



BAG

INDEX



საქართველოს ბიზნეს ასოციაცია
BUSINESS ASSOCIATION OF GEORGIA



Leibniz Institute for Economic Research
at the University of Munich



Research

BAG INDEX



**BUSINESS
CLIMATE**



**EMPLOYMENT
BAROMETER**

**II QUARTER
2021**

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	9
Financing	11
Exchange rate expectations	13
BAG Employment Barometer	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 and exchange rate expectations. For the purposes of this index, BAG members are divided into the following four sectors: trade, service, manufacturing and construction.

IN Q2 OF 2021, THE SURVEYED BUSINESSES ASSESS THEIR PRESENT BUSINESS SITUATION NEGATIVELY, WHILE THEIR EXPECTATIONS FOR THE NEXT SIX MONTHS ARE POSITIVE. THE BAG BUSINESS CLIMATE INDICATOR AMOUNTS TO 20.5 POINTS IN Q2 OF 2021, WITH THE PRESENT BUSINESS SITUATION INDICATOR SITTING AT -2.2 AND THE BUSINESS EXPECTATIONS INDICATOR AT 45.8.

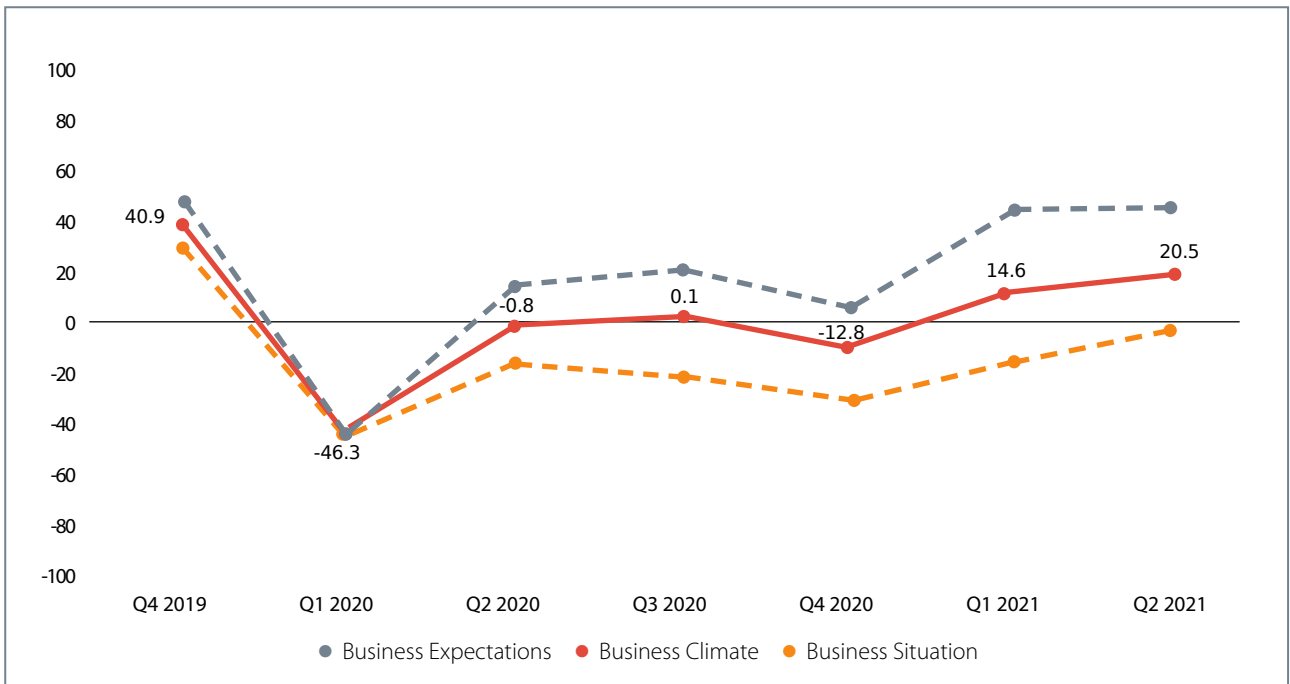
Encouragingly, in Q2 of 2021, compared to Q1 of 2021, the BAG Business Climate improved by 5.9 points. Moreover, in this period, the assessment of the present business situation and business expectations for the next six months improved, by 9.6 points and 0.9 points, respectively.

The figures for Q2 of 2021 demonstrate a significant improvement compared to Q2 of 2020. In Q2 of 2020, the BAG Business Climate indicator amounted to -0.8 points, while the business situation indicator amounted to -12.3, and the business expectations indicator was 12.2 (See Graph 1).

It is worth noting that in Q2 of 2020, Georgia operated under a state of emergency and economic activity was staggered, while the positive outlook in the Q2 of 2021 is attributed to the relaxing of the curfew, the inception of a vaccination program, the reopening of restaurants on weekends, announcements of scheduled international flights, and the opening of land borders starting from June.

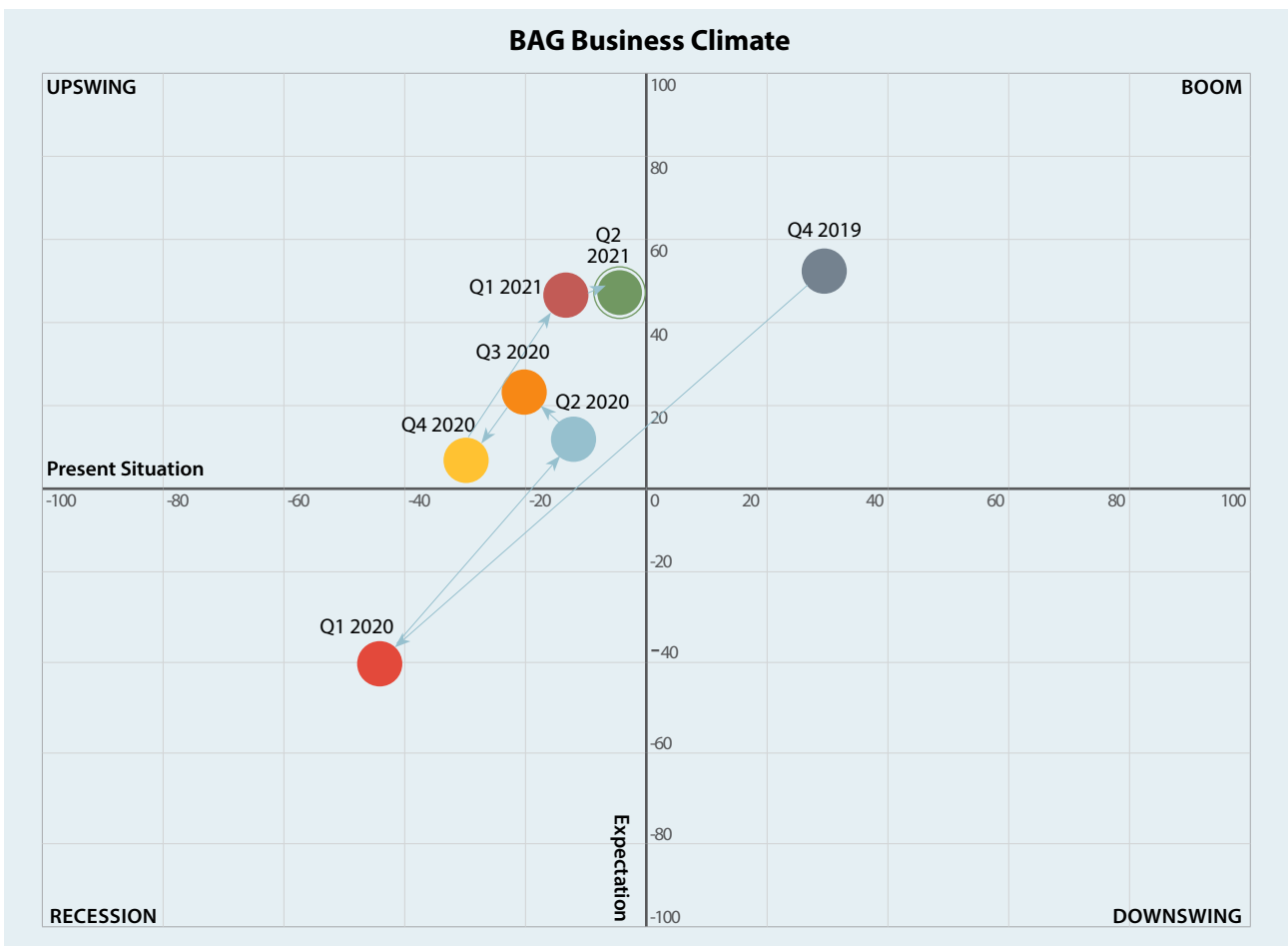
¹ In the first quarter of 2021, a change was made in the methodology of the BAG index. As a result, the number of companies surveyed increased: enterprises that belong to the corporate group of member companies were added to the existing survey respondents.

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 Q2 2021, BAG Business Climate is in **the upswing 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

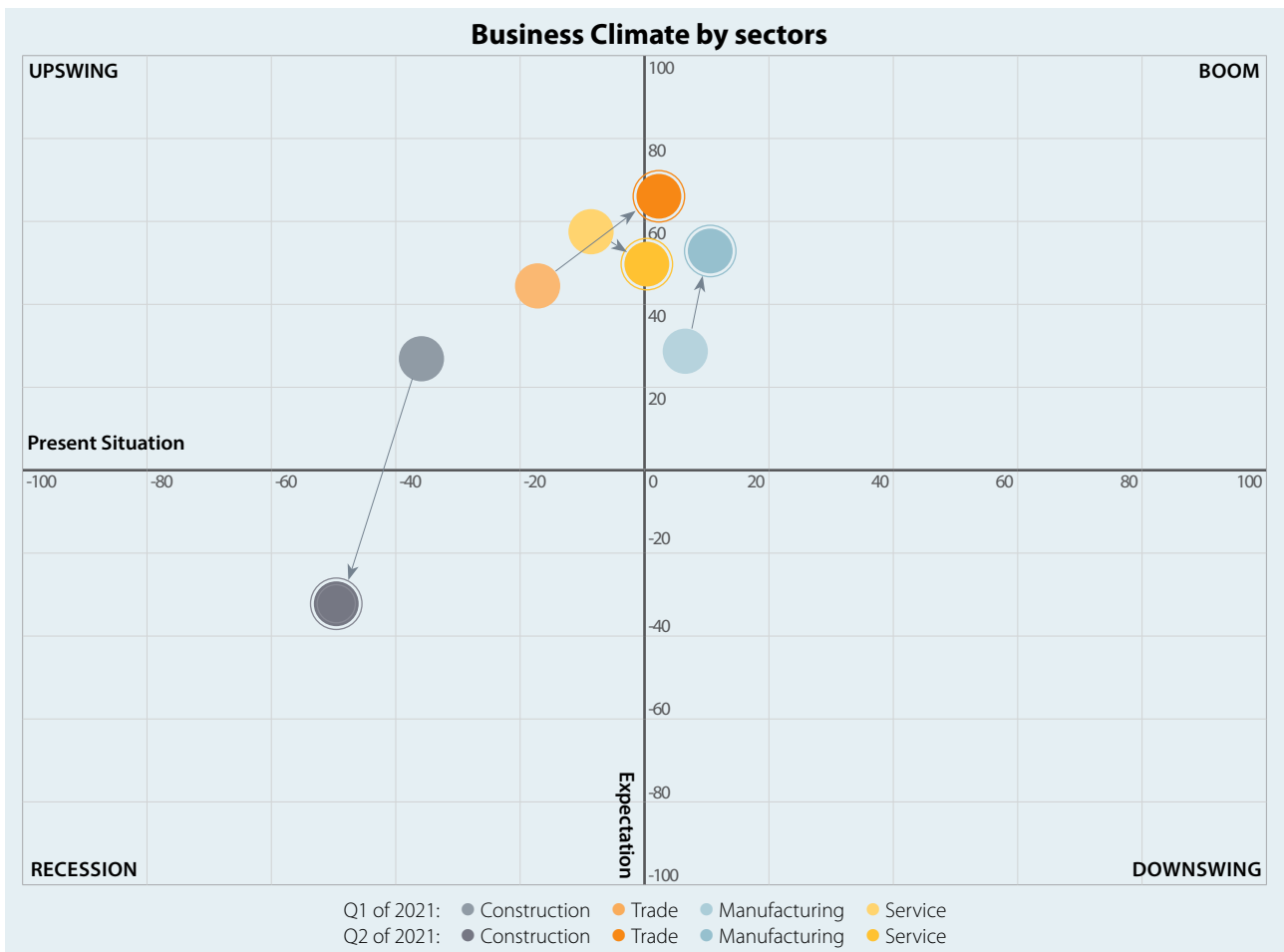
In Q2 of 2021, compared to Q1 of 2021, the **BAG Business Climate** indicator improved in almost all sectors and was positive for all sectors, except construction in which the indicator worsened by 37.7 points (See Table 1). It is worth noting that in Q1 of 2021, among the sectors, the construction sector was the only sector with a negative business climate indicator.

In Q2 of 2021, compared to Q1 of 2021, **the business situation** indicator improved in almost all sectors. The most positive assessment of the present business situation was recorded in the manufacturing sector, while the construction sector was the only one in which such assessment was negative. This could be attributed to a decrease in sales in Q2 of 2021. Pertinently, in this period, an increase in sales was not recorded, while 37.5% of respondents stated that sales decreased (See Graph 6). In the construction sector, 63% of respondents stated that in Q2 of 2021, the set prices either only just cover the costs or even did not fully cover their costs.

In Q2 of 2021, **the business expectations** indicator was positive for all sectors, except construction. The most optimistic predictions were recorded in the trade sector, largely due to an expected increase in sales prices and sales (See Graphs 6 and 7). In Q2 of 2021, compared to Q1 of 2021, expectations improved in the trade (by 25 points) and manufacturing (23.9 points) sectors, but worsened in the construction (-66.1 points) and service (-6.9 points) sectors.

Table 1: Balance values by sector in Q2 of 2021

	Business Climate	Present Business Situation	Business Expectation
Trade Sector	32.6	2.9	66.7
Service Sector	23.6	0	50.0
Manufacturing Sector	32.5	13.3	53.3
Construction Sector	-43.9	-50.0	-37.5
All Sectors	20.5	-2.2	45.8



Graph 3: Business Climate by sectors in Q1 and Q2 of 2021

Since Q1 of 2021, the assessment of the business climate in the trade sector has been positive and is still improving. This is likely to be attributable to positive dynamics in sales and sales prices in the given period and an optimistic outlook for the near future.

The service sector reflects a similar pattern. In Q1 and Q2 of 2021, the business climate indicator has been positive and is improving, which is linked to the positive outlook shared by many in the sector.

In the manufacturing sector, the business climate indicator has been positive since Q3 of 2020 and continues to improve. Unlike the trade and service sectors, in the manufacturing sector, the positive assessment of the business climate can be attributed to both a positive assessment of the current situation and optimistic expectations for the near future. In this period, local production and sales prices in the manufacturing sector have both been increasing in the majority of companies.

Across the covered sectors, the most negative assessment of the business climate is in the construction sector. In the generally gloomy Q1 2020 – Q2 2021 period, Q3 of 2020 was an exception when the business situation at that time was not assessed negatively by the construction sector. This can be attributed to a negative assessment of the current business situation. This can be attributed to the anti-crisis package provided by the Georgian government to developers, which included co-financing of mortgage interest rates until the end of 2020. However, despite this program, the assessment of the business situation in the construction sector worsened again starting from Q4 of 2020.



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

During the Q1 2020 – Q1 2021 period, the worst assessments of the business climate were mainly recorded in the construction sector.

During the Q1 2020 – Q1 2021 period, the most negative assessments of the business situation were mainly recorded in the service and construction sectors. In the given period, the assessments of the business situation were the least negative in the manufacturing sector (See Graph 4).

EMPLOYMENT, SALES, AND SALES PRICES BY SECTOR

Employment

Assessment of Q1 of 2021

- ✘ Only 18.3% of surveyed companies stated that the number of their employees increased in Q1 of 2021, compared to Q4 of 2020, while 18.3% stated that this figure had decreased. For the majority of respondents (63.4%), the number of their employees was unchanged.
- ✘ Across all sectors covered, the largest share of the surveyed companies in the service sector claim that the number of their employees had increased, in Q1 of 2021, compared to Q4 of 2020.

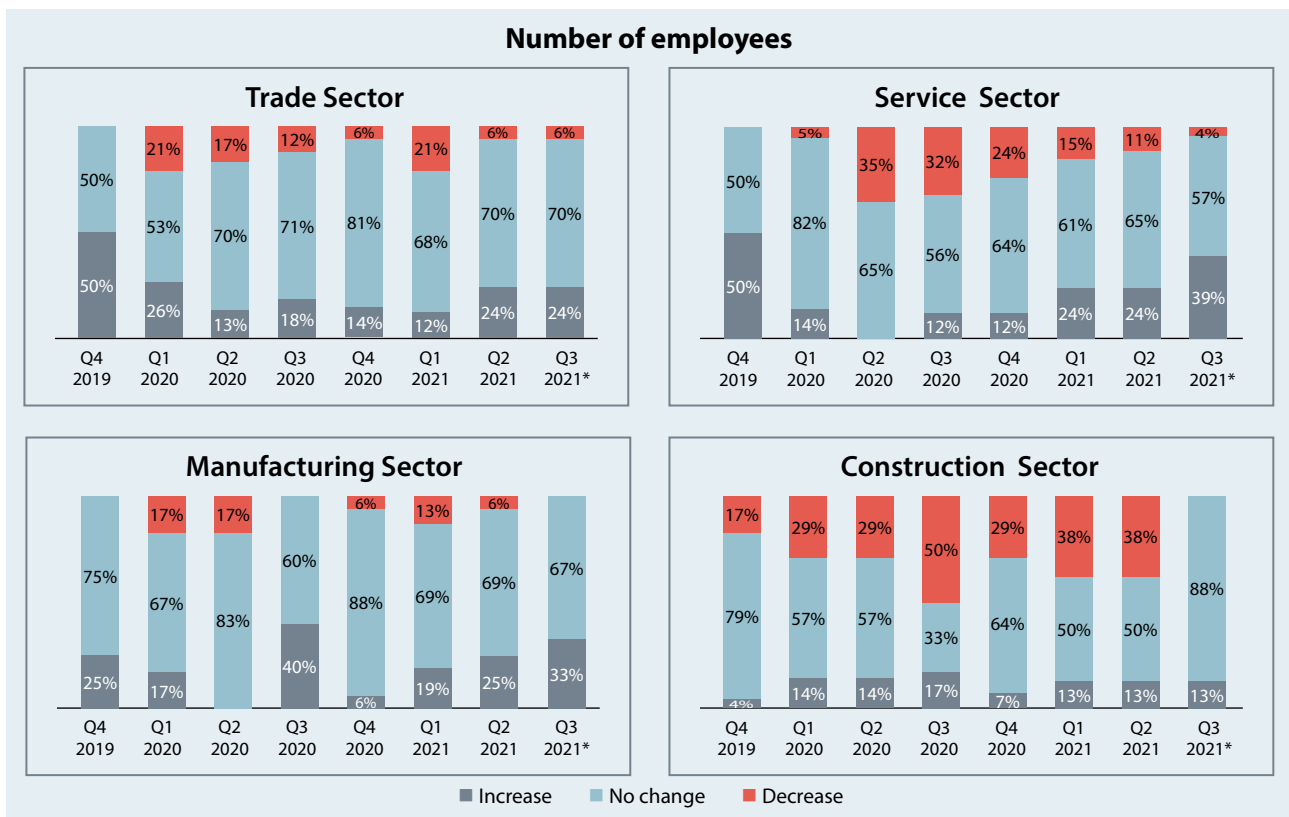
Situation in Q2 of 2021

- ✘ Overall, 23.3% of surveyed companies stated that in Q2 of 2021, compared to Q1 of 2021, the number of their employees increased, while 10.7% recorded a decrease. The majority of companies (66%) stated that the number of employees had not changed.
- ✘ Across sectors, the construction sector had the most surveyed businesses (37.5%) to claim that the number of their employees had decreased in Q2 of 2021, compared to Q1 of 2021. It is worth

noting here that in Q1 of 2021, among sectors, the construction sector was also responsible for the highest proportion of surveyed companies to report a quarter-on-quarter decrease in the number of hired employees.

Expectations for Q3 of 2021

- ✘ In total, 31.4% of surveyed companies expect that in Q3 of 2021, compared to Q2 of 2021, they will increase the number of their employees, while 3.9% expect a decrease. The majority of companies (64.7%) do not expect any change in the number of their employees in this period.
- ✘ The most positive outlook regarding employment was found in the service and manufacturing sectors. In Q3 of 2021, compared to Q2, 39.1% and 33.3% of surveyed businesses in these respective sectors expect an increase in the number of employees.



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

To sum up, during the Q1 2020 – Q2 2021 period, for the majority of surveyed companies the number of employees did not change. Moreover, from Q1 of 2021, regarding employment, the most positive trends have been recorded in the manufacturing and service sectors, with the number of employees in these sectors increasing in more and more companies every quarter. Meanwhile, since Q3 of 2020, the situation regarding employment has been worst in the construction sector, where a significant share of companies has reported a decrease 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 Q1 of 2021

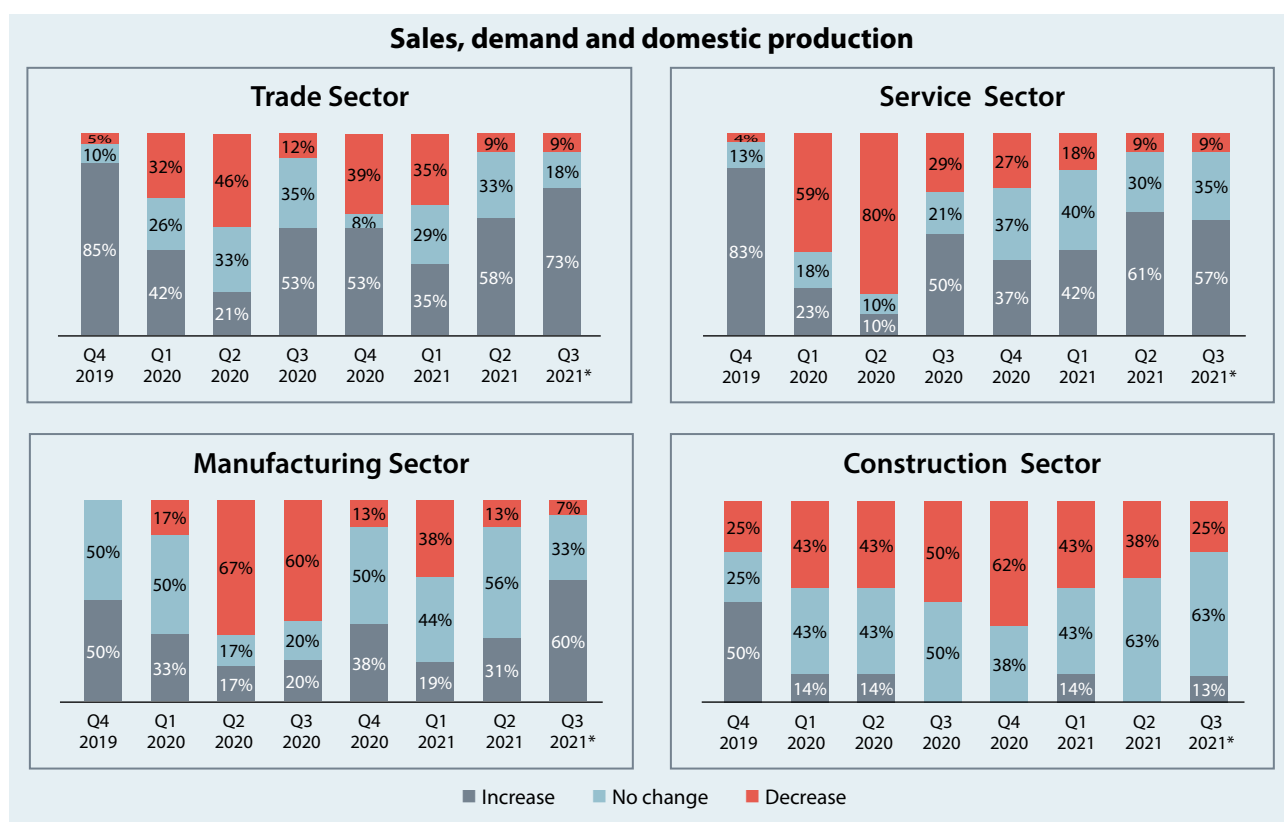
- ✘ The majority of surveyed businesses in the service and trade sectors claimed that their turnover/sales increased in Q1 2021, compared to Q4 of 2020.
- ✘ In Q1 of 2021, the situation regarding sales was assessed most negatively in the construction sector, where 42.9% of companies stated that their contracts/presales decreased, compared to the previous quarter.

Situation in Q2 of 2021

- ✘ Similar to Q1 of 2021, in Q2 of 2021 the situation regarding turnover/sales was assessed most positively by representatives of the service and trade sectors. In these respective sectors, 61% and 58% of surveyed companies recorded growth in sales/turnover in this period.
- ✘ In Q2 of 2021, the worst situation regarding sales was recorded in the construction sector. According to surveyed respondents, their sales did not increase during this period.

Expectations for Q3 of 2021

- ✘ For Q3 of 2021, compared to Q2 of 2021, the outlook regarding sales in most sectors is positive. Indeed, the surveyed companies in trade, manufacturing, and service sectors expect sales to increase.
- ✘ The most pessimistic expectations for Q3 of 2021 are in the construction sector, where only 12.5% of surveyed companies expect sales to increase.



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

To sum up, during the Q1 2020 – Q2 2021 period, the trade and service sectors showed the most positive trends regarding sales, wherein the majority of companies the volume of sales has been increasing every quarter. While the worst situation regarding sales has been recorded in the construction sector since Q1 of 2020, where for the significant share of surveyed companies the volume of sales has been decreasing every quarter. However, in Q2 2021, the situation has relatively stabilized, and the majority of respondents stated that the volume of sales did not change in this quarter.

Sales prices

Assessment of Q1 of 2021

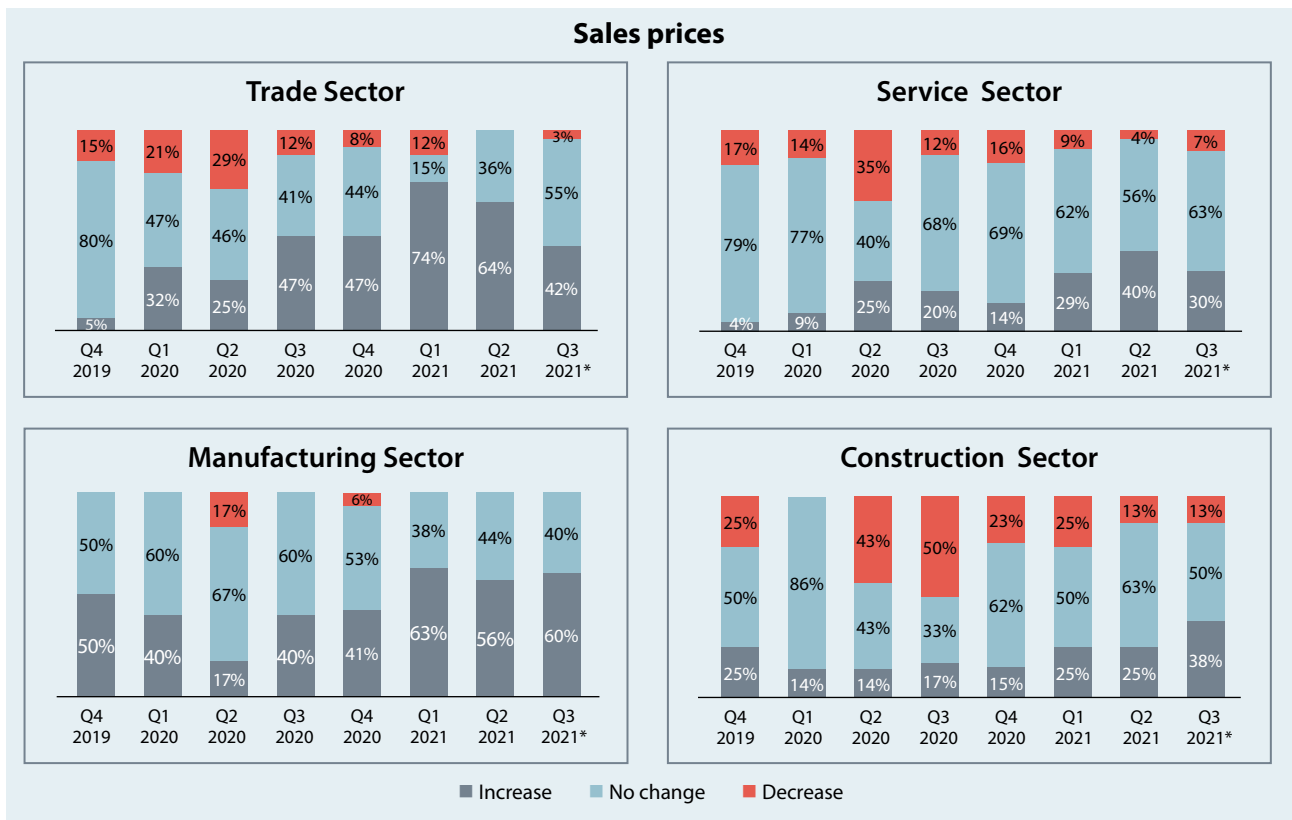
- ✘ Overall, 48.5% of surveyed companies stated that in Q1 of 2021, compared to the previous quarter, sales prices increased, while 41.8% stated that prices had gone unchanged. According to 9.7% of respondents, sales prices decreased in this period.
- ✘ Across the covered sectors, the majority of surveyed companies in the trade and manufacturing sectors recorded an increase in sales prices in Q1 of 2021, compared to Q4 of 2020.

Situation in Q2 of 2021

- ✘ In total, 49% of surveyed companies stated that in Q2 of 2021, compared to Q1 of 2021, sales prices had increased, while 48% stated that sales prices remained unchanged, and 3% claimed that sales prices had decreased.
- ✘ The majority of surveyed companies in the manufacturing and trade sectors stated that sales prices had increased in Q2 of 2021, compared to Q1 of 2021.
- ✘ Across the covered sectors, the construction sector had the largest share of respondents to report a decrease in sales prices in Q2 of 2021, compared to Q1 of 2021.

Expectations for Q3 of 2021

- ✘ Overall, 39.2% of surveyed companies expect sales prices to increase in Q3 of 2021, compared to Q2 of 2021, while 55.9% do not expect this figure to change, and 4.9% expect a decrease.
- ✘ Among the reviewed sectors, the most positive outlook regarding sales prices is recorded in the manufacturing sector, where 60% of surveyed companies expect sales prices to increase in Q3 of 2021, compared to Q2 of 2021.

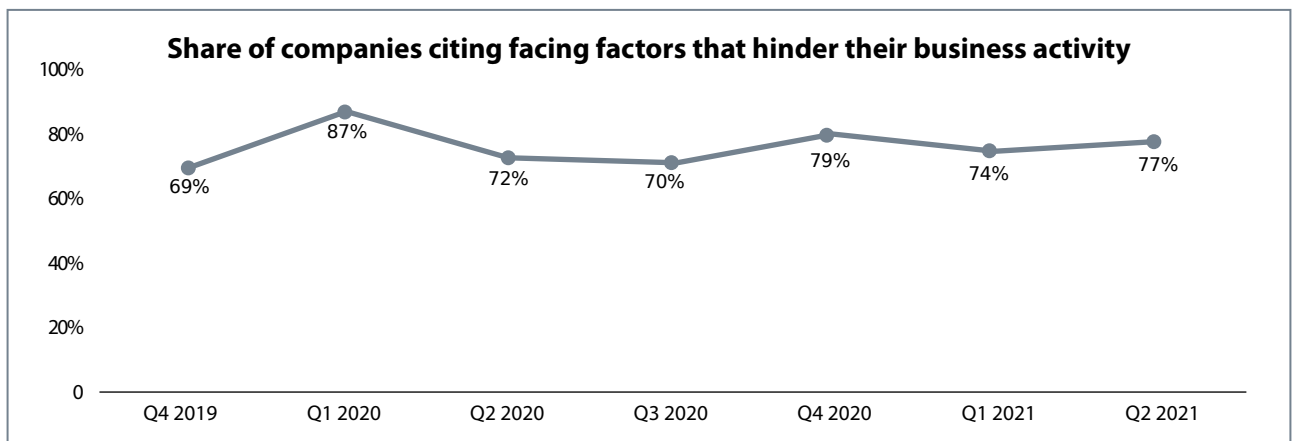


Graph 7: Sales prices in trade, service, manufacturing and construction sectors

To sum up, in the Q1 2020 – Q2 2021 period, among the covered sectors, the most positive tendencies were seen in the manufacturing and trade sectors regarding sales prices, where the majority of companies recorded an increase in sales prices on a quarterly basis. Meanwhile, in the Q1 2020 – Q2 2021 period, for the majority of companies in the service and construction sectors, sales prices remained unchanged.

FACTORS HINDERING BUSINESS ACTIVITY

In Q2 of 2021, compared to Q1 of 2021, the share of surveyed companies to claim there are factors hindering their business activity increased by 3 percentage points and reached 77%.

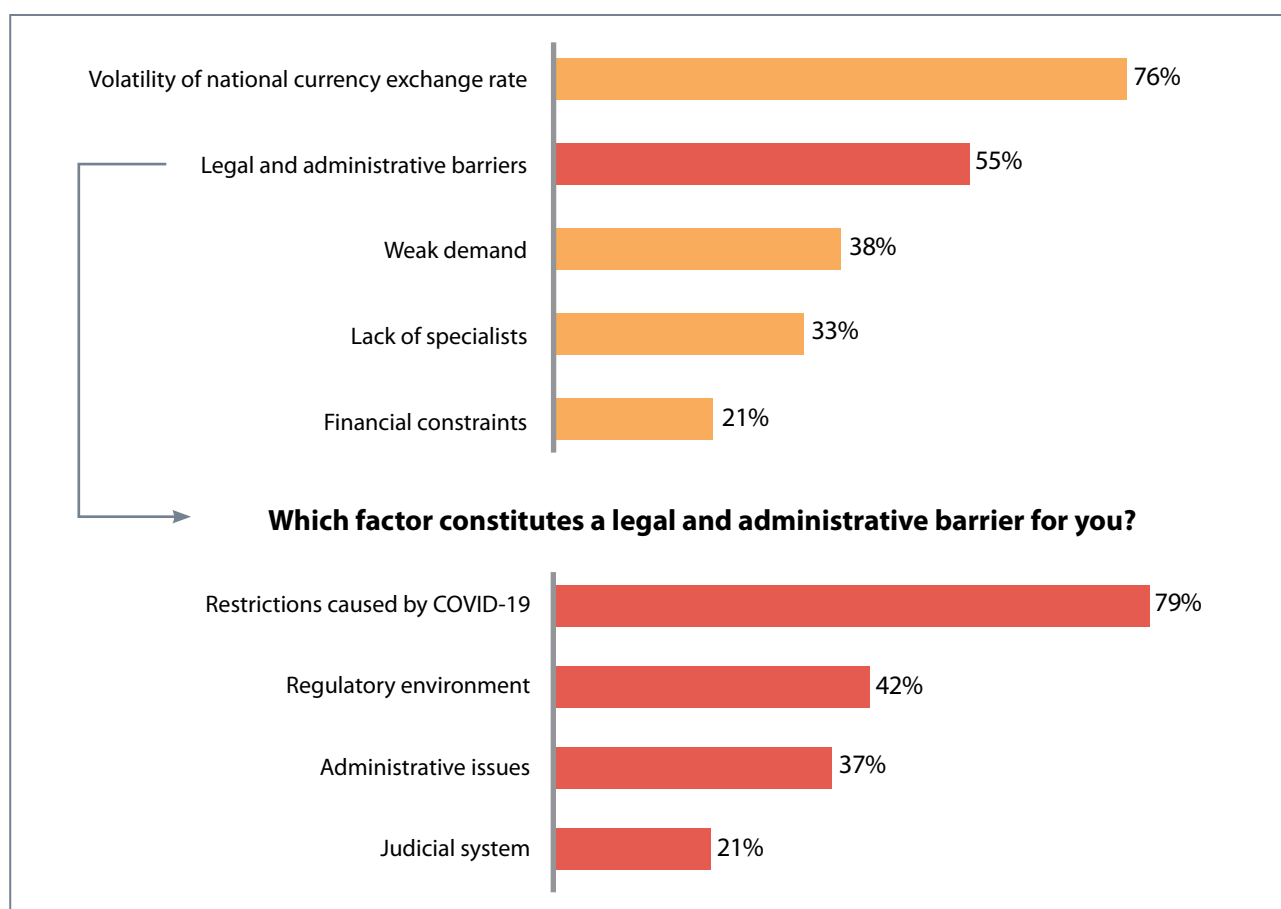


Graph 8: Existence of factors hindering business activity

In Q2 of 2021, five factors were emphasized as the most hindering for business activity: volatility of national currency exchange rate⁴, legal and administrative barriers, weak demand for products and services, a lack of specialists and financial constraints (See Graph 9).

In Q2 of 2021, the volatility of the national currency exchange rate was cited as the top factor hindering business. It was cited by 91% of companies in the manufacturing sector, 81% in the trade sector, 68% in the service sector, and 67% in the construction sector.

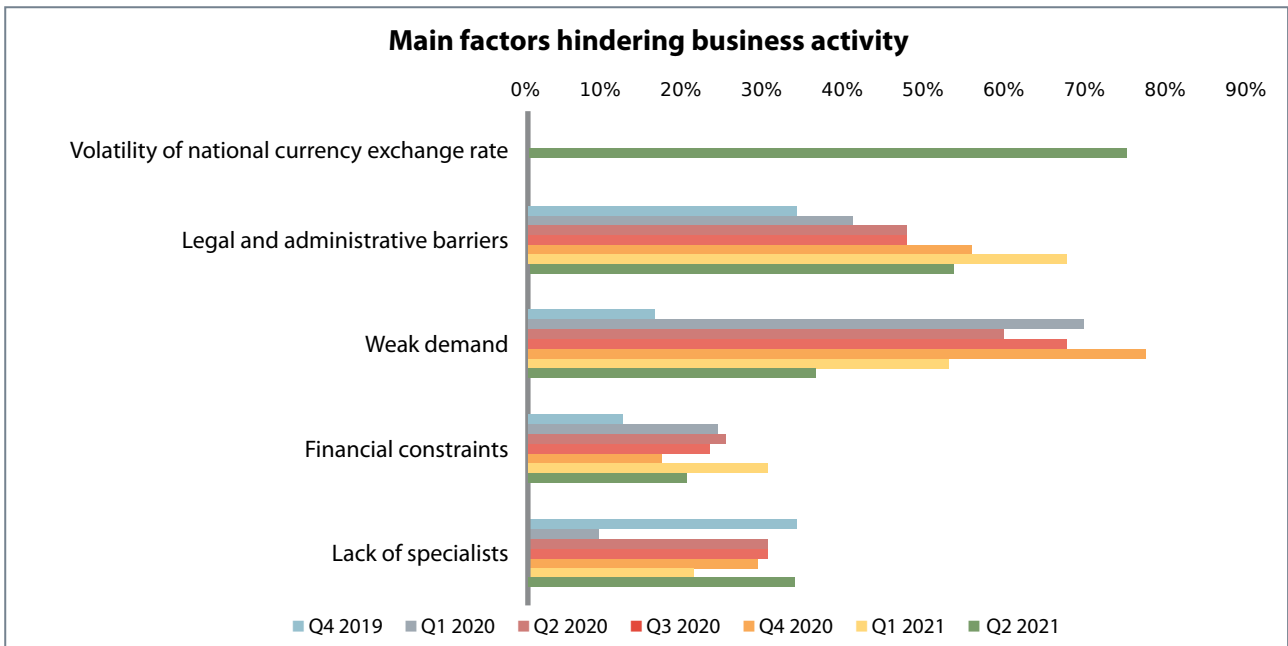
Among the factors hindering business activity, the share of companies citing weak demand as a hindering factor decreased the most, compared to the previous quarter (by 15 percentage points), while the largest increase was recorded in the problem regarding the lack of specialists (by 12 percentage points).



Graph 9: The main challenges that BAG businesses face in Q2 2021

In Q2 of 2021, similar to Q1 of 2021, restrictions caused by the COVID-19 pandemic are the main reason why legal and administrative barriers are named amongst the factors hindering business activity. This is followed by the regulatory environment.

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

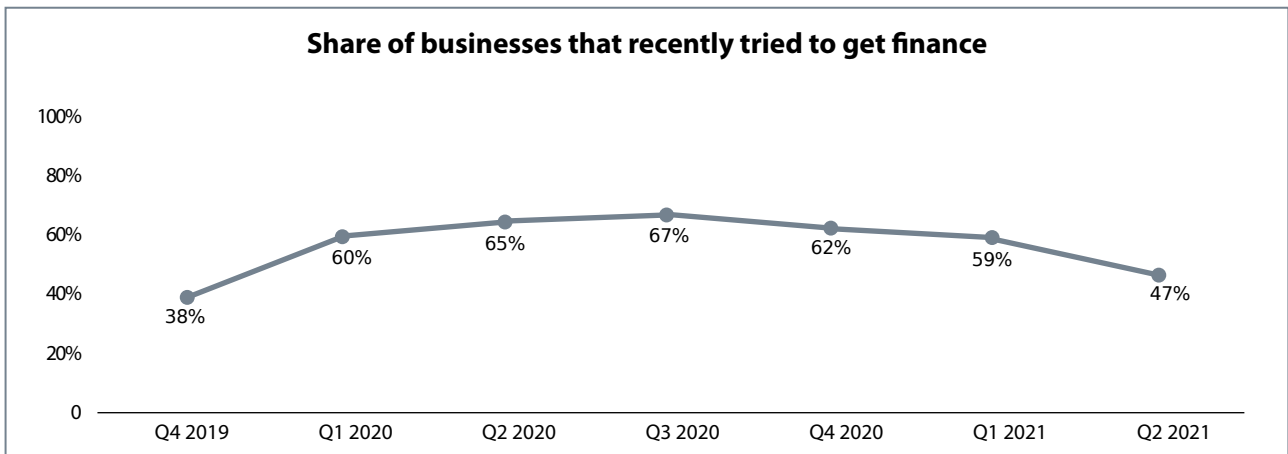


Graph 10: Main factors hindering business activity

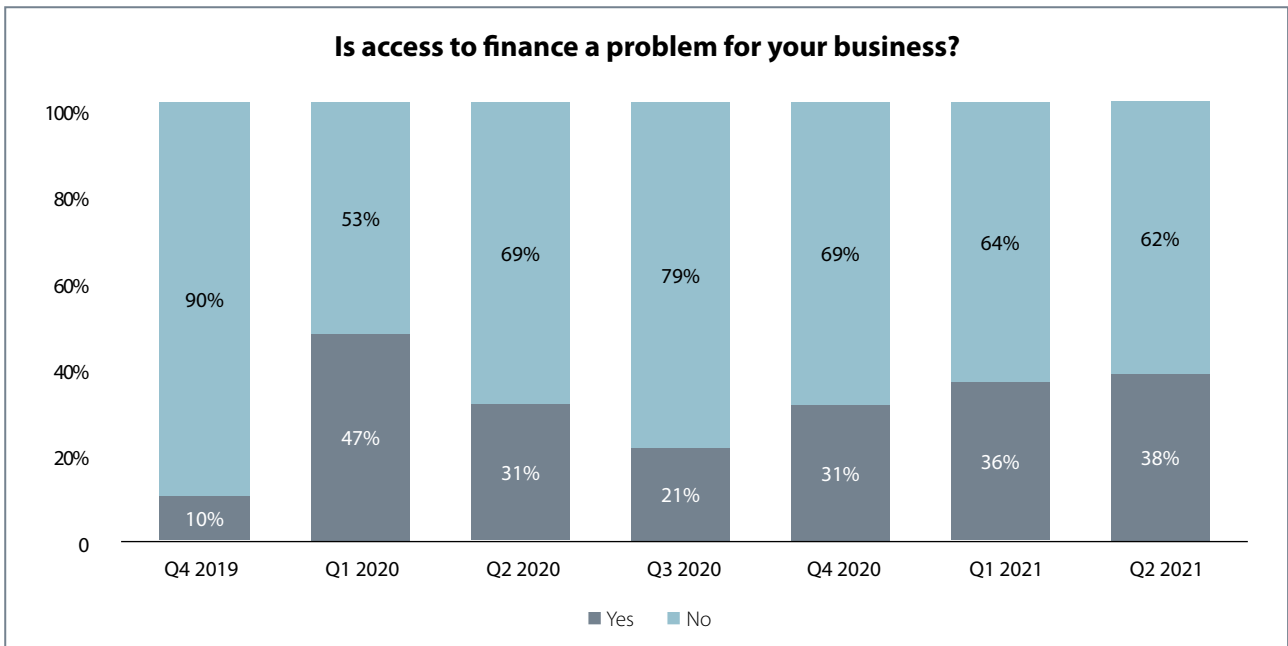
FINANCING

In Q2 of 2021, 47% of surveyed companies claimed to have recently tried to obtain finance, which is lower than the figure recorded in the previous quarter. The biggest figures in this regard were recorded in Q3 of 2020, but since Q4 of 2020, this indicator has been decreasing.

In Q2 of 2021, 38% of those companies that recently tried to access finance also noted that access to finance was a problem for their business.

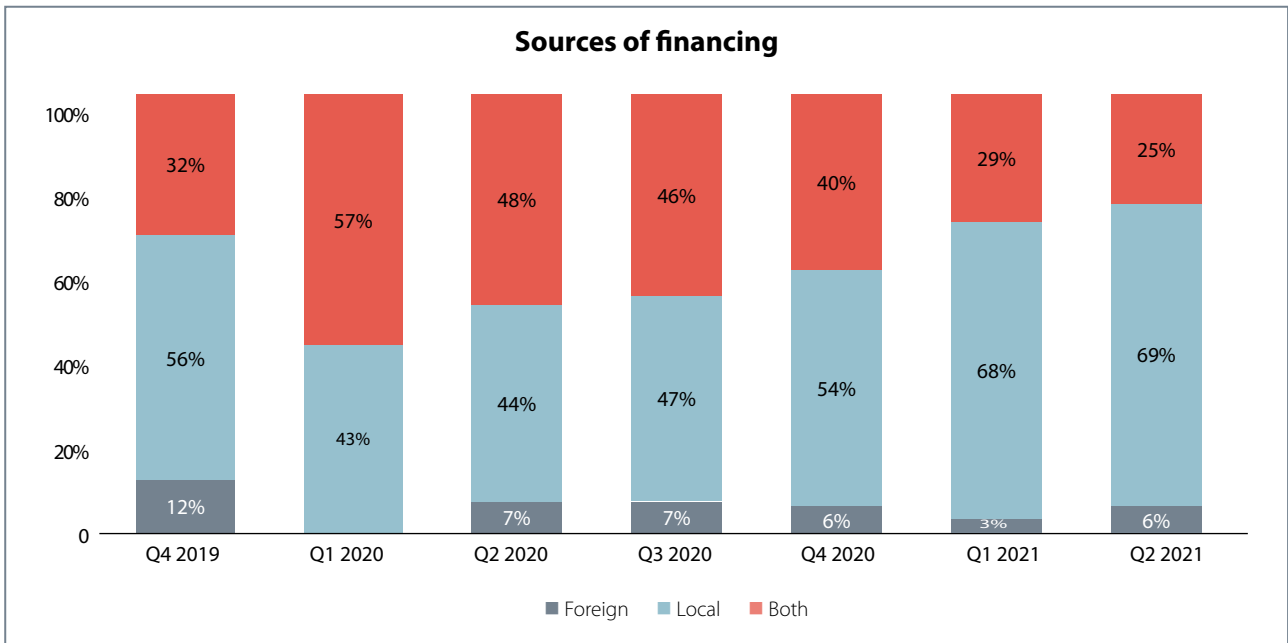


Graph 11: Businesses that recently tried to get finance



Graph 12: Access to finance⁵

Regarding the sources of financing⁶, in Q2 of 2021, similar to the previous quarter, the majority of surveyed companies stated that they are financed by local sources, while the share of companies financed by foreign sources remained low.



Graph 13: Sources of financing

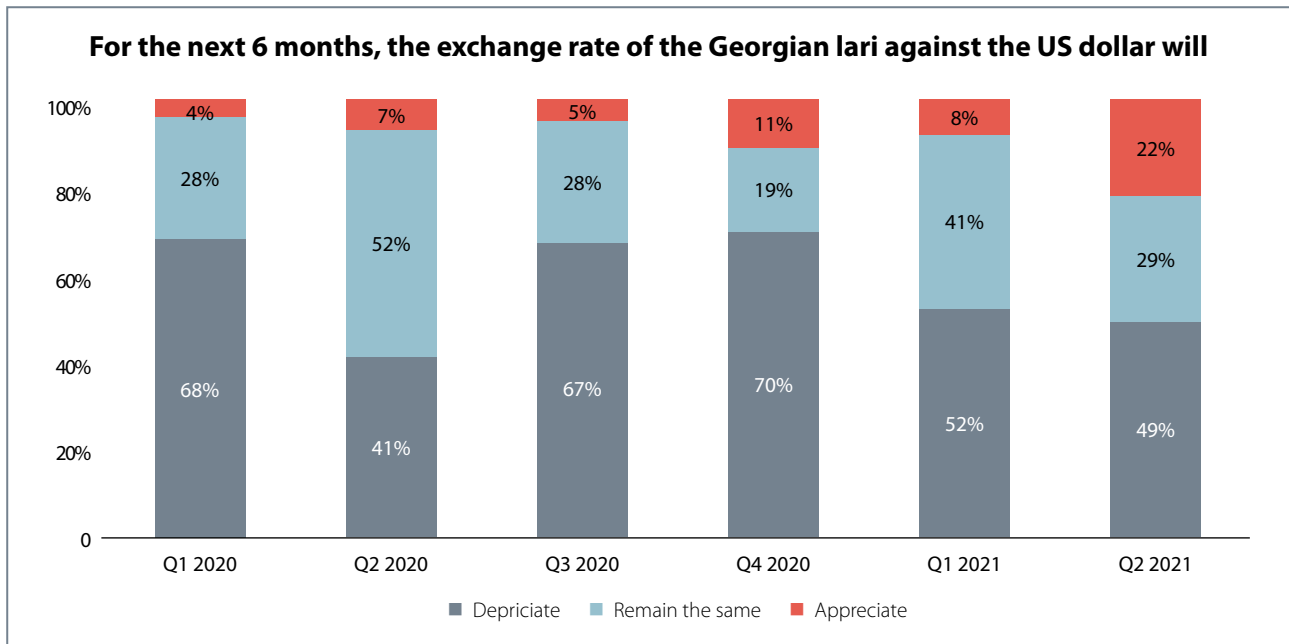
⁵ The question was only answered by those companies that stated they had recently sought finance.

⁶ 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.

EXCHANGE RATE EXPECTATIONS

In Q2 of 2021, compared to Q1 of 2021, the share of companies expecting that the national currency would appreciate against the US Dollar increased significantly. It is worth noting that such expectations had not been recorded even in the pre-pandemic period (Q4 of 2019). The optimism of respondents goes in line with the GEL's appreciation trend against the USD that was recorded after sharp depreciation in April.

Despite the recent appreciation of the GEL, the share of companies that expect the GEL to depreciate against the USD in the next six months remains high (49%).

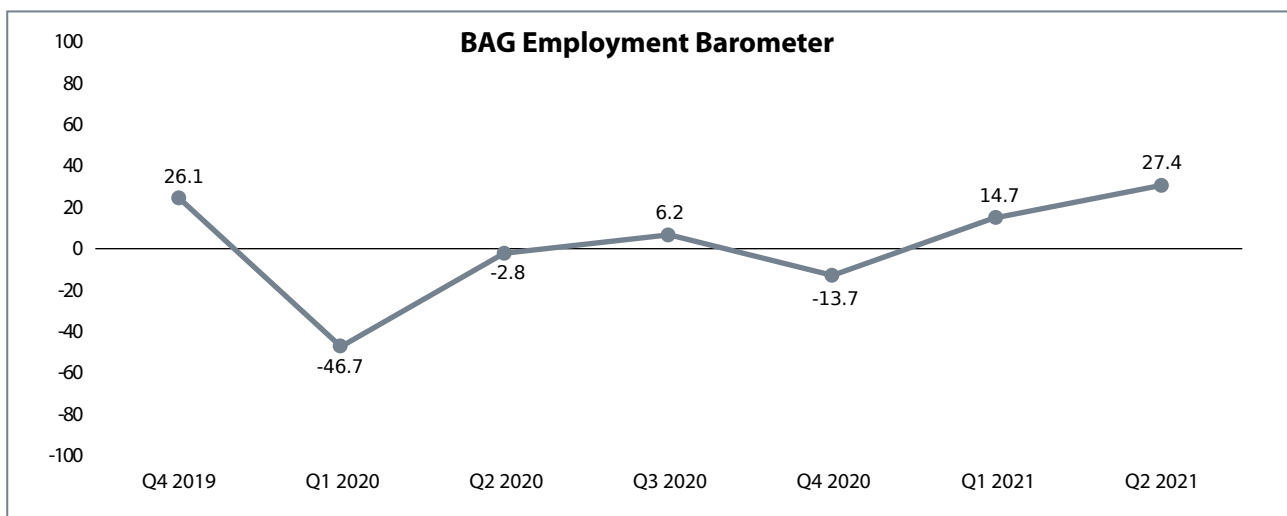


Graph 14: Exchange rate of the Georgian Lari against the US Dollar

BAG EMPLOYMENT BAROMETER

The BAG Employment Barometer reflects companies' expectations regarding changes in employment in the next three months.⁷

IN Q2 OF 2021, THE SURVEYED BUSINESSES GENERALLY HAD A POSITIVE OUTLOOK REGARDING EMPLOYMENT FOR THE NEXT THREE MONTHS. THE BAG EMPLOYMENT BAROMETER AMOUNTED TO 27.4 POINTS, MARKING A SIGNIFICANT IMPROVEMENT, COMPARED TO BOTH Q2 OF 2020 (BY 30.2 POINTS) AND Q1 OF 2021 (BY 12.7 POINTS).



Graph 15: BAG Employment Barometer

In Q2 of 2021, compared to Q1 of 2021, the employment barometer indicator improved for all sectors, except the construction sector. The expectations of companies regarding employment in the construction sector worsened compared to the previous quarter, with only 12.5% expecting an increase in their number of employees.

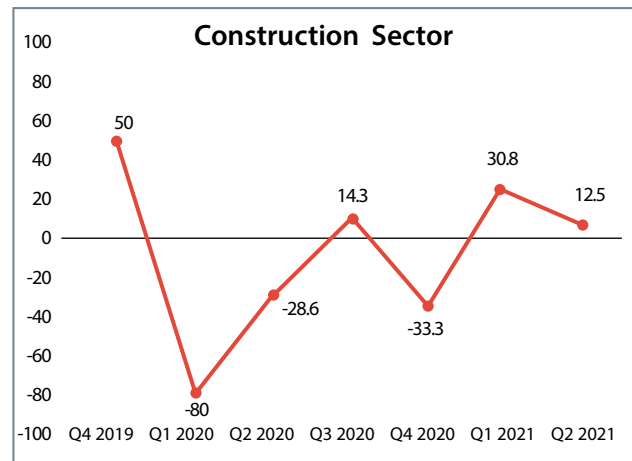
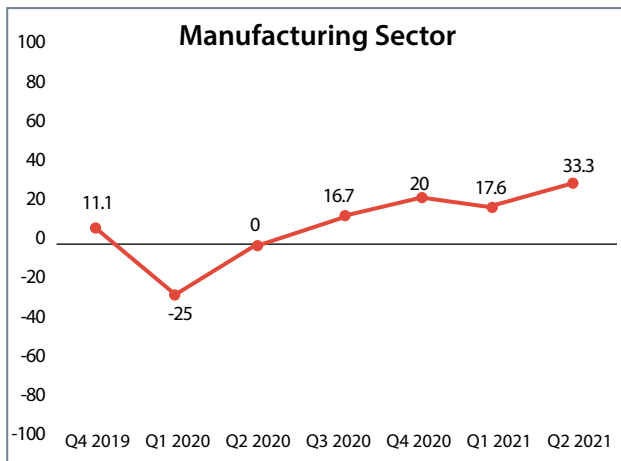
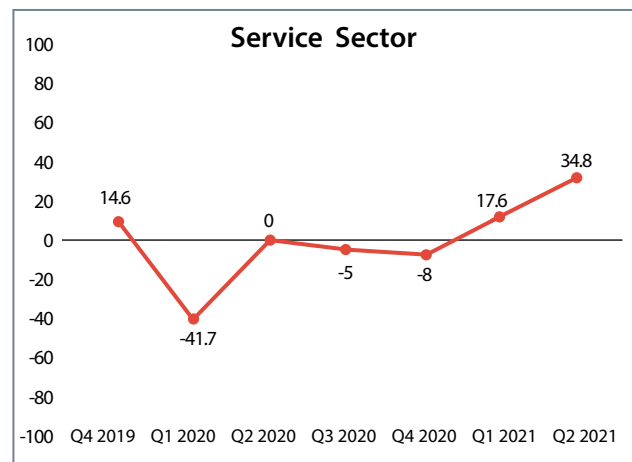
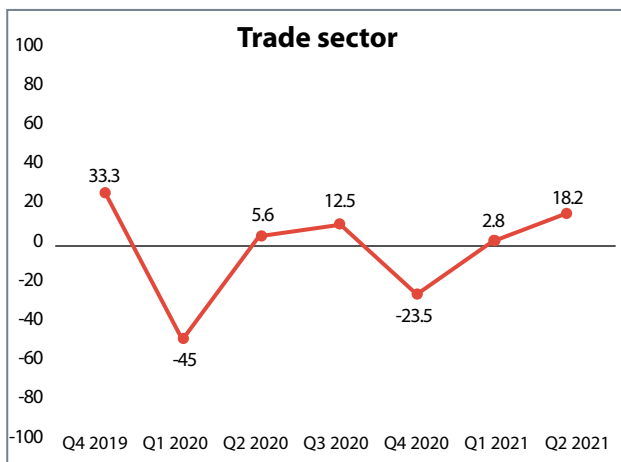
In Q2 of 2021, compared to Q1 of 2021, the improvement in the employment barometer indicator in the trade, manufacturing, and service sectors is a result of optimistic expectations regarding sales and sales prices in these sectors.

From a year-on-year perspective, it is worth noting that in Q2 of 2021, compared to Q2 of 2020, the employment barometer improved for all the reviewed sectors. The biggest improvement was recorded in the construction sector (by 41.1 points), while the smallest improvement was recorded in the trade sector (12.6 points).

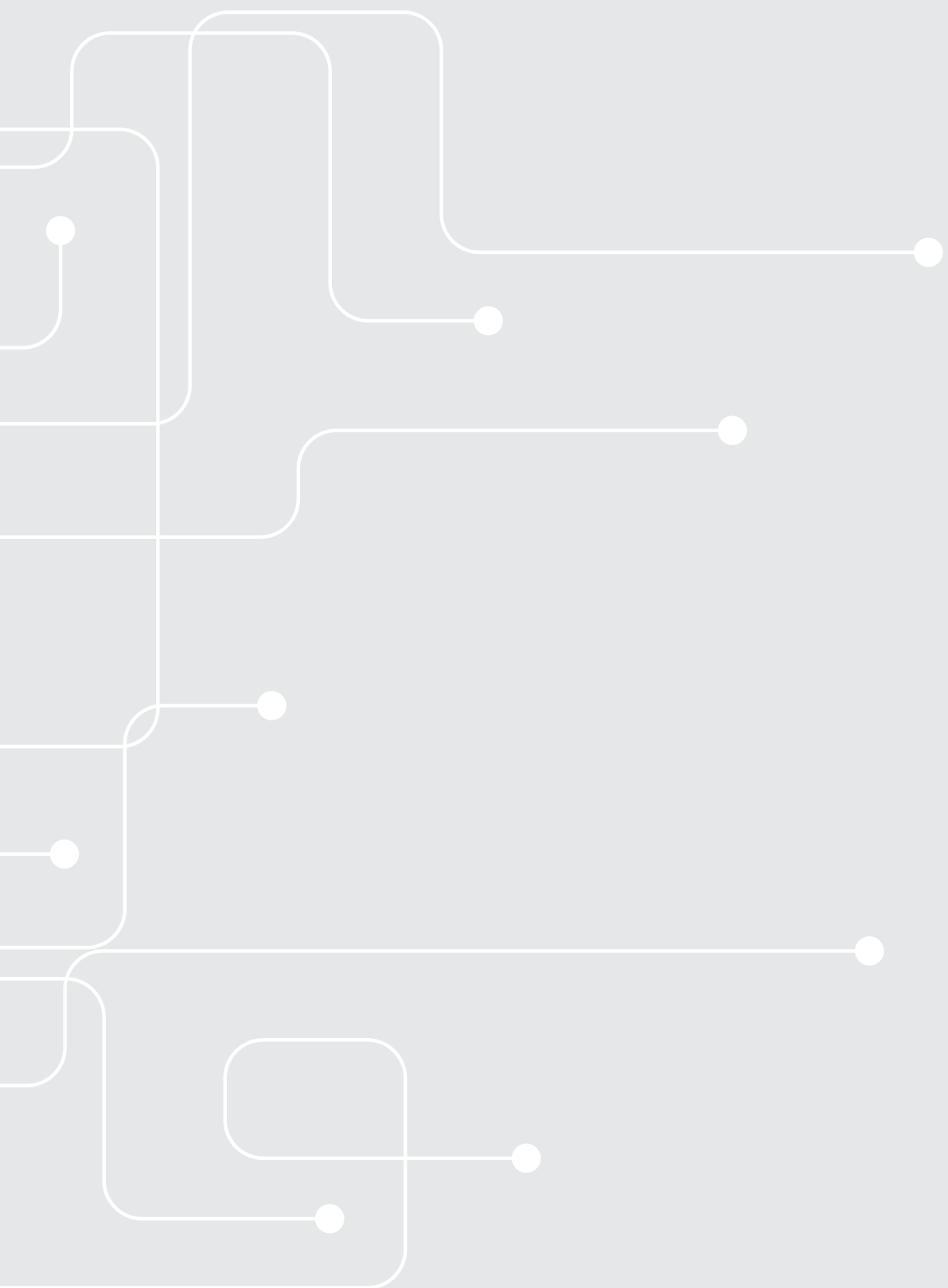
⁷ Respondents could describe their plans regarding the number of employees for the next three months as "increasing," "stable," or "decreasing." The balance value of these plans is the difference in the percentage shares of the "increasing" and "decreasing" responses. The BAG Employment Barometer is 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

	Q4 2019	Q1 2020	Q2 2020	Q3 2020	Q4 2020	Q1 2021	Q2 2021
Trade	33.3	-45.0	5.6	12.5	-23.5	2.8	18.2
Service	14.6	-41.7	0.0	-5.0	-8.0	17.6	34.8
Manufacturing	11.1	-25.0	0.0	16.7	20.0	17.6	33.3
Construction	50.0	-80.0	-28.6	14.3	-33.3	30.8	12.5
BAG Employment Barometer	26.1	-46.7	-2.8	6.2	-13.7	14.7	27.4



Graph 16: BAG Employment Barometer by sector



CONTACT:

2 Leonidze Street, Tbilisi, Georgia

☎ +995 32 2 202-215

✉ info@bag.ge

f Business Association of Georgia

www.bag.ge