

BAG INDEX

BUSINESS
CLIMATE



საქართველოს ბიზნეს ასოციაცია
BUSINESS ASSOCIATION OF GEORGIA



Leibniz Institute for Economic Research
at the University of Munich



Research

I QUARTER 2022

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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 Q1 of 2022 in period 14 – 28 February.

IN Q1 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 34.6 POINTS IN Q1 OF 2022, WITH THE PRESENT BUSINESS SITUATION INDICATOR SITTING AT 18.1 AND THE BUSINESS EXPECTATIONS INDICATOR AT 52.3.

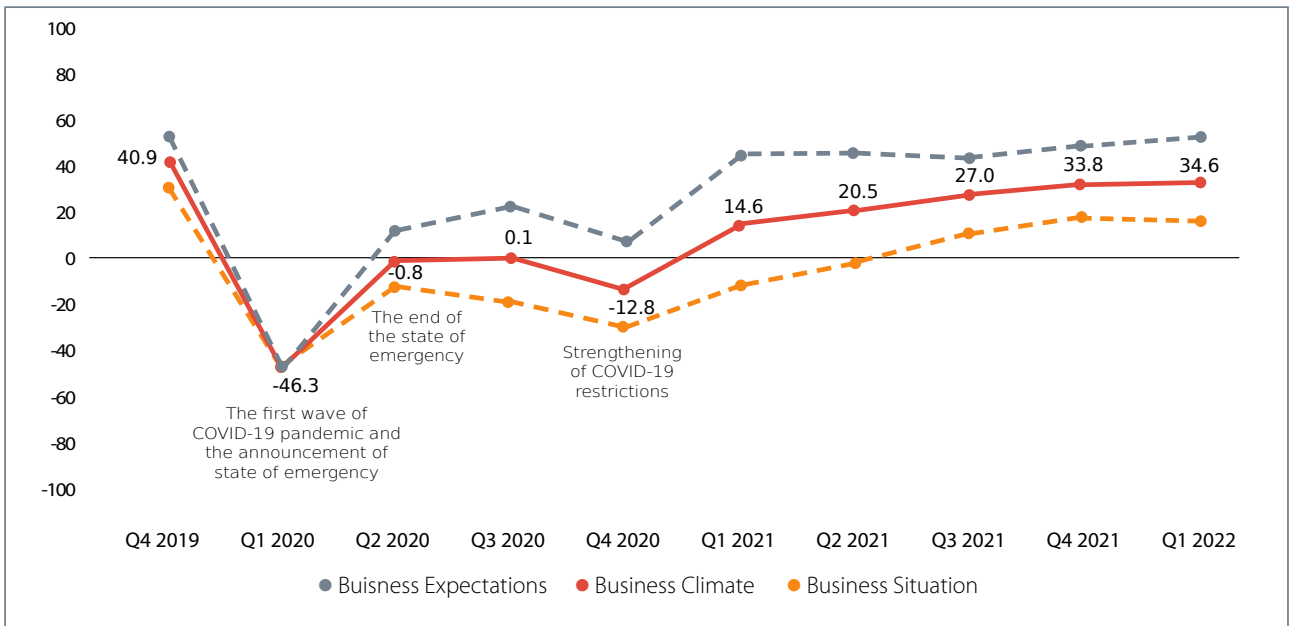
In Q1 of 2022, compared to Q4 of 2021, the BAG Business Climate improved by 0.8 points. Moreover, in this period, the assessment of the present business situation worsened (by 0.7 points) and business expectations improved (by 2.5 points).

The figures for Q1 of 2022 demonstrate an improvement compared to Q1 of 2021. In Q1 of 2021, the BAG Business Climate indicator was 14.6, the present business situation indicator equaled 11.8, while the business expectations indicator sat at 44.9.

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).

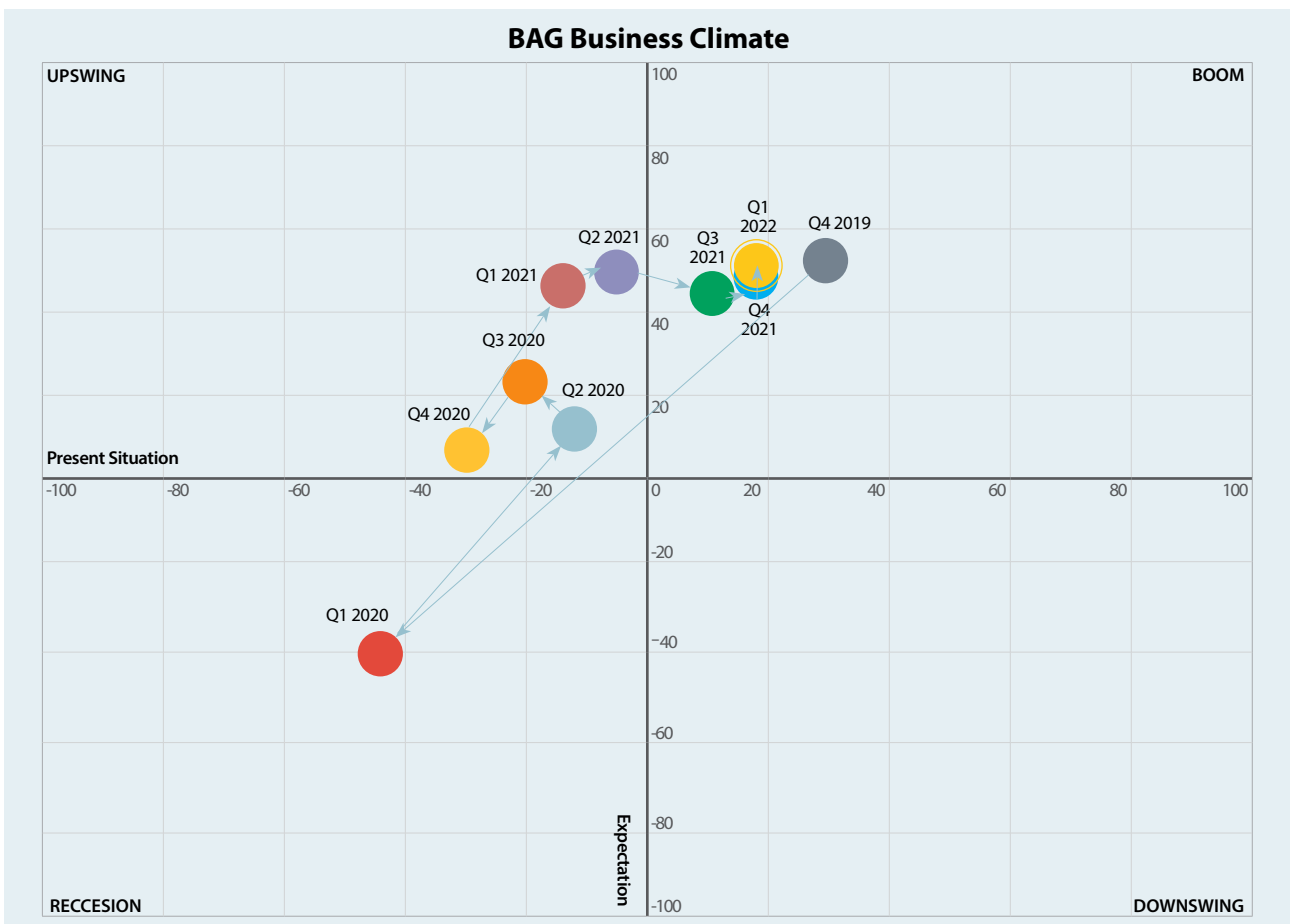
¹ In the first quarter of 2021, a change was made in the methodology of the BAG Index. As a result, the number of companies surveyed increased: enterprises that belong to the corporate group of member companies were added to the existing survey respondents.

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 Q1 of 2022, as in Q4 of 2021, 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

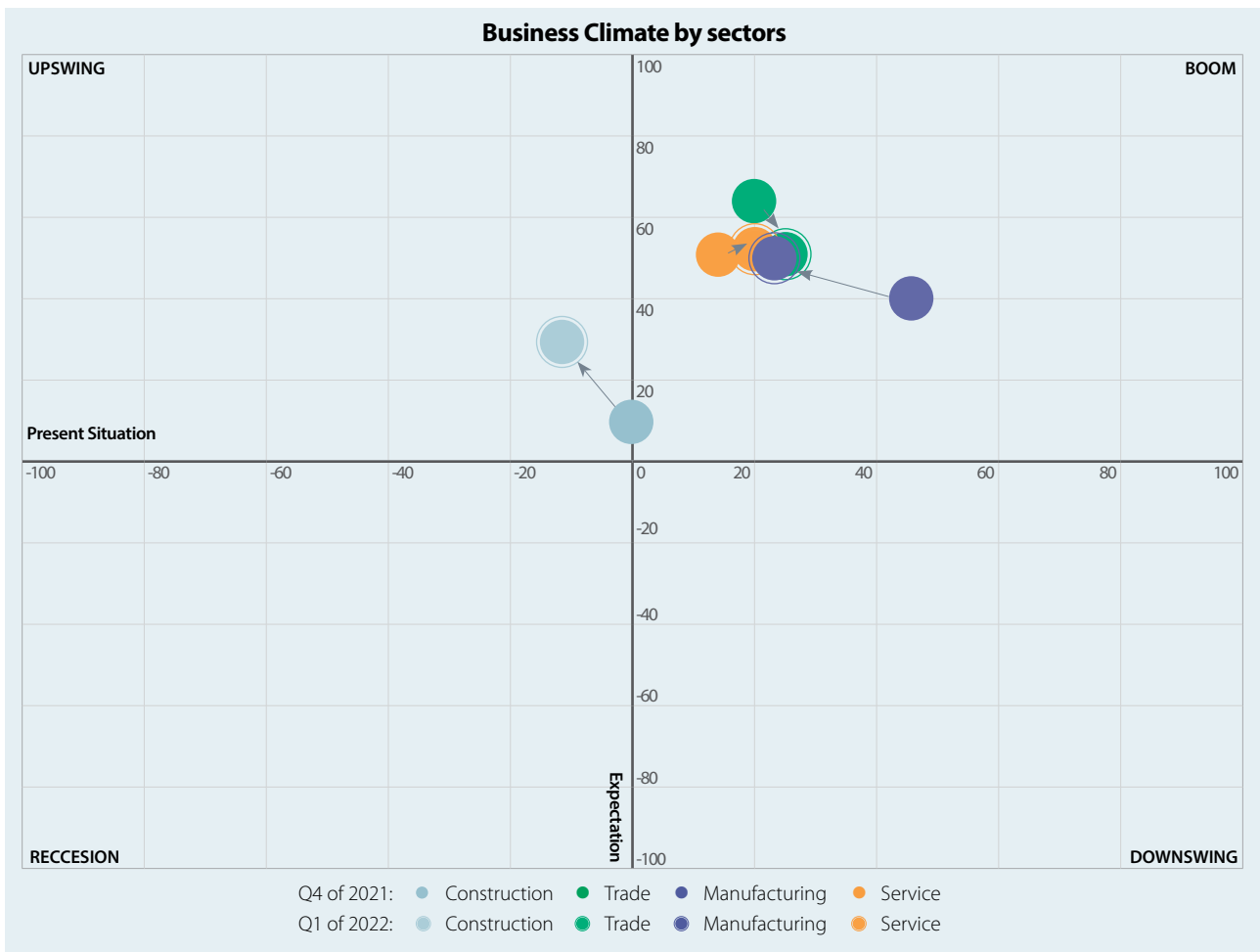
In Q1 of 2022, **the business climate indicator** was positive for all sectors. Compared to Q4 of 2021, in Q1 2022 the indicator improved in the construction and service sectors but worsened in the trade and manufacturing sectors (see Graph 3).

In Q1 of 2022, compared to Q4 of 2021, the **present business situation indicator** improved in trade and service sectors and worsened in manufacturing and construction sectors. Nevertheless, despite the overall view of the present business situation in manufacturing sector worsening, compared to the previous quarter, the surveyed businesses still assessed the present situation positively. Regarding the construction sector, it is worth noting that the indicator is negative. The negative assessment of present business situation in the construction sector could be attributed to decreased sales (37.5% of surveyed businesses stated that their sales decreased in Q1 2022 compared to Q4 2021 and only 13% stated an increase). The most positive assessment with respect to the present business situation was recorded in the trade sector.

In Q1 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 Q4 of 2021. Elsewhere, the business expectations indicator improved in service, construction and manufacturing sectors.

Table 1: Balance values by sector in Q1 of 2022

	Business Climate	Present Business Situation	Business Expectation
Trade Sector	38.7	24.3	54.1
Service Sector	37.1	20	55.6
Manufacturing Sector	36.4	23.5	50
Construction Sector	11.0	-12.5	37.5
All Sectors	34.6	18.1	52.3



Graph 3: Business Climate by sectors in Q4 2021 and Q1 of 2022

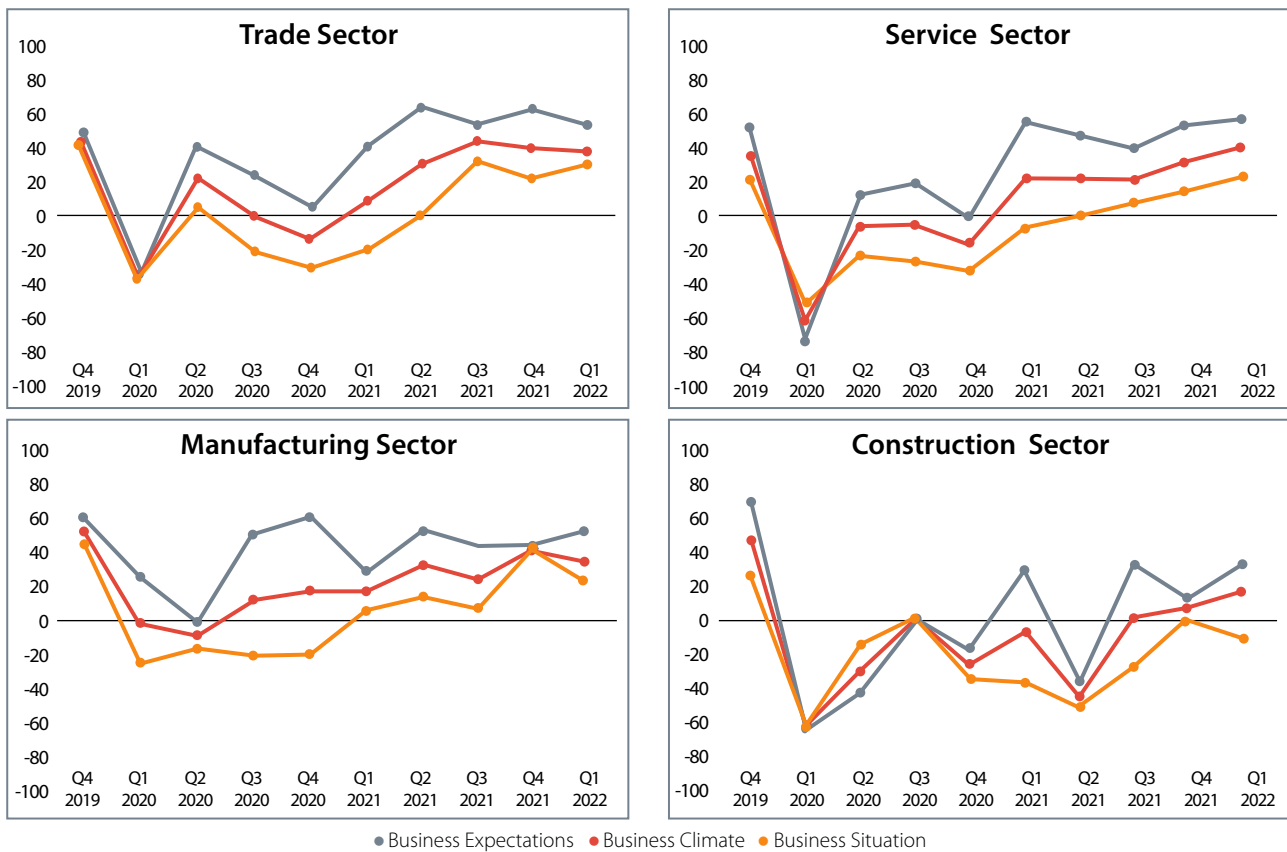
Since Q1 of 2021, the business climate indicator was consistently positive in the trade, manufacturing, and service sectors for the remaining quarters of 2021. In the construction sector however, the indicator was negative in Q1 and Q2 of 2021, however it turned positive in Q3 and Q4 as well as in Q1 of 2022, showing continued improvement compared to the previous quarters of 2021.

The business climate indicator has been improving for the trade sector specifically since Q1 of 2021, compared to the corresponding periods of the previous year. The positive business climate indicator in the trade sector reflects both positive expectations and positive assessments of the present business situation since Q2 of 2021.

Meanwhile, the business climate indicator in the service sector has been improving since Q1 of 2021 (except for a slight dip in Q3 of 2021) quarterly as well as YoY. The positive assessment of business climate could be due to positive business expectations and positive assessment of present business situation in the service sector since Q3 2021.

Similar to the trade and service sectors, in the manufacturing sector, since Q1 of 2021, the business climate indicator has been improving compared to the corresponding periods of the previous year. The positive business climate indicator in this sector is due to the optimistic outlook within the sector as well as the positive assessment of the present business situation.

Regarding the construction sector, the business climate indicator has been improving quarterly since Q3 of 2021. This improvement has been mainly due to the optimistic outlook under the business expectations element (see Graph 4).



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

EMPLOYMENT, SALES AND SALES PRICES BY SECTOR

Employment

Assessment of Q4 of 2021

- ✘ 32.7% of surveyed companies stated that the number of employees increased in Q4 of 2021, compared to Q3 of 2021. For the majority of respondents (60.7%) the number of employees was unchanged, while 6.6% reported a decrease.
- ✘ Across all sectors covered, the service sector was the one with the largest share of the surveyed companies (35.6%) claiming that the number of employees had increased in Q4 of 2021, compared to Q3 of 2021 (see Graph 5). This could be due to the rise in demand for production experienced by the majority of companies (57.8% of surveyed companies recorded an increase in demand for their production in Q4 of 2021).

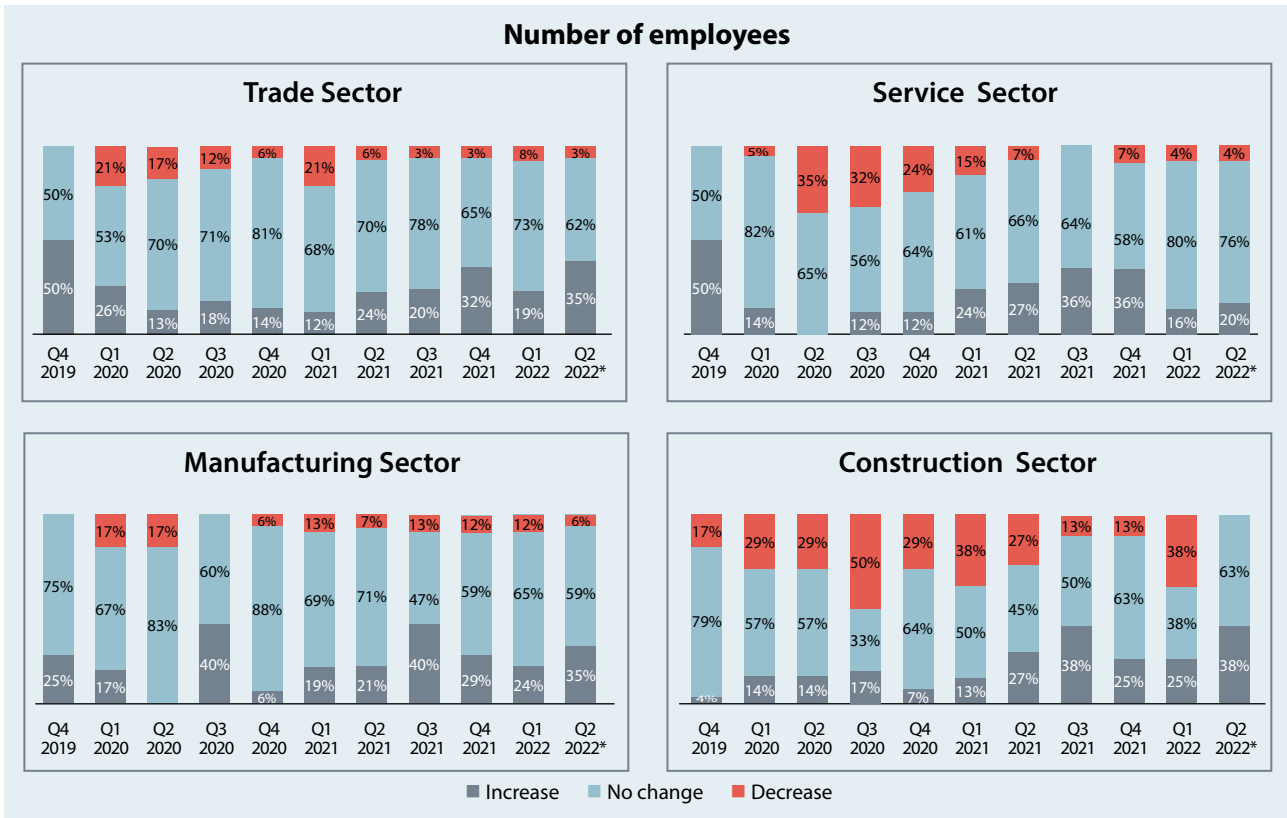
Situation in Q1 of 2022

- ✘ 18.7% of the surveyed companies stated that in Q1 of 2022, compared to Q4 of 2021, the number of employees increased, while 9.3% recorded a decrease. The majority of companies (72%) stated that their number of employees had not changed.
- ✘ A significant share of respondents in the manufacturing and construction sectors stated that the number of employees had increased in Q1 of 2022, compared to Q4 of 2021.

Expectations for Q2 of 2022

- ✘ 29% of the surveyed companies expect that in Q2 2022, compared to Q1 2022, the number of employees will increase, while 3.7% expect a decline. The majority of companies (67.3%) does not expect change in the number of their employees in this period.

- ✘ The most optimistic outlook regarding employment was found in the construction sector. 37.5% of the respondents in the construction sector stated that they expect an increase in the number of employees in Q2 2022, compared to Q1 2022, while none of the companies expect a decline. This could be explained by the optimistic outlook regarding sales in this sector.
- ✘ The largest share of respondents in the trade, manufacturing and service sectors expect that the number of employees will not change in Q2 2022, compared to Q1 2022 (62.2%, 58.8% and 75.6%, respectively).



Graph 5: The number of employees in trade, service, manufacturing and construction sectors³

In summary, the manufacturing and construction sectors appear to have been experiencing positive dynamics with regard to employment since Q1 of 2021, as throughout this period the share of the companies stating an increase in employment rose. However, in Q4 of 2021, compared to the previous quarter, this figure decreased for both sectors by 11 and 13 percentage points, respectively. Meanwhile, for Q2 of 2022, significantly higher shares of companies in both sectors are expected to increase their number of employees.

In the service sector, the share of companies to have recorded an increase in their number of employees has also been rising since Q1 of 2021. However, in Q1 of 2022, compared to the previous quarter, the relevant indicators decreased considerably, by 20 percentage points. It is expected that in Q2 of 2022, only 20% of companies in this sector will increase their number of employees.

Throughout 2021, unlike other sectors, the share of companies reporting an increase in their number of employees in the trade sector was relatively unstable. This figure fluctuated notably between 12% and 32% over the course of the year. Looking ahead to Q2 of 2022, it is expected that more companies in the trade sector will increase their number of employees.

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

* Expectation.

Sales/demand/domestic production

Assessment of Q4 of 2021

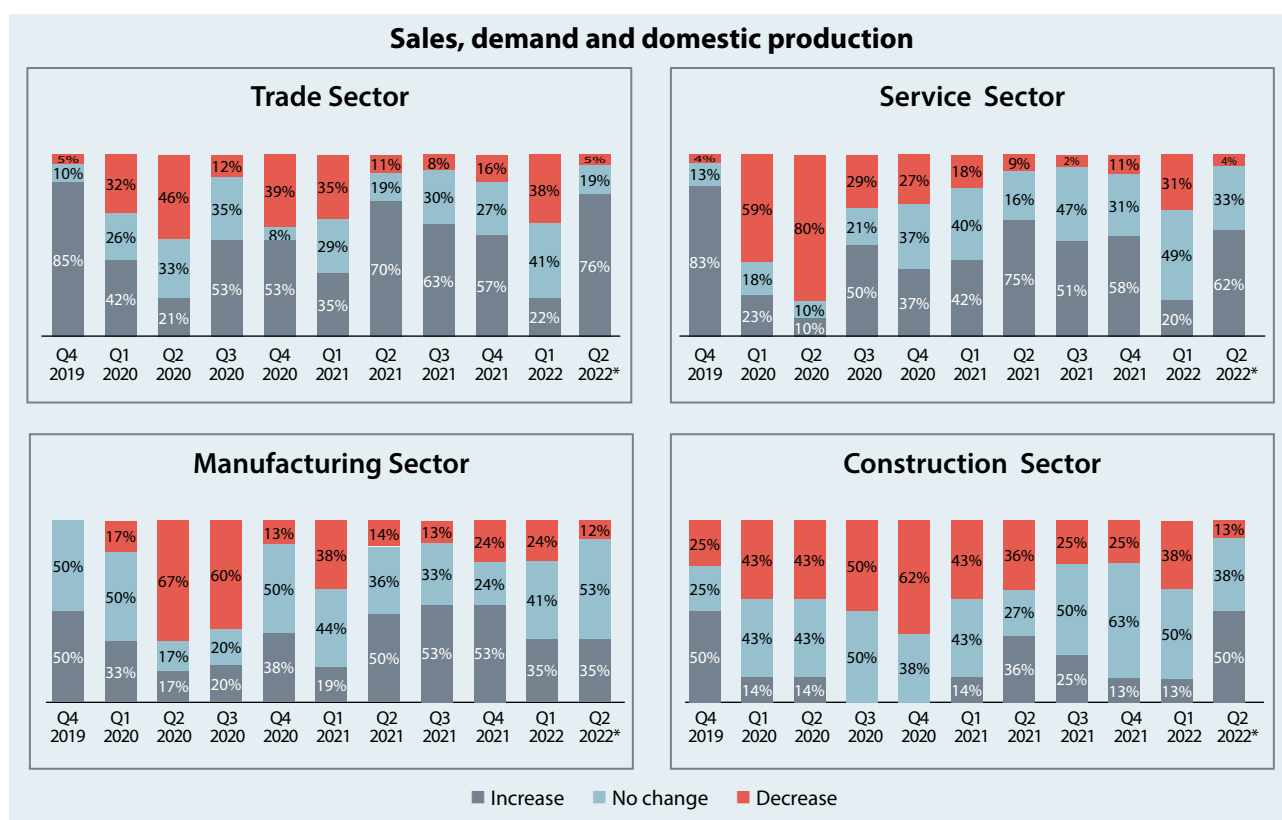
- ✘ More than half of the companies surveyed in the service, trade, and manufacturing sectors claimed that their sales increased in Q4 of 2021, compared to Q3 of 2021.
- ✘ In Q4 of 2021, the situation regarding sales was assessed most negatively in the construction sector, where 25% of surveyed companies stated that their contracts/presales had decreased, compared to Q3 of 2021 (see Graph 6).

Situation in Q1 of 2022

- ✘ In Q1 of 2022 the situation regarding sales was assessed the most positively by representatives of the manufacturing sector. 35.3% of surveyed companies recorded growth in sales in this period.
- ✘ In Q1 of 2022, the worst situation regarding sales was recorded in the trade and construction sectors. According to 37.8% and 37.5% of surveyed companies in each sector their sales decreased, compared to previous quarter.

Expectations for Q2 of 2022

- ✘ The most positive outlook for Q2 of 2022 regarding sales was recorded in the trade sector, where 75.7% of surveyed companies stated that they expect sales to increase.
- ✘ Comparing sectors, the highest share of companies to project sales to decrease in Q2 of 2022 was recorded in the construction (12.5%) and manufacturing (11.8%) sectors.



Graph 6: Sales, demand and domestic production in trade, service, manufacturing, and construction sectors

Overall, during 2021 there were some positive tendencies regarding sales in the trade, manufacturing, and service sectors, in which the majority of companies reported an increase in their quarter-on-quarter sales volumes. It is also worth noting that in Q1 of 2022, the proportions of companies in all three sectors to report such an increase dropped. However, for Q2 of 2022, a significant share of the companies in the trade, service, and construction sectors expect their sales to increase.

Compared to other sectors, the construction sector had the lowest share of companies to record an increase in sales during 2021 and Q1 of 2022. However, in Q2 of 2022, 50% of the companies in this sector expect an increase in sales.

Sales prices

Assessment of Q4 of 2021

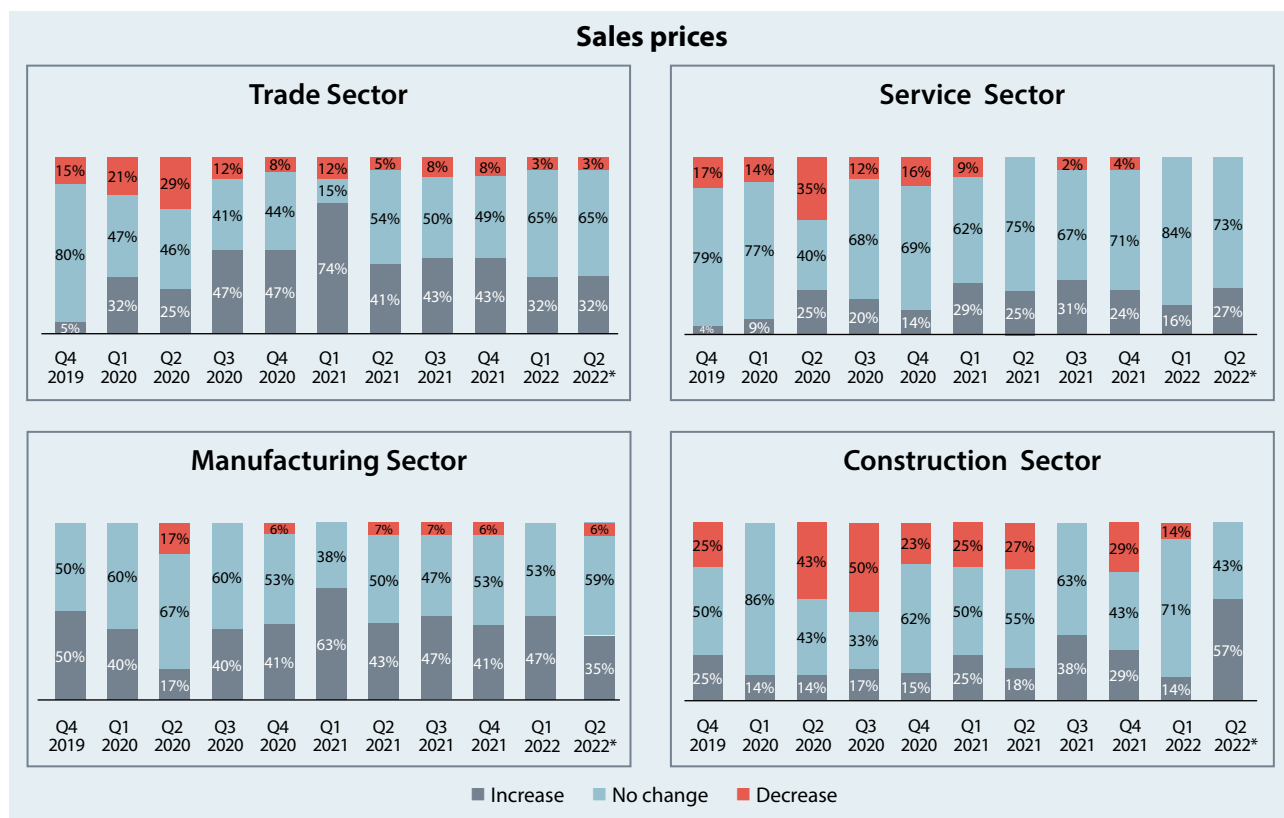
- ✘ A large share of surveyed companies (58.5%) stated that in Q4 of 2021, compared to Q3 of 2021, sales prices had not changed, while 34% stated that prices had gone up. According to 7.5% of respondents, sales prices had decreased in this period.
- ✘ Across the covered sectors, the majority of surveyed companies in all sectors stated that prices had not changed in Q4 of 2021, compared to Q3 of 2021. However, it must be noted that in trade and manufacturing sectors 43.2% and 41.2% of the companies stated an increase in sales prices in Q4 of 2021.

Situation in Q1 of 2022

- ✘ 26.4% of the surveyed companies stated that in Q1 of 2022, compared to Q4 of 2021, sales prices had increased, while 71.1% stated that sales prices remained unchanged, 1.9% claimed that sales prices had decreased.
- ✘ The most positive outlook regarding sales prices is recorded in manufacturing sector with 47.1% of surveyed companies stating that sales prices had increased in Q1 of 2022, compared to previous quarter.

Expectations for Q2 of 2022

- ✘ 32.1% of surveyed companies expect sales prices to increase in Q2 of 2022, compared to Q1 of 2022, while 66% do not expect this figure to change, and only 1.9% of the companies expect a decrease.
- ✘ Across the covered sectors, the construction sector had the largest share of respondents (57.1%) expecting an increase in sales prices in Q2 of 2022, compared to Q1 of 2022.

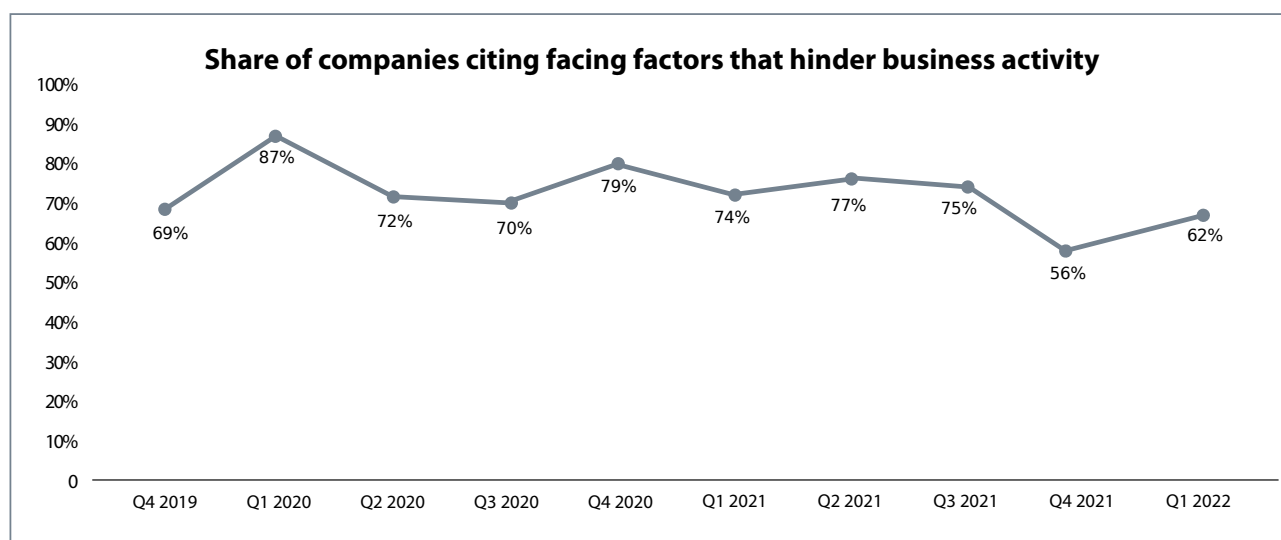


Graph 7: Sales prices in trade, service, manufacturing, and construction sectors

In summary, since Q2 of 2021, among all of the covered sectors, sales prices did not change in the majority of the surveyed companies. However, throughout 2021 a significant proportion (at times more than 40%) of companies in the trade and manufacturing sectors recorded an increase in their sales prices. In Q1 of 2022, in all four sectors, the proportion of companies reporting no change in their prices increased considerably.

FACTORS HINDERING BUSINESS ACTIVITY

In Q1 of 2022, compared to Q4 of 2021, the share of surveyed companies to claim there are factors hindering their business activity increased (by 6 percentage points). It must be noted that, in Q1 of 2022, compared to Q1 of 2021, the share of companies claiming that there are factors hindering their business activity decreased markedly (by 12 percentage points).



Graph 8: Existence of factors hindering business activity

In Q1 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 weak demand for products and services (see Graph 9).

In Q1 of 2022, similar to the previous two quarters, the volatility of the national currency exchange rate was cited as the top factor hindering business (62% of surveyed companies cited this factor as the most hindering). From a sector-by-sector view, this factor was cited by 71% of companies in the construction sector, 68% in the trade sector, 58% in the service sector, and 55% in the manufacturing sector.

In terms of size of enterprise⁵, the volatility of the national currency exchange rate was most cited by small enterprises as a factor hindering business activity (73% of surveyed small companies cited this factor as hindering). Meanwhile, it was cited by 63% of medium enterprises and by only 56% of large enterprises.

In Q1 of 2022, legal and administrative barriers was the second-most cited hindering factor (cited by 44% of surveyed companies). Across the covered sectors, this factor was most frequently pointed out in the construction sector (71% of surveyed companies in this sector cited this factor as the most hindering) and was considered least hindering for the manufacturing sector (9%). In the service and trade sectors, this factor was cited by 54% and 41% respectively of surveyed companies as a factor hindering business activity.

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

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

Legal and administrative barriers are most hindering for large enterprises (59% of them cited this factor as hindering), while only 33% of small and medium enterprises cited this factor as hindering.

In Q1 of 2022, a lack of specialists was cited as a hindering factor by 38% of surveyed companies. This issue was felt most acutely in the trade (41%) and manufacturing (36%) sectors, while it was less of a hindrance for the service (35%) and construction (29%) sectors.

A lack of specialists was considered most problematic for small enterprises (cited by 40% of them as a hindering factor), while 38% of medium enterprises and 37% of large enterprises cited this factor as a hindrance to their business activity.

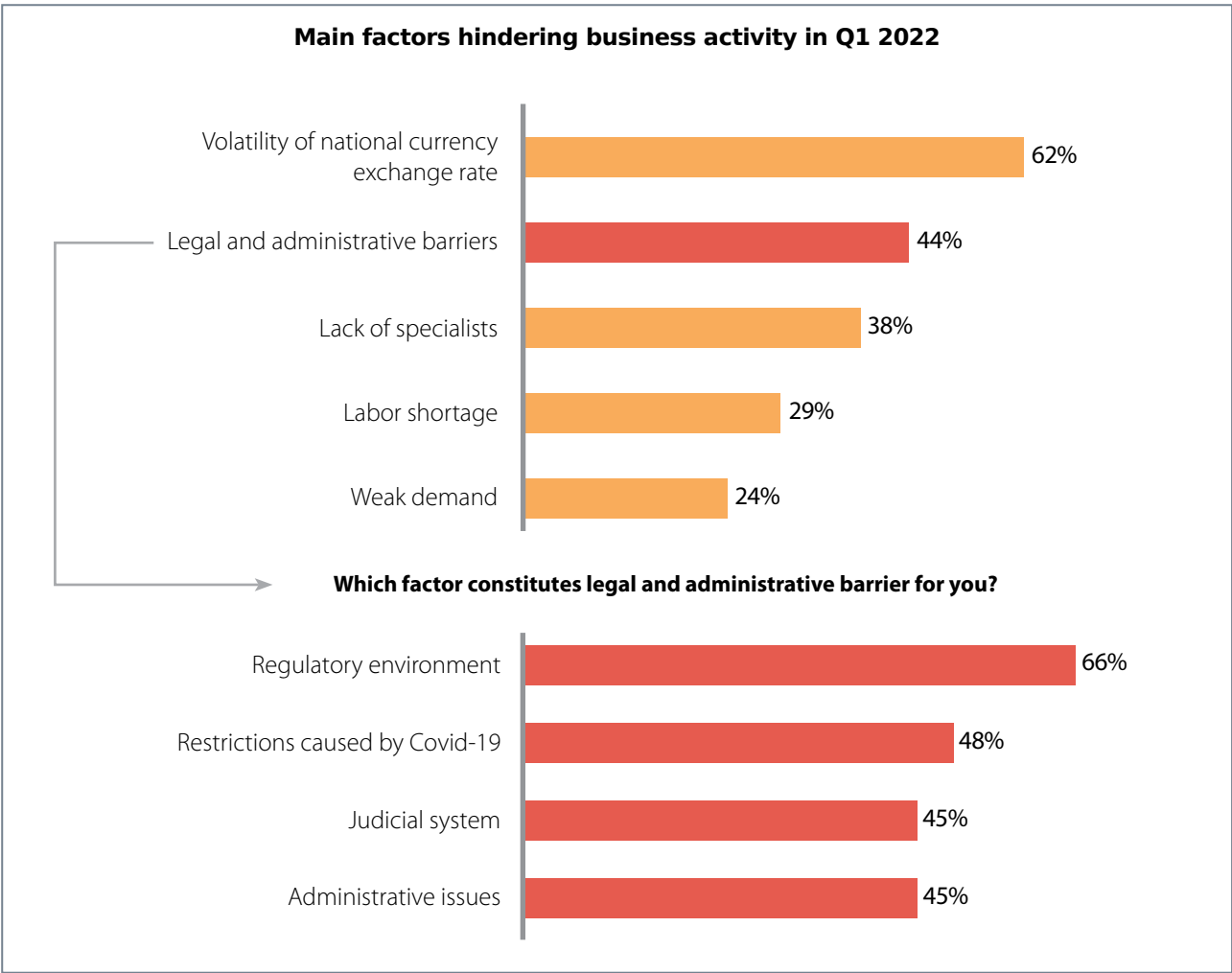
In Q1 of 2022, labor shortage was cited as a hindering factor by 29% of surveyed companies. Across the covered sectors, this factor was deemed most hindering for the trade sector (41%), while only a small share of companies in the construction and service sectors described this factor as hindering (14% and 19%, respectively). In the manufacturing sector, this came in at 27% which was close to the overall average.

In Q1 of 2022, labor shortage was considered most problematic for large enterprises (cited by 37%). Meanwhile, this factor was cited by just 13% of small enterprises and 29% of medium enterprises as hindering their business activity.

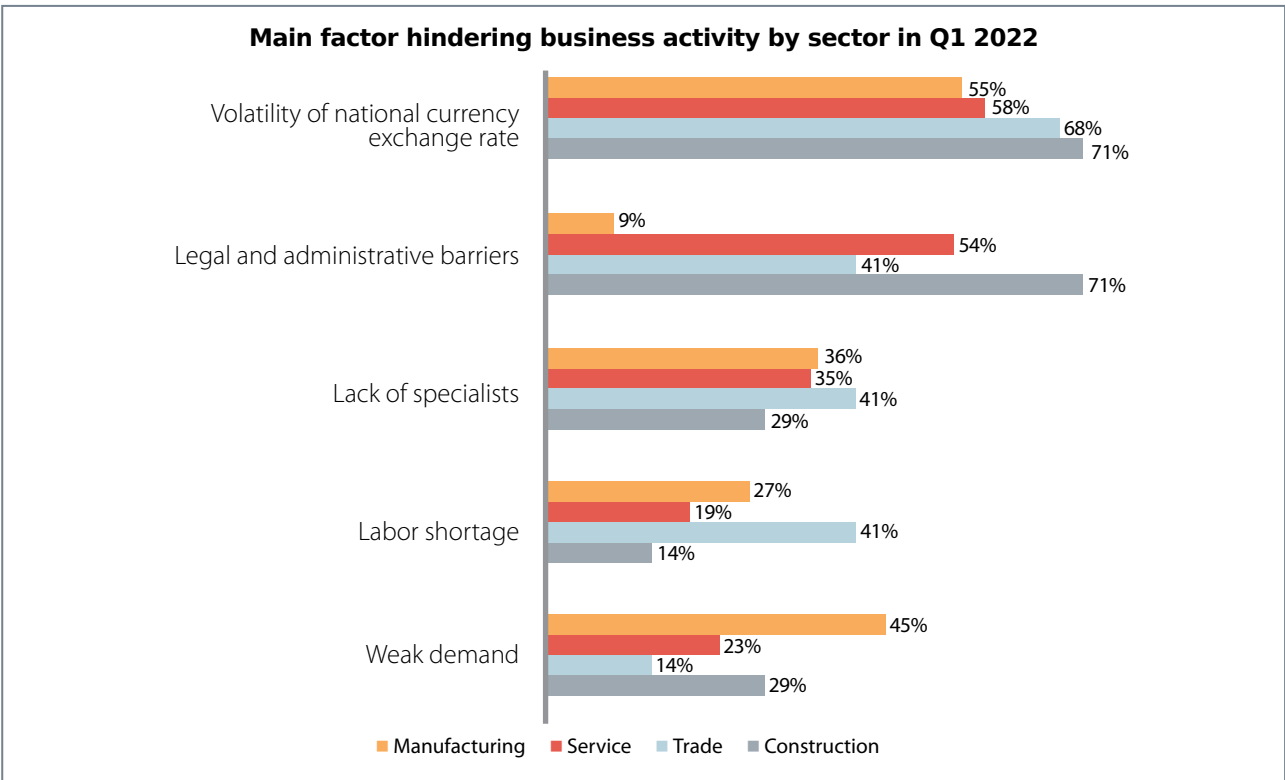
Weak demand for products and services was cited as a hindering factor by 24% of the surveyed companies in Q1 of 2022. This factor was most cited in the manufacturing sector (45%) and least cited in the trade sector (14%), while this indicator was close to the average value for both the service (23%) and construction (29%) sectors (see Graph 10).

The issue of weak demand was cited as a hindering factor to a similar degree across all four sectors. Indeed, it was cited as hindering by 22% of large enterprises, 21% of medium enterprises, and 20% of small enterprises.

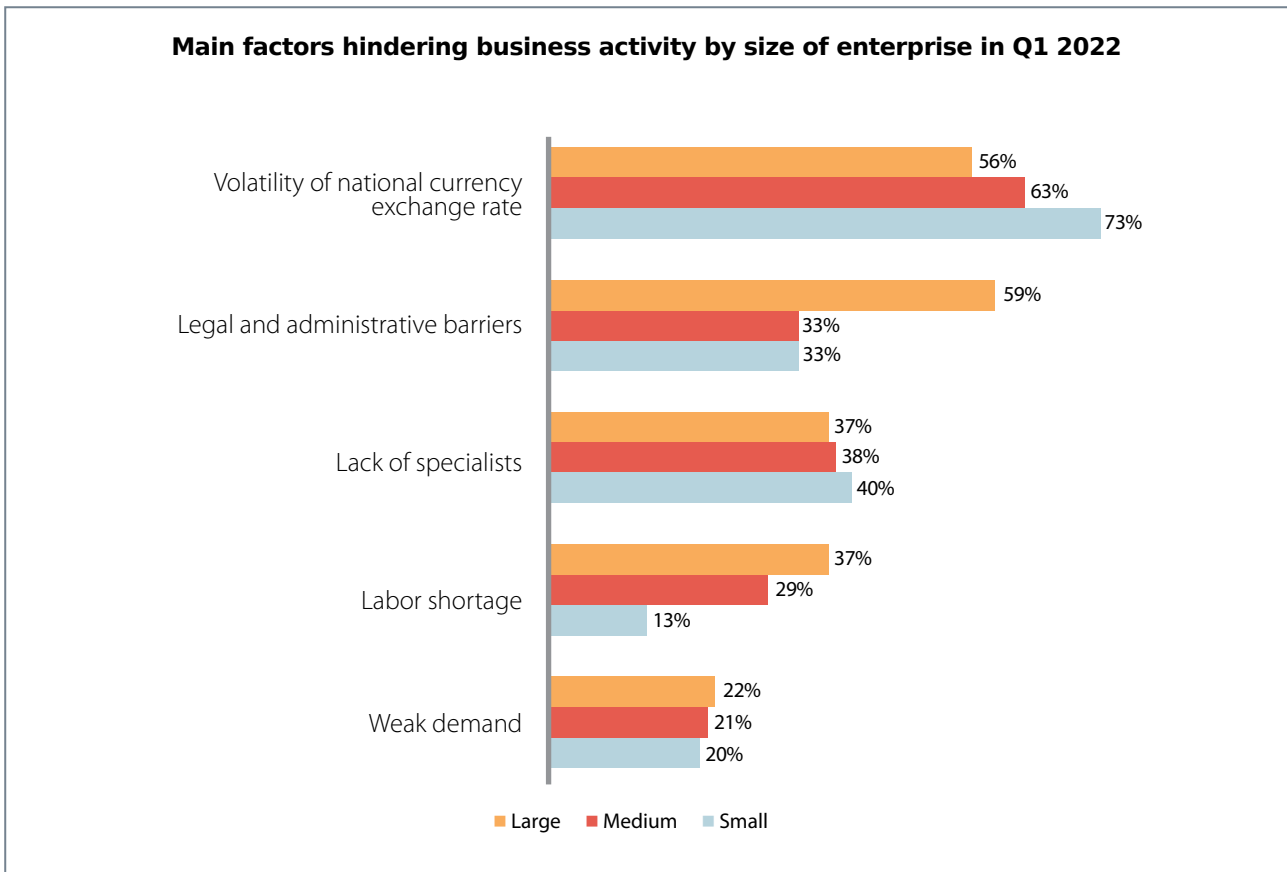
In Q1 of 2022, compared to Q4 of 2021, among the factors hindering business activity, the share of companies citing legal and administrative barriers decreased by 8 percentage points, while citations of the volatility of the national currency exchange rate decreased by 3 percentage points. Elsewhere, the share of companies citing weak demand as a hindering factor increased the most (by 7 percentage points) over the same period.



Graph 9: Main factors hindering business activity for surveyed companies in Q1 2022



Graph 10: Main factors hindering business activity by sector in Q1 2022



Graph 11: Main factors hindering business activity by size of enterprise in Q1 2022

Legal and administrative barriers

In Q1 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 construction (80%) and service (86%) sectors. The regulatory environment is deemed less hindering for the trade sector (cited by 33% of surveyed companies, while no companies surveyed in the manufacturing sector cited the regulatory environment as a hindering factor).

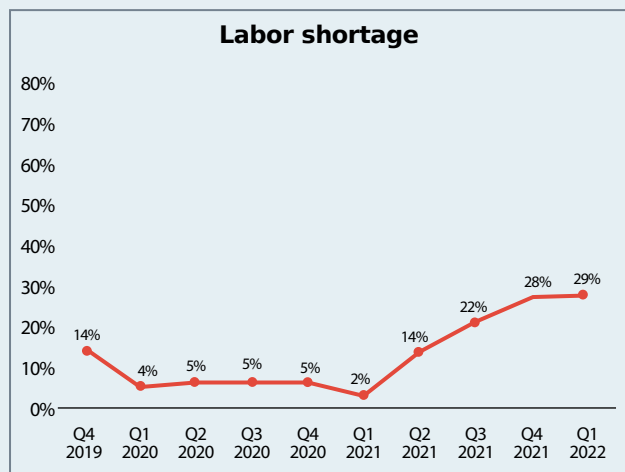
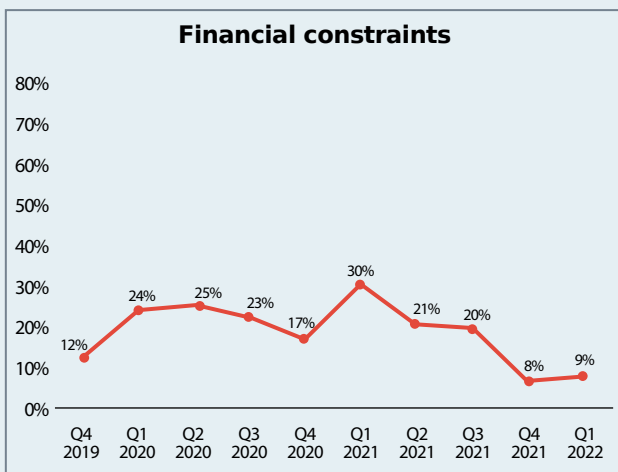
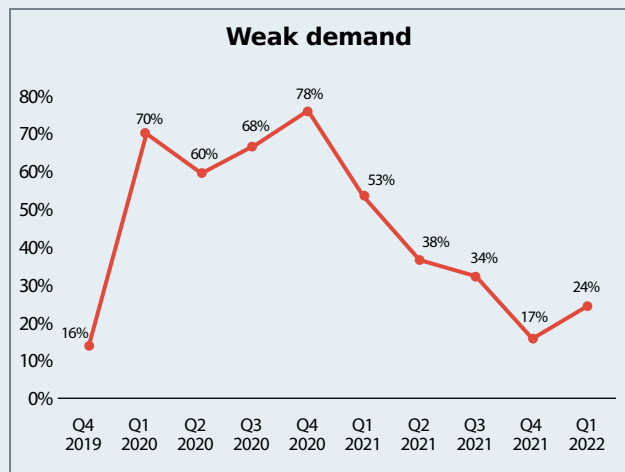
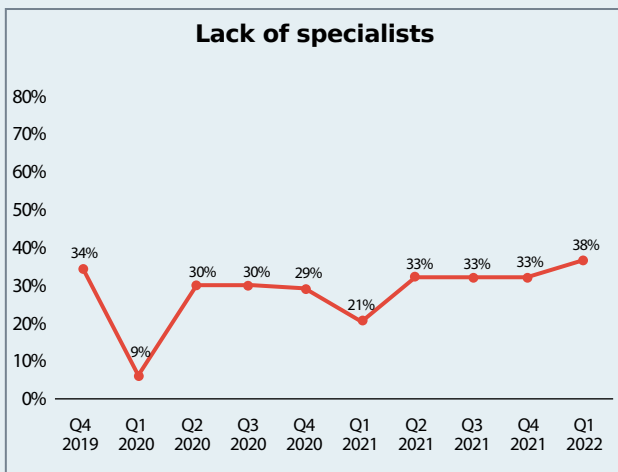
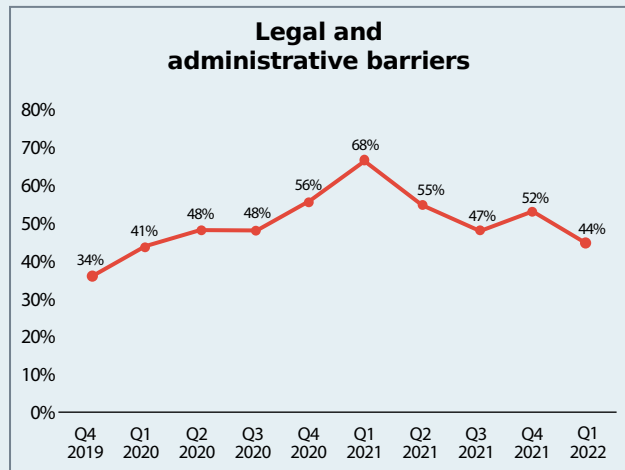
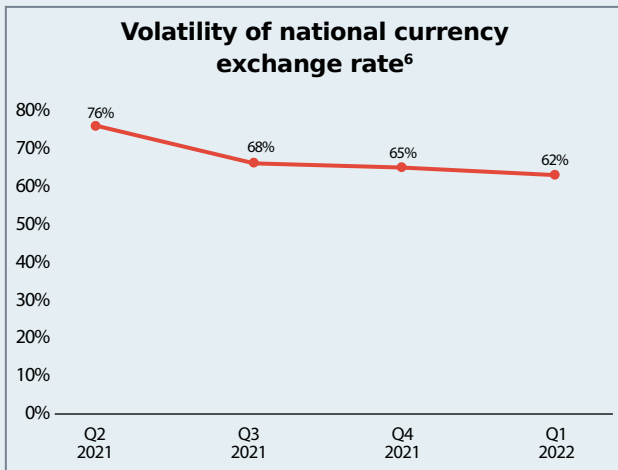
Among legal and administrative barriers, COVID-19-related restrictions were the second-most cited hindering factor. This was deemed the most hindering in the trade sector (78%), while for the manufacturing sector COVID-19-related restrictions were not considered a hindrance.

Meanwhile, the judicial system was the most cited as a hindering factor under legal and administrative barriers in the construction sector (cited by 60% of companies), while for the trade sector the judicial system was perceived as less of a hindrance (only 11% of surveyed companies in this sector cited it as a hindering factor).

Administrative issues were the most cited as hindering in the construction sector (cited by 80%), while it was least cited in the trade sector (22%).

In summary, in Q1 of 2022, compared to the previous quarter, the share of companies to cite the regulatory environment as a hindering factor decreased (by 5 percentage points), while the share of companies citing administrative issues as a hindering factor increased the most (by 16 percentage points).

Hindering factors for business activity Q4 2019-Q1 2022



Graph 12: Main hindering factors for surveyed companies

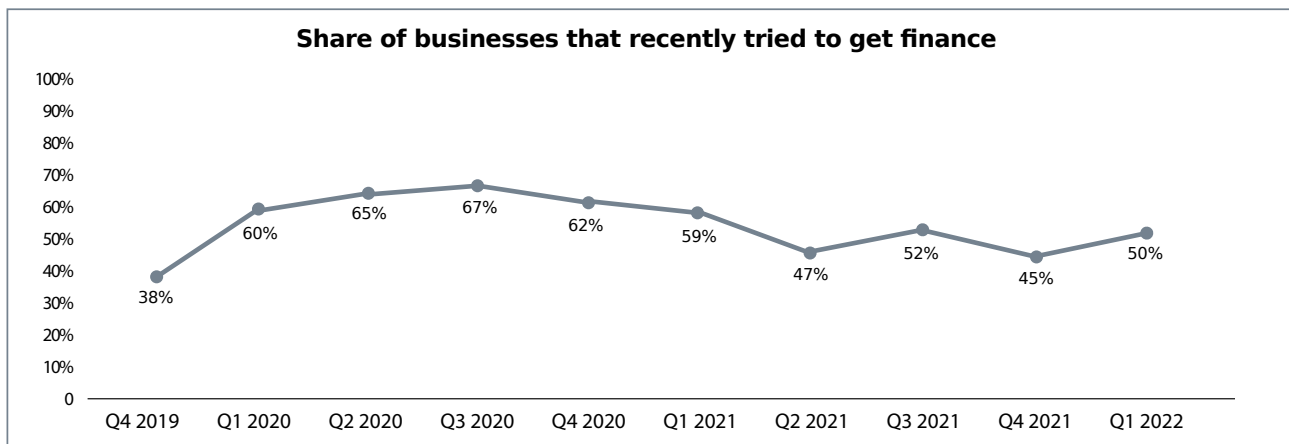
⁶ Volatility of national currency exchange rate as a factor hindering business was added to the survey questionnaire in Q2 of 2021.

FINANCING

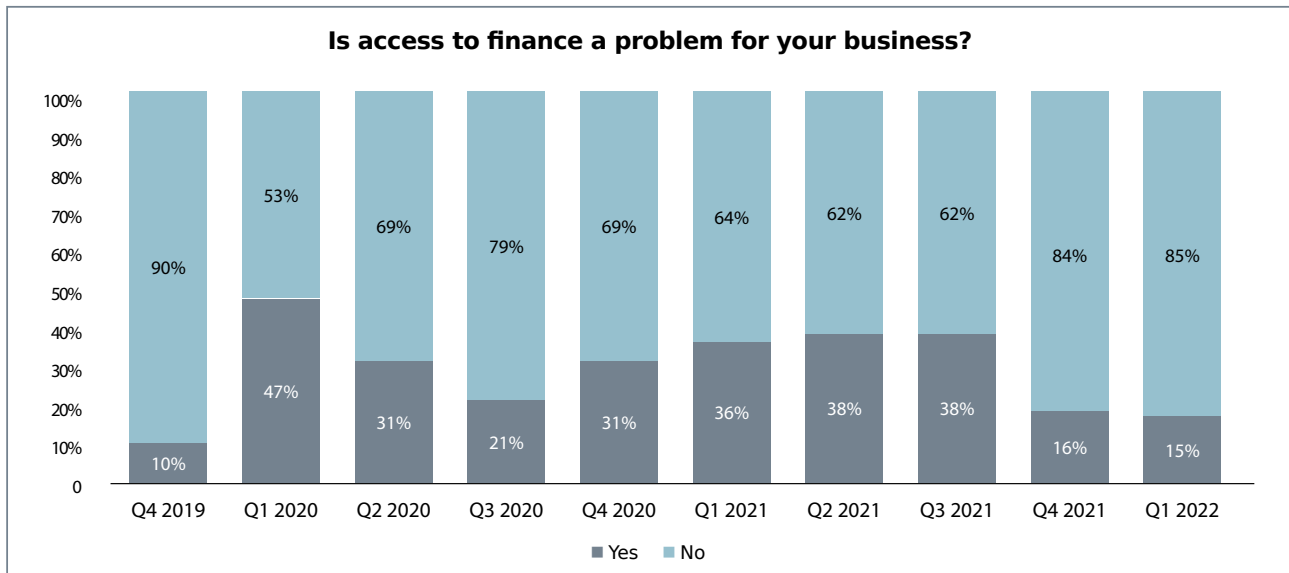
In Q1 of 2022, 50% of surveyed companies claimed to have recently tried to obtain finance, which is 5 percentage points higher than the figure recorded in the previous quarter (see Graph 13).

In Q1 of 2022, 15% of those companies that recently tried to access finance also noted that access to finance was a problem for their business. This figure is slightly lower (1 percentage point) than that of previous quarter (see Graph 14).

From an enterprise size perspective, in Q1 of 2022, access to finance was most cited as a problem by small enterprises (22% of surveyed small enterprises that tried to obtain finance recently). Access to finance was considered less problematic for large enterprises (only 13% cited it as a problem), while 16% of medium enterprises stated that access to finance was a problem for their business.



Graph 13: Businesses that recently tried to get finance

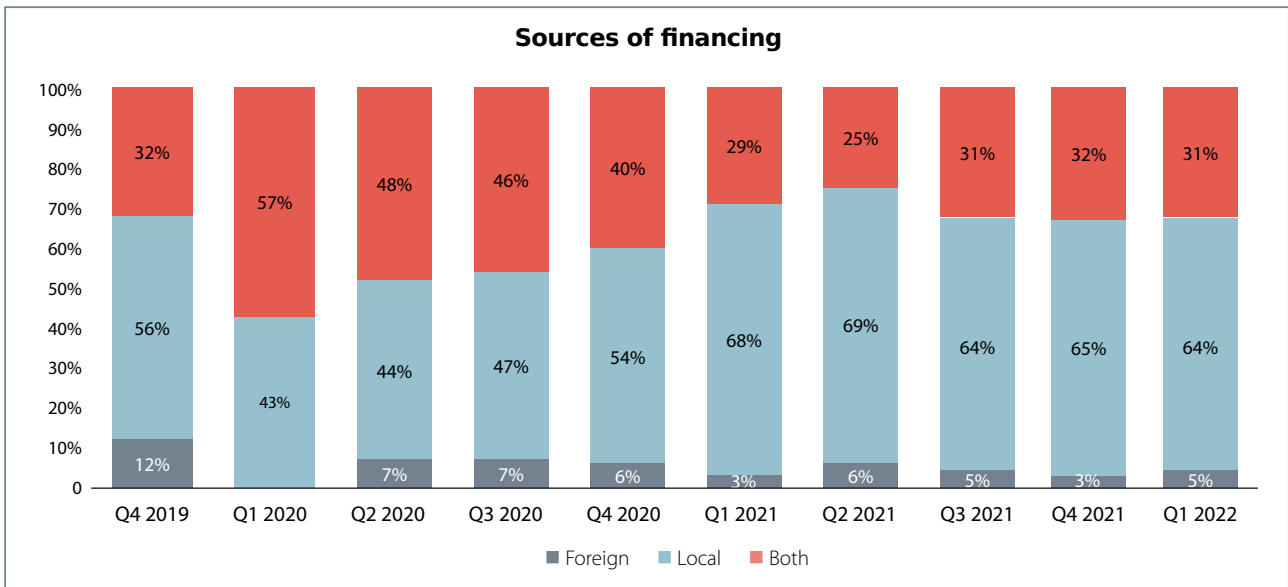


Graph 14: Access to finance⁷

Regarding sources of financing⁸, in Q1 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 increased by 2 percentage points in Q1 of 2022, compared to the previous quarter.

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

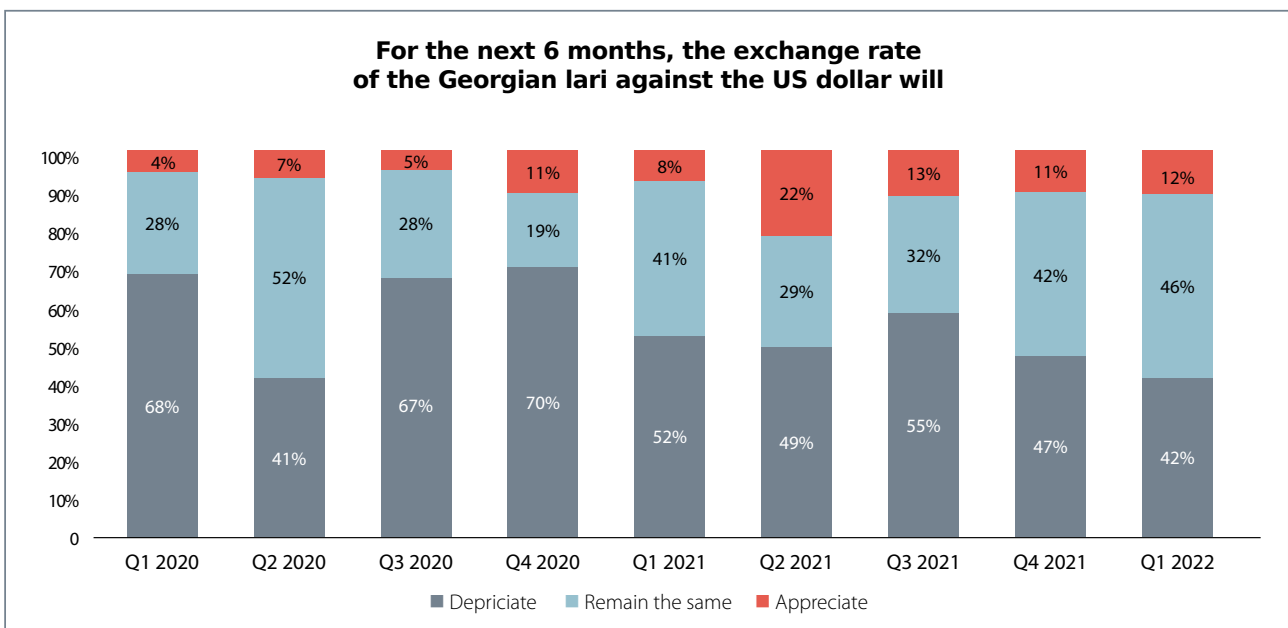
⁸ The change in methodology in Q1 of 2021 (i.e. the increase in the number of surveyed companies) altered the financing structure. This methodological change did not significantly affect any other indicators.



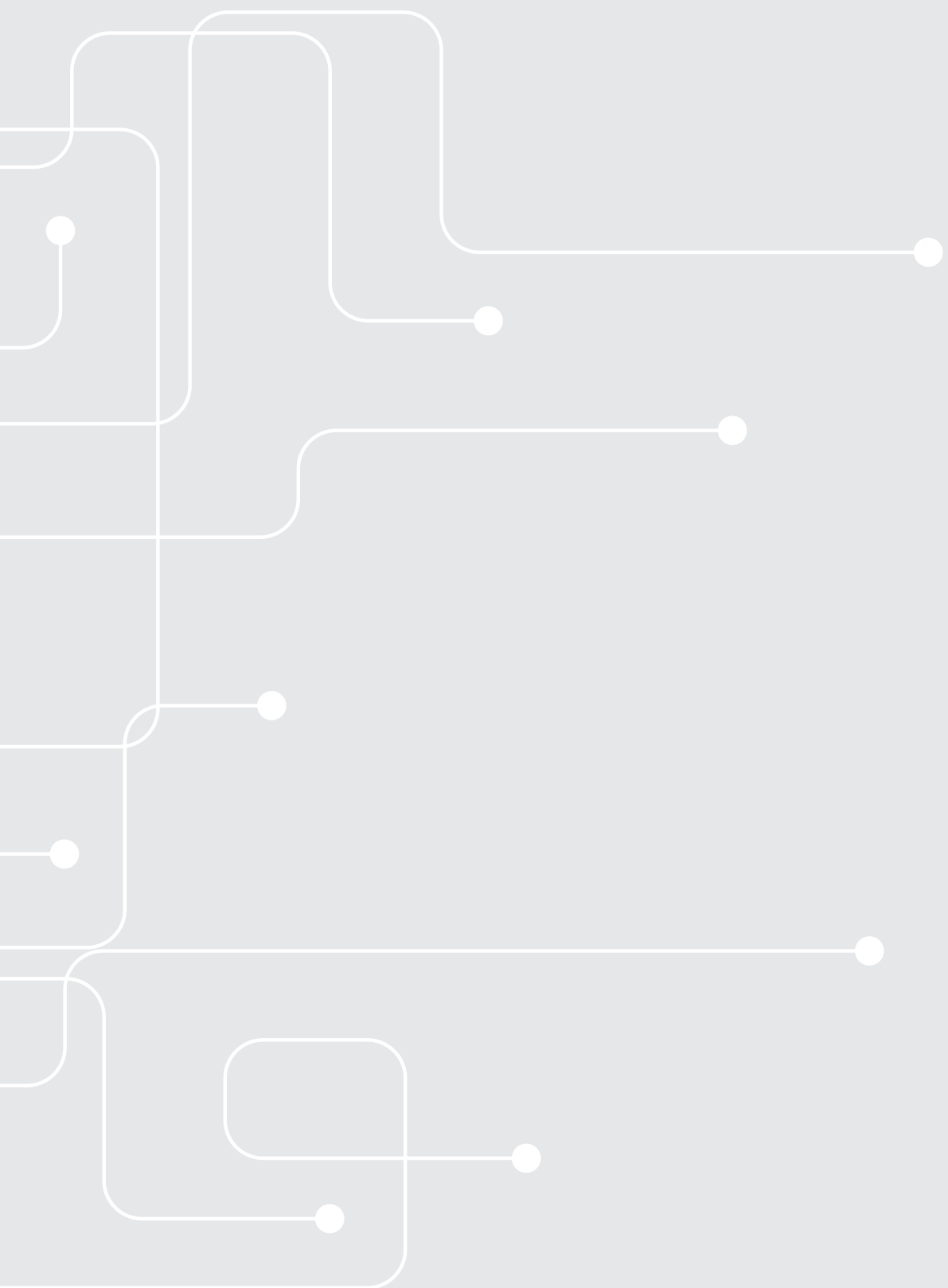
Graph 15: Sources of financing

EXCHANGE RATE EXPECTATIONS

In Q1 of 2022, compared to Q4 of 2021, the share of companies expecting that the national currency would depreciate against the US Dollar decreased by 5 percentage points. Moreover, in Q1 of 2022, compared to the previous quarter, the share of companies expecting that the national currency exchange rate would remain the same throughout the next 6 months, increased by 4 percentage points.



Graph 16: Exchange rate of the Georgian Lari against the US Dollar



CONTACT:

2 Leonidze Street, Tbilisi, Georgia

☎ +995 32 2 202-215

✉ info@bag.ge

f Business Association of Georgia

www.bag.ge