

BAG INDEX

BUSINESS
CLIMATE



საქართველოს ბიზნეს ასოციაცია
BUSINESS ASSOCIATION OF GEORGIA

ifo INSTITUTE

Leibniz Institute for Economic Research
at the University of Munich



Research

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CONTENTS

BAG Index	1
BAG Business Climate	1
BAG Business Climate by sector	3
Employment, sales and sales prices by sector	5
Factors Hindering Business Activity	8
Financing	13
Exchange rate expectations	14

The Business Association of Georgia (BAG) Index is a joint product of the Business Association of Georgia, PMC Research Center and the ifo Institute for Economic Research. The BAG Index summarizes the BAG Business Climate, BAG Employment Barometer and BAG Investment Environment, which are calculated according to the assessments of the top managers of BAG member businesses and companies in their corporate group¹. PMC Research Center publishes the BAG Index on a quarterly basis.

BAG BUSINESS CLIMATE

The BAG Business Climate is based on the responses of BAG member businesses and companies in their corporate group. Companies assess their present business situation and outline their expectations for the next six months². Apart from this, businesses are also asked to assess their situation regarding sales, sales prices, and the number of employees for the last quarter, current quarter and the next quarter. Moreover, companies are asked questions related to factors hindering their business activity, access to finance, exchange rate expectations and investment environment. For the purposes of this index, BAG members are divided into the following four sectors: trade, service, manufacturing and construction. The survey was conducted in Q3 of 2022 in period 29 August – 18 September.

IN Q3 OF 2022, THE SURVEYED BUSINESSES ASSESS THEIR PRESENT BUSINESS SITUATION AND EXPECTATIONS FOR THE NEXT SIX MONTHS POSITIVELY. THE BAG BUSINESS CLIMATE INDICATOR AMOUNTS TO 43.2 POINTS IN Q3 OF 2022, WITH THE PRESENT BUSINESS SITUATION INDICATOR SITTING AT 39 AND THE BUSINESS EXPECTATIONS INDICATOR AT 47.5.

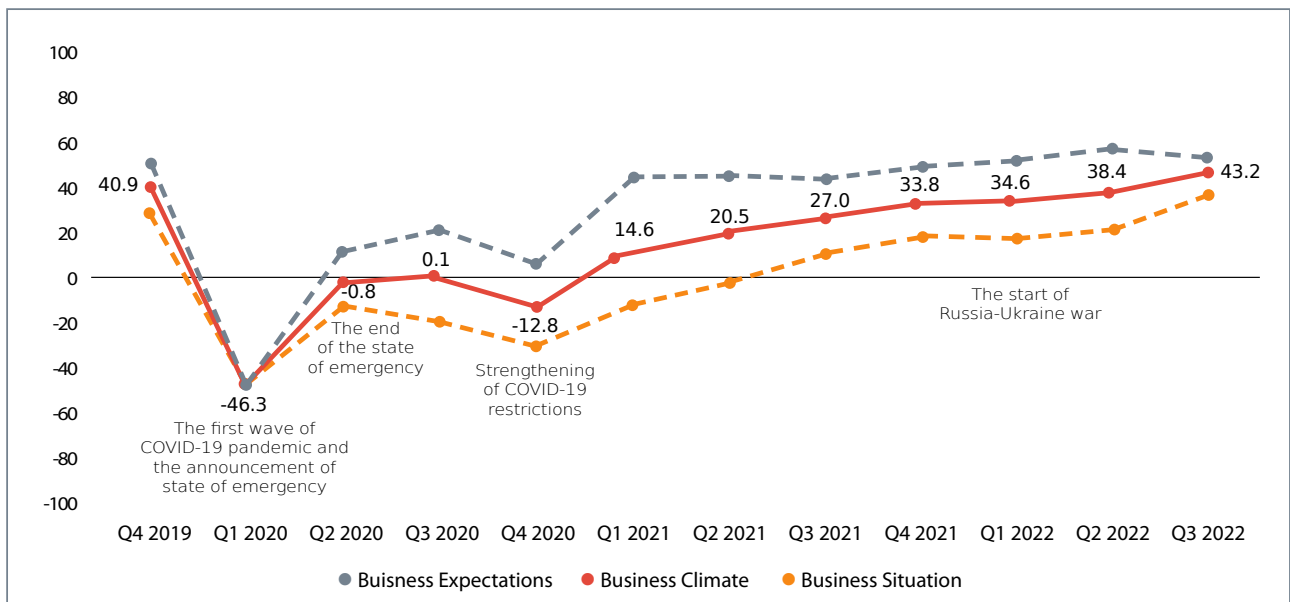
In Q3 of 2022, compared to Q2 of 2022, the BAG Business Climate improved by 4.8 points. Moreover, in this period, the assessment of the present business situation improved (by 17.4 points) and business expectations worsened (by 9 points).

The figures for Q3 of 2022 demonstrate an improvement compared to Q3 of 2021. In Q3 of 2021, the BAG Business Climate indicator was 27, the present business situation indicator equaled 10.8, while the business expectations indicator sat at 44.5.

It is worth noting that starting from Q1 of 2021, the BAG Business Climate indicator has been positive and gradually improving. In Q1 and Q2 of 2021, this was mostly caused by optimistic business expectations, while from Q3 of 2021 onwards the positive assessment of the present business situation by the majority of businesses played a part too (see graph 1).

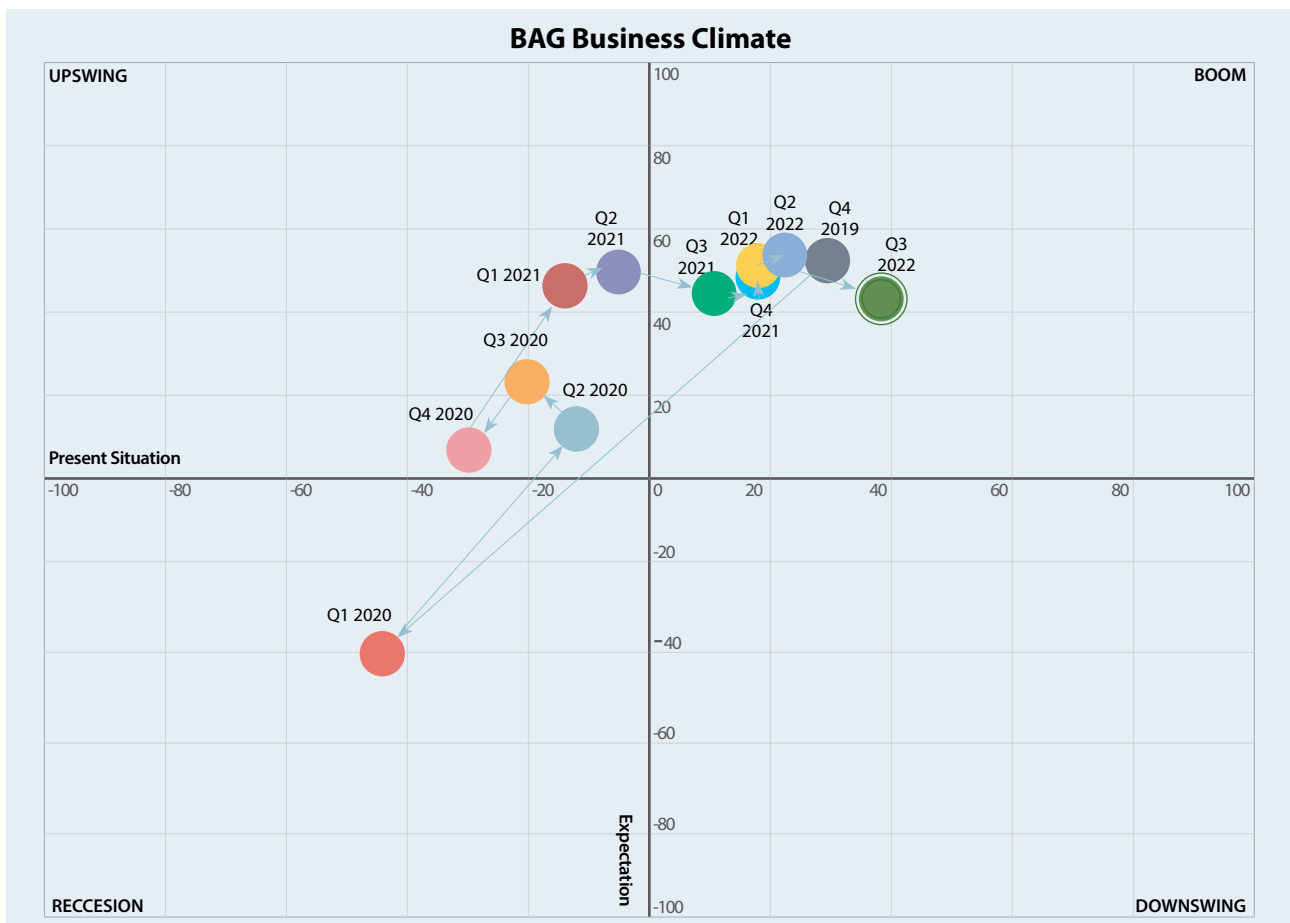
¹ In the first quarter of 2021, a change was made in the methodology of the BAG Index. As a result, the number of companies surveyed increased: enterprises that belong to the corporate group of member companies were added to the existing survey respondents.

² The balance value for the present business situation is the difference in the percentage shares of the "good" and "bad" responses, and the balance value for the expectations for the next six months is the difference in the percentage shares of the "more favorable" and "less favorable" responses. The BAG Business Climate is a transformed mean of the balance values of the present business situation and the expectations for the next six months. The BAG Business Climate can be between -100 and +100. +100 means that all surveyed businesses assess the business climate positively, while -100 means all surveyed businesses assess the business climate negatively.



Graph 1: BAG Business Climate, Business Expectation, and Present Business Situation

In Q3 of 2022, as in Q2 of 2022, the BAG Business Climate Indicator is in the **boom phase**.



Graph 2: BAG Business Climate

The Graph 2 depicts the relationship between the present business situation and business expectations for the next six months in a four-quadrant diagram. The quadrants are labeled “upswing,” “boom,” “downswing,” and “recession” and each of these are explained below:

- ✖ If survey participants assess the present business situation negatively but have positive business expectations for the next six months on balance, then the BAG business climate indicator falls in the **“upswing”** quadrant.
- ✖ If survey participants assess both the present business situation and business expectations for the next six months positively on balance, then the business climate indicator resides in the **“boom”** quadrant.
- ✖ If survey participants assess the present business situation positively but have negative business expectations for the next six months on balance, then the BAG business climate indicator is in the **“downswing”** quadrant.
- ✖ If survey participants assess the present business situation negatively and also have negative business expectations for the next six months on balance, then the BAG business climate indicator is placed in the **“recession”** quadrant

BAG BUSINESS CLIMATE BY SECTOR

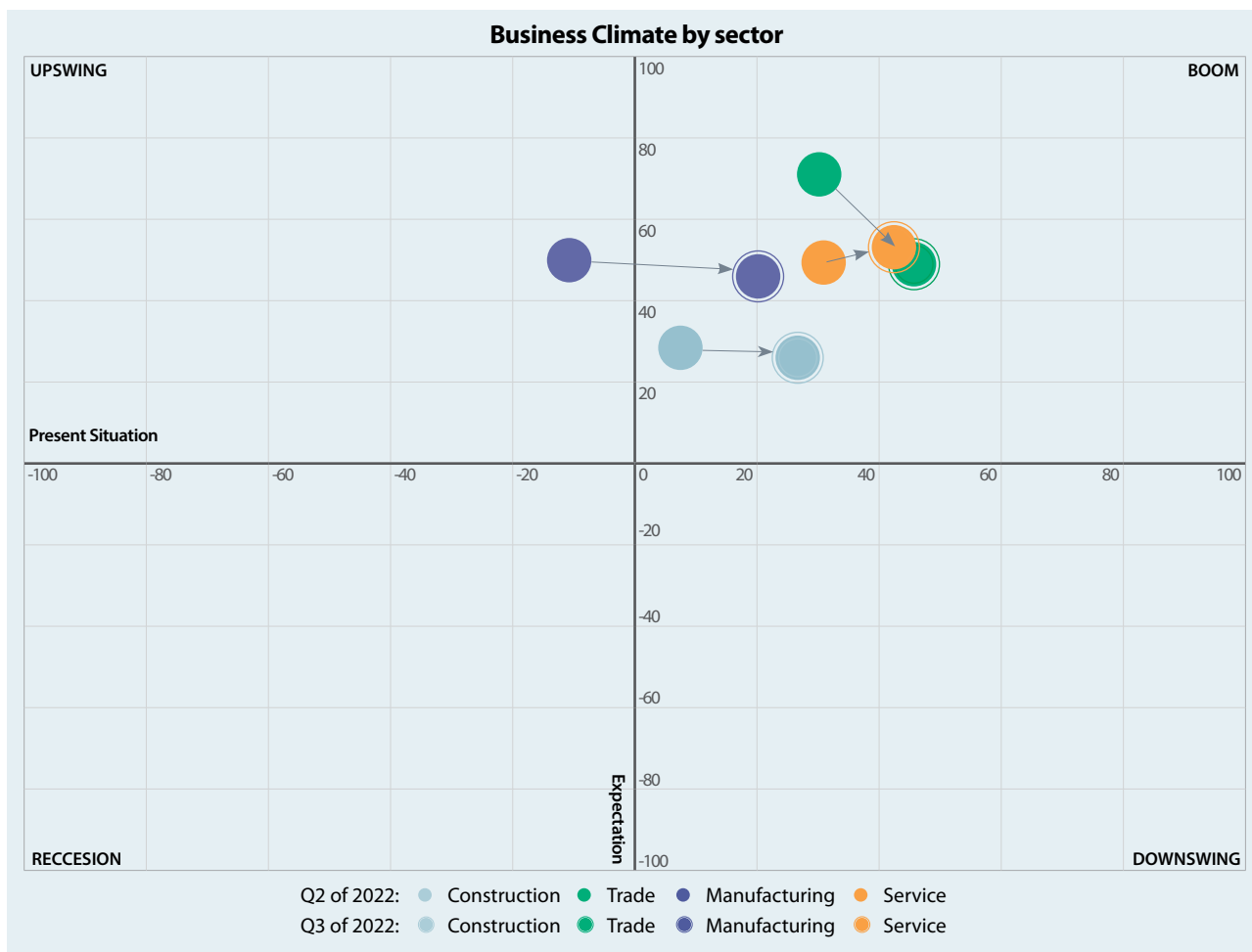
In Q3 of 2022, the **business climate indicator** was positive for all sectors. Compared to Q2 of 2022, in Q3 of 2022 the indicator improved in the manufacturing, construction and service sectors but worsened in the trade sector (see Graph 3).

In Q3 of 2022, compared to Q2 of 2022, the **present business situation indicator** improved in all sectors. It must be noted that in Q3 of 2022, the assessment of the present situation in the manufacturing sector improved significantly (by 32.5 points) compared to the negative assessment of the previous quarter. Among the sectors, the most positive assessment with respect to the present business situation was recorded in the trade sector, which could be attributed to increased sales (in the trade sector, the majority (68.3%) of the companies indicated an increase in sales in Q3 of 2022).

In Q3 of 2022, the **business expectations indicator** was positive for all sectors. It is worth noting that expectations significantly worsened for the trade sector compared to Q2 of 2022. The worsening of expectations is also visible in the manufacturing and construction sectors. Among the sectors, the business expectations indicator is most optimistic in the service sector.

Table 1: Balance values by sector in Q3 of 2022

	Business Climate	Present Business Situation	Business Expectation
Trade Sector	47.6	46.3	48.8
Service Sector	47.7	43.2	52.3
Manufacturing Sector	33.0	20.0	46.7
Construction Sector	27.3	27.3	27.3
All Sectors	43.2	39.0	47.5



Graph 3: Business climate by sector in Q2 2022 and Q3 2022

Since Q1 of 2021, the business climate indicator has been consistently positive in the trade, manufacturing, and service sectors. The positive assessment of the business climate reflects both the positive assessment of the present situation and optimistic expectations for the following quarter.

The business climate indicator has been improving in trade, service, and manufacturing sectors since Q1 of 2021, compared to corresponding periods of the previous year. Trade and service sectors sustained a tendency of improvement in Q3 of 2022. Meanwhile, since the drop in Q2 of 2022, the business climate in the manufacturing sector returned to an improving trend in Q3 of 2022.

In the construction sector, the business climate indicator was negative in Q1 and Q2 of 2021, however, it has been positive since Q3 of 2021 and gradually improving, compared to the corresponding periods of the previous year. Until Q2 of 2022, this improvement has been mainly due to the optimistic outlook under the business expectations element, however, since Q2 of 2022, the optimistic assessment of the present situation also became a determining factor (see Graph 4).

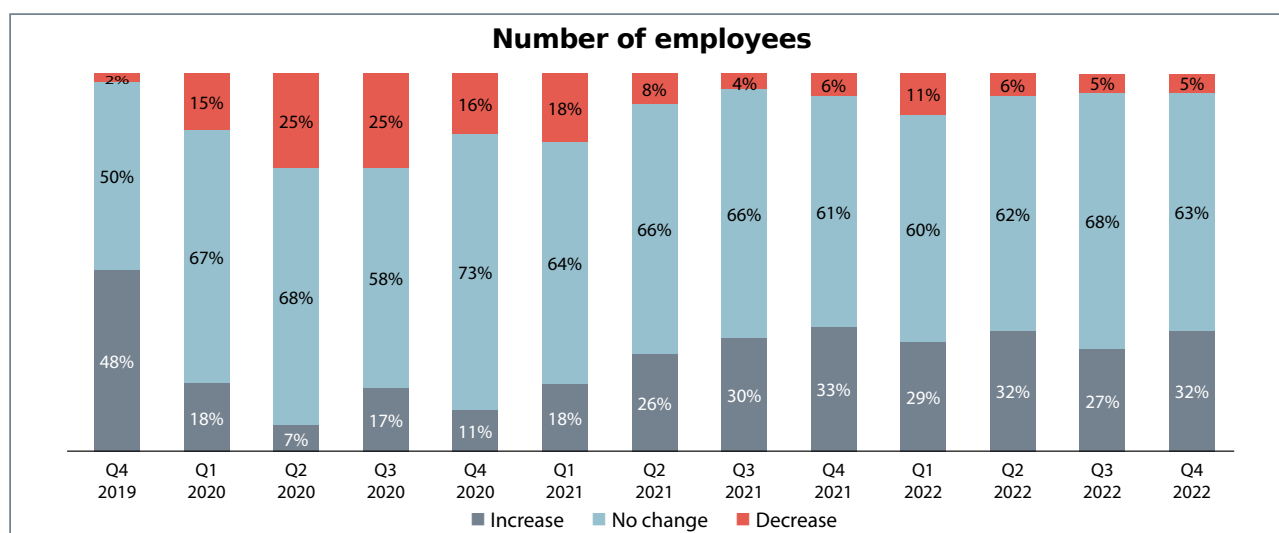


Graph 4: Business Climate, Business Expectation, and Present Business Situation in trade, service, manufacturing and construction sectors

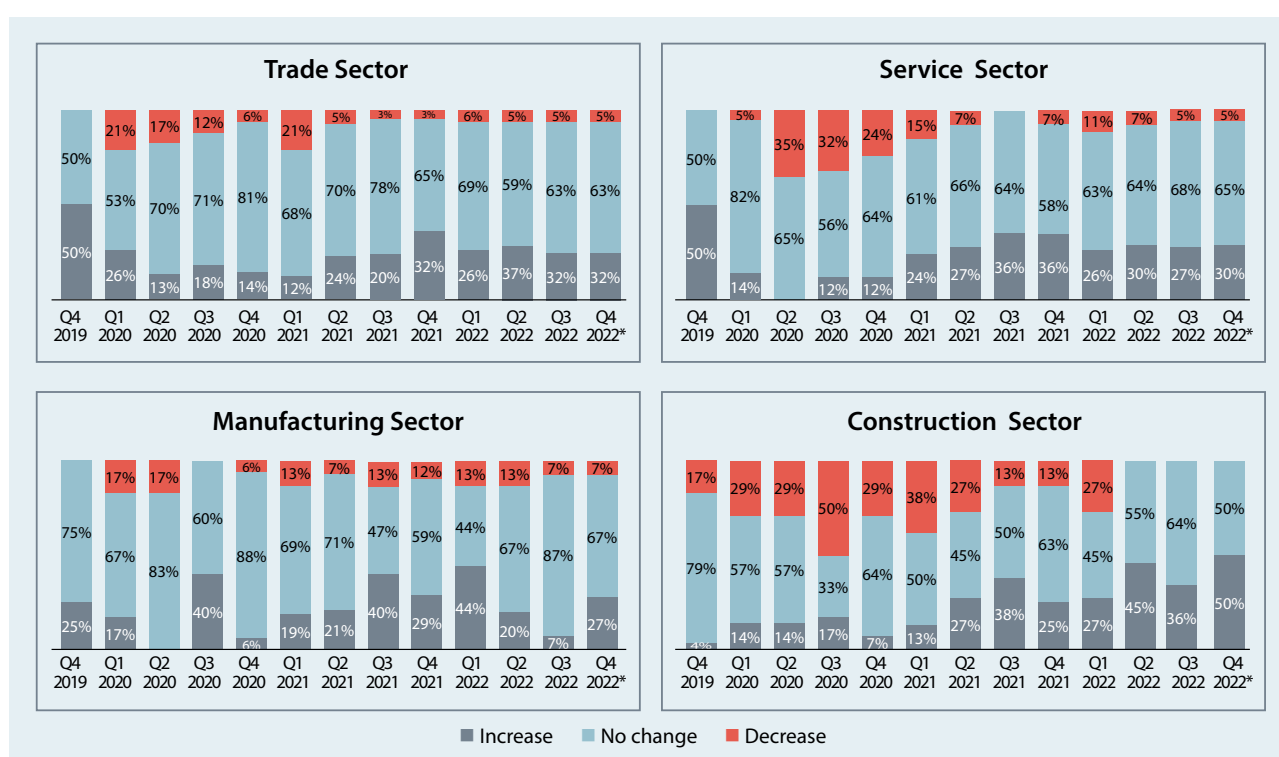
EMPLOYMENT, SALES AND SALES PRICES BY SECTOR

Employment

- ✖ 27% of surveyed companies stated that the number of employees increased in Q3 of 2022. At the same time, 31.8% expect the number of employees to increase in Q4 of 2022 (see Graph 5).
- ✖ Across the sectors covered, the situation regarding employment in Q3 of 2022 and the expectation for Q4 of 2022 is most positively assessed in the construction sector (see Graph 6).
- ✖ Meanwhile, the situation regarding employment in Q3 of 2022 and the expectation for Q4 of 2022 is most negatively assessed in the manufacturing sector. In the manufacturing sector, compared to other sectors, the highest share of companies stated a decline in the number of employees in Q3 of 2022. Besides that, 7% of surveyed companies in the sector expect the number of employees to decline in Q4 of 2022.



Graph 5: The number of employees in BAG member businesses and companies in their corporate group



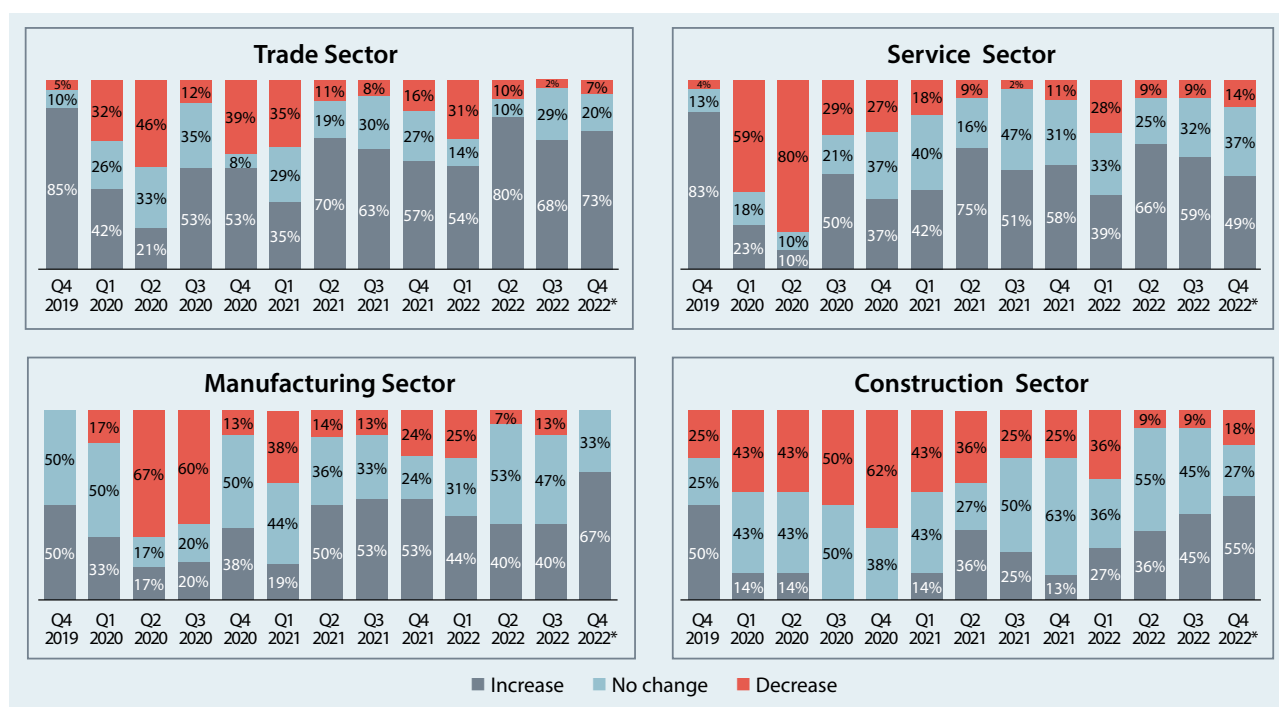
Graph 6: The number of employees in the trade, service, manufacturing and construction sectors³

Sales/demand/domestic production

- ✖ The situation in Q3 of 2022 and the expectation for Q4 of 2022 regarding sales were assessed most positively in the trade sector (see Graph 7)..
- ✖ Meanwhile, compared to other sectors, a small share of companies in the manufacturing and construction sectors stated that sales increased in Q3 of 2022. However, in Q4 of 2022, a significantly larger share of companies expects sales to increase.

³ Due to the rounding of number, in some graphs the sum of the data does not always equal 100%.

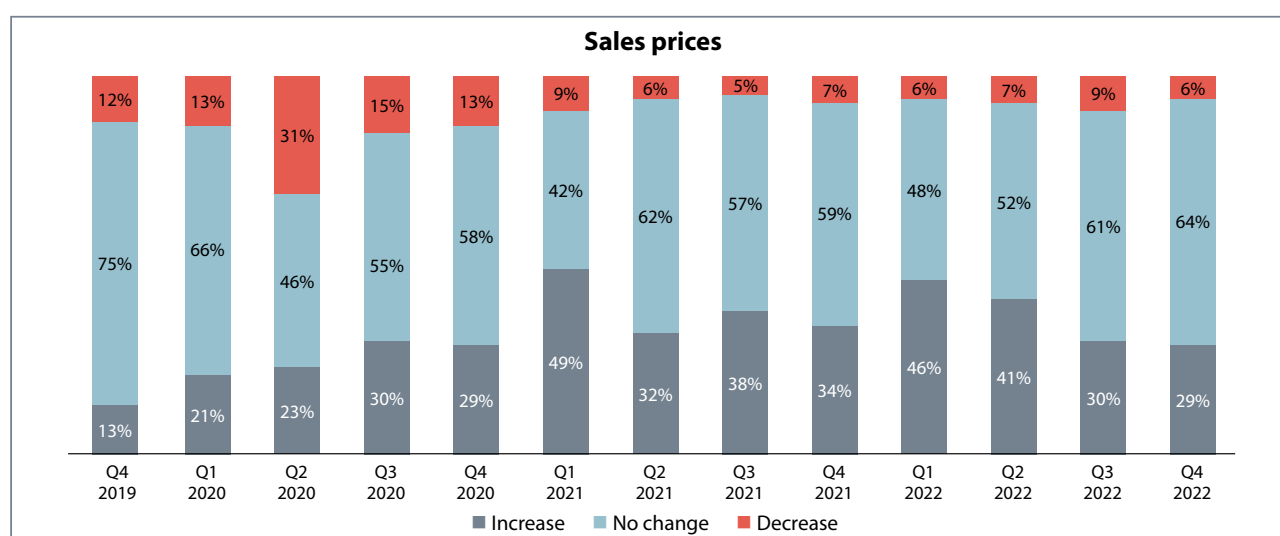
* Expectation.



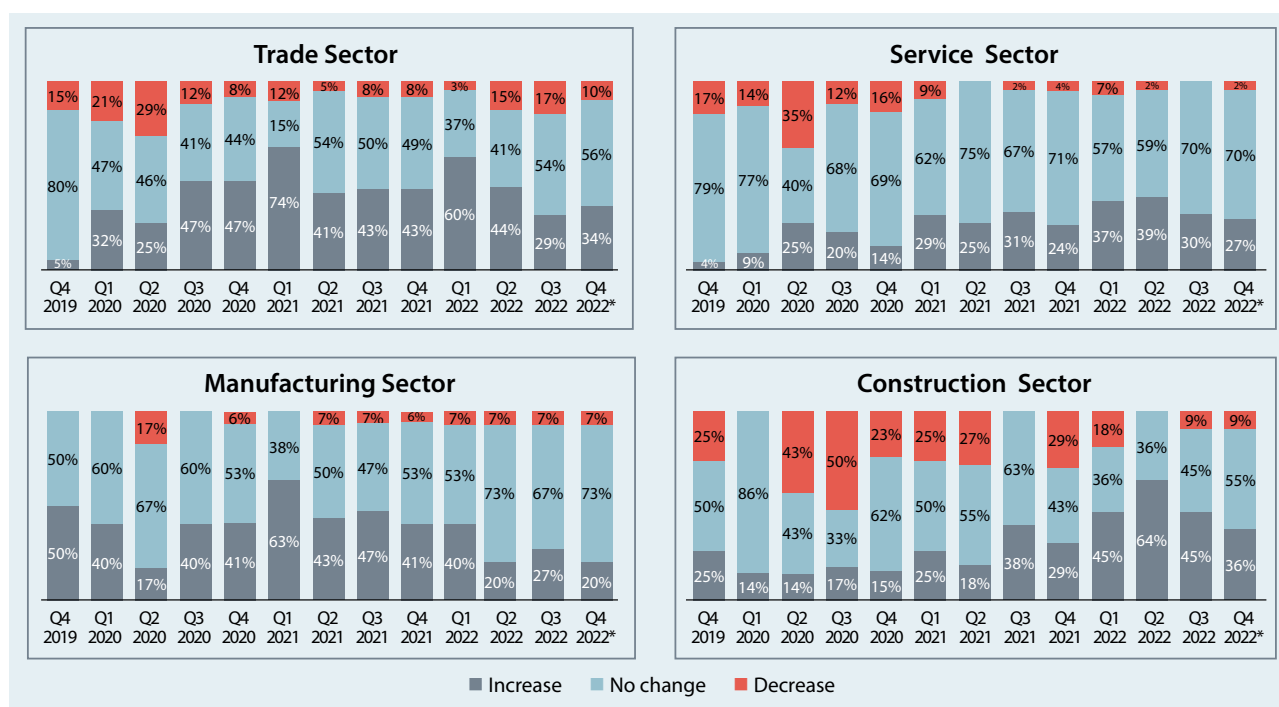
Graph 7: Sales, demand and domestic production in trade, service, manufacturing, and construction sectors

Sales prices

- ✖ In Q3 of 2022, 30.4% of surveyed companies increased sales prices, and 29.5% of the companies expect the prices to rise in Q4 of 2022 (see Graph 8).
- ✖ Among sectors, in Q3 of 2022, the share of the companies that are increasing sales prices is the highest for the construction sector, which could be attributed to increased construction materials prices due to the Russia-Ukraine war and increased demand for real estate (see Graph 9).
- ✖ The price increase dynamics are least present in the manufacturing sector, in which only a small share of companies stated that they increased prices on their products in Q3 of 2022.



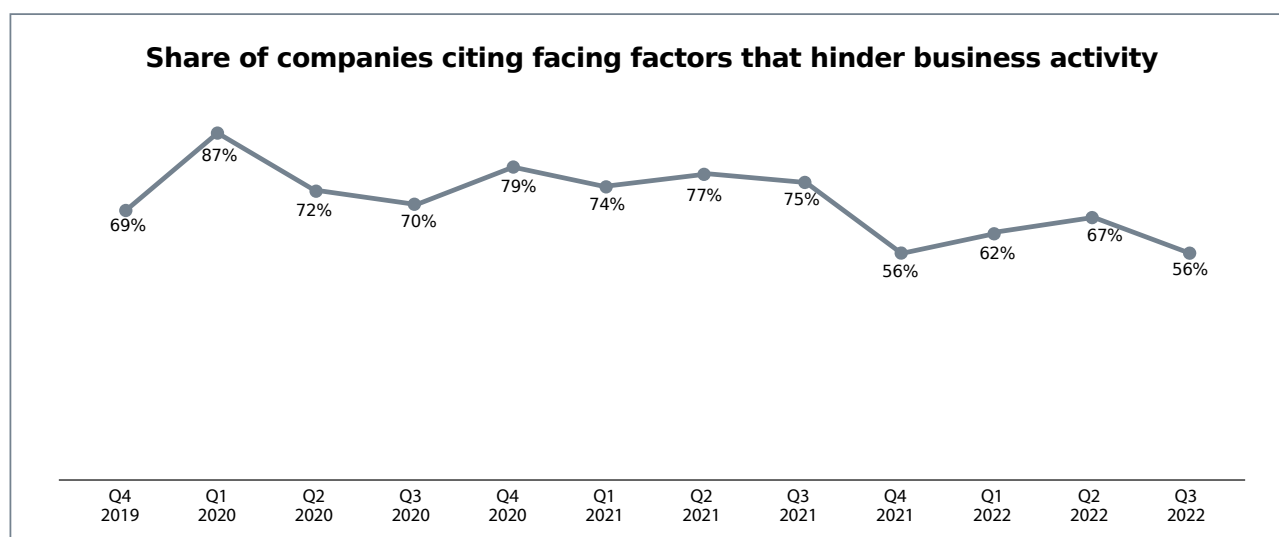
Graph 8: Sales prices in BAG member businesses and companies in their corporate group



Graph 9: Sales prices in trade, service, manufacturing, and construction sectors

FACTORS HINDERING BUSINESS ACTIVITY

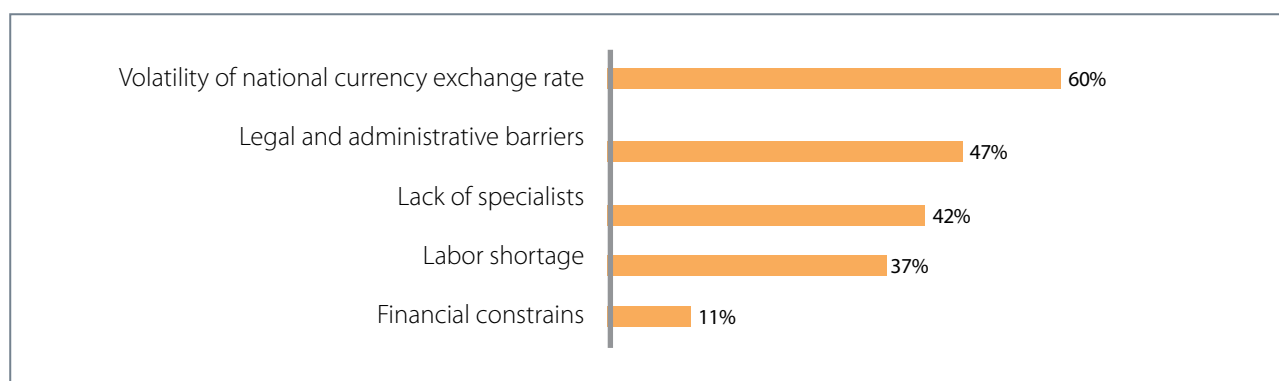
In Q3 of 2022, compared to Q2 of 2022, the share of surveyed companies to claim there are factors hindering their business activity decreased significantly (by 11 percentage points). It must be noted that, in Q3 of 2022, compared to Q3 of 2021, the share of companies claiming that there are factors hindering their business activity decreased markedly (by 19 percentage points).



Graph 10: Existence of factors hindering business activity

In Q3 of 2022, the following five factors were emphasized as the most hindering for business activity: volatility of national currency exchange rate⁴, legal and administrative barriers, a lack of specialists, labor shortage, and financial constraints (see Graph 11).

⁴ Volatility of national currency exchange rate as a factor hindering business activity was added to the survey questionnaire in Q2 of 2021.



Graph 11: Main factors hindering business activity for surveyed companies in Q3 2022

In Q3 of 2022, similar to the previous quarters, **the volatility of the national currency exchange rate** was cited as the top factor hindering business (60% of surveyed companies cited this factor as the most hindering). From a sector-by-sector view, this factor was most frequently pointed out in the construction sector (71%), while it was considered the least hindering for the service sector (48%) (see Graph 12).

In terms of the size of the enterprise⁵, the volatility of the national currency exchange rate was most cited by small enterprises as a factor hindering business activity (77% of surveyed small companies cited this factor as hindering) (see Graph 13).

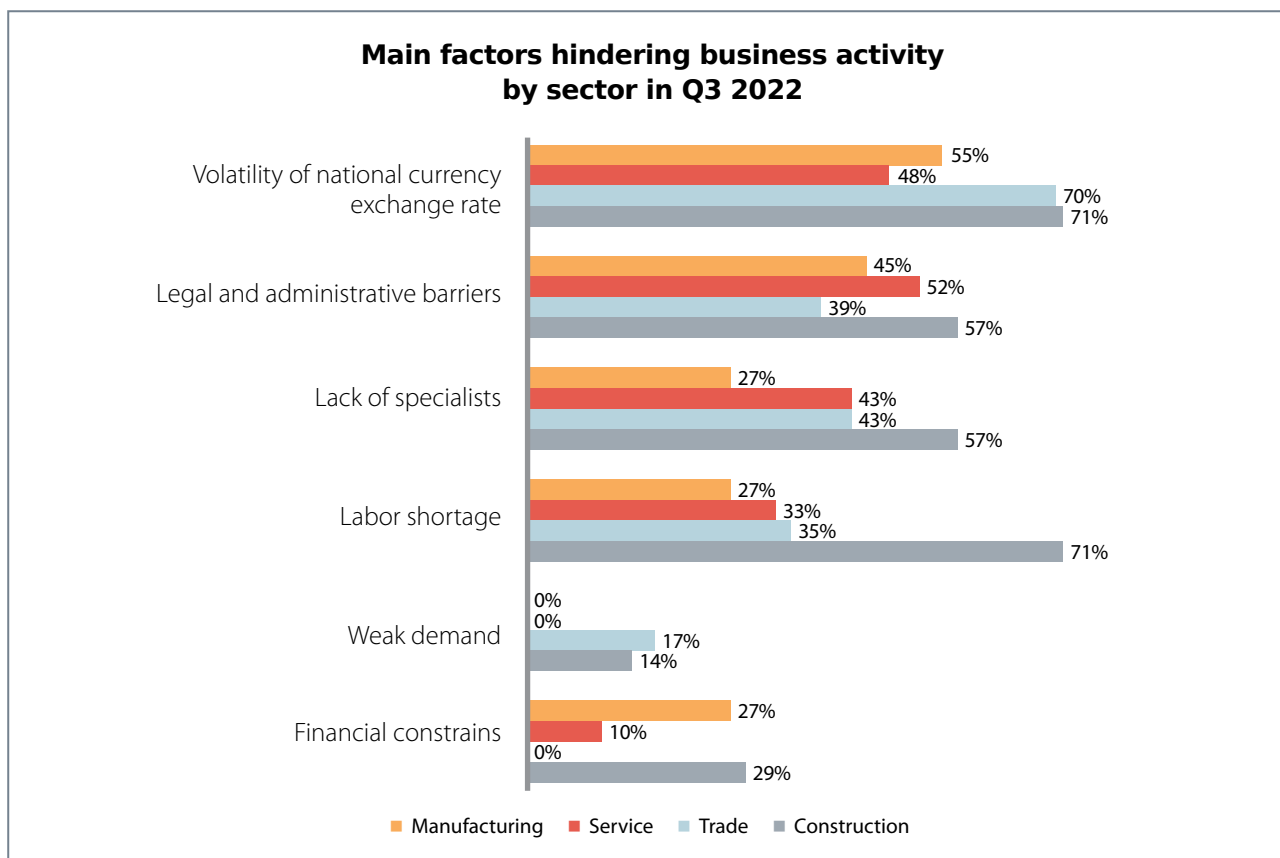
In Q3 of 2022, **legal and administrative barriers** was the second-most cited hindering factor (cited by 47% of surveyed companies). Across the covered sectors, this factor was most frequently pointed out in the construction sector (57% of surveyed companies in this sector cited this factor as the most hindering) and was considered the least hindering for the trade sector (39%). Legal and administrative barriers are most hindering for large enterprises (58% of them cited this factor as hindering).

In Q3 of 2022, **a lack of specialists** was cited as a hindering factor by 42% of surveyed companies. This issue was felt most acutely in the construction (57%), while it was less of a hindrance for the manufacturing sector (27%). A lack of specialists was considered most problematic for medium enterprises (cited by 52% of them as a hindering factor).

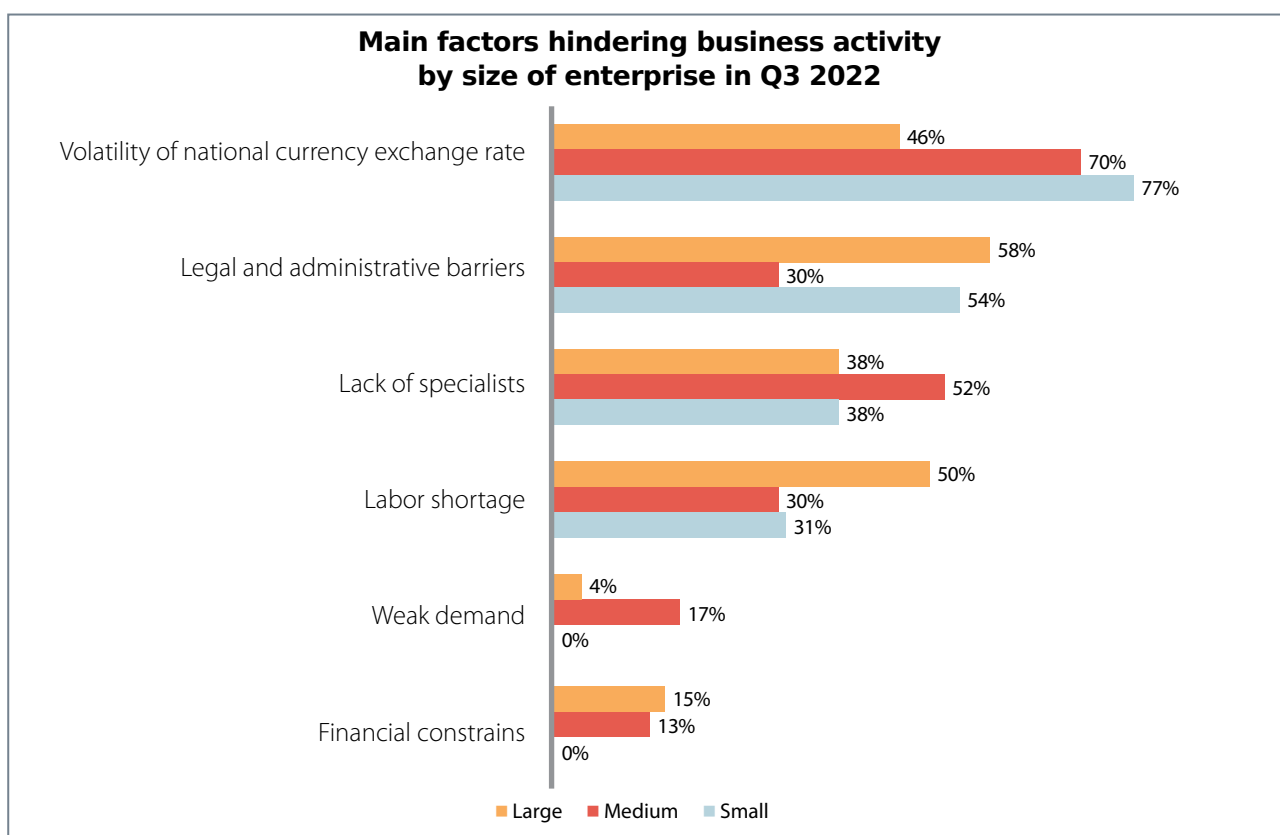
In Q3 of 2022, **labor shortage** was cited as a hindering factor by 37% of surveyed companies. Across the covered sectors, this factor was deemed most hindering for the construction sector (71%). In Q3 of 2022, labor shortage was considered most problematic for large enterprises (cited by 50%).

Financial constraints was cited as a hindering factor by 11% of the surveyed companies in Q3 of 2022. This factor was most cited in the construction sector (29%). It was considered most problematic for large enterprises (15%).

⁵ The size of enterprise was determined according to the methodology of the National Statistics Office of Georgia (i.e. small, medium, or large).

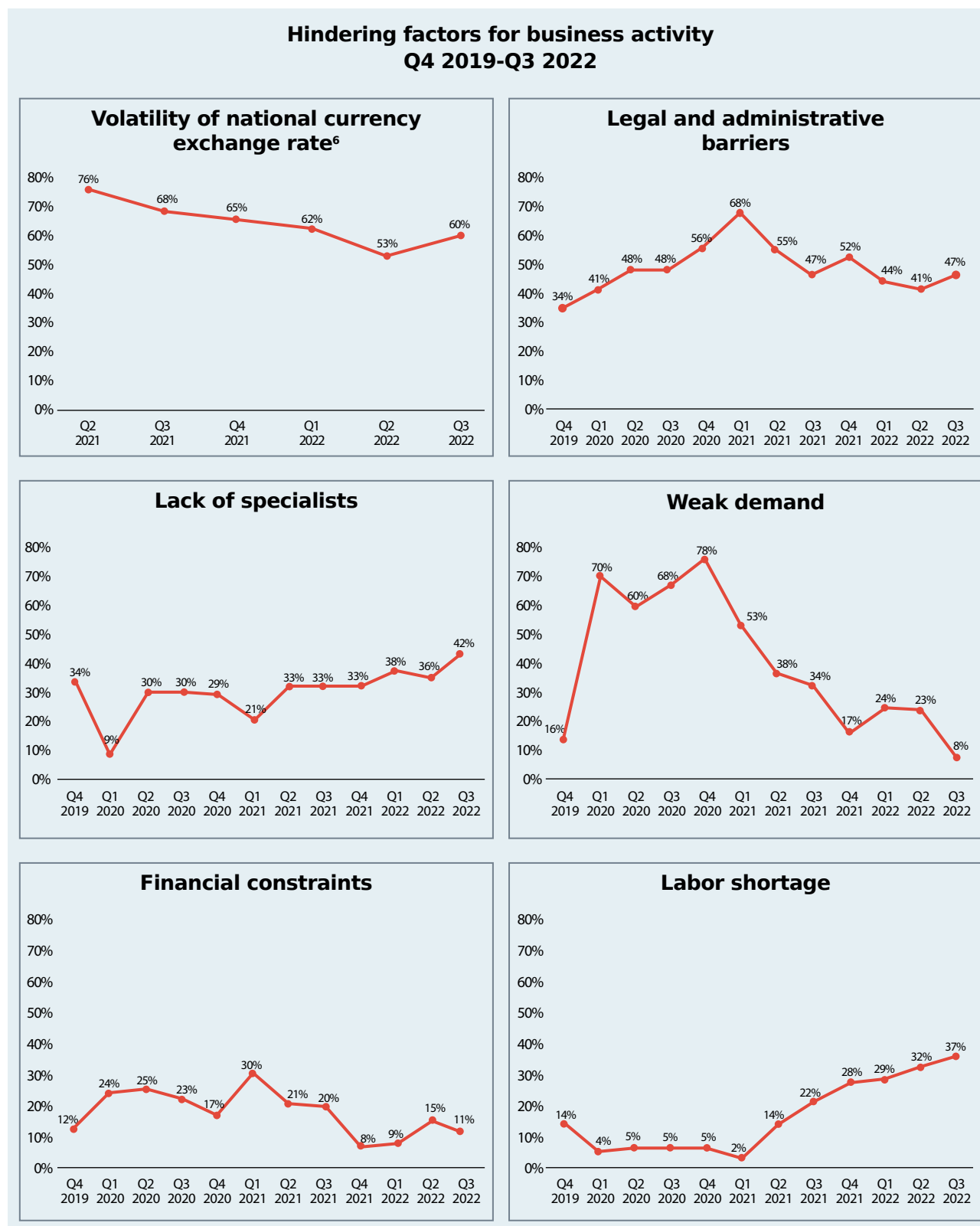


Graph 12: Main factors hindering business activity by sector in Q3 2022



Graph 13: Main factors hindering business activity by size of enterprise in Q3 2022

In Q3 of 2022, compared to Q2 of 2022, among the factors hindering business activity, the share of companies citing weak demand decreased the most (by 15 percentage points). Elsewhere, the share of companies citing volatility of the national currency exchange rate as a hindering factor increased the most (by 7 percentage points) over the same period (See Graph 14).



Graph 14: Main hindering factors for surveyed companies

⁶ Volatility of national currency exchange rate as a factor hindering business was added to the survey questionnaire in Q2 of 2021.

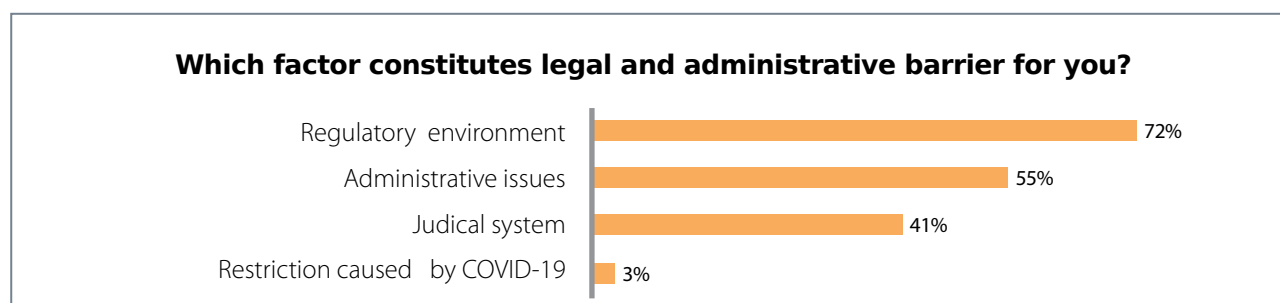
The main factors determining legal and administrative barriers for business

In Q3 of 2022, similar to the previous quarter, the **regulatory environment** has been considered the main element of legal and administrative barriers hindering business activity. Meanwhile, looking from a sector-by-sector view, the regulatory environment was most cited as a hindering factor in the service sector (90% of companies surveyed in the service sector for which there are legal and administrative barriers named the regulatory environment as a hindrance). The regulatory environment is deemed less hindering for the manufacturing sector (40%).

Among legal and administrative barriers, **administrative issues** were the second-most cited hindering factor. This was deemed the most hindering in the manufacturing sector (80%), while it was least cited in the service sector (36%).

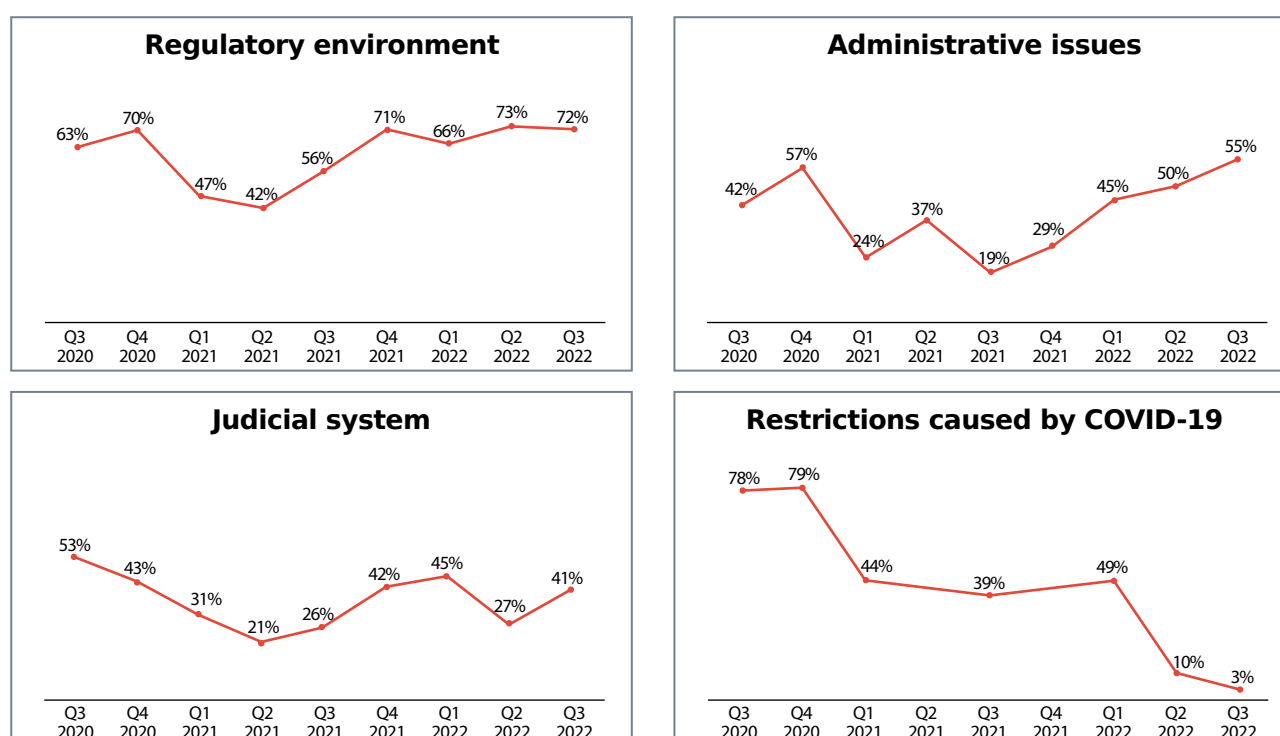
Meanwhile, the **judicial system** was the most cited as a hindering factor under legal and administrative barriers in the service sector (cited by 45% of companies), while it was least cited in the construction sector (25%).

Among legal and administrative barriers, **COVID-19-related** restrictions were cited by only 3% of companies. This was deemed as a hindering factor only in the construction sector.



Graph 15: Main legal and administrative hindering factors for surveyed companies

In summary, in Q3 of 2022, compared to the previous quarter, the share of companies to cite COVID-19-related restrictions and the regulatory environment as a hindering factor decreased (by 7 and 1 percentage point accordingly), while the share of companies citing the judicial system as a hindering factor increased the most (by 14 percentage points).

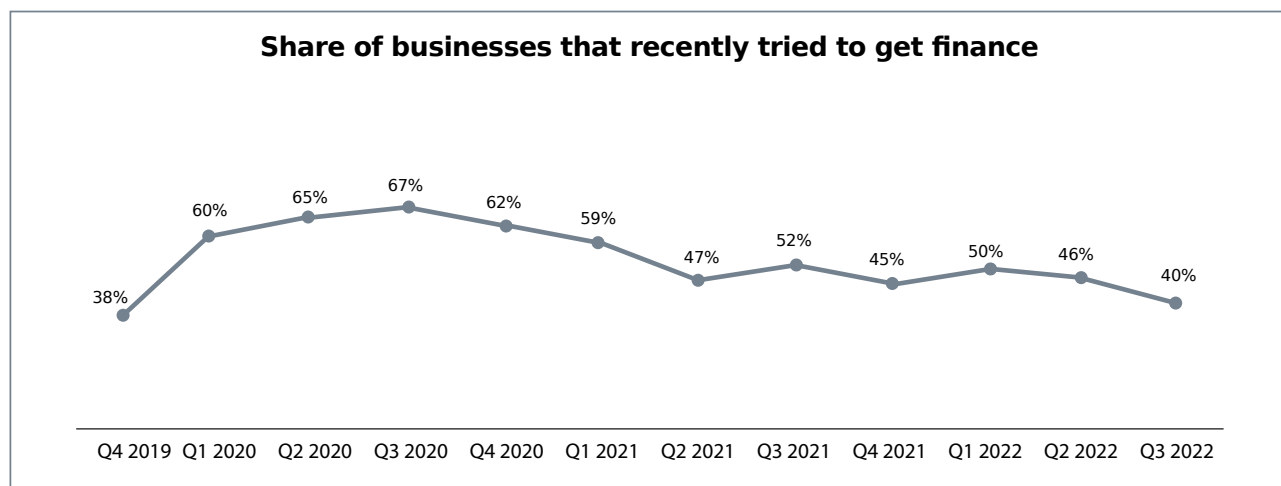


Graph 16: Main legal and administrative hindering factors for surveyed companies

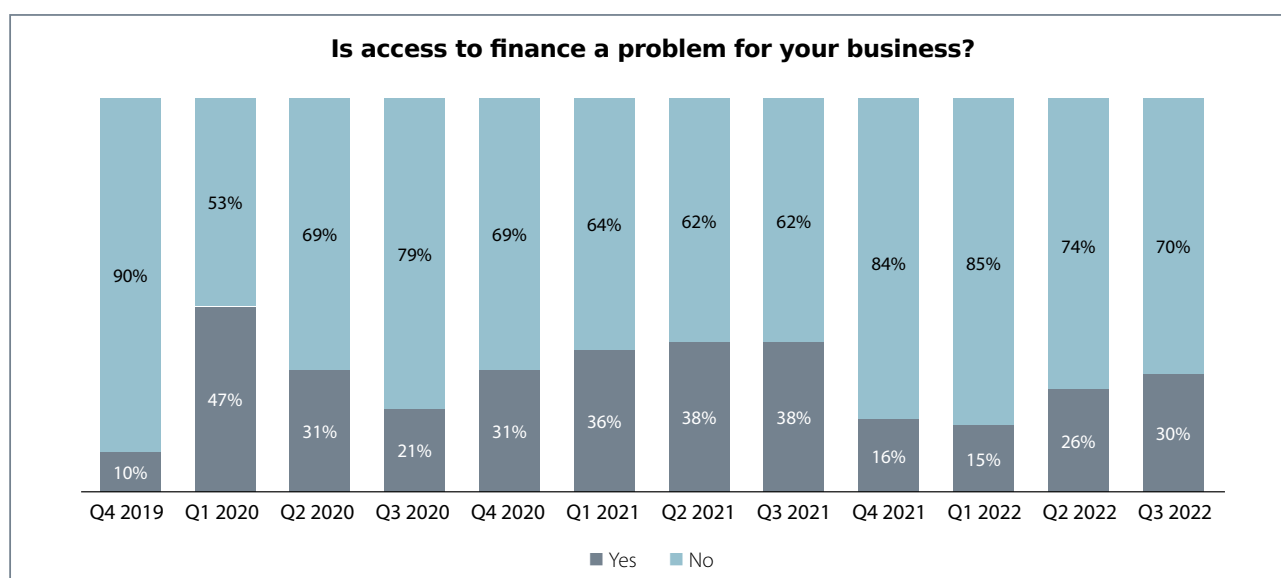
FINANCING

In Q3 of 2022, 40% of surveyed companies claimed to have recently tried to obtain finance, which is 6 percentage points lower than the figure recorded in the previous quarter (see Graph 17).

In Q3 of 2022, 30% of those companies that recently tried to access finance also noted that access to finance was a problem for their business. This figure is higher (4 percentage points) than that of the previous quarter (see Graph 18).



Graph 17: Businesses that recently tried to get finance

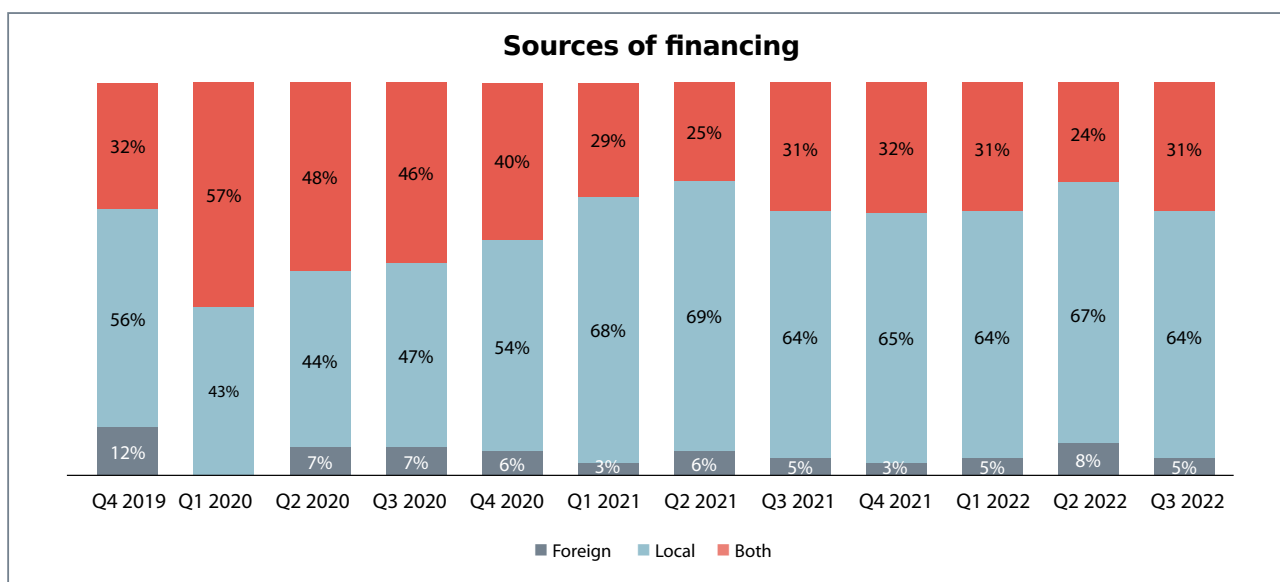


Graph 18: Access to finance⁷

Regarding sources of financing⁸, in Q3 of 2022, similar to previous quarters, the majority of surveyed companies stated that they were financed by local sources. The share of companies stating that they were financed by foreign sources decreased by 3 percentage points in Q3 of 2022, compared to the previous quarter.

⁷ The question was only answered by those companies that stated they had recently sought finance.

⁸ The change in methodology in Q1 of 2021 (the increase in the number of surveyed companies) altered the financing structure. This methodological change did not affect significantly any other indicators.

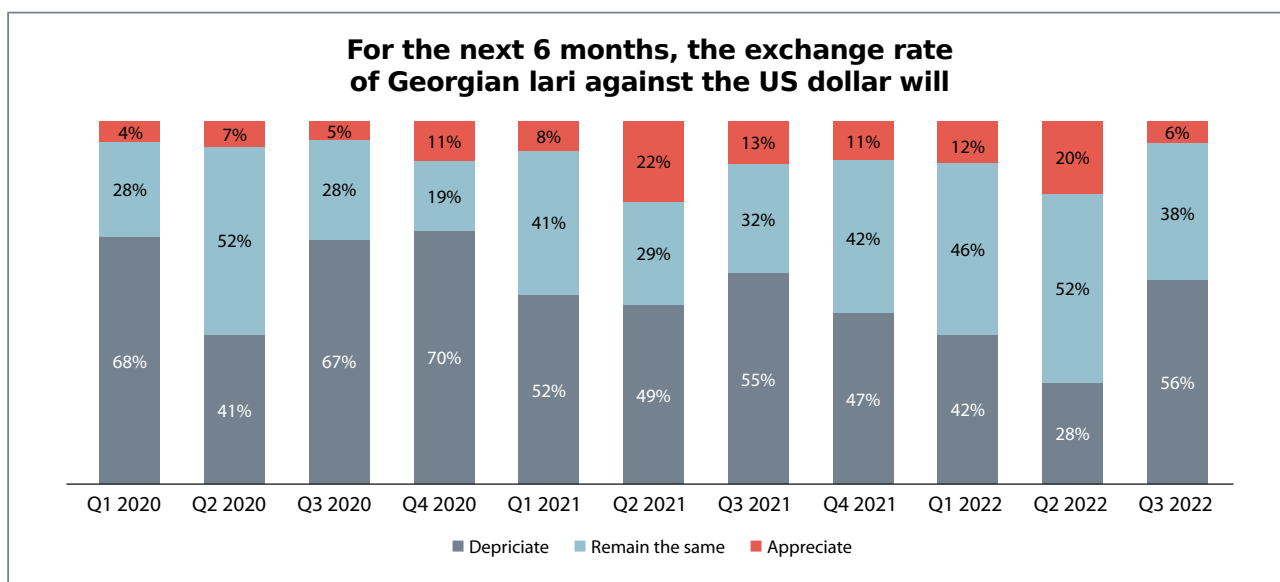


Graph 19: Sources of financing

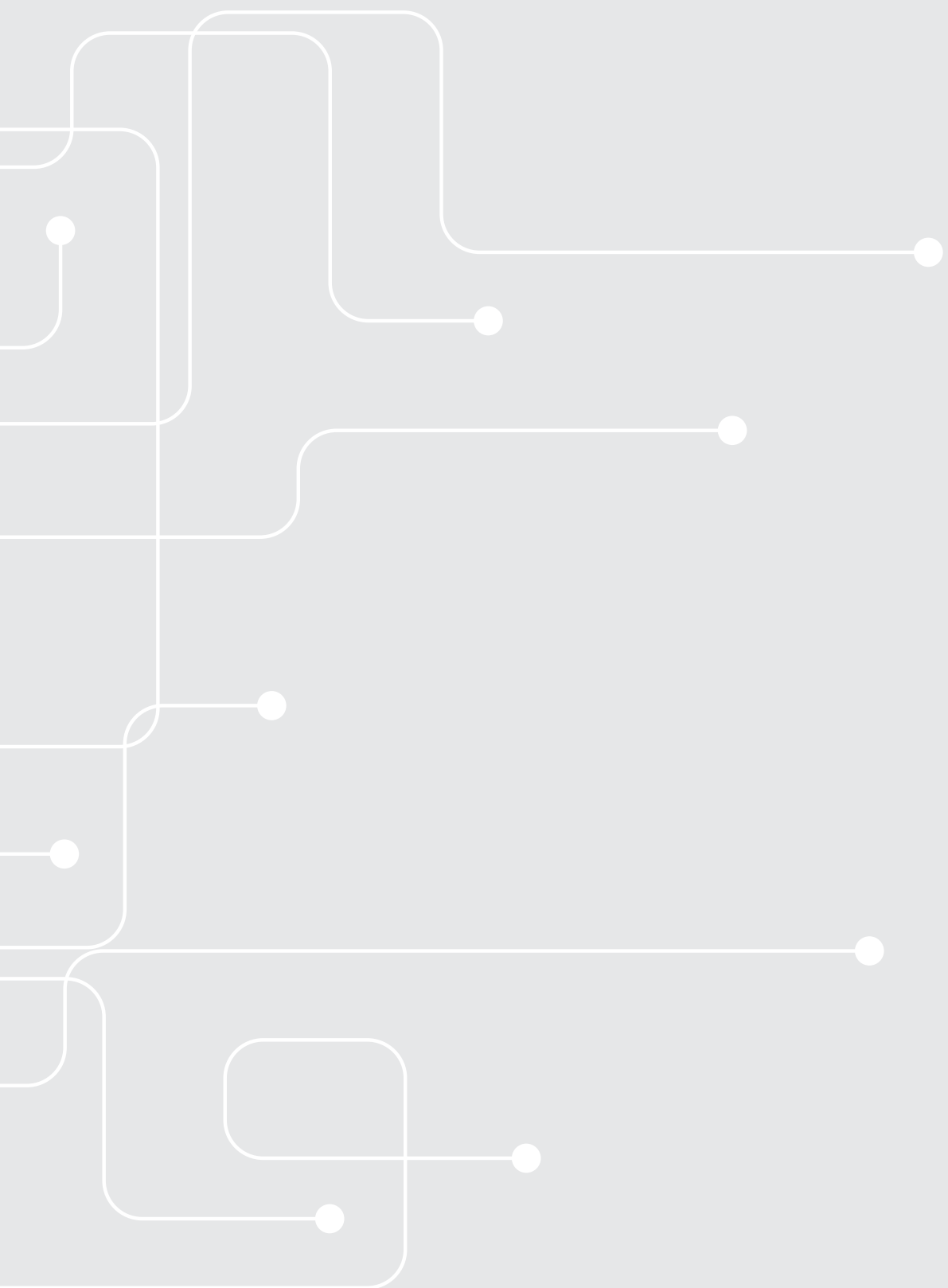
EXCHANGE RATE EXPECTATIONS

In Q3 of 2022, compared to Q2 of 2022, the share of companies expecting that the national currency would depreciate against the US Dollar doubled (increased by 28 percentage points). Moreover, in Q3 of 2022, compared to the previous quarter, the share of companies expecting that the national currency exchange rate would appreciate throughout the next 6 months, decreased by 14 percentage points.

It is worth noting that from Q4 2021 to Q2 2022, the share of companies expecting that the national currency would depreciate was decreasing quarterly. However, in Q3 of 2022, the corresponding number has returned to its figure from Q3 of 2021 (greater by 1 percentage point).



Graph 20: Exchange rate of the Georgian Lari against the US Dollar



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