

BAG INDEX

Index for the Business Association of Georgia

**IV QUARTER
2020**



Research

BAG INDEX

IV QUARTER, 2020

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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 and BAG Employment Barometer, which are calculated according to the assessments of the top managers of BAG member businesses. The report also includes analysis of the impact of COVID-19 on the members of BAG. 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. Companies assess their present business situation and outline their expectations for the next six months. They can describe their present business situation as “good,” “satisfactory” or “bad” and their expectations for the next six months can be categorized as “more favorable,” “unchanged” or “less favorable.” The BAG Business Climate is a transformed mean of the balance values¹ of the present business situation and the expectations for the next six months. For the purposes of this index, BAG members are divided into the following four sectors: trade, manufacturing, construction, and service.

Apart from assessing their present business situation and expectations for the next six months, BAG member businesses are also asked to assess their situation regarding sales prices, sales/turnover/demand, and the number of employees for the last quarter and the next quarter. Moreover, businesses are asked questions related to factors hindering their business activity, access to finance and exchange rate expectations.

BAG BUSINESS CYCLE CLOCK

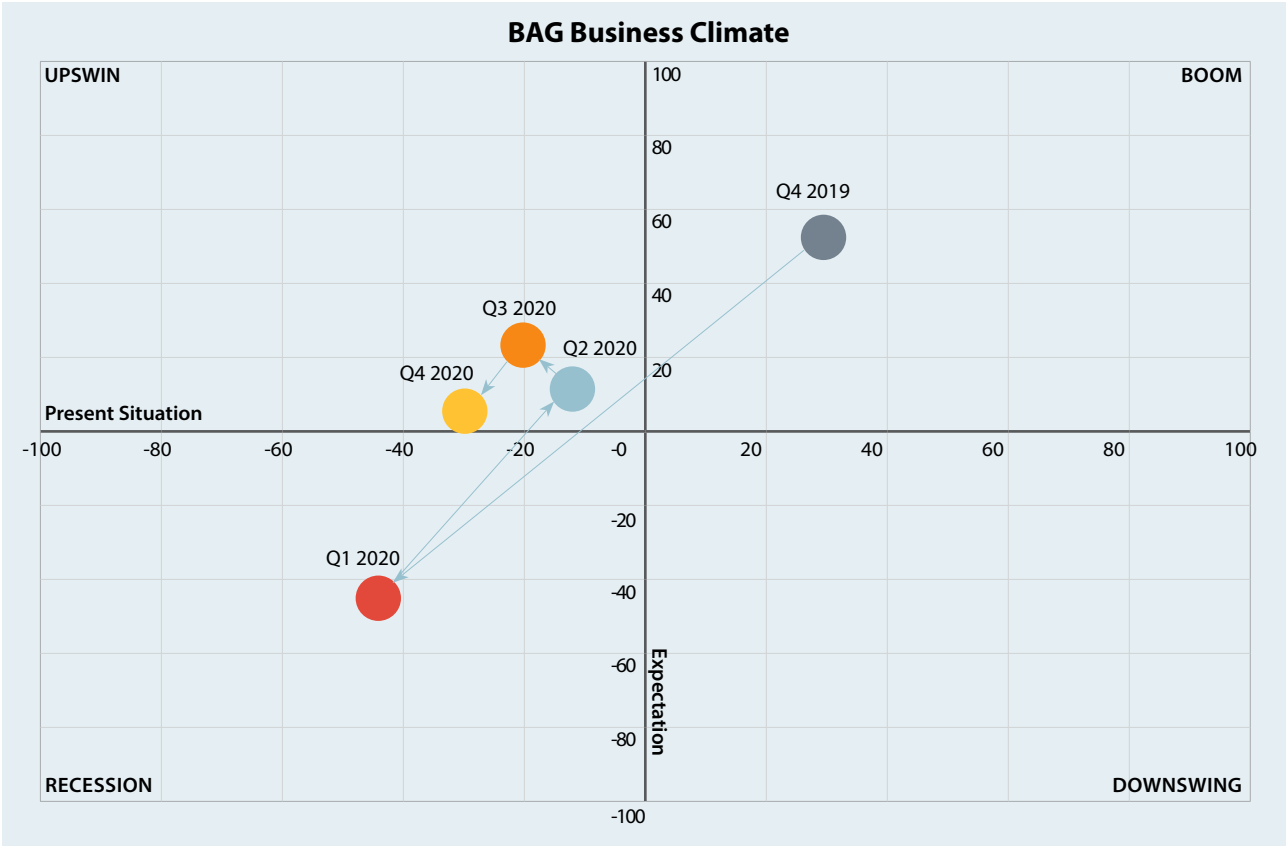
The BAG Business Cycle Clock depicts the relationship between the present business situation and business expectations for the next six months in a four-quadrant diagram. The quadrants are labeled “upswing,” “boom,” “downswing,” and “recession” and each of these are explained below:

- ✘ 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.

¹ 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 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 negat

IN Q4 OF 2020, BAG MEMBER BUSINESSES ASSESS THEIR PRESENT BUSINESS SITUATION **NEGATIVELY**, WHILE THEIR EXPECTATIONS FOR THE NEXT SIX MONTHS ARE **POSITIVE**. IN Q4 OF 2020, THE BAG BUSINESS CLIMATE INDICATOR AMOUNTS TO -12.8 POINTS, WITH THE PRESENT BUSINESS SITUATION INDICATOR SITTING AT -30 AND THE BUSINESS EXPECTATIONS INDICATOR AT 6.5.

It has to be noted that in Q4 of 2020, compared to Q3, assessment of BAG Present Business Situation and BAG Business Expectations has worsened.

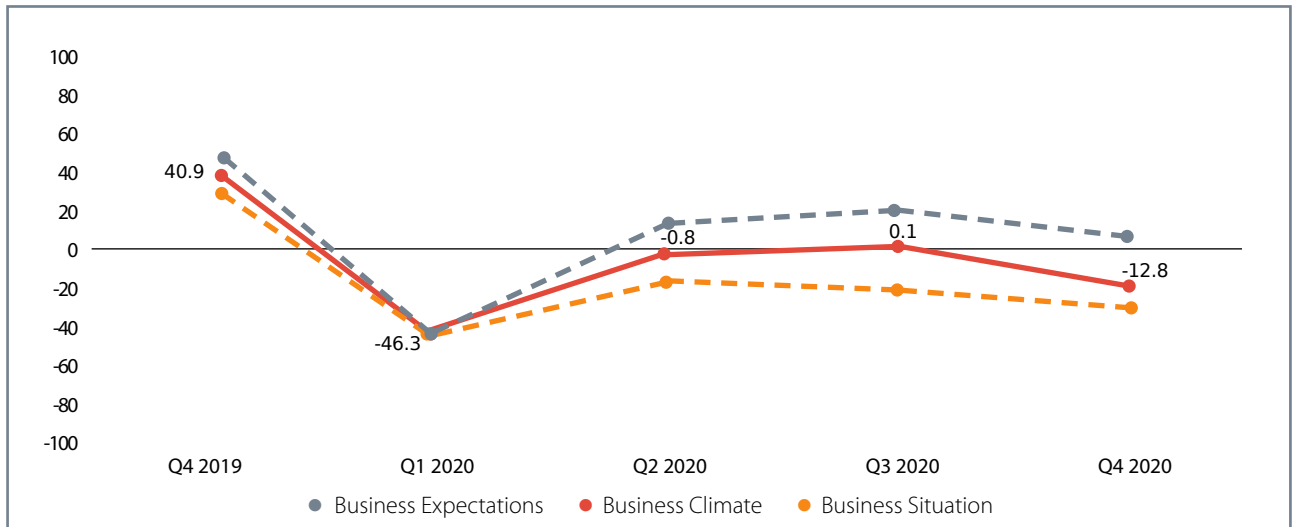


Graph 1: BAG Business Climate

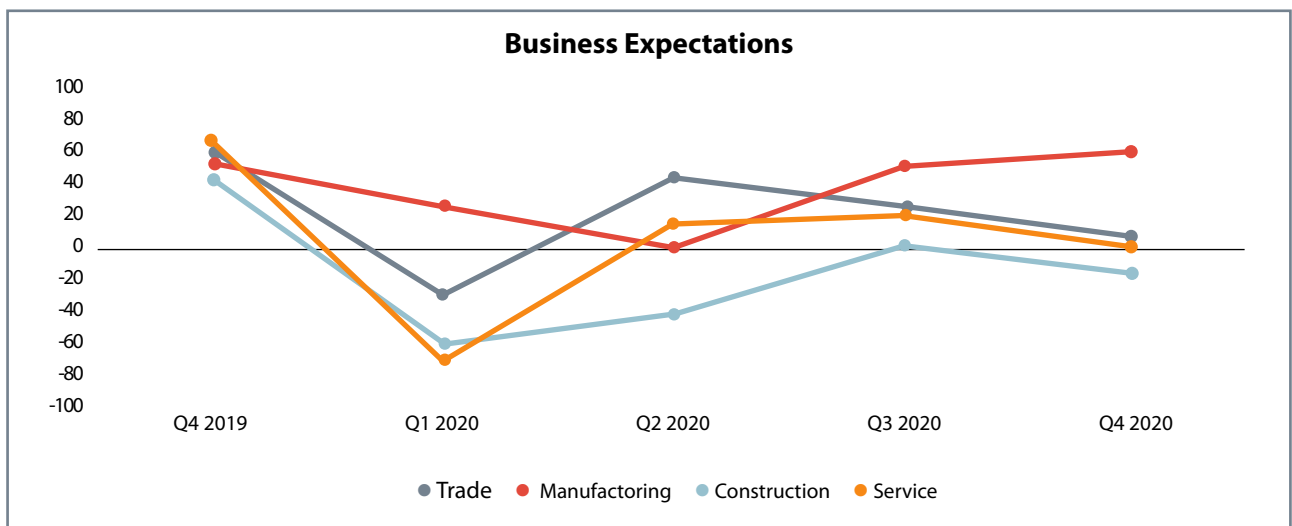
In Q4 of 2020, the BAG Business Climate indicator is negative for all sectors except the manufacturing sector. The positive business climate indicator in manufacturing sector results from a positive assessment of the business expectations. Meanwhile, business expectations are also positive in the trade sector. This indicator is negative only for the construction sector. However, the assessment of the business situation in all four sectors is negative. The most negative assessment of the present business situation per sector was in the construction.

Table 1: Balance values by sector in the IV quarter of 2020

	Business Climate	Present Business Situation	Business Expectation
Trade Sector	-12.4	-29.4	6.3
Manufacturing Sector	16.3	-20.0	60.0
Construction Sector	-25.2	-33.3	-16.7
Service Sector	-16.7	-32.0	0.0



Graph 2: BAG Business Climate, Business Expectation, and Present Business Situation



Graph 3: Expectation for the next six months



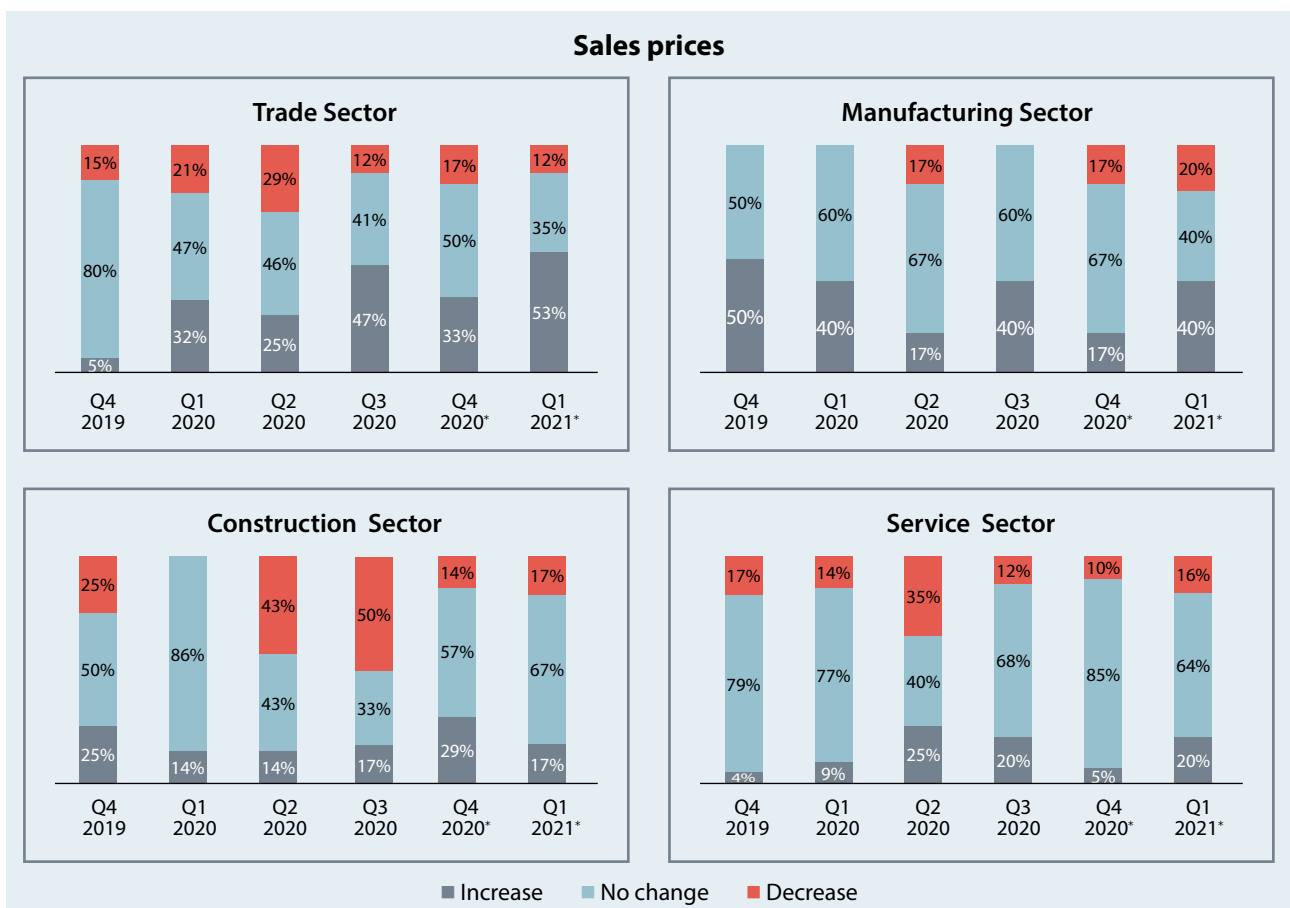
Graph 4: BAG Business Climate, Business Expectation, and Present Business Situation in Trade, Manufacturing, Construction, and Service Sectors

EXPECTATIONS FOR THE FIRST QUARTER OF 2021

- ✘ In Q1 of 2021, compared to Q4 of 2020, a small share of the surveyed BAG members (15.1%) expect an increase in the number of employees, while 28.3% predict a decrease. The majority of surveyed members (56.6%) do not expect any change in this regard.
- ✘ In Q1 of 2021, compared to Q4 of 2020, small proportions of respondents in manufacturing (20%), service (12%), construction (16.7%), and trade (17.6%) expect the number of employees to increase.
- ✘ In Q1 of 2021, compared to Q4 of 2020, 32.1% of surveyed BAG members expect sales prices to increase, while 52.8% do not expect this figure to change, and 15.1% expect sales prices to decrease.
- ✘ In Q1 of 2021, compared to Q4 of 2020, a large proportion of respondents in the service sector (64%) and the construction sector (66.7%) do not expect sales prices to change. Moreover, 35.3% of those surveyed in the trade sector and 40% of those surveyed in the manufacturing have the same expectation.
- ✘ In Q1 of 2021, compared to Q4 of 2020, half of surveyed companies in the construction sector expect sales to decrease.
- ✘ In Q1 of 2021, compared to Q4 of 2020, 80% of surveyed businesses in the manufacturing sector expect domestic production to decrease.
- ✘ In Q1 of 2021, compared to Q4 of 2020, 32% of respondents in the service sector expect sales to decrease, while 52.9% of respondents in the trade sector have the same expectation.

DEVELOPMENTS IN THE THIRD QUARTER OF 2020

- ✘ Only 17% of the surveyed BAG members stated that the number of employees increased in Q3 of 2020, compared to Q2 of 2020, while 24.5% stated that this figure decreased. For the majority of respondents (58.5%), the number of employees was unchanged.
- ✘ 50% of the surveyed companies in the construction sector stated that the number of employees decreased in Q3 of 2020, compared to Q2 of 2020. This figure in the service and trade sectors was 32% and 11.8%, respectively. It is worth noting that in the manufacturing sector none of the companies reported the decrease in the number of employees in this period.
- ✘ Almost one-third of respondents (30.2%) stated that in Q3 of 2020, compared to Q2 of 2020, sales prices increased, while 54.7% stated that prices went unchanged. According to 15.1% of surveyed companies, sales prices decreased.
- ✘ 50% of surveyed businesses in the construction sector stated that sales prices decreased in Q3 of 2020, compared to Q2 of 2020.
- ✘ 47.1% of surveyed companies in the trade sector stated that sales increased in Q3 of 2020, compared to Q2 of 2020.

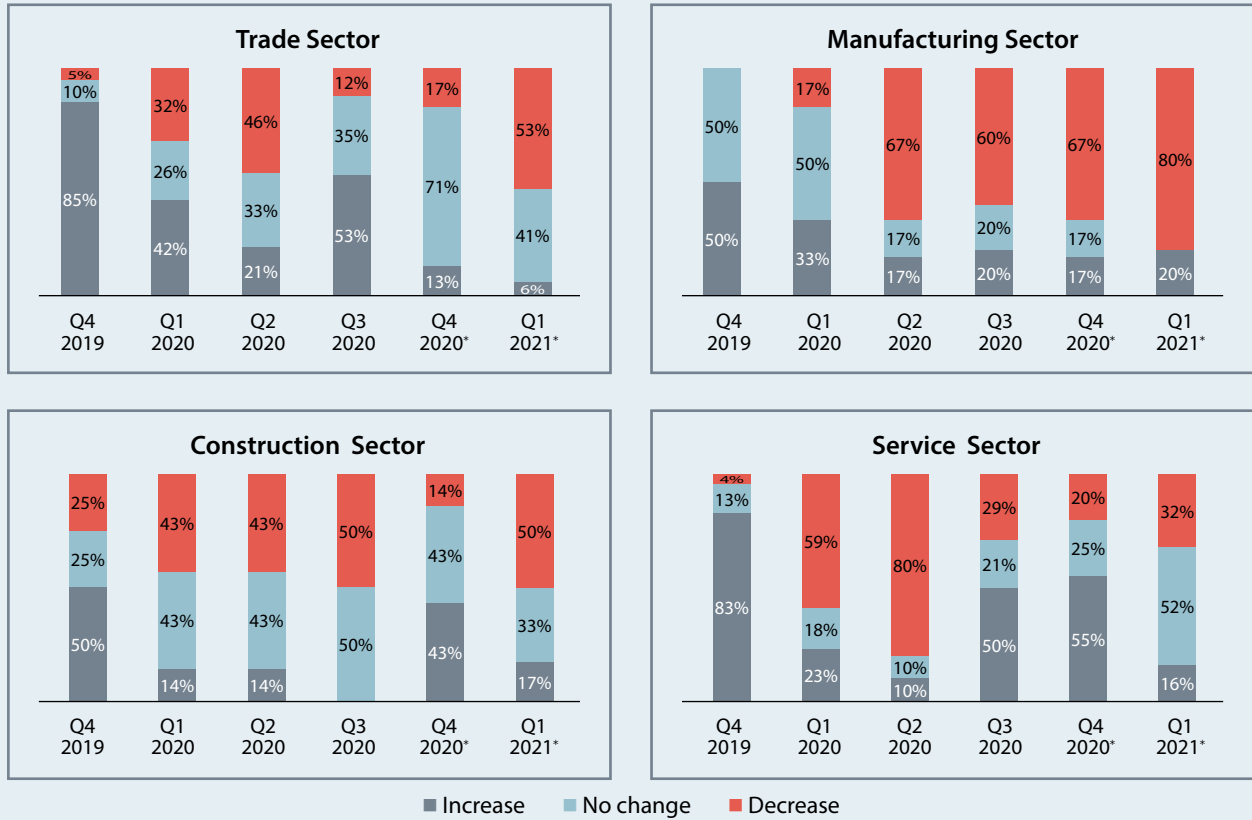


Graph 5: Sales prices in trade, manufacturing, construction, and service sectors²

* Expectation

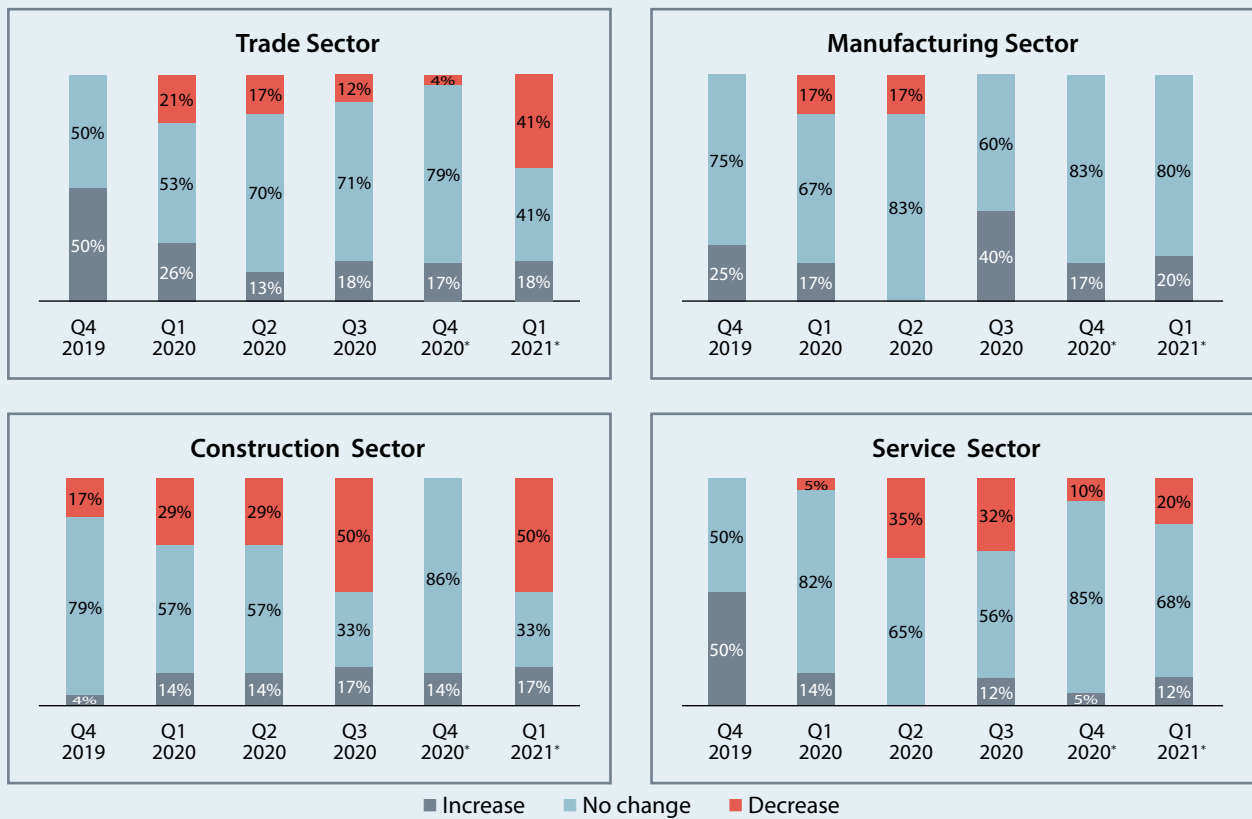
² Due to the rounding of number, in some graphs the sum of the data does not always equal 100%

Demand



Graph 6: Demand in trade, manufacturing, construction, and service sectors

Number of employees

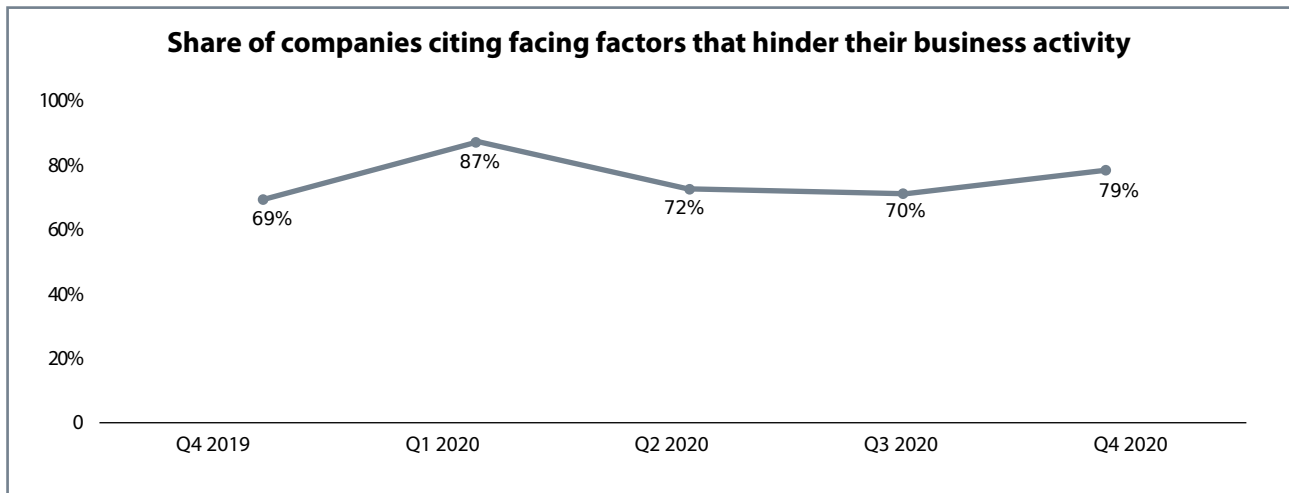


Graph 7: The number of employees in trade, manufacturing, construction, and service sectors

* Expectation

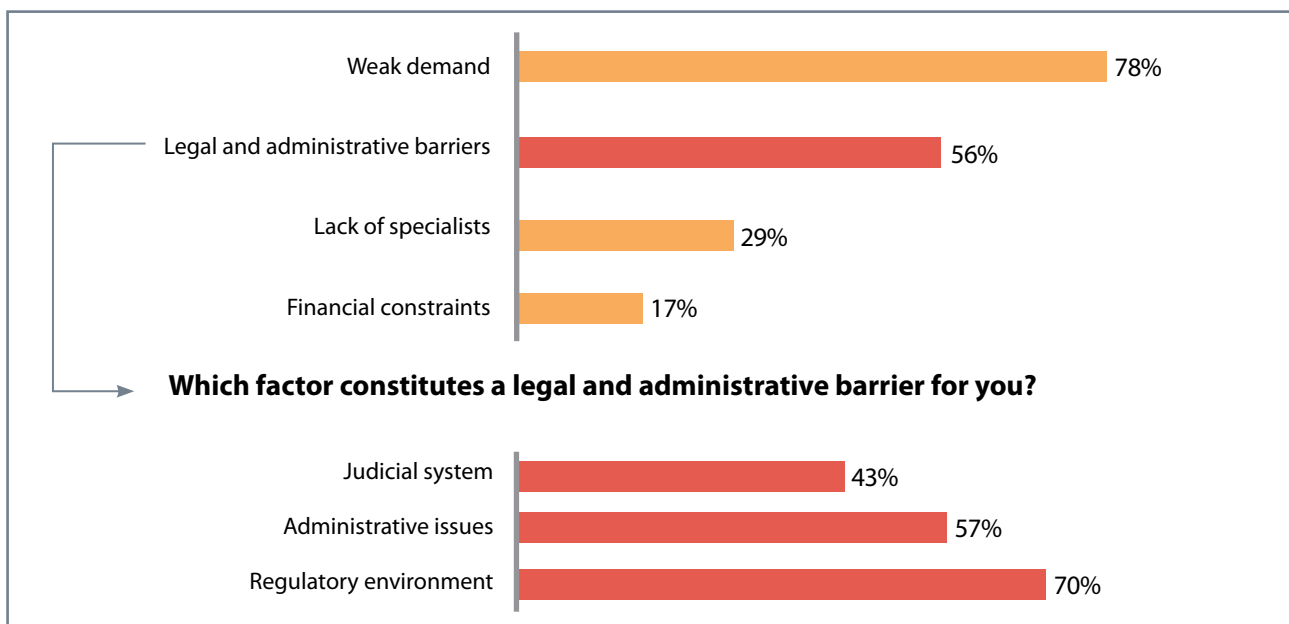
FACTORS HINDERING BUSINESS ACTIVITY

In Q4 of 2020, the share of surveyed companies to claim that there are factors hindering their business activity increased again and reached 78.7%. This increase was expected, as recently businesses have experienced the negative impacts of the ongoing pandemic even more severely. It is worth noting that the share of surveyed companies to state that their business activity was hindered by a lack of demand increased by 10 percentage points.



Graph 8: Existence of factors hindering business activity

In Q4 of 2020, as in previous periods, four most important factors hindering the business activity are: weak demand for products and services; legal and administrative barriers; lack of specialists; and financial constraints. Weak demand remained the most prominent factor in this regard. As mentioned above, this factor intensified in Q4 2020 and was cited by 78% of respondents. Meanwhile, legal and administrative barriers was cited as a hindering factor by 56% of respondents, which represents an 8 percentage points increase compared to Q3 of 2020.

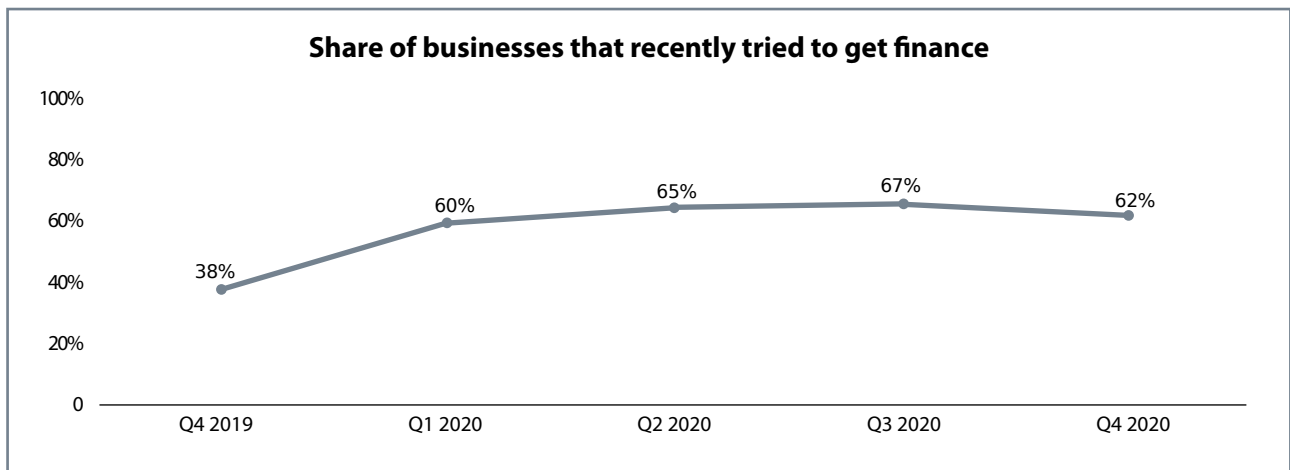


Graph 9: The main challenges that BAG businesses face in Q4 2020

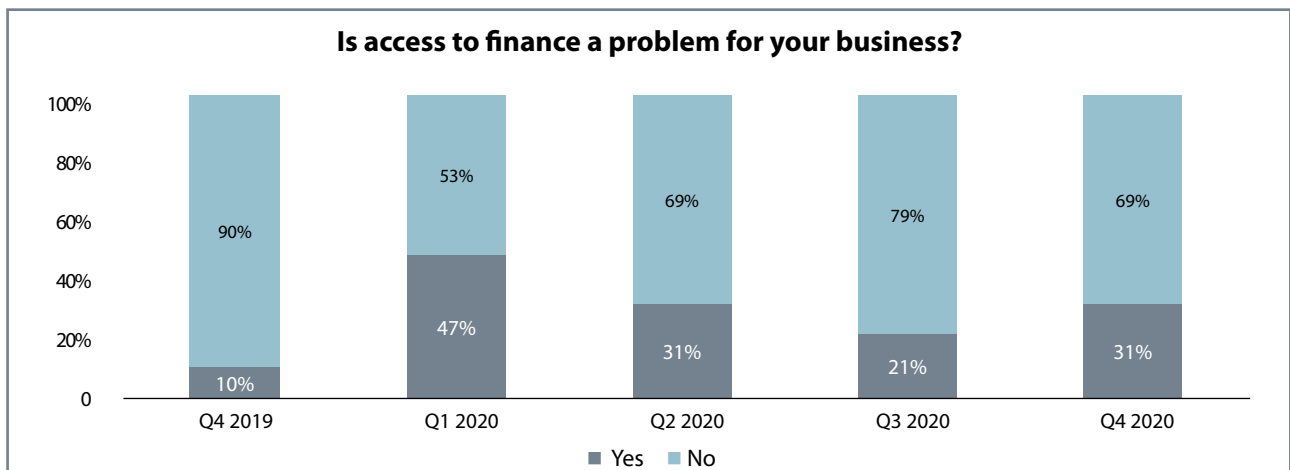
In Q4 of 2020, the majority of surveyed BAG members to name “legal and administrative barriers” as a factor hindering their business activity cited the regulatory environment as the major reason. These figures are very similar to those of Q3 of 2020.

FINANCING

In Q4 of 2020, the share of companies to name financial constraints amongst the factors hindering their business activity decreased by 6 percentage points compared to the previous quarter (dropping from 23% to 17%). The share of companies to attempt to access finance also decreased in Q4 of 2020, which could be explained by reduced business activity.

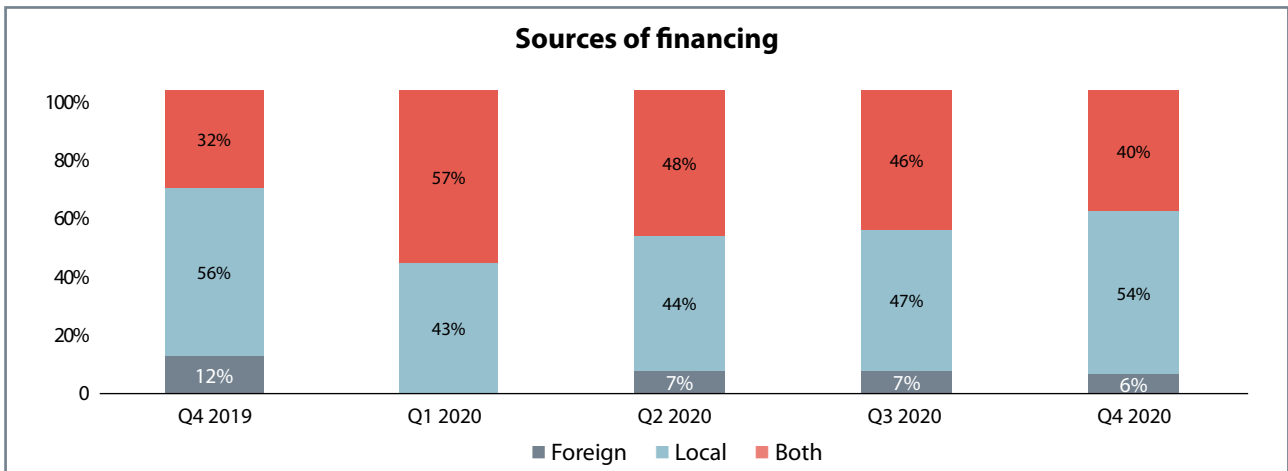


Graph 10: Businesses that recently tried to get finance



Graph 11: Access to finance³

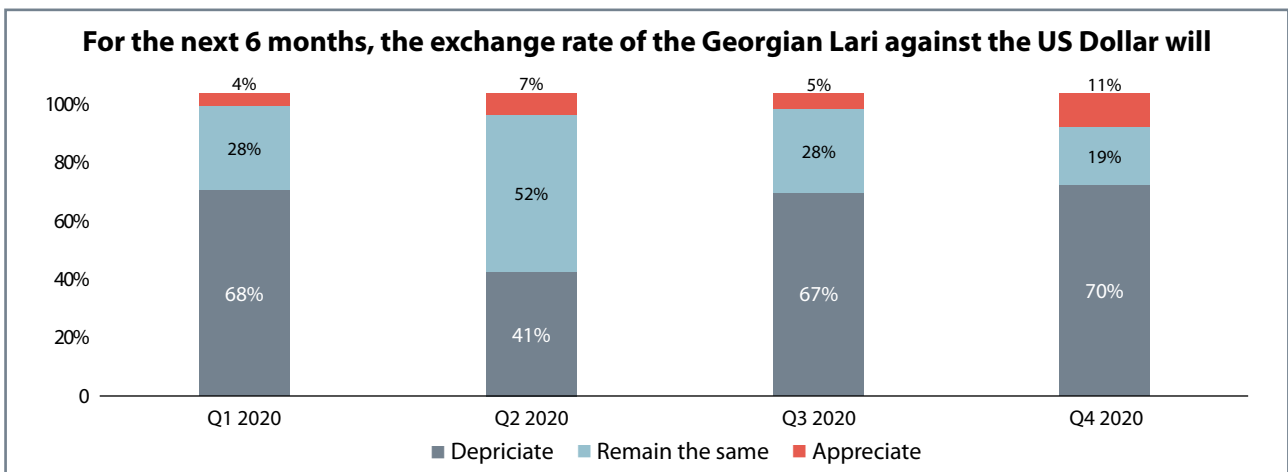
³ The question was only answered by those companies that stated they had recently sought finance.



Graph 12: Sources of financing

Despite the fact that in Q4 of 2020 the share of companies to name financial constraints as a factor hindering their business activity decreased, 31% of surveyed companies that tried to access finance recently named access to finance as a problem. It is worth noting that in the period of Q4 2019 – Q4 2020 the proportion of companies stating that access to finance was a problem peaked in Q1 2020 (47%).

EXCHANGE RATE EXPECTATIONS



Graph 13: Exchange rate of the Georgian Lari against the US Dollar

The current business environment, worsened economic indicators, and fluctuations of the national currency against the USD all contribute to negative expectations. In Q4 of 2020, compared to Q3 of 2020, the share of the surveyed companies expecting the national currency to depreciate increased from 67% to 70%. However, the share of companies with positive expectations also increased and reached its highest figure for 2020 (11%).

BAG EMPLOYMENT BAROMETER

The BAG Employment Barometer reflects companies' expectations regarding the change in employment in the next three months.⁴

IN Q4 OF 2020, THE SURVEYED BAG MEMBER BUSINESSES HAD A NEGATIVE OUTLOOK REGARDING EMPLOYMENT. THE BAG EMPLOYMENT BAROMETER AMOUNTED TO -13.7, WHICH REPRESENTS A DIP COMPARED TO THE PREVIOUS QUARTER. IN Q3 OF 2020, BAG MEMBER BUSINESSES HAD A POSITIVE OUTLOOK TOWARDS EMPLOYMENT AND THE BAG EMPLOYMENT BAROMETER AMOUNTED TO 6.2 POINTS.

In Q4 of 2020, the trade, service, and construction sectors expected a decline in employment. On the other hand, respondents in the manufacturing sector had a positive outlook on employment.

The BAG Employment Barometer dropped most strikingly in the construction sector, where half of the respondents expected the number of employees to decrease in the next three months. In Q4 of 2020, the assessment of the business situation as well as business expectations in the construction sector worsened significantly. In Q1 of 2021, half of the surveyed companies in the construction sector expect a reduction in demand. These pessimistic predictions for the sector affect employment expectations as well.

The Employment Barometer significantly worsened also in the trade sector. For Q4 of 2020, in the trade sector only 17% of surveyed companies planned to increase the number of employees, while 4% expected a decrease. As a result, the Employment Barometer was still positive. Taking into consideration current regulations imposed by the Georgian government, 53% of surveyed businesses in the trade sector expect a reduction of demand for their production. Therefore, 41% of surveyed companies in the trade sector expect the number of employees to decrease in Q1 of 2021.

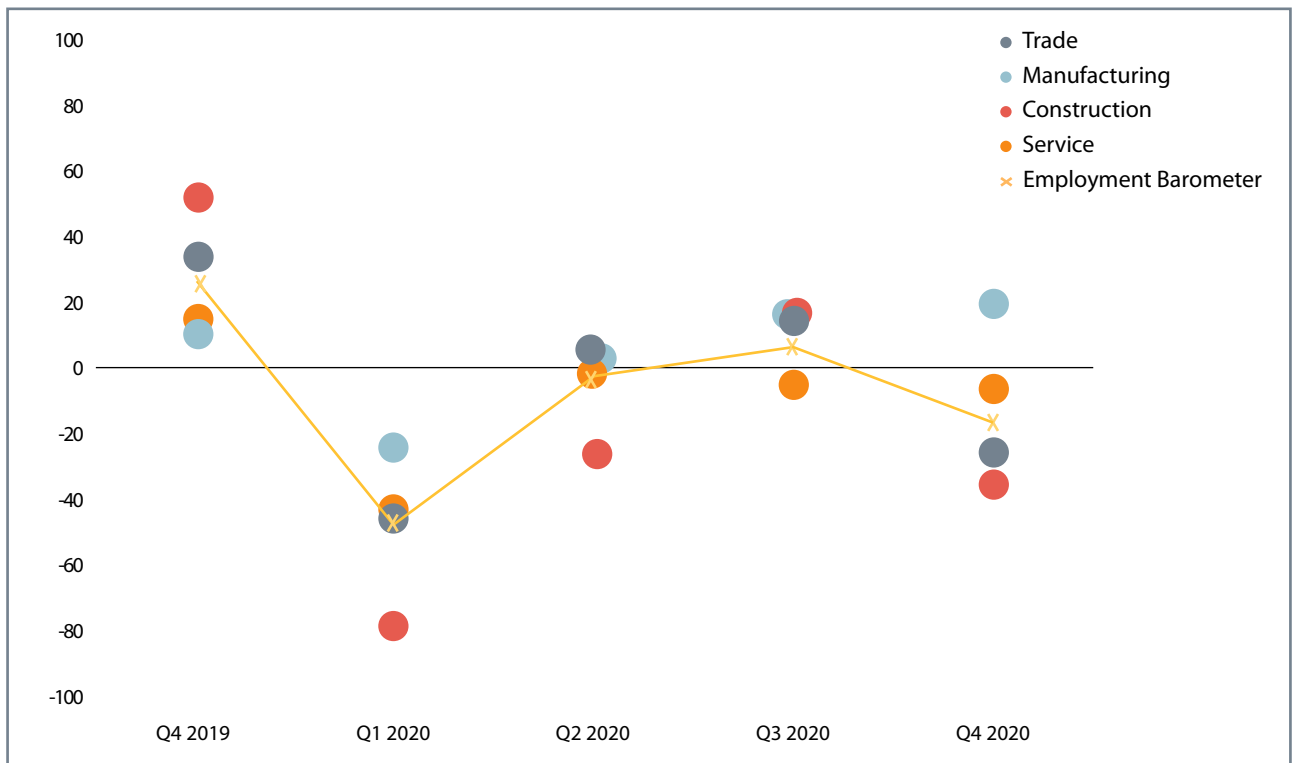
In the service sector, expectations are less pessimistic, with 32% of the surveyed companies expecting demand to reduce. Accordingly, only 20% of respondents in the service sector stated that the number of employees would decrease.

The situation in the manufacturing sector is somewhat different, with 80% of the surveyed companies in this sector expecting demand to reduce in Q1 of 2021. However, the same percentage of companies in this sector expect the number of employees to remain unchanged in this period, while the remaining companies expect an increase. Overall, the BAG Employment Barometer is positive for the manufacturing sector.

⁴ Respondents could describe their plans regarding the number of employees for the next three months as "increasing," "stable" or "decreasing." The balance value of these plans is the difference in the percentage shares of the "increasing" and "decreasing" responses. The BAG Employment Barometer is a weighted mean of the balances in different sectors. The BAG Employment Barometer can be between -100 and +100. -100 means all surveyed businesses expect employment to decrease in the next three months, while +100 means all surveyed businesses expect employment to increase in the next three months.

Table 2: Employment Barometer: Balance values by sector

BAG Employment Barometer by Sector (Balances)					
Sector	Q4 2019	Q1 2020	Q2 2020	Q3 2020	Q4 2020
Trade	33.3	-45.0	5.6	12.5	-23.5
Manufacturing	11.1	-25.0	0.0	16.7	20.0
Construction	50.0	-80.0	-28.6	14.3	-33.3
Service	14.6	-41.7	0.0	-5.0	-8.0
BAG Employment Barometer	26.1	-46.7	-2.8	6.2	-13.7



Graph 14: Balance values by sector and the BAG Employment Barometer

IMPACT OF COVID-19 ON BAG BUSINESS CLIMATE

In November 2020, the Inter-Agency Coordination Council imposed additional restrictions and widened existing ones in Georgia. In the survey conducted in Q4 2020, additional questions to assess the impact of COVID-19 on BAG member businesses were integrated.

The impact of COVID-19 on the association's members was assessed in Q1 2020 as well during the first wave of the pandemic, when a state of emergency and quarantine regime were imposed.

THE IMPACT OF COVID-19 ON BAG MEMBER BUSINESSES

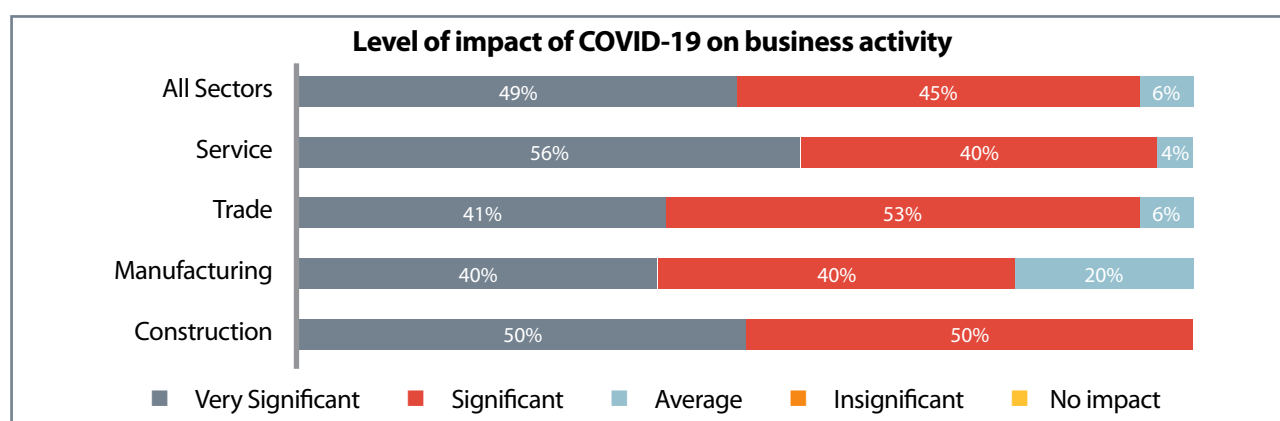
- ✘ In Q4 2020, the majority of surveyed BAG members (94%) stated that the impact of COVID-19 on their business activity had been very significant or significant. None of the surveyed companies stated that the impact of COVID-19 had been insignificant or had no impact.

It is worth noting that during the first wave of the pandemic, a slightly lower share of BAG members assessed the impact of COVID-19 on their activity as very significant or significant (89%). Moreover, 4% of respondents stated that COVID-19 had had no impact on their business or that the impact was insignificant.

- ✘ According to the survey conducted in Q4 2020, the construction and service sectors were the most affected by the COVID-19 pandemic. In those sectors, 100% and 96% of respondents assessed the impact of COVID-19 as very significant or significant.

These figures are higher compared to the results of the corresponding survey conducted during the first wave (construction – 80%; service – 92%). Meanwhile, for the trade sector, the assessment of the impact of COVID-19 as very significant or significant did not change significantly (previous survey – 95%; current survey – 94%).

- ✘ According to the survey conducted in Q4 2020, as well as in the survey conducted during the first wave of the pandemic, COVID-19 had the least impact on the manufacturing sector. In this sector, in the latest survey, 80% of surveyed BAG members stated that the impact of the pandemic on their business activity was very significant or significant. Meanwhile, during the first wave of the pandemic only 50% stated that the impact on their business was very significant or significant. Such assessments of the impact of COVID-19 on this sector can be explained by the fact that the manufacturing sector was the least affected by the imposed restrictions.



Graph 15: Level of impact of COVID-19 on business activity

BUSINESS ACTIVITY DURING COVID-19

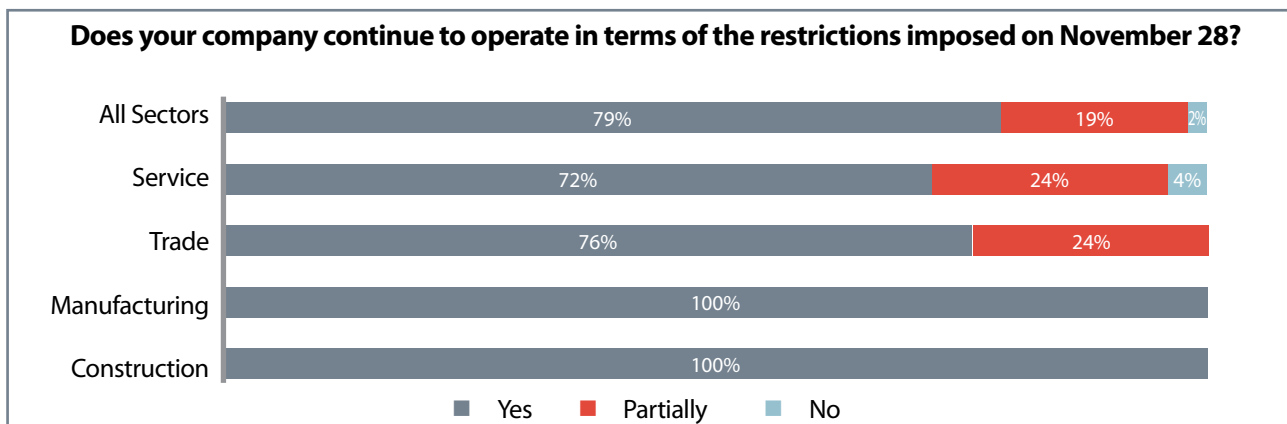
During the current survey, BAG member businesses were asked whether they were continuing their business activities since the introduction of new regulations on November 28 in Georgia. A similar survey was conducted during the first wave of the pandemic when the country underwent a lockdown and state of emergency.

It is worth noting that during the first wave of the pandemic, as a result of the restrictions a significant share of businesses stopped entirely, while under the current restrictions business representatives are able to continue their business activities.

- ✘ 79.2% of surveyed companies in Q4 2020 were continuing to fully operate after the November 28 restrictions, while 18.9% were partially continuing working, and 1.9% stopped operating entirely.

It is worth noting that according to the conducted survey during the first wave of the pandemic, 47.2% of surveyed businesses continued to fully operate, while 15.1% stopped working.

- ✘ Based on the survey conducted in Q4 2020, in terms of sectors, the greatest impact of the COVID-19 pandemic was experienced in the trade and service sectors. Approximately 28% of respondents in the service sector stopped their business activity partially or fully, while this figure for the trade sector was 23.5%.
- ✘ Based on the survey conducted in Q4 2020, COVID-19 has had the least impact on the manufacturing and construction sectors in which all surveyed companies continue to operate fully.



Graph 16: Business operation

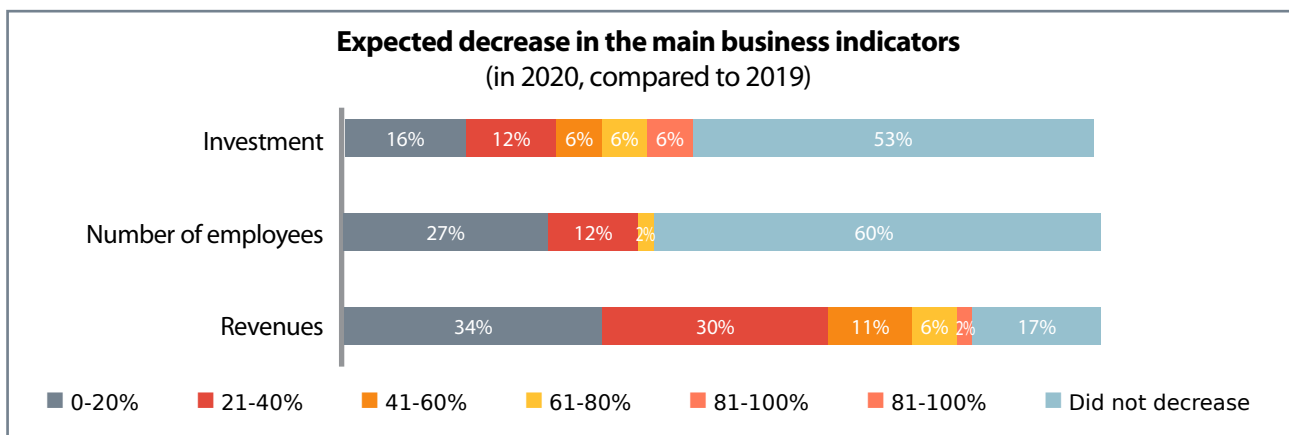
EXPECTED REDUCTION IN MAIN BUSINESS INDICATORS

In the survey, BAG members assessed changes in revenues, number of employees, and the volume of investments in 2020, compared to 2019.

Based on preliminary estimates, in 2020, compared to 2019:

- ✘ 64% of surveyed BAG companies stated that their revenues decreased by 0-40%. Meanwhile, 19% of companies stated that their revenues decreased by more than 40%, while 17% indicated no decrease at all.
- ✘ The majority of surveyed BAG members (59.6%) stated that their number of employees did not decrease. At the same time, 29.6% of respondents stated that their number of employees decreased only by 0-20%.

- ✘ 53.1% of respondents reported no decrease in the volume of investments, while 16.3% reported a decrease in investment by 0-20%.
- ✘ For all BAG members in the construction sector revenues decreased, but none of them reported the decrease of revenues by more than 60%. For half of the respondents in the construction sector, revenues decreased by 41-60%.
- ✘ 80% of respondents in the manufacturing sector stated that their revenues decreased by 0-40%, while 20% stated that their revenues did not decrease.
- ✘ In the service sector, similar to the manufacturing sector, 20% of surveyed companies stated that their revenues did not decrease. In the trade sector, the corresponding figure was 17.6%.
- ✘ 66.7% of the surveyed companies in the construction sector stated that their number of employees decreased by 0-40%. The corresponding figures in the trade and service sectors were 47.1% and 33.3%, respectively.
- ✘ None of the surveyed companies in the manufacturing sector stated that the number of employees in their company decreased. The number of employees did not decrease in 16.7% of surveyed companies in the construction sector, while in the trade and service sectors the corresponding figures amounted to 52.9% and 66.7%, respectively.
- ✘ A significant share of companies did not experience a reduction in the volume of investments. In the service sector, 66.7% of surveyed businesses did not reduce the volume of investments, while in the manufacturing sector it amounted to 60%, and in trade and construction sectors the corresponding figures were 41.2% and 33.3%, respectively.

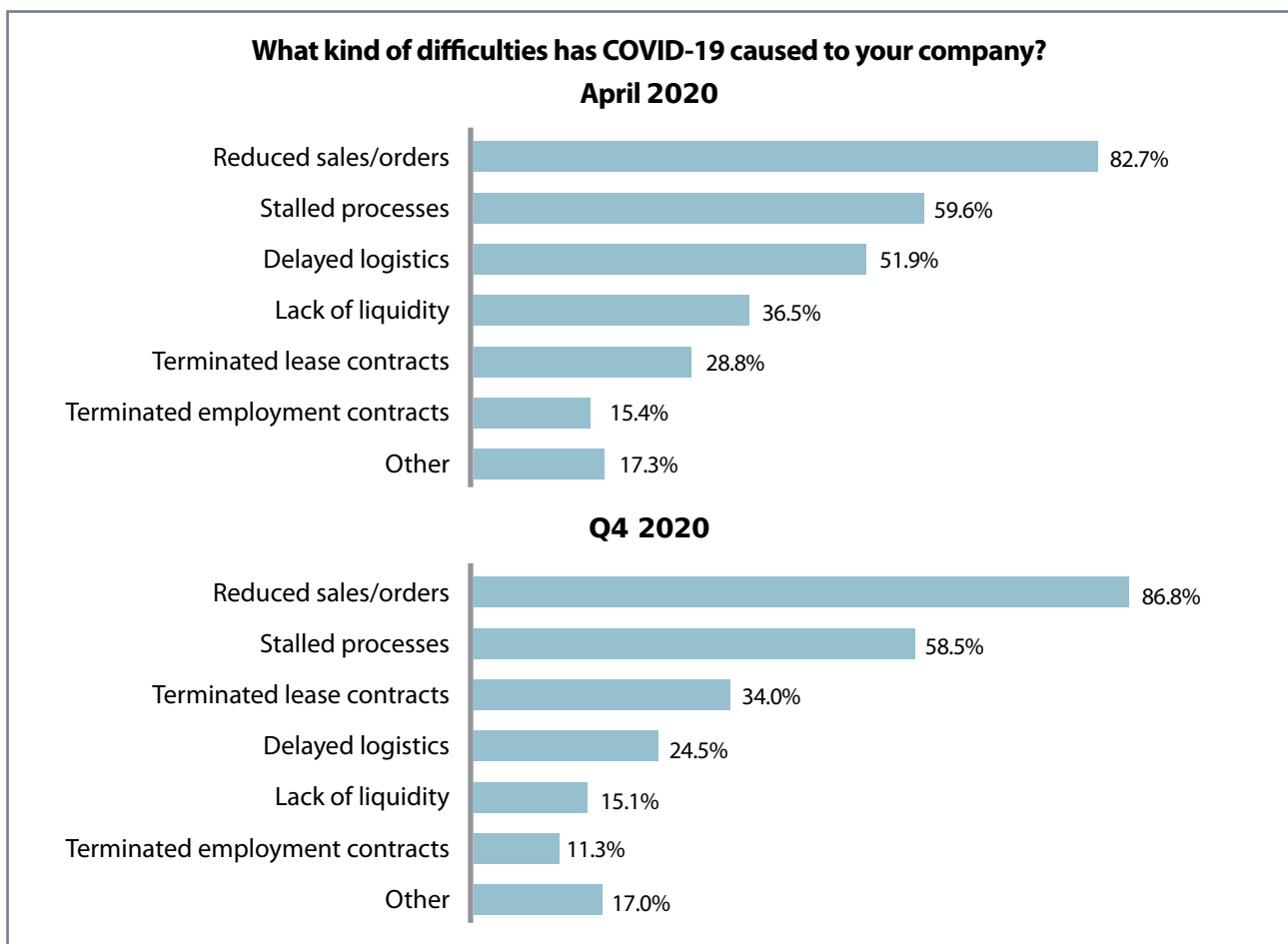


Graph 17: Expected decrease in the main business indicators in 2020 compared to 2019

THE MAJOR CHALLENGES BUSINESSES FACE DUE TO COVID-19

ACCORDING TO THE SURVEY CONDUCTED IN Q4 2020, THE BIGGEST CHALLENGE BAG MEMBER BUSINESSES FACE DUE TO COVID-19 IS REDUCED SALES/ORDERS. IT IS WORTH NOTING HERE THAT DURING THE FIRST WAVE OF THE PANDEMIC THE SAME CHALLENGE WAS NAMED AS THE MOST IMPORTANT.

- ✘ Reduced sales/orders and stalled processes as a result of the pandemic remain an important challenge for businesses.
- ✘ In Q4 2020, while assessing the problems caused by COVID-19, the percentage share of companies to name reduced sales/orders as a problem increased by 4.1 percentage points compared to the survey during the first wave of the pandemic.
- ✘ In Q4 2020, the number of companies to name delayed logistics as an important challenge during the first wave of the pandemic decreased (from 51.9% during the first wave of the pandemic to 24.5% in Q4 2020). This could be explained by the fact that the restrictions on movements imposed during the first wave have been lifted.
- ✘ In Q4 2020, while assessing the challenges associated with COVID-19, the percentage share of companies to name terminated lease contracts as a challenge increased by 5.2 percentage points compared to the first wave of the pandemic. This growth could be explained by the longevity of the pandemic and decreased economic activity.

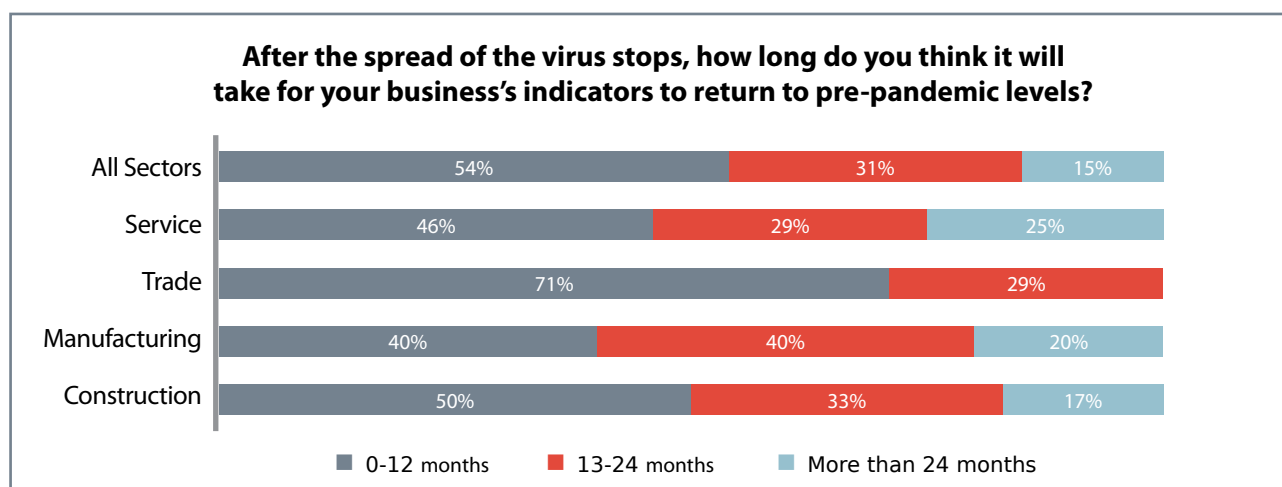


Graph 18: Difficulties businesses face due to COVID-19

ASSESSMENT OF THE DURATION OF COVID-19'S IMPACT

To assess the expectations of BAG member businesses regarding the duration of COVID-19's impact, companies answered a question on how long it will take for their company to reach pre-pandemic levels once the pandemic eventually ends.

- ✘ 53.8% of surveyed companies stated that in order to return to pre-pandemic financial indicators they would need 0-12 months after the end of the pandemic. Meanwhile, 30.8% of respondents think that they will need 13-24 months, and 15.4% stated that they will need more than 24 months. It is worth noting here that in the previous survey, the majority of respondents (74%) stated that 12 months would be enough for them to recover and reach pre-pandemic financial figures.
- ✘ 70.6% of surveyed businesses in the trade sector stated that 0-12 months would be enough to reach pre-pandemic financial figures. This figure represents a significant decrease compared to the previous survey when 85% had the same expectation. However, representatives in the trade sector are more optimistic in terms of returning to pre-pandemic levels, compared to other sectors.
- ✘ The most negative outlook in this regard was reported in the service sector. In this sector, 25% of the surveyed businesses stated that they would need more than 24 months to reach their pre-pandemic financial figures. Indeed, 20% and 16.7% of respondents indicated the same expectations in the manufacturing and the construction sectors, while in the trade sector none of the surveyed companies think that they would need more than 24 months to recover.



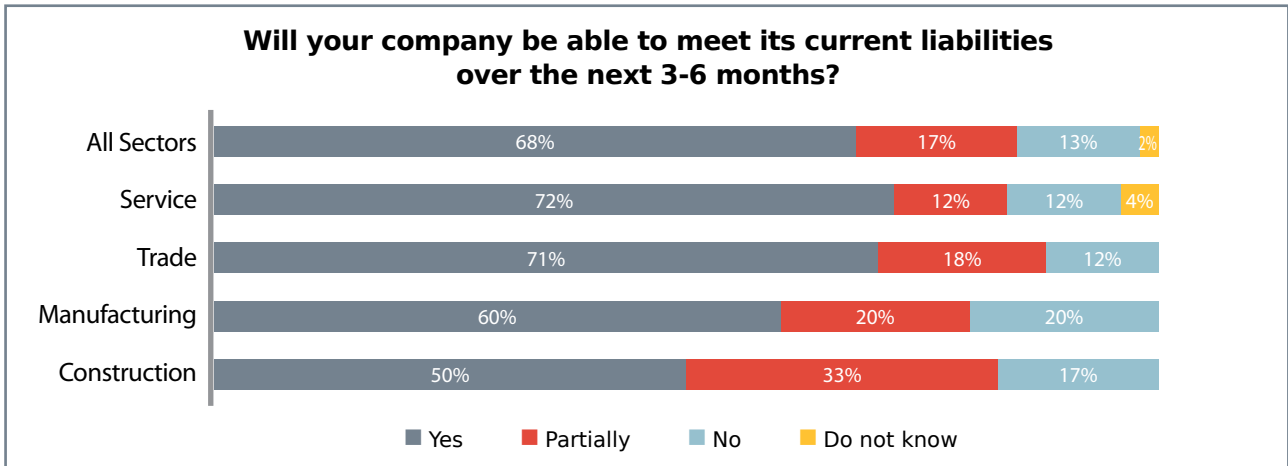
Graph 19: Expected duration to return to the pre-pandemic levels

COVERING CURRENT LIABILITIES DURING COVID-19 PANDEMIC

Taking into consideration the current situation, it is important to assess the ability of businesses to meet their liabilities in the short term. In this survey, BAG member businesses answered a question on whether they will be able to cover their liabilities for the next 3-6 months.

- ✘ 67.9% of surveyed businesses stated that they would be able to cover their current liabilities in the next 3-6 months. Meanwhile, 17% stated that they could cover their current liabilities partially. Otherwise, 13.2% had more pessimistic expectations and thought they would be unable to meet their current liabilities.

- ✘ The service sector reports the most optimistic expectations. Indeed, 72% of companies in this sector stated that they would be able to meet their current liabilities in the next 3-6 months. Similar expectations have been recorded in 70.6% of the surveyed businesses in the trade sector, while in the manufacturing and construction sectors the corresponding figures were 60% and 50%, respectively.

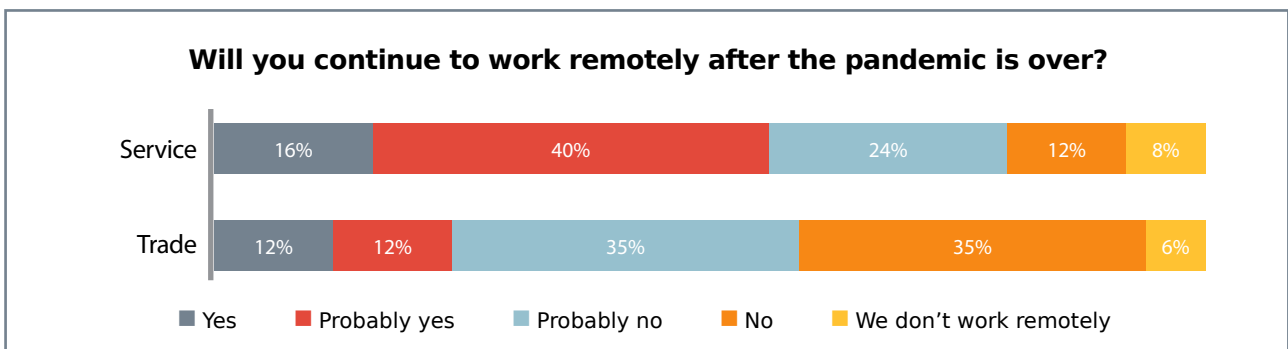


Graph 20: Expectations on meeting the current liabilities

THE POSSIBILITY TO CONTINUE WORKING REMOTELY

Due to the ongoing pandemic, a significant proportion of businesses had to switch to remote working. This has proved beneficial for some companies. The survey was interested, whether trade and service sector companies will maintain remote work style after the end of pandemic. The companies in those sectors answered the question, whether they will operate remotely after the pandemic ends.

- ✘ 56% of surveyed companies in the service sector stated that they would continue or probably would continue working remotely after the end of the pandemic. Only 23.5% of surveyed companies in the trade sector had the same expectations.



Graph 21: Remote working after the end of pandemic



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