

BAG INDEX

BUSINESS
CLIMATE



საქართველოს ბიზნეს ასოციაცია
BUSINESS ASSOCIATION OF GEORGIA



Leibniz Institute for Economic Research
at the University of Munich



Research

IV QUARTER 2021

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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 the need for labor resources. 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 Q4 of 2021 in period 15 November – 1 December.

IN Q4 OF 2021, THE SURVEYED BUSINESSES ASSESS THEIR PRESENT BUSINESS SITUATION AND EXPECTATIONS FOR THE NEXT SIX MONTHS POSITIVELY. THE BAG BUSINESS CLIMATE INDICATOR AMOUNTS TO 33.8 POINTS IN Q4 OF 2021, WITH THE PRESENT BUSINESS SITUATION INDICATOR SITTING AT 18.8 AND THE BUSINESS EXPECTATIONS INDICATOR AT 49.8.

In Q4 of 2021, compared to Q3 of 2021, the BAG Business Climate improved by 6.8 points. Moreover, in this period, the assessment of the present business situation (by 8 points) and business expectations improved (by 5.3 points).

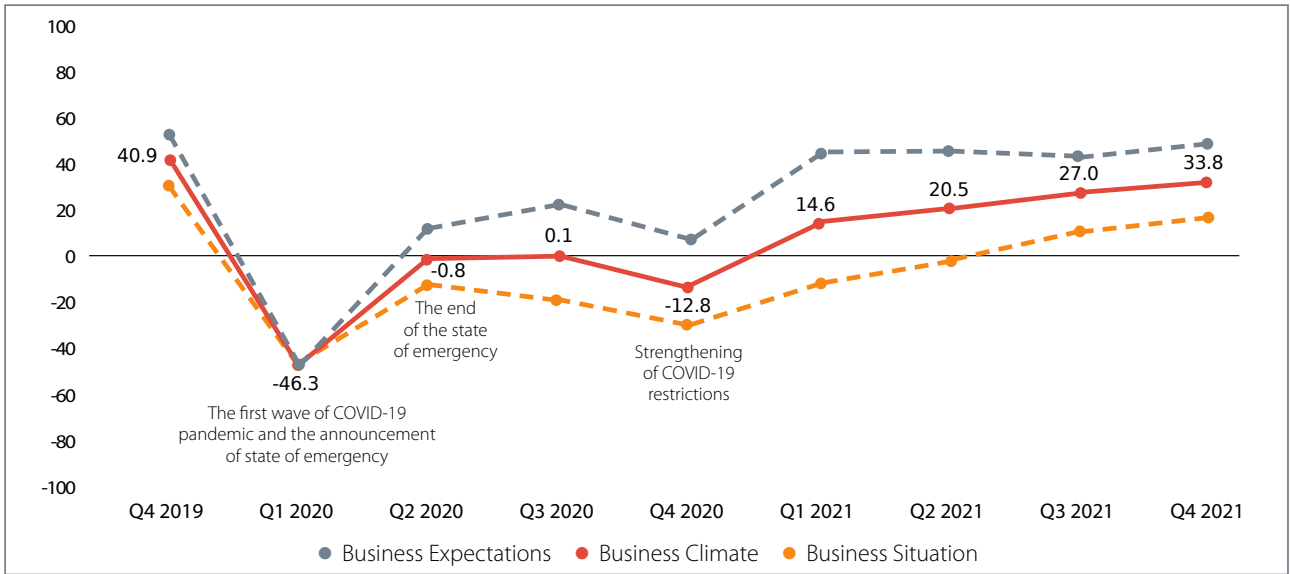
The figures for Q4 of 2021 demonstrate a significant improvement compared to Q4 of 2020. In Q4 of 2020, the BAG Business Climate indicator was -12.8, the present business situation indicator equaled -30, while the business expectations indicator sat at 6.5.

Despite the aforementioned improvement, the figures of Q4 of 2021 could still not reach pre-pandemic levels. In Q4 of 2019, the BAG Business Climate indicator was 40.9, the present business situation indicator was 29.6, while the business expectations indicator stood at 53.1 (see Graph 1).

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.

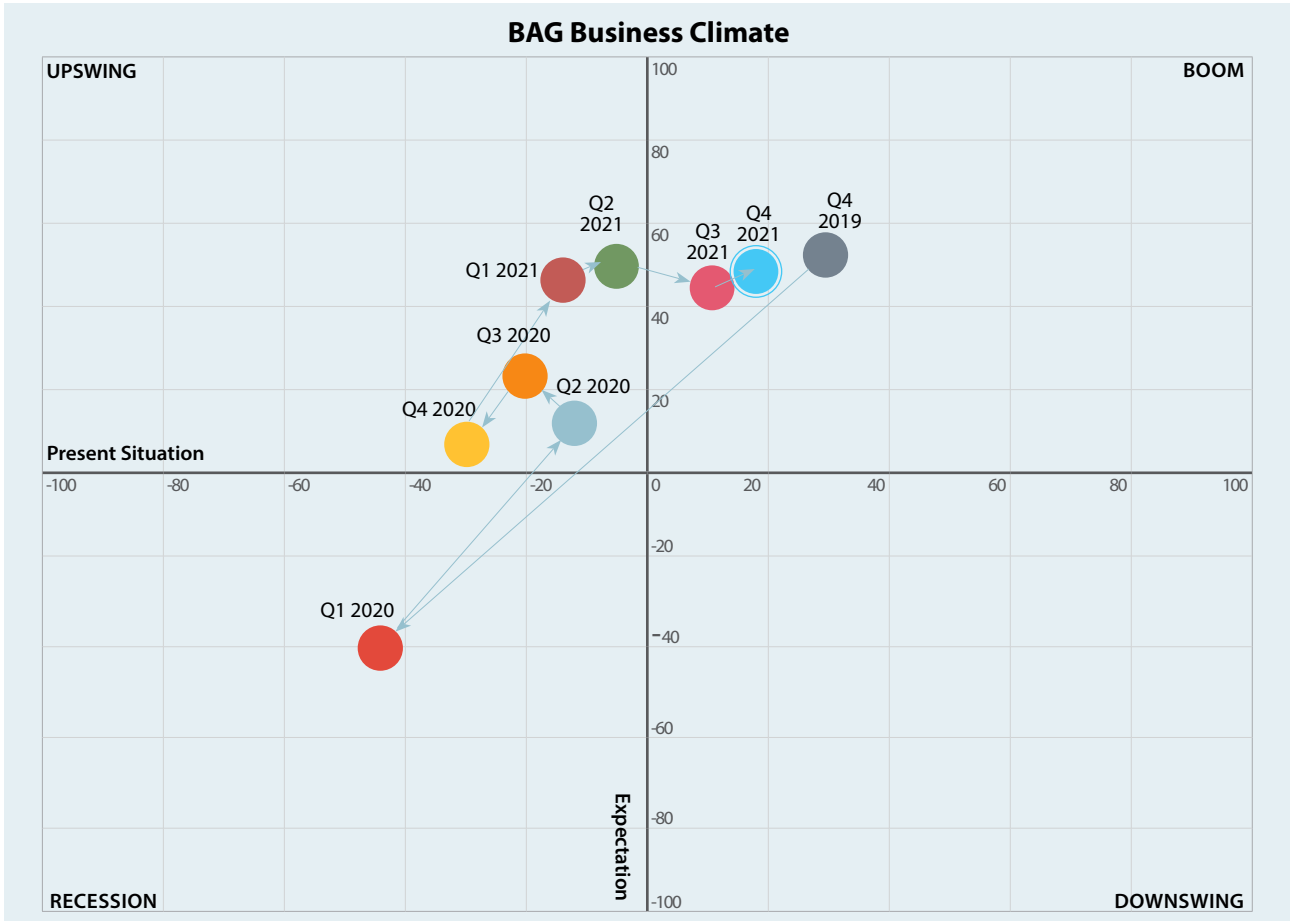
¹ In the first quarter of 2021, a change was made in the methodology of the BAG Index. As a result, the number of companies surveyed increased: enterprises that belong to the corporate group of member companies were added to the existing survey respondents.

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 Q4 of 2021, as in Q3 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

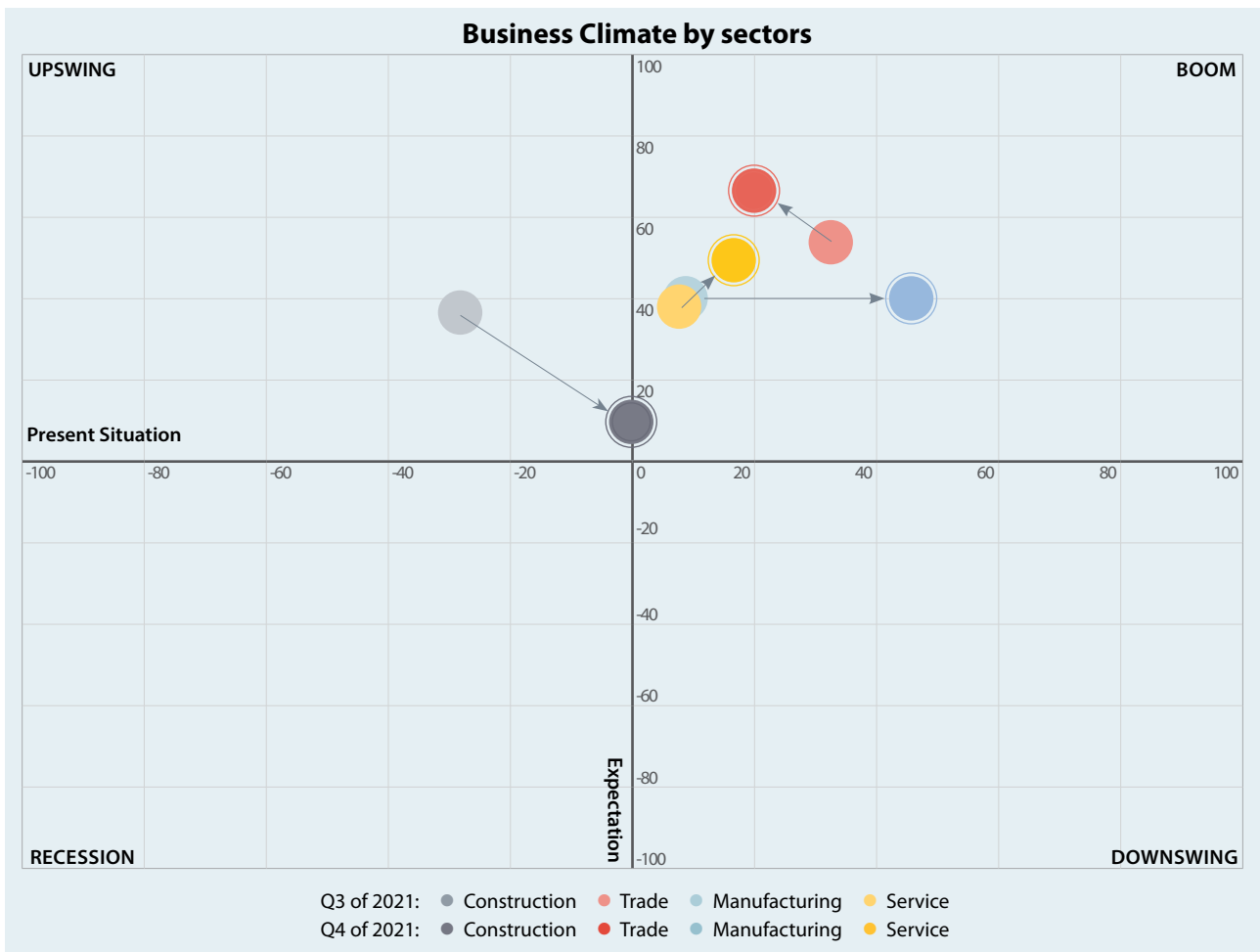
In Q4 of 2021, the **business climate indicator** was positive for all sectors. Compared to Q3 of 2021, in Q4 2021 the indicator improved in the manufacturing, construction and service sectors, but worsened slightly in the trade sector (see Graph 4).

In Q4 of 2021, compared to Q3 of 2021, the **present business situation indicator** improved in all sectors, except trade. Nevertheless, despite the overall view of the present business situation in trade worsening compared to the previous quarter, the surveyed businesses still assessed the present situation positively. Regarding the construction sector, it is worth noting that for the first time since Q3 of 2020 the indicator is not negative and amounts to 0. The most positive assessment with respect to the present business situation was recorded in the manufacturing sector, which could be attributed to an increase in demand in Q4 of 2021 (53.2% of surveyed companies stated an increase in demand for their products).

In Q4 of 2021, the **business expectations indicator** was positive for all sectors. However, expectations slightly worsened for the manufacturing sector and significantly worsened for the construction sector compared to Q3 of 2021. Elsewhere, the business expectations indicator improved in service and trade sectors.

Table 1: Balance values by sector in Q4 of 2021

| | Business Climate | Present Business Situation | Business Expectation |
|----------------------|-------------------------|-----------------------------------|-----------------------------|
| Trade Sector | 41.5 | 20.0 | 65.0 |
| Service Sector | 31.5 | 13.3 | 51.1 |
| Manufacturing Sector | 43.3 | 46.7 | 40.0 |
| Construction Sector | 6.2 | 0.0 | 12.5 |
| All Sectors | 33.8 | 18.8 | 49.8 |



Graph 3: Business Climate by sectors in Q3 and Q4 of 2021

During 2021, the business climate indicator has been positive in the trade, manufacturing, and service sectors. Moreover, it is worth noting that the business climate indicator has demonstrated an upward trajectory in sectors during 2021, compared to the corresponding periods of 2020. In the construction sector, the indicator was negative in Q1 and Q2 of 2021, before rising to positive in Q3 and Q4, compared to the corresponding period of the previous year.

The business climate indicator improved for the trade sector from Q1 of 2021 to Q3 of 2021, but slightly worsened in Q4 (by 1.5 points). The positive business climate indicator in the trade sector has been caused by the positive expectations and assessment of the present business situation during the last three quarters of 2021. It is worth noting here that trade is the only sector where the business climate indicator in Q4 of 2021 is higher compared to the pre-pandemic period of Q4 of 2019 (by 1.8 points).

During 2021, the positive assessment of the business climate in the service and manufacturing sectors has mainly stemmed from positive expectations about the near future as well as the positive assessment of the present situation.

The negative assessment of the business climate in the construction sector in Q1 of 2021 was due to a negative assessment of the present business situation, while in Q2 of 2021 the negative assessment of the business climate was caused by a negative assessment of the present business situation as well as pessimistic business expectations. In Q3 and Q4 of 2021, the positive assessment of the business climate was due to optimistic business expectations and the improved assessment of the present business situation compared to the previous quarters (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 Q3 of 2021

- ✘ 30.3% of surveyed companies stated that the number of employees increased in Q3 of 2021, compared to Q2 of 2021. For the majority of respondents (66%) the number of employees was unchanged, while 3.7% reported a decrease.
- ✘ Across all sectors covered, the manufacturing sector was the one with the largest share of the surveyed companies (40%) claiming that the number of employees had increased in Q3 of 2021, compared to Q2 of 2021 (see Graph 5). This could be due to the rise in demand for production experienced by the majority of companies (53.3% of surveyed companies recorded an increase in demand for their production in Q3 of 2021).

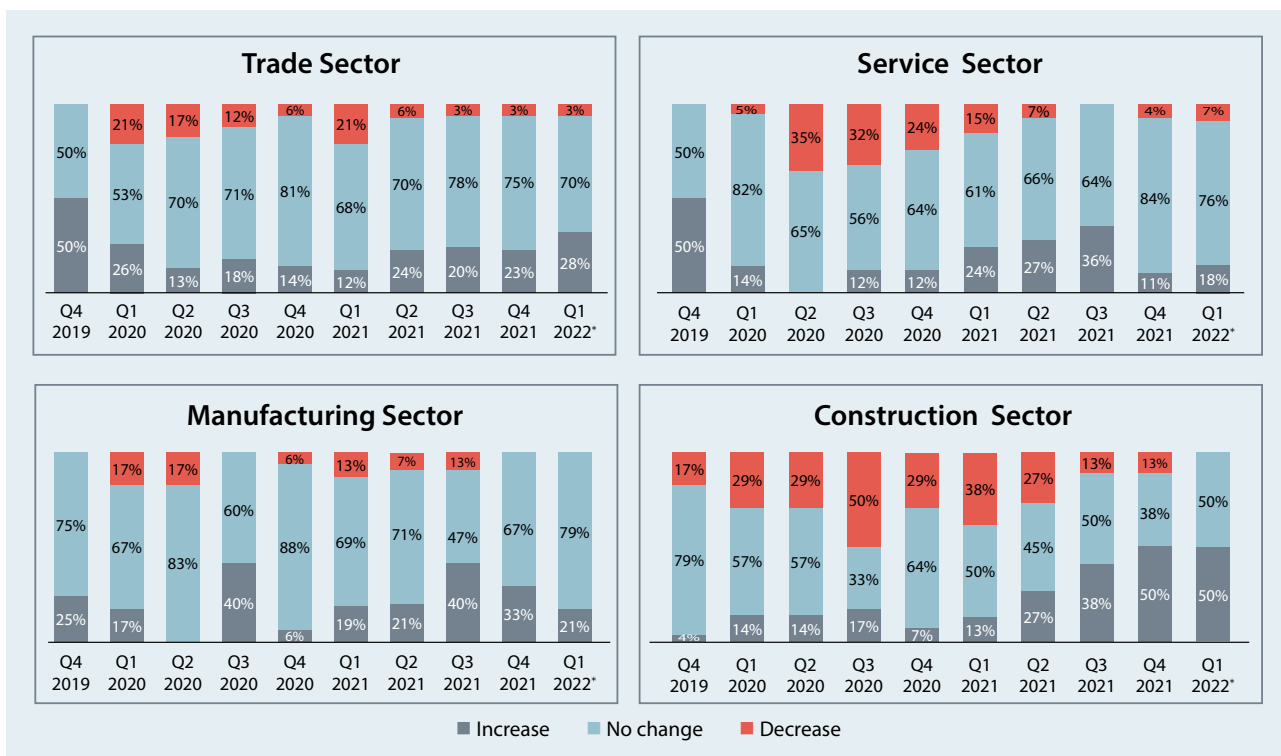
Situation in Q4 of 2021

- ✘ 21.3% of the surveyed companies stated that in Q4 of 2021, compared to Q3 of 2021, the number of employees increased, while 3.7% recorded a decrease. The majority of companies (75%) stated that their number of employees had not changed.
- ✘ A significant share of respondents in the construction and manufacturing sectors stated that the number of employees had increased in Q4 of 2021, compared to Q3 of 2021. This could be due to rising sales in both sectors in Q4 of 2020.

Expectations for Q1 of 2022

- ✘ 25% of the surveyed companies expect that in Q1 2022, compared to Q4 2021, the number of employees will increase, while 3.7% expect a decline. The majority of companies (71.3%) 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. 50% of the respondents in the construction sector stated that they expect an increase in the number of employees in Q1 2022, compared to Q4 2021. 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 Q1 of 2022, compared to Q4 of 2021 (70%, 78.6% and 75.6%, respectively).



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

To sum up, it could be argued that the construction sector has been experiencing positive dynamics regarding employment since Q1 of 2021. In Q1 of 2021, only 13% of surveyed companies recorded an increase in their number of employees, while in Q4 of 2021 this indicator stood at 50% and a similar rate is expected in Q1 of 2022.

In the manufacturing and service sectors, like in the construction sector, the share of companies to have recorded an increase in their number of employees has been rising since Q1 of 2021. However, in Q4 of 2021, compared to the previous quarter, the relevant indicators decreased by 7 and 25 percentage points, respectively. It is expected that in Q1 of 2022, fewer companies will increase the number of employees.

In the trade sector, the share of companies to record an increase in number of employees during 2021 was stable, unlike other sectors (in Q2-Q4 2021, 20-24% of companies recorded an increase in the 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 Q3 of 2021

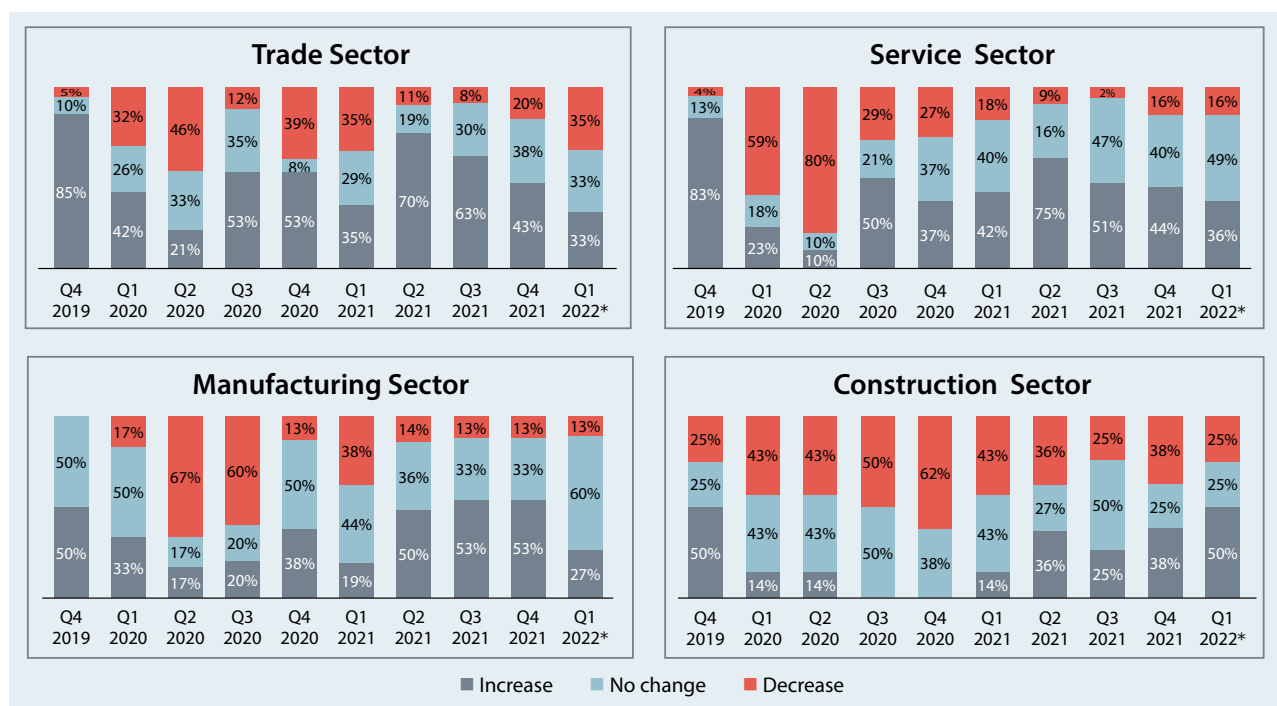
- ✘ More than half of the companies surveyed in the service, trade, and manufacturing sectors claimed that their sales increased in Q3 of 2021, compared to Q2 of 2021.
- ✘ In Q3 of 2021, the situation regarding sales was assessed most negatively in the construction sector, where 25% of surveyed companies stated that their contracts/presales had decreased, compared to Q2 of 2021 (see Graph 6).

Situation in Q4 of 2021

- ✘ In Q4 of 2021 the situation regarding sales was assessed most positively by representatives of the manufacturing sector. 53.3% of surveyed companies recorded growth in sales in this period.
- ✘ In Q4 of 2021, the worst situation regarding sales was recorded in the construction sector. According to 37.5% of surveyed companies in the construction sector their sales decreased.

Expectations for Q1 of 2022

- ✘ The most positive outlook for Q1 of 2022 regarding sales was recorded in the construction sector, where 50% of surveyed companies stated that they expect sales prices to increase.
- ✘ Comparing sectors, the highest share of companies to predict sales to decrease was recorded in the trade sector (35%).



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

To sum up, it could be argued that during Q1-Q4 2021 the most positive tendencies regarding sales were noted in the trade and service sectors, in which the majority of companies reported an increase in quarterly sales volumes.

It is worth noting that since Q2 of 2021, an increase in the volume of sales was recorded in the majority of the surveyed companies in the manufacturing sector. Compared to other sectors, the construction sector had the lowest share of companies to record an increase in sales during 2021.

Sales prices

Assessment of Q3 of 2021

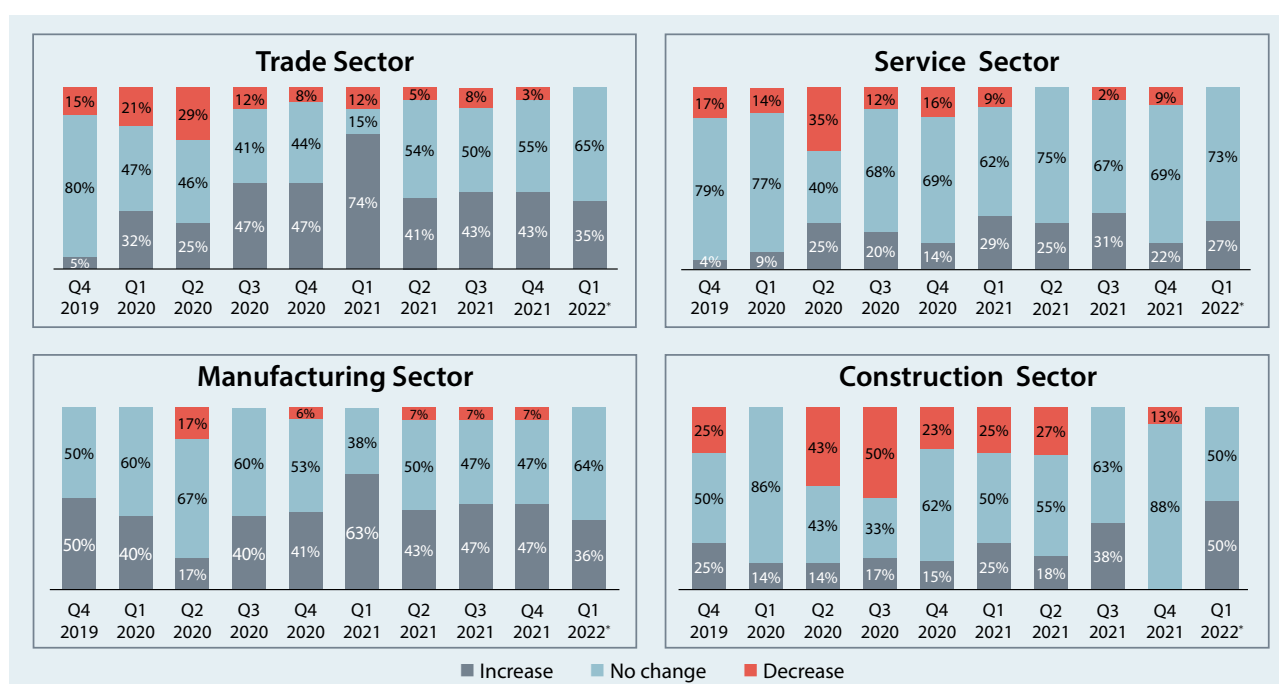
- Overall, a large share of surveyed companies (57.4%) stated that in Q3 of 2021, compared to Q2 of 2021, sales prices had not changed, while 38% stated that prices had gone up. According to 4.6% of respondents, sales prices had decreased in this period.
- Across the covered sectors, the majority of surveyed companies in all sectors stated that prices had not changed in Q3 of 2021, compared to Q2 of 2021 (see Graph 7).

Situation in Q4 of 2021

- In total, 31.2% of the surveyed companies stated that in Q4 of 2021, compared to Q3 of 2021, sales prices had increased, while 62.4% stated that sales prices remained unchanged, 6.4% claimed that sales prices had decreased.
- The most positive outlook regarding sales prices is recorded in manufacturing and trade sectors with 46.7% and 42.5% of surveyed companies stating that sales prices had increased in Q4 of 2021, compared to Q3 of 2021.

Expectations for Q1 of 2022

- Overall, 32.7% of surveyed companies expect sales prices to increase in Q1 of 2022, compared to Q4 of 2021, while 67.3% do not expect this figure to change, and none of the companies expect a decrease.
- Across the covered sectors, the construction sector had the largest share of respondents (50%) expecting an increase in sales prices in Q1 of 2022, compared to Q4 of 2021.

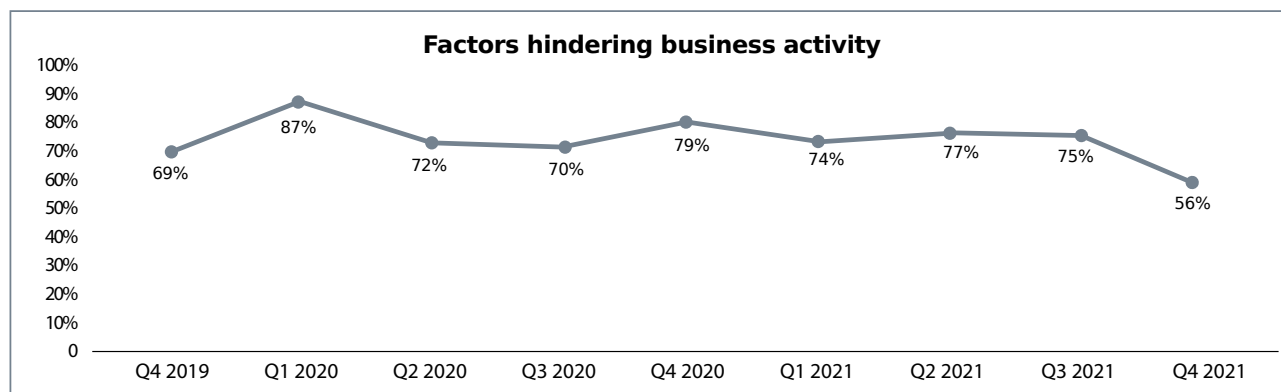


Graph 7: Sales prices in trade, service, manufacturing, and construction sectors.

In summary, during 2021, among all of the covered sectors, prices did not change in the majority of the surveyed companies. However, at the same time, since Q1 of 2021 a significant proportion of companies from all sectors have recorded an increase in their sales prices. During the given period, across sectors, the manufacturing and trade sectors had the highest percentages of companies to record increased sales prices.

FACTORS HINDERING BUSINESS ACTIVITY

In Q4 of 2021, compared to Q3 of 2021, the share of surveyed companies to claim there are factors hindering their business activity decreased significantly (by 19 percentage points). It must be noted that, in Q4 of 2021, compared to pre-pandemic period, the share of companies claiming that there are factors hindering their business activity decreased by 13 percentage points.



Graph 8: Existence of factors hindering business activity

In Q4 of 2021, 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).

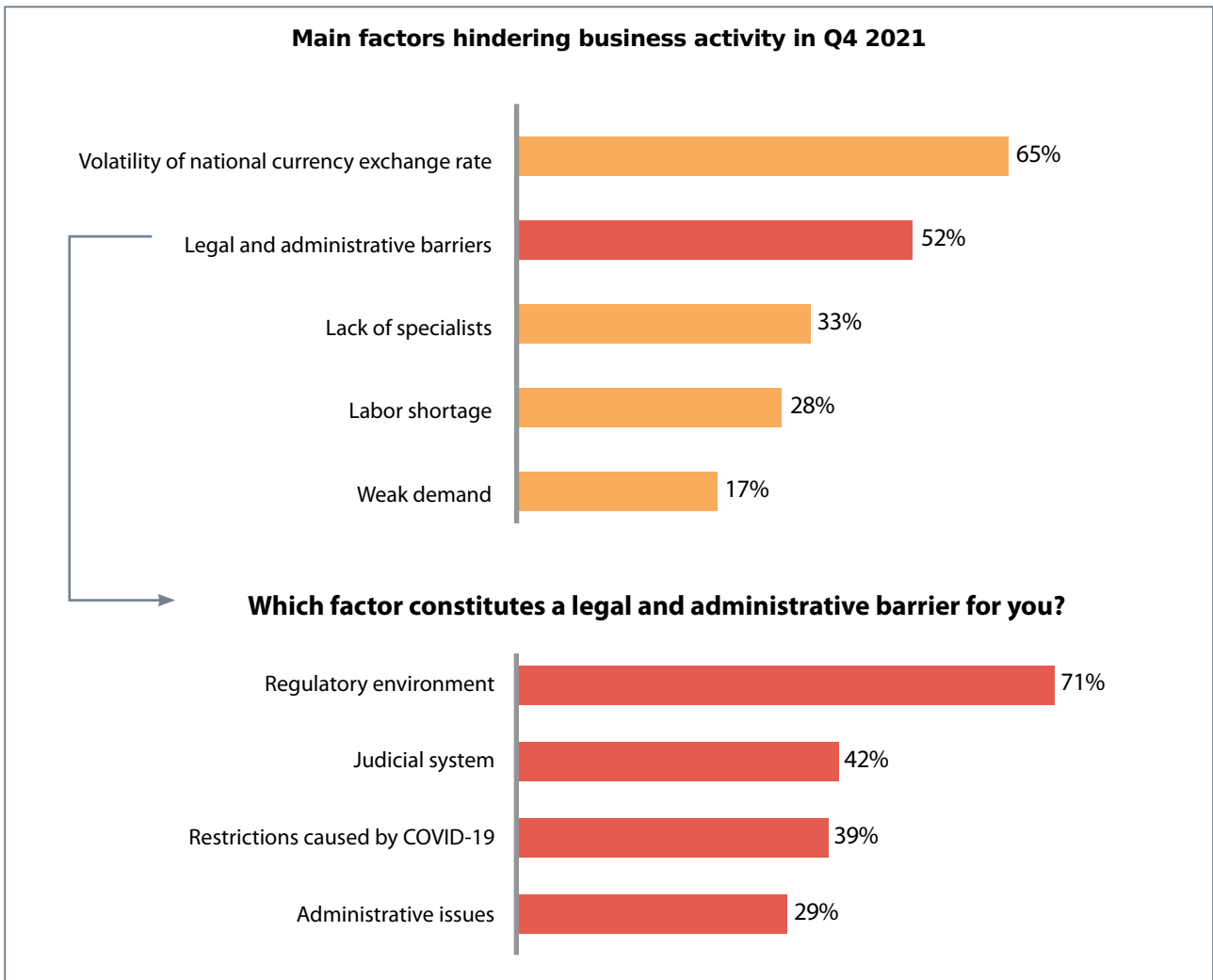
It is noteworthy that in Q3 and Q4 of 2021, financial constraints were no longer cited among the five most important hindering factors, while in the previous quarters this factor was always among the top impediments mentioned by surveyed companies.

In Q4 of 2021, similar to the previous two quarters, the volatility of the national currency exchange rate was cited as the top factor hindering business (65% of surveyed companies cited this factor as the most hindering). It was cited by 85.7% of companies in the construction sector, 71.4% of companies in the trade sector, 60% in the service sector and 42.9% in the manufacturing sector.

In Q4 2021, compared to Q3 2021, among the factors hindering business activity, the share of companies citing weak demand for products and services (decreased by 17 percentage points) and financial constraints (by 12 percentage points) as hindering factors decreased the most. While the share of companies citing legal and administrative barriers as a hindering factor increased the most (5 percentage points).

It should be noted that since Q2 of 2021, the share of companies citing weak demand for products and services and financial constraints as factors hindering business activity has been decreasing. Moreover, in that period, the share of the companies, for which the labor shortage is among hindering factors, has been stable. Meanwhile, the share of the companies citing legal and administrative barriers as hindering factors have been decreasing throughout Q1-Q3 of 2021, however, it increased in Q4 of 2021.

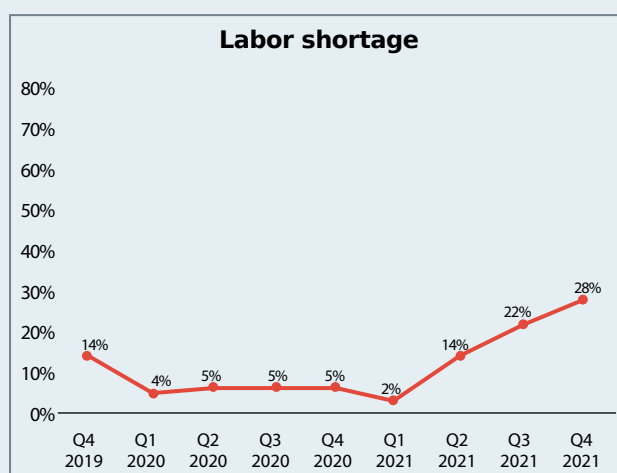
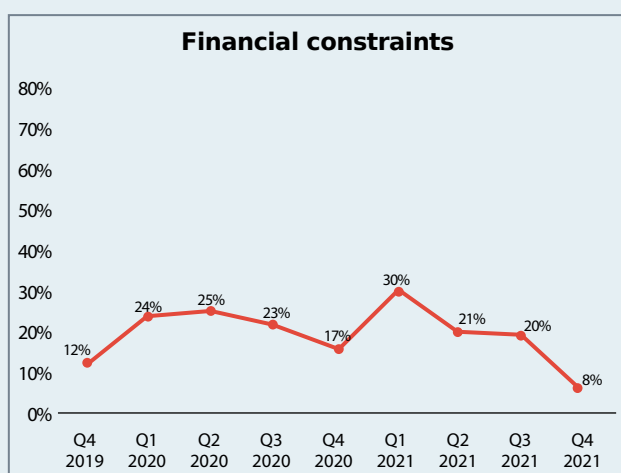
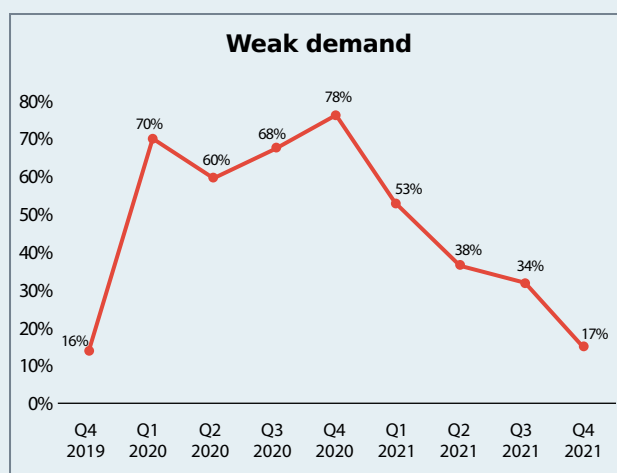
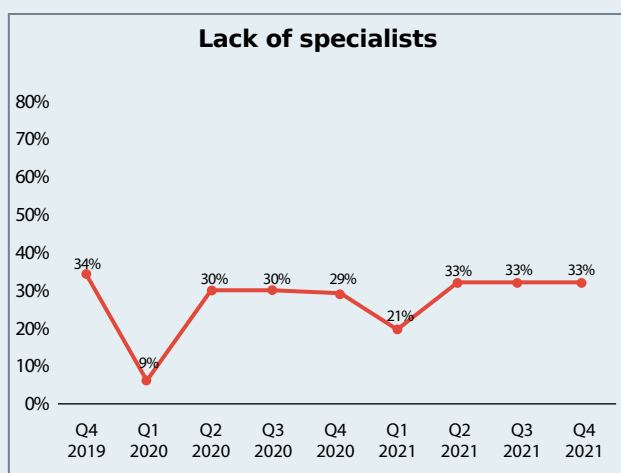
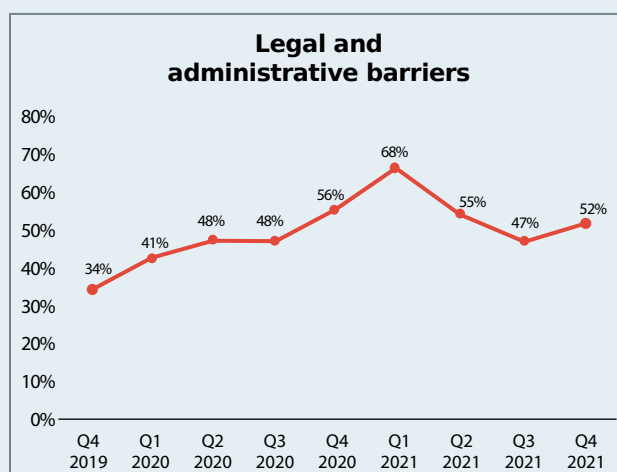
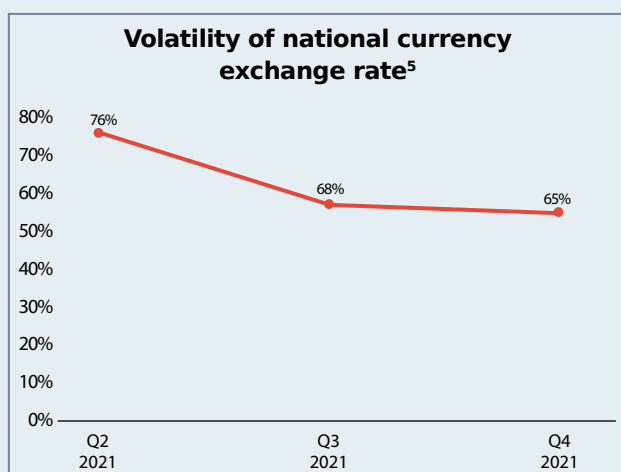
⁴ Volatility of national currency exchange rate as a factor hindering business was added to the survey questionnaire in Q2 of 2021.



Graph 9: The main challenges that BAG businesses face in Q4 2021

In Q4 of 2021, similar to the previous quarter, the regulatory environment is the main reason why legal and administrative barriers are named amongst the factors hindering business activity. This impediment was followed by the judicial system. It is noteworthy, that in Q4 of 2021, compared to previous quarter, the share of the companies to cite COVID-19-related restrictions as a hindering factor decreased (by 5 percentage points), while the share of companies citing the judicial system as a hindering factor increased the most (by 16 percentage points).

Main factors hindering business activity Q4 2019-Q4 2021



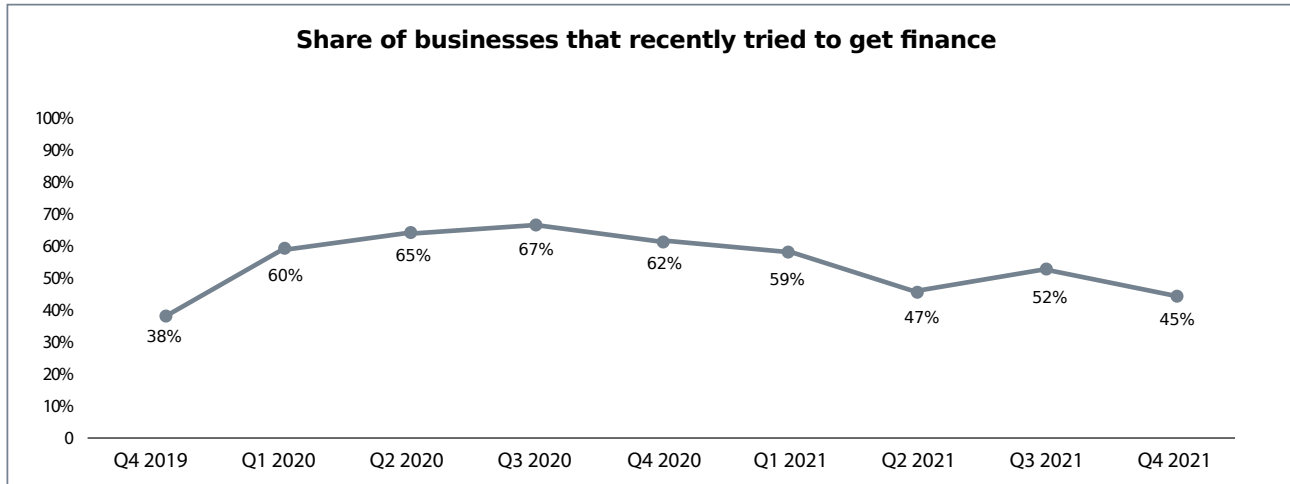
Graph 10: Main factors hindering business activity

⁵ Volatility of national currency exchange rate as a factor hindering business was added to the survey questionnaire in Q2 of 2021.

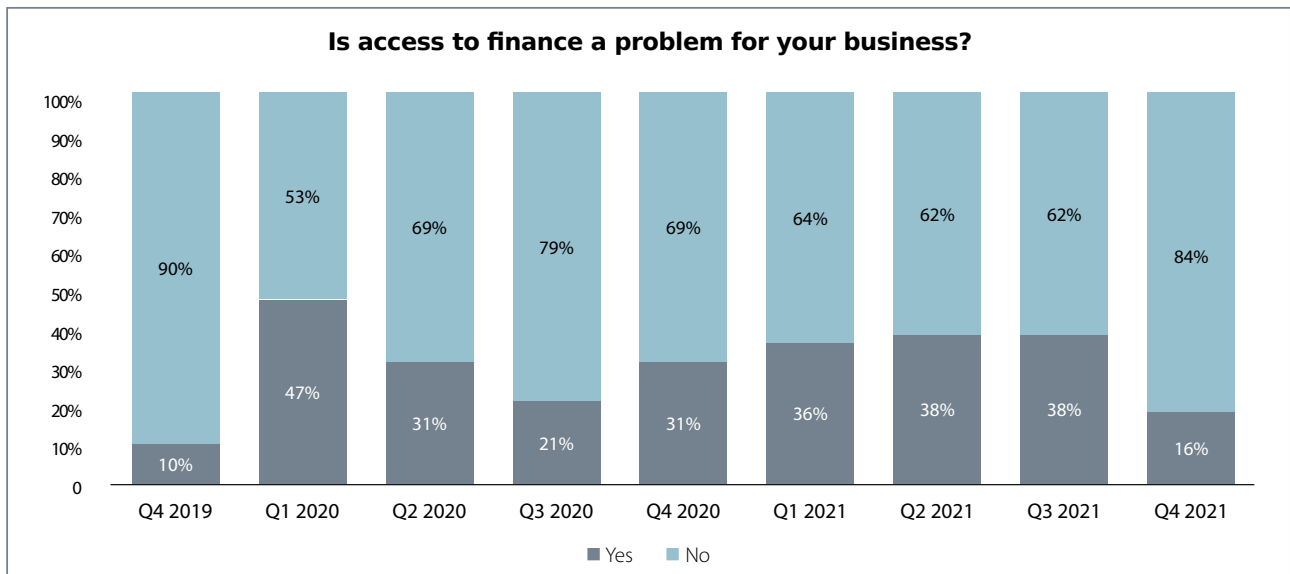
FINANCING

In Q4 of 2021, 45% of surveyed companies claimed to have recently tried to obtain finance, which is 7 percentage points lower than the figure recorded in the previous quarter.

In Q4 of 2021, 16% of those companies that recently tried to access finance also noted that access to finance was a problem for their business. This figure is significantly lower (22 percentage points) than that of previous quarter.



Graph 11: Businesses that recently tried to get finance

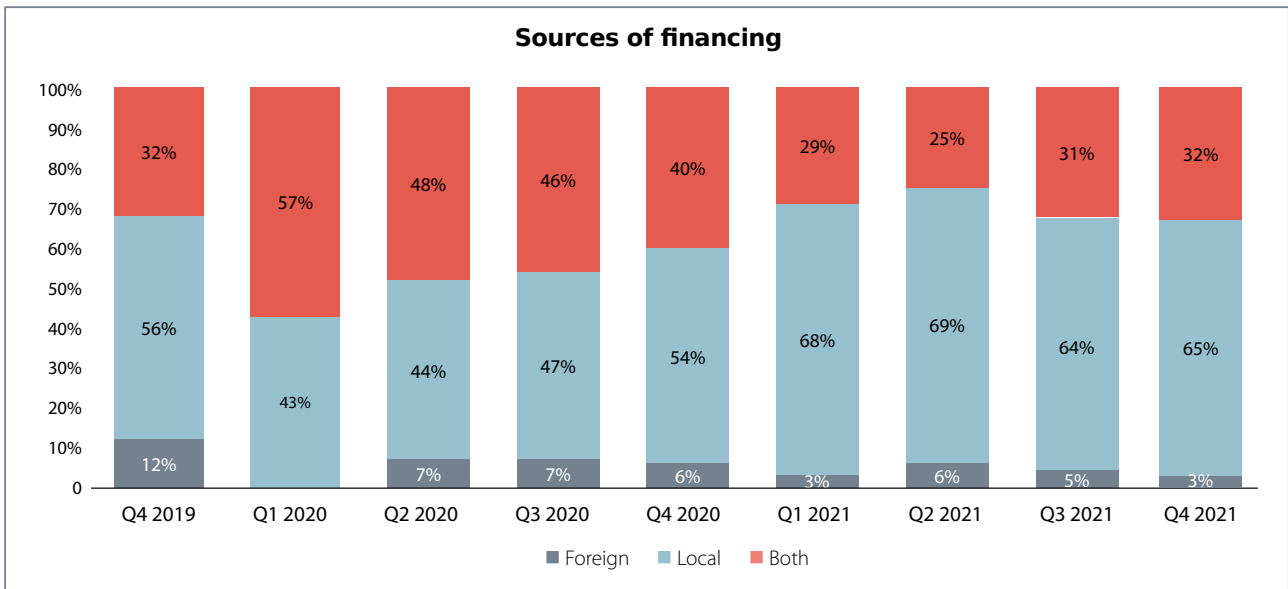


Graph 12: Access to finance⁶

Regarding sources of financing⁷, in Q4 of 2021, similar to previous quarters, the majority of surveyed companies stated that they were financed by local sources.

⁶ The question was only answered by those companies that stated they had recently sought finance.

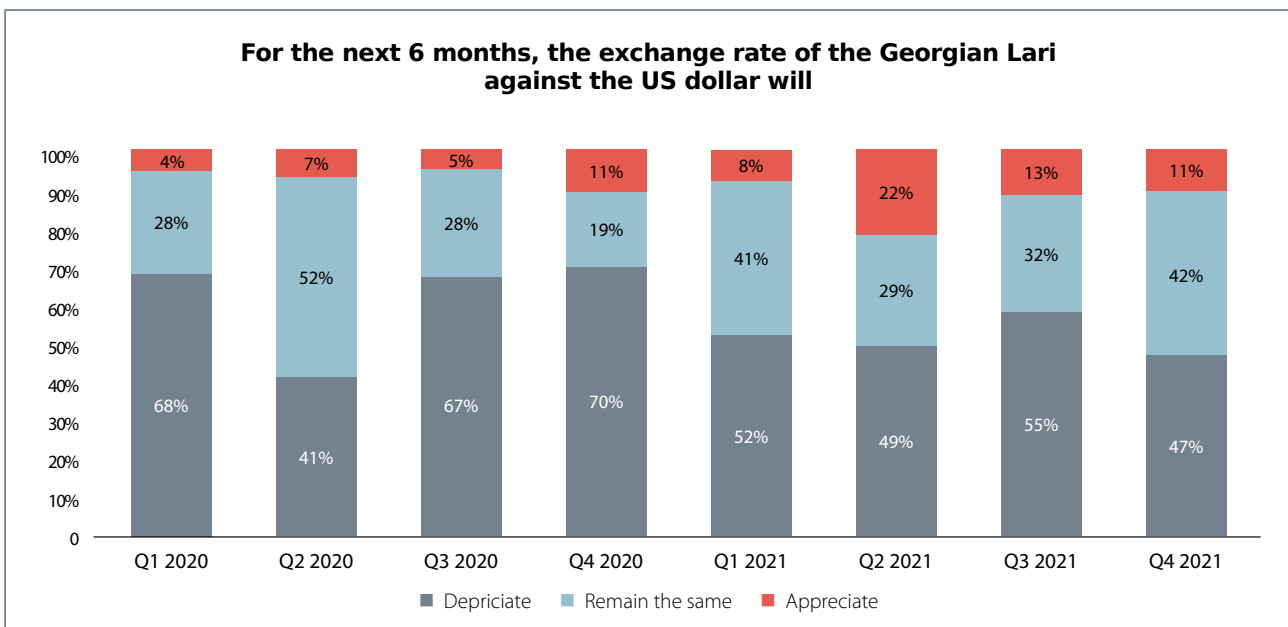
⁷ The change in methodology in Q1 of 2021 (the increase in the number of surveyed companies) altered the financing structure. This methodological change did not affect significantly any other indicators.



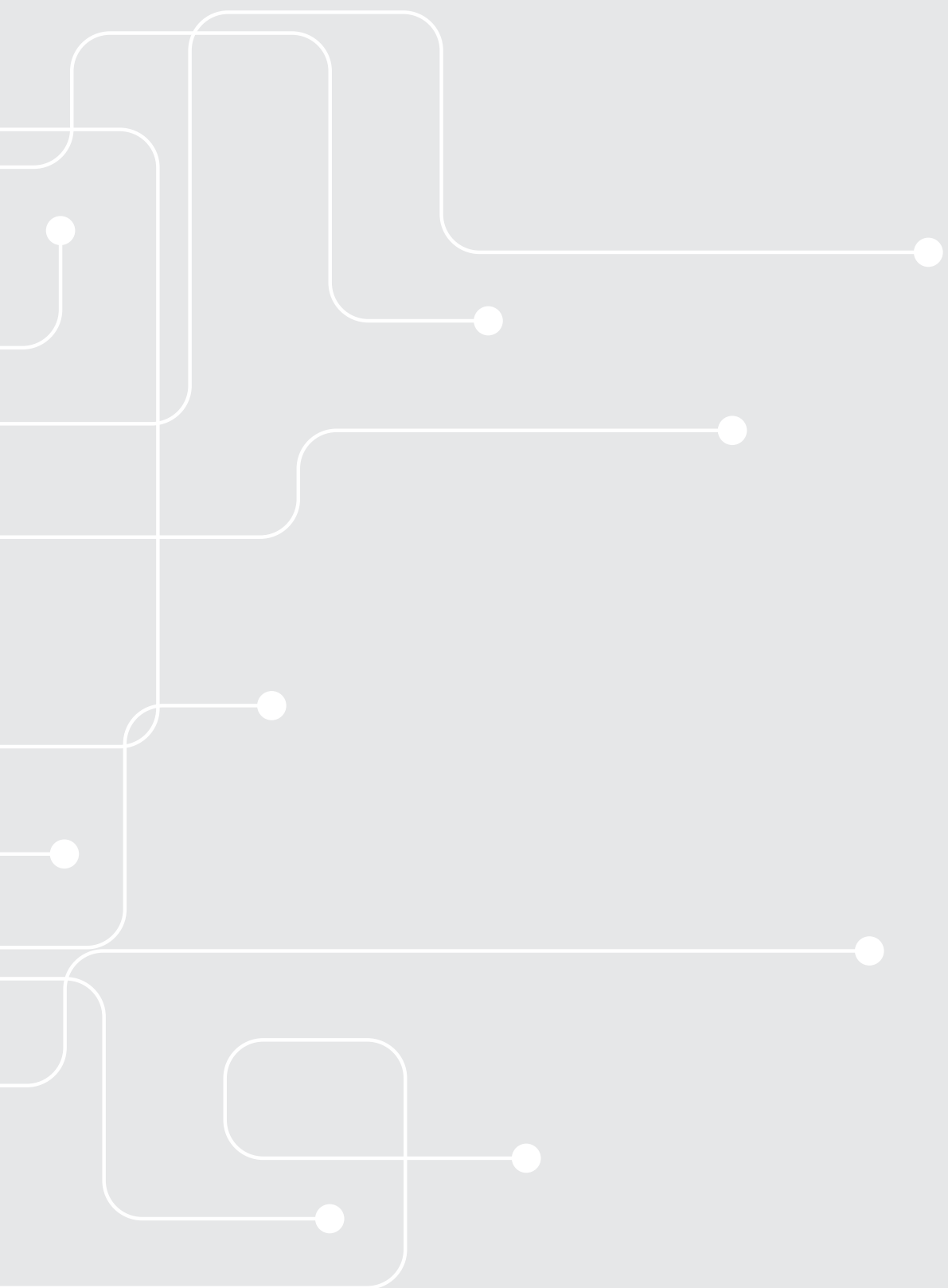
Graph 13: Sources of financing

EXCHANGE RATE EXPECTATIONS

In Q4 of 2021, compared to Q3 of 2021, the share of companies expecting that the national currency would depreciate against the US Dollar decreased by 8 percentage points. Moreover, in Q4 of 2021, 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 10 percentage points.



Graph 14: Exchange rate of the Georgian Lari against the US Dollar



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