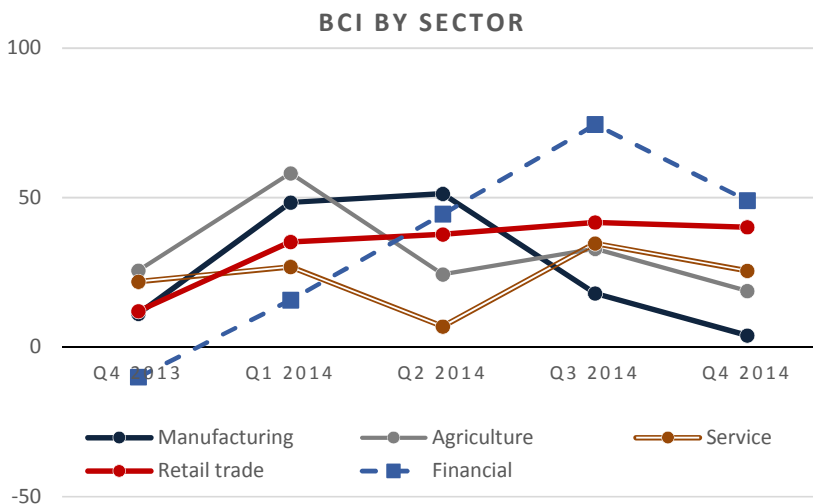


In the fourth quarter of 2014, the Business Confidence Index decreased and registered 24.9 on a scale of 100 points. This is down from the 40.4 recorded in the third quarter of the same year. The positive number indicates that the confidence factor among businesses is about 25 index points more positive than negative or neutral (e.g. a confidence index of 100 would have indicated that all firms in the sample reported a positive outlook. An index of zero would indicate that the weighted balance of positive and negative views reported by firms is about equal or, alternatively, that all firms reported no change in the current business situation. For more details, see the methodological notes). The reduction in the confidence index was driven by large firms in almost all sectors. At the same time, we note that SME business sentiment continues to grow.

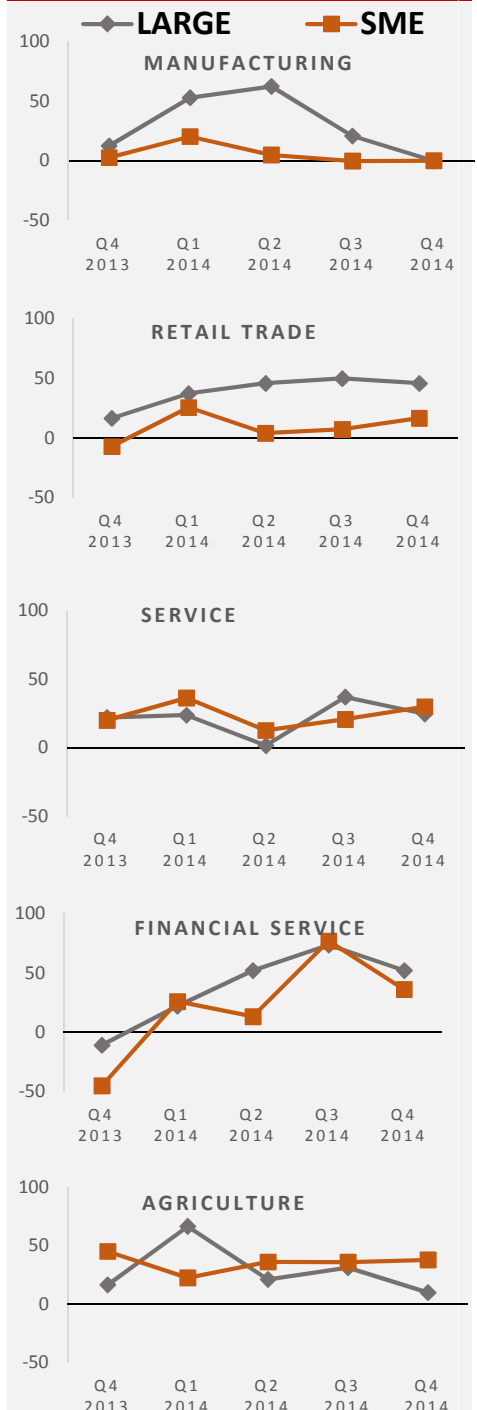
In anticipation of Christmas and the New Year holidays, there was a marginal decrease in the expectations index for the business community, dropping from 50.3 to 44.1 index points. This indicates that more firms are expecting to be more productive in the next three months as compared to the current situation.



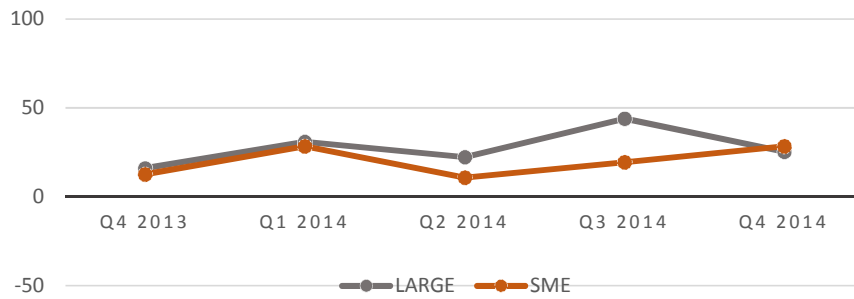
The good news this quarter is that, despite the drought in the period before the harvest, agriculture sector confidence has not reduced for SME farmers. The SME agricultural sector safeguards 43.3% of its labor force as self-employees. An increase in vegetables prices in October (12.5%) likely contributed to the positive outlook of small and medium farms. But the BCI decreased somewhat for large agro companies.

In general, the sectoral breakdown of the BCI shows that a positive outlook dominates in all sectors. This is not surprising, considering that the survey only covers businesses currently operating on the market and not those that have exited the industry. Clearly, firms still in operation are more likely to have a positive rather than negative outlook. At the same time, we note that decreases in the business confidence index were recorded in all sectors compared to the previous quarter.

**Overall business confidence by sector, for large firms and SMEs**

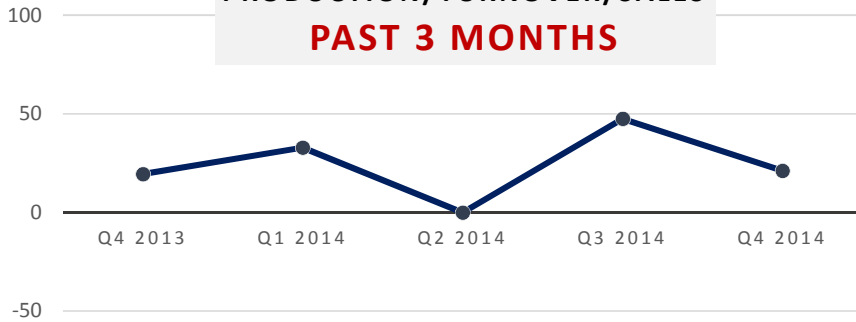


## BCI: LARGE VS. SME



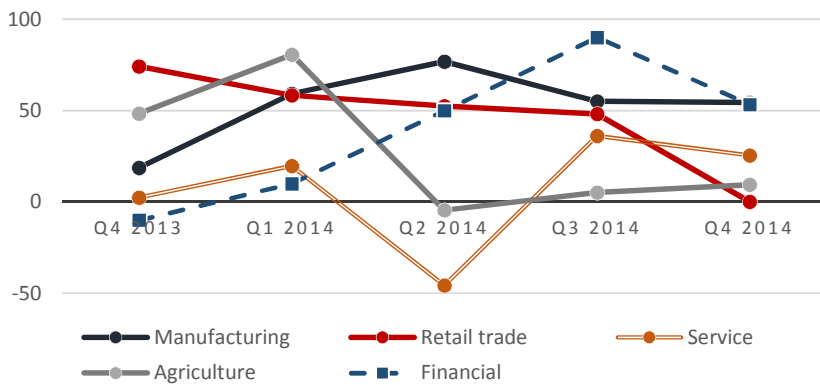
Business confidence was considerably reduced for large companies and the divergence between large firms and SMEs, as reported in previous periods, has diminished. One of the main driving factors behind this decline could have been the migration law that came into force in September 2014. The law will have had far-reaching implications for larger companies, as they not only rely on qualified foreign labor, but also on direct links with foreign investors. According to GeoStat, 40% of the total production value in the second quarter of 2014 was owned by foreign physical or legal persons. Instances of improper execution and an overly strict interpretation of the law has created uncertainty among foreigners and this has been reflected in business sentiment.

## PRODUCTION/TURNOVER/SALES PAST 3 MONTHS



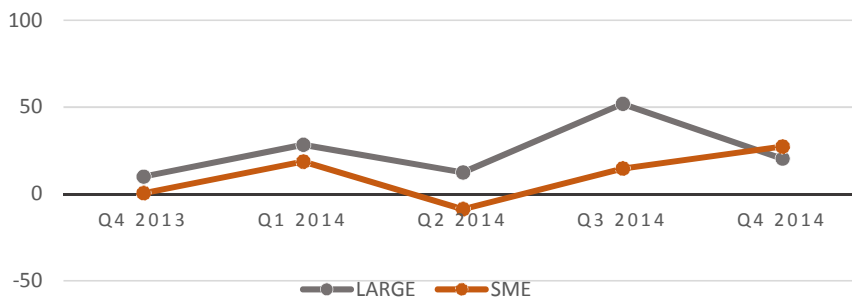
In the Q4 2014 reporting period, the sales (production or turnover) of the 100 firms surveyed decreased by 21.1 index points from 47.5. Meaning that firms' overall average activities increased going into Q4 2014, but did so less intensively as compared to the previous period.

## PRODUCTION/TURNOVER/SALES PAST 3 MONTHS



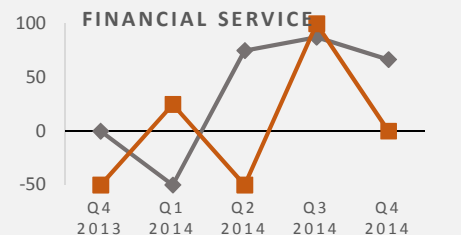
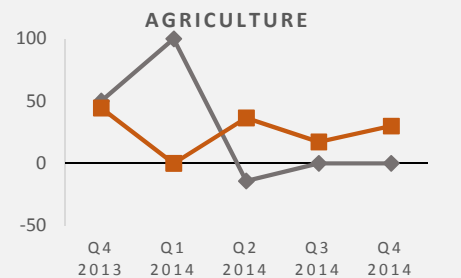
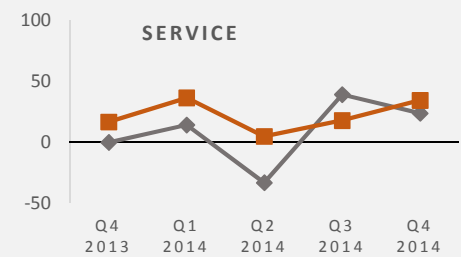
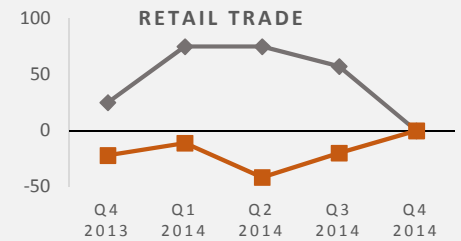
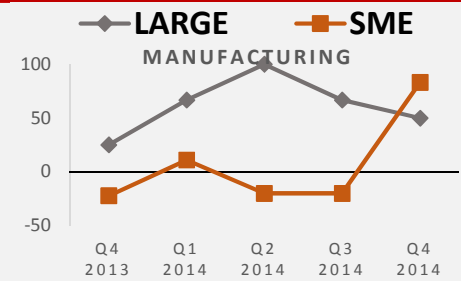
Fewer large firms, in almost all sectors, reported an increase in business activities, which explains the decrease in the index. A notable exception to this is agriculture, which maintained an increasing trend thanks to SMEs. The decrease in turnover was also felt by large retailers and large service companies. The latter was expected due to the seasonal nature of the services industry in Georgia.

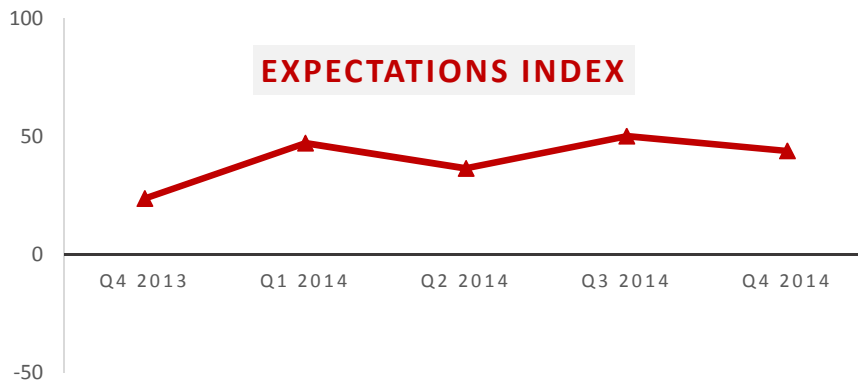
## PAST 3 MONTHS: L. VS. SME



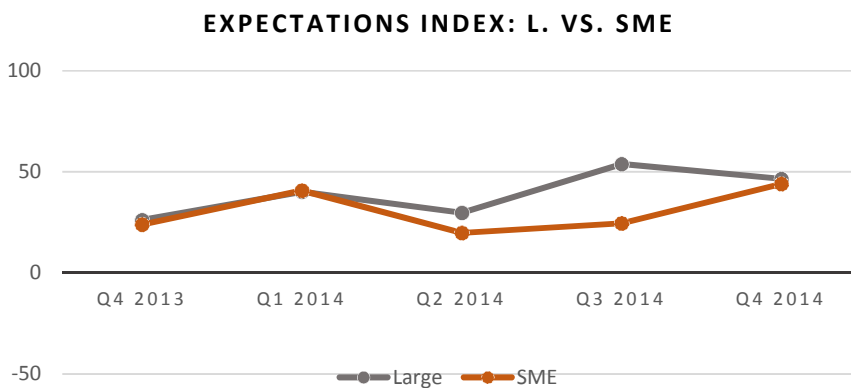
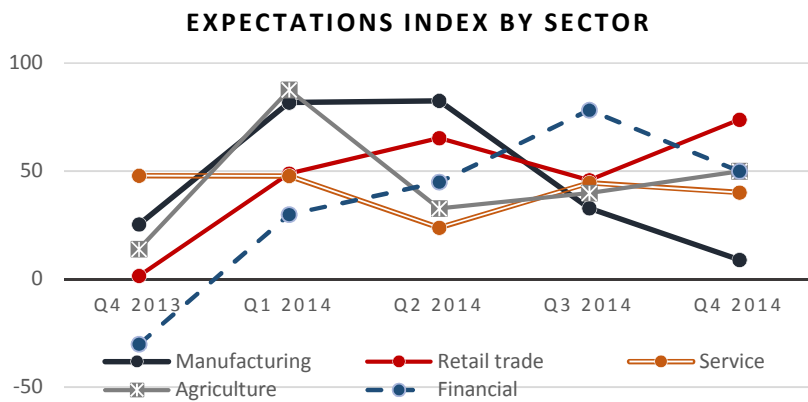
Overall, in the three months preceding July, SMEs in Georgia have fared better in terms of sales (turnover) than larger firms.

## Sales/production/turnover for past 3 months by sector, for large and small&medium firms



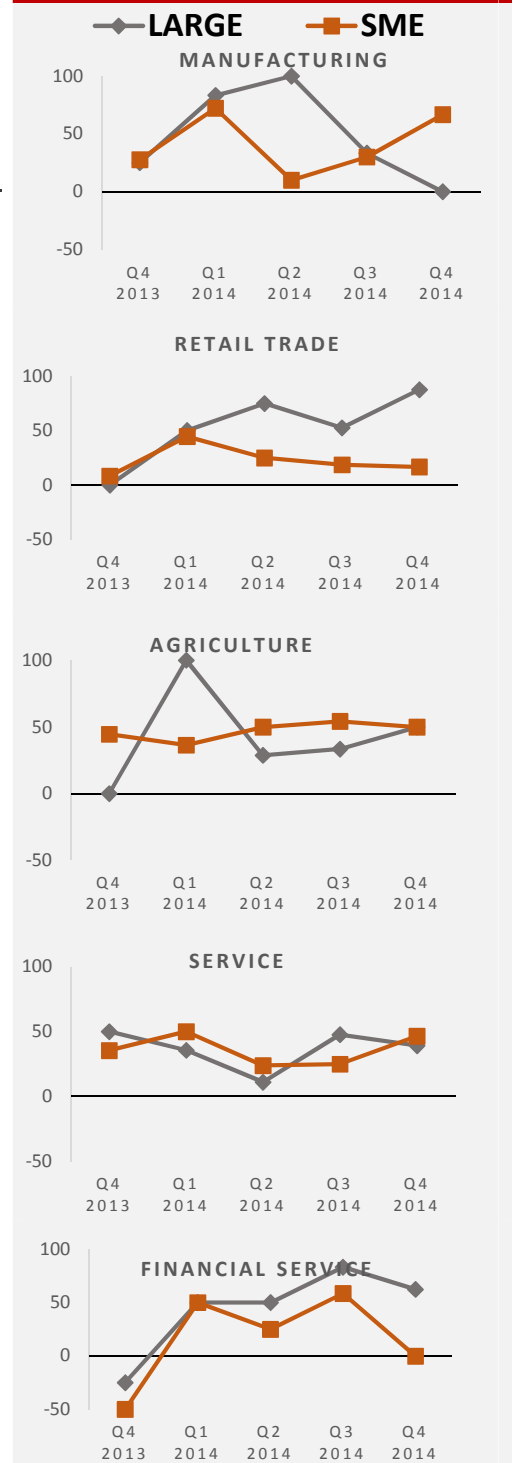


The expectations index remains stable. About 44% more firms are optimistic (rather than pessimistic or neutral) about the next three months. This optimism, which is driven by large retailers and large agriculture businesses, can be explained by the upcoming New Year period, which will traditionally increase demand on agricultural and retail products.

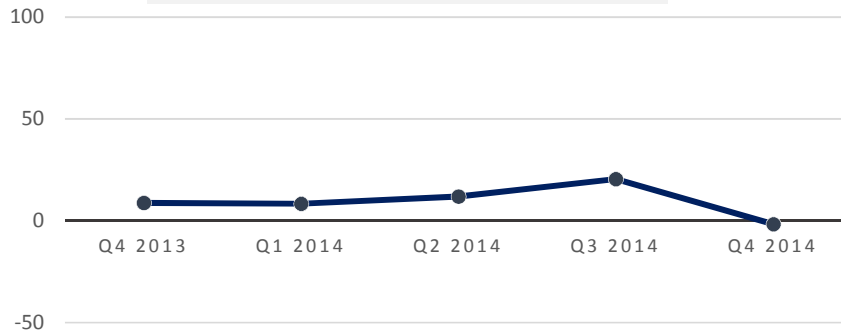


Once again, the expectations of SMEs kept improving and in Q4 2014 large firms' and SME's expectations have become equalized.

## Expectations index by sector, for large and small&medium firms

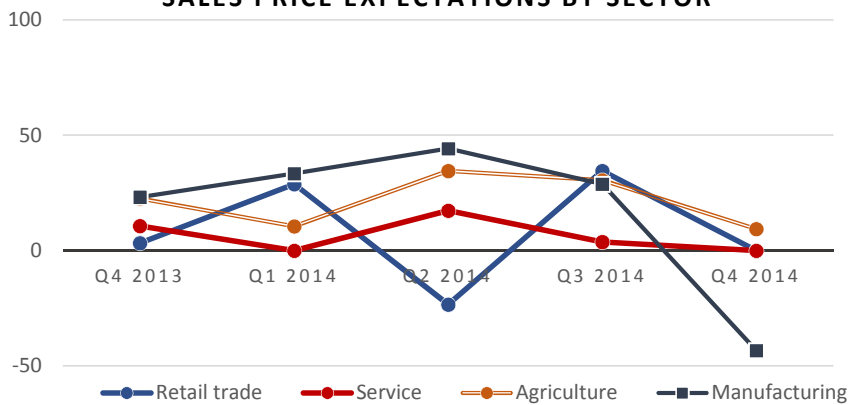


## SALES PRICE EXPECTATION



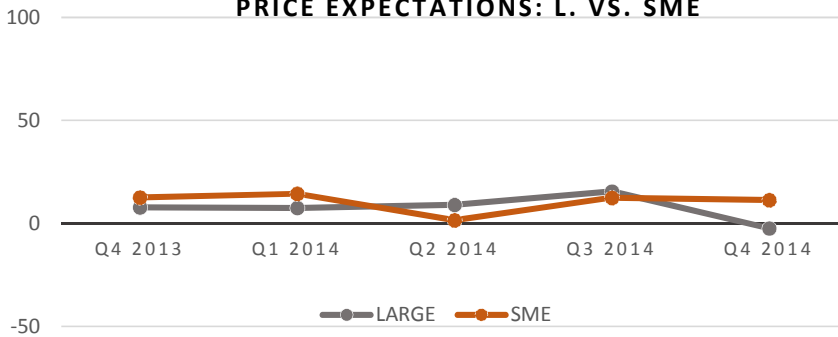
The sales price expectations index is -1.5, meaning that, on average, companies do not expect an increase in prices and even more firms think that prices will decrease. Inflationary pressure in the Georgian economy remains low, with inflation standing at 3.4% in October, which is well below the central bank's target of 6%. Given the business community's expectations, in the near future we should not expect a significant increase in inflationary pressure.

## SALES PRICE EXPECTATIONS BY SECTOR



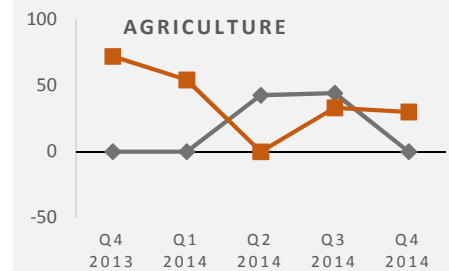
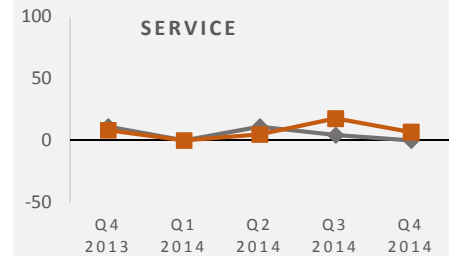
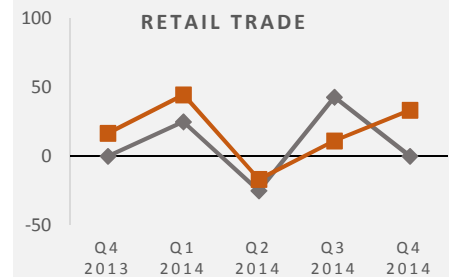
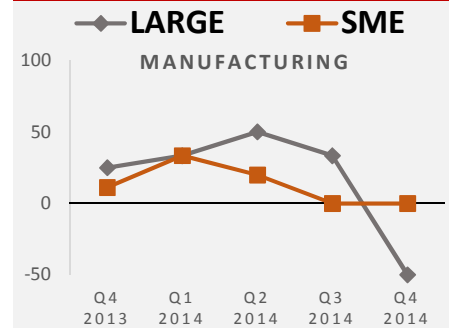
The agriculture and retail sectors' expectations are almost entirely based on an expected increase in demand. As we see it, the expected turnover increase is not driven by an increase in expected prices. In both of these sectors large companies do not expect any change in prices in the fourth quarter.

## PRICE EXPECTATIONS: L. VS. SME



Overall, the SME's price outlook remains stable and positive, but large companies do not expect any short run increases in the price level.

## Expectations index by sector, for large and small&medium firms



**WHAT ARE THE MAIN FACTORS CURRENTLY LIMITING YOUR BUSINESS?**

## What main factors are currently limiting your business?



As in the previous report, we find that the factor stated to be the most limiting for businesses is *insufficient demand*. A total of 31% of large companies report a shortage of demand to be obstacle; this index has increased from 23% in Q3 2014. SMEs, in particular, find it hard to operate on the market with unstable demand. However, in this quarter insufficient demand became a severe problem for large firms as well.

SMEs typically have more trouble attracting financial resources than large companies. The pattern is preserved in this quarter, although financial constraints appear to be less of a problem in general and for large companies in particular. On the other hand, the shortage of labor seems to be more of a problem for large enterprises. This is because large enterprises typically look to attract qualified workers, while SMEs may rely on unqualified labor to a greater extent.

**SAMPLE SIZE BY SECTOR (see methodology)**

Interviews were conducted during 10 October-15 November, 2014.

	Sector	Firm Size		Total
		Large	SME	
Q4 2014	Construction	4	1	5
	Financial Service	8	1	9
	Manufacturing Industry	2	3	5
	Retail Trade	4	3	7
	Service	23	29	52
	Agriculture	2	10	12
	Other	4	6	10
	<b>Total</b>	<b>47</b>	<b>53</b>	<b>100</b>

## \*Methodology

The ISET Policy Institute, working in partnership with the International Chamber of Commerce in Georgia (ICC), has implemented the Business Confidence Survey from December 2013 and publishes the Business Confidence Index (BCI) on a quarterly basis.

Business confidence for Georgia is measured by seven sector-specific indices focusing on: 1) services, 2) retail trade, 3) agriculture, 4) manufacturing industry, 5) financial service 6) construction and 7) other sectors. For each sector, confidence is measured through a simple survey instrument targeted at top business executives.

Answers obtained from the surveys are aggregated in the form of “balances”. Balances are constructed as the difference between the percentages of respondents giving positive and negative replies.

Using this method, a Confidence Index of +100 would indicate that all survey respondents were much more confident about future prospects, while -100 would indicate that all survey respondents were much less confident about future prospects.

VARIABLE	SCORE
Positive	+1
Neutral	0
Negative	-1

The methodology of compiling the indices is based on the Joint Harmonised EU Programme of Business and Consumer Surveys.

### DEFINITIONS

- The **Business Confidence Index** is calculated as a weighted average of the balances induced from all the answers about production/sales/turnover, competition, order books, volume of stock, demand evaluation, operation costs, profit, employment, and sales price setting;
- The **expectations index** is calculated based on two questions: production/sales/turnover for the next three months and employment plans for the next three months;
- A **large<sup>1</sup> firm** is one with a yearly average of over 100 people employed or a yearly average turnover exceeding 1.5 million GEL;
- **Small firms** are those with an average of fewer than 20 people employed over a year and an annual average turnover of less than 0.5 million GEL;
- **Medium firms** are those that are neither large nor small.

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<sup>1</sup> The size of the company is defined accordingly to the Main Indicators' Calculation Methodology of Business Statistics ([http://geostat.ge/cms/site\\_images/files/georgian/methodology/business/BS%20metodologia.pdf](http://geostat.ge/cms/site_images/files/georgian/methodology/business/BS%20metodologia.pdf))