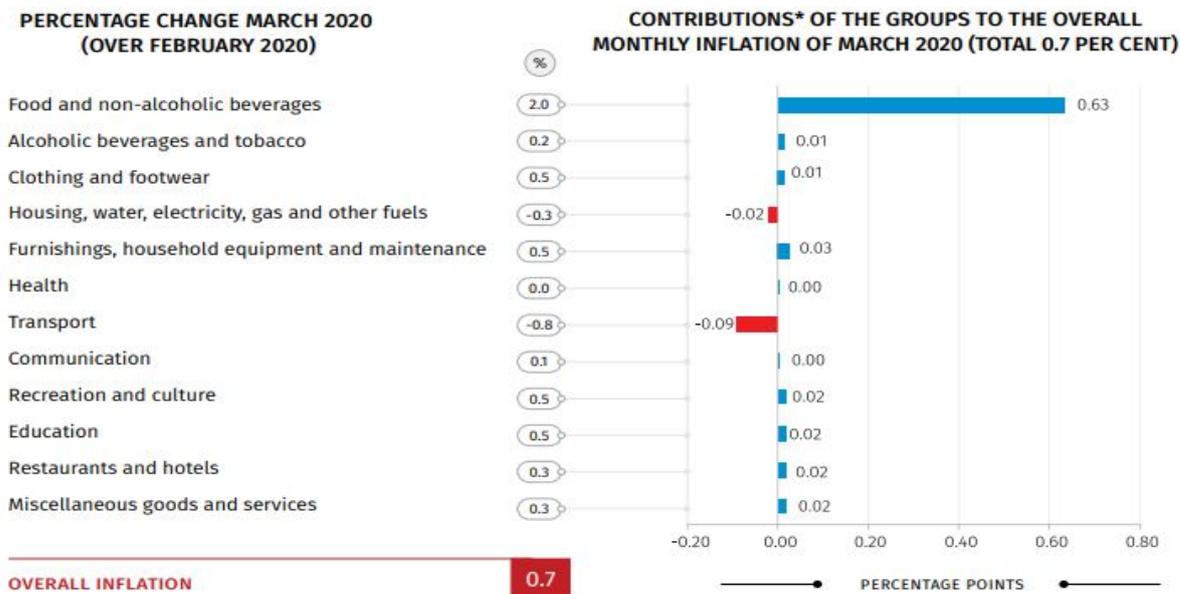
The above-mentioned table illustrates consumer price indexes for various goods and services.

The data reflects last two years and the comparisons of corresponding periods. The group of those primary goods and services that are highly inelastic consists of food and beverages. According to the data, there is no significant change in this group from the similar period of the previous year, however, if we compare their prices from March this year with the previous month, the index is increased almost by one unit. The point of it all was to highlight the fact that consumer price index is chained to monthly inflation rate. The index from March this year increased by 0,7 unit comparing to February, (March 102,0 – (February 101,3) = 0,7 %). Therefore, inflation in the corresponding group and period was 0.7%. Inflation rate for the whole basket of goods and services in March was 6.1% (increase of consumer prices from previous month).

It must be taken in consideration that calculation of inflation based on the basket of goods and services method disregards the following groups of products: food and beverages, energy carriers, administrative tariffs and transport services (certain tariffs). Unfortunately, method of such calculation has its flaws. These groups actually inflated the most and disregarding them in calculation of inflation is failing to provide the optimal indicator and the full picture of the situation. Despite the above mentioned, the following diagram clearly indicates that the largest contributor of inflation in March was the group of food and beverages, detecting the highest increase in prices among other groups.

**Percentage change in the prices of consumer goods and service groups in the consumer basket and the corresponding contribution to the overall inflation rate compared to the previous month (February-March)**

**Diagram №1**



Source: National Statistics Office of Georgia

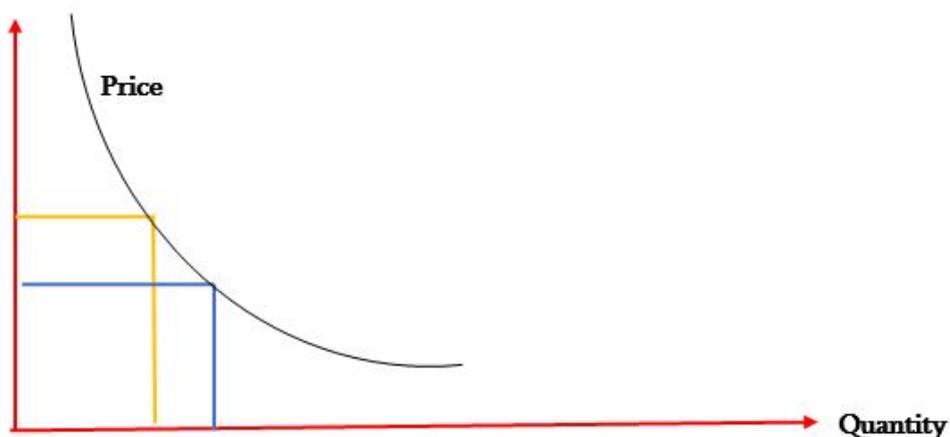
These factors indicate that, for a country like Georgia, the economic crisis caused by coronavirus has a significant impact on primary consumer goods. The main reason for this is that 80 percent of the main consumer basket depends on imports. Also negative expectations caused the depreciation of the national currency and it led to increase price on imports, which immediately reflected consumer prices. In such a situation, the society always uses all their resources for basic consumer goods such as food and they buy it at increased prices and refuse elastic goods and services.

At the same time, due to the negative expectations of the virus, the demand for primary consumer goods has significantly increased, which has also had some impact on the prices. Eventually, an increase of prices is caused by the crisis and the demand curve does not change in this circumstances and the result is that the consumer spends the same amount of revenue at an increased price but receives less goods and services. (See curve №1)

In such a situation, for a country like Georgia, it is crucial to bounce back and rehabilitate the local economic activity in order to overcome the crisis, in which customs policy should play an important role.

**Demand curve: inelastic demand, elasticity <1**

Curve №1



Note: Self-made diagram

"Georgia's involvement as an independent state in foreign trade has raised many important issues. It is very important to promote the development of local production in the conditions of such decreasing of the Georgian economy. The protection of local entrepreneurs from the excessive or unscrupulous competition of cheap imported goods plays a significant role in order to promote the development of local production."(Uridia, 2009: 224)

First of all, it is important to diagnose the economy of our country and identify the main factors of crisis symptoms. We have to ask the main questions about the negative consequences of the crisis in Georgia that was caused by coronavirus. The negative consequences of the crisis are as follows:

**Reduction of demand on the workplaces** - Economic entities in our country, that were creating jobs, were forced to stop or restrict the work process due to prevention caused by coronavirus. Therefore, they were forced to reduce their staff and even more there were cases when they have been laid off without any compensation;

**The obvious negative results of the economy that is switched to the service sector** - The service sector has been the engine of the Georgian economy for years. For example, revenues from tourism have statistically increased over the last five years. In 2018, for example, revenues from the tourism sector amounted to 3.2 billion US dollars. By 2019, that figure had risen by 47 million US dollars. Tourism is a rapidly recovering industry due to its specifics, but due to the specifics of the virus, the first punch to the world economy was taken by the tourism industry. There is no positive prognosis for the possible complete elimination of coronavirus, which indicates that the tourism sector in Georgia, as well as in the world, will have a negative impact on the dynamics in the future;

**It is necessary to encourage the small and medium business sector in this current crisis condition** - We get more stable economy when the reproduction of wealth in the form of goods and services are formed by the competition and this wealth should be consumed by our country on the one hand and also it should be used as the main means of international trade on the other hand. Today, there are very few such economic entities in Georgia, and if they are, they are part of the services of the tourism and hospitality sector;

**Deficit of local goods that could be used as a substitute of imported goods.** Our country has a negative trade balance, which indicates that our country is significantly dependent on import. By 2018, our country's negative trade balance was 5,780.8 million US dollars. By 2019, this figure was down slightly and amounted to 5306,3 million US dollars and the negative foreign trade balance amounted to 1,217.6 million US dollars in January-March of 2020. If we look at the mentioned data, we can conclude that 80% of our country's consumer basket is imported goods.

**IV. RESEARCH METODOLOGY**

It is impossible to study and realize an effective mechanism of customs policy without analyzing the current situation. It is important to assess all the components related to customs policy. In this regard, it is important to analyze the foreign trade statistics quantitatively and on the other hand, it should be also analyzed by the customs-legislative base. This allows us to develop an effective strategy and tactics for effective customs policy that will suit the local market and at the same time fully comply with international legal standards and requirements.

**V. THE INTERPRETATION OF THE RESULTS**

Customs policy is an effective tool that can be used to stimulate post-crisis economic growth, encourage exports and promote the development of industries that can substitute the import. Such positive signals in customs policy are implemented through effective tariff and non-tariff regulation measures. Tariff regulation is one of the most important effective instruments of state-customs regulation.

There is no doubt that taxes directly affect the price of goods and become an integral part of them. At the same time, it acts as an accelerator or a deterrent to the circulation of goods, depending on the purpose of the customs policy.

In order to recover the critical trauma which has been caused by the Coronavirus is to encourage the local production and this should be done by the effective customs-tariff policy.

The main goals related to customs tariff policies are:

1. Rationalization of the structure of importing and exporting goods from Georgia;
2. Protection of Georgian national and local production and products from competition with foreign products (by imposing anti-dumping duties);
3. Observance of the optimal ratio of imports and exports of products from Georgia;
4. Observing the optimal ratio of foreign exchange earnings and outflows.

It is important to define the main functions of customs and tariff policy: fiscal function and protectionist function. It is true that most of the functions of taxes are fiscal and redistributive, but customs tax has an additional protectionist function.

If the country's tariff policy is correctly defined, it is one of the main sources of the country's budget revenue growth, and therefore, the fiscal function is implemented by this way. As for the protectionist function, it involves the imposition of high rates on the customs taxation, thereby the customs tax rate increase causes the weakening of competitiveness of imported goods. It is directly proportional to the increase in fiscal function.

In the process of rehabilitating the crisis caused by coronavirus, it is the well-thought-out protectionist policy of the state that should ensure the recovery of the economy by stimulating local production and encouraging exports. Often protectionist policies are seen as a negative factor in stimulating the economy, which does not have a positive effect on the competitive environment. But this is not so, and it is the customs protectionist policy that must ensure the protection of local entrepreneurs, who often find themselves in an uncompetitive environment with imported cheap but low-quality products.

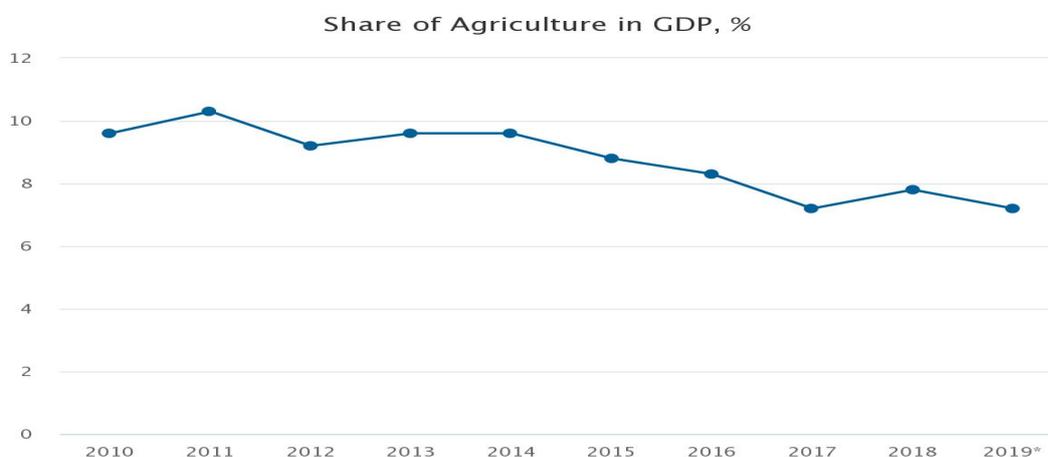
This is especially the case of agricultural products. Local agricultural products are constantly in non-competitive environment compared to imported agricultural products. This is due to several important factors: (Tsinaridze, Tssetskhladze, 2017: 9)

- 1) Produced agricultural products are quantitatively small because of low mechanization of agriculture;
- 2) Produced agricultural products are characterized by a short seasonality due to malfunction of the greenhouse;
- 3) There is a small amount of cultivated agricultural farming due to the deficit of agricultural reclamations and mechanization.

In the process of crisis rehabilitation, customs policy should provide protection of agriculture through the introduction of a customs tariff (special, especially duty) on imported agricultural products in order to stimulate agriculture through a protectionist mechanism

**The share of agriculture in GDP (Gross Domestic Product)**

**Diagram №2**



Source: National Statistics Office of Georgia

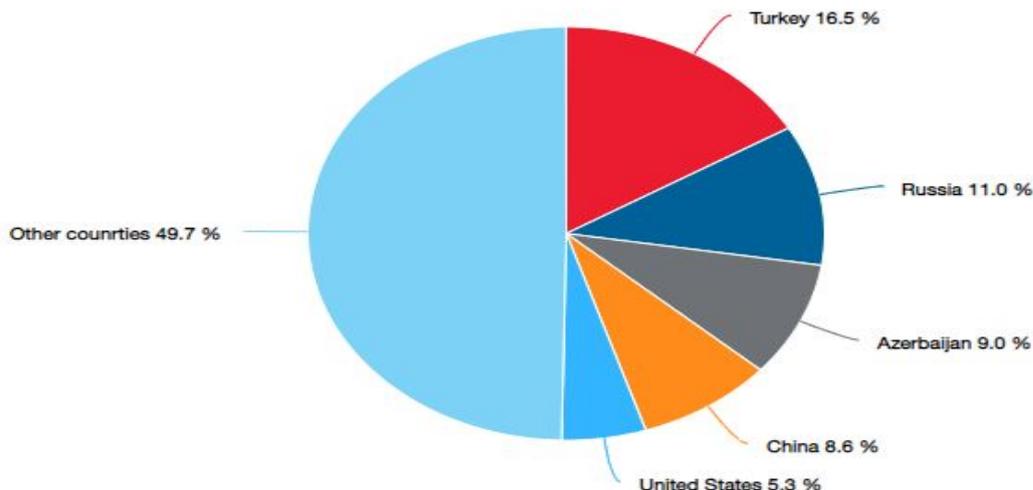
It is unfortunate that the share of agriculture in GDP has been declining significantly in recent years. While in Georgia, according to the National Statistics Office of Georgia, 41.3% of the population lives in rural areas. The main reason for this is the low incentives for agriculture, which the customs policy should provide in the post-crisis rehabilitation process.

Post-crisis protectionist policy of agriculture should be a combination of step-by-step effective measures. We need to develop a mechanism of moderate protectionism, because in the short term we have a shortage of agricultural products in the market, and as long as significant steps are not taken in this direction in order to substitute imported goods by local goods, it is dangerous to pursue an aggressive customs protectionist policy.

It is important to highlight that the export of goods from Georgia is completely freed from taxes. This policy is aimed at promoting local, national production. It gives an incentive to export from Georgia. However, there is one very important point to consider here. It should be done wisely.

**The share of the largest importing countries in total imports in January-February 2020**

**Diagram №3**



In the share of the largest importing countries, the top three from neighboring countries look like this: Turkey, Russia, Azerbaijan, followed by China and the United States. Georgia has free trade agreements with Turkey, Russia, Azerbaijan and China, which in itself implies the absence of customs tariffs or exemptions for some groups of goods.

Free trade agreements need to be revised in post coronavirus rehabilitation process because Georgia has much more to give or lose despite the fact that according to the agreement terms we have equal force ratio.

The main reasons for the above-mentioned negative factors are: 1) Georgia has much lower average tax rate compared to countries or unions with which our country has a free trade agreement or compared to countries that are our major trading partner; 2) Georgia does not have an advantage over these countries in terms of economic development.

**(Country / Economic Zones Rank by Customs average tariff MFN%)**

**Table №2**

№	Country	2012	2013	2014	2015	2016	2017	2018
6	<b>Georgia</b>	1,5	1,5	1,5	1,5	1,5	1,5	1,45
11	USA	3,4	3,4	3,5	3,5	3,5	3,4	3,45
19	Ukraine	4,5	4,5	4,5	4,5	4,5	4,5	4,51
25	<b>European Union</b>	5,5	5,5	5,3	5,1	5,2	5,1	5,23
27	Moldova	4,6	4,6	4,6	5,5	5,4	5,3	5,35
39	Kazakhstan	9,5	9,1	8,6	7,8	6,9	6,5	6,37
41	Armenia	3,5	3,5	3,7	6,1	6,2	6,0	6,5
48	<b>Russia</b>	9,9	9,7	8,4	7,8	7,2	6,7	6,79
72	<b>China</b>	9,6	9,9	9,6	9,9	9,9	9,8	9,77
84	<b>Turkey</b>	9,6	10,8	10,7	10,8	10,9	10,9	10,73

Source: World Trade Organization

These two components are the main factors that require another consideration. The first reason, named after the protectionist customs policy strategy, is to determine the effective customs tariff that will ensure the protection and stimulation of domestic production, resulting in economic growth.

If we look at the data in customs policy, there are also important measures to be taken in relation to the customs tax rate. With major trading partners such as Turkey, Russia, China, and the United States, our country has a much lower average tax rate. The free trade agreement with these countries and the customs tax rate should be revised and the customs tax rate should be increased. It is true that the customs tax will make imports more expensive and therefore it will be reflected in the consumer price (due to the indirect nature of the customs tax). But it will be an important step towards stimulating local production. The low customs tax somehow stimulates imports and, if maintained in the long run, makes the country dependent on imports. The main reason is the fact that our country's goods and services production costs are higher compared to developed countries costs. (technological upgrades, etc.) and therefore, the local production is in non-competitiveness condition compared to imported goods and services in terms of the consumer's price. Our country's economy is somehow "accustomed to imports", which is why local businesses or community groups have no incentive to produce goods and services, thus at least providing a local market.

In the post-crisis period, the main focus is on filling the food basket with local products. In this regard, it is important to introduce an already experienced agrarian customs tax in the European Union. It will directly protect the agro resources included in the food basket from the non-competitive environment. It will have a direct impact on imported agro-resources and will shape the pricing policy in the food market. This will stimulate local agricultural production to show their ideas and capabilities and contribute to import substitution measures.

This should be done in parallel with significant tax breaks, which will be a substitute for subsidies for the entrepreneur. This means that the state will not directly subsidize significant enterprises operating in agriculture, but will give them tax benefits in the short term until enterprises move to full load of organizational resources and sales of manufactured products.

The state's direct subsidy policy, especially in the agricultural sector, has not had a significant effect on Georgia. The main reason for this is that subsidies are often issued for projects that do not have in-depth research on their possible promising profitability. Therefore, tax benefits will be more effective especially in the process of production and then in the sales process.

The positive impact of transit and re-export as custom procedures (commodity operation) will be great during the post-coronavirus rehabilitation period. By active actions, our country should further strengthen international economic and customs connections, such as the transit hub. Because re-export and transit, in its specificity, contribute to the growth of foreign economic relations, export of services, in particular, the development of trade and monetary relations between countries, which has significantly reduced by the pandemic processes of coronavirus. The intensification of the re-export customs procedure should promote the development of Georgian business actors that will implement international business processes themselves, such as buying cotton in Asia at the best deal, importing goods and then selling it at affordable prices to any European country. Such post-crisis period, it is very important for the business actors to get the support from Government: first, it is crucial to restore international economic relations that is reduced after coronavirus and second, Georgian business actors that are engaged in indirect production processes will gain significant economic benefits using above mentioned mechanisms.

The mechanism for stimulating Georgian business actors to participate in the re-export event may be, for example, the exemption from the service fee related to the re-export procedure for Georgian firms that sell foreign goods in international markets through our country.

It's important to be brought in attention the establishment of greenhouses in the production of agricultural products. On the one hand, it will increase the seasonality of agricultural productivity, improve the social background by increasing employment and at the same time significantly increase the quality of manufactured products. In addition, the greenhouse has the ability to quickly fill a deficient food basket. In this regards, it is important to establish significant customs benefits for raw materials related to the arrangement of greenhouses, technologies, so that farmer can afford to run a greenhouse at low cost possible.

It is important for the state to assume the role of the main mediator between local entrepreneurs and consumers in the international market. This means that it is important for the state to set up the same agricultural processing facilities that will receive raw materials from local entrepreneurs, process them and supply them to the international market. Consumers of such facilities will be mostly small and medium-sized businesses. This is the segment of business actors that create the most jobs in the economy. Large firms are already processing and delivering their products to the international market, so their share in processing facilities will be minimal.

## VI. CONCLUSIONS

Finally, it can be said that the post-crisis period will be difficult for the world economy, including Georgia. With the right consistent policy, it will be possible to minimize the economic shock caused by the coronavirus that our country has received. The virus is named pandemic, and sciences assures that it will prolong or get seasonal character in the long run, indicating that the crisis caused by it will hit the world and our country in the future back again. Therefore, each of the above-mentioned customs policy-making actions requires a timely and tangible response. These measures are not a customs policy axiom and should be modified in parallel with the changing economic and social situation in the country and in the world.

In the process of regional integration, it is necessary to reconcile moderate protectionist policies and liberalization. The attention should be paid to regulatory measures when we are talking about customs policy. Customs tax should not only perform a fiscal function and thus shape budget revenues, but it should also play the role of regulator and controller and thus protect the national market from the expansion of foreign goods. The main goal of our country should be to develop a customs policy that maintains and strengthens Georgia's positions in the international economic space.

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