

PARLIAMENTARY ELECTIONS AFTERMATH IN GEORGIA:

Implications for foreign investors after a contested vote

3 November 2020

On October 31, Georgian voters went to the polls to elect the country's new parliament for the upcoming legislative term. While the ruling Georgian Dream party (GD) emerged victorious and is on course to claim an all-out parliamentary majority, opposition parties - contradicting the largely positive assessments of international observers – have so far rejected the results and refused to participate in the second round of the election. With Georgian politics entering a new period of uncertainty overshadowed by the severe impact of the coronavirus crisis, below we take a more detailed look at the election results, the aftermath of the contested vote, as well as likely scenarios and their impact for business.

ELECTION RESULTS¹

For the first time, Georgians cast their ballots in a newly introduced election system: 120 of the 150 seats being distributed via proportional representation and the remaining 30 via newly-drawn electoral districts across the country. As expected, the ruling Georgian Dream party, which has been in government since 2012, has maintained its position as the largest political force in the country, posting its third consecutive victory over rival United National Movement, led by former President Mikheil Saakashvili:

- With 100% of the votes counted, Georgian Dream received 48.2% of the popular vote, securing 61 of the 120 proportionally distributed seats,
- It expanded its electoral base by more than 70,000 votes (to almost 927,000) in comparison with 2016.
- In addition, Georgian Dream candidates came first in 29 of the 30 electoral districts, securing 14 seats in the first round of the vote, while the remaining 16 races will proceed with a run-off on November 21.
- The party already has 75 of the minimum 76 needed to form a parliamentary majority and it is poised to strengthen its advantage in the second round of the vote. The new election system also includes a capping mechanism limiting the majority party's seats to 90².

¹ See table for details on the page 2.

² For further explanation on this capping system, see [here](#)

While international observers, including those of the OSCE’s monitoring mission, declared that “overall, fundamental freedoms were respected” in the vote, an alliance of opposition parties led by the United National Movement (which had been targeting a leading role in a coalition government) has rejected the outcome and accused the country’s Central Election Commission of falsifying the election results on the GD’s behalf. Subsequent demonstrations took place on November 1 and November 2 in Tbilisi, with a mass opposition rally scheduled for the end of this week.

ELECTION RESULTS

Political Party	Popular Vote (%)	Party List MPs	Single-District MPs
Georgian Dream – Democratic Georgia (GD)	48.23	61	14
United National Movement (UNM)	27.16	35	0
European Georgia	3.78	5	0
Lelo for Georgia	3.16	4	0
Strategy Builders	3.15	4	0
Alliance of Patriots of Georgia	3.14	4	0
Girchi	2.89	4	0
Citizens	1.33	2	0
Labour Party	1	1	0
Runoff Seats			16
Total		120	30

Turnout: 56.1% (first round), Source: CEC Georgia

The election came in the aftermath of a tense few months for Georgia. In the summer of 2019, the ruling party faced months of public scrutiny after allowing Russian Communist Party MP Sergey Gavrillov to address the Georgian Parliament. Gavrillov’s speech (in Russian) triggered large-scale protests in Tbilisi, prompting President Putin to temporarily suspend all flights between Russia & Georgia, adding further tension to the two countries’ relationship.

Another wave of mass demonstrations was triggered last November, following the GD’s failure to renew the Georgian electoral system and introduce a more proportional one instead³. Although strains between the opposition and the Government remained high, the deadlock eventually ended with a Western-brokered agreement in March this year, resulting in the new election system. However, tensions were reignited over

³ Under the previous election system, 73 of the 150 MPs were elected through single-mandate districts. In 2016, the Georgian Dream received 48.7% of the popular vote but ended up controlling 115 of the 150 seats.

unresolved political issues, such as the allegedly authoritarian practices of the ruling party, as well as over the Government's handling of the coronavirus pandemic and the subsequent economic crisis.

A number of opposition parties which passed the 1% electoral threshold and could have been potential coalition partners to UNM have also denounced the election results. Following several consultations on November 2, all key opposition parties announced that they will neither take up their parliamentary mandates, nor participate in the second round of the elections and they will instead demand snap elections.

The first session of the new legislature is set to convene on December 20. According to Georgian law, if there is a minimum of 76 of the 150 newly elected MPs present during the session, the new parliament can be declared legitimate. However, should the opposition parties boycott not only the first session but (at least) a considerable part of the next legislative term, Georgia could face severe concerns over the actual legitimacy of the parliament, while opposition-driven protests could advance to a larger scale. Among the potential consequences of such a sequence of events is a negative impact on the country's business climate: a political crisis over the legitimacy of (a Western-brokered) election could undermine investor confidence in the Georgian economy and jeopardise foreign investment.

At the time of writing, it is yet to be seen if the unrest triggered by the opposition will escalate significantly. While Georgia has a track record of contested elections (the 2003 parliamentary elections that resulted in the so-called Rose Revolution and the 2016 parliamentary vote that was also contested - but not entirely refused - by the UNM over alleged vote rigging), the fact that international observers and Georgia's main international partners, particularly the EU and the US, accepted the overall election results suggests a potential settlement will be reached.

Nonetheless, the rising level of political polarization in Georgian society is a reason for future concern. With the competing sides refusing to find common ground, we expect Georgia's Western allies to step in and mediate, with the Georgian Dream likely to emphasize its commitment towards democracy by newly proposed constitutional amendments "to strengthen the party system" and transitioning to a fully proportional election system by 2024.

WHAT CAN INTERNATIONAL INVESTORS EXPECT MOVING FORWARD?

The aftermath of the first round of the elections indicates escalating tensions on the domestic political arena, with potential but not immediate concerns for the next convocation of the Georgian Parliament, both in terms of its legitimacy and having to deal with ongoing protests, should they continue.

- **Aside from EU/NATO membership (see below), the coronavirus crisis is the immediate priority.** The Georgian economy is expected to suffer a considerable recession in 2020 as a result of the pandemic. According to a recent IMF forecast, the economy will shrink by 5% in 2020 followed by a 5% rebound in 2021, while the World Bank predicts a 6% contraction this year and a 4% growth next year.

To counter the effects of the Crisis, the Georgian Government unveiled a detailed "Anti-Crisis Economic Action Plan", which included support for citizens who lost their jobs to the pandemic, one-time support for the unemployed, income tax waivers for low-income citizens, utility subsidies, profit tax waivers for enterprises in tourism, deposits for commercial banks and additional VAT refunds. In August, the society-focused Action Plan was extended with a one-time support for children, partially covering utility costs for Georgian households, as well as other measures. Among the immediate challenges facing the new cabinet are the need to continue an economic stimulus, while imposing tougher-than-previous COVID-19 restrictions if deemed necessary.

- › **Regardless of current events, Georgia remains one of the most business-friendly economies in the region.** Over the past decade and largely due to both the previous UNM and GD governments, Georgia has led the post-Soviet region in terms of economic freedom and the ease of doing business and has invested heavily in positioning itself as a top destination for foreign investment by simplifying its tax regime (to no more than six taxes applicable to international companies), introducing free industrial zones and providing government incentives.

Combined with high reserves on its labour market (11.6% as of 2019), this openness to international investment has attracted more than 19 billion USD in FDI for Georgia, with companies in the UK and the US among the largest investors, while Chinese investment has more than tripled to 600 million USD between 2012 and 2018.

Most recently, the Government decided to provide several international companies, including those in the maritime, logistics, trade and IT spheres, with significant tax relief by reducing profit and income taxes to 5%. Among other prioritized sectors for attracting foreign investment are manufacturing, tourism, energy, outsourcing and regional logistics. Prior to the elections, the Georgian Dream outlined a number of promises that could further strengthen the investment climate, including keeping taxes for business at low levels, providing support for developing workers in investment-heavy sectors, as well as easing administrative burdens.

FURTHER IMPLICATIONS OF A NEW GEORGIAN DREAM GOVERNMENT

Assuming Georgian Dream overcomes the current unrest in the coming weeks, the new Government, expected to be headed by current Prime Minister Giorgi Gakharia, will face challenges on multiple fronts due to the ongoing coronavirus pandemic and the corresponding economic crisis - in addition to a contested political environment and uneasy relations with Russia.

Although Gakharia is set to be confirmed once again as PM, overall power in the Government is expected to stay in the hands of Bidzina Ivanishvili, the billionaire businessman and founder of the Georgian Dream who previously served as Prime Minister but now operates in the background. Below we outline a number of likely scenarios and policy directions for the upcoming period:

- › **Uneasy relations with Russia continue as Georgia aims for NATO membership.** Following decades of tensions between the Georgian Government and Russia over the Abkhazian and Tskhinvali (South Ossetia) regions, relations reached a new low after the 2008 war that resulted in the loss of the two territories. The war took place shortly before NATO, for the first time, welcomed Georgia's membership aspirations.

Although the GD has often been accused of "being soft" on Russia, the ruling party remains committed to returning the occupied territories to the country and advancing Georgia's NATO membership. In 2014, Georgia - under the first GD government when Ivanishvili briefly served as Prime Minister - was invited to join NATO's so-called Enhanced Opportunity Partnership, the highest-level of cooperation with a non-NATO member, while shortly before the elections in September, NATO Secretary General Jens Stoltenberg told the Georgian Government to "prepare for membership."

We expect an acceleration of negotiations between the two sides as early as next year, however, Russia's recognition of the two breakaway regions and domestic political disputes could stand in the way of a future accession. While a future NATO membership could strengthen the country's already strong investment potential among the members of the Western community, the reaction from Moscow, which considers the alliance a security threat, will also be significant.

- According to a pre-election statement from Georgian Foreign Minister David Zalkaliani, the full restoration of ties with Russia could only take place if Russia withdraws its forces from Abkhazia and South Ossetia. However, we expect that the next Gakharia Government will most likely aim for a principled but pragmatic foreign policy approach.

The GD-led Government was instrumental in regaining access for Georgian producers to the Russian market: among other moves of reapprochement, Russia lifted a seven-year old ban on the import of Georgian wines in 2013, Georgia introduced a visa-free regime for Russian seeking short-term/tourist visits, while Georgian exports, in general, have skyrocketed since economic and trade relations were largely normalized.

A major turning point in economic relations occurred last July, however, when Russia banned direct passenger flights between the two countries over the June 2019 protests in Tbilisi that Moscow cited as Russophobic, with the ban still being in place in an extended format due to COVID-19 restrictions. With the pandemic hitting both Georgia's and Russia's economy, the new Government will likely explore ways to normalize relations, at least in economic terms, as soon as the coronavirus situation allows.

- **Advancing the country's integration with the European Union.** Georgia has been a member of the Eastern Partnership (EaP), the EU's neighbourhood initiative for political and economic cooperation with six former USSR states since 2008 and has refused to join the Russian-led Eurasian Economic Union (EAEU). In 2014, the Georgian Government also signed an EU Association Agreement, which includes a Deep and Comprehensive Free Trade Agreement (DCFTA), increasing market access between the two sides. In 2019, the GD-led Government - together with the then governments of Moldova and Ukraine - expressed interest in going beyond the Eastern Partnership and called for establishing an "EU+3 format" for the three countries. With the vast majority of Georgians supporting EU integration, the new Government is likely to push for a clear path for membership and an accession date in the next ten years and submit an official application for membership in 2024. As EU appetite for enlargement wanes, however, a strengthened partnership within or to some extent beyond the EaP is a more realistic aim for the next legislative term than an institutionalised path to EU membership.
- While Georgia maintains a leading investment position in the wider region, however, there have recently been worrying signs of a potential limit to the country's economic strategy (and freedom) that could jeopardise its attractiveness for foreign investors. A prime example was the cancellation of the Anaklia Deep Sea Port, the largest infrastructure project to date in Georgian history. Although repeatedly described as of strategic importance by both the Georgian Dream and the opposition, the Government in January moved to cancel an agreement with the project's investor consortium over alleged non-fulfilment of financial obligations. Suspicions arose that Russia pressured Georgia to sabotage a project openly backed by the US Government and funded by US investors (who later withdrew from the consortium, claiming an alleged lack of support from Georgian authorities).

CONCLUDING THOUGHTS

The upcoming days will prove crucial for Georgia's immediate political future and international reputation. While the opposition will likely put a certain level of public pressure on the Georgian Dream by organizing mass protests and voicing concerns over the results, the Georgian Dream will refer to the overall assessment provided by international election observers. Although other scenarios are possible, at present we expect that the ruling party will overcome the opposition-mounted challenge, supported by positions of the EU and the US. At the same time, discrepancies in Georgia's polarized political system, as well as actual concerns over the election system from both the inside and the outside could accelerate a political standoff.

About Kesarev

Kesarev - is the leading independent public affairs and government relations consultancy in Ukraine, Russia, the post-Soviet area, Central and Eastern Europe, Turkey and Israel, covering 25 countries and specializing in government and corporate affairs, risk management and corporate reputation services.

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