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Georgia in the World Merchandise Trade: Main Trends and Problems of Development

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Abstract

Foreign trade is the main factor in the country's integration into the world economic system. It promotes the socio-economic development of states, especially developing countries. After the restoration of state independence, Georgia actively cooperates with different countries within the framework of bilateral and multilateral agreements. Its foreign trade activity is based on a high level of openness of the economy and liberal policy, features of the market economy and new vectors of development. Georgia has been a member of the World Trade Organization since 2000 and has one of the most liberal and competitive trade regimes across the world. Georgia's foreign trade turnover has a cyclical growth pattern with a combination of periods of its fall. Over the entire post-Soviet period, the country has a negative trade balance and a high dependence on imports. Export characterizes a high degree of concentration of geographical structure and low level of diversification. The article analyzes the current state of Georgia's foreign trade, shows the main indicators of the country's foreign trade for the period of 1994-2014, and examines the main trends in its development and the importance of export diversification to improve the efficiency of foreign trade.

Keywords: foreign trade, merchandise, export, import, Georgia

1. Introduction

After the collapse of the Soviet Union, Georgia moved to a new stage in its historical development, characterized by a high degree of freedom and a liberal economic policy. In 2018, according to the Index of Economic Freedom, Georgia ranks 16th among 180 countries and is part of a group of mostly free states. Liberal foreign trade policy is one of the major principles of the economic policy of Georgia. The Government of Georgia has implemented reforms in the tariff policy. As a result, nowadays Georgia has one of the most liberal foreign trade policies in the world, which implies the assistance of foreign trade regimes and customs procedures, low import tariffs and minimal non-tariff regulations (MESD).

Foreign trade is the main factor in the country's integration into the world economic system. Export contributes to the increase in foreign exchange earnings and stimulates the social and economic development of the state. As G. Haberler (1970) noted, "International trade has made a tremendous contribution to the development of the less developed countries in the nineteenth and twentieth centuries, and can be expected to make an equally big contribution in the future if it is allowed to proceed freely ". In this regard, the main purpose of this work is to analyze the trends in the development of Georgia's foreign trade, determine its place in the world trade of goods and the opportunities for its further development based on of export diversification .

Literature rieview

The internationalization of production has been greatly accelerated and the international division of labor has deepened under the influence of globalization and scientific and technological progress (Korganashvili L. 2017, 2016). As a result of this international trade flows have increased. The need to include countries in international trade is explained by different

theories. The role of foreign trade in the pursuit of wealth of the nation is highly evaluated by the mercantilists (Magnusson 1994). The starting international trading axioms inherent in classical theories (Smith 1986 [1776], David Ricardo 1951), which, despite a number of assumptions, explain the benefits of trade. Fundamentals of the reasons that determine the direction and structure of international trade flows, as well as the possible advantages in the international exchange, are laid by E. Heckscher and B. Ohlin (Heckscher 1919, 2007, Ohlin 1933). According to their theory, a country will export goods that use its abundant factors intensively, and import goods that use its scarce factors intensively. In the two-factor case, it states: A capital-abundant country will export the capital-intensive good, while the labor-abundant country will export the labor-intensive good. Heckscher-Ohlin theory refined P. Samuelson (HOS-Heckscher-Ohlin-Samuelson Theory) (Suranovic 2010) and W. Stolper (Stolper-Samuelson Theorem) (Stolper&Samuelson 1941).

The standard model of international trade unites the various theories, developing the fundamental position of the classical theories. It is based on the concepts of the limit values and the general equilibrium of the economic system. It provides mathematical and graphical interpretation of international commodity exchange, and shows the real impact of international trade on the economies of individual countries (Edgeworth 1925, Marshall 1979, Haberler 1936), etc.

The alternative theory of international trade is critical to achieve reinterpreted predecessors and offered original interpretation of the participation of national economies in the international exchange of goods. Among these theories following should be noted: The trade theory based on economies of scale (Krugman 1981, Krugman&Obstfeld 1992, Lancaster 1980 et al.), The theory of technological gap (Posner 1986), The theory of a product life cycle (Vernon 1970), The theory of international competition (Porter 1986) and others. Since the second half of the XX century, dynamic comparative advantages became relevant. This question was studied by Krugman (1987), Grossman and Helpman (1989), Redding (1997) and others.

Although there are many theories of international trade, none of them can fully explain the nature of international trade. And there is ample empirical evidence that recognize the validity of the theory of comparative advantage (Bernhofen&Brown 2005, Schott 2004, Uchida & Cook 2004, Krugman&Obstfeld 2003). Moreover particularly noteworthy is the fact that most of the principles of the World Trade Organization (WTO) is based on the theory of comparative advantage (Root 2001). Currently, comparative advantages are used to assess the country's competitiveness in international trade (Korganashvili L. 2017, 2016,). .

Research methodology

The theoretical and methodological basis of the work constitutes the fundamental tenets of the theory of international trade. Well-known scientific methods were used for the study: statistical, comparative, deduction and induction, analysis and synthesis, and etc. Informational and empirical basis of the study is constituted by statistical, informational and analytical data of various international and national organizations, research papers, online resources, and etc.

The effectiveness of foreign trade is calculated as the ratio of exports to imports. If this ratio - efficiency coefficient is greater than 1, then the trade can be considered effective. On the other hand, the import dependence of the trading partners is calculated as the ratio of imports to exports. The country will be considered dependent on the other, if the ratio coefficient of import dependence is less than 1.

Comparative advantages of Georgia on certain goods are valued by index Balassa (Balassa 1965), which is calculated according to the formula

$$RCA_{ij} = (X_{ij} : X_{it}) / (X_{wj} : X_{wt})$$

where RCA_{ij} is Revealed Comparative Advantage Index, $X_{ij}$and $X_{it}$are the values of country i's exports of product j and world exports of product j and where X_{it} and X_{wt} refer to the country's total exports and world total exports. A value of less than unity implies that the country has a revealed comparative disadvantage in the product. Similarly, if the index exceeds unity, the country is said to have a revealed comparative advantage in the product.

Main trends in the development of Georgia's foreign trade

After the collapse of the Soviet Union, Georgia actively cooperates with different countries within the framework of bilateral and multilateral agreements. In 2017, the geography of its trade covered 140 countries. According to preliminary data, in 2017, the foreign trade turnover of goods amounted to $10707.4 million, including exports – $2728.0 million, imports – $7979.4 million (75%). Compared with 2016, foreign trade turnover increased by 13.8%, exports by 29.1% and imports by 9.4% (Geostat).

Foreign trade of Georgia is developing in the conditions of globalization. Its main development trends are followings:

The cyclical nature of the development of foreign trade turnover: a combination of growth with periods of its fall. For example, the growth cycles cover 1994-1997, 2000-2009 and so on (table 1, Growth rate to previous year, %).

Permanent negative trade balance and high dependence on imports. In 2017, the deficit was $5254.7 million – 49.0% of all of trade turnover (Geostat). Compared to 2016, it increased by $73.2 million (1.4%). This is the highest volume of trade deficit, but its highest share in foreign trade turnover was in 1998 – 64.7%. The peak of the share of imports to turnover was observed in 1998 (82.4%), to GDP in 2017 – 52.6% (Table 1).

Low share of exports both in foreign trade turnover and in GDP. In the foreign trade turnover of Georgia, exports with the highest share were present in 1994 – 36.1%, and in relation to GDP in 2017 – 18.0%.

In 2017, the share of foreign trade turnover reached 70.6%, and in 1994 it was 16.7% (Table 1).

Change in the share of groups of countries. In 1995, the CIS accounted for 62.5% of Georgian exports and 40.1% of imports, in 2005 these figures were 47.0% and 40.0% respectively, and in 2017 – 43.3% and 29.6%. The share of the European Union has also changed. If in 2005 the EU countries accounted for 25.0% of exports and 29.7% of imports, in 2017 these figures were 23.7% and 27.5%. On June 27, 2014, the European Union and Georgia signed the Association Agreement, which includes the Deep and Comprehensive Free Trade Area (AA / DCFTA), which provides preferential trade relations. Despite this, the CIS countries occupy an important place in the foreign trade of Georgia (Korganashvili, 2016)..

High degree of concentration of the geographic structure of Georgia's foreign trade: in 2017, 3 main trade partners accounted for 34.7% of turnover, for 5-48.2% and for 10-66.7%. As for exports, these figures were 30.0%, 44.5% and 67.4% respectively, and for imports – 36.2%, 44.5% and 66.5% (Geostat).In 2016, the market concentration index (HH-Herfindahl-Hirschman index) was 0.06, and in 2012 it was 0.04 (WITS, 2016).

Low level of diversification of exports and imports: 10 commodity items account for 63,3 % of country's exports and 64.7% of imports (Geostat). In 2017, the first place in the commodity structure of Georgia's exports is occupied by copper ore and concentrates – 15.4%, the second place is ferroalloy – 11.3%, followed by motor cars – 8.6% (in 2013 their share was 24.2%. Georgia is not a producer of cars, therefore, a high share of this commodity position in the country's exports testifies to a significant volume of re-export operations), wine from fresh grapes – 6.3%, medicaments put up in measured doses – 5.2%, etc. In the commodity structure of imports in the first place are petroleum and petroleum oils - 8.7% of the total import of the country. The following positions are occupied: motor cars – 5.9%, petroleum gases and other gaseous products – 4.4%, medicaments put up in measured doses – 4.3%, copper ores and concentrates – 4.2% and etc. In 2016, the index of Export Market Penetration for export was 2.41, in 2015 - 2.57 (WITS, 2012-2016).

A decline in the share of high-tech exports in manufacturing exports: in 2002, high-technology exports (% of manufactured exports) accounted for 41.1% of manufacturing exports, but in 2016 it declined to 3.9%. 38.35% of Georgia's exports and 53.54% of imports are consumer goods, 23.95% and 14.71% are intermediate goods, 32.97% and 9.62% are raw materials, 3.67 and 21.72% are capital goods. A small share of capital goods causes a low level of technological development (WB).

Increasing the level of liberalization of foreign trade policy. Georgia has been a member of the World Trade Organization (WTO) since 2000 and the Liberal foreign trade policy is one of the major principles. The Government of Georgia has implemented reforms in the tariff policy. As a result, nowadays Georgia has one of the most liberal foreign trade policies in the world, which implies the assistance of foreign trade regimes and customs procedures, low import tariffs and minimal non-tariff regulations (MESD). In 2015, compared to 2002, its average tariffs for the countries with the most favored nation (MFN) for all goods decreased from 9.65% to

0.87%, including agricultural products from 12.53% to 7.1 % and non-agricultural from 9.44% to 0.46%. In 2015, the average of preferential tariffs were 0.72%, 5.88% and 0.38%, respectively (Table 2).

Table 1. The main indicators of Georgia's foreign trade in merchandise, 1994-2017

Years	million current US$	Share in Turnover, %	Growth rate to previous year, %	Share in GDP, %

	Export	Import	Turnover	balance	Export	Import	balance	Export	Import	Turnover	balance	Export	Import	Turnover
1994	151,2	268,0	419,8	-116,8	36.1	63.9	27.9	-	-	-	-	6.0	10.7	16.7
1995	151,2	391,6	542,8	-240,4	27.8	72.2	44.3	100.0	146.1	129.3	205.8	5.6	14.5	20.1
1996	198,8	686,7	885,5	-487,9	22.5	77.5	55.1	131.5	175.4	163.2	203.0	6.4	22.2	28.6
1997	239,8	943,5	1183,3	-703,7	20.3	79.7	59.5	120.6	137.4	133.6	144.2	6.8	26.9	33.7
1998	189,0	883,2	1071,2	-694,2	17.6	82.4	64.8	78.8	93.6	90.5	98.6	5.2	24.5	29.7
1999	240,7	622,6	863,3	-381,9	27.9	72.1	44.2	127.4	70.5	80.5	55.0	8.6	22.2	30.8
2000	324,0	709,0	1033,0	-385,1	31.4	68.6	37.3	134.6	113.9	119.6	100.8	10.6	23.2	33.8
2001	317,6	753,3	1070,9	-435,7	29.7	70.3	40.7	96.2	107.6	104,0	113.1	9.9	23.4	33.3
2002	347,8	731,4	1079,2	-383,6	32.2	67.8	35.5	109.5	97.3	100.8	88.0	10.2	21.5	31.8
2003	465,3	1141,1	1606,4	-675,8	29.0	71.0	42.1	133.8	156.0	148.9	176.1	11.7	28.6	40.2
2004	646,9	1847,9	2494,8	-1201,0	25.9	74.1	48.1	139.0	161.9	155.3	177.7	12.6	36.1	48.7
2005	866,7	2490,9	3357,6	-1624,2	25.8	74.2	48.4	134.0	134.8	134.6	135.2	13.5	38.9	52.4
2006	993,1	3681,2	4674,3	-2688,1	21.2	78.8	57.5	114.6	147.8	139.2	165.5	12.8	47.4	60.2
2007	1240,2	5216,7	6456,9	-3976,5	19.2	80.8	61.6	124.9	141.7	138.1	147.9	12.2	51.3	63.5
2008	1497,7	6058,1	7555,8	-4560,4	19.8	80.2	60.4	121.8	116.1	117.0	114.7	11.7	47.3	59.0
2009	1133,6	4500,2	5633,8	−3366,6	20.1	79.9	59.8	75.7	74.3	74.6	73.8	10.5	41.8	52.3
2010	1677,5	5257,1	6934,6	−3579,6	24.2	75.8	51.6	148.0	116.8	123.1	106.3	8.1	25.3	33.4

2011	2186,7	7038,4	9225,1	−4851,7	23.7	76.3	52.6	130.4	133.9	133.0	135.5	9.0	28.9	37.9
2012	2376,2	8036,9	10413,1	−5660,7	23.3	76.7	54.4	108.7	114.2	112.9	116.7	9.1	30.7	39.8
2013	2909,5	8011,6	10921,1	−5102,1	26.6	73.4	46.7	122.4	99.7	104.9	90.1	10.8	29.9	40.7
2014	2860,7	8593,3	11454,0	−5732,6	25.0	75.0	50.0	98.3	107.3	104.9	112.4	10.0	29.5	39.3
2015	2204.7	7300.3	9505.0	-5095.6	23.2	76.8	53.6	77.1	85.0	83.0	88.9	15.8	52.2	68.0
2016	2113.1	7294.6	9407.7	-5181.5	22.5	77.5	55.1	95.8	99.9	99.0	101.7	14.7	50.7	65.4
2017*	2728.0	7982.7	10710.6	-5254.7	25.5	74.5	49.1	129.0	109.4	113.8	101.4	18.0	52.6	70.6

Source: The table is compiled and calculated according to the annual "Statistical Yearbook of Georgia" and "External Trade of Georgia", 1995-2017.

Table 2. Average tariffs for the import of products in Georgia

Product group	Tariff type	2002	2006	2010	2015
All products	Average of MFN tariffs	9.65%	8.68%	0.68%	0.87%
	Average of preferential tariffs	9.65%	8.16%	0.65%	0.72%
Agricultural	Average of MFN tariffs	12.53%	12.65%	9.16%	7.1%
	Average of preferential tariffs		12.05%	8.7%	5.88%
Non-agricultural	Average of MFN tariffs	9.44%	8.42%	0.07%	0.46%
	Average of preferential tariffs		7.91%	0.06%	0.38%

Source: ITC,Market Access Map.
http://www.macmap.org/CountryAnalysis/AverageTariffResult.aspx?country=SCC268|Georgia&bysection=0

The low level of Georgia's export diversification is one of the most acute problems of the country's economy, as it indicates the low efficiency of its foreign trade. Diversification of exports is directly related to the diversification of the national economy. Therefore, first of all, its progressive diversification is necessary: the main emphasis should be made on the development of industries with a high share of added value. At the same time, one should not limit oneself to exporting material and technical goods, special attention should be paid to trade in services and technologies. Diversification in this direction is of great importance for the Georgian economy, since the share of services in GDP in the country is about 2/3 (Korganashvili, 2017, 2014).

For the development of trade in technology requires a knowledge economy, the importance of which has increased greatly. This is due to the effect of the following trends: technological globalization and increasing role of human capital; the growth of innovation as an organized activity; the emergence of the "New Economy" on the basis of the revolution in information and communication technologies; development of innovative infrastructure and innovation management system at the national and international levels; mass and accessibility of higher education; the complication of the system "science-technology-production-consumption", etc. (Korganashvili L. 2015, 2014).

Georgia's integration into world trade in merchandise

Georgia is a small country and its role in world trade is insignificant. In 2016, the share of Georgia's exports and imports in world exports and imports of goods amounted to 0.01 and 0.04%.In terms of their volume, the country took 128th and 106th places (WTO). In 2017, five of the main trading partners were Turkey ($1,589,377.7 th. – 14.8%), Russia ($118,367.7 million – 11.1%), China ($939,518.6 th. – 8.8%), Azerbaijan ($881,904.2 th. – 8.2%) and Ukraine ($566,601.4 th. – 5.3%). Russia ($394,712.4 th. – 14.5%), Azerbaijan ($ 272172.5 th. – 10.0%), Turkey ($211.67 million – 7.9%), Armenia were the main export trading partners (7.7%) and China ($207218.0 th. – 7.6%), on imports – Turkey ($1372802.7 th. – 17.2%), Russia ($394788970.2 th. – 9.9%), China ($732,292.9 th. – 9.2%), Azerbaijan ($609721.8 thousand – 7.6%) and Ukraine ($ 445147.0 thousand – 5.6%) (Geostat).

The degree of integration of a country into world trade can be estimated by the Enabling Trade Index (ETI). It assesses the extent to which economies have in place institutions, policies, infrastructures and services, facilitating the free flow of goods over borders and to their destination. ETI is calculated using four sub-indexes: Sub-index A – market access; Sub-index B – border administration; Sub-index C – infrastructure; Sub-index D – operating environment. Sub-index A measures the extent and complexity of a country's tariff regime as well as tariffs. There are two pillars in this sub-index. Sub-index B measures border administration of a single pillar, which assesses the efficiency and transparency of the border administration. More specifically, it captures efficiency, transparency and costs associated with importing and exporting goods. Sub-index C assesses the availability and quality of transport infrastructure of the country, associated services, and communication infrastructure, necessary to facilitate the movement of goods within the country and across the border. Sub-index D consists of a single pillar, which has a significant impact on the quality of its products, imports, and trade and transport merchandise to do business. According to the Enabling Trade Index in 2016, Georgia ranks 41st among 136 countries, and in 2014 it was on the 46th place among 134 countries. Under sub-index A Georgia is on the 15th place, sub-index B – 39th, sub-index C – 73rd and sub-index D – 33rd (Table 3).

Table 3. Enabling Trade Index, 2016

	Rank	Score
Enabling Trade Index	41	4.8
Subindex A: Market access	15	5.2
Pillar 1: Domestic market access	9	5.9
Pillar 2: Foreign market access	33	4.6
Subindex B: Border administration	39	5.3
Pillar 3: Efficiency and transparency of border Administration	39	5.3
Subindex C: Infrastructure	73	3.8
Pillar 4: Availability and quality of transport Infrastructure	76	3.3
Pillar 5: Availability and quality of transport services	98	3.6
Pillar 6: Availability and use of ICTs	65	4.6
Subindex D: Operating environment	33	4.8
Pillar 7: Operating environment	33	4.8
Weforum. The Global Enabling Trade Report. 2016, pp.136-137 http://www3.weforum.org/docs/WEF_GETR_2016_report.pdf		

The most problematic factors for importing are: high cost or delays caused by international transportation, tariffs and non-tariff barriers, high cost or delays caused by domestic transportation, burdensome import procedures, inappropriate telecommunications infrastructure, domestic technical requirements and standards, corruption at the border. In turn the most problematic factors for exporting are: identifying potential markets and buyers, inappropriate production technology and skills, technical requirements and standards abroad, access to trade finance, difficulties in meeting quality/quantity requirements of buyers, access to imported inputs at competitive prices, burdensome procedures at foreign borders, high cost or delays caused by international transportation, rules of origin requirements abroad, corruption at foreign borders, high cost or delays caused by domestic transportation and tariff barriers abroad (Weforum, 136). For the further development of Georgia's foreign trade and its full-fledged integration into world trade in goods, first of all these problems should be resolved.

Table 4 shows the estimates of efficiency of foreign trade of Georgia and its import dependence on top trade partners in 2017. The effectiveness of foreign trade is the ratio of exports to imports and import dependence on trading partners shows

the ratio of imports to exports. As seen in Table 4, from 10 major trading partners of Georgia only trade with Bulgaria can be considered effective. Georgia has a strong import dependence on Germany, Turkey and China.

Table 4. Efficiency of Georgia's foreign trade and its dependence from imports of top trading partners, 2017

Countries	Exports, thsd. US Dollars	Imports, thsd. US Dollars	Export/Import*	Import/Export*
Total	2727971.5	7979435.0	0,34	2,92
Of which:				
Turkey	216567.1	1372802.7	0,16	6,34
Russia	394712.4	788970.2	0,50	2.00
China	207218.0	732292.9	0,28	3,53
Azerbaijan	272172.5	609721.8	0,4	2,24
Ukraine	124449.8	445147.0	0,45	3,58
Armenia	208701.5	281137.6	0,74	1,35
Germany	45361.6	433330.0	0,10	9,55
United States	121794.2	267746.1	0,45	2,20
Bulgaria	178827.4	155551.2	1,15	0,87
Italy	69278.0	217299.6	0,32	3,14
Other countries	888888.9	2675435.9	0,33	3,01
* Calculated by the author. Source: http://geostat.ge/cms/site_images/_files/english/bop/FTrade__2017_ENG-with%20cover.docx.pdf				

Despite the negative trends in the development of Georgia's exports, the country has the potential to increase it. As shown in Table 5, Georgia has revealed comparative advantages for such products as Minerals, Food Products, Vegetable, Metals, Transportation and Chemicals.

Table 5. Revealed comparative advantages of exported goods of Georgia

Products	Georgia $X_{ij} : X_{it}$	World $X_{wj} : X_{wt}$	RCA_{ij}
Animal	2.15	2.20	0.98
Vegetable	9.20	3.44	2.67
Food Products	17.52	3.40	5.15
Minerals	9.36	1.52	6.16
Fuels	2.70	11.01	0.25
Chemicals	10.17	9.14	1.11
Plastic or Rubber	1.24	4.34	0.29
Hides and Skins	0.26	0.73	0.36
Wood	0.95	2.47	0.38
Textiles and Clothing	3.18	4.50	0.71
Footwear	0.15	0.92	0.16
Stone and Glass	2.20	4.94	0.45
Metals	16.85	6.91	2.44
Mach and Elec	2.50	25.11	0.10
Transportation	20.56	10.13	2.03
Miscellaneous	1.02	9.25	0.11
Calculated by the author. Source: WITS http://wits.worldbank.org/CountryProfile/en/GEO, http://wits.worldbank.org/CountryProfile/en/Country/WLD/Year/2014/TradeFlow/Export/Partner/all/Product/90-99_Miscellan			

Conclusions

The processes of liberalization of the economy in Georgia significantly change the nature of foreign trade relations. The country is gradually improving the terms of trade, but there are serious problems in this area. Among them, one should note the strong dependence on imports, the irrational commodity structure, the decrease in the share of capital goods, the high level of concentration, the low level of diversification, the underdeveloped infrastructure, etc. In this regard, Georgia should optimize the structure of the economy, find resources to stimulate exports and implement policies substitution of imports, increase of innovative potential, etc. Addressing the trade deficit and increasing exports should become one of the main tasks of Georgia's economic development. The country needs a development strategy that will reduce the impact of negative external factors and increase the level of independent development.

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